Midstream: in our 2022 preview 6 months ago, we laid out a (conservative) case that midstream money flows were almost guaranteed to improve in 2022. Balance sheet repair and resilient cash flows meant an unprecedented free cash flow (FCF) harvest could be directed towards buybacks (even after dividend growth). Meanwhile, selling by dedicated midstream funds and ETFs peaked in 2020, subsiding by late 2021. Sure enough, with 4 months of 2022 in the books, buybacks are trending to the high end of our $3bn to 5bn range, and we estimate net fund flows are *positive* YTD. The result has been midstream sector performance reminiscent of the "uncorrelated" outperformance of the 2000s.

Natural Resources: Historic correlations have long suggested that inflationary environments benefit natural resources companies; in Q1 2022 we have significant data corroborating the relationship. Of the companies reporting earnings through May 7th, 2022, Energy and Materials exceeded earnings expectations more than any other global sector. More specifically, natural resources' earnings "beats" approximated 2% of market capitalization! Importantly, with strong balance sheets and capital discipline, more and more cash is being returned to shareholders.

Access Recurrent's new White Paper on the rising "risk premium" in the oil market
Access Recurrent's latest video on the impact of Russia's invasion

MLP & Infrastructure

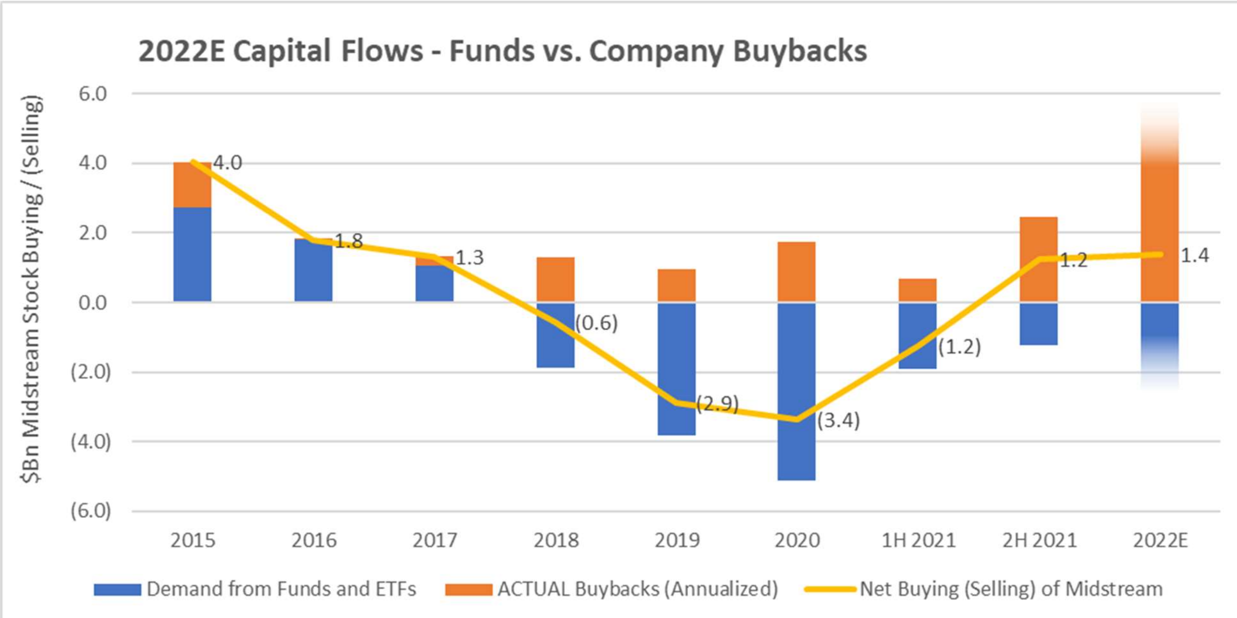
Performance review

During the month of April 2022, the Recurrent MLP & Infrastructure Strategy generated net returns of +1.48%, outpacing the -0.09% gross return of the Alerian MLP Index (AMZ) by +1.57%. Since the strategy's July 2017 inception, Recurrent's MLP & Infrastructure Strategy has outperformed the AMZ by +5.77% (annualized, net of fees). Please see the performance section at bottom for more detail.

Back in December, we forecasted an inflection in midstream money flows… YTD has been better than our projections

Given the massive FCF wedge for midstream companies, driven by rising cash flow and flat or falling capital expenditure budgets, we have spent time over the last 24 months forecasting a significant inflection in actual cash returns from midstream companies to investors, in the form of dividends and buybacks. Midstream equities have always offered meaningful yield, and sure enough, we've seen the dividend growth rate accelerate since we highlighted this trend last year. Buybacks, however, are a relatively new tool for midstream companies, arguably better-suited to address the midstream sector's discounted valuations since 2020.

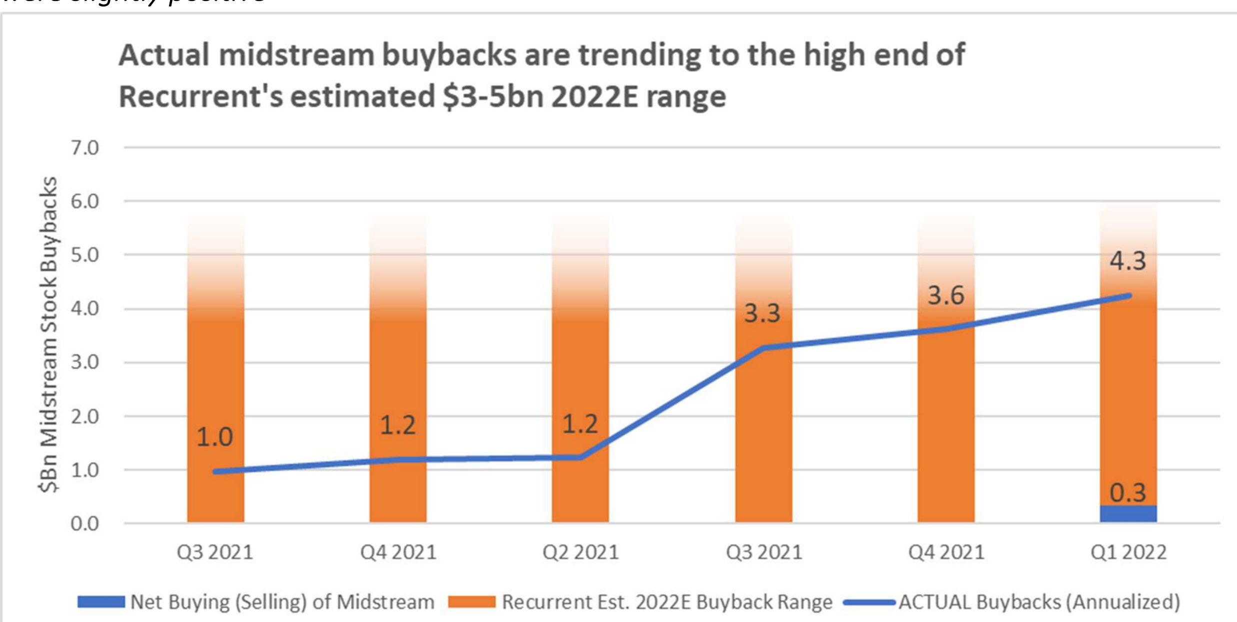
Exhibit 1: our Dec 2021 forecast saw up to $5bn of 2022E buybacks and better money flow for mutual funds/ETFs



Source: Recurrent research, Bloomberg data

As shown below in Exhibit 2, with Q1 results in the books, the pace buybacks is trending towards the high end of our $3bn to $5bn expectation. Meanwhile, fund flows were modestly positive at $340mm through April 30, 2022.

Exhibit 2: In Q1, midstream completed >$1.1bn of buybacks ($4.3bn annualized)… Q1 fund flows were slightly positive



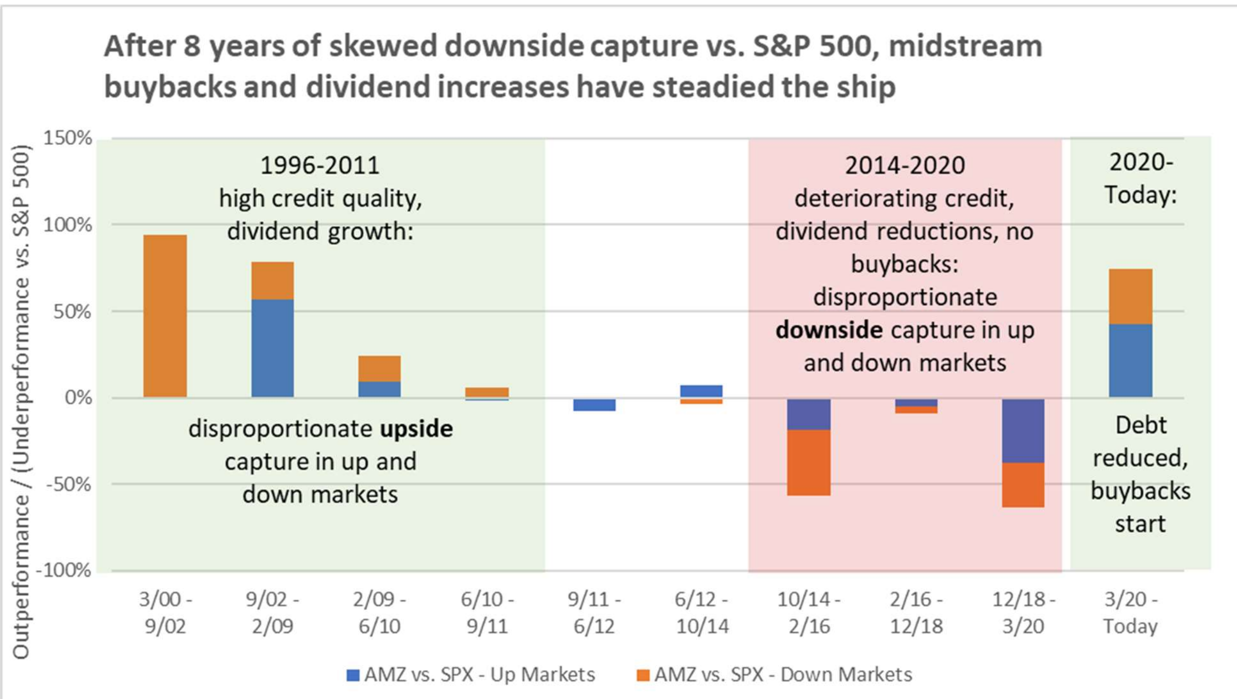
Source: Recurrent research, Bloomberg data

We return to a question from [December 2021]() – do buybacks even matter? It's getting harder to say no

While academic debates have raged for years about the efficacy of buybacks. Certainly, there is an argument to be made that cyclical sectors like energy are especially at risk of falling into the "buyback trap" - buying stock at high valuations, when flush with cash, and being forced to issue capital at low valuations, when the earnings cycle is nearing a bottom.

A definitive answer is impossible, but today, **midstream (and energy) buybacks are almost certainly working.** As shown below in Exhibit 3, upside capture and downside protection (measured as AMZ vs. S&P 500 performance) has improved dramatically as balance sheet repair has been completed and shifted to buybacks (and dividend increases).

Exhibit 3: buybacks are at least one explanation for the return of uncorrelated midstream outperformance



Source: Recurrent research, Bloomberg data

The argument against buybacks is also undercut by the uniqueness of today's market: ESG concerns and negative sentiment have kept valuations below midcycle levels even as profitability is rapidly approaching all-time highs, so there is an opportunity for companies to buy ostensibly cheap stock despite record cash flow. For the last several years, the midstream energy investor base has shrunk – and today, buybacks are filling the void left by these departing investors. Until we see a meaningful expansion of the energy investor base reflected in net money flows, we say to midstream companies, buyback away!

Natural Resources

Performance Review

In the month of April 2022, the Alma Recurrent Global Natural Resources Fund fell by -3.75% net of fees, outpacing the S&P Global Natural Resources Index's -4.38% return. Stock selection in the integrated oil sector significantly added to portfolio performance, with Cenovus Energy and Suncor Energy rising 11.38% and 10.28%, respectively. Alcoa Corp detracted from performance, falling -24.69% in the month, as the implications of COVID on Chinese demand raised short term concerns.

Investment Discussion

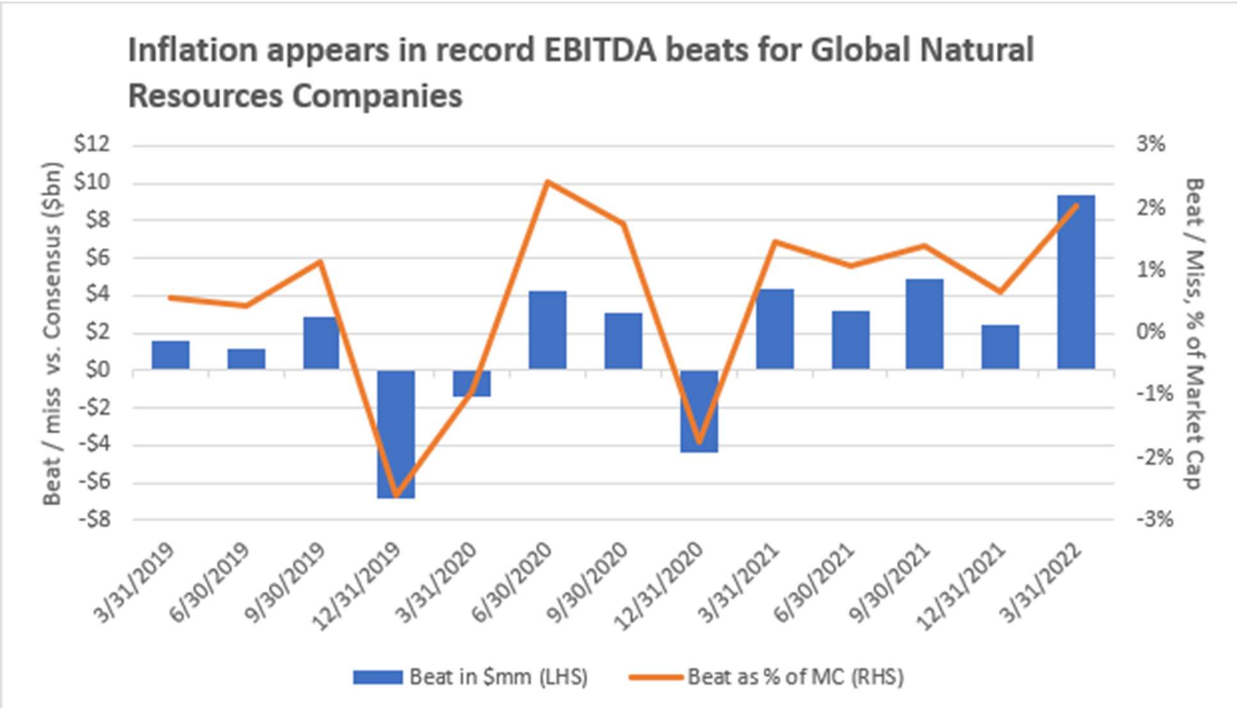
As the month of April came to a close, 1Q earnings offered the first indications of the impact of inflation on company earnings. As 2022 started, global inflation started to increase, with many developed markets exceeding 5% Year-over-Year (YoY) CPI growth. In February, Russia's invasion of Ukraine further disrupted supply chains and escalated inflationary pressures; by the end of the first calendar quarter YoY CPI accelerated to 7% as measured in the Bloomberg World Economic Inflation Measure (WOININFL).

With inflation reaching multi-decade highs, the question of company earnings comes into focus. From an earnings surprise perspective, natural resources companies are generally beneficiaries of increased commodity prices. Through May 7th, the results are strongly confirming the perspective that energy and materials companies are positively correlated to inflationary environments. In the chart below, we look at the dispersion of 1Q earnings surprises across the Vanguard Total World Stock ETF's sectors. With more than 50% of companies having reported, energy and materials stocks show the strongest earnings surprises, while in aggregate global financials, consumer staples and utilities sectors missed earnings 1Q estimates.

Source: Bloomberg, Recurrent Research

1Q 2022's earnings surprises were the largest in years, and relative to market cap were equally as large during the depths of COVID, with one major difference for shareholders today…

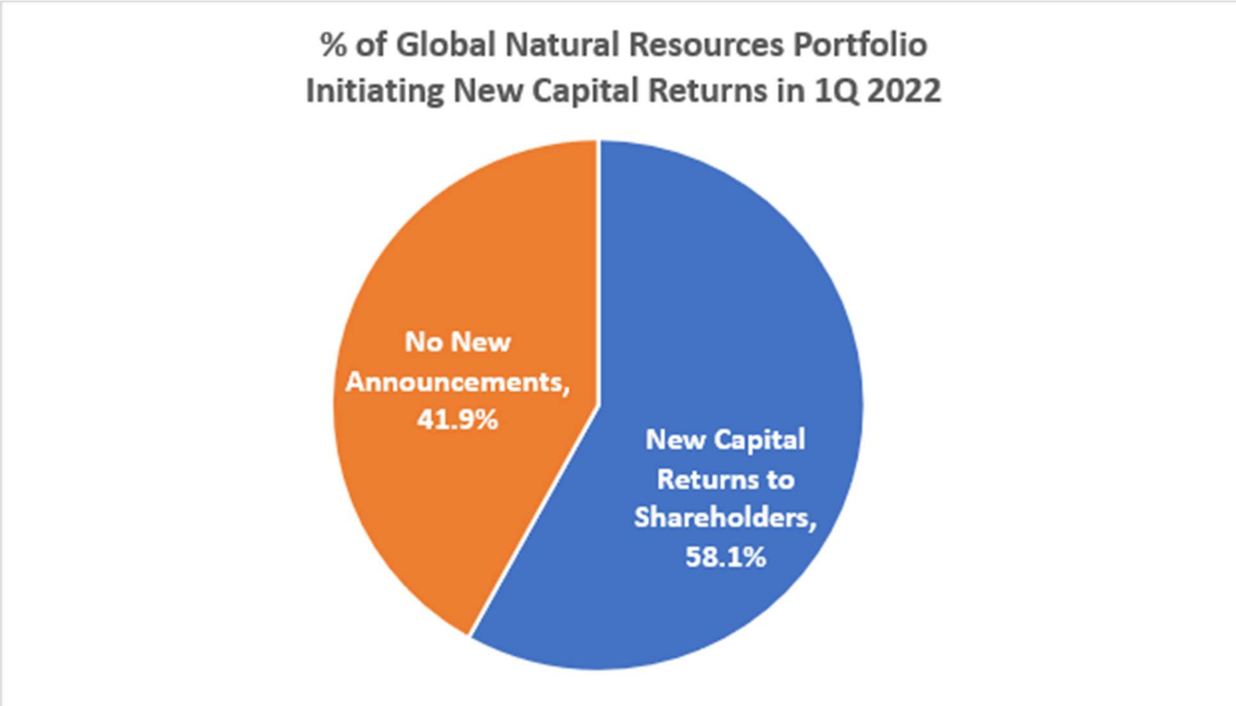
Earnings for bellwether natural resources companies beat expectations by significantly more than any time in the last few years. Additionally, the right axis shows the percent of market capitalization represented by the earnings beats. Only in the immediate aftermath of COVID, when earnings estimates initially plummeted as COVID spread, did companies beat earnings estimates by as much, when measured as a percent of market cap.



Source: Bloomberg, Recurrent Research

Capital discipline has led to healthy balance sheets; companies are returning capital to shareholders

In the middle of 2020, companies' earnings beat overly pessimistic sell side expectations. However, because companies were dealing with significant operational uncertainty, any excess earnings were used to pay down debt, and were not available to equity holders. Today the situation is notably different than the depths of COVID, where profitability is high and debt levels have been reduced. Importantly, due to continued capital discipline, an increasing amount of free cash flow is being returned to shareholders. In just the 1Q earnings period, portfolio companies accounting for approximately **58%** of the Global Natural Resources portfolio have announced new share buybacks or dividend increases.



Source: Bloomberg, Recurrent Research

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