Marketing material

Schroder Investment Solutions

Monthly update – October 2023

Welcome to our monthly update for the Schroder Investment Solutions range of model portfolios and multi-asset funds. This document provides a market commentary for the core asset classes and a performance summary for our portfolios and funds.

Market commentary

Need help with any of the term used in this update? Just visit our glossary here.

Overall, Global shares fell in October. This was primarily because investors were less willing to take on risk due to the uncertainty caused by conflict in the Middle East. Government bond yields rose, which meant prices fell, as interest rates are expected to stay higher for longer. These are a type of fixed income investment issued by a government to borrow money from investors.

US Equities declined in October. Inflation remains high and the broader US economy is still very strong. The Federal Reserve's (Fed) chair, Jerome Powell, indicated that policymakers had not ruled out further interest rate increases. Almost all sectors were down over the month with energy stocks the weakest performers. Consumer discretionary stocks, such as Tesla and Airbnb, also saw notable declines. Utilities were more resilient, while IT and consumer staples also held up comparatively well.

Eurozone Equities (stocks issued by companies that are based in countries that use the euro as their currency) fell in October. The traditional safe haven sectors of utilities and consumer staples posted small gains for the month. Energy and information technology also proved relatively resilient. Other sectors saw steeper falls. Healthcare was among the weakest performers after a large pharmaceutical company announced a lower profit outlook for next year. The European Central Bank (ECB) held interest rates steady at its October meeting, breaking a series of 10 consecutive increases.

UK Equities fell over the month. The large UK banks performed poorly amid concerns around the impact of higher interest rates on the performance of their lending businesses and mortgage books in particular. Related concerns around the health of the UK consumer were also reflected in several other sectors, where poor performance weighed on small to medium sized companies. Long-term market interest rates rose again over October and there was deterioration in the UK economic outlook. This all added to concerns that the UK may be in line for a long inflation battle, even as the economy slows.

Emerging Market Equities (stocks issued by companies that are based in emerging market countries such as Brazil and India) lagged their developed market peers over the month against a backdrop of rising yields and conflict in the Middle East. Turkey was the biggest underperformer as the currency weakened against the dollar. Chinese shares also fell in the month, with investor sentiment towards China continuing to weaken due to the country's economic slowdown and a lack of a convincing response from the Chinese government. The ongoing real estate debt crisis has also added to investor concerns. Brazil marginally outperformed, as did Thailand and India.

Government Bonds (an "I owe you" issued by a government to borrow money from investors) were driven by the expectation that interest rates would need to remain high for an extended period. Factors such as a robust US job market, persistent high inflation and growing concerns over US Treasury supply kept the pressure on US yields. In the UK, services inflation remained a key concern for the Bank of England (BoE). The Bank of Japan (BoJ) introduced more flexibility around the upper limit of interest rates at the 10-year point. This fell short of market expectations which anticipated a more substantial change.

Commodities, represented by the S&P GSCI Index (a composite index of commodity sector returns, representing an investable benchmark for the commodity markets), fell in October. The price of gold was sharply higher as renewed conflict in the Middle East prompted investors to seek assets perceived to be safe havens. Within the energy component, natural gas prices rose amid concerns over risks to supply stemming from damaged pipelines as well as the Middle East conflict. Energy otherwise saw declines for crude oil, heating oil and gas oil. Agriculture also gained, with sharply higher prices for coffee and cocoa. Within industrial metals, the price of zinc was sharply lower, while price falls for aluminium, copper, lead, and nickel were more modest.

Past performance is not a guide to future performance. The value of investments and the income received from them can fall as well as rise. Investors may not get back the amount invested. Exchange rate changes may cause the value of investments to fall as well as rise.

Portfolio update

Active Model Portfolios

All portfolios in the Active Model Portfolio range had negative returns for October. All portfolios in the range, except for Risk Portfolio 4 and 6, did not perform as well as other investments in similar categories as defined by their respective Investment Association (IA) peer groups.

The EdenTree Responsible & Sustainable Short Dated Bond Fund, in our Corporate Bond allocation, contributed to performance for October. The fund predominantly invests in bonds with a maturity typically between one to three years and up to five years and has an approximate current yield of 3.23%. This is an expression of the annual income (interest or dividends) divided by the current price of the fund. The Trojan Ethical Fund also contributed positively during the month. Performance was driven by holdings in the technology sector such as Microsoft which continues to see demand for their cloud computing services.

UK, Global and US Equities detracted from performance in October. The JO Hambro UK Dynamic Fund was negative primarily due to stock selection in the financial services sector. Barclays and HSBC account for nearly 10% of the fund and these were both down due to concerns around the impact of higher interest rates. The Schroders Global Sustainable Value Fund was also down. Detractors were from stock selection in the financial services, communication services and healthcare sectors. At a country level the UK, US and Japan were negative for the fund. In the US, the Artemis US Select fund detracted mainly due to holdings in the industrial and healthcare sectors. Positive contributions from the consumer discretionary sector, which includes Amazon, was insufficient to outweigh the negatives.

Sustainable Model Portfolios

All the Sustainable Model Portfolio range had negative returns for October and did not perform as well as other investments in similar categories as defined by their respective Investment Association (IA) peer groups.

The only asset class to contribute to performance over October was Global Corporate Bonds. Within the asset class, the EdenTree Responsible & Sustainable Short Dated Bond Fund had positive performance. The fund predominantly invests in bonds issued by governments and companies that the manager believes make a positive contribution to society and the environment through sustainable and socially responsible practices. The CT UK Social Bond Fund was also up over the month.

Global and Emerging Market Equities were negative overall for October. The Schroder Global Sustainable Value Fund was down due to stock selection in the financial services, communication services and healthcare sectors. At a country level the UK, US and Japan were negative for the fund. The Montanaro Better World Fund also detracted with the German pharmaceutical and laboratory equipment supplier, Sartorius Stedim Biotech, down over the month. In Emerging Markets, the Robeco Emerging Stars Equities Fund was negative over October with companies in China, South Korea and United Arab Emirates detracting.

Strategic Index Model Portfolios

The Strategic Index Model Portfolio range had negative returns for October. All portfolios in the range, except for Risk Portfolio 6, did not perform as well as other investments in similar categories as defined by their respective Investment Association (IA) peer groups.

All asset classes detracted from performance over the month. In the UK, companies in the financial services, healthcare and industrial sectors detracted. AstraZeneca, the multinational pharmaceutical company, was the top detractor after new data for its lung cancer drug was worse than expected and left a negative impression on market analysts. In Global Equity, companies in the healthcare, consumer cyclical and financial service sectors were down over the month. The largest detractor was Tesla, followed by NVIDIA and Exxon Mobil. At a country level, the US, Japan and Canada had negative returns in October.

Blended Portfolios

The Schroder Blended Portfolio range had negative returns for October. Risk Portfolios 3,4, 6 and 7 achieved higher performance compared to other investments in similar categories as defined by their respective Investment Association (IA) peer groups. Risk Portfolios 5 and 8 did not perform as well as other investments in similar categories as defined by their respective IA peer groups.

Although the Global Corporate Bonds asset class detracted overall for the month, the Vanguard Global Short-term Corporate Bond Index Fund was marginally up. The fund predominantly invests in bonds with a maturity typically between one to five years and has an approximate current yield of 3.25%. This is an expression of the annual income (interest or dividends) divided by the current price of the fund.

UK, US and Global Equity detracted from performance. The HSBC FTSE All Share Index Fund had negative returns with companies in the financial services, healthcare and industrial sectors struggling. AstraZeneca, the multinational pharmaceutical company, was the top detractor after new data for its lung cancer drug was worse than expected and left a negative impression on market analysts. The HSBC America Index Fund was down due to companies in the consumer cyclical, healthcare and energy sectors. The largest detractor was Tesla, followed by NVIDIA and Exxon Mobil.

Global Multi-Asset Portfolios and Managed Defensive Fund

The Schroder Global Multi-Asset Portfolios (previously the Schroder Tactical Portfolios) had negative returns for October. The Moderately Cautious and Growth Portfolios achieved higher performance compared to other investments in similar categories as defined by their respective Investment Association (IA) peer groups. The Cautious, Balanced and Adventurous Portfolios did not perform as well as other investments in similar categories as defined by their respective IA peer groups. The Schroder Managed Defensive Fund also had a negative return for October.

Markets were weaker across the board in October with heightened geopolitical instability, following the tragic events in the Middle East, weighing on investor sentiment. Despite this backdrop, we have tactically upgraded our view on equities to positive in the absence of shorter-term recessionary risks. We are expressing this view through an overweight position in US larger companies which we believe can perform well into year-end. Regionally, we remain positive on Japanese equities, and negative on German equities where the economic slowdown is gaining some broader momentum. This slowing European growth also motivated an overweight US dollar vs Euro trade.

We have turned neutral on government bonds overall. Although we expect bond yields to stabilise, given that we are not expecting an imminent recession, we prefer to have exposure to interest rates via credit. To this end, we added an overweight position in US high yield credit which provides an attractive yield and is supported by strong corporate balance sheets.

One bright spot over the month was commodities, particularly gold and energy which outperformed given their perceived hedging characteristics in a period of turmoil. The portfolio maintained an overweight commodities position. Elsewhere within currencies, an overweight Korean Won vs Singapore dollar position was opened in October. This is designed to capture signs of a recovery in exports from Korea.

Income Portfolio

The Schroder Income Portfolio had a negative return for October and performed similarly compared to other investments in similar categories as defined by its respective Investment Association (IA) peer group (IA Mixed Investment 20-60% Shares).

Although the Global Corporate Bonds asset class detracted overall for the month, the EdenTree Responsible & Sustainable Short Dated Bond Fund was marginally up. The fund predominantly invests in bonds with a maturity typically between one to three years and up to five years and has an approximate current yield of 3.23%. This is an expression of the annual income (interest or dividends) divided by the current price of the fund. The Vontobel TwentyFour Absolute Return Credit Fund was also up over the month.

Global, UK and US Equity were down over October. In global equities, the Robeco Sustainable Water Fund detracted from performance. The American biotechnology company, Avantor, was down over the month as market analysts anticipated the company announcing a decline on earnings over the last year. The company is a top holding for the fund and aims to be a global provider of mission-critical products and services to the life sciences, education, government, advanced technologies and applied materials industries. In the UK, the City of London Investment Trust had negative performance from companies in the financial services sector which outweighed positive performance from companies in the utilities and industrials sectors.

Investment objectives

Schroder Blended Portfolios
The funds aim to provide capital growth and income by investing in a diversified range of assets and markets worldwide with a target average annual volatility (a measure of how much each fund's returns may vary over a year) over a rolling five year period. This target volatility is fund specific and varies between 30% to 100%* of that of global stock markets (represented by the MSCI All Country World index), depending on the investment objective of each fund.

The Funds are part of the SISCo Schroder Blended Portfolio range, which offers six funds with different expected combinations of investment risk and return.

* Please refer to the Prospectus for the individual risk profile volatility target.

Schroder Global Multi-Asset Portfolios
The Funds aim to provide capital growth and income by investing in a diversified range of assets and markets worldwide with a target average annual volatility (a measure of how much each Fund's returns may vary over a year) over a rolling five year period. This target volatility is fund specific and varies between 30% to 90%* of that of global stock markets (represented by the MSCI All Country World index), depending on the investment objective of each Fund.

* Please refer to the Prospectus for the individual risk profile volatility target.

Schroder Managed Defensive Fund
The Fund aims to provide capital growth and income in excess of the ICE BofA Sterling 3-Month Government Bill Index plus 2% per annum (after fees have been deducted) over a three to five year period, whilst also seeking to mitigate the risk of incurring a loss greater than 10% over any investment period, by investing in a diversified range of assets and markets worldwide. The Fund will seek to achieve a target average volatility (a measure of how much the Fund's returns may vary over a year) over a rolling five year period of 4% per annum. This cannot be guaranteed and your capital is at risk.

Schroder Income Portfolio
The Fund aims to provide an income of 3% to 5% per year and capital growth by investing in a diversified range of assets and markets worldwide with a target average annual volatility (a measure of how much the Fund's returns may vary over a year) over a rolling five year period of between 50% to 65% of that of global stock markets (represented by the MSCI All Country World index). This is not guaranteed and could change depending on market conditions.

What are the risks?

Capital risk: All capital invested is at risk. You may not get back some or all of your investment. **Counterparty risk:** The portfolios may have contractual agreements with counterparties. If a counterparty is unable to fulfil their obligations, the sum that they owe to the portfolios may be lost in part or in whole. **Credit risk:** A decline in the financial health of an issuer could cause the value of the instruments it issues, such as equities or bonds, to fall or become worthless. **Currency risk.** The fund may lose value as a result of movements in foreign exchange rates, otherwise known as currency rates. **Derivatives risk:** Derivatives, which are financial instruments deriving their value from an underlying asset, may be used to manage the portfolio efficiently. The portfolio may also materially invest in derivatives including using short selling and leverage techniques with the aim of making a return. 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. **Derivatives risk – efficient portfolio management and investment purposes:** Derivatives may be used to manage the portfolios 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 portfolios. The portfolios 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. **Equity risk:** Equity prices fluctuate daily, based on many factors including general, economic, industry or company news. **High yield bond risk:** High yield bonds (normally lower rated or unrated) generally carry greater market, credit and liquidity risk. **IBOR risk:** The transition of the financial markets away from the use of interbank offered rates (IBORs) to alternative reference interest rates may impact the valuation of certain holdings and disrupt liquidity in certain instruments. This may impact the investment performance of the fund. **Interest rate risk:** The portfolios may lose value as a direct result of interest rate changes. **Investments in other collective investment schemes risk:** The portfolios will invest mainly in other collective investment schemes. **Leverage risk:** The portfolios use derivatives for leverage, which makes them more sensitive to certain market or interest rate movements and may cause above-average volatility and risk of loss. **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, meaning investors may not be able to have immediate access to their holdings. **Market risk:** The value of investments can go up and down and an investor may not get back the amount initially invested. **Money market & deposit risk:** A failure of a deposit institution or an issuer of a money market instrument could have a negative impact on the performance of the portfolios. **Negative yields risk:** If interest rates are very low or negative, this may have a negative impact on the performance of the portfolios. **Operational risk:** Operational processes, including those related to the safekeeping of assets, may fail. This may result in losses to the fund. **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.

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