

Schroder ISF* European Special Situations

Fund Managers: Leon Howard-Spink & Paul Griffin | Fund update: Q1 2024

Performance overview

- Pan-European equities gained in the quarter. The fund slightly lagged the MSCI Europe index's strong advance.

Drivers of fund performance

- The fund narrowly underperformed the benchmark in Q1. Relative performance was strong in February when the bulk of Q4 results for our portfolio companies were released, but slightly weaker for the quarter overall.
- Destocking is a theme that has negatively affected some of our holdings. The two main individual detractors – **Soitec** and **Infineon Technologies** – have both been impacted. Soitec is a specialist in engineered wafers which enhance the quality of semiconductors. It has had to reset its outlook three times in recent months. There is no doubt about the quality of Soitec's technology or market position but its main end-market – smartphones – has been soft. The need to reset the outlook highlights how visibility has been poorer than management had anticipated. We think growth has been delayed but not destroyed.
- Infineon is a maker of power semiconductors which are used in electric vehicles and industrial applications. This was the last semiconductor segment to enter the destocking phase and so is likely to be the last to recover. Meanwhile, the market is split over the extent of the competitive threat from Chinese chipmakers, potentially for export as well as domestically. However, Infineon's chips are highly complex and would be difficult to replicate.
- Other technology holdings performed positively in the quarter, notably semiconductor tools maker **ASML** which was the leading individual contributor. ASML reported robust order intake for Q4. This will help underpin growth in 2025 and beyond. ASML is a key beneficiary of demand for tools to make the complex semiconductors needed for AI applications.
- Elsewhere, chemicals distributor **Azelis** was a detractor. It has been affected weaker demand for both industrial and consumer chemicals. There is little clarity on when this destocking phase will end. At the same time, Azelis is a small and illiquid stock and its share price is more volatile than the underlying business.
- Another detractor was **Industrie De Nora**. This is a stock with exposure to green hydrogen and we have been cautious to limit the position size given the potential for volatile moves. The green hydrogen plans outlined in the US Inflation Reduction Act are yet to come to fruition. Details around how to unlock funding still need to be decided, and so the catalyst for green hydrogen is delayed. De Nora had to revise down its energy transition targets as a result. However, De Nora is not solely exposed to green hydrogen. It has an existing profitable business in other electrochemical processes, including water treatment.
- Aside from ASML, other positive contributors included pharmaceutical group **Novo Nordisk**. It disclosed an excellent set of results. These showed a surge in growth in the diabetes and weight loss franchises. Guidance for the coming year was also very positive.
- Testing and inspection group **Bureau Veritas** was a laggard last year but was a contributor after disclosing good results. There is growing market awareness that both sales and margins can grow. In an environment of increased regulation, Bureau Veritas can help companies report on how they are meeting standards.
- Medical products group **Convatec** is another business that was overlooked last year but the market is now appreciating its growth potential. Management has invested in research & development and there are new product launches to come.
- Cables maker **Prysmian** was a positive contributor. It continues to announce significant contract wins.

Portfolio activity

- During the quarter we took profits in some larger holdings that have performed well. These included **RELX**, **Prysmian**, **Schneider Electric** and **BESI**. We added to some names that have been weaker but where we have high conviction. These included **Experian**, **Assa Abloy**, **Siemens** and **Bureau Veritas**.

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

Outlook/positioning

- Aside from destocking, another persistent theme has been the outperformance of mega cap companies versus the rest. Small and mid cap companies have historically been a rich source of alpha generation for us but we do own some of the mega caps too, with ASML and Novo Nordisk contributing to performance this quarter.
- We remain focused on the long-term prospects for our holdings. The longer-term structural growth drivers embedded in the fund remain strong: the shift to bio-based materials; broad investment in the energy transition; the need to accommodate population growth and the medical infrastructure that implies; the growth of the smart city with all the technology development required.

Calendar year performance (%)

Year	Fund	MSCI Europe net return
2023	18.2	15.8
2022	-28.2	-9.5
2021	26.9	25.1
2020	11.7	-3.3
2019	35.9	26.7
2018	-16.8	-10.9
2017	16.2	10.2
2016	1.2	2.6
2015	17.7	8.2
2014	4.5	6.8

Source: Schroders, as at 31 December 2023. Fund performance is net of fees, NAV to NAV with net income reinvested, EUR C Acc. Please see factsheet for other share classes. The fund's performance should be assessed against its target benchmark being to exceed the MSCI Europe (Net TR) index. The investment manager invests on a discretionary basis and there are no restrictions on the extent to which the fund's portfolio and performance may deviate from the target benchmark. The investment manager will invest in companies or sectors not included in the target benchmark in order to take advantage of specific investment opportunities.

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Risk considerations

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.

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

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.

Higher volatility risk: The price of this fund may be volatile as it may take higher risks in search of higher rewards.

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.

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: Failures at service providers could lead to disruptions of fund operations or losses.

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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