

30 November 2022

Market review

November was a strong month for risk assets, with gains across equities, corporate bonds, sovereign bonds and commodities. The continued rally in risk assets was driven by lower-than-expected US and European inflation data.

The US Federal Reserve (Fed) hiked interest rates early in the month by 75 basis points (bps) bringing the federal funds rate to 4%. US October consumer price index (CPI) readings for both headline and core inflation came in lower than expected, although services (particularly shelter) remained an area of concern. Given this data and the most recent speech from the Fed's Chair Jerome Powell, the market now expects the pace of interest-rate hikes to moderate, with general market consensus pointing to a 50 bps Fed hike in December. However, Powell reiterated that the path of interest rates will continue to be data-dependent. Powell's speech led to a continued rally in US risk assets, with the S&P 500 posting gains of over 14% in two months. For investors, a key debate is how long this bear-market rally can be sustained.

In Europe, the CPI fell more than expected to 10%. In the UK, gilts continued to outperform as the turmoil from the previous mini-Budget announcement unravelled. Markets were fairly muted on the UK's Autumn statement, which included fiscal tightening measures aimed at reassuring investors of the UK Government's fiscal credibility.

During the month, China moved to reopen its economy through vaccine acceleration, particularly for the elderly. More provinces and cities also announced measures such as stopping mass testing and allowing home quarantine. The news was taken very positively by markets, with the Hang Seng Index up +27% and the Shanghai Composite Index up +9% in November.

Given the risk-on environment, the US dollar suffered losses for its second consecutive month and weakened against every other G10 currency. We also saw oil move lower given varied OPEC+ headlines. OPEC+ has

since decided to keep production at current levels. This follows the EU decision on Friday, after months of negotiations, to cap the price of Russian crude at \$60 per barrel.

Performance

The abrdn Global Absolute Return Strategies Fund returned -1.48% during the month (net of fees).

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, although we reduced this position in November, and long positions in developed-market government bonds.

Our ASEAN versus North Asia foreign-exchange strategy was the top performer this month. It was driven by strength in the Singapore dollar due to intervention from the Monetary Authority of Singapore and China's drive for economic equality and domestic security. Our long corporate-risk positions in global equity stable quality versus the market and contingent capital bonds performed well this month given the risk-on environment, as inflation momentum slowed and there was more supportive messaging from the Fed. The commodity carry strategy was also a top performer during the month, and we have recently taken profits from this strategy. Following the risk-on theme, our short corporate-risk trades were the biggest detractors this month, including short European equity, US equity low volatility versus US equity and short high yield. Similarly, our long favoured defensive foreign-exchange strategy underperformed due to the continued weakness in the US dollar. We have now slightly reduced our overall Fund exposure to the US dollar.

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

Activity

During November, we added a new position in US versus Italian rates. We added this position as we believe the spread has narrowed disproportionately when compared to corporate-bond spreads and the moves in equity markets, and we think this is unjustified. During the month, we exited our commodity carry trade following its positive performance, as we believe there is increased vulnerability and potential for losses with China reopening, winter weather in the coming months and US reserves post-midterms. We have also altered our foreign-exchange positions. We added long euro to our short sterling strategy with the aim of reducing our US dollar sensitivity and reducing the overall cyclical exposure of the trade. Lastly, we marginally reduced our short US equity position in order to move to a less short corporate-risk position and to take profit.

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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