

THE BIG SECRET ON WALL STREET

# Cold War 2.0 and the Coming Global Energy Wars

 America's Rise as a Natural Gas Superpower

FROM THE DESK OF PORTER STANSBERRY

SPECIAL REPORT

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## Cold War 2.0 and the Coming Global Energy Wars

### America's Rise as a Natural Gas Superpower

CIA director William Colby sighed as he picked up the telephone.

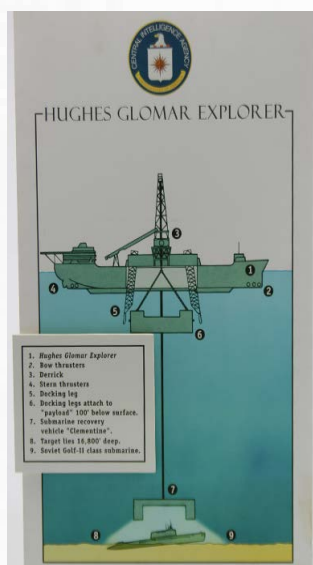
It was March 1975, and Colby had a tiresome task in front of him: Call every major national news outlet and beg them not to publish a “top secret” story... that they all already knew.

Deep in the throes of the Cold War, America's top intelligence agency had the clever idea to dredge up a sunken Soviet submarine to study its nuclear trappings.

One problem: the sub was three miles underwater off the coast of Hawaii.

How to retrieve it? Easy. Trap it in a huge globe of gas – imagine a really big soap bubble, and think of it underwater, with a submarine inside of it – and float it to the surface.

Naturally, that didn't work. So instead, the CIA built a 618-foot ship outfitted with a giant claw underneath – like an arcade prize machine. The claw itself was codenamed “Clementine.”



*A diagram of the ship's claw retrieval mechanism on display at the International Spy Museum.*

The ungainly ship – launched under the pretense of deep-sea mining – was under construction for months. It was about as secret as Victoria's Secret. And crack investigative journalist Seymour Hersh had a full expose ready to publish in the *New York Times*.

CIA Director Colby dutifully contacted news organizations in the know to tell them to keep quiet. As *Time Magazine* explained,

“

*The Washington Post, NBC, ABC,*

*Newsweek and the Washington Star all got wind of the project. In each case, after a call or visit from Colby there was a decision not to go ahead.”*

Eventually, with reporters pointedly excluded from the launch, the “Hughes Glomar Explorer” set to sea, dragging its massive claw like a crippled, one-armed Tyrannosaurus Rex.

And after all that brouhaha... the mission was a New Coke-level flop.

About halfway through the initial recovery operation, one of the grabber arms on the giant claw broke – and much of the just-retrieved Soviet sub sank back to the ocean floor. In the end, the CIA only recovered about 40 feet of the 300-foot vessel...along with the remains of six Soviet soldiers, whom they immediately buried again...at sea.

Hersh later released his story anyway (and went on to become a Pulitzer Prize-winning journalist over a fifty-year career). And the CIA added another entry to its long list of botched cover-ups – compounded by a botched operation in the first place.

The U.S. government has never been good at keeping secrets.

For a more recent example... take the Nord Stream pipeline.

Officially... on September 26, 2022, Russia blew up the pipeline that’s the major artery for transporting natural gas from its fields in Siberia and elsewhere, into western Europe.

“

*Russia is opening a new front on its energy war against Europe,”*

squawked the *Washington Post*.

**The Washington Post**  
*Democracy Dies in Darkness*

ENERGY

## Is Putin Fully Weaponizing the Nord Stream Pipelines?

“

*“First, it (Russia) weaponized gas supply, halting shipments,*

*including via the Nord Stream pipeline. Now, it may be attacking the energy infrastructure it once used to ship its energy,”*

the paper continued.

Following the bombing, President Biden (always a bastion of clear-headedness) announced he was working with U.S. allies to “*get to the bottom of exactly – precisely what happened.*” Never mind that it didn’t make sense for Russia to slit its own throat – that is, to blow up the vehicle of a major source of revenue.

Less than five months later, the real story came to light. (By comparison, Colby got the mainstream media to sit on the “claw ship” story for more than a year.) And, funnily enough, it was Seymour Hersh who broke the Nord Stream story, too.

Seymour, now 85, published a bombshell report on the Substack platform on February 8, 2023.

He claimed that the U.S. Navy, under authorization from President Biden, carried out the Nord Stream attack... *not* Russia.

Hersh reported that the attack was planned in December 2021 – three months before Russia launched its invasion into Ukraine. In June 2022, Hersh said, during a military training exercise, U.S. Navy divers planted remote-controlled explosives on three of the four Nord Stream pipelines. The bombs were remotely detonated three months later.

If Hersh’s reporting is accurate – and a lifetime of prize-winning exposes under his belt, including Watergate, suggest he’s rarely incorrect – the reality is that America was purposely weaponizing global energy markets. What’s more, it suggests that the U.S. was planning this energy war well before Russia invaded Ukraine, in February 2022. And the Nord Stream blowing up was just another example of misdirection (if not downright lying) by Uncle Sam.

What this means is that Cold War 2.0 is here – and global energy markets are the battlefield. America wants to replace Russian gas supplies to Europe with American shale gas, through liquefied natural gas (LNG) exports... and won’t let anything get in the way.

This reinforces one of the most important investment themes of the next decade.

## **America’s Rise as a Natural Gas Superpower**

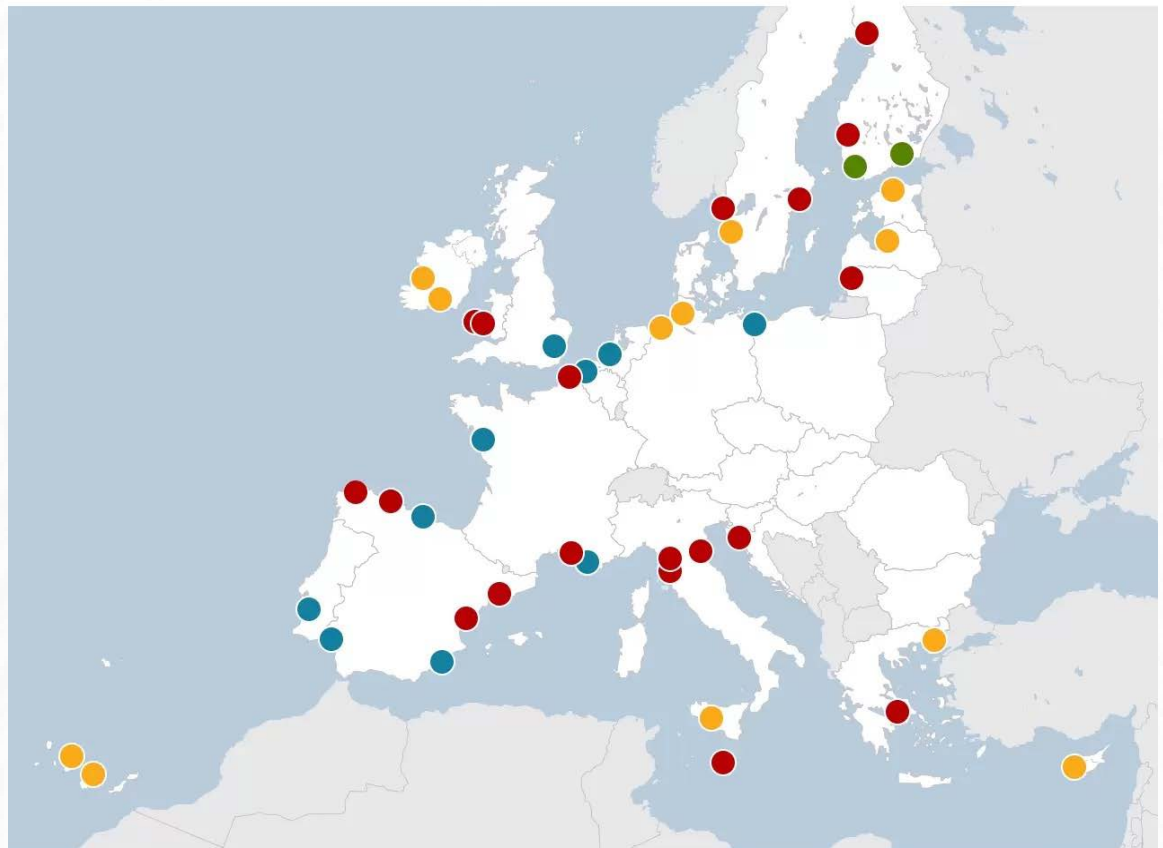
Before Russia invaded Ukraine in February 2022, the European Union relied on Russia for about 45% of its natural gas. After the geopolitical flareup between Russia and the West, the EU announced plans to stop using Russian gas by 2030.

As we’ve [written before](#), this means Europe will need to source its energy

somewhere else... and that's where American LNG (liquefied natural gas) comes in.

The map below shows more than a dozen new LNG import terminals planned or under construction across the European continent, as of December 2022:

## LNG ports in Europe



### Terminals for LNG

- Operational
- Under Construction
- Operational and expansion planned
- Planned

Source: European Commission, December 2022

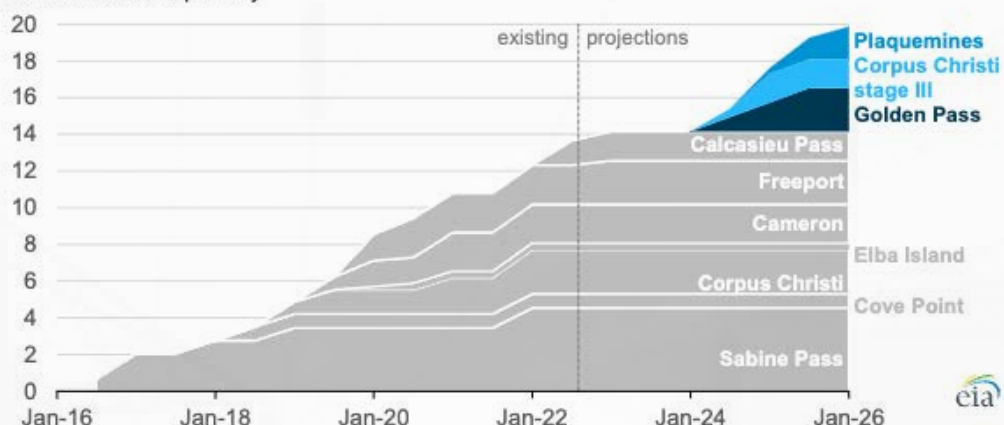
America has the export facilities – and the plentiful shale gas reserves – to feed those import terminals over the next decade. The U.S. is the leading supplier of LNG to Europe, with U.S. LNG shipments to Europe surging by more than 137% in 2022 versus 2021.

And over the next three years, a series of new LNG export facilities will boost U.S.

LNG exports by roughly 40%, from 14 billion cubic feet per day (Bcf/d) of capacity today to 20 Bcf/d by 2026.

## U.S. LNG export capacity to grow as three additional projects begin construction

**U.S. liquefied natural gas export projects: existing and under construction (2016–2025)**  
billion cubic feet per day



Data source: U.S. Energy Information Administration, *Liquefaction Capacity File*

Note: EIA estimates are based on information from Federal Energy Regulatory Commission and U.S. Department of Energy filings, company websites, trade press, and other industry sources.

Moreover, a second wave of 15 U.S. export projects is officially approved and waiting on funding. These new facilities represent a combined export capacity of approximately 19 Bcf/d, or nearly 50% more than current U.S. export volumes, and we expect many of them to come online by the second half of the decade

**Tellurian's Driftwood LNG terminal** is one of these projects. Although the company has faced challenges securing financing for its project, the scramble to lock in low-cost U.S. LNG supplies gives us confidence that a deal will eventually get struck.

Looking beyond Europe, American LNG remains in high demand across major Asian economies, including Japan, China and India...

Earlier this month, Indian Prime Minister Narendra Modi announced plans to increase the country's share of natural gas for power generation from 6% today to 15% by 2030, by increasing its LNG imports. Indian LNG importers are now in the market for long-term contracts, and we expect other countries will follow their lead. Research from energy consulting firm Wood Mackenzie projects that the global LNG market will tighten by 2026, and grow increasingly tighter through 2033.

Tellurian is in talks to pick up some of those very contracts. (See the Portfolio Update below.)

Right now, U.S. gas prices are among the lowest in the world. But as America increasingly expands its LNG export infrastructure, U.S. natural gas prices will increasingly converge with much-higher international prices. And the companies that own low-cost gas reserves today will reap a windfall.

The bottom line: the stage is set for a supercycle in U.S. natural gas... for decades to come.

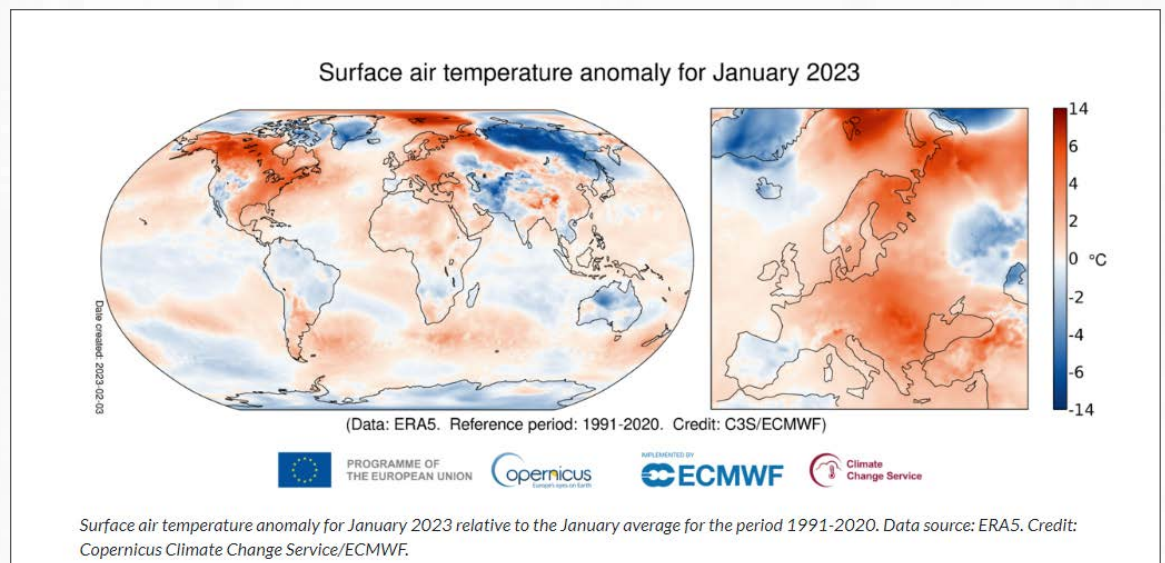
Despite this bullish backdrop in the long run, both European and American gas prices have recently fallen, thanks to a curveball from Mother Nature.

### Gas Supercycle Delayed by Balmy Winter

Last winter, extraordinarily warm weather crushed natural gas demand for heating around the globe. Following a mild autumn, a record-shattering heat wave swept across Europe at the end of December. This extreme end-of-year warmth capped off the hottest year on record in France, Spain, Ireland and the UK. The European continent as a whole registered its second-hottest year on record, going back to 1950.

New Year’s Day then set the tone for the rest of the month, when eight European countries broke new records for the hottest January 1 temperatures on record by wide margins. This was followed by above-average January temperatures – the single biggest month for gas heating demand – across the European continent. Meanwhile, the U.S. experienced its sixth- warmest January on record... concentrated in the heavily populated northeast, which is normally the highest-demand heating region.

The graphic below shows extreme warmth across much of the globe in January:

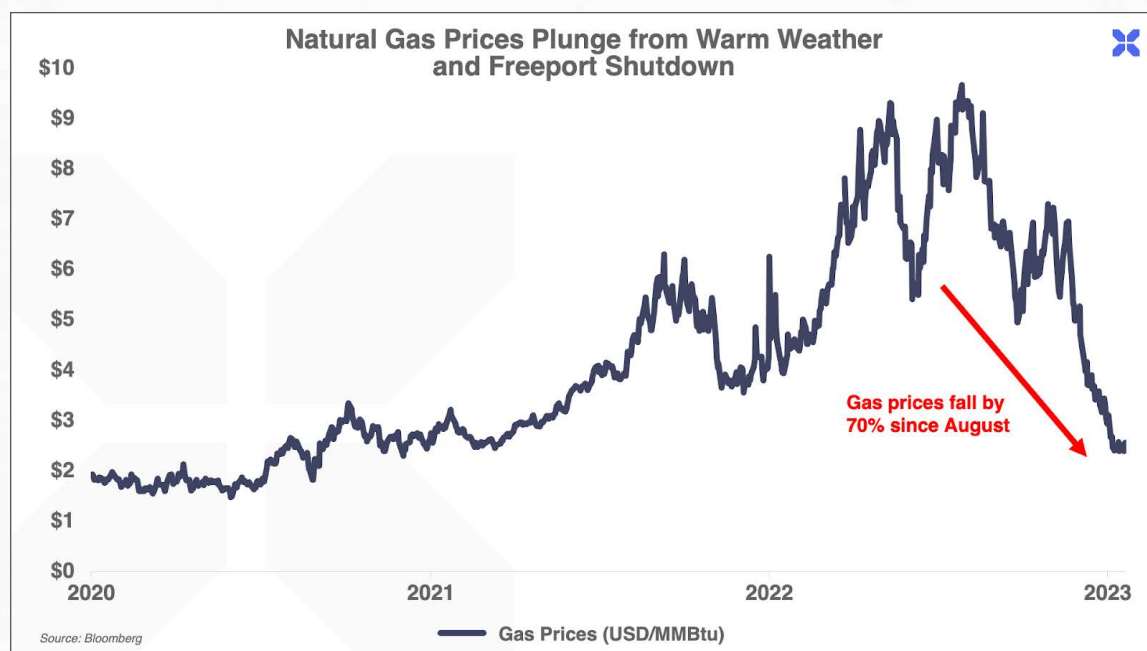


Source

February followed a similar pattern, with continued extreme warmth across the globe. As a result, European gas inventories have ballooned to 66.5% of capacity, or 23.2 percentage points above the five-year average storage capacity for this time of year.

Adding a little molten chocolate to the hotcakes, the U.S.'s second-largest LNG terminal, Freeport, was shut down for months after an explosion at the facility in summer 2022. With Freeport offline, gas demand for U.S. LNG exports fell by roughly 15% from July 2022 through January 2023.

The one-two punch of warm weather, and lost Freeport demand, flipped U.S. gas inventories from a 10% deficit in July 2022 to a 5% surplus to start 2023. This sent prices reeling from a 15-year high of \$10 per million British thermal units (MMBtu) in August 2022 to as low as \$2.00 per MMBtu in early 2023.



Freeport was gradually brought back online starting in February, and reached fully operational status by April, restoring roughly 2 Bcf/d of demand back onto the U.S. gas market.

But the demand losses from extremely warm weather, amplified by the previous disruption at Freeport, have resulted in a storage overhang that will likely keep pressure on U.S. gas prices for the remainder of 2023. And that positions us for a tremendous buying opportunity in top-tier U.S. gas companies, whose shares have sold off across the board... for 2024 and beyond.



## Today's Low Gas Prices Set the Stage for Tomorrow's Supercycle

Most public exploration and production companies (E&Ps) decide on their capital budgets in the first quarter of each year. Given the collapse in prices to as low as \$2.00 per MMBtu (well below break-even for many gas basins) to start the year, corporate boards will likely hesitate to outlay capital for much, if any, growth in production this year.

Here's the problem...

U.S. gas drillers *need* to grow production, and fast.

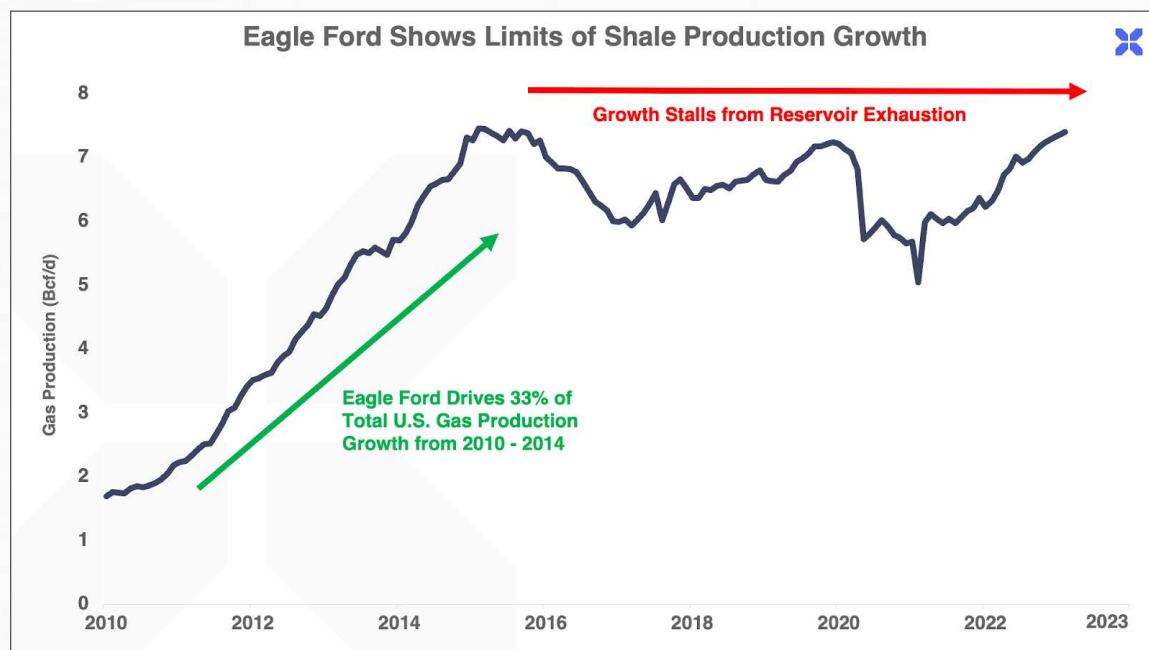
Remember all those new export facilities set to come online by the start of 2024? They all need gas to ship overseas. Absent meaningful production growth in 2023, E&Ps will need to add an average of 3 Bcf/d in 2024 and 2025.

This wouldn't have been a problem during the heyday of shale production from 2010-2019. During those years, U.S. natural gas production grew by an average of 4.2 Bcf/d.

But since then, drillers have exhausted their best drilling locations in many U.S. gas basins... and growth has dramatically slowed to just 1.3 Bcf/d each year, or a 70% decline in growth rates.

Consider the case of the formerly fast-growing Eagle Ford shale, which was responsible for one-third of the growth in U.S. gas production during the early days of the shale revolution.

The graph below shows how Eagle Ford gas production growth stalled starting in 2015. Even though gas prices reached as high as \$10 per MMBtu last year, Eagle Ford production has yet to reclaim its prior peak:



In addition to depleted resources, the oil industry is also battling the PC police. These days, draconian ESG mandates siphon money out of fossil fuels... a far cry from the shale revolution, when a virtually endless flood of cheap capital poured into the sector.

The combination of inventory depletion and capital constraints won't be solved without much higher prices.

To meet the massive new demand for U.S. gas hitting the market in 2024 - 2026, the rate of production growth will need to more than double from the previous three-year average of 1.3 Bcf/d to at least 3 Bcf/d starting next year.

That means oil prices will skyrocket no matter what. They'll either rise high enough to encourage a flood of new investment today... or shoot up later from a crippling gas shortage tomorrow.

In either case, top-tier E&P companies with leading acreage positions in low-cost basins will be the biggest winners.

EQT is one of these companies, with the dominant acreage position in the largest low-cost natural gas basin in the world – the Appalachian shale. EQT is led by two brothers – **The Gods of Gas** – who are transforming the global energy markets. In the fall of 2020, the Gods of Gas struck a huge deal with Chevron to acquire 800,000 acres in Appalachia for pennies on the dollar.

This deal was struck in the wake of the collapse in energy prices during the early days of the COVID-19 outbreak. EQT paid just \$735 million, while Chevron was

forced to take an \$8 billion write-off on the same land two months prior to the sale to EQT.

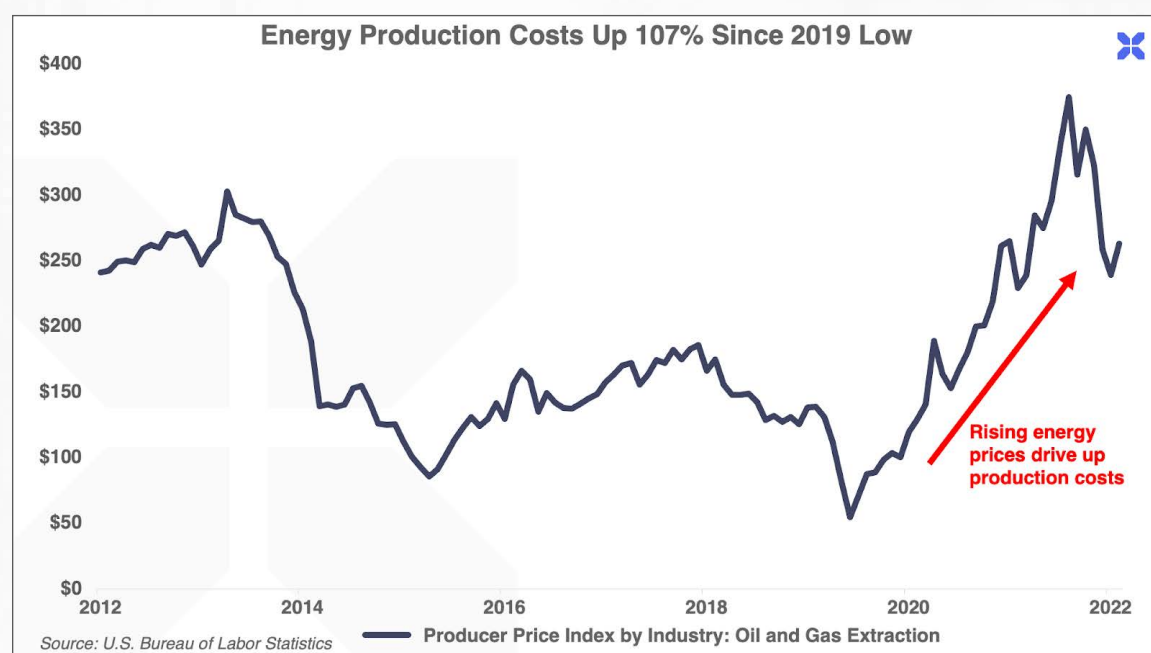
By making a big acquisition when the rest of the market was in panic, EQT set the stage for a cash flow windfall when prices recovered. In 2022, EQT returned over \$1.65 billion in capital to investors in the form of share buybacks (\$422 million), cash dividends (\$204 million), and debt retirement. With a \$2 billion share repurchase in place and the company guiding for \$12 billion of free cash flow between 2022 and 2027, EQT remains one of the best-positioned E&Ps.

EQT has recently sold off along with the temporary declines in gas prices. If you haven't bought shares of this company yet, it's a tremendous buy today.

EQT has proven to be a master of managing the commodity cycle, buying acreage cheap during bear markets (like its Chevron deal in 2020), and reaping a cash flow windfall during bull markets (like it did last year). Few other E&Ps have the discipline to act like true contrarians, and instead remain victims of the commodity cycle.

One of the challenges in the E&P business model comes in the form of heavy capital requirements. Drilling thousands of feet into the earth to tap oil and gas deposits is an expensive proposition. (We are reminded of the CIA's ill-fated claw operation.) And because each well begins depleting shortly after it's tapped, E&Ps are constantly on the capex treadmill.

During an inflationary environment, the cost of everything rises – including the inputs that go into drilling oil and gas wells. We're seeing this dynamic at work today, where rising energy prices have weighed down E&Ps with higher input costs.



Today, we're introducing a business model that offers the best of both worlds. This company provides upside exposure to higher energy prices, but without the heavy capital requirements associated with drilling holes thousands of feet into the earth.

Instead of drilling for oil and gas, this company owns the mineral rights to the land upon which other E&Ps drill their oil and gas wells. By owning mineral rights, this company is entitled to receive a percentage of the oil and gas produced from the wells drilled on its acreage.

The beauty of this royalty model is that it produces cash flows from oil and gas production, but without putting up any of the capital required to drill those wells.

These low capital requirements make energy royalties one of the most capital efficient businesses you'll find anywhere. [In September](#) 2022, we recommended an energy royalty company focused primarily on oil in the Permian basin. Today, we're doubling down on this business model, with an energy royalty company focused primarily on natural gas.

This company has a dominant acreage position in the heart of America's two fastest-growing gas basins. While other regions like the Eagle Ford have exhausted their core acreage, these basins are firing on all cylinders today. In each case, these basins barely suffered a hiccup during the COVID-19 meltdown in energy prices, and have since set new all-time production highs.

Best of all, the management of the company we're recommending today has a lot of skin in the game (insiders collectively own more than 25% of the business). They have proven to be world-class capital allocators, by establishing a leading acreage position in some of the most prolific gas basins in America. They manage the business like it's their own, using very little debt and pursuing a conservative hedging program that protects the downside.

Despite the recent collapse in gas prices to around \$2 per MMBtu, this company will be earning more than \$5 per MMBtu on the majority of their 2023 production, thanks to their proactive hedging program.

That's how, despite the recent collapse in U.S. gas prices, the company just announced an increase in its distribution, and now sports a juicy 12% yield.

## The Perfect Way to Play the Coming Natural Gas Supercycle

Black Stone Minerals (NYSE: **BSM**) is one of America's largest oil and gas mineral owners, with an asset base spanning 20 million gross acres across 41 U.S. states. The company has an estimated reserve base of 60 million BOE (barrels of oil equivalent), made up of 68% natural gas and 32% oil reserves.

Importantly, Black Stone is structured differently from standard equities. It's a master limited partnership (MLP), which means that an investor purchases "units" instead of shares, and receives "distributions" instead of dividends. Also, investors who buy MLPs are considered limited partners in the business. This unique business structure brings tax benefits, but also potential complications come tax time.

MLPs are considered "pass-through" entities, which means they pass through cash flows and tax liabilities to their limited partner investors. This is different from a regular corporation, which pays corporate taxes, and acts like a separate entity from the investor. The pass-through structure means MLPs avoid corporate taxes. Instead, the investors (as limited partners in the business), are responsible for their portion of the company's taxes.

So at tax time, investors receive a K-1 form instead of the more common 1099 form for stock dividends. While K-1s are more complicated than 1099s, most tax software programs are set up to process these forms in a matter of minutes these days.

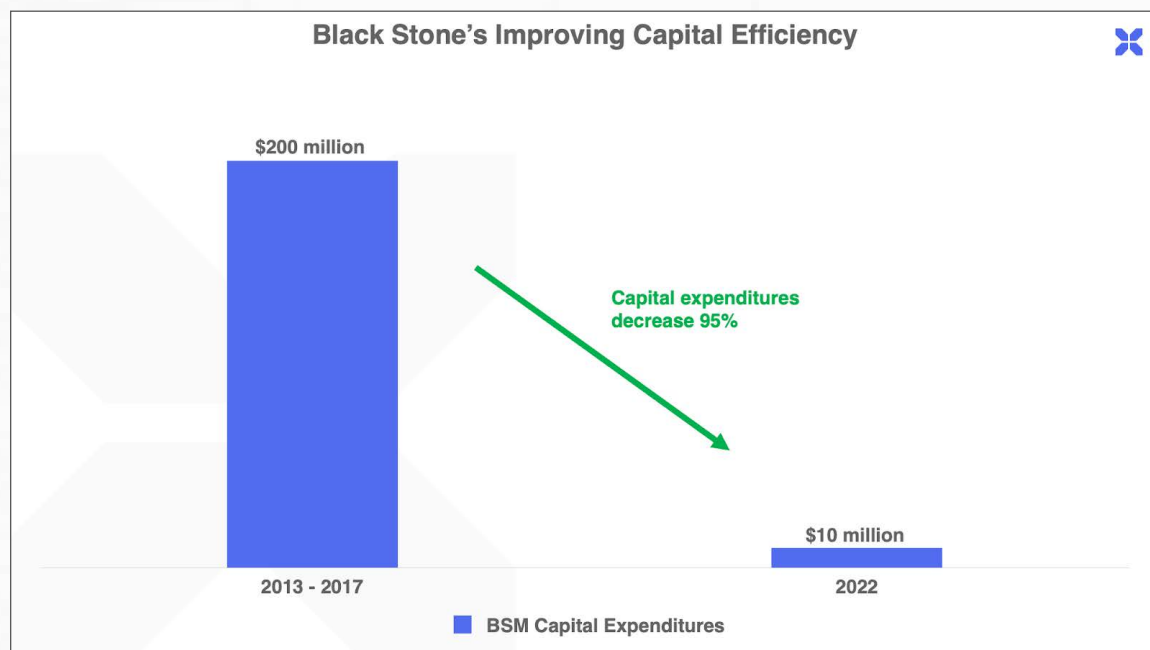
Historically, Black Stone focused on making two types of acreage acquisition deals: purchasing both royalty interests, and working interests.

The capital efficient royalty business model is compelling. As the owner of mineral royalties, Black Stone doesn't spend a dime of the capital expenditures associated with producing oil and gas. Instead, Black Stone receives a portion of the production from E&P companies that drill the oil and gas wells on the land it owns.

Working interests, on the other hand, are investments into wells that require payment for a proportion of the costs associated with drilling and operating those wells.

Starting in 2017, Black Stone began cutting its exposure to working interest acreage, transitioning towards a royalty pure play. Today, roughly 93% of Black Stone's acreage holdings are royalty interests versus just 7% for working interests.

This transition away from working interests has dramatically improved Black Stone's capital efficiency. In the five years from 2013 - 2017, the company averaged roughly \$200 million in annual capital expenditures. But over the last three years, Black Stone's capital expenditures have fallen to less than \$20 million on average, including \$12.6 million in 2022.



This shifting business model has boosted Black Stone's free cash flow margins from an average of 35% from 2013 - 2017 to 60% over the last three years. Likewise, Black Stone's return on equity has more than doubled from 17% in 2017 to an all-time high of 40% today.

Finally, another key measure of capital efficiency we analyze is the profitability per employee. A good company might earn a few hundred thousand dollars per employee, whereas world-class businesses might earn a million or more.

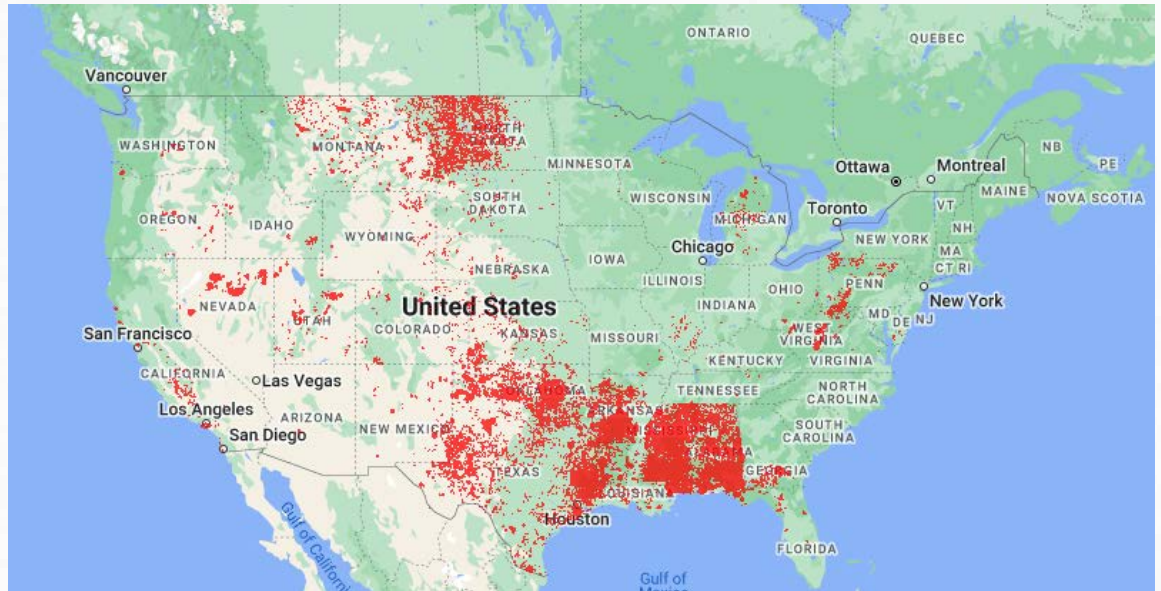
Black Stone has 93 full-time employees, plus 15 contractors, for a total of 108 workers. In 2022, the company earned \$391 million in net income, or nearly \$4 million in profit per employee. This makes Black Stone one of the most capital efficient businesses anywhere in the public markets.

Despite Black Stone's stellar economics, the company today trades at a discounted valuation of just 8x free cash flows – a roughly 50% discount versus 2017, before the company transformed into the beacon of capital efficiency that it is today.

The secret to Black Stone's strong financial performance is that its key acreage lies in the heart of America's two most prolific – and profitable – gas basins.

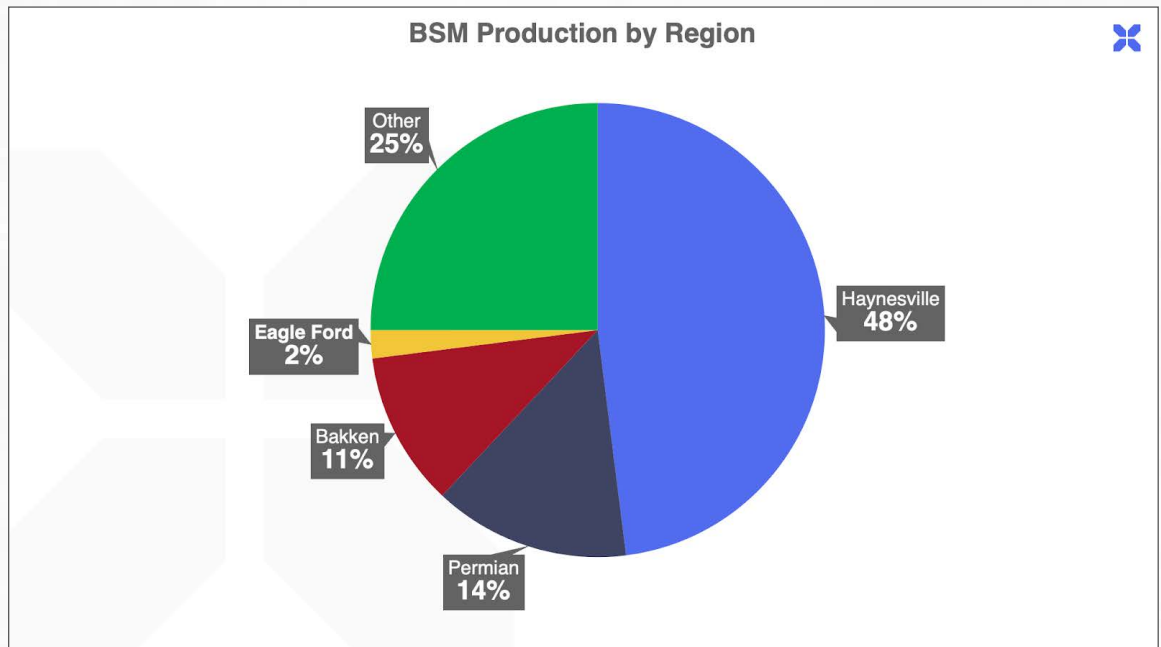
## Black Stone's Acreage Holdings

Black Stone's acreage spans across every major onshore U.S. oil and gas basin, but most of the land it controls is concentrated along the Gulf Coast region:



This puts Black Stone's key acreage in close proximity to America's booming LNG export infrastructure along the Texas and Louisiana Gulf Coast.

Approximately half of the company's royalty volumes come from the Haynesville shale formation, which stretches from east Texas and into Louisiana. The company's next biggest basin exposure is in the mid-continent/Delaware basin, which includes the Permian basin in West Texas and New Mexico, followed by a minority of exposure in the Bakken, Eagle Ford and smaller basins along the Gulf Coast.



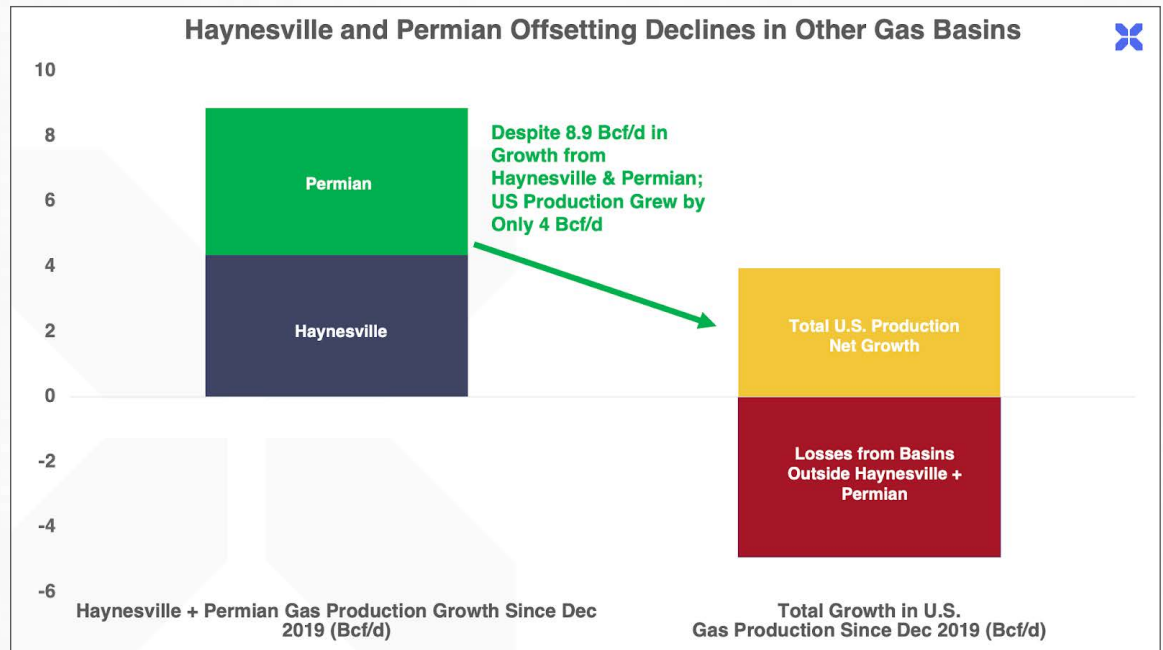
Together, the Haynesville and Permian make up nearly two-thirds of Black Stone’s production volumes. This positions Black Stone squarely in the heart of America’s two key natural gas production powerhouses.

Oil production generates a lucrative byproduct: natural gas. And the Permian, America’s leading oil producer, naturally leads the pack in gas, with output increasing by 4.5 Bcf/d over the past three years.

The Haynesville is a close second behind the Permian, which has grown gas production by 4.4 Bcf/d over the past three years. The Haynesville shale hosts the second largest source of gas reserves in America, behind the Appalachian shale. But unlike Appalachia, where growth is constrained by lack of pipelines, the Haynesville feeds an expanding suite of LNG export terminals along the Gulf Coast.

Many of America’s gas basins are past their peak production. In contrast, the robust growth in the Haynesville and Permian shales offsets declines elsewhere across the U.S.

In fact, the combined growth in these two basins has exceeded total U.S. production growth over the last three years:



Black Stone’s concentrated exposure in these two dominant U.S. gas basins makes it the perfect company to play the coming natural gas supercycle. And it’s already firing on all cylinders today...



## The Cutting Hedge

In 2022, Black Stone set new records in and operating results, ending the year with royalty volumes of 40 million barrels of oil-equivalent per day (BOE/d) – a new record high. The company also generated a record \$486 million in net income, up 60% from the previous record high of \$302 million in 2021.

Black Stone attributed most of this volume growth to rising drilling activity in the Haynesville and Permian. The number of active drilling rigs across its acreage jumped by 14% from 90 in 2021 to 108 in 2022. This is a trend we expect to continue, as the Permian and Haynesville remain the two fastest growing oil and gas basins in America.

Thanks to Black Stone's capital efficiency, the business returns capital to investors, instead of sinking it back into the earth. In 2022, Black Stone paid out total distributions of \$1.75 per unit, an 85% increase from 2021.

Black Stone currently pays out \$1.9 in annual distributions, or a nearly 12% yield.

How will Black Stone manage to support this 85% increase in its distribution in 2023, even despite the collapse in gas prices?

The answer lies with the company's conservative management team, who hedged Black Stone's 2023 price exposure during last year's rally in prices. As shown in the table below, the company locked in gas prices of between \$5.07 - \$5.15 for every quarter of 2023, for approximately 70% of its gas production:

Quarter	Volume (MMBtu)	Weighted Average Price (MMBtu)
1Q 2023	9,000,000	\$5.07
2Q 2023	8,190,000	\$5.15
3Q 2023	8,280,000	\$5.15
4Q 2023	8,280,000	\$5.15

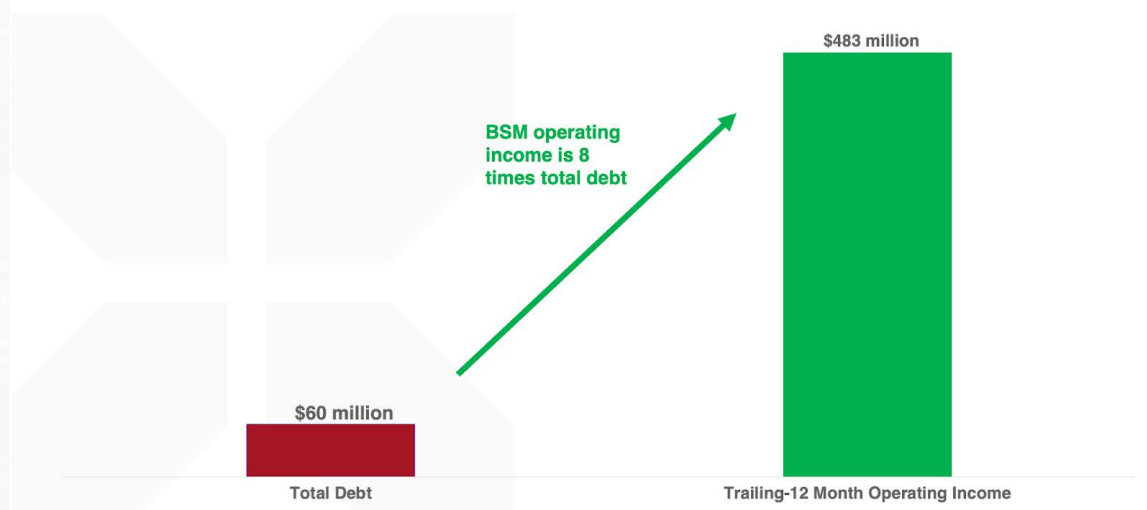
Black Stone's hedging program limited its upside in 2022, as the company locked in prices of around \$3 per MMBtu. As such, the company failed to reap the windfall that unhedged gas producers earned from last year's price rally.

But the purpose of hedging is to provide insurance against bear markets, even if that means paying a price (i.e., surrendering some upside) during bull markets. Today, the tables have turned. Any gas producers not sufficiently hedged are now suffering in today's bear market, while Black Stone's hedging program pays off in a big way.

And therein lies the final key piece of this story. *Black Stone is run and managed by owners with skin in the game.* Insiders own more than 25% of the company. They're not interested in putting the business at risk in order to chase every last penny of short-term upside. With millions of dollars of their own personal wealth at stake, they're focused on protecting the business above all else.

We can see further evidence of management's conservative approach to capital allocation through the balance sheet. Black Stone has just \$60 million in total debt versus operating income of \$483 million over the last 12 months. With a net leverage ratio of just 0.13x, Black Stone has a pristine balance sheet.

#### Black Stone's Conservative Balance Sheet



Looking ahead, Black Stone is positioned to thrive even in today's depressed pricing environment. With roughly 70% of its gas production volumes hedged at over \$5 per MMBtu for 2023, the company will likely continue reporting record operating results this year. Then, as the natural gas supercycle kicks into high gear with booming LNG export demand in 2024 and beyond, Black Stone could reap a true windfall from both higher production and higher prices.

In the meantime, investors get paid a 12% dividend to wait, supported by a growing earnings profile and a robust balance sheet.

We're not the only ones who see a bright future for the company. Recently, Black Stone's CEO Thomas Carter has purchased over three million of the company's units in the open market, at prices ranging from \$16.85 to \$19.46.

**Action to Take:** For the latest updates on our open positions, please visit our live portfolio [here](#).



A handwritten signature in black ink that reads "Porter Stansberry".

Porter & Co.

Stevenson, MD

P.S. If you'd like to learn more about the Porter & Co. team – all of whom are real humans, and many of whom have Twitter accounts – you can get acquainted with us [here](#). You can reach me (Porter) personally via:



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