

Tortoise QuickTake EnergyPodcast



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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.

While the Ides of March were clearly unkind to MLP investors, at least fans of four universities can rejoice in March Madness as teams punched their ticket to the Final Four, including my Kansas Jayhawks. It was a sweet overtime victory against a national rival, but there is still work to be done. Maybe MLPs and midstream companies can follow suit and get some victories of their own as the first quarter of 2018 winds down.

To tip things off, I'll recap the market performance:

- On the commodity front, crude oil was strong, up approximately 5.6%, while
- Natural gas was weak, falling 3.6%
- Shifting to equities, the broader S&P Energy Select Sector[®] Index decreased 92 basis points
- Exploration and production companies, as measured by the Tortoise North American Oil & Gas Producers IndexSM fared better, higher by 1.6%
- And finally MLPs felt like fans of teams that came up one game short of the prize, as the Tortoise MLP Index[®] moved lower by 5.3%

Crude oil obviously had a big move last week, notably because of concerns of rising geopolitical tensions.

Perhaps most impactful, President Trump announced that John Bolton would replace HR McMaster as national security adviser. This was not long after the announcement of Mike Pompeo replacing Rex Tillerson as Secretary of State. The significance is due to both Bolton and Pompeo generally not being fans of the current nuclear agreement with Iran. Bolton has been highly critical of the agreement forged out by the Obama administration, which is why many believe there is a high likelihood that sanctions will be re-imposed on Iran.

Saudi Crown Prince Mohammad bin Salman visited President Trump on his U.S. tour, likely discussing Iran, fueling more speculation about the administration's views and potential actions on the current nuclear agreement.

Additionally, it's believed that Pompeo may consider further sanctions on Venezuela. Clearly already struggling in terms of crude oil production, additional sanctions could cripple production levels and drive them below one million barrels per day.

Crude also received continued support from OPEC members as Saudi Arabia and Russia both reiterated goals to extend the production cut agreement. Certainly too early to tell whether or not that will happen but the rhetoric out of OPEC has actually been pretty consistent in favor of extension and compliance remains quite high.

OPEC also discussed potentially changing the inventory target levels to be consistent with the seven year average inventory levels as opposed to the five year average levels. This is important because the five year average is somewhat elevated due to the last few years of extremely high inventory numbers. Extending to seven years will require further reduction and likely require the agreement to extend beyond the middle part of the year, when most pundits believe we will hit the five year average.

With refinery maintenance season almost over, inventories are close to switching to seasonal draws, with May historically starting the process.

In summary, crude oil clearly has multiple bullish signals for price and fundamentally continues to be very strong, despite the negative rhetoric from investors. One could say it resembles a team going into the tournament with a lot of momentum.

And if that is the description of crude oil, MLPs currently resemble the Cinderella story that no one believes in. Almost like an eleven seed trying to make the Final Four, or a sixteen seed attempting to take down a one seed.

One of my favorite Wall Street analysts said he has never witnessed a bigger disconnect between sentiment and fundamentals. The question we continually are getting from investors is “What am I missing?” Essentially, we get virtually zero pushback from investors that the fundamentals are pretty robust right now for midstream. However, clearly the sentiment is not nearly as good.

In fact, valuations are at levels not seen since February 2016 and as far back as the financial crisis of 2008. Something has to give.

What could those catalysts be? Most likely it will have to be continued execution by companies and proof that 1) they can consistently fund capex with limited access to public equity markets, 2) cash flow per unit grows on a steady basis and 3) the recent FERC decision is truly as benign as management teams’ are advising. For the record, as we have stated on this podcast as well as a special podcast, we independently came to the same conclusion as those same management teams.

What I can confirm is that last week I attended multiple finals presentations, met with other interested investors via phone and have a similar schedule this upcoming week as investor interest in the space is higher than I’ve seen in over two years.

Perhaps investors are paying heed to one of Warren Buffett’s famous quotes, “Be fearful when others are greedy and greedy when others are fearful.” I think it’s safe to say, much like during Buffett’s quote in 2008, investors are fearful in MLPs, so time to be greedy.

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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