Linn Energy is Not Your Father's MLP

Master Limited Partnerships (MLPs) are best when they’re boring over the short term. Predictably raising your cashflows and distributions leads to long term excitement at the very reasonable cost of being tedious to watch on a daily basis.

In 2014, Linn Energy (LINE) was the antithesis of this. While most MLPs own midstream energy infrastructure assets with their toll model, LINE is engaged in Exploration and Production (E&P) of oil and natural gas. The consequent commodity price exposure makes both their cashflows and stock price highly volatile. This contradicts the point of owning MLPs, which is to extend the holding period indefinitely so as to maximize the tax shield that the deferral of income affords. The best MLPs are those that are stable, boring and whose valuation doesn’t hit either extreme of rich or cheap. Because selling an MLP usually creates a tax bill, greatly impeding overall returns.

LINE fell 67% in 2014 because of its exposure to oil. It was obviously a great sale earlier last year above $30. It may be a great buy now at around $11, given that they’ve done the inevitable and cut their distribution. But timing MLPs isn’t easy, and investing in businesses like LINE requires some timing skills on the part of the investor because it’s not always a good name to hold. This is LINE’s second collapse since their 2006 IPO. In fact, even a buyer in 2008 at the stock’s absolute low is now barely ahead of breakeven following a six year roller coaster.

So buying LINE may be a good trade as it’s fallen so far. But buying and then inevitably selling it is unlikely to be a tax-efficient investment. Boring is better, and after taxes far superior.