

Schroder Sustainable Global Core PIE Fund

Q3 2024 Investment Report

This quarterly investment report is provided to you in supplement to your monthly performance report and other monthly investment reporting. It must be read in conjunction with your monthly performance report, which provides full details in a standard reporting format of the performance of your investment. This supplemental reporting is intended to provide you with an overview of portfolio activity during the period and should not be relied upon to make investment decisions or otherwise.

Q3/2024

Schroders

Schroder Sustainable Global Core PIE Fund

In this report

The Team

Fund Overview

Market Summary and Performance Review

Portfolio Activity and Policy

Outlook

Active Ownership

Portfolio Analysis

Market Analysis

The Team

Portfolio Manager
QEP Investment Team
Tel: +44 20 7658 6000

Investment Approach

An index-relative strategy designed to produce consistent and repeatable performance with low index-relative risk. Stocks are evaluated using a diverse range of Value and Quality criteria to build a highly diversified portfolio, typically holding in excess of 400 stocks.

Fund Performance

Periods 30 September 2024

Total returns NZD	1 month %	3 months %	6 months %	YTD %	Inception % pa
Fund at closing prices (gross)	-0.09	0.78	2.54	19.67	21.90
Fund at closing prices (net)	-0.12	0.63	2.32	19.29	21.46
Benchmark [^]	0.15	1.81	2.54	18.21	21.02
<i>Difference (gross)</i>	-0.24	-1.03	+0.00	+1.46	+0.88
<i>Difference (net)</i>	-0.27	-1.18	-0.22	+1.08	+0.44

Fund Performance (Hedged)

Total returns NZD	1 month %	3 months %	6 months %	YTD %	Inception % pa
Fund at closing prices (gross)	1.34	3.51	7.86	20.13	24.62
Fund at closing prices (net)	1.30	3.32	7.61	19.72	24.12
Benchmark [^]	1.54	4.59	7.84	19.08	24.01
<i>Difference (gross)</i>	-0.20	-1.08	+0.02	+1.05	+0.61
<i>Difference (net)</i>	-0.24	-1.27	-0.23	+0.64	+0.11

Both funds inception date: November 30, 2023.

Source: Schroders, FundRock as of September 2024. Performance shown reflects past performance, which is no guarantee of future results. Current performance may be higher or lower than the performance shown. Principal value and investment returns will fluctuate so that shares, when redeemed, may be worth more or less than their original cost. Performance for periods less than one year is not annualized. NAV performance may differ from performance calculated at closing market prices. The difference between the portfolio and benchmark returns may not equal stated excess returns due to rounding. Since inception from 30 November 2023. [^]Benchmark is the MSCI World ex Tobacco NR NZD for the unhedged and MSCI World ex Tobacco NR NZD Hedged for the hedged. Indices are net dividend reinvested (NDR).

Summary

Whilst the third quarter delivered strong returns across both developed (+6.4%) and emerging markets (+8.7%) (all figures in USD terms), it was more a tale of three distinct months with sharp swings of sentiment throughout. In the absence of a dominant theme driving markets, Fed-watching, Q2 earnings and a late quarter stimulus announcement in China drove much of the action. This was manifest in sector rotation and an uptick in market participation, at least when compared to the first half of the year.

July started with a rotation away from the prior mega-cap leaders whilst lower quality value areas outperformed. Cooling inflation in the US alongside a weakening labour market, which stoked recessionary fears, contributed to the shift. August kicked off with a massive technical correction, swiftly followed by a rebound on the expectation of more aggressive rate cuts. Softening US employment figures, preceded by a somewhat unexpected BoJ hike, triggered a big carry trade unwind to the detriment of many crowded momentum trades. Equity markets returned to strength in September, as the Federal Reserve commenced its long-awaited rate cutting cycle with a big 50-basis point move. As the quarter drew to a close, Beijing launched an economic stimulus package, delivering Chinese equities their best week since 2008. The positive sentiment rippled quickly across risk assets, with global equity markets finishing back at or near their all-time highs.

From a sector perspective, there was much movement through the quarter. The Fed's new course was met with relief and provided the catalyst for a return to favour of big tech at the expense of higher quality defensives (health care and staples), although bond proxies (utilities and REITs) continued to perform well. Energy also rolled off due to weakness in commodity prices. Q2 earnings reports were another key driver of volatility as stocks which missed expectations were heavily punished. Nvidia, as the poster child, had been relatively weak into late August and whilst it largely met expectations, concerns about the sustainability of its strong recent growth left it below its mid-June peak.

Elsewhere, having seen little action through the quarter, emerging market stocks marched higher in late September on the strength of China, as Beijing announced a raft of new stimulus measures including a \$114bn package explicitly aimed at boosting the stock market. This was largely isolated to China as the other large Asian markets underperformed (e.g. India, Korea and Taiwan). Similarly Latin America was mixed, as were emerging markets in EMEA.

Market Summary and Performance Review

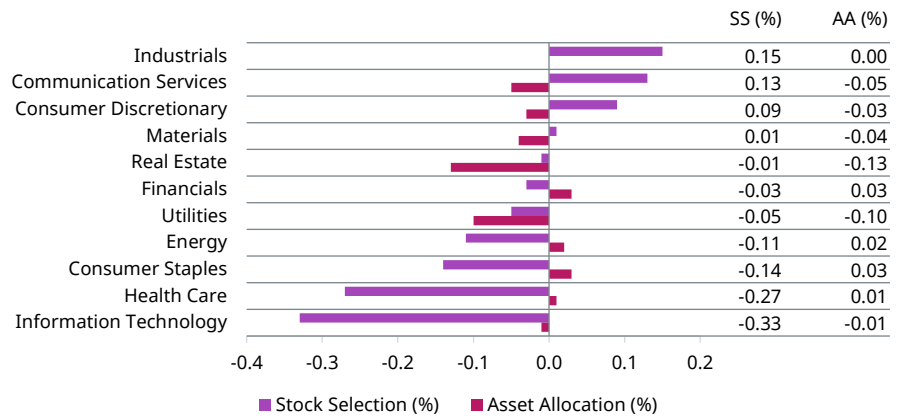
The strategy gave back a portion of the gains posted earlier in the year during the third quarter, with much of the impact seen in July. However, it remains well ahead of its benchmark over the year to date. Notably, the July underperformance was not dominated by the reversal in fortunes for the big index stocks (where we are now broadly neutral). Indeed, we have been actively taking profits and trimming hot positions all year, particularly in technology. Instead, it was driven more by investors covering lower quality shorts. The strategy was mainly impacted by a combination of us avoiding low quality rate sensitive areas, which were buoyed by expectations of rate cuts, and holdings in higher quality companies which underperformed. Performance for the rest of the quarter was largely flat despite the backdrop of market volatility which saw sharp swings in sentiment from the early August panic through to late September, when markets rallied following the Fed's pivot to rate cuts.

Outside of the big stocks, exposure to technology provided the greatest headwind as many areas previously in favour rolled over, most notably our holdings within the application software and semiconductor industries. Similarly, high quality defensives were a drag within health care and staples. The flip side of this was underexposure to interest rate sensitive areas (e.g. real estate sector and utilities) which rebounded due to a greater preference for bond proxies. Partially offsetting this, stock selection within higher quality industrials supported relative performance.

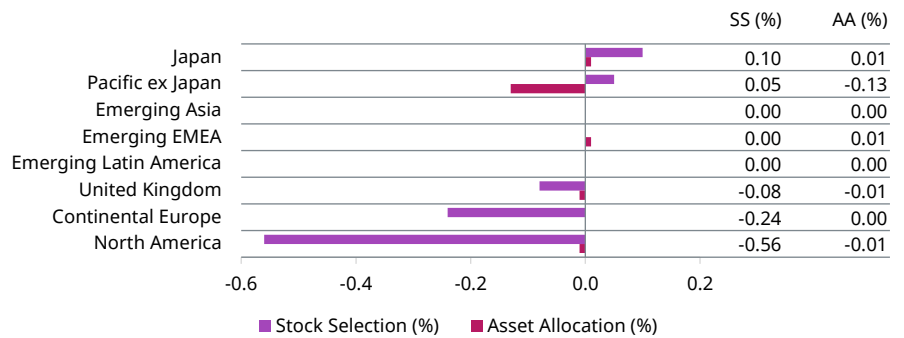
Schroders Schroder Sustainable Global Core PIE Fund

Relative Fund Performance vs MSCI World ex Tobacco

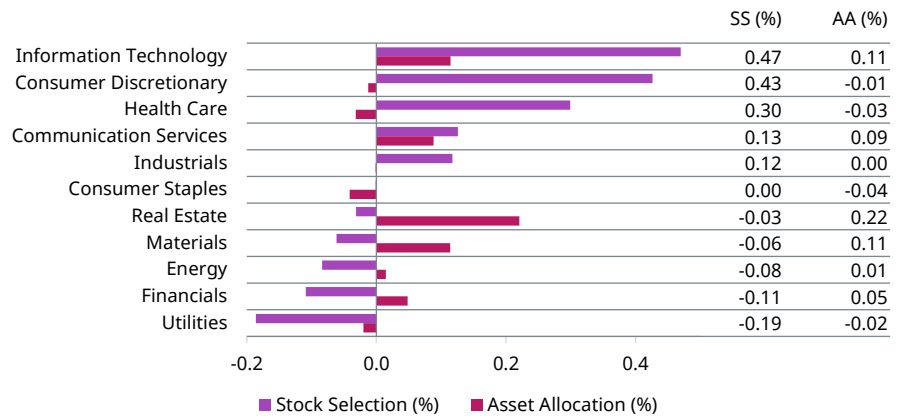
Sector
3 months to 30 Sep 2024



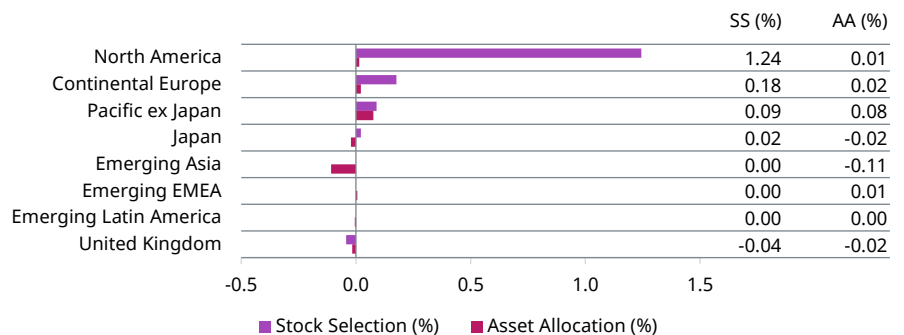
Region
3 months to 30 Sep 2024



Sector
Calendar Year to 30 Sep 2024



Region
Calendar Year to 30 Sep 2024



Source: Schroders & Investment Team Classifications. The above attribution is shown based on the unhedged portfolio and in USD terms.

Portfolio Activity and Policy

Across all our portfolios, the team continue to diversify exposure across a wide range of themes anchored in our assessment of both Quality and Value. Alongside this, the broader focus remains on maintaining a balanced exposure to help diversify the strategy's allocations and manage for a range of potential market outcomes. This remains of high importance as we look to navigate a period of uncertainty ahead.

To this extent, we have remained disciplined in our approach to rotating the portfolio opportunistically. Namely, we looked to capitalise on the volatility of July and August and allocated towards new opportunities higher up the quality spectrum. Prior to this, narrow breadth had resulted in better valuation prospects in overlooked companies. As opportunities to purchase higher quality names at better entry points opened, our process naturally repositioned. Within technology, having taken profits earlier in the year, we added selectively to application software, hardware and IT services. Elsewhere, we also topped up on higher quality cyclicals in financials and industrials. We focused on the highest financial strength names, increasing our allocation to both investment services and simple banks, although our preferred industry allocation remains within insurers, where we have gradually increased positioning over the year. In industrials, we are highly selective but allocated towards manufacturing and business services. In part this was funded from a reduction in our exposure to consumer staples, particularly home products.

At the end of the quarter, positioning remains balanced across structural growth, cyclical and defensive positions. Technology is again an overweight, focused on stocks demonstrating stronger growth characteristics alongside palatable valuations within application software, hardware and IT services. Elsewhere we remain discerning in financials due to balance sheet considerations, with our holdings mainly in insurers and high-quality diversified banks. In consumer discretionary, we retain a preference for retailers and homebuilders where valuations are more favourable. Within the more defensive parts of the market, we have rotated exposure, primarily reducing our position in less favourable industries, while retaining our longstanding overweight to pharmaceuticals within health care. We continue to focus on areas which help provide a hedge against potential downside risks, with the stocks we hold boasting some of the highest quality profiles in the market.

Regional allocations have not changed materially. We continue to hold a higher than index allocation to the US while maintaining a modest underweight to the UK and Europe which tend to offer deeper value opportunities.

Outlook

With most major global equity indices quickly shrugging off the volatility of July and August and ending the third quarter close to all-time highs, the buy on the dip trade appears to be alive and well. This does however hide an underlying current of nervousness. The question as to whether markets will hold on to these gains will largely depend on whether the widely expected global economic slowdown is of the hard or soft variety. The US Federal Reserve's short-term course is now clearer as it travels back to a neutral policy rate although even the Fed itself doesn't appear confident about what level this is. However, it seems unlikely that we will return to the ultra-loose policy that characterised much of the past decade. The market has clearly priced in a soft-landing but is also more optimistic than the Fed about the extent of rate cuts, which could spell disappointment ahead, but this already feels like a more traditional easing cycle rather than a necessary reaction to unforeseen events. To that extent, the Fed is doing its utmost to not fall behind the curve. This means that the shape of economic data in the coming months will remain critical, albeit the focus is likely to be more on the labour market than inflation.

Surveys of global equity investors suggest that they are uneasy bulls but will remain on the bandwagon for now. Strategists have been sorely wrong-footed by both the strength of global growth this year, most notably in the US, and the momentum behind equities. Whilst we still have another quarter to go, the S&P500 is currently more than 15% above the average end-year target predicted by strategists at the end of 2023 with most recent projections suggesting there is still more in the tank.

The few dissenters to this rosy outlook point to the yield curve which has recently uninverted after two years, which was itself the longest period of inversion by some margin since at least the late 1970s. Before each of the last six US recessions, the curve was inverted and for the four recessions since 1990, the inversion switched back to its normal upward slope prior to the onset of recession, driven by the expectation of falling short term rates. This time may be different but in general equities have performed well if a deep recession is avoided, which is why it's important that the Fed does not fall behind the curve.

There is also a US Presidential election to navigate this quarter which is likely to be a key driver of short-term volatility given the still very uncertain outcome. Recent research by Research Affiliates suggests that the political affiliation of the winning candidate in US elections has less bearing on markets than how close the election was. In the 24 US elections since 1928, the S&P500 generally weakened in the run up to a close election but then rallied in the

final week and continued to improve, albeit with greater volatility, after the election. History also suggests that markets do much better after a close election is resolved compared to when a landslide is the expected and realised outcome. Regardless, the market is probably going to struggle to make meaningful headway until the election is out of the way in early November. That said, the key message from previous elections based on longer time horizons is that markets often do not care who wins after the initial instability subsides.

The US election will also have implications for the US dollar. Trump is clearly advocating the benefits of a weaker currency to improve the country's trade deficit but his proposal to increase US trade tariffs is likely to have the opposite effect (e.g. the 2018-2019 US China trade war), particularly if tariffs are accompanied by looser fiscal policy (i.e. fewer rate cuts). The dollar (DXY index) declined by 5% during the third quarter in anticipation of looser monetary policy so some of this is already in the price, meaning that the risks are for dollar strength if Trump wins. If realised, this will be a headwind to emerging markets in particular.

After the Fed pleased the market with a 50bp rate cut in September, it was not a surprise to see a revival in Big Tech, but it was also fuelled by stock specifics as the AI land grab continues. Despite much short-term noise, as a group, they broadly matched the wider market during Q3 but with some dispersion, primarily weakness in Amazon offset by the stronger performance of Meta and Tesla (although Tesla was playing catch-up after a weaker start to 2024). Year to date, their performance is more than double that of the MSCI World index but this is purely attributable to Nvidia (+145%) and Meta (+62%) as the performance of the other "Magnificent 7" stocks are all within spitting distance of the index.

The big question is whether the big AI trade of the past 18 months will continue. Once again, fund managers appear to be increasingly cautious. The massive ramp up in AI related infrastructure investment has obviously benefitted the largest hyperscalers (Amazon, Microsoft, Meta) as well as Nvidia. However, the debate over whether this capex will be justified is becoming less clear cut. In a recent Goldman Sachs research report titled "Gen AI: Too much spend, too little benefit", the authors suggest that Big Tech and other corporates are expected to spend around \$1 trillion on capital expenditures in the coming years to support AI but so far have little to show for it. The paper suggests there we will see limited economic upside from AI over the next decade, arguing that the technology isn't designed to solve the complex problems that would justify the costs.

Despite the enormous investment, no one can convincingly argue that the capacity will be used and over what time frame. That said, there is also an awareness that AI will be increasingly important and, having learnt the lessons of the internet 20 years ago, few corporates will want to take the risk of missing out on a new disruptive technology. Advocates of the AI trade point to recent earnings reports where companies like Walmart and Amazon have started to explain how it is improving supply chains and reducing developer costs, which may go some way to allay concerns about return on investment. On the other side, Morgan Stanley is more in the "AI winter" camp suggesting that the global chip industry will soon face huge oversupply.

The consensus appears to be that AI is here to stay and we are not in a bubble but that the initial hype is unlikely to be sustained, which would be a healthy development from our perspective. As for the Magnificent 7, they all score well from a quality perspective except for Tesla although none are "cheap" with Alphabet appearing the least stretched. But neither are they egregiously expensive. Our best guess is that the increase in performance dispersion we have seen this year will continue rather than them trading in unison. The expected path of their earnings will therefore remain under heavy scrutiny in the quarters ahead.

There are also increasing reasons to argue that better opportunities are now to be found outside of the index behemoths. In particular, their contribution to EPS growth has already started to shrink and by the end of next year, it is forecast that they will only account for 25% of earnings growth for the S&P500 (broadly their weight in the index) with the other 493 stocks generating the rest. By way of comparison, in the second quarter of this year, the Mag 7 accounted for more than more than 80% of S&P500 earnings growth with Nvidia alone representing 25%. This suggests that the July/August rotation from semis and AI to bond proxies, defensives and beneficiaries of lower rates was rational, but much will still depend on the Fed and whether the elusive soft landing is achieved. If it is and rates fall more quickly than the market expects, it could be a good environment for cyclicals (materials & industrials) but these have already performed surprisingly well and much will depend whether the Fed is forced to cut by more to avoid a deeper downturn.

Amidst the rotation that characterised the third quarter, only the energy sector lagged consistently, and surveys suggest that fund managers are the most underweight the sector in four years. With signs of a recovery in oil production and an end to OPEC+ cuts alongside no evidence of a rebound in demand, the risks to oil prices would appear skewed to the downside, albeit the more recent escalation in the middle east conflict may prove otherwise.

At the risk of repeating ourselves, the wide range of potential outcomes ahead suggests that the best policy is to remain diversified, particularly given the very high dispersion of valuations across the broader market. Whether we look at the distribution of multiples or simple charts of cap weighted vs equally weighted indices, the narrowness of the market in recent years has set up a wide range of opportunities where valuations are not commensurate with fundamentals. This is not to say that the big trade going ahead will be to buy small and mid-cap Value stocks, as even many high-quality companies appear underpriced. Instead, it suggests that good stock selection will increasingly be important going ahead, whereas "beta" and the AI theme will increasingly become less of a driver of stock returns. This all bodes well for improving market breadth which suits our process well, particularly given that Big Tech no longer appears to be in the driving seat as earnings support broadens.

In summary, greater clarity on the scope for global policy accommodation as inflation returns to more normal levels and some signs that the AI hype is fading, has not created any more certainty about what the next market phase will look like, regardless of the US Presidential election. Our best guess is that it will be more of a range bound market with greater opportunities to exploit rotation as leadership transitions. Earnings will remain the dominant driver at the stock level, but this will be less about whether Nvidia beats or misses and more about recognising good value in the average stock, which has been left behind. Rotation into better prospects (affordable quality) is long overdue as the opportunity set in "Quality at a reasonable price" is unusually good. Quality is not restricted to typical defensives (e.g. pharmaceuticals, home products) but can also be found broadly across the market (e.g. insurers, business services).

We will also remain diligent in taking profits, particularly if volatility picks up, and use the capital to seek out oversold stocks whilst explicitly avoiding taking a view on the macro by being diversified across all sectors and regions. Portfolio construction & risk management will remain critical. From a bottom-up perspective, we aim to balance our portfolios across different flavours of Value and Quality to participate in a wider range of potential market environments. Our confidence that this will be the winning strategy for the next five years has increased in recent months.

Active Ownership

The QEP investment team works in close collaboration with Schroders' Sustainable Investment team to facilitate our engagement activity. Company engagements play an important role in our process, with the information gained key in helping us to understand the sustainability issues corporations face and the specific strategies they have in place to address them. It also allows us to promote change and make clear our transition expectations for the companies in which we invest. The central store of engagement information available to us, covering all Schroders firmwide engagements, also provides useful qualitative information on issues that may otherwise be difficult to capture from traditional ESG data sources. Schroders' engagement blueprint includes six priority engagement themes capturing issues relating to environmental (climate change, natural capital & biodiversity), social (human rights, human capital management, diversity & inclusion) and corporate governance.

Climate change and biodiversity continue to be key subjects of engagement, and we held engagements with several consumer staples companies on the topic of deforestation. With Kimberley Clark we sought to understand the company's strategy to manage forestry risks and plastics usage. The company confirmed that they have comprehensive practices in place. Specifically, Kimberley Clark conduct forest & agricultural land refreshing practices and are already in compliance with the EU's deforestation regulation (EUDR) ahead of time. This regulation applies to companies with exposure to certain commodities, with a requirement to demonstrate their products are not linked to forest degradation or illegal harvesting practices. The company also highlighted their intent to set more ambitious environmental targets, improving their forest land and agricultural practices and their ongoing efforts to reduce their plastic footprint. Future discussions are planned to delve further into the topics of water use and timelines for TNFD (Taskforce on Nature-related Financial Disclosures) reporting. In our discussions with Procter & Gamble they explained their increased support for smallholder farmers in their efforts to increase yields while minimising their environmental impact to meet sustainable production standards. While the company acknowledges traceability challenges for palm oil production, they are working on satellite monitoring capabilities to improve their exposure.

We also engaged with several pharmaceutical companies on a range of social and governance topics. We engaged with Pfizer on their Access to Healthcare initiative and approach to Antimicrobial Resistance (AMR). We requested further details on their progress in combating AMR and their targets for 2025 following the company's commitment to limit the discharge of pharmaceutical ingredients into wastewater. We also raised our concerns about the combined CEO/Chair role and the lengthy tenure of KPMG as auditor. We are awaiting the client's responses here but have encouraged them to re-evaluate their approach to better align with global best practice. We also engaged with Bristol-Myers Squibb on AMR, who highlighted their commitment to sustainable business practices and their Pharmaceutical Discharge Assessment Program. This program evaluates potential impacts of medicines on water ecosystems and human health. Furthermore, the company partners with the Pharmaceutical Supply Chain Initiative (PSCI) to implement supply chain best practices and reduce potential environmental impacts.

Our stewardship process extends to a proactive voting programme, a mechanism we leverage using the weight of Schroders' asset base and associated voting rights to drive our engagement priorities. We make considered use of our voting rights, acting in line with our fiduciary responsibilities in what we deem to be the best interests of our clients. As a firm, Schroders votes on all resolutions unless we are specifically restricted from doing so with all voting carried out by Schroders' corporate governance specialists. We voted at over 200 meetings on over 2,000 resolutions for companies held across the QEP desk in the third quarter of 2024. Within these votes, around 13% were not with management. Votes against management were focussed on compensation plans, the election of directors or auditor related. We voted against Linde's ratification of their current auditor given excessive auditor tenure. We also voted against Auto Trader's remuneration policy as we did not see their performance targets as sufficiently stretching and disagree with the addition of EPS Growth as a performance metric in their long-term incentive plan.

**Portfolio Characteristics
at 30 Sep 2024**

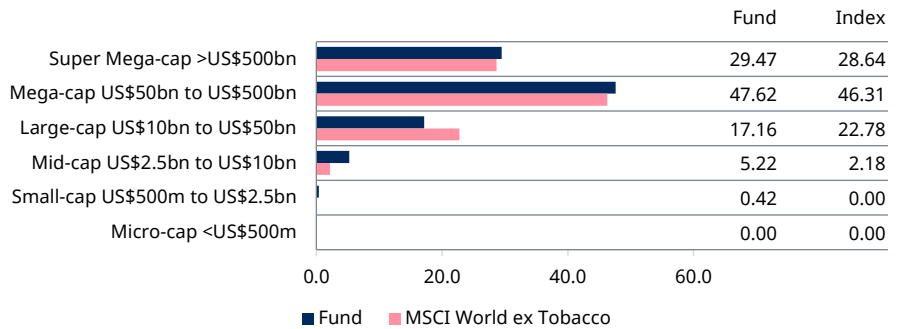
Characteristics	Fund	Index
Active Share	33.4%	-
Weight in non-index stocks	7.1%	-
Ex ante Tracking Error	1.2%	-
Beta	1.02	-
Number of stocks	467	1,405
Company Market Cap	723,868	710,482
Dividend Yield (Gross)	1.6%	1.7%
Carbon Intensity (CO2 t/M\$ Sales)	70.3	100.9

Source: Schroders & MSCI. Tracking Error is sourced from Aladdin.

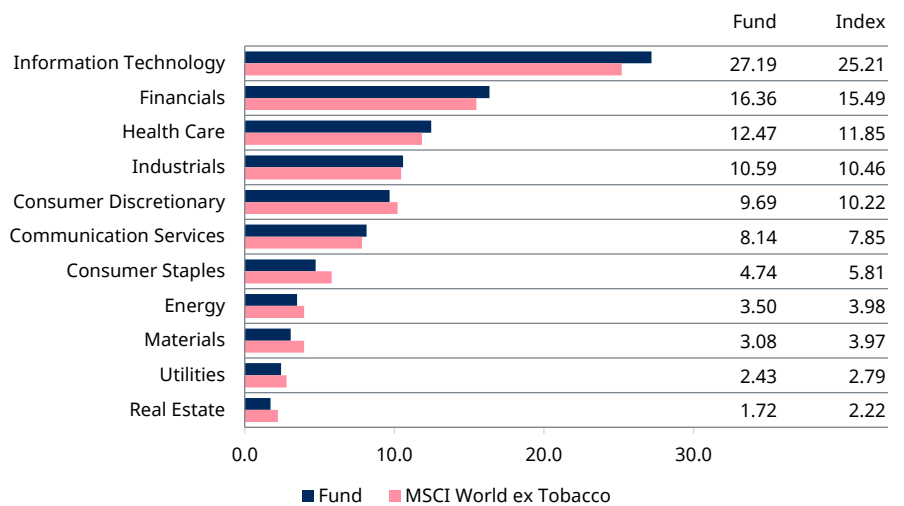
Index: MSCI World ex Tobacco

Portfolio Analysis

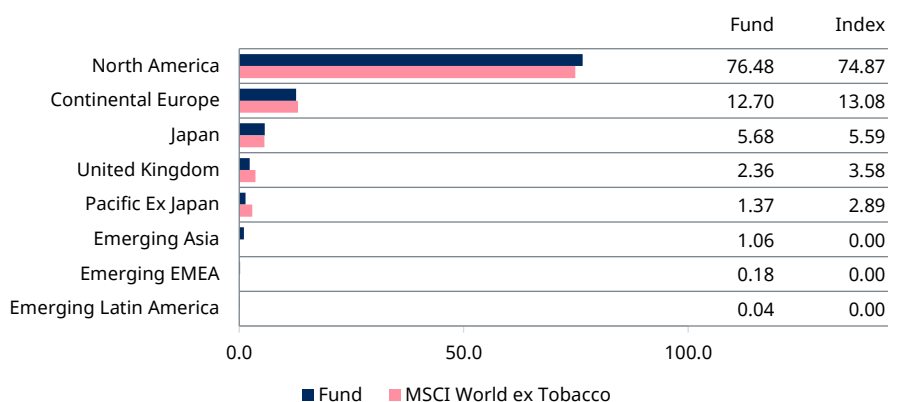
Portfolio Weightings Market Capitalisation (%) at 30 Sep 2024



Sector (%) at 30 Sep 2024



Region (%) at 30 Sep 2024



Source: Schroders & Investment Team Classifications

Notes

Responsible Investment: Schroders Socially Responsible Investment and Corporate Governance policies can be found on our website <http://www.schroders.com/global/about-schroders/corporate-responsibility/responsible-investment/>. We also publish regular articles on Socially Responsible Investing, which can be found on Schroders Talking Point www.schroders.com/talkingpoint.

Important Information

FundRock NZ Limited (FundRock) is the issuer of Schroder Investment Funds (Scheme). The Scheme's product disclosure statement (PDS) is available from FundRock, and on the Disclose Register (companiesoffice.govt.nz). The information contained in this document is not an offer of units in the funds within the Scheme, or a proposal or an invitation to make an offer to sell, or a recommendation to subscribe for or purchase, any units in the funds within the Scheme. Any person wishing to apply for units must complete the application form which is available from FundRock.

This document has been prepared by Schroder Investment Management Australia Limited, ABN 22 000 443 274, AFS Licence 226473 (Schroders) as the investment manager of the Scheme, and is intended solely for the information of the person to whom it is provided, and is subject to change without notice. In preparing this document, Schroders has relied upon and assumed, without independent verification, the accuracy and completeness of all information from available sources. Schroders does not give any warranty as to the accuracy, reliability or completeness of information which is contained in this document. Except insofar as liability under any statute cannot be excluded, Schroders and its directors, employees, consultants or any company in the Schroders Group do not accept any liability (whether arising in contract, in tort or negligence or otherwise) for any error or omission in this document or for any resulting loss or damage (whether direct, indirect, consequential or otherwise) suffered by the recipient of this document or any other person. This document does not contain, and should not be relied on as containing any investment advice (for the purposes of the Financial Markets Conduct Act 2013, as amended by the Financial Services Legislation Amendment Act 2019), or any accounting, legal or tax advice. Past performance is not a reliable indicator of future performance. Unless otherwise stated the source for all graphs and tables contained in this document is Schroders. For security purposes telephone calls may be taped. Third party data is owned by the applicable third party identified above and is provided for your internal use only. Such data may not be reproduced or re-disseminated and may not be used to create any financial instruments or products or any indices. Such data is provided without any warranties of any kind. Neither the third party data owner nor any other party involved in the publication of this document can be held liable for any error. The terms of the third party's specific disclaimers are set forth in the Important Information section at www.schroders.com.au. This disclaimer extends to FundRock, and any entity that may distribute this document.