MIDSTREAM Monitor

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FEATURES

The Old Is New For Energy

PAUL HART
HART ENERGY

AUSTIN, Texas—Like the song, everything old is new again for oil and gas. The business is re-entering an age of energy abundance much like the 1950s and 1960s and that's good news for the midstream, according to the chief economist of Houston-based Phillips 66 Co. (NYSE: **PSX).**

Horace Hobbs, speaking April 16 at the 97th annual convention of the GPA Midstream Association, said energy executives "need to change the way they think" as production swells from unconventional shale plays. He said the switch "is a whole new phenomenon" for nearly everyone in oil and gas because for 45 years the industry has been focused on supply following the OPEC embargo during the 1973 Yom Kippur War. That spans the careers of nearly everyone in the business today.

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Now, the question is finding demand.

"We have been exploring for oil in the Arctic and deepwater offshore, we don't need to do that anymore," Hobbs said. "It's a substantial change in the way we think." Development of the shale plays has become predictable "mining" in comparatively easy-to-reach, land-based plays, he noted. The shales' abundance means swelling proved reserves that go out 30 to 40 years, even with no additions.

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The economist was one of many speakers to present at the sector's largest annual conference. The event drew more than 2,200 attendees, its largest crowd in several years.

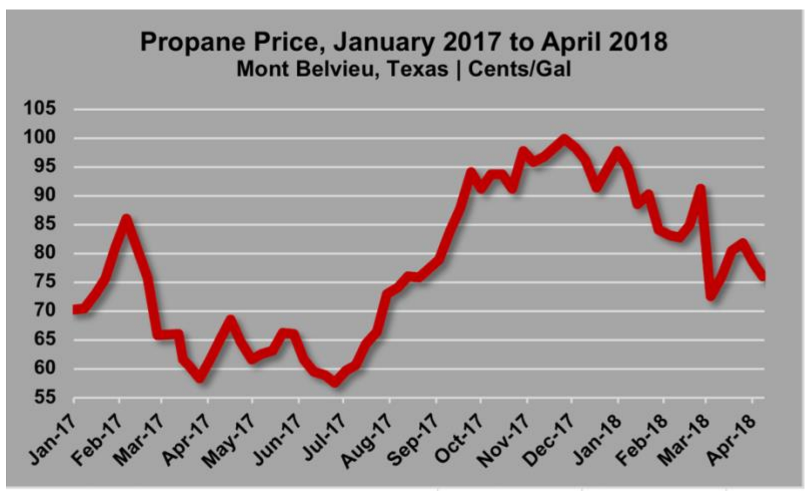
Hobbs admitted he and other energy economists have struggled to understand how a demand-based energy business works since their careers, too, have focused on supply. His research meant multiple trips to dingy warehouses full of yellowing records in Bartlesville, Okla., the headquarters of Phillips 66's predecessor, Phillips Petroleum Co. In the 1950s and 1960s, Phillips was one of the nation's premier refining and marketing firms.

"I hated going to Bartlesville," Hobs quipped, since his trips meant hours of work digging through dusty files in old boxes, studying the time when Phillips was an integrated major and one of only two firms to market petroleum products in all 50 states. The other firm to accomplish that remarkable feat was Texaco. ■

Threatened Tariffs Could Shake Up Markets

China's threat to impose tariffs on U.S. propane and polyethylene is unlikely to have a significant near-term impact on exports, an analyst said.

But the U.S. could be hurt if China decided to place tariffs on LNG to retaliate for U.S.-imposed tariffs on steel, Uday Turaga, founder and CEO of **ADI Analytics LLC,** told Hart Energy.



Source: Bloomberg, Hart Energy

"If China would have put a tariff on LNG I think that would have had some impact because LNG markets are oversupplied right now," Turaga said. "China buys a lot of LNG so it could have hurt them a lot more which is why they probably didn't look at LNG."

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Many experts, including Turaga, question the wisdom of trade wars in general. On April 16, top diplomats of China and Japan issued a statement that a trade war could have serious consequences for the world economy. A **piece by Philippe Legrain** in *Foreign Policy* opined that the U.S. had much more to lose than China if one erupted.

While ample supplies are available, especially from Australia and Qatar, U.S. LNG is proving to be more competitive on the global market than other suppliers, Turaga said. China has also made it clear that it doesn't want to be locked into one supplier.

"They try to go after a wider range of sources," he said.

Turaga said he believes that the threat against propane and polyethylene, two of 106 items that could be subject to Chinese tariffs, are mostly symbolic.

"It seems that China went after commodities that they can buy easily [elsewhere]," he said. "The U.S. can find other buyers for [these commodities] so the impact of this is small." **—JOSEPH MARKMAN** | HART ENERGY

FRAC SPREAD

What's In Storage? Not Much, It Turns Out

JOSEPH MARKMAN | HART ENERGY

NGL prices rose across the board last week as the Middle East heated up and the northern half of the U.S. cooled off.

Ethane cracked 27 cents per gallon (gal) at Mont Belvieu, Texas, for the first time since the end of January with the margin improving by 8.85% to about 9 cents/gal. The hypothetical NGL barrel climbed above $31 for the first time in seven weeks.

CURRENT FRAC SPREAD (CENTS/GAL)

APRIL 20, 2018	Conway	Change from Start of Week	Mont Belvieu	Last Week
Ethane	14.95		27.00	
Shrink	20.25		18.02	
Margin	-5.30	19.23%	8.98	8.85%
Propane	68.83		81.70	
Shrink	27.97		24.89	
Margin	40.86	16.59%	56.81	10.59%
Normal Butane	73.03		86.85	
Shrink	31.67		28.18	
Margin	41.36	6.90%	58.67	9.12%
Isobutane	107.95		91.80	
Shrink	30.42		27.06	
Margin	77.53	7.47%	64.74	7.98%
Pentane+	151.10		152.14	
Shrink	33.87		30.13	
Margin	117.23	4.56%	122.01	7.32%
NGL $/Bbl	27.62	8.18%	31.22	6.17%
Shrink	11.16		9.93	
Margin	16.47	7.89%	21.29	8.73%
Gas ($/mmBtu)	3.05	8.61%	2.72	1.06%
Gross Bbl Margin (in cents/gal)	37.26	8.44%	49.38	8.89%
NGL Value in $/mmBtu (Basket Value)				
Ethane	0.82	5.28%	1.49	3.53%
Propane	2.39	13.21%	2.84	7.50%
Normal Butane	0.79	7.63%	0.94	6.37%
Isobutane	0.67	7.79%	0.57	5.85%
Pentane+	1.95	5.44%	1.96	6.02%
Total Barrel Value in $/mmbtu	6.62	8.61%	7.79	6.09%
Margin	3.57	8.62%	5.08	9.00%

Price, Shrink of 42-gal NGL barrel based on following: Ethane, 36.5%; Propane, 31.8%; Normal Butane, 11.2%; Isobutane, 6.2%; Pentane+, 14.3%, Fuel, frac, transport costs not included. Conway gas based on Midwest region, Mont Belvieu based on Houston region. Shrink is defined as Btus that are removed from natural gas through the gathering and processing operation.

Traders have a tendency to react to instability in inherently unstable regions but this time, **En*Vantage** notes, prices should be rising because demand is going up as supply is going down. That statement may seem peculiar because U.S. oil production, particularly in the Permian Basin, is on the upswing. Global production, however, is not because Venezuela continues in a downward spiral, both in production and in social fabric.

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Notice how nobody uses the term "overhang" anymore? Global inventories of crude were 302 million barrels (MMbbl) above the five-year average in January 2017. This January, inventories were only 53 MMbbl above the five-year average. In the U.S., this trend translates to a 25.2 day supply of inventory, compared to the five-year average of 28.9 days, En*Vantage notes.

The natural gas differential is sharper. In the week ended April 13, storage of natural gas in the Lower 48 experienced a decrease of 36 billion cubic feet (Bcf), compared to the Bloomberg consensus forecast of 24 Bcf, the U.S. Energy Information Administration (EIA) reported.

The figure resulted in a total of 1.299 trillion cubic feet (Tcf). That is 38.3% below the 2.107 Tcf figure at the same time in 2017 and 25.7% below the five-year average of 1.748 Tcf.

Infrastructure Overhaul Key To Mexico Energy

HOUSTON—As energy reform in Mexico forges ahead the critical hurdle remains finding investors to help overhaul the lagging infrastructure in Mexico.

With U.S. oil and gas companies getting set to move in after 80 years of Pemex's monopoly, it's clear that midstream infrastructure must be improved, and in some cases installed, to get the lucrative export business moving in Mexico. Experts at King & Spalding law firm's Mexico Energy Forum in Houston on April 12 warned that political uncertainty on top of other challenges are making the beginning of the reforms challenging, but the return on investment will be substantial for the early investors.

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"There are all of these risks involved but that's just because of the emerging development," said King & Spalding partner Vera de Gyarfas, whose firm handles a lot infrastructure projects. "Project development is hard but if you are coming in first you are going to have a much bigger profit than when the market is stable."

There is definitely the opportunity for big gains, but there are major risks especially with the political uncertainty ahead in Mexico. Current Mexico president Enrique Pena Nieto was instrumental in opening up the energy sector as part of his economic agenda during the 2013-2014 legislative overhaul.

But leftist Andres Manuel Lopez Obrador, who is the frontrunner for the July 1 presidential election, has threatened to undo the reforms once in office. **—TERRANCE HARRIS | HART ENERGY**

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