ETF & MUTUAL FUND UPDATE

IN THIS ISSUE

Market Radar		
Markets	**TSX Composite**	**S&P 500**
P/E	12.52	18.45
Yield (%)	3.41	2.24
YTD Performance (%)	-9.76	-20.46
Top Performers	**ETF**	**Mutual Fund**
1-Month	Black Diamond Distressed Opportunities ETF	Black Diamond Distressed Opportunities A
YTD	Horizons Natural Gas ETF	FGP Small Cap Canadian Equity D
3-Year	Horizons Global Uranium ETF	Ninepoint Energy Series F

Market data as of October 5th, 2022; top performers as of month-end.

A Bad Year Makes Good Mutual Funds Cheaper

By Ricahrd Morrison, CIM

Like every other investor, many solid, well-managed Canadian mutual funds have had a miserable year so far in 2022. Funds that have beaten underlying indexes every year for the past decade are suddenly down by 25 percent or more. Their investors may be grumbling, but their unit prices now trade at what appear to be bargain levels.

Tech funds have suffered the most, tumbling from what in hindsight were overly optimistic levels last November—before central bankers' warnings about inflation popped the bubble.

A brief look at the largest technology companies shows why tech funds have been crushed. As of 20 September 2022, shares of tech giants have crushed by atleast 30 percent, some up to 60 percent. Only Apple Inc. (down 13 percent on the year) and Tesla Inc. (down 12 percent) have sustained relatively minor setbacks.

The technology giants also happen to be the largest of all types of companies, which means they appear among the top holdings for almost every equity mutual fund with a U.S. focus. The weighting of the tech giants within each fund determines the level of this year's pain. A fund with, say, five per cent of its assets in each of the worst performers (and arguably more speculative names) will have much worse year-to-date results than a fund with five per cent in tech companies with strong cash flows such as Apple and Tesla. At the other extreme, fund managers who made a big bet on wireless provider T-Mobile U.S. Inc., which is up 20 percent in 2022, look clever.

Remember that mutual funds, like cars, are sold, not bought. Mutual funds typically come in many different series, each with a different management expense ratio (MER). Some series have initial sales charges or front-end loads, some carry level charges, and some have deferred sales charges or back-end fees. Although there are exceptions, generally, series-A funds are those sold to retail investors as they have low minimum investments, series-D funds are for self-directed accounts and have lower MERs, while F-series are sold through fee-based advisors versus those sold by commission-based advisors. The end result is that one series of a fund can carry an MER that is more than twice that of another series.

Here is a brief look at a few long-term outperformers hurt in 2022.

T.D. Science & Technology

This volatile fund appears near the top of every long-term performance list, having achieved an average annual return of 16.79 percent over the past ten years. The fund clocked a huge 68 percent gain in 2020, but this year has been a horrible one as it was down a full 43.9 percent between January 1 and the end of August 2022. An investor who put $10,000 into the fund at its launch in January 1994 would have more than $240,000 at its peak last year but would have lost half their money since then.

The fund's $1.38 billion in assets is allocated among some well-known tech giants along with an assortment of lesser-known names. Roughly 71 percent of the fund's constituent holdings are based in the United States, with 15 percent in Europe and nine percent in the Asia-Pacific rim.

Fidelity Technology Innovators

This long-term outperformer has a 10-year annual average total return of more than 21 percent, even after a 16 percent setback so far this year. An investor who put $10,000 into the fund at its launch in June 1997 would have $86,500 at the end of 2021, slipping to $69,700 as of 20 September 2022. The fund has $516.4 million in assets invested in 104 companies, including the giants Microsoft, Apple, plus Salesforce Inc., Samsung Electronics, KLA Corp., Texas Instruments, and other tech names. More than two-thirds of the fund is made up of U.S. companies.

Dynamic Power American Growth

Guided by Noah Blackstein since its inception in 1998, this actively managed bottom-up fund has a superb track record, vastly outperforming virtually every index through most calendar years despite a 2.99% MER. As of the end of August, the fund was down 32 percent on the year, its worst performance since the banking crisis year of 2008, when it fell 44 percent. An investor who put $10,000 into the fund at its June 1998 launch would have about $147,000 at its peak last year, slipping to about $95,000 at the end of August. Unlike many other U.S. funds, Dynamic Power American Growth is not simply an expensive proxy for broad market indexes or a collection of technology giants. The fund's five largest holdings as of the end of July were CrowdStrike Holdings Inc., MongoDB Inc., Enphase Energy Inc., Five9 Inc. and Datadog Inc., among a portfolio of just 24 names.

Although their long-term results have not been as spectacular as technology funds, European mutual funds are also down about 23 percent on the year, thanks to the Russian invasion of Ukraine, inflation, and rising interest rates. Charts from TeleTrader.com show stock markets in Austria, Belgium, Czech Republic, Denmark, Finland, France, Germany, Greece, Ireland, Italy, Netherlands, Poland, Spain, Sweden and Switzerland, all showing varying degrees of a downward slope. The few rising countries, such as England and Norway, have indexes dominated by oil giants.

IG Mackenzie European Equity

A steady long-term performer, this fund is down 20.37 percent so far in 2022 to the end of August, placing it in the first quartile of European equity funds. An investor who put $10,000 into the fund at its 2003 launch would have about $22,000 at its peak last year, slipping to about $18,000 as of the end of August. The fund's $1.87 billion in assets is spread among 75 large companies from a variety of industries, largely based in France, the U.K., Switzerland, Netherlands, and Germany.

The fund's major holdings include such well-known names as Swiss food maker Nestle SA and healthcare giants Roche AG, also of Switzerland, Novo Nordisk A/S of Denmark and England's AstraZeneca PLC, French luxury goods maker LVMH Moet Hennessy Louis Vuitton SE, energy giants Shell PLC and TotalEnergies SE, Swiss bank UBS Group AG and French cosmetics giant L'Oreal SA.

Sun Life MFS International Value

This fund's 10-year performance puts it in the first quartile of international funds, but 2022 has been painful, and its unit price has fallen by 27 percent so far in 2022. The fund's portfolio of 99 names focuses on giant companies in developed markets. An investor who put $10,000 into the fund at its inception in 2010 would have $37,000 at its peak last year, slipping to about $27,000 as of mid-September. More than half of the fund's holdings are in companies based in Japan, France and Switzerland, with roughly another 10 percent in each of the U.K., Germany and the United States.

The fund's largest holdings include Nestle SA, Schneider Electric S.E., Cadence Design Systems Inc., Pernod Ricard SA, L'Oreal SA, Diageo PLC, Givaudan S.A., Reckitt Benckiser Group PLC, Taiwan Semiconductor Manufacturing Co. Ltd. ADR and Legrand SA.

Conclusion

Mutual fund managers and salespeople are often criticized as working for the benefit of themselves at the expense of investors, and indeed, most mutual funds lag underlying indexes because of their fees. The problem is especially acute in Canada, where mutual fund MERs are among the highest in the world. The funds mentioned here are among the few with long-term returns that reflect value for investors' money. This year's downturn has depressed unit prices, making them much cheaper than they were a year ago.

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ETF Spotlight: Yield and Downside Protection with CI Energy Giants Covered Call ETF (NXF)

by Chris White, CFA

Energy Market Backdrop

Reversing the clock and looking back at the 2018 to 2019 timeframe, we see the price of oil hovering between ~$45 and ~$75 a barrel. Fast forward to the early part of 2020 and the price of oil had declined to (~$40). It's hard to believe now, but this is the situation that unfolded, and the subsequent global events that took place following 2020 resulted in the price of oil climbing to as high as ~$130 and has stabilized around the mid-$80s.

Since the bottom for oil prices back in 2020, the energy sector has been the best performing sector in both 2021 and year-to-date 2022. These developments have left energy companies full of free cash flows and rising dividend payments. We have also seen energy companies share prices appreciate to levels not seen in years. This has left some investors that have exposure to energy considering if they should increase, maintain, or decrease their exposure.

In this article, we review the CI Energy Giants Covered Call ETF (NXF) and how it can help investors with exposure to energy hedge in the event of a declining/stagnating energy market.

CI Energy Giants Covered Call ETF (NXF) Overview

The NXF ETF was created in early 2015 and provides investors with a great distribution yield on a quarterly basis by using a covered call strategy on not more than 25% of the underlying securities in the portfolio.

The ETF holds equal weightings of the 15 largest energy companies by market cap on a North American exchange.

The fund uses a covered call strategy to generate the high yield it offers which provides investors with the opportunity for capital appreciation. The fund has good liquidity, a reasonable Management Expense Ratio (MER), high-quality names underlying the fund, and boasts a high distribution yield of ~8.1%.

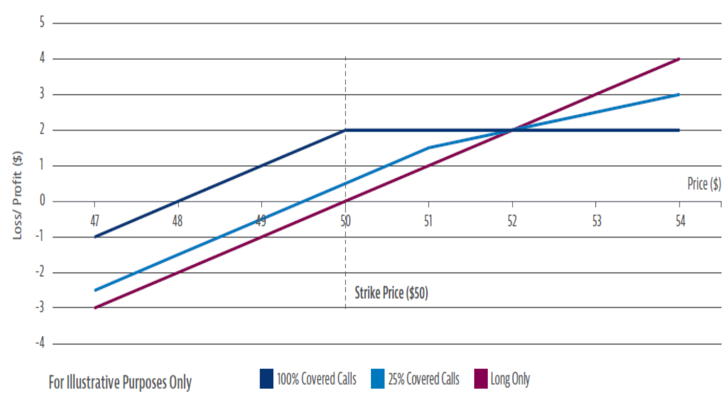
Fund Details	Value
Net Assets Under Management	$480.8M
Management Fee	0.72%
Holdings	15
Distribution Yield	8.10%
Distribution Frequency	Quarterly
Performance	
3-Month	-5.7%
6-Month	12.6%
YTD	36.8%
1-Year	57.3%

Source: CI Energy Giants Covered Call ETF Website

We can see in the table above that the performance across a six-month timeframe and longer has been phenomenal, which reflects the performance of the energy markets. The fund's high distribution yield is achieved through covered calls, allowing investors to participate in any share appreciation from the underlying holdings, but also earn yield in the event of stagnating or declining markets.

Here are three possible scenarios of investment strategies: long-only, 100% covered calls, and 25% covered calls. Without going into too much detail of how covered call strategies work, the long-only strategy performs best in a rising bull market but will also perform the worst in the event of a pullback. The 100% covered call position will perform best in a stagnant/declining market but will perform the worst in the event of a large run-up in price. The 25% covered call strategy (light blue line) will perform right in the middle between these two strategies—participating in any price appreciation but to a lower extent than a long-only position and will defend better against a drawdown in price than long-only. NXF uses a 25% covered call strategy.

EXAMPLE: CALL OPTION INVESTING SCENARIOS



Source: CI Energy Giants Covered Call ETF – Covered Call ETFs

The fund has roughly half of its assets based in the U.S., just under half are international, and about 10% are based in Canada.

Asset allocation	(%)
US Equity	48.44
International Equity	39.03
Canadian Equity	12.18
Cash and Equivalents	0.36
Other	-0.01

Source: CI Energy Giants Covered Call ETF Website

Analyzing the Benefits of the NXF ETF

By utilizing a covered call strategy, the fund benefits when its underlying companies decline or remain flat in price, but also benefits through its underlying company holdings appreciating in price. This contrasts with an ETF that does not use covered calls or a single stock that only benefits from rising share prices and/or relevant dividends.

This counterbalance within the NXF ETF gives it a lower level of annual volatility than the SPDR Energy Select Sector Fund (XLE) and individual energy names, such as Occidental Petroleum (OXY), Devon Energy (DVN), and

Petroleo Brasileiro (PBR). These three individual energy companies are the top three underlying holdings in the NXF ETF. Below we have outlined the annual volatility figures for each fund and stock by year, and the average annual volatility. Visually, we can see that NXF has seen lower levels of volatility than the other names listed and showcases a lower average volatility over the years.

Annual Volatility					
Year	NXF	XLE	OXY	DVN	PBR
2016	0.28	0.25	0.26	0.60	0.68
2017	0.16	0.13	0.18	0.31	0.39
2018	0.23	0.22	0.26	0.40	0.50
2019	0.18	0.19	0.30	0.42	0.34
2020	0.51	0.61	1.19	1.00	0.86
2021	0.26	0.30	0.57	0.52	0.50
2022	0.29	0.33	0.56	0.53	0.44
Avg. Vol	0.27	0.29	0.47	0.54	0.53

Source: Koyfin

Looking to the price return side of things, in periods of stagnating and flatlining oil prices/energy markets, the NXF has demonstrated its outperformance against the XLE and OXY. Mid-2015 through 2019 marked a stagnant period for energy prices, and this did not bode well for individual energy companies such as OXY, but we can see that NXF outperformed the non-covered call ETF, XLE, in this timeframe largely due to its stronger yield and covered call strategy.

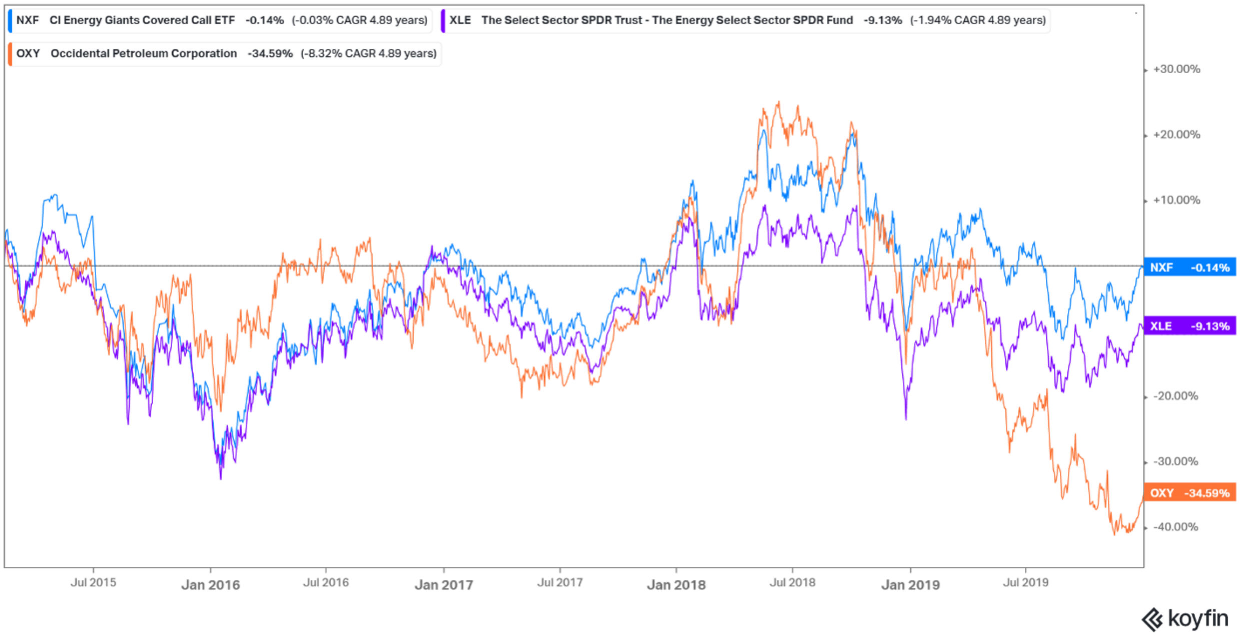
Looking at NXF's yield, we have outlined the annual returns for NXF, XLE, and OXY since 2017 grouped by returns excluding and including yield. One of the first items to notice is that NXF consistently has the highest distribution yield across the group of companies. Annual returns including yield, NXF has slightly underperformed XLE across the years, and significantly underperformed individual energy companies such as OXY, however, the outperformance by the other companies has come at the cost of higher volatility and reduced annual yield.

Annual Returns			
Year	NXF		
Returns	Without Yield	With Yield	Distribution Yield
2017	(4%)	3%	7%
2018	(16%)	(9%)	7%
2019	(1%)	6%	8%
2020	(43%)	(35%)	7%
2021	27%	41%	13%
2022	30%	36%	6%
Total Returns	(7%)	41%	48%

Annual Returns			
Year	XLE		
Returns	Without Yield	With Yield	Distribution Yield
2017	(4%)	(1%)	3%
2018	(21%)	(18%)	2%
2019	5%	12%	7%
2020	(37%)	(33%)	4%
2021	46%	53%	7%
2022	45%	48%	3%
Total Returns	34%	61%	27%

Annual Returns			
Year	OXY		
Returns	Without Yield	With Yield	Distribution Yield
2017	3%	8%	5%
2018	(17%)	(13%)	4%
2019	(33%)	(28%)	5%
2020	(58%)	(57%)	1%
2021	67%	68%	0%
2022	125%	127%	1%
Total Returns	88%	105%	16%

Source: Koyfin



The Risks of a Covered Call ETF

While there are benefits to owning a covered call ETF, such as earning a higher yield than would have otherwise been earned, or reduced volatility and increased upside in stagnant markets, there are also risks associated. By using a covered call strategy, NXF foregoes potential investment returns during a rising market as it may be forced to sell securities if the call option strike price is met. The asset base of the ETF can be reduced by Return of Capital (RoC) distributions in order to meet the fund's goal to provide investors with high yield, particularly in the event of a rapidly declining energy market.

The fund's performance has been excellent over the past 1-2 years, but since inception it has declined, and while part of this decline can be attributable to the energy markets, the use of a covered call strategy can erode the value of the ETF relative to non-covered call ETFs. The NXF ETF may not be suitable for all investors, as it serves a unique purpose to provide investors with high yield, the ability to participate in upside in the energy markets, and low levels of volatility. These qualities can be useful for certain investors but may not be suitable for all investors.

Conclusion

Amid events of rising global inflation, macroeconomic uncertainty, and a tight energy supply, the energy market has been one of the better places to hide over the past couple of years. This outperformance by the energy markets has resulted in two consecutive years of the energy sector leading the markets, and energy investors with expanding allocations to energy names.

We feel that the NXF ETF provides these investors with an attractive annual yield, lower annual volatility against non-covered call energy ETFs and individual energy names, and some form of downside protection. It is unclear exactly what will happen in the energy markets in the years to come, but for those seeking exposure to the energy markets while also protecting against the possibility of a stagnant or downward trend in energy markets, the NXF ETF helps to achieve these goals.

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Revision to ETF Model Portfolios

by Barkha Rani, CFA

Exchange-Traded Funds (ETFs) are an easier and often cheaper way to diversify a portfolio and maintain tactical exposure to desired sectors and regions. It can be used for passive and active investing, collecting dividend distributions, and/or assisting in balanced portfolio exposure. While a long-term strategy involving buy and hold is good in theory, without any active changes, the structure can and will drift over time. This drift is driven by market movements within positions. Portfolio rebalancing comes into play here to realign a portfolio back to the strategic asset allocation, to maintain investment discipline and to control the risk-return characteristics of the overall portfolio.

This month, we begin with the Balanced ETF portfolio.

The Balanced ETF model portfolio was created with a balanced approach in mind, considering asset classes and regional exposure. It offers a sample template of broader investment opportunities in equity and fixed income markets with decent distribution yield and the potential for capital appreciation.

The model portfolio diversifies across market capitalization and was developed versus emerging markets, with a higher weighting in North American securities. Like the benchmark, Vanguard's Balanced ETF Portfolio, the Balanced ETF model portfolio follows a 60/40 breakdown between equities and fixed income. Geographic exposure is represented with Canada at 62%, the U.S. at 24%, developed markets outside of North America at 9%, and emerging markets at 5%. The model portfolio offers a similar distribution yield as the benchmark at 3.26%.

So far, 2022 has not been short of surprises, with market sentiments swinging back and forth with no sustained footing. Surprisingly, but not shockingly, cash has been cited as a top market pick often this year. While that can be a subjective choice, we investigated how individual ETFs contributed to the overall return for the model portfolio. The contribution to the total return is driven by the underlying ETF performance and overall weight relative to the portfolio.

All ETFs have declined year-to-date, with the least negative contributions from the iShares 1-5 year Laddered Government Bond Index ETF (CLF) and CI Morningstar Canadian Momentum Index ETF (WXM). Looking at the other side, the worst contributors to the total return were iShares S&P/TSX 60 Index ETF (XIU), iShares Core MSCI EAFE IMI Index ETF (XEF), and BMO S&P500 Index ETF (ZSP).

We think that the model portfolio is overweight on the TSX 60 index and would reduce portfolio weight by 7.0%, from 23.0% to 15.0%. While we do not hold a negative view towards the TSX60, we think the relative weight in the portfolio is on the higher side. Using the proceeds, we started a position in iShares Core U.S. Aggregate Bond ETF (AGG).

The AGG ETF tracks the Index comprised of the total U.S. investment-grade bond market with an average maturity of 8.65 years and an average yield to maturity of 4.77%. The 12-month trailing yield stands at 2.14%, and the ETF charges a Management Expense Ratio (MER) of 0.03%. In terms of the range of maturities, the ETF is well-diversified in a range of maturities from one-to-two years to 20+ years, with over 70% of the holdings rated AAA.

Nearly 40% of the total assets under management are held in treasuries, with nearly 27% in mortgage-backed securities, with industrial and financial companies accounting for 15% and 8%, respectively. Bonds have had a tough year this year, and we still believe in the benefits of diversification. Looking at the yield story, we think there is much to look forward to with respect to the bond market.

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Issue Name	Ticker	Portfolio Weight	# of Shares	3 Mo Total Return	Total Return	Price - Close	Portfolio Value	Contribution to Return	Dividend Yield
Balanced ETF Portfolio		100.00%		-0.53	-11.05	53.86	993,731	-11.05	3.12
iShares US Technology ETF	IYW-US	1.70%	158.54	-2.10	-26.39	106.46	16,879	-0.52	0.58
iShares Russell 2000 Growth ETF	IWO-US	5.35%	177.33	7.00	-18.66	299.57	53,124	-1.00	1.15
iShares Core MSCI EAFE IMI Index ETF	XEF-T	8.97%	3,149.29	-4.08	-18.32	28.31	89,157	-1.79	3.90
iShares S&P/TSX Cdn Preferred Share Idx ETF-Co	CPD-T	4.61%	4,046.38	-6.18	-16.13	11.31	45,765	-0.83	5.52
Vanguard FTSE Emerging Markets All Cap Index I	VEE-T	4.40%	1,411.83	-4.89	-16.10	30.96	43,710	-0.77	4.46
BMO S&P 500 Index ETF	ZSP-T	11.99%	2,125.59	1.94	-14.24	56.05	119,139	-1.72	1.43
BMO Aggregate Bond Index ETF	ZAG-T	17.16%	12,569.37	0.28	-11.73	13.57	170,566	-1.96	3.54
Vanguard US Dividend Appreciation Index ETF	VGG-T	5.86%	891.50	2.05	-10.74	65.36	58,268	-0.60	1.43
iShares S&P/TSX 60 Index ETF	XIU-T	15.06%	5,045.75	-1.79	-6.85	29.66	149,657	-1.63	3.10
iShares 1-5 Year Laddered Government Bond Id	CLF-T	4.71%	2,807.83	-0.18	-4.16	16.66	46,778	-0.17	2.16
CI Morningstar Can Momentum Idx ETF	WXM-T	12.24%	5,010.15	0.93	0.07	24.28	121,646	-0.07	5.00
iShares Core US Aggregate Bond ETF	AGG-US	7.95%	598.48			132.07	79,041		2.60
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