The Power of the MLP GP

Yesterday was Williams Companies' (WMB) Analyst Day. The company gave a strong presentation across each of their divisions. It highlighted the many opportunities to build new infrastructure in response to the shale developments, especially in the Marcellus. WMB's dividend yield is 3.3% but such is the earning power of the assets they control that management extended their dividend growth forecast of 20% out to 2016 (from 2015) with further strong performance expected beyond that. Much of this is driven by assets held at WMB's MLP, Williams Partners (WPZ), since WMB owns the General Partner are therefore receives 50% of each additional dollar of distributable cashflow.

WMB controls Transco, a pipeline network that runs from the NE U.S. down to Texas. One of the more memorable pieces of information came when Rory Miller, SVP of the Atlantic-Gulf Operating Area, noted that he'd once asked his team to estimate the cost of rebuilding the Transco system and the figure they came up with was $100 billion (for comparison, WPZ's enterprise value is $33 billion). This pipeline was first laid 60 years ago, and decades of population growth and development all along the route make the cost of building something similar today prohibitive.

Interestingly, today Goldman upgraded Kinder Morgan (KMI) from Buy to Conviction Buy. Kevin Kaiser of Hedgeye, a small research firm in Connecticut, has been a long-time critic of MLPs and the Kinder complex in particular. KMI owns the GP for Kinder Morgan Partners (KMP) and El Paso (EPB) and while it doesn't sport the type of growth prospects of WMB we think it's a similarly attractive security leveraged to the continued development of energy infrastructure in the U.S. Kaiser has long argued that firms such as KMI skimp on maintenance, something not supported by metrics such as operating performance or accident statistics. But the Transco example above suggests that in at least some cases MLPs own assets that are substantially undervalued, at least on a replacement basis.

KMI has been a weak performer over the past year or so, providing at least some vindication for Kaiser (although their business performance has been fine and his negative call on MLPs as a whole has been dead wrong). For our part, we think both companies are very well positioned and are long both WMB and KMI.