

Schroder ISF* Global Bond

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Market overview

- September was a positive month for bond markets overall, with yields across developed government bond markets falling, led by longer-dated bonds.
- The US Federal Reserve's (Fed) meeting was a key focus during the month. Although the 25bp cut to 4.0% - 4.25% was widely anticipated, market participants watched closely for any indications on near-term monetary policy. Guidance from the Fed suggested a further two rate cuts this year would be appropriate.
- In the eurozone, the focus was on French politics, with Prime Minister Bayrou losing the confidence vote aimed at garnering support for the government's deficit reduction agenda. In acknowledgement of this 'political fragmentation' and 'weak fiscal record' Fitch downgraded France's sovereign rating from AA- to A.
- As expected, The European Central Bank (ECB) kept policy rates on hold at 2%. The inflation forecast was revised down further below the central bank's target of 2% and markets are now expecting interest rates to remain unchanged
- In the UK, the Bank of England kept the base rate unchanged at 4% while slowing the pace of its annual quantitative tightening programme from £100 billion to £70 billion. Vulnerabilities over the UK's fiscal position were highlighted by data released showing that public sector net borrowing year-to-date was £11.4bn higher than the Office for Budget Responsibility forecast back in March.
- US investment grade credit spreads tightened further during September, down to multi-decade lows. Increased supply over the month was well absorbed, underpinned by ongoing investor demand for yield amid a relatively constructive outlook for corporates.
- Credit spreads were also tighter across the euro and sterling investment grade markets, generating excess returns over government bonds. High yield markets produced similar excess returns for US and euro-denominated securities, although the sterling market lagged.

Drivers for fund performance

- Fund performance was positive and outperformed the benchmark in September. Asset allocation was the primary driver of outperformance, while rates strategies detracted overall.
- In asset allocation, an overweight to securitised assets was additive, with US agency mortgage-backed securities in particular benefitting from lower market volatility.
- In investment grade credit markets, issuer selection generated additional returns.
- In rates, the most significant detractor from performance came from a curve steepening position in the US.

Portfolio activity

- Outright duration (interest rate risk) was increased, moving the overall position from underweight to neutral. This was achieved by closing the underweight positions in Germany and in Japan, where the market moved to price in three interest rate hikes by the Bank of Japan. This is at the upper end of our expectations, so we took the opportunity to take profit on the position.
- In the US, we reduced our curve steepening position following September's Fed meeting. Over previous months, concerns around political influence on the Fed and therefore its ability to control longer-term inflation has steepened the yield curve. This time around, two Fed governors who were previously dovish dissenters voted for the rate cut, reducing this concern for now.
- We also reduced a similar position in the eurozone, where in addition to markets having a relatively high sensitivity to global developments, there were also reports suggesting Dutch pension reform might be delayed, reducing our conviction in the position.
- We introduced a cross-market overweight to Australia against the US. Given the decline in US Treasury yields, we consider this a more defensive route to establish an outright underweight to the US. Both valuations and technical factors are also supportive for the Australian market.

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

- In asset allocation, we marginally increased exposure to euro-denominated covered bonds, where we identified attractively priced new issues.

Outlook/positioning

- As we move into the final quarter of 2025, we continue to be in an environment of slowing US growth, albeit not dramatically. Our base case is for a soft landing, although the risks around this remain skewed to the downside.
- For direction on interest rates, the US labour market will be key. For a Fed that has a dual mandate of maintaining ‘full employment’, not to mention political pressure to ease policy, the growing risks to the downside in the labour market will accelerate the easing cycle, assuming inflation remains well behaved. Early signs are promising here.
- We do not envisage a sharp deterioration of the US labour market, which would be problematic for cyclical assets, but a stabilisation consistent with the positive outlook for corporate profitability. Nevertheless, with corporate spreads trading at historically tight levels, we remain defensively positioned, looking for opportunities within bond selection to enhance returns.
- Similarly, in the eurozone we remain positive on the economic outlook as manufacturing growth is improving and the labour market remains strong. We continue to find corporate valuations expensive but with better opportunities in shorter-dated maturities.

- From a yield perspective, we continue to identify value across emerging market debt as well as securitised assets, including agency mortgage-backed securities and covered bonds.

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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