SPOTLIGHT

A Joint Venture by
RBN Energy and East Daley Capital

DCP Midstream Partners

We Get Back Up Again

- **DCP Midstream, general partner of DCP Midstream Partners (DPM) is one of the largest gas processors, NGL producers and NGL marketers in the U.S.**
- **The company has a large exposure to the Eagle Ford Shale play in South Texas, which is experiencing a significant decline in oil and gas production, relative to other shale plays. Net income from DPMs Eagle Ford Natural Gas Services (NGS) unit could decline from $157 million in 2014 down to $25 million in 2017.**
- **DPM's NGS East Texas and Other Consolidated NGS businesses could also experience steep declines**
- **These declines are likely to be partially offset by DPMs operations in the DJ Basin and their interest in the offshore Gulf of Mexico Discovery System.**
- **Also offsetting declines in the NGS businesses are the company's NGL Logistics business, which are likely to provide solid growth in profits in future years, driven primarily by DPM's interest in jointly owned NGL pipelines (Sand Hills, Southern Hills, & Front Range) and solid performance from DPM's Marysville LPG storage unit.**
- **The Company's Propane Logistics business serves a stable demand market but its small size is unlikely to make an impact on total company performance.**

DCP Midstream Partners, LP (DPM) is a master limited partnership (MLP) which owns and operates a diversified portfolio of midstream energy assets. Its general partner is DCP Midstream, LLC, a 50/50 joint venture of Phillips 66 and Spectra Energy Corp. DPM gathers, processes, transports, and stores natural gas; fractionates, transports and stores natural gas liquids (NGLs) and is a wholesale propane marketer. The company primarily operates in the Gulf Coast markets but also has extensive assets in the Rocky Mountain and Mid-Continent regions.

Similar to most MLPs, DPM's share price has declined by more than 50% over the past year. Although most of DPM revenues are not directly impacted by energy commodity prices, reductions in drilling activity, production declines and narrowing price differentials all have negative implications for DPM and other midstream companies in the U.S. In the future, DPM will benefit from its strong fee based businesses and it is moving to increase the amount of its fee based revenues.

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DPM's level of success will be dependent on how well it navigates todays challenging energy markets. This report examines DPM's prospects based on a fundamental analysis of DPM's businesses, examining each piece of the company's operations through a robust bottoms-up assessment, including throughput, volumes, prices, and contract structures. This analysis is summarized into DPM's three operating divisions: Natural Gas Services (NGS), NGL Logistics (NGL) and Propane Logistics (PL).

1.1 Fundamental Analysis Highlights

Most of DPM's net income is derived from the natural gas processing and NGL markets and that is expected to continue into the foreseeable future. DPM's NGL Logistics business, via its pipelines assets, is the company's growth engine, leveraging its strength in Gulf Coast, Rocky Mountain and Mid-Continent markets. Much of that growth is due to a series of key investments DPM made over the past few years in the minority interests of several NGL pipeline companies. The most prominent among these is a 33.3% interest in the Sand Hills Pipeline that transports raw mix (Y-grade) NGLs from the Eagle Ford Shale (South Texas) and the Permian Basin (West Texas and New Mexico) to Mont Belvieu. Along with other strong performing jointly owned NGL pipeline assets including the Southern Hills and Front Range systems, the NGL Logistics segment net profit is expected to reach $240 million in 2017 from $121 million in 2014.

DPM's Natural Gas Services segment is expected to be weak, primarily due to very difficult market conditions in two of the company's most significant operating areas – the Eagle Ford Shale and East Texas. The bright spots in this segment are the Denver-Julesburg (DJ) Basin System (Northeast Colorado and Southeast Wyoming) and its 40% investment in Discovery Producer Services, LLC. The DJ Basin System is expected to benefit from increasing production from this basin. Discovery Producer Services is a natural gas gathering and processing system servicing the shelf and deep-water areas of the eastern Gulf of Mexico. Its primary asset is the Keathley Canyon Connector, a natural gas gathering pipeline serving the Keathley Canyon, Walker Ridge and Green Canyon areas in the Gulf of Mexico. Earnings for the Natural Gas Services segment peaked in 2014 at $469 million, and we expect earnings to be slashed by more than half in 2015 due to lower commodity prices and system impairment charges. Segment earnings are expected to continue declining in 2016 and 2017.

Net income during 2015 was impacted by goodwill impairments of $87 million year-to-date 3Q/15 in the Natural Gas Services segment, which were associated with the Piceance (Collbran), Michigan, and Southeast Texas assets. This analysis does not imply any impairments in the forecast, and there is a zero balance for goodwill in Natural Gas Services after the 2015 impairments. The other two reporting segments, NGL Logistics and Propane Logistics, have a combined $72 million balance of goodwill as of 3Q/15.

The outlook implied by this analysis suggests that DPMs net income will increase from $226 million in 2015 to $269 million in 2017, a 20% gain. The NGL Logistics segment will be the prime mover of net income for DPM, which may increase from $174 million in 2015 to $240 million in 2017. The Natural Gas Services segment earnings are expected to be flat in the near future reaching $182 million in 2017, about $1 million less than its 2015 net income. The Propane Logistics business will provide a steady stream of earnings with possible upside during periods of cold weather in its end use markets.

1.2 DCP Initiatives

DCP Midstream Partners is responding to today's difficult market environment through a number of initiatives. In its Natural Gas Services segment, the company has struggled from the recent collapse in oil prices as earnings and cash flow have been slashed due to the company's reliance on gas processing contracts with commodity price exposure. To address this situation, the company is transitioning its contract portfolio away from commodity indexed agreements and further down the fixed fee path. The company estimates 68% of its contract portfolio will be fee based in 2016. If successful, this would take a significant level of commodity price risk out of the company's Natural Gas Services business, adding more stability to cash flow and earnings streams.

DCP Midstream Partners is highly levered to some marginal oil and gas producing basins primarily the Eagle Ford Shale. If current low crude oil prices are sustained, drilling and completion activity could further slow, eventually reducing crude oil, natural gas and NGL production. Recently, Pioneer Natural Resources was the latest producer to suspend or reduce drilling in the Eagle Ford due to poor economics. Reductions in Eagle Ford volumes not only impact DPMs Natural Gas Services segment, but also impact its pipelines and fractionators that rely on Eagle Ford volumes.

DPM will rely on continued strong volume growth from the DJ basin to offset volumes lost in the Eagle Ford Shale, East Texas and other producing areas hit hard by low oil and gas prices. Although the DJ basin has also experienced these low prices, a fortunate combination of factors, including relatively attractive break-even prices have supported drilling in the play.

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2.1 What is Spotlight?

Spotlight reports provide a deep dive into the fundamentals that shape the outlook for midstream energy companies. In each report we “Spotlight” a midstream energy firm, usually one operating within an MLP structure. Our goal is to provide a comprehensive, fundamental based view of our Spotlight companies based on a bottoms-up analysis of their assets and operations. We tear apart their asset structure to reveal what volumes are flowing, what rates are (and can be) charged, how they are exposed to commodity price risk, how their assets fit together, and what aspects of their operations provide competitive advantages in today’s extremely volatile energy marketplace. This report, covering DCP Midstream Partners is the second edition of the Spotlight report series. The first edition covering ONEOK was published in December 2015.

Spotlight is a joint venture of RBN Energy, LLC and East Daley Capital Advisors, Inc. We have joined together with the support of Oil & Gas Financial Analytics, LLC to provide a comprehensive, detailed insight into the companies we select for our analysis. We use publically available data, combined with the deep experience of our combined teams to get to the answers that can be overlooked in the more high-level assessments that are in the marketplace today. Instead of such a high-level approach, we get into the micro-level detail, integrating fundamentals data, market data and company data in a comprehensive model that provides a clear picture of the company and its prospects.

As with all energy fundamental analysis, Spotlight reports rely on estimates and approximations of volumes, throughputs and fees. No non-public data from the subject company or any other source has been used in the preparation of this report.

2.2 How can I get Spotlight?

Spotlight is available to RBN Backstage Pass subscribers. Non-subscribers may purchase individual company Spotlight reports separately. For more information about Spotlight, go to rbnenergy.com/spotlight.