abrdn Multi-Asset Real Return Fund

31 July 2023

Market review

Australian equity markets advanced in July, with the S&P ASX 200 Net Total Return Index returning 2.89% (in Australian dollars, AUD), while the MSCI World (hedged to AUD) Index returned 2.84%. With the Australian dollar appreciating against the US dollar (USD) over the month, the MSCI World (unhedged) Index returned 2.53% in AUD.

Australian equities rose in July, driven by strength in the technology and energy sectors. However, there was a slight pullback towards the end of the month, as robust US economic data raised concerns about potential further policy tightening by the US Federal Reserve (Fed). The Reserve Bank of Australia (RBA) held its cash rate at 4.1% in July to evaluate the effects of previous rate increases. Despite a drop in Australia's inflation rate to 6% in the second quarter, it remained above the central bank's target range of 2-3%. Elsewhere, Australian retail sales fell by 0.8% in June.

In fixed income, the Australian 10-year government bond yield remained stable near 4%. Investors are now keeping an eye on the RBA's future interest rate decisions. Finally, July was a volatile month for the Australian dollar, which started the month slightly above the 0.66 level and approached 0.69 mid-month. Yet, the AUD depreciated in the second half of July and ended the month above 0.67.

US equities rose in July, as results from the second-quarter earnings season have generally been positive. The NASDAQ Composite Index continued its advance, outperforming the broader S&P 500 index. European shares also performed well. In the UK, mid and small-cap FTSE 250 Index outperformed the blue-chip FTSE 100 Index. Developed Asia Pacific markets mostly rose. However, Japan was flat. Emerging markets were also strong in July, with rises in India, China and Latin America.

In global fixed income, sovereign bonds mostly fell, although corporate bonds performed better over the month. Both the Fed and the European Central Bank raised rates by 25 basis points (bps). European and US Treasury yields rose, while in the UK, Gilt yields fell.

Performance

In July, the Fund returned 1.66% in gross terms and 1.58% net of fees.

Most asset classes posted positive returns with the bulk of the contribution coming from equities and alternatives exposures over the month. Our fixed income duration exposures, on the other hand, detracted slightly on the back of higher yields.

Activity

In July, we increased global equities exposures toward the new Strategic Asset Allocation (SAA) target, funded out of cash. We also added to our USD exposures against AUD given the more dovish RBA vs Fed positioning, and indirectly reduced China risk associated with the Australian dollar. Lastly, with the US market looking stretched, we rolled the existing SPX Put spread and bought VIX call to protect the portfolio from a near term technical pull back.

Outlook & strategy

With the resolution of US debt ceiling, market focus has shifted towards pricing growth and inflation dynamics, central bank policies, and market liquidity. The resilience of US economic activity reduces the risks of an imminent recession. Despite the weakening manufacturing sector, the service sector is still expanding. Core service inflation remains sticky, and the labour market continues to surprise to the upside. Against this backdrop, in July the Fed raised rates by 25bps, as expected. The Fed also stressed that further hikes would be dependent on economic data.

In Asia, we expect strong economic growth relative to the US and an improving corporate earnings outlook, driven by China reopening and a bottoming tech cycle. China's growth momentum moderated in the second quarter and the risk of a double dip is on the rise, but things might still improve in the second half of 2023 as policy makers still have the option to introduce further easing measures to support

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).

consumption and employment. Meanwhile early signs of resumed communication between the US and China indicate reduced geopolitical risks. We anticipate strong performance in regions like Korea where the chip cycle is soon to reach its bottom, benefiting the tech-heavy Korean market as yields moderate. Chinese equity's cheap valuation is difficult to ignore, but its near-term direction will be determined by forcefulness of policy stimulus and geo-political development.

In summary, we expect the US to potentially avoid a recession this year. Headline inflation in the developed world seems to be moderating but core inflation remains persistent. Asia is projected to be the primary driver of global growth. Most central banks will continue rate hikes in the second half of 2023 but reach terminal rates by year end. This translates to yields peaking as central banks reach terminal rates, providing support for Treasuries. Stress on US Treasuries due to debt ceiling default risks is expected to diminish, allowing Treasuries and duration to perform as US growth moderates.

Specific share class 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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