Stock and Energy Market Environment

Stocks have been hovering near correction territory since late October, driven by comments from Fed Chair Jerome Powell, and fears of a China economic slowdown related to current and pending tariffs. Since climbing to over $75 in late September, WTI oil futures have traded down more than 30%[1]. The sharp decline can be attributed to normal seasonal weakness, over production by China, unexpected embargo waivers for Iranian oil exports, overall declines in the stock market and associated fears over declining demand.

We believe the stock and oil markets are likely to stabilize and move higher over the next month as we expect the Fed to moderate its stance based on weaker global growth, tightening financial conditions, and moderation in housing and investment activity. In addition, the Fed could acknowledge that inflation pressures have moderated due to lower oil prices and a strong dollar. We expect there to be some progress on China/US trade negotiations that delay the additional $250 billion of tariffs that have been proposed. Finally, we expect Saudi Arabia to moderate production, even if there is no formal OPEC cut to production quotas.

MLP Market

MLPs have traded down more than 15% from their highs with the market down 9% and energy stocks down 18%[2]. At the same time Industry fundamentals remain strong with wide transportation differentials demonstrating tightness in the midstream market. Production has continued to surprise to the upside and 2019 E&P production expectations are likely to remain stable despite lower oil prices. Importantly, fundamentals have been reflected in MLP earnings reports with the average company in the AMZI Index exceeding 3Q'18 expectations by over 5%[3].

We believe the industry has completed the cycle of restructurings and distribution cuts that resulted in 12 companies in the Alerian Index reducing their effective distributions in 2018. Also, there are four pending acquisitions of MLPs which we expect to reduce the amount of MLP equity by over $26 billion[1]. With these restructurings behind us and a favorable operating environment, MLP yields remain elevated at 8%[3] and we anticipate sector distribution growth in 2019. As an additional tailwind, historically there has been a strong January effect where MLPs outperform the market. Since 2010 the AMZI Index has averaged a 1.5% total return in January versus 0.5% returned by the S&P500[4]. Consequently, dollar cost averaging during December can be advantageous.

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[1] Compiled using Bloomberg data as of 11/26/2018

[2] 52 week high through 11/26/2018 using Bloomberg. "MLP", "Market" and "Energy" refer to the AMZIX Index, SPX Index and the IXE Index, respectively

[3] Compiled using Bloomberg consensus data

[4] Compiled using Bloomberg data from 12/31/2010 – 11/26/2018

DISCLOSURE

Fund Risks

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