REPRINTED FROM MAY 8, 2017

THE WALL STREET TRANSCRIPT
Connecting Market Leaders with Investors

Seeking Value and Growth at a Reasonable Price in a High-Valuation Environment

GREGG T. ABELLA, AIF, is a Co-Principal and Portfolio Manager at Investment Partners Asset Management. Earlier, he worked at Chubb & Son in the International Division of the Surety Credit Department handling Latin America and Europe. He later established and managed the Guaranty Department for the subsidiary, Chubb do Brasil, in Sao Paulo, Brazil. He graduated from Bowdoin College with degrees in economics and Spanish.

SECTOR — GENERAL INVESTING

TWST: Could you tell me a little bit about the firm?

Mr. Abella: Sure. We are an independent registered investment adviser located in central New Jersey. We have a high-touch practice, managing assets for mass-affluent and high net worth individuals, as well as for wealth-transfer vehicles, corporations and not-for-profits. We have a particular preference for value and growth at a reasonable price, and our staff all have prior business experience in other industries before working in the investment management industry. So we have expertise in credit and lending, technology, health care and biotech, energy, basic materials, and those are sectors that we tend to follow.

TWST: And do you have a unique investment philosophy?

Mr. Abella: Yes, we have a preference for value and growth at a reasonable price. We'll search for value, and we prefer absolute value, but in this environment, with equities trading at high valuations, we are struggling to find things at absolute values, but there are still some relative values out there.

TWST: And when you use those terms, absolute value and relative value, what do you mean by those?

Mr. Abella: Companies that trade at very low multiples of book, very low multiples of cash or cash flow, dividend-payment capacity that is far in excess of what the market might be perceiving, those are the sort of metrics that we find attractive. But in managing clients' assets, while we stick to our knitting and use the strategies that we employ, when we are allocating a whole account, we will use outside management to round out the portfolio through closed-end funds, ETFs, and open-end funds.

TWST: And why have you found that strategy to be successful?

Mr. Abella: By using our particular expertise and then rounding it out with other managers, we feel like there is no monopoly on brains out there. So while we are big believers in value and growth at a reasonable price, there are other managers who do things that we simply don't do, whether that's emerging markets, or high yield, or international investing. We found there are some very, very compelling funds in the closed-end funds, ETFs, and open-end fund space that can really diversify a client's portfolio and achieve their objectives, while we do the piece that we are familiar with, which is value and growth at a reasonable price.

TWST: Did you want to talk about some specific companies or funds?

Mr. Abella: I'll start with the caveat that not all of these investments might be appropriate for everyone and anyone who is reading this piece should seek their own adviser to help them decide whether the things I'm going to talk about are appropriate for them or not. But in our specific screening process, we look for companies, again, that have strong cash flow and future dividend-payment capacity.

And one company that we own a little bit of here and are looking to maybe buy more of it — if it trades lower — would be **Kinder Morgan** (NYSE:KMI). **Kinder Morgan** is previously a high flyer in the MLP space. They subsequently converted into a C-Corporation, but it is one of the larger, if not the largest midstream and downstream energy companies, meaning oil and gas pipelines and storage.

In January, the company held an analyst day to lay out its plans for the coming year, and while the energy sector has been a real downer for the last two and half years, the company is using this opportunity to use its own internal cash flow to pay down debt and rightsize its balance sheet. It is doing all the right things to maintain its dividend-paying capacity and remain an investment-grade credit. And we think that over time, that strategy will pay off and that the ability for them to pay a better dividend going forward, in the years to come, will probably start to

become evident in the later part of this year or early part of next year.

TWST: And I understand they are thinking about doing a pipeline project for moving natural gas.

Mr. Abella: They have many important projects in their backlog. An extremely significant one is what's called the Trans Mountain pipeline expansion, which has received Canadian federal government approval, British Columbia provincial approval, and has met environmental assessment requirements. So the hope is that they will be able to monetize that asset in the future, and then use that as means to reduce leverage and increase their cash flow going forward.

The company is the largest pipeline company in the country. So the dividend-payment capacity that we think that they have looks solid if natural gas and oil prices were to stabilize. We think their cash flow should more than cover their dividend going forward. And then, hopefully, by the end of the year, they will be in a position to substantially increase that dividend, hoping that some of the internal capex projects that they have will come to fruition. Then, they can start to focus on using that internal cash flow and start turning that distributable cash back to shareholders in the form of the increased dividend.

TWST: So the main benefit from this pipeline is increased dividends, or are there some others too?

Mr. Abella: There are so many projects that they are working on at any given time. They made a strategic decision — I guess it was at the end of 2015 — to use what would have been distributable cash flow, and instead of tapping the capital markets to continue to fund their growth, that they would use their distributable cash flow to fund operations and fund capex at least through last year, and now, we are on year two of that effort. So I'd say, going forward, we are getting toward the end of their need to have to continue to do that. They have a call at the end of this year to talk about their dividend-payment capacity, and we are hoping that, at that time, they are going to say where they stand regarding cash flow and also the forward guidance to let investors know at what point they can start using more of their distributable cash flow in the form of dividends.

TWST: And do you think they are being helped by the policies of the Trump administration and maybe by policies of some other governments?

Mr. Abella: I think it doesn't hurt, certainly doesn't hurt. But while they are helped by the current regulatory environment, as we talk on April 21, I think there are a number of risks here. Among them is that there is still a glut of oil and natural gas. The technology to take these commodities out of the ground has gotten so much better, so much faster than I think a lot of people anticipated. We are still awash in oil, and natural gas prices, I think, are going to be range-bound for many years to come.

They factor that into their business model. They have internal controls that every dollar down on oil impacts distributable cash flow by a certain amount, and every $0.10 down on natural gas impacts their distributable cash flow by a certain amount, and they know what those numbers are. So the risks here are that we have oil and gas that trade at these levels or even substantially lower for many years to come. But I think by being very responsible about their balance-sheet management, they have done a good job making sure that the company remains stable and that it remains an investment-grade credit risk. I think their ability to pay at least the current amount in dividend is probably secure, but the hope is that if the commodity prices remain at these levels or probably even higher, going forward, they will have very stable cash flow to increase capital distribution to investors.

If you look back in history, their revenue levels, even in 2013 when commodity prices were much higher, were not too much different than they are now, and their gross profit is about 50% of their sales. And their cash flow has remained relatively stable, even through all of this. As a pipeline and storage company, they have commodity risk, but they don't have it to the same extent, obviously, that an upstream exploration and production company does. Having said that, lower prices don't help them necessarily.

TWST: And do you want to talk about another company or fund?

Mr. Abella: Sure. One of the companies that we are also looking at, and this is not a C-Corporation business, but rather, it is in the form of an LP, is **Blackstone** (NYSE:BX), which is an investment management firm that specializes in alternative investments, specifically private equity, real estate, hedge funds, and investing in distressed and specialty credits. So people probably remember this, but they went public almost 10 years ago, almost exactly 10 years ago, and it was a hot IPO back in the day that people were clamoring for. Well, 10 years later, it is trading at about the same price, and that's one of the things we like to look for. When something was a hot investment years ago but subsequently gets ignored by the Street, then it may be time to take a good look as to whether or not this is a company that we should start to put on our screens.

Highlights

Gregg T. Abella discusses Investment Partners Asset Management. The firm has a preference for value and growth at a reasonable price. In addition, the firm tends to follow and has expertise in the sectors of credit and lending, technology, health care and biotech, energy and basic materials. When searching for value, Mr. Abella prefers absolute value, but in the current high-valuation environment, he is looking at relative values for investments The metrics he finds attractive in a company include trading at a low multiple to book, low multiples of cash and a dividend-payment capacity in excess of what the market perceives. To round out and diversify a client's portfolio, Mr. Abella will look to outside management for closed-end funds, ETFs and open-end funds.
Companies discussed: Kinder Morgan (NYSE:KMI) and Blackstone Group LP (NYSE:BX).

"But I think by being very responsible about their balance-sheet management, they have done a good job making sure that the company remains stable and that it remains an investment-grade credit risk. I think their ability to pay at least the current amount in dividend is probably secure."

So **Blackstone** is an interesting company. The investment thesis here is one more of forward p/e and dividend. Again, we like to get paid while we wait on an investment. So a year ago, private equity, real estate, hedge funds and other alternative investment strategies were out of favor — not only just with high net worth individuals, but also institutions. Pensions have been getting out of these sorts of investments en masse because of the criticisms of the returns and the fees and the rest.

But as we get to be very mature in traditional asset classes, we are starting to see, and I think we are going to continue to see, that in order to meet expectations for future return, some of these institutions and high net worth individuals are starting to look at these alternative strategies again. If they feel that, with the forward p/e on the S&P approaching 20, the excess returns you will get in the traditional stock market are probably at a peak, it might be time to look at others strategies.

Blackstone is seeing that dynamic in this quarter's results. The assets under supervision have gone up, and all of their strategies have had increased inflows. The revenues, just on management fees, are up about 5%, but the carried interest and performance compensation they have gotten on some of their funds have gone way up. So this is probably a story that, as the traditional investment vehicles out there mature, more and more capital, I believe, will flow into alternative strategies, and **Blackstone** should be a beneficiary of that.

TWST: And what should investors know about some of their more recent approaches, where they put their own money?

Mr. Abella: Well, they invest in their own funds. So indirectly, you'll end up owning some of their funds, because through the carried interest and performance, they will end up owning the very strategies that they are invested in. But that represents an opportunity and a little bit of a risk, because as you were mentioning about the current administration, and whether that's a positive or negative for a particular investment, as tax reform comes to the fore, I think you're going to see some pressure on the private equity firms' ability to use carried interest income at long-term capital gains tax rates.

So that could impact a company like this pretty substantially. I think that from a tax standpoint that would probably be the case, but I'm not sure that's going to have a dramatic impact over the long term, as I think they are going to get a lot of capital inflows. Hopefully, the inflows would make up for the increased tax exposure that they might have.

TWST: And did you want to mention a third company or fund?

Mr. Abella: So this is actually similar thematically. Hedge fund strategies, I think, have gotten a very bad rap. Some of that might be deserved because the performance has not been there the way it was in the mid-2000s. With very low levels of volatility, and traditional asset classes and passive strategies working, alternative investing has been out of favor paying a two-and-twenty fee for hedge funds that have underperformed broader indexes. The very nature of a hedge fund though is, as its name suggests, to hedge. So there is a place in some client portfolios to use hedge fund replication strategies as a way to dampen risk or get an absolute return when markets are more volatile or even go the other way.

So one of the liquid alternatives that we found very interesting recently is a fund called the **Goldman Sachs Absolute Return Tracker** (NASDAQ:GJRTX). There are a number of funds that have been launched in this space that are considered daily liquid alt hedge fund replicators, which use a variety of liquid strategies to try to replicate the returns of hedge funds. This one in particular attempts to replicate the return by analyzing about 2,000 hedge funds and then uses liquid strategies with exchange-traded funds, index futures, commodity futures and options to try to get the same or similar type of absolute return.

Their initial strategy was one that was evaluated once a month and then reviewed annually. Then, they decided a couple of years ago to make the process a little more dynamic and have interperiod adjustments, and their performance in the last couple of years relative to the multialternative category has improved since then. So this is not a fund or strategy that you're going to make a ton of money with.

"Well, 10 years later, it is trading at about the same price, and that's one of the things we like to look for. When something was a hot investment years ago but subsequently gets ignored by the Street, then it may be time to take a good look as to whether or not this is a company that we should start to put on our screens."

What it strives to do is bat for singles and doubles, and when I say that, I mean, like singles and doubles in baseball terms, not get double on your money. It tries to make money regardless of market direction, and it serves as ballast for a small, very moderate portion of a client's portfolio as a hedge. And by using a strategy like this in a liquid form, with an expense ratio of little more than 115 basis points, it's a lot cheaper than the two-and-twenty model that you would need to be in a hedge fund, plus you have daily liquidity.

So again, this is not something to make a whole portfolio out of. But you could use it as ballast when you have a very, very diversified portfolio with traditional asset classes like core equity, core fixed income and strategic satellites. Then, you would add this as sort of a counterbalance to dampen volatility. So as the markets trend up, and we feel a little anxious about valuation, this is a good tool in the toolbox to get access to strategies that have traditionally been reserved for very, very high net worth individuals and institutions.

TWST: So this might make sense for both the retail investor as well as an institutional investor as part of their overall portfolio?

Mr. Abella: Yes, it could. These are strategies that traditionally have been reserved for institutions and for very high net worth individuals and wealth transfer vehicles and very sophisticated investors, but it has a place even for a retail investor that understands what the strategy is, and intends to use it as a tool to try to get a little bit of return in a down market potentially and not have the same sort of volatility that you might have otherwise. But again, it's not something that you would use for an entire portfolio. It's just a tool in the toolbox for a relatively moderate to low percentage of the total just to counterbalance volatility that might occur in more traditional asset classes.

TWST: And changing gears a bit, when you speak with investors and clients now, what are some of their concerns that they have as they look at 2017 and beyond?

Mr. Abella: Well, the main concern in particular for clients coming in with fresh cash is: Can I expect to get the same sort of returns going forward that the market has given us over the past eight and a half years? And as value guys and growth-at-reasonable-price guys, we are

looking at the bell curve of possibilities right now. On one end of the curve, you have that everything works out as expected in a perfect world. You have tax reform and an infrastructure program that put a lot of people to work, you get GDP growth in excess of 2%, and you keep low rates. But that's where we believe the market is factoring in all of those attributes as if they were certain.

On the other side of the bell curve with a fat tail is that public policy is a disappointment, that there are conflicts in the form of trade wars and actual wars. We don't believe the markets are currently pricing in that sort of risk appropriately, and so the clients that come in are, more so than in the past, more worried about the fat tails on the negative end of the curve, and less concerned about, "If I put money into the market, I'm going to make double-digit, high-teens sort of returns going forward." We just don't see that happening in the U.S. markets because they're so mature.

So a main concern people have is that, if they have an investment goal or intergenerational transfer goal that might be occurring five to 10 years in the future, they can't budget for that with the sort of traditional stock-market returns of high-single-digit or low-teens going forward. And I would posit that I think the easy money has been made, and now, it's going to be much tougher and will require a lot more diversification than in the past along with more sophisticated tools in the toolbox to even get sort of mid-single-digit returns on an annualized basis.

TWST: Thank you. (ES)

GREGG T. ABELLA, AIF
Co-Principal & Portfolio Manager
Investment Partners Asset Management
10 Station Place
Metuchen, NJ 08840
(732) 205-0391
(732) 205-0395 — FAX
www.investmentpartners.com

Disclosure: The views expressed in this article are those of the interviewee and not necessarily those of Investment Partners Group, its subsidiaries, affiliates, and/or employees thereof - including Investment Partners Asset Management ("IPAM"). Nothing in this article should be considered a recommendation, solicitation, or offer by Investment Partners Group, its subsidiaries, affiliates, and/or employees thereof - including IPAM - to buy or sell any securities, futures, options or other financial instrument or to provide any investment advice or service. Nor should this article be considered a complete analysis of any company, fund, industry, economy, or market. Investments or strategies referenced in this article may be subject to a high degree of risk, may not be suitable for all investors, and may not develop as anticipated or expressed. Past results are not a guarantee of future performance. As of the writing of this article, some clients and affiliates of IPAM own investments discussed herein, however, due to various subsequent factors, including changing market conditions, future ownership of such investments may change materially.

© 2017 The Wall Street Transcript, 622 3rd Avenue, New York, NY 10017
Tel: (212) 952-7400 • Fax: (212) 668-9842 • Website: www.twst.com