Aberdeen Standard Global Absolute Return Strategies Fund

31 January 2022

Market review

January was a volatile month for financial markets. Although fears over the Omicron variant of Covid-19 receded, jitters around the less supportive shift from several central banks and geopolitical tensions between Russia and Ukraine intensified the market downturn. Risk assets retreated in the face of central banks tightening monetary policy more aggressively than earlier expectations, particularly the Federal Reserve (Fed) amid its efforts to tackle inflationary pressures.

Global equities delivered the worst performance since the initial height of the Covid-19 pandemic, accompanied by a dramatic rotation from growth to value as investors questioned the sustainability of some share price valuations. In commodities, tension over the Ukrainian-Russian border and the perceived risk of conflict supported oil prices, with both West Texas Intermediate and Brent crude delivering solid returns.

Developed market sovereign bonds stumbled as statements from central banks emboldened expectations of interest rate rises. Shorter-term interest rates increased significantly relative to longer-term rates. The UK's higher-than-expected inflation print also put upward pressure on yields. Corporate bonds also fell as risk sentiment soured.

Elsewhere, the US dollar advanced against developed market peers but lost ground against some emerging market currencies.

Performance

The Aberdeen Standard Global Absolute Return Strategies Fund returned -2.55% during the month (net of fees). The benchmark Bloomberg AusBond Bank Bill Index returned 0.01% during this period.

The Fund positioning has been based on the expectation that growth and inflation will remain strong as we move through the first half of 2022, prompting central banks to tighten policy. In this environment, we have been focused on owning higher-yielding assets across equities, bonds, currencies and volatility strategies.

Our global equity volatility risk premia and emerging markets income strategies produced positive performance, with the latter also helped by emerging market currencies appreciating against the US dollar. However, that was not enough to offset negative performance from our risk-facing exposures, such as our equity and high yield-related positions.

Elsewhere, our commodity carry strategy also lost ground amid the surge in the oil price caused by fears over oil supply if Russia invades Ukraine. This loss was only partially offset by positive performance from our favoured defensive foreign exchange strategy.

Activity

We adjusted portfolio exposures given the less supportive rhetoric coming from central banks. At the beginning of the period, we switched our European yield curve steepener position into a US flattener versus European steepener. This reflects our view that the prospect of higher interest rates in the US will reduce the difference between long and short-term interest rates there relative to the Eurozone. We closed the European yield-curve steepener towards the end of the month but retained our exposure to the US market where we have greater conviction. We also closed our US dollar versus euro pair given the significant interest rates hikes already priced into the US market. Near the end of the period, we closed our short UK inflation strategy amid lower conviction in the underlying drivers and reduced our European inflation position given the growing risk of monetary tightening in Europe. Similarly, we also closed our US inflation strategy.

Outlook

We remain guided by the conviction that growth continues to be strong and inflation runs above central bank targets. In this environment, we expect positive returns from risk assets, like equities and bonds. Gradual removal of policy accommodation will create an opportunity to generate returns from a variety of sources.

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

Beyond our central case, we also consider the possibility and asset implications for a variety of alternative scenarios. In one of the upside cases, the US Federal Reserve could tolerate higher inflation than expected, pushing real interest rates lower and supporting cyclical stocks. Alternatively, in a downside scenario, central banks (the Fed in particular) could start removing stimulus earlier than expected, delivering a shock to markets and sending equities lower.

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