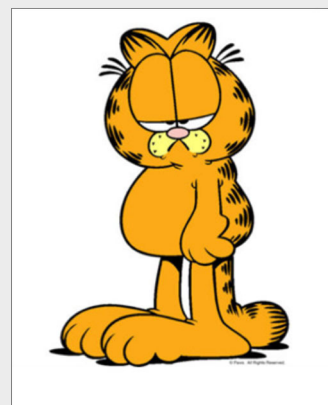


EGA Energy MLPs and Midstream Companies

From the EGA Portfolio Management Team

Nothing Should Surprise Us Anymore, Yet Here We Are

You would think that nothing should surprise us anymore, yet here we are. Was it weak stock price performance in the second and third quarters? Not really. The sector slipped along with energy prices, though the Alerian MLP Index has held on to year-to-date gains (+11%) and in our view is behaving as a defensive energy sector should (contrast with OIH down 16%). Is it the inability for high-yielding Midstream to catch a bid in a market starved for yield? No. Midstream still has a credibility problem that needs to be resolved before investors return en masse. The surprise for us was Energy Transfer's (ET) decision to pay a 65% premium to purchase struggling SemGroup (SEMG). Yes Garfield, 65%.



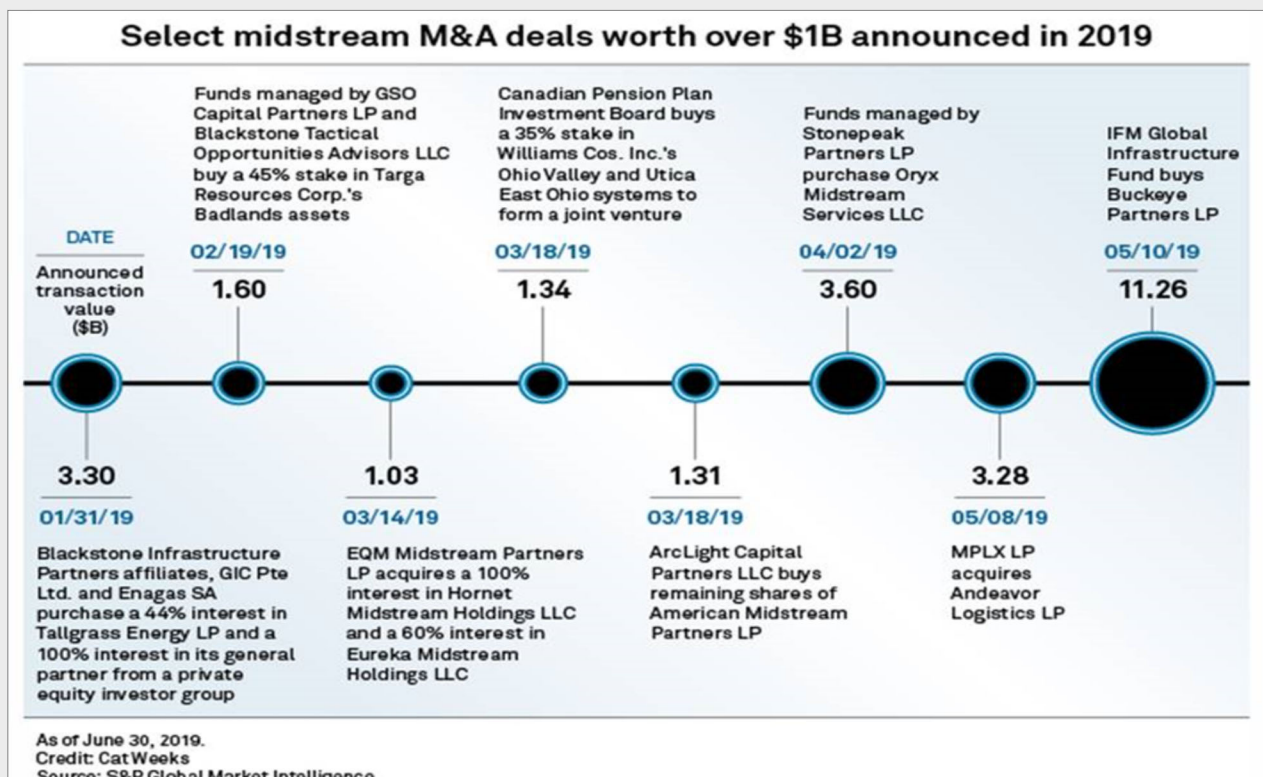
However, after our initial jaw drop we put on our fundamental hats, updated our models, and tapped our industry contacts. We determined the acquisition has significant strategic value and the premium paid fairly represents where the market is for Midstream assets, especially considering the recently released proxy showed there where multiple public companies and private equity firms making offers. So, while we understand why CEO Kelcy Warren makes investors tear their hair out, there was method to this perceived madness.

Building An Integrated Network Sometimes Requires Acquisitions

To say Energy Transfer has been active on the acquisition front would be a gross understatement. A sampling of its major acquisitions includes: (1) Purchasing LDH Energy Asset Holdings from Louis Dreyfus Highbridge Energy for \$1.925 billion. Strategic to Energy Transfer was Louis Dreyfus' natural gas liquids (NGLs) infrastructure assets, particularly in the key hub of Mont Belvieu; (2) Acquiring Southern Union for \$7.9 billion. Strategic to Energy Transfer was Southern Union's natural gas infrastructure assets; (3) Acquiring Sunoco for \$5.3 billion and its strategic refined products infrastructure assets (Permian takeaway pipes, Netherland terminal). Energy Transfer was able to utilize Sunoco's asset footprint to raise its profile in NGLs as well. Each acquisition improved the company's vertical integration that in turn opened up growth opportunities.

That brings us to Energy Transfer's \$5 billion acquisition of SemGroup. We believe, and the company has verified, that the strategic rationale for this acquisition is the Houston Ship Channel assets that adds increasingly critical export capabilities to Energy Transfer's vertical integration. Today, more and more energy products are being exported from U.S. shores. Controlling the product from the wellhead to multiple markets is critical, and the final domestic frontier is exports. There is a view that getting your molecule to Houston alone is not enough. Therefore, Energy Transfer's acquisition of SemGroup was strategic because of the latter's ownership of export capable assets on the Houston Ship Channel. But does the strategic value of the assets justify the price (i.e. premium) paid?

In today's market there is plenty of private equity money looking to acquire assets, and the ET / SEMG deal proxy outlines that to be the case for this transaction. This continues a trend most recently evidenced by private Australian investor IFM Global's 27.5% market premium takeout of Buckeye (BPL), GIP's \$3.125 billion investment in Enlink Midstream (ENLC) via buyout of Devon's (DVN) interest, and Blackstone's \$3.3 billion initial investment in Tallgrass Energy (TGE) and subsequent \$3.1 billion offer to take the company private. The private sector is, at the moment, willing to pay a significant premium for stable cash flows with embedded growth opportunities. For Energy Transfer, the high premium for SEMG was necessary in order to win the auction. However, only time will tell if the deal is a success, as this will be determined by what Energy Transfer does with the acquired assets.



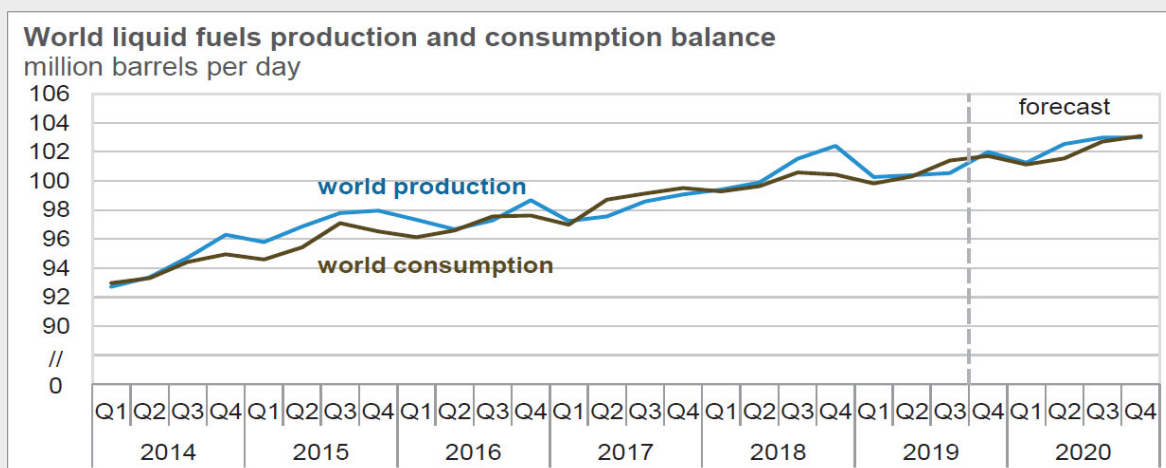
A Few Final Thoughts..

Lest you forget, Saudi Arabia is still very important. On September 14 there was an airborne attack on a major oil processing plant in Saudi Arabia, knocking about 5 million barrels per day (~5% of world supply) of oil offline and driving oil prices 15% higher. Saudi Arabia announced a rapid repair timeline and said it would tap its strategic reserves to maintain its market share, which calmed the markets enough that nearly two weeks later oil prices had returned to pre-attack levels.

Country	Million barrels per day	Share Of World Total
United States	17.9	18%
Saudi Arabia	12.4	12%
Russia	11.4	11%
Canada	5.3	5%
China	4.8	5%
Iraq	4.6	5%
Iran	4.5	4%
United Arab Emirates	3.8	4%
Brazil	3.4	3%
Kuwait	2.9	3%
Total Top 10	71.0	70%
World Total	100.7	

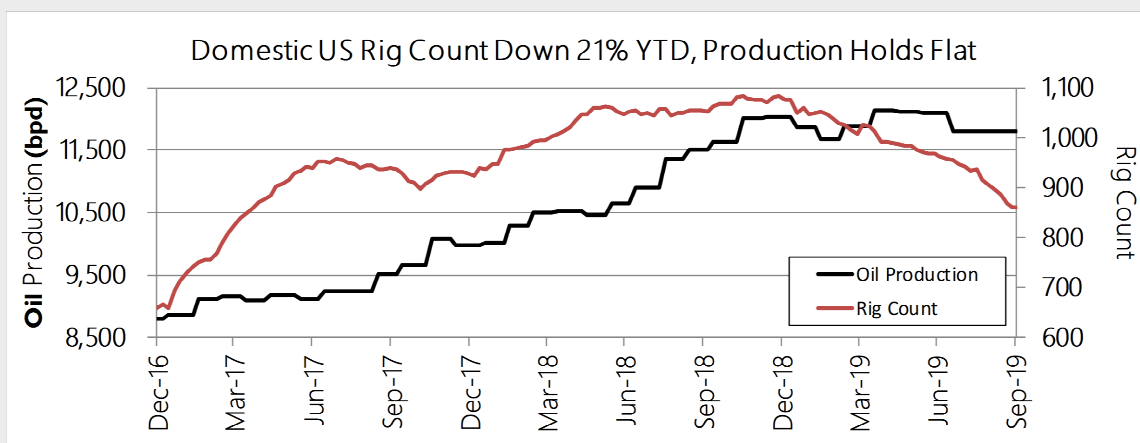
Source: Energy Information Administration (EIA)

Lost in the mix of the shale revolution and subsequent energy price declines over the last several years is the supply/demand gap remains quite tight (see below exhibit). The small supply/demand gap (aka “spare capacity”) means short-term shocks like the Saudi Arabia attack can create significant volatility in energy prices. In addition, a closer look at the top ten oil producers list several countries with significant geopolitical risk, which when considering these top ten account for 70% of total oil production places more risk around global supply. Add geopolitical risk with the fundamental risk of global under-investment in oil and you have an environment where higher oil prices are a real risk. It’s difficult to grow spare capacity when the U.S. shale revolution is slowing (detailed below) and international investment remains at lower-than-historical levels. In our view, this means risk to oil prices is to the upside absent a major macroeconomic correction.



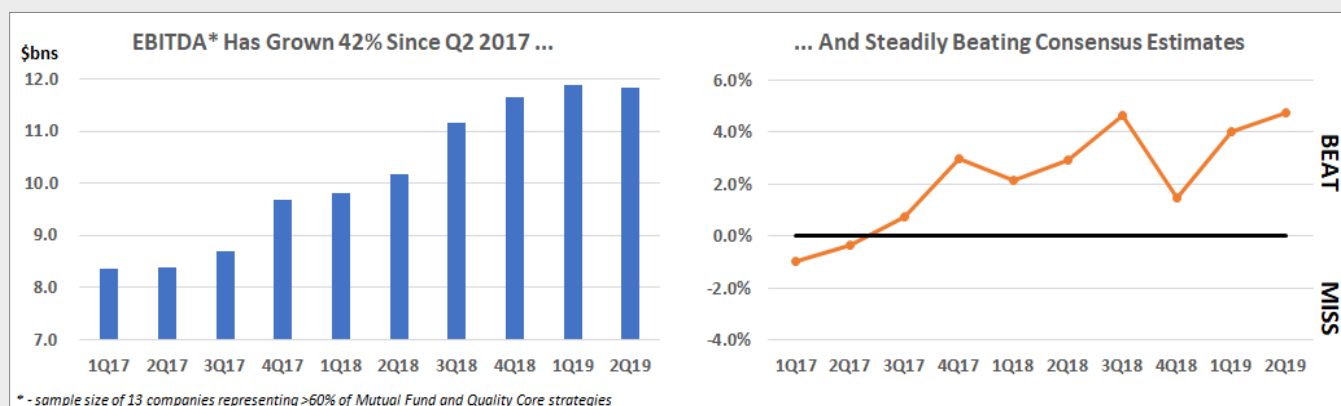
Source: Energy Information Administration (EIA)

Meanwhile back in the United States, rig count declines forecast slowing production growth. Weak energy prices and an investor-driven focus on capital discipline have driven larger E&Ps to reconsider their capital spending and pushed smaller producers to the brink of bankruptcy. The Oil Services sector is in complete disarray as the rig count drops in response to these market conditions. The rule of thumb within the energy industry is it takes roughly six months for changes in rig activity to have an impact on production, which means a flat rig count in 2H18 has led to relatively flat U.S. production growth in 1H19. With rig count down 21% YTD there is an expectation that production will slip lower in 2H19-1H20, although improvements in technology driven rig efficiency and well design (i.e., energy players are getting more out of a well with less spending) should moderate potential declines. Nonetheless, potential production declines present a risk to select midstream companies and we continue to incorporate this risk in our models and adjust our portfolios accordingly. On the other hand, the margin for error is very thin within the energy markets and with international capital spending continuing to run at historically low levels and geopolitical risk on the rise, the risk of oil price shocks is very real.



Source: Baker Hughes, EIA

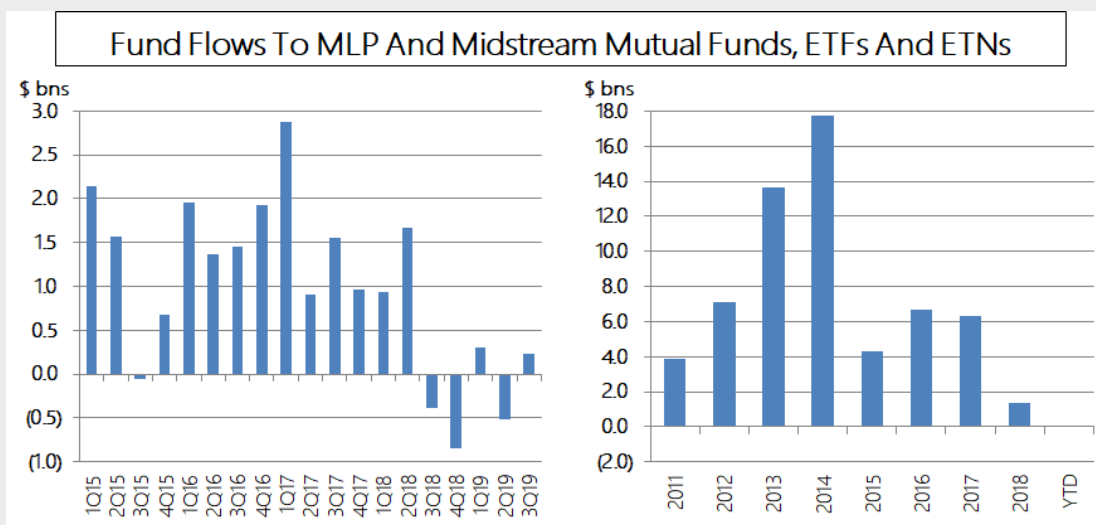
Another quarter, another EBITDA beat. We reviewed 13 companies that represent a majority of our portfolio holdings to see how they're performing versus consensus expectations. Over the last ten quarters EBITDA has grown 42% and has beaten the Street's consensus estimates for eight consecutive quarters (see below charts). However, analyst expectations for aggregate EBITDA among this sample was roughly flat, a forecast that companies in aggregate only matched. We are encouraged by the ability of management teams to deliver on EBITDA expectations in a tough market, which goes a long way towards accomplishing de-leveraging strategies and rebuilding investor confidence in the sector.



Source: Bloomberg, Company data

Capital Flows And Access To Capital

Capital flows improved in the third quarter following what was a poor second quarter. Identifying any trend remains elusive as well, as capital inflows in July and August of \$191 million and \$135 million were followed by a capital outflow of \$100 million in September. Inconsistency appears to be the theme this year for capital flows, and one we expect to continue given weak sentiment within both Midstream and broader energy. We reiterate our view that the slightest tailwind in capital flows could drive an outsized rally in the absence of any company-directed capital formation.



As of 9/30/19 Source: U.S. Capital Advisors

Separately, the third quarter was relatively quiet in regard to equity issuance. NGL Energy Partners (NGL) raised just over \$700 million of preferred equity in two separate direct capital raises, with proceeds directed to helping finance their purchase of water assets from Mesquite and Hillstone Environmental. Separately, Occidental Petroleum (OXY) sold its long-held position in Plains All American (PAA/PAGP) as it continues to raise cash following its purchase of Anadarko Petroleum earlier this year. This has added meaning given as part of OXY's purchase of Anadarko they also purchased a controlling interest in Western Midstream (WES), of which investors are still waiting to hear what OXY will do with.

MLP Team Update

There were no significant team related news items to highlight this quarter. We continue to focus on the research and portfolio execution effort and are in constant dialogue with industry experts and management teams. We attended multiple major Midstream conferences over all three months of the third quarter and saw minimal recovery in sentiment following the sharp deterioration in the second quarter. While Midstream has held up materially better than more cyclical sectors (i.e., E&Ps and Oil Services), there remains a dark cloud over sentiment that is encouraging both investors and management teams to emphasize a cautious approach. We reiterate our cautious optimism on 2019 as the sector's structural upgrades position it to benefit from the world's increasing appetite for energy infrastructure.

We thank you for your continued patronage of Eagle Global Advisors. We believe the long-term return outlook for Midstream remains attractive, and we look forward to communicating the results of your investment in an Eagle managed account next quarter.

- The Eagle MLP Team