Participants

Pat Sanchez, COO of Sanchez Midstream Partners (SNMP)

Nate Abercrombie, The Stock Podcast

Interview Transcript

Nate: Thank you so much, Pat, for joining us. And a sincere thanks from me, for sticking your neck out, and being the first interview on the podcast. I'm sure our listeners would love to hear what Sanchez Midstream does, and what your business is all about.

Pat: So, all right. Well, thank you. I will first talk to you about SNMP, and kind of walk you through who we are, in the MLP space. If you're familiar with the MLP space, it's infrastructure assets, we process natural gas into dry gas, and then move it towards different markets. We also move wet gas into natural gas liquids.

I probably should back up, and talk about the reason I mentioned wet gas, and I was like, "Well, who understands what gas actually is?" You know, I almost want to start back from the beginning.

Nate: No, no. I think that's a great idea.

Pat: Yeah, you know, I mean. Like, I had mentioned wet gas, like the way we mentioned, it you knew, understand what wet gas is. Wet gas is the first molecule that comes out of the ground. So, our MLP functions as kind of the transport company, for upstream companies, in a very diverse basin of operators. And what we do, is move the molecules to the market. And our basin is the Eagle Ford.

So what do we do in the Eagle Ford? We move water, natural gas, oil, and natural gas liquids. Where do we move them to? We move them to markets, where we receive the highest, what we call "net back," for the product. And what do we move them through? We move them through pipes, and they're stored in tanks, and those are called "terminals." We charge fees, those fees are long term fees. We call them "long term commitments," or "minimum volume commitments."

The reason that we charge minimum volume commitments, is to secure a base rate of return, so that we, over time, have transparency and line of sight, into paying a dividend to our investors. So as time goes by, the investors, and the unit holders, have line of sight into increase in distributions, and into distribution growth.

Now, what has happened recently, in this market, is an anomaly. If you've seen that many MLPs have started to convert into corporations, and you've seen the collapse of joint general partners and limited partnerships, into one entity. That is one path that companies have taken. The other path that companies have taken, is the collapse and the conversion into a corporation.

So, to talk about Sanchez Midstream Partners, what is it that we do? We have about, over 200 million cubic feet, a day, of gas processing capacity, with our Raptor plant in South Texas. That is a plant that we jointly own with Targa. Targa's a midstream operator, they operate. In addition to that, we have in Western

Catarina, over 200 million cubic feet, a day, of gas gathering facilities. We have this, what we call Seco dry gas processing, a dry gas pipeline down to Encinal, which is a small town in South Texas, and from there it can go to different markets. One of those markets being Mexico.

Our gas processing facility, cryogenic gas processing plant, that we own 50% of, with Targa, is called Raptor. And that is in La Salle County, in South Texas.

Nate: Could you tell me a little bit, what is processing?

Pat: So, what is processing? So, gas processing is the wet gas, when gas comes out of the ground, we call it wet gas. And that means that is has natural gas liquids in it, with methane, which is the dry gas portion, is combined. And it has oil and condensate. That is knocked out and separated at the field level. Okay?

Then oil and condensate are separated, at the field level. Those are trucked, most likely, or piped to market, in what's called ... a center point in South Texas, called Gardendale. At that point, the wet gas stream, the methane, and the natural gas liquids ... And the natural gas liquids are made up of approximately four to five components, ethane, propane, isobutane, and natural gasoline. The wet gas and the dry gas, are then sent to a cryogenic gas processing plant, which we own 50% of, with Targa. Targa joint venture collects a fee. Okay?

All of this is governed under long term contracts, under acreage dedication. It's a steady business, we move ... and from there the cryogenic gas processing plant, it is separated. Dry gas then goes down our ... And this is all in the investor presentation. Dry gas then, is moved through our dry gas pipeline, Seco, to Encinal, and then some of it goes to different markets.

And the natural gas liquids, goes to Mount Bellevue, near Houston. And there, it gets fractionated. And that is a separate process. And once you fractionate natural gas liquids, you know, you fractionate into, you divide them into ethane, propane, isobutane.

So to, kind of touch on, what is it that SNMP does, we see tremendous growth, and tremendous opportunity, at SNMP because of the acreage dedication, and the volume growth associated with the acreage dedication, SNMP has.

Nate: Is that acreage dedication from Sanchez Energy?

Pat: Energy, it is. It's from Sanchez Energy. Sanchez Energy went public, approximately seven, eight years ago, little over eight years ago, with over 600, approximately 600 barrels a day. So you could see the growth trajectory, and so, SNMP hopes to benefit from that growth trajectory, and capture some of that volume certainty.

Nate: Could you walk me through the difference between processing and fractionation? Is it just, you're pulling out different molecules at different periods of the process, or stages of the process? Or?

Pat: I can high level, but I'm not an engineer. I can't get into the molecular-

Nate: Yeah, sure. I don't want that.

Pat: Yeah, yeah.

Nate: Yeah, this isn't a science podcast.

Pat: Yeah, [inaudible 00:07:14]. But you're basically breaking down, it's a molecular chain, that you're breaking down. You're heating and cooling, to break down different molecules.

Nate: Okay.

Pat: And so it's, when you think of vinyls, resins, plastics, most of those come from ethane. Ethane then is further cracked into a steam cracker, an ethane cracker, to produce ethylene. Ethylene then can be used to produce polypropylene, and different types of products. And those go into, you know, your low linear density, you know, different types of plastics and resins, in which you see, you know, almost everything around.

Nate: Yeah, yeah. This is something that I think is lost on a lot of people, who don't have an interest in investing in energy.

Pat: But they buy everything around them.

Nate: Exactly.

Pat: Yes.

Nate: Like all the electric vehicles are using the plastics, and the resins that are coming from the oil and gas industry.

Pat: From [crosstalk 00:08:11] gas, yes.

Nate: I actually remember having this dinner, it was a big buy side dinner, with a large integrated midstream company, where the conversation was centering around their PDH facility, and just the delays associated with it. And I remember looking around the room and seeing a lot of blank faces, when the subject of this ... their PDH facility and the delays associated with, came up. And what exactly is a PDH facility, and what do they produce? Because nobody wants to look like they don't know what management's talking about, in those types of situations. The subject was just glossed over, nobody really focused on it.

And that's one of the things that is lost on a lot of investors, who, maybe they don't want to own an oil and gas stock, because they think that gasoline demand is going away, or at least it's declining, or at least the outlook isn't very bright. Because they think that electric vehicles are going to supplant all of the gasoline and diesel fueled vehicles, that are currently in the global fleet. They don't recognize the fact that plastics and other things that we use in our daily lives, are produced, at least the raw materials that go into those products, are coming from hydrocarbons or petroleum products.

And just to clarify, PDH stands for propane dehydrogenation. And so you're taking propane, which is a hydrocarbon, you dehydrogenate the molecule, to create a synthetic polymer, which is used to create things like polypropylene, and polyester. And these are the things that are used to manufacture carpet, and fleece vests, and things that people use in their everyday lives. And I think that's something that's probably lost on a lot of investors.

Pat: And they're specialty plastics. And so, all of your electronic vehicles, all of your specialty plastics, your carbon fiber, your ... all of those are coming from hydrocarbons. And so, if you take a hard look, when people think of energy, they think of quote, unquote, "big oil." But they don't think about all of the benefits that this industry has on society.

A shale boom, in the United States, has been a tremendous, tremendous period of time, in our history. It has decreased the cost of living. It has made us globally competitive. Companies are moving into the United States, because you can set up shop here, whether you're in plastics, whether you're in specialty plastics, paint, chemicals, any type of ... Whether Formosa, LyondellBasell, DuPont, any type ... Ineos inside of Europe, Sasol, South African, the Brazilians, they're all setting ... There's a reason that they are spending billions of dollars, and their manufacturing facilities, their specialty chemical facilities, in the Texas Gulf Coast. It's because the feed stock is cheapest here.

Nate: Yeah.

Pat: And they're creating thousands of jobs here.

Nate: Yeah, yeah.

Pat: And those are 20, 30 year jobs.

Nate: Yeah. Yeah, or longer. Right?

Pat: Or longer.

Nate: Yeah.

Pat: And so those, you know, there's those ... are producing products. And so in order for MLPs, like SNMP, or transporting the product, to the facilities that are going to further break down the molecules, that feed these petrochemical complexes.

Nate: You mentioned, you didn't wanna talk about Sanchez Energy, but I was curious if you might just touch on the relationship between Sanchez Midstream and Sanchez Energy? And just kind of, if you wouldn't mind describing what a ROFO is, and what are the assets that could eventually be dropped. And whether or not, you know, you wanna get into any of those details, I think could just be helpful for people to hear.

Pat: Yeah, sure. I mean, the way that we're set up here, I mean, Sanchez Oil and Gas is not a revenue center. It is ... it does not hold assets, it's an employee base. That's where the employees sit. And then we have management services agreements with two entities, and that is Sanchez Midstream Partners and Sanchez Energy. And the time sheets, and allocated ... We allocate time, based upon projects, and initiatives, and you know, literally, we review this, how much time an individual spends on a project. That's how expenses are allocated to the two entities. And then SNMP has a "Right of First Offer," on the midstream assets of Sanchez Energy.

So as Sanchez Energy grows, Sanchez ... It does not have to spend capital on midstream build out. It can spend its capital in a much more efficient manner, on recycling its capital through the drill bit. And Sanchez

Midstream Partners spends capital in the midstream side, and the water infrastructure, and the frack water, recycling. And allows Sanchez Energy to recycle its capital, in much more efficient manner, through the drill bit.

Nate: So, and forgive me, 'cause I'm not as familiar with this part of the business, does Sanchez Energy have midstream assets, currently in the Sanchez Energy portfolio, that could be dropped down? Or is it just, when you talk about ROFO, it's really in reference to the acreage dedication? So anything that's built-

Pat: It does.

Nate: Okay.

Pat: There are some midstream assets.

Nate: Okay.

Pat: There are some water assets, and there are a backlog of assets.

Nate: Okay. Have you talked about much, in terms of EBITDA? And again, if you don't want to get into it-

Pat: We have, yeah. We prefer not to get into EBITDA, the backlog-

Nate: Okay.

Pat: ... drop downs. But there are a backlog.

Nate: Okay.

Pat: There are plenty of assets to drop down. And we're working towards dropping them down.

Nate: And how are the decisions made, in terms of how much of the infrastructure that's built out, and the capital expenditures that are realized at Sanchez Midstream, versus what's going on at Sanchez Energy?

Pat: Well, I think it's a delicate balance. I mean, it's about capital allocations, about capital discipline, and it's about being able to raise the capital. As you well know, the MLP space is going through a different period. And we have transitioned through it. Some entities are collapsing the GPLP structure, others are converting to corporations. But we sit down, like any other company or organization, and we go through the projects and see what we can try to develop. So it's just a ... it's a feasibility study, like most entities go through.

Nate: Yeah. And what are your thoughts on, just sort of the evolution of what's been going on in the midstream space, with you know, we have seen these collapses, we have seen a lot of corporate structure changes? And does Sanchez Midstream have a particular view on what has transpired over the past year to 18 months? And does that influence how you're thinking about what the appropriate structure is for Sanchez Midstream, in terms of the GP and the LP?

Pat: Yeah, I mean, we thoroughly review the corporate structure, and look at all possibilities, and review different opportunities to maximize value. We reviewed the different tax laws, the different tax changes, different fiscal changes, and we review them on a one-off basis. But at the end of the day, we're going to focus on long term value, and not make any decisions, not make any knee jerk decisions. We're very thorough, we've very disciplined, and that's how we run our business.

Pat: The GP is owned by ... it's privately owned, by our family. And we're long term holders.

Nate: Could we go back to, you mentioned minimum volume commitments, and you know, that's something that is required for a midstream company to earn a minimum rate of return. Could you just help the audience understand, what is a minimum volume commitment?

So let's just say that I'm an EMP, and I'm an upstream producer, and I'm gonna go drill on my acreage, but I need someone to transport and process the natural gas liquids, the wet gas, that comes out of the well bore. What is the dialogue between you, Sanchez Midstream, and potential customers to use Sanchez Midstream services, for gathering, and processing, and transportation?

Pat: Sure. So, I think the easiest way to think about it is a toll road. So, when you build out a system, an infrastructure system, or some type of toll road, you need to generate a certain return, a level, on your capital that you deployed. So in our case, we purchased, from SN, the Western Catarina gathering system, for a certain dollar amount. Okay? So we need to earn a certain rate of return on that capital.

Pat: So in order to ensure that a certain amount of volume of hydrocarbons, over time, is going to flow through that system, at a certain per unit charge, per MCF charge. So we charge an amount based upon the unit of gas that flows through the system. It's basically a floor.

Pat: So if gas drops, if the upstream producer ... And this is common within the industry. If the upstream producer, for whatever reason, maybe commodity prices drop, slows back, or pulls back on the pace of development, he can do that. He can pull back on rigs, he can pull back on the number of wells that he drills within a given year. But he's still, then at point, if he drops below that floor, has to pay a deficiency fee.

Pat: So that the midstream operator, like SNMP, is guaranteed a certain amount. So that, in turn, I can pay the unit holders, who invested and put up the capital to purchase that system, in the first place. And that's called a "minimum volume commitment."

Nate: Is production higher than the minimum volume of commitment?

Pat: On the Western Catarina asset, we're we have minimum volume commitment, yes.

Nate: Okay.

Pat: That's where the MVC is.

Nate: And has it ever gone below the minimum volume commitment? Based on where commodity prices have sort of fluctuated over the past few years?

Pat: No.

Nate: When you think about the MVC, and fluctuations in commodity prices, I guess one of the things that I'm trying to highlight about, at least my understanding of how the correlation between volumes and commodity prices isn't one-to-one. Or it isn't 1.0. And what I mean by that, is commodity prices from 2014, into 2016, and 2017, were basically halved.

I mean, they were more than halved, for oil. WTI oil prices went from north of a hundred bucks, per barrel, to, I mean, they bottomed at $26, but you know, they've averaged somewhere around, call it 50 bucks. And natural gas went from four dollars, in MMCF, to you know, call it averaging around two bucks, $2.50, I mean, they're $2.70 today.

But the point being, is that commodity price decline was much more significant than the decline in volumes, that the industry witnessed. And so, I guess I'm just trying to quantify what the direct commodity exposure is, for a midstream company like Sanchez Midstream.

Pat: I think that's a good question. One of the reasons that volumes did not fluctuate significantly, in some of the past commodity downturns, on the property is, that there's a minimus, as per the lease. It's a contiguous 100 thousand acre block. And as per the lease, there's a minimum number of wells that has to be drilled, per year, that the upstream operator has to drill.

Pat: So there's additional safety, or protection, to the stability, to the cash flows, to SNMP. You have the 50 wells per year, as per the lease, then you have the MVCs, then SNMP. So-

Nate: Thanks, Pat. That's helpful. Could you talk a little bit about system utilization? Or just the overall utilization of your system, and the JV with Targa?

Pat: In terms of utilization, we're working towards, obviously Sanchez Energy, just made an acquisition. They purchased [inaudible 00:22:03] Eagle Ford assets. We're working towards signing up those working interest partners, to become part of the Carnero JV, which includes Raptor, and the Carnero line. And increase the volumes through Seco, and increase the volumes through, and expand Raptor.

Okay, so if you think of that JV with Targa, how else can it be expanded? You have other operators in the area, that over the next couple of years, have contracts rolling off. Many contracts, over the next couple of years, are going to roll off. And we're going to aggressively pursue those contracts, to try to fill up our assets, and our gas plants.

In addition to that, you have oil. You have oil, our contracts coming off from ... You have some oil opportunities, you have a large amount of gas coming in from the Permian, trying to get to Corpus Christie, what's called Agua Dulce, which is a major dry gas hub.

We are in between Agua Dulce and the Permian. So any ... we're a natural fit to pick up our volumes on the way. We're gonna ... we would like to participate, the way we participated with Targa, on the infrastructure. So if our hydrocarbons travel through the pipe, we would like to participate, equity participation in the infrastructure.

Nate: Okay, okay. That's great. But could you talk a little bit about high level thoughts on what gas takeaway from the Permian, could mean for natural gas prices? But also what that means for ... and you just explained, that anything that comes from the Permian, should cross over your acreage, or at least come close, and you could find an outlet for that natural gas. But just what that means for natural gas takeaway, from the Permian, what that means for Sanchez Midstream?

Pat: What is obvious, is that there is a significant issue in the Permian, when it comes to dry gas, and natural gas takeaway. Over the past couple of days, you've seen, and I'm sure you've read many articles, where natural gas is close to being worthless because of takeaway issues. The way that we view our advantage, or an upcoming opportunity for us, is we ... most of that Permian gas is gonna try to get to South Texas, to be able to move towards the Mexican market.

The Mexican market is soaking up an enormous amount of dry gas. They're moving it through the Permian. But the problem with the Permian, going straight to Mexico from the Permian, is its obvious location. Mexico City, Monterey, and the industrial complex along the Gulf of Mexico, is a natural fit for that natural gas. As opposed to the desert, the Sonoran Desert, which you would have to cross.

So we, SNMP, and it's volumes of natural gas, which it has a right of first offer on, are in between stranded gas, in the Permian, and the market in which the Permian gas is trying to get, which is Agua Dulce, in South Texas. And that is a major transport hub, and many ... several companies have recently announced some dry gas takeaway options, to Agua Dulce. And in addition to, many ... or not many, it's three or four, companies, have also announced crude pipelines to Corpus Christie.

So across the ... I mean, there have been a natural gas liquids, an ARIES backed company, a natural gas liquids pipeline, from the Permian, to Corpus, several crude oil pipelines to Corpus, and several natural gas pipelines to Corpus. And so, we feel confident that we're strategically located, where we're gonna be asked ... we'll contribute your volumes to a partnership, where, you know, we can move your volumes.

So Nate, what do you think some of the headwinds or tailwinds are, in the MLP space? Specifically, if you exclude some of the collapses, and some of the reorganizations, in terms of structures, corporate structures, from a retail, institutional point of view, capital flow, what are some of the headwinds?

Nate: So some of the headwinds that I see? Well, I think that maybe, the headwind that's front and center for me, having left the firm that I left, and also after, having spoken with a lot of financial advisors, and trying to do my market research in putting this IwtB business together, is just the lack of sponsorship. And by that I mean, there just aren't that many equity investors that are interested in owning midstream, right now.

And part of that, is just due to the fact that, the stocks have been ... well, they've underperformed, and energy's been very volatile. But I think that it's also partly due to the fact, there have been some bad actors. And by bad actors, I mean, too much debt, and setting out growth objectives that just weren't obtainable, especially given the collapse in the commodity price, which then led to leverage concerns, and what I think was just frustration with the entire space. And so, nobody has an interest in investing in energy, in general, and midstream in particular.

And for those listeners out there, who don't understand how the midstream model works, midstream companies have, in the past, issued shares in order to fund growth. Because most of the projects are funded, you know, just call it roughly 50/50, debt and equity. And that put them in a difficult situation, in terms of being able to fund current growth projects, things that they've already started, and they couldn't walk away from.

So what's the natural next step? Well, you cut the dividend. A financial adviser who's managing a retiree's investment portfolio, probably just looks at that and says, "Well, there's something wrong here." And then, on top of that, and this is something that I talked about in the podcast intro, which is, we've seen an enormous migration towards passively managed funds. And midstream companies aren't ... energy in general is not a very large component of the big index funds that are out there.

So with respect to retail sponsorship, I think that it's going be an extremely difficult uphill climb, from here. Interest rates could continue going up, which obviously create issues from a cost of capital perspective. And so, if you don't have sponsorship on the equity side, and if you don't have sponsorship ... and if your cost of debt is going up, your overall cost of capital can get out of whack, pretty quickly.

If there's one thing I heard, quite consistently, from management teams, over the past two years, it was that the space needed a consistent three, four quarters of relatively benign, or absolutely no bad news. Meaning, no announcements of distribution cuts, and midstream stream companies hitting the numbers, hitting guidance. But we saw a lot of that in 2017, and retail investors just have not come back into the space.

Unfortunately, things got even more complicated. Last year there was a lot of concern about taxes, whether or not the MLP structure would exist through Trump's tax reform. And then there's also regulatory issues, and that was highlighted in the recent [00:29:44] FERC ruling around the tax disallowance. It's almost like a pick-your-poison type of scenario, because there are so many different things that are going wrong in the midstream space, that are affecting fundamentals, but also affecting perception.

But I would say, that regulatory issues and tax issues are the biggest headwinds, because you just don't know what's going to happen. You know, I used to work in the wind space, developing wind energy projects. And every single year, it came down to the wire, as to whether or not Congress was going to extend the production tax credit, or the PTC. And so I imagine, it's extremely difficult, for an industry like yours, to plan ahead for the next investment cycle, when you don't whether or not they'll be changes to regulation, or to taxes.

So then there's the bigger picture, or longer term issue, of the environment. So water disposal and sourcing. So how much water's gonna be available for upstream companies to inject into wells, in order to fracture them? You need to have fresh water, at least you need to have water that doesn't damage your equipment. And then, disposal of water.

My wife is an environmental engineer, and she's worked for a couple of companies, over the past few years, that have done a lot of work for refineries. And there was one refinery, in particular, that I remember her telling me about, could no longer dispose of their waste water in a local well, or a local disposal well. I think the pressures just got too high, or I'm not sure what the details were, exactly. But-

Pat: Yeah, they exceeded injection pressure. And so they started injecting into other zones, and it was a mess.

Nate: And so, yeah. If you could just talk about, could you talk a little bit about, disposal and sourcing of water, for Sanchez?

Pat: Water's not as big of an issue, and water sourcing is not as big of an issue, because of aquifer levels in South Texas. We're very cautious about the disposal process, and that is governed by the Texas Railroad Commission. But the sourcing of water is not as big of an issue, because of the aquifer levels, currently. But we do go through low level, low aquifer levels, and have in the past.

Nate: And when they, when aquifer levels go low, then does the Texas Railroad Commission come to-

Pat: If I'm not mistaken, the aquifer is governed by Water Boards, local Water Boards. And then you're restricted on how much water you can pump, per water well, and it's a calculation, based upon, I think, the surface owners. So then you get to the point, where you have to recycle some of your fracked water, and use natural gas to power generators, and the facilities, to recycle water.

Nate: Does Sanchez recycle water?

Pat: Well currently, we do not, on a large scale, recycle water, SNMP does not.

Nate: You said, no issues on sourcing of water, but in terms of disposing water, what are the issues there? And is it much of a concern for Sanchez?

Pat: No, currently, it's not. It's not. Disposing of water is not an issue. Because typically, the Eagle Ford is not a high water producing formation. Yes, it's not like the Mississippi Lime.

Nate: Yeah, it's funny that you mention the Mississippi Lime. I'm actually from Oklahoma, and I still go visit my family for the occasional holiday. And I remember, a couple of years ago, I was there for Christmas, and I had the flu. And I spent my entire Christmas break laying on a couch. And it was at a point in time, when the earthquakes in Oklahoma were at their peak.

Pat: Oh, yeah.

Nate: And I remember being woken up by an earthquake, that just scared the shit out of me. I mean, it was the first time that I had ever experienced anything like that. But probably not the most appropriate story for this podcast.

Nate: Could you just talk about, what are the tailwinds and headwinds, for growth? For Sanchez Midstream?

Pat: Well, I think that the tailwinds are, obviously, some of the events of the past within the MLP space. And convincing institutional investors, certainty of distribution, certainty of volume growth, that we can hit our projections, and that we can operate our business in a very predictable manner. Like you mentioned earlier, there were some entities that took on too much debt, and cut distributions, and the whole sector suffered.

We are a very strong company. We're levered approximately two-and-a-half times, a little under two-and-a-half times. We have strong coverage ratios, line of sight towards distributions, line of sight towards volume growth. And we'd like for people, just to look into our story, look into our assets, and understand our platform. Understand the Eagle Ford basin, we're very close to the demand centers, the feed star, the petrochemical complexes that need the feed star. We are not stranded in some remote basin, where it's gonna take hundreds, and hundreds of millions of dollars, to transport molecules to get further processed.

We're along the Texas Gulf Coast, and we're moving hydrocarbons to get fractionated, hydrocarbons to get natural ... to get processed further, through natural gas processing plants. We're gonna own Tourmaline assets. We're moving dry gas to points, then to get moved to Mexico, demand centers along the Texas Gulf Coast for natural gas. And hopefully, in the future, be able to build out fractionation units that can provide propane, to different demand centers, along the Texas Gulf Coast.

Nate: Yeah, I think that's a very important point that you mention, about the Eagle Ford, because I think that, you know, there for a while, the Eagle Ford was the big story, call it three years ago. And then, all of the sudden, everybody's talking about the Permian, and the resource. I think that the fact that ... that distance from the Permian to demand centers, is lost. As well as, the proximity of the Eagle Ford to demand centers, is lost ... has been lost on investors over the past couple of years, because of this Permian craze. So, I think it's important that you mention that.

So, what about headwinds, though?

Pat: I pretty much, I like all your headwinds. I think the headwinds are getting institutions and the retail base, comfortable. And getting them back into the space, getting them comfortable with the story, comfortable with the energy space. And for several years, you know, there was a big drop in commodity prices. We want from, you know, over a hundred dollars, down to in the high 30s. Balance sheets are shoring up. Companies are starting to live within their cash flows.

I think the other issue is, you had the tech industry sap investor interest out of every sector. And so there are several headwinds. But if we remain disciplined, and we remain focused, and we just focus on running our business in a very disciplined manner, and make good decisions, and you know, operate it within that two-and-a-half times leverage, I think, in the long term, investors will reward us.

Nate: So, yeah. The next thing that I was gonna get at, you say the long term, and what I think is just absolutely mind boggling about the Sanchez Midstream story, is that, you've continued to ... I don't think there's another midstream company out there, who has had, over the past few years, leverage as low as Sanchez Midstream, two-and-a-half times, continue to grow their distribution, but their dividend yield is still mid-teens. Are you aware of any other midstream company out there-

Pat: I'm not aware of one.

Nate: Yeah. And so, when I think about, you know, getting the ... getting investors interested in energy, or in the midstream space, what do you think midstream, in particular, what do you think the space needs to do? And what do you think that Sanchez ... I mean, I don't think Sanchez needs to do anything, because you did what you were supposed to do, what you told investors you were going to do. But what do you think the midstream space needs to do? In order to get greater investor appetite, in the space, and?

Pat: I'm not sure what the space, as a whole, needs to do. We focus on our business.

Nate: Yeah.

Pat: And we get out there, we sit down with investors, we sit down with institutional investors, we sit down with retail investors, we walk them through our models, we walk them through, most importantly, line of sight towards distributions, we walk them through our assets. We explain to them where we're transporting hydrocarbons, and we walk them through high level, the demand centers, where our natural gas liquids are going, where our dry gas is going, where our oil's going. And let them kind of put the pieces of the puzzles together. We explain to them the volume trajectory of SN. And we have a right of first offer.

Pat: And we pound the table, day in, day out, on that. And we're not going to over-lever this entity. We have a strong coverage ratio. And that's about it. We really don't worry about other, you know, other organizations' story, or what they're doing. We just focus on ... Running one company's hard enough. When you start worrying about, what other groups are doing, that's when I think, you get distracted.

Nate: For Sanchez Midstream, what's the benefit of being public right now? Why not just go private?

Pat: Well, I think there're many benefits to being public, and even thought it's not true, at the moment, the obvious one, is access to capital. Access to different types of securities, whether they're hybrid equity debt securities, preferred. You know, different types of ... What would the benefits to being private be, if right now, there are ... the disadvantages are that there's no access to capital, even if you're public.

Nate: For you in particular, you're the largest individual shareholder of Sanchez Midstream Partners, and you're also the COO, what keeps you up at night from a business pers-

Pat: Am I the largest individual?

Nate: Well, that's what it shows on Bloomberg.

Pat: Oh, wow. So, I'm the largest individual?

Nate: Let me double check. But I do believe you're the largest individual shareholder of Sanchez, Midstream, that is. But what keeps you up, from an operational business perspective? And then, what keeps you up from a personal, from the largest personal shareholder's perspective?

Pat: Well, I think what keeps me up at night ... And I'll take your word for it, I haven't checked myself, that I'm the largest individual shareholder. But what keeps me up at night? Difficulties of running the business.

We run a business that entails hundreds of miles of pipe, small leaks do occur. We transport several hundred billion cubic feet, a day, of gas. We transport hundreds, of you know, thousands of barrels of oil. We transport hundreds of millions of cubic feet of dry gas. And there're inherent, you know, dangers and complications associated with doing that.

So we have to ensure that the process ... the safety processes are in place, to mitigate those risks. We also have to ensure, on a daily basis, that the safety ... I mean, that the processes are in place, in terms of everything from cost controls, to accounting, finance [inaudible 00:42:15], all of your back office functions.

And that they are constantly being updated, and checked to make sure that they are accurate, and are providing us with data and reports, to make the best decisions.

And so, it's a constant work in progress, to collect data, interpret the data, and use it in a manner that's gonna allow us to make better decisions. But first and foremost, is the safety of the individuals at the field level. Are we operating the system in a safe manner? That's what I think about.

Nate: You are number ... You're the largest individual shareholder, but you're number three on Bloomberg. Is there anything that keeps you up, from you know, the perspective of the largest individual shareholder?

Pat: Same thing that keeps me up as President and Chief Operating Officer.

Nate: Yeah.

Pat: Yeah.

Nate: That's a good answer. So a favorite investor interaction story, so you know, I'm kind of framing this podcast up as, you know, this is corporate access, but it's also, what corporate access is, and what they buy side, sale side, are, and what does the buy side do, in order to go out, and you know, learn more about companies, and it's going to these investor meetings. And so, do you have any funny, interesting stories, about when you, you know, you walked into a meeting and?

Pat: Well sure, you always get some off hand, bizarre questions. We go through ... So we're very active on conference circuit, and you know, at each conference you have one-on-one meetings. And I think, we were asked something along the lines of, why we weren't in solar.

Nate: Why you weren't in solar?

Pat: Yeah, yeah.

Nate: So why aren't you in solar?

Pat: Well, we didn't have an answer, but we offered him a cookie. There were some cookies on the table, and we told him we'd think about it. We weren't sure that it fit our business plan, and also the qualified income aspect, might be an issue. But you do receive some questions sometimes, that are pretty interesting.

Nate: So last question, just parting thoughts, or next steps for an investor who's interested in learning more. What should they focus on? What do you think they should do, in order to get comfortable with Sanchez Midstream? Or uncomfortable?

Pat: Well, first and foremost, call us. Call us, come drop by, sit with our Investor Relations, Kevin Smith. Investor Relations, we're in Houston, (713) 783-8000. Kevin Smith is our Head of Investor Relations. Sit down, we can walk you through our business, we can walk you through our models, we can walk you through our vision, our growth plan. And then, you make the decision. But give us the opportunity to walk through our road map.

Nate: So, I guess, maybe it's helpful if ask the question just a little bit differently. What do you think's being missed, in the market?

Pat: I think what's being missed in the market, is the volume growth through our infrastructure. People are not looking at our assets, and the right of first offer. They're not looking at the existing infrastructure, and tying it back to the volumes from Sanchez Energy, and looking at the volume growth that Sanchez Energy has publicly disclosed.

Nate: Okay. Well-

Pat: And I will add one thing, that they're also ... is the strong balance sheet.

Nate: Yeah.

Pat: I mean, name one other company, one other MLP, you know, our peer, in our peer group, that's two-and-a-half times levered, with our coverage ratio.

Nate: Well, Pat Sanchez, thank you very much, for your time. It's been a pleasure talking to you, and I really appreciate you taking the time to speak with Investing with the Buyside.

Pat: Thank you, Nate. I appreciate your time.

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