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

BROMPTON FUNDS

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.

Technology Sector Review & Outlook

We continue to reiterate our positive outlook for the technology sector given attractive fundamentals; increase enterprise and consumer demand driving top line growth and cash flow generation with innovation expanding market opportunities. The pandemic accelerated the digital transformation trends that had already been in motion and we see these trends (cloud, 5G, intelligent automation and Internet of Things) continuing to grow. We note that digital transformation is a long-tailed opportunity for the technology sector.

Global IT spending is expected to rebound in 2021, up 8.6% to $4.2 trillion according to Gartner. Growth is expected to be driven by devices (up 14% Y/Y) as a hybrid work from home environment boosted demand for laptops and tablets while the 5G cycle continues to trickle-demand for hardware upgrades. Enterprise software is expected to grow 13% to $600 billion in 2021 as organizations shift their focus to providing a more comfortable, innovative, and productive environment for their workforce. Data center spending is projected to grow of 7.4% in 2021 as providers accelerate data center build out given the increasing demand for cloud computing and resumption of enterprise data center expansion. Overall, IT spending continues to be robust as economies reopen and large-scale system deployment slowly hit a cadence.

The global semiconductor market is firing on all cylinders with growth projected to increase 24% in 2021 breaking the $500 billion level for the first time in history according to IC Insights. Every major general-purpose analog and application-specific analog market segment is expected to post a double-digit increase in 2021 according to IC Insights. An unexpected robust demand for semiconductor chips in data centers and consumer devices during the pandemic along with strong recovery in cyclical industries have overwhelmed the supply chain causing industry wide shortages that could last well into 2022 according to Bloomberg. The semiconductor industry continues to drive innovation, as large players are expected to shift their process technology from 5 nanometer to 3 nanometer later this year with 2 nanometer expected to be commercialized in 2024 using next generation extreme ultraviolent lithography systems according to Bloomberg. These next generation chips will be used for 5G and artificial intelligence systems such as self-driving and automation.

During Q3, significant changes in yields drove factor rotations away from growth into value, with value outperforming growth by 386 bps according to Bloomberg. The heightened volatility around interest rates would contribute to frequent rotations between growth and value in our view. Our portfolio is well position to benefit from these factor rotations given our barbell approach in actively managing over weights on growth and value styles.

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 and quantum computing, 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 up 0.5% in Q3 2021 versus the S&P 500 Equal Weighted Information Technology Index, which was down 0.4%.

The Fund's overweight exposure to software contributed to outperformance relative to the benchmark. Top performing holdings Fortinet (up 22.6%), ServiceNow (up 22.6%) and Cadence (up 10.7%).

An underweight exposure to semiconductors did not overly detract from the Fund's performance, which was ahead of the benchmark. Top performing holdings include ASML (up 7.9%), NXP (up 3.8%) and Nvidia (up 3.6%).

The Fund's underweight exposure in IT services underperformed the benchmark. Top performing holdings include Accenture (up 8.8%) and Paychex (5.4%).

An overweight exposure to hardware negatively impacted performance which lagged the benchmark. Our top performer was Apple (up 3.5%).

The Fund is overweight technology-related sub sectors such as interactive media and internet media given its holdings in Alphabet (up 6.3%) and Amazon (down 4.5%).

Laura Lau, SVP & CIO

Michael D. Clare, VP & PM

Annual Compound Returns[4]	YTD	1-Year	3-Year	5-Year	10-Year	Since Inception[2]	Since Inception[3]
Brompton Tech Leaders Income ETF (CAD Hedged)	12.7%	26.0%	21.7%	24.5%	17.1%	14.7%	-
Brompton Tech Leaders Income ETF (USD)	13.1%	26.6%	-	-	-	-	31.2%
S&P 500 Equal Weight Information Technology Index	14.4%	38.4%	21.4%	24.0%	22.1%	18.4%	28.9%

(1) Returns are for the periods ended September 30, 2021 and are unaudited. The table shows the Fund's compound returns for each period indicated compared with the S&P 500 Equal Weight Information Technology Index ("Technology Index"). The Technology Index, a sub-index of the S&P 500 Index, tracks the performance of major North American information technology companies on an approximately equal weight basis. Since the Technology Index contains a substantially larger number of companies, it is not expected that the ETF's performance will mirror that of the Technology Index. The Technology Index is calculated without the deduction of management fees, fund expenses and trading commissions, whereas the performance of the ETF is calculated after deducting such fees and expenses.

(2) Inception Date May 20, 2011.

(3) Inception Date August 8, 2019.

The Fund has changed its technology benchmark from the S&P Information Technology Index to the S&P Equal Weight Technology Index. The S&P Equal Weight Technology Index tracks the performance of information technology companies included in the S&P 500 Index on an approximately equal weight basis. The S&P Information Technology Index, a sub-index of the S&P 500 Index, tracks the performance of information technology companies on a market cap weighted basis. Since the Fund also invests on an approximately equal weight basis the Manager believes that the S&P Equal Weight Technology Index provides a more comparable benchmark to assess relative performance of the Fund.

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INTEGRITY
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Investor Relations
PHONE 416.642.6000
TOLL FREE 1.866.642.6001
FAX 416.642.6001
EMAIL info@bromptongroup.com

Website
www.bromptongroup.com

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