

Aberdeen Standard Multi-Asset Real Return Fund



31 December 2021

Market review

Equities rallied strongly in December and outperformed bonds, as investor fears around the Omicron variant receded. Markets brushed off worries about a return of restrictions and increasing inflation pressures, helping the US, UK and Europe to post solid gains. Meanwhile, major central banks acted to control inflation by reducing policy support, which tempered the performance of fixed income.

Most global stock markets rebounded in December after the discovery and spread of the Omicron variant in late November sparked market falls. The highly transmissible variant spread globally during the month, with record daily infections in the US and numerous European countries. While Governments have taken differing approaches to control the spread, with some reinstating travel bans and social restrictions, the UK Government resisted calls to lock down England before Christmas. Both European and UK equities advanced strongly, while the US rose slightly below the global average, although major US indices hit record highs late in the month, boosted by retailers. Developed stocks in the Asia Pacific region rose but generally less than their global peers. Although Covid-19 concerns weighed on markets, sentiment was later boosted as initial data indicated a less severe illness. Moreover, by the end of the month, South Africa relaxed its curfew, stating the fourth wave may have already passed. Australian equities finished the year on a high, breaking their three-month downward trend and finishing with a positive month. Concerns over Omicron and a change in rhetoric from the US Federal Reserve (Fed) regarding inflation worried investors early on. However, these concerns abated over the month, as hospitalisations remained low and markets appeared to suggest that inflation could be controlled without significant rate hikes. In Japan, the Government announced the 2022 fiscal year annual budget, which was the largest yet at ¥107.6 trillion, and included social spending for the elderly and record defence spending. Elsewhere, emerging market returns were more mixed, with China one of

the weakest countries.

In fixed income, the Bank of England hiked interest rates to 0.25% at its December meeting, while the Fed and European Central Bank announced plans to taper their support programmes in an attempt to control rising prices. Policymakers at the Fed also indicated that rates may rise three times in 2022. UK, US and European government bonds fell in December. Elsewhere, global investment-grade corporate bonds fell marginally, while emerging market debt rose. In Asia, the Bank of Japan held interest rates but announced plans to begin tapering its market support. However, Governor Kuroda stated that the central bank would lag its contemporaries in normalising policy. The Reserve Bank of Australia decided to keep rates at 0.1% and maintain the rate of bond purchases until at least February 2022. Meanwhile, Chinese government bonds continued outperforming. Shorter-dated bond yields fell sharply, in line with the People's Bank of China's more supportive inclination of late regarding the slowing economy and beleaguered property sector, including through the announcement of a reduction in the 1-year prime loan rate to 3.80% from 3.85% on 20 December.

Elsewhere, oil partially recovered from November's falls as concerns that the spread of Omicron would impact demand receded.

Portfolio review

In December, the Fund rose by 1.93% in gross terms and by 1.86% net of fees. The portfolio's exposure to fixed income, equities and infrastructure contributed. The Fund's spot exposures and options detracted slightly from returns. Over the year to date, the Fund remains up by 10.07% (gross of fees).

In view of potential volatility in equity markets, we continued to buy calls on the VIX Index, funded out of short S&P 500 Index (SPX) puts, to provide cost-efficient protection. We consider this a strategic, rather than tactical, move to hedge against a major sell-off in US stocks. In such a

Investment strategy

The Fund will apply dynamic asset allocation to a diversified portfolio of traditional and alternative assets, without reference to a benchmark. The Fund may shift its investments quickly and significantly, based on valuations and expected returns, and may completely divest from a particular asset class. Fund volatility will be controlled through the use of dynamic asset allocation and effective diversification of assets.

Investment objective

To achieve a real return equivalent to 5% per annum above inflation (before fees) over a full market cycle (generally 3 to 5 years).

situation, gains from the long VIX calls will more than offset losses from short SPX puts. The entry positions on both contracts are sized so that the net cost is close to zero.

Meanwhile, we added 2.5% to MSCI World Index futures, in light of the recent weakness in equities. As we have seen more data on Omicron, it is a variant with higher transmissibility but less severe symptoms, so we do not think it will derail the global recovery.

Outlook

Uncertainties remain on the new variant, central bank policy and inflation outlook. Omicron has caused cases to surge but the market impact has been somewhat muted, as infections have been milder than previous variants. The Fed announced at December's Federal Open Market Committee meeting that it would begin reducing asset purchases by US\$30 billion per month, up from the previously announced US\$15 billion. Meanwhile, projections showed three rate hikes in 2022 and another three hikes in 2023. The consumer price index (CPI) remains hot, and the Fed has removed the word "transitory" in reference to inflation. However, economists have observed some improving trends: despite the hotter CPI print, inflation is unlikely to remain at problematic levels, while expectations for high short-term inflation are likely to converge with lower long-term levels over time. Given these uncertainties are likely to persist over the coming months, we are closely monitoring portfolio beta and duration, but we believe the rising yield backdrop will ultimately benefit equities.

Fund performance is available on the relevant factsheet.

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