Tortoise QuickTake Energy Podcast

Dec. 3, 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.

Happy Holidays! It's time to breakout the classic holiday movies. In the can't miss movie during the holiday season, after Uncle Lewis burns the Christmas tree and receiving a jelly-of-the month club for an annual bonus, Clark Griswold declares to Ellen "We're on the threshold of hell." In some ways, this declaration is being made by oil traders after a month when oil prices fell by 24% representing the worst monthly performance since October 2008. Fortunately for energy sector investors, stock prices did not fall as much oil prices. The energy sector as represented by the S&P Energy Select Sector® Index fell by 1.7% in November while MLPs represented by the Tortoise MLP Index® declined by less than 1%. Now, while Clark Griswold appropriately assesses the recent oil price environment, we have experienced periods of sharp declines in oil prices before. During these periods, I tend to follow the wisdom of Winston Churchill who said "If you're going through hell, keep going". At Tortoise, we keep going. While oil prices are volatile, one thing remains the same: our unwavering conviction in the long-term potential of the U.S. energy sector.

Last week, the EIA released another record setting report for the U.S. energy sector. This record setting report further supports our strong long-term conviction in the sector. What am I talking about? The EIA reported the highest levels of U.S. crude oil and natural gas proved reserves in history. What are proved reserves? They are estimated volumes of oil and natural gas that can be recovered with reasonable certainty based on existing economic and operating conditions. Proved reserves of U.S. crude oil increased by 19.5% surpassing peak levels set in 1970. Proved reserves of natural gas increased by 36.1% exceeding records set in 2014. In my opinion, it is remarkable that these records are being set as the data is lagged by one year, so the 2017 records were set in a $50 oil price and $3 natural gas price environment. This report solidifies the U.S. as a low cost producer of energy. Over the next several decades, the U.S. will produce, transport and ultimately export many of these low cost proved reserves.

It's OPEC week with the 175th OPEC meeting scheduled for December 6th in Vienna, Austria. And here are our latest thoughts going into the OPEC meeting. When OPEC entered into its production cut agreement in November of 2016, WTI oil prices had declined into the $40s as a global oil glut emerged with oil inventories exceeding normal as represented by the 5-year average by 175 million barrels. OPEC's production cut resulted in an undersupplied global oil market that eliminated the glut returning global inventories back to normal. Throughout 2018, inventories have been at or below normal. Over the last two months, OPEC specifically Saudi Arabia raised production levels in anticipation of Iranian oil exports declining to zero in November. However, six month waivers granted by the U.S. to certain purchasers of Iranian oil resulted in continued Iranian exports of approximately 1.5 million barrels per day. This caused the global oil markets to become oversupplied. Global oil inventories are on the rise again and recently exceeded the 5-year average triggering the 33% decline in oil prices since October 3rd. So, how will OPEC respond? In theory, the solution seems simple. OPEC led by Saudi Arabia should alleviate the oversupplied market by reducing current production volumes by 1.5 million barrels per day. This would balance the global oil market and prevent a global supply glut from happening. If Iranian oil exports ultimately end up being reduced to zero, then OPEC could return necessary volumes back the market to prevent a price spike. In reality, a solution is more complicated. First, increasing or decreasing the oil supply is not like turning on your water facet. It takes months rather than seconds to increase or decrease the flow of oil. Second, Saudi Arabia needs other members of OPEC as well as Russia to agree to cut production. Often OPEC politics trump rational decision making leading to unpredictable outcomes. So, the billion dollar question is will OPEC announce a production cut on December 6th? We think OPEC will cut production by around 1.5 million barrels per day because it is actually a fifty-five billion question for Saudi Arabia. Saudi Arabia can continue to produce 11 million barrels per day of oil and earning $40 per barrel or they can reduce production to 10 million barrels per day and earn $60 per barrel. The simple math of lower volumes and higher prices results in an additional $55 billion of annual revenue. If OPEC chooses not to cut production, we would expect consumers to reap the rewards of having a little more money in their pockets for the holiday season as oil prices and gasoline prices likely fall by at least 10%. No matter what decision OPEC makes, we believe at Tortoise that the U.S. energy sector is in the initial stages of building a mountain of cash flow over the next several years to combat the wall of worry associated with the broad market and commodity prices. The mountain of cash flows increases the number of shareholder friendly options available to U.S. energy company management teams including raising dividends and stock buybacks. To achieve this mountain of cash flow, energy infrastructure companies like MLPs simply need the record level of U.S. oil and gas reserves previously discussed to be produced and transported over an expanding network of energy infrastructure assets. For oil and gas producers, a stable oil price around $60 per barrel and $3 per mcf for natural gas is necessary.

In my opinion, we are nearing the end of simplification transaction announcements. Last week, Equitrans Midstream announced a complicated simplification transaction. In a series of transactions, the newly created publicly-traded Equitrans Midstream Corporation ticker symbol ETRN announced an agreement with certain unitholders of EQGP Holdings, L.P. to acquire limited partner interests for $20 per unit in cash. Upon closing of these private purchases, ETRN plans to exercise the Limited Call Right under EQGP's partnership agreement allowing ETRN to acquire the remaining units of EQGP. ETRN will use cash proceeds from a Term Loan B to finance the purchase of the EQGP units. In addition, ETRN made a proposal to EQM Midstream Partners for the exchange of its IDRs for 95 million units in EQM subject to the closing of the previously mentioned purchase of EQGP units. The IDR buyout are subject to negotiation with the board of directors of EQM's general partner or its conflict committee. Once these transactions are closed, the number of ticker symbols for investors to invest in these energy infrastructure assets drops from 3 to 2.

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.

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.

MLPs = The Tortoise MLP Index® is a float-adjusted, capitalization weighted index of energy master limited partnerships (MLPs). 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 indices are the exclusive property of Tortoise Index Solutions, LLC, which has contracted with S&P Opco, LLC (a subsidiary of S&P Dow Jones Indices LLC) ("S&P Dow Jones Indices") to calculate and maintain the Tortoise MLP Index®, Tortoise North American Pipeline Index℠ and Tortoise North American Oil and Gas Producers Index℠ (each an "Index"). S&P® is a registered trademark of Standard & Poor's Financial Services LLC ("SPFS"); Dow Jones® is a registered trademark of Dow Jones Trademark Holdings LLC ("Dow Jones"); and, these trademarks have been licensed to S&P Dow Jones Indices. "Calculated by S&P Dow Jones Indices" and its related stylized mark(s) have been licensed for use by Tortoise Index Solutions, LLC and its affiliates. Neither S&P Dow Jones Indices, SPFS, Dow Jones nor any of their affiliates sponsor and promote the Index and none shall be liable for any errors or omissions in calculating the Index.

Disclaimer: *Nothing contained in this communication constitutes tax, legal, or investment advice. Investors must consult their tax advisor or legal counsel for advice and information concerning their particular situation. This podcast contains certain statements that may include "forward-looking statements." All statements, other than statements of historical fact, included herein are "forward-looking statements." Although Tortoise believes that the expectations reflected in these forward-looking statements are reasonable, they do involve assumptions, risks and uncertainties, and these expectations may prove to be incorrect. Actual events could differ materially from those anticipated in these forward-looking statements as a result of a variety of factors. You should not place undue reliance on these forward-looking statements. This podcast reflects our views and opinions as of the date herein, which are subject to change at any time based on market and other conditions. We disclaim any responsibility to update these views. These views should not be relied on as investment advice or an indication of trading intention. Discussion or analysis of any specific company-related news or investment sectors are meant primarily as a result of recent newsworthy events surrounding those companies or by way of providing updates on certain sectors of the market. Tortoise, through its family of registered investment advisers, does provide investment advice to Tortoise related funds and others that includes investment into those sectors or companies discussed in these podcasts. As a result, Tortoise does stand to beneficially profit from any rise in value from many of the companies mentioned herein including companies within the investment sectors broadly discussed.*