Brompton Global Healthcare Income & Growth ETF (TSX:HIG; HIG.U)

BROMPTON FUNDS

Portfolio Manager Commentary - March 31, 2022

Global Markets Review

First quarter of 2022 was a difficult start after a stellar 2021, with a majority of global equity markets experiencing turbulent performance. The Russia-Ukraine war, monetary uncertainty, and inflation concerns fueled a rise in market anxiety. For the three-month period ended March 31, 2022, the MSCI World Index fell by 5.0%. The index fell to the quarter-low in early March, followed by a sharp rebound through month-end. Energy was the best-performing sector, up 31.0%, while Consumer Discretionary was the bottom-performing sector, down 10.6%. In North America, the S&P 500 dropped 4.6%, while the S&P/TSX Composite gained 3.8%, well ahead of most global equity markets. The energy sector was the top performer in both the S&P 500 and S&P/TSX Composite. In Europe, the STOXX 600 was down 5.9%. The U.K. was the only developed European market that a registered positive return, with FTSE 100 up 2.9%. Spain and Switzerland fell by -2.6% and -4.3% respectively. France, Italy, and Germany also finished the period in negative territory with the CAC 40 down 6.7%, FTSE MIB down 8.1%, and DAX down 9.3%.

As the global economy was looking to emerge from the COVID-19 pandemic, the war between Russia and Ukraine became the top exogenous shock that escalated the existing concerns over inflation pressure and supply chain disruptions. Major economic indicators were mixed during the first quarter. U.S. Manufacturing PMI entered March at 57.1, the lowest reading since September 2020. On the positive side, we continued to see sequential decline in unemployment rates. However, inflation kept rising, as the March CPI data hit 8.5%, particularly through food and gasoline. Global yields rose sharply, with the U.S. Treasury market suffering from one of its worst selloffs on record. The 2-year and 10-year Treasury spread narrowed during Q1 and turned negative by the end of March for the first time since August 2019. The U.K. Gilt yield curves also flattened during the quarter, but not as pronounced as the U.S. Value stocks dominated in Q1 as rising rates weighed on growth names. Commodity-oriented stocks, such as crude oil, natural gas, and agricultural producers, led the rally amid the fear of tightening supply. This was also due to the Russia-Ukraine war and sanctions from the U.S. and its allies.

During the first quarter, central banks in developed economies delivered more hawkish stances of their monetary policy to combat inflationary risks. At the March Federal Open Market Committee ("FOMC") meeting, the Federal Reserve raised interest rates by 25 basis points, lifting its 0%-0.25% policy rate since March 2020. The policy rate change also marks the first rate hike since December 2018. As the Fed signaled further hikes at all six remaining meetings this year, the market is pricing in a 2.5%-2.75% target rate by year-end. The Committee also indicated in the recent Fed Minutes that they will begin to reduce the size of their balance sheet at a faster pace than was experienced in 2017-2019, reflecting more aggressive tightening and upward pressure on yields.

In Canada, the Bank of Canada (BoC) also commenced the tightening cycle to raise the overnight policy rate by 25 basis points to 0.5% at the March meeting. Even though Governor Macklem did not provide a detailed timeline on changing the reinvestment plan, he suggested that they will end purchases of government bonds, rather than slowly taper the reinvestment phase once the process of balance sheet reduction starts. The Bank is also open to 50-basis-point moves at individual meetings to tackle the rising inflation.

The European Central Bank (ECB) kept the benchmark interest rate unchanged at -0.50%. ECB President Christine Lagarde did not rule out the possibility of raising the policy rates this year. The Governing Council was clear on the necessity to reduce the asset purchases program (APP) over the coming months, while leaving it to the June meeting to decide on when to end the program. The decision is set to taper the APP from EUR40 billion in April to EUR30 billion in May, and EUR20 billion in June. Meanwhile, the pandemic emergency purchase program (PEPP) ended in March as stated in previous ECB meetings. In the U.K., the Bank of England (BoE) voted to lift the policy rate by two consecutive 25 basis points in its February and March meetings to 0.75%. The BoE also expected inflation to peak around 7.25% in April and dissipate over time. However, as the projections were published in February before the Russia Invasion of Ukraine, the upward pressure on inflationary risks could persist longer than projected.

The geopolitical tensions have been on the center stage in the first quarter, where Russia surprised the world with a full-scale military action on the Ukrainian border in late February, marking the first major military conflict in Europe in decades. Many developed countries have imposed economic sanctions on Russia, including banning Russian oil exports and its financial institutions from SWIFT. As a result, the conflict sent commodity prices such as crude oil, natural gas, and wheat sharply higher, which exacerbated the already-high inflation and supply chain bottlenecks, especially in Europe. In response, the U.S. announced to releasing 180 million barrels of crude oil over a six-month period from its Strategic Petroleum Reserve (SPR). The global oil supply had been tight even before the war. This has largely benefited commodity producers, resulting in Energy being the best-performing sector among most global equity indices.

As market sentiment rose in response to the war, concerns over a global economic slowdown have been intensifying. Looking forward to the rest of 2022, the global economy and broad equity markets will continue to be driven by high inflation readings, normalized monetary policies, and the unknown war duration.

In addition, the impact of COVID-19 cannot be ignored yet, as many countries have seen rising cases after loosening pandemic measures. China in particular has extended strict lockdowns on major cities to contain the outbreak. In this vein, it would be inevitable to see market turbulence persist in the near-term, which raises the importance of active portfolio strategies. The barbell approach (owning both cyclicals and defensive) remains our preferred strategy, while favoring dividend-paying quality companies, which generally demonstrate solid balance sheets, stable earnings growth, and reasonable valuations. In our stock selection process, we also carefully examine the candidate's Russian exposure and pricing power to deal with the uncertainties arising from geopolitical conflict and rising inflation.

Healthcare Sector Review & Outlook

We continue to believe that healthcare offers an attractive risk/reward opportunity with the overhang from political drug pricing risk abating. The fundamentals continue to be attractive given the sector's earnings growth and high pricing power. We also note that healthcare has a positive correlation to both rising rates and falling breakevens and as a result rising nominal rates could be a tailwind for the sector. In addition, the healthcare sector has typically outperformed the broader market following yield curve inversions since 1978 according to Goldman Sachs. While geopolitical risk continues to be a concern given the Russian-Ukraine conflict, we note that Russia's pharma market is heavily genericized and represented 1% to 2% of large cap pharma sales in 2021 according to Bloomberg. In addition, patient enrollment for Phase III trials are limited in the region. As a result, topline headwinds from geopolitical risk will muted in our view.

Some of the key healthcare opportunities that could materialize in 2022 include 1) Alzheimer's – multiple clinical and regulatory updates that could reduce uncertainty regarding commercial rollout 2) New generation obesity treatments expect to be launched in Europe 3) Interim data for developing a mRNA flu vaccine (improve efficacy through strain matching, expanding coverage by adding antigens) and 4) early detection cancer diagnostic screening (trial data for asymptotic colorectal cancer expected in H1 2022). These opportunities are significant as global costs associated with dementia is over $1 trillion (World Alzheimer's 2020 Report) and obesity is associated with over $1 trillion of healthcare costs (Goldman Sachs – December 2021).

The Life Sciences sector has benefited from pandemic-related tailwinds given the outsized demand for virus-related work such as molecular testing and bioprocessing. We believe this demand will remain elevated, as the virus renews focus on drug production and likely widens opportunities for cross-selling. Liquid biopsy is a promising opportunity in the early cancer detection market. Liquid biopsies are noninvasive blood tests that search for cancer-related genetic signatures to diagnose early-stage patients prior to symptoms. The global next-generation sequencing oncology testing market (screening, therapy selection and monitoring) is expected to grow at a 27% CAGR reaching $75 billion in 2035 according to Bloomberg.

From a policy perspective the Build Back Better Act (BBB Act) provides some clarity regarding drug pricing. The legislation will allow the Centers for Medicare and Medicaid Services to negotiate a maximum price with manufacturers for a subset of Medicare-covered drugs (10 products initially, expanding to 20 after a few years). Manufacturers will have to pay a penalty for increasing prices faster than CPI. In addition, the BBB Act expands Medicare and Medicaid by providing states an incentive to expand home-base services and provide coverage for hearing-related services. While the BBB Act failed to receive support in the Senate, Democrats are looking to propose a smaller spending bill which would include reducing prescription costs amongst other deficit reducing measures.

Healthcare innovation remains a focal point especially given the success in novel platforms such as Moderna's mRNA platform in the rapid development of a COVID-19 vaccine. We believe there will be a renewed focus on evaluating the potential for unrealized value across biotech companies that offer revolutionary platform technologies and processes. Examples include 1) gene editing - making permanent, precise edits to the genome to repair underlying genetic mutations or to create engineered immune cells for enhanced therapeutic benefit and 2) use of machine learning algorithms and artificial intelligence to better understand native biology and thus aid in the design and development of novel therapies.

Portfolio Review

Brompton Global Healthcare Income & Growth ETF (the "Fund") was down 8.5% in Q1 2022 versus the MSCI World Health Care Index which was down 3.2%.

The Fund's underweight position in the Biotechnology subsector contributed to performance which was ahead of the benchmark. Top performers include Abbvie (up 21%).

An overweight position in the Life Sciences subsector detracted from performance. Our holdings were on average down 14% which was in-line with benchmark holdings.

The Fund's overweight exposure to the Healthcare Equipment subsector detracted from performance which lagged the benchmark. Top performing holdings include Sonova (up 7.3%) and Stryker (up 0.23%).

The Fund was underweight the Pharmaceuticals subsector, which negatively impacted performance, lagging the benchmark. Top performers include Astrazeneca (up 16%), Merck (up 8%) and Bayer (up 6%).

The Fund's market weight exposure to the Managed Healthcare and Facilities sectors contributed to performance which was ahead of the benchmark. Top performers include Humana (up 11%) and United Health (up 2%).

Annual Compound Returns[1]	YTD	1-YR	3-YR	5-YR	Since Inception[2]	Since Inception[3]
Brompton Global Healthcare Income & Growth ETF (CAD Hedged)	(8.5%)	13.8%	10.3%	9.8%	8.1%	-
Brompton Global Healthcare Income & Growth ETF (USD)	(8.5%)	13.8%	-	-	-	11.0%
MSCI World Health Care Index	(3.2%)	15.5%	15.0%	13.5%	11.0%	17.5%
MSCI World Index	(5.0%)	10.6%	15.6%	13.0%	13.1%	17.3%

(1) Returns are for the periods ended March 31, 2022 and are unaudited. The table shows the Fund's compound return for each period indicated compared with the MSCI World Health Care Index ("Health Care Index") and the MSCI World Index (together the "Indices"). The Health Care Index represents the healthcare industry group of the MSCI World Index. The Fund's portfolio is expected to invest in at least 15 large capitalization global healthcare companies. It is not expected that the Fund's performance will mirror that of the Indices since the Health Care Index contains a substantially larger number of companies. Further, the Indices are 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. (2) Inception Date September 24, 2015.

(3) Inception Date August 8, 2019.

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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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