TortoiseEcofin QuickTake Podcast

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Welcome to the TortoiseEcofin QuickTake podcast. Thank you for joining us as we provide timely updates on the market.

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

We are officially in the dog days of summer, with July and August heat hitting all over the country. Thank goodness for the Olympics to keep us busy with something to watch until the football season starts. Needless to say, it's not much fun watching the Royals battle to stay out of last place in their division. But the United States performed with usual excellence in Japan, hoisting the most medals yet again, for the seventh consecutive Olympics. I keep hoping maybe one day American football can be contested in the Olympics…now that would be fun.

Moving to the markets, let's start things off with performance for the week that was:

- On the commodity front, crude oil was down sharply, with prices falling 7.7%, while
- Natural gas was positive on spot prices, trending higher by 7.5%,
- Shifting to equities, the broader S&P Energy Select Sector Index® was just in the green, higher by 36 bps, but near the bottom of the S&P sectors
- Exploration and production companies, as measured by the Tortoise North American Oil & Gas Producers Index℠ were essentially flat, down 8 bps
- Utilities, per the Dow Jones Utility Index, outperformed, increasing 2.2% and near the top of S&P sectors
- And finally MLPs, as represented by the Tortoise MLP Index® finished in negative territory, lower by 3.5% for the week, despite continued earnings beats

I'll start with the big picture and work our way down. Of course the dominant theme of late has been the delta variant of Covid-19 and its rapid spread. Let me first state, we are only evaluating this topic on the basis of its impact to financial markets, so please keep that in mind. The concern from that end is the potential impact on economies if we experience more lockdowns. In highly vaccinated countries, it would appear lockdowns will not be needed, but in other areas, such as Asia, some countries are being hit harder with less of the populace vaccinated. In the United States we are currently in a period of rising case growth, yet mobility does not appear to be changing much at this point. Even in states that have been harder hit, such as Florida, foot traffic remains at similar levels of just a few months ago.

The key will be to watch hospitalizations and deaths. If the U.K. is any type of indicator of what we might experience here in the U.S., the spike in cases is quick and the move lower has been fast as well, yet it has not led to anywhere close to the same level of deaths. Of course every country is different, yet the U.K. has experienced about 91% fewer deaths than the prior peak from January based on a 3 day moving average. Many analysts are estimating the U.S. will peak in either late August or September. Despite the rise in cases, several of the big banks, such as JP Morgan, believe the impact will be transitory and not change the overall recovery.

Tied in very closely with the delta variant concern has been the move in the 10 year treasury. We were seemingly on our way to 2% yields before the news started to pick up around the latest virus concern. Since that time, it's been a sharp reversal, moving from 1.6% in early June to a recent low of 1.17% earlier in the week. A strong jobs report, with the unemployment rate dipping to 5.4%, helped push the 10 year yield back higher, finishing the week at 1.3%. The energy markets have been linked to an extent with the 10 year, moving in tandem with the yield. Lower 10 year yields, lower energy markets. This makes some sense as the energy trade has been tied to the reopening of the economy and of course when things look dicey, the 10 year yield drops as investors flee to safety.

We also had some movement on a potential bipartisan infrastructure package, with details still being hammered out. Agreement seems to be coalescing around a $550B package of new spending, of which about 20% would be energy related.

Most of that would be directed towards transmission, but carbon capture was able to carve out a nice chunk of change as well.

I noted oil had a rough week and that was directly tied to the rise in the delta variant, specifically concerns in China. On the other side of the coin, the Iranian situation continues to worsen. Matt noted a few weeks ago we appeared to be getting further away from a deal and this past week only drove that home even more, with Iran being blamed for a recent tanker attack. Hard to handicap geopolitical issues, but it feels like a deal that would bring more Iranian barrels back on the market is not even remotely close at this point.

Finally, it was a crazy week of earnings for the energy sector, with over 60 companies reporting. Obviously that's a lot to go through, so I'll just throw out some key takeaways from the busiest week of the quarter for earnings.

- On the upstream front, the rhetoric was very stable and consistent; muted production growth, lower leverage and increased capital returned to shareholders
    - Similar to Rob's comments last week, companies continued to emphasize discipline
    - Showing up strong was Devon Energy, with a fixed plus variable dividend payment that equates to a robust 7.5% yield
    - The theme from this last week was to raise production guidance, while lowering capex, which happened with several companies
    - Additionally, the higher commodity prices are allowing for a much faster deleveraging than many anticipated
- On the midstream front, the theme was also pretty similar to last week, earnings beats for the quarter and a consistent refrain of either raising full year guidance or declarations of coming in at the high end of previously provided guidance
    - We continue to see lots of excess free cash flow after dividends being generated
    - Which is being put to work mostly to reduce leverage
    - However, some companies are executing on share buybacks, such as the highest for the quarter, MPLX, buying back yet another $150M plus of stock, pushing their total to $343M in under 9 months' time

In general, earnings for the 2nd quarter have gone exceptionally well, despite the stock prices not reacting accordingly. Another case of the macro outweighing the micro, i.e. delta variant concerns.

That will change though, as investors catch-up to the cash flow generation capability of the energy sector.

With that, 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 episode. Have topics you want covered or other feedback to share? Write us at info@tortoiseecofin.com.

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The Dow Jones Utility Average is a stock index from S&P Dow Jones Indices that tracks the performance of 15 prominent utility companies traded in the United States.

Broad Energy = 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.

Producers = Tortoise North American Oil & Gas Producers Index℠
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