

Inside: Top ETF trends of 2021

First cryptocurrency
ETFs launch in Canada

Sustainable investing
is here to stay

Protecting your assets
from inflation

Investors look beyond
Canada's borders

More exceptional
ETF growth ahead

2021 Mackenzie Investments Year-End ETF Report

ETF inflows and assets break records – again



MACKENZIE
Investments

As much as everyone wants the pandemic to end, this is certainly one of the more exciting times in business and investment history. Not a day goes by where Canadians aren't getting a crash course on something, whether it's supply chains, lumber costs, inflation, energy pricing or global economics, and while many of these issues could be concerning depending on how the pandemic plays out, markets have so far continued to shine. In 2021, the S&P 500 rose by about 27%, while Canada's S&P/TSX Composite Index climbed by 22%. Go back further and the gains are even more impressive: Since March 23, 2020, when stocks hit their crisis bottom, these two indexes have climbed by 110% and 89%, respectively.

One area that's benefited from both the uncertainty and strong market gains is exchange-traded funds (ETFs), which continue to experience massive year-over-year increases in assets under management (AUM), inflows, product growth and innovation. According to National Bank, in 2021, Canadians invested \$53 billion in domestic-listed ETFs, far exceeding last year's record. AUM reached \$323 billion, also a record. As well, there are now 1,177 Canadian-listed ETFs on the market, up 202 from a year earlier.

Why the big gains? One reason is that market disruptions, such as what we saw during the early days of the pandemic, have helped investors get increasingly comfortable with the resilience and value of ETFs. "During a market disruption or a liquidity issue, the ETF market has once again passed the stress test," says Michael Cooke, Head of ETFs at Mackenzie Investments.

But there's more to it: with a growing number of innovative products to choose from, including bitcoin ETFs, inflation-protection funds and sustainability-focused products, it's becoming much easier for advisors and investors to create a portfolio that specifically meets their needs and allows them to respond to market conditions. "Investors are taking greater comfort in knowing they can manage risk and volatility effectively with ETFs, whether it's liquidity management, transition management, strategic asset allocation or tactical allocation," says Cooke. "The sheer versatility of ETFs opens the eyes of investors."

TOP TRENDS:

ETF market continues to evolve

With the Canadian ETF market rapidly evolving – 454 ETFs traded on the TSX five years ago with about \$115 billion in AUM – several key trends emerge every year. Here are a few that investors should know about.

New cryptocurrency offerings

It was only in 2021 that the first bitcoin ETF became available for purchase – and it was created by a Canadian company. Another bitcoin ETF followed soon after – it too was developed by a Canadian firm that also created an ethereum ETF – while a bitcoin futures ETF came to



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market in the U.S. in October 2021. These cryptocurrency ETF launches are significant, says Prerna Mathews, Vice President of ETF Product and Strategy at Mackenzie Investments, because they speak to just how forward-thinking the Canadian market can be, which bodes well for more innovative product creation. "Crypto was an important category last year, providing investors access to a diversifying new asset class – that's definitely been an area where we've seen more product issuance," she says.

A focus on sustainable investing

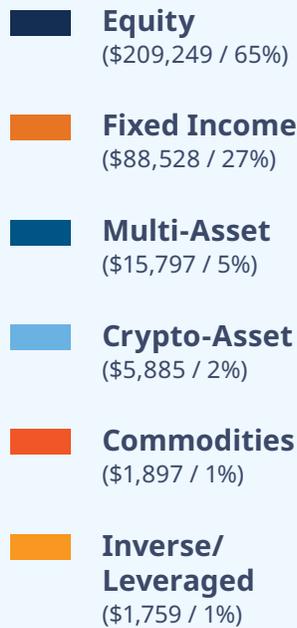
The pandemic has also put a greater spotlight on environmental, social and governance (ESG) issues. As of November 2021, a record \$371 billion flowed into ESG ETFs globally, according to ETFGI, in part because ETFs make it a lot easier for investors to buy products that align with their values. Most of the new issuances that will come out in the months ahead will likely focus on the environment, says Mathews, and will cover everything from negative screening – a fund that excludes certain investments – to more impact investing, which focuses on businesses that are, say, directly helping with the transition to a low-carbon economy. While index providers are evolving their approach to sustainable investing, the active selection model used by asset managers is proving to be an effective strategy in this burgeoning ETF category. "There is currently more of an inclination towards using active management for these exposures," says Cooke.

Protecting against inflation

With consumer prices rising, inflation-protecting funds are getting their due. What investors are buying, though, is varied, as different options may be needed depending on the economic environment. For instance, when inflation rises at an above trend rate, investors might consider purchasing either gold, commodities or Treasury inflation-protected securities (TIPS). In each of these cases, the value of the underlying holdings can potentially rise along with inflation. Emerging market stocks and real estate securities also tend to do well in inflationary periods when the economy is also expanding. Given the uncertainty around where inflation and economic growth are headed,

ETF AUM (CAD\$) by asset class in 2021

Source: National Bank of Canada



ETFs IN 2021

Source: National Bank of Canada/ETFGI

\$53 billion
Total inflows for 2021

27%
Year-over-year increase in total inflows

1,177
Number of ETFs in Canada

202
Year-over-year increase in ETFs

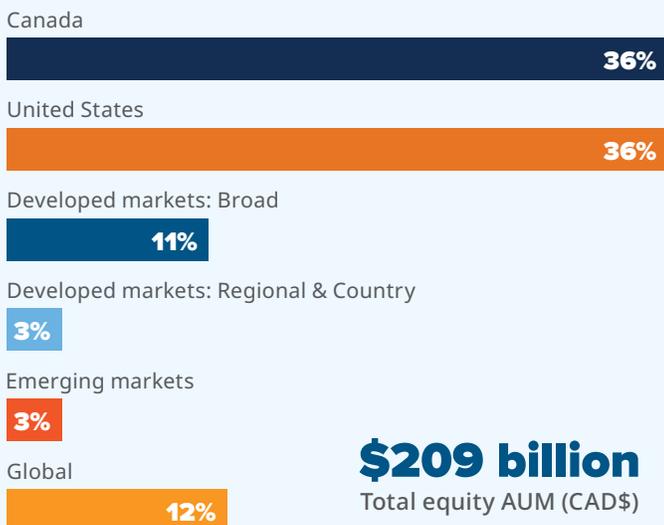
25.5%
Year-over-year increase in AUM

\$9.9 trillion
Global ETF assets under management (As of Nov. 2021)

9,700
Number of ETFs and ETNs for purchase globally (As of Nov. 2021)

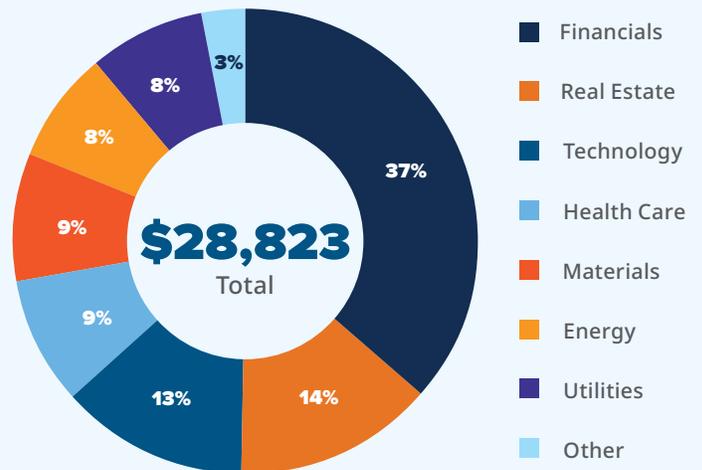
Equity ETF AUM by geography

Source: National Bank of Canada



Equity AUM (CAD\$) by sector

Source: National Bank of Canada



Year-end returns

Source: S&P Capital IQ

Stock Markets (1-yr returns)	26.8% S&P/TSX	21.7% S&P 500	20% MSCI World
Canadian Economy	6.0% Unemployment rate (Nov. 2021)	5.4% GDP growth (Q3 2021)	4.7% Inflation rate (Nov. 2021)

Crypto and commodities

Source: S&P Capital IQ

			
Bitcoin \$46,306.45 (US)	Natural Gas \$4.5 /Mmbtu (US)	Gold \$1,815.77 /oz. (US)	Oil \$95.18 WTI/barrel (US)

investors may want to own a variety of asset classes, says Cooke. ETFs make that easy to do. “ETFs can deliver that exposure very efficiently, whether you want it in a single investment or if you want to combine some of these asset classes within a diversified portfolio,” he notes.

International opportunities

International ETFs, both developed and emerging, have also been a favourite destination for Canadians, with more than \$10.7 billion of net flows going into this category, according to National Bank. With an ever-increasing amount of Canadian-listed international ETFs, investors can more easily diversify their portfolios and broaden their exposure – to specific sectors or countries or areas within certain locales – than ever before. The move into international ETFs isn’t pandemic-related, says Mathews, but rather, Canadians are becoming increasingly more comfortable with purchasing products that hold more than domestic stocks. “We have one of the strongest home biases versus other markets, so it’s great that investors are diversifying,” she says. “That’s especially a good thing when you think about valuations and interest rates and how they might look different across different markets coming out of the pandemic.”

More ETF growth ahead

It’s hard to know where things go from here, given that we haven’t exited a pandemic in more than a century. As a result, the shape of the global economic recovery and its impact on interest rates and equity valuations is difficult to predict. The potential for above-trend inflation is one example of how investors will need to think differently about building portfolios. “You’re going to have to think more creatively about sourcing portfolio returns and managing risk,” says Cooke. But, in a post-pandemic world, the versatility of ETFs in providing precise and efficient exposure to many different asset classes and geographies is particularly relevant. Investors need to anticipate a broader range of investment scenarios going forward, and ETFs give them more tools with which to build better portfolio outcomes, says Cooke.

It’s partly for that reason that the ETF market will continue to break records in the years ahead. A lot of investors continue to allocate to core holdings, like Canadian equity or fixed-income index tracking ETFs, but with more products to choose from, many are also now complementing their main holdings with other kinds

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of funds, such as bitcoin and ESG, or themed ETFs like robotics and artificial intelligence, notes Cooke.

At the same time, investment professionals and investors are becoming more comfortable and proficient with ETF usage. That’s especially true with millennials, who are familiar with ETFs, and are set to inherit trillions in the decades ahead. “Millennials are already significant users of ETFs and will continue to increase their exposure,” says Mathews. Women are also big ETF users – they prefer packaged solutions, she says – and will soon control about 50% of all financial assets.

For advisors and investors looking for diversified, cost-effective exposure to balanced portfolios, asset allocation ETFs have become a compelling option. These all-in-one portfolios provide different combinations of core equity and fixed income ETF exposure with regular rebalancing, allowing asset allocation ETFs to keep risk levels aligned to investor objectives and risk tolerance. With broad appeal in Canada, asset allocation ETFs accounted for 11% of all net flows in Canadian ETFs in 2021.

More financial advisors are also accelerating their usage of ETFs, adds Cooke, due to their cost and practice efficiencies. ETFs allow advisors to effectively allocate client fee budgets based on the outcomes that different investment strategies deliver. As well, the ease of access to specific strategies or exposures provided by ETFs allows advisors to achieve desired client outcomes, and free up time to focus more on servicing their clients, explains Cooke.

All of this adds up to more inflows and assets into ETFs. “So many trends in financial services indicate that ETFs will continue to grow in relevance, and set records for inflows and assets under management,” says Cooke. “It’s like the growth rings on a tree trunk, more investors are making large allocations and all that adds to more accelerated usage in the years ahead.”

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