

## Schroder ISF\* Hong Kong Equity

Fund Manager: Toby Hudson | Fund update: Q2 2024

## Performance overview

- Hong Kong equities rose modestly over the quarter but were behind those of both China and other Asian markets in aggregate.
- Technology was the best-performing sector during the period, rising by over 18%, followed by telecommunications, which climbed just over 13%.
- Energy was the biggest loser, down by 45.5%. Consumer discretionary was also notably weak.
- The fund produced a positive return but underperformed the benchmark over the period.

## Drivers of fund performance

- At the sector level, stock selection was strong, especially in energy and consumer discretionary. However, allocation weighed on returns, with the overweight to consumer discretionary having a pronounced negative impact.
- At the market level, selection in Hong Kong detracted. On the positive side, the position in China contributed positively.
- The best-performing stock positions were the holdings in **Tencent**, **Crystal International Group** and **Dah Sing Banking Group**.
- The weakest returns came from our positions in **Samsonite International**, **Hong Kong Exchanges & Clearing** and **H World Group**.

## Portfolio Activity

- We purchased a stake in **ANTA Sports** as we expect the ANTA brand to turn around under the leadership of the new management team. We also bought **Trip.com** owing to the continued recovery in China's travel industry, as well as the international expansion that is supporting the company's growth. A further addition was **AIA Group**, which we bought on share-price weakness.
- We trimmed our exposure to **China Mengniu Dairy** due to softer demand and the oversupply of milk. We reduced the position in **WuXi AppTec** owing to geopolitical tensions that continue to cloud the company's business outlook, while also selling **China Pacific Insurance**.

## Outlook/positioning

- Hong Kong's economy is facing cyclical and structural challenges. Worries about the strength of consumer spending are mounting, as the recovery in outbound travel outpaced inbound mainland visitors. The recent marked appreciation of the Hong Kong dollar has also changed cross-border shopping behaviour. Heightened geopolitical tensions and higher-for-longer interest rates have been weighing on external demand and asset prices.
- Owing to the high interest-rate environment and the weak macroeconomic backdrop, Hong Kong's property market has remained sluggish. Rental demand, on the other hand, has risen as property users shift from buying to renting. Office occupancy, however, remained subdued. Looking ahead, there is hope that inflation in the US has peaked and interest rates will gradually come down later this year. If we were to see a peak in the current rate cycle, there would likely be scope for a property market recovery in Hong Kong.
- Market performance softened in June, owing to the absence of any major policy announcements in China and heightened geopolitical tensions. We also believe the market is waiting for more policy signals from the Third Plenum in mid-July and the Politburo meeting at the end of the month.
- If we were to see more favourable policies from the upcoming meetings that support a more sustainable macroeconomic improvement in China, there is certainly scope for a recovery in the Hong Kong stock market. The market is currently undervalued, and investors' positioning is very light.
- Portfolio construction remains focused on keeping a healthy level of diversification across growth and value ideas. We hold quality stocks that show value at the current level, and those longer-term growth ideas that are less cyclically exposed.

Past performance is not a guide to future performance and may not be repeated. 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	Target	Comparator
2023	-15.1	-12.7	-12.8
2022	-12.5	-7.0	-15.1
2021	-11.6	-4.1	-11.6
2020	21.2	7.5	11.4
2019	16.1	11.8	12.9
2018	-14.3	-10.2	-12.8
2017	50.5	36.3	40.7
2016	0.4	4.1	0.6

2015	-5.1	-4.3	-5.0
2014	4.2	2.2	1.6

Source: Schroders, net of fees, NAV to NAV, with net income reinvested. USD A Acc share class, as at 31 December 2023. The fund's performance should be assessed against its target benchmark being to exceed the FTSE Hong Kong (Net TR) index and compared against the Morningstar Hong Kong Equity Category. The fund's investment universe is expected to overlap to a limited extent with the components of the target benchmark. The comparator benchmark is only included for performance comparison purposes and does not have any bearing on how the investment manager invests the fund's assets.

## Risk considerations

**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.

**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.

**Derivatives risk – efficient portfolio management:** 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.

**Emerging markets & frontier risk:** Emerging markets, and especially frontier markets, generally carry greater political, legal, counterparty, operational and liquidity risk than developed markets.

**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:** 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 macroeconomic environment, investment objectives may become more difficult to achieve.

**Stock connect risk:** The fund may be investing in China "A" shares via the Shanghai-Hong Kong Stock Connect and Shenzhen-Hong Kong Stock Connect which may involve clearing and settlement, regulatory, operational and counterparty risks.

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