Fortem Capital Absolute Return Fund

Quarterly Commentary – 30th September 2024

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As has become the norm, the third quarter of 2024 saw risk assets reprice higher, but not without the odd bout of volatility to contend with. In fact, risk assets performed so well that to the end of Q3 the S&P 500 has enjoyed its best start to a calendar year since the turn of the century.

Total Return	2024	Q3
UK 100	9.8%	1.8%
US 500	21.7%	5.8%
Europe 50	13.1%	2.4%
Japan 225	14.8%	-3.6%
Hong Kong 50	29.0%	21.5%
US 2000	11.2%	9.3%
Swiss 30	12.8%	1.6%
Global Equity	18.9%	6.4%
Global Bond	7.0%	3.6%
Commodities	1.7%	-0.6%
PGF	**5.2%**	**1.2%**
AGF	**1.8%**	**1.0%**
DGF	**5.1%**	**1.6%**
USI	**20.9%**	**5.8%**
ARF	**5.3%**	**1.3%**
CARF	**-**	**1.9%**

Early August did see some volatility as the already thin liquidity at that time of year was strained further when US data soured just as the Bank of Japan hiked rates, leading to an unwind of the ever-popular Yen carry trade. However, this was something of a storm in a teacup; the VIX did see a significant rise, but go even a little out on the term structure and volatility remained relatively subdued. The VIX's use as a barometer for volatility continues to wane. Those who were short gamma did get burned. As ever, when clipping some volatility to pay for protection; buyer beware.

The episode did likely prompt the Federal Reserve to take Jackson Hole as its opportunity to announce a turn in the cycle and pivot away from their inflation mandate, the war having been won (sic), and to employment, which has been weakening in the US for a year or so, as is normal for this stage in the cycle. This turn in the narrative prompted risk assets to resume their rise and at the time of writing, with the first 50 basis point cut in the books, the benchmark index is at a new all-time high.

As a result, the bond market is where the more notable moves have been seen, and where pricing for a while remained far ahead of the Fed's own Summary of Economic Projections. The cuts being priced were suggestive of a full-blown crisis rather than the softest of landings that equities were foretelling. Again, both of the major asset classes cannot be right. It remains to be seen which is.

Commodity markets have until recently been out of vogue for some time within the minds of multi-asset investors. During the quarter, an escalation in tensions in the Middle East not seen for at least twenty years brought them front and centre. Israel's incredible retaliation against another of Iran's proxies in Hezbollah caused Iran to enter the conflict directly, firing missiles directly into Israel. The reaction in energy markets was volatile, but it is important for investors to understand that the world has moved on from the 70s with regards to its resources. Shale has entered, proving unbreakable in the 20-teens, and Saudi have dropped the ball once more over the past 18m ceding market share to OPEC+ members unwilling to stick to their quotas. Before now, taking back that market share would likely have led to oil prices of sub-$50. As long as the Strait of Hormuz remains open, Saudi are likely to plug any gap in supply that an Israeli strike may cause.

Against that backdrop the Fund returned 1.3% over the quarter and 5.3% in the calendar year-to-date.

Income

The Fund is fully collateralised by short-dated, high-grade debt. As such, its liquidity profile extends to the liquidity profile of the Income portfolio.

Beta

The Fund does not allocate to the beta portfolio.

Diversifier

The Fund's diversifier portfolio consists of an equity long / short strategy with a low and stable beta of ~0.2 to global equities. That beta has been very stable through time and environments and is maintained through monthly rebalancing of the long and short legs back to target weights.

The long leg, which overweights the factors of quality, value, momentum and size (favouring smaller companies) was positive for the quarter with quality, value and trend adding positively as factors while size was a negative detractor

The short leg is to benchmark global equities, which has much more of a tilt to growth given that the benchmark is so dominated by a cohort of very large growth stocks. During periods in which those growth stocks perform so strongly, it would be expected that the benchmark index would outperform the long leg which actively targets factors other than growth, the factor that drives the fortunes of the rest of a multi-asset portfolio.

During Q3 the long equity index outperformed as market breadth began to grow. The long leg contributed 1.0% and the short leg -0.2%, leaving the Diversifier portfolio up 0.8% overall.

Protection

The Fund makes no allocation to protection.

Outlook

The Fund has delivered significant positive returns with low beta to equity since its launch. That has been achieved through a combination of returns from the Income and Diversifier portfolios with the consistent low beta overhang contributing positively during a period in which the factors which the Fund targets lagged growth.

During the previous quarter, the first cracks in the growth story began to make themselves known to investors en masse; consistent downward revisions meant cracks have been appearing once the surveyors had left for the past year at least, but initial estimates turning lower was a root cause of the volatility seen in August.

Moving forward, if there is a reversal in fortune for growth and therefore for the benchmark equity and much of the equity content in multi-asset portfolios, the Fund should be a beneficiary of that move. If, as it did in 2022, that coincides with a sharp move lower in equity then the exposure to the non-growth factors as well as income should mean that the Fund weathers the storm effectively, indeed as it would have done in 2022, during which time its return would have been positive. It makes a lot of sense for investors to take exposure to factors other than growth within alternatives given its prevalence elsewhere in portfolios currently.

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