May 2, 2022

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

Good to be with you today, I am Quinn Kiley, Managing Director and energy Portfolio Manager at Tortoise and I am happy to host this week's QuickTake Podcast. Having entered earnings season, we are experiencing dramatic volatility in all areas of the market. Crude oil as measured by the West Texas Intermediate (WTI) front month contract oscillated from a low of $95 per barrel to a high of $105. The ten-year U.S. Treasury yield traded from just shy of 3.0% down to 2.7% and then back up to 2.9%. The NASDAQ Index was down over 6% at one point last week with many of its names moving up or down double digits in a single trading day throughout the week. Earnings weren't the only driver of volatility last week. Uncertainty around China's zero-COVID policy lockdowns and the Commerce Department's estimate that U.S. GDP contracted in the first quarter by 1.4% despite positive consumer sentiment reports during that period. Consensus had been for an increase of one percent in Q1. The main drivers of the contraction were weak net imports and lower government spending, both of which economists view as transitory. Markets continue to be concerned about a hawkish Federal Reserve, those views were supported by Friday's release of the Personal Consumption Expenditure index. The index was higher by 6.6% year-over-year, a forty year high.

The result of all the volatility last week was weaker markets:

- The Alerian MLP Index lost -3.2%, and the Index now sits up 18.5% for the year
- Other energy stocks, represented by the Energy Select Sector Index, were down -1.3% for the week
- In broader markets, the S&P 500 was down -3.3%

As I mentioned earlier, earnings announcements are starting to ramp up and there were some notable reports last week. I'll start with the oil majors ExxonMobil and Chevron, both of which reported last Friday. Exxon reported a slight miss on earnings per share, perhaps a surprise given strong energy commodity pricing during the quarter. The miss appears to be due to timing of certain cash flows and weather; analysts expect both of these issues to rebound in the second quarter. Importantly, the company continues to pay down debt maturities and indicated a tripling of its share repurchase plan to $30 billion. Chevron missed on earnings as well. The company did report production growth in the Permian basin which is encouraging. Chevron signaled some confidence in the business by suggesting that their share buybacks would come in closer to $10 billion compared to the previous range of $5-$10 billion. Both companies reported some poor international results offset by domestic strength and a strong outlook. All in all, the reports suggest some short-term weakness with a constructive long-term framework.

On the refining front we had two notable earnings reports from Valero and Phillips 66. Both companies beat expectations as they are advantaged relative to international peers by the structurally cheaper natural gas price environment in the U.S. Other similarities include a continuation of debt pay downs and a resumption of share repurchases. Phillips is the most diverse U.S. refiner and interestingly they reported higher than expected earnings from their sizable midstream business, perhaps a positive read through to the midstream companies we own. The outlook for U.S. refining is positive given strong recovery in demand post pandemic and lower cost feed stocks compared to international competitors.

We had some initial reports from the upstream subsector last week. EQT reported a positive quarter and very strong long-term outlook. The $14.5 billion market-cap company projected it would earn $17 billion in free cash flow over the next five years. With that outlook, the company will continue to pay down debt, grow its dividend, and buy back its public shares. The earnings call spent considerable time on the potential to "unleash U.S. LNG exports." The idea being that ample and cheap U.S. natural gas can be exported around the world to replace coal as a fuel to produce electricity. This replacement of coal by natural gas is already occurring in the U.S. and is the single largest contributor to reducing greenhouse gas emissions. If a policy is taken to enable U.S. natural gas to reach more global markets, this could prove positive for U.S. natural gas producers and the environment overall. Range Resources reported last week, as well. The commodity back drop was a tailwind for Range, as it was for EQT. Perhaps the most interesting part of Range's call was around valuation. Range declared that using quarter-end strip commodity price the present value of their proved reserves, or PV10, per share was $60 per share. This is striking because the company trades at about $30 per share currently and the PV10 only accounts for drilling on proved reserves for the next five years. Range has decades worth of drilling sites on its proved reserves and resources above and beyond those that are not accounted for in PV10 calculations. Needless to say, Range is not unique in this regard and their report is just another indication that U.S. energy companies remain significantly undervalued.

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Midstream was relatively quiet on the earnings front last week. Hess Midstream announced in-line earnings and re-affirmed 2022 guidance. The big take-away was the recent impact from severe winter weather in recent weeks. Production in North Dakota was severely restricted as a result and second quarter volumes could be impacted. As of today, we understand that production is recovering, but investors should be mindful of the impact that weather could have on Bakken producers and midstream service providers in the second quarter. There was bad weather in the first quarter as well, and CEQP posted a slight miss as a result. Contrary to Hess, CEQP did not flag recent April weather as negatively impacting activity on their acreage. We will see which narrative prevails as company announcements from the Bakken continue. Multiple midstream companies announced distribution or dividend increases last week, including a 14% increase from Energy Transfer. While we would like to see more equity buybacks, midstream companies seem to be focused on returning cash to equity holders through increased pay outs. TC Energy posted a slight miss versus consensus expectations for the first quarter. Capital expenditures are pushing higher for the company, in part due to inflation impacts. A positive takeaway from the announcement was high utilization of the company's U.S. midstream assets; again, a good read through for the U.S. midstream companies we own. Finally, Enterprise Products announced strong first quarter earnings this morning. The company had recently held an investor day, so the fact that they did not change guidance is not surprising.

The war in Ukraine continues to impact the global energy outlook. Last week Russia cut off natural gas supply to Poland and Bulgaria, perhaps foreshadowing other preemptive restrictions of supply to Europe. On the crude oil front, the European Union is discussing a plan to replace Russian supply by year end. Both of these developments lead to a world long on demand and short of supply for oil and gas and could set us up for a higher price environment as the year progresses. Thanks for joining us and we will be back next week. Please stay safe.

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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