Sevens Report Alpha Webinar:

What Is Happening in the Energy Markets?

Thursday, October 14th, 2021

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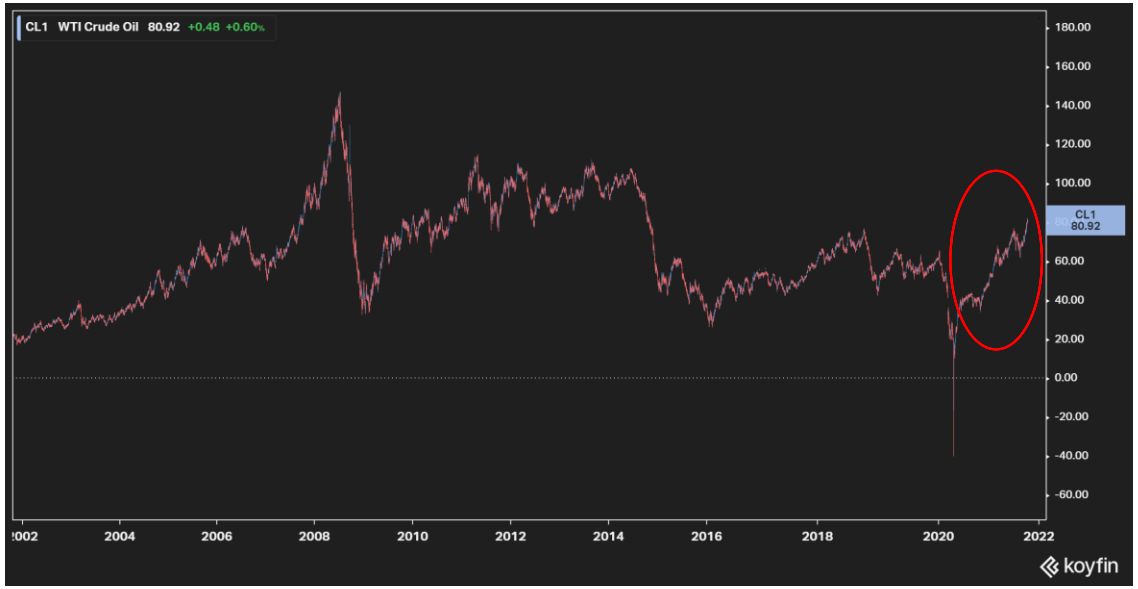
What is Happening in the Energy Markets?

- In response to surging demand as the world reopens, energy commodity prices have surged.
- This has been amplified by OPEC limiting supply increases and by production declines in the U.S.
- One time weather events, including the storm in Texas during the winter and floods in China recently have further exacerbated the problem.



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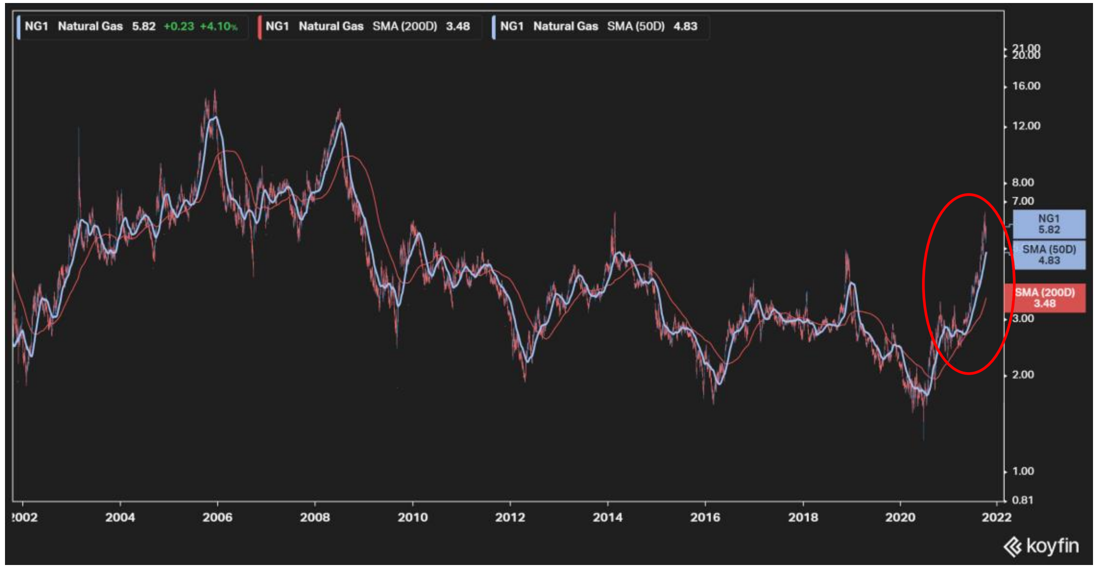
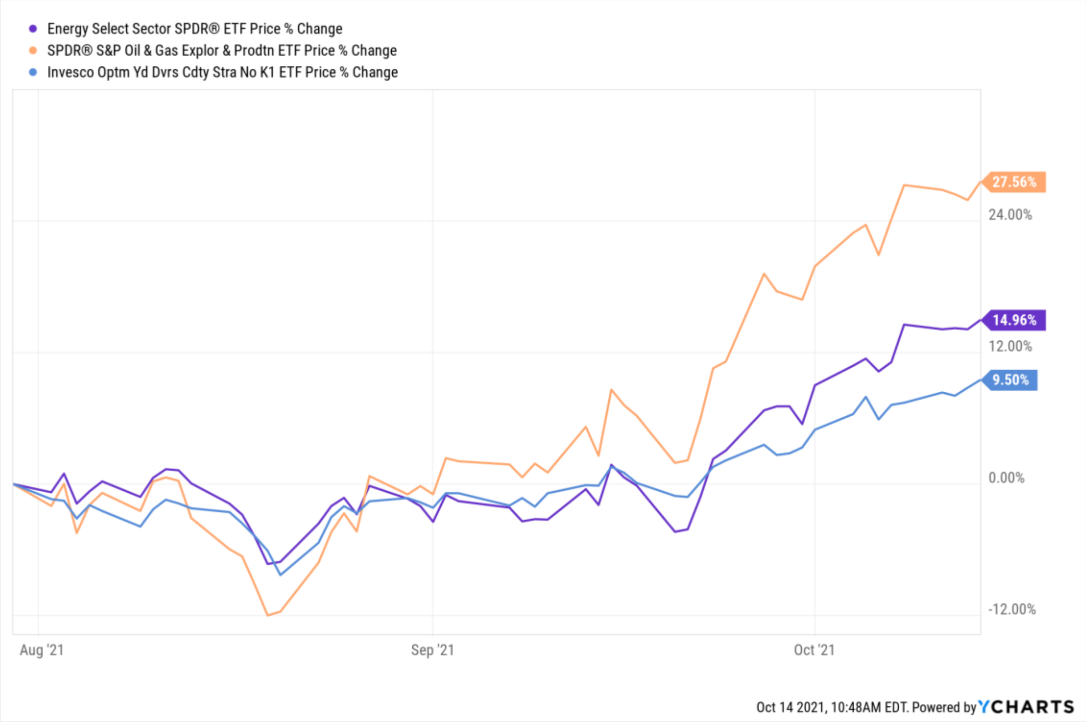


What is Happening in the Energy Markets?

- These issues have resulted in:
  - Gasoline shortages and rationing in the UK in late September/early October.
  - Rolling blackouts in China
  - Fears of further supply disruptions in the winter, especially in Europe if the weather is unseasonably cold.

What is Happening in the Energy Markets?

- As a result, energy equities, and natural resource stocks and broad commodities have surged.



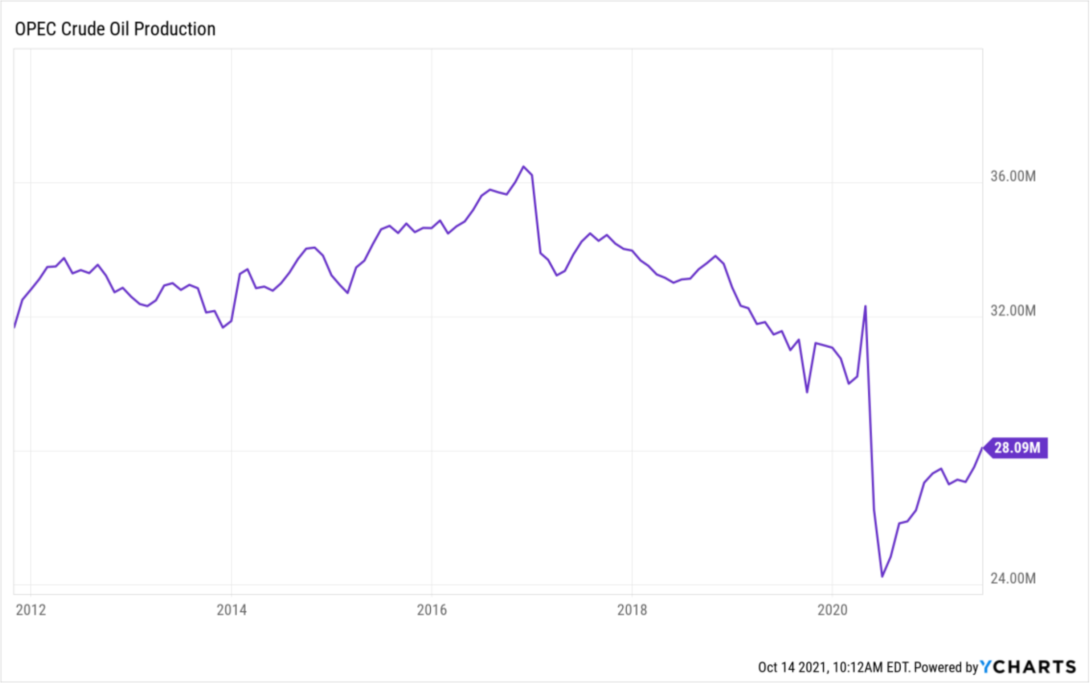
Why Is This Happening?

- Supply and Demand
- Demand for energy has recovered very quickly from pre-pandemic levels.
- But, supply has not risen to match surging demand.

- According to the EIA, Total World Petroleum and Other Liquids demand will be just 4% below 2019 levels this year, and essentially at 2019 levels in 2022.
- There has been no sustainable dip in energy consumption and it is coming back very quickly, but supply has contracted sharply.

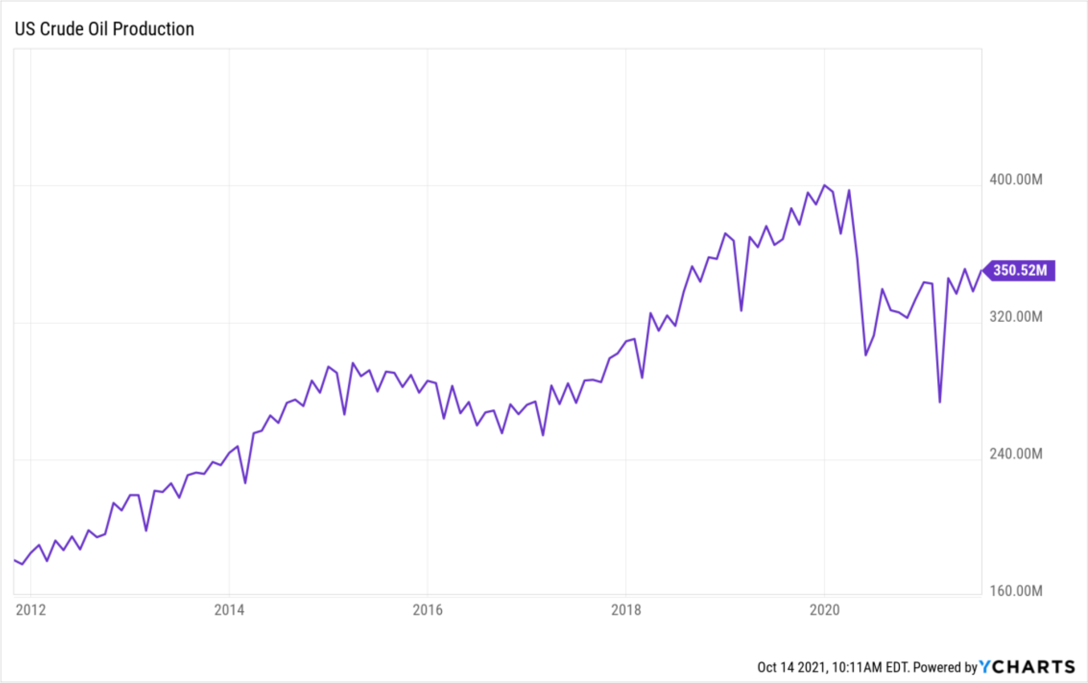
Why Is This Happening?

- OPEC oil production is several million barrels/day below pre-pandemic levels.



Why Is This Happening?

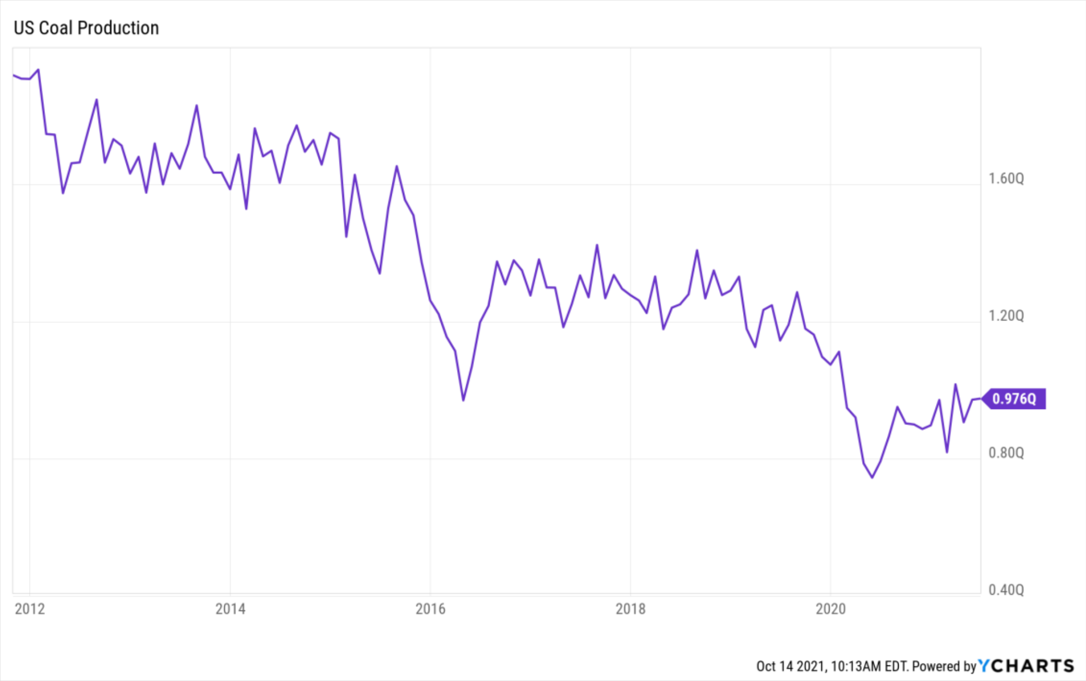
- US oil production is more than 10% below pre-pandemic levels.



Why Is This Happening?

- US coal production is down substantially over the past several years.

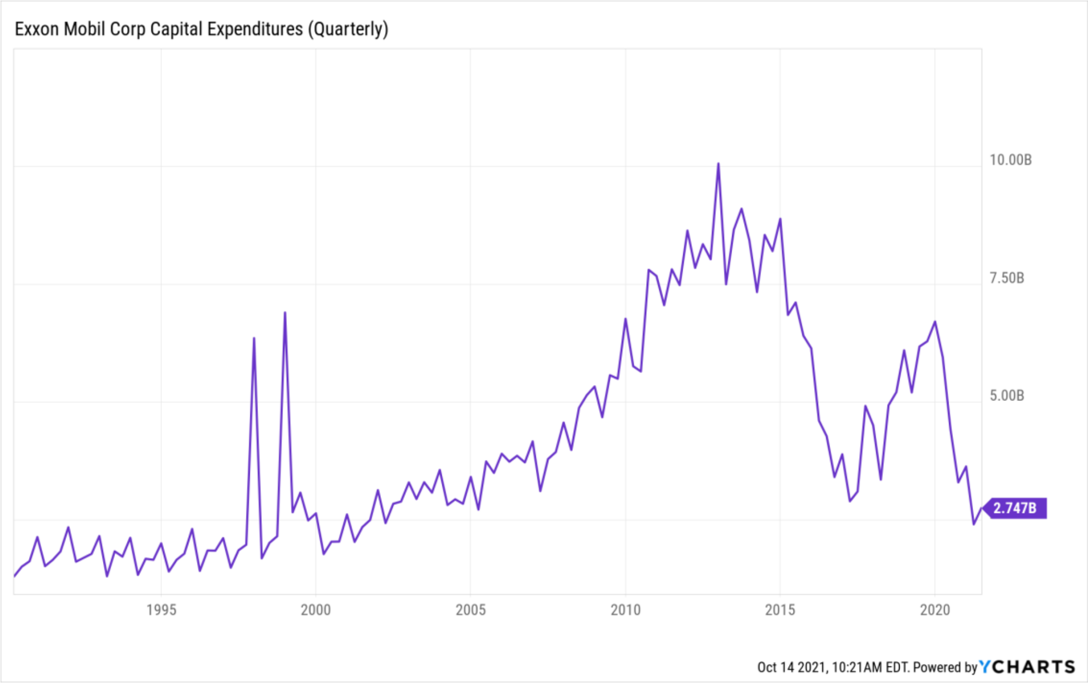
- **Bottom Line: Supply Is Down, And Demand Is Up. That Equals Higher Prices.**

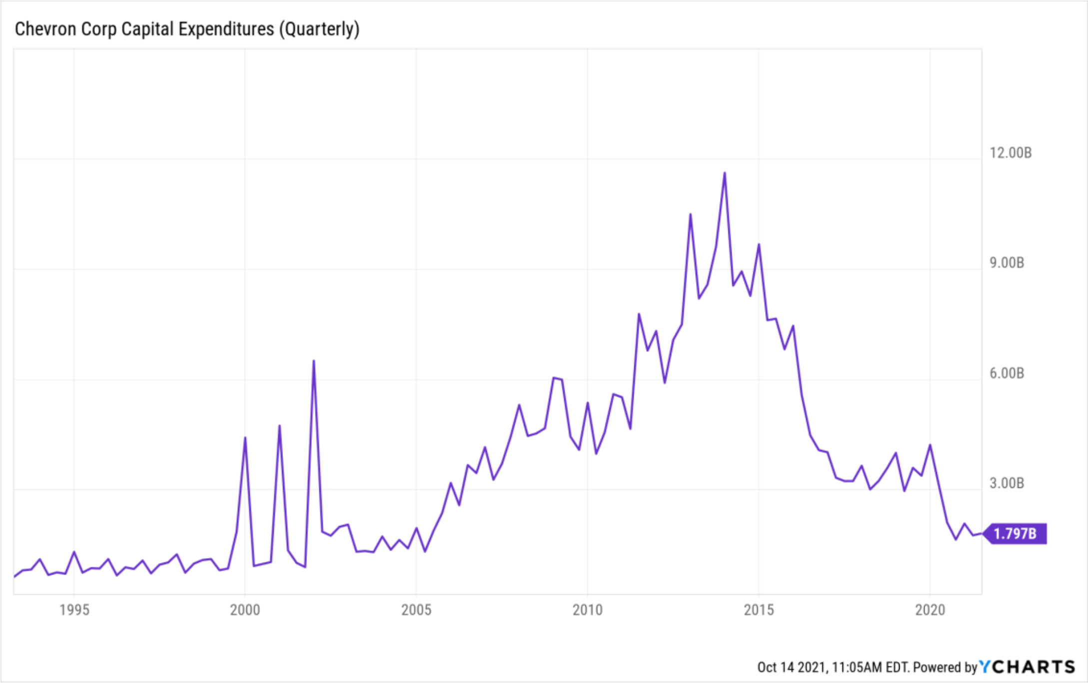


So, Will It Get Fixed Quickly? No.

- As the saying goes, the best cure for high prices is high prices, as it invites more exploration and development from large oil companies.
- But, in an economy and market very focused on carbon reduction, major energy companies are not investing in energy production the way we would expect.
  - Investors at energy firms have demanded capital return rather than increased Cap-Ex.
  - Additionally, many investors are demanding energy companies increase carbon offset and reduce their carbon footprint.
  - Banks are now reluctant to lend to energy companies and instead are preferring alternative energy, further restraining new supply.

So, Will It Get Fixed Quickly? No.

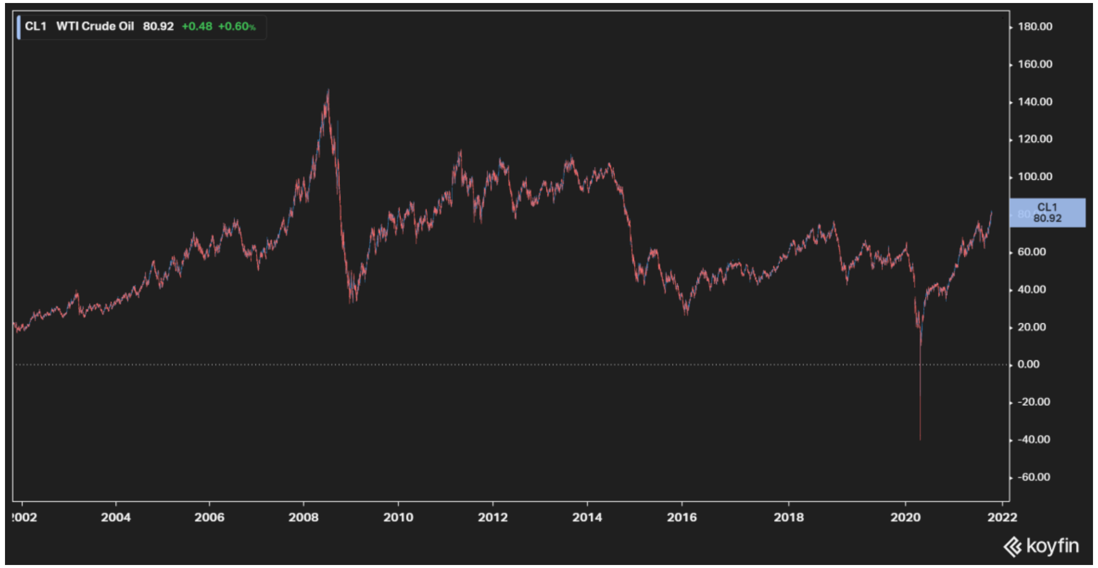




So, Will It Get Fixed Quickly? No.

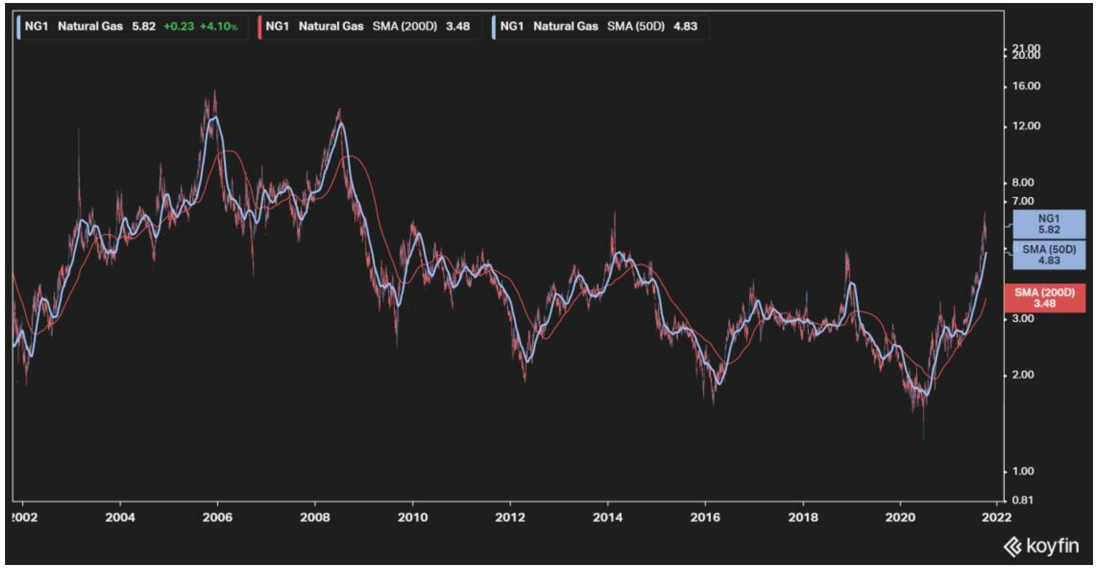
- The U.S. rig count, which is essentially the leading indicator of energy production, is down sharply from pre-pandemic levels, and until we see the rig count increase, we should expect higher energy prices.

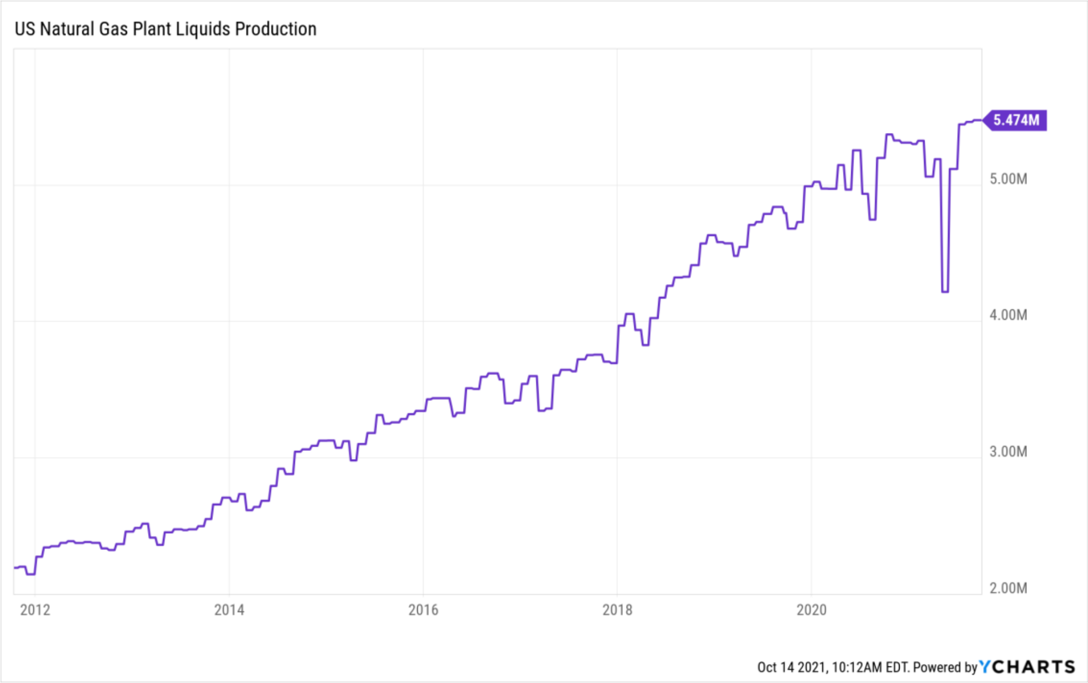
So, Will It Get Fixed Quickly? What About OPEC?



- In 2016, when oil fell to $30/bbl, OPEC essentially collapsed prices to shut down exploding U.S. shale production. And, it worked, as oil hovered between $40-ish and $60-ish for the next several years.
- Now that prices are high again, OPEC is only gradually increasing supply, because they are making the bet that climate policy will trump economics and that shale production won't rise materially despite high prices.
- **Whether that bet is right or not will determine whether we are facing structurally higher energy prices going forward.**

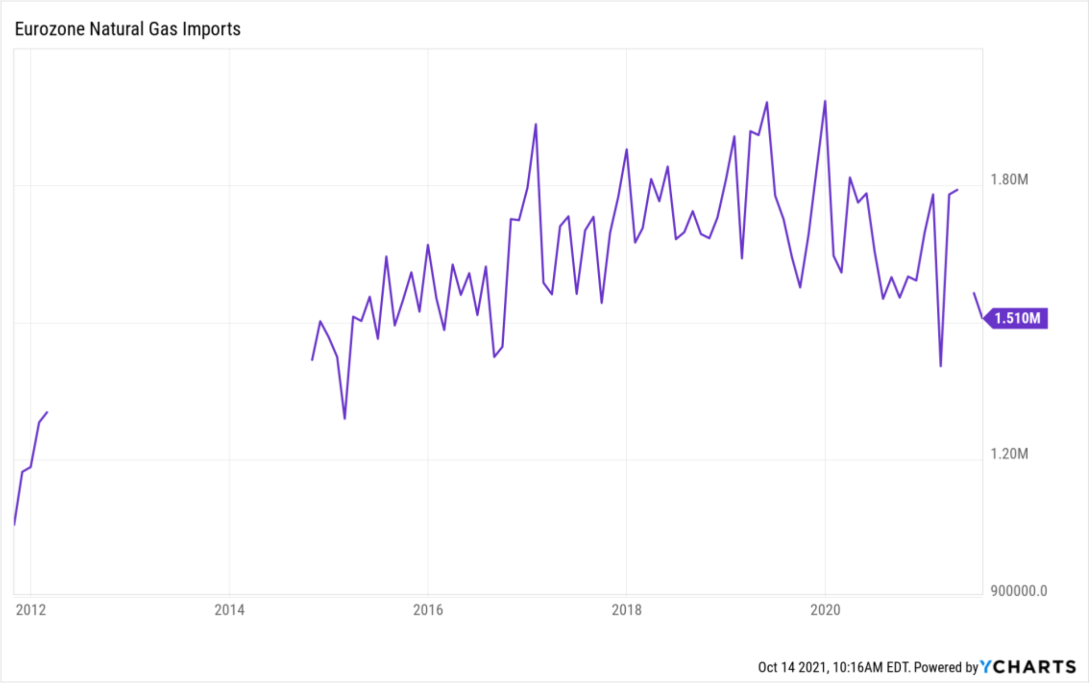
How Can We Make Money Off This Reality? Natural Gas





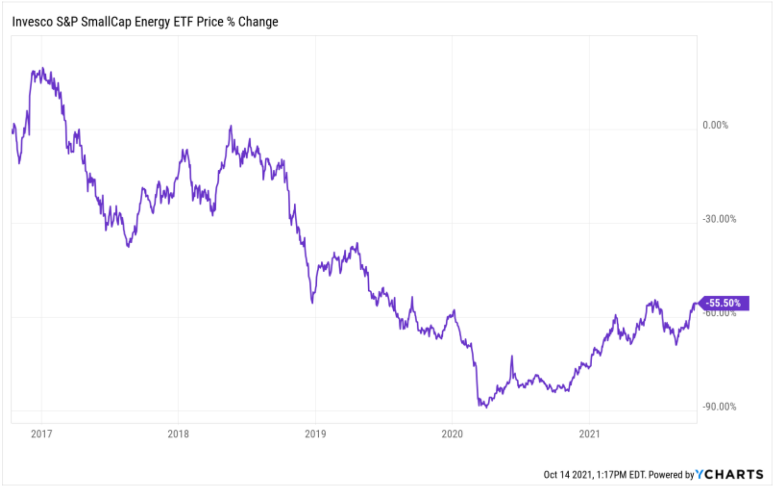
How Can We Make Money Off This Reality? Natural Gas

- Natural Gas is viewed as the "cleanest" fossil fuel.
- And, since 80% of U.S. power production still comes from fossil fuels (and it's a higher percentage around the globe) Natural Gas is potentially in the sweet spot to provide "clean" energy now.



How Can We Make Money Off This Reality?

- With the major energy companies restraining Cap Ex, there is an opportunity for more nimble, smaller producers to profit from higher prices.
- PSCE: Invesco S&P Small Cap Energy ETF



How Can We Make Money Off This Reality? Natural Gas Focus

- XOP (SPDR Oil & Gas E&P ETF)
- EPD (Enterprise Products Partners). 7% yield.
- TGP (Teekay LNG Partners). 6.9% yield.