

Evolve Dividend Stability Preferred Share Index ETF

Preferred Shares are hybrid securities with both equity and fixed income characteristics. PEF invests primarily in preferred equity securities of companies listed in Canada.

TSX

PEF

ETF TICKERS: PEF (UNHEDGED)

North American markets made solid gains in 2021. In Canada, the S&P/TSX Composite Index returned 21.7%, while the S&P/TSX Composite Index was up 24.4%.

In the U.S., the S&P 500 gained 26.9% (US\$), while the Dow Jones Industrial Average rose 18.7% (US\$) and the Nasdaq Composite 21.4% (US\$).

Comparatively, the broad markets outperformed preferred shares which gained 13.6% on the S&P/TSX Preferred Shares Index.

The lack of new preferred share supply and several redemptions, coupled with the expectations of future redemptions because of the issue of Limited Recourse Capital Notes (LRCN), contributed to the positive returns for the market. In addition, rising yields and the expectation of higher inflation has made the preferred share market a sought-after asset class

Following the issuance of LRCNs, preferred shares rose because investors recognized that a large portion of the Canadian preferred share market would be redeemed in the coming quarters. In 2020, \$3.4 billion worth of preferred shares were redeemed; and by mid-October 2021, over \$7 billion were redeemed so far for the year, with another \$1.5 billion-plus expected to be redeemed by the end of the year.¹

Incidentally, LRCN allow financial institutions to count the security as preferred equity on their balance sheets, except that they pay interest and get an interest deduction on them. This means that LRCNs are much cheaper for banks to issue, than paying after-tax preferred dividends.²

In June, The Royal Bank of Canada, the pioneer in the LRCN space in Canada, announced the offering of \$1 billion of non-viability contingent capital (NVCC) Additional Tier 1 (AT1) Limited Recourse Capital Notes, Series 3 (LRCNs). The LRCNs will bear interest at a rate of 3.65% annually, payable semi-annually, for the initial period ending November 24, 2026. Thereafter, the interest rate on the LRCNs will reset every five years at a rate equal to the prevailing 5-year Government of Canada Yield plus 2.665%. The LRCNs will mature on November 24, 2081.³

In December, BCE Inc. announced that 501,717 of its 22,735,621 fixed-rate Cumulative Redeemable First Preferred Shares, Series AK have been tendered for conversion on December 31, 2021, on a one-for-one basis, into floating-rate Cumulative Redeemable First Preferred Shares, Series AL. In addition, 956,408 of its 2,254,079 Series AL Preferred Shares have been tendered for conversion on December 31, 2021, on a one-for-one basis, into Series AK Preferred Shares.⁴

Power Corporation also announced in December that it intends to redeem all 86,100 of its outstanding Cumulative Redeemable First Preferred Shares, 1986 Series on January 15, 2022.⁵

On the other hand, Canadian Utilities Limited announced in November that it has entered into an agreement with a syndicate of underwriters who have agreed to buy 7,000,000 4.75% Cumulative Redeemable Second Preferred Shares Series HH at a price of \$25.00 per share for aggregate gross proceeds of \$175,000,000. The proceeds will be used for capital expenditures, to repay indebtedness and for other general corporate purposes.⁶

Performance Attribution

For the 12-month period ending December 31, 2021, TC Energy Corp., followed by Enbridge Inc. and Brookfield Asset Management Inc. made the biggest contribution to the Fund. By weight, the Fund's largest exposure at the end of the year was to TC Energy Corp, followed by Enbridge Inc. and Pembina Pipeline Corp.

Sources:

1. <https://www.morningstar.ca/ca/news/215641/preferred-shares-still-have-room-to-run.aspx>
2. <https://www.morningstar.ca/ca/news/215641/preferred-shares-still-have-room-to-run.aspx>
3. <https://ca.finance.yahoo.com/news/royal-bank-canada-announces-nvcc-205100615.html>
4. <https://www.prnewswire.com/news-releases/bce-reports-results-of-series-ak-and-al-preferred-share-conversions-301447209.html>
5. <https://www.newswire.ca/news-releases/power-corporation-announces-redemption-of-preferred-shares-819486641.html> Power Corporation
6. <https://www.canadianutilities.com/en-ca/about-us/news/2021/122645-canadian-utilities-limited-announces-preferred-share-issue.html>

Commissions, trailing commissions, management fees and expenses all may be associated with exchange traded mutual funds (ETFs) and mutual funds. Please read the prospectus before investing. ETFs and mutual funds are not guaranteed, their values change frequently and past performance may not be repeated. There are risks involved with investing in ETFs and mutual funds. Please read the prospectus for a complete description of risks relevant to the ETF and mutual fund. Investors may incur customary brokerage commissions in buying or selling ETF and mutual fund units. This communication is intended for informational purposes only and is not, and should not be construed as, investment and/or tax advice to any individual.

The indicated rates of return are the historical annual compound total returns net of fees (except for figures of one year or less, which are simple total returns) including changes in per unit value and reinvestment of all dividends or 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. The rates of return shown in the table are not intended to reflect future values of the ETF or returns on investment in the ETF. ETFs are not guaranteed, their values change frequently, and past performance may not be repeated.

Certain statements contained in this documentation constitute forward-looking information within the meaning of Canadian securities laws. Forward-looking information may relate to a future outlook and anticipated distributions, events or results and may include statements regarding future financial performance. In some cases, forward-looking information can be identified by terms such as "may", "will", "should", "expect", "anticipate", "believe", "intend" or other similar expressions concerning matters that are not historical facts. Actual results may vary from such forward-looking information. Evolve undertakes no obligation to update publicly or otherwise revise any forward-looking statement whether as a result of new information, future events or other such factors which affect this information, except as required by law.