

Schroder ISF* EURO High Yield

Fund Manager: Hugo Squire | Fund update: April 2025

Performance overview

- April was a volatile month for all financial assets, including European credit markets. So called 'Liberation Day' saw President Trump unveiling larger and broader-based tariffs than expected (a 10% tariff rate on all US imports and higher reciprocal tariffs for countries with which US has large trade deficit). Facing negative market ramifications, he later suspended some tariffs imposed on most nations for 90 days. Simultaneously trade tensions with China escalated.
- In euro high yield (HY) credit markets, spreads peaked at their widest levels year-to-date in what was a traditional 'risk-off' move. A subsequent improvement in risk sentiment on the back of softer political headlines drove a partial retracement in spreads. Total returns in euro HY were positive over the month, outperforming US HY markets.
- Risk averse sentiment was also reflected in the marked weakness of the lower tier of the investment grade market, with higher yielding BBB rated credits significantly underperforming those rated single-A.
- European government bond markets fared relatively well in comparison with US Treasuries, with yields falling across all eurozone markets. Falling eurozone inflation, which decreased to 2.2% in March, enabled the European Central Bank (ECB) to implement a further 25bps interest rate cut in April, bringing the deposit rate to 2.25%. The key message was that disinflation is "well on track", while growth uncertainty has increased.

Drivers of fund performance

- The fund posted a negative total return, underperforming the ICE BofA Euro High Yield Constrained index in April.
- An overweight position in the energy sector detracted, as oil prices fell sharply. The drop in prices was due to a combination of increased supply from the OPEC+ Countries, with production set to rise substantially in May, and concerns that US trade tariffs will significantly weaken the global economy.
- An emphasis on single-B rated and CCC-rated issues detracted over the month as spreads decompressed.

- A substantial underweight position in the autos sector made a positive contribution as the announcement of US trade tariffs triggered a sharp sell-off among both auto manufacturers and component suppliers.

Portfolio activity

- During April, we added exposure to the energy sector on weakness, increasing the holding in Kosmos Energy which has recently commenced liquefied natural gas production from a joint venture with BP off the west African coast.
- Similarly, we continue to favour subordinated insurance issues where favourable solvency ratios underpin credit quality. We added to the holding in Dutch insurer Achmea, while also establishing a new holding in single-A rated debt from Nippon Life Insurance.
- We took profits on holdings in satellite operator Eutelsat, Telecom Italia and Almagora – an Italian digital technology group.
- On valuation criteria, we hold a significant underweight allocation to BB-rated issues.
- We remain comfortable with our barbell strategy and a reduced risk profile, maintaining investment grade BBB exposure and overweight to single-B and CCC rated issues.
- We added new single-B holdings in the financing vehicle of UK pharmaceutical company Advanz and Spanish hotel chain Servatur, while increasing our position in healthcare technology group Helios Software.
- The narrowing differential in credit spreads between BB and BBB-rated securities shifts the risk/return profile in favour of the latter, while also acting as a buffer against market volatility.
- Accordingly, we have maintained a significant allocation to investment grade corporate bonds, adding BBB-rated holdings during April in closed-end fund Pershing Square and technology investment group Prosus.

Outlook/Positioning

- The immediate prospects for the eurozone economy are heavily contingent on the outcome of trade negotiations with the US, following the introduction

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and subsequent suspension of significant tariffs in early April.

- Although conditions in the manufacturing sector remain challenging, the eurozone PMI (purchasing managers index) is now signalling potential expansion. This improvement appears to be a response to the European Commission's recent relaxation of fiscal rules, allowing for additional spending on defence. Furthermore, Germany's easing of the 'debt brake', alongside the recent announcement of a €500bn infrastructure and defence fund, has increased optimism within the manufacturing and industrial sectors.
- Monetary policy should continue to provide some support for European bond markets, with investors anticipating further ECB rate cuts over the coming months, with interest rates projected to stabilise around 1.75% by the year end.
- Credit markets have already responded sharply to the change in outlook. The dramatic market moves in recent weeks, and the outperformance of European corporates over the US, leads us to maintain a strong emphasis on quality and a cautious approach to investing in more cyclical sectors, particularly autos. Going forward, we are looking for opportunities in companies with business models that are mostly insulated from the trade uncertainty.
- The volatility in April has improved valuations in euro credit and the dispersion in the market. In such circumstances investment opportunities arise, particularly where markets are mispricing a substantial change in outlook. However, we remain very mindful of credit risk particularly in view of the economic

uncertainty. Going forward, a combination of positive carry and idiosyncratic opportunities should underpin total returns from the European high yield 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
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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