Schroders

Marketing material for Singapore Investors only

Schroder Asian Growth Fund

Investment Report

1Q 2024

For illustrative purposes only and does not constitute a recommendation to invest in the Fund.

Schroder Investment Management (Singapore) Ltd.
Registered No. 199201080H Singapore.
Regulated by The Monetary Authority of Singapore.

Overview

Performance (as at end of March 2024)

Total returns in SGD

	1 mo. %	3 mo. %	YTD %	1 year %	3 years % p.a.	5 years % p.a.	Since inception* % p.a.
Portfolio	3.4	4.6	4.6	-1.0	-8.8	1.2	7.8
Benchmark**	2.9	4.7	4.7	5.6	-6.7	1.9	5.5
Difference	**+0.5**	**-0.2**	**-0.2**	**-6.5**	**-2.1**	**-0.7**	**+2.3**

Past performance is not a guide to future performance and may not be repeated. The value of investments and the income from them may go down as well as up and investors may not get back the amounts originally invested.

Source: Schroders, Morningstar. Please note that past performance is not indicative of future returns. Performance above reflects that of the Fund's SGD Share Class.

* Inception date: 8th May 1991.

** On 01/03/2016 the benchmark changed from MSCI AC Far East ex Japan (NDR) to MSCI AC Asia ex Japan (NDR). The full track record of the previous index has been kept and chain linked to the new one.

Market Summary

Asian equities achieved modest gains in the first quarter, with share prices bouncing back from recent lows and investors displaying cautious optimism that the gloom surrounding China may be starting to lift. Taiwan, India, and the Philippines were the strongest markets in the region while Hong Kong, Thailand, and China ended the quarter in negative territory. Stocks in Taiwan achieved strong growth in the quarter, driven by on-going investor enthusiasm for AI-related stocks and technology companies.

Despite rallying somewhat in the middle of the quarter, Chinese stocks still ended the quarter modestly lower as foreign investors remain cautious amid ongoing fears about the outlook for the Chinese economy. Stocks in Hong Kong also experienced sharp declines in the first quarter, with many investors looking to other markets amid ongoing fears over the state of China's post-pandemic economic recovery.

Indian stocks also performed well in the first quarter with investors hopeful that the political stability that has unpinned India's recent stock market growth will continue if Narendra Modi wins a third electoral victory this year. India has gained from overseas investment in manufacturing as companies seek to diversify supply chains outside of China, while the country's physical and digital infrastructure has also improved.

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Performance Review

Performance Review

Asian equities gained in the first quarter despite an initial challenging start to the year, as the rate cut outlook has lent support for a liquidity seeking AI-fueled growth, while robust holiday spending in China during the week-long Lunar New Year holiday, and accommodative monetary policies by the PBoC supported sentiment. Against such backdrop, the portfolio advanced, and outperformed the target benchmark. At the regional level, stock selection across Taiwan and Indonesia were the key contributors. Meanwhile, Hong Kong was mixed as the positive stock selection was offset by the overweight exposure as the market lagged behind regional return. From a sector perspective, stock selection in real estate, consumer discretionary, industrials and technology were notably positive, while selection in financials and consumer staples, coupled with overweight in real estate, partially trimmed some outperformance.

At the individual stock level, our select semiconductor holdings were among the key contributors over the quarter. Share price for leading Taiwanese foundry name, TSMC, was supported by solid growth outlook for 2024, and robust AI demand is expected to drive continuous margin expansion from advanced chips in the coming years. Similarly, fabless IC design house, Mediatek, was another notable contributor, supported by AI-driven re-rating story, and further abetted by China smartphone orders proving better than feared. Meanwhile, structural improvements in Indonesian macro and the removal of election uncertainty saw Indonesia's Bank Mandiri advancing higher, while 4Q23 net profits also came in above market expectation. HK-listed power tool maker, Techtronic Industries, traded higher on the back of 2H23 results beat, and solid revenue and earnings growth which are reaccelerating following two relatively sluggish years. Elsewhere, Indian retail mall operator, Phoenix Mills, rose as the company remains a strong proxy play for organized retailing and the growth of luxury brands in India. Significant asset additions and growing exposure to the affluent cohort locally also boosted sentiment on the stock.

On the negative side, our financial holdings detracted during the period. Regional insurer, AIA, declined on persistent macro headwind in Hong Kong and China, as well as elevated policy risk as its strong business growth from Mainland Chinese Visitors post Covid may draw regulatory scrutiny especially given the weakening balance of payment in China. Meanwhile, our Indian financial holdings, such as HDFC Bank, struggled along with the sector amid concerns around growth trajectory and margin pressure. Bandhan Bank also traded lower following a weaker set of 3Q results due to lower other income and higher provisions. Outside of financials, our healthcare name, Wuxi Bio, delivered disappointing performance because of investor concerns over the negative impact to its US business if the proposed biosecurity bill which limits the use of Chinese biotech companies on US taxpayer dollars is cleared by Senate. Elsewhere, Korea's battery maker LG Chem saw share price correction on investors' worries over slowing EV demand, while low chemicals margin and metal prices also remained key headwinds for near term earnings.

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Portfolio Activity

Key Purchases & Sales (3 Months as at end of March 2024)

Purchases	
Sk Hynix	Initiated position given its leadership in High Bandwidth Memory, making it a key beneficiary of the fast-growing trend on AI devices which are memory intensive and will likely drive higher memory content growth.
Ayala Land	Initiated position as the property developer name in Philippines is a positive beneficiary of expected rate cuts and improving residential demand.
Indusind Bank	Initiated position on the back of continued loan growth momentum in India, coupled with stable margins and controlled credit costs.

Sales	
TSMC	Trimmed position as single stock exposure exceeded 10% NAV limit following share price rally.
Phoenix Mills	Trimmed position to take profit in the Indian retail mall operator after strong outperformance.
Bandhan Bank	Exited position after another quarterly results miss driven by challenges in operating profit margin with higher opex and lower non-interest income.

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Market Outlook

After a difficult start to the year, broader Asian equity indices have continued to rebound and were modestly higher in March, tracking gains in broader global equities. Expectations for US monetary policy continue to ebb and flow with incoming data, and March saw a further reduction in the number of rate cuts priced into markets. This reflected stronger-than-expected economic growth and inflation data. Since the beginning of 2024, Fed fund futures have moved from pricing in six quarter-point interest-rate cuts this year to only three currently, with the first cuts now not expected until June. Despite this more hawkish rate outlook, sentiment towards equity markets remains benign as investors continue to discount a soft landing for the US economy. Consensus opinion is that growth will steadily slow in 2024, but there will be no recession and inflation will gradually ease towards the US Federal Reserve's (Fed) 2% target. Equity markets have also been buoyed by continued optimism around the AI theme globally, with bellwether stock Nvidia rallying another 15% in the last month as it unveiled its latest generation of processor chips; the shares are now up about 80% year to date. This 'goldilocks' US economic scenario – growth not too hot, or too cold – and the momentum behind large-cap technology stocks are a favourable backdrop for Asian markets. Taiwan and Korea were the strongest regional markets over the last month, benefiting from their heavy exposure to semiconductor stocks. Samsung Electronics and Taiwan Semiconductor Manufacturing Company (together comprising approximately 15% of the Asia ex-Japan index benchmark) rallied about 10% in March. Both are likely key beneficiaries of the accelerating rollout of AI server infrastructure globally.

In addition to the AI theme, investors have positioned for a broader improvement in demand and pricing for semiconductors and IT products in the coming quarters. End-market demand remains fairly soft, and inventories are still above average levels in some parts of the supply chain. However, recent comments from companies in the industry point to a stabilisation in the Chinese smartphone market and optimism about a modest rebound in personal computer and mainstream server demand through 2024. As inventories normalise, a more regular ordering pattern and improved pricing backdrop should allow for renewed top-line growth and better margins. Consumer electronics companies are starting to discuss a new generation of AI-enabled PCs and smartphones that may also help to encourage shorter replacement cycles and push up selling prices over time. As a result, we continue to think that the underlying structural drivers for semiconductors will remain strong in the coming years and valuations for large-cap industry leaders within the sector remain attractive. At the same time, however, we do have concerns that the recent excitement over the revenue potential for some companies in the AI supply chain may be excessive. This reflects heavy retail investor trading volumes in Taiwan, in particular, that have pushed valuations to very elevated levels.

In addition to gains in semiconductor memory stocks, Korean equities have found support this year from hopes that a new government-led plan to improve local corporate governance – the "Corporate Value-Up" plan – and hence valuations, could trigger a re-rating for the market. A similar initiative in Japan is credited with driving more market friendly behaviour by corporates in recent quarters, and helping deliver strong equity-market gains. The upside potential in Korea could be significant, given that historically the market has suffered from a material corporate governance discount against international peers. However, making broad generalisations about the potential 'winners' at this stage is difficult. So far, we are yet to see detailed proposals from the government and regulators, and the response from the key industrial 'chaebol' groups is unlikely to be uniform, given

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their different ownership structures and internal priorities. Much will also depend on the outcome of the upcoming presidential election in the middle of this year. Bottom-up, stock-by-stock assessments will be key to picking the real beneficiaries.

Indian equities have also performed very strongly in recent months. Sentiment towards the local economy and its longer-term potential remains very positive at a time when China's fortunes are increasingly being questioned by investors. A healthy domestic growth outlook, geopolitical tailwinds, the scope to increase market share in global manufacturing at the expense of China and steady domestic fund inflows into local equity markets are all factors in the market's favour. Valuations remain elevated in many sectors, so this positive outlook is well-discounted today – especially for small- and mid-cap stocks that have been the focus of domestic buying and where expansion in valuation multiples is most marked. We continue to see strong longer-term fundamentals in areas such as private-sector banks, healthcare and select consumer-related stocks, which remain core positions in regional portfolios.

While Taiwanese, Indian and Korean equities have continued to perform well year to date and sentiment in some areas of these markets is approaching euphoric levels, this remains in stark contrast to Hong Kong and China. In these markets, investors remain very cautious and valuations are close to historic lows. The slump in Chinese markets over the last year has been triggered by disappointing macroeconomic data and a lacklustre policy response. This, in turn, has undermined investor confidence, not only in the near-term cyclical outlook, but also in longer-term growth forecasts. Geopolitical tensions between China and the US also remain a serious overhang. In the face of these concerns, international investors have continued to reduce positions in Chinese equities.

After initial optimism over the rebound in economic growth following China's abandonment of Covid controls in late 2022, sentiment steadily deteriorated. The market view has swung towards a new consensus that the cyclical recovery is disappointing and the scope for stimulus is limited as China deals with deleveraging in its real estate sector and addressing local-government debt bubbles. Although we have seen a rapid normalisation in travel patterns and most other aspects of day-to-day life, consumer and business confidence are still fragile after two years of intermittent lockdowns and disruptions. A weak labour market, pressure on household incomes and falling property prices have all heightened concerns and depressed consumption. Although luxury spending has been more robust – as seen in the healthy results in the last year from leading European brands – 'down trading' is apparently common in the mass market, where the majority of consumers remain more cautious. Perhaps most importantly for the Chinese economy, the property market and the broader construction industry continue to deteriorate. Sales volumes have collapsed and prices are under pressure as buyers step back from the market and deflationary expectations set in. Developers are reluctant to start new construction projects, or are unable to, given their severe cash constraints. Many of the largest private players are facing solvency issues that are further undermining confidence in the pre-sale market as project completions are delayed in many cities. Given the huge scale of the construction industry, and all the related activities across China, this weakness remains a major headwind for broader economic growth. Property is also the largest store of household savings, so falling prices are likely dampening consumer confidence. Manufacturing industries, meanwhile, have also experienced a slowdown, reflected in much weaker recent Chinese export data,

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which is acting as a drag on private investment spending and job creation across the economy.

Given these very visible headwinds for growth, the debate among investors in recent months has moved away from China's cyclical upside potential towards a refocus on longer-term structural issues. These include a shrinking working-age population, the large debt overhang at the local government level, property market difficulties and elevated geopolitical risks; all are contributing to a more deflationary environment. Investors are impatient for renewed policy stimulus from the Chinese authorities to underpin demand, and a shortage of concrete policy measures in recent months has contributed to the market weakness. We have seen reductions in interest rates and an easing of downpayment requirements for mortgages. Additionally, the government has approved an extra borrowing quota to finance infrastructure investment. However, these measures are still deemed too small, given the scale of the problems. The drip feed of modest policy easing appears to have done little to shift broader consumer confidence and buyer sentiment towards the property market. We continue to expect further targeted stimulus measures in the coming months to provide an element of downside protection for the economy. However, there is little evidence currently that the authorities are considering much more aggressive fiscal measures to kick-start consumption and investment.

Despite the weaker headline macroeconomic data and property market troubles, the operating performance from the Hong Kong and Chinese equities we own has been more encouraging, as reflected in recent results. The strongest operating performance has been in the travel and leisure-related sectors – hotels, gaming, restaurants, luggage and beverage companies. Here, the rebound in activity and earnings in China has broadly met, or in some cases exceeded, initial expectations in the last year. E-commerce and online advertising sales have also seen a modest rebound, helping the key large-cap online players to deliver improved bottom-line growth, aided by greater cost discipline and, in some cases, aggressive share buybacks. All of this points to a broader economy, outside of the property development industry, that may be sluggish, but is not in a downward spiral. Unfortunately, in most cases, stock prices for these companies have remained under pressure, despite the healthier earnings. Where earnings disappoint, the market is extrapolating weakness. Where they have surprised positively, the market does not trust that this will be sustained. As a result, we have seen a dramatic de-rating of most segments in the Hong Kong and China markets in recent months as investor outflows have exaggerated share-price moves.

We share many investors' concerns about the structural headwinds China faces. A 'new normal' of much slower nominal GDP growth in China in coming years is our base case. However, given the extremes of negative sentiment, there is still room for the authorities to surprise positively with better-coordinated policy support going forward. This was evident in February, when markets bounced sharply in response to more proactive efforts by regulators to support local equity markets. In addition, better-managed businesses with stronger franchises can still deliver growth, even against a softer economic backdrop. There have also been signs of more 'self-help' among Chinese corporates recently, with a notable increase in dividend payouts and buyback activity, which is encouraging and may offer more downside support for stocks over time. After recent market weakness, share prices in many sectors in Hong Kong and China are not far off levels seen in the depths of the Covid restrictions when the earnings outlook was far more uncertain for most companies. Given this mismatch in share-price performance against

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operating fundamentals, and the current very low expectations for the Hong Kong and China markets, we continue to see attractive opportunities in selective areas on a bottom-up basis.

Aggregate valuations for regional equities are close to longer-term average levels. As usual, there remains a significant spread in multiples between those stocks and sectors in favour today, and the apparently 'deep value' on offer in less popular areas. Markets such as India and Taiwan that performed strongly in the last year are trading at marked premiums to their historical averages and expectations are very elevated. At the same time, the Hong Kong and China indices are sitting close to all-time low multiples as sentiment remains very depressed. Gains in Asian equities generally require a more stable global macroeconomic backdrop, a less hawkish Fed, reduced volatility in US-China relations and a more positive Chinese cyclical outlook. These factors are important to attract flows back into the market from foreign investors. Visibility remains limited on many of these fronts – most importantly the China policy backdrop in 2024 and the impact of the upcoming US elections. Nevertheless, we remain hopeful of a continued gradual recovery in activity in key stocks and sectors in China, and a rebound in technology sector fundamentals through 2024. This could underpin our preferred Asian equities over the medium term. In the meantime, we remain very selective in our exposure, given the continued uneven nature of the recovery in the region, and disciplined about valuations.

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China country risk: Changes in China's political, legal, economic or tax policies could cause losses or higher costs for the fund.

Counterparty risk: The counterparty to a derivative or other contractual agreement or synthetic financial product could become unable to honour its commitments to the fund, potentially creating a partial or total loss for the fund.

Currency risk: The fund can be exposed to different currencies. Changes in foreign exchange rates could create losses.

Derivatives risk: A derivative may not perform as expected, and may create losses greater than the cost of the derivative.

Emerging markets & frontier risk: Emerging markets, and especially frontier markets, generally carry greater political, legal, counterparty and operational risk.

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Leverage risk: The fund uses derivatives for leverage, which makes it 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.

Operational risk: Failures at service providers could lead to disruptions of fund operations or losses. Shanghai-Hong Kong Stock
Connect and Shenzhen-Hong Kong Stock Connect risk: The fund may be investing in China "A" shares via the Shanghai-Hong Kong Stock Connect and Shenzhen-Hong Kong Stock Connect which may involve clearing and settlement, regulatory, operational and counterparty risks.

Capital risk / distribution policy: the expenses of this share class are paid out of capital rather than out of investment income. Capital growth will be reduced and in periods of low growth capital erosion may occur.

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Schroder Investment Management (Singapore) Ltd
138 Market Street #23-01 CapitaGreen Singapore 048946
Telephone: 1800 534 4288 Fax: +65 6536 6626
Registration No.: 199201080H

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