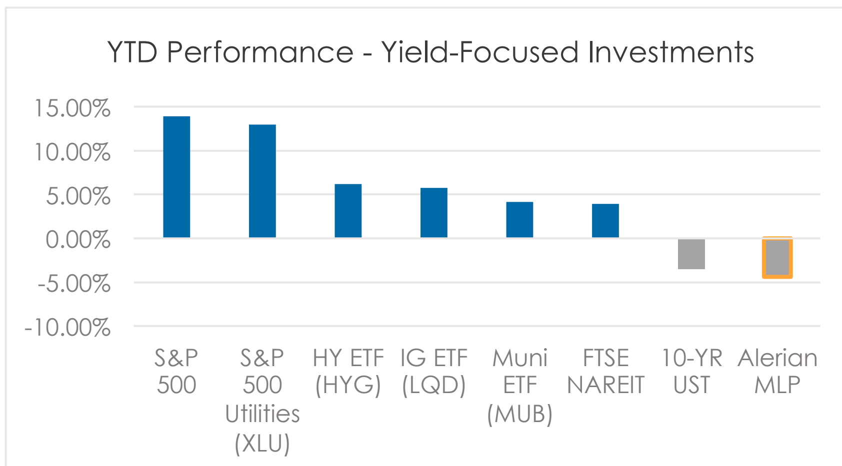
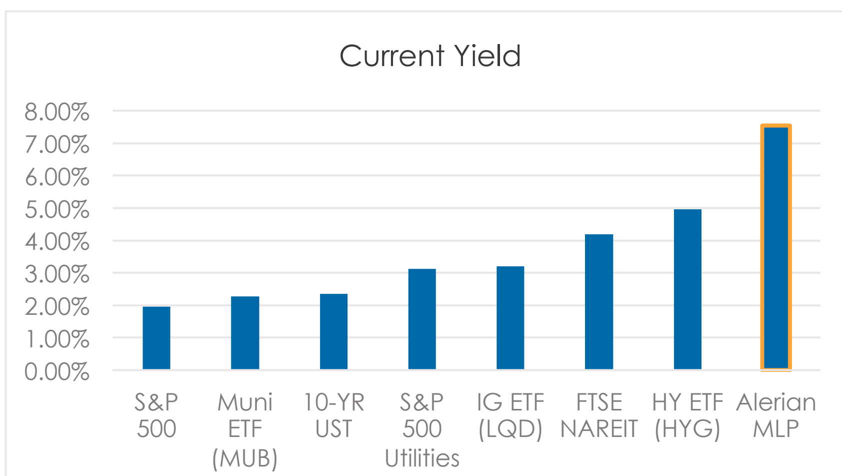
A LOOK AT MLPS: OPPORTUNITY IN AN ORPHANED ASSET CLASS

HIGHLAND CAPITAL MANAGEMENT

OCTOBER 2017

The Exploration & Production (E&P) sector appears much healthier these days following the wave of bankruptcies of the last two years; however, Master Limited Partnerships (MLPs) have not seen the same benefit. Year to date, they have drastically underperformed other yield-focused investment sectors. This performance is reminiscent of periods in 2015 and 2016 when MLPs were dragged down by the negative perception of the energy industry as a whole, despite their ability to maintain economical operations in a subdued commodity price environment.

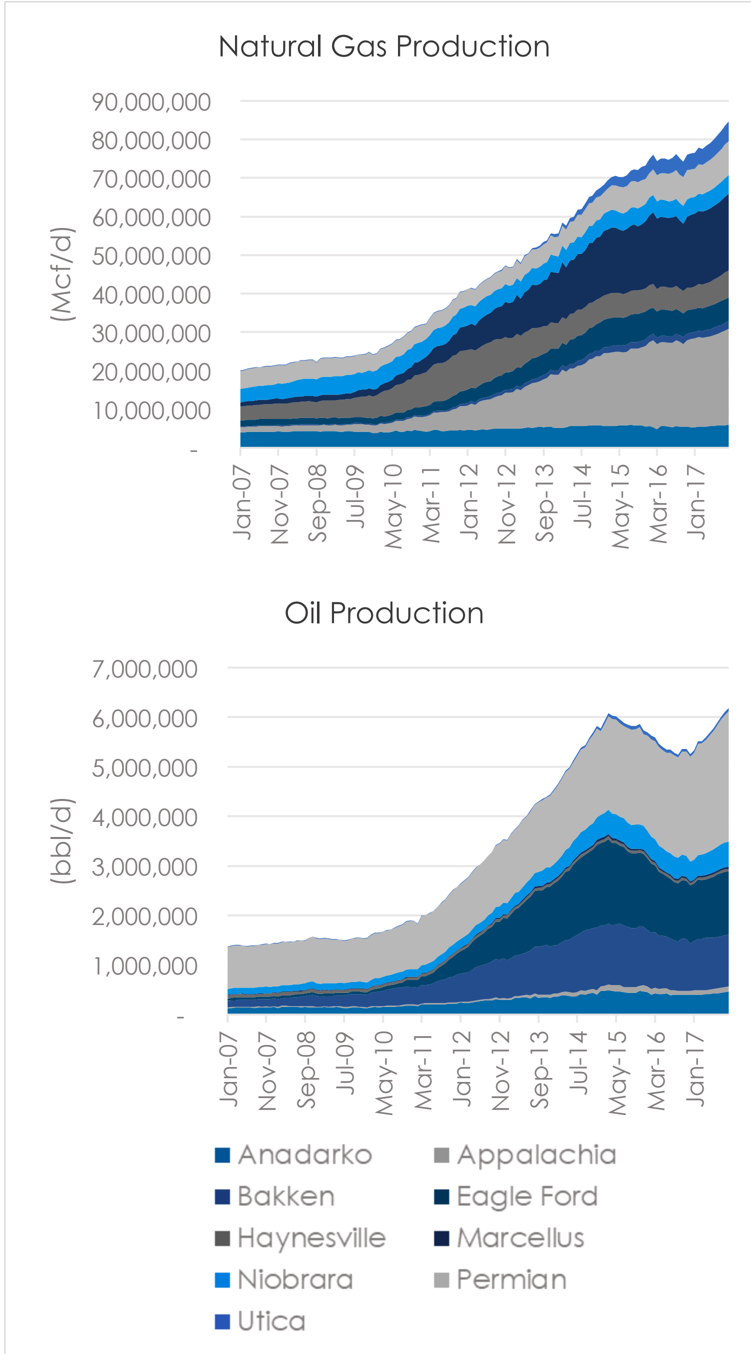




Source: Bloomberg (as of 10/9/2017)

We remain constructive on MLPs and are among the few paying close attention to this orphaned asset class. Though it remains to be seen whether or not the broader investment industry will fully appreciate the differences here, we expect MLPs to gradually fall back into favor thanks to a few catalysts on the horizon. However, even without those catalysts in place, the fundamentals around MLPs remain stable in our view, and we currently see opportunity even while others have all but forgotten this corner of the energy space.

Shale-based crude production is close to its all-time high, and natural gas production continues to increase.



Source: U.S. Energy Information Administration (EIA)

Lagging YTD Performance Despite Healthy E&P Sector

The severity of the crude price downturn demonstrated the resiliency of a number of areas of the energy industry. Efficiency improvements and the advancement of technology kept many E&P companies alive even in the most challenged commodity price environment.

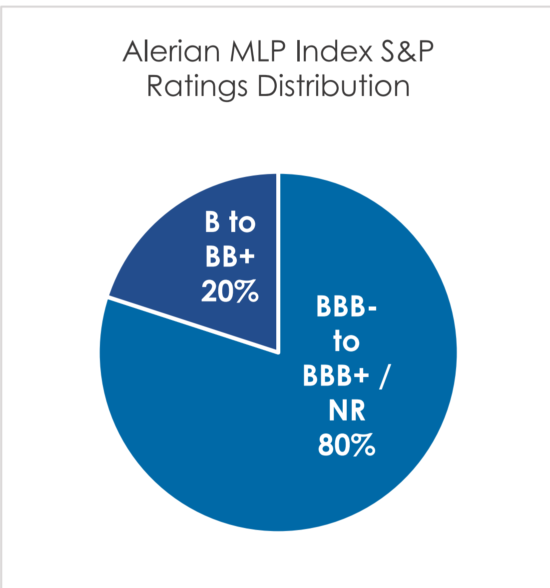
With prices stabilized, shale-based crude production is now close to its all-time high, and natural gas production has continued to increase.

These trends go hand in hand with positive momentum in midstream infrastructure, and there is a clear need for expansion in certain basins with resilient production profiles. And over the longer term, the limits of current takeaway capacity in the U.S. suggest a broader need for additional energy infrastructure throughout the country.

As a volume-based business, these underlying trends should support the outlook for MLPs; however, the misunderstanding of the asset class has left it undervalued despite the prospects for growth.

Middle Child Syndrome: Misunderstood Risk in MLPs, Midstream

In addition to the misunderstanding of the relationship between MLPs and other areas of energy, there is a misunderstanding of the credit risk in the space.



Sources: Bloomberg, Alerian, Standard & Poors (as of 10/9/2017)

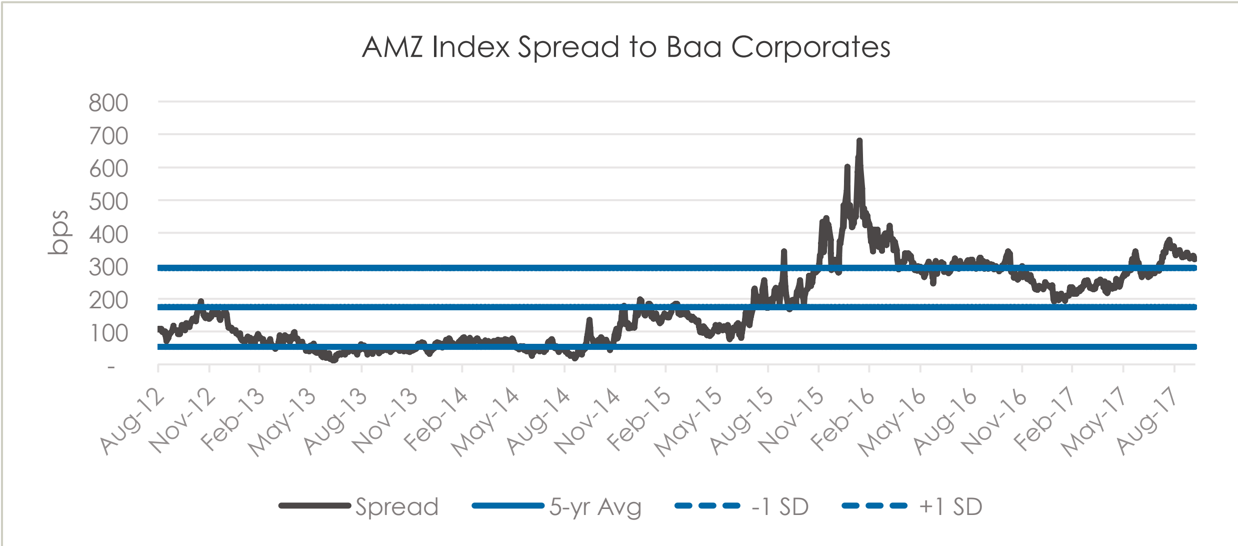
Some investors have raised concerns about cash flow sustainability in the wake of perceived counterparty credit risk. Looking at the credit quality makeup of counterparties as well as post-bankruptcy situations, it is apparent that these fears are overblown.

*Only **20%** of the AMZ index market cap is below investment grade – and nothing within that is rated below single-B*

For one, most contracts have remained in place after counterparty bankruptcies. Further, only 20% of the AMZ index market cap is rated below investment grade—and within that 20%, none has a rating below single-B.

Realistic Spread Compression Could Translate to Meaningful Price Upside

As MLPs continued to dislocate throughout the third quarter, yield spreads reached levels not seen since early-2016 when crude prices were flirting with $25 per barrel.

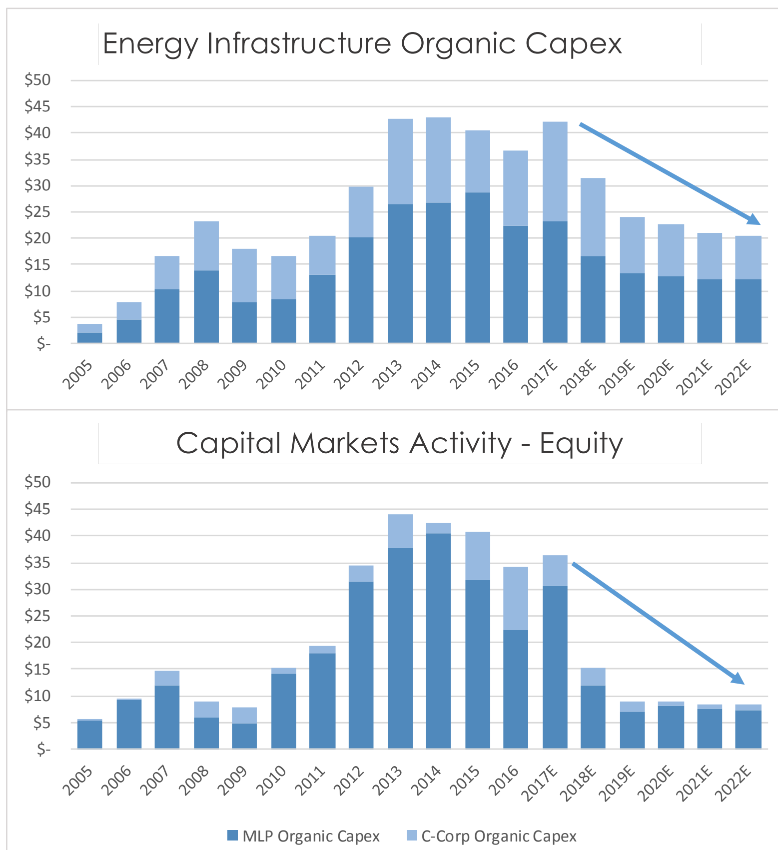


Source: Bloomberg, Moody's (as of 10/9/2017)

We believe spreads decreasing to the +1 standard deviation level would equate to notable price upside and total return in the Alerian MLP Index, while a decrease to the five-year average—spreads were approaching this level at the beginning of this year—would have a major impact.

Capex Catalysts

Further, as organic growth capex slows, we anticipate the need for MLPs to issue equity to decline. We believe this impending catalyst will remove an overhang on the sector.



Source: Wells Fargo

Investment Outlook & Opportunity

We believe that MLP performance is not reflective of the fundamentals and growth outlook for the asset class.

MLPs have been cast aside by much of the investment world and we believe that performance is not reflective of the fundamentals and growth outlook for the asset class. With the current health of the E&P sector and outlook for added strength emerging on the heels of steadily increasing shale-based crude and natural gas production, we anticipate what we believe to be the already sound fundamentals of the asset class to further improve. As a volume based business, these trends support the outlook and fundamental growth for MLPs.

Finding attractive, sustainable income is also top of mind for investors given the current rate environment. While realistic spread compression could result in meaningful price upside for the asset class, MLPs should continue to offer investors an attractive current yield.

Even without these catalysts and continued price stabilization bringing investors back to the asset class, the fundamentals around MLPs remain solid, and we see current opportunity within this corner of the energy landscape.

Risk Disclosures & Notes

Do not copy or distribute. The information herein is being provided in confidence and may not be reproduced or further disseminated without the permission of Highland Capital Management, L.P. ("Highland"). The information contained in this document is subject to change without notice. Model/target returns described herein have been prepared by the projected management team of Highland on the basis of estimates and assumptions about the performance of the company. Actual results may differ materially from these estimates. The above results are presented for illustrative purposes only and do not represent guaranteed results. Past performance does not guarantee future results.

This commentary is provided as general information only and is in no way intended as investment advice, investment research, a research report or a recommendation. Any decision to invest or take any other action with respect to the securities discussed in this commentary may involve risks not discussed herein and any such decisions should not be based solely on the information contained in this document. It should not be assumed that any securities discussed in this commentary will increase in value. Highland will not accept liability for any loss or damage, including, without limitation, any loss of profit that may arise directly or indirectly from use of or reliance on such information.

Statements in this communication may include forward-looking information and/or may be based on various assumptions. The forward-looking statements and other views or opinions expressed herein are made as of the date of this presentation. Actual future results or occurrences may differ significantly from those anticipated and there is no guarantee that any particular outcome will come to pass. The statements made herein are subject to change at any time. Highland disclaims any obligation to update or revise any statements or views expressed herein.

No representation or warranty is made concerning the completeness or accuracy of the information contained herein. Some or all of the information provided herein may be or be based on statements of opinion. In addition, certain information provided herein may be based on third-party sources, which information, although believed to be accurate, has not been independently verified.

Highland and/or certain of its affiliates and/or clients hold and may in the future, hold a financial interest in securities that are the same as or substantially similar to the securities discussed in this commentary. No claims are made as to the profitability of such financial interests, now, in the past or in the future and Highland and/or its clients may sell such financial interests at any time.

The information provided herein is not intended to be, nor should it be construed as an offer to sell or a solicitation of any offer to buy any securities. This commentary has not been reviewed or approved by any regulatory authority and has been prepared without regard to the individual financial circumstances or objectives of persons who may receive it. The appropriateness of a particular investment or strategy will depend on an investor's individual circumstances and objectives. Highland encourages any person considering any action relating to the securities discussed herein to seek the advice of a financial advisor.

The performance of the indices may be materially different from the individual performance attained by a specific investor. In addition, the investors holdings may differ significantly from the securities that comprise the indices. The indices have not been selected to represent an appropriate benchmark to compare an investor's performance, but rather are disclosed to allow for comparison of the investor's performance to that of certain well-known and widely recognized indices. Index returns assume reinvestment of dividends and other income. Indices are unmanaged and have no fees or costs. An investment cannot be made directly in an index.

ID#13538