

**PORTFOLIO MANAGER COMMENTARY - SEPTEMBER 30, 2021****Global Markets Review**

Following a stormy month in September, global equity markets narrowly extended positive gains during the quarter. For the three-month period ending September 30, 2021, the MSCI World Index edged up 0.1%, led by the Financials sector, which gained 2.2%; Energy was the second-best performing sector, rising 1.6% during the quarter and boosted by robust oil and gas prices. In North America, the S&P 500 was up 0.6%, also driven by Financials, while the S&P/TSX Composite was up 0.2%, with Consumer Staples and Industrials as the top performing sectors. In Europe, the STOXX 600 rose 1.0% during the quarter. Italy and the U.K. were the best-performing countries, where the FTSE MIB was up 3.0% and the FTSE 100 was up 1.9%. CAC 40 and IBEX 35 ticked up 0.4% and 0.3%, respectively. Switzerland and Germany finished the period in negative territory, down 2.4% and 1.7%, respectively.

Global economies continued the path to recovery through the third quarter, while sentiment on the growth deceleration has weighed on the market. U.S. manufacturing PMI came in at 61.1 for September, the strongest reading during the quarter, while the unemployment rate also saw sequential improvement. Nonetheless, inflationary pressures remained elevated, with August core CPI at 4%, despite dropping from the June high (4.5%). Global yields spiked after bottoming in August. The U.S. 10-year Treasury yield peaked above 1.5% after a mildly hawkish Federal Open Market Committee (FOMC) meeting. The U.K. 10-year Gilts also mirrored its U.S. peer, touching 1% for the first time since May 2019. These triggered market selloffs of high-growth names especially among Information Technology and Healthcare sectors in the back half of September, while value stocks in Financials and Energy sector were buoyed on the back of rising yields. Although growth still outperformed value during the quarter, the gap has narrowed since mid-September, which coincides with rising yields. At the same time, uncertainties around China's slowing economic momentum and contagion risks due to the property developer Evergrande's debt crisis also sent market volatility higher in September.

There were few major monetary policy changes among global central banks in developed economies during the quarter, with inflationary pressures becoming the key variable for the pace of policy shifts. The Federal Reserve left the policy rate unchanged at 0%-0.25% at the September FOMC meeting, while acknowledging that "a moderation in the pace of asset purchases may soon be warranted". The latest median dot plot projects the fed funds rate at 1% by the end of 2023 and 1.75% by the end of 2024. Moreover, the 2021 inflation outlook was substantially lifted again to 4.2%, 80 bps above the June estimate, reflecting stickier inflation than had previously been expected. Real GDP forecast for the year was also revised down to 5.9% from 7%, implying headwinds in the near-term economic growth outlook.

In Canada, the Bank of Canada (BoC) kept all policy variables unchanged in the September statement, including the overnight policy rate at 0.25% and government bond purchases at C\$2 billion per week. On inflation, the central bank still saw the current spike as transitory, highlighting that wage increases have been moderate and medium-term inflation expectations are well anchored. BoC Governor Tiff Macklem also released a roadmap to exit monetary stimulus, outlining that once the new stimulus is removed the first step would be to move to the reinvestment phase of the QE program (most likely cutting bond purchases from C\$2 billion per week to C\$1 billion). He also reiterated that the reinvestment would be maintained well past the initial rate hikes.

The European Central Bank (ECB) kept the benchmark interest rate unchanged at -0.50%. President Christine Lagarde repeated in September that the upswing in inflation was temporary, and that base effect and rising energy prices would not result in lasting inflation. The Governing Council decided to moderately lower the pace of purchases under the pandemic emergency purchase program (PEPP) from that of the past two quarters, with an unchanged envelope of EUR1.85 trillion through the end of March 2022 at the least. Purchases under the asset purchase program (APP) will progress at a monthly pace of EUR20 billion. The ECB raised their projections on 2021 annual real GDP growth for the euro area to 5% from 4.6% in the June assessment and annual inflation rate to 2.2% from 1.9% in June. Despite the bullish tone on the economic rebound, it is still too early to call for an end of the PPEP, as the decision will still depend on upcoming economic data before the December meeting. The Bank of England (BoE) voted in September to keep the policy rate unchanged at 0.1% and maintain the asset purchase target of £875 billion, while revising down the Q3 GDP forecast to 2.1% from 2.9%. BoE also reiterated that it expected CPI inflation to rise slightly above 4% this year, double its target, largely on the back of upside risks posed by hefty energy and goods prices. On the political front, Olaf Scholz of the Social Democrats narrowly led Chancellor Angela Merkel's Conservatives in the German election. This narrow victory suggests that long negotiations lie ahead before a coalition government can emerge, which could raise extended period of market and policy uncertainties.

According to the statistics compiled by the World Health Organization, the number of confirmed infections worldwide exceeded 233 million by the end of September, while the weekly cases have continued to drop after peaking in August. On the other hand, global vaccination efforts are well underway, with 70% of the population fully vaccinated in Canada and 56% in the U.S. However, due to fears of vaccine effectiveness against the Delta variant and delay of the vaccine rollout for ages 5-11 in the U.S., the pace of reopening was slower than previously anticipated during the third quarter. Fiscal support in Q3 was a mixed bag. The American Rescue Plan, along with other assistances such as Child Tax Credit, continued enhancing household savings, which were channeled into consumer spending amid reopening. Furthermore, the U.S. Senate passed a \$1.2 trillion infrastructure package in August, with the House vote delayed to the end of October. However, as many fiscal stimuli are fading, the fiscal impulse on growth could turn negative next year according to Goldman Sachs.

Looking ahead to the rest of 2021, sector rotations into value and cyclical could persist if the yield curve finds its support and ticks up. However, volatility would potentially linger into the fourth quarter given rising inflation expectations and contracting monetary gauges, as well as global supply chain issues and China's growth deceleration. Market leaderships would be rotating among value/growth and cyclical/defensive alternatively within short timeframes. In this regard, the barbell approach to our portfolios is still the preferred strategy, supplemented by opportunities in the covered call writing amid high volatility risk in the near term. We expect to have clearer visibility after upcoming waves of corporate earnings for Q3 and key economic releases. At the same time, widening vaccine coverage, resilient fiscal support, and abundant household savings should keep fueling economic growth.

## **Portfolio Review**

Brompton Split Banc Corp. (the "Fund") invests in a portfolio consisting primarily of the six largest Canadian banks as well as up to 10% of the portfolio can be invested, from time to time, in global financial companies through an investment in the Brompton North American Financials ETF ("BFIN"). BFIN is an exchange-traded fund that invests in the equity securities of North American financial services companies with a market capitalization of at least \$5 billion.

In Q3 the Fund was up 0.6% versus the S&P/TSX Financials Index, up 1.1%, and the S&P/TSX Banks Index, which was down 0.2%. We continue to have a positive view of Canadian banks as increasing COVID-19 vaccinations rates provides strong support for economic recovery. Meanwhile, a U.S. Treasury yield spike after a more hawkish FOMC meeting helped Canadian banks rebound from the quarter low. Profitability has seen improvement in Q3, while loan growth is on an upward trend. We believe these factors will provide a tailwind to bank bottom-line growth in the coming quarter, but it is still too complacent to call for "normalized" earnings as consumer activity remains subdued, and deposit and capital levels stay elevated. Capital ratios for the large Canadian banks are at historically high levels after a further uptick from Q2. Following the US and UK, we anticipate that the regulator will relax the restrictions on dividend increases and share buybacks by year-end. We believe that raising the domestic stability buffer (DSB), effective October 31, 2021, is the first step before OSFI removes the aforementioned restrictions and the increase in the DSB suggests confidence in the current economic environment and bank capital levels. Provisions for credit losses at Canadian banks continue to moderate as we expected, with a net recovery position in Q3 compared to a charge during the same period last year. Canadian banks remain undervalued on a forward P/E and P/B basis, after normalizing 2022E core EPS and factoring in the banks' excess capital. We believe there is room for multiple expansion as the economy continues to improve in a post pandemic world.

The Fund benefited from its holdings in BFIN, which was up 2.8%. BFIN's performance was driven by its overweight exposure in Data Processing & Outsourced Services, Investment Banking, and Asset Management.

Laura Lau, SVP & CIO

Michael D. Clare, VP & PM

Annual Compound Returns <sup>1</sup>	YTD	1-YR	3-YR	5-YR	10-YR	Since Inception <sup>2</sup>
Brompton Split Banc Corp. - Class A	47.9%	99.7%	13.2%	16.7%	17.0%	12.2%
S&P/TSX Capped Financials Index	24.8%	45.6%	10.9%	12.0%	12.4%	8.9%
Brompton Split Banc Corp. - Preferred	3.8%	5.1%	5.1%	5.0%	4.9%	5.1%
S&P/TSX Preferred Share Index	17.4%	26.0%	5.1%	7.3%	3.3%	3.0%
Brompton Split Banc Corp. - Unit	28.5%	51.6%	9.6%	11.8%	11.6%	9.0%

<sup>(1)</sup> Returns are for the periods ended September 30, 2021 and are unaudited. The table shows the Fund's compound return on a Class A share, Preferred share and unit for each period indicated compared with the S&P/TSX Capped Financials Index ("Financials Index") and the S&P/TSX Preferred Share Index ("Preferred Index") (together the "Indices"). The Financials Index is derived from the Composite Index based on the financials sector of the Global Industry Classification Standard. The Preferred Index tracks the performance, on a market weight basis, of a broad index of preferred shares trading on the TSX that meet the criteria relating to size, liquidity and issuer rating. The Fund passively invests on an approximately equal weight basis in a portfolio comprised of six Canadian banks which are in the Financials Index but may hold up to 10% of its assets in global financial services companies. Since the Indices have more diversified portfolios, it is not expected that the Fund's performance will mirror that of the Indices. The Indices are calculated without the impact of management fees, fund expenses and trading commissions, whereas the performance of the Fund is calculated after deducting such fees and expenses. Further, the performance of the Fund's Class A shares is impacted by the leverage provided by the Fund's Preferred shares.

<sup>(2)</sup> Inception Date November 16, 2005.

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You will usually pay brokerage fees to your dealer if you purchase or sell shares of the Fund on the Toronto Stock Exchange or other alternative Canadian trading system (an "exchange"). If the shares are purchased or sold on an exchange, investors may pay more than the current net asset value when buying shares of the investment fund and may receive less than the current net asset value when selling them.

There are ongoing fees and expenses associated with owning shares of an investment fund. An investment fund must prepare disclosure documents that contain key information about the Fund. You can find more detailed information about the Fund in the public filings available at [www.sedar.com](http://www.sedar.com). The indicated rates of return are the historical annual compounded total returns including changes in share value and reinvestment of all distributions and do not take into account certain fees such as redemption costs or income taxes payable by any securityholder that would have reduced returns. Investment funds are not guaranteed, their values change frequently and past performance may not be repeated.

Certain statements contained in this document constitute forward-looking information within the meaning of Canadian securities laws. Forward-looking information may relate to matters disclosed in this document and to other matters identified in public filings relating to the Fund, to the future outlook of the Fund and anticipated events or results and may include statements regarding the future financial performance of the Fund. In some cases, forward-looking information can be identified by terms such as "may", "will", "should", "expect", "plan", "anticipate", "believe", "intend", "estimate", "predict", "potential", "continue" or other similar expressions concerning matters that are not historical facts. Actual results may vary from such forward-looking information. Investors should not place undue reliance on forward-looking statements. These forward-looking statements are made as of the date hereof and we assume no obligation to update or revise them to reflect new events or circumstances.



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#### Investor Relations

PHONE 416.642.6000  
TOLL FREE 1.866.642.6001  
FAX 416.642.6001  
EMAIL [info@bromptongroup.com](mailto:info@bromptongroup.com)

#### Website

[www.bromptongroup.com](http://www.bromptongroup.com)

#### Address

Bay Wellington Tower,  
Brookfield Place  
181 Bay Street  
Suite 2930, Box 793  
Toronto, Ontario M5J 2T3