Tortoise QuickTake Energy Podcast

Aug. 26, 2019

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 Tortoise Managing Director and Portfolio Manager Brian Kessens with this week's QuickTake podcast.

Energy and the broad markets were logging a solid week last week until trade tensions escalated on Friday with China's retaliatory tariff announcement and President Trump's intention to respond. All-in, MLPs finished down 1.2%, the broader S&P 500 was off 1.4% and broader energy fell 1.9%. Prior to Friday, all were in the green. Crude oil as measured by WTI finished the week just shy of $54 per barrel, or down 1.4%. Trade concerns overshadowed a constructive draw in US crude oil inventories of 3.5 million barrels and Saudi Arabia indicating its production is the lowest in five years.

In midstream acquisition news last week, Pembina Pipeline Corp. announced the acquisition of Kinder Morgan Canada for $15 per share, or a 37% premium to the previous close. The assets fit well with Pembina's existing footprint in Canada, with Pembina expecting $50 million in synergies with only nominal investment. Further, Pembina is acquiring the Cochin Pipeline from Kinder Morgan for $2 billion or at a 13x EBITDA multiple. The Cochin Pipeline connects Pembina's Canadian assets to Edmonton and NGL hubs Mont Belvieu, Texas, and Conway, Kan. The board also approved a 5% increase in the dividend upon closing. We think the transaction makes good sense for Pembina due to the strategic fit and nature of the cash flows which are supported by long-term, fee-for-service, take-or-pay contracts, with investment grade counterparties.

For Kinder Morgan which held a 70% stake in its Canadian public business unit Kinder Morgan Canada, expected use of proceeds is three-fold: reduce debt, invest in projects and look to potential share buybacks. And as a reminder, Kinder Morgan already committed to a 25% dividend bump in 2020.

Kinder Morgan is not the only pipeline company with capital allocation options. With midstream growth capex likely declining next year and many projects coming on-line generating new revenue streams, free cash flow, after dividends and capex, is set to materialize. Building on what James noted last week about takeaways from a recent energy conference, we were speaking with one large cap midstream company about this capital allocation or that one when we were corrected in that it is not an 'or' decision, but rather an 'and' one. We expect the improvement in balance sheets and cash returned to shareholders to only accelerate next year.

On the regulatory front, the Nebraska Supreme Court approved the alternate route for TC Energy's Keystone XL pipeline. This is a small step forward for Keystone XL, as many other approvals remain, including the likely support of the 2020 US Presidential election winner. If completed, the 830 mbpd pipeline would alleviate Canada's pipeline transportation constraints, which are currently forcing barrels to less efficient transportation like rail.

It seems like every week we talk LNG and this week is no exception as Venture Global announced a milestone achievement - final investment decision on its Calcasieu Pass, LA LNG export project. The project, expected to startup in 2022, is backed by 20 year sales and purchase agreements with Shell, BP and Repsol, among others. This announcement is particularly significant because the project (1) represents a second wave of U.S. LNG projects that will be completed between 2022 and 2025 following the first wave of completion between 2016 and 2020 and (2) the Venture Global facility will be the world's largest scale modular LNG plant, which is designed to deliver the lowest cost U.S. LNG. Note, Baker Hughes GE is supplying the 18 modularized trains providing 1.3 Bcf/d of capacity. Next up, look for a potential final investment decision from public companies NextDecade and Tellurian.

In other LNG news, Freeport LNG started production and Cheniere's Sabine Pass facility completed its scheduled maintenance. Following, LNG exports were at 6.5 Bcf on Thursday last week, an all-time high. That's a record you can bet will be broken soon however as Kinder Morgan's Elba Island export facility is expected to begin production soon.

What to take away from last week? Trade tensions remain in the spotlight as the key driver of broad market sentiment, and in energy, LNG developments accelerated while midstream transactions continue at levels around 13x EBITDA, well above the 10x EBITDA that the public markets value midstream.

This week has the potential to be a quiet one ahead of the Labor Day holiday - there are no industry conferences, the Jackson Hole central bank retreat is over and 2Q earnings reporting is through. Yet we won't be surprised if geopolitical news keeps the market on edge as some try to enjoy the right edge of summer. We'll be back next week to explain what might have come down. Thanks for listening.

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