Brompton North American Low Volatility Dividend ETF

BROMPTON FUNDS

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Global Markets Review

The global economic reopening remains on track as the vaccine rollout gathers pace. All in all, global markets finished the quarter with solid performance, especially for pro-cyclical sectors, as several of them enjoyed double digit returns. The MSCI World Index gained 13.3% with the Energy sector being the best performer, gaining 33.2% during the first half of 2021; Financials was the second-best performing sector returning 21.1%, outperforming the MSCI World Index by 7.8%. In North America, the S&P 500 was up 15.2%, also led by the Energy sector, while the S&P/TSX Composite was up 17.3%, with Energy and Financials as the top performing sectors. In Europe, the STOXX 600 was up 15.8% for the first half of this year. France and Italy continued to be the best-performing countries, where CAC 40 and FTSE MIB were up 19.5% and 14.7%, respectively. Germany's DAX gained 13.2%. Spain and the U.K. also finished 1H21 with solid returns as the IBEX 35 and FTSE 100 increased 10.5% and 10.9%, respectively.

During the first half of 2021, global economies continued the path to recovery. U.S. Manufacturing PMI entered June at 60.6 after peaking at a record high of 64.7 in April, while the unemployment rate continued to decline, reaching 5.9% in June. In the U.S., Biden's sharp focus on immunization efforts in combination with unprecedented fiscal stimulus pushed stock markets to new highs by the end of 1H21. Global yield curves were mainly subdued in Q2 and flattening in June, with the U.S. 5 year to 30 year Treasury spreads narrowing to August 2020 levels. The U.K. yield curve also mirrored its U.S. peers. This has driven the sector rotation back from value to growth in the past month. Cyclical parts of the economy led the equity market rally during the first half of this year, with Energy, Industrials and Financials gaining the most, even though Financials were negatively affected by flattening yield curves in June. Performance of Information Technology stocks was lackluster during Q1, due to investor sentiment shifting away from large capitalization growth names, but they have had a big run since mid-May as investors took some profits and rotated back to high-growth names, sending both the S&P 500 and NASDAQ to new highs in June. Pro-cyclical stocks are still favored, while the risk-on mentality would keep sending growth stocks higher.

During the second quarter, several central banks in developed economies started to gradually shift their monetary policy stance amid growing concern over inflationary risks. During the June Federal Open Market Committee (FOMC) meeting, despite no policy rate hike, the Federal Reserve's dot-plot projections indicated at least two rate hikes in 2023, signaling an earlier than expected tightening. In response to inflation concerns, the Fed also lifted its inflation expectations to 3.4%, 100 bps above its previous estimate. Potential tapering of the bond-purchase program could commence late 2021 or early 2022. On the fiscal front, President Biden signed a US$1.9 trillion pandemic relief bill in March, titled the American Rescue Plan, into law. The plan includes additional stimulus cheques, enhanced unemployment aids, rental assistance, and childcare support among other assistance. In late June, a bipartisan group of senators and the White House reached a preliminary agreement on a potential $1.2 trillion infrastructure package. While the details are still under discussion, the bill would be another wave of robust fiscal stimulus.

By the end of the second quarter, the number of confirmed infections worldwide exceeded 183 million, about 2.15 times greater than the number of infections at the end of 2020. On the other hand, global vaccination efforts are well underway, with 47% of the population fully vaccinated in the U.S. and 31% in Canada. According to the latest World Economic Outlook update issued by the International Monetary Fund (IMF) in April 2021, the global economy is projected to grow 6.0% in 2021, up from the previous forecast of 5.2%. The contraction of 2020 was also smaller than the previous projection due to outsized growth in the second half of 2020, driven by the easing of lockdown measures. However, there still remains a high degree of uncertainty surrounding the global economic outlook, such as whether the current vaccines are effective again new COVID-19 strain, capacity adjustments in the economy, and effectiveness of global policies.

Looking forward to the rest of 2021, with a growing percentage of the population fully vaccinated, the U.S. labor market recovery is accelerating so we expect to see further decline in the unemployment rate and pickup in labor force participation. Meanwhile, household savings have piled up in the past year to support strong spending, as more states open for business. On the monetary policy front, we believe Fed tapering is not likely until the last quarter this year or first quarter next year. On the fiscal policy front, the Biden administration is laser-focused on boosting economic growth through the American Rescue Plan, which should be supportive of further economic recovery.

Portfolio Review

Brompton North American Low Volatility Dividend ETF (the "Fund") focuses on lowering total portfolio volatility through investing in a diversified blend of North American equities with a minimum market cap of $5 billion. During the first half of the year, BLOV was up 5.1% versus the MSCI Minimum Volatility USA Index (the "Benchmark"), which was up 9.3%.

The Fund was significantly overweight the Consumer Staples sector relative to the Benchmark, which detracted somewhat from performance as the sector underperformed during the period. Top performing holdings include Loblaw (+26%), Archer Daniels Midland (+22%) and Costco (+5%). The Fund was overweight Utilities, which also contributed to underperformance relative to the Benchmark. The top performer in this sector was Brookfield Infrastructure (+15%).

The Fund was also underweight Financials and Information Technology, both of which contributed to underperformance as these sectors performed well. Given the higher volatility nature of these sectors, we remain underweight.

The Fund benefited from an overweight position in Consumer Discretionary, which contributed to outperformance relative to the Benchmark. Top performing holdings include Target (+38%) and Garmin (+3.7%). A market weight position in Communication Services also contributed to Fund's performance versus the Benchmark as a result of strong stock selection. Top performing holdings include BCE (+19%) and Telus (+16%).

In 2020, for the first time in over a decade, the low volatility factor produced a full year of negative returns. In 1H 2021 poor performance has persisted, with the low volatility factor continuing its negative streak (along with negative performance from all other factors except value). This is attributed to heightened interest rate volatility given reflation of the yield curve due to fiscal stimulus - bond market turbulence can lead to equity investors making sudden shifts in factor allocations. In our view, this short-term data point does not signify either a trend or an inflection point given the long historic outperformance of the low volatility factor. Although the low volatility factor has underperformed, we note that the low volatility factor has generated a positive premium in every decade since 1929, with a higher level of statistical significance than the other factors[1]. We expect the low volatility factor to mean-revert to its historical performance premia over time as excessive risk taking by investors makes low volatility equities relatively underpriced, which bodes well for long- term risk-adjusted returns for the low-volatility factor.

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Annual Compound Returns[1]	YTD	1-YR	Since Inception[2]
Brompton North American Low Volatility Dividend ETF	5.1%	15.7%	14.4%
MSCI USA Minimum Volatility Gross TR USD Index	9.3%	23.6%	21.5%

(1) Blitz, David and van Vliet, Pim and Baltussen, Guido, The Volatility Effect Revisited (August 26, 2019).

(2) Returns are for the periods ended June 30, 2021 and are unaudited. The table shows the Fund's compound returns for each period indicated compared with the MSCI USA Minimum Volatility Gross TR USD Index ("Minimum Volatility Index"). The Minimum Volatility Index is designed to reflect the performance characteristics of a minimum variance strategy applied to the large and mid cap U.S. equity universe. The Minimum Volatility Index is calculated using Barra Optimizer to optimize its MSCI parent index for the lowest absolute volatility with a certain set of constraints. The Fund invests in equities from North American issuers with a minimum market cap of $5 billion and employs quantitative analysis with an active fundamentals overlay to construct a portfolio with lower overall volatility than the market. It is therefore not expected the Fund's performance will mirror that of the Index. Further, the Index is 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.

(3) Inception date April 30, 2020.

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