Brompton Tech Leaders
Income ETF (TSX: TLF; TLF.U)

BROMPTON FUNDS

PORTFOLIO MANAGER COMMENTARY - MARCH 31, 2020

Technology Sector Review & Outlook

At the beginning of the year, Gartner Inc. originally forecasted Worldwide IT spending to grow 3.4% in 2020, up from a modest 0.4% growth in 2019. We expect this to be revised downwards given headwinds from the global pandemic and subsequent recession. We note that any slowdown in technology spending is typically deferred (not permanently impaired) and manifests in pent up demand during an economic rebound. IT areas that typically see this deferred spending are growth-oriented projects rather than maintenance or “keep the lights on” IT. In some instances, pressures on IT budgets sometimes accelerates digital transformation initiatives as legacy systems are more costly to maintain, and adoption of modernized infrastructure frees up budget for more growth-oriented initiatives.

The market volatility in Q1 has reminded investors about the defensive business model of technology firms, particularly software and platform-oriented ones. Software can be viewed as defensive, particularly mission-critical applications and productivity enhancing tools. In addition, the subscription-based model from the ‘as-a-service’ paradigm help drive recurring revenues resulting in high earnings and cash flow visibility. Many software platforms benefit from scale and network effects that generate high rates of return from incremental capital invested.

If this pandemic has taught us anything, it has demonstrated our ability to leverage technology to work from home. A Gartner Inc. HR survey revealed that 50% of organizations reported 81% or more of their employees are working remotely during the pandemic. In a post-pandemic world, we believe that work from home arrangements could become more mainstream thus driving continued demand for work from home-oriented solutions (remote access connectivity, online collaboration, cybersecurity, streaming and cloud infrastructure). Post-pandemic, 41% of employees are likely to work remotely at least some of the time according to Gartner.

Overall, the technology sector remains an attractive structural growth story. The digital transformation opportunity, which is underpinned by enabling technologies such as cloud, hyper connectivity (e.g. 5G), digital media, e-commerce, payments and intelligent automation, provides many avenues for growth both in the near and long term. Disruptive emerging technologies, such as artificial intelligence, are expected to reshape business models and drive economic value add in the global economy. Stocks in our portfolio are uniquely positioned to benefit from this growth given their respective market position in the products and services they offer as well as degree of innovation that enhances competitive moats.

Portfolio Review

Brompton Tech Leaders Income ETF (the “Fund”) was down 15.9% in Q1 versus the S&P 500 Information Technology Index, which was down 11.9%, and the S&P 500 Index which was down 19.6%.

The Fund is overweight technology-related sub sectors such as interactive media and internet media given its holding in Alphabet and Amazon with the latter being resilient during the market sell off (up 5.5%). In the current environment Amazon continues to benefit from increased demand for e-commerce given its massive scale.

In the semiconductor subsector, the Fund is slightly underweight. During the quarter we exited our holdings in Texas Instruments and Marvell Technology as we felt the risk-reward was not justified given headwinds in the end-markets in which they operate. We entered a position in Nvidia given the company’s exposure to the data center market which is seeing continued demand in the current environment. In addition, Nvidia is a market leader in machine learning processing which provides an attractive risk-reward prospect in the long-term.

The Fund is underweight software given the relatively large weight of Microsoft in the index (20.3% of the benchmark vs 6.6% of the portfolio). Top performing software positions include ServiceNow (up 1.5%) and Microsoft (up 0.3%). We continue to have a favourable view of the software subsector which offers both growth and defensive characteristics as its subscription-based model helps drive recurring revenues resulting in high earnings and cash flow visibility.

Our market weight position in IT services negatively impacted the Fund's performance. However relative to the benchmark performance was on par. Our positions in Visa, Mastercard, Accenture and Fiserv were down 18% on average. We continue to have a favorable view on the subsector given the long-term trends from digital transformation and we like the oligopolistic position of Visa and Mastercard in the payment networks.

The Fund benefitted from its significant underweight position in hardware as a result of the disproportionate weight of Apple in the benchmark 20% vs 7.4%. Apple was down 13% but its impact to the Fund was ~100 bps.

A large overweight position in the electronic equipment subsector negatively impacted the Fund's performance. Our holdings in Keysight, Amphenol and CDW were down 28.5% on average. Demand for sensors, electronic components, related test equipment and network equipment is expected to slowdown in the near-term. However longer-term trends in automotive markets (autonomous driving), industrial (IoT), data centers (increasing scale) and 5G continue to remain favorable.

Laura Lau, SVP & CIO

Michael D. Clare, VP & PM

Annual Compound Returns[1]	1-Year	3-Year	5-Year	Since Inception[2]
Brompton Tech Leaders Income ETF (CAD Hedged)	(2.1%)	13.0%	9.8%	9.5%
S&P 500 Information Technology Index	10.4%	17.6%	17.0%	16.4%
S&P/TSX Composite Index	(14.2%)	(1.9%)	0.9%	2.8%

[1] Returns are for the periods ended March 31, 2020. The table shows the Fund's compound returns for each period indicated compared with the S&P/TSX Composite Index (''Composite Index'') and the S&P 500 Information Technology Index (''Technology Index'') (together the "Indices"). 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 Technology Index, a sub-index of the S&P 500 Index, tracks the performance of major North American technology companies on a market weight basis. Since the Indices contain a substantially larger number of companies, it is not expected that the Fund's performance will mirror that of the Indices. The Indices are calculated without the deduction of management fees, fund expenses and trading commissions, whereas the performance of the Fund is calculated after deducting such fees and expenses.

[2] Inception Date May 20, 2011.

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