FitchRatings

RATING ACTION COMMENTARY

Fitch Affirms Schroders at 'A+'; Outlook Stable

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Fitch Ratings - London - 19 Sep 2023: Fitch Ratings has affirmed Schroders plc's Long-Term Issuer Default Ratings (IDRs) at 'A+' with a Stable Outlook and Short-Term IDR at 'F1'.

The rating action has been taken in conjunction with Fitch's traditional investment manager sector review.

KEY RATING DRIVERS

Strong Franchise; Sound Financial Metrics: Schroders' Long-Term IDR reflects its well-established and increasingly diversified franchise relative to peers, sound risk management, low risk appetite and robust financial metrics, including sound asset performance and good profitability. Schroders has no external debt, which Fitch views as a rating strength. However, the ratings also consider well-managed incremental credit and liquidity risks related to the group's growing wealth management business.

Increasingly Diversified: Schroders has a long-established investment management and wealth management franchise in the UK where it is listed, supplemented by material franchises in Europe, APAC and the Americas. Schroders' historical strength has been in equities, but it has progressively diversified, developing its franchise in multi-asset, solutions, private assets and alternatives, in part via bolt-on acquisitions and strategic partnerships, including with Lloyds Banking Group in wealth management and Lloyd's of London in investment management.

Joint Ventures in Growth Markets: Management are seeking to expand further outside the UK, in particular China and India where business is mainly conducted through joint ventures with Bank of Communications in China and Axis Bank in India. Schroders has obtained a license to operate a wholly foreign-owned public fund management company in China. Fitch believes that while these regions could offer good growth prospects, operational risks are likely to be elevated in the near term as Schroders establishes itself in these newer investment management markets. Elsewhere, modest exposure to the US is via the co-branded Hartford fund range.

More Volatile Net Flows: Schroders' net new business flows recovered in 1H23: +2% of opening assets under management (AuM; annualised) after modest outflows of -0.3% in 2022 and robust net inflows in preceding years. Investment valuation losses had a bigger impact and contributed a 1% decline to Schroders' AuM in 1H23 to GBP618 billion (net of associates and joint ventures; -11% yoy in 2022). Schroders' increasingly diversified business lines have provided some stability to AuM in periods of uncertainty and risk aversion, as shown in 2022 net fund outflows from retail and institutional clients being mitigated by net inflows from Schroders Capital and the wealth management business.

Bolt-On Acquisitions: Schroders Capital was bolstered by the 2022 acquisitions of Greencoat Capital and Cairn Real Estate and certain strategies have proved in demand, such as infrastructure. The established wealth management franchise of Cazenove Capital and Schroders Wealth has been enhanced by the more recently established joint venture with Lloyds Banking Group, Schroders Personal Wealth.

Schroders' funds on average performed very well in 2022 and 1H23, with 77% of assets outperforming their stated comparator over three years.

Moderate Pressure on Margins: Schroders' revenue base is generally stable, supported by its substantial AuM, on which recurring management fees are earned. Profitability, as measured by fee-related EBITDA (excluding share of profit of associates and joint ventures)/gross fee revenues, is declining, following the AuM trend, but was still solid at 25% in 1H23 (28% in 2022). Mutual funds can attract the highest fees but flows can also be more volatile in uncertain markets. Nevertheless, margin pressure remains across the industry and Schroders is targeting continued expansion of more stable fee earning business lines, such as Schroders Capital, Schroders Solutions and Wealth Management.

No External Debt: Schroders' leverage and coverage metrics compare favourably with peers, as the group has no drawn wholesale debt. On a consolidated basis, it is subject to capital supervision by the UK Prudential Regulation Authority due to the banking license held within its wealth management division. It retains comfortable buffers, with a common equity Tier 1 ratio of 18.6% at end-2022.

Schroders' Short-Term IDR of 'F1' is the baseline option for the 'A+' Long-Term IDR, in accordance with Fitch's view of the group's funding and liquidity.

Stable Outlook: The Stable Outlook on Schroders' Long-Term IDR reflects our expectation that the group will be able to report adequate profitability in most market conditions while maintaining strong liquidity and capitalisation, without material leverage.

RATING SENSITIVITIES

Factors that Could, Individually or Collectively, Lead to Negative Rating Action/Downgrade

-Evidence of an increase in balance-sheet risk appetite (e.g. from taking on material leverage resulting in a gross debt/(F)EBITDA ratio exceeding 1.5x);

-An unexpected operational or reputational event challenging the robustness of Schroders' risk control framework;

-Significantly reduced earnings (e.g. in the light of material net AUM outflows or a prolonged period of depressed market conditions reducing fee-earning AUM without adequate compensating savings in Schroders' cost base); and

-Downgrade of the UK's sovereign rating to a level below Schroders' Long-Term IDR.

Factors that Could, Individually or Collectively, Lead to Positive Rating Action/Upgrade

-Near-term upgrade potential is limited, as ratings in the 'AA' category require performance stability that is difficult for investment managers to achieve, given the inherent sensitivity of their earnings to falling asset values amid market stress.

-In the medium term, positive rating action would likely require growth that leads to both greater scale efficiencies and enhanced diversification of revenue.

ADJUSTMENTS

The Standalone Credit Profile has been assigned in line with the implied Standalone Credit Profile.

The funding, liquidity & coverage score of 'a+' is below the 'aa' category implied score due to the following adjustment reason: historical and future metrics.

REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

ESG CONSIDERATIONS

The highest level of ESG credit relevance is a score of '3', unless otherwise disclosed in this section. A score of '3' means ESG issues are credit-neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity. Fitch's ESG Relevance Scores are not inputs in the rating process; they are an observation on the relevance and materiality of ESG factors in the rating decision. For more information on Fitch's ESG Relevance Scores, visit https://www.fitchratings.com/topics/esg/products#esg-relevance-scores.

RATING ACTIONS

ENTITY / DEBT	RATING			PRIOR
Schroders plc	LT IDR	A+ Rating Outlook Stable	Affirmed	A+ Rating Outlook Stable
	ST IDR	F1	Affirmed	F1

VIEW ADDITIONAL RATING DETAILS

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APPLICABLE CRITERIA

Non-Bank Financial Institutions Rating Criteria (pub. 05 May 2023) (including rating assumption sensitivity)

ADDITIONAL DISCLOSURES

Dodd-Frank Rating Information Disclosure Form

Solicitation Status

Endorsement Policy

ENDORSEMENT STATUS

Schroders plc	UK Issued, EU Endorsed

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