The Energy Investor

November 2016
Election Opportunities and Lithium Profits

I’ve tried my best to avoid politics here on the pages of Energy Investor.

Truth is, there will always be opportunities to capitalize on the energy sector — even more so now that we have the wind at our backs and are staring at steady recovery ahead for oil prices… or are we?

Crude prices have been steadily falling since breaking above $50 per barrel.

And the market is growing more skeptical that an output deal will be reached by OPEC members later this month. It’s almost like riding the same roller coaster every day for 56 years — it’s all too easy to predict the way its members act.

I’ve mentioned a few times before that we’ll inevitably see the divisions tear the oil cartel apart. That, or they might as well get used to giving new memberships to net oil importers.

We can’t ignore the fact that these countries are in dire straits because of Saudi Arabia’s oil price war.

Everybody is hurting from cheap oil prices.

All we need to know is what each individual’s threshold is… the point when a deal has to be struck no matter what they have to concede.

Thing is, I strongly believe that some countries not only have passed that threshold, but that collapse is all but certain.

And Venezuela is one of those countries...

The entire nation is teetering on the brink, and perhaps the most damning aspect to their situation is that $60/bbl oil will do nothing to help. The rumor running around now is that $80/bbl won’t save them either.

Because Venezuela’s crude is among the poorest quality on Earth, it’s a very cost-intensive project to extract it.
The numbers are absolutely grueling to think about…

Approximately 95% of the country’s exports are in some way related to its oil industry. Rolling blackouts have become commonplace, as are severe food shortages.

Now toss in the fact that the Saudis have been gaining more of a foothold in the U.S. Gulf of Mexico, where refineries geared toward heavy crude are highly sought after. Then again, it also doesn’t help when U.S. output itself has nearly doubled since 2008, which has led to lower imports.

After the latest OPEC gossip made its way around the campfire, the market then settled into an incredibly bearish EIA petroleum report, which showed a 14.4 million-barrel build in U.S. inventories.

This isn’t to say we’ve lost our appetite for oil plays.

Although prices have been declining recently, one good takeaway is that the United States is more addicted than ever to crude oil.

It turns out that we consumed a record amount of gasoline during this past summer. In fact, demand for finished motor gasoline peaked at 9.7 million barrels per day in June.

Now, we have an event looming next week that could either send oil shooting higher or cause the delicate recovery taking place right now to crumble.

And no matter how hard we try, we just can’t avoid this election.

But does it really matter who wins? It’s not like there’s much of a surprise where a candidate stands.

We know about Hillary’s plan to power half of the U.S. with renewable sources by 2030 and that she supports clean energy over anything that can be put in the same sentence with hydraulic fracturing. We know she’s against drilling in the Arctic.

Believe me, nobody wants to drill in the Arctic, which is home to some of the harshest conditions on the planet.
I’m also pretty sure you don’t need me to tell you where Trump stands, which includes any and everything under the sun (except for the sun, probably). He’s even said he'll get the Keystone XL Pipeline project going again.

Neither candidate will have much of an impact, because both recognize how vital fossil fuels are to our energy mix right now.

Forget the pandering, the promises, and the politics. If nothing else holds true, it’s that the world's thirst for more energy will continue to grow over the long term.

Let me put it this way…

Even if Bernie Sanders were elected next Tuesday, there would never be a nationwide ban on hydraulic fracturing.

Yes, it’s simply that critical to meeting our energy needs. Oil and natural gas accounted for two-thirds of our energy consumption last year!

Today, roughly six out of every 10 barrels of crude extracted in the U.S. are from just six oil-producing regions — all of which are tight or shale plays, which require some form of fracture stimulation.

I don’t know if we even want to think of the consequences of shutting down the shale industry by banning a practice that has been used on over a million wells since the 1940s.

If you ever asked me what insane event would have to take place for us to see crude oil surge over $100 per barrel overnight, I’d concede that banning hydraulic fracturing would be one.

Granted, we’ll have a better idea of which path to take after next Tuesday.

A Quick Lithium Interlude...

Demand, demand, demand.

Keep saying that to yourself, like a mantra to hum as you watch our lithium plays
move higher. Perhaps one of the best stories in today’s energy sector has been growing lithium demand.

In order to keep up with demand forecasts for 2020, the world will have to boost its supply of lithium carbonate by at least 30%.

Considering how there has only been one large-scale lithium brine plant built in the last 20 years (spoiler alert: the plant is operated by Orocobre), that means the rock-mining operations will be forced to significantly ramp up production.

Of course, we also can’t ignore Nevada as a variable, though it’s best to wait for more progress in those lithium brine projects before we start tacking it on to global supply.

There’s a reason the market calls it a lithium revolution.

And it’s one that has led to several monster gains for us over the last year.

But before I get into that, let me quickly say something regarding a question that a lot of you have been asking me lately...

**Reader Questions**

*Hey Keith, are things really THAT bad out there for coal?*

—Erin E.

This is the one question that I absolutely knew I was going to address this month.

After all, coal prices came roaring back over the last six months, with analysts from both Goldman Sachs and Citi proclaiming it this year’s hot commodity.

So over the short term, perhaps, it certainly hasn’t been that bad for coal.

Unfortunately, the entire industry has been in an irreversible death spiral ever since the shale gas boom erupted nearly a decade ago.
Nothing is going to change that.

In fact, the Energy Information Administration confirmed my dismal outlook recently. As you can see, coal’s share in our energy consumption has been declining for more than a century!

Moreover, we know for a fact that nearly all new capacity planned in the U.S. will be powered by wind, solar, or natural gas. The more coal plants that are decommissioned, the further the industry will fade away.

Don’t get me wrong; I’m not suggesting this will happen overnight. You and I both know how long it will take to transition ourselves away from fossil fuels.

Coal only accounted for 16% of our total energy consumption in 2015. The problem, however, is that approximately 91% of our coal demand was used in the electrical generation sector, where natural gas and renewable energy have been edging out coal for decades.

It has put the entire sector in a lose-lose situation.
Even an election won’t change that. Whoever ascends the throne next week will come to the quick conclusion that clean coal is a myth and that it’s much better to talk about our plentiful natural gas supplies.

Believe me, I know how tempting it is to call a bottom in coal, but I’m not willing to put our hard-earned gains this year on the line betting on a prolonged rally for coal.

Monthly Spotlight: Orocobre Ltd

Ticker Symbols:
TSX: ORL
OTC: OROCF
Market Capitalization: $565.4 Million
Shares Outstanding: 210.2 Million
52-Week Range: $0.94–$3.80

It shouldn’t be much of a shock that our monthly spotlight is from the lithium sector.

Despite the incredible volatility we’ve seen over the last two years, lithium is one of the few (if not the only) commodities in a strong uptrend.
There’s no question that lithium carbonate prices have been surging on strong demand. And even though prices softened during the second half of the year, remember that prices have exploded since 2015:

And that, dear reader, brings us to Orocobre Ltd.

Along with Toyota Tsusho Corp. and Jujuy Energia y Minería Sociedad del Estado (it’s a mouthful, I know), Orocobre is now operating the first large-scale lithium brine plant to be commissioned in about 20 years.

Located in the Jujuy province, the company’s flagship project is the Olaroz Lithium Facility. Now, the Salar de Olaroz is a long-life, high-quality resource that is capable of sustaining production for more than 40 years.

The company has proven it can grow production, too. Below, you can see for yourself how Olaroz production has increased more than 700% since the third quarter of 2015 (that’s assuming the company will hit its production estimates):
Speaking of growth, you may have noticed when shares spiked more than 26% in late October.

It turns out the company reported a strong quarter, which sparked a buying frenzy over the next few days.

During the last quarter, Orocobre generated $33.5 million (a 45% quarter-over-quarter increase), which represented the first full quarter of commercial production and sales from the Olaroz Lithium Facility. Moreover, the company sold approximately 3,593 tonnes and achieved record production of 1,125 tonnes during September.

Of course, it helps when lithium demand drives the price of your commodity higher. The company’s third-quarter sales price was $9,334 per tonne, approximately 24% higher than the previous quarter.

It’s almost too easy to see that there’s more growth in store for Olaroz, too. The company is operating at a low cost of approximately $3,555/t and expanding production in the project to between 35,000 and 42,500 tonnes per year by the third
quarter of 2018.

The bottom line here is simple. Keep in mind that Orocobre isn’t like the lithium plays driving Nevada’s lithium exploration.

We’re talking about a company that is actually producing lithium in Argentina’s Jujuy province, is cash flow positive, and is poised to be a strong lithium carbonate producer in the years and decades ahead.

After watching shares of Orocobre surge as much as 330% since we established our initial position, we knew it wasn’t a good idea to chase prices higher. That’s why Orocobre has been rated a “Hold” for most of 2016.

As expected, shares soon corrected nearly 30% during the last four months… and it’s time we take advantage of the selling and grab this opportunity.

Orocobre is now rated a “Buy” under $3.85.

**Rankings and Portfolio**

**November’s Top 10 List:**

1. Matador Resources
2. Cheniere Energy Partners LP
3. Cypress Energy Partners
4. Orocobre Resources
5. Approach Resources
6. Gastar Energy
7. Oasis Energy
8. Range Resources

9. Scorpio Tankers

10. Abraxas Petroleum

**Abraxas Petroleum (NASDAQ: AXAS)**

After months of savings and cuts, we’re finally seeing Abraxas’ production on its core acreage.

In late October, Abraxas announced that its most recently completed wells in the Bakken shale play had reached an average production rate over 1,100 boepd in their most productive 30 days.

With this kind of production keeping up, the company could have an average production around 8,000 boepd in the fourth quarter of this year.

Despite the tough time the industry has been having, Abraxas has managed to keep itself well positioned. In the past year, it’s sold off non-core assets and focused its production on only the best areas, both saving money and increasing liquidity.

I should have more concrete information for you on the company’s activities after it releases its third-quarter 2016 results on November 14th.

*Abraxas is rated a buy under $3.*

**Apache Corp. (NYSE: APA)**

Apache is an oil, gas, and NGL exploration, development, and production company with major operations in the Permian Basin shale play.

Not much news has come out of this company since it announced a massive oil discovery last month, so let’s take this opportunity to look over some recent operational improvements.
In August, Apache reported that its Delaware Basin assets (pre-discovery) had been expanded. During the second quarter, the company placed two gross wells onto production. In the Midland Basin, the company brought a total of 16 wells online and added another two wells in the SCOOP play.

The company drilled with a 100% success rate in the North Sea, where production averaged approximately 71,000 boepd. Apache is focusing on the Beryl area of the North Sea and brought online three wells in the second quarter.

Finally, the company’s operations in Egypt seem to be going smoothly. Apache’s existing wells produced an average of 350,000 boepd, and 15 new wells were drilled in the second quarter with a 93% success rate.

Apache, like most of our positions, is looking to cash in on the latest upswing in oil. However, it’s still keeping its focus on the most valuable assets in the most productive areas it can. We’re not quite out of the woods yet.

We’ll take a look at this company’s earnings in our next update. Analysts are expecting to see a loss of $0.07 per share but a positive EPS in the fourth quarter.

*Apache Corp. is rated a buy under $60.*

**Aqua America (NYSE: WTR)**

Aqua America offers water utility and wastewater services to nearly 3 million people across eight U.S. states, with a goal of expanding that customer base by 2% by the end of 2016.

Another quarter gone, and I’m still glad to be holding this stock in our portfolio.

In its latest earnings announcement, Aqua America reported third-quarter revenues of $22.6 million, a full $5.5 million (2.5%) increase over the same period last year.

Furthermore, EPS came in at $0.41, beating both last year’s total and analyst estimates.

The company also noted a reduction in market-based activities and production costs that saved $2.7 million for the quarter.
Of course, that doesn’t mean Aqua America isn’t spending money. The company’s infrastructure improvement plan calls for investments totaling more than $1.1 billion through 2018. This includes improvements and expansions of its existing infrastructure, which will reduce the cost of operations down the road.

For the first nine months of the year, the company put $270 million towards this goal, and it plans to spend another $80 million before the year is out.

So far in 2016, the company has added 5,700 customers to its books through both business acquisitions and organic growth. Its goal for the year is to reach a year-over-year customer base increase between 1.5% and 2%, and it’s very nearly reached the lower end of that estimate already.

Water services continue to be essential to keeping our industries running, and as long as they’re making money like this, we’ll be glad to keep buying.

*Aqua America is a buy under $40.*

**Centrica (OTC: CPYYY)**

Centrica is a generator, trader, and optimizer of nuclear, wind, thermal, and natural gas energy with an international reach.

We haven’t yet heard any big updates on Centrica’s recent moves. In recent months, the company has gone through some adjustments to set itself up for success.

In August, the company announced that it would be zeroing in on its Connected Home Business by expanding its device and service offerings there, while also cutting back on its oil and gas investments.

Then in September, I explained that Centrica was acquiring FlowGem Limited, which is developing a system to detect leaks in pipes remotely.

I still don’t blame Centrica for putting all of its efforts into improving these utility services rather than jumping back into the oil and gas game. There’s still some recovery to be done yet.
We'll have to see how those improvements have done for this position at the end of the year, and I'm hoping we'll see some positive numbers on all fronts.

Centrica is considered a buy under $17.

**Egdon Resources (LSE: EDR.L)**

Egdon is an oil and gas exploration company building an asset base in the UK’s North Sea.

This company’s position in the North Sea just jumped, and in the best way possible: totally free.

In October, the company announced that it had been granted partial ownership of a number of assets in the Gainsborough Trough, Widmerpool Basin, and Humber Basin areas of the East Midlands. The new area adds 1,141 square kilometers (281,979 acres) to Egdon’s assets.

These licenses were previously held by Celtique Energie Petroleum Limited and were transferred to Egdon with no acquisition costs.

This company just increased its foothold in the UK’s premier oil and gas destination without spending a penny.

And while it’s true that what it does with the new assets is what really matters, this is a major step forward for our growing company.

Egdon Resources is rated a buy at current prices.

**Enbridge Inc. (NYSE: ENB)**

Enbridge is an oil and natural gas transportation and processing company.

It operates 32,500 miles of liquid and gas pipelines and a number of processing plants throughout the U.S. and Canada.
I’m sure you’ve heard both sides of the controversy going around about the Dakota Access Pipeline. Without taking a political stance here, I have to admit it’s not doing great things for Enbridge.

Already, the drop in production from the North Dakota Bakken area has caused the company to put off its planned Sandpiper pipeline indefinitely.

Now, the company has announced that its partnership, Enbridge Energy Partners, lost $406 million in the third quarter of this year due to problems with its stake in the new Bakken pipeline system planned to get oil from North Dakota to Texas.

This system included the much-debated DAPL, which was the main reason for the company’s loss.

Enbridge is also selling off its liquids pipelines in the South Prairie Region as of late September. The transaction will earn the company $1.075 billion and close later this year.

Lucky for investors, Enbridge still has a much larger pipeline network already in place.

These projects are far from bringing the company to its knees. In fact, despite the trouble, Enbridge reported quarterly earnings of $0.09 per share.

Not every project can be a billion-dollar winner, and let’s keep in mind that this one isn’t entirely dead yet… there’s still a lot that can be done to end these pipeline disputes in success for both the company and its investors.

_Enbridge Inc. is rated a buy under $48._

**Encana Corp. (NYSE: ECA)**

Encana is an oil, gas, and NGL developer, explorer, producer, and marketer. Its operations are located in the Permian, Eagle Ford, Duvernay, and Montney shale plays.

Encana updated investors on its five-year plan last month, and the news was nothing but good.
First, the company ran through its past two phases between 2013 and 2016. During this time, it managed a “major portfolio transformation,” adjusted its capital allocation processes, strengthened its balance sheet, and increased efficiencies across the board.

Now it’s entering the “growth phase” of its plan, which starts formally in 2017.

Between 2016 and 2021, the company expects to deliver more than 300% growth in cash flow, 60% growth in production, 35% growth in returns from its core four wells, and continued competitive operations with a balanced mix of oil and gas.

You know what they say about the best-laid plans…

But the point here is that Encana has set itself up so that these gains aren’t anywhere out of reach. By divesting non-core assets, reducing debt, and cutting costs over the past few years, the company is already well on its way to awesome growth!

Encana’s latest earnings came out just barely too late to make it into this update, but we’ll take a look at the numbers here next month.

Encana Corp. is currently rated a buy.
EnerSys (NYSE: ENS)

EnerSys is a widely integrated company that manufactures, markets, and distributes batteries of all types and sizes.

EnerSys reached an exciting milestone last month: it just delivered its 10,000th NexSys battery to Estenson Logistics, a long-time customer with business in 47 states.

The batteries are thin plate pure lead and will replace older flooded lead-acid batteries, the kind that need water replaced periodically. The reduced maintenance will do wonders for both Estenson and EnerSys.

“We are very pleased to recognize this achievement as it represents our growth in the material handling and transportation industries,” said the company’s general manager specialty markets, Chad Uplinger.

October was also a big time for EnerSys to show off its technologies. Its VaultFlex outdoor battery enclosures and NexSys batteries were featured at three different conferences.

Short of drumming up new customers, this is an easy way for companies to get a good view of the competition. Already, EnerSys is a leading provider of battery technology, but it’s always beneficial to keep a finger on the pulse of the market.

We’ll see how it’s all paying off when EnerSys announces earnings on the 10th. Analysts are estimating earnings per share of $1.08.

EnerSys is a buy for us under $80.

Gastar Exploration (NYSE: GST)

Gastar is an independent energy company that explores, develops, and produces oil, gas, and NGL in U.S. unconventional shale plays.

In October, Gastar announced that it had entered into an agreement to jointly develop assets in the Kingfisher County STACK play of Oklahoma.
The partner, a private global investment fund, will pay 90% of the drilling costs in as many as 60 wells on the company’s 18,000 acres of undeveloped land. In return, it will earn 80% of the company’s working interest in each new well at first.

That may reduce the amount of income Gastar will get in the beginning, but at the cost of vastly reducing the cost of those wells to begin with.

The drill program will be done in phases of 20 wells each. The first will be done in the Meramec and Osage formations, with the other two phases to be decided upon later.

This is a great opportunity for Gastar… and even though it won’t have full control of the wells, it will be getting them on its books at a discount. Moreover, they’ll still be located in a notably productive area of Oklahoma shale, and well worth the cost, no matter who’s paying.

*Gastar is rated a buy under $3.*

**ONEOK Partners (NYSE: OKS)**

ONEOK Partners is a gas and NGL gatherer, processor, storer, and transporter. Its pipeline network runs 37,000 miles through 17 states and the Gulf of Mexico.

As of the third quarter of 2016, ONEOK Partners saw a 21% increase in net income: $274.3 million compared to $227 million for the same period last year. The company also saw a 16% increase in EBITDA during the quarter, from $403.7 million to $469.4 million.

Not surprisingly, we can attribute this good news to the increase in natural gas volumes, which benefited from the completion of the company’s Bear Creek processing plant and the five newly connected third-party plants this year.

These have all increased ONEOK’s exposure to both the STACK and SCOOP shale plays in Oklahoma, which are becoming increasingly lucrative for producers in the industry.

And that’s not all, folks.
“In October, we completed the second phase of the joint venture Roadrunner Gas Transmission Pipeline and the complementary ONEOK WesTex expansion project,” explains President and CEO Terry Spencer.

He notes that both projects were done ahead of schedule and under budget. Both will provide the company with new partnership opportunities and “long-term fee-based earnings.”

If you’ll remember from previous updates, our midstream plays have been focusing on these fees to counter reduced commodity prices in recent months.

Clearly, it’s paying off nicely.

.ONEOK Partners is rated a buy at current prices.

**Ring Energy (NYSE MKT: REI)**

Ring Energy is another company planted firmly in the Permian Basin.

It was a rough quarter for the company, which generated a loss of $0.49 per share for the quarter due to an impairment charge. Short of that, earnings would have been flat.

Ring also reported that oil sales had gone down, though natural gas sales rose 114% as compared to the same period in 2015.

Net production during the quarter was approximately 209,000 barrels of oil equivalent, a slight increase over the same period a year ago.

The silver lining here is that these earnings reflect the poor commodity price environment that we were in during the first half of the year.

Ring actually took advantage of it by cutting a deal that doubled its net acreage, as well as increased its horizontal footprint in West Texas.

. Ring Energy is rated a buy under $11.
**Tsakos Energy Navigation (NYSE: TNP)**

Tsakos is an operator of crude, petroleum product, and LNG tankers. Its fleet travels worldwide.

As of this company’s latest earnings report, more than half of its 65-vessel fleet was under contract, with an average length of 2.8 years.

The company’s young fleet has remained attractive for clients, too. Tsakos’ fleet is just 7.2 years old, as compared to the industry average of 9.9. Furthermore, 21 of those vessels also have ice-class capabilities, increasing access to routes and customers.

During the second quarter, Tsakos generated a net income of $16.4 million, or approximately $0.15 per share.

With its current contracts underway, the company’s total backlog amounts to $1.4 billion, plus profit shares that apply to several of the vessels.

Granted, it’s also good to know that the company’s dividend is going strong. The current quarterly payout of $0.08 per share that Tsakos offers us is actually a small increase over its 2015 quarterly payout of $0.06.

And with big names like ExxonMobil, BP, Chevron, Shell, and Petrobras on its books, Tsakos doesn’t need to worry about losing business.

*Tsakos Energy is a buy under $8.*

**On the Radar**

There is only one final note I want to bring up before heading out today.

Last week, I told you that I was finishing up my due diligence on our next trade, and that it was almost time to pull the trigger. And as much as I was hoping to release that new recommendation before today’s monthly issue was published, it just wasn’t the right time to do so.
We’re going to have to remain patient for the time being, but you’ll receive an immediate trade alert the moment we’re ready to act.

Good investing,

Keith Kohl
Energy Investor

P.S. Your next issue of Energy Investor is scheduled to be published on Friday, December 9, 2016.