MIDSTREAM Monitor

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FEATURES

'Year of Recovery'

PAUL HART
HART ENERGY

SAN ANTONIO—This has been "a year of recovery" for the oil and gas business. The current trends have created "positives for global growth" in future years, according to John England, partner and vice chairman for the U.S. oil and gas practice of Deloitte during a wide-ranging review of the global economy in general and the oil and gas business in particular at Hart Energy's DUG Eagle Ford conference and exhibition.

"If you're like me, I was impacted pretty heavily by [Hurricane] Harvey last year," the Houston-based executive said. "A lot of people in this area are recovering from a natural disaster, or from an epic downturn in our industry. We've all been in recovery mode; 2018 is certainly that year."

There are indications that the future will be better, he said, noting the stock market hit record highs the same day as his presentation (Sept. 20), while crude oil prices continue to climb. The benchmark Brent crude oil price has climbed to nearly $80/bbl this year while West Texas Intermediate has topped $71/bbl.

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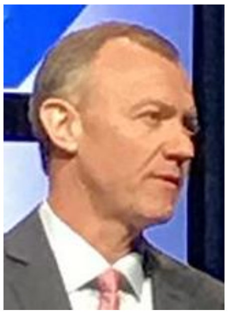
But offsetting those positives "are trends we didn't expect." One of particular concern to England is unsettled currency markets. Why should the industry care about currency exchange rates when its products, worldwide are bought and sold in dollars?

"Because demand growth primarily comes from emerging markets and it's important that emerging markets have stable economies," he said. "That's critical to the overall demand that is creating this recovery that we have had."



Another offset "is this trade war that's going on," England added. "That hits us on two fronts. One is it puts a wrench in the overall global economy. Global trade is critical to making the global economy—and the U.S. economy—work. When there is a slowdown, it hurts. Second is the direct impact on a lot of things in our industry. It makes many of the materials and services we need to buy more expensive."

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Of particular concern is China's proposed 10% tariff on U.S.-produced LNG, which could go as high as 25%. That may not be a big concern now, given China buys a small slice of American LNG production, "but we're looking to China to underpin a lot of the future Gulf Coast LNG terminals. So it could be a big deal going forward as it makes it harder to get those plants built."

Also, energy stocks "have not followed the path upward" as the stock market, overall, soared this year. That's due to "a lack of confidence by the public" about the ability of oil and gas players to be consistently profitable. "They're in a 'show me' phase," he added.

If the industry's current economic recovery has been hard, there's a reason.

"The downturn we just went through was not like any downturn we've ever had before," England said. Industry old timers may shrug it off as just part of the industry's cycle but this industry collapse was special.

"It was longer than any previous downturn. The time to the bottom was 404 days, longer than any previous downturn. And we're still not back to the peak of over $100 [per barrel]. So it was really unique," England explained.

Analyst Sees Shorter Crude Market Cycles

The U.S. oil and gas industry is about to get even bigger in the next decade, with the country continuing to grow in its role as a global energy superpower. Domestic producers have been exporting gas, liquids, crude and petrochemicals, and these volumes will keep growing.

What will the impact be on prices? At first glance it would be easy to predict they'll go up as the U.S. gains market share in various regions. However, other countries are also increasing their export volumes, demand dynamics are changing and there are important geopolitical considerations that will impact pricing in both the short and long terms.

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"We'll start to see shorter cycles in the crude oil market so that instead of 15-year cycles, we're going to see three- to four-year cycles," Dan Lippe, managing partner, Petral Consulting Co., told Hart Energy.

That may sound like the market will become less orderly, but that's far from the case. In many ways, the global crude market is about to become both more competitive and more efficient. And the biggest driver of this change will be production out of West Texas, according to Lippe.

"West Texas is the only place that matters. Production in the region has increased so much that all of the pipelines are full. Fortunately, we're building new pipeline like mad and should have at least an additional 1 million barrels per day [bbl/d] of additional crude pipeline capacity by the end of next year. New capacity will start to alleviate the current constraints, which have slowed down the growth rate in West Texas crude production," he said. What's most impressive about West Texas is that even with this slowdown, the annualized growth rate for the U.S. overall in second-quarter 2018 was still an impressive 1.5 million bbl/d. —**FRANK NIETO** | CONTRIBUTOR

FRAC SPREAD

Trump Challenges Oil Prices

JOSEPH MARKMAN | HART ENERGY

The president spoke and oil prices dropped.

"OPEC and OPEC nations, are, as usual, ripping off the rest of the world, and I don't like it," President Donald Trump told the United Nations General Assembly on Sept. 25. "Nobody should like it. We defend many of these nations for nothing, and then they take advantage of us by giving us high oil prices. Not good.

"We want them to stop raising prices," the president continued, "we want them to start lowering prices, and they must contribute substantially to military protection from now on. We are not going to put up with it—these horrible prices—much longer."

CURRENT FRAC SPREAD (CENTS/GAL)				
SEPTEMBER 28, 2018	Conway	Change from Start of Week	Mont Belvieu	Last Week
Ethane	10.75		46.80	
Shrink	18.87		19.73	
Margin	-8.12	49.48%	27.07	-15.08%
Propane	77.75		105.50	
Shrink	26.07		27.26	
Margin	51.68	-1.25%	78.24	-2.70%
Normal Butane	93.95		121.00	
Shrink	29.51		30.86	
Margin	64.44	2.77%	90.14	-1.45%
Isobutane	124.85		128.58	
Shrink	28.35		29.64	
Margin	96.50	0.03%	98.94	-17.41%
Pentane+	132.20		156.47	
Shrink	31.56		33.01	
Margin	100.64	10.57%	123.46	4.48%
NGL $/Bbl	28.26	1.70%	40.16	-1.80%
Shrink	10.40		10.87	
Margin	17.86	1.32%	29.29	-4.14%
Gas ($/mmBtu)	2.85	2.37%	2.98	5.09%
Gross Bbl Margin (in cents/gal)	41.06	0.94%	68.64	-4.36%
NGL Value in $/mmBtu (Basket Value)				
Ethane	0.59	-17.31%	2.58	-7.60%
Propane	2.70	-0.06%	3.66	-0.80%
Normal Butane	1.01	2.64%	1.31	0.14%
Isobutane	0.78	0.56%	0.80	-13.12%
Pentane+	1.70	8.49%	2.02	4.61%
Total Barrel Value in $/mmbtu	6.79	0.57%	10.36	-2.55%
Margin	3.94	-0.70%	7.39	-5.33%

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.

The impact of the president's words on crude oil's price might be called questionable, though. Soon after his speech, West Texas Intermediate (WTI) closed for the day up 20 cents to $72.28 a barrel. The next day, WTI did, in fact, slip by 1% but that decrease coincided with release of the U.S. Energy Information Administration's (EIA) report showing **crude inventories increasing** by 1.9 million barrels for the week ending Sept. 21.

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"It is our opinion that fundamentals will override the comments by President Trump," wrote **En*Vantage Inc.** analysts, referring to the president's **first demand** that OPEC lower prices on Sept. 20. "The consortium of OPEC and Russia has limited options to increase production to offset global demand growth, the production declines in Iran and Venezuela, and the possible disruptions that could occur in Libya."

Despite the weekly uptick, the EIA's data show U.S. oil inventories at about 75 million barrels below the level in 2017 at this time. The Brent-to-WTI spread remains wide ($10 premium for Brent), which should propel exports and tighten balances even more, En*Vantage said.

Exports of crude oil increased by 273,000 barrels per day (bbl/d) to 2.64 million bbl/d, the EIA reported. Since the week ended Sept. 7, U.S. crude exports are up 44.4%.

The Mont Belvieu, Texas, hypothetical NGL barrel slipped 1.8% in the past week but remained above $40 as price corrections claimed ethane and isobutane. One week after averaging almost 51 cents per gallon (gal), ethane dropped below 47 cents/gal.

Changing SOX: Enron-Inspired Law In Flux

It doesn't seem like that long ago. The massive financial collapse of Enron Corp. took place back in 2001, finally culminating with the company's declaration of bankruptcy on Dec. 2 of that year. Enron shareholders lost a total of $74 billion. Enron employees lost billions' worth of 401(k) plan benefits.

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At the time, it was the largest corporate bankruptcy ever.

Enron's virtual disintegration exposed unprecedented accounting and corporate fraud. When the U.S. Securities and Exchange Commission (SEC) launched a probe into Enron's finances in October 2001, many pipeline executives were afraid that the industry would face a complete loss of credibility in the financial community.

No pipe problem

But Enron's pipeline business wasn't the problem. During the dot-com era in the 1990s, Enron reinvented itself. It was no longer just a pipeline company; it launched initiatives in energy supply and the Internet. It built power plants and started an online trading business. Enron also entered the broadband communications market and even launched a water company.

—**MIKE SQUYRES** | CONTRIBUTOR

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