

# Schroder ISF\* EURO High Yield

Fund Manager: Hugo Squire | 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.
- 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.
- Third quarter economic growth for the eurozone was slightly better-than-expected while inflation remains broadly in line with the ECB's 2% target. The Eurozone Composite Purchasing Managers Index (PMI) for October recorded its strongest expansion in 17 months, with a sharp acceleration in services sector activity, although manufacturing output registered only a slight increase.
- In the US, the Federal Reserve 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.

## Drivers of fund performance

- The Fund posted a negative total return, underperforming the reference benchmark during October.
- The key detractor was our position in a German packaging company Kloeckner Pentaplast. News of a material profit warning was the catalyst for a substantial restructuring of the balance sheet, funded by bond holders.
- The holding in specialty chemical group Ineos weakened as the impact of overcapacity and higher energy costs continues to erode margins throughout the sector.
- Holdings in French commercial property group Foncia and UK debt collector Lowell also detracted, with the latter weakening on the prospect of a further restructuring.
- Contributors over the month included Mediterranean-focused gas exploration and production group Energean, boosted by the ceasefire in the Middle East.
- The holding in Branicks, an owner of German office and logistics assets, continued to perform well as recent progress on refinancing has been positive for bondholders.
- Security selection in automotives and subordinated banking had a positive impact on returns.
- Our underweight exposure to basic industries and portfolio protection contributed as well.

## 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.
- Among BB-rated securities, we acquired a holding in an issue of senior secured notes from Italian financial services group doValue, which is intended to fund an acquisition in Germany.

- We also added to our holding in Asda, which has a strong foothold in the competitive UK supermarket sector.
- We exited the holding in Kloeckner Pentaplast, following the recent profit warning.
- 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 bonds, mainly BBB-rated securities, which act as a buffer against market volatility.
- During October, we took profits on our holding in investment grade bonds issued by Spanish banking group Santander.
- Relative to the reference benchmark, the Fund has an overweight allocation to the real estate, energy and financial services sectors. Significant underweight allocations are in autos, telecoms and basic industries.

## Outlook/Positioning

- 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.
- We remain positive on the economic outlook for the eurozone, as manufacturing growth is improving from low levels and the labour market remains strong. 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 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 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 (%)

	A Acc	I Acc	Target
2024	10.9	12.3	8.6
2023	11.8	13.1	12.0
2022	-13.9	-12.9	-11.5
2021	4.5	5.8	3.3
2020	4.2	5.6	2.7
2019	9.8	11.1	11.2
2018	-5.5	-4.4	-3.6
2017	6.7	8.0	6.7
2016	10.0	11.4	9.1
2015	3.5	4.8	0.7

Source: Schroders, as at 31/12/2024. All performance net of fees (where applicable), NAV to NAV (bid to bid), EUR. Target : ICE BofA Euro High Yield Constrained Index.

## 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.

- **Currency risk / hedged share class:** 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. 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.
- **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.
- **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.
- **Sustainability risk:** The fund has environmental and/or social characteristics. This means it may have limited exposure to some companies, industries or sectors and may forego certain investment opportunities, or dispose of certain holdings, that do not align with its sustainability criteria. Therefore, the fund may underperform other funds that do not apply similar criteria. The fund may invest in companies that do not reflect the beliefs and values of any particular investor.

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