

# Two Views of the Stock Market

JUNE 30, 2020

## SOCIETY HOLDS CONFLICTING VIEWS OF THE STOCK

market. Millions of people continue to take a long-term view, investing in equities with an eye towards funding retirements that may be decades away. Yet, on a daily basis, commentators use the market as a gauge of how things are going *right now*. When stock prices are high, politicians and executives are quick to pat themselves on the back and yammer on about how high stock prices are proof positive that all is well. When stocks plunge, the talking heads are just as sure that things have never been worse, with no hope in sight.

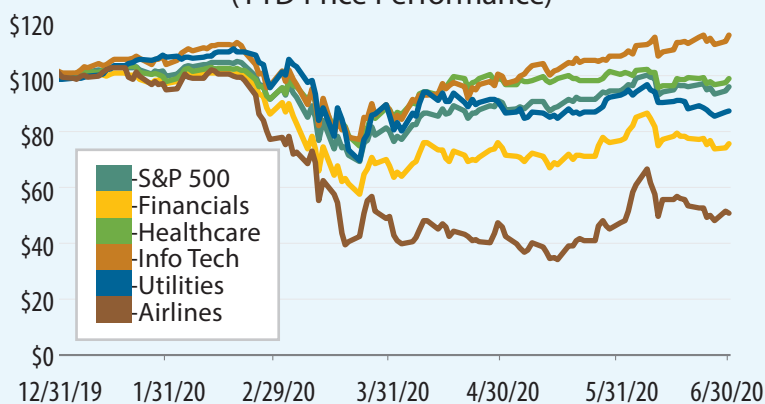
Recent market gyrations have brought this dichotomy into stark relief. The S&P 500 Index peaked on February 19th, then fell by roughly a third over the next five weeks. Since then the market has shot up, rising roughly 40% through quarter end. From the standpoint of a short-term barometer, the market swings are easy to explain. Initially, the market's take on the coronavirus was to ignore evidence that a pandemic had started. Panic set in when it became clear that western democracies would partially shut down their economies to control the spread. Markets roared back when both governments and central banks around the world made it clear that there would be a nearly limitless amount of stimulus applied to the ailing economy. The market recognized that the economy would survive, even as the number of COVID-19 cases and deaths trended higher.

While this year's market swings make sense as a gauge of sentiment, these fluctuations are impossible to understand from the standpoint of long-term investing. The coronavirus presents an enormous healthcare challenge, but in our opinion its economic impact will be finite and relatively short-term. Either a vaccine will be developed, or the disease will run its course through the population. The latter scenario ended the pandemic a hundred years ago. From a human standpoint, that was a tragic outcome, but it did end after a couple of years. We all hope for a successful vaccine, but in any case, the duration of the pandemic will be limited.

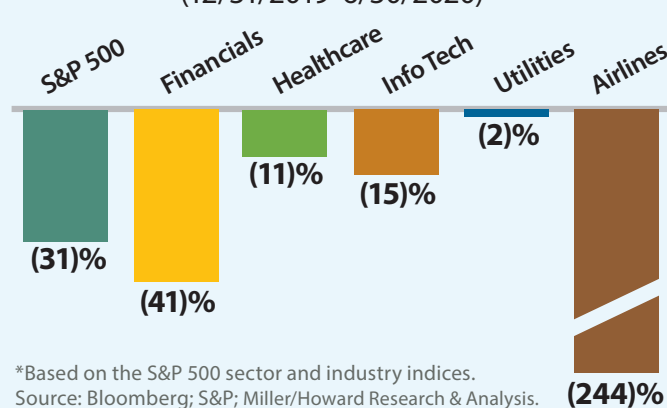
By contrast, equities are truly long-duration assets. Stock prices reflect forecasted earnings far into the future. When a stock trades at a price/earnings (P/E) ratio of 20x, the value of next year's earnings is roughly 5% of the total equity's value. So even if earnings are zeroed out for an entire year, the rational drop in market value would be on the order of 5%—not the wild price swings we have seen.

In the charts below, we compare the year-to-date price performance for the S&P 500 and five key sectors, and the change in 2020 consensus earnings estimates over the course of the first half of this year. From high to low, the S&P 500 swung 36 percentage points. Over the same period, the coronavirus caused a cut of 31% from expected 2020 earnings for the S&P 500—significant, but not even close to a lost year. The swing shows the emotional roller coaster the market has been on, disconnected from any reasonable view of future earnings.

**S&P 500 Industries Indices**  
(YTD Price Performance)\*



**Change in Estimated EPS**  
(12/31/2019-6/30/2020)\*

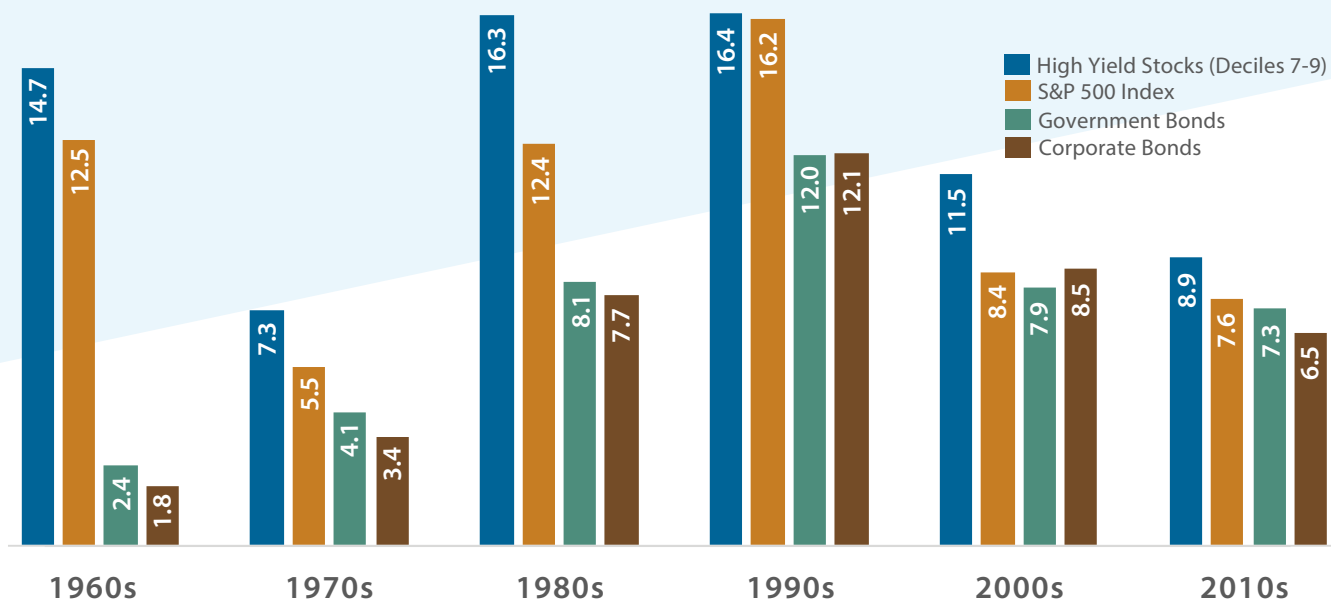


\*Based on the S&P 500 sector and industry indices.  
Source: Bloomberg; S&P; Miller/Howard Research & Analysis.

Continued on page 2.

## Average Rolling 10-Year Total Returns by Decade

(January 1, 1951 - December 31, 2019)



Data are through December 31, 2019. Based on the rolling 10-year annualized total returns, ending each calendar year, averaged by decade.

Source: Miller/Howard Research & Analysis; 2019 Stocks, Bonds, Bills and Inflation (“SBBI Yearbook”) and S&P 500 Index data as reported to Morningstar Direct. High Yield Stocks data is provided by Fama/French Research data library (value weighted deciles); Long-term government and corporate bond returns are based on the SBBI Yearbook.

Even sectors with little change in earnings estimates, such as healthcare, tech and utilities, still endured wide swings. Only the downturn in the airlines makes sense given the possibility of major bankruptcies. Otherwise, we can only conclude that the equity market is highly volatile, far more than could possibly be explained by any sort of rational financial analysis.

### Implications of Market Volatility

Even to experienced investors, wild market swings can be unnerving, but volatility also creates opportunity. Over the long-term, volatility is what scares many investors away from equities as an asset class. Bond investors clearly sacrifice long-term returns to avoid equity volatility.

The chart above shows the rolling average returns for high yield stocks, the S&P 500, government bonds and corporate bonds using 10-year holding periods. Equities outperformed bonds in all of these decades, showing the rewards for buy-and-hold equity investing.

What may surprise readers is that high yield equities (Deciles 7-9) outperformed the S&P 500 on average *in every one of these decades*. Naturally returns can look quite different over shorter periods, as we have seen recently. The outperformance of high-dividend yield stocks over the long-term primarily relates to what a dividend signals about a company and management.

### Dividends are a Signal:

- Public companies are run by executives who are strangers to the average investor and should not be trusted blindly. A dividend is a commitment by management to run the firm quarter-after-quarter with shareholder cash return as a priority.
- While management statements should be treated with appropriate skepticism, executives know more about their business than shareholders do. By committing to a regular dividend, management is using more than just words to signal that they expect their business to be resilient, even in a changing environment.

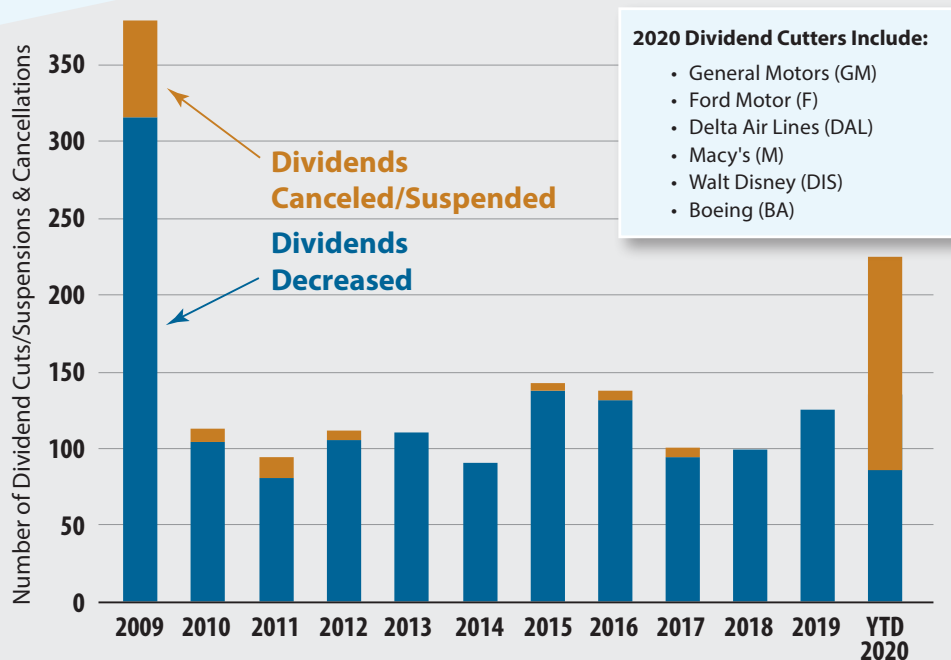
In addition, dividends represent regular cash flow that can be reinvested to compound over time.

In recent years, high-yielding stocks underperformed the broad market. This has largely coincided with the underperformance of value stocks. Dividend investing and value investing are different disciplines, but the universes partially overlap. Many expensive stocks simply cannot afford to pay good dividends. (A company with a P/E of 50x, that pays out half of its earnings, would only yield 1%.)

*Continued on page 10 - Why value has trailed growth.*

# Tough Environment for Dividends

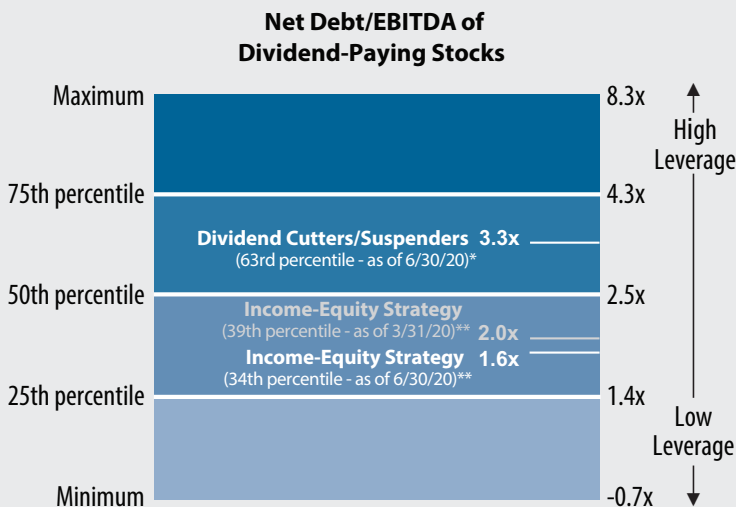
Companies have cut or canceled dividends at the highest rate since 2009.



As of June 30, 2020. Source: The Wall Street Journal; S&P Capital IQ; Eikon; FactSet; StreetAccount; Miller/Howard Research & Analysis. Based on US companies and public investment funds (REITs, etc). Year-to-date 2020 dividend data are based on stocks with market capitalizations >\$1B, as tracked by Miller/Howard Investments. Data prior to 2020 are sourced from the Wall Street Journal and S&P Capital IQ. As of June 30, 2020, GM, F, DAL, M, DIS, BA were not held in Miller/Howard's Income-Equity Strategies.

**MORE THAN 200 US COMPANIES ANNOUNCED DIVIDEND CUTS IN THE FIRST HALF OF 2020, GREATER THAN double what we typically see in a full year.** Many of the cutters were well-known companies such as General Motors, Disney, and Boeing. Miller/Howard strategies largely avoided dividend cuts. We had no cuts in our Income-Equity Strategies with one possible exception of Coca-Cola European Partners, a twice-yearly payer, delaying its second quarter dividend until they have better visibility.

Our success in largely eluding dividend cuts comes principally from avoiding stocks with high leverage. The chart below shows the cumulative distribution of leverage, measured by Net Debt/Trailing EBITDA, for the entire dividend-paying universe (excluding financials). As the chart shows, median leverage for the universe was 2.5x, a half-turn higher than our Income-Equity Strategy at the end of Q1. Over the course of the second quarter, we moved our Income-Equity holdings towards firms with less leverage, ending the quarter with a weighted average of 1.6x.



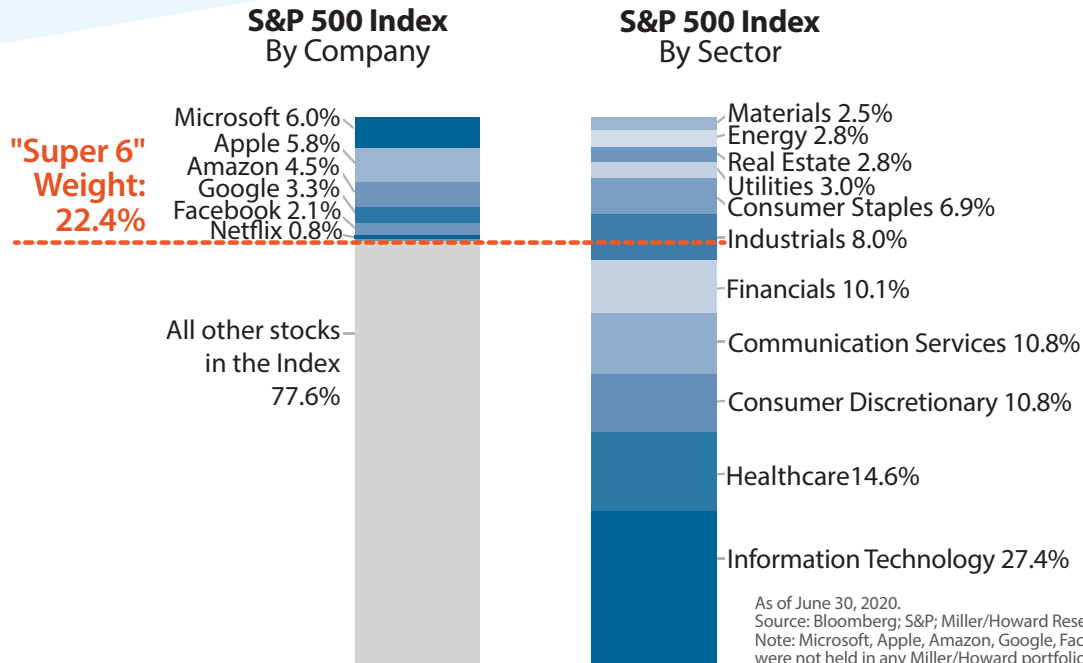
As of June 30, 2020. Source: Eikon; Bloomberg; MHI Research & Analysis. Bloomberg Screen: All US-traded equities with a market cap >1B and with a dividend yield >0% on 12/31/2019 and were paying a dividend on 3/31/2020. Top/Bottom 5% of outliers are excluded from both cutters/suspenders universe, and all dividend-payers universe. Financials are excluded. Stocks where data is not available are excluded. \* simple average \*\* weighted average

In contrast, dividend cutters on average had much more debt, averaging 3.3x. The dividend cuts in 2020 have confirmed Miller/Howard's belief that dividends from highly-leveraged companies are not reliable.

Dividend cuts had a big impact on stock performance. Dividend cutters were down 39% over the first half of the year. On average, the dividend cutters fell 49% prior to announcing the cut, as the market anticipated what was coming. On average the cutters rebounded somewhat following the cut, along with the rest of the market. To answer a common question: no, buying a stock ahead of a dividend cut doesn't lead to a single certain result. Some stocks will continue to plummet while others rally. What's clear is the importance of staying away from companies that could be forced to eliminate their dividend. This remains a pillar of Miller/Howard's approach to active management of dividend equity portfolios.

# Income-Equity Strategies

Quarterly Report 2Q 2020



## HAPPY TIMES ARE HERE AGAIN? NOT REALLY.

The US equity market bottomed on March 23, and then preceded to rise 39% through the end of the second quarter, driven largely by the realization that the economy would have, at least, a partial reopening. A fair summary would be that office work never stopped, manufacturing and construction slowed but then found ways to work safely, and consumer businesses such as restaurants remain challenged. Increased optimism translated into good returns for cyclical sectors such as energy, materials, and industrials, while defensive sectors such as utilities and staples lagged.

The S&P 500 Index was up 20.5% during the quarter, with one-third of that return driven by the “Super 6.” Index concentration in these six stocks—Microsoft, Apple, Amazon, Google, Facebook, and Netflix—is high (22.4% of the S&P 500!), and they have increasingly rich valuations and below-market or no dividend yields.

The Income-Equity Strategies outperformed the major dividend and value indices\*, powered by stocks in a variety of sectors. What the stocks all have in common is a good dividend yield, prospects for dividend growth, and a strong balance sheet.

Our trades during the quarter lowered the average leverage among our holdings, measured by net

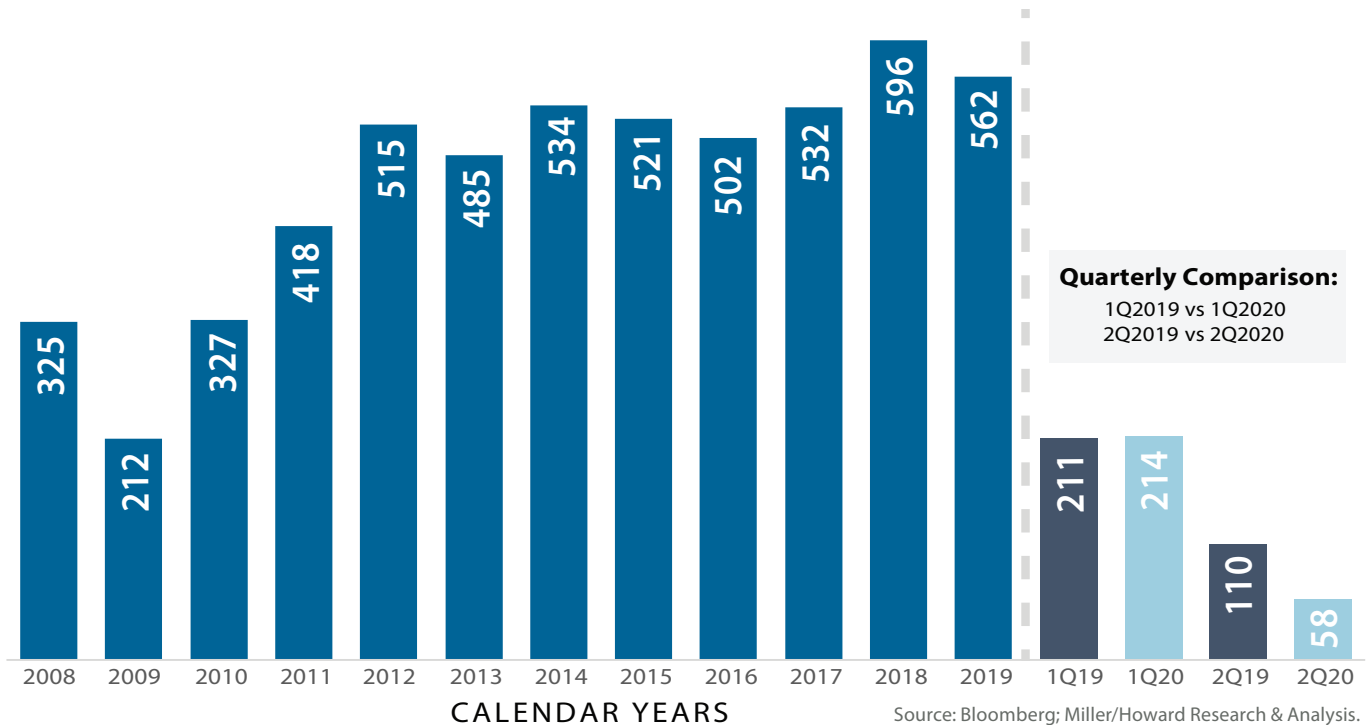
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\*Russell 1000 Value and the Dow Jones Select Dividend Index.

## Portfolio Highlights

- Dividend increases.** Our Income-Equity Strategies had two dividend increases this quarter, **Target (TGT)** and **Cardinal Health (CAH)**. **Coca-Cola European Partners (CCEP)**, a twice-yearly payer, delayed their Q2 dividend pending better visibility.
- Portfolio Income.** On a year-over-year basis, based on representative accounts, income from Income-Equity Strategy rose 4.4% and Income-Equity (No MLP) Strategy rose 5.4%.
- Avoiding dividend cuts.** Eight stocks formerly held in Income Equity cut dividends this quarter. Four were sold in 2019: **CenterPoint (CNP)**, **HSBC**, **Kohl’s (KSS)**, and **Six Flags (SIX)** were all sold in 2019. We sold **Total (TOT)**, **Brixmor (BRX)**, **Kimco (KIM)**, and **Lamar (LAMR)** in the second quarter prior to their cut announcements.
- Sales.** In addition to the four stocks listed above that we sold in 2020, we also sold **Regions Financial (RF)** on concerns over potential loan losses in the oil & gas industry.
- Buys.** We initiated three new positions. We were able to enter **Western Union (WU)** and **Interpublic Group (IPG)** after both stocks traded off on economic concerns. Both offer good free cash flow, dividend yield and balance sheet strength. We bought **Coca-Cola (KO)** at an unusually high yield for this long-time dividend grower.

## Number of Dividend Increases: Russell 1000 Index



debt/EBITDA. As you can see from the tables on page 11, average leverage in the Income-Equity Strategies is low relative to their history.

Investors have been particularly concerned about potential dividend cuts by the banks. The Fed announced its stress test results at the end of June for all major US banks, including the five held in the Income-Equity Strategies. The Fed's stress test did force Wells Fargo, a stock not owned in Income-Equity, to reduce its dividend. All of our bank holdings will be able to pay their third quarter dividend. All banks are required to resubmit to the Fed before announcing Q4 dividends. We believe our bank holdings have the balance sheet strength to be resilient in the face of the current downturn, but we will continue to monitor the outlook for credit losses and regulatory changes.

### Looking Ahead

Our long-term goal is to not merely avoid dividend cuts, but actually grow the portfolios' income over time. The graph above shows why this has become more difficult in the current environment. The number of companies in the Russell 1000 Index increasing dividends each year has been relatively steady over time, even in the first quarter of this year. In 2Q 2020, however, we witnessed a large drop (compared to the 2Q 2019) in the number of dividend increases as companies across many sectors sought to retain capital in the face of great uncertainty generated by the COVID-19 pandemic.

We continue to believe that our portfolios should be able to grow income steadily, once the market has more clarity on the coronavirus outlook. As the tables on page 11 show, our holdings have strong coverage ratios, giving dividends room to grow. More importantly, we have emphasized investing in companies positioned to participate in long-term secular growth trends. For example, **Broadcom (AVGO)**, **Cisco (CSCO)**, **Taiwan Semiconductor (TSM)**, and **Texas Instruments (TXN)** should all benefit from the shift to 5G and the internet-of-things, **Magna (MGA)** should play an important role in the development of autonomous driving, and our pharmaceutical holdings have exciting potential therapeutics in their research labs. The current year will be challenging for dividend increases, but we believe that our portfolio is well-positioned for income growth over the long term.

See *Income-Equity Strategies yield tables* on page 11.

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# MLP Strategy

Quarterly Report 2Q 2020

## IT WAS THE QUARTER OF THE PENDULUM SWING.

Crude started out around \$20/barrel, briefly plummeted to *negative* \$38/barrel, and rebounded to average about \$38/barrel during the month of June. Midstream stock prices followed a similar pattern, with higher beta names (think lots of debt and distribution cuts) swinging with the price of crude.

However, we continue to believe that focusing on the highest quality names in the sector – names with integrated systems, stable cash flows, and financial strength – will not only meet our client promise but will drive strong relative performance over the long-term.

We believe that investors are drawn to the sector for income and growth of income. To that end, our MLP Strategy has had one company cut its distribution—we held **Plains All American Pipeline (PAA)** and its tracking stock (**PAGP**)—well below the Alerian MLP Index (**AMZ**), which saw 16.

The benchmark companies that we consider to have lower financial strength bounced off the market bottom in March through this quarter end. We believe this junk/beta rally has overextended itself given the current macro/commodity environment. It goes against our philosophy to chase a beta rally, as we don't believe it adds value long-term.

These companies generally have riskier income streams as evidenced by the distribution cuts, lower financial strength, and more dependence on higher commodity prices.

We typically also avoid these companies due to the nature of their operations, which include a high percentage of gathering and processing assets, second- and third-tier basin exposure, less take-or-pay contracts, and, in some cases, less fee-based exposure.

We invest in higher quality companies as evidenced by our portfolio's overweight to investment grade holdings, superior distribution growth outlook, and better estimated EBITDA growth.

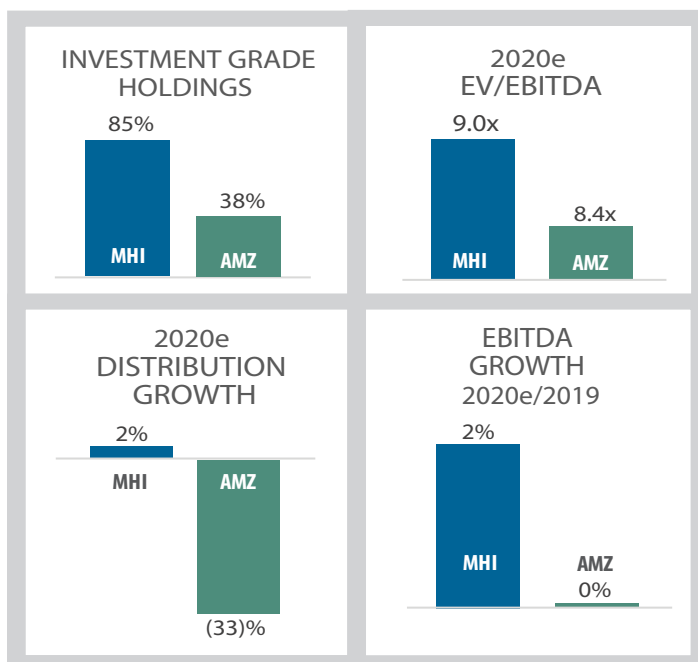
## Looking Ahead

The outlook for crude oil, refined products, and natural gas demand remains uncertain, and COVID-19 cases are on the upswing in the US. It is important to remember that crude is currently priced in the neighborhood of \$40/barrel through 2021 according to the strip. We believe this price is too low to incentivize a significant acceleration of development in US onshore volumes outside of restarting wells that were temporarily shut-in. We estimate oil demand destruction from the COVID-19 containment efforts to be roughly 30 million barrels per day.

We believe, given the uncertain and volatile environment, that it is more important than ever to own stronger and more stable names. Over the long term, high quality midstream energy companies are rewarded, and we view this quarter's performance as a temporary relief rally. We have positioned the portfolio in names where we see the distributions are secure, and we believe long-term fundamentals will, once again, favor these high-quality names.

## Portfolio Highlights

- **Distributions increases.** Year-to-date 11 of our 16 holdings announced dividend increases. The average increase was 6.2% year-over-year.
- **Portfolio holdings.** We initiated a position in **Holly Energy Partners (HEP)**, where refinery logistics assets provide a relatively more stable cash profile, and minimum volume commitments support the distribution. We trimmed our two largest positions, **Enterprise Products Partners (EPD)** and **Energy Transfer Equity (ET)**, to allocate to the new name. More recently, we bought **Western Midstream Partners (WES)** after selling in the first quarter, as the company's financial strength and new yield are appealing after the company cut its distribution in April of this quarter. We trimmed **Phillips 66 Partners (PSXP)**, **ET**, and **ONEOK (OKE)** to accommodate this buy.

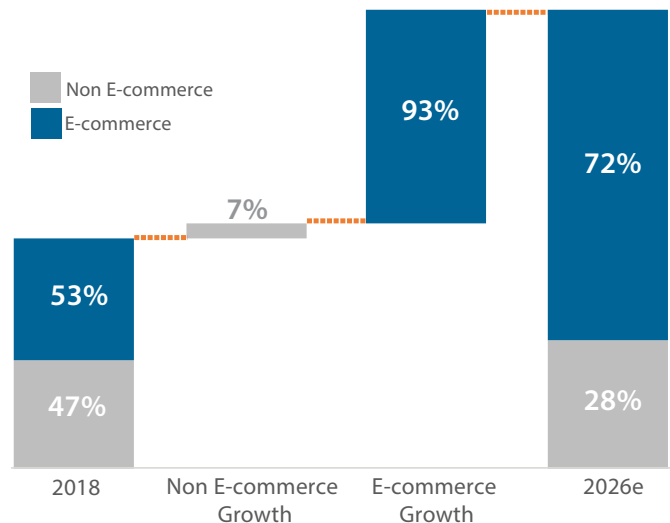


As of June 30, 2020. Source: Refinitiv, Alerian, Miller/Howard Research & Analysis.

**Over 90% of projected US parcel delivery volume growth through 2026 to come from e-commerce**

Source: FedEx analysis as of September 2019. Non e-commerce includes business-to-business and residential non e-commerce deliveries.

## Projected Total US Domestic Parcel Delivery Volume Growth



**AHEAD OF REALITY, MARKETS BEGAN FOCUSING ON A REBOUND** JUST as Americans were entering nationwide lockdowns. During the quarter, the S&P 500 Index gained 20.5%, with all 11 sectors carding positive returns. Investors used their time at home to gravitate towards positive data points, delivering the best quarter for the market in over 20 years.

The four primary sectors within the Infrastructure strategy followed suit, with leadership an almost mirror image of first quarter losers. Midstream (Energy) had the best performance, as West Texas Intermediate nearly doubled despite a brief and almost unfathomable drop to *negative* \$38/Bbl amid the settlement of monthly futures contracts. Industrials were second, with transportation and logistics names benefitting from reopening hopes and residential deliveries. Communication Services were third, although towers bucked the recovery theme with strong relative returns in back-to-back quarters. Utilities were a material laggard as they failed to participate in the market rally. With relative valuation more attractive than in recent years, we increased our exposure to the group.

### Looking Ahead

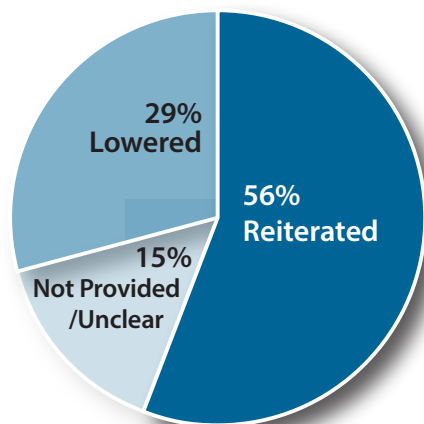
Identifying essential service providers with high barriers to entry has long been an integral part of our investment process. Historically, these types of businesses have generated durable cash flow streams that can better weather economic cycles and shocks. COVID-19 is like a one-hundred-year storm, highlighting consumers' continuing requirement for basic necessities like water, energy, household goods, and telecommunications. The dramatic disruptions of these past few months instill us with renewed confidence of the merits of this strategy. A dependable power grid, reliable transportation of freight and materials, trash services, and voice and video connectivity are keys to maintaining normalcy, and the last things consumers cut back on. Whether the virus is quickly cured, flames out, or instead, sees a tragic resurgence, few of our companies are likely to be more than marginally financially impacted by these events, in our view. Indeed, the absence of life's luxuries reminds one of the importance of necessities, creating a timely moment for our holdings.

### Portfolio Highlights

- Broadening utility exposure:** We used relative weakness among utilities to establish new positions in **Evergy (EVERG)**, **PPL Corp. (PPL)**, **FirstEnergy (FE)**, and **Entergy (ETR)**. We purchased **EVERG** on improved prospects for consolidation following the emergence of an activist investor. **PPL** has regulated operations in the US and UK, and trades at a discount to peers. And we expect **FE** and **ETR** to re-rate as investors become more familiar with their streamlined, regulated asset bases.
- Adding an airport:** We established a position in **Grupo Aeroportuario del Centro Norte (OMAB)** after the name sold off due to coronavirus-induced passenger reductions. A strong balance sheet puts the Mexican airport operator in a position to benefit from recovering air travel when pandemic pressures dissipate.
- Tactical allocations:** We added to **Veolia Environnement (VEOEY)** on weakness. We had trimmed the position in Q1 after a period of relative strength.

## 2020 Guidance Commentary

Provided with Q1 Earnings



Source: Refinitiv; Miller/Howard Research & Analysis.  
Based on the Utilities Plus representative account as of June 30, 2020.

### UTILITIES MOSTLY TREADED WATER WITH THE S&P 500 UTILITIES INDEX

returning 2.7% during the quarter. While the largest names within the S&P 500 Utilities Index have led the index YTD, performance was more uniform across capitalizations during the quarter.

We believe several factors kept utilities from participating in this quarter's rally. First, coronavirus-related demand destruction and fears that unpaid bills would likely reduce earnings weighed on the sector. Second, sustained lower interest rates could reduce the returns that utilities are permitted to earn in future rate cases. A more technical and short-term driver may be the simple fact that the market was fixated on a high-beta recovery trade—traditionally defensive sectors like utilities and staples did not fit the narrative.

While investor apprehension is not unfounded, it is still a bit confounding that defensive utilities have underperformed in the face of a pandemic. As point of fact, 56% of our portfolio holdings have reiterated 2020 guidance compared with the market trend of companies withdrawing forecasts or lowering forecasts in the wake of the pandemic.

### Looking Ahead

While utilities weren't favored this quarter, we remain confident that the current health crisis does not alter the sector's long-term value proposition. COVID-19 headwinds are manageable even in the context of rising cases across numerous states, and indeed, several state regulators have already moved to recompense utilities for lost revenues. Regardless of near-term demand, companies have an opportunity to deploy capital in high-return renewable generation projects, as carbon is removed from our energy economy. As the largest owners of wind and solar, listed utilities can offer an ideal way to participate in the energy transition.

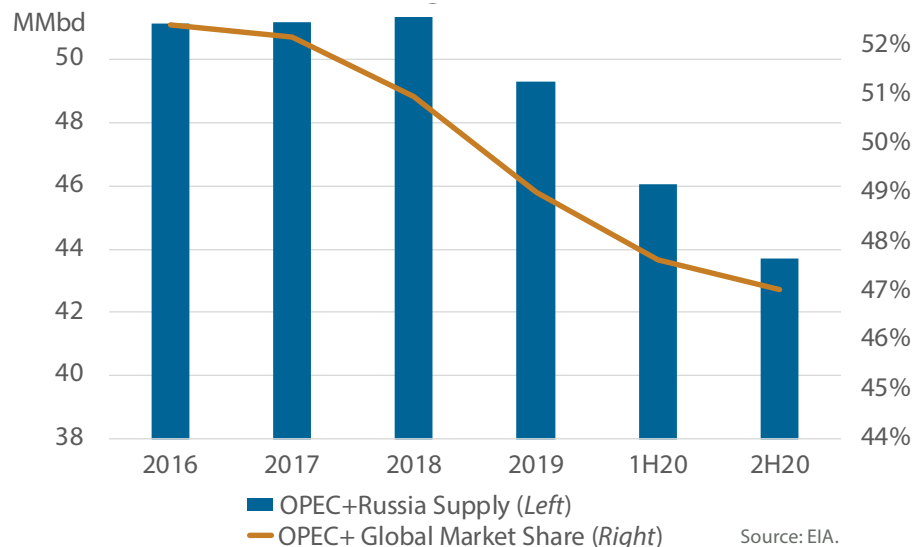
Looking towards the November elections, utilities are less exposed to potential increases in corporate tax rates than companies in other sectors, as their taxes are recovered in ratepayer bills. Too, a leftward political shift in 2020 could bolster renewable energy credits, providing new development opportunities.

After recent weakness, utilities' relative valuation is more attractive than in recent years, supporting a reasonable entry point to participate in what we view as solid industry fundamentals. We believe this should ultimately provide long-term earnings and dividend growth.

### Portfolio Highlights

- **Dividend growth is still available:** UGI Corp. (UGI) increased its dividend, payable on July 1, by 10% Y/Y.
- **M&A potential:** We increased our position in Energy (EVRG) on improved prospects for consolidation following the emergence of an activist investor.
- **Increased conviction:** We increased our weights in MDU Resources Group (MDU), Eversource Energy (ES), and FirstEnergy Corp. (FE). MDU has a compelling valuation, and its construction services and construction materials segments could be a direct beneficiary from fiscal stimulus supporting infrastructure spending. ES benefits from strong regulated growth with offshore wind projects providing upside to long-term growth expectations. Finally, we expect FE to re-rate as investors become more familiar with its T&D-focused asset base, following the separation of its merchant subsidiary.
- **Reallocating UK exposure:** We exited our position in National Grid (NGG) and increased our position in PPL Corp. (PPL), two utilities with regulated operations in the US and UK, based largely on an unwarranted valuation discrepancy.

## OPEC Continues to Cede Market Share to Support Oil Price, Pressuring Petrostate Economies



**THIS QUARTER MARKS THE NINTH ANNIVERSARY OF THIS STRATEGY,** originally conceived to benefit from rising production and consumption of technology-enabled North American energy supplies. The emergence of shale has coincided with, and contributed to, a tumultuous period economically, geopolitically, and financially. Thankfully, we’ve always taken an expansive view of energy investing, recognizing that cycles are inevitable, and that some of the most important participants are those tied not to commodity prices, but to volumes and activity. This approach has helped mitigate volatility, and provided us a broader opportunity set that can prosper in a variety of scenarios. Consequently, through time we’ve captured over 86% of the upside in the S&P 1500 Energy Index, while participating in just 70% of the downside. While 2020 has dealt headwinds, a more granular review offers cause for optimism: The portfolio navigated the worst of the first quarter energy collapse, while participating in the rebound this quarter. As global economies begin to heal, we remain confident in our process and approach to investing in energy.

### Looking Ahead

Supply and demand both impact energy prices. Demand growth will be tied to the resumption of economic activity, but it’s important to remember this is not simply a function of case counts. While many will continue working from home, others will buy cars instead of riding the bus or train—a structural positive for energy demand. Prior to the pandemic, the supply-side looked increasingly favorable: Shale producers all but abandoned growth in favor of dividends, deleveraging and buybacks, while OPEC+ maintained coordinated production cuts. Since then, shale has retrenched even further, while OPEC+ deepened their market support. While the near term may look bleak for the energy sector, we believe it’s not outside the realm of possibilities that industry conditions rebound quicker than expected. As energy stocks trade at deep discounts to “normalized” earnings, we think that any return to stability could spell opportunity in the space.

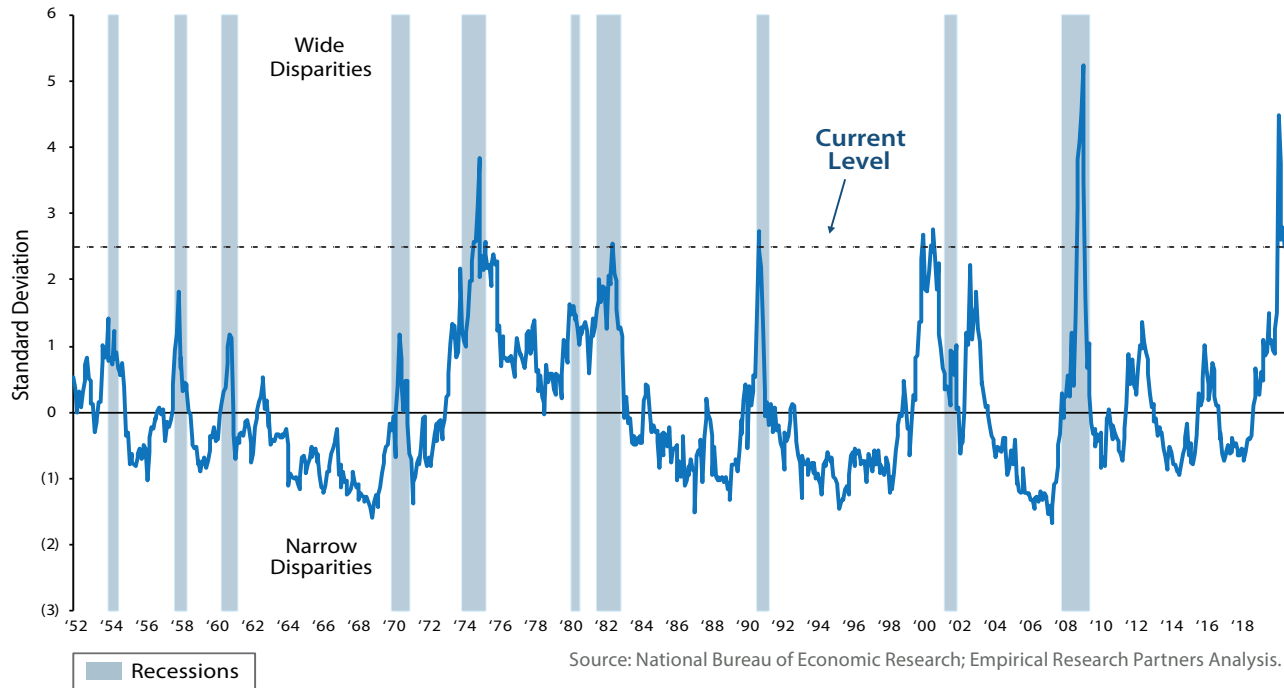
### Portfolio Highlights

- Energy and income.** It may come as a surprise that, despite 4 dividend cuts, 11 portfolio holdings have raised dividends this year, and underlying portfolio income is currently higher than at the beginning of the year. \$100,000 invested on January 1st was projected to generate annual income of \$3,900 based on underlying indicated yields at the time. Due to dividend increases, and portfolio trades, the same hypothetical investment is currently indicated to generate about \$4,300, despite the industry turmoil.
- Along the Energy Value Chain.** After increasing natural gas exposure last quarter, we reduced our positioning this quarter following strong relative price performance. We reallocated towards downstream refiners, which should benefit from gasoline demand green shoots. Generally, we remained more active than normal due to significant price volatility.

# Two Views of the Stock Market

(Continued from page 2)

## US Large-Capitalization Stocks Valuation Spread (The Top Quintile Compared to the Average – 1952 through June 2020)



### Value has trailed growth during the last decade primarily for two reasons:

- The run-up of “Winner Take All” growth stocks such as Netflix, Amazon, and Facebook. Investors have rewarded these stocks with fulsome valuations, suggesting that they will maintain high growth rates for decades.
- The increase in bond surrogate stocks, such as some consumer staples and certain utilities, that have reliable dividends but have limited growth potential. Historically low interest rates have enticed some bond investors to buy bond-like equities.

Value investing tends to work best coming out of recessions, following periods in which investors have bid up the prices of stocks offering safety. The relative price of the cheapest 20% of stocks has varied over time, and March 18, 2020 saw a spread so wide it has only been seen two other times in history. Value rallies have typically started during periods of wide valuation spreads. The classic example was the end of the Tech Bubble which led to a sustained rally in value stocks that lasted seven years. Even with valuation spreads narrowing from the recent peak, they are currently just under the level seen at the peak of the Tech Bubble, leaving plenty of room for value to rebound.

In our view, the key catalyst needed for a value rally is for investors to see a clear path to the end to the pandemic. The case count increase in many states is clearly concerning, but we think there will be accommodations to allow the economy to recover. We continue to believe that most jobs can be restructured by social distancing, mask wearing, and temperature checks so that the economy can move forward. A successful vaccine would represent a bright green light, but we would expect the market to trade up strongly on initial news of successful clinical results for any of the hundred plus vaccines under development.

Value rally or not, we expect our dividend strategies to continue to produce reliable income. Over time, dividend income has proven to be an important component of equity returns, and dividends are much less volatile than the overall stock market. A key to dividend investing is avoiding dividend cuts which undermine the premise and the Miller/Howard strategies have largely avoided dividend cuts during this difficult period.

## Yield, Growth, Strength, Stability

- Our Income-Equity Strategies each offer a high dividend yield that is over 2x the yield on the S&P 500 Index, and have ample dividend coverage and reasonable leverage levels (net debt/EBITDA).
- Both portfolios trade at a significant discount to the broad market on price-to-earnings as well. Value investing historically has done best coming out of a recession, so the historically low valuations should set the Income-Equity Strategies up for a strong recovery, in our view.
- The near-term picture is cloudy for projected dividend growth. However, we believe the portfolios are well-positioned to weather this downturn and poised to return to dividend growth when economic conditions improve.

### Income-Equity Strategy (with MLPs)

	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2Q2020
Income-Equity Yield	5.1	5.1	4.8	4.4	4.2	4.7	4.0	3.7	4.3	3.7	4.2
S&P 500 Yield	1.9	2.1	2.2	1.9	2.0	2.2	2.1	1.9	2.2	1.9	1.9
Ratio	2.7x	2.4x	2.1x	2.3x	2.1x	2.2x	1.9x	2.0x	2.0x	2.0x	2.3x
Income-Equity Projected Dividend Growth*	6.2	6.8	7.5	7.5	7.5	5.8	5.0	6.3	7.8	7.3	4.0
S&P 500 Projected Dividend Growth**	5.8	5.9	5.1	5.9	4.7	4.2	4.0	4.2	5.2	4.2	2.6
Ratio	1.1x	1.1x	1.5x	1.3x	1.6x	1.4x	1.2x	1.5x	1.5x	1.7x	1.6x
Income-Equity Dividend Coverage Ratio	1.3x	1.4x	1.5x	1.3x	1.3x	1.3x	1.3x	1.5x	1.9x	2.3x	2.2x
Income-Equity Net Debt/EBITDA***	2.2x	2.4x	2.5x	2.6x	4.2x	2.8x	2.0x	1.9x	1.4x	1.9x	1.6x
Income-Equity P/E Ratio Trailing	13.4	13.3	14.1	13.4	16.4	14.2	17.2	17.7	12.6	12.8	12.5
S&P 500 P/E Trailing	15.4	13.4	14.4	17.4	18.4	18.8	20.5	21.7	16.5	21.6	22.2
Premium/Discount	-13%	-1%	-2%	-23%	-10%	-24%	-16%	-18%	-23%	-41%	-44%

### Income-Equity Strategy (No MLPs)

	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2Q2020
Income-Equity (No MLPs) Yield	4.9	5.0	4.7	4.1	4.0	4.6	3.9	3.7	4.2	3.6	4.1
S&P 500 Yield	1.9	2.1	2.2	1.9	2.0	2.2	2.1	1.9	2.2	1.9	1.9
Ratio	2.6x	2.4x	2.1x	2.2x	2.1x	2.1x	1.9x	2.0x	2.0x	2.0x	2.2x
Income-Equity (No MLPs) Projected Dividend Growth*	6.3	7.0	7.6	8.2	7.7	5.9	5.0	6.4	7.9	7.5	4.0
S&P 500 Projected Dividend Growth**	5.8	5.9	5.1	5.9	4.7	4.2	4.0	4.2	5.2	4.2	2.6
Ratio	1.1x	1.2x	1.5x	1.4x	1.6x	1.4x	1.2x	1.5x	1.5x	1.8x	1.6x
Income-Equity (No MLPs) Dividend Coverage Ratio	1.6x	1.4x	1.4x	1.3x	1.3x	1.3x	1.3x	1.5x	1.9x	2.3x	2.2x
Income-Equity (No MLPs) Net Debt/EBITDA***	2.1x	2.4x	2.5x	2.7x	2.6x	2.6x	2.2x	2.1x	1.4x	1.9x	1.6x
Income-Equity (No MLPs) P/E Ratio Trailing	13.2	13.5	14.5	14.6	17.2	16.5	18.2	18.0	12.9	13.5	12.7
S&P 500 P/E Trailing	15.4	13.4	14.4	17.4	18.4	18.8	20.5	21.7	16.5	21.6	22.2
Premium/Discount	-14%	0%	1%	-16%	-6%	-12%	-12%	-17%	-22%	-38%	-43%

Source: Bloomberg; S&P 500; Miller/Howard Research & Analysis. The data above is based on representative accounts in our Income-Equity Strategies both with and without MLPs and is subject to change.

\* Projected Dividend Growth—Miller/Howard Portfolio Team's 3-year annualized projected dividend growth based on data from various sources, adjusted to reflect our view of future economic and market conditions. There is no assurance projections will be realized.

\*\* Bloomberg Dividend per Share 3-year forward estimates.

\*\*\* Excludes financials.

Dividend yields shown for Miller/Howard portfolios exclude cash.

All data is as of year-end, unless otherwise noted.

**Common stocks do not assure dividend payments.** Dividends are paid only when declared by an issuer's board of directors, and the amount of any dividend may vary over time. Dividend yield is one component of performance and should not be the only consideration for investment. See definitions and full disclosure on page 12.

# Our Focus is Risk Reduction in Our Investments & Sustainable Income Opportunities™ for Our Clients.

## OUR ESG AND PORTFOLIO MANAGEMENT TEAMS WORK TOGETHER

We seek to gain the fullest possible understanding of companies held in, or under consideration for our portfolios, by working collectively. We see how each company manages its ESG assets and opportunities and apply a materiality lens, looking for issues that have the greatest potential to impact the company now and in the future.

### ESG insights inform our investment decisions, with recent examples including:

- **Opportunities Identified:** We expect renewable energy to play a larger role going forward, so when we identified a utility company that presented an opportunity to increase our exposure to renewable energy, we bought the stock.
- **Position Sold:** An industrial company's auditor found a "material weakness" in its financial controls, and we subsequently sold the stock.
- **Weights Adjusted:** We exited our position in one energy company and increased our position in another, citing corporate governance as among the key reasons for the trades. The company we sold had executive compensation practices that we believe are misaligned with minority shareholder interests. We reallocated and increased the weight in an energy company that provides exposure to substantially similar assets but has, we believe, a better corporate culture and a cleaner balance sheet.

A company's management of human, financial, and natural resources contains within it the seeds of possible success or failure. And now, in a time of a global pandemic, this lesson has even more relevance.

Miller/Howard has spent nearly thirty years working with companies to improve their operations and impact, and we will continue to work on behalf of our clients to offer *Sustainable Income Opportunities*.™

See our *Shareholder Advocacy Newsletters and Engagement Report (Summer 2020)*, available on our website.

This report represents Miller/Howard Investments' views. The statistics and projections cited in this report have been provided by sources generally considered to be reliable, but are not guaranteed. Opinions and estimates offered constitute Miller/Howard Investments' judgment and are subject to change without notice, as are statements of financial market trends, which are based on current market conditions. This material is solely informational. The information and analyses contained herein are not intended as tax, legal, or investment advice and may not be appropriate for your specific circumstances; accordingly, you should consult your own tax, legal, investment, or other advisors, at both the outset of any transaction and on an ongoing basis, to determine such appropriateness. The material may also contain forward-looking statements that involve risk and uncertainty, and there is no guarantee they will come to pass. **Any investment returns—past, hypothetical, or otherwise—are not indicative of future performance.** The information provided should not be considered a recommendation to buy or sell any security, and should not be considered investment, legal, or tax advice.

Securities mentioned are being shown for informational purposes only. Buy and sell rationales are the express opinions of MHI's investment team. These securities should not be considered a recommendation to buy, sell, or hold any of the securities and are not intended to imply that any one security listed above, or the portfolio as a whole, is suitable for a particular client. There is no assurance that the securities purchased have remained or will remain in the portfolio or that securities sold have not been or will not be repurchased.

**Common stocks do not assure dividend payments.** Dividends are paid only when declared by an issuer's board of directors, and the amount of any dividend may vary over time. Dividend yield is one component of performance and should not be the only consideration for investment.

#### DEFINITIONS

**Earnings Before Interest, Taxes, Depreciation, and Amortization (EBITDA)**—A non-GAAP measure used to provide an approximation of a company's profitability. This measure excludes the potential distortion that accounting and financing rules may have on a company's earnings; therefore, EBITDA is a useful tool when comparing companies that incur large amounts of depreciation expense because it excludes these noncash items, which could understate the company's true performance.

**EPS**—Earnings Per Share

**Net Debt to EBITDA**—A measure that computes the company's ability to pay off its debt by utilizing the earnings before interest, taxes, depreciation, and amortization (EBITDA).

**Price-Earnings Ratio (P/E)**—The ratio of a company's share price to its earnings per share. The ratio is used as a valuation tool and can help determine whether a company is overvalued or undervalued.

**T&D**—Transmission & Distribution

**Notification to Clients:** Contact your Advisor with any material changes to your financial profile that would impact your appropriateness for investment.

