

## Schroder Global Emerging Markets Equity

### Strategy Overview

#### Summary

The Schroder Global Emerging Markets Equity strategy provides exposure to a range of developing countries around the world. We believe that these countries are generally characterized by a stronger growth potential than mature economies

which leads to the potential opportunity for premium returns. The investable universe is commonly defined by the MSCI Emerging Markets Index, which covers 26 countries and over 1,100 stocks.

#### Firm highlights

- Founded in 1804, with a strong family presence to this day
- Asset management is our main business
- Over 740 investment professionals worldwide
- Truly global reach: based in London, with offices in 32 countries
- Expertise in Fixed Income, Equities, Multi-Asset, Solutions, and Alternatives

#### Team highlights

- World class investment team led by Tom Wilson, CFA, Head of Emerging Markets Equities, and supported by a dedicated team of 46 investment professionals with an average of 14 years investment experience
- Stock analysts based locally in regional offices around the world
- Centralized asset allocation and portfolio construction
- London-based portfolio managers

#### Key features

- Targets 50% added value added from country and 50% from stock decisions
- Proprietary quantitative country model drives country decisions and detailed fundamental research drives stock selection
- Rigorous active risk management, including tracking error target range, risk monitoring at the country portfolio level and a stop-loss rule<sup>1</sup>

<sup>1</sup>This is not a guaranteed stop-loss and may be temporarily suspended during periods of market volatility.

#### Investment objective

The strategy seeks to outperform the MSCI Emerging Markets Index (Net TR) over rolling three-year periods.<sup>1</sup>

<sup>1</sup>There can be no guarantee that any investment objectives or outcomes will be achieved.

## Investment philosophy

We believe that emerging stock markets are inefficient and provide strong potential for adding value through active management. This value can be extracted through both country and stock selection. We believe that it is inappropriate to apply a systematic style bias across so many countries at such different stages of development.

We believe that as portfolio 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.

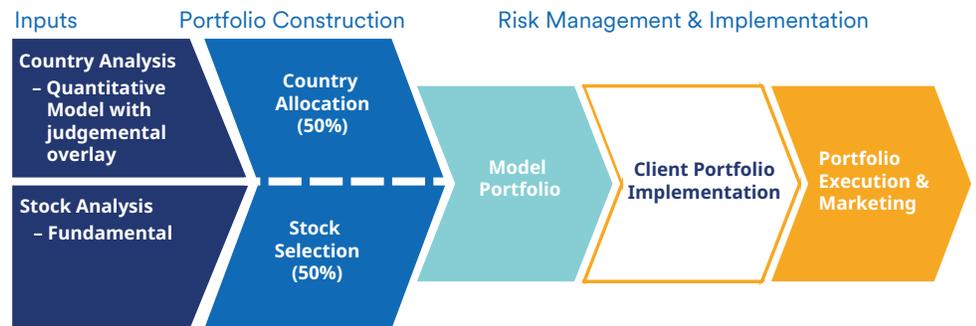
## Investment process - overview

Schroders has a balanced approach to investing in global emerging market equities, using a mix of top-down analysis and bottom-up stock selection. We look to derive 50% of our added value from country allocation driven by our proven proprietary quantitative model with judgmental overlay and 50% from stock selection driven by in-depth fundamental research.

Our investment process begins with the gathering and analysis of information on both countries and stocks. That information is then used to decide allocations for the

portfolio. Country allocation is driven by a quantitative model, to which the team applies judgmental overlay in a controlled manner, while fundamental research forms the basis of the stock selection process. We have the resources to follow a large number of companies within our universe. This breadth of coverage, coupled with the local nature of our research provides the means of generating unique investment ideas at the stock level.

Our investment process is summarized in the following diagram:



Source: Schroders.

## Investment process - country analysis

Decision-making at the level of country allocation is driven by a proprietary quantitative model which processes relevant information on the countries in our universe. This model uses four groups of factors, which are scored to produce a ranking of the countries in the global emerging market universe on a monthly basis, although we aim to re-balance the portfolio quarterly. The data inputs to the model are independent of Schroders' views as they are sourced from third parties. We are long-term fundamental investors and this is reflected in the proprietary

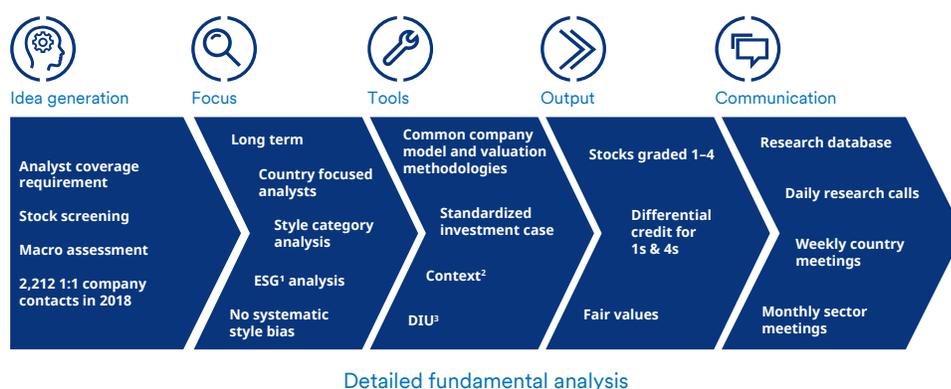
quantitative country allocation model. We constantly monitor the model and the value it is adding to our process is reviewed at each weekly investment team meeting.

The model output forms the basis of country allocation discussions at the team's monthly strategy meeting, which is attended by all members of the investment team, as well as Schroders' economists. Additional quantifiable factors (e.g. economic crisis vulnerability) and non-quantifiable factors (e.g. politics and environmental issues) are also discussed.

## Investment process - stock analysis

The stock selection process is driven by fundamental research conducted by our in-house analysts, based across the world and thus in direct contact with the companies and markets which they are analyzing.

The following chart summarizes the stock selection process:



Source: Schroders, December 2018. <sup>1</sup>ESG=Environmental, Social and Governance. <sup>2</sup>A proprietary ESG tool. <sup>3</sup>DIU= Data Insights Unit.

Our research process is based on an evaluation of business model and management track record. We have developed direct relationships with many of the companies we cover, and in 2018 we had more than 2,800 meetings with EM companies. Through this 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 produce three year financial projections, run scenario analyses, assess catalysts, and establish fair value. While analysts are free to use a range of valuation measures appropriate to each industry, fair value estimates will include a discounted cash flow (DCF) analysis based on Schroders' three-stage DCF model.

An assessment of Environmental, Social and Governance (ESG) factors is integrated into our analysts' work and an ESG review is completed each time a company is researched. Analysts identify and assess the potential impact of ESG issues on the investment case for a stock and reflect this in their final valuation and recommendation. Schroders' dedicated Sustainable Investment team supports the team's work in this area, providing guidance on best practice, producing thematic research, and engaging with companies. They have also developed a proprietary ESG analysis tool, Context, which allows the analysts to incorporate structured, data-driven analysis into their ESG assessment.

Our analysts and portfolio managers are also able to draw on Schroders' Data

Insights Unit (DIU), a centralized team of data scientists. With their support, the team is able to incorporate alternative data sources and sophisticated data science techniques into their analyses, helping to confirm their investment theses. For example, this has included tracking app downloads for internet companies, providing results of brand perception surveys, and gathering geospatial data for analysis of retail companies. Our investment data analyst works with the DIU to support our efforts in this area.

Once the stock analysis is complete, the analysts assign a rating from 1 to 4, where 1 represents a high conviction that a stock will outperform its local market, and 4, a high conviction that it will underperform. There is no hold rating. In addition, high conviction grades (1s and 4s) are encouraged by the design of our assessment system for analysts, which awards only partial credit for correct calls on 2 and 3 ranked stocks.

All analysts' output, including stock grades, valuation models and research notes, is stored in our proprietary global research investment database. This is an intranet-based platform for processing and distributing our research, which incorporates external research alongside our internal coverage and delivers it to Schroders' network worldwide. This provides investment professionals with instant access to all research by our analysts across the world, and the ability to interrogate and aggregate data that has been compiled using consistent methodology and inputs.

## Portfolio construction

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Country allocation decisions are guided by the quantitative model and discussed and decided at the team's monthly strategy meeting, which is attended by all team members plus representatives from Schroders' economics team. Given the country allocation, the three global emerging markets fund managers then construct stock portfolios for each of their countries, after consulting with the relevant analysts and regional portfolio managers. They focus on the analysts' highest conviction ideas, using 1- and 2-rated stocks where possible, and only use 3- or 4-rated stocks for risk management purposes\* to ensure that each country portfolio is within its risk budget. If 3- or 4-rated stocks are included in the portfolio

they must be underweight. This ensures that portfolio risk is aligned with conviction. The process is dynamic; fund managers are free to make changes to their country portfolios at any time.

A decision to sell a stock (independent of country allocation moves) may be prompted if the share price reaches our fair value; or we identify a more attractive investment opportunity in that country; or the investment case changes and is no longer valid; or significant ESG concerns arise. In addition, we employ a stop-loss policy which leads to an investment case review if the stock underperforms its local market index by 15% from purchase price or high since purchase.

\*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.

## Why Schroders for Global Emerging Markets Equity?

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- Local expertise throughout emerging markets
- Strong centralized asset allocation and portfolio construction function
- Proprietary quantitative model drives country allocation
- Detailed fundamental research drives stock selection
- Proactive and rigorous risk management

## Risk management

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We believe that risk is more proactively managed in our investment process than is common in emerging market equity management and this is a key differentiator of our process. Our aim is to provide consistent incremental outperformance with a positively biased return profile for our clients within an asset class that has historically been volatile. To this end, we alpha operate a tracking error target, monitor risk at the country portfolio level and make use of a stop-loss rule at the stock level.†

Our fund managers monitor the risk of their portfolios frequently to ensure that the optimal level of risk is being taken. They do this using risk reports produced by Aladdin, which is updated on a daily basis and provides information on a variety of potential sources of risk. The fund managers are ultimately responsible for the level of risk in a portfolio.

†The asset class, position, issuer and country limits mentioned for risk control are targets and are subject to change. These limits may be exceeded during periods of actual or forecasted market turmoil.

## Risk disclosures

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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, risk 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 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.**

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