Schroders

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Schroder ISF* Strategic Credit

Fund Manager: Peter Harvey | Fund update: October 2025

Market overview

- Despite a generally encouraging earnings season, a combination of the US government shutdown, renewed tariff-related concerns, and the collapse of two US firms – First Brands and Tricolor – created a risk-off tone for credit markets in October.
- In high yield markets, spreads widened on both euro-denominated and US dollar denominated credit. In Europe, there was significant weakness among single-B rated issues in basic industries – notably chemicals and packaging – and financial services, focused on debt collectors.
- It was a mixed picture in investment grade markets, with credit spreads tightening modestly across Europe, while US spreads widening over the month. Despite increased scrutiny around US regional bank exposures to non-bank financial institutions (NBFI), US financials performed broadly in line with other sectors overall.
- In the US, the Federal Reserve (Fed) cut interest rates by 25bps to 3.75%-4% in what was a split vote and announced an end to its programme of quantitative tightening (which was designed to shrink its balance sheet). However, the main surprise was in Fed Chair Powell's push back against market expectations of a further rate cut in December. Meanwhile, the Supreme Court ruled that Governor Cook would remain in place until hearings in January – allaying concerns about Fed independence for now.
- October's European Central Bank (ECB) meeting was uneventful, with interest rates held at 2% as expected. French politics remained in the spotlight, with Prime Minister Lecornu's resignation then subsequent reappointment. He later survived two votes of no-confidence following concessions on pension reforms. S&P downgraded France's sovereign rating to A+ (previously AA-) citing ongoing political instability.

Drivers of fund performance

- The Fund generated a positive total return during October.
- Exposure to UK government bonds made a positive contribution over the month, as gilts outperformed other major markets after September's inflation print surprised to the downside causing markets to reassess the likelihood of near-term interest rates cuts.
- The rally in gilts also boosted several longer-dated holdings in the banking sector, notably Lloyds Banking Group as well as sterling-denominated bonds issued by European banks, notably Intesa San Paolo and Deutsche Bank.
- In the financial services sector, the holding in payments processing group Worldline was additive over the month, rallying after the ECB had sold its stake in the bonds during September.
- The holdings in UK specialty chemical group Ineos and French chemical company Kem One weakened as the impact of persistent overcapacity and higher energy costs continues to erode margins throughout the sector.

Portfolio activity

- In the real estate sector, we participated in a re-financing from Eastern European commercial developer GTC, which focuses on shopping centres and offices. The re-financing package strengthens the company's balance sheet with the issuance of senior secured bonds. The issue has the added attraction of a high coupon.

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

- We participated in a tap issuance from Neinor Homes, Spain's leading housebuilder, which will partially fund the takeover of AEDAS Homes, enlarging its landbank. A combination of lower interest rates and improving mortgage affordability is positive for transaction volumes in the Spanish housing market.

- On the disposals side, we trimmed the holdings French utility group EDF, German pharmaceutical Nidda Healthcare and UK restaurant group Wagamama.

- With credit spreads in the high yield market now at substantially tighter levels, we continue to hold a significant proportion of the portfolio in investment grade corporate bonds, mainly BBB-rated and AA-rated securities, as well as exposure to gilts, which act as a buffer against market volatility

Outlook/Positioning

- As we head towards the year-end, we continue to be in an environment of slowing growth, albeit not dramatically. Our base case is for a soft landing in the US, 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 monetary policy - the growing risks to the downside in the labour market have led investors to price in another interest rate cut in December.
- We do not envisage a sharp deterioration of the US labour market – something which would be problematic for cyclical assets – but a stabilisation consistent with the positive outlook for corporate profitability.
- In the US, credit spreads offer a limited cushion against any deterioration in the economic fundamentals. Isolated bankruptcies in the loan market indicate growing vulnerabilities across the credit spectrum.
- We remain moderately positive on the economic outlook for the eurozone. Manufacturing growth is improving from low levels; however we do not see a broad recovery yet and the order to inventory ratio in many sectors is still negative. However, the labour market remains resilient. In contrast to the rise in unemployment in the US, eurozone unemployment has equalled all-time lows in recent months, while inflation measures suggest an underlying trend that is hovering around or slightly above its 2% target.
- Notwithstanding geopolitical developments, we also expect corporate fundamentals in the eurozone to remain stable and the default rate to stay relatively low in comparison with the US.
- However, we are mindful that credit spreads in euro high yield, at index level measured over government bonds, are expensive relative to historic levels. Accordingly, we continue to place a greater emphasis on higher quality credit, with an element of exposure to cash and sovereign debt awaiting investment opportunities in the euro credit markets.
- We also remain focused on identifying idiosyncratic opportunities across high yield markets that can provide strong total returns in a variety of market environments. The recent dispersion in single-B rated issues could prove to be a fertile hunting ground for active investors over the coming months.

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.

Calendar year performance (%)

	C Acc	Target
2024	8.2	5.2
2023	11.3	4.6
2022	-7.7	1.3
2021	3.7	0.0
2020	3.8	0.3
2019	8.8	0.8
2018	-1.8	0.7
2017	4.3	0.4
2016	5.9	0.5
2015	3.4	0.6

Source: Schroders, as at 31/12/2024. All performance net of fees (where applicable), NAV to NAV (bid to bid), GBP returns. Target : ICE BofA Sterling 3-Month Government Bill Index.

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.

Risk considerations

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.

Derivatives risk – efficient portfolio management and investment purposes: 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. The fund may also materially invest in derivatives including using short selling and leverage techniques with the aim of making a return. When the value of an asset changes, the value of a derivative based on that asset may change to a much greater extent. This may result in greater losses than investing in the underlying asset.

Event risk: The fund will take significant positions on companies involved in mergers, acquisitions, reorganisations and other corporate events. These may not turn out as expected 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.

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

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.

Important information