Tortoise QuickTake Podcast with James Mick

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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.

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

Well, so much for the new year leading to a different outcome. Unfortunately for the energy market, the start of 2016 looks a lot like 2015. In what is becoming more the norm than the exception, volatility within the energy space continued unabated.

This time, however, the broad market was the likely leader, as it too sold off following consistent negative headlines out of China, including a devaluation of the Chinese national currency and renewed concerns around growth. Despite rising tensions in the Middle East and a strong jobs report, crude oil hit 12 year lows and the negative sentiment was too much for energy stocks.

As for last week's performance,

- On the commodity front, crude oil was down 10.5%, settling at just over $33 while
- Natural gas was actually higher for the week, up 5.8% due to colder weather
- Shifting to equities, the broader S&P energy index was down 6.8%
- Exploration and production companies were down 9.1%
- And MLPs finished down 8.2% for last week

Tackling the macro issues first, China dominated headlines as renewed concerns about growth led to stock market turmoil and the tripping of circuit breakers, which shut down China's stock market for the better part of one day as well as part of another. Those concerns were extrapolated to all emerging markets and spilled over to the US as stocks also tumbled domestically.

On the positive side of the economic ledger, last Friday provided a robust jobs report, which included previous months being revised higher as well. Slack in the labor market continues to tighten, yet inflation is not moving higher, potentially providing for continued accommodative policy.

From an energy perspective, it was an up and down week.

The negative macro events in China clearly had an impact on crude prices as globally the concern is that crude oil demand will falter with a slowdown in China as well as other emerging markets.

Tensions between Iran and Saudi Arabia continued to escalate, yet the market shrugged it off. Additionally, ISIS set ablaze crude oil terminals in Libya, but the market again simply shrugged it off.

What was front and center was a substantial build in gasoline inventories in the U.S. Despite a draw in crude oil inventories, the market was keenly focused on the gasoline build, worried that demand may be weaker in 2016.

So what to make of all these various events?

Demand for crude oil worldwide is clearly a big issue. And while Chinese GDP has been slowing for some time, gasoline demand has actually been pretty robust, up 11% year to date. Commodities more focused on the industrial side in terms of manufacturing no doubt feel more pain than crude, which has a backstop of increasing usage by consumers as more and more drive cars and SUVs.

Domestically, gasoline comps on a year over year basis in the U.S. will certainly be more difficult in 2016, yet a couple of factors provide a positive outlook in our view. One, gasoline demand has a strong correlation to employment and the recent jobs report supports continued strength in labor markets. Two, there is generally a lag of approximately 6 months from the fall in gasoline prices before driving habits start to change materially. We feel this should provide additional demand for 2016.

Clearly, there is very little risk premium being priced into crude oil for geopolitical tensions, as evidenced by the aforementioned lack of movement despite issues between two of OPEC's key players. As a sign of the times, where any news is bad news, the discord was viewed as potential evidence that the chances of OPEC working together in 2016 are essentially zero, hence no production cuts.

And finally, we recently attended a large industry conference with a variety of energy companies, including multiple refiners. The message regarding the large gasoline inventory build was two-fold: one, inclement weather resulted in fewer exports and two, end of year accounting by the government reporting agencies tend to play havoc on those numbers, so use caution when assessing weekly numbers from the end of a year for longer term trends.

Speaking of the conference, the keynote speaker was ExxonMobil's CEO Rex Tillerson. While he had many interesting anecdotes and advice, what was most interesting to me was his view of his role in the company. He noted that he is making decisions right now for 15-20 years down the road. That's the time horizon he is focused on. Quite a contrast to the week to week or even quarter to quarter focus of so many companies and investors. And certainly a good lesson to keep in mind.

Thanks for listening and we look forward to speaking with 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@tortoiseadvisors.com