The Real Solution for Inflation

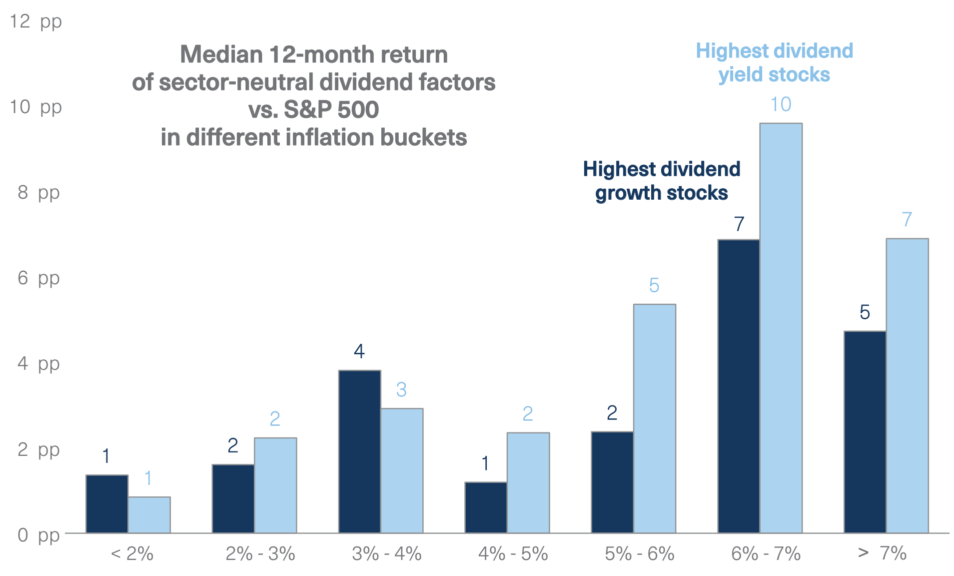
Fund in focus: Brompton Sustainable Real Asset Dividend ETF (BREA)

The S&P 500 has officially entered a bear market regime as of June 14, having sold off 22% from its closing high on January 3, 2022. The selloff this year was triggered by a combination of factors, including record high inflation, the Russia-Ukraine war, and a substantial tightening of financial conditions driven by the Federal Reserve ("Fed"). Over the past 40 years the market has become accustomed to falling inflation, low/declining interest rates, and periods of quantitative easing, which led to high equity valuations and strong returns. Long-duration assets benefited the most in this type of regime. However, we argue that the current market environment is the opposite of the previous cycles. Characteristics including high inflation, rising interest rates, slowing GDP growth, and a hawkish Fed warrant a shift in investment strategy. Investors should generally look to position their portfolios more defensively than in the past. Additionally, investors need to look for strategies that can act as an inflation hedge and that have moderate to high dividend yields, which provide a margin of safety in volatile markets. One area of the market that meets these criteria is real assets equities, which we believe present an excellent opportunity for investors in the current market environment.

Inflation is currently sitting at the highest level in four decades. May's surprisingly strong U.S. CPI print of 8.6% jolted the market and subsequently propelled the Fed to shift their stance more hawkishly during the most recent Federal Open Market Committee ("FOMC") meeting. As a result, the FOMC decided to raise interest rates by 75bps at the July FOMC meeting in an attempt to tame inflation.

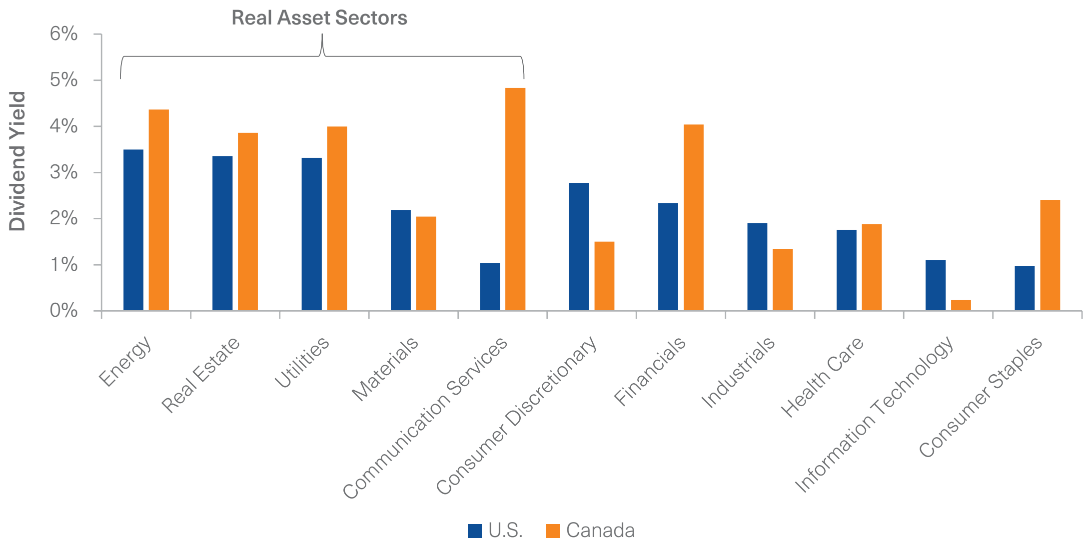
During periods of high inflation, stocks with high dividend yields tend to outperform the market (Exhibit 1). Real asset companies encompass many of the top dividend-yielding sectors in both the U.S. and Canada, such as Energy, Utilities, Real Estate, Communication Services and Materials (Exhibit 2). It is the ideal basket to own for investors that are looking to hedge inflation risk while achieving natural diversification.

Exhibit 1: Median 12-month return of high dividend stock stocks vs S&P 500 at various inflation rates



Source: Goldman Sachs as of March 2, 2022

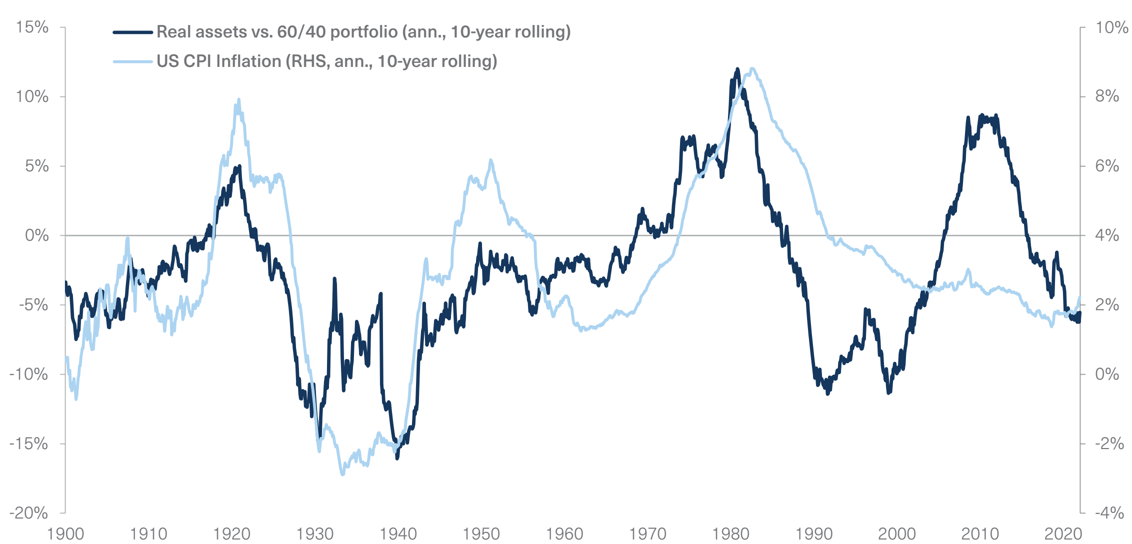
Exhibit 2: Estimated 2022 dividend yield by sector



Source: Bloomberg as of June 17, 2022. Reflects dividend yields of S&P 500 Index and S&P/TSX Composite Index sectors.

Stagflation, which is defined by high inflation and slowing economic growth, has also become a real concern. During periods of stagflation, investors face lower equity returns from traditional 60/40 portfolios. Long-duration equities sustain more severe drawdowns as their multiples compress more than shorter-duration equities, and bond prices decline due to rising yields. Real assets have historically outperformed a 60/40 portfolio in periods of high and rising inflation (Exhibit 3). Exposure to real return generating assets can better combat stagflation, as real asset companies are more capable of passing on inflation to consumers. Additionally, real asset sectors, such as Utilities, Communication Services and Real Estate, are less sensitive to economic growth. Their cash flow models tend to be more predictable, and revenues tend to be stickier. This is in contrast with high beta sectors, such as Information Technology, which have significantly underperformed during the current selloff.

Exhibit 3: Real Assets have outperformed a 60/40 portfolio in periods of high and rising inflation



Source: Goldman Sachs as of March 14, 2022

Brompton's Approach

Brompton Sustainable Real Asset Dividend ETF (BREA) provides diversified exposure to global real asset companies including Utilities, Energy, Communication Services and Real Estate sectors. We prefer to invest in high dividend-yielding companies that are market leaders with strong balance sheets and have predicable free cash flow. We believe this strategy provides better risk-adjusted returns, particularly in an inflationary or stagflationary environment. In addition, diversified sector exposure mitigates investment risks in a volatile macro environment. We actively manage the Fund's sector weightings to strive to provide investors with optimal sector exposure depending on the state of the economy. We also use an actively managed call writing overlay to harvest volatility risk premium which enhances risk-adjusted returns.

BROMPTON FUNDS

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