Tortoise QuickTake Energy Podcast

Tortoise

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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 Tortoise Managing Director and Portfolio Manager Rob Thummel with this week's Tortoise QuickTake podcast.

Another week and another change in the direction of a U.S. and China tariff negotiations. Last week, the U.S. and China agreed to resume trade talks in early October. This news combined with Federal Reserve Chairmen Powell's comments related to keeping the U.S. economic expansion going lifted stocks last week with the S&P 500 rising by almost 2%. The energy sector as represented by the S&P 500 Energy Select Sector Index followed suit rising by almost 3%.

The fall conference season kicked off last week with the annual Barclays CEO Energy-Power Conference. All of the energy industry heavyweights attended and so did we. Let me give you some of the highlights of what we heard and how many of conference themes align with initiatives already in motion at Tortoise. Exxon Mobil is the largest energy company in the world and its CEO Darren Wood delivered a message to a packed house outlining the future of the energy sector. Mr. Wood rarely speaks on quarterly conference calls so like the E.F. Hutton slogan from the 1970s goes, when Darren Wood talks, people listen. What we heard were some similar themes that have been discussed in several of our podcasts. Exxon's CEO believes energy is essential. But Mr. Wood said we are in the midst of an energy transition yet energy transitions take a long time. He pointed out that it took oil 100 years to eclipse coal as the primary fuel mix. In the meantime, the world's rising demand for energy must be met. Looking forward, Mr. Wood pointed out that energy consumption rises as standard of living increases.According to Wood, this is a significant opportunity for the energy sector as 50% of the global population lives in countries with low to medium standards of living based on the U.N. Human Development Index. As the standard of living in these countries increases so will global energy consumption. However, Exxon also recognizes the challenges associated with higher energy consumption. That challenge is carbon emissions. Exxon is committed to addressing the carbon emissions challenge. To address emissions, low carbon solutions need to be adopted by China and India now. In addition, wind and solar need a large scale battery solution for the world to maintain the energy reliability standards that we have become so accustom to. It was national news when the lights went out in New York City for five hours earlier this summer. According to Exxon, lithium is not the solution to energy storage, therefore, research and development needs to be accelerated to find a better solution.

The timing of Exxon's comments coincides with a soon to be released white paper from us here at Tortoise entitled T*he Teal Energy Deal*. In this paper, we address what we think are the fastest and least expensive ways to reduce global carbon emissions as the global demand for energy increases. Here is a sneak peek at the core themes of the soon to be released white paper. Global energy demand will continue to rise driven by electrification. We believe that the world can reduce carbon emissions even in periods of rising demand by eliminating coal and replacing it with low carbon fuels like natural gas as well as renewables. The U.S. plays an important role as part of the solution through exporting low carbon, low cost energy to the rest of world. We go into much more depth about each of these topics in the paper that will be released on our website very soon. Our CEO Kevin Birzer is very passionate about this topic. Videos of Kevin's perspectives will be on the website as well. In addition, we have a large team of over 50 investment professionals committed to the *Teal Energy Deal* and we are looking for investment opportunities every day as the energy transition unfolds.

Back to other highlights from the Barclays conference. Google says the two most popular celebrities right now are Kylie Jenner and Kim Kardashian. I say the two most popular energy companies at the conference were Antero Resources and Range Resources. My assessment was based on the size of the crowd attending the presentations put on by these companies. I'm pretty sure that the number of people in the meeting room exceeded allowed capacity. Going into the conference Range and Antero were two of the most heavily shorted stocks in the energy sector with short interest representing 33% and 19% of the respective float of each company given near-term weak natural gas prices and current debt levels of both companies. Both Marcellus producers articulated compelling arguments for rising global demand for natural gas and the role that the Marcellus will play in filling a significant portion of that demand. The crowd must have liked what it heard as Range and Antero were two of the best performing stocks in the energy sector last week rising by 10% and 11%, respectively.

A new theme that permeated this year's conference from oil and gas producers was a drive toward higher dividends from generation of free cash flow. The producers have been talking about generation of cash flow in excess of capital expenditures or free cash flow for a while but now that this is becoming a reality we are getting more insight on how the excess cash will be allocated. Most of the oil and gas producers that presented want to increase dividends until their dividend yield is in-line with the S&P 500. After that, buying back stocks seems to be the most popular choice.

While the producers are going in the right direction, in my opinion, the presenters at this conference missed out on an opportunity. The current yield for the 10-year Treasury is around 1.5%. Investors around the world are starving for yield. According to Bloomberg, the dividend yield of the energy sector is currently 3% that is 1.5x the yield of the S&P 500 while EV/EBITDA multiple of the energy sector is half that of the S&P 500. It's important that these producers raise dividends in-line with energy sector peers to attract new investors to the space. Of course, energy infrastructure dividend yields are already quite compelling with most energy infrastructure stocks yielding 6% or higher. If the economy falters a little, investors want to own stocks that pay cash dividends. If the economic expansion continues and your return expectations for equities is 8% to 10%, it seems reasonable to buy energy stocks that could deliver half of your expected return from dividends. Buying energy infrastructure stocks could possibly get you 75% to 100% of your expected return from cash dividends. I think you get the point.

The last notable comment from the Barclays Conference came from the sage of the energy industry Mark Papa. Mr. Papa is the former CEO of EOG Resources and is now the CEO of Centennial Resource Development Corporation. Papa stated that estimates for 2020 U.S. oil production growth are too high. In fact, he believes that U.S. oil production growth will slow to 700,000 barrels per day which is 40% lower than the 1.2 million barrels per day expectations. We agree with Papa and a decline in the rig count for the third consecutive week is making that prediction look even more likely. Our view is that lower U.S. oil production growth is a positive for the U.S. energy sector as it will stabilize energy prices.

Those are the highlights from last week. Thanks for listening. We will talk to you next week.

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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The **PCE inflation rate** is the Personal Consumption Expenditures Price Index. It measures price changes for household goods and services. Increases in the PCEPI warn of inflation while decreases indicate deflation.

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