Will Inflation Ruin Your Retirement?

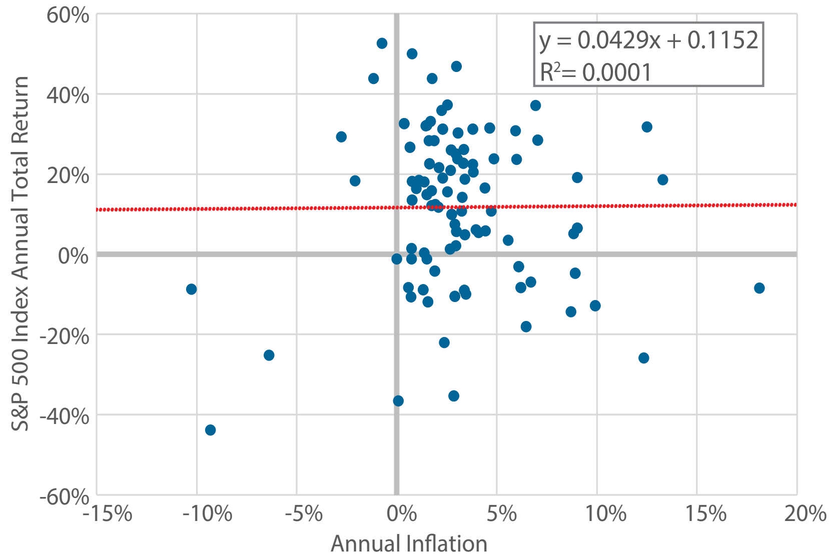
SEPTEMBER 30, 2024

WHAT IF YOUR HARD-EARNED DOLLARS ARE not worth as much in retirement? Depending solely on investments to meet spending needs can be a daunting challenge when *both* spending and investment returns are hard to forecast. The spike in inflation in the last few years has heightened client concerns over whether their savings will be enough to support their retirement plans.

Conventional wisdom says that stocks are immune to inflation—prices go up, costs go up, corporate profits go up…what's the problem? As plausible as this may sound to the theoretically minded, actual inflation and investment returns over the past century do not support the notion that inflation is somehow magically passed on in equity returns. The correlation between inflation and equity market returns has been basically nil. Years with elevated inflation have had both high and low stock market returns—we see no evidence that stock market returns neutralize inflation.

Given the threat of inflation, how should we think about engineering our investments so that we can balance high returns versus the risk of running out of money during retirement? Sometimes clients frame the problem in an overly negative fashion, effectively asking how they can cope if inflation goes up forever while stock prices go down forever. Bad outcomes may be looming, but our view is that the past century has provided plenty of negative scenarios to battle test our investment plans. This period includes the horrible equity market returns in the Great Depression, spiking inflation after World War II and again in the 1970s, and an assortment of bull and bear markets. Rather than conjuring up implausibly negative scenarios, let's examine how alternative retirement strategies would have fared given the real-life vicissitudes of the past century.

Virtually No Relationship Between Market Returns and Inflation



As of December 31, 2023.
Data range: 1928-2023.
Sources: Morningstar Direct; Federal Reserve Bank of St. Louis.
Inflation is the year-over-year change of the Consumer Price Index for All Urban Consumers (CPI Index).
Red dotted line= trend line.

WHICH ASSET ALLOCATIONS DO BEST IN RETIREMENT?

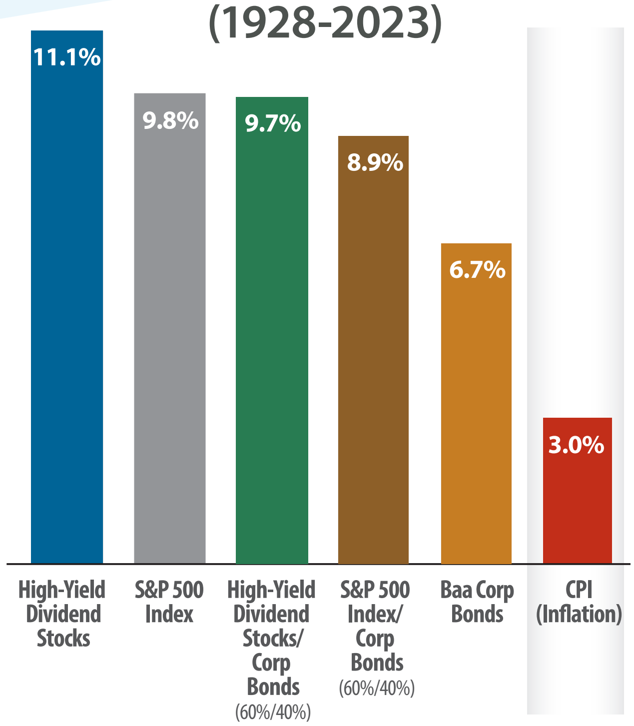
To answer this question, we compiled investment returns for the S&P 500 Index, high-yield dividend stocks (stocks in deciles 7, 8, & 9 as provided by Fama/French), and corporate bonds (dating back to 1928, the earliest shared date across our sourced datasets). Using these historical returns, we simulated 67 30-year retirements, starting from 1928-1957 (all ranges are inclusive), 1929-1958, and so on through 1994-2023. We use the "4% rule" to model spending in retirement, with the retiree spending 4% of savings in the first year of retirement and then growing spending by the rate of inflation.

Our first conclusion is that depending solely on corporate bonds during retirement has a high risk of failure, defined as running out of money prior to 30 years of retirement. In our simulations, retirees using just corporate bonds failed in 30 of the 67 periods. In another 16 of the 67 periods, retirees ended the 30-year retirement with investments worth less than their starting point on an inflation-adjusted basis.

Why do bond-only strategies perform so poorly in this exercise? First, the average return for corporate bonds from 1928-2023 was only 6.7%. This may not sound bad, but we are trying to cover 4% withdrawals plus inflation, which averaged 3% over the period. Bond returns were frequently not high enough to cover inflation-adjusted spending.

The second observation on bonds is that the last failure was the 30-year period beginning in 1967. Bond returns generally fall when interest rates rise, as they did in the decades before rates peaked in 1981. In recent decades, bond-only portfolios have been successful in meeting the 4% plus inflation bogey. Yet we believe, this should not give anyone confidence in a bond-only strategy. Given the threat of inflation and the low starting point for interest rates, in our view, it's unlikely that interest rates will trend down over the next three decades. If long-term interest rates grind higher (as they did from 1941-1981) or remain roughly flat, retirees depending only on bonds will run a high risk of failure.

Annualized Returns vs. Inflation (1928-2023)



As of December 31, 2023. Sources: Morningstar Direct; Federal Reserve Bank of St. Louis (FRED); Fama/French; Damodaran Historical Returns US (NYU Stern School of Business). High-Yield Dividend Stocks=total return reflects a basket of the returns for deciles 7, 8, & 9 as provided by Fama/French (value weighted). Inflation is the year-over-year change of the Consumer Price Index for All Urban Consumers (CPI Index). Baa Corp Bond returns are calculated by Damodaran dataset using Moody's Seasoned Baa Corporate Bond Yield (BAA), retrieved from FRED. 60/40 portfolios are rebalanced annually.

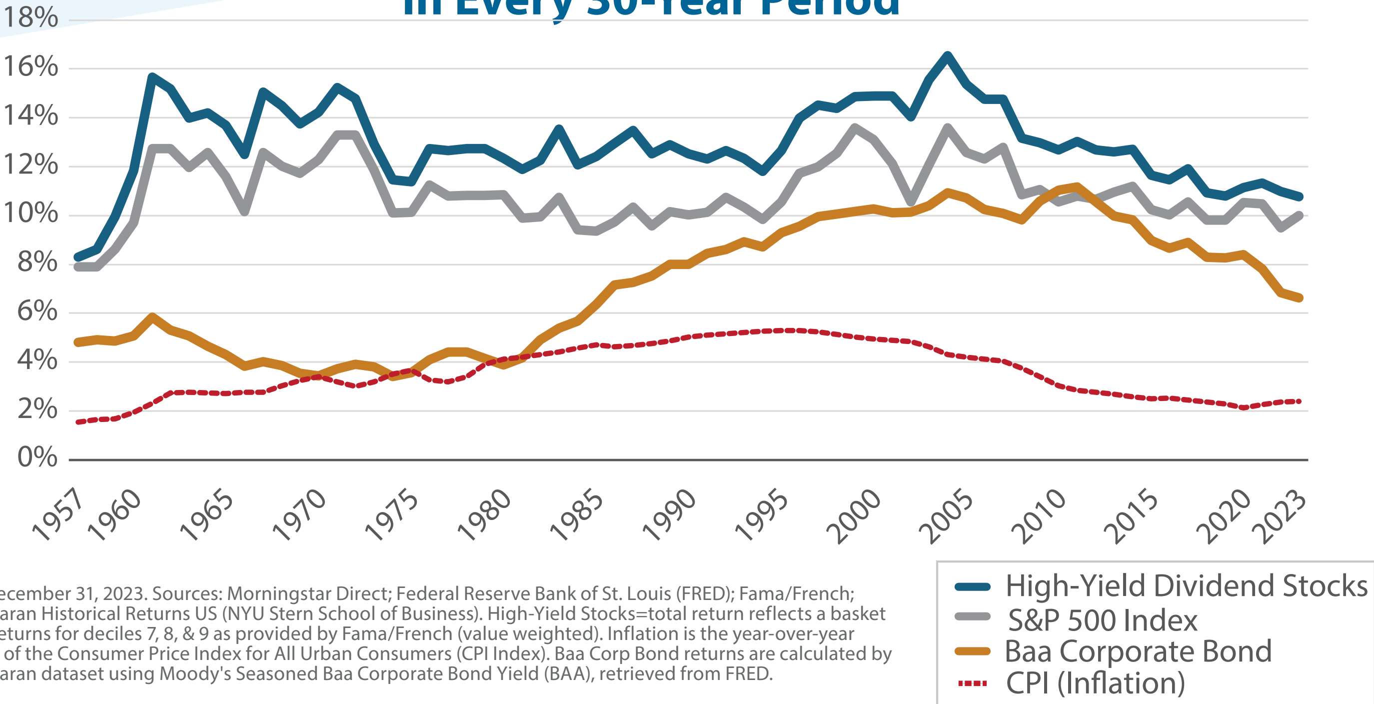
Bond-Only Portfolios Frequently Lead to Failure

30-Year Retirements with Inflation Adjusted 4% Annual Withdrawal

	Baa Corporate Bond	High-Yield Dividend Stocks	S&P 500 Index	High-Yield Dividend Stocks/ Corp Bond (60%/40%)	S&P 500 Index/ Corp Bond (60%/40%)
Failure	30	1	5	0	1
Reduced Ending Estate	16	2	6	3	16
Higher Ending Estate	21	64	56	64	50

As of December 31, 2023. Sources: Morningstar Direct; Federal Reserve Bank of St. Louis (FRED); Fama/French; Damodaran Historical Returns US (NYU Stern School of Business). High-Yield Stocks=total return reflects a basket of the returns for deciles 7, 8, & 9 as provided by Fama/French (value weighted). Inflation is the year-over-year change of the Consumer Price Index for All Urban Consumers (CPI Index). Baa Corp Bond returns are calculated from Damodaran dataset using Moody's Seasoned Baa Corporate Bond Yield (BAA), retrieved from FRED. "Reduced Ending Estate" and "Higher Ending Estate" starting values are post inflation adjusted withdrawal versus initial retirement account. 60%/40% portfolios are rebalanced annually.

High-Yield Dividend Equities Outperformed S&P 500 in Every 30-Year Period



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Based on our simulations, equity-based retirement strategies have a much higher likelihood of success than bond-based approaches. Allocating all funds to the S&P 500 resulted in successful retirements in 62 out of 67 30-year periods, with the resulting estate typically being ahead of the starting retirement account on an inflation-adjusted basis. High-yield dividend stocks fared even better, with retirees running out of money in only 1 out of 67 30-year periods. With high-yield dividend equities, the ending estate was worth more than the starting value, adjusted for inflation, in 64 out of 67 periods.

High-yield dividend stocks had a higher success rate than the S&P 500 in large part because high-yield dividend stocks had higher average total returns in every 30-year period between 1928-2023. Most importantly, high-yield dividend stocks held up better for retirees hit by high inflation in the 1973-81 period. In contrast to high-yield dividend stocks, average returns for the S&P 500 softened during and following this high-inflation period, just when retirees needed better performance to deal with elevated living expenses.

Success Rate was Higher for High-Yield Stocks than S&P 500 Index

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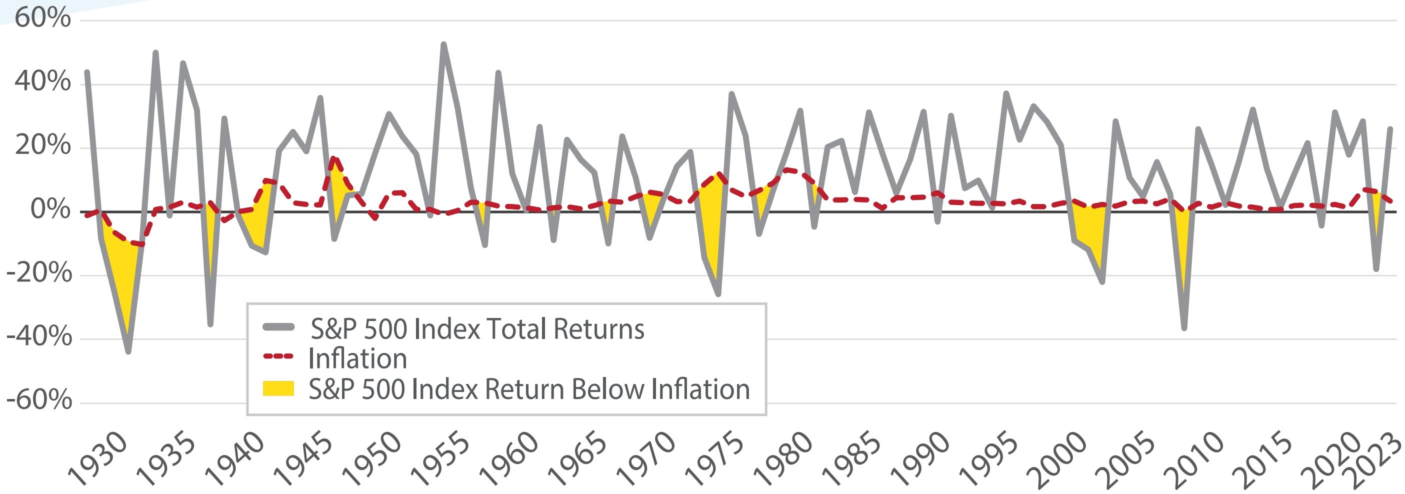
Market Returns Periodically Trail Inflation



As of December 31, 2023. Sources: Damodaran Historical Returns US (NYU Stern School of Business); Federal Reserve Bank of St. Louis. Inflation is the year-over-year change of the Consumer Price Index for All Urban Consumers (CPI Index).

Prior to retirement, buy-and-hold investors can ride through bad markets without selling. Investing during retirement is fundamentally different—spending continues regardless of how investments are faring. Rather than buy low/sell high, retirees are forced to sell at low prices during bad markets to fund spending. This can be particularly stressful when investment returns trail inflation for multiple year periods.

Using the classic 60%/40% stock/bond strategy is one way for retirees to avoid selling low. The key to the 60/40 stock/bond strategy is regular rebalancing—when stocks zoom up, you sell stocks and buy bonds to get back to 60/40. More importantly, when stocks fall, the retiree sells bonds and buys stocks at low prices. Overall, the 60/40 strategy reduces average returns because bonds are a lower returning asset class. But the key point is that returns are smoothed, reducing the chance that a bad streak in the equity market shrinks the investment account below the level required for spending. For both high-yield dividend stocks and the S&P 500, employing a 60/40 strategy reduced the frequency of failed retirements. The high-yield dividend stock/corporate bond 60/40 strategy did not have any failures during the 1928-2023 period.

60/40 Portfolios Have Low Failure Rates

30-Year Retirements with Inflation Adjusted 4% Annual Withdrawal

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Each of us get just one retirement, so being told "on average" everything will be fine is not great comfort. Let's examine the retirement failures in our simulations to see what we can learn. Setting aside the large number of failures associated with bond-only strategies, we saw five failures using the S&P 500, one using high-yield dividend stocks, and one using a 60/40 S&P 500/bond allocation. The seven failures using equity or equity/bond strategies all shared one of two time periods:

Great Depression Stock Market

The S&P 500 allocation failed when beginning in 1929 or 1930 and high-yield dividend stocks failed when starting in 1929. The stock market fell for four straight years beginning in 1929, down a cumulative 65%, providing a real pressure test for any retirement plan. ***What can we learn?***

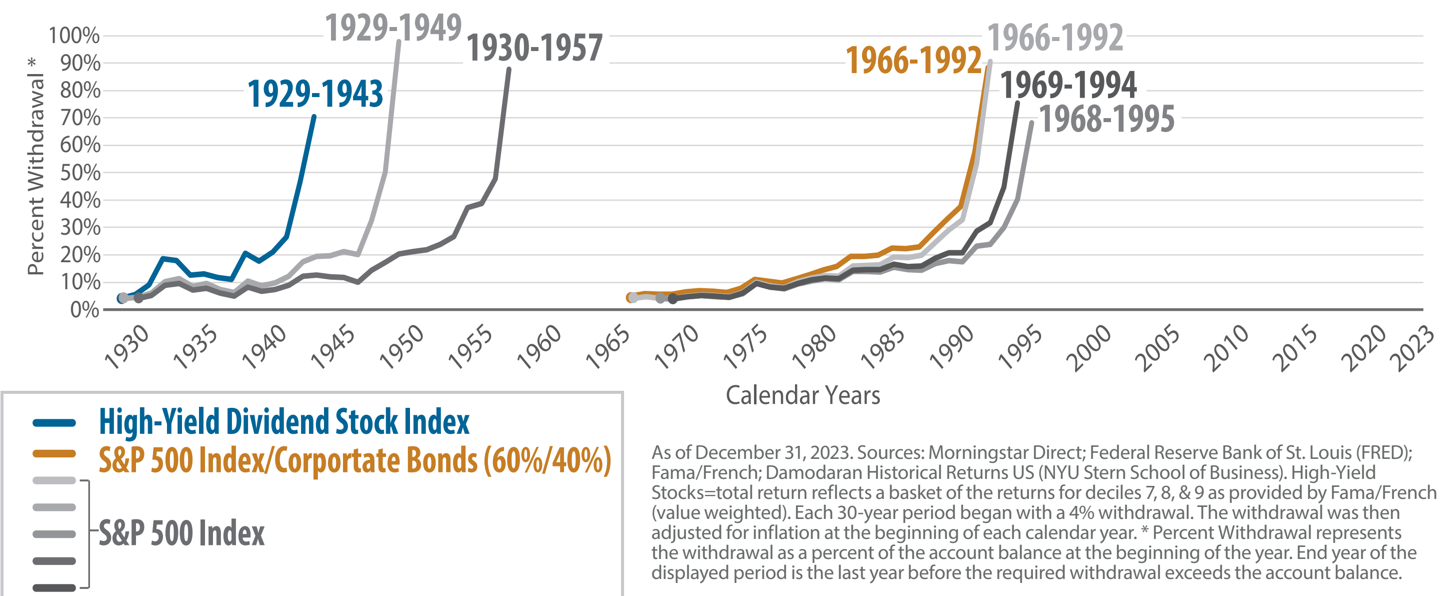
- None of the 60/40 strategies failed in this period. Investors using these strategies would have allocated more to equities as stocks fell, thus benefitting more from the eventual rallies.
- Retirement simulations beginning in 1928 (when the market was up 44%) did not fail. Failures occurred when the market fell immediately following retirement and continued for multiple years.
- Even with the steep market drop, the failed retirements beginning in 1929 were still able to maintain their spending plans into the mid-1940s. Low investment returns combined with inflation spikes in the early/mid-1940s pushed these accounts into a downward spiral with spending racing ahead of investment returns.

1973-1981 High Inflation

Between 1973-1981, inflation averaged 9.2% while the S&P 500's annualized return was only 5.3%, putting a great strain on those who retired in the late 1960s. In our simulations, retirements using the S&P 500 beginning in 1966, 1968, and 1969 failed. In addition, retirements using a 60/40 S&P 500/bond strategy beginning in 1966 also failed. Here's what we can conclude from the period:

- Strategies using high-yield dividend stocks did not fail in this period. Between 1973-1981, high-yield dividend stock returns averaged 10.7%, allowing retirees to stay ahead of inflation.
- Inflation can indeed ruin a retirement. Even when the rate of inflation moderated in the 1980s, prices facing consumers were permanently higher. For the four S&P 500-based failures, this meant that withdrawal rates rose to double-digit rates, eventually draining accounts in the tepid early 1990s stock market.

Failure Simulations: Low Returns and High Inflation Cause Spending to Exhaust Savings (1928-2023)



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It's completely understandable that clients' questions tend towards worst case scenarios—everyone wants to enjoy retirement free of worry. Many clients have the intuition that relying on bonds during retirement is the sensible, low-risk solution. Unfortunately, the truth is that bonds frequently have not generated enough return to stay ahead of inflation. The other solution that appeals to some clients is to just buy and hold the S&P 500 or some other market-cap-weighted index. The success rate for the S&P 500 in our simulations was much higher than for bonds, but it still had five failures in the 67 30-year periods we examined. In our experience, many clients will find this failure rate to be too high.

Using high-yield dividend equities or a 60/40 S&P 500/corporate bond strategy each had just one failure in the 67 30-year periods. The simulation using 60/40 high-yield dividend stocks/corporate bonds did not have a single failure. These calculations are based just on historical investment returns, inflation rates and the well-known 4% spending rule. In our opinion, there are two reasons why high-yield dividend stocks and 60/40 strategies were better at avoiding failure than bonds or the S&P 500:

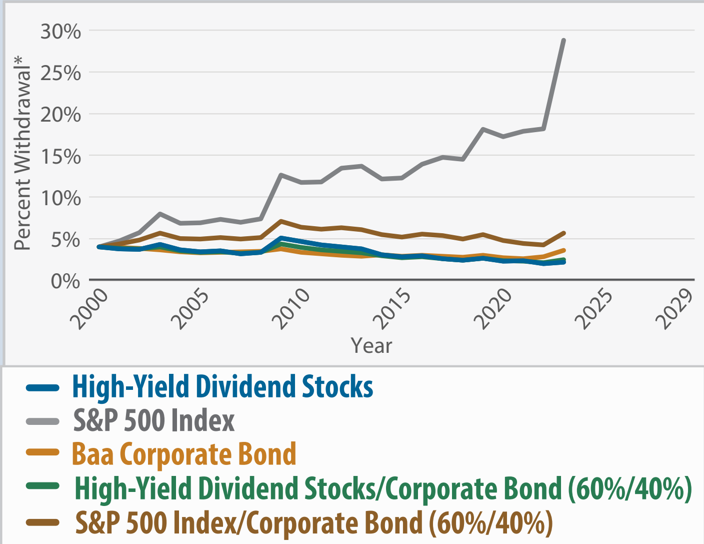
1. The best strategies had high enough returns to stay ahead of inflation. Bonds have lower volatility, but, in our view, the sacrifice of returns is too great, making the strategy vulnerable to bouts of inflation.
2. High-yield dividend stocks and 60/40 allocations are "buy low/sell high" strategies. Stock prices are more volatile than dividends, so appreciating stocks can fall out of the high-yield dividend category while stocks with falling prices can join it. When the high-yield dividend category is reconstituted (annually in our calculations), investors are effectively buying low and selling high. The same is true with the 60/40 strategies. In contrast, the S&P 500 is market-cap-weighted, so is truly a "buy and hold" strategy that does not take advantage of price fluctuations.

Recent Challenge: 2000 Retirement

The crash of the tech bubble in 2000 followed by the Great Financial Crisis in 2008 provides the most recent stress test. We won't reach the 30-year mark until the end of 2029, but it seems clear how our simulation for a retirement beginning in 2000 will fare—withdrawal rates in the mid-single digits for high-yield dividend stocks, the 60/40 strategies and bonds all bode well for a retirement that is in its third decade.

In contrast, a retirement using only the S&P 500 would have floundered. The S&P 500 fell by a cumulative 37% during 2000-2002, pushing withdrawal rates up to meet spending needs. Poor returns in 2008 propelled the withdrawal rate above 10%. Sometimes high market returns and low inflation can save retirements with high withdrawal rates, but bad times reappeared—high inflation and the S&P 500 falling 19% in 2022 sent the 2023 withdrawal rate to 29%, almost surely on the road to failure.

Market Downturns and High Inflation Can Cause Withdrawal Rates to Spike



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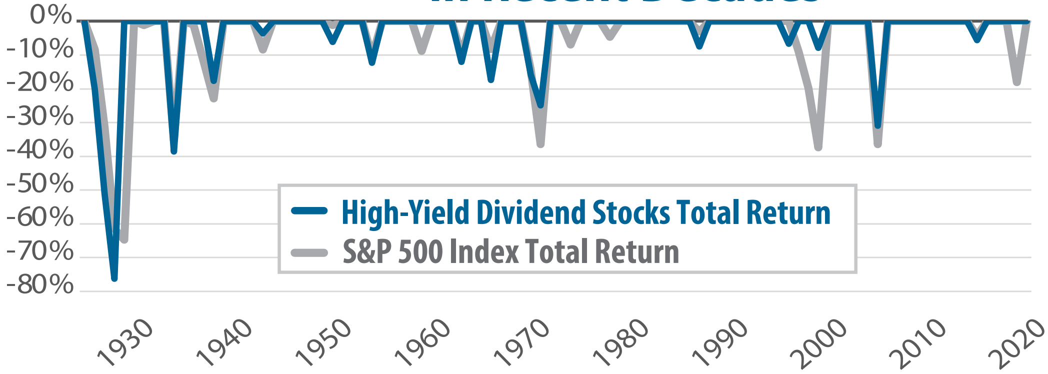
High-Yield Equities had Lower Drawdowns in Recent Decades



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During saving years, investors following the adage that 'time in the market is better than timing the market' will tilt towards equities as the highest-returning asset class. The same logic applies to retirement years—but with a twist. Spending in retirement complicates the issue because severe drawdowns might lead to an empty account. Another layer of complication comes from inflation which has returned episodically with no reliable pass-through to equity returns. The best retirement plan will have plenty of "time in the market" with high-returning assets but must be able to survive severe drawdowns and bursts of inflation.

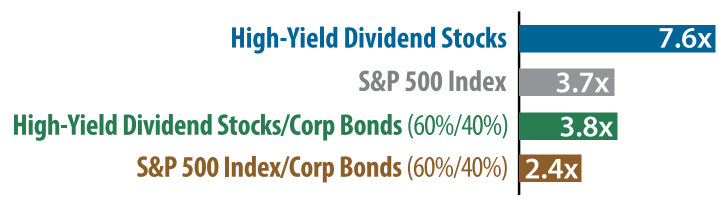
During the 1928-2023 period:

- High-yield dividend equities had the highest return for every 30-year period.
- Both high-yield dividend equities and the S&P 500 had severe drawdowns at the outset of the Great Depression. On average, high-yield dividend equities had smaller drawdowns than the S&P 500 over the past 80 years.
- Using all high-yield dividend equities only failed when retirement started in 1929—otherwise returns were high enough to stave off inflation.
- Allocating only to the S&P 500 resulted in failure for two starting dates in the Great Depression and three starting dates in the 1960s. Additionally, an all-S&P 500 retirement starting in 2000 is not performing well in our simulation.
- A 60/40 strategy using high-yield dividend equities and corporate bonds had no failures, but resulted in a lower ending account balance.

In choosing between an all-equity strategy and a stock/bond mix, retirees need to judge whether we could ever have another period like the Great Depression. View another Great Depression as a distinct possibility? Then some mix of high-yield dividend stocks and corporate bonds with periodic rebalancing is the right strategy, in our opinion. If you trust the Fed to halt any spiral towards a repeat of the 1930s (arguably as they did in the pandemic) then a 100% high-yield dividend equity allocation would make sense.

We have rightly focused here on avoiding tail risk, but what will successful retirements look like using equity and 60/40 strategies? For our successful retirement simulations, withdrawal rates averaged well below 5% for 30 years. For high-yield dividend equities, the average withdrawal rate is just above 1% after 30 years, meaning that investment returns have typically galloped well ahead of inflation-adjusted spending. The investment account left at the end of 30 years is typically a multiple of the starting amount *even adjusted for inflation.* For high-yield dividend equities, the average ending account balance is 7.6 times the starting amount adjusted for inflation. Those pondering retirement can conclude that they can possibly spend more or that they will likely leave a handsome estate. Either way, the key point is that high-yield dividend equities have typically generated high enough returns to prevent inflation from ruining a well-deserved retirement.

Ratio of Inflation Adjusted Estate vs. Initial Investment



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Income-Equity

QUARTERLY REPORT 3Q 2024

MARKET BROADENS

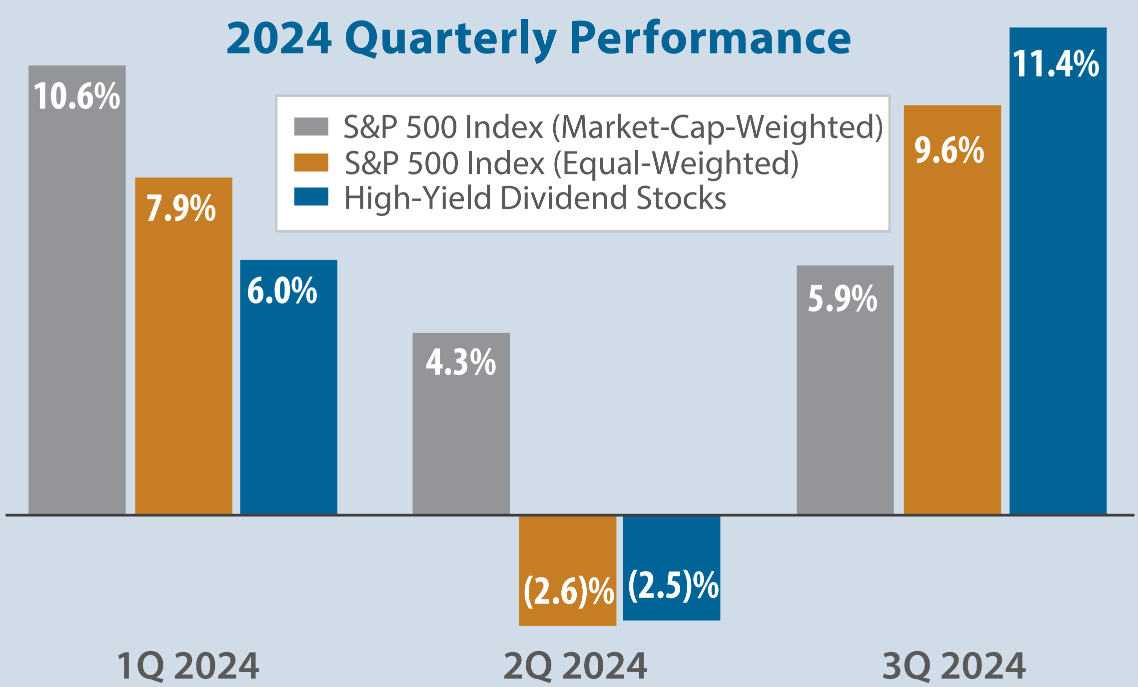
Big, bigger, even bigger. Has it ended? During 2023 and the first two quarters of 2024, the very largest companies outran the rest of the market, resulting in a narrow set of stocks driving returns for the broad market.

In our Quarterly Report for 1Q 2024, entitled "Dividend Investing: Requiem or Revival?", we argued that the historic outperformance of high-yield dividend stocks (stocks in deciles 7, 8, & 9 as provided by Fama/French) would likely resume once markets broadened. The first three quarters in 2024 provide a good test of our thinking. Our preferred measure of market breadth is the spread between the market-cap-weighted S&P 500 Index total return and the equal-weighted S&P 500—same stocks, just different weights. As in 2023, the market-cap-weighted S&P 500 outperformed the equal-weighted version in the first and second quarter, and consistent with our argument, high-yield dividend stocks lagged the broad market. In contrast, the equal-weighted S&P 500 outperformed the market-cap-weighted version in the third quarter, leading to outperformance of high-yield dividend stocks as predicted.

The relationship between market breadth and the performance of high-yield dividend stocks is explained by the historical observation that bouts of market concentration have been driven by swelling price-to-earnings ratios (P/E). Paying a high but well-covered dividend is impossible with a high price-to-earnings multiple. For example, a company trading at 50x earnings with a 50% payout ratio will only yield 1%. High P/Es are not compatible with

Portfolio Highlights

- **Dividend increases:** Income-Equity (no MLPs) had 7 dividend increases in the quarter, including **Bank of New York Mellon (BK), Goldman Sachs (GS), Bank of America (BAC), Lamar Advertising (LAMR), JP Morgan Chase (JPM), Texas Instruments (TXN),** and **OGE Energy (OGE).** Income-Equity (with MLPs) had the same 7 increases plus an 8th increaser, **Enterprise Products Partners (EPD).**
- **Exited positions:** We exited our position in **Cardinal Health (CAH).** Our investment thesis had largely played out, with margins recovering in their medical products distribution business. Going forward, they face challenges from the loss of a major contract.
- **New buys:** We initiated a position in **Entergy (ETR),** a regulated utility in the southeast that is benefitting from growing industrial investment along the Gulf Coast.



As of September 30, 2024. Sources: Bloomberg. High Yield Stocks (decile 7-decile 9) performance was created by creating a screen of active dividend paying common stocks, REITs, and ADRs traded on the NASDAQ and NYSE with indicated dividend yields in deciles 7 and 9, where 10 is the highest and 1 is the lowest, and with a market capitalization of $4 billion or greater. The resulting model was rebalanced monthly; returns are equal-weighted. Master Limited Partnerships (MLPs) were excluded from our screen. All performance is total return.

high dividend yields. A broadening of the market should shift the size effect from a headwind to a tailwind, in our opinion.

In the third quarter, our Income-Equity portfolios performed well above the S&P 500, and also slightly outpaced the Russell 1000 Value Index.

Looking Ahead

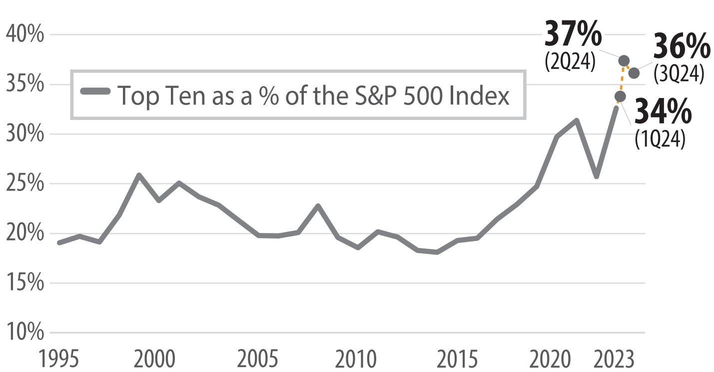
The market remains extremely concentrated relative to history. The path is unclear, but we believe that the market will eventually broaden further, benefiting high-yield stocks. A measure of concentration that most clients find intuitive is the combined market capitalization of the top 10 stocks as a percentage of S&P 500. The top 10 stocks of the S&P 500 hit a peak of 37% at the end of the second quarter before dropping to 36%, still well above the prior 30-year average of 22%.

Recent market concentration into the top 10 stocks has largely been driven by optimistic forecasts for artificial intelligence (AI). No doubt some excitement is warranted but the question is whether the stock prices account for the inherent uncertainty of AI's future. The poster child for the trend is Nvidia (NVDA – not held) which can legitimately tout high earnings growth. But its customers pay for their chips using profits from selling proven products such as smart phones, software, cloud computing, online retailing, online advertising and the like–not profits from AI-based businesses. There's a high hurdle for AI-based businesses to achieve profitability simply because AI requires massive spending. In our view, without actual evidence that AI can turbocharge corporate profitability, it would be unwise to continue to bid up the prices of stocks with AI halos.

A significant portion of the outperformance of large-cap stocks has come from multiple expansion. Aside from the Internet Bubble period, the price-to-earnings multiple for the equal-weighted S&P 500 has closely tracked the P/E of the market-cap-weighted S&P 500. In other words, the variance in P/E's across stocks usually reflects risks and growth prospects, but not mere size. Recently the price-to-earnings ratio for the market-cap-weighted S&P 500 has bulged to four turns above the equal-weighted S&P 500. This is a remarkable difference, not seen outside of the Internet Bubble period.

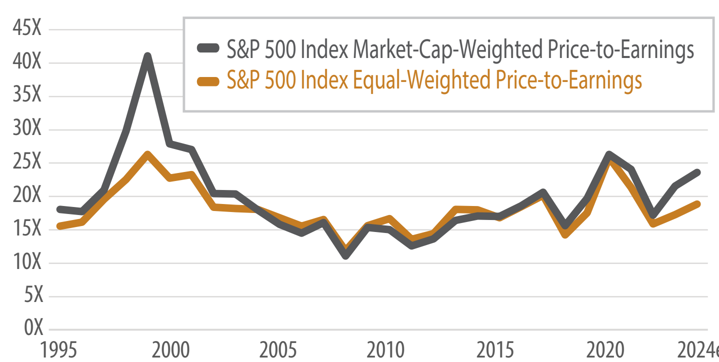
While the market did broaden this quarter, we view the large P/E spread as fuel for further broadening. As we discussed in our first quarter of 2024 Quarterly Report, over 10-year holding periods, the equal-weighted S&P has historically outperformed the market-cap-weighted S&P 500 75% of the time since 1980, so a broadening of the market would represent a return to a more normal market, likely benefiting high-yield dividend stocks, in our view.

Market Concentration Peaked in 2Q 2024



As of September 30, 2024. Sources: Bloomberg; Miller/Howard Research & Analysis. Note: We ran two screens for members of the S&P 500 Index by calendar year-end date. Members were ranked by market capitalization where 1 was the highest. The first screen was limited to the top 10 by market cap. The second screen was all other members. The total market cap of each selection period was used to calculate top ten percent totals. Stocks with multiple classes (e.g., Alphabet) were combined so as to include their market captilization once in the total sum.

Divergence in Price/Earnings Multiples Driven By Mega-Cap Concentration



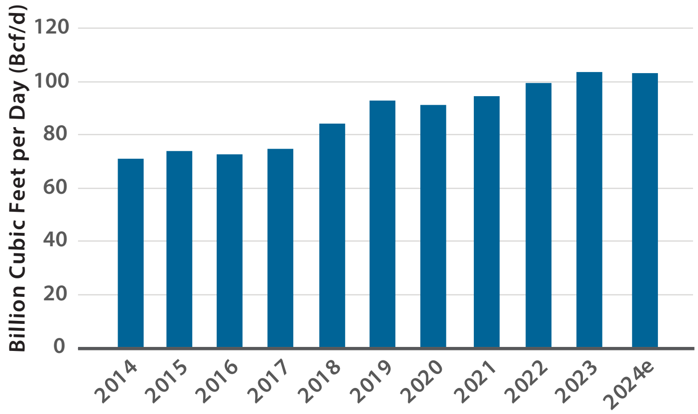
As of September 30, 2024. Sources: LSEG; Bloomberg; Miller/Howard Research & Analysis. Note: For years prior to 2010, equal-weighted S&P 500 Index price-to-earnings (P/E) was calculated as the aggregate of members equal-weighted positive trailing-12 month net income in relationship to the aggregate of their equal-weighted market capitilzation. For the market-cap-weighted S&P 500 Index, P/E was calculated as the aggregate of members value-weighted positive trailing-12 month net income in relationship to the aggregate of their value-weighted market capitilzation. P/E ratios above 100 were winsorized at 100x. All other years were sourced from Bloomberg.

MLP & MIDSTREAM ENERGY INCOME turned in another positive quarter and continues to better the overall market year-to-date. We see the sector as being driven by growth from several thematic tailwinds—longer-term natural gas demand growth, exports, and data centers—that we believe should increase volumes over the long term. In addition, midstream fundamentals and valuations remain favorable, in our opinion.

One tailwind is the mighty Permian. Production in the Permian (both oil and natural gas) continues to be strong. Along with higher production, wells are becoming gassier, resulting in more opportunities for the midstream sector to provide additional gathering, transportation, and processing infrastructure.

A second tailwind, and the one getting the most recent attention, is data centers. To date, there have been several new project announcements from midstream companies to service data centers, mainly in the US southeast. In our view, midstream natural gas companies should continue to benefit for years to come as there are estimates that data centers will require between 6 billion cubic feet per day (Bcf/d) and 10 Bcf/d of natural gas (slightly less than the demand coming from the next wave of liquefied natural gas projects). Putting an exact number on the potential buildout is difficult because there is not a clear picture of how much incremental demand is going to come from AI and data centers. But the recent announcements are encouraging, in our view.

US Natural Gas Production



Sources: US Energy Information Administration, Short-Term Energy Outlook, September 2024; Miller/Howard Research & Analysis.

A third tailwind for the sector, new liquefied natural gas (LNG) terminals should add approximately 12 Bcf/d of new natural gas demand in the coming years. As a reminder, the US produces slightly north of 100 Bcf/d of natural gas. By the end of the decade, new LNG terminals, re-shoring of manufacturing, EVs, electrification trends, and the data center buildout could add potential incremental demand of greater than 20 Bcf/d in total, in our view.

The last tailwind is shareholder returns. Our MLP & Midstream Energy Income portfolio offers a compelling yield compared with the broader market and has been consistently increasing its distributions. Add in some share buybacks and you have an attractive total return proposition, in our opinion.

Portfolio Highlights

- **Distribution increases:** This quarter 3 of our 15 holdings announced dividend increases. The average increase was 6.4% year-over-year.
- **Sales:** We trimmed **Antero Midstream (AM)** and **Energy Transfer (ET)** to deploy cash to better opportunities. We continue to view both AM and ET as core holdings.
- **Buys:** We increased our position in **Cheniere, Inc. (LNG)** as the company is projected to have one of the best midstream shareholder returns profiles through 2026, including a 15% dividend increase in 2024, 10% per year thereafter, and a targeted $4 billion in share buybacks. We also increased **Hess Midstream (HESM)** as the company screens well on yield, distribution growth, free cash flow (FCF) yield, leverage, and valuation (EV/EBITDA).

Looking Ahead

We will continue to monitor the aforementioned tailwinds and the continuing M&A activity in the sector. We expect further positive updates during the next earnings season from midstream companies.

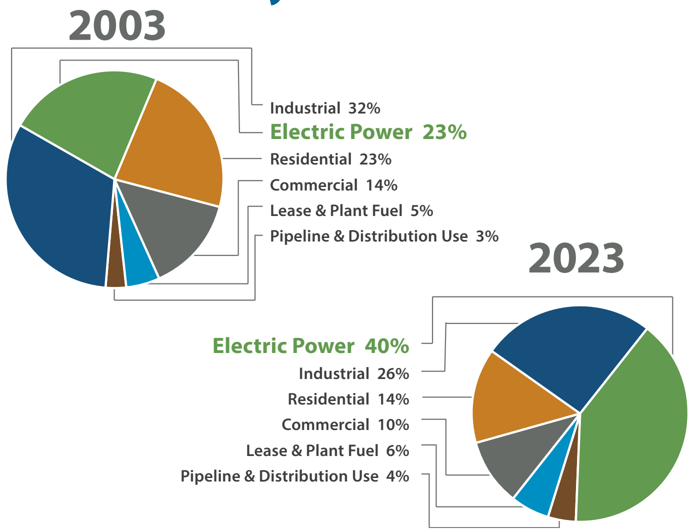
Infrastructure

QUARTERLY REPORT 3Q 2024

INFRASTRUCTURE RECORDED ITS BEST quarter of performance in five and a half years. Despite its lower beta, our Infrastructure portfolio outperformed both its benchmark and the S&P 500 Index, which both finished squarely in positive territory. Relative performance versus the broad market was its best in over two years.

Within the portfolio, interest rate sensitivity was a key driver behind relative performance. Declining interest rates created tailwinds for REITs (cell towers) and utilities, which led the portfolio. Thematically, the utilities and midstream sectors continued to benefit from accelerating power demand fueled by datacenter proliferation. Notably, all sectors recorded positive performance.

US Natural Gas Consumption by End Use



As of December 31, 2023. Sources: EIA; Miller/Howard Research & Analysis.

Looking Ahead

Over the last 20 years, US natural gas consumption has marched steadily higher. Total natural gas consumption has been driven by the electric power sector as residential, commercial, and industrial consumption has been stagnant. While total electricity demand has been roughly flat for the last two decades, natural gas' share of electricity generation has increased from 17% in 2003 to 43% in 2023 as it has displaced coal. As a result, electric power has become a much larger piece of natural gas demand, rising from 23% to 40% of consumption over the same time period.

We feel that growing power demand from datacenter trends should add another leg to this growth story. Natural gas will be used to meet a portion of the incremental demand, as intermittent renewable power will have to be supplemented with dispatchable generation.

Our Infrastructure portfolio remains well-positioned to take advantage of these drivers, in our view. Benefits extend beyond midstream realizing higher natural gas processing, throughput, and storage volume. Utilities also may benefit from additional opportunities to deploy capital in regulated transmission and generation projects, and independent power producers can benefit from tightening power markets. Overall, we believe these tailwinds should continue to enhance the portfolio's ability to provide a high- and rising-income stream for investors.

Portfolio Highlights

- **Dividend increases:** This quarter, 3 of our 34 holdings announced dividend increases with an average increase of 15% [including a 35% increase declared by **T-Mobile US Inc (TMUS)**].
- **Redeploying capital:** We exited our position in **NextEra Energy Partners (NEP)** on an increasing chance of a future dividend cut and trimmed our positions in **Ameren Corp. (AEE)** and **NiSource (NI)**. The sales enabled us to redeploy capital into more attractive opportunities.
- **New position:** We initiated a position in **American Water Works Company (AWK)** and expect the company to benefit from peer-leading growth that is supplemented by consolidation opportunities across a fragmented industry. AWK is among the highest quality names in the sector due to its diversified footprint across constructive jurisdictions, track record of execution, and solid balance sheet.
- **Increasing positions:** We added to **Cheniere Energy (LNG)** after a period of underperformance versus our other midstream holdings. We continue to expect LNG to benefit from long-term demand trends and a return of capital to shareholders.

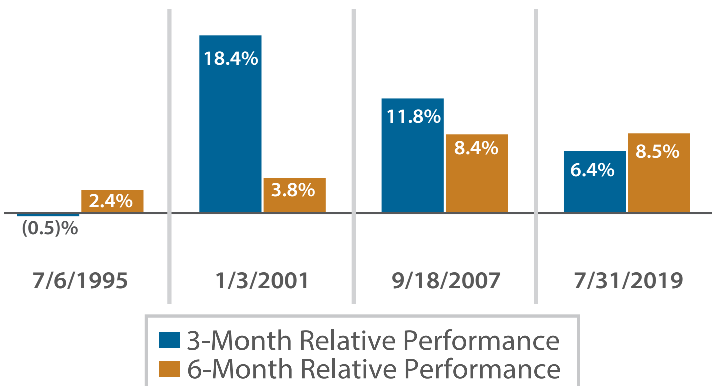
Utilities Plus

QUARTERLY REPORT 3Q 2024

UTILITIES MAINTAINED THEIR POSITIVE momentum and recorded their best quarter of performance in over 10 years. Utilities outpaced the broader market and were the best performing sector within the S&P 500 Index. Strong performance during the quarter pulled utilities ahead of the broader market year to date.

Utilities benefited from increasing visibility into a lower-rate environment. This culminated with the Federal Reserve lowering rates for the first time since 2020. During the quarter, the yield on the 10-year Treasury declined ~60 basis points.

Relative Utility Performance Following Initial Easing



Sources: Bloomberg; Miller/Howard Research & Analysis. Relative performance of the S&P 500 Utilities Index vs. the S&P 500 Index. Easing cycles are determined using the upper bound of the federal funds target rate starting after the first target rate reduction following a period of rising rates. Interest rate cycles are smoothed to adjust for minor intra-cycle volatility in target rates.

Within the group, large-cap utilities outperformed mid- and small-cap utilities. Thematically, independent power producers (IPPs) continued to lead the group as rising electricity demand from datacenter trends remained at the forefront of investors' minds. IPP performance was relatively flat until late September when Constellation Energy (CEG) announced a 20-year power purchase agreement with Microsoft (MSFT – not held) that included the restart of one of the nuclear units at Three Mile Island to match power demand from MSFT's datacenters. The announcement created a catalyst that pushed the group higher through quarter end.

Looking Ahead

Over the last few years, we have frequently noted that rising interest rates are a headwind to utility performance. With the Federal Reserve cutting interest rates in September, it appears these headwinds are set to reverse.

Over the last 30 years, interest rates have seen four other easing cycles. Following the first rate cut of each cycle, utilities outperformed the broader market over the next three months in three out of the four cycles. Over the next six months, utilities outperformed the broader market in all four cycles. Over both time periods, utility performance was, on average, positive on an absolute basis. While this backdrop is clearly encouraging, we expect utilities to deliver high and growing income for investors regardless of the ultimate interest rate trajectory.

Portfolio Highlights

- **Dividend increases:** This quarter, 7 of our 32 holdings announced dividend increases with an average increase of 4.1%.
- **High grading:** We initiated a position in **American Water Works Company (AWK)** and expect the company to benefit from peer-leading growth that is supplemented by consolidation opportunities across a fragmented industry. In our view, AWK is among the highest quality names in the sector due to its diversified footprint across constructive jurisdictions, track record of execution, and solid balance sheet.
- **IPP Mania:** We exited our position in **NextEra Energy Partners (NEP)** on an increasing chance of a future dividend cut. Additionally, we increased our positions in **Atmos Energy (ATO)** which we expect to benefit from a premium growth profile and balance sheet, and **Duke Energy (DUK)** which we expect to benefit from encouraging regulatory outcomes and accelerating load growth. Overall, we feel these transactions reduced the risk profile of the portfolio.

North American Energy (without K-1s)

QUARTERLY REPORT 3Q 2024

LOWER RATES PROMPTED A ROTATION INTO rate-sensitive sectors this quarter. Energy, however, failed to participate. Oil prices declined on global economic growth concerns, particularly in China, and on rumblings of an OPEC+ supply increase.

Our portfolio's emphasis on the full, diversified energy value chain mitigated some of the drawdown. A rotation last quarter into natural gas-focused midstream stocks, which delivered strong returns, partially offset oil producer and refiner weakness. While investors often view energy as a monolithic bet on oil prices–a notion supported by the composition of passive sector indices–roughly a third of the stocks in our portfolio were positive this quarter, despite a 17% decline in oil prices.

Looking Ahead

Looking to 2025, energy stocks face major cross-currents. On demand, US economic data suggest everything from recession to soft landing to no landing may be possible. China, the largest oil importer, is also a wildcard with weak current demand potentially rekindled by fiscal stimulus. On supply, things are equally opaque. Aside from potential Mideast disruptions, OPEC+ seems intent on increasing production, while production in Canada, Guyana and Brazil grows. US production appears poised to flatline after years of growth. Meanwhile, across our holdings, valuations remain near rock bottom, and balance sheets are strong.

The chart below shows breakeven pricing for major shale plays. Two things stand out. First, at current oil prices the average producer remains profitable.

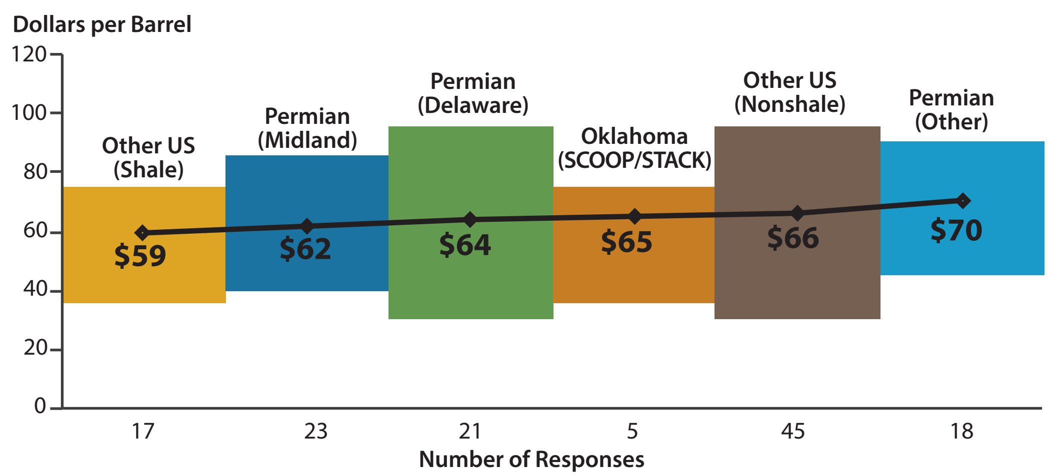
Portfolio Highlights

- **Energy and income:** The portfolio currently offers an indicated yield of 3.4%, which we project is sustainable down to approximately $40 oil, combined with a significantly larger variable return of capital commitment at higher commodity prices.
- **Along the energy value chain:** We added two energy services companies this quarter, both possessing idiosyncratic drivers. **Select Water Solutions (WTTR)** is investing in a large low-cost network of water and wastewater pipelines to support E&Ps (Exploration & Production). **Atlas Energy Solutions (AESI)** owns low-cost sand mines and is building a 42-mile conveyor system that should lower product costs to the core of the Delaware Basin.

Second, there is a huge range. In recent years, we've devoted significant resources to understanding remaining shale drilling inventory–both quantity and quality, and who owns it. As a result, we feel confident regardless of near-term oil trajectories that 1) our producers and their midstream counterparties will remain profitable and that 2) inventory-constrained companies are likely to curtail drilling faster than prior cycles which, in turn, should help restore market balance more quickly than in prior cycles.

Come what may for oil, confidence in our diversified approach remains high. From the date of this portfolio's inception in 2013, oil prices are down 25%. Yet, over that same period our diversified portfolio has cumulatively returned well over 100%.

What WTI Oil Price Does Your Firm Need to Profitably Drill a New Well?



Source: Federal Reserve Bank of Dallas. Notes: Line shows the average, and bars show the range of responses. 87 E&P firms answered this question from March 13-21, 2024. Executives were surveyed about the top two areas in which their firms were active.

Small Cap Dividend

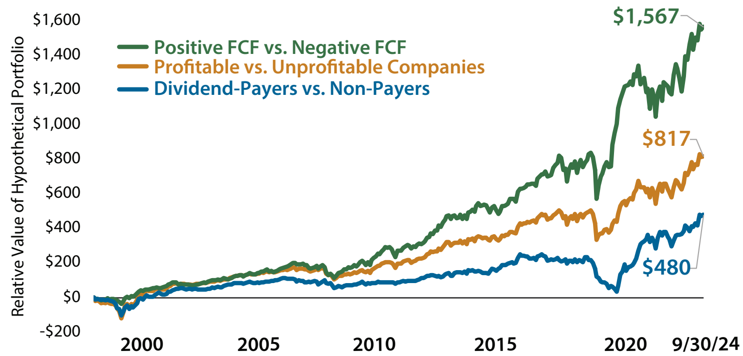
QUARTERLY REPORT 3Q 2024

AFTER A SLUGGISH FIRST HALF, SMALL-CAP stocks outpaced the broader market this quarter, buoyed by a shift in investor sentiment towards an improved economic outlook. Small-caps are generally more sensitive to economic fluctuations—roughly a quarter of the small-cap Russell 2000 Index is comprised of unprofitable businesses that need everything to go "right" for them to succeed. As economic forecasts change, profitless small-cap companies have historically seen higher levels of stock price volatility (and volatility can be a return killer, see our 3Q 2023 Quarterly Report).

Some small-cap investors prefer gambling on whether this week's headline-making, money-losing venture can survive long enough to hit its lofty revenue projections. At Miller/Howard, we prefer a more sustainable approach to small-cap investing. In our view, long-term outperformance can be realized through a diversified portfolio of profitable, free-cash-flow-positive companies that pay dividends. Profitable businesses with healthy cash flow tend to offer greater downside protection compared to money-losing ventures. Similarly, we believe that dividends often indicate management's confidence in the long-term resilience of their business.

After four straight quarters of outperformance relative to its Russell 2000 benchmark, our Small Cap Dividend portfolio trailed its benchmark slightly during the third quarter despite realizing strong absolute returns. Both **Medpace (MEDP),** our leading contributor to portfolio returns in the first quarter, and **Amkor (AMKR),** our top contributor in the second quarter, gave up some of their outsized gains in the third quarter, significantly detracting from this quarter's performance. Earlier in the year, we proactively trimmed our positions in both holdings as part of our risk management process. Year-to-date, portfolio returns have comfortably surpassed that of the benchmark.

Relative Growth of $100
Profitability, Free Cash Flow, & Dividend Factors
within the Russell 2000 Index (12/31/1998 - 9/30/2024)



Data as of September 30, 2024. Sources: Bloomberg; Miller/Howard Research & Analysis. Stocks in the Russell 2000 Index were divided into six groups (profitable vs. unprofitable, positive free cash flow vs. negative free cash flow, dividend-paying vs. non-paying), market-cap-weighted, and rebalanced at month end. The chart shows the hypothetical difference in relative portfolio value for $100 invested in each group starting on December 31, 1998 and held to September 30, 2024. Profitable (unprofitable) is defined as positive (negative) trailing GAAP net income at quarter end. Free cash flow (FCF) is defined as cash from operations less capital expenditures (excludes real estate and financials). GAAP = Generally Accepted Accounting Principles.

Looking Ahead

Historically, we've found that profitability, free cash flow, and dividends are key factors in supporting superior long-term returns within the small-cap universe. Our Small Cap Dividend portfolio is designed to take advantage of these three factors with the goal of creating a diversified, all-weather portfolio of small-cap companies that should outperform the Russell 2000 Index over long holding periods in our opinion.

Portfolio Highlights

- **Dividend increases:** Five holdings raised their regular dividend this quarter—**Hawkins (HWKN), Boise Cascade (BCC), Benchmark Electronics (BHE), InterDigital (IDCC),** and **SM Energy (SM).**
- **Special dividend:** Three holdings declared a special dividend this quarter—**Ethan Allen Interiors (ETD), Boise Cascade (BCC),** and **Chord Energy (CHRD).**
- **Sales:** We exited **California Resources (CRC), Simulations Plus (SLP), Equitrans Midstream (ETRN), Franklin Electric (FELE), FNB Corporation (FNB), Cabot (CBT), Vontier (VNT), Orion S.A. (OEC), Haemonetics (HAE), MSC Industrial Direct (MSM),** and **Quanex (NX).**
- **Buys:** We initiated positions in **Flowers Foods (FLO), ACI Worldwide (ACIW), HealthStream (HSTM), Premier Financial (PFC), ConnectOne Bank (CNOB), Progyny (PGNY), ADMA Biologics (ADMA), Kulicke & Soffa (KLIC), Sylvamo (SLVM),** and **Argan (AGX).**

Yield, Growth, Strength, Stability

- Our Income-Equity portfolios each offer a high dividend yield that is over 2.5x 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.
- We believe the portfolios are well-positioned for dividend growth throughout the full market cycle.

Income-Equity (with MLPs)

	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	3Q24
Income-Equity Yield	4.2	4.7	4.0	3.7	4.3	3.7	3.6	3.3	3.6	3.7	3.6
S&P 500 Yield	2.0	2.2	2.1	1.9	2.2	1.9	1.5	1.5	1.8	1.5	1.3
Ratio	2.1x	2.2x	1.9x	2.0x	2.0x	2.0x	2.3x	2.2x	2.0x	2.4x	2.7x
Income-Equity Projected Dividend Growth*	7.5	5.8	5.0	6.3	7.8	7.3	5.1	6.0	6.1	5.5	5.1
S&P 500 Projected Dividend Growth**	4.7	4.2	4.0	4.2	5.2	4.2	3.3	5.9	4.8	4.5	5.0
Ratio	1.6x	1.4x	1.2x	1.5x	1.5x	1.7x	1.5x	1.0x	1.3x	1.2x	1.0x
Income-Equity Dividend Coverage Ratio	1.3x	1.3x	1.3x	1.5x	1.9x	2.3x	2.1x	2.0x	2.7x	2.1x	2.1x
Income-Equity Net Debt/EBITDA***	4.2x	2.8x	2.0x	1.9x	1.4x	1.9x	1.9x	1.2x	2.0x	1.8x	2.2x
Income-Equity P/E Ratio Trailing	16.4	14.2	17.2	17.7	12.6	12.8	16.7	14.0	13.6	14.5	16.4
S&P 500 P/E Trailing	18.4	18.8	20.5	21.7	16.5	21.6	27.6	24.1	18.6	21.9	24.7
Premium/Discount	-10%	-24%	-16%	-18%	-23%	-41%	-40%	-42%	-27%	-34%	-34%

Income-Equity (No MLPs)

	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	3Q24
Income-Equity (No MLPs) Yield	4.0	4.6	3.9	3.7	4.2	3.6	3.5	3.2	3.5	3.4	3.3
S&P 500 Yield	2.0	2.2	2.1	1.9	2.2	1.9	1.5	1.5	1.8	1.5	1.3
Ratio	2.1x	2.1x	1.9x	2.0x	2.0x	2.0x	2.3x	2.1x	2.0x	2.2x	2.6x
Income-Equity (No MLPs) Projected Dividend Growth*	7.7	5.9	5.0	6.4	7.9	7.5	5.2	6.0	6.0	5.6	5.1
S&P 500 Projected Dividend Growth**	4.7	4.2	4.0	4.2	5.2	4.2	3.3	5.9	4.8	4.5	5.0
Ratio	1.6x	1.4x	1.2x	1.5x	1.5x	1.8x	1.5x	1.0x	1.3x	1.2x	1.0x
Income-Equity (No MLPs) Dividend Coverage Ratio	1.3x	1.3x	1.3x	1.5x	1.9x	2.3x	2.1x	2.0x	2.8x	2.3x	2.2x
Income-Equity (No MLPs) Net Debt/EBITDA***	2.6x	2.6x	2.2x	2.1x	1.4x	1.9x	1.9x	1.2x	1.8x	1.6x	2.1x
Income-Equity (No MLPs) P/E Ratio Trailing	17.2	16.5	18.2	18.0	12.9	13.5	16.8	14.0	13.8	14.6	16.4
S&P 500 P/E Trailing	18.4	18.8	20.5	21.7	16.5	21.6	27.6	24.1	18.6	21.9	24.7
Premium/Discount	-6%	-12%	-12%	-17%	-22%	-38%	-39%	-42%	-26%	-33%	-34%

As of September 30, 2024. Sources: Bloomberg; S&P; Miller/Howard Research & Analysis. The data above are based on representative accounts in our Income-Equity portfolios both with and without MLPs and are subject to change. Median P/E ratio trailing is published for our Income-Equity portfolios.
* 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 are 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 last page.

2023-2024 ESG REPORT: Integration and Active Ownership

PARTNERSHIP ACTIVITY

- Discussions and calls about audit quality
- Investor letters urging improved ESG action by regulators, sectors, and governments

A UNITED MILLER/HOWARD

The ESG and Portfolio Management Teams work together on analysis, active ownership, and the creation of Sustainable Income Opportunities.®

The ESG Team participates in Portfolio Management meetings, and the Portfolio Management Team participates in engagement calls.

DIVESTMENT

Optional custom exclusions for clients (where feasible under custodian restrictions)

PROXY VOTING

Of 5,823 ballot items across 467 meetings, our research led us to vote contrary to management's recommendations over 30% of the time.

ENGAGEMENT

- 12 companies engaged on ENVIRONMENTAL issues
- 8 companies engaged on SOCIAL issues
- 41 companies engaged on GOVERNANCE issues

Sustainable Income Opportunities® – Doing Good and Doing Well.

More information is available on our website, including insight papers that articulate our positions on specific issues and past ***ESG Reports.*** *There you can also access a database of the shareholder proposals we filed.*

Proxy Data for FY 2023; Engagement Data from 2Q23 - 2Q24.
Miller/Howard Investments Inc. is an independent, research-driven investment boutique with over three decades of experience managing portfolios for major institutions and individuals in dividend-focused investment portfolios. The firm is 100% employee-owned through an Employee Stock Ownership Plan (ESOP).

We continue to evolve and develop portfolios that strive to provide investorswith various levels of current income and dividend growth. With a primary goal of reliable income and long-term returns, coupled with a belief that investors can play an important role in securing a sustainable future, our portfolios include environmental, social, and governance (ESG) research and/or screening, direct engagement with companies, filing shareholder resolutions, proxy voting, coalition building, and/or public policy involvement.

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 appropriate 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. To receive a list of all recommendations for the previous year, please email compliance@mhinvest.com. 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. The returns on a portfolio that utilizes environmental, social, or governance (ESG) criteria for stock selection may be lower or higher than portfolios where ESG factors are not considered, and the investment opportunities available to such portfolios may differ.

DEFINITIONS: 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. **MLP** = Master Limited Partnership. **S&P 500 Index®** widely regarded as the best single gauge of large-cap US equities and serves as the foundation for a wide range of investment products. The Index includes 500 leading companies and captures approximately 80% coverage of available market capitalization. **S&P 500 Equal Weight Index** includes the same constituents as the capitalization weighted S&P 500, but each company in the S&P 500 EWI is allocated a fixed weight - or 0.2% of the index total at each quarterly rebalance. **Russell 1000 Index®** measures the performance of the large-cap segment of the US equity universe. It is a subset of the Russell 3000 Index® and includes approximately 1,000 of the largest securities based on a combination of their market cap and current index membership. The Russell 1000 Index® represents approximately 92% of market capitalization of the US market. **Russell 1000 Value Index** offers investors access to the broad value segment of US equity value universe and is constructed to provide a comprehensive and unbiased barometer of the broad value market. **Russell 2000 Index** measures the performance of the small-cap segment of the US equity universe and is a subset of the Russell 3000® Index representing approximately 10% of the total market capitalization of that index. It includes approximately 2,000 of the smallest securities based on a combination of their market cap and current index membership. Investors cannot invest directly in an index and unmanaged index returns do not reflect any fees, expenses or sales charges.

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