Tortoise QuickTake Podcast

October 2, 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.

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

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.

Before we get started, we'd like to note our thoughts are with those impacted by the tragedy in Las Vegas.

After the weak first half performance of the energy sector, we have talked about the potential of a second half comeback. Now that the third quarter has ended, let's take a look at how the energy sector performed. The energy sector is showing signs of life. The sector as represented by the S&P Energy Select Sector Index® rose by 7% during the third quarter. Only the tech sector outperformed energy during the quarter. Even better - the tide is turning as investor sentiment toward the energy sector appears to be turning positive. For the month of September, the energy sector blew away the competition rising by 10% outperforming the S&P® 500 by 8%. Do you remember the last time that the energy sector delivered the best monthly performance relative to the other sectors within the S&P® 500? Let me give you a clue. Barack Obama was still the President and Ted Cruz and Bernie Sanders had just won the Wisconsin Primaries. It was April 2016.

Oil prices led the comeback in energy stocks as West Texas Intermediate or WTI rose by 12% during the third quarter and by 9% during the month of September. In fact, many news agencies have said oil is in a bull market as prices have risen 22% from a low of $42.31 on June 21, 2017.

Why such strong performance? Lots of variables that we have talked about in past podcasts are assisting in the recovery of oil prices including ginormous declines in U.S. and global inventories, rising global oil demand, lower OPEC imports. A variable re-emerged last week that is providing an extra boost for oil prices. This variable is kind of like the glaze that covers the famous Hostess Ding Dong chocolate cake. It provides the extra sweetener that we think could propel oil prices even higher in the future. What am I talking about? Geopolitical risk. In the past, geopolitical risk has added a significant premium to oil prices but has essentially disappeared since the OPEC 2014 Thanksgiving Day oil price plunge. Geopolitical risk was heightened last week with the Iraqi Kurds voting to declare independence from Iraq. In retaliation, Turkey threatened to block oil exports out of Kurdistan that could disrupt the flow of as much as 500,000 barrels per day. Additional geopolitical risk is present in Iran who is the third largest OPEC oil producer, producing over 4 million barrels per day. President Trump has suggested that Iran is violating the nuclear deal. Iran oil production has increased by approximately one million barrels per day after the sanctions targeting Iran's oil and gas sector were removed in early 2016. If sanctions were re-instituted on Iran's oil and gas sector then oil prices would likely move higher.

While oil prices propelled the energy sector in the third quarter, MLPs were unexpectedly left behind. MLPs as represented by the Tortoise MLP Index® declined by 2% during the quarter. In our view, MLPs continue to be perplexing. Ultimately, cash flow growth drives value and this is what MLPs do. At Tortoise, we believe that investors will reward companies that continue to increase dividends and distributions paid to shareholders.

As we shift to the third quarter reporting season for the energy sector, here are some things that are interesting to us here at Tortoise. Hurricane Harvey will likely be a popular topic. A few oil and gas producers provided some additional insight last week. Parsley and Noble Energy highlighted third-party pipeline issues that impacted production volumes as a result of Hurricane Harvey. Parsley adjusted third quarter production down by an immaterial amount of 2%. Once again, we don't expect Hurricane Harvey to have a material impact on any of our upstream or midstream investments. Other things of interest include U.S. oil and gas producers' outlooks now that WTI is above $50 per barrel. For perspective, WTI oil prices were below $50 per barrel for 84 of the 92 days of the third quarter. Consequently, the Baker Hughes rig count at the end of the third quarter is at the exact same levels as the rig count on June 30. Related to the midstream sector, MLPs and energy infrastructure corporations will provide updates on new infrastructure to support Permian Basin development including gathering and processing plants and pipelines. Last week, a relative unknown company, EPIC Pipeline, announced the newest potential natural gas liquid pipeline, stretching 650 miles, originating in the Permian with a destination of the Gulf Coast. Also, several strategic pipelines that are owned by private equity appear to be up for sale and could be nice additions to the asset profiles of many energy infrastructure companies.

Lastly, the Republicans released a framework for tax reform last week. While the details will be in the hands of the tax-writing committee, we still believe that MLPs will retain their favorable tax status. Based on the information released, we think MLP investors could benefit from the new tax framework as pass through income will be taxed at 25% compared to higher ordinary income tax rates today.

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@tortoiseinvest.com.

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The Tortoise MLP Index® 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.

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