Tortoise Capital Advisors

Tortoise QuickTake Podcast

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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.

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

The oil bulls found several May flowers last week, citing another drop in the US rig count by 5, raging wildfires in Northern Alberta Canada impairing upwards of 1 million bpd of crude oil (check out the videos on YouTube if you want to see a scary reality) and US oil production continued its downward trajectory, falling 113,000 bpd week on week to 8.8 million bpd, though a majority of the decline was in Alaska with 30,000 bpd of the decline coming from the lower 48.

On the demand side, the EIA reported that in February US gasoline demand rose at the fastest annual rate in almost 40 years. At 9.2 million bpd, it is up 556,000 barrels a day from a year earlier, the biggest annual increase since 1978. Also, estimates are that global vehicle sales reached a record in March at 8.9 million, surpassing the peak set in March 2015.

Yet the bears won the argument with WTI down 2.8% after crude oil built more than analyst estimates at 2.8 million barrels and OPEC did not commit to anything at the forthcoming June 2 meeting. And over the weekend, it was reported that Saudi Arabia dismissed its long-serving oil minister Ali al-Naimi. This suggests a potential production 'freeze' is even less likely.

Following the oil price decline, producers were lower by 5.8%, broader energy by 3.0%, and MLPs off the least by just less than 1.0%.

In capital markets, MLPs tested the waters with one common equity offering as Phillips 66 Partners raised $575 million. Proceeds were used to fund an accretive dropdown. Given the deal was upsized, indicating healthy demand, we would not be surprised to see more offerings post earnings from MLPs with visible growth.

The Energy Transfer / Williams epic added another chapter. On Energy Transfer's earnings call, it was verbally confirmed that Latham and Watkins would not be able to deliver an opinion related to the tax-free nature of the transaction, a requirement to close the merger. Hence there is apparently no deal. Our working assumption is that the deal does not close, yet we think the script writers are anxiously writing the next chapter.

Last week was the largest for reported first quarter energy earnings. Producers continued to improve productivity and capital efficiency which remained a central theme. Due to this focus, production consistently came in higher than expected with companies marginally increasing full year production guidance, especially for those operators in the Permian basin. A few producers also noted that they would put rigs back to work at crude prices above $45 per barrel, with others indicating $50 per barrel needed. The biggest question will be how fast the service companies can facilitate given the reduced human capital available. Notably, services companies believe the second quarter will emerge as the lowest from a business perspective.

On that note, the biggest oilfield service news related to the largest deal in the sector. Halliburton confirmed it is abandoning its of acquisition of Baker Hughes. Industry complaints, objections in Europe and a law suit from the Department of Justice led to the decision. As a result, Halliburton is paying the $3.5 billion break-up fee and moving on.

Also, upstream deal flow activity is picking up though asset packages have a mix of quality. A good example is the largest natural gas purchase last week. EQT paid $400 million for Marcellus acreage from Statoil. To finance it, EQT reduced its overall leverage, raising $700 million in equity proceeds – by far the largest producer equity deal of the week.

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In midstream, earnings generally exceeded expectations. Notably, liquids volumes transported were weaker in the Eagle Ford, yet remained resilient in the Permian. Capital expenditures continue to be deferred where there is producer agreement and as expected, export infrastructure continues to ramp for ethane, propane, and LNG. All in all, the sense is investors are looking past near-term volume declines to a healthier US energy sector in the second half of 2016 and 2017. One CEO summed the industry's future best, stating, "We do not need 50 rigs drilling thousands of wells per year. It will take far less capital to grow production at strong double digit rates…we can return to triple digit direct rates of return with oil as low as $60 per barrel and if history is any indication, we will continue to push the oil price needed for triple digit returns, even lower."

This week, our thoughts and prayers are with those residents and families in Alberta displaced from their homes due to the widespread fire. We'll be looking for industry implications from those fires and following the last week of first quarter earnings.

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

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