Reaves Asset Management

Market Commentary
First Quarter 2021

REVIEW AND OUTLOOK

Performance as of 3/31/21	Q1 2021	5 Year Annualized
Reaves LTV Wrap Composite[1], gross of Fees	1.93%	10.28%
Reaves LTV Wrap Composite[1], net of Fees	1.30%	7.50%
S&P 500 Index[2]	6.17%	11.74%
Russell 1000 Value Index[3]	11.26%	16.29%

INTRODUCTION

The Reaves LTV Wrap Composite[1] gained 1.9%, before fees, in the first quarter of 2021. This is compared to a gain of 6.2% for the S&P 500 Index. Beneath the surface of the strong market performance was a quarter characterized by high volatility and rapid rotation. Generally, stocks that have been strong since the FDA approval of the Pfizer vaccine in November continued upwards in January and February. Investors piled in the most speculative stocks with weak balance sheets and negative earnings to capture the most upside possible as the economy reopens, culminating in short squeezes in stocks like Gamestop and AMC Entertainment. Most of the portfolios managed by Reaves have assets invested in high quality, defensive companies, which unfortunately continued to underperform, especially as interest rates rose. Operationally speaking, these companies were putting up strong numbers, but the stocks were out of favor for reasons beyond their control.

Gladly, this dynamic changed in March and defensive stocks outperformed with utilities leading the way. Encouragingly, the gains happened as interest rates continued to march higher. Many defensive stocks had become so discounted relative to the S&P 500 that investors started to overlook the impact of higher rates. Even after last month's rally, we noticed many utility stocks are still valued 10% to 20% below historical averages.

The catalyst for defensive companies to rally in the face of higher interest rates may have been the unveiling of Biden's infrastructure proposal at the end of March. Aside from transportation and housing, the bill emphasizes renewable energy development, lead pipe removal, and high-speed broadband access, all of which could help portfolio holdings. Direct payments and extensions of renewable energy tax credits, as well as incentives for electric vehicle charging stations, could spur massive investment in the electric grid and real demand growth for the first time since the early 2000s. Stimulus dollars aimed at improving broadband connectivity could serve as a material tailwind to cable unit growth and future profitability. The biggest negative impact of the bill is the proposed increase in the corporate tax rate. However, much of the communications assets are invested in real estate investment trusts (REITs) which don't pay taxes, while for utilities, taxes are passed through to customers so this will have minimal impact to earnings and may even help cash flow depending on the level of tax credits.

The combination of attractive valuations plus positive catalysts in the form of the infrastructure bill position our portfolio well for future performance.

COMMUNICATIONS

At quarter's end, 43% of the portfolio was positioned in communications infrastructure companies[4] , which declined a modest 0.7% over the first three months of the year. Broadly speaking, the best performing stocks in the sector during 2020 underperformed at the start of the year because of the market rotation that began with approval of COVID-19 vaccines late last year.

The best performers this quarter all had economic re-opening themes. Shares of Alphabet have been particularly strong due to a faster-than-expected recovery from the advertising recession and an improved outlook for the company's large travel and leisure category. Improved execution at Google Cloud and the potential for increased capital returns helped lift the stock after its fourth quarter earnings report. Comcast benefited from economic re-opening optimism as well. The outlook for both the theme parks and media businesses improved, offsetting weakness in the cable broadband business.

Cable broadband holdings in Altice USA and Charter Communications fared less well to start the year. Both securities were impacted in part by the re-opening rotation within global markets. Additionally, investors have expressed concern about slowing growth rates for cable broadband and the potential for increased regulation from the new administration. A lack of detail in the President's infrastructure proposal related to broadband objectives has thus far been negatively interpreted by the market. Investors have expressed concern about the potential for new competition to cable operators and the possibility of price regulation. However, our research indicates that both concerns are likely to prove overstated, and we believe cable broadband will continue to be well-positioned.

UTILITIES

Utilities, at 38% of the portfolio, returned 0.6% in the first quarter. Similar to the communications sector, companies that performed well in 2020 have underperformed since the approval of the vaccines. For utilities, the underperformance centered on environmental, social, and governance (ESG) favorites like Enel SPA, an Italian utility that is a leading international developer of solar generation, American Water Works, and NextEra Energy.

The best utilities performers were ordinary companies not caught up in the ESG rally of 2020. Among the top three contributors were Alliant Energy, Public Service Enterprise Group, and XCEL Energy. All these companies have exceptionally long runways of investment opportunity and are well-positioned to deliver consistent earnings and dividend growth.

The most significant event of the quarter was the weather disaster in Texas. Millions were left without power for several days in freezing conditions, resulting in a humanitarian tragedy. Financial damages to both consumers and providers was significant. The episode has raised consciousness about the need for reliable energy infrastructure in the country that should serve the industry well as we enter a period of extreme grid transformation.

INDUSTRIALS

Transports, at 11% of the portfolio, performed well in the first quarter as investors bid up shares of companies with tangible exposure to economic recovery. In addition, ongoing COVID-related restrictions spurred still healthy gains in ecommerce and demand for logistics related services.

The biggest positive contributor was Kansas City Southern Railroad (KSU), which agreed to Canadian Pacific Railway's (CP) acquisition offer at a significant premium. KSU has been one of the fastest growing railroads due to its ownership of one of Mexico's two major rail lines and significant associated cross border shipping growth. CP's purchase of KSU brings together the two smallest rails in North America and creates a company with the network breadth to better compete with Union Pacific and Canadian National Rail. We continue to like Class I rail companies[5] like these for their significant barriers to entry, self-help initiatives, and pricing leverage.

We also saw notable returns from Prologis. Demand for warehouse space has been very strong despite meaningful capacity additions as supply chains adjust to a surge in e-commerce growth as well as the implication of long, complicated global supply chains. Supply chains in particular will be increasingly in focus and likely lead to a reversal in the long-term trend of just-in-time inventory practices and greater onshoring of mission critical component manufacture. All this should keep warehouse demand strong for the foreseeable future.

SUMMARY

While it's hard to remain patient when our stocks are out of favor, by focusing on high quality, defensive companies, we are positioned to perform well when sentiment changes. Strong gains in March may have been the start of that shift, but the speed of today's market plus the unprecedented amount of monetary and fiscal stimulus make any short-term forecast especially uncertain. In the long term, we're confident in the ability of companies in the portfolio to grow earnings and dividends in any economic environment, and that growth should allow the investments to compound value at an attractive and competitive pace.

[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] *Communication infrastructure companies include Communications Services and Real Estate Investment Trusts (REITS).*

[5] *In the United States, railroad carriers are designated as Class I, II, or III, according to size criteria set by the Surface Transportation Board in 1992 and adjusted for inflation annually.*

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***Past results do not guarantee future performance.** Further, the investment return and principal value of an investment will fluctuate; thus, investor's equity, when liquidated, may be worth more or less than the original cost. This document provides only impersonal advice and/or statistical data and is not intended to meet objectives or suitability requirements of any specific individual or account.*

All investments involve risk, including loss of principal.

All data is presented in U.S. dollars.

Cash is cash and cash equivalents.

Portfolios holdings are rounded to the nearest whole percent, and returns are rounded to the nearest tenth of a percent.

An investor cannot invest directly in an index.

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***Fees:** Net performance reflects the deduction of advisory fees which are described in detail in our Form ADV Part 2A.*

Please contact your financial professional, or click the following links, for a copy of Reaves' Form ADV Part 2A and Form CRS.

Additional information about Reaves may be found on our website: www.reavesam.com.

Reaves Asset Management

10 Exchange Place, 18th Floor
Jersey City, NJ 07302
www.reavesam.com

For further information, please contact:
Thomas M. Grimes, Director of Investor Relations
Email: tgrimes@reavesam.com • Phone: 201.793.2384