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Schroder ISF* US Dollar Bond

Fund Manager: Lisa Hornby and Neil Sutherland | Fund Update: Q1 2024

Market overview

- The first quarter was notable for the elevated yield levels as many had predicted lower rates with peak inflation having passed. However, inflation readings for January and February came in firmer than expected and economic growth has proved resilient, forcing investors to dial back their rate-cut bets. The other notable story for the quarter was the record new issuance in investment grade corporate debt. It was a record for a first quarter and the second largest quarter on record (Q2 2020 is the record). While some had suggested that higher rates might limit new issuance, the resilient economy, strong labor markets and positive growth meant the all clear for corporations to issue. Perhaps more remarkable was that the new issuance was digested by the market without any indigestion as evident by spreads grinding tighter over the period and by the generally constant flows into the asset class. The all-in yields above 5% have been attractive on an outright basis despite valuations and the demand from institutional clients (i.e. insurance companies and pension funds) has been constant.
- For the quarter, spreads as measured by the Bloomberg Corporate Bond Index were tighter by 9 basis points (bps) ending at 90 bps. This is remarkable given the record new issuance for the quarter for high grade issuers and reflects the strong technical supporting the market. Corporates (89 bps) posted positive excess returns to Treasuries with financials the best (115 bps) followed by utilities (101 bps) and industrials (72 bps). Among the broad sectors of the Bloomberg Aggregate Bond Index, securitized assets (-14 bps) were well behind corporates in excess return terms whereas sovereigns (60 bps) were nearly in line. Tax-exempt municipals (17 bps) were also positive in excess return terms however well behind corporates and taxable municipals (117 bps). Treasuries were in the headlines as the eagerness to price in rate cuts evaporated over the period and yields moved higher with the 10-year tenor up 32 bps and shorter tenors up more (2-year tenor up 37).

Drivers of fund performance

- The portfolio outperformed the benchmark over the quarter due to contributions from asset allocation and issue selection.
  - Asset allocation was driven from the overweights to sovereigns, energy, banking and ABS. Issue selection was also positive with contributions driven by sovereigns, treasuries as well as cyclicals.

Outlook/positioning

- Looking forward to April the portfolio will remain with the overweight to financials. Although the sector has out-performed other corporates year to date, the strong balance sheets and bank reserves still make them attractive, even at the current level of spreads (near the post-GFC tights). To be fair, valuations are not attractive on a spread basis. However, the all-in yields are as evident by the consistent demand to start the year. Should the current heavy volume of new issuance abate, as the market is well past estimates for the time frame, this would be supportive for corporate credits going forward as well.

Calendar year performance (%)*

Year	Fund	Target	Comparator
2023	5.4	5.5	4.7
2022	-16.0	-13.0	-9.8
2021	-1.4	-1.5	-1.5
2020	10.3	7.5	6.9
2019	9.3	8.7	7.7
2018	-1.6	0.0	-1.1
2017	4.4	3.5	3.6
2016	2.8	2.7	2.2
2015	-1.2	0.6	-0.7
2014	6.0	6.0	4.4

Source: Schroders, as at 31 December 2023. Fund performance is net of fees, NAV to NAV with net income reinvested, C Acc shares. Please see factsheet for other share classes. The target benchmark is Bloomberg Barclays US Aggregate Bond Index and comparator is Morningstar USD Diversified Bond. The fund's investment universe is expected to overlap to a limited extent with the components of the target benchmark.

*Schroder International Selection Fund is referred to as Schroder ISF throughout

Past performance is not a reliable indicator of future results. The value of investments and the income from them may fall as well as rise and investors may not get back the amount originally invested. Some performance differences between the fund and the benchmark may arise because the fund performance is calculated at a different valuation point from the benchmark. Please see the respective fund factsheets for the performance of other share classes.

Investment Objective

The Fund aims to provide income and capital growth in excess of the Bloomberg US Aggregate Bond (TR) index after fees have been deducted over a three to five year period by investing in fixed and floating rate securities denominated in USD.

Risk considerations

– **ABS and MBS risk:** The fund may invest in mortgage or asset-backed securities. The underlying borrowers of these securities may not be able to pay back the full amount that they owe, which may result in losses to the fund.

– **Capital risk / distribution policy:** As the fund intends to pay dividends regardless of its performance, a dividend may represent a return of part of the amount you invested.

– **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.

– **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.

– **Credit risk:** A decline in the financial health of an issuer could cause the value of its bonds to fall or become worthless.

– **Currency risk:** The fund may lose value as a result of movements in foreign exchange rates.

– **Currency risk / hedged share class:** The hedging of the share class may not be fully effective and residual currency exposure may remain. The cost associated with hedging may impact performance and potential gains may be more limited than for unhedged share classes.

– **Derivatives risk:** Derivatives may be used to manage the portfolio efficiently. The fund may also materially invest in derivatives including using short selling and leverage techniques with the aim of making a return. 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.

– **High yield bond risk:** High yield bonds (normally lower rated or unrated) generally carry greater market, credit and liquidity risk.

– **IBOR risk:** 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.

– **Interest rate risk:** The fund may lose value as a direct result of interest rate changes.

– **Issuer risk:** The fund is permitted to invest more than 35% of its scheme property in transferable securities and money market instruments issued or guaranteed by an EEA State / governments of the following country: United States of America.

– **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.

– **Market risk:** The value of investments can go up and down and an investor may not get back the amount initially invested.

– **Operational risk:** Operational processes, including those related to the safekeeping of assets, may fail. This may result in losses to the fund.

– **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.

– **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 chosen by the investment manager. The fund may invest in companies that do not reflect the beliefs and values of any particular investor.

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