



December 2011

Quarterly Report

# Schroder Global Smaller Companies Fund

## Total return %

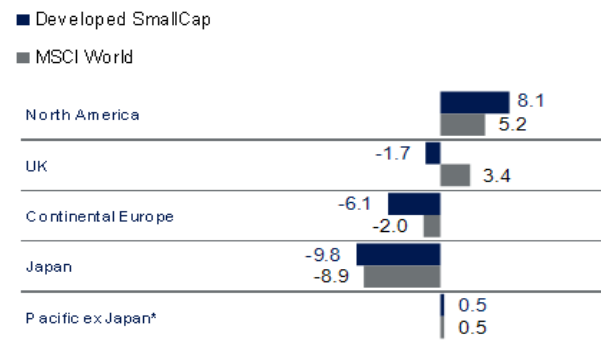
Schroder Global Smaller Companies Fund (post-fee)	
S&P Developed Ex-Australia SmallCap	
<b>Relative performance (post-fee)</b>	
Schroder Global Smaller Companies Fund (pre-fee)	
S&P Developed Ex-Australia SmallCap	
<b>Relative performance (pre-fee)</b>	

	3 mths	1 yr	3 yrs p.a.	5 yrs p.a.	Inception p.a.
Schroder Global Smaller Companies Fund (post-fee)	2.2	-9.4	1.5	-5.2	5.9
S&P Developed Ex-Australia SmallCap	2.1	-8.3	2.3	-6.2	5.2
<b>Relative performance (post-fee)</b>	<b>0.1</b>	<b>-1.1</b>	<b>-0.8</b>	<b>1.0</b>	<b>0.7</b>
Schroder Global Smaller Companies Fund (pre-fee)	2.5	-8.3	2.8	-4.1	7.0
S&P Developed Ex-Australia SmallCap	2.1	-8.3	2.3	-6.2	5.2
<b>Relative performance (pre-fee)</b>	<b>0.4</b>	<b>0.0</b>	<b>0.5</b>	<b>2.1</b>	<b>1.8</b>

Inception Date: 28 October 1996

Past performance is not a reliable indicator of future performance  
Please refer to [www.schroders.com.au](http://www.schroders.com.au) for post-tax returns

## S&P / MSCI quarterly returns by region %



\* Includes Australia and New Zealand  
Source: S&P, MSCI

## Top ten holdings %

Country	Stock	Fund
US	Questar	1.1
US	Energen	1.1
US	Silgan Holdings	1.0
US	Amdocs	1.0
US	Crown Holdings	1.0
US	Airgas	1.0
US	Cleco	1.0
US	Partnerre	0.9
US	Big Lots	0.9
US	Comerica	0.8
<b>Total</b>		<b>9.8</b>

## Characteristics

	Fund	Benchmark
Number of securities	407	5,791
P/E 12mths Fwd (x)	14.1	15.8
Dividend yield (%)	1.5	1.7
Price/book (x)	2.1	1.8
3 year earnings growth (%) p.a.	11.9	13.8
Return on equity (%)	13.2	12.4
Market capitalisation (%)		
>A\$7 billion	3.4	1.0
A\$3-7 billion	32.8	19.1
<A\$3 billion	63.8	79.9
5 Yrs Standard Deviation (%)	12.9	14.4
5 Yrs Historic Tracking error (%)	3.8	

Unless otherwise stated figures are as at the end of December 2011  
Benchmark is the S&P Developed Ex-Australia SmallCap  
Please note numbers may not total 100 due to rounding

## Commentary

After the sharp market corrections of the third quarter, the last three months have seen much volatility and a modest rise in the level of equity indices, with the S & P Developed ex Australia Smallcap Index up 2.1% overall. The financial crisis in Europe continued to grab its full share of headlines, but developments elsewhere were modestly supportive for sentiment, including US data modestly ahead of general expectations, selective easing of interest rates and credit conditions in a number of emerging economies (responding in part to weaker commodity led inflationary pressures and slowing economies) and further round of quantitative easing/currency interventions (United Kingdom, Japan, Switzerland).

Smaller company stocks have, however, performed inline with their larger peers, with the MSCI World Index also registering a 2.1% rise. With smallcaps often seen as riskier, it is unsurprising that the gravitation towards larger companies was marked in Europe where smallcap industrials and consumer cyclical performed poorly, while in the United Kingdom the larger cap integrated energy stocks did well along with defensive yield plays in health care, consumer products and telecommunications.

Smallcaps fared slightly better in Asia relative to their larger peers, although absolute returns in Japan were disappointing, as much a function of consolidation following the strong relative showing in the third quarter. Smallcaps in the rest of Asia kept pace with larger peers, led by energy, information technology and utilities.

In North America both large and smallcaps outperformed the rest of the world as economic data surpassed downbeat expectations. Smallcaps outperformed large led by financials and information technology stocks recouping some of the underperformance earlier in the year.

## Fund Review

The Fund marginally outperformed the benchmark in the quarter primarily due to stock selection in North America and the UK as well as the underweighting in Japan. The main negative has been stock selection in Japan.

Positive selection in the United Kingdom was primarily due to holdings in the industrial (Hamworthy following an offer for the company, and Senior) and energy (Exillon, John Wood) sectors. Partial offsets came from information technology (RM, TT Electronics) and consumer cyclical (William Hill).

The main headwind for the Fund in Japan was selection in the more cyclical sectors such as consumer cyclical (Koito Manufacturing, Musashi Seimitsu), and industrials (Nitta, Trusco Nakayama), slightly offset by materials (Kureha) and a positive contribution from the sectoral positioning, primarily the underweighting in financials.

Overall performance in continental Europe was broadly inline with the benchmark, with positive selection in financials (Azimut, Forbo) telecoms (freenet) and I.T. (Kapsch Trafficom, Uster, LBI) offset by shortfalls in materials, industrials (gategroup, Eurotunnel, Imtech), and energy (Fugro, Bourbon).In

Pacific ex Japan stock selection was positive in Singapore (STX OSV, Biosensors, First Resources) and software company Shanda Games. The main offsets were selection in Korea (BS Financial) and battery manufacturer Leoch in Hong Kong.

In North America our positive stock selection came from our positions in consumer discretionary with Bally Technologies and Rent-A-Center performing strongly after reporting better than expected results. Materials (Airgas, Reliance Steel & Aluminium), information technology (Verisign, Newstar, Arrow) and telco (SBA Communications) selections all added value. M&A remained a theme with Pharmaceutical Product Development, a healthcare CRO being acquired by private equity. These positives more than offset the negatives coming from our industrial (Republic Services, Waste Connections) companies.

## Regional exposure versus the benchmark

Fund (%)	Index (%)			3 month change in active weight (%)
9.8	4.8	Pacific ex Japan	5.0	+1.0
8.0	8.9	UK	-0.9	+0.1
57.3	59.2	North America	-1.9	+2.4
7.5	9.9	Japan	-2.4	+0.1
14.3	17.2	Continental Europe	-2.9	-2.5
3.1	0.0	Cash	3.1	-1.1

## Quarterly attribution

Relative performance (pre-fee)	Stock selection	Country allocation	Total*
North America	0.8	0.0	0.8
UK	0.2	0.1	0.3
Japan	-0.2	0.3	0.1
Continental Europe	0.0	0.0	0.0
Pacific ex Japan	0.2	-0.2	0.0
Cash	-	-0.6	-0.6

\*Contribution to performance relative to S&P Developed SmallCap World Index (ex Australia)

Source: Schroders

## Country changes - 3 months to December 2011

**North America** - Our underweight in North America continued to be reduced during the quarter with economic data surprising on the upside. Going forward risks to earnings remain but estimates are arguably more realistic following downgrades during the quarter. Corporates are in a robust financial position due to improved productivity and strong cashflows and this, in part, is leading to increased levels of M&A. We are now neutral health care having cut our position and also reduced our position in industrials. Our two biggest underweights are financials and consumer stocks although have reduced the size of the underweight to both.

**Continental Europe** - We reduced Europe (ex UK) during the period in favor of Asia and North America. There was little change to the policy of focusing on the core at the expense of the periphery. The continued deflationary pressures, weakening asset price and high unemployment, represents a difficult environment for more domestically oriented smaller companies. The sizeable portion of our exposure remains in industrials and consumer cyclicals primarily in core Europe and Scandinavia where operating conditions remain more favorable.

**UK** - We have added marginally to the United Kingdom but remain underweight. This appears the right balance between what remains a very tough domestic growth environment (fiscal retrenchment allied to a very accommodating monetary policy and high but falling inflation) and the breadth and wide opportunity set which UK smallcap represents. Merger and acquisition activity has been restrained although this may reflect the short-term impact of regulation rather than a slackening in underlying demand for good quality businesses. The emphasis of our portfolios remains upon good quality companies offering growth despite the subdued outlook with the main exposure in industrials, information technology and consumer cyclicals.

**Japan** - We have made little change to the underweight allocation to Japan. Growth will be relatively robust in 2012 thanks to reconstruction and easy comparisons, but this in itself is not that supportive of smallcap equities in our view. There is plenty of value, but continued absence of thoroughgoing corporate governance reform to unlock it. We retain an external exposure, not least due to the underweighting in financials.

**Pacific ex-Japan** - We have added to the (Pacific ex Japan) region, augmenting the degree of overweighting. Following the third quarter weakness, valuations are now decidedly below the long-term averages, and the prospects of slowing exports and lower earnings expectation appear well reflected. Leading indicator on inflation have improved, and there are early signs of some loosening in credit conditions in some countries. However, we continue to take a balanced approach between domestic demand stocks and exporters which look excellent value currently.

## Fund review continued

For the year as a whole, the fund performed in line with the Index. Stock selection was broadly in line with poor selection in the Pacific and continental Europe offset by strong selection in North America and the UK. Regional allocation was neutral with the negative from the overweighting in Pacific ex Japan and the underweight in North America offset by the underweight to continental Europe and holding any cash during the period.

## Outlook

The year opens amid enormous uncertainties for the global economy. The big fundamental issue is the excess leverage, estimated at some 20% of global GDP. The bulk of this debt burden resides within the developed economies, split in varying degrees between the private (primarily household) sectors and national governments. The most obvious manifestation is within the euro bloc, though this is largely a function of the strains within the currency union engendered by financial but not political and fiscal pooling of sovereignty. As this is essentially a political issue, the markets are justifiably sceptical that the will exists to face the hard decisions including fiscal transfers and/or a material reduction in the cost bases of the peripheral economies.

Challenges outside Europe (a fifth of global GDP) are less eye catching, but no less troubling. Recent economic statistics out of the United States have generally defied the sceptics, but can scarcely be described as robust, and are hostage also to political calculations, most notably whether the payroll tax credit and unemployment insurance are renewed. Meanwhile, among emerging markets, the prospect of an orderly slowdown in China remains unclear as the authorities attempt to defuse the debt and investment led boom of the last three years.

Reflecting these factors, we see OECD growth in 2012 at 0.3%, and it is growth of 4.5% in emerging markets (itself down from 6% in 2011) that is the key contributor to 2% growth in global economic activity. Within the developed world, there is a significant contrast between contracting Europe and modest positive growth in the United States and Japan.

The implications for equities are twofold; a challenging environment for revenue growth, and potential vulnerability in margins given currently high levels by historic standards. Some of this has been recognised both in the correction we have seen in markets since midyear, and the widespread downward revision in expectations for earnings growth in 2012. However, significant earnings risks remain, and we therefore continue to believe that it is important to maintain our focus upon companies with strong management, sound balance sheets and relatively visible growth prospects, though relative valuations suggest that some cyclical growth areas offer attractions on a longer-term view.

North America has been the bright spot globally from a market perspective helped by economic data surprising on the upside albeit from low expectations. The US is now entering a Presidential election year, which can be expected to have periodic impacts on the market but means it is unlikely that any major legislation will be enacted in 2012. With valuations less demanding and earnings more realistic following analyst cuts the size of our underweight to North America has been reduced by cutting the size of our underweights in consumer and financial stocks. Additions in the consumer sector included Liberty Media, BorgWarner and Asbury Automotive. Within consumer staples we bought Viterra the largest grain handler in Canada where the company is benefiting from the on going deregulation of the export market. New financials included CIT Group a commercial finance house who has restructured their balance sheet, reduced costs and has a good core business. Elsewhere we reduced industrials to an underweight position following sales of Shaw Group, ITT and moved healthcare down to a more neutral position following sales of Hospira and Amerigroup and the takeover of Pharmaceutical Product Development.

## Performance attribution – Periods to December 2011

Total returns	3 months	12 months	3 years	5 years
	%	%	% p.a.	% p.a.
Stock selection	0.9	1.1	1.3	2.0
Country weightings	-0.5	-1.4	-0.9	-0.1
Currency hedging	0.0	0.0	0.0	0.0
Residual	0.0	0.3	0.1	0.3
<b>Total value added</b>	<b>0.4</b>	<b>0.0</b>	<b>0.5</b>	<b>2.2</b>

Unless otherwise stated figures are as at the end of December 2011  
Benchmark is the S&P Developed Ex-Australia SmallCap

### Fund objective

To outperform the S&P Developed SmallCap World Index (ex Australia) over the medium to long term.

### Key features

- Large team of dedicated smaller companies analysts located regionally around the world combined with an experienced portfolio management team.
- Robust investment process and risk management framework.
- Access to the global smaller companies markets which are difficult for individual investors to access directly.
- Financial strength of the Schroders Group, with over 30 years history of investing in smaller companies worldwide.

### Fund details

#### Schroder Global Smaller Companies Fund

APIR code	SCH0008AU
Fund size (AUD)	\$120,476,437
Redemption unit price	0.6776
Fund inception date	October 1996
Buy / sell spread	0.50%/0.50%
Management costs	1.25%
Minimum investment	\$50,000
Distribution frequency	Normally twice yearly - June and Dec

### Outlook continued

Although Japan lagged in the fourth quarter, it has been a strong relative performer for 2011 as a whole. Its virtues as a perceived safe haven appeared less compelling particularly in the wake of the authorities' intervention to weaken the yen at the end of October, and the corporate scandal at Olympus places the spotlight on corporate governance weaknesses. Although Japan should register amongst the strongest growth among developed economies in 2012, much of this is a function of the fiscal boost of post-earthquake reconstruction and easy comparisons versus last year. We continue to see few attractive opportunities in the domestic sectors, while the sole new holding has been in Unipres, a producer of press processed auto-parts. This was partly funded by reductions in a number of other auto related holdings such as Nifco.

The macro outlook for Europe is undoubtedly challenging, and we have little to add to the wide range of views on how or whether then strains within the euro can be resolved without either a destabilizing break-up or intolerable strains on the peripheral economies. While we have reduced exposure over the quarter, attractive valuations and a wide opportunity set constrain a more marked underweight. The key exposures remain in the core markets, with the main focus on conservative financials (Helvetia, Delta Lloyd), globally oriented quality industrials (Imtech, gategroup, MTU Aero Engines) and consumer cyclicals, the latter split between global businesses such as Ipsos and Codere, and more domestic names with exposure to core Europe and Scandinavia (Statoil Fuel & Retail, Tom Tailor).

We remain underweight in the United Kingdom. Fiscal conservatism has been rewarded by the credit market despite debt and deficit levels which remain alarming. Concerted QE is providing some support to asset prices and with pessimism widespread there is scope for upside surprise. Corporate managements are generally realistic, and even in relatively challenged areas the stronger companies are exhibiting resilient results. M & A activity has been notably quieter although this may be as much due to some Take-over Code changes as a slackening of underlying appetite. New holdings included De La Rue (global security printing) and Debenhams the department store retailing group.

Pacific ex Japan remains our sole regional overweighting, with the focus upon Hong Kong, Singapore and Australasia. A fragile environment for global trade and negative economic and corporate earnings revisions is balanced by an improved inflation outlook (courtesy of subdued commodity prices), signs of policy easing in a number of countries and the relatively strong state of most of the regional economies external balances and banking systems. New holdings established over the quarter included Techtronic, the manufacturer of power tools and floor care products, and UOL Group, following measures by the Singapore government to cool the local real estate market. Outright sales included Shougang Concord given the deterioration in the visibility of its key end markets.

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Benchmark is the S&P Developed SmallCap World Index (ex Aus)

### Contact

[www.schroders.com.au](http://www.schroders.com.au)

E-mail: [simal@schroders.com](mailto:simal@schroders.com)

Schroder Investment Management Australia Limited

ABN 22 000 443 274 Australian Financial Services Licence 226473

Level 20 Angel Place, 123 Pitt Street, Sydney NSW 2000

Phone: 1300 136 471 Fax: (02) 9231 1119

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