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.

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

We have certainly entered the dog days of summer as temperatures are routinely hitting triple digits in many parts of the country, especially when considering the humidity. With Republican and Democratic conventions also taking place over a two week time frame, it feels like the heat is on everywhere. Likewise, we are entering another earnings season, which kicked off this past week. Similar to the baseball season, we are a little past the halfway point and companies are looking to finalize plans, build for the future and set themselves up for a strong stretch run to end the year.

Let's take a quick look at performance:

- On the commodity front, crude oil was down almost 4% as sentiment continues to be negative, while
- Natural gas performed well due to the aforementioned heat, plus .76% for the week
- Shifting to equities, the broader S&P 500 Energy Select Sector® Index finished lower, down -1.3%
- Exploration and production companies, as measured by the Tortoise North American Oil & Gas Producers IndexSM, also declined, down -2.1%
- And finally MLPs edged higher as the Tortoise MLP Index® finished up .82% last week

On the commodity front, crude oil continued to retrace from its highs in early June, when it was briefly over $50 per barrel. Concerns seem to be centered on a potential gasoline inventory glut despite peak seasonal demand. The narrative is based on the warm winter weather and resultant weak diesel cracks forcing refiners earlier in the year to shift away from the normal seasonal diesel production and instead favor gasoline. The result was a build of gasoline and while demand has been strong, it has not been enough to overcome the negative sentiment. Despite concerns, gasoline inventory levels are still within the 5-year range and just a few days above normal on a days-supplied basis when factoring in the current higher level of overall demand. With refinery maintenance coming up in September, this definitely is something to watch for in regards to near-term crude oil prices.

Weather continues to drive natural gas prices higher. We are almost exactly half-way through the natural gas injection season where storage typically rebuilds after drawing all winter. Per the EIA, injections so far have been almost 30% lower than the five year average. Warmer than normal weather as well as a low gas price has led to significant power burn and coal to natural gas switching. With the rebound in natural gas prices however, coal has become economical again in some parts of the country, yet midway through the season the inventory balance has been trimmed substantially and provides an avenue for natural gas to get back closer to balance by the end of injection season in early November.

Earnings season kicked off with the largest midstream company, Kinder Morgan, posting earnings this past Wednesday and the two largest oil field services companies, Haliburton (Ticker: HAL) and Schlumberger (Ticker: SLB) reporting Wednesday and Friday, respectively.

Kinder Morgan had an in-line quarter from an EBITDA and earnings perspective. Some of the key highlights we noted included:

- Product pipelines were 8% higher year over year in terms of earnings
- Natural gas volumes were up 5% year over year on strong demand for power burn
- Debt to EBITDA is now projected to end the year at 5.3x versus the previous estimate of 5.5x due to joint ventures on some projects and assets
- And finally, Kinder expects projects in the backlog to generate a 6.5x EBITDA multiple, which is very attractive for midstream projects

Moving to oil field services, both HAL and SLB reported this past week and while results were generally fine, the real story was the bullish call by both management teams that the bottom had been reached in the oil patch and customer sentiment, which refers to E&P companies, had turned more bullish of late.

As HAL's CEO noted, "Our customers are thinking about growing their business again rather than being focused on survival."

Similar sentiment was echoed by SLB's CEO when he stated, "We have seen a slow but steady increase in oil prices as the market data continues to show a tightening of the supply and demand balance, and with the outlook clearly suggesting that these trends will further accelerate going forward."

Note, we haven't exited the downturn yet by any stretch, but perhaps we have found the bottom and can now start the recovery.

Another confirmatory weekly rig count report showed an increase of 15 rigs in the U.S., including 14 on the oil side. It was the 4th consecutive increase and 7th in the last 8 weeks, per Baker Hughes.

That's certainly a positive trend, but we should note, the impact of those rigs won't be felt for likely 6-9 months, which is consistent with our thoughts of a crude production recovery starting in 2017.

Earnings season will really start to pick up in the coming weeks, wrapping in mid-August.

Finally, as the only company to host an analyst day last week, Sempra Energy highlighted their continued opportunities in Mexico as well as LNG. Notably, they expect Cameron LNG to begin operations in 2018, yet another milestone for U.S. LNG exports.

And with that, we hope you stay cool and make it through the dog days of summer. Thanks for listening and we look forward to speaking with you again 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

The S&P Energy Select Sector® Index

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.

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The Tortoise North American Oil & Gas Producers IndexSM is a float-adjusted, capitalization weighted index of North American energy companies primarily engaged in the production of crude oil, condensate, natural gas or natural gas liquids (NGLs). The index includes exploration and production companies structured as corporations, limited liability companies and master limited partnerships but excludes United States royalty trusts.

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