Tortoise QuickTake Energy Podcast

May 17, 2018

Welcome to the Tortoise QuickTake podcast. Thank you for joining us. Today, senior members of Tortoise provide a timely update on trending topics in the market.

Hello I am Rob Thummel, Tortoise portfolio manager, and I'm here to talk to you about a special podcast, to update you on the latest simplification announcements today. So first, let's talk about what happened. There was a flurry of simplification transactions announced today by Williams, Enbridge and Cheniere. Here's some highlights. So first of all, Williams Companies (WMB) the corporation, they plan to acquire Williams Partners L.P. the MLP, (WPZ).

The transaction, whereby WMB plans to acquire all of the outstanding common units in WPZ in a stock-for-unit transaction at a 1.494 ratio of Williams common shares per unit of Williams Partners. This transaction was announced and it represents a premium of 6.4% based on the closing stock price of WPZ on May 16, 2018

So what does this do for the company? According to the management team, the benefits are a simplified organizational structure and retention of significant distributable cash flow that allows the company to re-invest in capital projects. After this transaction, Williams, the corporation expects to have coverage of about 1.7 times its distributable cash flow. Also, and just as importantly, Williams is not expected to be a cash taxpayer through 2024. This is important because this allows closed-end funds to likely continue to hold companies like Wiilliams even though they're structured as corporations now and are no longer MLPs. The merger will close or is expected to close in the fall of 2018 and will be subject to Williams shareholder approval. Now, one thing we always like to follow is "Will your distributions as unitholders be reduced?" And in this case, due to the timing of this Williams announcement, WPZ or the MLP shareholders are expected to receive five dividends or distributions during the calendar year 2018, which equates to approximately a 15% increase in the previously-guided 2018 distributions. That assumes that the closing occurs before the Williams' third quarter dividend record date. A lot of details there, but the net result is the impact to the cash flows investors received will likely be mitigated and will not result in as much of a cut as investors had originally anticipated.

We think this transaction benefits both parties. Both Williams corporation shareholders as well as the MLP, Willams Partners, LP. Unlike the Enbridge announcement we think clearly benefits Enbridge corporation but not the MLPs as much.

In the case of Enbridge, corporation (ENB) offered to acquire Enbridge Energy Partners (EEP), Enbridge Energy Management (EEQ), Spectra Energy Partners (SEP), and Enbridge Income Holdings Inc. (ENF). Three out of the four of those entities are MLPs. Now the parent corporation in this case is offering a fixed exchange ratio of common shares for the underlying units of the sponsored vehicles, those being the MLPs. Here's why we think it was done the wrong way. Spectra Energy holders, Enbridge Energy Partners holders and Enbridge Energy Management holders received 0% premium to the May 16th, 2018 closing price. In addition, post-transaction, the management of Enbridge stated that unitholders would experience reductions in distributions. Spectra Energy unitholders will see distributions decline by about 29%. While Enbridge Energy Partners, and Enbridge Energy Management unitholders will see distributions fall by 53% and 56%, respectively. Now, reasons why this transaction was announced? Once again, trying to simplify the structure. Effectively, you're taking five entities here and consolidating them into one. Accomplishes that. It also simplifies the corporate and capital structure of Enbridge. But it also reduces the risk associated with the FERC MLP income tax allowance elimination that we previously talked about earlier this year and identified Enbridge and Spectra in particular as two companies that had the most exposure to this MLP tax allowance.

The last simplification announced today, was Cheniere Energy, Inc. (LNG) offering to acquire the outstanding shares of Cheniere Energy Partners LP Holdings, LLC (CQH) at an exchange ratio of 0.45 of LNG shares for each outstanding CQH or Cheniere Energy Partners Holdings share which represented about a 1% premium to the May 16, 2018 closing price.

This was a smaller transaction, we won't spend a lot of time on that, but the underlying question that everybody has I think is "Where these expected?" And I think the answer was, I think its been very clear, that Williams and its acquisition of Williams Partners was expected. That had been pretty well telegraphed in the market and obviously ended up happening in what we think was a pretty good way. The Enbridge acquisition of Enbridge Energy Partners was expected, but I do not think that the Enbridge acquisition of Spectra Energy Partners was expected. Nobody expected both entities to be acquired at a 0% premium. Now I would state on both of these transactions, and this is really important, that both of these offers in the case of Enbridge are subject to approval of the board of directors of Enbridge, its corporate subsidiaries, its sponsored vehicles and its conflicts committee so there is still an opportunity for shareholders to potentially receive a premium should that be required by the board of directors of the various entities.

So, how did the market react? Well in a day when the broad market, the Dow and the S&P were either flat or down, you saw very strong performance out of the MLP asset class and the energy sector in general. Why is that? I think finally, and we've been talking about this on podcasts throughout the year, that there's been a shift in investor sentiment and now the focus of investors is on assets and away from structure. And what we know at Tortoise in our history of looking at energy infrastructure assets all the way back to 2002, is the energy infrastructure sector and assets are essential. Demand is growing and to fill that demand you need more energy infrastructure assets. Now in our view, MLPs do remain an effective structure and one of the most cost-effective ways of building new energy infrastructure assets. MLPs simply do not pay income taxes. That gives them a competitive advantage. But the market response to these transactions I think shows you there is a simple premise. These assets are too good, too important, too critical to be valued this cheaply So as a result, we were happy to see the market reaction and expect to the MLP asset class to continue to perform well and if you look at performance in the MLP asset class this month it's been one of the top performing asset classes in the month of May, which is a good thing as well.

To wrap up. Thank you for listening and we'll talk to you again next week.

Thank you for joining us. And stay tuned for our next cast. Have topics you want covered or other feedback to share? Write us at info@tortoiseadvisors.com.

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