Tortoise QuickTake Energy Podcast

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

Hello, I am Matt Sallee, Energy Portfolio Manager at Tortoise.

It was a wild ride last week as the market downloaded a deluge of earnings and was hit with the one-two punch of a reinvigorated trade war and Jerome Powell talking after the Fed decision was announced. I kid you not, as we sat in our conference room talking about some portfolio moves, Rob Thummel saw Powell appear on television and said “Oh no, here we go.” Sure enough, within about 30 minutes the Dow lost 500 points.

With that as our backdrop, I’ll hit the big earnings hits and misses for the week. Do you want the good or bad news? Let’s get the bad out of the way.

Concho, which historically has been a blue chip of Permian upstream, got taken out to the woodshed after reporting a current quarter that was roughly in line but a production mix that was gassier than expected, while cutting oil volume growth for the balance of the year but maintaining its capex guidance. Not a combo we like see. Adding fuel to the dumpster-fire was their update on the 23 well “Dominator” pad. The only thing it dominated was losing money as it turns out the well spacing was too tight and the well performance was not good. Oh yeah, and they lowered their assumed gas price realizations for the rest of the year due to wider differentials. Add all this up and what do you get? You get a stock that dropped over 20% erasing $4 billion of market cap and pulled the entire E&P space down with it. Suffice it to say, the upstream market is struggling to determine the appropriate valuation of these names as the industry shifts its focus from production growth to free cash flow. In our view, one result of this evolution of the space will be some much needed consolidation of E&P companies resulting in more resources in fewer and more disciplined hands. Further we see this happening through the majors acquiring smaller independents and mergers of equals among smaller companies.

On the midstream side, it was Western Gas who soiled the bed. The company missed on the quarter and lowered full year EBITDA guidance 8% while holding capex flat. Now part of the reduction in EBITDA was due to a non-cash accounting change, but majority was due to a reduction in volume expectations after operational issues with the key customer Anadarko which are expected to continue for the balance of the year. Along with this, some well connects are getting pushed to next year as producers across the country pump the brakes on lower gas and NGL prices, especially with basis differentials currently plaguing the Permian. They are also getting hit by those lower NGL prices at their Rockies processing plants.

Last but not least, pretty much every other G&P company was beaten like a rented mule last week regardless of whether they missed on the quarter or not. I guess $2 natural gas and 43 cent NGLs will do that.

On the flip side, those with integrated NGL infrastructure or demand pull assets are big winners of low commodity prices. You know who I’m taking about…Enterprise, Oneok, Magellan, MPLX and Williams.

Let’s start with Enterprise, we got more of the same this quarter with a beat across segments but led by gas pipes benefiting from gas price differentials across Texas. Their outlook is boosted by $3.2 billion of capex to be placed in service by year-end. Thanks to a new contract with Chevron, they are proceeding with the Sea Port Oil Terminal, or SPOT, a 2 million bpd crude export facility. The cool thing about SPOT (beyond its clever name) is that it frees up capacity at their existing docks to switch from crude to NGL exports which are currently maxed out across the country…and the rich get richer.

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Oneok beat on strong Bakken processing volumes which flows into downstream assets driving volume across the system. On the call they stated that 2020 EBITDA is now expected to be up more than the previous 20% guidance versus the 2019 midpoint. They also have another 100 mbpd of NGL supply dedicated to the Elk Creek pipeline from plants that are coming on through early 2021. Not to mention their Permian NGL volumes increased 20% sequentially and the contract rates will be moving higher on West Texas LPG pipeline as below-market contracts roll.

Magellan pulled another beat and $40 million full year EBITDA guidance raise as they're benefitting from solid growth on their midwest refined products network but they are also getting spot volumes on their Texas crude pipes which weren't counted on in guidance.

I've given a lot of detail already so I won't elaborate on Williams and MPLX but I thought it would be helpful to provide more color on why some companies' headwinds are other companies' tailwinds.

The bottom line is the market has been volatile and commodity prices have really hit producers hard but for our midstream portfolios, just over 2/3 of the portfolio has reported. Of this, half have beat ours and consensus estimates generating significant cash flow per unit growth. And also, as we highlighted earlier this year, we expected that we were past distribution cuts and we would return to distribution growth this year. This quarter the trend is continued, and we're on pace for mid-single digit, weighted-average portfolio distribution growth. We believe this is why midstream is finally decoupling from commodity prices. Note that natural gas and natural gas liquids are each down about 25% for the year midstream is up about 20%.

I'll leave it there for now.

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@tortoiseadvisors.com.

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