October 2019

CIBC MULTI-ASSET ABSOLUTE RETURN STRATEGY (MAARS): A GUIDE

By Michael Sager[1]

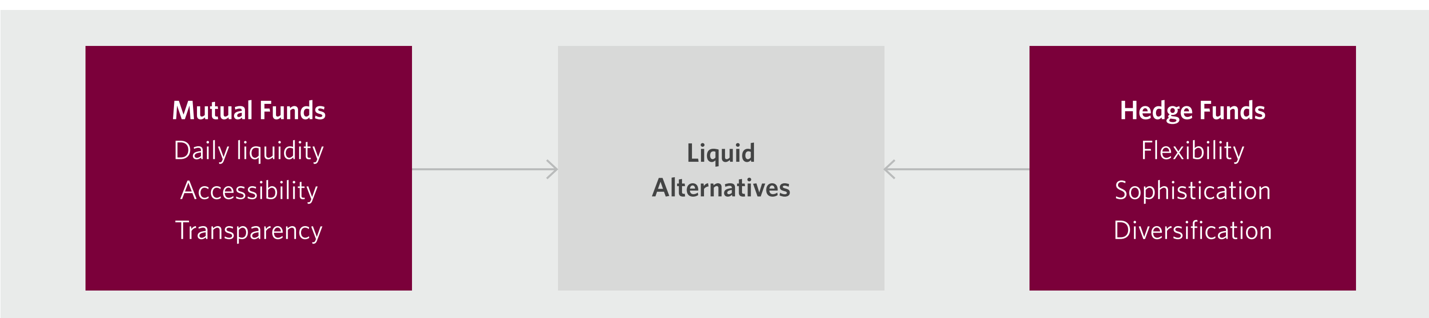
1. MAARS

- A liquid alternative multi-asset strategy, encompassing long-only and long/short exposures to equities, bonds, currencies, and commodities.
- A top-down investment strategy, with no individual security selection.
- Managed by CIBC Asset Management's (CAM) Multi-Asset and Currency Management team.
- Targets an annualized absolute return of 5% plus cash, on average over rolling 3-year periods. Cash is defined as the 91-Day Government of Canada T-bill interest rate.
- Targets bond-like risk, with an expected return better than (expected) fixed income outcomes.[2]

2. What are liquid alternatives?

Combine best-in-class hedge fund strategies with mutual fund liquidity, regulation, transparency, and fees.

Figure 1 – Characteristics of Liquid Alternatives



[1] Michael Sager is a Client Portfolio Manager in the Institutional Asset Management Team.
[2] The strict definition of the long-term MAARS risk target is an annualized volatility equivalent to one half of the MSCI All Country World Index (in CAD terms), calculated over rolling 3-year periods.

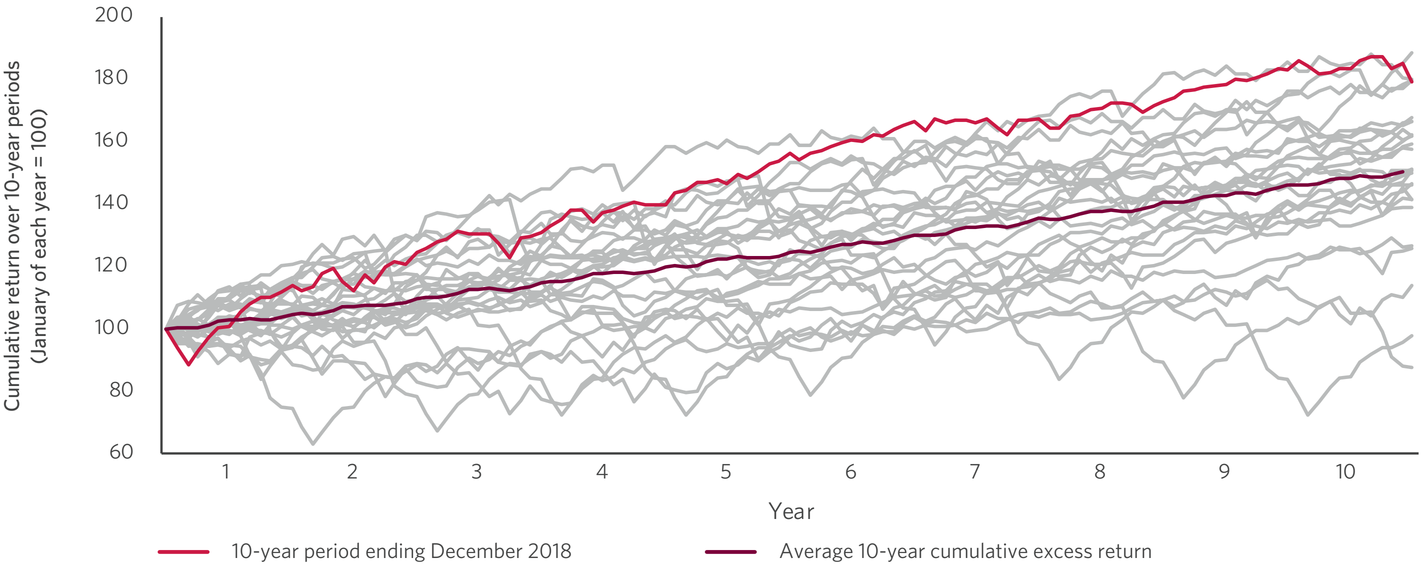
3. What challenges do liquid alternatives address?

Challenge #1: low expected returns to most asset classes, including public equities and fixed income, but also many illiquid alternatives—including Private Equity, Infrastructure, and Real Estate.

The weak outlook for returns suggests the performance of a Global Balanced portfolio will be less attractive over the next ten years as compared to the last decade (Figure 2). An allocation to liquid alternatives can help improve expected portfolio performance.

Figure 2 – Expected Returns to a Global Balanced Portfolio are Relatively Low[3]

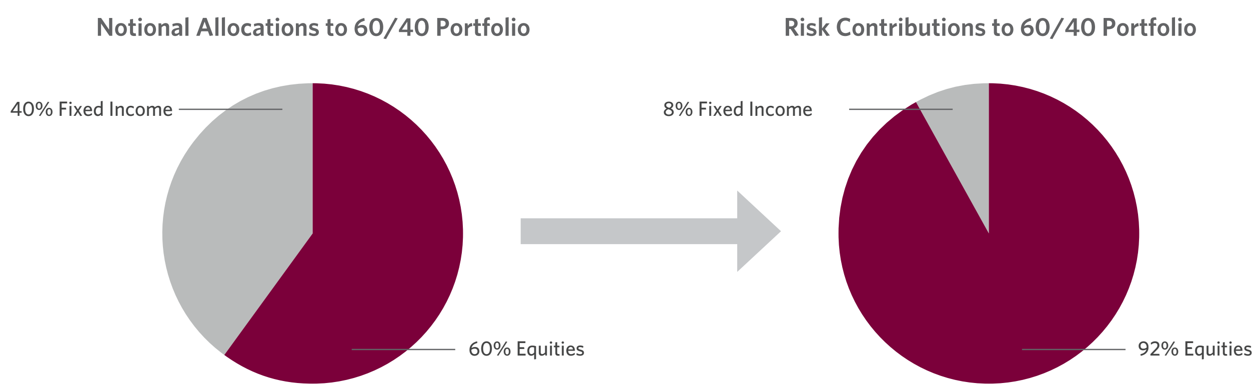
10-Year Cumulative Returns to Balanced Portfolio in excess of the cash rate



The information was prepared by CIBC Asset Management Inc. using the following third party service providers' data: Bloomberg, Bridgewater.

Challenge #2: a high concentration of risks within Global Balanced portfolios, dominated by public equities (Figure 3).

Figure 3 - Global Balanced Portfolio Risk is Concentrated in Equities

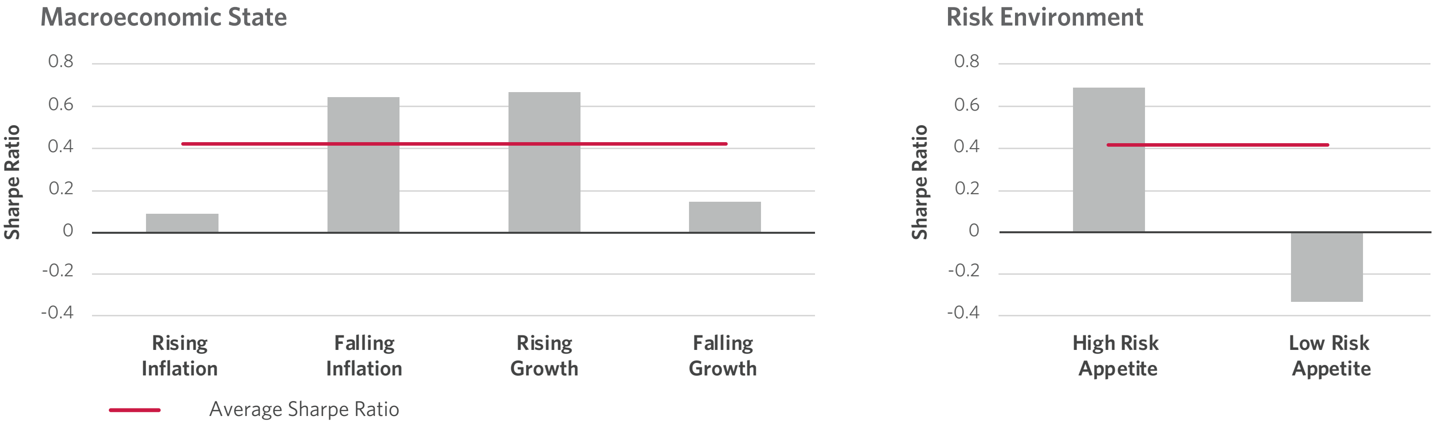


The information was prepared by CIBC Asset Management Inc. Illustrative example.

[3] Each gray and red line reports the 10-year cumulative return to a Global Balanced 60/40 portfolio in excess of a 3-month cash interest rate starting in January of each year in sample. Full sample is 1988 to 2018. Global Balanced portfolio constructed as: Equities (30% Canada (S&P/TSX), 15% U.S. (S&P 500), 10% EAFE®, 5% Emerging Market (MSCI EM)); Fixed Income (20% Canadian sovereign bonds (FTSE TSX), 20% US sovereign bonds (Barclays US Aggregate Bond Index)).

This risk concentration makes portfolio performance episodic, and sensitive to the macroeconomic environment: performance is expected to be good in periods of strong growth and low inflation, and less favourable in periods of weaker growth and higher inflation (Figure 4).

Figure 4 - Global Balanced Performance depends on Macroeconomic Conditions



The information was prepared by CIBC Asset Management Inc. using the following third party service providers' data: Bloomberg.

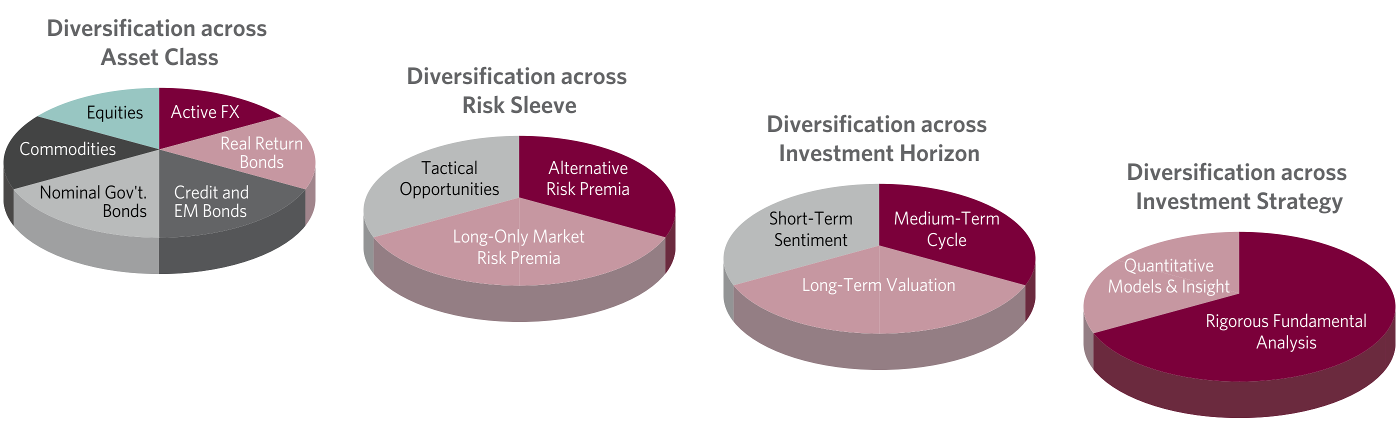
4. Why MAARS?

CIBC Asset Management (CAM) has implemented absolute return strategies on behalf of institutional clients since 1996. The Multi-Asset and Currency Management team has achieved significant success during this time.

2018 regulatory reform allowed CAM to efficiently offer its accumulated experience and expertise to retail investors.

> MAARS offers best-in-class Hedge Fund investment strategies within a liquid, transparent, low fee mutual fund framework (Figure 5).

Figure 5 – MAARS diversification across asset classes, investment strategies, & horizons is expected to achieve smoother, more attractive returns than traditional equity-centric portfolios



The information was prepared by CIBC Asset Management Inc..

- Numerous competing liquid alternative funds have been launched in the wake of 2018 Canadian regulatory changes, often with similar return and risk objectives to MAARS.
- Unlike CIBC AM, many investment managers now active in liquid alternatives have little experience of implementing absolute return strategies. They have no performance track record.

5. How to allocate to MAARS?

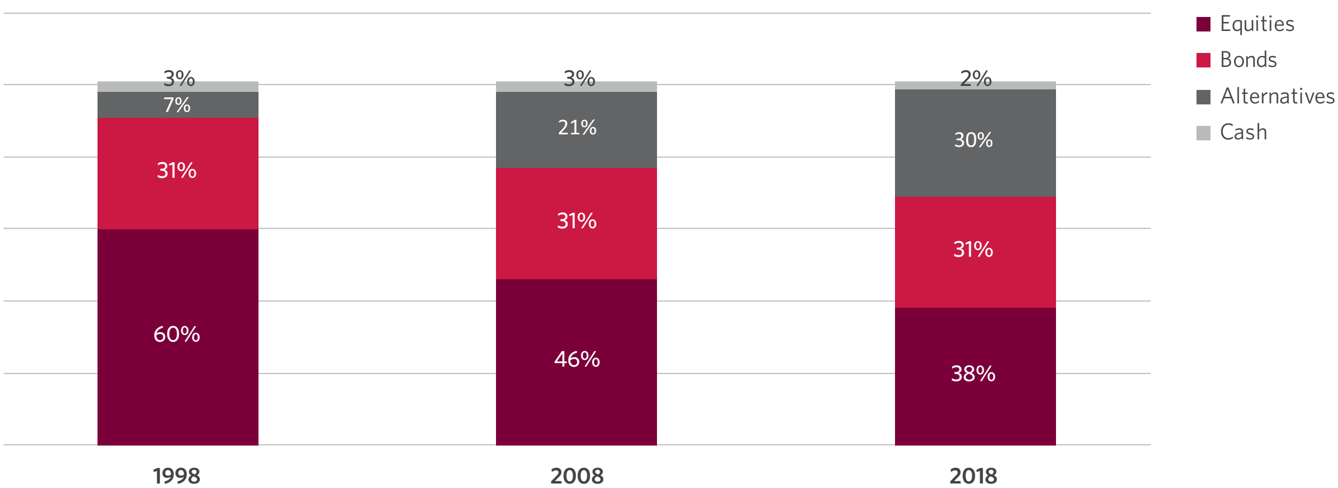
- Many investors see MAARS as a substitute for a portion of existing allocations to fixed income. MAARS targets bond-like risk, but with a more attractive expected return.
- An allocation to MAARS funded from fixed income also makes sense from a tax perspective. Reflecting the use of derivatives to implement investment views, returns to MAARS will be taxed as a mix of income and capital gains.
- Other investors allocate to MAARS from existing equity holdings. In this case, MAARS targets a lower long-term risk than equities, but a similarly attractive expected return.
- MAARS is expected to diversify away from macroeconomic growth—the main driver of equity returns—and so contribute to smoother, more consistent portfolio performance.

6. How much to allocate to MAARS?

Asset allocation decisions for small and medium-sized Canadian pension funds may be a template for High Net Worth (HNW) retail investors; there are increasing similarities between the two groups.

Pensions have progressively allocated away from equities, particularly Canadian equities, in favour of alternatives (Figure 6). The typical strategic allocation of these plans is now 40/30/30 to equities/fixed income/alternatives.

Figure 6 – Strategic Asset Allocation of Average Canadian Pension Plan (pies from MAARS booklet)



The information was prepared by CIBC Asset Management Inc. using the following third party service providers' data: Willis Towers Watson. Due to rounding, amounts presented herein may not sum to 100%.

Within alternatives, allocations are often split evenly between: illiquid asset classes (infrastructure and real estate); illiquid strategies (private equity and niche hedge fund strategies); and liquid alternatives, such as MAARS.

904 | 09/2021