

Master Limited Partnerships - A Primer

A Short Guide to Master Limited Partnerships and the S&P MLP Index

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- Master Limited Partnerships (MLPs) are limited partnerships that are publicly traded on a U.S. securities exchange. This combines the tradability of common stocks with the corporate structure of partnerships.
- The current size of the U.S. MLP market is over US\$ 100 billion.
- The majority of MLPs operate in the energy infrastructure space. The number of listed energy MLPs has increased by over 200% in the last seven years.
- Master Limited Partnerships generally offer stable yields that are higher than those of common stocks. This is useful for investors seeking high current income.
- MLPs have returns that have low correlations with stocks and bonds, making them good for portfolio diversification. Risk factors include regulatory risk and interest rate risk.
- The S&P MLP Index is designed to serve the investment community's need for an investable benchmark representing the MLP market. The index consists of leading, liquid energy MLPs trading on a major U.S. exchange.

Introduction to Master Limited Partnerships

What are Master Limited Partnerships (MLPs)?

Master Limited Partnerships (MLPs) are limited partnerships that are publicly traded on a U.S. securities exchange. The limited partnership structure results in favorable tax treatment by avoiding the corporate income tax. MLPs as an asset class originated in the 1980s through laws passed by Congress designed to encourage investment in energy and natural resources. Early partnerships that took advantage of these laws had mixed results. Many partnerships were taking advantage of tax avoidance to extend their scopes beyond those originally envisioned. In response to this, Congress strengthened regulations to ensure that an MLP must generate at least 90% of its income from qualified sources, most of which pertain to natural resources. As a result, the majority of MLPs in existence today operate in the energy infrastructure industry, although recent issues have included companies operating in a variety of different industries. This asset class has grown rapidly in recent years, with the number of listed energy MLPs roughly tripling since 2000.

What are the distinguishing characteristics of Master Limited Partnerships?

1. **Tax Treatment** - Since MLPs are structured as partnerships they do not pay corporate income taxes. Taxes are only paid when distributions are received, thus avoiding the double taxation faced by investors in corporations.
2. **Consistent Distributions** – MLPs face stringent provisions including the requirement to pay minimum quarterly distributions to limited partners, by contract. Thus, the distributions of MLPs are very predictable.
3. **Energy Infrastructure** – The majority of MLPs operate in the energy sector, particularly in energy infrastructure industries such as pipelines, which provide stable income streams. The performance of companies in the energy infrastructure industry is not highly correlated with the price of oil and other types of energy, but rather with the demand for energy. The demand for energy is far less volatile than commodity energy prices and generally increases steadily over time, resulting in steady, predictable cash flows for companies in these industries.

What are the similarities and differences between MLPs and LLCs (Limited Liability Corporations)?

- In general, MLPs and LLCs are considered as belonging to the same asset class. Both MLPs and LLCs enjoy the same tax treatment. They are non-taxable entities with a tax shield on distributions, thus avoiding the double taxation of corporate profits.
- There are two types of partners in an MLP structure, general partners and limited partners. The MLP is managed by the general partner. On the other hand, an LLC does not have a separate general partner. Limited partners have voting rights in an LLC but not in an MLP.
- The general partner in an MLP has what are called Incentive Distribution Rights (IDRs). IDRs are terms defined in the MLP partnership, which allow for the general partner to claim a higher proportion of incremental amounts of the distribution payments as these payments grow over specified levels. This is designed to provide general partners with a strong incentive to increase distributions, further enhancing the appeal of MLPs based on large, growing distributions. On the other hand, it raises the cost of equity for the MLP and can dilute the ownership claim of limited partners.

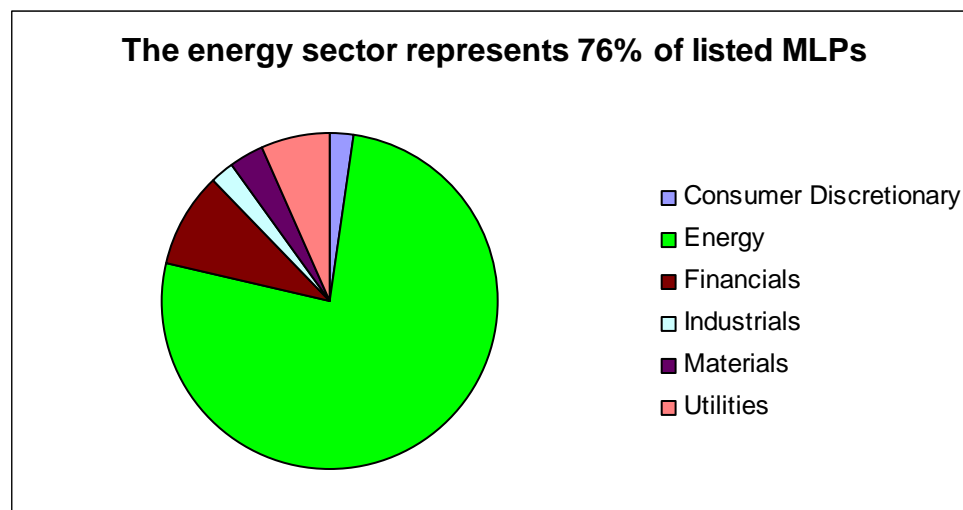
What are the risks of investing in Master Limited Partnerships?

- **Regulatory Risk** - One of the most attractive characteristics of MLPs is the tax treatment of this asset class. If MLPs were no longer able to pass through taxes to limited partners a large benefit of investing in MLPs would be removed. Also, the fees that pipelines are able to charge are highly regulated by the government resulting in additional regulatory risk.
- **Interest Rate Risk** - As with high-yielding equities, MLPs are often more appealing to investors at times of low interest rates, as this results in higher yields for MLPs relative to bonds and money market instruments. Increasing interest rates would result in lower relative yields versus other alternative assets.

What are the advantages of investing in Master Limited Partnerships?

- The partnership structure of Master Limited Partnerships results in favorable tax treatment due to the avoidance of double taxation.
- High, consistent distributions make MLPs an attractive asset class for investors looking for high yielding securities. Average yields have recently been in the 8% range.
- Historically, MLPs have been able to steadily increase their cash flows and, thus, distributions over time. High distribution growth provides MLPs an advantage over other high-yielding assets.
- MLPs have returns that have low correlations to both stocks and bonds. This makes them good for diversification in a stock/bond portfolio.
- Cash flows and distributions are relatively stable and immune to the business cycle.

What is the breakdown of Master Limited Partnerships by Sector?

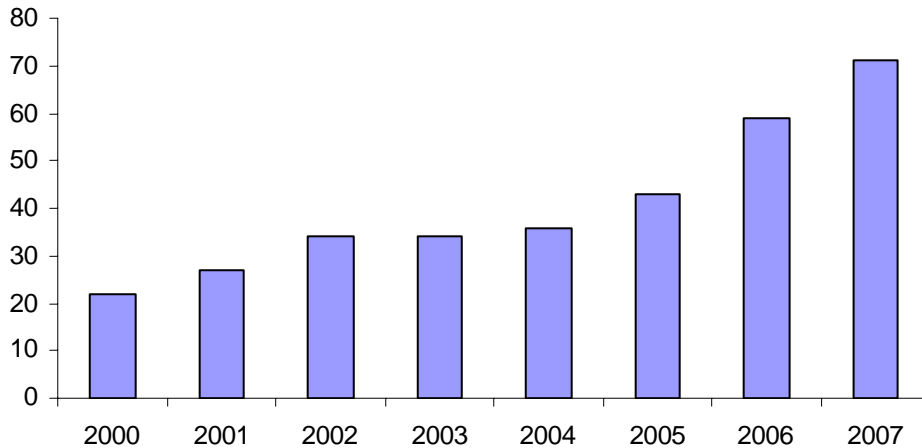


Sources: Standard & Poor's.

How big is the Master Limited Partnership market?

As of August 2008, the total market capitalization of Master Limited Partnerships was over US\$ 100 billion.

The Number Of Listed Energy MLPs Has Increased



Sources: Standard & Poor’s.

What is the return and volatility profile?

Master Limited Partnerships can complement stock and bond portfolios

	Bonds	Common Stocks	MLPs
Annualized Returns	4.51%	-0.75%	9.30%
Annualized Volatility	3.76%	14.78%	14.74%
Correlation	11.81%	39.67%	

Sources: Standard & Poor’s and Lehman Brothers. Figures are from July 31, 2001 through October 31, 2008. Common stocks refer to the S&P Composite 1500, bonds refer to the Lehman Brothers U.S. Aggregate and MLPs refer to the S&P MLP Index. Compound ROR and Standard Deviations are on an annualized basis.

Is investing in energy-related Master Limited Partnerships a proxy for investing in energy stocks or commodities?

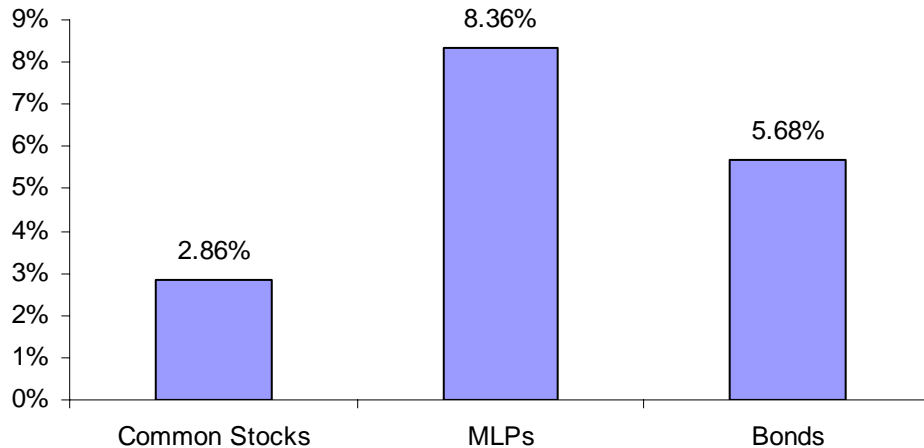
No. Income from Master Limited Partnerships is dependent primarily upon the demand for energy rather than on the price of oil and gas. As energy demand is much less volatile than energy prices the performance of MLPs is not highly correlated with the short-term price changes of oil and gas or with the performance of energy stocks. Over the last seven years the correlation between the S&P MLP Index and the S&P Composite 1500 Energy Sector Index has been only 36.39%. Also, over the same time period the correlation between the S&P MLP Index and spot oil prices, as measured using West Texas Intermediate Crude, has been only 19.76%.

	Energy Stocks	Crude Oil	MLPs
Compound ROR	10.76%	13.93%	9.30%
Standard Deviation	21.64%	32.49%	14.74%
Correlation	36.39%	19.76%	

Sources: Standard & Poor’s and Bloomberg. Figures are from July 31, 2001 through October 31, 2008. Energy stocks refer to the S&P Composite 1500 Energy Sector, Crude Oil refers to West Texas Intermediate Crude and MLPs refer to the S&P MLP Index. Compound ROR and Standard Deviations are on an annualized basis.

What are the yields of Master Limited Partnerships?

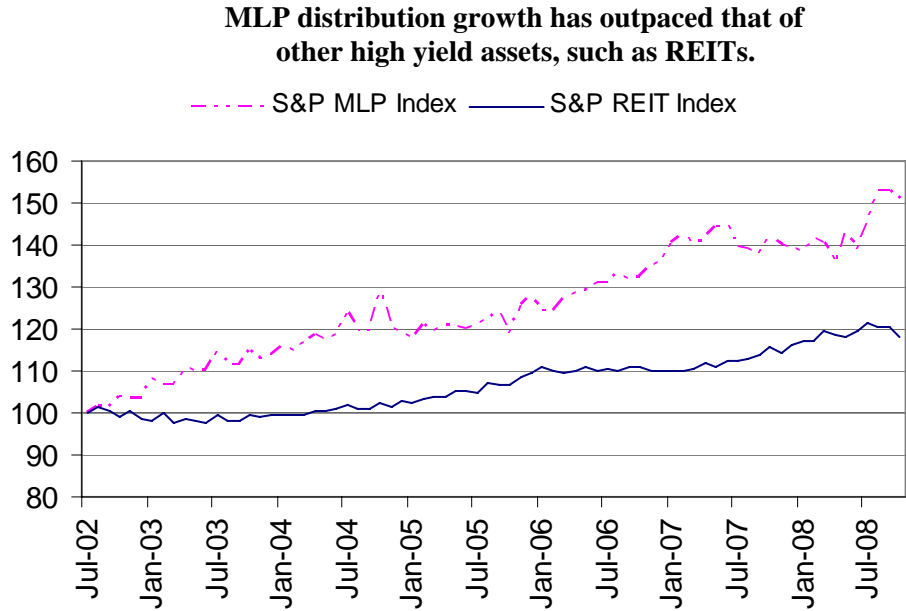
MLPs Have Attractive Yields Relative to Stocks & Bonds



Source: Standard & Poor’s, Lehman Brothers. Yields for common stocks are for the S&P Composite 1500, yields for bonds are for the Lehman U.S. Aggregate Index, yields for MLPs are for the S&P MLP Index. Data as of October 31, 2008.

How have distributions of Master Limited Partnerships grown over time?

Index dividends for the S&P MLP index have increased at an annualized rate of 6.44% over the last six years.



Source: Standard & Poor's. Data from July 31, 2002 through October 31, 2008. Indices rebased to July 31 2002 = 100.

The S&P MLP Index

What is the S&P MLP Index?

The S&P MLP Index is comprised of the largest Master Limited Partnerships trading on a major exchange in the United States, which meet specific investability requirements and operate in the energy industry.

How are constituents selected and weighted?

The index is calculated with a modified capitalization-weighted scheme based on the following principles:

- At each rebalancing all Master Limited Partnerships trading on the NASDAQ, NYSE or AMEX exchanges are screened based on market capitalization and liquidity. All MLPs meeting these eligibility requirements are included in the index.
- Constituents are market capitalization-weighted with adjustments being made, if necessary, so that no single stock has a weight of more than 15% in the Index.

How many constituents are there in the index?

The index does not have a set number of constituents. Rather, the number of constituents floats based on how many companies are eligible at each rebalancing. As of October 31, 2008, the index had 42 constituents.

What types of Master Limited Partnerships assets are included in the index?

The S&P MLP Index focuses on energy companies. MLPs must be classified in either the GICS Energy Sector or the GICS Gas Utilities Industry to be considered for inclusion in the index.

How do the constituents break down as far as size?

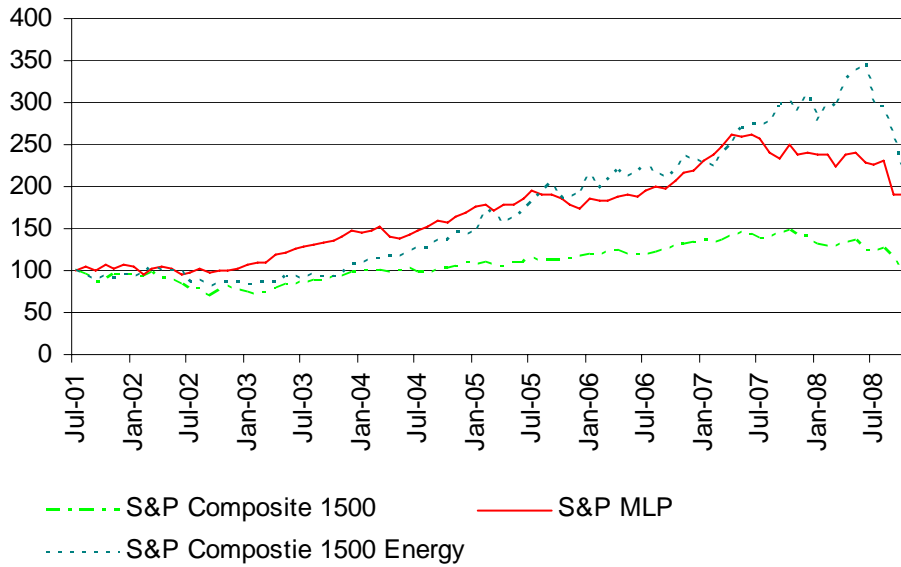
The weighted average market capitalization of index constituents was US\$ 4.2 billion as of October 31, 2008 and ranges from US\$ 67 million to US\$ 10.6 billion. There is, however, no specific targeting for size distribution in the index. Therefore, this measurement will change over time.

How does this index compare to the U.S. equity market and the U.S. energy sector?

	S&P MLP	S&P Composite 1500	S&P Composite 1500 Energy
Compound ROR	9.30%	-0.75%	10.74%
Standard Deviation	14.74%	14.78%	21.64%
Maximum Drawdown	-27.76%	-35.99%	-39.86%
Sharpe Ratio	14.59%	-4.35%	13.34%

Source: Standard & Poor's. Figures are from July 31, 2001 through October 31, 2008. Compound ROR and Standard Deviations are on an annualized basis.

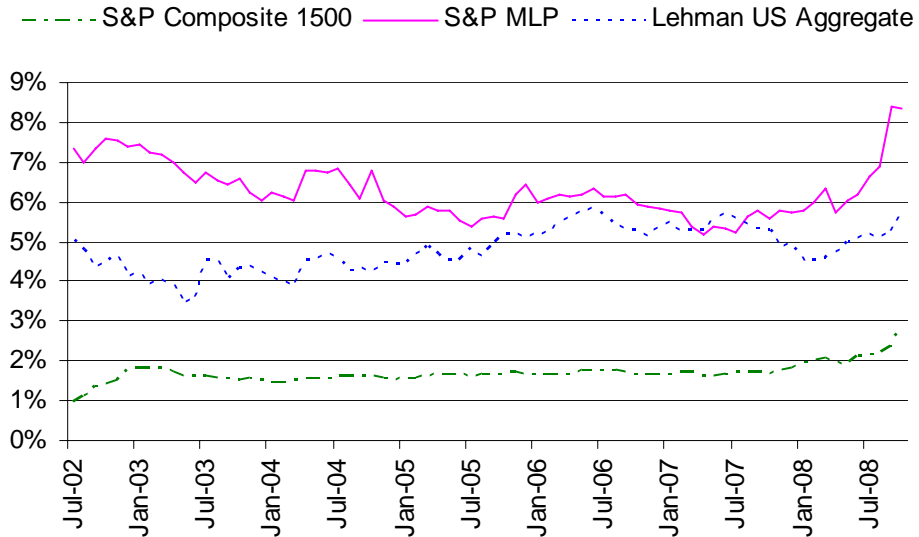
Index Performance



Source: Standard & Poor's. Data is from July 31, 2001 to October 31, 2008. Indices rebased to July 31 2001 = 100.

How has the yield of the index changed over time?

The yield of the MLP index has ranged between 5% and 8% over the last six years.



Source: Standard & Poor's, Lehman Brothers.

How often are constituents added and removed from the index?

The index is reviewed and rebalanced once a year, after the close of the third Friday in July. Throughout the year, constituents may be deleted due to corporate events such as mergers, acquisitions, takeovers or delistings. There are no intra year additions to the index. The complete methodology is available on the web at www.indices.standardandpoors.com.

What are the ticker symbols for the index?

Index	Bloomberg	Reuters
S&P MLP Index	SPMLP	.SPMLP
S&P MLP Total Return Index	SPMLPT	.SPMLPT

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