Tortoise QuickTake Podcast

July 5, 2017

Welcome to the Tortoise QuickTake podcast. Thank you for joining us. Today, a senior member of 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, highlighting the top energy events of last week.

We've reached halftime in the equity markets. The first half was one that energy investors want to forget. The energy sector represented by the S&P Energy Select Sector Index fell by 13% in the first half of the year. Energy has been the worst performing sector in the S&P 500 in 2017 so far. MLPs (as represented by the Tortoise MLP Index®) fared much better, declining by 3% year-to-date. Looking back at the energy sector, the best first half performance was the refining sector, where the average return was 3% during the first half. Conversely, offshore oilfield services operators performed the worst, declining by 41% through June 30th.

Although the energy sector is down, it is certainly not out. At Tortoise, we believe that the energy sector is setup for a second half comeback. An improvement in crude oil prices could provide the support for a second half rally. What is the catalyst for higher oil prices? Our expectation is that both U.S. and global oil inventories decline throughout the second half of 2017. We are entering the period when oil demand is the strongest, and the supply glut should see a meaningful impact from the OPEC production cuts. As global oil inventories move closer to the five-year average, we expect crude oil prices to respond positively and move back toward $50 per barrel.

One minor factor associated with oil prices that we have been getting a few questions about is the Strategic Petroleum Reserve. What is the Strategic Petroleum Reserve? It's crude oil stored by the United States Department of Energy for emergency purposes to mitigate any potential supply disruptions. The current reserve of 682 million barrels of oil represents a little over 30 days of supply. The reserve is the largest emergency supply in the world. What is happening? The U.S. is gradually reducing its reserves, which makes sense since the U.S. has been so successful in finding new sources of crude oil supply. In 2017, the Strategic Petroleum Reserve has been reduced by 12.6 million barrels. The latest announced reduction allows for the sale of 10 million barrels in May and June under the 21st Century Curves Act. Through June 23rd, the Department of Energy had sold seven million barrels, so an additional three million barrels will likely be reported as sold in the EIA report later this week. Why is this important? On a weekly basis, the EIA reports two separate U.S. crude oil inventory numbers. The first is commercial oil inventories, while the second is the Strategic Petroleum Reserve. Think about it this way: You have two glasses of water. One empty glass represents commercial oil inventories, while the second full glass of water represents the Strategic Petroleum Reserve. Selling oil from the Strategic Petroleum Reserve is similar to pouring water from the reserve glass into the commercial glass. However, the challenge that this creates for the oil markets is that traders only focus on the commercial inventory levels. Reducing the Strategy Petroleum Reserve effectively increases commercial inventories. At Tortoise, we believe that U.S. commercial oil inventories need to consistently decline in order for oil prices to rise. We are approaching the end of the current Strategic Petroleum Reserve sales program, which should contribute to a second half comeback for crude oil prices.

Speaking of the government and Department of Energy, did you know that it was energy week last week at the White House? It wasn't former Saturday Night Live cast member Fred Armisen hosting the press briefing last Tuesday, it was his look-a-like Department of Energy Secretary Rick Perry who talked about several interesting topics related to the U.S. energy sector. First, he discussed a theme of America achieving energy dominance. At Tortoise, we have talked consistently about entering a new era in the energy sector. In this new era, the U.S. will become a supplier of low cost crude oil, natural gas and natural gas liquids to the rest of the world. Energy companies across the energy value chain, from oil and gas producers to energy infrastructure to downstream providers, will benefit as the U.S achieves energy dominance. Second, the secretary made an interesting point, stating that the U.S. has been a net energy importer since 1953, but by 2018 the U.S. is expected to be a net energy exporter of natural gas. Based on this comment, it appears that the U.S. government will continue to be supportive of liquefied natural gas exports. Mr. Perry also discussed clean energy, highlighting that the U.S. already leads the world in lowering emissions. We have talked on this podcast in the past how electricity consumption has increased, while emissions have remained flat thanks to increased use of natural gas and renewables. Lastly, in a bit of a surprise, nuclear energy was discussed at length. We believe that nuclear energy will require more education of the public before being accepted by most constituents.

In company related news, it was Permian week. The largest Permian acreage acquisition to occur last week was when Carrizo acquired 16 thousand acres in the Delaware Basin for $648 million. Carrizo issued $227 million in common stock to finance the acquisition. Carrizo's stock price rose by almost 6% last week, doubling the 3% return of the Tortoise North American Oil & Gas Producers Index℠.

On the infrastructure side, Enterprise Products announced the largest Permian infrastructure project last week, adding a 300 million cubic foot per day natural gas processing plant that is expected to be available in the third quarter of 2018. Once again, this displays the continued need for new infrastructure in the Permian.

Those are 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@tortoiseinvest.com.

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The **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.

The **Tortoise MLP Index®** is a float-adjusted, capitalization-weighted index of energy master limited partnerships. 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.

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. The index includes exploration and production companies structured as corporations, limited liability companies and master limited partnerships, but excludes U.S. royalty trusts.

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