

Schroder ISF* Global Bond

Fund Manager: Julien Houdain, James Ringer, Martin Coucke and the Global Unconstrained Fixed Income Team | Fund update: June 2025

Market overview

- Geopolitical headlines dominated news flow during June, with the conflict in the Middle East and a spike in oil prices driving market uncertainty. Meanwhile, economic data reflected slowing growth momentum although concerns over an imminent recession remained low. With central banks nearing the end of their cutting cycle, attention is now shifting away from monetary policy towards the potential impact from fiscal policy.
- The US Federal Reserve (Fed) kept interest rates on hold with the average of Federal Open Market Committee (FOMC) members continuing to forecast two rate cuts for the remainder of the year. The FOMC reduced its growth forecast, while raising its inflation outlook, largely due to tariffs.
- Elsewhere, European central banks continued to ease monetary policy conditions with interest rate cuts by the Norwegian, Swedish and Swiss central banks alongside the European Central Bank (ECB). While the ECB's 25 bps rate cut was expected, the significant development was in President Lagarde signalling that they have now 'nearly concluded' their rate cutting cycle.
- There was divergence across government bond markets, with benchmark 10-year US Treasury and gilt yields falling, in comparison to Germany where yields rose during the month.
- Credit markets were resilient to ongoing geopolitical risks, and market volatility actually fell to the lowest in a year following the ceasefire in the Middle East. Investment grade (IG) credit spreads contracted across the US, euro and sterling denominated corporate bond markets, outperforming similar maturity government bonds.
- Given the resurgent appetite for risk, high yield (HY) corporates outperformed their IG counterparts in both the euro and US markets.

Drivers for fund performance

- The fund delivered returns in excess of the benchmark during June, with rates and credit strategies driving outperformance.
- In rates, we benefited from the comparative underperformance of Canadian bonds, through a cross-market position, overweight UK versus Canada.
- A preference to underweight German bunds, both outright and versus the UK and the US, worked well.
- Curve positioning was also additive, notably a curve steepener in the US (ie positioned for longer maturity bonds to underperform shorter dated bonds).
- In asset allocation, the main contributors came from overweight positions in securitised credit and US MBS (mortgage-backed securities).

Portfolio activity

- In terms of strategy, despite geopolitical risks, economic fundamentals are little changed over the month. Growth is softening, but not to the degree that warrants recessionary concerns. Consumer spending, particularly in the US, remains robust, supported by high real income growth (when adjusted for inflation).
- Accordingly, we have maintained headline duration at a modest underweight, preferring instead to exploit market divergence.
- We continue to see value in an overweight to the UK on a cross-market basis, where we prefer the five-year point of the yield curve. We are seeing clearer signs of a slowdown in the UK labour market as well as a softening of underlying inflation pressures, such as wage growth, which warrants some convergence with market pricing for interest rates in other markets. During the month, we took profit and closed an overweight UK versus Canada and rotated into an overweight UK versus Germany position.
- Similarly, we used Germany to fund an overweight to the US, given our view that fiscal stimulus out of Germany suggests a positive medium-term trajectory for European growth. The position was later closed, taking profit following the ceasefire in the Middle East.

- In terms of yield curve strategies, we closed a UK curve steepener preferring instead to focus on cross-market positions. Meanwhile, we kept a curve steepening bias in the US and added a similar strategy in the eurozone, where we expect the front end of the curve to perform relatively well as inflation underwhelms.
- We made no major changes to the fund's asset allocation and retain a notable overweight to US securitised debt. In corporate credit, we retain a neutral position in investment grade credit, favouring shorter-dated euro denominated names.
- We managed our long US high yield exposure, temporarily cutting the position ahead of the release of US payrolls data. We viewed this as a potential risk event, but payrolls came in broadly in line with consensus and we added back the exposure judging the US economy to be stable enough to warrant a position in high yield, which continues to offer attractive levels of income.
- Elsewhere, we added some exposure to government-related issuers, particularly dollar and euro-denominated emerging market sovereign debt. We believe that lower market volatility should support this asset class.

Outlook/positioning

- From a macroeconomic perspective, we continue to see a 'soft landing' as the likeliest outcome. This makes us generally cautious on outright duration, preferring instead to capture market divergence through cross-market strategies.
- Attention is beginning to turn more forcibly away from an easing of monetary policy to fiscal policy. Nevertheless, we view the higher level of terminal rate pricing in the UK as an outlier to both the US and eurozone, which presents tactical opportunities cross-market favouring UK duration.
- A fall in market volatility should continue to support strong investor interest in credit markets. We view US and euro denominated IG as generally expensive, but still find opportunities in shorter dated euro names. High yield spreads have tightened significantly post-'Liberation day' and the valuation argument has diminished somewhat. While the potential for spreads to contract is now more limited, the asset class continues to offer attractive levels of income.
- Agency mortgage-backed securities (MBS) remain our top pick in asset allocation given the spreads on offer and the lower volatility.
- As we head into the third quarter, we anticipate continued divergence across global markets. Choosing the right point of the yield curve will be increasingly important as governments look to

implement greater fiscal spending, although the ability to do so varies from country to country.

- More broadly, how different segments of the bond market are reacting to global developments makes it even more important to have a strategic but agile approach to portfolio construction. Recognising and reacting to regime changes when they happen, while being disciplined enough not to be too reactive to news headlines, we believe, is key to generating positive excess returns.

Past performance does not predict future returns. 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.

Calendar year performance (%)*

Year	Fund (A Acc)	Fund (I Acc)	Target
2024	-2.1	-1.2	-1.7
2023	4.5	5.4	5.7
2022	-19.1	-18.4	-16.2
2021	-5.7	-4.8	-4.7
2020	8.4	9.2	9.3
2019	8.8	9.7	6.8
2018	-3.5	-2.6	-1.2
2017	7.1	8.0	7.4
2016	2.1	3.1	2.1
2015	-5.1	-4.2	-3.2

Source: Schroders, net of fees (where applicable), bid-bid, with net income reinvested as at 31 December 2024. Target is BBgBarc Global Aggregate TR.

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.
- **Bond Connect risk:** The fund may be investing in the China Interbank Bond Market via the Bond Connect which may involve clearing and settlement, regulatory, operational and counterparty risks.
- **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.
- **Contingent convertible bonds:** The fund may invest in contingent convertible bonds. If the financial strength of the issuer of a contingent convertible bond falls in a prescribed way, the value of the bond may fall significantly and, in the worst case, 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.
- **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 shareclass:** 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.

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