Schroder Absolute Return Income (Managed Fund)

An active ETF designed to boost income while preserving capital

Chi-X code: PAYS

Quarterly Report - March 2021

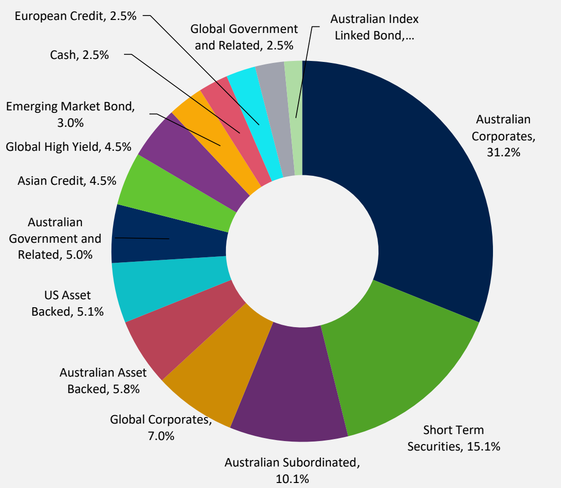
For more information about the Fund visit www.schroders.com.au/pays

Total return %	1 mth	3 mths	6 mths	1 yr	Inception p.a.
Schroder Absolute Return Income (Managed Fund) (post-fee)	-0.09	-0.10	1.46	5.38	2.33
RBA Cash Rate	0.01	0.03	0.06	0.19	0.31
Relative performance (post-fee)	**-0.10**	**-0.12**	**1.40**	**5.20**	**2.02**

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

Portfolio inception 19/11/2019, 1 years and 4 months

Asset allocation %



Portfolio statistics

Duration	0.57 yrs
Yield to maturity	1.43%
Average credit rating	A-
Number of securities	2927

*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 Mar 2021

*Benchmark is the RBA Cash Rate

Market review

Equity markets overcame initial concerns around higher bond yields and rallied through March, being supported by a strong outlook for corporate earnings and the US congress giving final approval to Biden's $1.9 trillion fiscal support package. The fiscal package is roughly equivalent to 9% of US GDP and has seen growth estimates for the US revised up to around 6% for 2021. Australian growth has also been revised higher, though to a smaller degree, with expectations of 4% growth for the year. US bond yields continued to rise through March driven by the prospect of higher growth and inflation, while yields in other core markets fell moderately through the month. US Federal Reserve Chair Powell has stressed that a pick-up in inflation is expected, but is likely to be transitory rather than structural. On the data front, the US ISM index posted another strong reading, while global property markets also performed strongly. Locally, property prices increased by 2.8% over the month, while Sydney prices had their strongest monthly increase in 33 years, rising by 3.7% through March.

Global equities returned 4.2% in local currency terms through March, while the Australian market underperformed with a return of 2.4%. The style rotation towards value continued, with value equities outperforming growth equities by about 5% in the month, though growth has still outperformed over a one-year timeframe. Emerging market equities had a negative return over the month, -1.5% in USD terms (mostly due to a negative return in Chinese equities), as a stronger US dollar and a slower than expected vaccine rollout weighed on sentiment. Over the quarter, growth assets performed strongly, with Australian equities returning 4.3% and global equities returning 6.2%. US 10-year treasury yields increased by 0.34% through March to end the month at 1.74%, while Australian 10-year treasury yields moved in the opposite direction, falling by 0.13% to end the month at 1.79%. Similarly, longer end bond yields also fell in Germany and Japan by 0.03% and 0.06% respectively over the month. Over the quarter, Australian and US 10-year treasury yields both increased by approximately 0.8%. Credit spreads also diverged during March, with high yield spreads continuing to compress, global investment grade relatively flat, and Australian investment grade spreads moderately wider.

Portfolio review

The Schroder Absolute Return Income Fund returned -0.10% (post fees) over the quarter, taking the 1 year return to 5.38% (post fees) or 5.20% (post fees) above the RBA Cash Rate.

The main story over the quarter was the rise in bond yields – largely off the back of the improving growth outlook and rising inflation expectations. Whilst not dramatic, we did see Australian 10-year bond yields rise 70bp over the quarter and they are now 100bp from their lows in October last year. We hold low levels of duration, however the upward move in sovereign bond yields did detract from portfolio returns. Also, the strength of the Australian dollar detracted – particularly against the USD and Yen.

Credit markets remained well supported and, despite the move in sovereign bond markets, credit spreads have been relatively well behaved. In a zero-rate world the search for yield continues as abundant liquidity looks to find a home. The carry from coupons and positive return from credit spreads moving tighter added to portfolio returns.

Outlook and strategy

With vaccine rollouts progressing across the globe and the backdrop of stimulatory fiscal and monetary policy settings, the reopening of trade is in full swing as stimulus and liquidity feed into higher asset prices. Whilst there is little likelihood of stimulus being withdrawn anytime soon, arguably much of the good news is being priced into markets. Future expected returns are likely to be more subdued given the current starting point of valuations of many assets.

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^	-0.09	-0.09	1.48	5.38	3.12	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%.

Outlook and strategy continued

The next phase of markets is expected to be more challenging. In credit markets, valuations in some segments are moving into expensive territory as the search for yield-based assets continues largely unabated. Many companies have weathered the storm to date and whilst there have been some issues in the hedge fund space, at this stage ample liquidity is keeping the level of corporate defaults lower than would otherwise be the case. We know that in the absence of a meaningful shock, valuations can stay at expensive levels for extended periods as we enter more of a 'carry' phase.

In terms of duration, the back up in long end bond yields has improved their attractiveness, particularly in the world of zero cash rates. The Australian 10-year treasury bond has risen 100bp off its lows and with a yield of around 1.7% is beginning to look more interesting. That said, the risk to capital values has arguably increased. There is an increasing tension between central bank policy settings and investors, with the latter concerned excessive stimulus will lead to a significant rise in inflation. Central banks remain firmly committed to low policy rates and their ongoing aggressive support of markets. This resolve will be firmly tested if economic data continues to print firm and concern about inflation continues to build. Any material upside surprise to upcoming inflation data could provide some real headwinds as the market either looks through any spike as a shorter-term cyclical uplift or views it as more of a structural shift in the inflation regime.

In terms of portfolio positioning, given valuations we reduced our Australian investment grade credit holdings by 3% into cash. Our hybrid exposures remain unchanged and provide a good source of income to the portfolio. We retained our tactical tilt to global high yield at 3% of the portfolio which continues to provide one of the highest available yields compared to cash. We have reduced our US investment grade holdings by 1% given the long duration of this market and sensitivity to widening spreads. We have retained our US securitised credit exposures which continue to be defensive in nature and are typically senior in the capital structure. Asian credit exposures continue to provide reasonable yields over cash and assist with portfolio diversification.

In terms of duration we did reduce outright duration over the quarter to around 0.4 years. As such, we insulated the portfolio from much of the rise in bond yields. Overall, we remain liquid and high quality with a low level of sensitivity to interests rates and moderate currency exposures. Over time we envisage reducing the credit risk in the portfolio and adding to duration-based assets should yields continue to rise. Currency-based allocations are currently more moderate, although the AUD/USD has recently moved to more attractive levels, and should we see a rise in risks we will likely add back to our USD exposures.

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March 2021

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 Chi-X 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

Chi-X Code:	PAYS
Fund size (AUD)	$36,966,926
Redemption unit price	$9.8709
Fund inception date	November-2019
Management costs	0.54%
Distribution frequency	Monthly

Top ten holdings %

	Portfolio
AUSTRALIA COMMONWEALTH OF (GOVERN 2.0 21-AUG-2035 Reg-S	1.5%
TREASURY NOTE 2.625 15-FEB-2029	1.3%
TREASURY NOTE 1.75 15-NOV-2029	1.2%
AUSNET SERVICES HOLDINGS PTY LTD 3.1351 06-OCT-2080 Reg-S (SUB)	1.1%
BRISBANE AIRPORT CORPORATION PTY L 3.9 24-APR-2025 Reg-S (SECURED)	1.0%
SANTOS FINANCE LTD. 4.125 14-SEP-2027 Reg-S (SENIOR)	1.0%
QPH FINANCE CO PTY LTD 2.85 29-JAN-2031 (SECURED)	0.9%
SCENTRE GROUP TRUST 2 5.125 24-SEP-2080 Reg-S (SUB)	0.9%
SYDNEY AIRPORT FINANCE COMPANY PTY 3.625 28-APR-2026 Reg-S (SECURED)	0.9%
AUSGRID FINANCE PTY LTD 3.75 30-OCT-2024 (SECURED)	0.8%
Total	**10.7%**

Maturity Profile %

	Portfolio
0-3 Years	36.0
3-5 Years	19.8
5-7 Years	15.6
7-10 Years	15.7
10-15 Years	3.4
15+ Years	9.5

Security profile %

	Portfolio
Fixed rate	63.3
Floating rate	34.1
Other	2.6

Regional exposure %

	Portfolio
Australia	58.1
USA	32.5
Europe ex UK	5.4
UK	2.3
Asia inc Japan ex EM	0.1
Emerging Markets	1.5

Holdings by composite broad credit rating %

	Portfolio
AAA	11.6
AA	5.6
A	10.7
BBB	41.9
Below BBB	10.1
Cash and Equivalents	19.1
Not Rated	1.0

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 March 2021

Figures may not total 100 due to rounding

Regional exposure is expressed by currency pre-hedging

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