

Tortoise QuickTake Podcast

April 24, 2017

Welcome to the Tortoise QuickTake podcast. Thank you for joining us. Today, a senior member of Tortoise provides a timely update on trending topics in the market.

Thanks for joining us today on the Tortoise Quick Take Podcast. I'm James Mick, Managing Director and Portfolio Manager with Tortoise Capital Advisors.

William Feather was an American author and publisher, as well as being very quotable, in particular about business. One I read recently struck me as very apt for today's energy environment. It states, "Success seems to be largely a matter of hanging on after others have let go." I suppose the definition of perseverance would also work in this regard. So how does that tie into energy markets? It appears a sector that is not very loved at present will never get better. And yet, we know that is hardly ever the case. Especially when we are dealing with something as vital to the world as energy. It clearly makes the world "move" if you will. And while energy seems to be out of favor with generalists and the average investor, to astute market observers, that should present opportunity. That's what we see, opportunity, despite the walls of worry the market seems to throw at energy stocks on a consistent basis. Maybe earnings season, which just kicked off and will pick-up steam over the next few weeks will allow for some positive sentiment to develop and grow.

Let's start with a recap of market performance:

- On the commodity front, crude oil was lower by 6.7%, while
- Natural gas also felt the pain, down almost 4%
- Shifting to equities, the broader S&P Energy Select Sector Index® finished lower, down 2.1%
- Exploration and production companies, as measured by the Tortoise North American Oil & Gas Producers IndexSM, were also down, falling 2.9%
- And finally MLPs were marginally lower, as the Tortoise MLP Index® fell 54 bps

Given earnings started for energy, let's touch on a few of the most notable reports.

The first and only midstream company to report earnings last week was industry bellwether Kinder Morgan. The quarter was generally in-line from an earnings perspective and relatively light on news. Kinder remains on-track to announce either a joint venture or an IPO of its massive Trans Mountain project centered around Canadian crude oil, yet nothing new was provided. Importantly Kinder reiterated plans to announce revised dividend guidance later in the year.

The largest oil field services company, Schlumberger, reported on Friday. SLB generally had a weak quarter, with international markets remaining challenged. Notably, we believe the earnings power of the company is still compelling, but maybe a bit further out than anticipated by some. SLB's CEO stated, "Outside of OPEC and the U.S., we are heading towards a third year of significant underinvestment, which increases the likelihood of a medium-term supply deficit as produced reserves are not replaced in sufficient volume."

Nextera Energy was the only utility to report, but it was a very solid start to the year, with an excellent quarter. Management reiterated the top-end of their growth guidance of 6-8% through 2020 for earnings per share. Additionally, the company continues to expand its backlog of wind and solar projects.

On the macro front, the driver of energy markets appeared to be related to negative headlines centered on crude oil. The EIA released the drilling productivity report, which is essentially an estimate of future production based on rigs in operation, that predicts another 100,000 bpd plus increase in U.S. production for May. On Friday, the Baker Hughes rig count showed another five-rig addition in the U.S., marking the 14th consecutive week of increases. The market responded negatively to the continued rise in U.S. production and the fear it will overwhelm the OPEC cuts. And of course the increasing rig count served to validate that concern.

So what should be made of the U.S.'s ability to increase crude oil production? Let's hit on some key numbers and ideas. The EIA currently predicts a 340,000 bpd increase in U.S. production, year over year. That equates to a December 2016 to December 2017 exit rate increase of 860,000 barrels per day. Going back to the early 1980s, the largest exit-to-exit rate growths we have seen occurred in 2012, 2013 and 2014. In each of those years, the U.S. exceeded one million barrels per day of production gains, with a high of 1.136 million bpd added in 2013. That equated to an average growth of 1.24 million bpd in 2013, again the highest noted. But let's say we see December to December exit rate growth of the highest on record at 1.175 million barrels per day. That would equate to an average gain of just over 500,000 barrels per day for 2017. About 200,000 barrels per day higher than the current EIA estimates. Keep in mind, we currently anticipate a 600,000 bpd deficit worldwide, assuming OPEC does not continue with their production cuts. So in our view a 200,000 barrels per day increase in the U.S. does NOT derail the rebalancing story. Yes, it may push it out a bit, but it does not undo what is being done. Additionally, if OPEC extends their cuts, and rhetoric out of the major players has been positive recently, that will allow for deeper inventory draws to take place, despite an increase in U.S. production. In summary, a record year from the U.S. will obviously not help the rebalancing, but it is far from a silver bullet to ruining the story. The market of course will have to be convinced, since they don't believe right now. Time will tell.

That will do it for today...have a great week and we look forward to speaking with you again soon.

Thank you for joining us. And stay tuned for our next cast. Have topics you want covered or other feedback to share? Write us at info@tortoiseinvest.com.

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Tortoise North American Oil & Gas Producers IndexSM The Tortoise North American Oil & Gas Producers IndexSM is a float-adjusted, capitalization weighted index of North American energy companies primarily engaged in the production of crude oil, condensate, natural gas or natural gas liquids (NGLs). The index includes exploration and production companies structured as corporations, limited liability companies and master limited partnerships but excludes United States royalty trusts.

The Tortoise MLP Index[®] The Tortoise MLP Index[®] is a float-adjusted, capitalization weighted index of energy master limited partnerships (MLPs). The index is comprised of publicly traded companies organized in the form of limited partnerships or limited liability companies engaged in transportation, production, processing and/or storage of energy commodities.

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