Schroders

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Schroder ISF* Italian Equity

Fund Manager: Timothy Pedroni | Fund update: Q1 2024

Performance overview

- Italian equities posted very strong gains in Q1.
- The fund underperformed the FTSE Italia All-Share.

Drivers of fund performance

- The fund posted a positive absolute return but lagged the benchmark's strong advance. Stock selection within financials weighed on relative returns and non-performing loan manager **DoValue** was the main individual detractor. This was due to the continuation of adverse industry trends. There has been no growth in the formation of new non-performing loans, despite high rates and a slower economy. This, coupled with the company having to refinance half of its outstanding debt, led to a sell-off. We have reduced the size of our position.
- Lack of exposure to **Ferrari** weighed on relative performance. We have not previously owned the shares due to valuation grounds, preferring to gain exposure to the luxury goods sector via other holdings. Ferrari is a large part of the benchmark. At the end of the period we initiated a position to manage tracking error. Ferrari is still a significant underweight in the fund.
- In the utilities sector, **RWE**, a German company primarily operating in renewable power generation, was a detractor. The entire sector has been performing poorly due to regulatory changes and changing sentiments around renewable energy generation. We have reduced the position significantly but continue to hold it as its Italian equivalent is more expensive.
- On the positive side, not owning ENI or Snam, and having underweight exposure to **Enel**, added value. The energy and utilities sectors underperformed in the quarter so our relative lack of exposure to these companies proved advantageous.
- In the banking sector, our positions in **Intesa Sanpaolo**, **BPM** and **UniCredit** aided relative performance. Strong stock selection within industrials supported relative returns. Banks have maintained strong momentum in terms of repricing and the ability to pay dividends and share buybacks.

Portfolio activity

- We exited the position in **HelloFresh**. The meal kit industry, particularly in the US which is a key market for HelloFresh, is going through a challenging period. Additionally, HelloFresh issued a profit warning.
- We sold out of industrial machinery firm **Interpump**, which has reached our estimate of fair value. There are similar positions in the portfolio that offer more upside.
- We initiated a position in gaming firm **Lottomattica**, partly to diversify our consumer exposure. Lottomattica's gambling and gaming operations are seen as recession-resistant behaviours, offering a degree of stability. Coupled with the release of a compelling new industrial plan, we believe it offers high quality defensive consumer exposure.
- Another addition was **BFF Bank**, a financial services company specialising in buying receivables from large pharmaceutical companies. This was done with the aim of diversifying our financial sector exposure, as we have reduced our stake in DoValue. BFF Bank has a strong track record of generating high returns and its business has significant barriers entry.
- We started a new position in **Leonardo**, an aerospace and defence company. We wanted defence exposure given rising defence spending globally in response to Russia's invasion of Ukraine and other risks. We see Leonardo as attractively valued and note that it has shown significant improvement under its current management.
- We also added **Acea** to the portfolio to diversify our utilities exposure. Acea has a new industrial plan which we believe is promising.

Outlook/positioning

- The global economy appears to be heading for a soft landing, with the US in particular proving resilient in terms of growth. Growth in Europe has been slower and China remains sluggish. Meanwhile, inflation has remained above target in most developed countries. Our economics team believe that the market may be anticipating too fast a pace of monetary policy easing. We are therefore not positioning the portfolio for a sharp slowdown or acceleration in the cycle.
- As part of our risk management, we have re-sized the top ten active loads in the fund to account for

*Schroder International Selection Fund is referred to as Schroder ISF throughout persistent small cap underperformance. However, the portfolio remains focused on businesses with sustainable long-term earnings growth and we continue to believe that the small and mid cap space is the best place to find such earnings growth.

Calendar year performance (%)

Year	Fund	Target	Comparator
2023	24.1	32.3	22.0
2022	-14.0	-10.3	-13.3
2021	29.0	27.9	31.0
2020	1.7	-3.5	-4.1
2019	28.7	32.5	25.8
2018	-19.1	-13.9	-16.1
2017	21.3	19.1	20.8
2016	-8.1	-6.4	-8.1
2015	22.8	18.5	21.0
2014	2.1	2.3	0.7

Source: Schroders, as at 31 December 2023. Fund performance is net of fees, NAV to NAV with net income reinvested, EUR C Acc shares. Please see factsheet for other share classes.
Target benchmark is FTSE Italia All-Share TR and comparator is the Morningstar Italy Equity sector. The fund's investment universe is expected to overlap materially with the components of the target benchmark. The comparator benchmark is only included for performance comparison purposes and does not determine how the investment manager invests the fund's assets. The investment manager invests on a discretionary basis and is not limited to investing in accordance with the composition of the target benchmark.

Past performance is not a guide to future performance and may not be repeated. The value of investments and the income from them may go down as well as up and investors may not get back the amount originally invested.

Risk considerations

Liquidity risk: In difficult market conditions, the fund may not be able to sell a security for full value or at all. This could affect performance and could cause the fund to defer or suspend redemptions of its shares.
Operational risk: Operational processes, including those related to the safekeeping of assets, may fail. This may result in losses to the fund.
Currency risk: The fund may lose value as a result of movements in foreign exchange rates.
Concentration risk: The fund may be concentrated in a limited number of geographical regions, industry sectors, markets and/or individual positions. This may result in large changes in the value of the fund, both up or down.
Derivatives risk: Derivatives may be used to manage the portfolio efficiently. A derivative may not perform as expected, may create losses greater than the cost of the derivative and may result in losses to the fund.
Counterparty risk: The fund may have contractual agreements with counterparties. If a counterparty is unable to fulfil their obligations, the sum that they owe to the fund may be lost in part or in whole.
Higher volatility risk: The price of this fund may be volatile as it may take higher risks in search of higher rewards.
Performance risk: Investment objectives express an intended result but there is no guarantee that such a result will be achieved. Depending on market conditions and the macro economic environment, investment objectives may become more difficult to achieve.
IBOR: The transition of the financial markets away from the use of interbank offered rates (IBORs) to alternative reference rates may impact the valuation of certain holdings and disrupt liquidity in certain instruments. This may impact the investment performance of the fund.
Market risk: The value of investments can go up and down and an investor may not get back the amount initially invested.
Sustainability risk: The fund has environmental and/or social characteristics. This means it may have limited exposure to some companies, industries or sectors and may forego certain investment opportunities, or dispose of certain holdings, that do not align with its sustainability criteria. Therefore, the fund may underperform other funds that do not apply similar criteria. The fund may invest in companies that do not reflect the beliefs and values of any particular investor.