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Schroders

Schroder ISF* European Special Situations

Fund Managers: Leon Howard-Spink & Paul Griffin | Fund update: February 2023

Performance overview

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

Drivers of fund performance

- European shares moved higher in February, extending gains made in the prior month. The fund outperformed the index, supported by stock selection in the healthcare and materials sectors.
- **Gerresheimer**, a specialist in drug packaging and drug delivery systems, was the leading individual contributor. The company disclosed good full-year results showing accelerating top-line growth. Gerresheimer has been shifting its focus towards higher value-add packaging and devices and its investment in this area is now starting to pay off. We feel our patience with the stock, after a difficult 2022, is now starting to be rewarded.
- Still within the healthcare sector, **Lonza Group** was another leading contributor. The latest updates from Lonza have given investors better visibility on the company's long-term growth prospects.
- Elsewhere, Nordic bank **DNB** aided relative returns with the share price bouncing back after weakness in January. DNB's full-year results were good, leading to estimate upgrades. DNB is an extremely high quality lender.
- In the IT sector, **BE Semiconductor Industries** added value. There is positive sentiment towards the stock amid strong demand for its innovative tools, especially its hybrid bonding technology.
- Refrigeration and cooling technology specialist **Beijer Ref** was another positive contributor. It released well-received results showing 18% organic sales growth in Q4. Regulatory changes are very supportive of Beijer Ref's energy efficient technology, providing good visibility on future growth prospects.
- In the materials sector, **Borregaard** supported relative performance. Borregaard operates a sustainable biorefinery and uses wood products to produce environmentally friendly biochemicals. The market has previously had concerns over the outlook for pricing, but Borregaard's strategy of specialisation and making high value-add products seems to be paying off.
- On the negative side, credit bureau **Experian** was the main individual detractor. The market appears to have some concerns that a slowing US economy could mean reduced demand for credit score reports, although we note that activity tends to be similar whether the economy is in a slowdown or an upturn.
- Electrical cables specialist **Prysmian** was another detractor with the shares pulling back slightly after a strong run since September.
- **EssilorLuxottica**, a maker of lenses and frames, was also among the detractors as the market favoured more cyclical stocks. Lack of exposure to the oil & gas sector also weighed on fund returns as the energy sector performed well.

Portfolio activity

- We have initiated a small new position in French-listed building materials supplier **Saint Gobain**. It has a global presence and is oriented towards the renovation and refurbishment markets. We see long-term growth coming from the need to improve the sustainability profile of buildings. This includes using more sustainable construction methods, reducing the embedded carbon in buildings, and making buildings more energy-efficient. Regulatory trends on this front are supportive. Saint Gobain has historically been a volatile, low return business. However, management has taken steps to decentralise decision-making, make the business less bureaucratic, and to sell lower quality parts of the portfolio. Results for 2022 were resilient. We see potential for it to become a higher return business and this is not reflected in the share price.

Outlook/positioning

- The debate is ongoing in both Europe and the US as to the outlook for inflation, the likely path of interest rates, and what it means for economic growth. Central bank policy remains the main driver of short-term market moves.
- Rather than trying to predict the next move for interest rates, we remain focused on the long-term prospects for our holdings. The longer-term structural growth drivers embedded in the fund remain strong: the shift to bio-based materials; broad investment in the energy transition; the need to accommodate population growth and the medical

*Schroder International Selection Fund is referred to as Schroder ISF throughout infrastructure that implies; the growth of the smart city with all the technology development required.

– As of early March, most of our companies have reported their annual results. So far it has been a pleasing earnings season for the portfolio. Holdings across different sectors and exposed to varying degrees of cyclicality have reported numbers that were in line with or ahead of market expectations, and there have been no significant disappointments. The resilience of our companies' business models has been evident, highlighting the importance of focusing on quality attributes such as recurring revenues.

Calendar year performance (%)

Year	Fund	MSCI Europe net return
2022	-28.2	-9.5
2021	26.9	25.1
2020	11.7	-3.3
2019	35.9	26.7
2018	-16.8	-10.9
2017	16.2	10.2
2016	1.2	2.6
2015	17.7	8.2
2014	4.5	6.8
2013	15.0	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. 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 target benchmark. The investment manager will invest in companies or sectors not included in the target 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

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.
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 chosen by the investment manager. The fund may invest in companies that do not reflect the beliefs and values of any particular investor.