Tortoise QuickTake Energy Podcast

Sept. 10, 2018

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.

Hello. I am Tortoise Managing Director and Portfolio Manager Rob Thummel with this week's Tortoise QuickTake podcast.

Looking back at performance last week. Oil prices fell by 3% mostly due to continued concerns of tariffs slowing global growth. Consequently, the energy sector as represented by the S&P Energy Select Sector® Index declined by 2.2%. MLPs closed flat for the week despite declines in both oil prices and the energy sector.

Last week also kicked off the fall conference season with the annual Barclays CEO Energy and Power Conference in New York City. Over 100 CEOs and CFOs of North American energy companies provided business updates. The U.S. energy sector has significantly transformed over the past 15 years that I have attended this conference. Think about it, technology such as hydraulic fracturing and horizontal drilling have unlocked significant supplies of oil and natural gas in the U.S. The positive impact of these technologies has been felt around the world thru lower energy prices. U.S. oil production has doubled to over 10 million barrels per day. In fact, the U.S. is forecasted to export 5 million barrels per day of oil in the next five years. This amount of exports would be equivalent to total of U.S. oil production in 2009. I find this remarkable. Also, remember when Cheniere Energy was building a natural gas import terminal due to concerns over the U.S. running out of natural gas? Today, Cheniere is the leading exporter of U.S. produced natural gas. The U.S. is projected to export up to 12.5% of the natural gas it produces. In fact, the U.S. is expected to export oil and natural gas for decades.

Many are reminiscing about Burt Reynolds upon his death last week. What was your favorite 1970's Burt Reynolds movie? Mine was Smokey and the Bandit. You also might recall that the 1970's was also a period when the U.S. and the world experienced an energy crisis. Thanks to the ingenuity and perseverance of many of the U.S. energy sector CEOs and CFOs that were present at the Barclay's energy conference last week, we don't have to worry about an energy crisis anymore.

At the conference, we were in search of the lodestar and I think we found him or them at least as it relates to the outlook for the energy sector for the next several years. Three veterans of the energy industry each with over 30+ years of experience in the industry shared their outlooks for the U.S. energy sector. All three were optimistic. First, Bill Thomas, CEO of EOG Resources - one of the most respected energy companies in the U.S., stated that they have never been in a better position than they are in now. Second, Mark Papa, former EOG CEO and current Centennial Resource Development CEO highlighted the small margin for error in the global oil markets due to a very tight supply/demand balance that tightens further in 2019 as well as a very low global surplus or spare capacity estimating it to be 1.5 million barrels per day. Lastly and probably the most bullish was Continental Resources CEO Harold Hamm who discussed the potential for the next U.S. oil investment super cycle that could last until 2025 due to low excess crude oil capacity, increasing global demand for light, sweet crude, U.S. access to global markets, and underinvestment in global long-lead time projects. Hamm highlighted that U.S. crude oil is poised to fill the supply gap during his self-proclaimed super cycle. If you have been listening to our podcasts for a while, these themes sound familiar as they align with much of the commentary that you have heard from Tortoise.

Looking across the energy value chain here a few highlights from company CEOs:

U.S. oil producers are remaining disciplined despite higher oil price environment. U.S. oil producers are not looking to increase capital spending, rather most are focused on improving their metrics to become more attractive relative to other sectors in the S&P 500® by increasing returns of equity and generating free cash flow. Evidence of this discipline is in the oil rig count that was effectively unchanged over the last three months.

Natural gas producers are assessing capital spending in a sub $3 price environment. As an example, the largest natural gas producer in the U.S., EQT Corporation, noted that growth continues as long as natural gas prices remain at current levels but growth could slow if prices fall to around $2. Natural gas prices continue to be a quandary. Last week, natural gas inventory levels set a new 5-year record low for inventories for the weekly period ending August 31. Increased use of natural gas continues to make an impact on reducing carbon dioxide emissions. Last week, the EIA highlighted a 14% decline in CO_2 emissions since 2005 as natural gas has gained market share displacing coal as fuel supply.

Updates from oil field service management teams were not as positive. Halliburton expressed near-term concerns about its U.S. frac business due to lower equipment utilization as a result of the Permian Basin bottlenecks as well as pricing pressures in multiple basins. With no relief in sight until 2019, the news from Halliburton weighted on OFS stocks with the OFS index falling by 6% last week.

The midstream sector updates revolved around positive regulatory decisions and new capital projects to support growing U.S. production volumes. EQT Midstream received regulatory approval to re-engage construction on its Mountain Valley Pipeline. Energy Transfer, Magellan Midstream, MPLX and Delek plan to build a new 600-mile crude oil pipeline from the Permian Basin to the Gulf Coast to be operational by mid-2020. Kinder Morgan and EagleClaw are proceeding with their $2 billion Permian Highway Pipeline Project that will transport up to 2 bcf/d of natural gas from West Texas to the Gulf Coast.

Lastly, refining sector CEOs expressed optimism about the current operating environment generating free cash flow that can be used for dividend increases and share buybacks. One refiner, Delek Corporation, announced a $100 million share repurchase plan for the third quarter of 2018. Delek expects to have repurchased approximately 5% of its current market cap by the end of September.

Those are the 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@tortoiseadvisors.com.

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.

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

The MVIS US Listed Oil Services 25 Index is comprised of common stocks and depositary receipts of U.S. companies in the oil services sector. Such companies may include small & medium-cap companies and foreign companies listed in the U.S.