

Schroder ISF* US Small & Mid Cap Equity

Fund Manager: Robert Kaynor, CFA | Fund update: Q2 2024

Performance overview

- The second quarter of 2024 saw mixed performances in major US equity indices.
- The fund underperformed the benchmark during the quarter.

Drivers of fund performance

- Stock selection and sector allocation contributed positively to performance while style factors detracted.
- The top contributors from a sector perspective were consumer discretionary, industrials and financials. Within consumer discretionary, stock selection in the hotels, restaurants and leisure industry groups added the most value. **Aramark** was a top performer as it reported strong revenues and profits. Industrials was led by stock selection within the marine transportation and professional services groups. In financials, the capital markets sub-sector performed well, with **PJT Partners** leading the way after reporting first-quarter results that surpassed market expectations. The fund's exposure to insurance also benefited performance..
- The top detractors for the quarter were communication services, real estate and consumer staples. Communication services lagged due to stock selection primarily in the interactive media and services group. The fund's real estate stocks underperformed because of exposure to specialised REIT stocks, specifically timber REITs. **PotlatchDeltic** declined as consumers and homebuilders have spent less on timber because interest rates have stayed higher for longer. Consumer staples detracted due to both stock selection and sector allocation. **Darling Ingredients** was a weak performer owing to a combination of lower seasonal volumes, operational outages and persistent weakness in both DGD (diamond green diesel) and feed margins.
- In terms of the alpha sources¹, "mispriced growth", "steady eddies" and "turnarounds" all outperformed.
- Major contributors included **Kirby Corporation**, **Stericycle** and **MACOM Technologies Solutions**.
- Major detractors included **Regal Rexnord**, **Viavi Solutions** and **Hayward Holdings**.

Portfolio activity

- We added **Informatica** and **Iridium Communications**.
- We exited **Stericycle** and **Etsy**.

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 (%)

Year	Fund	Target	Comparator 1	Comparator 2
2023	12.2	11.3	18.4	15.0
2022	-13.3	-18.5	-20.4	-13.0
2021	21.6	17.8	19.4	24.4
2020	6.8	20.4	22.4	13.0
2019	28.9	28.6	29.9	26.7
2018	-12.4	-11.5	-10.8	-12.9
2017	15.2	17.2	16.1	15.9
2016	17.6	16.4	13.6	19.4
2015	0.7	-3.2	-2.6	-2.7
2014	11.6	7.8	8.3	10.8
2013	35.0	38.4	37.7	34.6
2012	9.1	14.7	12.0	15.0

Source: Schroders, net of fees, NAV to NAV, with net income reinvested. USD C Acc share class as at 31 December 2023. The fund's performance should be assessed against its target benchmark being to exceed the Russell 2500 Lagged (Net TR) index and compared against the Morningstar US MidCap Equity Category and the S&P Mid Cap 400 Lagged (Net TR) Index. The fund's investment universe is expected to overlap materially with the components of the target benchmark and the S&P Mid Cap 400 Lagged (Net TR) Index. The comparator benchmarks are only included for performance comparison purposes and does not determine how the investment manager invests the fund's assets. The investment manager invests on a discretionary basis and there are no restrictions on the extent to which the Fund's portfolio and performance may deviate from the target benchmark or the S&P Mid Cap 400 Lagged (Net TR) Index. The benchmark(s) does/do not take into account the environmental and social characteristics or sustainable objective (as relevant) of the fund. Please see appendix III of the fund's prospectus for further details.

¹ We target three types of opportunities: "mispriced growth stocks" – stocks where we think the market continues to undervalue a company's growth prospects; "steady eddies" – strong companies with recurring revenues and/or cashflows; and "turnarounds" – firms that are addressing their problems, often with new management, which are likely to outperform over time.

Outlook/positioning

- The magnitude of the discrepancy between mega-cap and small/mid-cap performance during the first half of the year means small and mid-caps are recording their greatest period of underperformance in history. Momentum can take time to shift, especially when investors want their capital to stay in dollars and deem investing in US mega-cap technology stocks more favourable than long-duration Treasuries.
- However, there are reasons the tide could turn, especially if mega-cap stocks start to fall short of ever-increasing expectations or earnings growth begins to slow. The high valuation of the semiconductor sector is anchored on the belief that the pace of sales growth will continue indefinitely. The cyclical and capital-intensive nature of the sector makes this unlikely. Encouragingly for small and mid-caps, consensus estimates are forecasting an inflection in relative earnings growth that favours this part of the market, beginning this quarter and proceeding into 2025.
- Earnings revisions are starting to turn more positive in aggregate. This should continue as interest rates peak and borrowing costs fall, as they have done for two consecutive months. High-yield spreads remain supportive of capital flows and capital markets appear to be opening up, allowing companies to secure necessary funding and refinancing.
- When speaking to our companies, we have been hearing signs of a slowing economy, making it no surprise that this is beginning to show up in government data, which always lags. Consumer spending is patchy and more focused on trading down in price or being much more selective. Business activity is still benefiting from the large fiscal stimulus, but investors need to be selective on where they allocate capital at this part of the cycle. We favour companies exposed to fiscal stimulus initiatives and those that have seen inventories and supply chains destocked after the Covid-related supply-chain challenges.
- The second half of the year will not be without obstacles, including elevated geopolitical risk, challenging earnings comparisons, high expectations for market leaders and a hurricane season that could be significantly worse than normal. We anticipate more volatility in markets, which of course creates risk and opportunity.

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.

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.

Currency risk: The fund may lose value as a result of movements in foreign exchange rates.

Currency risk / hedged shareclass: 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.

Fund Disclosure: SIF US Small & Mid-Cap Equity: The fund invests primarily in equity and equity related securities of small and mid-sized US companies. - The fund invests in equity would subject to equity investment risk. - The fund invests in concentrated region/sector and subjects to higher level of risks than a fund investing

in a more diversified portfolio/strategy. - The fund may invest in smaller companies which are relatively less liquid and more volatile than larger companies. - The fund may use derivatives to meet its investment objective. Derivatives exposure may involve higher counterparty, liquidity and valuation risks. In adverse situations, the fund may suffer significant losses from their derivative usage for hedging. - For share classes with a general dividend policy, expenses will be paid out of capital rather than out of gross income. The amount of distributable income therefore increases and the amount so increased may be considered to be dividend paid out of capital. Share classes with a fixed dividend policy may pay out both income and capital in distributions. Where distributions are paid out of capital, this amounts to a return or withdrawal of part of your original investment or capital gains attributable to that and may result in an immediate decrease in the net asset value of shares. You should not make any investment decision solely based on this document. Please read the relevant offering document carefully for further fund details including risk factors.

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.

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.

Smaller companies risk: Smaller companies generally carry greater liquidity risk than larger companies, and they may also fluctuate in value to a greater extent.

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 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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