all outperformed their benchmark by over 10%, with 50% less volatility. There was no better environment to test them in."

The one variable First Trust didn't foresee was the impact the hedging cost would have on performance. "These products are CAD-hedged," Cheong explains. "We wanted to deliver the outcome as close to the S&P 500 but eliminate the currency fluctuation as much as possible. The hedging cost came up around 80 basis points, so that was the one input we had to weight to determine performance."

> "Even as we went through March, they all outperformed their benchmark by over 10%, with 50% less volatility"

Still, in light of the positive results for the first ETF in the lineup, and with the next – NOVB.F – due to hit the one-year mark soon, First Trust has more plans for its targeted outcome ETF suite.

"If we get enough interest and understanding on how they work, and if they continue to perform well in volatile times, we will look at launching on a more monthly basis so advisors can ladder them further," Cheong says. "We are also looking at international markets, which have been difficult for investors. If people are looking for diversification, they may look at something like that. We have first mover advantage and will continue becoming known for this product, delivering the results and will develop more of a following."

Mike Dragosits
Portfolio manager
HARVEST PORTFOLIOS

Years in the industry
12

Fast fact
The Harvest Equal Weight Global Utilities Income ETF holds 30 securities from 10 countries and seven sub-sectors

Q&A

How to approach utilities ETFs

What trends have you noticed in global utilities this year?
Prior to the pandemic, utilities companies performed quite well on positive fundamentals. This pushed their valuations to relatively high levels. Once the pandemic hit, concerns around demand were compounded by the potential for customer bill payment issues. This caused utilities to sell off harder than in a normal recessionary environment. As the market settled into the reality of a COVID-impacted world, investor flows did not return to the defensive utilities. This has left utilities valuations lagging at much more palatable levels and at a very deep discount relative to metrics on the broad S&P 500.

For now, it seems that for those utilities with exposure into a pickup in cyclical growth and renewables, there is a premium valuation being attributed, but the safe haven and higher income generation of more traditional regulated utilities should remain.

Were there any areas that underperformed or overperformed and forced you to shift weightings?
Our fund is set up under a formula-based approach to stock selection on a quarterly rebalancing basis. This removes the active component of the stock-picking in favour of an approach that targets broad exposure to global utilities, telecom and pipeline companies, particularly ones that provide a higher-than-average yield.

How great is the need for exposure to different areas within utilities to diversify risk?
There would be some benefits to having wider diversity of exposures over the longer term by including telecommunications and pipeline names with utilities, as well as diversifying away some geographic concentration risks through global stocks. However, we do recognize that in the current environment, the energy space has been negatively impacted by the macro environment, and pipelines have been a drag on the portfolio. That said, we think the need and use of oil and gas is one that will remain in high demand for a long time, with potential for pipelines to make steady cash flows, despite the slow turn toward a renewables future.

What's your outlook for the space going forward?
One topical discussion is the US election, and there are minimal US election disruption risks to the sector. The companies have generally navigated the COVID-19 waters well, which would suggest lower-volatility characteristics should return and attract investors seeking income and stability.

Another important aspect is interest rates. The outlook suggests low nominal bond yields are here to stay. Fundamentally, this is a cost containment benefit for a utilities sector that employs very large levels of debt in their operations. Utilities valuations are much cheaper now.

Lastly, we cannot forget about decarbonization and ESG investing. We think utilities companies are a prime area where investors can get access to companies that are potentially in line to benefit from political desires to fund renewable initiatives.