Midstream: Over the last 8 years, as midstream companies pivoted from dividend maximization to a total return strategy based on lower payouts and debt reduction, they have also moved away from the MLP structure, opting instead for the greater allocation flexibility, tax deductions, and larger investor base available to C-corporations. This trend accelerated in May, when OneOK (a C-corp) unveiled plans to buy Magellan (an MLP) for a modest premium, shortly after PSX-DCP announced a similar low-premium, tax-inefficient MLP buyout. In the case of OKE-MMP, we view the goal as being a transfer of a large tax bill from OKE to MMP shareholders. Ironically, investors misread the deal's implications, and bid up small-cap MLPs in May, despite the risk of tax-inefficient M&A. As we review below, we believe our approach – looking for capex-efficient, high-return businesses, mainly in flexible corp structures – offers more attractive exposure than a SMID-cap pure MLP portfolio, despite MLPs' recent outperformance.

Natural Resources: With its recent announcement to acquire PDC Energy, Chevron highlighted the desirability of high-cost but quick to turn on/off US Shale production. As we highlighted in our 2022 white paper, "The Twilight of the Energy Transition Becomes a New Dawn for Shale," concerns around the energy transition have increased costs of capital for energy companies. Accordingly, quick paybacks now matter more than low costs per barrel. Based on cost alone, it is difficult to understand why Chevron would dilute its low-cost assets with PDC's high-cost assets. However, PDC assets provides CVX with the ability to flex capex lower today and higher in the future, instead of sinking capital in long-duration megaprojects.

Click here for the latest white paper on the long-term relationship between inflation and capex
Click here for our 2022 white paper on Shale's increased strategic importance in a time of ESG
(noteworthy in light of CVX-PDC deal)

May 2023 Performance Summary and Market Commentaries

Please find below performance and commentary for our strategies – MLP & Infrastructure and Natural Resources. Performance follows at the bottom of the commentary. For additional information, please contact us at (832) 241-6400 or info@recurrentadvisors.com.

MLP & Infrastructure

Performance review

During the month of May 2023, the Recurrent MLP & Infrastructure Strategy generated net returns of -4.76%, lagging the Alerian MLP Index's (AMZ) -0.52% return by -4.25%. The primary cause of this relative underperformance was the OKE-MMP merger announcement and the subsequent strong outperformance of MLP-structured midstream companies vs. corp-structured companies. This continues a trend kicked off by the PSX-DCP announcement from late 2022. We expect that this small-cap MLP outperformance will normalize in the coming months for the reasons we discuss below. Since the strategy's July 2017 inception, Recurrent's MLP & Infrastructure Strategy has outperformed the AMZ by +2.56% (annualized, net of fees). Please see the performance section at bottom for more detail.

Our goal: building a midstream portfolio to maximize FCF via capex discipline – regardless of C-corp or MLP structure

While we believe the noteworthy MLP outperformance seen in recent months was the result of M&A-related factors, we occasionally review portfolio fundamentals to gauge our underlying investment thesis, and to compare with an "MLP only" portfolio as well as other energy subsectors. We have written extensively how the key driver of midstream FCF generation is capex discipline – midstream assets can be highly capital efficient once brought into operation. It is part of our job as portfolio managers to make sure that the *potential* for capital discipline is actually delivered by management teams, and that restrained capex allows for maximum FCF generation and cash returns to shareholders.

Below, we pose 3 questions and examine the evidence for each plank of our investment thesis:

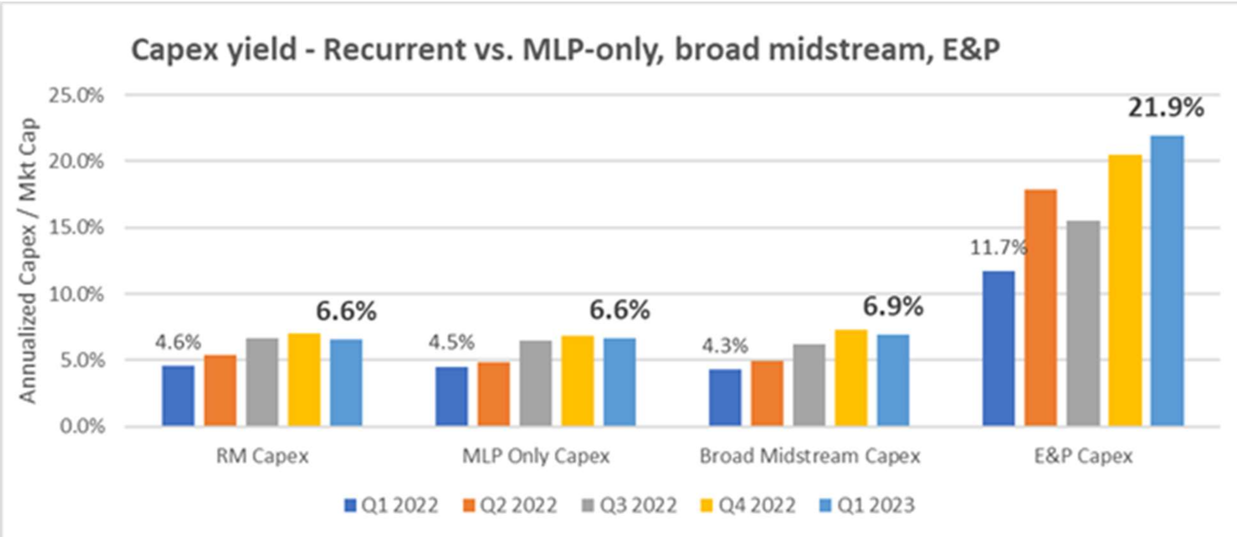
- **Thesis 1:** A key advantage of midstream is that capex can be restrained through a commodity cycle without adversely impacting companies' long-term cash flow generation.
  - **Question 1:** Is the Recurrent Midstream (RM) portfolio exhibiting capex discipline?
- **Thesis 2:** The best businesses continue to generate high levels of free cash flow (FCF) even as capex remains restrained.
  - **Question 2:** Are the businesses in the RM portfolio able to grow free cash flow over time even as capex remains low?
- **Thesis 3:** Businesses with durable FCF should be able to return significant and stable amounts of cash flow back to investors.
  - **Question 3:** Is the RM portfolio FCF translating into meaningful and recurring cash returns to shareholders?

5 quarters into a commodity inflation cycle, we examine how the Recurrent Midstream (RM) portfolio stacks up against an "MLP only" portfolio, a "Broad Midstream" portfolio with Corps and MLPs, and an upstream shale-dominated "E&P" portfolio?

Testing our first thesis – how does our portfolio's capacity for capex discipline compare?

When we measure the last 5 quarters, we can see that the RM portfolio has demonstrated comparable capex discipline compared to a pure MLP portfolio ("MLP Only"), and slightly better than the broad midstream sector ("Midstream" = Corps and MLPs). By comparison, our avoidance of short-duration Shale assets (and our underweighting of associated midstream gathering and processing businesses) is justified by Shale's inflationary capex, which is currently consuming nearly 22% of E&P market cap on an annualized basis.

Exhibit 1: RM portfolio capex is in-line with MLPs, slightly better than broad midstream, and much better than the E&P universe



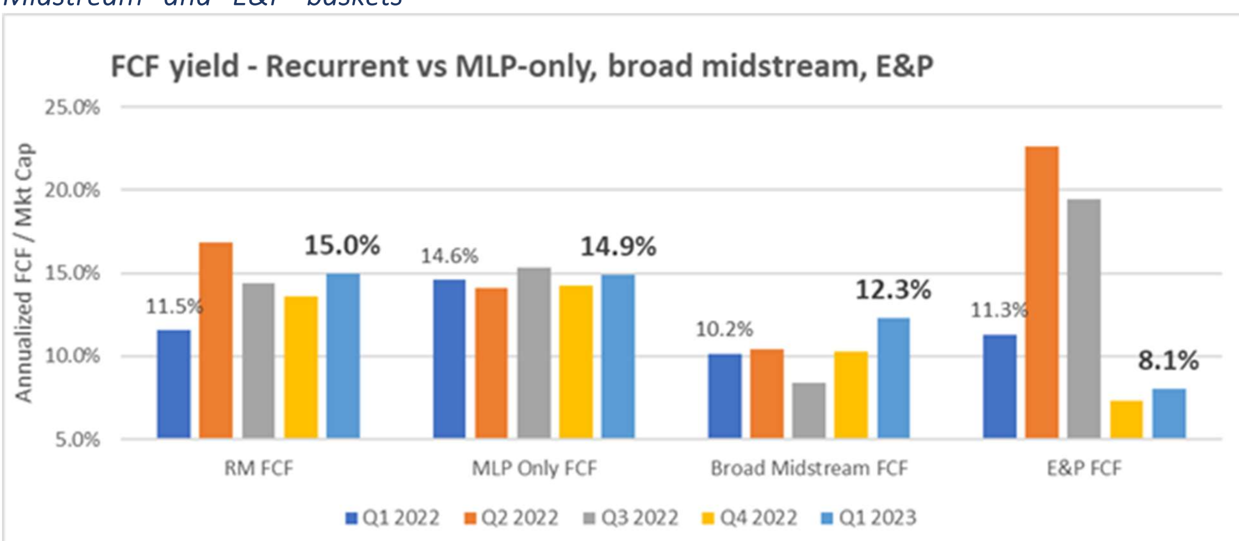
Note: RM = Recurrent Midstream. MLP Only = Alerian MLP Index. C-corp+MLP Mid= Alerian Midstream Energy Index. E&P = S&P Oil & Gas E&P Select Index.
*Capex yield = most recent capital expenditures * 4 / market cap. Market cap is measured as of 5/31/23, 2/28/23, 11/30/22, 8/31/22, 5/31/22.*
Source: Recurrent research, SEC filings, Bloomberg

Second thesis: Is capex restraint driving a higher FCF yield, and superior FCF growth over time?

While inflation has cooled in the broad economy, inflationary pressures remain high in the oil and gas sector. We have prioritized companies whose cost inflation can be effectively controlled (primarily due to longer asset lives and lower reinvestment rates) even as broader oil industry inflation is multiples higher than CPI.

By controlling capex inflation in our portfolio, we have maintained a FCF yield that is not only superior to a basket of MLP-only investments and broader midstream, but is now significantly higher than E&Ps, as E&P FCF has faded due to out-of-control capex.

Exhibit 2: Recurrent Midstream (RM) portfolio FCF has grown faster YoY vs. "MLP-only", "broad Midstream" and "E&P" baskets



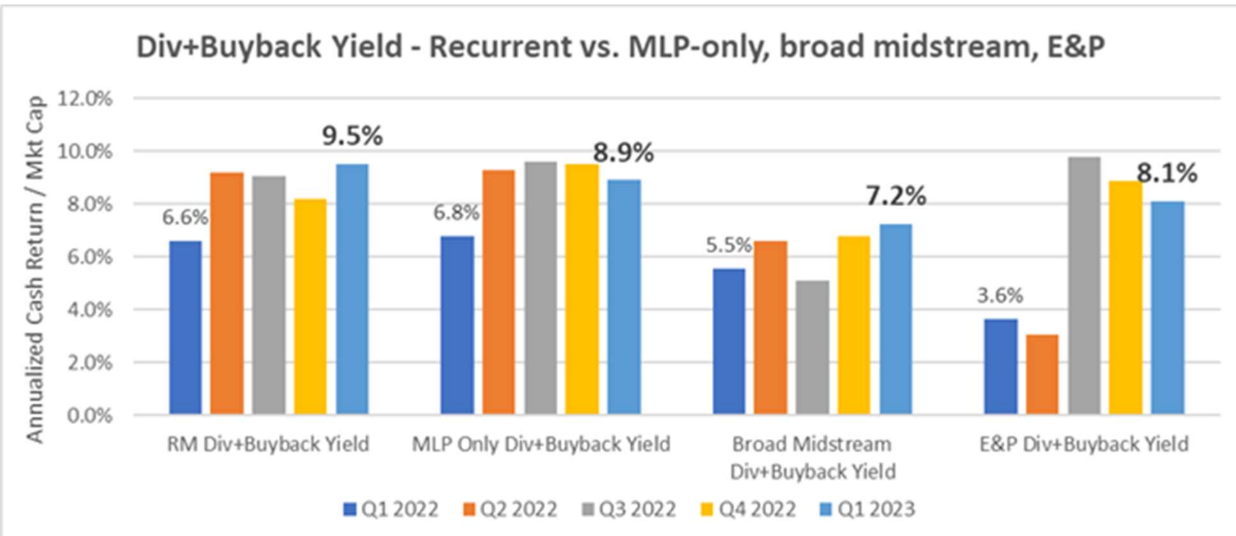
Note: RM = Recurrent Midstream. MLP Only = Alerian MLP Index. Midstream = Alerian Midstream Energy Index. E&P = S&P Oil &

Gas E&P Select Index.
*FCF yield = (most recent cash flow from ops less capital expenditures) * 4 / market cap. Market cap is measured as of 5/31/23, 2/28/23, 11/30/22, 8/31/22, 5/31/22.*
Source: Recurrent research, SEC filings, Bloomberg

Third thesis: is superior FCF translating into cash returns to shareholders? Largely, yes

With a 15% FCF yield based on Q1 results, the RM portfolio has had ample cash flow to generate a meaningful cash return to shareholders. In Q1, the annualized cash return of the RM portfolio was nearly 10%, exceeding the MLP-only universe, broader midstream, and E&Ps. The 9.5% total cash return for RM represents roughly 60% of the total 15.0% FCF yield, while payout ratios across "Broad Midstream" and "E&P" are significantly higher than the RM portfolio.

Exhibit 3: Recurrent Midstream (RM) portfolio FCF has translated into a robust and stable cash return



Note: RM = Recurrent Midstream. MLP Only = Alerian MLP Index. Midstream = Alerian Midstream Energy Index. E&P = S&P Oil & Gas E&P Select Index.
*Div+Buyback yield = (dividends + buybacks) * 4 / market cap. Market cap is measured as of 5/31/23, 2/28/23, 11/30/22, 8/31/22, 5/31/22.*
Source: Recurrent research, SEC filings, Bloomberg

A final thought: one area where our portfolio lags is dividend payout ratio as a % of FCF… potential for future dividend growth

While we continue to believe that the Recurrent Midstream portfolio offers a compelling mix of FCF generation, capex discipline, and shareholder cash returns, we would note that there is one area where it sits below peers: dividend payout ratio. While a conservative dividend payout is not a bad thing, we would note that Q1 2023 has seen broadly lower commodity prices than a year ago, and yet the RM portfolio has continued to grow FCF. In Q1, RM dividend payout was below 42%, compared to MLP and Broad Midstream payout ratios which are closer to 50% or 55%. This could leave the RM portfolio with more potential to hike dividends in 2023 and 2024 compared to comparable MLP-only or even diversified midstream-only portfolios.

Natural Resources

Performance Review

In the month of May 2023, the Alma Recurrent Global Natural Resources Fund fell by -9.62% net of fees, slightly more than the S&P Global Natural Resources Index's -9.48% return. During the month, portfolio holdings in the Paper Products industry performed well, remaining flat while broader markets fell. Heavily cyclical sectors such as Aluminum and Fertilizer & Agricultural Chemicals fell more than the benchmark, and detracted from relative portfolio performance.

Investment Discussion: The prospect of oil obsolescence is changing how companies make capital allocation decisions

In our 1Q 2022 white paper titled "The Twilight of the Energy Transition Becomes a New Dawn for Shale", we outlined how concerns about oil obsolescence were changing corporations' key decision variables for capital allocation. Historically, when companies assumed oil demand would only grow, oil companies prioritized cost over speed, using low discount rates that justified low-cost megaprojects, even if those projects took years (or decades) to materialize.

However, with growing concerns over the potential for long-term oil obsolescence, an additional decision variable needed to be included in corporate decision-making processes – time. With time as an added decision variable, the "low cost" mindset must change to a returns-based framework, in which both profits and time combine to determine capital allocation. In a "low cost" framework, the highest cost supply – i.e. US shale – struggles to attract capital. However, in a returns-based environment, shale's quick-to-market attributes proves very competitive on a global scale.

From low-cost barrels to project returns

In the last five years, the evolution of thought has been identifiable from public corporate presentations. Below is the first page of the corporate overview from Chevron's 2019 analyst day presentation. Note that the asset portfolio is identified as "low breakeven", highlighting the low cost per barrel nature of the upstream segment. Traditionally, supermajors such as Chevron, ExxonMobil, Shell, BP and Total amass a portfolio of large-scale oil and gas resources, and bring their capital and engineering resources to bear over multi decade time horizons, to generate low costs per barrel, in search of favorable returns.

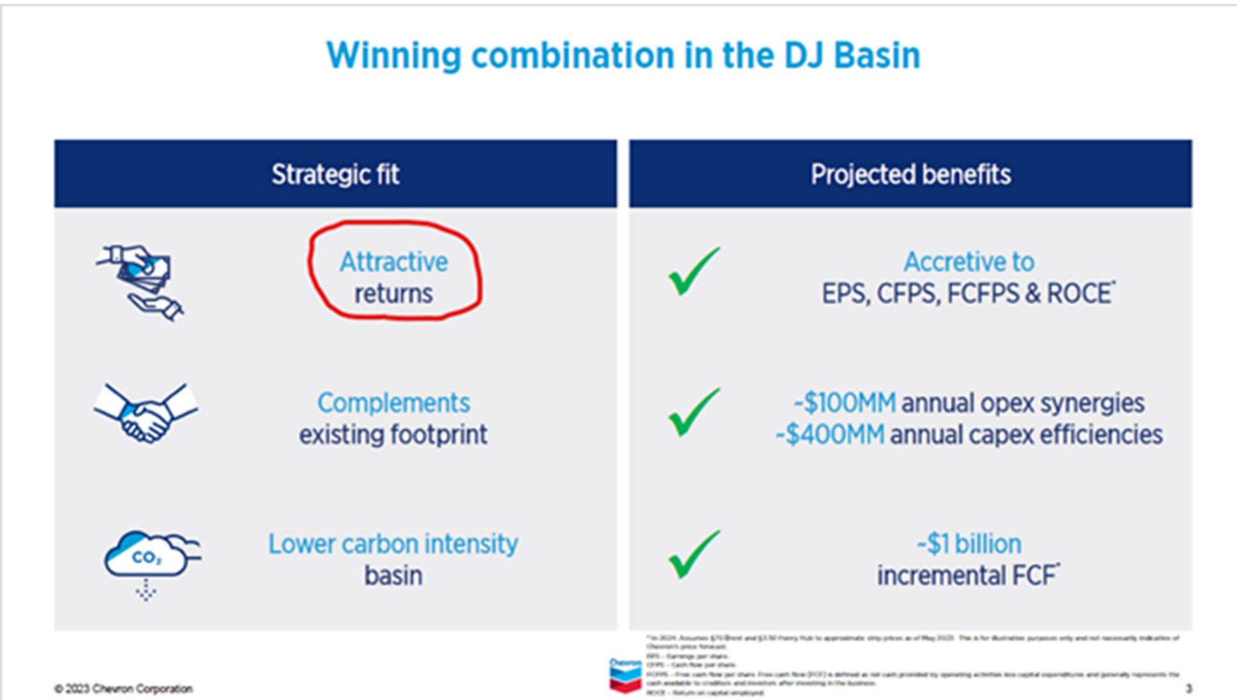
Source: Chevron Investor Presentation, 2019

Interestingly, just 4 years later, the points of emphasis have changed markedly. The 2023 Analyst Day slides are simply titled “Higher Returns”, without a single reference to the upstream portfolio’s cost per barrel.

Source: Chevron Investor Presentation, 2023

Chevron-PDC deal only makes sense in a world where returns are more important than cost

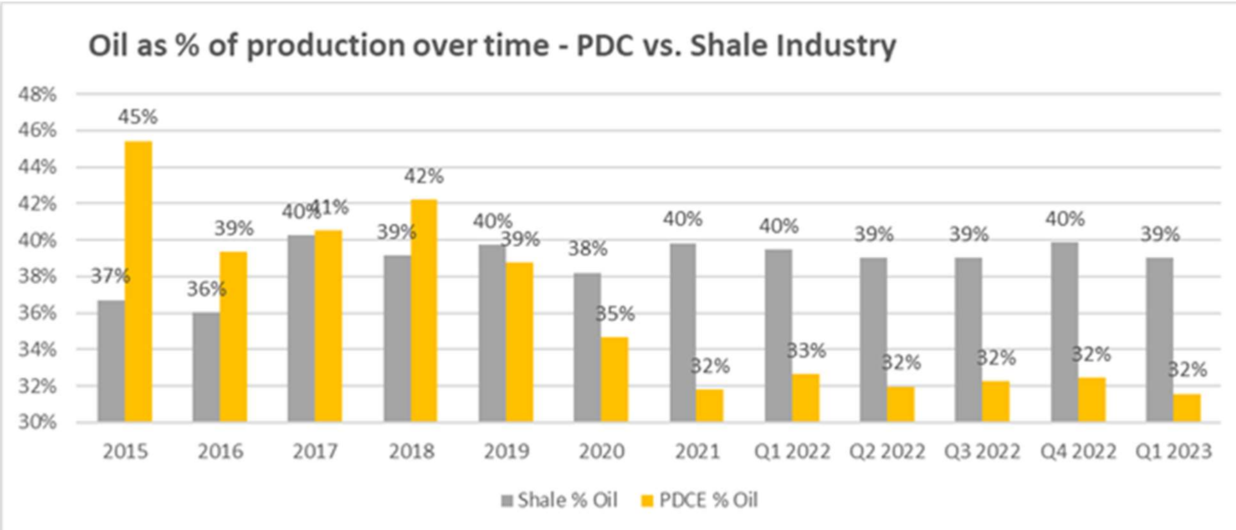
Furthermore, in May 2023, Chevron announced plans to acquire PDC Energy (PDCE), a DJ Basin (Rocky Mountains) and Permian Basin oil and gas producer. Strategically, the acquisition confirms the value of high-cost/short-duration US shale production within the many options of global oil and gas production. In the associated analyst presentation, the first slide highlights the potential for "attractive returns", with no mention of costs per barrel.



Source: Chevron Investor Presentation, 2023

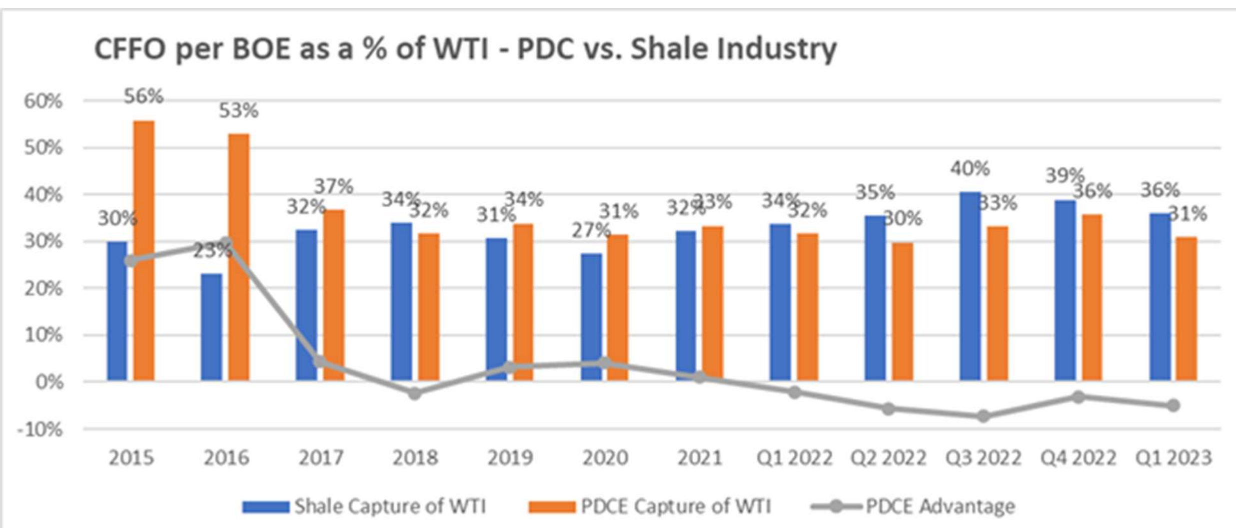
Even as company specific finances are facing shorter term headwinds due to lower percentages of oil production and cost/CAPEX inflation…

From a purely financial perspective, PDCE reflects many of attributes commonly referenced in shale producers. Since the mid-2010s, PDCE has seen oil as a % of production fall from nearly 50% in 2015 to approximately 33% today.



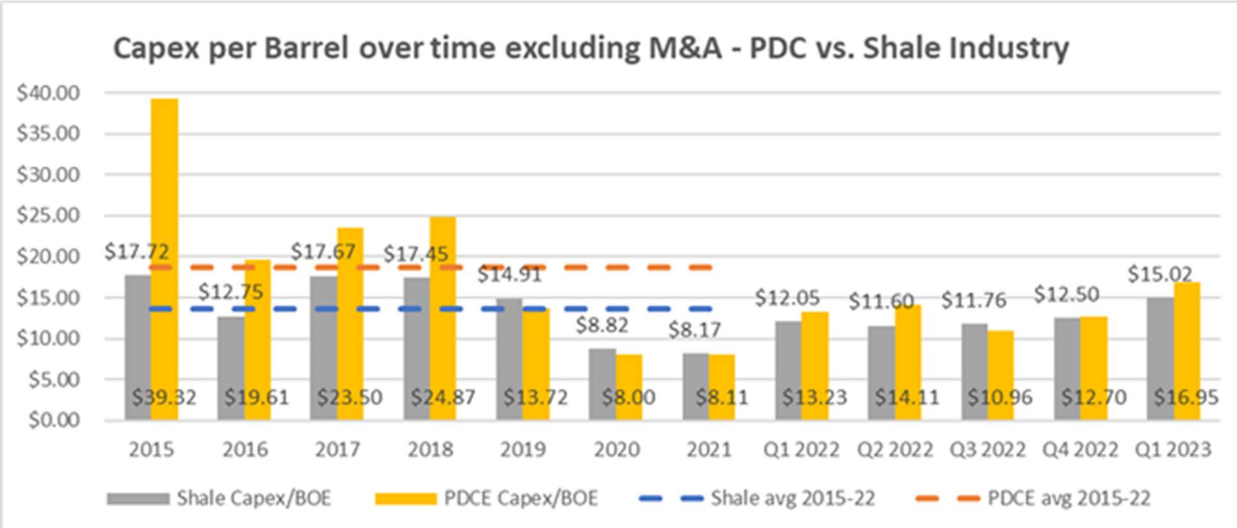
Source: SEC filings, Recurrent research, Bloomberg

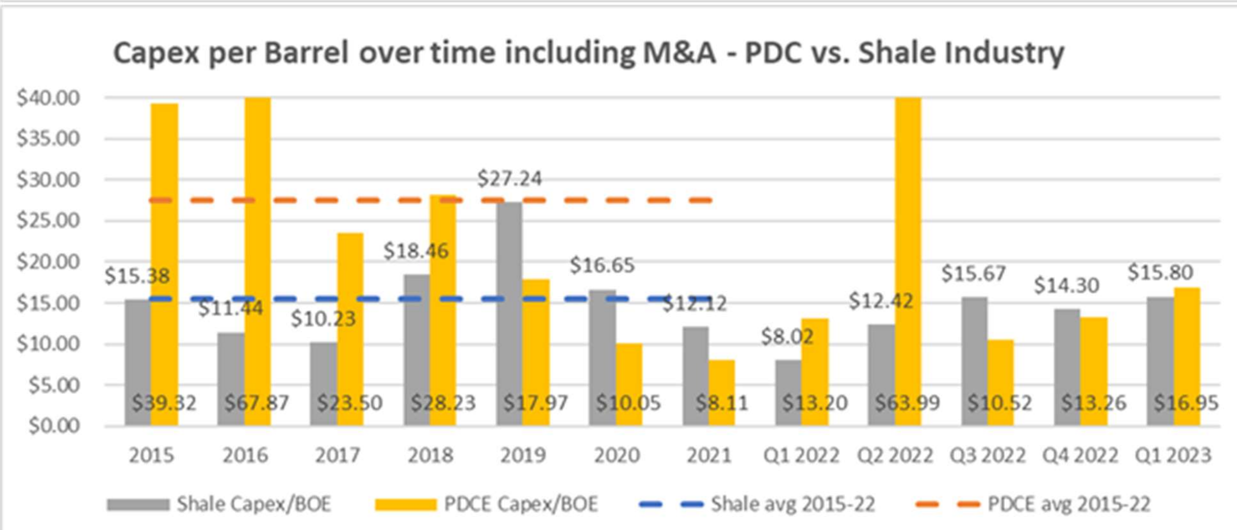
Since oil volumes are more valuable than natural gas volumes, even when normalized on a BTU-equivalent basis, the fall in revenues per barrel-equivalent (BOE) is material. Accordingly, PDCE's cash flows per BOE have realized smaller percentage of WTI crude price per barrel over time, and PDC has gone from capturing higher value per barrel in 2015-2021 to capturing less than the Shale industry average since 2021.



Source: SEC filings, Recurrent research, Bloomberg

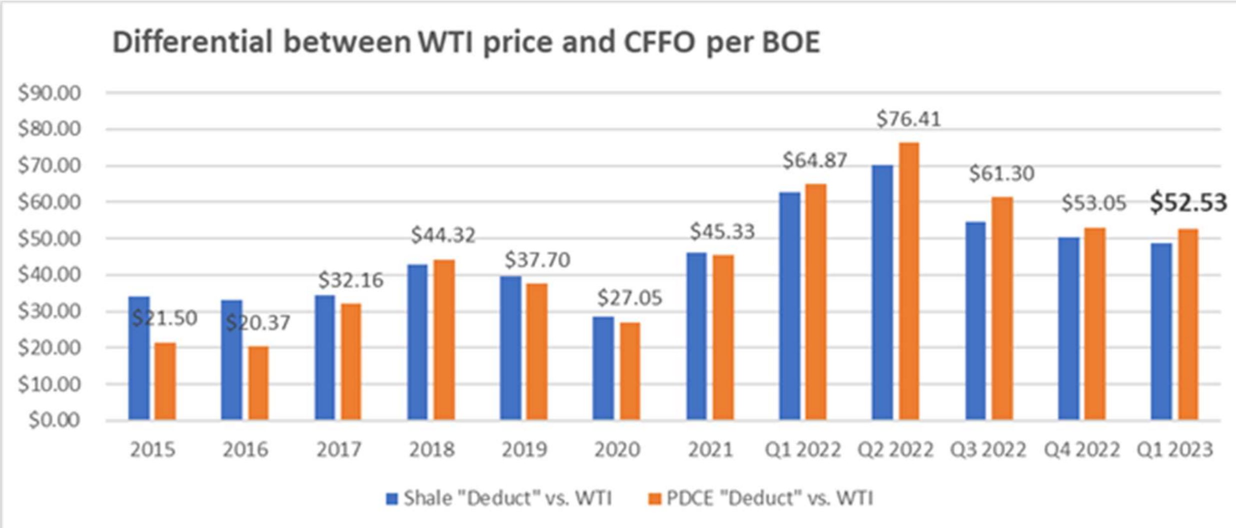
Lastly, even as commodity prices have fallen over the last 12 months, PDCE's CAPEX inflation has continued to accelerate. From a $8.00/barrel low in 2020, CAPEX has risen to $16.95 by Q1 2023, despite production growth being relatively similar in both periods. Lastly, if M&A is included in CAPEX to account for new acreage acquisition, then the CAPEX costs per barrel rise further to $17/BOE in 1Q 2023. Notably, including M&A, the full capex+M&A per BOE has averaged $12/BOE higher vs. the Shale industry average.





Source: SEC filings, Recurrent research, Bloomberg

If, in Q1 2023, WTI was $76, PDC captured CFFO per BOE of $23.57 (only 31% of WTI, or $52.53/BOE less than WTI price), and capex was ~$17/BOE – then the impact of lower value production, operating costs, and capex costs total more than $69/BOE. In the context of cost based "dispatch curve", PDCE would rank toward the high end of shale peers, as well as the cost curve on a global basis, with inflation accelerating costs for PDCE more so than other US shale peers.



Source: SEC filings, Recurrent research, Bloomberg

With PDCE's relatively unfavorable profit and cash flow metrics, why would Chevron be interested in making an $8 billion enterprise value acquisition, more than 50% of Chevron's 2023 pre-merger total CAPEX expectations? Compared to global oil and gas production alternatives, PDCE's return profile has the potential to be much better than its cost structure would suggest due to the short "duration" of its production. In other words, when oil prices increase to well over $70, Chevron can accelerate PDC's production quickly and profitably. When oil prices are lower, Chevron can quickly pull back. Indeed, Chevron's acquisition announcement indicated that PDC capex would fall by 30% after the acquisition's close.

As we outlined in our 1Q 2022 white paper, Chevron traditionally focused on large global oil and natural gas resources where significant capital and engineering might reduce costs-per-barrel over decades. As the potential "end of the oil age" debate continues, rather than investing in lower-cost but long-duration projects, Chevron is increasing its investment in higher-cost but shorter-cycle opportunities.

One other element worth noting is the ownership structure of short cycle, high decline assets like US shale. As a public company with a narrowly defined portfolio of assets, PDCE had an undiversified asset base and was beholden to shareholders, which at times limited management's flexibility to increase or decrease production to maximize returns. However, as PDCE is incorporated into Chevron's broader portfolio, the asset's productivity can be more easily managed to maximize returns, without the same level of investor scrutiny.

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