ELCO
Management Company, LLC

QUESTIONS AND ANSWERS IN THE CORONA ENVIRONMENT

How has the Portfolio team reacted to current market conditions?

- With equity markets and energy prices falling /displaying unprecedented volatility, we have focused the portfolio on the Midstream companies we believe are best positioned to rebound post crisis
- Specifically, the portfolio is concentrated in market leading companies that have strong balance sheets, dividend coverage ratios, manageable leverage, attractive / strategic assets and importantly, the financial flexibility to weather challenging shorter-term economic conditions.
- We are in regular communication with the management of all companies in the portfolio, and are confident in their ability (and commitment, as indicated by continued insider buying) to manage their businesses in and through stressed operating environments

What is the investment case for owning midstream energy companies?

- Fossil fuels (particularly natural gas) will continue to serve as a base for global power generation, transportation, and general economic activity, despite the evolution of alternative "clean" energy sources, for the foreseeable future (20+ years);
- This fact is particularly true for emerging market economies, where the infrastructure is geared to now much more inexpensive fossil fuel prices; in any case, natural gas (in particular) will serve as a very important "bridge" to cleaner energy over the next 50 years across the globe
- Midstream companies are by nature, "asset rich" infrastructure businesses (pipelines, storage facilities, etc.) that generate steady and long-term cash flow streams which support attractive investor distributions / dividends (think of toll roads as an analogy). While it is possible that some companies may lower or eliminate distributions in the current environment to conserve cash and potentially implement share buybacks, they will still likely provide payouts to investors that significantly exceed those available in the overall market.

- The United States has become a lower cost developer of natural gas…this will fuel demand for the commodity here and importantly abroad as we expand natural gas exports
- The large integrated midstream companies have diversified businesses that handle, process, and transport natural gas from the well head to the end customer (i.e., large industrial customers, utilities, or export facility).
- While not currently a focus of the investment community, the operations of the strongest midstream companies are insulated from the price of the actual commodities they transport. Contracts are now strictly "take or pay" or fee-based, unlike in years past where midstream companies had significant exposure to commodity price volatility.

What is currently influencing midstream investor perception and pricing in the market?

- The confluence of three events has been extremely punishing to midstream investors
    - The potential economic impact of the Coronavirus
    - The oil price collapse in response to falling short term economic demand and the failed OPEC+ output meeting, Saudi / Russian price war
    - The excess leverage used by closed end fund and other structured investment product managers.
        - Large investment managers in the midstream space (i.e., Goldman Sachs, Invesco, and ALPs) utilized leverage sometimes in excess of 20% in their closed end products. As equity prices fell these managers were subject to margin calls, which in turn caused severe pressure on the midstream equity prices. Unfortunately, as we've seen in the past – managers subject to margin calls sell the most liquid names and their decisions are not made with fundamentals in mind

While not completely an "apples to apples" comparison, the current extreme environment is reminiscent of the 2008 experience which also wreaked havoc on the midstream industry. At that time, oil prices collapsed, and midstream companies sold off due to leveraged investor liquidations and the overall lack of confidence the industry could sustain its cash-flow and dividend payments. Our portfolio declined over 53% that year, but ultimately, the economy did recover from the Financial Crisis as governments around the globe stepped in to rescue financial institutions, and failing core industries. At that time, the provision of needed liquidity and relief helped to stabilize the global economy, leading to renewed growth in 2009 and beyond (the ELCO portfolio appreciated over 99% that year as the energy industry, along with the economy, recovered). We strongly believe that the economy will similarly recover as governments again commit to aggressive stimulus packages to help stem the economic pain caused by the virus. We thus believe that the current downturn, as scary and uncertain as it feels, is creating a generational opportunity to invest in midstream companies that will help fuel the recovery.

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