# Brompton Global Healthcare Income & Growth ETF (TSX:HIG; HIG.U)

BROMPTON FUNDS

**PORTFOLIO MANAGER COMMENTARY - DECEMBER 31, 2020**

### Healthcare Sector Review & Outlook

The COVID-19 pandemic placed a spotlight on the healthcare sector and 2020 will stand out as a banner year for innovation with the speed and scale of vaccine development highlighting how quickly disruptions can occur. Large shares of developed market populations could be vaccinated by mid-2021 according to Goldman Sachs. Recently discovered strains of COVID-19 should not impact the efficacy of the recently approved vaccines. However, there is a possibility that a revised COVID-19 vaccine could be needed every 2-3 years depending on the amount of antigenic variability developed in the virus. As vaccinations progress through 2021, we expect gradual normalization of medical trends and increasing utilization across subsectors within healthcare. However, lockdowns in Q1 2021 given the resurgence of COVID-19 cases could shift the timing of the recovery path.

The pharma subsector continues to face near-term headwinds from delayed drug launches (given lockdowns) and the low rates of diagnoses of certain diseases which require regular doctor visits. Partially offsetting this is the benefit of pandemic-driven cost savings which could suggest a longer-term change in which drugs are marketed and sold. Pricing pressure continues to be a headwind, impacting large pharma sales in the mid-single digits and would likely continue over the next few years according to Bloomberg. This is attributed to negative channel mix from high unemployment which are pushing people to lower-priced channels.

While the changing political landscape could bring some uncertainty, we believe major structural changes to drug pricing will be challenging given the slim Democratic control in the US Senate. However there has been some near-term focus on the Most Favored Nation (MFN) Model, which tests an innovative way to lower prescription drug costs by paying no more for high-cost Medicare Part B drugs and biologicals than the lowest price that drug manufacturers receive in other similar countries. The pharma industry has already filed a legal challenge to MFN, which creates a risk of implementation.

The re-emergence of biosimilars continues and 2020 saw meaningful adoption with 28 biosimilars of 7 biologic drugs growing their market share by 15%. There are over 50 biosimilars in development in the US across more than 20 biologics and further adoption of these products could have a meaningful impact. Biosimilars are near-identical versions of biologics made by different manufacturers, to stimulate competition in hopes of driving down costs and expanding access. Biologic drugs are large complex molecules typically manufactured in genetically engineered organisms which are remarkably effective in treating a variety of illnesses (ranging from autoimmune diseases to cancer) but their high prices pose significant barriers to patient access.

Healthcare innovation remains a focal point especially given the success in novel platforms such as Moderna's mRNA platform in the rapid development of a COVID-19 vaccine. We believe there will be a renewed focus on evaluating the potential for unrealized value across biotech companies that offer revolutionary platform technologies and processes. Examples include 1) gene editing - making permanent, precise edits to the genome to repair underlying genetic mutations or to create engineered immune cells for enhanced therapeutic benefit and 2) use of machine learning algorithms and artificial intelligence to better understand native biology and thus aid in the design and development of novel therapies.

The healthcare sector has underperformed the broader market over the past 2 years given policy uncertainty regarding drug pricing and potential reform towards a single-payor system (Medicare-for-All) in the US. We believe that the current environment provides an attractive entry point for investing in healthcare given the sector is trading at the steepest discount to the S&P 500 in over 30 years, according to Bloomberg. The cheap valuations already reflect the pricing pressures in the sector, which has been an ongoing issue for several years. In addition, the healthcare sector has strong earnings growth, second only to only technology, and it has had the most consistent earnings estimates of all S&P 500 sectors, which demonstrates the defensive properties of the sector. The pandemic created several backlogs in healthcare, which provide tailwinds during the recovery. This includes delayed elective surgeries, dental procedures and biotech launches, which should drive volumes during the rebound and provide meaningful earnings upside in the near-term. While we acknowledge that government policy remains an uncertainty for many sectors including healthcare slight overhang, we note that President Biden's healthcare policy calls for a public option for consumers to receive health insurance which differs from a more drastic single-payer proposal (Medicare-For-All). We also think that it will be difficult for the Biden administration to make substantial changes given they have only a very narrow majority in congress. Overall, we believe the healthcare sector plays a defensive role in portfolios while offering solid return potential, and unlike more cyclical sectors tied to economic growth, increased spending on health care is likely to be secular in nature given the aging global population and increasingly longer life spans.

**Portfolio Review**

Brompton Global Healthcare Income & Growth ETF (the "Fund") was up 6.3% in 2020 versus the MSCI World Health Care Index which was up 14.1%.

The Fund benefitted from an underweight exposure to Pharmaceuticals with relative performance better than the benchmark. Top performers include Merck (+47%), Zoetis (+26%) and Novo-Nordisk (+23%).

An overweight exposure to the Healthcare Equipment subsector contributed positively to overall performance but lagged the benchmark. Top performers include Danaher (+45%), IDEXX (+39%) and Abbott (+28%).

The Fund's underweight exposure to Biotechnology negatively impacted performance relative to the benchmark. Top performers include Abbvie (+28%) and Alexion (+25%).

An overweight exposure to Life Sciences contributed positively to overall performance. Top performers include Thermo Fisher (+44%), Agilent (+22%) and PerkinElmer (+18%).

The Fund was market weight Managed Care sub sector which did not overly detract from performance relative to benchmark holdings. Top performers include United Health (+21%) and Humana (+13%).

Laura Lau, SVP & CIO

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| Annual Compound Returns[1] | 1-Year | 3-Year | 5-Year | Since Inception[2] | Since Inception[3] |
|---|---|---|---|---|---|
| Brompton Global Healthcare Income & Growth ETF (CAD Hedged) | 6.3% | 10.8% | 7.2% | 7.5% | - |
| Brompton Global Healthcare Income & Growth ETF (USD) | 8.4% | - | - | - | 11.4% |
| MSCI World Health Care Index | 14.1% | 13.3% | 10.4% | 10.5% | 20.1% |
| S&P/TSX Composite Index | 5.6% | 5.7% | 9.3% | 8.4% | 8.2% |

*(1) Returns are for the periods ended December 31, 2020. The table shows the Fund's compound return compared for each period indicated compared with the MSCI World Health Care Index ("Health Care Index") and the S&P/TSX Composite Index ("Composite Index") (together the "Indices"). The Health Care Index represents the healthcare industry group of the MSCI World Index. The Composite Index tracks the performance, on a market weight basis, of a broad index of large-capitalization issuers listed on the Toronto Stock Exchange. The Fund invests in at least 15 large-capitalization healthcare companies. It is not expected that the Fund's performance will mirror that of the Indices, since the Health Care Index contains a substantially larger number of companies and the Composite Index is more diversified across multiple industries. Further, the Indices are calculated without the deduction of management fees, fund expenses and trading expenses, whereas the performance of the Fund is calculated after deducting such fees and expenses.*

*(2) Inception Date September 24, 2015.*

*(3) Inception Date August 12, 2019.*



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