Frontier MFG Select Infrastructure Fund
Institutional Class (FMSIX), Service Class (FMSSX)
Sub-advised by MFG Asset Management – Sydney, AU

FRONTIER FUNDS

Quarterly Commentary, June 30, 2023

Global shares gained in the June quarter, as the Federal Reserve approached the end of its rate-hiking campaign, U.S. bank turmoil eased with few observable new casualties and optimism about the potential of recent developments in Artificial Intelligence (AI) continued. Nine of the eleven sectors advanced in local currency terms, but gains were largely concentrated in the Information Technology (+15.0%), Consumer Discretionary (+11.3%) and Communication Services (+10.2%) sectors that benefited from growing confidence in the potential for AI to drastically influence societies and economies. The detractors were the Energy (-1.0%) and Utilities (-0.7%) sectors that fell as the outlook for commodity prices softened.

On a regional basis, there was growing confidence in Japan in the outlook for profit growth and still accommodative monetary policy pursued by the Bank of Japan under new leadership. U.S. shares were the other standout performer in the June quarter on the back of continued excitement about developments in AI and signals the Federal Reserve is nearing the end of its rate-tightening cycle as inflation continued to improve. Importantly, economic momentum in the U.S. appeared to be relatively sound, with unemployment still low, and construction activity assisted by increased homebuilder confidence and the Inflation Reduction Act.

In Europe, pressures on economic activity have been larger and inflationary pressures more intense, partly because wages in Europe are more often contractually tied to past increases in consumer prices than in the U.S. and are hence stickier.

Chinese shares meanwhile came under pressure, as fears about the Chinese economic recovery continued to mount. Expectations for a reopening boom have failed to materialize so far this year, forcing policymakers to step in with some incremental interventions to increase stimulus during the quarter. To date, interventions have been small-scale rather than material as policymakers balance competing priorities including reducing leverage in the system.

The Fund recorded a negative return in the June quarter as 10-year bond rates lifted as jobs and spending remained resilient, suggesting central banks would need to do more to tame inflation. The stocks that contributed the most were U.S. rail companies CSX and Norfolk Southern, as well as Netherlands-listed toll road and airport group Ferrovial. CSX and Norfolk Southern lifted on better-than-expected pricing growth and improved network fluidity. The Ferrovial share price rose as it completed its relocation to the Netherlands and as airport passenger traffic continued to rebound across its portfolio.

The stocks that detracted the most were the investments in UK water utilities United Utilities and Severn Trent, and U.S. transmission and distribution company Eversource. Listed UK water utilities fell notwithstanding their robust fundamentals and improving capital investment outlook, impacted by contagion associated with concerns over the solvency of heavily indebted unlisted peer, Thames Water. Eversource Energy declined as rising bond yields and adverse regulatory developments in Connecticut, a jurisdiction accounting for approximately 30% of the company's earnings, unsettled investors.

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Notwithstanding our expectations for greater volatility in the short to medium term driven by inflation and interest rates, we are confident that the underlying businesses we have included in our defined universe and in our investment strategy will prove resilient over the longer term. We regard the businesses we invest in to be of high quality and, while short-term movements in share prices reflect issues of the day, we expect that share prices in the longer term will reflect the underlying cash flows leading to investment returns consistent with our expectations.

The strategy seeks to provide investors with attractive risk-adjusted returns from infrastructure securities. It does this by investing in a portfolio of listed infrastructure companies that meet our strict definition of infrastructure at discounts to their assessed intrinsic value. We believe that infrastructure assets, with requisite earnings reliability and a linkage of earnings to inflation, offer attractive, long-term investment propositions. Furthermore, we believe the resilient nature of earnings and the structural linkage of those earnings to inflation means that investment returns typically generated by infrastructure stocks are different from standard asset classes and offer investors diversification when included in an investment portfolio. In the current uncertain economic and investment climate, we believe the historically reliable financial performance of infrastructure investments makes them attractive, and an investment in listed infrastructure has the potential to reward patient investors with a long-term time frame.

Index movements and stock contributors/detractors are based in local currency terms unless stated otherwise.