Tortoise QuickTake Energy Podcast

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Welcome to the Tortoise QuickTake podcast. Thank you for joining us. Today, senior members of Tortoise provide 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.

Well I would say everyone living outside the state of Massachusetts is probably a bit bummed this morning. Not only did the Patriots win yet again, but it was a pretty miserable game to watch. My favorite prop bet was, would Adam Levine be wearing a leather jacket for the halftime show. At least I hope you had a better evening than the Bud Knight. Luckily energy markets have not been dealing with angry dragons, as the show to start 2019 has been much more watchable than the finish to 2018.

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

- On the commodity front, crude oil was higher by 3.3% on a variety of news items, while
- Natural gas was down sharply on warmer forecasted weather, dropping almost 13%
- Shifting to equities, the broader S&P Energy Select Sector Index® rose 3.2%
- Exploration and production companies, as measured by the Tortoise North American Oil & Gas Producers Index℠ were also in the green, up 85 bps
- And finally MLPs continued their strong start to 2019, as the Tortoise MLP Index® increased by 2.1%

It was an eventful week on the crude oil front, with several noteworthy items.

- First, the U.S. government instituted sanctions on Venezuela's national oil company, PDVSA, effectively stopping all crude oil shipments to the U.S.
    - The move is seen as a direct attempt to unseat the Maduro regime
    - Venezuelan oil production has been in free fall, dropping from as high as 3.3 million barrels per day as recently as 2005, to now just over 1 million barrels per day
        - Clearly this will not help matters and in our view could very likely push production much lower still
    - We've spoken before about global trade and how fungible products can be re-routed, but it does take time and the complex refineries along the Gulf Coast are the biggest users of Venezuela's heavy crude, so this will certainly be disruptive to the global shipping chains
    - In addition, PDVSA's refineries in the U.S., operated under the Citgo brand, are large purchasers of the heavy crude, but any profit will be trapped, hence hard to know how that will actually impact operations
- Second, Wednesday's DOE inventory numbers finally showed a draw in total U.S. oil inventories, the first in a while
- Third, Saudi signaled it would continue to reduce output in February
- Finally, the rig count in the U.S. was also down 15 oil rigs

All of these data points led to higher crude oil prices for the week.

Beyond commodities, it was a relatively heavy earnings week. With so many companies reporting, we'll hit a few key themes rather than go through all of them.

On the midstream front, two themes stood out.

First, Enterprise Products, the largest MLP by market cap posted strong results for 4Q. CEO Jim Teague noted EPD set 23 operational and financial records in 2018. Just a phenomenal year. But the big news was the announcement of a $2 billion dollar unit buyback program. As you may recall, we have been touting how MLPs and midstream companies will step up the return of capital to unit and stockholders as we move through 2019 and even more so in 2020 and beyond. This is the next step as EPD plans to add buybacks to the arsenal.

Beyond the buybacks, we appreciated how EPD also focused primarily on cash flow statement metrics, discussing growth in free cash flow for 2019. In fact, one of our key themes for the next three years is just that, growth in free cash flow. With that growth, companies can figure out the best way to allocate capital, be it increasing dividends, buying back stock, paying down debt, etc. But all should result in positive returns for stockholders.

Second, Tallgrass Energy announced that Blackstone was acquiring 100% of the general partner interest and 44% of the economic interest in the company for approximately $3.3 billion dollars. As Brian noted a few weeks ago with KKR and SemGroup striking a deal, private equity continues to be heavily involved in midstream as we believe they clearly see a valuation gap.

Blackstone brings not only significant capital to help in project buildout, but also has a suite of midstream assets in other funds that could potentially make their way into Tallgrass. Still a lot to be figured out here, but it continues a theme we have been espousing now for a while in terms of private equity participation in midstream.
The third major theme was major indeed. The big guys, Exxon, Chevron, Shell, ConocoPhillips were just a few of the several E&Ps to report this past week. As many of the very largest companies in energy, they obviously draw significant attention.

A couple of interesting points from some of the calls:

- Chevron had a Permian production rate of 377,000 bpd in 4Q, up 84% compared to the same period last year
- Chevron also instituted a $25 billion dollar share buyback program of indefinite life
- Exxon had a nice beat as well, delivering solid earnings ahead of consensus
- Interestingly, it was the first time in 15 years that the CEO has spoken on the quarterly call
- Permian production for XOM was up 93% year over year
- Alongside the growing Permian production, XOM announced it was expanding its Beaumont refinery by 250,000 bpd, or 65% to handle more light, sweet crude, specifically from the Permian
- And finally on XOM, they are expected to reach FID, or final investment decision on LNG project Golden Pass in the very near future
- Shifting to Shell, they also beat consensus for the quarter
- And not to be outdone in the Permian, have increased their production 200% since January 2017

Hopefully you are catching on to the theme here and that is the majors are seriously investing in the Permian basin. When we put together our 5 year outlook about 18 months ago, we noted that one of the key themes was the move from long-cycle projects to short-cycle projects such as shale and I think that is exactly what we are seeing as the majors have latched on in a big way to shale oil production, specifically in the Permian.
Lots more earnings to come in the next few weeks.

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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