

31 October 2022

Market review

October proved to be a stronger month for financial assets, with the major equity indices posting significant gains. This was driven by speculation that central banks may begin to slow the pace of rate hikes, European natural gas prices may decline further and the UK's market turmoil may stabilise after Rishi Sunak's appointment as prime minister.

The narrative that the US Federal Reserve (Fed) and other central banks may pivot on monetary policy was supported by the Reserve Bank of Australia and the Bank of Canada hiking interest rates by less than anticipated. An article by Nick Timiraos in the Wall Street Journal suggested that the Fed will hike by 75 basis points (bps) in November but will entertain a smaller increase in December. A European Central Bank (ECB) conference also contained a number of more supportive elements. However, economic data continued to undermine this narrative, with US headline inflation at 8.2% and Eurozone headline inflation hitting a record high at 10.7%.

In Europe, the ECB delivered a 75 bps hike in October, with markets pricing in a 63 bps hike at the next meeting in December, indicating that market opinion is split between a 50 bps and 75 bps hike. Natural gas futures ended the month down 34.7%, as prices were pushed lower due to the unusually warm weather across Europe, enabling storage facilities to remain full.

In the UK, the market turmoil stabilised after the Government reversed the majority of their mini-Budget, which outlined the biggest programme of tax cuts for the UK since 1972. Political pressure pushed now-former Prime Minister Liz Truss to resign, with former Chancellor Rishi Sunak appointed as prime minister.

Performance

The abrdn Global Absolute Return Strategies Fund returned -1.50% during the month (net of fees). The benchmark Bloomberg AusBond Bank Bill Index returned 0.24% during this period.

The Fund's positioning reflects what we see as a challenging period ahead for markets. At present, the rhetoric around inflation and central bank tightening is dominating market dynamics. This is a theme we expect to evolve as the focus moves to the consequence of weaker growth. Against this backdrop, we have positioned the Fund to take advantage of tightening financial conditions into slower growth via defensive positions in relative-value strategies and a bias towards short corporate-risk positions. In addition, we maintain longs in the US dollar and developed-market government bonds.

Our ASEAN versus North Asia foreign-exchange strategy was the top performer this month, driven by strength in the Singapore dollar due to intervention from the Monetary Authority of Singapore while growth and political concerns weighed on China. The UK versus emerging-market-equity relative-value strategy contributed positively, as a more supportive market interpretation of central bank tightening and some stabilisation in UK politics helped the UK equity market relative to emerging-market equities. While sterling remained weak against historic levels, the reversal of the majority of the UK government's mini-Budget benefitted the pound; as a result, our short sterling foreign-exchange strategy contributed negatively this month. Furthermore, our short equity relative-value strategies, including our long US investment-grade corporate-bond versus short equity strategy and our US equity low-volatility versus US equity strategy were negatively affected by the strong equity performance on the back of speculation that the Fed may start to pivot. Our global equity zero hunger basket benefitted from this strength in equities and contributed positively as a result.

Activity

At the start of October, we reduced our short US equity and short high-yield corporate-bond positions after the drivers played out in September, providing an opportunity to reduce the level of risk deployed. During the month, we exited our UK versus emerging-market-equity

Investment strategy

The Fund will invest in the Underlying Fund and may hold up to 5% of its assets in cash.

The Underlying Fund aims to deliver a return of ESTR plus 5% per annum, before charges, over rolling three-year periods.

The investment team who actively manage the Underlying Fund have a wide investment remit to help them try to achieve this aim. The team look to exploit market inefficiencies through active allocation to a diverse range of market positions.

The Underlying Fund utilises a combination of traditional assets (such as equities, bonds, cash and money market instruments) and investment strategies based on advanced derivative techniques resulting in a highly diversified portfolio.

The Underlying Fund can take long and short positions in markets, securities and groups of securities through derivative contracts.

Investment objective

The primary investment objective of the Fund is to deliver a positive absolute return over the medium to long term in all market conditions.

The Underlying Fund is actively managed, with a wide investment remit to target a level of return over rolling three-year periods equivalent to cash* plus 5% per year, before charges. We would expect it to exhibit annualised volatility** of between 4% and 8% in ordinary market conditions or, more broadly, between one-third and a half of the risk of global equities***.

*Cash returns are currently referenced to ESTR (which has been chosen as a proxy for the return on cash deposits), however the reference index may change over time. Performance of the Australian dollar hedged share class will instead be compared with the Bloomberg AusBond Bank Bill Index.

** Measured over 3 years of monthly returns.

*** The investment objective is expressed before the deduction of management fees, expense recoveries and taxation

relative-value position, as the strategy reached our return target. We reduced our US investment-grade corporate-bond allocation within the US investment-grade versus equity position following strong performance driven by the central bank pivot narrative. We exited our European real-yields position, as European inflation continued to surprise to the upside, and our Asia high-yield position, as tight monetary policy negatively affected the strategy. We increased our long favoured defensive foreign-exchange position, as we expect it to perform well in a risk-off environment.

Outlook

The Fund is positioned to perform well in a scenario where monetary tightening leads to a recession (with both growth and inflation declining) while also delivering positive returns under a continuation of the environment observed since the start of 2022 (with inflation elevated).

Fund performance is available on the relevant factsheet.

The opinions expressed are those of abrdn as of the date of publication and are subject to change at any time due to changes in market or economic conditions.

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