Another way investors can play the US shale boom

By Javier E. David - April 3, 2014

A high pressure gas line crosses over a canal in an oil field over the Monterey Shale formation where gas and oil extraction using hydraulic fracturing, or fracking, is on the verge of a boom on March 23, 2014 near Lost Hills, Calif.

The next phase of U.S. energy independence has arrived—in the form of infrastructure construction fueled by billions in private capital.

With the U.S. turning out near-record amounts of oil and natural gas, a frequent complaint among producers has been the lack of pipelines needed to send fuel to hungry markets, both domestic and abroad. Filling that demand are master limited partnerships (MLPs), publicly traded investment vehicles that combine debt and equity. MLPs are attracting billions in capital commitments from private equity giants like BlackRock and Blackstone.

In a study last month, the Interstate Natural Gas Association of America said North America's shale revolution will require a cumulative $30-billion-a-year in investment through 2035—a figure other energy watchers say actually may be conservative.

energy sector feeds manufacturing, may overtake it

The once small and sleepy MLP market has soared in value. Its cumulative market capitalization of less than $50 billion in 2003 is now more than $450 billion, said Adam Karpf, a portfolio manager for MLP strategies at Atlantic Trust, which has $24 billion in assets under management.

Soaring shale production is feeding "rapid growth in the industry," Karpf said. "MLPs are better able to handle capital spending requirements for U.S. industry. It's no longer a sleepy industry."

North Dakota's flare for capturing energy.

Gov. Jack Dalrymple, R-N.D., explains how his state is attempting to improve natural gas production by capturing more than a third of the product that burns away.

MLP prices have risen accordingly. For instance, in 2009—the start of the U.S. energy boom—energy MLP Enterprise Product Partners traded under $20. On Thursday, it traded above $70, just shy of a record high and was up more than 18 percent this year.

The natural gas association estimates that between Canada and U.S. shale plays, at least $2.5 billion per year through 2035 will be needed to build needed nat gas infrastructure, with an additional $12.4 billion dedicated to crude oil pipelines.

The American Petroleum Institute, an industry trade group, puts oil and gas infrastructure needs at a larger $94 billion per year for the next 12 years.

In an interview, Seth Appel, co-head of energy investment banking at MLV & Co., estimated that the MLP sector will spend at least $40 billion per year.

A big reason for that, he said, is the growing realization that rails and trucks aren't sufficient to meet demand.

"You have these newer shale developments that are completely underserved by legacy pipeline capacity," said Appel, who helped put together $5.5 billion worth of energy deals in 2013. "Over 70 percent of the crude produced in the Bakken [North Dakota] was transported out of region by rail, due to insufficient pipeline capacity."

LNG exports feed interest

The domestic production growth spurt, and the prospect of the U.S. becoming an energy exporter, has pried open the door more for MLPs. The approval of five liquefied natural gas export terminals in the last year is triggering a flurry of new investment, such as $965 million that Blackstone has invested across six different energy partnerships.

The private equity giant plans to spend $2 billion on an MLP that Cheniere Energy Partners will use to construct an LNG terminal in Sabine Pass, La. Dominion Resources–a utility owner whose stock has more than tripled since 2009, will form its own MLP that will partly fund the Cove Point LNG plant in Maryland.

Read MoreLouisiana terminal gets OK to export natgas

The investments are of course not without risks. Energy projects often run into thickets of political resistance, one of the few things that most observers say could impede growth in MLPs. For instance, the Keystone XL pipeline remains mired in regulatory limbo, with no immediate resolution in sight.

But one of the most attractive features of an MLP is its tax-friendly structure, and the fact that MLPs "are isolated from commodity price risk," said Jay Jacobs, research analyst at Global X, which has three energy MLPs with more than $169 million in total assets.

Because pipeline operators "are compensated based on amount of what they transport, not the value … MLPs will stand to benefit as U.S. moves to energy independence," he said.