BMO US Put Write ETF (ZPW, ZPW.U)
BMO US Put Write Hedged to CAD ETF (ZPH)

BMO US Put Write ETF is an alternative income strategy that is constructed by selling out of the money (OTM) put options on U.S. equities. While this strategy does not typically hold the underlying equities it generally delivers a high level of income in excess of bond yields.

The ETF combines market options and options on individual securities to provide both passive and active approaches to option writing. Market options provide greater consistency and predictability while individual security options achieve more tactical positioning.

The goal of the put write strategy is to generate income by selling downside protection in equity securities. The ETF does not maintain exposure to the underlying equities. However, if the options are exercised the ETF has the ability to hold the equity for up to 90 days, if a price reversal is anticipated.

Large Cap U.S. Equity

→ **Market Options**
- Maximum 50%

→ **Security Selection**
- Minimum 50%
- Technical and fundamental screens
- 30-50 names

→ **Write OTM Put Options**
- Cash secured
- Identify exercise price to earn diversified yield

Individual Security Selection Process

Technical Screens

Market Risk (Systematic)

1. **Lower exposure to downside systematic risk (compared to upside systematic risk)**
   - Calculate “up market beta” and “down market beta” for every stock.
   - Select stocks that have the highest differential between up market and down market beta, in order to favour stocks with better upside performance, and less volatility on the downside.

Security Risk (Non-systematic)

2. **High implied volatility relative to its history**
   - Measure implied volatility relative to the stock’s historical range.
   - Identifies stocks with higher volatility that can potentially generate a high level of premium and in turn a higher level of income.
3. **High skew relative to its history**
   - Skew measures the willingness of investors to pay for downside protection. A high skew implies demand for puts relative to calls and that investors are willing to pay a higher premium for downside protection.

Fundamental Screen

4. **Qualitative Oversight**
   - Once the three screens are applied our portfolio management team applies a qualitative oversight and evaluates each position on an individual basis to understand company specific risks such as earnings announcements that may impact future stock performance.

Construction

Stocks on the short list are analyzed using fundamental factors and technical indicators to assess specific downside risk. The stocks are then analyzed in the context of the options market to determine the most optimal moneyness and tenor of each position. Using names selected from the short list, approximately 60% of the portfolio is constructed with options written on 30-50 securities. The remainder of the portfolio will be options written on the market itself (large cap U.S. equities). The securities portion of the portfolio will also have a sector cap of 20% to ensure that the ETF is not overly concentrated in one sector.

Tenor and Moneyness of Positions

Our portfolio will generally write puts 1 to 6 months to expiry and we will aim to diversify option maturities. The shorter the tenor, the greater the effect of time decay. However, this also leaves less time for a stock to recover, should it experience a significant downside move. Moneyness of the option in part will be determined by the tenor selected. Generally, the target range for option moneyness will be 10 to 20%.

Rolling Positions

We will generally hold options until maturity. When a security moves higher, we may look to roll the option position into a future option that can provide a higher risk adjusted yield over the remaining time to maturity. If exercised, the fund has the ability to hold the security for up to 90 days if a price reversal is anticipated.

Frequency of Screening

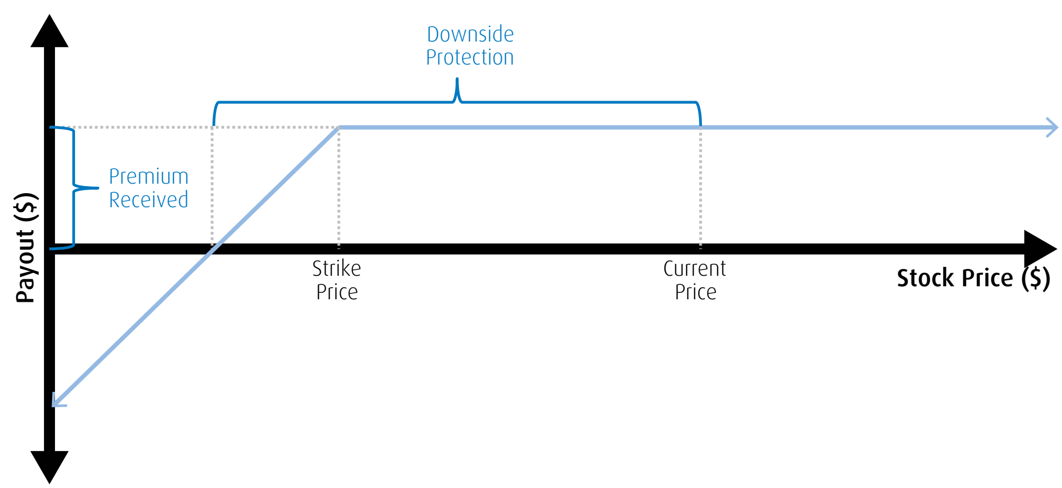
The screen will be run, and a short list of potential options will be created on a monthly basis, in advance of options expiry. The portfolio manager will also have daily oversight on each option. Candidates will remain on the short list for the month until the screen is run again. Should cash flows require new put positions to be implemented intra month, the same list of candidates will be used to select from. New lines on existing or new securities altogether may be selected.

Return Environment

The advanced screens and portfolio constraints ensure the portfolio is constructed to perform well in flat or moderately advancing equity markets. In high return scenarios, this strategy will underperform as it does not have equity exposure. In significant market downturns this strategy will decline as the puts move into the money.

Our put write strategy provides exposure to short dated options that are appealing to investors looking to generate income with low correlation to other asset classes.

Payoff Characteristics of Selling an OTM Put Option



For illustrative purposes only.