Schroder Absolute Return Income (Managed Fund) (Ticker: PAYS)

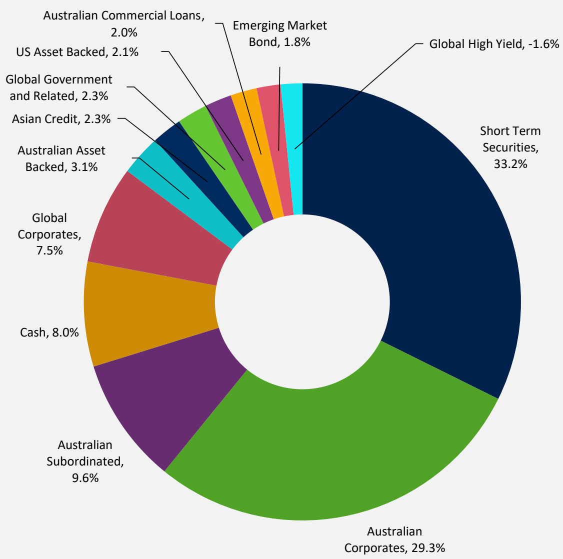
Monthly Report - April 2022

For more information about the Fund visit www.schroders.com.au/pays

Total return %	1 mth	3 mths	6 mths	1 yr	Inception p.a.
Schroder Absolute Return Income (Managed Fund) (post-fee)	-0.27	-1.63	-1.60	-1.55	0.76
RBA Cash Rate	0.01	0.02	0.05	0.10	0.22
Relative performance (post-fee)	**-0.28**	**-1.66**	**-1.65**	**-1.65**	**0.55**

Past performance is not a reliable indicator of future performance. Returns over 12 months are annualised.

Portfolio inception 19/11/2019, 2 years and 5 months



Portfolio statistics

Duration	0.22 yrs
Yield to maturity	1.99%
Average credit rating	A-
Number of securities	2473

*Please note numbers may not total 100 due to rounding

*The Portfolio may have a sizeable exposure to securities, including cash instruments, issued by each of the four major Australian banks.

*Unless otherwise stated figures are as at the end of Apr 2022

*Benchmark is the RBA Cash Rate

Portfolio review

Over the month of April the Schroder Absolute Return Income (Managed Fund) returned -0.27% (post fees), bringing the 12 month performance to –1.55% (post fees) or 1.65% below the RBA cash rate.

Largest contributors

The key contributor to performance was our interest rate strategy overlay. Our active management of the duration of the underlying assets allowed us to largely neutralise the negative effect of rising yields though hedging the risk with futures positions. The higher coupons from corporate bonds also contributed, however the move wider in credit spreads outweighed this.

Largest detractors

The Japanese yen (JPY) exposure detracted from performance as the JPY continued to weaken. With its status as a safe haven currency coming into question, at least in the shorter term, we exited the long yen position.

Our Australian corporate exposures also detracted from performance. The Australian credit market continues to come under pressure as reduced liquidity has exacerbated some of the negative influences as credit spreads pushed wider.

Market review

Equities

Global equities fell sharply over the month, with concerns around tighter monetary policy from central banks globally, the impact of a hard Chinese lockdown and the ongoing effects of the conflict in Ukraine all weighing on risk assets. The selloff was led by the NASDAQ index which was down over -13% for the month and has fallen -21% year to date. Broader global developed market equities fell by -7% in local currency terms, while the Australian market outperformed delivering a negative return of -0.9% in April. Emerging market equities fell by -5.6% in US dollar terms. In the US, the first quarter earnings season is well underway with 80% of companies having reported so far. While the proportion of companies beating their estimates remains relatively strong at over 75%, the degree of upside surprise has fallen sharply compared to last year (4% upside surprise now vs over 15% through 2021). Furthermore, there is also evidence of margin contraction as earnings increased at a slower pace than headline sales.

Fixed Income

Bond yields moved higher globally as markets moved to price in more central bank official rate increases given the elevated levels of inflation. With headline inflation reaching 8.5% in the US, 7.5% in the Eurozone and 5.1% in Australia, central banks have turned increasingly hawkish as they try to manage inflation. Yields moved higher across the yield curve, with multiple 50 bp rate hikes already being priced in for the US Federal Reserve for its next few FOMC policy meetings, which could see the Fed Funds rate move above 2.5% through the latter stages of this year. The futures market has also priced in similar levels for the RBA cash rate in the local market. Australian 10 year bond yields increased by 0.3% to close the month at 3.13%, while US 10 year yields jumped by 0.6% to finish April at 2.93%. One exception to this shift, has been Japan, where inflation remains relatively low at 1.2%, and the Bank of Japan has reaffirmed its commitment to yield curve control through offering to buy an unlimited amount of 10 year Japanese Government Bonds at 0.25%, effectively capping the yield. Credit spreads moved wider across all sectors, most notably in global high yield.

Schroders

Post-fee performance of the underlying Schroder Absolute Return Income Fund, offered by Schroders as a Unit Trust

	1 mth	3 mths	6 mths	1 yr	3 yrs p.a.	mFund Code
Schroder Absolute Return Income Fund - Wholesale Class^	-0.27	-1.63	-1.60	-1.54	1.46	SCH55

^The fund on offer is unlisted. An application into this fund may be made through an application form attached with the PDS, which is available on our website at www.schroders.com.au. The management fee for the Schroder Absolute Return Income Fund (Wholesale Class) is 0.54%.

Market review continued

Currencies

The US dollar (USD) continued to strengthen as the broad sell off across equities, bonds and credit resulted in strong safe haven flows. Most currencies weakened against the US dollar, with the Australian dollar (AUD) falling by 6% in April, the Japanese yen (JPY) by 6.5%, while both the Euro (EUR) and British pound (GBP) fell by over 4%. The yen continued to weaken as the Bank of Japan reiterated its commitment to yield curve control, while the AUD was impacted by both the sell off in risk assets, as well as the impact of the Covid zero policy in China. Commodities continued to strengthen, driven by strong food and energy prices, with the broader Bloomberg Commodity Index rallying by over 4% through April.

Outlook and strategy

April proved to be another challenging month as most major financial assets performed poorly. Fixed income markets were hit particularly hard with credit markets and sovereign bond markets again posting negative returns. Currency markets were also challenging as some traditional safe-haven currencies, namely the JPY, also struggled.

To some extent the move in markets is not entirely surprising. As we have mentioned previously, we are in a transition phase, moving to more appropriate monetary and fiscal policy settings, and liquidity is being withdrawn from the market as the US Federal Reserve (Fed) looks to reduce its balance sheet. These transitions rarely, if ever, happen in a straight line and with them bring heightened market volatility and greater uncertainty. Questions around the growth outlook and path of inflation along with other factors including the conflict in the Ukraine and China's zero COVID-19 policy add to the challenging backdrop investors face.

To some extent we are in unfamiliar territory, at least in terms of recent history. The disinflationary environment that began in the 1980s is potentially coming to an end. With this may bring the end of the multi decade bull market in bond prices as markets adjust to the reality of higher inflation and the need for central banks to act, results in higher yields. These moves higher in sovereign bond yields and deeply negative returns have left many investors questioning the use of traditional fixed income, given its failure to provide adequate diversification to falling risk assets.

It is with this in mind we believe an absolute return focus is one that allows us to navigate a variety of market conditions. The recent rout in bond markets reinforces the view that being structurally long duration (interest rate risk) is not always appropriate, particularly in such a transition phase. Being active and having the ability to carry no interest rate risk allows us to partially insulate the portfolio from the effect of rising rates, manage potential downside risk and focus on preserving capital. Being active also allows us to also add duration to the portfolio once term premia has rebuilt and valuations improve.

With this approach and the current market environment it is not surprising we continue to have close to zero outright duration. This has been our positioning for some time now as we essentially sit on the sidelines and wait. There are however some interesting opportunities emerging at some points of the yield curve. For example, three-year government bond yields in Australia are near 3% which is beginning to look interesting. Further out the yield curve is more challenging and hence we remain patient.

The counterbalance to the lack of duration is holding higher levels of cash, currently close to 42%. This is the highest in the long history of the Fund and reflects the fact that cash is capital stable. In addition, holding cash provides flexibility or 'option value' and the ability to easily take advantage of opportunities as they arise.

Our credit positioning continues to be very defensive. The credit we do hold has an average investment grade rating. This, combined with our active stock selection serves to limit the likelihood of capital loss from defaults. We have negative exposure (a short position) to global high yield through derivative hedges and hold small exposures to emerging market debt.

Currency has been used as a downside risk hedge given duration has been ineffectual, however that has also been a challenge. Traditionally the Japanese yen (JPY) is a safe haven currency (performing well when equities are negative), but this has been strongly challenged recently. The fall of the yen against major currencies is reflective of the imbalance between the Bank of Japan (BOJ) and other central banks. With the Fed and the RBA hiking and the BOJ sticking to its yield curve control policy, the pressure on the yen has intensified. We have been reducing our long yen position and this month have completely exited the position as BOJ attempts to manage the slide have failed.

Looking forward, the positive point to note is that risk premia and term premia are rebuilding across global interest rate markets. This can be painful as asset prices adjust to reflect rising risks. However, it does lead to new opportunities and the ability to reset the portfolio on a more positive footing. That said we are patient. It is possible that we are closer to the beginning than the end of the adjustment phase and the markets can always overshoot on the downside. As such we are waiting for the balance between risk and reward to move more in our favor before actively adding interest rate and credit risk back into the portfolio.

Schroder Absolute Return Income (Managed Fund)

Monthly Report
April 2022

Fund Objective

To outperform the RBA Cash Rate after fees over the medium term while aiming to avoid negative returns over any rolling 12-month period.

Key Features

– **Reliable monthly income:** Predictable and stable monthly income assists investors with planning their retirement income needs.
– **Global diversification:** Provides diversification across broad global fixed income markets with flexibility to respond to changing market conditions.
– **Strong risk management:** Actively managed to provide strong risk management, helping to avoid losses and preserve capital, should markets fall.
– **Competitively priced:** Competitive management fee of 0.54% p.a.
– **Easily accessed via one trade:** Contact your broker, financial planner or invest via your online trading account using the Cboe code: **PAYS**.
– **Brought to you by Schroders:** A leader in fixed income, with an experienced local team backed by specialists in 12 locations around the world.

Fund details

Cboe Code:	PAYS
Fund size (AUD)	$59,671,972
Redemption unit price	$9.4315
Fund inception date	November-2019
Management costs	0.54%
Distribution frequency	Monthly

Top ten holdings %

	Portfolio
AUSNET SERVICES HOLDINGS PTY LTD 3.3842 06-OCT-2080 Reg-S (SUB)	1.3%
TREASURY NOTE 2.625 15-FEB-2029	1.2%
SCENTRE GROUP TRUST 2 5.125 24-SEP-2080 Reg-S (SUB)	1.1%
TREASURY NOTE 1.75 15-NOV-2029	1.1%
SANTOS FINANCE LTD. 4.125 14-SEP-2027 Reg-S (SENIOR)	1.1%
AUSTRALIA (COMMONWEALTH OF) 1.75 21-JUN-2051 Reg-S	0.9%
AMPOL LTD 3.7458 09-DEC-2080 Reg-S (SUB)	0.9%
BRISBANE AIRPORT CORPORATION PTY L 3.1 30-JUN-2026 (SECURED)	0.8%
LONSDALE FINANCE PTY LTD 2.45 20-NOV-2026 Reg-S (SECURED)	0.8%
SGSP (AUSTRALIA) ASSETS PTY LTD 3.25 29-JUL-2026 Reg-S (SENIOR)	0.7%
Total	**9.9%**

Maturity Profile %

	Portfolio
0-3 Years	53.1
3-5 Years	14.6
5-7 Years	10.1
7-10 Years	12.4
10-15 Years	0.9
15+ Years	8.9

Security profile %

	Portfolio
Fixed rate	50.5
Floating rate	49.8
Other	-0.3

Regional exposure %

	Portfolio
Australia	71.1
USA	22.8
Europe ex UK	3.8
UK	1.3
Asia inc Japan ex EM	0.0
Emerging Markets	0.9

Holdings by composite broad credit rating %

	Portfolio
AAA	4.8
AA	3.6
A	10.5
BBB	45.2
Below BBB	5.3
Cash and Equivalents	28.4
Not Rated	2.2

Credit ratings are scales by which the future relative creditworthiness of a security is measured and express an opinion about the vulnerability of default. Credit ratings may be issued by an independent credit rating agency, or represent internal ratings prepared by Schroders. A change in a published credit rating can impact the price and liquidity of the security(ies) being re-rated.

Investors should not rely on credit ratings in making investment decisions or view them as assurances of credit quality or the likelihood of default. The ratings issued included in the monthly report are intended to be used by wholesale investors as a guide only and should not be relied on by retail investors when making a decision to buy, hold or sell any securities or make any other investment decisions.

Unless otherwise stated figures are as at the end of April 2022

Figures may not total 100 due to rounding

Regional exposure is expressed by currency pre-hedging

Contact www.schroders.com.au
E-mail: web.queries@computershare.com.au

Schroder Investment Management Australia Limited ABN 22 000 443 274 Australian Financial Services Licence 226473 Level 20 Angel Place, 123 Pitt Street, Sydney NSW 2000 Phone: 1300 136 471 Fax: (02) 9231 1119

Schroders