# Schroders

# Schroder Asia Pacific Fund

## Monthly - May 2020

**Total return %**

| | 1 mth | 3 mths | 1 yr | 3 yrs pa | 5 yrs pa | Inception pa |
|---|---|---|---|---|---|---|
| Schroder Asia Pacific Fund (post-fee) | -3.06 | -10.36 | 2.61 | 7.11 | 8.55 | 7.69 |
| MSCI AC Asia (ex Japan) Index | -1.79 | -8.00 | 4.39 | 5.35 | 4.91 | 5.10 |
| **Relative performance** | **-1.27** | **-2.36** | **-1.78** | **1.76** | **3.64** | **2.59** |
| Schroder Asia Pacific Fund (pre-fee) | -2.94 | -10.05 | 4.01 | 8.58 | 10.04 | 8.99 |

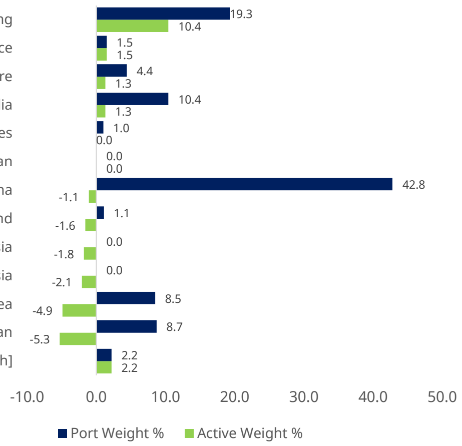
Inception date of the Schroder Asia Pacific Fund is April 1995
Past performance is not a reliable indicator of future performance.

Please refer to www.schroders.com for post-tax returns

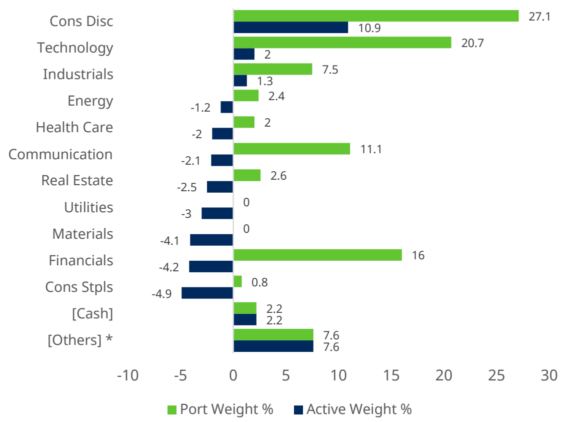
**Top ten holdings %**

| Country | Stock | Fund % |
|---|---|---|
| China | Tencent Holdings Ltd | 8.91 |
| Taiwan | Taiwan Semiconductor Manufacturing | 8.00 |
| South Korea | Samsung Electronics Ltd | 7.77 |
| China | Alibaba Group Holding Adr Represen | 7.04 |
| Hong Kong | Aia Group Ltd | 4.77 |
| China | New Oriental Education & Technolog | 3.12 |
| Hong Kong | Techtronic Industries Ltd | 3.02 |
| China | Alibaba Group Holding Ltd | 2.40 |
| Singapore | Oversea-Chinese Banking Ltd | 2.17 |
| China | Midea Group Ltd A | 2.12 |

**Regional exposure vs benchmark %**




**Sector exposure versus the benchmark %**




*refers to the exposure held through units in the Schroder ISF Indian Equity Fund.

**Commentary**

Asian equities finished the month in the negative territory as performance was dampened by the re-emergence of US-China tensions over the month. Greater China markets were the key drag given the flaring up of tensions between the US and China again, this time across a number of fronts including technology, capital flows, and trade. Hong Kong was the weakest market amid China's move to impose a new national security law, triggering a fresh round of protests locally.

Elsewhere, India, where the financial sector was as drag, also posted a loss, so too did Singapore. Meanwhile, a better-than-expected earnings season boosted the Korean market, while the ASEAN (Association of Southeast Asian Nations) markets of Thailand and Malaysia also posted strong gains. Across the region, the worst-performing sectors were real estate and financials, while healthcare and consumer discretionary outperformed.

**Performance Review**

The portfolio posted a loss over the month and trailed the regional index moderately amid another round of confrontation between the US and China across multiple fronts, dampening Emerging Markets performance. The proposal of a national security law in Hong Kong has weighed heavily on sentiment in the city, making it the worst performing market in the region over the month of May despite a gradually resumption of activities in the city as many of the COVID-19 lockdown measures were being relaxed.

Amid worries of a fresh round of local protests and ongoing social instability, our exposure to some of Hong Kong's real estate and conglomerate names (Swire Properties, Jardine Matheson) were under pressure and detracted from performance. Insurance names such as AIA and China Pacific Insurance also traded lower alongside the sector given the impact of lower interest rates and bond yields in China which pressured investment returns while sales was weak during the lock-down period. Taiwanese chipmaker TSMC was another key detractor as the stock came under pressure on stricter US restriction on exporting technologies to Chinese companies including Huawei, which could negatively impact the sales outlook of TSMC.

Meanwhile, it wasn't all negative for our Hong Kong exposure. Businesses with strong global footprint and competitiveness (Techtronics, Samsonite) continued to see share price recover from recent lows as the COVID-19 situation globally seemed to be more contained. Activities in China continued to pick up "ahead of the curve" while many western economies have begun allowing some parts of their economies to gradually reopen. The resumption of activities in China also supported the share price of Chinese consumption-related names such as Midea, Oppein Home and LVMH, adding to portfolio performance.

**Market Outlook & Strategy**

Equity markets around the world crashed during March as the Covid-19 virus spread rapidly through Western countries and authorities moved to lock down their populations, even as the data in China started to improve. Although patient data during most of April remained very depressing in Europe and the US, and numbers in other large emerging markets such as India and Indonesia also started to spike higher, markets rallied very sharply during that month. This very rapid recovery was largely on the back of the massive fiscal and monetary stimulus from Western governments and central banks. These new measures are unprecedented in their cumulative scale, relative to GDP. They aim to underwrite the costs of the current economic decline for businesses and households, and reduce the risk of the current cyclical slump extending into a more structural depression. During May, the virus patient data in many Western countries started to improve more clearly, and governments began to relax the most stringent controls. However, equity markets did not make much further progress. Although patient data is looking much more encouraging, the near-term earnings outlook has continued to deteriorate in almost all countries. It seems unlikely business activity will return to normal for quite some time, given the problems involved in fully withdrawing social distancing measures, and until a more robust testing and treatment regime is available.

On top of the uncertainties triggered by the virus, Asian market have also recently been rattled by geopolitical issues, with a deterioration in the relationship between the US and Chinese governments. Notably, the US has further tightened restrictions on the sale of technology products to Huawei, making the situation harder for non-US companies that use US equipment as part of their manufacturing or design process. China has also announced plans to introduce controversial national security legislation in Hong Kong, bypassing the local legislature. This move has drawn criticism from the US and other Western countries, and prompted Washington to threaten to suspend Hong Kong's special trading status. These moves have increased uncertainty towards regional technology supply chains and Hong Kong's role as an international financial centre, and have contributed to heightened volatility in recent weeks.

In China, it is very positive that the number of new Covid-19 cases has fallen to extremely low levels and that industrial capacity, and daily life more generally, is almost back to pre-pandemic levels. With China taking the pain of its own lockdown before the rest of the world, the country is now slightly 'ahead of the curve'. However, the recovery is likely to remain patchy as some segments of the domestic economy, such as tourism, are likely to take much longer to normalise than others. Export sectors also now face a secondary demand shock, given the collapse in demand as Western countries have moved into lockdown. This will have a material impact on employment, income and investment spending if the downturn lasts for more than a few months. Given the fragility of the recovery in China, we would watch for any further stimulus measures announced to help underpin activity. This would likely comprise both increased spending in areas such as infrastructure, and measures to support household incomes and private consumption.

Unless otherwise stated figures are as at 31 May 2020.
Benchmark is the MSCI AC Asia (ex Japan) Index.
Please refer to www.schroders.com.au for post-tax returns.
Please note numbers may not total 100 due to rounding.

Schroders

# Schroder Asia Pacific Fund

Monthly report
May 2020

## Fund details

| | |
|---|---|
| APIR code | SCH0006AU |
| Fund size (AUD) | $31,950,276 |
| Redemption unit price | $2.7529 |
| Fund inception date | April 1995 |
| Buy / sell spread | 0.30%/0.30% |
| Management costs | 1.37% |
| Minimum investment | $20,000 |
| Distribution frequency | Normally twice yearly - June and Dec |

## Fund objective

To outperform the MSCI AC Asia (ex-Japan) Index over the medium to long term.

## Key features

- 12 Asia Pacific ex Japan fund managers based in Singapore and Hong Kong.

- 38 regional Asia Pacific ex Japan analysts in 7 countries conduct close to 3,000 company visits per year.

- Joint venture with third largest private sector bank in India, Axis Bank; acquired 25% stake in September 2012 in Axis Asset Management Company

- Joint venture with Axis Asset Management Company in 2017

- Schroders' Indian research coverage - local capabilities through the Mumbai-based team at Axis AMC; they also manage local funds under the Axis Mutual Fund range and advise on another Schroders

## Market Outlook & Strategy continuation

Given the lack of visibility on the timing of an end to current global lockdowns, and the shape of the subsequent recovery in activity, it is no surprise that companies are providing little concrete guidance on their outlooks for 2020. In our interaction with managements, it has been more important to understand what measures they have been taking to deal with the crisis and how well-placed they are to ride out the downturn – operationally and financially. For many companies, this year's earnings are likely to be something of a write-off, so it is less important to focus on the outlook over the next few months. Markets will be willing to look through this crisis as long as there is scope for a healthy recovery next year to a more 'normalised' level of profitability. Our attention is, therefore, more focused on establishing the medium-term prospects for the businesses in which we are invested.

In terms of strategy, we believe that the impact of the virus and the economic lockdowns, has been to further accelerate many of the pre-existing macro trends, rather than turn the investment world on its head. For instance, the online businesses that were already gaining share before the crisis, have received a further boost during lockdown, while the weaker offline retailers have been pushed even closer to the brink. Demand for many technology hardware products has also received a further boost from the increased demand for cloud-based computing and remote access during the lockdowns. Meanwhile, at the other end of the spectrum, the banking sector in many countries has performed poorly since the global financial crisis. This has partly resulted from falling return on equity, which has been pressured by higher capital ratios, stricter regulation and depressed interest rates. The latest moves to further slash interest rates globally, encourage banks to cut dividends and allow debt moratoriums for struggling borrowers in many countries just heightens uncertainty for the banking industry. Further, it has led to valuations in the sector plumbing new lows in many cases. Given these trends, our focus remains very firmly on identifying the stronger businesses that are best placed to survive and thrive in this hostile macroeconomic environment. This is our preference, rather than necessarily looking for depressed headline valuation multiples, as these are often aligned with the weaker franchises in the market.

We believe China has moved ahead of the curve during this year's troubles. It possesses a very large, diverse domestic market that, in many cases, is relatively insulated from overseas problems. With this in mind, we have added to several of our preferred consumer stocks that have pulled back to more attractive levels during the market sell-off. Given the long-term, supportive trends of demand within the technology sector, we have also felt comfortable increasing weighting to this area. Much of the optimism around the 5G roll-out in 2020 has now deflated, and with expectations and valuations more realistic, we see scope for upside again over the medium term.

Valuations in Southeast Asia and India have been hit very hard in the recent sell-off, and headline multiples for these markets have reached the lows seen in previous crises. However, we are still reluctant to increase weightings in this area. This reflects the very heavy exposure of these equity markets to more vulnerable banks and energy-related stocks, and the difficulty of bringing the virus decisively under control in populous countries such as India and Indonesia, with weaker healthcare infrastructure. With interest rates being cut dramatically to support growth, and credit risks increasing as economies enter recession, bank earnings and returns on equity are likely to be under pressure, both structurally and cyclically. Additionally, the outlook for oil prices remains inherently unpredictable given the geopolitics that are driving the supply side of the market at present. Share prices in the smaller number of better-quality domestic consumer companies have started to correct as well, but valuations are not yet compelling.

| Five largest contributors | Portfolio weight % | [1] Load difference % | [2] Impact % |
|---|---|---|---|
| James Hardie | 1.70 | 1.50 | 0.20 |
| Novatek Microelectronics | 1.40 | 1.30 | 0.20 |
| Alibaba | 6.40 | 0.70 | 0.10 |
| Vipshop | 1.20 | 1.10 | 0.10 |
| CSL | 2.90 | 1.40 | 0.10 |

| Five largest detractors | Portfolio weight % | [1] Load difference % | [2] Impact % |
|---|---|---|---|
| Bank Of The Philippine Islands | 1.70 | 1.60 | -0.20 |
| Sina | 1.30 | 1.20 | -0.20 |
| China Mengniu Dairy | 2.30 | 2.10 | -0.10 |
| Incitec Pivot | 1.10 | 1.10 | -0.10 |
| Ncsoft | 1.30 | 1.20 | -0.10 |

Source: Schroders, Factset, Performance Attribution, using monthly data, gross of management fees
Data above is unaudited and should be treated as indicative due to problems with stock mapping.
1. Load Difference: The stock weight in the portfolio less the stock weight in the benchmark.
2. Impact: The impact is calculated by combining multiple sub periods.
Weights shown above are average period weights.

www.schroders.com.au
E-mail: 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



Schroders