Santander Asset Management

Santander GO Absolute Return

4 / 2022

Fund commentary

Market Review:

After a bad Q1, there was little respite for markets in April as concerns over global growth continued to gather pace. Indeed, it was a terrible month across asset classes, and for only the second time so far in the 21st century, we simultaneously saw the S&P 500 fall more than -5% and US Treasuries lose more than -2%. The losses were driven by multiple factors including the ongoing Russian invasion of Ukraine and the risk of further escalation, the Chinese lockdowns to deal with Covid, and growing fears that central banks will be unable to achieve a soft landing as they continue to grapple with strong inflation.

In terms of the drivers of this performance, growing inflationary pressures were a continued theme in April as they have been for some months now. This meant that April was an incredibly bad month for sovereign bonds. US Treasuries (-3.2%) lost ground for a fifth consecutive month, taking their YTD losses to -8.6%, whilst EU sovereigns (-3.7%) saw their worst monthly performance since 1999.

Credit spreads continued to suffer from concerns about higher financing costs and slowing economic growth, and the European Itraxx Investment Grade index widened by 17bps to +90bps, whilst the Itraxx High Yield Index widened by 89bps to +424bps.

Russia's ongoing invasion of Ukraine was another worrying factor for the market, and energy prices have remained elevated in response, with WTI crude oil (+4.4%) moving higher for a 5th consecutive month. Fears about slowing Chinese growth dented demand for Gold and Copper, with Gold falling -2.1% and Copper depreciating nearly -6%.

With this array of risks on the horizon, equities sold off again in April, with the S&P 500 (-8.7% in total return terms) putting in its worst monthly performance since March 2020, although Europe's STOXX 600 (-0.6%) only saw a modest decline. A major underperformer were the mega cap tech stocks in the US, with the FANG+ index down -18.9% in April, marking its worst monthly performance since the index was launched, and bringing its YTD decline to -27.9%. The MSCI World index fell -8.3% and the MSCI Emerging Markets index dropped -5.6%.

On the FX side, it was all about US Dollar strength, with the Dollar Index rallying +4.7%, and the Dollar appreciating 5% against the Euro. The Japanese Yen was the big loser, falling -6.6% against the Dollar and -1.7% against the Euro.

Portfolio Review:

Overall, the Portfolio delivered a negative return in April 2022, driven by our Macro directional positions. Our relative value Satellite positions were positive and our Hedges protected the portfolio by adding some positive performance, as equity markets fell and bond yields were higher.

Our Macro Strategy pillar underperformed and was the most significant driver of overall portfolio losses during April, with most of the damage coming from our "risky asset" positions. On the positive side, our long US Dollar position was almost single-handedly responsible for the out-performance of our "FX Majors" strategy, whilst our long Global

Inflation position benefitted from the ongoing rise in inflation rates seen around the globe, as investors continued to revise upwards their forecasts for inflation. Another strong performer was our long Commodities position, which gained from the increase in the oil price and other commodity indices seen in April, as Europe appeared closer to banning imports of Russian oil and gas. However, on the downside, the sell-off in global equity markets meant that our long US Equity position detracted, even though the position was substantially reduced during the month. With widening credit spreads, our long Global High Yield position and long Global Investment Grade positions also underperformed. Despite also reducing our duration exposure during the month, our long Non-EUR Duration position and long EUR Duration positions detracted from fund performance, whilst our Macro Spread position also lost money (the bulk of this position is a long 10yr Italy vs short 10yr Germany bond trade, and Italian BTP spreads widened versus German Bunds in April). On the Thematic side, all positions were fairly flat in performance contribution terms, with the exception of our Robotics and Gold positions, which lost some ground.

As might be expected when equity markets and credit markets sell-off strongly during the period under review, our equity, fixed income and credit hedges outperformed and helped to protect the portfolio from further drawdowns. As a reminder, to protect the portfolio against an equity market correction (which would hurt overall fund performance given our long equity exposure), we have put options on various equity markets. Given that global equity markets again performed poorly in April, these put options moved closer to the money and became more valuable, generating some nice profits. The main outperformer was our hedges on US equity indices. Our Fixed Income hedges also helped protect the portfolio against the significant rises in bond yields seen on both sides of the Atlantic, whilst our credit hedges (particularly on the US & European High Yield side) also generated some nice gains as the European Crossover index widened by 89bps to 428bps.

The ability of our portfolio managers to generate alpha in difficult market conditions was once again demonstrated in April as we enjoyed good positive performance from the large majority of the sub-pillars in our Satellite part of the portfolio, with our Quant Models and Interest Rates sub-pillars leading the way. In our Quant Models sub-pillar, our Cross Asset model was the main contributor (mainly short 10yr US Treasuries, short 10yr Italian BTP's and short the Japanese Yen) but we had positive contributions from the majority of our models during April. Our Interest Rates sub-pillar also generated positive performance, mainly from a short US Treasury position, whilst our Trading Curves strategy made money from a long 10yr French OAT/short 10yr German Bund position. On the FX sub-pillar, our short South African Rand and short Taiwanese Dollar versus long US Dollar positions all made positive contributions whilst our Equity sub-pillar also made a minor positive contribution during April, mainly driven by our positioning in our US Equity sectors relative value position. Here our short positions in Financials, Technology and Consumer Discretionary sectors proved profitable as the general market fell during April. Our basket of ESG Leaders stocks also out-performed during the market sell-off. Our Satellite – Spread sub-pillars made some small negative contributions to overall performance as credit spreads generally widened and absolute yields rose, and Italian corporate spreads were notable underperformers. Finally, our Inflation, Commodity & Volatility sub-pillar also had some negative performance as USD & GBP inflation curves continued to flatten and invert, whilst we are positioned for steeper curves.

In terms of portfolio activity, our equity exposure decreased from 16.7% at end-March 2022 to 7.5% by end-March. We are now short US equities (-2.2%) compared to end-March's exposure of +8.2%, whilst we slightly increased our position in Europe EMU from flat to +1%. Our exposure to Europe ex-EMU continued to increase, rising this month from 2.7% to 4.2%, and we increased our short position in Chinese equities from -0.9% to -1.7%. Our overall duration stance also decreased from 1.0yrs to -0.1yrs as we believe bond yields may have further to rise. Our spread duration dropped from 1.6 years to 1.0 years. Our overall commodity exposure increased slightly from 6.4%to 6.7%. Our US Dollar exposure increased from +10.4% at end-March to +25.2% by end-April. After the Euro and the US Dollar, the Canadian Dollar is our largest currency position at +3.7%.

Outlook:

We expect that markets will remain quite volatile in the coming weeks and months. Therefore, it's appropriate that we maintain our cautious stance, as evidenced by our relatively low exposure to risky assets at present. By keeping our exposure low, we hope to limit any potential drawdowns – something that is key to the way we manage the portfolio. We are keeping hedging strategies in place to protect the portfolio, such as equity options, yield curve hedges and credit hedges. We continue to manage liquidity dynamically, keeping the appropriate buffers in place, as we expect that liquidity issues are increasing likely to become a concern to investors.