Uncovering tactical opportunities across markets

BlackRock.

Elevated volatility and higher correlation between stocks and bonds have resulted in increased interest in diversifying investment strategies. We believe global macro strategies that invest across asset classes and geographies are well-suited to capitalize on opportunities in the current environment. Strategies with low correlations to stocks and bonds can also improve the consistency and overall results of portfolios. Tom Becker, portfolio manager of the BlackRock Tactical Opportunities Fund, tells us more.

Tom Becker, PhD
Portfolio manager,
Tactical Opportunities

What is the history of the Tactical Opportunities Fund?

Our team has managed global tactical asset allocation strategies for over 15 years, and we launched Tactical Opportunities strategy* in 2016. The portfolio contains all of our tactical global macro insights and has delivered consistent returns with limited correlation to traditional equity or fixed income markets. Today, we manage numerous types of absolute return strategies for institutional and retail clients around the world. The market backdrop and the need for diversifying strategies have created interest across a variety of asset owners.

Thinking broadly about the evolution of tactical asset allocation ("TAA") as an investment strategy, it originated in the 1980s with a focus on the single asset allocation decision of the day – whether to overweight or underweight equities or fixed income relative to the typical 60/40 allocation. It was very much about the market timing of cyclicality or defensiveness.

Today, our TAA approach is multidimensional and higher breadth. By higher breadth, I mean looking across numerous asset classes and geographies over multiple time horizons. We invest in the stock and bond markets of around two dozen countries. That diversified set of active exposures ultimately helps us deliver a more consistent and less correlated outcome for clients.

The fund is unique in that it uses both discretionary and systematic processes. Can you compare them?

Diversification is at the center of what we are trying to do in Tactical Opportunities. That includes diversification across asset class and geographic exposures, but also diversification across investment styles. While many managers implement either a discretionary or systematic process, we manage both as we believe each has the ability add value in complementary ways.

Both investment processes are data intensive. In both our systematic and discretionary processes, we use traditional macro data (e.g., GDP, inflation, and unemployment rates) and have increasingly incorporated more advanced data. Unstructured data is information that has not been organized in a pre-defined format; it includes text-heavy sources like central bank speeches or geospatial data like satellite imagery. We can form a more timely and nuanced view on growth, inflation, and policy around the world by using both structured *and* unstructured data.

> **"Diversification is at the center of what we are trying to do in Tactical Opportunities."**

*Strategy inception is July 1, 2016. Prior to that date, the fund followed different investment strategies under a different name..

Spotlight: Using big data to analyze central bank speeches

Our team built a data-driven tool to analyze central bank speeches to measure monetary policy stances around the world. We combine quantitative analysis of text via natural language processing with fundamental insights to interpret the data. This tool is powerful for comparing the direction and level of policy stance across countries.

Where our discretionary and systematic processes diverge is in the *way* we use the data to form portfolio positions. Our discretionary process is opportunistic and takes a smaller number of high conviction positions. We use human context to interpret data and identify macro themes we believe will be relevant for asset prices. This is especially important around discrete events like an election or in unprecedented situations like the COVID pandemic. For example, our decision to add equity risk in March 2020 was based on an observation that forced-selling by certain market participants had driven equity prices to lower levels than were justified by the macro outlook, even taking into account the massive pandemic-induced growth shock. This ultimately played out as markets began to recover into the end of the month.

The systematic investment process is rules-based and more continuous. The portfolio holdings gradually evolve as data updates across the globe. Strengths of this process include breadth and the ability to identify numerous opportunities across multiple markets. For example, our Sovereign Bond Relative Value strategy changes positions based on shifts in growth, inflation, policy and pricing data across developed bond markets. It takes long positions in countries with falling inflation and dovish central banks and short positions in countries with higher inflation and more hawkishness.

Managing both a discretionary and systematic investment process on-team improves our awareness of their relative strengths and blind spots. Another advantage is that our team investment discussions span a more expansive set of investment ideas. I think it is a really healthy way to approach investing – to have conversations with different starting perspectives and a healthy amount of skepticism.

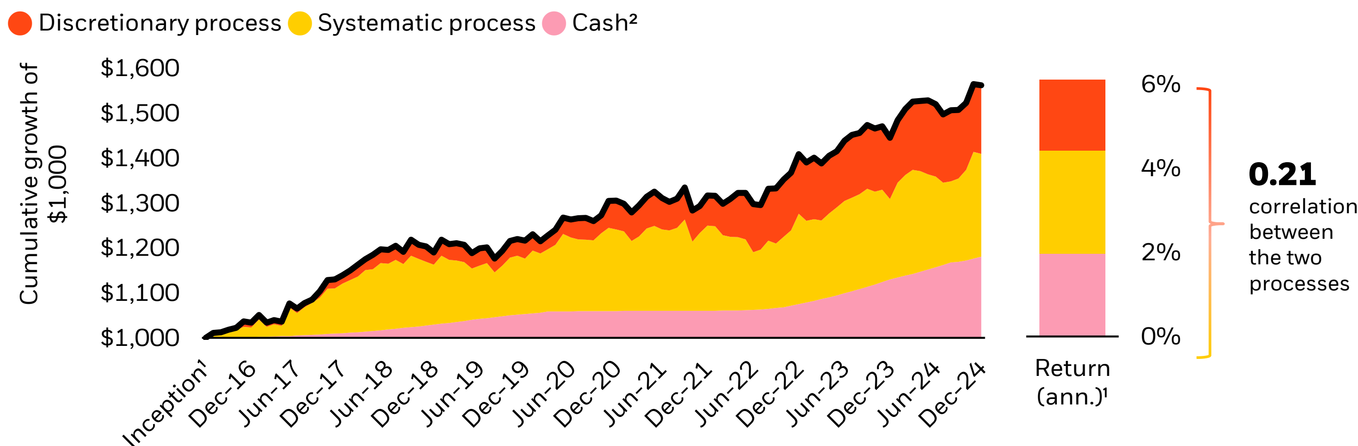
Our portfolio construction process seeks to balance active risk across discretionary and systematic such that each contributes meaningfully to the portfolio.

Spotlight: Exploring the impact of environmental shocks

We collaborate with colleagues from BlackRock's Systematic Active Equity team to **use large sets of data** from NASA and FEMA to geolocate **natural disasters** and identify macro investment opportunities globally. We have found that that asset returns respond to physical climate events in multiple ways. For example, natural disasters cause unanticipated shifts in economic activity, both from the initial disruption and subsequent reconstruction. Similarly, extreme temperature events shift economic activity at the country-level in an often-underappreciated manner.

Two proven and complementary processes

Quarterly return contribution by investment process since strategy inception[1]



Past performance is no guarantee of future results. All fund performance and data based on Institutional shares, other share classes will vary. Performance data quoted represents past performance and does not guarantee future results. The investment return and principal value of an investment will fluctuate so that an investor's shares, when redeemed, may be worth more or less than their original cost. Current performance may be lower or higher than the performance data quoted. All returns assume reinvestment of all dividend and capital gains distributions. Refer to website at blackrock.com to obtain performance data current to the most recent month-end. Source: BlackRock as of 31 December 2024. Attribution is estimated, unaudited, and gross of all fees and expenses, including management fees. 1 Tactical Opportunities' strategy incepted 01 July 2016. 2 The Fund earns a return on cash in addition to alpha from discretionary and systematic investments. Cash reflects returns to physical cash as proxied by the ICE BofA 3 Month Treasury Bill Index.

What market environments do you expect the fund to perform well or poorly in?

We invest globally and a large share of the portfolio is in relative value, cross-country positions. That means that dispersion of macro data and policy regimes across countries creates more opportunities for us. In 2022, for example, dispersion in growth and inflation across countries led to different policy responses and market returns. As one example, higher inflation in the US led the Federal Reserve to raise rates while falling inflation in China allowed the People's Bank of China to loosen monetary policy. Even as both global stocks and bonds sold off, we were able to generate positive returns by identifying and positioning for a number of cross-country divergences.

On the other hand, market environments like 2021 tend to be challenging. Central banks maintained ultra-accommodative policy despite rapidly increasing inflation and strong growth. This meant that asset prices did not respond to macro data as they typically would, and also resulted in low dispersion across countries.

I would also point out the fund's low beta to traditional equity and bond markets – which is by design – means that Tactical Opportunities may not keep up in periods when directional stocks and bonds are roaring. On the flip side, we would expect the fund to differentiate itself during periods of market stress.

The design of the product can help it to be a diversifier when incorporated alongside equity and bond allocations within a portfolio.

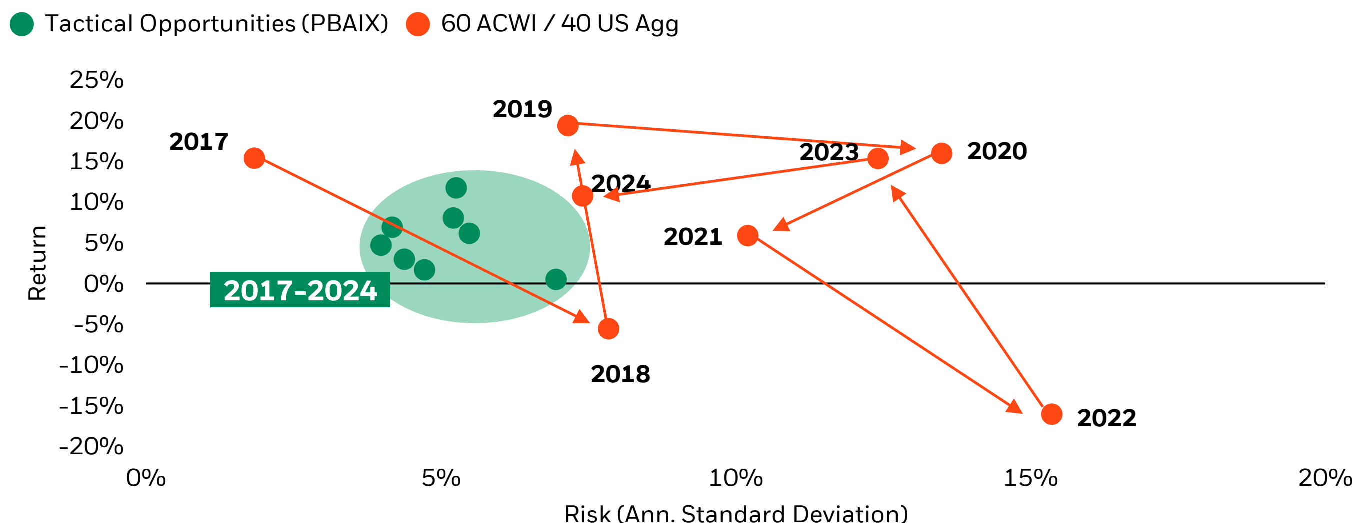
As we look ahead, we believe we have entered a market regime that is likely to be characterized by higher volatility, greater country dispersion, and less negative stock-bond correlations. A more dynamic approach in portfolios can capitalize on potential alpha opportunities across countries.

Your opportunity set consists of global equities, bonds, and currencies. Why these asset classes?

These three asset classes are most sensitive to our insights on growth, inflation, and policy. Equities react to corporate earnings growth while bonds are sensitive to inflation and monetary policy shifts. Exchange rates are also sensitive to changes in policy as well as relative economic competitiveness. Pricing across asset classes varies through time, so we benefit from the flexibility to express views in different asset classes depending on the degree of mispricing.

Sometimes we're asked why we don't venture into more specialist asset classes like commodities or volatility. We believe these asset classes, while having a role in diversified portfolios, possess idiosyncrasies that are not conducive to our more top-down, macro

The fund has delivered more consistent risk and return outcomes
Calendar year returns and risk, 2017-2024



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approach. For example, while we often use commodity prices to inform our macro views, we choose not to invest directly because commodity prices are often influenced by bottom-up supply dynamics. Volatility is a derivative asset of equity markets. We prefer to get exposure directly through equity indices for two primary reasons: Direct exposures are cheaper to transact and, second, volatility has an undesirable "up the stairs and down the elevator" return profile.

What role does Tactical Opportunities play in a holistic client portfolio?

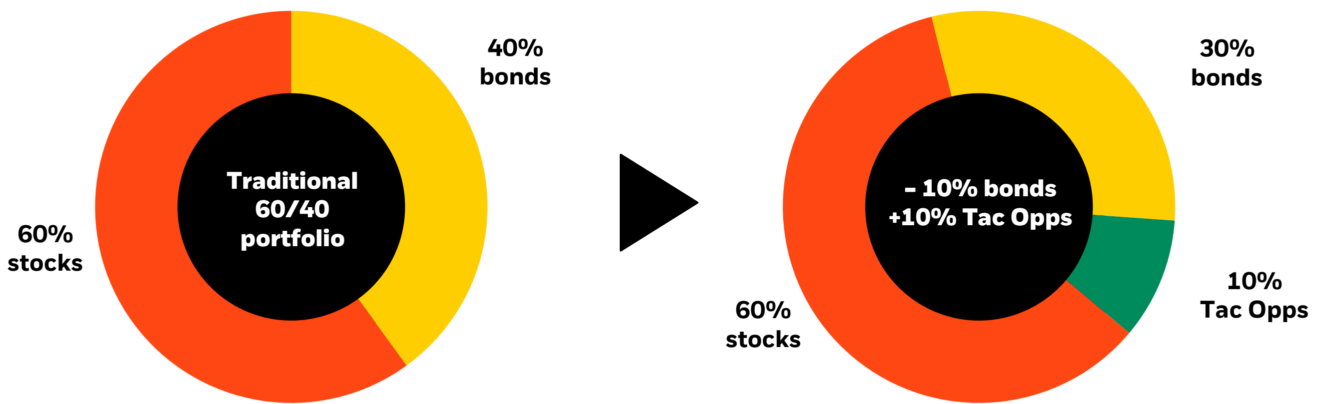
Investors considering allocating to alternatives in their portfolios need to start by identifying how it can help to achieve the overall outcome they are seeking. BlackRock focuses on four outcomes that alternative investments can help to achieve: hedge, diversify, modify, or amplify. Within this framework, Tactical Opportunities fits squarely within the "diversify" objective. The fund's record of delivering low correlation to traditional asset classes means that its returns have helped to deliver more consistent overall portfolio outcomes.

An important decision that investors need to make when adding a strategy to their portfolio is the sourcing of the capital. The volatility profile of Tactical Opportunities means that many clients fund allocations from fixed income. However, we have seen some clients source capital from a combination of equities and fixed income if they are looking to reduce the overall risk of their portfolio.

Spotlight: Portfolio in practice

Michael Gates, Head of BlackRock's Model Portfolio Solutions team, has advocated **using alternatives** in client portfolios. Given increased stock/bond correlations, he deliberately sources allocations to diversifying alternatives from fixed income in an effort to provide greater return potential and more consistent outcomes. His team considers an expansive universe of BlackRock and third-party managers and currently diversifies the alternatives exposure in their model portfolios across four funds, including Tactical Opportunities.

Adding Tactical Opportunities to a hypothetical stock-bond portfolio would have resulted in superior risk/return[1]



	60% stocks / 40% bonds	60% stocks / 30% bonds / 10% Tac Opps	
Ann. return	9.3%	9.8%	✔ Higher return
Ann. std. dev.	10.5%	10.2%	✔ Similar risk
Sharpe ratio	0.73	0.79	✔ Higher Sharpe

Past performance is no guarantee of future results. Investment return and principal value will fluctuate with market conditions and may be lower or higher when you sell your shares. Current performance may differ from the performance shown. For most recent month-end performance see blackrock.com. For standardized performance, see the end of this document. Source: Morningstar Direct, BlackRock as of 31 December 2024. Risk, as measured by standard deviation, and return calculated since Tactical Opportunities strategy inception of 01 July 2016. Hypothetical 60/40 portfolio comprised of 60% iShares Core S&P 500 ETF (IVV) and 40% iShares Core US Aggregate Bond ETF (AGG). Sharpe ratios assume risk free rate of cash, as represented by ICE BofA 3-Month Treasury Bill Index. 1 Tactical Opportunities represented by the fund's institutional share class (PBAIX) since strategy inception of 01 July 2016. Different share classes may have different results. Institutional shares are not available to all investors. Performance, fees and rankings for other share classes could be higher or lower.

Annualized total returns (%) as of 31 December 2024	1 year	3 years	5 years	10 years
Tactical Opportunities PBAIX	11.74	6.89	5.58	4.16
ICE BofA 3-Month Treasury Bill Index	5.30	3.96	2.48	1.75

Annualized total returns (%) as of 31 December 2024	1 year	3 years	5 years	10 years
iShares Core S&P 500 ETF IVV	24.98	8.91	14.49	13.06
iShares Core U.S. Aggregate Bond ETF AGG	1.37	-2.37	-0.34	1.31

Annualized market price (%) as of 31 December 2024	1 year	3 years	5 years	10 years
iShares Core S&P 500 ETF IVV	24.94	8.91	14.51	13.06
iShares Core U.S. Aggregate Bond ETF AGG	1.31	-2.36	-0.35	1.29

Performance data quoted represents past performance and does not guarantee future results. The investment return and principal value of an investment will fluctuate so that an investor's shares, when redeemed, may be worth more or less than their original cost. Current performance may be lower or higher than the performance data quoted. All returns assume reinvestment of all dividend and capital gains distributions. Refer to website at blackrock.com to obtain performance data current to the most recent month-end. Gross expenses for Institutional shares: 0.82%. Investment-related expenses include acquired fund fees of 0.00%, interest expense (cost of borrowing securities to seek to enhance return or reduce risk) of 0.00%, and certain other expenses, if applicable. Expenses stated as of the fund's most recent prospectus. The fund's returns prior to 1 July 2016 are the returns of the fund when it followed different investment strategies to invest a significant portion of its assets in other investment companies and directly in securities. Expense ratio for iShares Core S&P 500 ETF (IVV): 0.03% and iShares Core U.S. Aggregate Bond Index (AGG): 0.03%.

Shares of ETFs are bought and sold at market price (not NAV) and are not individually redeemed from the fund. Any applicable brokerage commissions will reduce returns. Beginning August 10, 2020, market price returns for BlackRock and iShares ETFs are calculated using the closing price and account for distributions from the fund. Prior to August 10, 2020, market price returns for BlackRock and iShares ETFs were calculated using the midpoint price and accounted for distributions from the fund. The midpoint is the average of the bid/ask prices at 4:00 PM ET (when NAV is normally determined for most ETFs). The returns shown do not represent the returns you would receive if you traded shares at other times.

Visit blackrock.com, iShares.com or contact your financial professional for a prospectus or summary prospectus, which includes investment objectives, risks, fees, charges, expenses and other information that you should read and consider carefully before investing. Investing involves risk, including possible loss of principal. Consult with your financial professional for additional information.

Important risks: *The fund is actively managed and its characteristics will vary. Stock and bond values fluctuate in price so the value of your investment can go down depending on market conditions. Investing in small-cap companies may entail greater risk than large-cap companies, due to shorter operating histories, less seasoned management or lower trading volumes. Investing in mid-cap companies may entail greater risk than large-cap companies, due to shorter operating histories, less seasoned management or lower trading volumes. Fixed income risks include interest-rate and credit risk. Typically, when interest rates rise, there is a corresponding decline in bond values. Credit risk refers to the possibility that the bond issuer will not be able to make principal and interest payments. International investing involves special risks including, but not limited to political risks, currency fluctuations, illiquidity and volatility. These risks may be heightened for investments in emerging markets. Asset allocation strategies do not assure profit and do not protect against loss. The fund may use derivatives to hedge its investments or to seek to enhance returns. Derivatives entail risks relating to liquidity, leverage and credit that may reduce returns and increase volatility.*

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Glossary: Alternative investment strategies include those that invest in private assets such as private equity, private credit, infrastructure and real estate as well as funds that use less traditional tools such as short-selling and leverage to deliver investment results. **Standard deviation** measures the volatility of returns. Higher standard deviation represents higher volatility. **Beta** is a measure of volatility in relation to the overall market. Beta greater than 1.0 indicates greater moves than the broad market. **Correlation** measures the degree to which two variables move in relation to each other. If the two variables move in the same direction, then those variables are said to have a positive correlation. If they move in opposite directions, then they have a negative correlation. **Sharpe ratio** is a measure of risk-adjusted return. It describes how much excess return you receive for the volatility of holding a riskier asset. **Discretionary** is an investment approach that takes positions based on portfolio manager assessment of information. **Systematic** is an investment approach that takes positions based on pre-established rules. **Long/short** is an investing strategy that takes long positions in securities that are expected to perform more strongly and short positions in securities that are expected to perform less strongly. This strategy seeks to generate returns while minimizing market exposure.

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