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Schroder ISF* China A

Fund Manager: Jack Lee | Fund update: February 2023

Performance overview

- Onshore China equities fell, largely on profit-taking. A re-escalation in US-China tensions also weighed on sentiment, while the dollar's strength was a further headwind, leading to weakness in the yuan.
- The fund fell over the month and was marginally behind the benchmark index.

Drivers of fund performance

- Stock selection was mildly negative and was weak in financials and, to a lesser degree, consumer discretionary, offsetting positive returns from materials.
- At the stock level, the greatest relative gains came from the fund's holdings in **Zhongji Innolight**, **Piesat Information Technology** and **Mango Excellent Media**.
- The greatest detractors were the holdings in **Zejiang Huayou Cobalt**, **WuXi AppTec** and **Shenzhen Sunlord Electronics**.

Outlook/positioning

- China's equity markets have rebounded significantly from the lows of late October, driven by multiple policy pivots, notably the exit from stringent Covid restrictions and more supportive housing market policies.
- The fast-paced removal of the tight Covid-related restrictions in China is expected to provide substantial support to the recovery in consumer spending, which in turn will support domestic earnings in many sectors.
- Regarding the property sector, the government has moved to further support the market, with a clear intention of boosting developer financing. The aim is to underpin buyer confidence and pull away from the downward spiral in activity that occurred in 2022. A stabilised housing market is a pre-condition for a strong cyclical rebound in 2023.
- Fiscal and monetary policies should stay accommodative in the first half of 2023, which will lend support to the economy and equity markets. However, we are conscious of the inflation risk from the sharp cyclical rebound, which could limit room for more loosening in China.
- Externally, Chinese equities will likely continue to be influenced by the global macroeconomic backdrop, especially the extent of rate hikes and the shape of the economic slowdown in the US and Europe. Ongoing geopolitical tensions will also remain a key risk in the market in 2023, in our view.
- We remain positive on the near-term market outlook in China, but further gains will likely be led by fundamental improvements rather than multiple expansion. To see a more sustained rally, improving employment trends are required to further support the Chinese consumer recovery. Additionally, private capital expenditure will also need to pick up to help support economic growth.

Calendar year performance (%)

Year	Fund	Target	Comparator
2022	-30.5	-27.2	-28.4
2021	5.0	4.0	-0.6
2020	62.7	40.0	43.3
2019	37.8	37.5	35.0
2018	-22.7	-33.0	-27.3
2017			
2016			
2015			
2014			
2013			

Source: Schroders, net of fees, NAV to NAV, with net income reinvested. USD A Acc share class, as at 31 December 2022. The fund's performance should be assessed against its target benchmark being to exceed the MSCI China A Onshore (Net TR) index and compared against the Morningstar China A Shares Category. The fund's investment universe is expected to overlap to a limited extent with the components of the target benchmark. The comparator

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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.

Derivatives risk – efficient portfolio management and Investment Purposes: 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. The fund may also materially invest in derivatives including using short selling and leverage techniques with the aim of making a return. When the value of an asset changes, the value of a derivative based on that asset may change to a much greater extent. This may result in greater losses than investing in the underlying asset.

Emerging markets & frontier risk: Emerging markets, and especially frontier markets, generally carry greater political, legal, counterparty, operational and liquidity risk than developed markets.

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.

Onshore renminbi currency risk: The fund can be exposed to different currencies. Changes in foreign exchange rates could create losses. Currency control decisions made by the Chinese government could affect the value of the fund's investments and could cause the fund to defer or suspend redemptions of its shares.

Operational risk: Operational processes, including those related to the safekeeping of assets, may fail. This may result in losses to the fund.

Concentration risk: The fund may be concentrated in a limited number of geographical regions, industry sectors, markets and/or individual positions. This may result in large changes in the value of the fund, both up or down.

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 macroeconomic 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.

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