

Webinar Replay: Middle East Developments & What It Means for Global Energy Markets #8

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Mark Marifian:

All right, good morning, good afternoon, depending on where you're at. And welcome. Thanks for joining our timely webinar, The Middle East Crisis and what it means for global energy markets. My name is Mark Marifian and I am the head of product at Tortoise. So we've been doing these webinars weekly, really designed to continue to unpack any and all complexities in the energy space. And so this is a topic we've been covering really since the beginning of the year. So we'll continue to keep everyone up to speed. Just a quick housekeeping note before we dive in. We will leave some time at the end for Q&A. So do feel free to submit any questions that come to mind during the webinar. For those new to the webinar, thanks for joining. Welcome to Tortoise. We are the energy specialist. We have more than two decades of experience.

Today we manage about \$11 billion in AUM across the energy value chain, really from wellhead to the end user. So what we'll try to do here is go through a few slides, framing what is happening in the macro and then ultimately bringing it home to what's happening more closely to us domestically within the energy sector. So if we go to the next page.

Okay. I think we all know why the Strait of Hormuz matters at this point and its impact in terms of carrying 20% of the crude and 25% of the LNG through that narrow corridor. What we have now seen is two months essentially of physical disruption since the war began. Since March 1st, we really have only had a limited number of tankers consistently make it through the Strait. You can see this chart here. You're looking at about two million barrels a day or 10% of pre-war levels. So if we just recent news flow, it continues to unfold week by week, day by day. I'd say more recently we enforced a blockade on April 13th. Iran, in some sign of negotiation, they opened the Strait for one day and then reclosed it. Then on our side, US extended the ceasefire temporarily, didn't put a timeline on it. And that was last week. And then we had in-person negotiations in Pakistan and negotiated. It's now happening virtually. So that's kind of the high level news flow that we know of. If we go to the next page, this is where we start getting into the dynamics of what's happening with the market. Okay. So if you've been joining us each week, you'll know that we've been utilizing a lot of the research, particularly from Goldman Sachs on the market. And so I'm going to steer you to the right-hand side of this chart. So we have 20 million barrels a day flowing through the Strait, and we can see how that water falls down. We did see a few slight changes this week from last, most notably that the redirections of pipeline flows, that dropped from five to three and a half. So slight decrease there. We also saw Gulf builds.

That also fell from a previous week to 0.7, and it was at one and a half. Now, so that would be negative. And then the other thing you're seeing is for the first time, we had an ad or a forecasted add to what demand destruction is going to be. And you can see that's that blue bar there. So the forecast is 2.4 million barrels a day of demand destruction. That's really the first time we've seen that quantified. And so we'll dig into that a little bit more in a few pages. But ultimately, when you go from the left hand side on the red bar of 20 million barrels a day, we are at a supply demand implied deficit of about 11, 11 and a half million barrels per day. Now, on the left-hand side, we're seeing more

analysis done on inventory draws. I think the most probable case, in my opinion, is that we're seeing under reported inventory draws and that's what's been making up the deficit, frankly, here of that 11.3.

And that's part of the reason why we haven't seen, if you will, an insane price spike. Right now, you can see that what's modeled here by Goldman and Groups is about 6.2 million barrels a day of invisible draws. So again, once these inventories that we're drawing from become fully tapped out, I think that's when you can possibly see prices really spike. And that's also when you should expect to see more serious demand destruction occur at scale. If we go to the next page, I think this was a helpful update too. We've shown this slide in weeks past, but now what we were showing was overall market observable barrels. And so we're here at zero today and that horizontal line. In the past, that was about upper 7, 7,800 or so observable inventories of crude oil. Now, what has happened year to date is we spiked and those crude inventories were elevated up to about 8.2 million barrels a day. And you can see that we had built a nice cushion going into 25 throughout 25 before the war started. And ultimately, now you're seeing this chart is starting to draw down a bit more. So what they're showing here is on a percentage basis, which I think it makes it a little bit more relatable to understand how serious the drawdown and the magnitudes of the inventory drawdowns are. So in 2026, inventories are about 2.5% above historical levels and what's being projected now is that inventories are going to be anywhere from four to 7.5% below historical values going all the way back to 2018. So we are entering, if you will, uncharted territory in terms of how much of a drawdown we've had for global inventories. And again, you're getting point after point, you're seeing how the system is really burning through its shock absorbers. We're going to be somewhere between four and 7.5% below historical levels.

If we go to the next chart, okay, I think this is becoming more topical as well now that the US has its own blockade. The question is how long can Iran survive a blockade of its own in terms of getting its barrels up to market before they have to shut in production? Their ability to store oil is finite. And again, once storage capacity is reached, shut-ins will overall trigger a much more severe economic stress for Iran. So Iran, just for reference, they produce about three and a half million barrels a day, about two million barrels a day of that three and a half is exported. So the thought is they have potentially two to three weeks of storage capacity remaining until production shut-ins become unavoidable. I think if you listen to experts, some will say potentially four to five, maybe even a few weeks longer than that.

But the point is, I think we're starting to see that the stress is real. I saw earlier this week that Iran had sanctioned a tanker that hadn't been used in 30 years to store crude and it was on floating in the Gulf. So that is a sign that they're looking for ways, any which way possible they can to alleviate their storage capacity issue. So just as the US aligned Gulf producers or the Saudi, UAE, Kuwait, Iraq, they're experiencing these production shut-ins and constraints. Iran also is experiencing these production shut-in constraints. And so I would say that, again, with any of these, damaged to the reservoirs is the more severe case, and it really extends the timeline to bring production back online. So what we did here is try to quantify who's impacted to what degree. This is from the IEA, and what you're seeing here is a Gulf country production by reservoir pressure.

And so basically the higher the pressure, the easier it is to bring production back online and the lower the pressure, the harder it is to bring production back online. And so you can see the US aligned states are generally more aligned, better aligned for certain Saudi Arabia and UAE than Iran here, which you can see that orange bar, they have quite a bit in low reservoir pressure. So that could

potentially be crude that would not be coming back to market if it is shut in. If we go to the next page, okay, and I think the Iran blockade and how long can they survive has been a question that's popped up more and more. And I think the other question is, just going back to demand destruction, is where is it occurring and not occurring? And so again, Goldman is estimating about 2.4 million barrels a day of demand destruction.

And so what the left-hand chart here is showing is basically each region, if you will, and the percent that they're impacted relative to the pre-Hormuz level. So you can see this is most severe in the Middle East and in Africa. And so that's where we've had the larger percent of demand downgrades there. Less impacted, I think positively has been Asia. And so we thought potentially those numbers will be a little bit higher, but what you're seeing is a map on the right-hand side of Asian economies and their oil consumption intensity. And I thought this was very interesting here in that India in particular, they're at about a third of the level of oil consumption intensity that they were in the year 2000. It's for all the reasons that we know, but you're seeing more demand elasticity or supply elasticity here, whether it be work from home, public transit, EVs, these are all substitutes that are allowing for less consumption of crude.

And so I think that's a relative positive and maybe one that we weren't necessarily forecasting as much. Now, jet fuel prices, we're not showing that today. We showed it in the past. Those are continuing to spike higher. I saw United Airlines raise prices for the summer months based on higher crude prices. So you're going to see it everywhere. Last week we saw that the EU was similarly telling Europeans to conserve energy to work from home and that they're starting to see some flight cancellations there as well. The rumor was that potentially we're six weeks away or you have six weeks or so of remaining jet fuel supplies per the head of the EIA last week. So we'll continue to watch this, but I think for now we have been able to avert some of this demand destruction, but we are quantifying it here. You're seeing it quantified for the first time.

Okay. If we go to the next slide, all right, this is a slide we've shown for some time. This is when we first published what could happen if there's conflict in the Middle East. At that time, crude prices were near \$60. So I think one and two are certainly out the door. And I'd say short term, you're seeing number four is a more likely scenario, and number three is really what's being priced as the more medium-term scenario at this point. If you talk to investors on the street, I'd say the whisper is that near term prices should be higher and then backwardation is far too deep. So we'll continue to watch this, but though I'd share that with everyone. In terms of where we're at from a price target, I think we're viewing kind of \$75 as the more long-term appropriate target at this point.

Before that, we were closer to \$60, \$65 pre-conflict. So you can see how that's moved up. Just updating those on ... There's been no meaningful escalation around energy infrastructure, that's good. Again, just to recap that, we've had 80 energy infrastructure facilities targeted throughout the war. Qatar's LNG export facility being impacted was the most severe. And so they account for 20% of LNG supply and about 17% of their supply is offline. What you're seeing now is really a sudden improvement and leverage for US LNG projects. And so last week we saw Glencore and EQT each commit to additional LNG for Commonwealth LNG, and we saw 20 year contract sign there. So that's moving the Commonwealth LNG project closer to a material FID final investment decision. Let's go to the curve itself. Okay. This is just showing the weekly changes. Green was last week. Blue bar is this week.

Again, more kind of under the radar, but front month prices were up about 10% week over week. I think more significantly now, 2026, you're now pricing just about \$90 for the remainder of 26 for the curve. I mean, that's up significantly. That's up almost \$25 from where we were pre-conflict. 2027, 28, better, but you're still kind of in the low to mid 70s at about \$72 on average. It was 61 pre-conflict. And then even as you get into the outer years, you're up about \$7. So you've seen the curve shift materially based on what's happened here.

If we go to the next page, we can now turn our attention to the US and a few slides here. So we've shown this chart in the past. Rick counts, not much movement. We actually had a decline in rig count last week, so you're not seeing new activity being meaningfully accelerated. You still have great capital discipline for the companies that they're focusing on drilled with uncompleted wells, and it's just a more measured approach to growth. We've seen US oil production flat the last two and a half years, and so the days of a million barrels a day growth are behind us. Now, that being said, we are going to benefit from improved technology, and so basins that we're drilling longer laterals than ever before. We have new technology, better digital tools, and AI. So this is going to help improve production. And then we did hear from the North Dakota Department of Mineral Resources this week, they said they're seeing a notable shift in work over rigs.

So those are rigs that are already working today. You're essentially enhancing output from existing wells, and we've seen the deployment there, or they've seen the deployment there up 13%. So I think that's where you're seeing the first arrays into trying to expand production. It's focusing on those existing wells that lines up with what continental resources had said a few weeks back in terms of increasing production. So again, US productions at 13.5 million barrels a day, even single digit growth would be very, very meaningful for global supply. Okay. And then we got a couple more slides left. Okay, this is US exports. So we've shown this chart for a number of weeks here on the left-hand side, you can see the total US energy exports approaching 18 million barrels a day, and we're exporting all types of energy, whether it be crude oil, LNG, natural gas, liquids, or refined products.

So we can't underscore how important America is to global supply. This week, I wanted to highlight a slide from one of the largest midstream energy infrastructure companies, EPD, and they highlighted the focus on LPGs. And LPGs, what they're focusing on in the right-hand side is really the waterborne supply, what gets exported from the Houston ship channel abroad. And so the US is 47% of that market. And so I think there's questions, why have we seen propane prices, why crude prices have kind of gone up and then dipped? And same with LNG prices. Why have propane prices continued to pull up into the right? The propane prices are at the highest they've been. I think you're seeing a big demand pull from the US. And so we are about 47% of waterborne supply, and a big source of that is going to China.

Okay. And then last slide, this is just energy more broadly, still under owned, still reasonably valued. When we take a step back, I think it's pretty wild that prices and performance, whether you look at the broad energy sector, E&Ps, refiners and midstream, you're up in the low to mid-single digits since the start of the war. So is there an opportunity for potentially a nice uplift here? Yes, I think this may start to come as investors realize just how hard it is for the logistics that we've discussed throughout the call to start to untangle themselves and moving these energy commodities, whether it be crude or another commodity from one place to another is really much harder than the market is currently pricing.

We showed this last week, I'll just reiterate it, but this is just positioning of energy overall. And so right now you're seeing on the left hand side, energy trade is still attractively valued from PE multiples



perspective. You're at about 15 times forward earnings, S&P's at 21 times. And then you're also seeing on the right-hand side that mutual fund positioning, yes, it's slightly overweight versus a 10-year average, but I would just caveat that energy is still a very small percent of the S&P 500 at 4% of the total index. So is there room for energy to grow overall? In the past, as recently as 2008, it was 15% of the index. And in terms of earning revisions, it's been significant year to date. About half of the earning revisions higher have come from energy. So something that you don't want to discount. And then I think just as a whole, how does it fit in the portfolio?

It's very strategically important. You have reasonable valuations and you have ownership that really hasn't recovered despite accrue prices and commodity prices moving higher. So from a portfolio perspective, you're getting inflation sensitivity, you're getting income generation, particularly with those midstream assets, and then you get a geopolitical hedge when you have periods of supply disruption or demand disruption as well. So I will see if there's no current questions today. We appreciate everyone jumping on. If you do have follow-up questions, please reach out and we're happy to discuss some more offline. Also, please reach out to your Tortoise sales representative if you have any questions. So again, thanks everyone for joining. We'll talk to you all soon and have a good day.

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