VIEWS FROM THE
EQUITY INCOME TEAM

Dynamic Global Infrastructure Fund

July 6, 2023

Q2 Portfolio Review

In 2023 infrastructure earnings have been fairly healthy on balance, and the sub-sector experience will be discussed in more detail below. Despite this the markets continue to be hesitant to embrace capital intensive sectors given the rise in interest rates, especially those that require external financing to meet their growth potential. Furthermore, investors are likely looking to the safety of risk-free investments as a substitute for defensive equities like infrastructure given the interest rates on offer and seem to be ignoring the yield + growth potential in the infrastructure space. On top of sustainable dividends and earnings growth, the third leg of the total return stool, valuations, have also come back to be in-line with long-term historical levels for infrastructure stocks, which can be seen in the growth and valuation table at the end of this commentary.

The narrative on the big picture continues to be inflation is cooling, along with the economy, and the guessing game involving central bank interest rate hikes or cuts continues. Cost inflation pressures are easing, as are supply conditions and logistics, while credit conditions are tighter but stable. We see this as both a push and pull on the infrastructure sector, as project execution risks have calmed down, yet financing costs have gone up. The net effect is likely a bit of a haircut to near-term earnings growth, say 0.5%-1.0%, but no impact on the longer term growth potential. We expect the pricing power of infrastructure businesses and necessity of growth investments to align future project returns with the higher financing cost conditions that are likely here to stay.

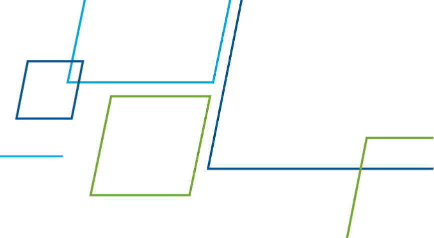
We summarize the changes made in Dynamic Global Infrastructure Fund (the "Fund") over the first half of the calendar 2023 year below:

	Asset Mix (%)		
	Q223	Q123	Q422
Airports	8.7	9.3	8.4
Toll Roads	8.4	9.7	9.4
Rails	9.7	7.4	6.2
Regulated	37.1	37.6	34.9
Water	2.9	3.2	2.2
Data	3.1	3.0	2.6
Renewables	14.3	13.1	18.1
Pipelines	9.3	7.3	1.4
Diversified	4.0	3.6	4.9
Cash	2.6	5.7	11.8
Total	**100.0**	**100.0**	**100.0**

	Currency Hedging		
	Q223	Q123	Q422
AUD	50%	69%	75%
CHF	73%	73%	81%
DKK	50%	---	87%
EUR	86%	84%	89%
GBP	51%	80%	84%
USD	49%	68%	69%

Source: Dynamic Funds as of June 30/23

- We have brought the pipeline and rail weights much closer to a target sector weight, taking advantage of price corrections during the first half of 2023.

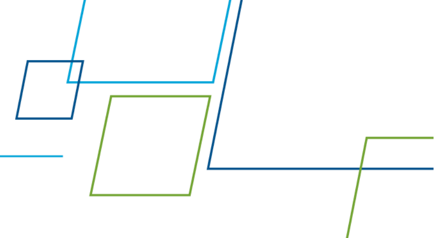


- We added to regulated utilities, primarily international, but also to higher quality U.S. utilities as conditions in Europe stabilized after a tumultuous 2022, and valuations became quite reasonable for higher quality regulated utilities, in both the electric and water sectors.
- Early in the year we reduced exposure to renewable power although we modestly added back at better valuation levels. On net, the exposure is lower compared to the beginning of the year.
- We took some modest profits in the airport and toll road sectors at times when valuations looked to be discounting a more than reasonable traffic recovery expectation in the near term. We remain very constructive on these sectors over the long-term as they possess unique inflation protected exposure to global GDP growth.
- Based on the above cash has come down from over 11% at year-end 2022 to just under 3% at the end of June 2023.
- We have changed our target foreign currency hedge ratio to 50% from 70%, as we felt it appropriate to carry a higher unhedged exposure to USD as a natural shock absorber to sudden risk off conditions. This has resulted in about 1/3rd of the Fund exposed to foreign currency fluctuations, up from 10%-20% under the previous target. The vast majority of this exposure is to USD.

What Has (and Has Not) Worked in 1H23

- Airports and toll roads have delivered very good results as mobility improved dramatically and consumption of travel and leisure continues to recover back to pre-pandemic levels. In Europe, where most of the sector exposure to these two areas resides, stocks have performed well this year as the continent escaped the potentially severe impact of the war-induced energy crisis last year.
- Renewable power and data infrastructure stocks performed poorly. The data infrastructure sector exposure has been well below target weight this year as valuations continued to be mis-aligned with the current interest rate environment. There is also a fair amount of debt on the balance sheets for these stocks. In renewables, investors continue to be cautious due to the higher financing costs and capital expenditure levels seen in this sector. In both sectors valuations look to have normalized, while financing costs and conditions look to have stabilized.
- Rails have produced an expected result so far this year, with resilient pricing power and strong free cash flow offsetting weak volumes. We also believe we added to exposure at very attractive prices, and our preference remains to be mostly exposed to U.S. rails due to the better valuations and equally attractive benefit available to increased onshoring of manufacturing to North America.
- Regulated utilities and pipelines have treaded water so far this year. In the case of utilities a weak start to the year due to poor weather conditions, higher competition from risk free interest rates, and a general aversion to high-capex investments in the market have created headwinds. Offsetting this is a steady long term growth outlook of mid-to-high single digits and sustainable dividend yields between 3.5% and 4.0%. Pipelines have come off the boil from last year and look to be consolidating, and underneath the surface are delivering high single digit sustainable dividend yields with low-single digit growth potential. They also have some correlation to energy commodities, which have sold off this year.

We conclude with the summary of historical and prospective growth expectations of the infrastructure investments in the Fund, along with the valuation summary below. The steady earnings growth expectations are driven by long-term investment in energy, water and data infrastructure while the valuations have compressed significantly since the pre-pandemic peak to long-term historical average levels. We do not know exactly when dividend yields + growth will begin to outweigh the headwind of the multiple contraction, although a stabilization of interest rates and credit conditions is likely the first step needed.



Sector	Dividend Yield	Pre-Pandemic Cycle Average Annual Earnings Growth 19/09	During the Pandemic Average Annual Earnings Growth 21/19	Post-Pandemic Cycle Average Annual Earnings Growth 26/22	Valuation Multiple 19	Valuation Multiple 23	Valuation Multiple 24	Valuation Multiple 10-Year Med.	Valuation Multiple LT-MED
AIRPORTS	0.0%	8%	-39%	35%	11.5	10.5	9.6	11.5	10.8
TOWERS	3.8%	8%	6%	7%	20.8	16.7	15.8	17.2	15.5
PIPELINES	7.0%	7%	2%	4%	21.1	17.1	16.9	19.3	18.1
RAILS	2.3%	21%	5%	8%	19.2	18.3	16.8	18.6	15.0
RENEWABLES	5.0%	10%	11%	10%	18.1	14.2	12.3	14.4	14.3
TOLL ROADS	3.8%	11%	-8%	8%	18.5	17.5	15.8	15.7	15.0
REGULATED UTILITIES	3.5%	7%	4%	7%	23.3	16.8	15.8	17.2	15.5
FUND	**3.8%**	**8%**	**4%**	**7%**	**20.7**	**16.3**	**15.3**	**17.0**	**15.5**

Source: Bloomberg as of July 4, 2023
Earnings = EBITDA for airports and toll roads and renewables, AFFO for towers, and EPS for rails, pipelines, and regulated utilities.
The above is a simply average, not weighted average.
Valuation Multiple LT-Median is based on 30 years, as long as the historical data is available, or as long as the stock has been listed.

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