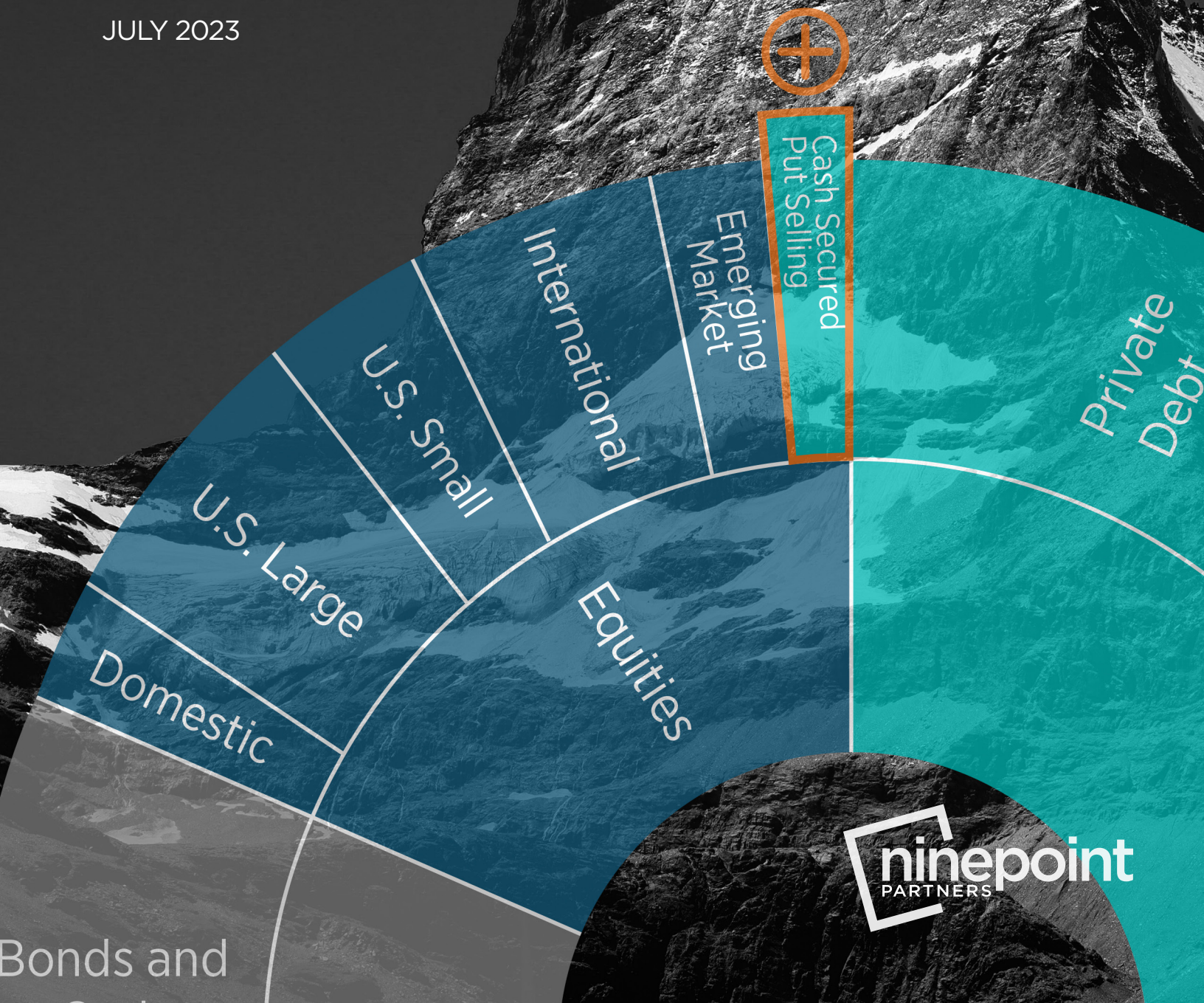


# CASH SECURED PUT SELLING

CASE STUDY

JULY 2023



## Ninepoint Partners: Case Study

Traditional income generating portfolios tend to rely on higher dividend yielding equities, longer maturing fixed income instruments, or a combination of, to produce returns. In 2022, with the rise in long-term interest rates, equity market drawdowns, and the corresponding increase in correlation between stock and bonds, this approach has produced higher volatility and lower returns than expected.

A cash secured put selling strategy can offer an alternative source of income generation for portfolios, with potentially lower downside exposure than traditional equity allocations, by generating income through a combination of options premiums and short-maturity money market instruments.

To illustrate, a potential historical portfolio was constructed using the benefits of a cash-secured equity put selling strategy on the S&P 500, combined with a traditional income focused balanced allocation. We find that over the period examined, risk-adjusted returns are improved when the put selling strategy is substituted for the equity exposure. We also find that standalone downside capture of the put selling strategy is lower than both the equity and balanced portfolio in most of the highlighted periods of market declines.

**How it works:** A cash secured put selling strategy generates income through a combination of premiums collected from selling put options, and reinvesting the cash held as collateral in short-term money market securities. The put selling index referenced within the constructed portfolio, systematically sells 1 year expiry 10% out-the-money put options laddered quarterly, on the S&P 500 underlying. This provides rolling downside protection of -10% before options premiums and investment principal are put at risk contributing to the defensive properties of the strategy.

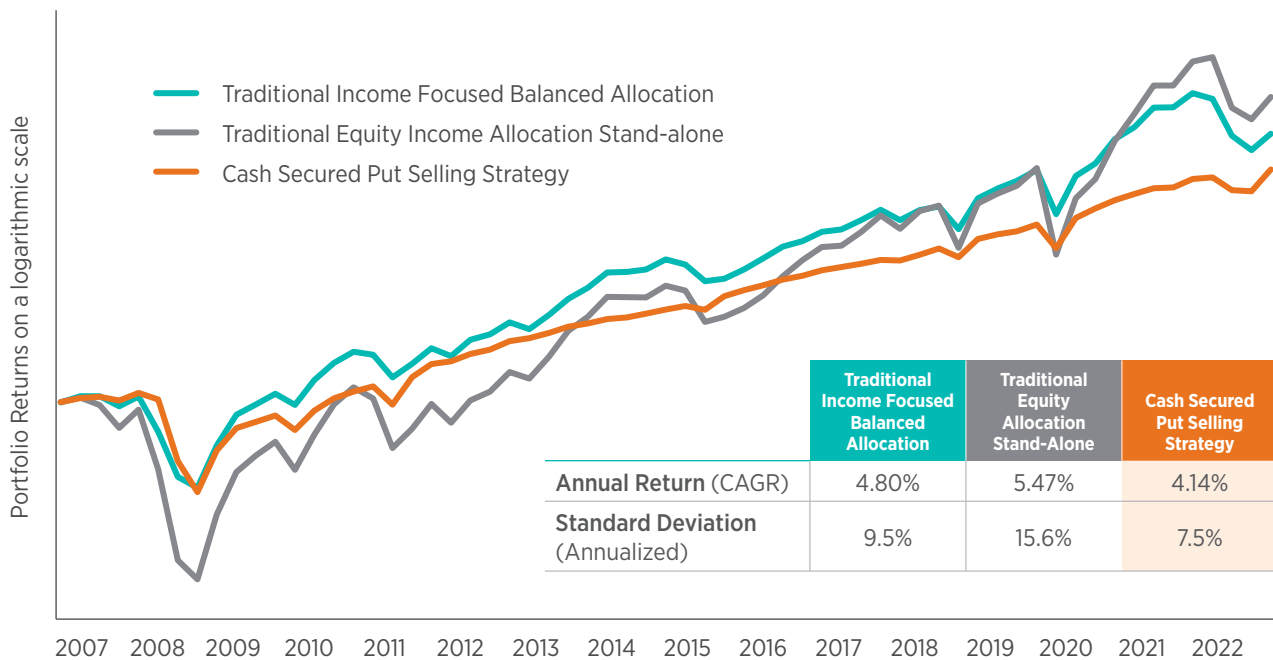
## What are the risks of investing in a traditional income focused balanced allocation?

- Fixed income portfolios may fail to provide sufficient diversification to a portfolio in stressed market environments.
- Investors must take on the higher volatility of equities and longer maturity bonds to generate the desired income through dividends payments and coupons.
- Inflationary periods can drive poor performance for both stock & traditional bond portfolios.

## How does a cash secured put selling strategy help manage those risks?

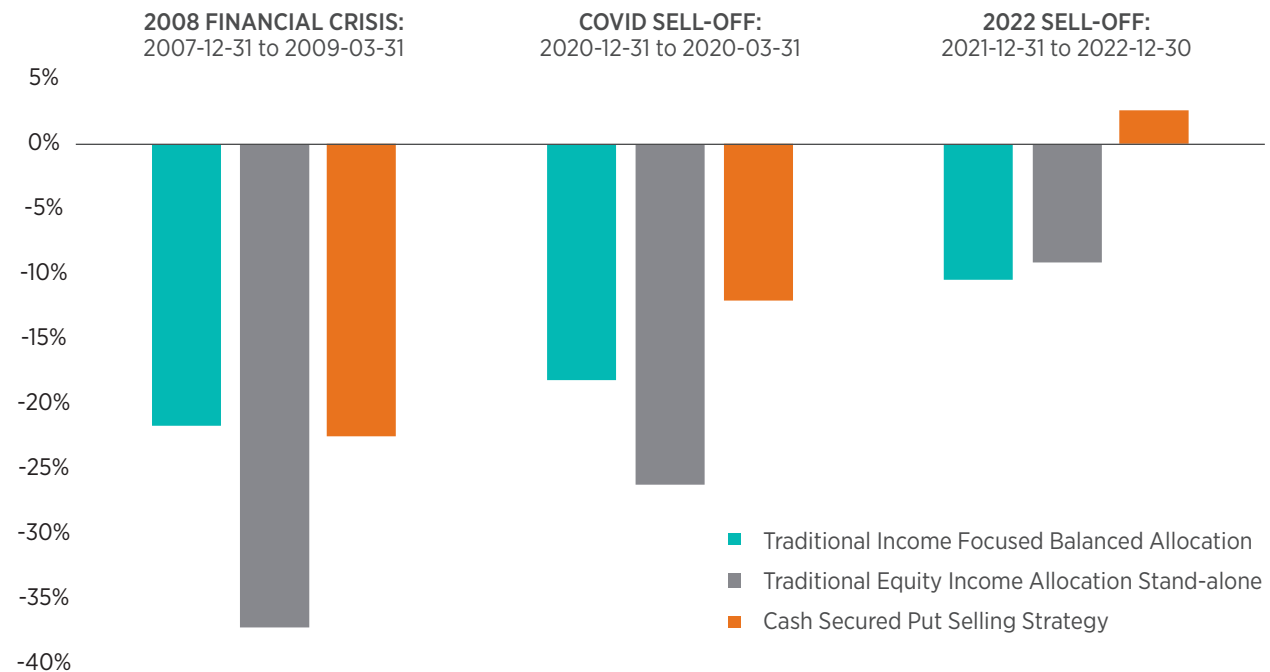
- Improved diversification when undesirable correlation between stocks and bonds occurs.
- Differentiated income stream through harnessing the volatility risk premium inherent in options.
- Higher potential for positive risk adjusted returns in periods of poor risk asset performance.

## Portfolio Returns



For illustrative purposes only and is not indicative of future performance. Subject to change without notice.

## Downside Performance Scenarios



Income Focused Balanced Allocation: 6% SPTSX High Dividend Index (TXEITR), 30% TSX Composite (0000AR), 24% MSCI ACWI Local Currency Equity Index (NDLEACWF), 39% Bloomberg Barclays US Aggregate Bond Index CAD Hedged (LBUSTRDH), 1% FTSE Canadian 1 month Treasury Index (SPFICTBT).

Equity Stand Alone Allocation: 10% SPTSX High Dividend Index (TXEITR), 50% TSX Composite (0000AR), 40% MSCI ACWI Local Currency Equity Index (NDLEACWF).

Cash Secured Put Selling Strategy: RBC US 90 Strike Put Selling Strategy (RBCUS90P) quarterly return + Canada Bankers Acceptance 1M Maturity Index (CDOR01) beginning quarterly yield calculated as a total return.

All strategies are rebalanced to the specified allocations on a quarterly basis with graphs and charts depicting quarterly timeseries.

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	Income Focused Balanced Allocation <sup>1</sup>	Adding Cash Secured Put Selling Strategy			
		10%	20%	30%	40%
Sharpe Ratio <sup>2</sup>	0.38	0.40	0.42	0.45	0.48
Annualized Return (CAGR)	4.8%	4.6%	4.5%	4.3%	4.1%
Standard Deviation (Annualized)	9.5%	8.6%	7.7%	6.9%	6.1%
<b>Allocation</b>					
Cash	1%	1%	1%	1%	1%
Equities	60%	50%	40%	30%	20%
Fixed Income	39%	39%	39%	39%	39%
Cash Secured Put Selling Strategy <sup>3</sup>	0%	10%	20%	30%	40%

Source: Bloomberg and Ninepoint calculations, quarterly rebalancing using quarterly return data 2007-06-29 to 2022-12-21  
All strategies are rebalanced to the specified allocations on a quarterly basis with graphs and charts depicting quarterly timeseries.

<sup>1</sup> Balanced Allocation: 6% SPTSX High Dividend Index (TXEITR), 30% TSX Composite (0000AR), 24% MSCI ACWI Local Currency Equity Index (NDLEACWF), 39% Bloomberg Barclays US Aggregate Bond Index CAD Hedged (LBUSTRDH), 1% FTSE Canadian 1 month Treasury Index (SPFICTBT)

<sup>2</sup> Sharpe Ratio: Annualized Total Return of allocation minus annualized return of FTSE Canada 1 month Treasury Index divided by standard deviation

<sup>3</sup> Cash Secured Put Selling Strategy: RBC US 90 Strike Put Selling Strategy (RBCUS90P) quarterly return + Canada Bankers Acceptance 1M Maturity Index (CDOR01) beginning quarterly yield calculated as a total return.

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## RISKS

Put selling strategies may experience gains and losses in value as markets fluctuate. As the underlying asset price approaches the strike price of the put option, the magnitude of the gain/loss can increase. A cash secured put seller faces the risk of losing both the initial investment and put option premium should the underlying asset price trade below the strike price. Losses increase as the underlying asset price declines further below the option strike price. Money market securities held within the portfolio bear fixed income investment risk and can experience losses independent of the options portfolio. Put selling strategies may bear increased counterparty risk if executed outside of a centrally cleared exchange.

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