Schroders

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Schroder ISF* European Large Cap

Fund Manager: Nicholette MacDonald-Brown | Fund update: February 2023

Performance overview

- Pan-European equities gained in February.
- The fund outperformed the MSCI Europe index.

Drivers of fund performance

- European shares extended their recent advance with further gains in February. Fears of a severe recession have abated, partly due to easing energy price pressures. The fund slightly outperformed the index, supported by stock selection in financials and consumer discretionary.
- Emerging markets focused lender **Standard Chartered** was the leading individual contributor. Banks continue to benefit from the rising interest rate environment and from valuations which remain attractive. Standard Chartered unveiled a $1 billion share buyback programme in February and increased its dividend. The bank also has been the subject of takeover interest from First Abu Dhabi Bank. Our positions in **Bank of Ireland**, **Intesa Sanpaolo**, and **SEB** also added value.
- Carmaker **Stellantis** was another positive contributor. The group announced a €1.5 billion share buyback alongside resilient full-year results.
- Ball bearings manufacturer **SKF** was another positive contributor. It released good Q4 results, showing that it has now been able to put through price rises to offset the higher cost of components. This has resulted in better profit margins. SKF is also benefitting from China's re-opening and signs of an improved economic backdrop in the US and Europe. Meanwhile, activist investor Cevian is pushing SKF to review its portfolio.
- Not owning certain mega cap stocks was also favourable for relative returns. Mega caps outperformed last year but lagged in February so the portfolio's lack of exposure to Roche, ASML Holding and LVMH added value.
- The main individual detractor was **Software AG**. The group is still investing in its transition to the cloud, and to a Software as a Service model. This means the anticipated improvement in profit margins has been delayed.
- Lack of exposure to the oil & gas sector also weighed on fund returns as the energy sector performed well.
- Mining group **Anglo American** was another detractor in the wake of its full-year results. The firm announced a $1.7 billion writedown to its Woodsmith polyhalite project due to change to the scope of the project.

Portfolio activity

- We have initiated a new position in **Siemens Energy**. It specialises in power equipment such as gas turbines, wind turbines and transmission networks. Siemens Energy is a play on the need for energy security as well as the transition to renewable energy. It recently took full control of wind turbine specialist Siemens Gamesa, which accounts for around half of the business. Orders have been strong but, like the whole wind turbine peer group, Siemens Gamesa has suffered supply chain disruptions, logistics problems and rising costs leading to losses on fixed price contracts. We see profits recovering from 2024 as supply chain issues ease and average selling prices move up.
- Another new holding is **Worldline**. The shares had de-rated following Worldline's acquisition of Ingenico as the market had doubts about the price paid and some of Ingenico's legacy technology. However, Worldline is selling the Ingenico terminals business, which allays some of those worries. Worldline continues to grow market share, adding new merchants to its network. It is a beneficiary of inflation as this adds to its own sales growth.

Outlook/positioning

- After a poor 2022, European shares have been strong in recent months. The economy has proved more resilient than feared. The latest eurozone purchasing managers' indices were back above 50, indicating growth.
- Inflation may be at its peak, although the European Central Bank has signalled its intention to keep tightening monetary policy. Gas prices have fallen amid warmer weather and energy saving measures, reducing the pressure on corporates and consumers. The earnings season is still ongoing in Europe but has been encouraging so far.

*Schroder International Selection Fund is referred to as Schroder ISF throughout

- We think markets this year are unlikely to experience the extreme dispersion that was such a feature of last year. Higher rates are likely to support value over growth but we anticipate the difference between the two styles will be more muted. Similarly, last year's large outperformance of large cap stocks as opposed to small or mid-caps is unlikely to be repeated.

In a more normal market environment, with muted dispersion, stockpicking will come to the fore. We take risk at the individual stock level rather than by sector or style. Our Blend approach means we are not relying on taking large style or factor bets, but focus instead on individual mispriced opportunities while retaining diversification.

Calendar year performance (%)

	Fund	Target	Comparator
2022	-14.5	-9.5	-13.1
2021	16.8	25.1	23.0
2020	1.1	-3.3	-0.9
2019	24.0	26.7	24.5
2018	-13.0	-10.9	-12.7
2017	10.0	10.2	10.1
2016	2.1	2.6	-0.2
2015	13.1	8.2	11.1
2014	1.8	6.8	5.6
2013	22.8	19.8	19.8

Source: Schroders, as at 31 December 2022. Fund performance is net of fees, NAV to NAV with net income reinvested, EUR C Acc. Please see factsheet for other share classes. The fund's performance should be assessed against its target benchmark being to exceed the MSCI Europe (Net TR) index, and compared against the Morningstar Europe Large Cap Blend Equity Category. 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 benchmark. The investment manager will invest in companies or sectors not included in the benchmark in order to take advantage of specific investment opportunities.

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 amount originally invested.

Risk considerations

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.
Currency risk: The fund may lose value as a result of movements in foreign exchange rates.
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.
Higher volatility risk: The price of this fund may be volatile as it may take higher risks in search of higher rewards.
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.
Market Risk: The value of investments can go up and down and an investor may not get back the amount initially invested.
Operational risk: Failures at service providers could lead to disruptions of fund operations or losses.
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.