# Fortem Capital Absolute Return Fund

## Quarterly Commentary – 31st December 2024

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| Total Return | 2024 | Q4 |
|---|---|---|
| UK 100 | 9.6% | -0.2% |
| US 500 | 24.4% | 2.3% |
| Europe 50 | 11.0% | -1.8% |
| Japan 225 | 20.8% | 5.3% |
| Hong Kong 50 | 22.6% | -4.9% |
| US 2000 | 11.5% | 0.3% |
| Swiss 30 | 7.5% | -4.7% |
| Global Equity | 18.7% | -0.2% |
| Global Bond | 1.3% | -3.1% |
| Commodities | 5.4% | -0.5% |
| **PGF** | **5.3%** | **0.0%** |
| **AGF** | **1.2%** | **-0.5%** |
| **DGF** | **5.4%** | **0.3%** |
| **USI** | **23.2%** | **1.9%** |
| **ARF** | **7.1%** | **1.7%** |
| **CARF** | **-** | **-1.0%** |

2024 saw equity markets post another stellar year of returns led by the US, which posted its second consecutive year of returns greater than 20%. Global bonds in general continued their poor performance as government bond yields remain elevated, but investors found a happy hunting ground in high yield credit where spreads continue to tighten, buoyed by the general optimism over risk assets.

The US economy continued to decouple from the rest of the global economy with the job market remaining buoyant, growth solid and inflation stubborn. The past few years have not been without growth scares with SVB, the tightening of conditions in summer 2023 brought on by US Treasury issuance, and the deterioration in data in summer 2024 all encouraging action from policymakers to loosen conditions significantly each time. These policy reactions had the effect of prolonging economic strength and strong labour conditions.

The latest of those reactions was the start of the cutting cycle following some relatively poor data in July. However, unlike most cutting cycles, conditions, led by increased term premium, have tightened significantly since the first cut in September; the market, in the absence of willingness from policymakers, is taking it upon itself to finally kill off inflation. This can and will only be achieved by a slowing of growth and dampening of demand. There is also, after a Republican clean sweep in November, a new administration which will decide its response to this slowing; they have been openly critical of the previous administration's Treasury issuance policy and have less tools at their disposal to loosen conditions.

The market has not priced this slowdown and is unprepared for this as an outcome.

The Absolute Return Fund returned 7.1% over the year and 1.7% over Q4.

### Income

The Fund is fully collateralised by very short-dated, high-grade debt. As such, its liquidity profile extends to the liquidity profile of the Income portfolio. The Fund has a 70% overhang of Income. Therefore, when the risks free rate is high so is the base level of return available to the strategy. It allows investors to somewhat 'have their cash cake and eat it' within an alternative allocation.

### Beta

The Fund does not allocate to the beta portfolio.

### Diversifier

The Fund's diversifier portfolio consists of an US dollar 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) whilst maintaining the same ex-ante volatility of the parent index underperformed the heavily large cap and growth biased parent index over both the quarter and 2024 as a whole. In spite of this, the low and stable beta that the strategy employs allowed the Diversifier Portfolio to post a positive return for the year.

2024 was another year in which big was beautiful as stock market returns were once more dominated by a few very big names. This concentration is so stark that the 'Mag 7' make up more of the parent global equity index than the entirety of the stock markets of the UK, France, Germany, China and Japan combined, and it is not particularly close.

Over 2024, value and size were the particular laggard in terms of the factors the strategy targets, while quality did have a good year, it still lagged growth heavily. Momentum was the stand out factor in another year in which little rotation was seen.

In spite of the continued underperformance of the target factors within the strategy against growth, 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.

**Outlook**

The investment landscape has become dominated by a very small, very large cohort of high growth stocks such that it has become near impossible for the equity component of multi-asset portfolios to not follow the same path. This increased concentration alongside the move to passive equity investing has provided for a positive feedback loop as rebalancing has forced ever more money into those names and left benchmark equity indices dependent on the performance of a few stocks which share similar characteristics.

The risk to the equity component in most portfolios moving forward is a reversal in the tailwind provided to stocks with those characteristics, whether brought about by a change in the prognosis for growth, policy or both, they are clearly neither mutually exclusive and more likely causative.

Equity beta is the most persistent and rewarding market beta that exists. Therefore, allocating a small portion of alternative allocation should provide for positive returns above the risk free rate through time. However. When the concentration in factors within the equity component of portfolios is so skewed to growth, one really should diversify that factor exposure within the alternatives allocation in order that it is not simply closet equity. That is exactly what the strategy achieves for investors.

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