Tortoise Energy Podcast

July 27, 2020

Welcome to the Tortoise 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 Quick Take Podcast. I'm James Mick, Managing Director and Energy Portfolio Manager with Tortoise.

Finally…the last time I was on the pod, I was touting an agreement for the eventual return of the NBA. This past week I watched Sporting KC play soccer, opening day for Major League Baseball and we are within days of the aforementioned NBA season starting up. As a sports junkie, it's great to be back. What's not great to see return is escalation of U.S./China tensions, this time in the form of consulate closures. Fortunately, the market seemed to shrug off this latest flare-up. Let's hope that remains the case.

Moving to the financial markets, let's start things off with performance for the week that was:

- On the commodity front, crude oil was up modestly, increasing 1.4%, while
- Natural gas was strong, with futures prices rising over 5%,
- Shifting to equities, the broader S&P Energy Select Sector Index® was an S&P sector leader, higher by 2.1%
- Exploration and production companies, as measured by the Tortoise North American Oil & Gas Producers Index℠ led energy, moving up 5.2%
- Utilities, per the Dow Jones Utility Index, were modestly negative, down 35 bps
- And finally MLPs delivered a solid week as the Tortoise MLP Index® improved by 1.6%

This week kicked off earnings season for energy companies, with several notable prints.

First, the week was heavy on oil field services earnings as all three of the big guys reported, Halliburton, Baker Hughes and Schlumberger. The story was all about taking costs out of the system to save margins and ultimately cash flow in a fully anticipated rough 2Q for upstream companies. After all, we did see the swiftest rig count decline back to at least 1987, when tracking began in earnest. Of course, technology continues to play a big role for all three and similar to what we have seen in past downturns, oftentimes these companies come out much more lean and efficient than they went in. Yet to see how this downturn plays out, being it is clearly unprecedented, driven by the virus, but we'll be watching closely.

Kinder Morgan was the first midstream company to report for 2Q and the results were a slight miss to our estimates. KMI's 2020 guidance from the first quarter call had adjusted EBITDA down about 8% versus their original budgeted expectations. That estimate was revised here at the halfway point with a newly estimated, slightly more than 8% impact. Based on our updated estimates, we are anticipating approximately 9% below original guidance. The main difference between now and the April estimate is due to lower gathering and processing volumes expected for the remainder of 2020. It should be noted, refined product volumes in the 2nd quarter were down about 31% versus last year and 1Q 2020, which was better than the original guidance of 40% declines. Kinder stuck with previous guidance for 3Q and 4Q refined product declines of 11% and 5% respectively. Finally, Chairman Rich Kinder noted that they are in a maturing business segment and with less expansion opportunities than previous. If that's the case, he noted they will plan to use the substantial cash flow thrown off by the assets to increase their dividend, pay down debt and/or buyback shares of stock. That sounds a lot like what we have been preaching over the last 6-8 quarters.

The largest utility in the U.S. by market cap also announced earnings as Nextera Energy did what we are accustomed to, beat estimates. Additionally, they reported a very impressive addition to the current Energy Resources backlog of renewables of over 1,730 megawatts. In line with the clean energy story, management noted they intend to retire their last remaining coal unit in early 2022. This is the culmination of a plan that started in 2015 and will result in the retirement of 2,700 megawatts of coal capacity. In other news Nextera is proposing a $65M hydrogen project at Florida Power and Light, with an in-service target of 2023. What's great is this will be utilizing excess solar power than would have otherwise been wasted to produce green hydrogen. Finally, they also reiterated guidance for the full year 2020 and out to 2022.

In one of the odder stories of the week, Ohio based utility FirstEnergy was caught up in a potential bribery scandal involving the Ohio Speaker of the House, Larry Householder. What appears to be at issue is the funding, lobbying and potential dark pool of money that helped save two nuclear plants in Ohio previously owned by First Energy. The total dollar amount is upwards of $1B in taxpayer money to save the failing plants, so no small chunk of change. FirstEnergy had a good quarter by all accounts, but as to be expected, almost the entire call was spent on the scandal and the issue at hand. While denying any wrongdoing, we'll have to stay tuned as there is surely more to come.

In a quick hit news item for this week, we saw our first increase in the oil directed rig count since mid-March when the Saudi-Russia falling out first took place. It was a paltry one rig gain, but it feels like we have found a potential floor here.

Finally, I wanted to touch on some projections I recently ran across from a research service. This group aggregated several sources together, including Pew Research and the United Nations, to detail out world population projections. Currently the world has about 7.8 billion people. By 2050, that number is projected to be just shy of 10 billion. Why bring this up you ask? Well, in our Teal Energy Deal that we laid out one year ago, we made the case for rising demand for energy, based primarily on more people, with many of those people improving their standard of living and hence, utilizing more energy. In fact, it's been proven that higher energy use per capita is directly correlated with an increasing human development index. In the projections, Africa's population is expected to almost double by 2050, reaching 2.5 billion people. As their standard of living increases, it stands to reason they will utilize more energy. In short, energy is core to our lives and essential to our standard of living. Clean, affordable, abundant energy will continue to be produced, delivered and consumed around the world.

Have a great week, stay safe, 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.

The S&P 500® Index is a market-value weighted index of equity securities.

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℠
The Tortoise North American Oil & Gas Producers Index℠ 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.

MLPs = 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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