Reaves Asset Management

Market Commentary
Fourth Quarter 2020

REVIEW AND OUTLOOK

Performance as of 12/31/20	Q4 2020	YTD 2020	5 Year Annualized
Reaves LTV Wrap Composite[1], Gross of Fees	6.61%	4.08%	12.02%
Reaves LTV Wrap Composite[1], Net of Fees	5.96%	1.50%	9.17%
S&P 500 Index[2]	12.15%	18.40%	15.22%
Russell 1000 Value Index[3]	16.25%	2.76%	9.74%

INTRODUCTION

In 2020, Reaves' LTV Wrap Composite[1] performed in line with what one may have expected from a defensive equity strategy in a year that included a global pandemic, a market crash, record high unemployment, and a disputed presidential election. Most companies in the portfolio grew earnings and raised dividends despite the challenges during the year, highlighting the essential nature of their services and the potential to remain profitable through the economic cycle.

Monetary and fiscal stimulus delivered at the beginning of the crisis was multiples greater than the liquidity provided during the 2008 financial crisis. That excess liquidity found its way into the stock market, often benefiting the companies that had the most to gain in an economic recovery. While defensive equities, like the ones in which we invest, did not appreciate quite as much on a relative basis, we believe the portfolio is set up well for 2021. Valuations are compelling relative to the broad market[4] and even more so relative to fixed income alternatives. The outlook for growth within Reaves' areas of focus has strengthened and improved. We believe that investments in renewables and digitization will drive growth for the next several years, and our approach is to own the critical infrastructure that enables it.

COMMUNICATIONS INFRASTRUCTURE[5]

Communications infrastructure represented the largest part of the portfolio's assets at the end of 2020 at about 45% of total. These investments generated a return of +8.0% during the fourth quarter.

Cable stocks were the standout performers during 2020. Consumer broadband became an increasingly essential service in 2020, and cable's incumbency advantage remains tough to assail in most of the U.S. Altice USA led performance in the quarter. Altice's management decided to repurchase 18% of the company's shares after efforts to acquire Atlantic Broadband proved unsuccessful. The announcement, coupled with a leverage target that has been reset in the near term to allow for continued share repurchases, sparked a furious rally. As we look out to 2021, we continue to view cable stocks as structural, secular leaders.

Data centers and wireless towers make up the next biggest pieces of our communications strategy. High barriers to entry and increased reliance on broadband and cloud infrastructure provided favorable safe-haven status during the pandemic and underwrite long-term, secular growth trends. These investments corrected a bit in the fourth quarter, particularly when risk appetites returned amid encouraging news about the Covid-19 vaccines but were winners for the full year. For tower stocks, the risk-on market[6] compounded concerns about network spending delays at T-Mobile and Dish, resulting in growth estimates being pushed out. The short-term concerns offer an attractive entry point as tower companies carry the least risk of technological displacement in our sector, in our view. Likewise, we believe bipartisan enthusiasm for making spectrum available to satisfy consumer wireless demand should drive growing rental income for years to come.

UTILITIES

The utility sector makes up 37% of the assets in the portfolio and returned +4.9% in the quarter. Our strategy is to focus on companies that can achieve consistent mid-to-high single-digit earnings and dividend growth, and by and large the investments in the utility sector achieved this. The utilities in the portfolio grew dividends by 7.8%; in 2020 on a weighted average basis[7]. Using actual numbers for the first three quarters[8] and consensus estimates[9] for the fourth quarter, earnings per share are expected to have grown about 5.0% on a weighted average basis.

The setup entering 2021 is constructive. U.S. utilities should be a beneficiary of the Biden administration's focus on carbon reduction. In December, Congress extended tax credits for solar, battery storage, and offshore wind for several more years. Treasury yields are significantly lower today than at the end of 2019, and credit spreads are much tighter. Utility valuations relative to long-term interest rates have become compressed, allowing for the possibility of improvement if rates are flat and protection if they rise modestly.

In the fourth quarter, utilities behaved similarly to communications stocks as winners throughout the pandemic corrected upon news of the vaccines. One laggard during most of the year, Edison International, benefited from this rotation. The risk of catastrophic wildfire damage led to a depressed multiple for the first ten months of the year, but increased appetite to take on risk post the vaccine news combined with the end of a less-than-feared fire season led to a strong rally. As investors looked past the risks posed by the fire season, they saw a relatively inexpensive utility with strong long-term growth potential driven by California's aggressive climate change and carbon reduction policies.

Midwestern utilities and renewable-focused companies lagged post-vaccine news after leading for much of the year. Interestingly, given the context, NextEra Energy performed well in both market environments. The company has distinguished itself as the leader in renewable energy in the U.S., and the stock has benefited from investors speculating that renewable projects would receive a boost in demand under the Biden Administration.

TRANSPORTATION

Railroad stocks, at about 13% of the portfolio, delivered gains of +7.3% in the quarter. Optimism about an accelerated economic recovery boosted stocks to new highs. Operationally, the companies have become significantly more effective at managing costs, leading to higher margins that have buoyed earnings during the recession and potentially higher earnings growth when the recovery arrives.

SUMMARY

We believe the portfolio is positioned well heading into 2021. The growth potential in these industries has increased, driven by improving environments for renewables and digitization, while valuations continue to appear attractive.

[1] Reaves' Long Term Value Strategy (Reaves LTV) seeks a high risk-adjusted total return. The strategy tends to be invested in relatively larger companies with strong balance sheets, good cash flow and a history of dividend growth. Core positions are accumulated in financially strong, high-quality companies and generally have the following characteristics: strong management, above industry-average growth rates, large/mid-market capitalization and low price-earnings multiples.

Beginning December 2019 Reaves Long Term Value Strategy (LTV) is represented by the LTV SMA Wrap Composite. This composite contains those LTV discretion¬ary portfolios with wrap (bundled) fees. Wrap accounts are charged a bundled fee which includes the wrap sponsor fee, as well as Reaves' investment advisory fee. Due to compliance requirements, the net-of-fees calculation is computed based on the highest annual fee assigned by any wrap sponsor who utilizes this portfolio in an investment wrap program (300 basis points from 1/1/03 through 12/31/16 and, effective 1/1/2017, 250 basis points). LTV SMA Wrap Composite performance consists of money-weighted, time-weighted returns and it includes the reinvestment of all dividends and other earnings. The inception date of the composite is December 2002; however, the composite was created in January 2013. This composite has been managed in a similar manner to the Reaves LTV ERISA Composite which ended in December of 2019. The LTV SMA Wrap Composite does not represent all of Reaves' assets under management.

[2] The S&P 500 Index is a capitalization-weighted index of 500 stocks designed to measure performance of the broad domestic economy through changes in the aggregate market value of 500 stocks representing all major industries. The typical Reaves portfolio includes a significant percentage of assets that are also found in the S&P 500. However, Reaves' portfolios are far less diversified, resulting in higher sector concentrations than found in the broad-based S&P 500 Index.

[3] The Russell 1000 Index, a subset of the Russell 3000 Index, represents the 1,000 top companies by market capitalization in the United States. The Russell 1000 typically comprises approximately 92% of the total market capitalization of all listed stocks in the U.S. equity market and is considered a bellwether index for large-cap investing.

[4] Usually refers to indices that track the performance of thousands securities, rather than the more narrow measures.

[5] Communications investments include Communications Services and Real Estate Investment Trusts (REITS).

[6] A risk-on market occurs when traders and investors are prepared to take risks and they are focused on return on investment. A risk-off market occurs when traders and investors are risk averse and the focus is on preserving capital.

[7] Weighted average is a calculation that takes into account the varying degrees of importance of the numbers in a data set. In calculating a weighted average, each number in the data set is multiplied by a predetermined weight before the final calculation is made.

[8] Earnings per share (EPS) growth numbers are prepared using adjusted EPS metrics as defined by Bloomberg.

[9] A consensus estimate is a forecast of a public company's projected earnings based on the combined estimates of all equity analysts that cover the stock. Generally, analysts predict a company's EPS and revenue numbers for the quarter, fiscal year (FY), and future FYs.

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Reaves' portfolio characteristics, holdings and sector weightings are subject to change at any time and, unless otherwise noted, are based on our Long Term Value Strategy SMA Wrap Composite portfolio. Holdings, sector weightings and portfolio characteristics of individual client portfolios may differ, sometimes significantly, from those shown. This information does not constitute, and should not be construed as, investment advice or recommendations with respect to the securities and sectors listed.

An investor cannot invest in an index.

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