Tortoise Energy Podcast

September 8, 2020

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

Good to be with you today, I am Quinn Kiley, Managing Director and energy Portfolio Manager at Tortoise and I am happy to be with you for this week's Energy Podcast. As we exit the summer doldrums the saga that is the Dakota Access Pipeline continued to plod along. The Army Corps of Engineers announced it has begun work on an environmental impact statement, something the district court has been requesting for the better part of year. Another requirement of the court was that the Corps determine a remedy for the fact that the pipeline no longer has a permit to cross Corps land. In an interesting twist the corps stated that it would require no immediate action, essentially saying it did not think the court had any jurisdiction over the matter. We are closely monitoring this story as it has potential impacts on several midstream names we own. Last week saw other pipeline news, as the Mountain Valley Pipeline received its expected biological opinion from the U.S. Fish and Wildlife Service. This is a necessary step for the construction of the pipeline to continue and for it to be in service in early 2021. This bodes well for Equitrans Midstream, as the regulatory process has been an overhang on the stock. With that quick update, let's look at market performance for the week.

Markets were mixed:

- The Alerian MLP Index finished down -4.7%, and remains down over -39.5% year to date
- Other energy stocks, represented by the Energy Select Sector SPDR (XLE), were down -4.3% for the week
- In broader markets, the S&P 500 lost -2.3% for the week and the ten-year treasury was generally flat

As economies re-open in a somewhat disorderly way, energy demand has recovered from its lows of the spring. Refinery utilization was operating at mid-sixty percent of capacity in April and May, those utilization rates are now in the low eighties. This tepid recovery has seen crude oil prices range-bound all summer, generally in the low $40's per barrel in the U.S. While it appears a bottom is in, the path of an ultimate economic recovery is uncertain and appears highly reliant on fiscal and biologic outcomes. The macro outlook for both is promising, but timing is far from certain. This backdrop has led to some interesting outcomes in the energy industry overall. Saudi Aramco, the largest energy company in the world, has delayed multiple capital projects given the uncertainty, according to the Wall Street Journal. According to the paper, Aramco has slashed its capital budget in half and delayed projects across the globe. Refinery investments in Saudi Arabia, the United States, Pakistan, India, and China have all been postponed. The apparent motive is not only a reaction to soft energy demand but also to protect its dividend. This is a different course than other oil majors have taken recently, but understandable when your government is a 98% owner and relies on the dividend to fund its operating budget.

The newly adopted mantra of capital discipline in the energy industry is having broader impacts across the energy value chain. Schlumberger (SLB), a leading global oilfield service provider, announced it was divesting its U.S. hydraulic fracturing business to Denver based Liberty Oilfield Services Inc. (LBRT). Early commentators viewed this transaction as Schlumberger giving up on the U.S., but by taking a 37% equity interest in Liberty the company is far from divested in the U.S. fracking story. Schlumberger's shares are locked up for nine months, so we will find out their long-term intentions over time. This transaction consolidates two meaningful players into a market leader in hydraulic fracturing. Barron's reported last week that Liberty's CEO expects the number of frac spreads operating in the U.S to double from current levels by sometime in 2021. This will be an interesting story to follow, and it wouldn't surprise us if this is one of many consolidating transactions we will see in the energy patch in the weeks and months to come.

While day to day commodity price moves have little impact on the fundamentals of the energy infrastructure companies we invest in, these price swings do impact investor sentiment and are worth following from that standpoint. Last week saw some confusing price action in crude oil as the EIA reported bullish inventory numbers but prices fell. The nine-million-barrel draw on inventories was better than expected, but there were some timing impacts that perhaps made the number look better than it actually was. Hurricane Laura impacted shipping activity two weeks ago. The Houston ship channel limited import activity before limiting export activity, all else being equal this alone should lead to a bigger than expected draw on inventories. There was also news that Saudi Arabia had reduced its shipments to the Gulf of Mexico, a net positive for inventory draws. We don't want to read too much into week to week data but the market clearly showed some skepticism towards last week's number. In other oil related news Iraq requested an extension on its plan to cut production and compensate other OPEC members for previous poor compliance, but then quickly backtracked. This may be an indication that the coalition is holding together better than in years past. Finally on oil, some oil price bulls are beginning speak out. The latest was Goldman Sachs with a bullish call on energy equities undergirded by an above consensus call on crude oil. Goldman sees WTI crude at $58 per barrel next year. With that said, crude is off meaningfully this morning on news of Saudi Arabia lowering its official selling price for October.

Last week saw the month of August wrap up and we thought it might be useful to sum up how energy faired during that month. On the commodity front, crude oil as measured by WTI, was up almost six percent while natural gas was up close to 45 percent during the month. Energy equities diverged from the underlying commodity in August. Both the XLE and the Alerian were down a little over one percent in what proved to be another frustrating month for energy investors. This was against a backdrop of broader indices reaching all-time highs as the S&P 500 returned seven percent during the month.

Thanks for joining us and we will be back next week. Please stay safe.

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.

Alerian MLP Index is the leading gauge of energy infrastructure Master Limited Partnerships (MLPs). The capped, float-adjusted, capitalization-weighted index, whose constituents earn the majority of their cash flow from midstream activities involving energy commodities, is disseminated real-time on a price-return basis (AMZ) and on a total-return basis (AMZX).

Henry Hub: The best known of all natural gas trading points in North America and standard delivery point for New York Mercantile Exchange's natural gas futures contracts in the United States.

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.

S&P 500® Index is an unmanaged, market-value weighted index of stocks that is widely regarded as the standard for measuring large-cap U.S. stock market performance.

West Texas Intermediate (WTI): Light, sweet crude oil commonly referred to as "oil" in the Western world. West Texas Intermediate is the underlying commodity of the New York Mercantile Exchange's oil futures contracts.

It is not possible to invest in an Index.

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