Tortoise QuickTake Energy Podcast

Tortoise

April 16, 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.

Brian Kessens: Hello, I am Tortoise Managing Director and Portfolio Manager Brian Kessens with this week's QuickTake podcast. Green shoots were in the spring air last week in the energy sector. Broad energy moved higher by 6%, producers by 8% and MLPs found the green, up 3.2%. All bettered the S&P 500®'s gain of 2%.

Helping energy sentiment were crude oil prices, which ended the week up 8.6% to their highest levels since November 2014. Partly driving the increase was an increase in Middle Eastern tensions as rebels in Yemen stepped up attacks on Saudi Arabian infrastructure, and a chemical attack on Syria resulted in a strong Western response. Further, the IEA sees OECD stockpiles merely 30 million barrels above the five-year average and anticipates reaching the five-year average as early as May. Part of the reason for the quick drawdown is OPEC's strong 163% compliance with its supply cut agreement in March. That news outweighed the weaker U.S. inventory report indicating a crude oil build of 3.3 million barrels.

In midstream news, Kinder Morgan announced a halt to non-essential spending on their proposed TransMountain pipeline expansion following regulatory uncertainty. Unless regulatory clarity is put in place prior to May 31st, Kinder indicated it would not commit additional resources to the project. Both the federal government and Alberta stated strong support for the project with British Columbia continuing to call for more study. We think the TransMountain project and other takeaway projects are acutely needed for Canada to economically continue to grow its crude oil production. Increasingly, Canadian volumes are being placed on higher cost rail, driving the price differential between WTI and Western Canadian crude to $15 per barrel currently, though the differential has been as high as $25 this year.

Magellan Midstream held the only analyst day last week. The day started off by reemphasizing that the company does not expect a material impact from the FERC income tax allowance policy change and that management believes the best corporate structure for Magellan is an MLP. You can tell what is on investors' minds. Regarding crude oil. Magellan noted a price spread of greater than $4 per barrel between Midland and Houston. That is supportive of producers shipping barrels on a spot basis. Magellan also noted the key to its proven track record is the stability of its underlying business and focus on growing fee-based activities while managing for the long-term through business cycles. Finally, after targeting 8% distribution growth in 2018 with 1.2x distribution coverage, in the future, the company plans to manage distribution growth in-line with DCF growth projections of 5% to 8% per year.

In upstream news, Diamondback Energy pre-announced a solid first quarter production number versus expectations. Some concerns remain about adequate takeaway capacity out of the Permian given Midland to Cushing spreads are above $4 per barrel. Diamondback indicated 90% of its production is on pipelines versus rail and trucking – it should be insulated from the issue.

In LNG, Dominion Energy looks ready to ship its first commercial cargo from its Cove Point Maryland terminal. Two tankers are scheduled to arrive over the next week.

We keep saying the fundamentals in midstream are healthy and this week demonstrates that – basis differentials remain wide in Canada and the Permian. This indicates a strong need for more takeaway capacity, so much so that the Canadian government is promising financial backing for TransMountain. We expect midstream capital investment to continue at a robust level.

This week, energy first quarter earnings begin with Kinder Morgan and Schlumberger announcing results on Wednesday and Friday respectively. At Kinder, we'll look for any update on TransMountan and the company's views for free cash flow – stock buybacks versus debt pay-down. At Schlumberger, we'll be looking for signs that U.S. service activity is accelerating and whether international activity is starting to turn for the better. We expect the forecast to outweigh any first quarter weather related softness. Thanks for listening.

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 500® Index is a market-value weighted index of equity securities.