Ecofin Sustainable Listed Infrastructure UCITS Fund (ESLIF)

Q2 2022 QUARTERLY COMMENTARY

Please note that this Ireland domiciled Ecofin Sustainable Listed Infrastructure UCITS Fund ("ESLIF") is a newly-launched fund (launch date 23 February 2022) which does not have a full year of performance. A UCITS fund with the same strategy and investment management team as ESLIF was previously launched under Luxembourg domiciliation in August 2019 ("Lux Fund"); however, due to platform onboarding issues in Luxembourg, Lux Fund was placed into liquidation in early June 2022 after the largest investor had transferred its investment to ESLIF.

Performance

Over the quarter, the fund's NAV decreased by 0.3% compared with the S&P Global Infrastructure Index which declined by 1.7% (total returns in Euros). Over the period since ESLIF's inception on 23 February 2022, the NAV rose by 8.3% while the benchmark index, which has a larger energy infrastructure content which performed strongly given much higher energy commodity prices, increased by 9.0%.

As of 30 June 2022

(All total returns in EUR)	3 months %	Since inception* %
ESLIF NAV	-0.3	8.3
S&P Global Infrastructure Index	-1.7	9.0

*24 February 2022

Performance of Lux Fund from August 2019 to 31 May 2022 (Lux Fund was closed in early June 2022)

(All total returns in EUR)	2019 %	2020 %	2021 %	2022 %	Since inception* %
Lux Fund NAV	10.8	4.1	21.0	3.3	44.1
S&P Global Infrastructure Index	8.7	-14.2	19.5	14.0	27.1

*6 August 2019. For strategy information purposes, performance information for the Lux Fund from its inception on 6 August 2019 to 31 May 2022 is provided below. Although both ESLIF and Lux Fund are managed by Ecofin Advisors Limited to the same strategy, Lux Fund's performance information DOES NOT constitute ESLIF's performance as it is provided for background information purposes only.

Market overview

It was a dismal quarter for equity markets and seemingly all financial and commodity markets experienced extreme volatility. Global equities fell sharply (the MSCI World Index dropped by 10.2%), compounding the first quarter's losses. Central bank interest rate rises were underway in major markets to tackle very high inflation rates stoked by pandemic-induced shortages and the upheaval caused by the war in Ukraine, and benchmark 10-year government bond yields rose sharply for much of the period on concerns about more entrenched inflation. China's extended Covid lockdowns were incrementally jeopardising global supply chains and contributed to the risk-off mood. By May, thoughts turned to the restraint on growth that higher policy rates would likely deliver, there was a moderation in rate rise expectations and longer term yields fell once again with weak economic data emerging globally.

The fund's utilities performed relatively well while risks radiated for the global economy and markets tried to price in lower growth. Generally strong earnings also encouraged sentiment. Renewables names, which had been under pressure for many months, came back to life as fossil fuel commodity prices moved even higher. More generally, inflation pass-throughs in infrastructure company business models contributed to portfolio shares generally holding up well in the nervous markets.

High oil and natural gas prices continued to underpin higher power prices on both sides of the Atlantic. European carbon prices remained strong too. For renewables operators, power purchase agreement (PPA) appetite has grown significantly in Europe amongst commercial and industrial buyers keen to lock in cost bases; price inflation in PPAs in the U.S. is also material with operators at least able to pass on cost increases they are experiencing. In both regions this marked an about-face in pricing power.

The affordability – and availability – of energy in Europe continued to be a major political issue and these pressures remained a burden for stock prices. Some Continental names were also reflecting stressed hydro output in Iberia and northern Europe as drought conditions continued. The UK government's imposition of a windfall levy on the profits of oil & gas companies operating in the UK for the next 12 months hit the share prices of UK electricity generators too, for fear their profits could also become a target. The actual impact of windfall measures instituted in Europe and the UK this year appear less stringent than initially feared though, and in our meetings with companies the feedback has been consistent: companies are seeking to reduce exposure to Russian gas flows ASAP, pricing realisations are extremely favourable, margins have expanded, and 10-15 year solar and wind PPA prices have increased 10-20%. Engie, for example, raised guidance in April due to incremental output and higher power prices.

Performance attribution

The 5 best and worst contributors to the NAV during the quarter were:

Company	Avg. net exposure	NAV contribution %
Top 5:		
Atlas Arteria	3.1	0.52
Atlantia	2.2	0.39
Acciona Energias Renovables	2.4	0.25
American Electric Power	3.5	0.16
Redes Energeticas Nacionais	2.4	0.16
Bottom 5:		
Veolia	2.7	-0.61
Enel	3.5	-0.53
Drax	3.3	-0.43
E.ON	2.0	-0.41
AES Corp.	2.3	-0.36

Infrastructure names in Australia continue to be the subject of takeover interest by private capital, most recently involving Atlas Arteria. IFM Global Infrastructure Fund increased its ownership of Atlas Arteria to 15% in May and is considering a bid for the rest of the company. Atlas' shares responded accordingly and, if a deal comes to fruition, this will add to the series of such listed infrastructure asset takeovers in Australia (Sydney Airport, power networks owners Spark Infrastructure and AusNet). Infrastructure group Atlantia, the airport and motorway operator headquartered in Rome, was the subject of a takeover offer from the Benetton family and Blackstone. The share price of Acciona Energias Renovables, a Spanish renewable energy company with a global asset base, was up slightly in the quarter. The company recently spun out from its parent and has ambitions for substantial growth in its renewables asset base. In addition, the company should stand to benefit from higher power prices in Europe from next year onwards as it has increasing levels of unhedged power price exposure in the years ahead. Fully regulated, Ohio based electric utility American Electric Power stands to benefit from higher commodity and power prices in its markets too. Redes Energeticas Nacionais (REN), the concession holder for Portugal's two energy infrastructure networks (electricity & gas) and the owner of power transmission lines and sub-stations in Chile, reported solid earnings and is an example of a fully regulated business with inflation protection in its regulatory formula.

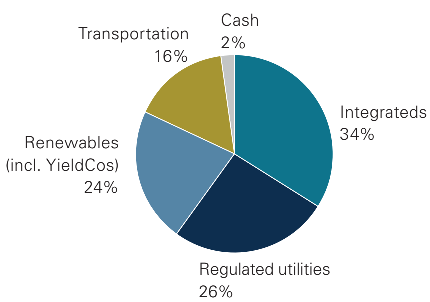
Veolia, the water management, waste management and energy services giant which completed the acquisition of its competitor Suez earlier this year, saw its shares weaken as economic forecasts for Europe were pared during the quarter, affecting near term prospects for its commercial and industrial business segment.

Enel, Drax and E.ON were buffeted by the uncertainties in the European utilities sector caused by actual or potential political interventions in the wake of energy unaffordability. Drax's shares had also been very strong for many months previously given the pellet and biomass specialist stands to benefit significantly from higher electricity prices in the UK.

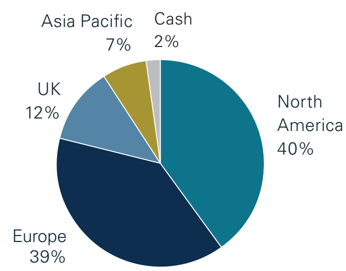
AES Corp.'s shares were weak early in the second quarter probably due to the Commerce Department's pending investigation of solar tariff circumvention and investor concerns about inflationary pressures for renewables developers generally. Q1 results were also a bit shy of consensus expectations but guidance was reaffirmed and its renewables project backlog continues to grow (AES' solar panels are U.S. sourced). Solar specialists like AES were helped late in the quarter by the White House's action to waive import tariffs on solar panels from southeast Asia for 2 years, thereby easing a bottleneck and deployment timelines. AES also announced deals with Amazon and Microsoft to provide each with renewable energy (solar & energy storage); PPAs have been signed and the energy will be sourced from AES' own renewable portfolio.

As of 30 June 2022

By sector (% of NAV)



By geography (% of NAV)



Portfolio changes

During the quarter, stock purchases occurred immediately following cash inflows to the fund in May, and these were invested according to Ecofin's investment strategy.

Two new names were added to the portfolio during the quarter, Vinci and Xcel Energy. Vinci is a France-based developer and operator of transport (motorways, airports – including Gatwick and 52 others around the world) and energy (renewables projects) infrastructure and concessions globally. We established the holding in Vinci at attractive levels prior to the French presidential election. Xcel Energy is a regulated, integrated electric and natural gas utility operating across 8 states and a leader in renewable generation investment. The company has a strong record and we expect EPS growth of 5-7% p.a. to be driven by rate base growth opportunities in Minnesota and Colorado, renewables (there is above average wind resource across XEL's service territory) and transmission. Xcel was added to the portfolio further to the sale of PPL Corp.

We increased holdings in high conviction European stocks Enel, SSE, National Grid, E.ON and EDF which had dipped to inexpensive levels. The position in NextEra Energy (NEE), which had de-rated while the U.S. government investigates whether solar panels manufactured in Southeast Asia are circumventing import duties on panels from China, was topped up. While a decision was pending, solar stocks had been weak. Although there could well be a delay in NEE's solar deployment (from 2022 to 2023), in our view this should have a very modest impact on EBITDA for 2022 and the company's medium term targets are intact.

Yield

The yield on the portfolio was 3.9% at 30 June (3.8% at 31 March 2022). We saw a very strong rebound in dividend receipts in 2021 given the resilience in demand for most of the portfolio's essential services, the economics for renewable energy and a strong recovery where certain companies had been prevented from paying dividends in 2020. We anticipate that longer term growth in income will be +5-7% per annum.

Strategy

The war in Ukraine is a major short-term risk for economies but potentially marks a significant turning point in energy policies and the energy transition. A search for alternative sources to diversify natural gas supply will be a focus of attention for years to come. Although some coal and natural gas fuelled power plants are having to be run longer than planned in the short run, the longer term solution will involve alternative gas supplies, energy efficiencies and significantly more renewables and nuclear in the generation mix. This should be unambiguously favourable to most of the fund's portfolio companies as the key enablers of this transition.

Interest rates are rising to combat sharply higher inflation which should benefit companies in the portfolio through direct adjustments in regulatory remuneration rates and/or higher commodity prices. Although utilities are often considered 'bond proxies' and therefore vulnerable to rising rates in the short term, rising prices offer considerable inflation protection in the medium to longer term.

We expect strong revenues for many power companies this year thanks to the combination of better renewables resources than in 2021 and higher power prices. This should particularly benefit companies with fixed cost generation assets and higher margins locked in through forward hedges. Longer term, an acceleration in renewables development activity as countries and companies work to improve their security of supply should lead to growth upgrades for renewables developers both in Europe and North America.

Intervention through price regulation and windfall taxes by governments trying to mitigate the impact of higher power prices on consumers is the biggest risk to higher profits at present. In our view, the share prices of many European integrated utilities already discount harsh pressure on margins.

The fund's portfolio is performing relatively well while investors' risk appetite is diminished, helped by the inflation linkage in the pricing formulas of the companies. Equity market volatility is providing opportunities to add value but the principal source of added value will be stock selection for the long term in this broad and undervalued investment universe.

This strategy continues to screen well in terms of carbon emissions, i.e. tonnes of CO_2 emitted per megawatt hour of electricity generation. Ecofin does not set firm limits on fossil fuel exposure and invests in companies transitioning to better growth and ESG profiles (rather than permitting only 'clean' stocks). Nevertheless, at a portfolio level our approach delivers an emissions profile which is well within the spectrum of typical impact funds. As of 30 June, this portfolio's electricity generators had CO_2 emissions which were 20% below the average emissions of the electricity grids in which the companies operate, largely because of a relatively small reliance on coal (c. 9% of the mix), and 26% lower than those of companies in the global utilities index (as measured in tCO_2/$million invested). On a forward-looking basis, specifically due to our focus on companies in transition, the portfolio's emissions profile looks even better, with almost all companies having committed to both a full phase-out of fossil fuels in the medium term and a net zero emissions target in the long run.