

Portfolio Manager Commentary - March 31, 2022

Preferred Market Conditions

A new wall of worry began to build as we turned calendars to 2022, with inflation levels unseen in over 30 years, concern that Fed policy is behind the curve, and an unprovoked invasion of Ukraine by Russia in late February. These worries advanced for most of Q1 as interest rates moved higher and the yield curve flattened. Credit spreads widened as credit markets experienced negative flows, and volatility in all markets increased. Spikes in commodity prices related to Russia-Ukraine have only heightened inflation concerns.

Given the sharp rise in interest rates over Q1, portfolio duration has been an important determinant of performance. Our focus on intermediate duration and call protection – owning fixed-reset structures with healthy backend reset spreads and avoiding most low-coupon fixed-rate securities – has resulted in less overall impact from higher rates than some other segments of the preferred market. In fact, if reset today, many of the securities held by our Funds would set at higher rates than their initial front-end coupons (although many won't reset for another 2-5 years). Passive preferred ETFs, in contrast, focus on \$25-par retail preferreds, with a much higher allocation to fixed-rate coupons and longer durations than our Funds. They have had below-average performance year-to-date. Passive ETFs experienced high turnover in recent years due to issuer call options and replaced many of those called securities with newer low-coupon fixed-rate preferreds.

In addition to higher interest rates, credit spreads widened to reflect conditions discussed above – higher inflation, allocations away from credit, and the various economic impacts of the Russia-Ukraine war (sanctions, inflation, political climate, etc). Investors are requiring higher rates of return in all credit sectors, and senior bonds entered 2022 at historically tight levels. Preferreds and contingent capital securities (CoCos) earned extra spread over senior bonds given subordination premiums, and they have weathered the storm comparatively well considering uncertainty in markets.

Outlook

While uncertainty has increased over the last quarter, and we are only one rate hike into a Fed cycle that likely includes at least 6-7 additional hikes, we continue to believe credit quality is a highlight of the preferred and CoCo market. Banks remain very well capitalized, highly regulated, and most are asset-sensitive – which means earnings will increase with higher interest rates. Direct exposure to Russia-Ukraine appears to be limited and contained to manageable earnings events, if anything. Insurance companies have been longing for higher interest rates to boost portfolio yields, and they finally have arrived. Energy issuers, pipelines in our case, have been buoyed by higher commodity prices and potential increases in usage because of a shifting energy landscape. Higher interest rates are likely to be more concerning for high-yield (junk) issuers as they have weaker balance sheets and greater exposure to rising interest costs.

In the long-run, modestly higher interest rates and spreads should be a healthy adjustment for credit markets, including preferreds and CoCos. Investors have struggled to find income for years and have often increased risk chasing income goals. Additionally, higher interest rates could eventually be positive for coupons of certain fixed-reset or floating securities. Ultimately, we believe preferreds and CoCos will provide investment-grade credit risk (low rates of default and deferral), intermediate duration, and a subordination premium that more than compensates for a move down in capital structure.

Nevertheless, there remains much to consider as we navigate the current environment. An overly aggressive Fed, prolonged Russia-Ukraine war causing more severe economic disruptions, COVID resurgence, or other risks could push global economies towards recession. However, preferred and CoCo valuations are attractive, and we look forward to managing the transition to higher rates and taking advantage of dislocations in the market as they present themselves.

Annual Compound Returns ¹	YTD	1-YR	3-YR	5-YR	10-YR	S.I. BPRF ²	S.I. BPRF.U ³
BPRF - Brompton Flaherty & Crumrine Investment Grade Preferred ETF (CAD-H)	(6.0%)	(2.2%)	4.3%	-	-	4.6%	-
BPRF.U - Brompton Flaherty & Crumrine Investment Grade Preferred ETF (USD)	(6.0%)	(2.1%)	-	-	-	-	4.2%
BEPR - Brompton Flaherty & Crumrine <i>Enhanced</i> Investment Grade Preferred ETF (CAD-H)	(8.5%)	(1.2%)	4.5%	4.5%	7.8%	-	-
ICE BofAML 8% Constrained Core West Preferred & Jr Subordinated Securities Index	(6.4%)	(2.5%)	4.5%	-	-	5.3%	3.4%

⁽¹⁾ Returns are for the periods ended March 31, 2022 and are unaudited. The table shows the Fund's compound returns for each period indicated compared with the ICE BofAML 8% Constrained Core West Preferred & Jr Subordinated Securities Index ("Preferred & Jr Subordinated Securities Index"), (the "Index"). The Preferred & Jr Subordinated Securities Index tracks the performance of US dollar denominated high grade and high yield preferred securities and deeply subordinated corporate debt issued in the US domestic market. Qualifying securities must be rated at least B3, based on an average of Moody's, Standard & Poor's and Fitch and have a country of risk of either the U.S. or a Western European country. 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. Past performance does not necessarily indicate how the Fund will perform in the future. The information shown is based on Net Asset Value per unit and assumes that distributions made by the ETF on its units in the period shown were reinvested at Net Asset Value per unit in additional units of the Fund.

⁽²⁾ BPRF inception date October 15, 2018.

⁽³⁾ BPRF.U inception date August 8, 2019.

The benchmarks from ICE Data Indices, LLC ("ICE Data") are used with permission. ICE Data, its affiliates and their respective third-party suppliers disclaim any and all warranties and representations, expressed and/or implied, including any warranties of merchantability or fitness for a particular purpose or use, including the indices, index data and any data included in, related to, or derived therefrom. Neither ICE Data, its affiliates nor their respective third-party providers shall be subject to any damages or liability with respect to the adequacy, accuracy, timeliness or completeness of the indices or the index data or any component thereof, and the indices and index data and all components thereof are provided on an "as is" basis and your use is at your own risk. ICE Data, its affiliates and their respective third-party suppliers do not sponsor, endorse, or recommend the Fund.

This document is for information purposes only and does not constitute an offer to sell or a solicitation to buy the securities referred to herein. The opinions contained in this report are solely those of Flaherty & Crumrine Incorporated ("F&C") and are subject to change without notice. F&C makes every effort to ensure that the information has been derived from sources believed to be reliable and accurate. However, F&C assumes no responsibility for any losses or damages, whether direct or indirect which arise from the use of this information. F&C is under no obligation to update the information contained herein. The information should not be regarded as a substitute for the exercise of your own judgment. Please read the prospectus before investing.

Commissions, trailing commissions, management fees and expenses all may be associated with exchange-traded fund investments. Please read the prospectus before investing. The indicated rates of return are the historical annual compounded total returns including changes in unit value and reinvestment of all distributions and do not take into account sales, redemption, distribution or optional charges or income taxes payable by any securityholder that would have reduced returns. Exchange traded 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.



VALUE
INTEGRITY
PERFORMANCE
THE FOUNDATION FOR EXCELLENCE

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