

30 September 2023

Market review

Australian equity markets declined in September, with the S&P ASX 200 Net Total Return Index returning -2.8% in Australian dollars (AUD)*, while the MSCI World (hedged to AUD) Index returned -3.7%*. With the Australian dollar depreciating against the US dollar (USD) over the month, the MSCI World (unhedged) Index returned -3.9% in AUD*.

Australian equities fell during September. Although all sectors ended in the red, losses were especially led by the real estate, tech and healthcare sectors. The Reserve Bank of Australia (RBA) held the cash rate at 4.1% for the third consecutive month[1]. The Melbourne Institute's Monthly Inflation Gauge for September[2] remained unchanged after an increase of 0.2% in the previous month. The Judo Bank Australia Composite PMI increased from 48 to 51.5[3], signaling private sector expansion, led by the service industry, while the manufacturing sector faced a faster decline due to economic challenges and higher interest rates. Employment grew in both sectors, leading to a reduction in the backlog of work. Retail sales in Australia showed a modest 0.2% monthly growth in August[4] while the Westpac-Melbourne Institute Consumer Sentiment index dropped 1.5% to 79.7 in September[5], reflecting declining savings, a less hawkish RBA outlook and concerns surrounding budget and taxation.

In fixed income, the Australian 10-year government bond yield ended the year close to 4.5%[6], its highest since October 2011, driven by global expectations of prolonged higher interest rates to combat inflation. Finally, in September, the Australian dollar eased slightly against the US dollar. The AUD started the month at the 0.645 level versus the US dollar but fell below 0.635 later in the month[7]. Yet it closed the month around 0.643. Elsewhere, global equities also faced continued selling pressure in September, as investors remained concerned about rising energy costs, and higher bond yields. In the US, investors pulled back from technology giants and as a result, the NASDAQ Composite Index performed worse than the S&P 500 Index. European stocks also underperformed. The UK was a rare bright spot, particularly the commodities-heavy FTSE 100 Index. Emerging markets (EMs) had a mixed performance. Brazil and India rose, while Chinese companies fell as woes in China's property sector persisted. In global fixed income, sovereign bonds fell globally, resulting in higher yields. In the

US, the yield on 10-year Treasuries hit the highest levels in 16 years or since before the 2008 global financial crisis. Corporate bonds underperformed sovereign issues worldwide. Annual inflation declined in the UK and Europe. In the US, consumer price inflation (CPI) rose to 3.7% in August[8], although the rate of increase in the core CPI fell back to 4.3%[9]. The Federal Reserve and the Bank of England both chose to skip a rate rise in September, while the European Central Bank (ECB) continued to raise them. At the end of the period, the US Congress agreed on a funding deal that avoids a government shutdown. The US dollar index, which tracks the greenback against six other major currencies, hit a new high for 2023.

Performance

In September, the Fund returned -2.01% in gross terms and -2.07% net of fees. Risk assets including equities and the Australian dollar were the largest detractors. The exposures to NASDAQ and the VanEck Wide Moat strategies declined the most as tech stocks sold off. Global equities were also dragged down by the underperformance of US shares. Australian equities were also down in September as deteriorating risk sentiment and continued concerns around China weighed on the local market.

Fixed income overall also detracted over the month — especially the long duration exposures. Australian and US government bonds sold off as yields rose. Shorter duration exposures managed to post positive returns over the month including syndicated loans, floating rate note and subordinate debt exposures.

Activity

Over the month we increased our US dollar exposure after, potentially, the last rate hike by the ECB and Eurozone's relatively weaker growth outlook. We also closed out the September VIX call option before expiry given the subdued volatility level.

Outlook & strategy

Expectations that central banks will keep interest rates higher for longer, as well as a significant increase in term premia, are sending bond yields higher. While we wouldn't necessarily take central bankers at their word about keeping interest rates elevated should the economy weaken as we expect, we think that the drivers of higher term premia are structural and long lasting. Financial markets have been volatile, amid the significant sell-off in developed market (DM) government bonds and a partial

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).

recovery as geopolitical uncertainty has spiked. Our policy rate forecasts envisage a period of rates remaining at or around current levels until the middle of next year to squeeze out remaining inflationary pressures, but then followed by an easing cycle from the second half of 2024 onwards. Looking ahead, we expect monetary policy tightening to weigh on growth in the next 12 months, but major DM economies are likely to avoid a recession this year before a more challenging 2024 starts. Global growth remains supported in the near term, making inflation re-acceleration and continued policy tightening a plausible scenario. In such an environment, we expect the USD to stay strong against other currencies. Equities will be supported by the growth backdrop. DM government bonds are under pressure from a macro and supply-demand perspective but the rapid rise in yields and increasingly appealing valuation levels could lead to a short-term reversal. Across credit we prefer investment grade over high yield given the rising default rate in lower quality space.

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.

* Source: FactSet 31/08/2023 to 30/09/2023

1. Australia Interest Rate - 2023 Data - 1990-2022 Historical - 2024 Forecast - Calendar (tradingeconomics.com)
2. Australia Melbourne Institute Inflation Gauge MoM - September 2023 Data (tradingeconomics.com)
3. Australia Judo Bank Composite PMI - September 2023 Data - 2016-2022 Historical (tradingeconomics.com)
4. Australia Retail Sales MoM - September 2023 Data - 1982-2022 Historical (tradingeconomics.com)
5. Australia Consumer Confidence - September 2023 Data - 1974-2022 Historical (tradingeconomics.com)
6. Australia 10-Year Government Bond Yield - 2023 Data - 1969-2022 Historical (tradingeconomics.com)
7. Australian Dollar - 2023 Data - 1971-2022 Historical - 2024 Forecast - Quote - Chart (tradingeconomics.com)
8. United States Inflation Rate - September 2023 Data - 1914-2022 Historical (tradingeconomics.com)
9. United States Core PCE Price Index Annual Change - September 2023 Data (tradingeconomics.com)

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Important information

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