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.

Thanks for joining us today on the Tortoise QuickTake Podcast. I'm James Mick, Managing Director and Energy Portfolio Manager with Tortoise.

Despite the World Series ending almost two weeks ago, I would be remiss if I didn't bring up one of the best series moments in years. The thrilling seven games provided a highlight for the ages by the Nationals Jeff Adams. No, Jeff is not a specialized lefty reliever out of the bullpen who faces one batter every three games. Rather, he's a normal fan who was in the outfield bleachers, when in Game 5, returning to his seat, he was faced with a dilemma. See Jeff had two Bud Light beers, one in each hand, when Astros sensation Yordan Alvarez hit a rocket towards left center. Jeff, in a moment of clarity and outright laser focus, made the decision to take the home run ball off his chest rather than drop the beers and save himself from any bodily harm. Jeff was ultimately rewarded with a trip to game six in Houston by Budweiser and of course the home run ball. How can you possibly tie this back to energy? Well, it's this kind of focus that energy management teams must have on capital discipline to pull us out of the current energy malaise.

We'll start things off with market performance for the week that was:

- On the commodity front, crude oil increased approximately 1.9%, while
- Natural gas was white hot, increasing 13%
- Shifting to equities, the broader S&P Energy Select Sector Index® rose 2.4%
- Exploration and production companies, as measured by the Tortoise North American Oil & Gas Producers Index℠ were also strong, up 4.2%
- And finally MLPs were the opposite, struggling as the Tortoise MLP Index® fell 2.2%

Let's quickly hit the macro first, as news out of China on the trade front was positive, citing the Ministry of Commerce stating that an agreement in principle to roll-back tariffs in a phased approach had been reached. Not to be out-tweeted, is that even a word, President Trump said on Friday that was not the case, casting a bit of doubt on the cyclical rally that had taken place.

Crude oil was higher mainly due to positive trade war news. Additionally, OPEC released its 2019 World Oil Outlook, which highlighted a lower OPEC output in 2024 versus current due to growing U.S. supply and other areas outside of OPEC. Global demand is forecasted to reach 110 million barrels per day by 2040, pretty consistent with the outlook we have shared previously.

Natural gas felt the love this past week as future temperatures are expected to be significantly colder in many parts of the country. It didn't hurt either that natural gas producers continue to espouse a flat production outlook with lower capex.

In global commodity news, England noted it is halting all hydraulic fracturing within its borders. This is more symbolic than anything as there simply isn't much drilling taking place. That being said, the U.K. continues to utilize natural gas as a fuel source, mainly from offshore production and European pipelines.

Renewable energy company Pattern Energy Group received a buyout offer from the Canada Pension Plan Investment Board.

Midstream company DCP Midstream was the latest MLP to pull the trigger and eliminate its incentive distribution rights. Good to see as this was one of the last larger companies left.

Phillips 66 and Phillips 66 Partners held an analyst day in New York on Wednesday. Overall it was a positive update as the refining company continues to execute on delivering shareholder value in the form of dividends, share repurchases and growing cash flows. The midstream entity is also very well positioned with several organic growth projects in the works and a suite of drop-down assets available when needed.

There was an equity offering in the market this past week and it was not great for midstream sentiment. Likely misunderstood, but impactful nonetheless. A secondary offering of Antero Midstream shares held by private equity firms Warburg Pincus and Yorktown Energy Partners for approximately $170 million was executed and it definitely put pressure on the midstream space. Buyers likely sold other midstream names to make room. I would note, this was NOT a primary offering by the company and Antero is not selling any stock, nor receiving any proceeds.

Earnings were heavy this past week with frankly too many to mention. The main discussion points remain centered around capex and cash flow.

The one that caught many investors' attention though was Chesapeake Energy, ticker CHK. As you may know CHK was at the forefront of the shale era, scooping up acreage, often at high prices and notably centered on natural gas. The problem was that was when natural gas was trading about four times higher than it has for some time. Hence, CHK has been chronically over-levered and burdened not only by legacy acquisition costs, but also by a variety of agreements with pipeline companies for transport signed at around those same times. While many of those have been renegotiated, a few still remain.

That being said, the primary issue was language placed in the 10-Q regarding the solvency of the company and its risk as a going concern. This is certainly not new information, the stock has been trading below $5 for almost four years. Yet maybe being in writing was the flashpoint. Either way, the thought of this has not been well received by midstream investors with any exposure. Never mind that midstream contracts have held up very well in previous bankruptcies, at this point nothing short of perfection seems to be good enough for midstream. We should gain more clarity as time goes on, but we have run many of these numbers before and don't see substantial impact to any midstream companies. In addition, CHK has plenty of options at its disposal and a bankruptcy is not imminent in our view.

Despite the negative sentiment around CHK, it wasn't all bad, as several energy companies reduced capex and the stocks generally reacted positively, certainly on a relative basis.

The playbook is out there, just be disciplined and slow capex in accordance with supply and demand on the E&P side and volume growth on the midstream side. Finally, be ready to ramp again when the time comes and it's needed. The U.S. energy story is not dead, it just needs a breather.

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@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.

Broad Energy = The S&P Energy Select Sector® Index is a capitalization-weighted index of S&P 500® Index companies in the energy sector involved in the development or production of energy products.

Producers = Tortoise North American Oil & Gas Producers Index℠
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