

## Schroder Frontier Markets Equity

### Strategy Overview

#### Summary

Schroders Frontier Markets strategy provides access to some of the most dynamic and fastest growing economies in the world, supported in many cases by strong secular growth drivers. We believe the investment opportunities are similarly favorable

as market liberalization is accelerating. Moreover, Frontier Markets' relatively low correlation with developed (and emerging) markets may offer investors significant potential diversification benefits.

#### Firm highlights

- Founded in 1804, with a strong family presence to this day
- Asset management is our main business
- Over 700 investment professionals worldwide
- Truly global reach: based in London, with offices in 27 countries
- Expertise in Fixed Income, Equities, Multi-Asset, Solutions, and Alternatives

#### Team highlights

- Dedicated Emerging and Frontier Markets Equity team of 45 investment professionals, average 15 years' investment experience (as of June 30, 2017; includes three team members TBD)
- Local expertise throughout developing markets including team members based in Dubai (the Middle East represents a significant proportion of the MSCI Frontier Markets index)

#### Key features

- Targets 50% value added from country and 50% from stock decisions
- Country allocation guided by a proprietary country model with judgemental overlay
- Stock selection driven by strong proprietary fundamental bottom up company research
- Pro-active approach to risk including disciplined risk controls tools

#### Investment objective

Outperform MSCI Frontier Markets Index<sup>1</sup> by 2.5% p.a. (gross) over 3 year rolling periods.

<sup>1</sup>The MSCI Frontier Markets Index is a free float-adjusted market capitalization index that is designed to measure equity market performance of frontier markets. There can be no guarantee that any investor objectives or outcomes will be achieved.

## Investment philosophy

We believe that **developing stock markets** are inefficient and provide strong potential for adding value through active fund management and that this value can be extracted through both country and stock selection. We believe that it is **inappropriate to apply a systematic style bias** as Frontier Market countries may differ in their stage

of development. We believe that as fund managers we should manage both return and risk. Our aim is to achieve returns with the minimum level of risk through a **pro-active approach to risk control**. We believe that applying a **systematic, disciplined approach**, with a **strong team culture** increases our ability to add value.

## Investment process — overview

Schroders has a balanced approach to investing in frontier markets. We use a mix of topdown analysis and bottom-up stock selection, looking to derive 50% of our added value from country allocation and 50% from stock selection. Our core investment process does not target any particular style bias and aims to outperform in most market environments. Our investment process begins with the gathering and analysis of information on both countries and stocks. This information is then used to decide

allocations for the portfolio. Country allocation is guided by a quantitative model to which the team applies judgmental overlay while fundamental company research forms the basis of the stock selection process. We have the resources to follow a large number of companies within our universe. It is this breadth of coverage, coupled with the local nature of our research that we believe provides the means of generating unique investment ideas at the stock level.

## Investment process — country analysis

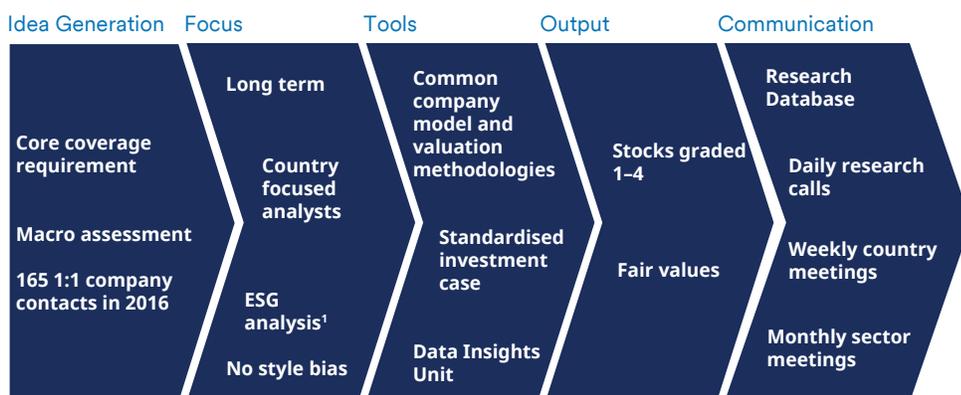
We use a proprietary quantitative model to guide our country allocation process. The model produces a ranking of the countries in the MSCI Frontier Markets universe by scoring them on five groups of factors: Valuation, Growth, Currency/Risk, Momentum and Interest Rates. Judgemental overlay is applied to the output of the model by reviewing the country weightings recommended by the model at the monthly strategy meeting,

to determine if there are any reasons not to follow its recommendation for Frontier countries. The strategy meeting is attended by all members of the Emerging Market Equities Team responsible for Frontier Markets. However, final allocation among the Frontier countries is determined by the named portfolio managers, Rami Sidani and Tom Wilson, following judgemental overlay.

## Investment process — stock analysis

We believe that in-depth local research provides us with the best insight into frontier markets at the stock level. The stock selection process is driven by

fundamental research conducted by our in-house analysts who are in direct contact with the companies and markets which they are analyzing.



Source: Schroders, FactSet. <sup>1</sup>Where possible.

## Investment process — stock analysis (continued)

---

Our primary investment universe consists of all stocks in the MSCI Frontier Markets Index, although we also aim to find good investments from the wider Frontiers universe. The analysts' initial focus is on the first 70% of market cap in each country. Stocks in our core coverage are required to be modeled and graded at all times. Stocks below the 70% of market cap cut-off and non-index stocks are defined as non-core and, although followed, will only be modelled and graded on an opportunistic basis, i.e. if they are likely to be given the highest grade. As a further source of non-core ideas, we have established a developed market company screen which is run quarterly for those companies listed in developed markets which generate over 50% of their revenue from developing markets. Results from the screen are reviewed by the team and detailed analysis carried out on potential investment ideas. Strong opportunities are presented at the monthly strategy meeting for inclusion in the portfolio on a bottom-up basis. The exposure to non-benchmark stocks is monitored as part of the risk control process.

The stock selection process is driven by in-depth fundamental research conducted by our in-house analysts based in London and Dubai, which we believe gives us a significant advantage over our competitors.

Through the extensive program of company visits we evaluate a company's management team, obtain key inputs for earnings models, assess the company's strategy and review their operations.

Analysts then use Schroders' proprietary company valuation model (CVM) to generate three-year earnings and cashflow forecasts, and a range of valuation measures that include Price / Net Asset Value, Price / Book and Price / Cashflow ratios. A major input to the stock decision is our estimate of the fair value or, simply, what we believe a stock is worth in today's terms. These fair values incorporate Schroders' three-stage Discounted Cashflow (DCF) Model.

## Portfolio construction

---

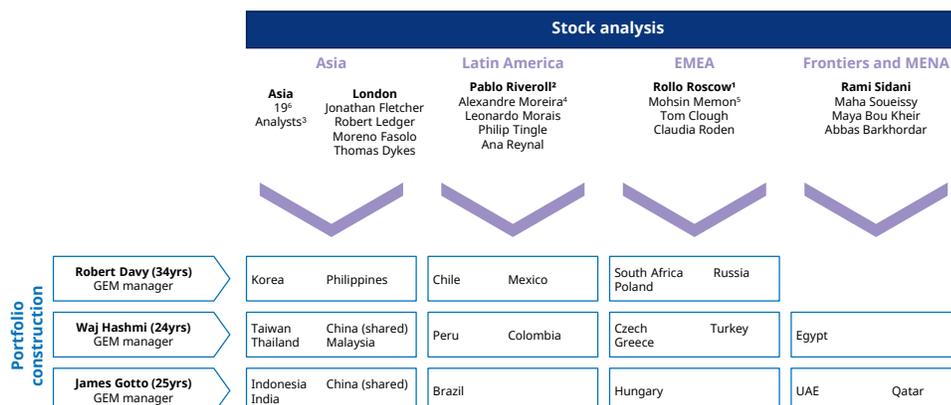
At the country level, allocation is guided by a proprietary quantitative model to which judgemental overlay is applied as discussed earlier in this document.

At the stock level, Rami Sidani constructs the country portfolios working closely with the relevant analysts to identify their highest conviction recommendations. He also draws on discussions with other Emerging Markets team members. When selecting stocks he focuses on the analysts' highest conviction ideas, using 1- and 2-rated stocks where possible, and only using 3- or 4-rated stocks for risk control purposes to ensure that each portfolio is within its risk budget.<sup>1</sup> If 3- or 4-rated stocks are included in the portfolio they must typically be underweight. Stock selection is a dynamic process and Rami is free to make changes to the stocks in the country portfolios at any time.

A decision to sell a stock, independent of those resulting from a country allocation decision, may be prompted by a change in an analyst's recommendation or a stock price reaching its fair value. We also implement a stop-loss policy, which causes a stock to be sold if it underperforms by 15% relative to the local market from purchase price or high since purchase. In exceptional circumstances we may allow a fund manager to override the stop-loss rule. Portfolios are reviewed every week to ensure that any overrides are fully discussed and justified. This is not a guaranteed stop-loss rule, and may be temporarily suspended during periods of market volatility.

<sup>1</sup> 1 represents a high conviction that a stock will outperform the relevant country's index and a 4 is a high conviction that it will underperform.

**Tom Wilson (15yrs)** – Head of Emerging Markets  
**Alan Ayres/Edward Evans/Shawn Levesque (US)** – EM Client Portfolio Managers  
**Nicholas Field (26yrs)** – Emerging Markets Strategist/Portfolio Manager  
**TBA** – Emerging Markets Strategy Analyst



Source: Schroders, as of June 2017. <sup>1</sup>Head of Research. <sup>2</sup>Deputy Head of Research. <sup>3</sup>Plus access to the research of 6 analysts from our Joint Venture in India. <sup>4</sup>Manages some local Brazilian funds. <sup>5</sup>Co-manager of the Schroder ISF Emerging Europe fund (Schroder International Selection Fund), not available to US investors. <sup>6</sup>Includes two TBA. Countries/regions are mentioned for illustrative purposes only and should not be viewed as a recommendation to buy/sell.

## Risk management

We aim to remain fully diversified across a broad range of countries and stocks in the benchmark. We will also invest in non-benchmark Frontier countries and stocks in developed and emerging countries that generate over 50% of their revenues from Frontier countries, provided the fund remains within its tracking error target range.

We do not actively allocate to sectors and therefore there are no formal limits on sector weightings relative to the benchmark, although sector exposures are monitored as part of the risk control process.

We do not constrain our portfolio managers to any maximum stock position, but we do operate to tracking error targets both at the overall portfolio level and at the stock per country level, and also have a stop-loss rule in place at the stock level.<sup>1</sup>

The tracking error target for the overall portfolio is 5%. We establish a wider range of 2% – 8% to provide some flexibility. We then disaggregate the risk down to the stock level and derive a stock tracking error target for each country of 10%. We again establish a range around this target to give flexibility of 4%-15%. Within this range, the risk target allocated will be higher for a country portfolio that is performing well and lower for one performing poorly, i.e. they are alpha-adjusted.

<sup>1</sup>There can be no guarantee that the stop-loss rule will prevent losses in the strategy.

## Why Schroders for Frontier Markets?

- Local expertise throughout developing markets including team members based in Dubai (the Middle East represents a significant proportion of the MSCI Frontier Markets Index)
- Proprietary quantitative model guides country allocation
- Detailed fundamental research drives stock selection
- Proactive and rigorous risk management

All investments, domestic and foreign, involve risks including the risk of possible loss of principal. The market value of the portfolio may decline as a result of a number of factors, including adverse economic and market conditions, prospects of stocks in the portfolio, changing interest rates, and real or perceived adverse competitive industry conditions.

Investing overseas involves special risks including among others, risks related to political or economic instability, foreign currency (such as exchange, valuation, and fluctuation) risk, market entry or exit restrictions, illiquidity and taxation. These risks exist to a greater extent in emerging and frontier markets than in developed markets.

**Important Information: The views and opinions herein are those of Schroders' investment professionals, and are subject to change over time.**

This document does not constitute an offer to sell or any solicitation of any offer to buy securities or any other instrument described in this document. The information and opinions contained in this document have been obtained from sources we consider to be reliable. No responsibility can be accepted for errors of facts obtained from third parties. Reliance should not be placed on the views and information in the document when making individual investment and/or strategic decisions. Schroders has expressed its own views and opinions in this document and these may change. Past performance is no guarantee of future results. The value of investments can go down as well as up and is not guaranteed. Sectors/securities illustrate examples of types of sectors/securities in which the strategy invested and may not be representative of the strategy's current or future investments. Portfolio sectors/securities and allocations are subject to change at any time and should not be viewed as a recommendation to buy/sell. The opinions stated in this document include some forecasted views. We believe that we are basing our expectations and beliefs on reasonable assumptions within the bounds of what we currently know. However, there is no guarantee that any forecasts or opinions will be realized. Schroder Investment Management North America Inc. (SIMNA Inc.) is registered as an investment adviser with the US Securities and Exchange Commission and as a Portfolio Manager with the securities regulatory authorities in Alberta, British Columbia, Manitoba, Nova Scotia, Ontario, Quebec and Saskatchewan. It provides asset management products and services to clients in the United States and Canada. Schroder Fund Advisors LLC (SFA) markets certain investment vehicles for which SIMNA Inc. is an investment adviser. SFA is a wholly-owned subsidiary of SIMNA Inc. and is registered as a limited purpose broker-dealer with the Financial Industry Regulatory Authority and as an Exempt Market Dealer with the securities regulatory authorities in Alberta, British Columbia, Manitoba, New Brunswick, Nova Scotia, Ontario, Quebec and Saskatchewan. This document does not purport to provide investment advice and the information contained in this material is for informational purposes and not to engage in a trading activities. It does not purport to describe the business or affairs of any issuer and is not being provided for delivery to or review by any prospective purchaser so as to assist the prospective purchaser to make an investment decision in respect of securities being sold in a distribution. SIMNA Inc. and SFA are indirect, wholly-owned subsidiaries of Schroders plc, a UK public company with shares listed on the London Stock Exchange. Further information about Schroders can be found at [www.schroders.com/us](http://www.schroders.com/us) or [www.schroders.com/ca](http://www.schroders.com/ca). Schroder Investment Management North America Inc. 7 Bryant Park, New York, NY, 10018-3706, (212) 641-3800.