



Introducing the Global X MLP & Energy Infrastructure Covered Call ETF (MLPD)

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On May 8, 2024 we listed the [Global X MLP & Energy Infrastructure Covered Call ETF \(MLPD\)](#) on the New York Stock Exchange. MLPD is an ETF designed to offer investors a potential source of current income and positive relationship with volatility that can be incorporated into their respective portfolios. Concurrently, the fund seeks to provide exposure to MLPs and other energy infrastructure corporations.

The energy sector is one in which you might typically find an income-seeking investor. Many of its constituents operate business models that tend to experience steadily appreciating production volume and, within the midstream space specifically, this has led to meaningful cash flow generation and the payment of competitive distributions with relative consistency. The [Global X MLP & Energy Infrastructure ETF \(MLPX\)](#) is one such example of a fund that carries exposure to this midstream infrastructure space. This not only grants it a stake in these potentially rising volumes. It also makes it a model underlying investment opportunity in the application of a covered call option strategy, in our view, granting investors exposure to the potentially generous distributions made payable by midstream firms, while leaving the possibility open to enhance yield further through the premiums received for writing covered calls.

Key Takeaways

- The [Global X MLP & Energy Infrastructure Covered Call ETF \(MLPD\)](#) operates a systematic buy-write strategy wherein it purchases the Global X MLP & Energy Infrastructure ETF and writes call options on the same asset against 100% of its notional holdings monthly.
- Covered call option strategies aim to harness the positive relationship that option premia and volatility typically share with one another to drive current income. The energy sector, where MLPX maintains its holdings, has the propensity to display these relatively widely oscillating pricing patterns.
- U.S. energy companies are swiftly expanding their global market share, but many are still exposed to volatile energy prices. Manicuring sector-specific holdings to target the midstream portion of the space may help alleviate some of this concern, while pursuing higher yields, consistent sources of income, and less sensitivity to short-term energy prices.

MLPD Operates a Systematic Covered Call Option Strategy

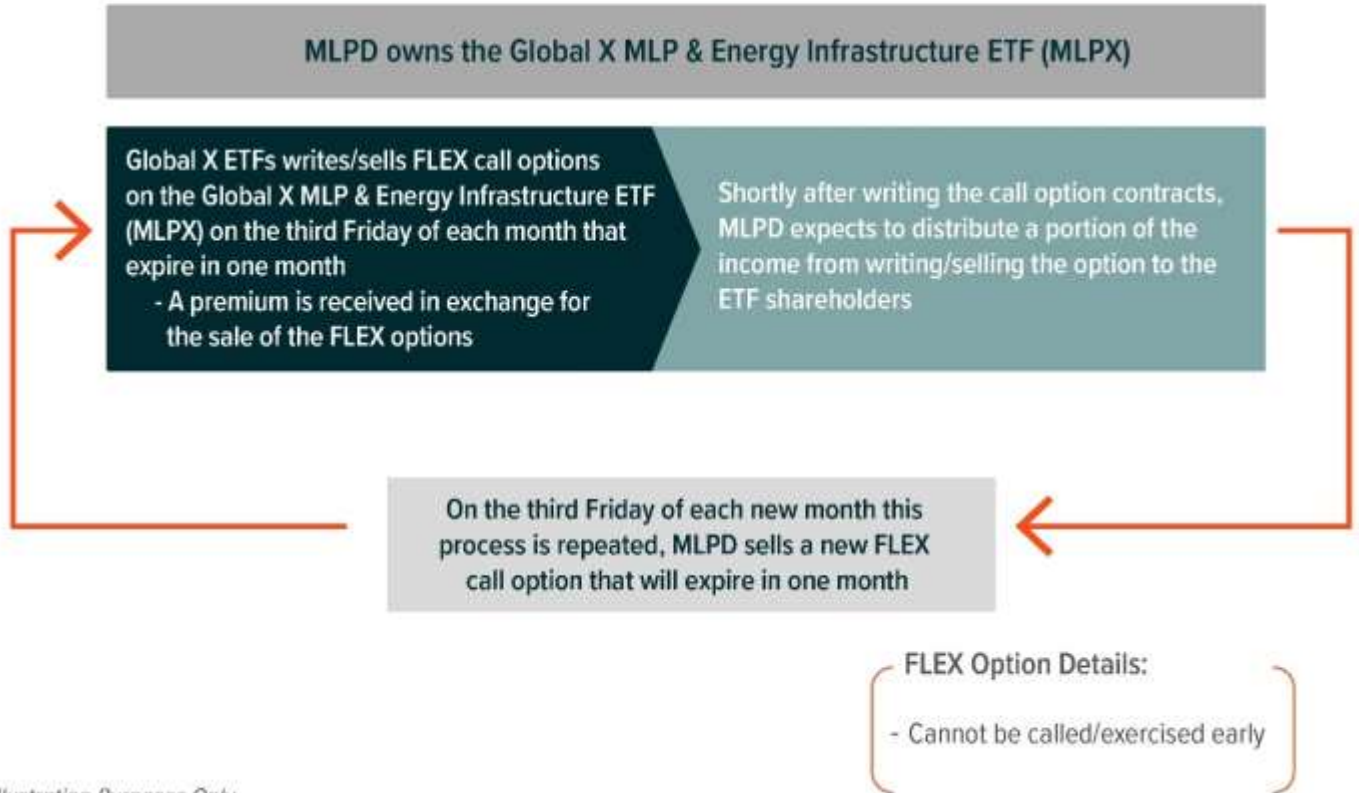
Following a passive, rules-based approach, MLPD is a fund that seeks to maintain an underlying long position in the [Global X MLP & Energy Infrastructure ETF \(MLPX\)](#) and write monthly European-style at-the-money FLEX call options on the same ETF at a value equal to 100% of its notional portfolio. Its use of FLEX options allows it to customize a multitude of key contract terms including strike price, exercise style, and expiration date. To wit, the options written by MLPD are European in style, which means they cannot be exercised prior to expiration. They are also written at-the-money on a monthly basis. The calls are written at-the-money in an effort to attract the highest possible premiums available while minimizing the likelihood that the options are exercised. And to be sure that the option cannot be exercised by the party to whom it is sold, the fund will buy the call back on the day before the monthly roll date and proceed to enter into a new covered call position on the third Friday of every month. Notably, the fund's distribution methodology will see it pay out the lower of half its option premium received or 1% of its NAV in the form of a dividend, while any dividends it receives from its underlying equity holdings should act as a solid support system to promote a higher overall fund net asset value until paid out to shareholders.



COVERED CALL PROCESS EXPLAINED

Sources: Global X ETFs.

As an example of how an ETF can implement a covered call strategy, the Global X MLP & Energy Infrastructure Covered Call ETF (MLPD) maintains exposure to the stocks in the Global X MLP & Energy Infrastructure ETF, while writing call options each month.



For Illustration Purposes Only

Making a Case for Covered Call Writing on Energy Markets

When seeking out an underlying investment vehicle on which to write covered calls, it is important to consider what the broader strategy’s risk and reward profile will look like. By writing call contracts on a held asset, the investor is establishing a strike price at which they will no longer benefit from the upside price appreciation of that asset. This opportunity cost is taken on in an effort to earn premium income. Meanwhile, the investor remains exposed to the downside moves of the underlying asset, with the potential to outperform in declining markets owing to the premium income that is received.

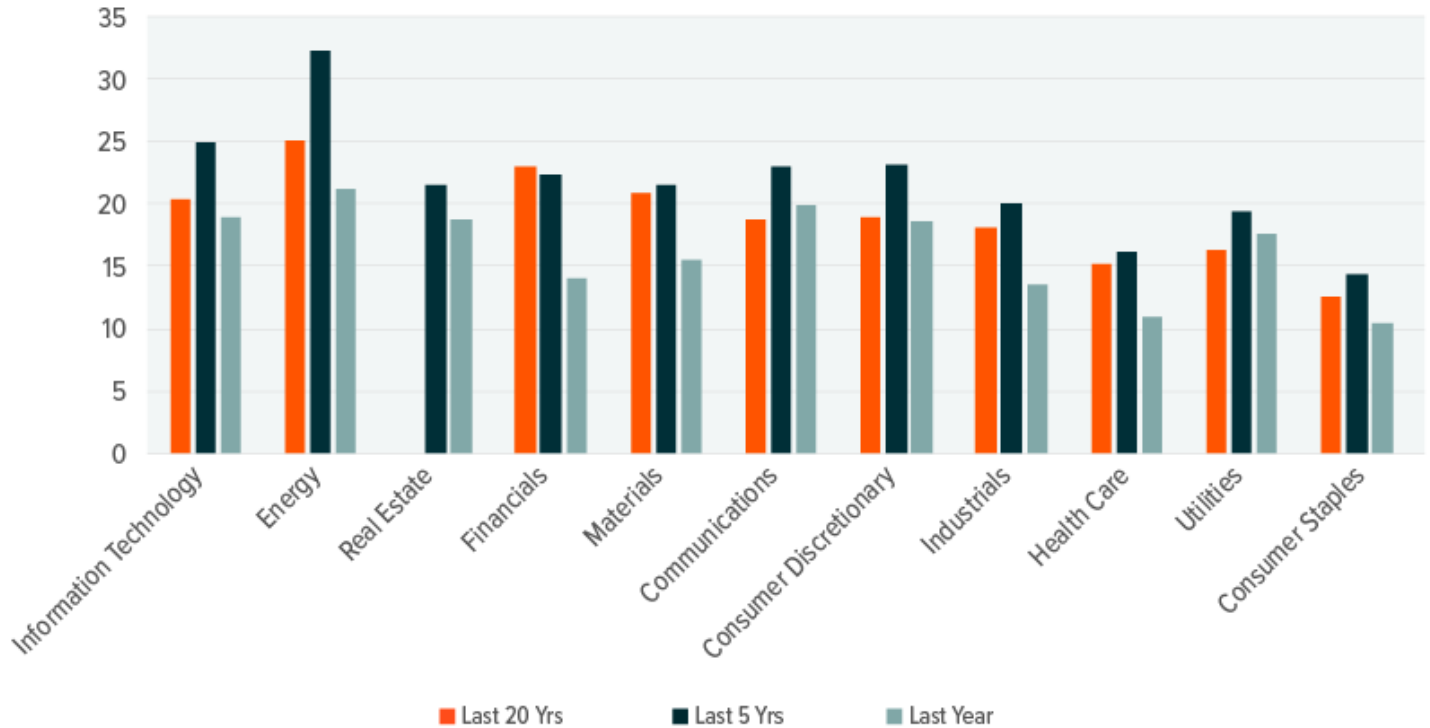
The makeup underscores the importance of pursuing the highest possible premium values available in exchange for writing the call contracts, and one supportive means by which to do so is by incorporating a relatively volatile reference asset when implementing the strategy. Option premiums generally share a positive correlation with volatility because it becomes more likely that an option contract will move into the money and become exercisable when an underlying instrument is trading widely in value. This makes the contract more valuable and, thus, the purchaser will typically pay more to attain it.

The energy market is a solid example of a space that may exhibit elevated volatility due to historic boom-and-bust cycles. Its constituency is often dependent upon the prices of underlying commodities, and it is similarly subject to risks involving global economics that can alter the value of these instruments materially over a short time horizon. In fact, over the last five years the energy sector has represented the single most volatile segment of U.S. markets.



THE ENERGY SECTOR HAS EXPERIENCED MARKET-LEADING VOLATILITY IN RECENT YEARS

Sources: Global X ETFs with information derived from Bloomberg L.P. Thirty-day price volatility measured as the annualized standard deviation of the relative price change for the thirty most recent trading days using closing prices from April 1, 2003 to March 28, 2024. Data retrieved April 11, 2024. Sectors represented by S&P 500 sector indices. 20 year data not shown for Real Estate due to index inception date.



Given the elevated volatility that we've seen in the energy sector, investors seeking exposure may wish to take more defensive positioning amongst midstream infrastructure firms. Companies in this arena generally exhibit less sensitivity to volatile energy spot prices because they deal in the transportation and storage of energy rather than in its exploration and production. Midstream earnings are tied to energy transport volumes, which generate fixed fee revenues, and are therefore more predictable in nature. By contrast, exploration and production revenues are more closely tied to spot and futures energy prices, which are more sensitive to supply and demand.

The volume-dependent business of midstream infrastructure companies may allow them to perform well during periods of elevated production, even if oil & gas prices fluctuate. As the U.S. energy industry has generally continued to ramp up its production volume, producing record levels of oil & gas, investors may find an attractive long-term growth story in midstream infrastructure. The Global X MLP & Energy Infrastructure ETF offers broad exposure to MLPs and corporations that operate in the midstream energy space.



INFRASTRUCTURE BUILDOUTS CONTINUE DESPITE GAS PRICE FLUCTUATIONS

Sources: Global X ETFs with information derived from Bloomberg L.P. Data shown from April 3, 2023 through March 28, 2024. MLP & Infrastructure Total Return represented by the Solactive MLP & Energy Infrastructure Index; Energy Sector Total Return by the Energy Select Sector Index; Natural Gas Price by the Henry Hub Natural Gas Spot Price.



Index returns are for illustrative purposes only and do not represent actual Fund performance. Index returns do not reflect any management fees, transaction costs or expenses. Indexes are unmanaged and one cannot invest directly in an index. Past performance does not guarantee future results.

This positioning may well have a pacifying impact on volatility, which could diminish option premiums. However, it could also potentially result in softer drawdowns within the underlying MLPX exposure when commodity prices are on the decline. Additionally, the generation of covered call premiums may enhance the already-attractive distribution yield potential on midstream infrastructure companies, supplementing any potential payouts.

A Potentially Chippy Outlook Supports the Case for This Strategy

The midstream energy sector has gone through some dynamic changes over the last few decades. U.S. export activity has expanded quickly according to the U.S. Energy Information Administration, and after rising to gain net-energy-exporter status in 2019, the U.S. has gone on to represent the top producer of all oil and natural gas in the world.^{1,2} The undertaking has lent significant support to the midstream space, as well as the holdings of MLPX, and we’re likely to see production continue to pick up over the next few years.³



U.S. FIELD PRODUCTION OF CRUDE OIL

Sources: Global X ETFs with information derived from the U.S. Energy Information Administration. U.S. crude oil production from February 3, 2014 to January 31, 2024. Data retrieved on April 11, 2024.



The undertaking has come about while other geographies typically known for their energy production have faced challenges. This includes Eastern Europe, where the recent Russia/Ukraine war has impaired supply capabilities, and nations like Saudi Arabia, Iraq, and UAE, where ongoing supply cuts implemented by OPEC have also probably led to reduced output.

MLPX’s dynamic midstream exposures do not necessarily excuse it from the ebbs and flows of changing underlying market dynamics. Indeed, fluctuating spot prices still have an impact on shipping volume, as purchasers decrease their commodity consumption when prices rise. What’s more, the midstream space is still exposed to geopolitical risks and shipping disruptions, like that which has been experienced recently across the Red Sea. The environment supports the notion of continued price volatility and generally serves as a solid backdrop for the implementation of a covered call option strategy.

Conclusion: MLPD Could Serve as a Potential Multi-Purpose Income Pipeline

Implementing a covered call strategy on the Global X MLP & Energy Infrastructure ETF may provide investors with a competitive yield, a positive relationship with volatility, and energy sector exposure, which can help diversify broad portfolio risks. Its structure makes it a multi-purpose potential income pipeline, particularly considering the discretion that investors have over the premium income distributions that they stand to receive. Concurrently, these premium distributions may be able to help offset drawdowns for the underlying MLPX or act as a supplementary boost to the performance of a diversified portfolio when markets are holding their value or experiencing gains.

Related ETFs

[MLPD – Global X MLP & Energy Infrastructure Covered Call ETF](#)

[MLPX – Global X MLP & Energy Infrastructure ETF](#)

Click the fund name above to view current performance and holdings. Holdings are subject to change. Current and future holdings are subject to risk.



Footnotes

1. U.S. Energy Information Administration (2023, August 9). U.S. Energy Facts Explained.
2. U.S. Energy Information Administration (2023, September 21). Oil and Petroleum Products Explained.
3. U.S. Energy Information Administration (2024, February) Short Term Energy Outlook.

Glossary

Roll Date: In the operation of a systematic option strategy, the roll date is the date on which the fund will divest its existing option positions and purchase or write new options to maintain a near-perpetual level of option exposure.

Strike Price: The price at which an option becomes exercisable, once the price of the underlying asset moves into the money.

Buy-Write Strategy: A Buy-Write strategy is a covered call option strategy, which entails buying or maintaining holdings in an investment instrument and proceeding to write call option against the same instrument, placing some semblance of a cap on the upside price appreciation potential that can be realized by the investor.

Standard Deviation: A statistical measure of the variation or dispersion within a set of numbers. In investing it is used to discuss the volatility in returns. Typically, fixed income returns are more stable while equity returns have a higher level of volatility.

At-The-Money: An option contract is considered to be “At the Money” when its strike price is equivalent to the current price value of its underlying asset.

Drawdown: A peak to trough decline that takes place over a given period of time for a specific investment vehicle.

Opportunity Cost: An opportunity cost is the loss of a potential gain on an investment that is taken on when a decision is made to pursue an alternative investment opportunity.

This material represents an assessment of the market environment at a specific point in time and is not intended to be a forecast of future events, or a guarantee of future results. This information is not intended to be individual or personalized investment advice and should not be used for trading purposes. Please consult a financial advisor for more information regarding your situation.

Investing involves risk, including the possible loss of principal. Diversification does not ensure a profit nor guarantee against a loss. Investments in securities of MLPs involve risk that differ from investments in common stock including risks related to limited control and limited rights to vote on matters affecting the MLP. MLP common units and other equity securities can be affected by macro-economic and other factors affecting the stock market in general, expectations of interest rates, investor sentiment towards MLPs or the energy sector, changes in a particular issuer’s financial condition, or unfavorable or unanticipated poor performance of a particular issuer (in the case of MLPs, generally measured in terms of distributable cash flow). MLPX invests in the energy industry, which entails significant risk and volatility.

MLPX invests in small and mid-capitalization companies, which pose greater risks than large companies. The Fund also expects to pay distributions, which will be treated as a return of capital for tax purposes rather than from net profits and shareholders should not assume that the source of distributions is from the net profits of the Fund.

MLPX derives substantially all of its cash flow from investments in equity securities of MLPs. The amount of cash that the Fund will have available to pay or distribute to you depends entirely on the ability of the MLPs that the Fund owns to make distributions to their partners and the tax character of those distributions. Neither the Fund nor the Adviser has control over the actions of underlying MLPs. The amount of cash that each individual MLP can distribute to its partners will depend on the amount of cash it generates from operations, which will vary from quarter to quarter depending on factors affecting the energy infrastructure market generally. Available cash will also depend on the MLPs’ level of operating costs (including incentive distributions to the general partner), level of capital expenditures, debt service requirements, acquisition costs (if any), fluctuations in working capital needs, and other factors. The MLP holdings of the Fund expect to generate significant investment income, and the Fund’s investments may not distribute the expected or anticipated levels of cash, resulting in the risk that the Fund may not have the ability to make cash distributions as investors expect from MLP-focused investments. Past distributions are not indicative of future distributions. There is no guarantee that dividends will be paid.

MLPD is subject to the same risks as MLPX. In addition, MLPD engages in options trading. An option is a contract sold by one party to another that gives the buyer the right, but not the obligation, to buy (call) or sell (put) a stock at an agreed upon price within a certain period or on a specific date. A covered call option involves holding a long position in a particular asset and writing a call option on that same asset with the goal of realizing additional income from the option premium. By selling covered call options, the fund limits its opportunity to profit from an increase in the price of the underlying asset above the exercise price, but continues to bear the risk of a decline in the asset. A liquid market may not exist for options held by the fund. While the fund receives premiums for writing the call options, the price it realizes from the exercise of an option could be substantially below the asset’s current market price. MLPX and MLPD are non-diversified.

Shares of ETFs are bought and sold at market price (not NAV) and are not individually redeemed from the Fund. Brokerage commissions will reduce returns.

Carefully consider the funds’ investment objectives, risks, and charges and expenses before investing. This and other information can be found in the funds’ full or summary prospectuses, which may be obtained at globalxetfs.com. Please read the prospectus carefully before investing.

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