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# Canadian Pension Risk Strategies Summit

May 7, 2015 | Toronto | Four Seasons Hotel

## The Shifting Fixed Income Landscape

*Aubrey Basdeo, Head of Canadian Fixed Income*

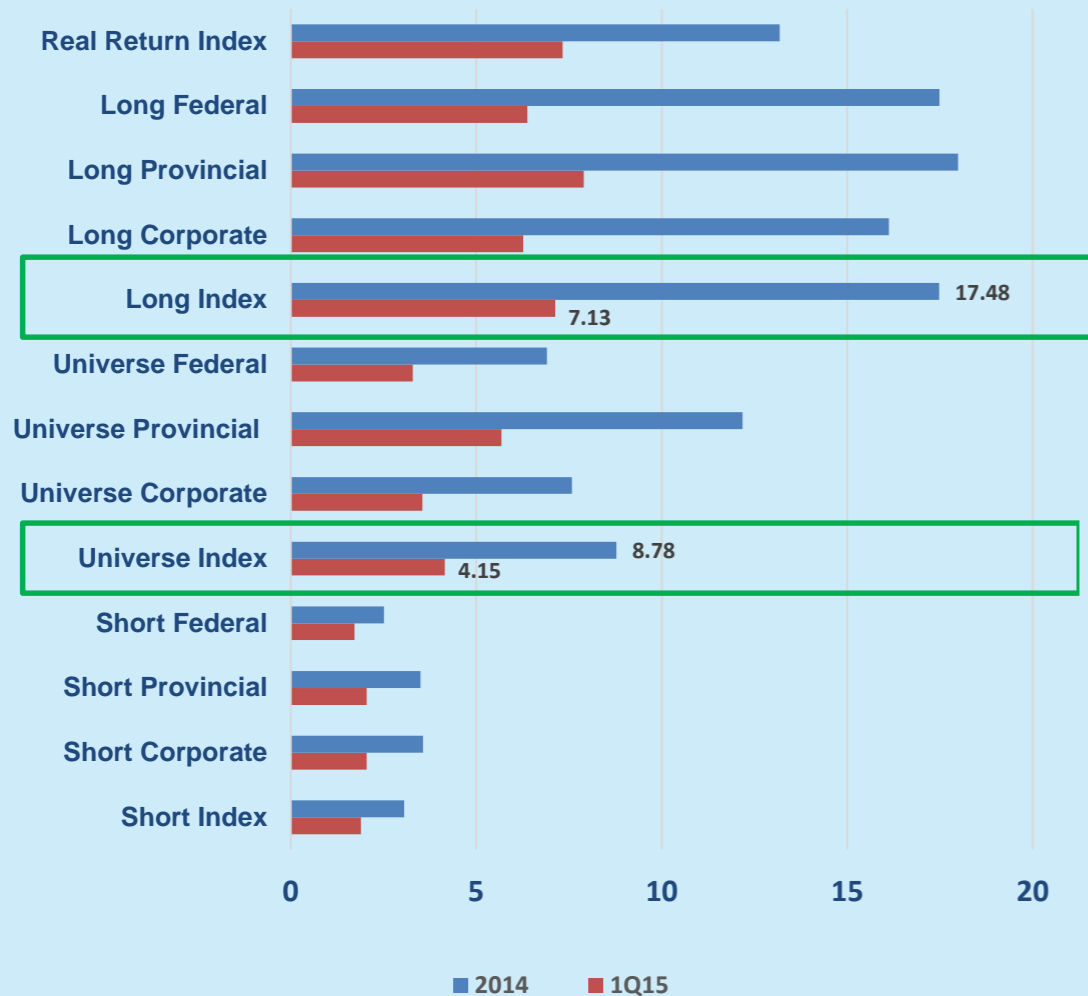
*Chris Barr, Co-Head of Multi Sector Institutional Product Strategy*



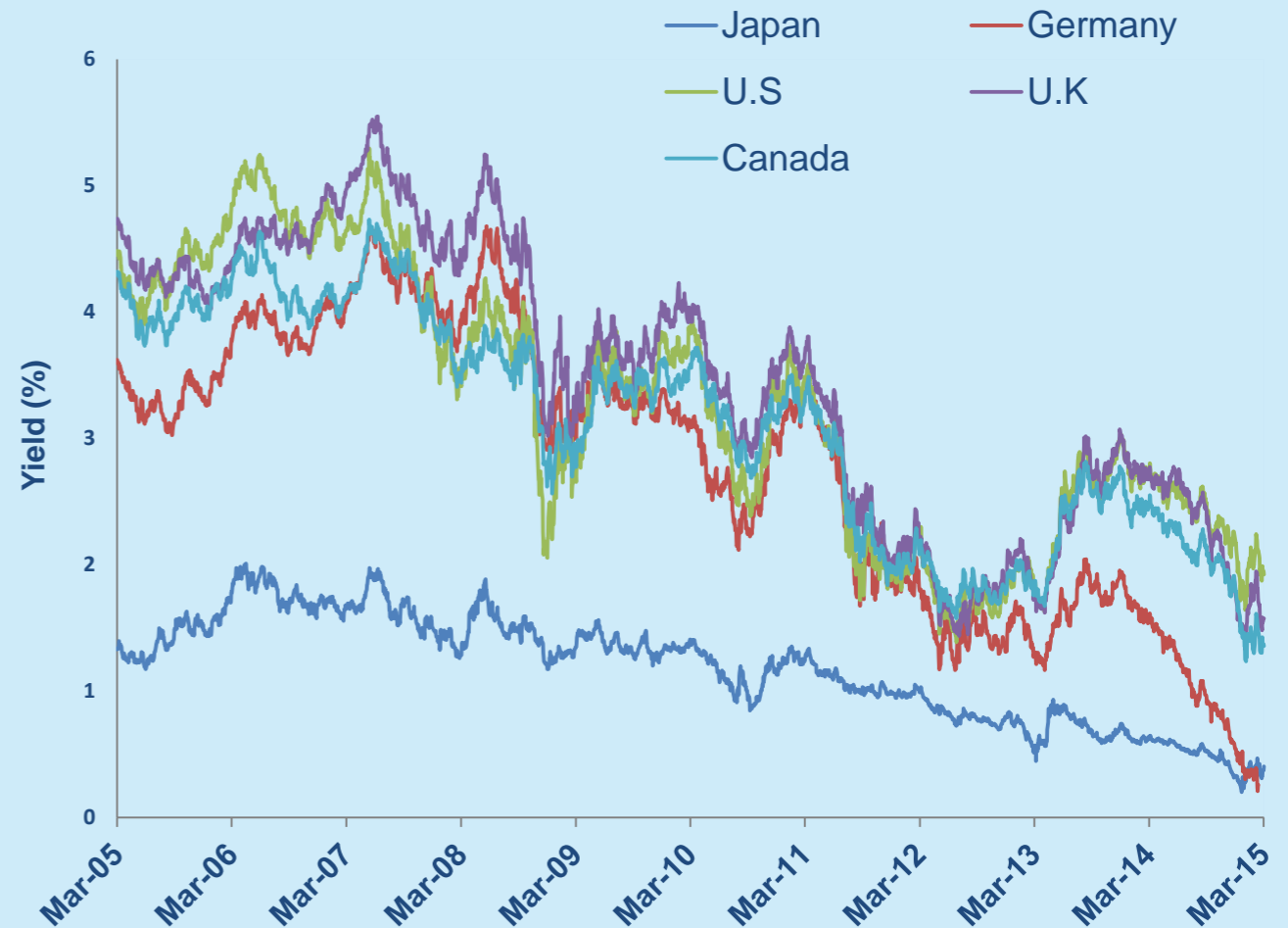
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# 2014 recap: The year investors squeezed out more juice in most assets

## Asset class performance in 2014 (total return %)



## 10 Year Yields



Performance in calendar year to date – percent  
 Source: Bloomberg, L.P. ("Bloomberg") FTSE TMX Global Debt Capital Markets Inc., 3/31/15  
 Full index names in appendix.

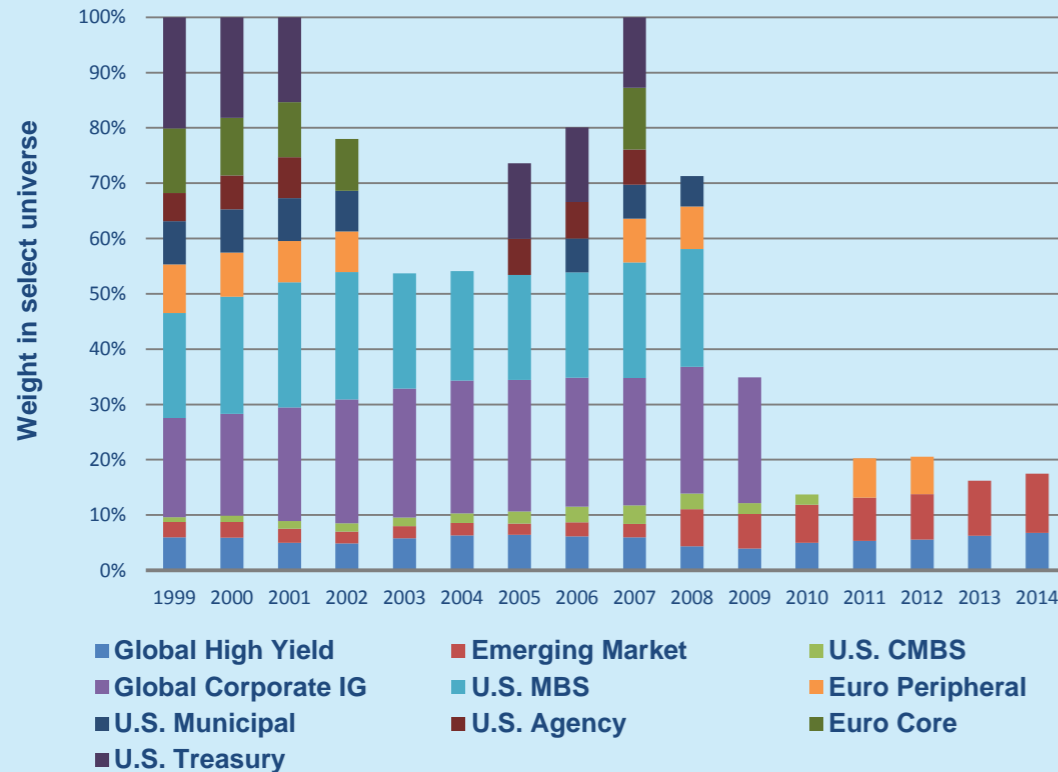
## Polling

What was the annual total returns for Canadian Core Fixed Income over the last 30 years?

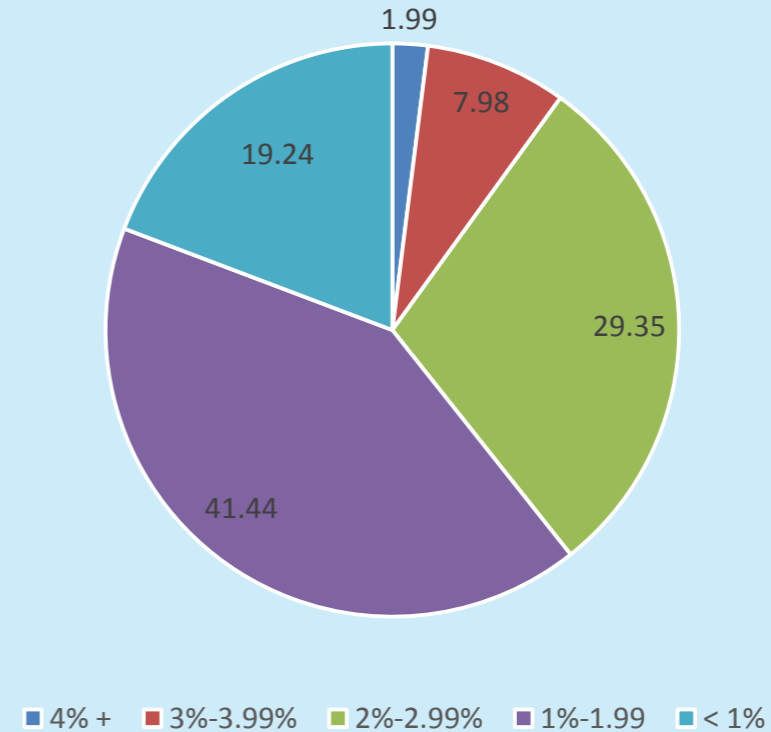
- 1) 5.40%
- 2) 10.20%
- 3) 8.60%
- 4) 7.10%

# Global financial repression has left scarce yield in its wake

The amount of global fixed income yielding greater than 4% has decreased...<sup>1</sup>



...and less than 2% of the FTSE TMX Canadian Universe Bond Index yields more than 4%<sup>2</sup>

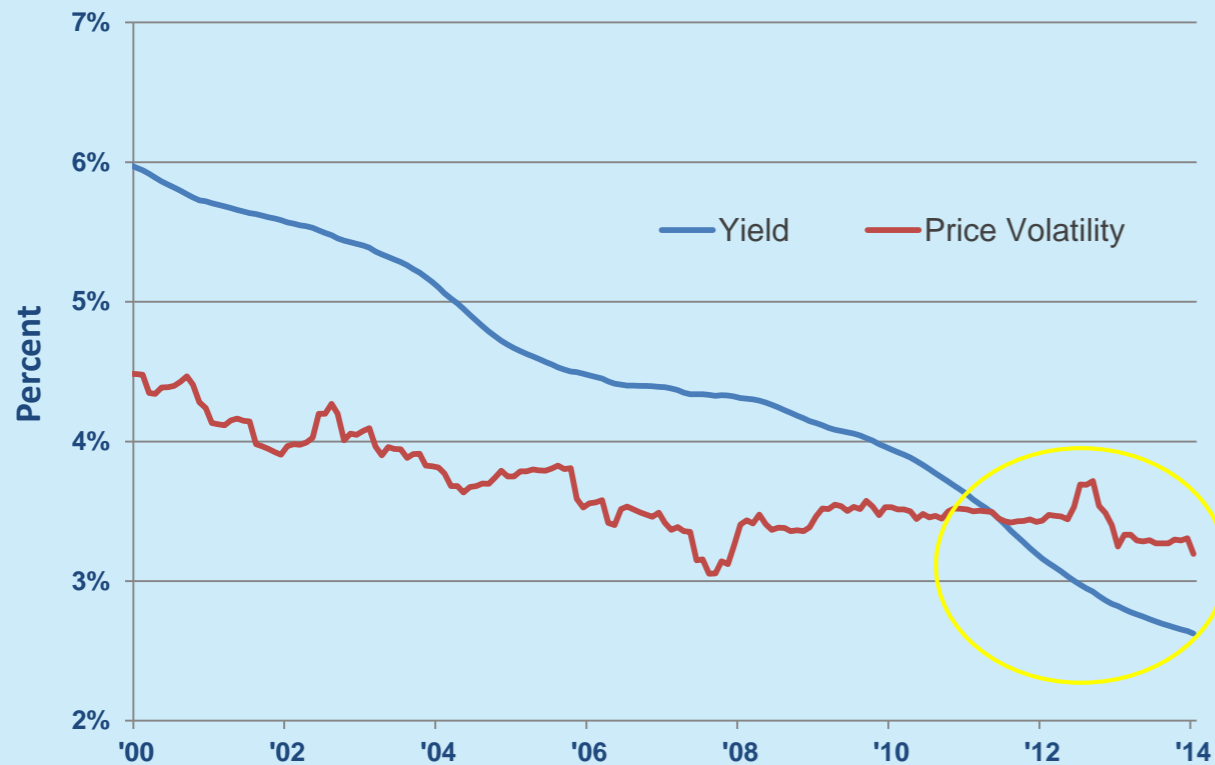


<sup>1</sup> Includes the following Indices: US Treasury, US Intermediate Treasury, US Long Treasury, US Aggregate, US Agency, US Government Sovereign, US Credit, US Credit Corp, US Credit Industrial, US Credit Utility, US Credit Finance, US Securitized, US MBS, US CMBS Aggregate, US Intermediate Corp, US Credit Corp 10+ Yrs, US HY, Global Emerging Markets, Global Agg, Asian Pacific Aggregate. Sources: BlackRock Investment Institute, Barclays and Thomson Reuters, June 2014. Notes: The bars show market capitalization weights of assets with an average annual yield over 4% in a select universe that represents about 70% of the Barclays Multiverse Bond Index. Euro Core is based on French and German government debt indexes. Euro Peripheral is an average of government debt indexes for Italy, Spain and Ireland. Emerging markets combine external and local currency debt.

<sup>2</sup> Source: FTSE TMX Global Debt Capital Markets Inc, as of March 31, 2015

# Generating yield without sacrificing principal protection has become increasingly challenging

At current yields, traditional fixed income offers little protection<sup>1</sup>



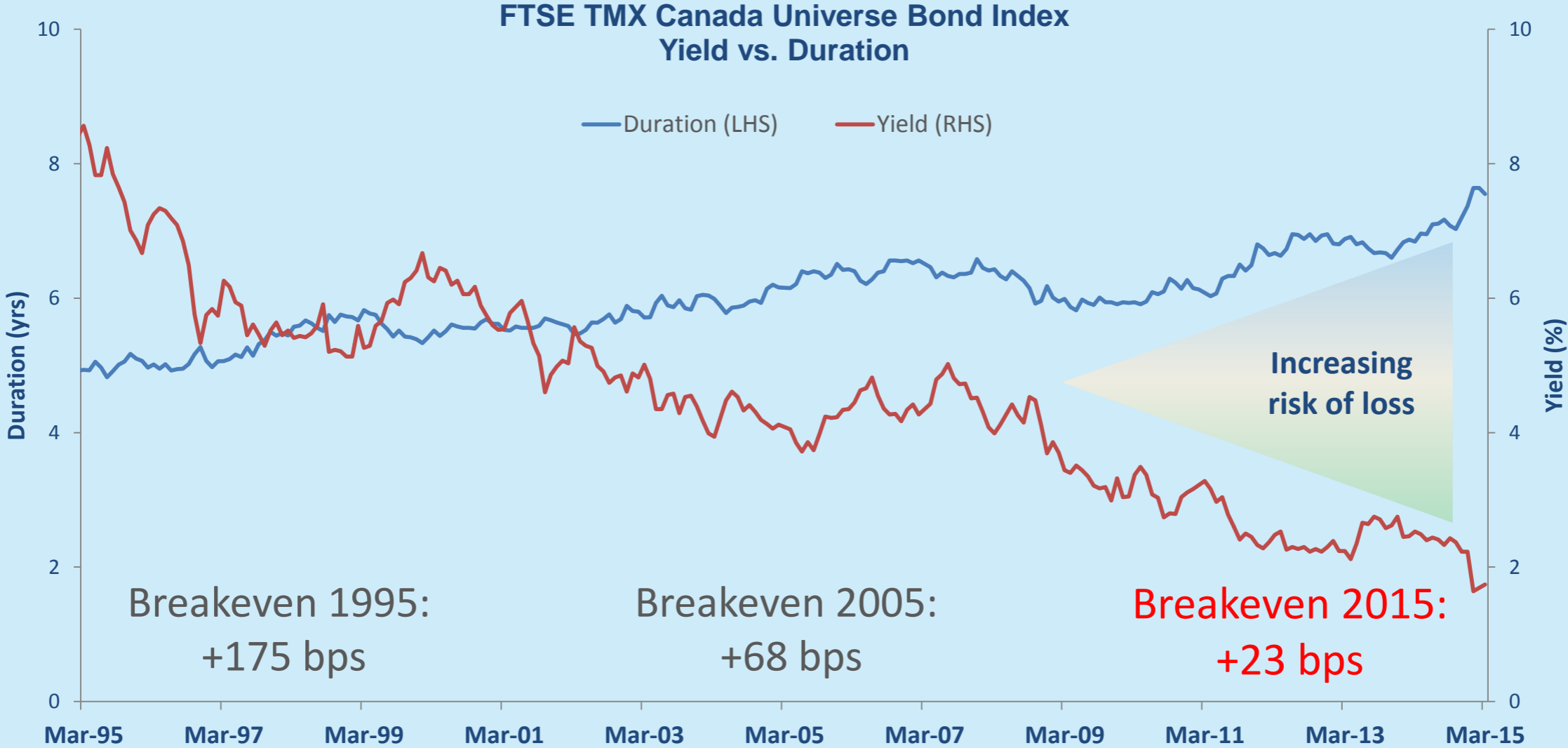
Elevated risk of negative returns may continue<sup>2</sup>



1. Source: FTSE TMX Canada, Based on rolling 5 year annualized yield and index price return volatility; data through 31 March 2015

2. Source: FTSE TMX Canada, Bloomberg. Calculation includes return and volatility as variables (assuming a normal distribution) to generate probability. Data as of March 31, 2015

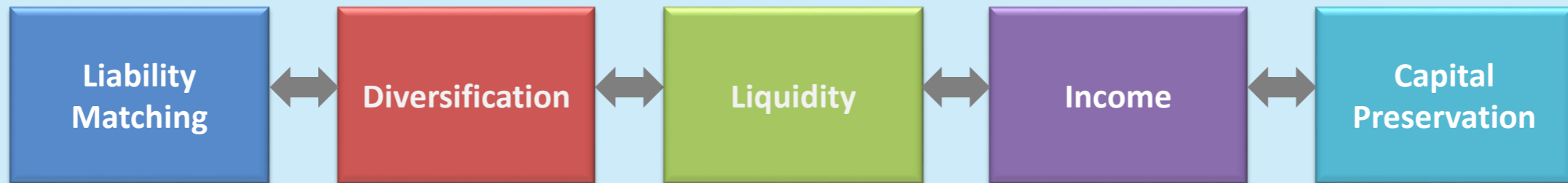
# ...and the cushion keeps shrinking – increased risk of negative returns



Source: FTSE TMX Canada. Data as of March 31, 2015

# Asymmetry: Implications and options

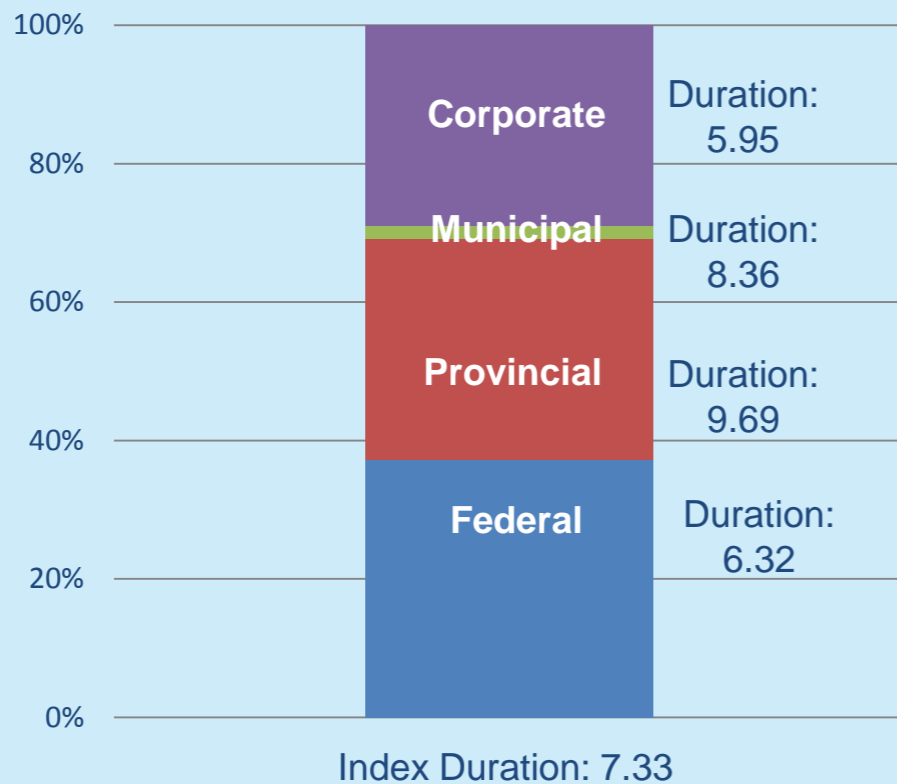
- The FTSE TMX Canada Universe Bond Index rate and return environment has changed materially in the last few years
- The spectrum of risk/return trade-offs fundamentally change in a low yield / long-term rising rate environment
- Investors should evaluate the ability of the benchmark to meet asset class objectives in the current environment



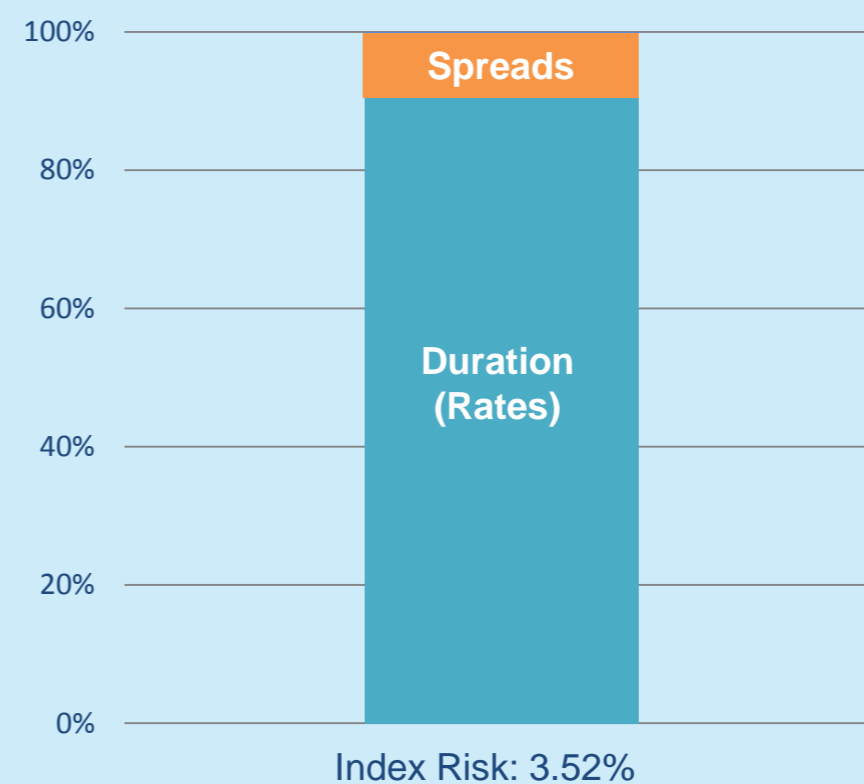
# Canadian Fixed Income: Sector vs Risk Factor Diversification

## FTSE TMX Canada Universe Bond Index

### Sector profile



### Risk profile

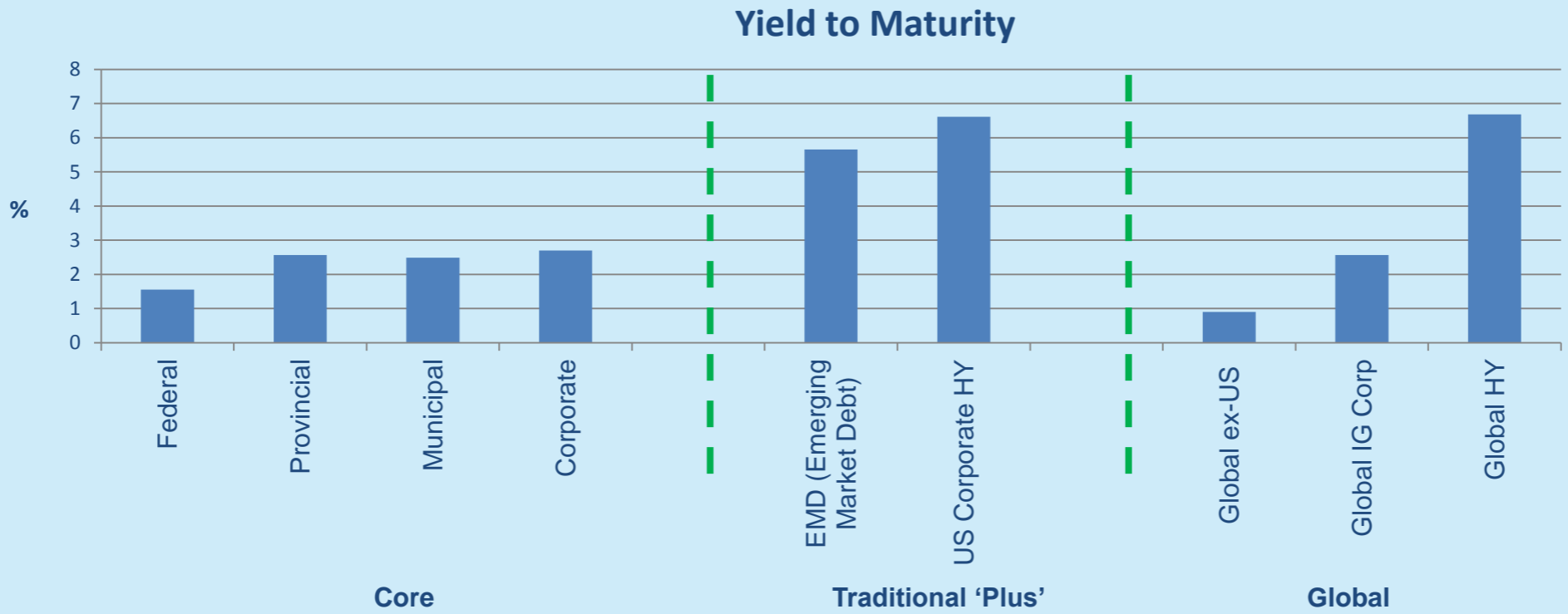


Source: FTSE TMX Canada, BlackRock Solutions as of 12/31/2014



# Benefits of diversification by expanding fixed income opportunity set

Adding “degrees of freedom” outside of the FTSE TMX Canada Bond Universe requires skill, liquidity, and markets where risk can be managed efficiently

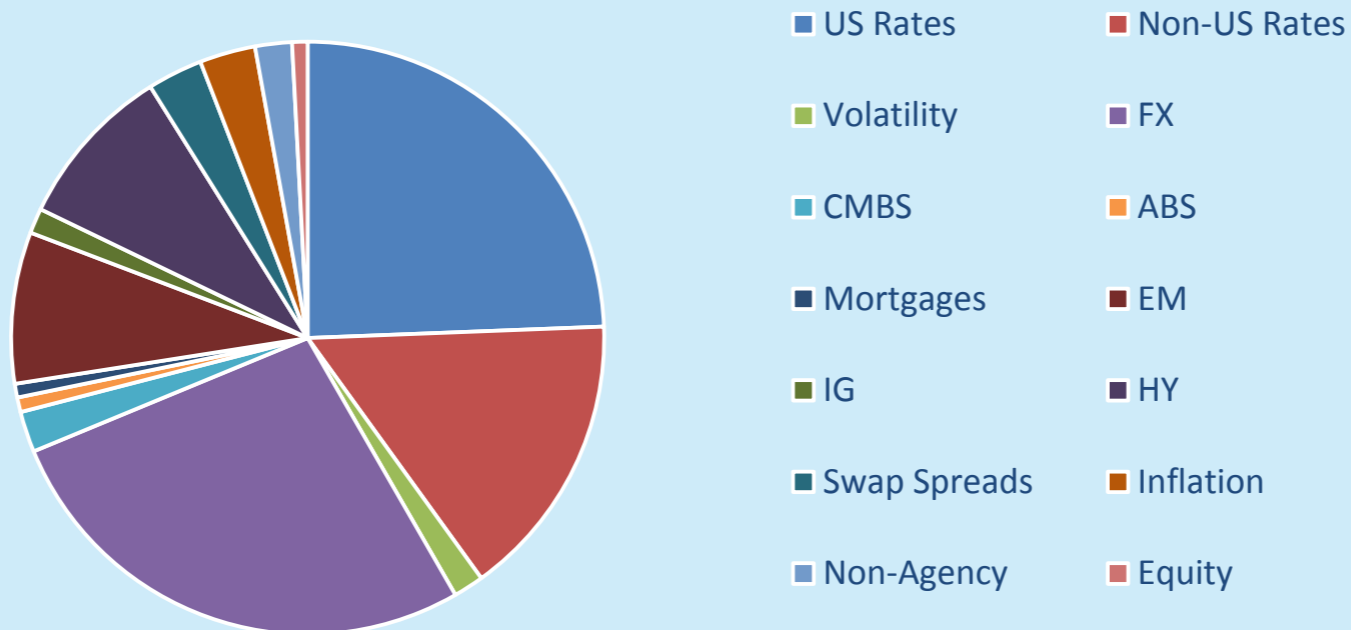


	Core				Traditional 'Plus'			Global		
<b>Duration (years)</b>	6.32	9.69	8.36	5.95	5.89	4.25		7.14	6.28	4.29
<b>Market Cap. (trillion)</b>	C\$0.46	C\$0.38	C\$0.02	C\$0.36	\$1.41	\$1.33		\$24.63	\$7.58	\$2.13

Source: Barclays, FTSE TMX Canada Bond Universe, BlackRock, data as of 31 Dec 2014.

# Unconstrained strategies should offer risk factor diversification to perform in all rate environments

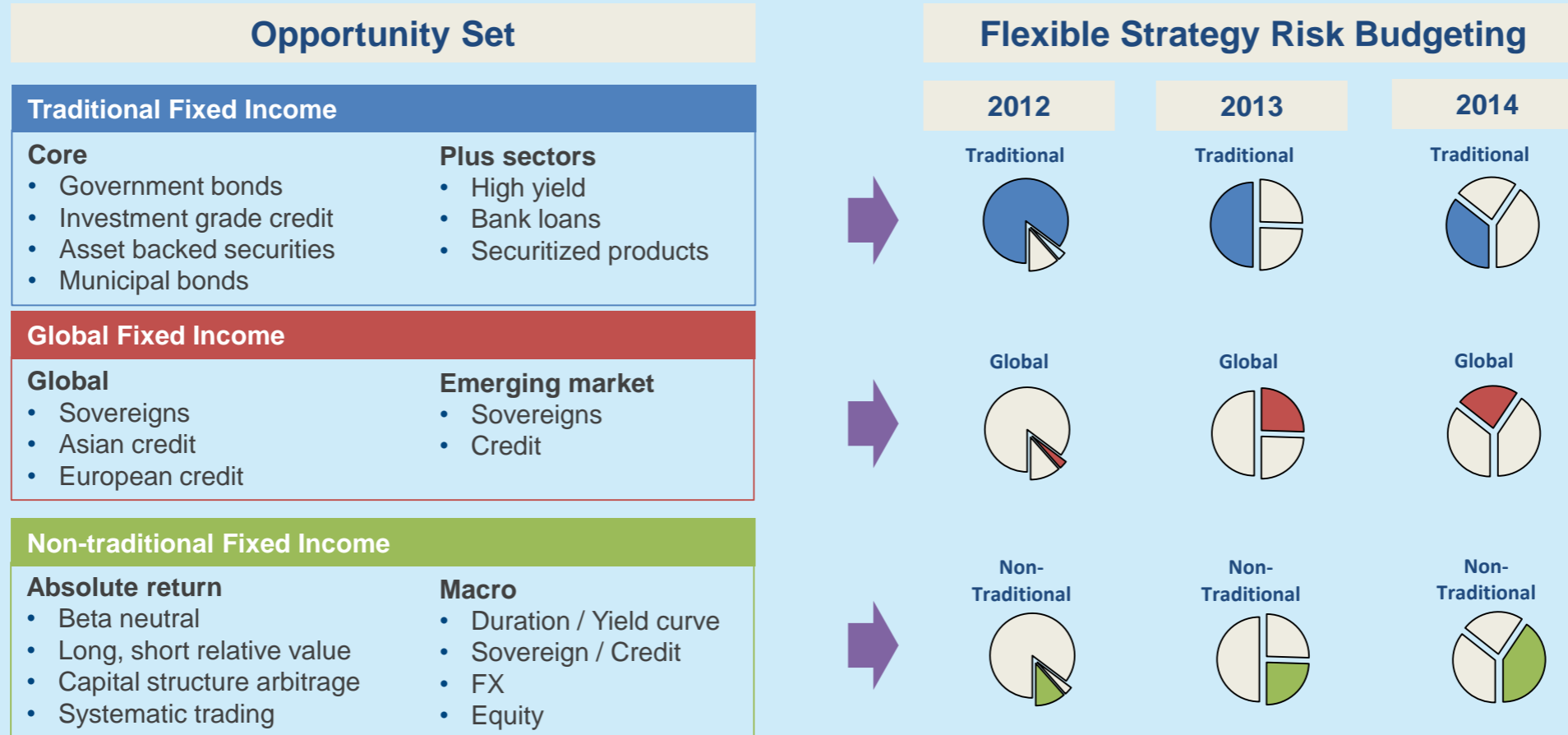
## Unconstrained Portfolio – Risk Allocation



Duration	1.61
Yield	2.30 %
Risk# :	172 bps
<b>Flexibility translates into attractive risk adjusted returns</b>	

- \*Yield as of 31 January 2015. Yields for fixed income indexes are yield-to-worst, calculated based on all possible call dates, reflecting lowest potential yield that can be received without the issuer actually defaulting.
- # The above pie charts show the distribution of Stand Alone Risk within the Barclays Global Aggregate and BGF FIGO. Source: BlackRock Solutions (BRS);
- All data as of 31 January 2015. Source BlackRock

# Flexible Process Defined: Sector *and* strategy diversification

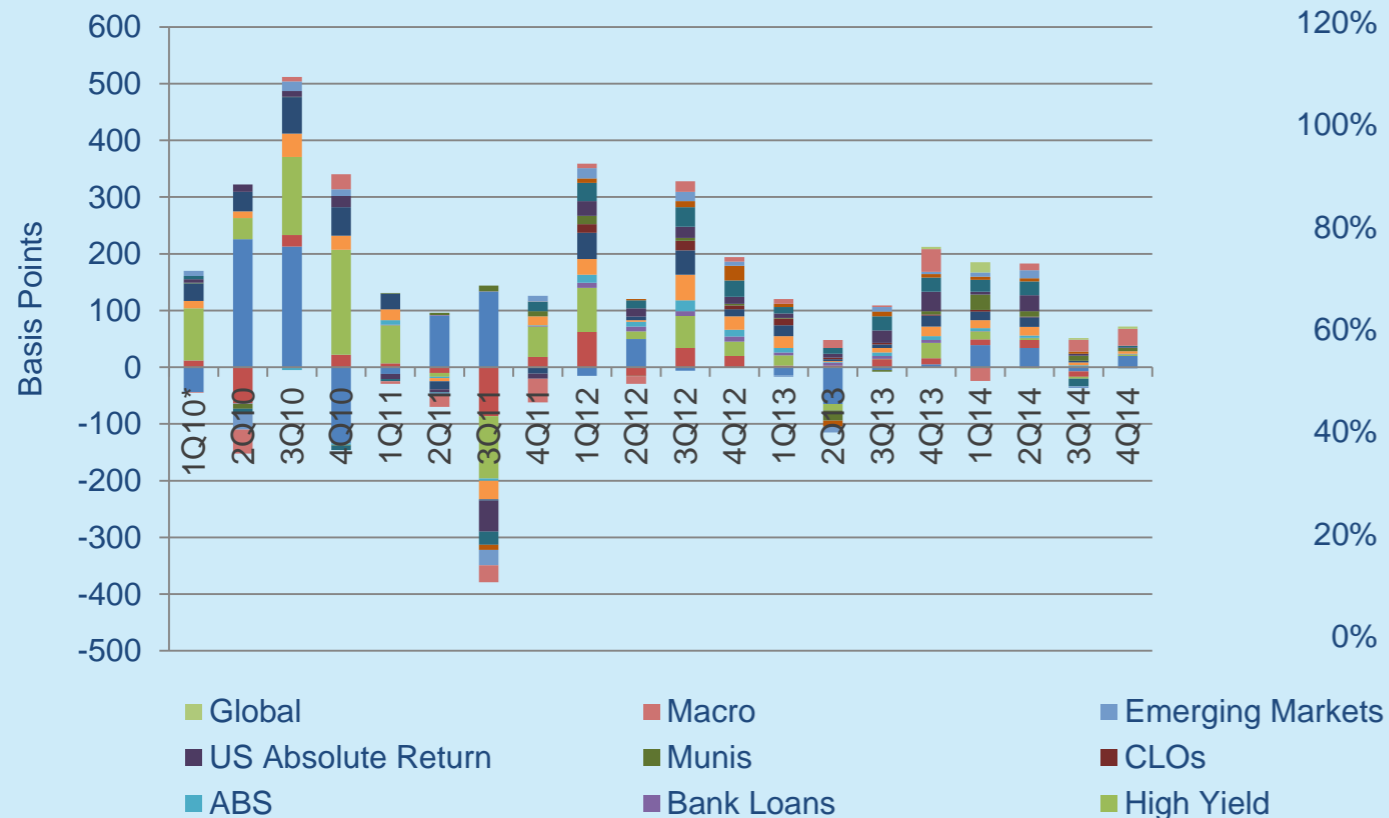


Source: BlackRock. Strategy weights as of 30 June 2014 of respective years. For illustrative purposes only.

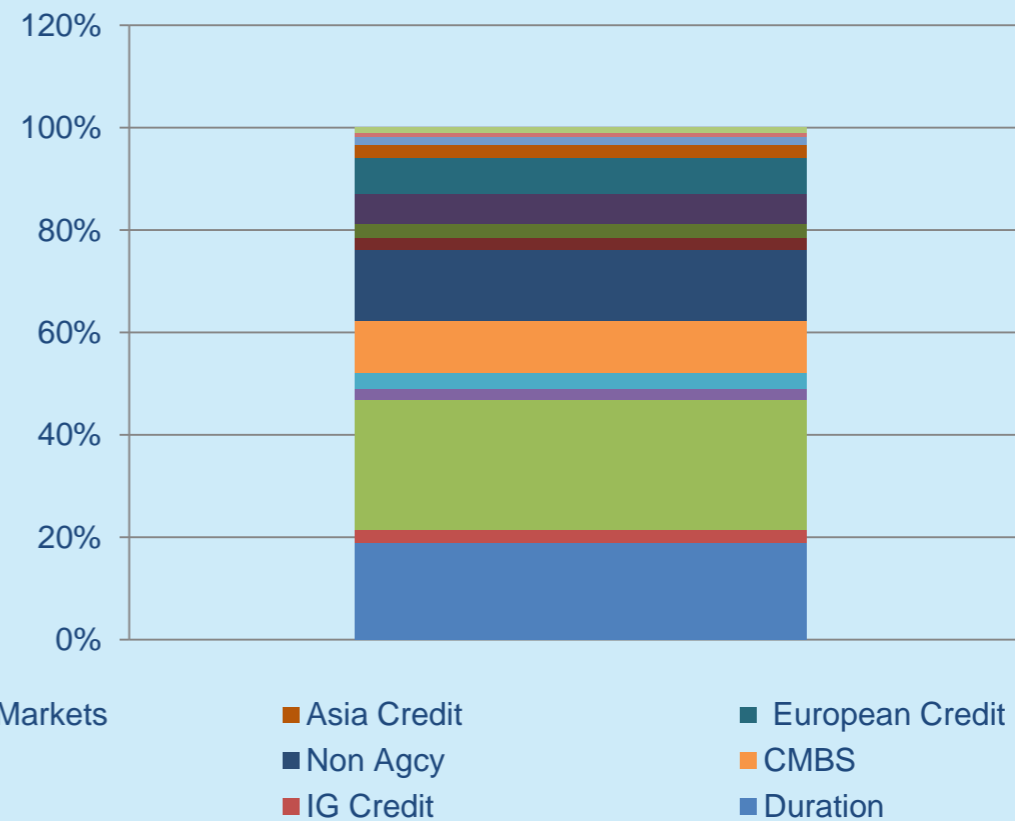
# Proof Statement: Diversified risk means diversified alpha

- Look for un-concentrated alpha
- No single alpha source has contributed more than 25% of total performance since inception

## Quarterly Return Attribution

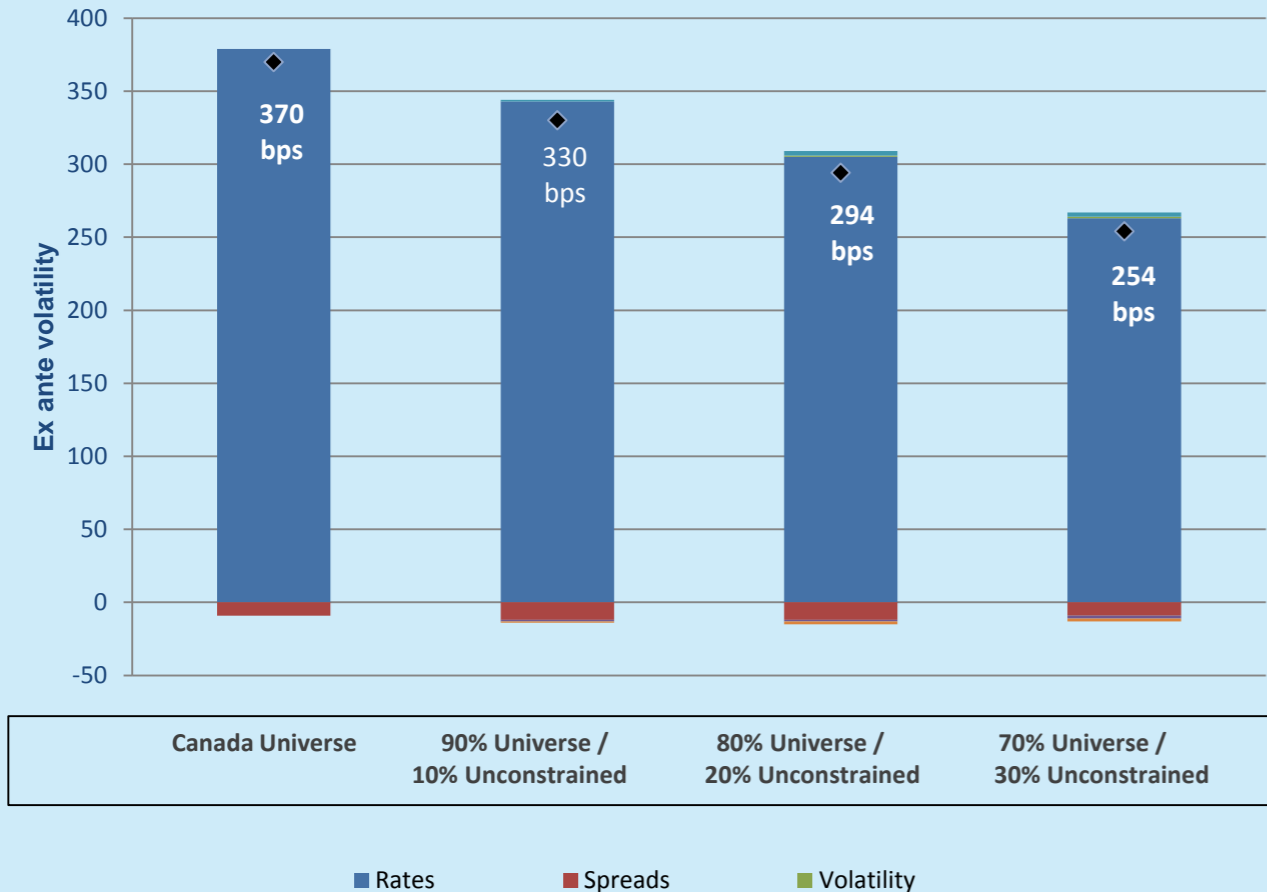


## Contribution to Alpha



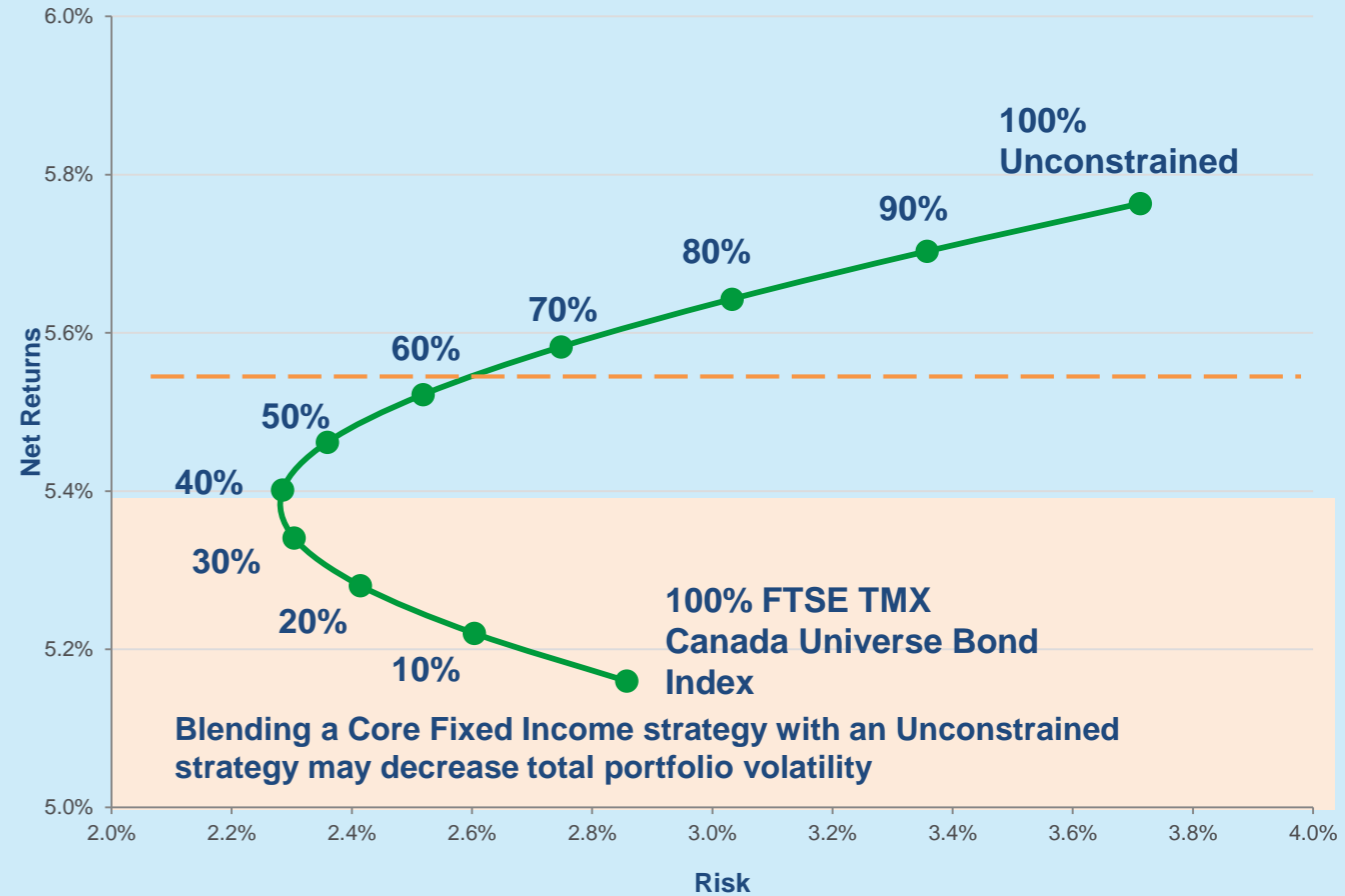
# Impact of varying size of an unconstrained allocation to a core CAD Universe holding

Overall risk is reduced, but rates remain the primary exposure



For illustrative purposes only.  
Source: BlackRock Portfolio Risk Tools.

Net returns and risk



Blending a Core Fixed Income strategy with an Unconstrained strategy may decrease total portfolio volatility

Source: Morningstar, FTSE TMX Canada, BlackRock; Net Returns for FTSE TMX Canada Universe Bond Index and BlackRock Strategic Income Opportunities Fund (Institutional share class) are dated from March 31<sup>st</sup>, 2010, the first full month after the SIO investment strategy changed, to April 30<sup>th</sup>, 2015. Risk figures are calculated based on the historical Net Returns for both Funds, adjusted by the allocation to each Fund.  
Risk is measured as the standard deviation of monthly returns for the given time period.  
Past performance is no guarantee of future results.

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