Vontobel

Institutional Clients | Conviction Equities & Quantitative Investments

Portfolio-Update: August Correction

Vontobel Fund (CH) – Sustainable Swiss Equity Income Plus

Produced for institutional investors in Switzerland

What happened?

At the beginning of August, major stock indices faced significant losses. Weak U.S. economic data, including disappointing purchasing managers' indices and labor market data, fueled recession fears and triggered substantial market disruptions. A mixed earnings season, geopolitical tensions, and concerns that the Fed is already “behind the curve” intensifying the risk-off sentiment. The VIX, a key measure of market volatility, briefly spiked to 65 on this "Black Monday," marking the third-highest level since the financial crisis and the COVID-19 pandemic, before settling at 39 by the end of the day. Swiss equities were not immune to these global turbulences, although losses were somewhat milder than in other regions. Nevertheless, the SPI index declined by over 6% in the first two trading days of August.

How did the portfolio respond? What actions did we take?

While the portfolio slightly lagged behind the SPI index during the strong market phases of Q2, the benefits of the implemented covered-call strategy in the fund became evident during the current correction. In the first trading days of August including Wednesday 7th, the fund outperformed the market by 0.67%, with options premiums providing a partial cushion against the downturn.

On top, the portfolio's stock selection had been gradually adjusted to a more defensive stance in recent weeks. In anticipating a global economic slowdown, the market beta was already reduced from over 1 to 0.95.

Given our assessment that the markets overreacted on Monday after two highly negative trading days, and considering that a strong and rapid market recovery (V-shape formation) would be unfavorable for a covered-call strategy, we employed an additional derivative strategy by purchasing a call option on the SMI to reduce upside risk. From today’s perspective, the timing was favorable: if the market rebounds by approximately 5% from Monday's lows within the next few weeks, the fund will hold a 5% higher market exposure.

Finally, in light of recent sharp daily movements, we have adopted a more cautious approach for our scheduled option rebalancing which took place on Thursday this week. Given the strong market movements over the past few days, the new options will be written over two to three days instead of one single day under normal market conditions. Also our quantitative dynamic strike price model suggested significantly higher strike prices (further out of the money). However, the current volatility environment could promise higher premium income than in recent option rebalancings.

Outlook:

The Swiss stock market stabilized mid-week and has already initiated a rebound. The sustainability of this recovery will be tested in the coming days and weeks. While we believe that the sharp correction earlier in the week appears to have stopped for now, equity markets remain fragile due to geopolitical tensions and a weakening global economy. Consequently, a quick return to new highs in the coming weeks seems less likely. In this market environment, investments in our fund strategy, which benefits from multiple income streams—market participation, premium income, and dividends—remains a valid option.

Source: Vontobel, as of 7.8.2024.

Risks

- Limited participation in the potential of single securities.
- Success of single security analysis and active management cannot be guaranteed.
- It cannot be guaranteed that the investor will recover the capital invested.
- Derivatives entail risks relating to liquidity, leverage and credit fluctuations, illiquidity and volatility.
- Price fluctuations of investments due to market, industry and issuer linked changes are possible.
- Investments in mid and small cap companies may be less liquid than investments in large cap companies.
- With the use of a covered call options strategy the participation in the potential positive price development of the underlyings is limited.
- There is no guarantee that all sustainability criteria will always be met for every investment. Negative impact on subfund's performance possible due to pursuing sustainable economic activity rather than a conventional investment policy.
- The Sub-Fund’s investments may be subject to sustainability risks. The sustainability risks that the Sub-Fund may be subject to are likely to have an immaterial impact on the value of the Sub-Funds’ investments in the medium to long term due to the mitigating nature of the Sub-Fund’s ESG approach.
- The Sub-Funds' performance may be positively or negatively affected by its sustainability strategy.
- The ability to meet social or environmental objectives might be affected by incomplete or inaccurate data from third-party providers.
- Information on how environmental and social objectives are achieved and how sustainability risks are managed in this Sub-Fund may be obtained from Vontobel.com/SFDR.

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