

Schroder ISF* Sustainable EURO Credit

Fund Manager: Saida Eggerstedt | Fund update: June 2025

Market review

- Despite geopolitical headlines dominating news flow during June, with the conflict in the Middle East and a spike in oil prices driving market uncertainty, it was another positive month for credit markets. Spreads in the euro investment grade (IG) market tightened further, generating excess returns over government bonds.
- In the euro IG credit market, fund remain strong, focused on the shorter dated maturity segment which have attracted further inflows as the European Central Bank (ECB) has continued to reduce interest rates. In addition, Asian investors looking to diversify away from the US have been increasing exposure to higher yielding credit.
- Meanwhile, although concerns over an imminent recession remain low as monthly eurozone composite PMI (purchasing managers index) is still anchored above the expansionary threshold, growth throughout the region is still muted. So far, there is little sign of tariff-related inflation with the eurozone core consumer price index remaining steady at 2.3% in June. Significantly, the strength of the euro year-to-date against the US dollar appears to be offsetting any wider price pressures.
- As expected, the ECB cut interest rates to 2% in early June, while signalling that it is now near the end of its rate-cutting cycle. Accordingly, investors scaled back expectations for further rate cuts, with just one further reduction now anticipated during the second half of the year. Attention is now shifting away from monetary policy towards the potential impact from fiscal policy.
- In contrast to other sovereign markets, European government bond yields rose in June, notably in Germany, as investors awaited more clarity on forthcoming trade tariffs.

Drivers of fund performance

- The fund delivered positive returns over the month and outperformed the reference index (net of fees). Meanwhile, the fund continues to deliver on Sustainability performance metrics including a high SustainEx™ overall impact score and MSCI ESG rating.
- Security selection contributed positively to active returns, with notable gains in real estate, junior subordinated banking, telecommunications, and services. Additionally, overweight positions in lower tier 2 insurance and tier 1 banking provided further positive impact.
- While there were few relative detractors, performance was negatively affected by security selection in senior financial services as well as underweight allocations to energy and senior banking.

Portfolio activity

- Throughout the month, we increased our exposure to senior banking, tier 2 banking, utilities, telecommunications, senior financial services, among others. In contrast, we reduced our exposure to media and healthcare.
- Our investment strategy focuses on a broad range of sustainable themes and bonds, including waste recycling and biodiversity, sustainable infrastructure, the circular economy, and responsible consumption. We also prioritize opportunities in decarbonizing technology and health and education. In alignment with our commitment to sustainability, we exclude investments in fossil fuels, weapons, alcohol, tobacco, and companies that violate the UN Global Compact.
- The fund increased holdings in green bonds within utilities, such as a British energy provider and a Danish company that transitioned from coal-intensive operations to global renewable energy leadership in under a decade.
- Elsewhere, we remain invested in our preferred responsible finance names, including green, social, and sustainability-linked bonds issued by UK and European companies.
- The fund's carbon emissions intensity, as measured by tonnes CO2e per \$mn sales (scope 1 and 2 emissions), is less than half that of the reference index. Additionally, our overall SustainEx™ impact score remains significantly higher, as we strive to identify improvers, limit laggards, conduct ESG research, utilize tools, and focus on positive sustainability themes.

Outlook

- The immediate prospects for the eurozone economy are heavily contingent on the outcome of trade negotiations with the US, the impact of higher fiscal spending and more accommodative monetary conditions. Although conditions in the manufacturing sector remain challenging, the eurozone PMI is signalling potential expansion with the latest survey for June highlighting expansion across the manufacturing and services sectors. 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.
- Inflation is expected to decline further based on lower energy prices, as the recent spike in the oil price quickly dissipated, and the weaker US dollar.

- We also expect corporate fundamentals to remain stable and the default rate to stay low.
- Monetary policy should continue to provide some support for bond markets, with interest rates projected to stabilise around 1.75% by the year end.
- Bond markets have already responded sharply to the change in outlook. The market moves in recent weeks lead us to maintain a strong emphasis on quality and a generally cautious approach to investing in more cyclical sectors. While industrials should benefit from increased infrastructure and defence spending in Germany, this has already been largely discounted by investors.
- In addition, we are also looking to identify companies with business models that are mostly insulated from the ongoing trade uncertainty. We see idiosyncratic opportunities both in higher yielding issuers and single A-rated names.
- Overall, we remain very mindful of credit risk particularly in view of prevailing economic uncertainty and tighter credit spreads. Going forward, a combination of positive carry and idiosyncratic opportunities should underpin total returns from European credit markets. For now, uncertainty persists, which makes an agile approach to portfolio construction crucially important.

Calendar year performance (%)

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.

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.

| | C Acc | A Acc | I Acc | Target** |
|------|-------|-------|-------|----------|
| 2024 | 5.6 | 5.2 | 6.3 | 4.7 |
| 2023 | 8.3 | 7.8 | 8.9 | 8.0 |
| 2022 | -12.4 | -12.7 | -11.8 | -13.9 |
| 2021 | 0.7 | 0.3 | 1.3 | -1.0 |
| 2020 | 5.6 | 5.2 | 6.2 | 2.6 |
| 2019 | - | - | - | - |
| 2018 | - | - | - | - |
| 2017 | - | - | - | - |
| 2016 | - | - | - | - |
| 2015 | - | - | - | - |

Source: Schroders, as at 31/12/24. All performance net of fees (where applicable), NAV to NAV (bid to bid), EUR. ** ICE BofAML Euro Corporate TR.

Risk considerations

ABS and MBS risk: The fund may invest in mortgage or asset-backed securities. The underlying borrowers of these securities may not be able to pay back the full amount that they owe, which may result in losses to the fund.

Contingent convertible bonds: The fund may invest in contingent convertible bonds which are bonds that convert to shares if the bond issuer's financial health deteriorates. A reduction in the financial strength of the issuer 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: If a borrower of debt provided by the fund or a bond issuer experiences a decline in financial health, their ability to make payments of interest and principal may be affected, which may cause a decline in the value of the fund.

Currency risk: If the fund's investments are denominated in currencies different to the fund's base currency, the fund may lose value as a result of movements in foreign exchange rates, otherwise known as currency rates. If the investor holds a share class in a different currency to the base currency of the fund, investors may be exposed to losses as a result of movements in currency rates.

Currency risk / hedged share class: The currency 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, which are financial instruments deriving their value from an underlying asset, may be used for investment purposes and/ or 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.

High yield bond risk: High yield bonds (normally lower rated or unrated) generally carry greater market, credit and liquidity risk meaning greater uncertainty of returns.

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, meaning investors may not be able to have immediate access to their holdings.

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 the objective of sustainable investment. 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 chosen by the investment manager. The fund may invest in companies that do not reflect the beliefs and values of any particular investor.

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