Schroders

Schroder ISF* Asian Dividend Maximiser

Fund Manager: Richard Sennitt and Structured Fund Management Team | Fund update: February 2023

Performance overview

– The fund aims to provide an income of 7%[1] p.a. via a call option overlay and an actively managed Asia (ex Japan) equity portfolio.
– Pacific ex-Japan equities declined in February, partly on profit-taking after a strong January. China was the weakest performer, owing in part to a re-escalation in US-China tensions. Indonesia and Taiwan were exceptions to the general sell-off.
– The fund produced a negative return, outperforming the MSCI AC Pacific ex Japan index, but trailing the MSCI AC Pacific ex Japan High Dividend Yield (Net TR).

Drivers of fund performance

– In the equity portfolio, both stock selection and allocation contributed positively to the fund's stronger relative returns. At the regional level, underweight exposure to China was the principal contributor to fund performance. Stock selection was also positive in China and, to a lesser degree, in Hong Kong. This offset weaker stock selection in South Korea.
– At the sector level, allocation had a positive impact, mainly due to the underweighting of consumer discretionary. Stock selection also contributed positively, particularly in communication services.
– While continuing to generate the enhanced income, the options were a positive for performance in February when measured in mark-to-market terms (+0.33%, reflecting expired options and those yet to expire). The effect was slightly negative in net cash terms however (reflecting only expired options), weighing -0.08% as three tranches expired.
– A total of 113 option positions were sold across the three expiring tranches, of which 22 finished above their strike prices (requiring a settlement). Most of these 'in-the-money' names were within the first of the expiring trades - a period in which the portfolio posted strong double-digit gains.
– **TSMC**, **Ping An**, **Shenzhou International** and **Hang Lung** were among the stocks to finish in-the-money, but having had notional decisions in place (reducing the amount we overwrote), we were able to capture a greater share of the increase than if the stocks had been fully overwritten.

Outlook/positioning

– In China, it appears that Covid case numbers have peaked and society is rapidly moving on after two to three years of severe disruption. Meanwhile, investors are closely watching for further signs of policy support for the cyclical recovery.
– Markets have now pulled back from their January highs, and aggregate valuations are back to slightly below longer-term average levels. Earnings growth revisions have been negative for some time and are now quite moderate.
– Although dividends have recovered with earnings, there is still uncertainty as to where near-term dividend payments will go, given the ongoing economic uncertainties and downward earnings pressure to stocks across the region. However, aggregate corporate balance sheets look relatively robust and company profitability has recovered from the pandemic lows, meaning dividend pay out ratios are not extended. In the medium-to-long term, dividends tend to follow earnings.
– We are maintaining a bottom-up investment approach and continuing to look for good companies where we can clearly see a strong income case and potential for capital growth.
– In terms of the option strategy, we continue to employ multiple overlapping option trades (overwriting around 7.5% of the NAV in any single tranche). This creates regular expiries and hence regular opportunity to trade new options – meaning we can tailor the overlay as markets move and help to smooth through shifts in share prices, volatility and dividend expectations. At present, around 45% of the fund's NAV is overwritten with options, leaving around 55% to rise unconstrained.

[1] The gross yield is an estimate and is not guaranteed.
*Schroder International Selection fund is referred to as Schroder ISF throughout

Calendar year performance (%)

	Fund Net	Comparator 1	Comparator 2
2022	-9.6	-18.8	-6.8
2021	3.9	-5.8	6.5
2020	10.2	23.0	1.5
2019	14.4	20.3	15.1
2018	-8.8	-14.5	-8.6
2017	26.0	36.9	24.8
2016	8.5	7.5	10.3
2015	-7.2	-9.6	-16.3
2014	5.4	1.5	4.2
2013	na	na	na

Source: Schroders, net of fees, NAV to NAV, with net income reinvested. C Acc share class, as at 31 December 2022. The fund's performance should be assessed against the income target of 7% per year, and compared against the MSCI AC Asia Pacific ex Japan (Net TR) index (comparator 1) and MSCI AC Pacific ex JP High Dividend Yield index (comparator 2). 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 comparator benchmarks.

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

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.
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. The fund may also materially invest in derivatives including using short selling and leverage techniques with the aim of making a return. 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.
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.
Maximiser funds: Derivatives are used to generate income (which is paid to investors) and to reduce the volatility of returns but they may also reduce fund performance or erode capital value.
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.
Stock Connect risk: The fund may be investing in China "A" shares via the Shanghai-Hong Kong Stock Connect and Shenzhen-Hong Kong Stock Connect which may involve clearing and settlement, regulatory, operational and counterparty risks.
Market risk: The value of investments can go up and down and an investor may not get back the amount initially invested.
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.