

# Schroder ISF\* EURO High Yield

Fund Manager: Hugo Squire | Fund update: June 2024

## Performance overview

- Although credit markets generated positive returns, the performance of corporates lagged government bonds, with spreads widening across the board. European bond markets particularly were unsettled by the announcement of elections in France. Amongst European high yield bonds, credit spreads widened throughout the market, apart from the interest rate sensitive real estate sector which saw a further significant compression.
- As expected, the European Central Bank (ECB) announced a 25bp cut in the deposit rate - the first since 2019. The accompanying statement and upgrade to inflation forecasts were interpreted by the bond markets as relatively hawkish. However, the major market-moving event was around political developments in France where government bonds rose over the month after President Macron unexpectedly called parliamentary elections. The first round of voting at the end of June highlighted strong support for the hard right National Rally (RN). Additionally, the formation of a left-wing alliance generated greater uncertainty, not only about the outcome of the parliamentary elections, but also highlighted concerns about France's already unstable fiscal position.
- The 10-year US Treasury yield declined from 4.50% to 4.41% at the end of the month. The German 10-year bund yield fell from 2.65% to 2.49%. In contrast, equivalent French yields rose from 3.15% to 3.29%, while fiscal concerns also impacted in Italy, where the 10-year government bond yield rose from 3.99% to 4.06%.

## Drivers of fund performance

- The fund outperformed the ICE BofA Euro High Yield Constrained index in June.
- A tactical hedging trade to protect the portfolio against near-term market weakness was the main factor that made a positive contribution during June, as political uncertainty in France triggered a sell-off in bond markets.

- Security selection in the media, financial services, basic industries and autos sectors was additive over the month.
- In the media sector, our holding in a German cable TV and internet provider performed well following an encouraging trading update.
- Amongst financial services providers, our position in a leading credit management services company made a positive contribution on a proposal for a restructuring to cut debt levels was well received by investors.
- Security selection the energy and healthcare sectors detracted.

## Portfolio activity

- In the primary market, we participated in an issue of from an oil services business secured as first lien senior debt.
- We added to our holding in a hybrid issue from a large European manufacturer of railway carriages. The announcement of a rights issue to reduce debt levels is a positive development for the company's credit outlook.
- Over the month, we increased the allocation in off-benchmark investment grade bonds, focused on BBB-rated issues.
- We reduced exposure to cyclical sectors, taking profits on our holding in a UK specialty chemicals group, as well as holdings in the autos sector.
- Overall, we reduced the allocation to securities with a single-B credit rating given the compression in spreads over recent months.
- We continue to limit the sensitivity of the portfolio to changes in credit spreads, with active spread duration at the lower end of its permitted range, as a buffer against market volatility.

## Outlook/Positioning

- Looking at the outlook for European credit markets, the macroeconomic backdrop is supportive with Eurozone growth on a gradually improving trajectory while the corporate sector is in a healthier financial shape. Nevertheless, we have become more cautious

on the near-term prospects for credit given both the speed and the extent of spread compression

- We have seen peak tightness of financial conditions and the European Central Bank is expected to loosen its monetary policy, however less than expected at the beginning of the year.
- After delivering its first interest rate cut in June, we concur with market expectations for only two further rate cuts from the ECB over the second half of this year as services sector inflation remains sticky.
- In the European high yield sector, we are looking to corporate actions, such as asset sales and debt restructuring, for investment opportunities particularly in the primary market. Debt refinancing is progressing at a pace which continues to run ahead of maturity schedules, presenting several opportunities to participate in new issues on attractive yields. We remain particularly mindful of credit risk amongst CCC-rated issues, and have maintained a high selectively approach in this segment of the bond market.

*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
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
2014	5.0	6.3	5.4

Source: Schroders, as at 31/12/2023. 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.

## Important information

Marketing material for professional clients only. This document does not constitute an offer to anyone, or a solicitation by anyone, to subscribe for shares of Schroder International Selection Fund (the "Company"). Nothing in this document should be construed as advice and is therefore not a recommendation to buy or sell shares. An investment in the Company entails risks, which are fully described in the prospectus. Subscriptions for shares of the Company can only be made on the basis of its latest Key Investor Information Document and prospectus, together with the latest audited annual report (and subsequent unaudited semi-annual report, if published), copies of which can be obtained, free of charge, from Schroder Investment Management (Europe) S.A. These documents may be obtained in English, free of charge, from the following link: [www.eifs.lu/schroders](http://www.eifs.lu/schroders). Information for Switzerland: Schroder Investment Management (Switzerland) AG is the Swiss representative («Swiss Representative») and Schroder & Co Bank AG is the paying agent in Switzerland of the Luxembourg domiciled Schroder International Selection Fund. The prospectus for Switzerland, the key information documents, the articles of association and the annual and semi-annual reports may be obtained free of charge from the Swiss Representative. For Luxembourg, these documents can be obtained in English at [www.schroders.lu](http://www.schroders.lu). For the UK, these documents can be obtained in English, free of charge, from the Facilities Agent Schroder Investment Management Ltd, 1 London Wall Place, London EC2Y 5AU or at [www.schroders.co.uk](http://www.schroders.co.uk). Schroders may decide to cease the distribution of any fund(s) in any EEA country at any time but we will publish our intention to do so on our website, in line with applicable regulatory requirements. The fund has environmental and/or social characteristics within the meaning of Article 8 of Regulation (EU) 2019/2088 on Sustainability-related Disclosures in the Financial Services Sector (the "SFDR"). Any reference to sectors/countries/stocks/securities are for illustrative purposes only and not a recommendation to buy or sell any financial instrument/securities or adopt any investment strategy. 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 amounts originally invested. Exchange rate changes may cause the value of investments to fall as well as rise. Schroders has expressed its own views and opinions in this document and these may change. Schroders uses SustainEx™ to estimate the net impact of an investment portfolio having regard to certain

sustainability measures in comparison to a product's benchmark where relevant. It does this using third party data as well as Schroders own estimates and assumptions and the outcome may differ from other sustainability tools and measures. Third party data including MSCI data is owned or licensed by the data provider and may not be reproduced or extracted and used for any other purpose without the data provider's consent. Third party data is provided without any warranties of any kind. The data provider and issuer of the document shall have no liability in connection with the third party data. The terms of the third party's specific disclaimers, if any, are set forth in the Important Information section at [www.schroders.com](http://www.schroders.com). Schroders will be a data controller in respect of your personal data. For information on how Schroders might process your personal data, please view our Privacy Policy available at [www.schroders.com/en/privacy-policy/](http://www.schroders.com/en/privacy-policy/) or on request should you not have access to this webpage. A summary of investor rights may be obtained from <https://www.schroders.com/en/lu/professional-investor/footer/complaints-handling/>. For your security, communications may be recorded or monitored. Distributed in the UK by Schroder Investment Management Ltd, 1 London Wall Place, London EC2Y 5AU. Registration No 1893220 England. Authorised and regulated by the Financial Conduct Authority.