MACKENZIE
Investments

**Accessible Alternatives™**

# Build resilience in volatility

## Absolute return strategies and how they are built to deliver in rising and falling markets

Volatility is generally the enemy of traditional equity funds. Spikes in market volatility often come with deep portfolio losses and extended periods of negative or flat returns, even for investors with relatively good stock selection.

In contrast, elevated volatility can be beneficial for absolute return funds. Absolute return funds can dynamically invest both long and short, so they are able to generate positive returns from falling markets in some environments. They can also engage in relative value trading across securities within a market, and by doing so can strip out the effect of the overall market direction. Moreover, during volatile environments there is often greater dispersion among securities, making relative value trading potentially more profitable.

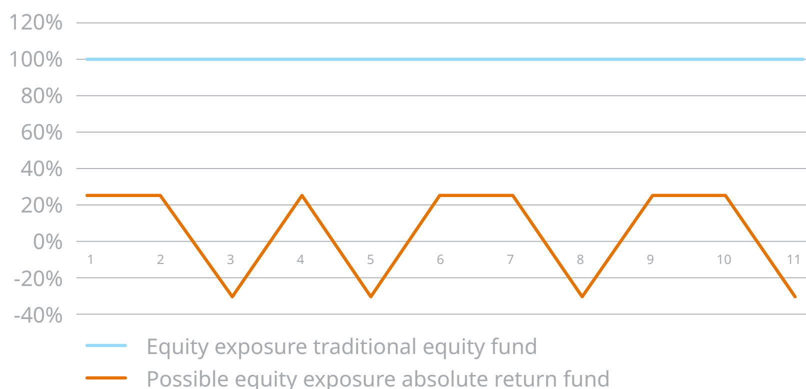
This flexibility to short-sell entire asset classes and individual securities allows absolute return funds to potentially add considerable value during volatile environments when traditional long-only portfolios need the most help. This makes absolute return funds complimentary tools to equity and bond funds in portfolio construction.

## Dynamic asset allocation is essential for a more resilient portfolio

Instead of simply over- and under-weighting equity exposure versus a benchmark, dynamic asset allocation within absolute return liquid alternatives allows that exposure to be positive, zero or even negative, depending on market conditions.

By dynamically changing the amount and sign of different asset class exposures in a portfolio, it is possible to produce a positive return over a period where equity markets have been quite volatile and overall flat or negative.

### Traditional equity vs absolute return equity market exposure




For illustrative purposes only

**It is possible to produce a positive return over a period where equity markets have been quite volatile.**

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## Relative value trading and generating positive absolute returns in a market neutral fashion

Liquid alternative strategies can engage in a form of security selection known as relative value trading, by going long and short two related securities. This can be done with individual stocks in the equity market such that the investor captures all the return differential between two stocks but none of the performance of the broader equity market.

For example, if a portfolio was long stock A and short stock B, and stock A went down -10% while stock B went down -15%, the return on that relative value trade is +5%. The long position outperformed the short position by 5% and they were equally weighted. It did not matter that both stocks were down as only the relative return matters in market-neutral pair trades such as this. Trading bond, currency and commodity pairs are other common forms of relative value trading found in absolute return strategies.

**Positive results from relative value trading depends on two things:**

1. **Skill**
2. **Opportunity**

Positive results from relative value trading depends on two things: skill and opportunity.

Another word for opportunity in this context is high dispersion, which means there are wide gaps in the performance of different investments within a larger asset class. No dispersion means zero opportunity to add value through relative value trading, and high dispersion means more opportunity.

Often, highly volatile equity markets and uncertain macro-economic conditions lead to heightened levels of dispersion within currency, commodity, fixed income and equity markets. This allows investors with demonstrable skill to capitalize on a larger set of opportunities and generate positive absolute returns in a market neutral fashion, when investors need it the most.

**More opportunity for return in a volatile market with wider dispersion between winners and losers:**

## Achieve greater diversification with our accessible alternatives

The advent of liquid alternative mutual funds in Canada has made it relatively easy for investors to achieve a more complete degree of diversification. One example would be Global Macro strategies, such as Mackenzie's Global Macro Fund. These are mutual funds that make wide use of non-directional strategies to generate return patterns that can be very different from those found in traditional long-only stock, bond and balanced funds. Incorporating an allocation to a global macro allocation to a global macro strategy is an effective way for investors to improve portfolio diversification.

**Explore whether alternative investments are an appropriate choice for you. Speak to your financial advisor today.**

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