BROMPTON FUNDS

Brompton Insights

November 2020

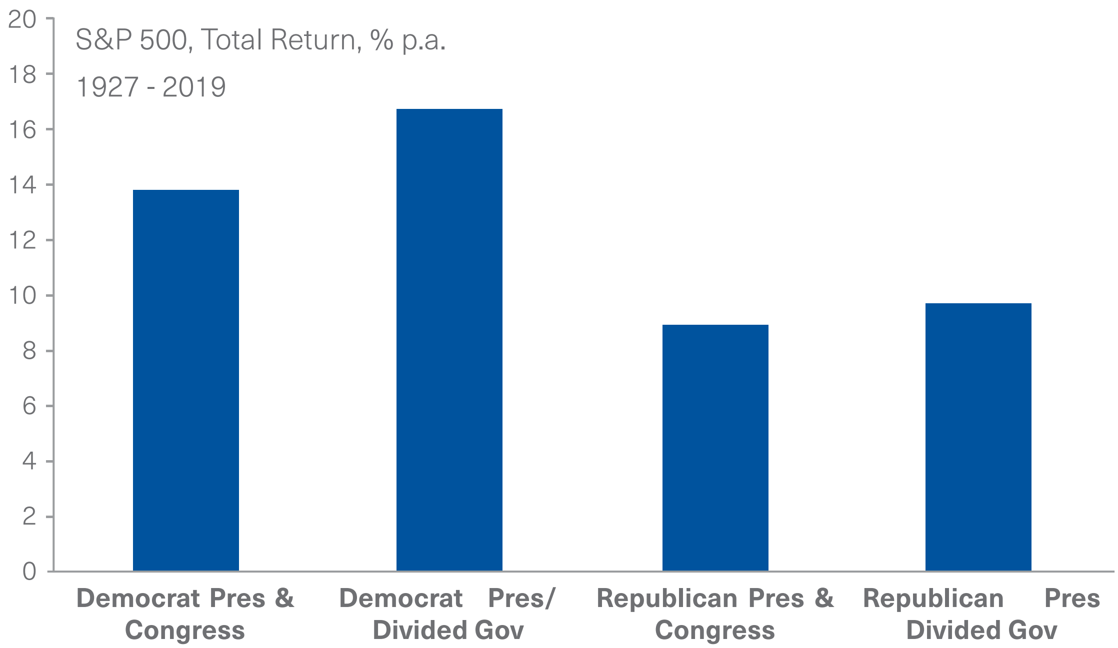
Post election, where do we go from here?

Fund in focus: Brompton Global Real Assets Dividend ETF (BREA)
Brompton North American Financials Dividend ETF (BFIN)
Brompton Global Healthcare Income & Growth ETF (HIG)
Brompton Tech Leaders Income ETF (TLF)

Despite legal challenges, all indications are that Joe Biden has been elected the 46th President of the United States. President-elect Joe Biden will likely have to work with a Republican Senate majority, but the final result will depend on the two Georgia run-off Senate elections on January 5, 2021. A divided government would mean that the major legislative changes proposed and supported by Biden and the Democratic party, including a substantial fiscal stimulus and higher individual and corporate tax rates, are unlikely to materialize. The US$2.2 trillion fiscal stimulus package proposed by Democrats is unlikely to be passed if Republicans retain control of the Senate; but we still expect a fiscal package in the US$1 trillion range. Albeit at less than half of the original proposal, we believe the injection of additional liquidity into the U.S. economy is beneficial for equity markets. The removal of election uncertainly will likely drive up inflation expectations. Additionally, any vaccine related progress will help speed up the economic recovery.

A divided government has historically been beneficial for the stock market (Exhibit 1). Overall, the S&P 500 performance is better under Democratic presidents, with an average return of 14.6% per annum since 1927. The average return is even higher when a Democratic president is combined with a divided Congress, yielding an average return of more than 16% per annum since 1927.

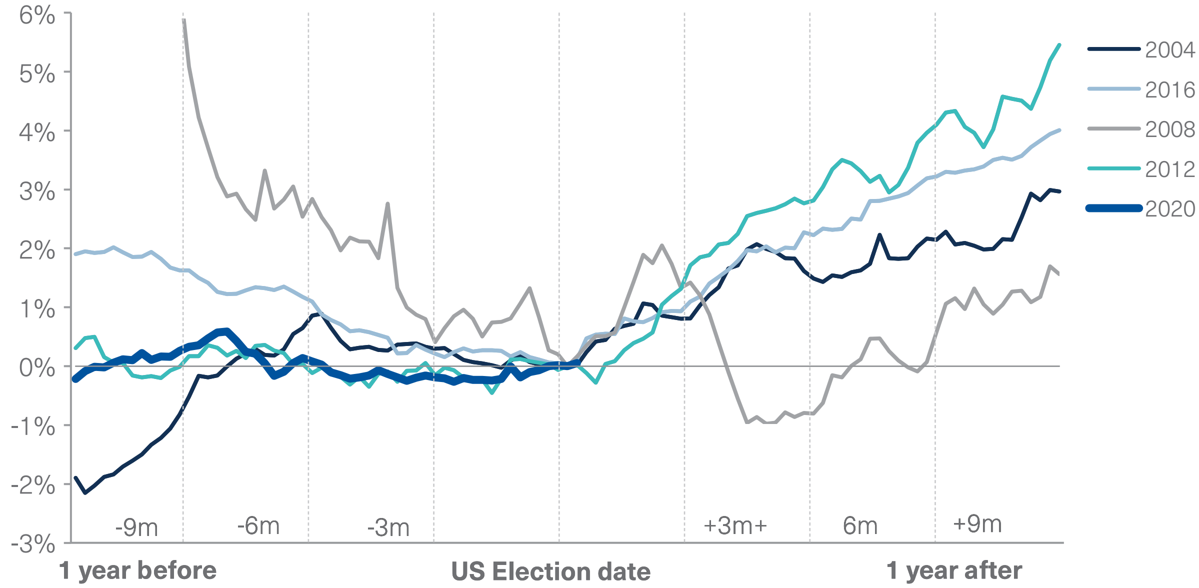
U.S. Market Returns by Political Configuration



Source: Bloomberg, August 2020.

Fund flows also point to a more constructive setup for equities post-election. Equity fund flows tend to be negative ahead of election day and rise substantially post election as election risks abate. As evident from the chart below, equity fund flows post U.S. presidential elections since 2004 tend to be strong in December and tend to continue into the following year.

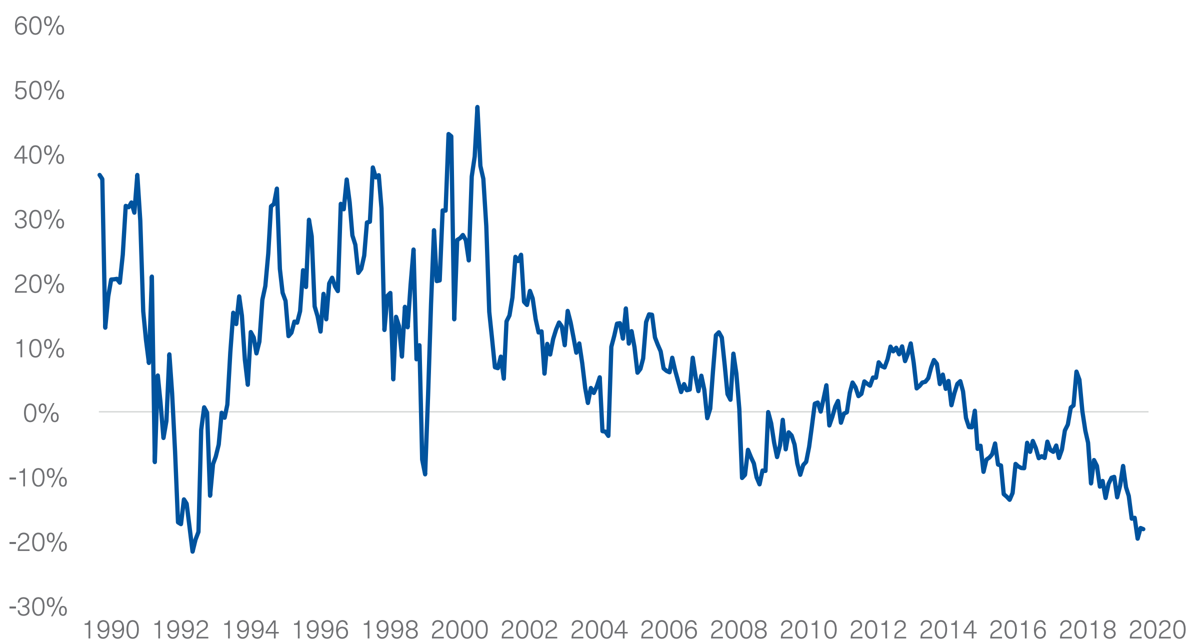
Exhibit 2: Global equity fund flows as a % of AUM around U.S. presidential elections since 2004



Source: Goldman Sachs as of Nov 4, 2020.

The outcome of the U.S. presidential election has major implications for individual sectors. The market started pricing in a Democratic sweep since the beginning of October, which sparked a major rally in pro-cyclical sectors including Industrials and Consumer Discretionary, as well as Utilities companies, especially those with meaningful renewables exposure. Investor sentiment was bearish for Healthcare, Financials and Information Technology. A divided government will partially reverse investor sentiment in the other direction.

Exhibit 3: U.S Healthcare Sector FY2 P/E Premium & Discount vs S&P 500 Premium/Discount



Source: Bloomberg as of October 31, 2020.

Health Care

Prior to the election, Healthcare stocks priced in a high probability of a Blue Wave: expectation of major legislative changes around drug pricing, Medicare negotiations and tax increases were high as health policy is perceived to be a major legislative focus for the Biden administration. This led to depressed valuations of the sector as a whole (Exhibit 3) an 18.1% discount vs the S&P 500 on October 31, a record valuation discount since 1992) and especially the

Pharmaceutical and Managed Care subsectors. A Republican controlled Senate implies that the Senate Democrats have a slim chance at eliminating the filibuster, which significantly reduces the regulatory risks for major pharmaceutical companies. We believe the current valuation presents an attractive entry point. Furthermore, the Healthcare sector has historically outperformed the S&P 500 during the 6 months following presidential elections. This is because the incoming president typically outlines health care policy decisions early on during the presidency, thereby removing any political and regulatory uncertainty/overhang for the sector.

Information Technology

Tax-related considerations will have a lesser impact on the sector, yet it's exposed to its own unique set of election risks. On one hand, the Biden administration is expected to adopt a more accommodative trade policy with China than under the Trump administration. The semiconductor subsector has the highest percentage of sales to China; any relaxation of trade policy will be accretive to the sector. For this sector, Biden has also proposed increasing research and development and bringing more manufacturing back to U.S. soil. On the other hand, mega tech companies will likely continue to face pressure from regulators. Data privacy regulation is a bi-partisan issue. We see the prospect of a new law to enhance the Federal Trade Commission's oversight power and new regulations around data usage, even under a divided congress. Large tech companies will likely face increased compliance costs and more intense competition. Any acquisitions will likely undergo extensive review and face increased scrutiny from regulators.

Utilities and Energy

Utilities are set to benefit from a Biden administration given Biden's focus on clean energy. During his campaign, Biden set the ambitious goal of investing US$2 trillion into clean energy and targeted 100% carbon-free electricity production by 2035. Under a Republican Senate, the extent of the program could be smaller an expected, though any type of clean energy regulation would be accretive to rate base growth. We believe the shift towards renewable energy is a powerful underlying trend for Utilities for years to come. We also see potential for renewable credit extension for renewable energy producers, which should further propel traditional fossil fuel producers to transition into clean energy production.

Financials

There are two opposing factors impacting the sector as a result of the U.S. election. First, expectations of a Blue Wave drove up inflation expectations prior to election day; however, a divided government accompanied diminishing prospect of a sizable fiscal stimulus, which in turn drove a compression in the yield curve. A flattened yield curve and low U.S. 10-year yield would imply no meaningful uplift to banks' net interest margin. Second, the diminished risk of a corporate tax raise is a positive for U.S. banks. U.S. banks tend to earn more domestic income compared to other sectors, which would have been severely impacted by meaningful hike in corporate tax rate. Tighter regulation is unlikely since confirmations would have to be approved by a Republican Senate. We think ultimately, inflation expectations need to improve for Financials to see a sustainable rally and vaccine optimism could be the trigger.

Brompton's Approach

Healthcare has been a laggard; however, with most of the worst-case scenarios out of the way, the sector has become more investable through Brompton Global Healthcare Income & Growth ETF (HIG). The same is true for Financials which would have taken a big earnings hit with the proposed tax hike that is highly unlikely to be passed. Brompton North American Financials Dividend ETF (BFIN) has over 60% invested in U.S. Financials. In Brompton's broad mandates, we are overweight renewable energy with the highest weight at nearly 40% in Brompton Global Real Assets Dividend ETF (BREA). Technology needs an active approach to navigate the political landscape. That's why Brompton Tech Leaders Income ETF (TLF) takes an active approach to balance the risks and growth opportunities in this face-paced and evolving sector.

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VALUE

INTEGRITY

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