Schroder Real Return Fund (Managed Fund) ASX Code: GROW

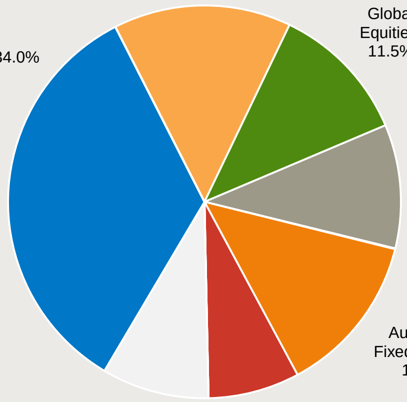
Monthly Report - May 2017 | **For more information about the Fund visit www.schroders.com.au/grow**

Total return %	1 mth	3 mths	1 yr	3 yrs p.a.	5 yrs p.a.	Inception
Schroder Real Return Fund (Managed Fund) (pre-fee)	0.28	2.12	-	-	-	5.59
Schroder Real Return Fund (Managed Fund) (post-fee)*	0.20	1.89	-	-	-	4.83

Portfolio inception 09/08/2016, 0 years and 9 months

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

Asset allocation



Fund objective

To deliver an investment return of 5.0% p.a. before fees above Australian inflation over rolling 3 year periods. Inflation is defined as the RBA's Trimmed Mean, as published by the Australian Bureau of Statistics.

RBA CPI Trimmed Mean* as at 31 March 2017

3 months	0.48%
1 year	1.86%
3 years. p.a.	1.97%
5 years. p.a.	2.18%

*The RBA CPI Trimmed mean returns are published quarterly by the ABS. Historical returns may be subject to revisions.

Portfolio refers to investment in the Schroder Real Return Fund (Managed Fund)

Unless otherwise stated figures are as at the end of May 2017

Portfolio review

May was a mixed month for investment markets and was reflected in a modest positive return for the Real Return Fund (ASX: GROW) of 0.2% (post-fees).

The most notable aspect of market behaviour in May was the rally in key sovereign bond markets matched by gains in key equity markets. Australian equities were the exception with weaker commodity prices impacting resources while banking stocks were hit by the politics of the bank levy in the May budget and growing questions about the resilience of the Australian economy and housing in particular. What's harder to reconcile is the dichotomy between bonds (reflecting more moderate growth numbers and still nonthreatening core inflation) and a resilient US equity market in the face of problematic valuations. While trying to over-finesse explanations about short term gyrations in asset prices is a mug's game, there is still clearly an element of "bad news is good news" as it keeps central bank support on the table.

From a performance perspective, while our duration, yield curve and currency positions captured some of these machinations, our preference for Australian equities over US equities was a drag.

Outlook and strategy

I regularly get asked about our views on individual markets. A key element of our investment process is the development of valuation conditioned return forecasts and these numbers naturally give us something to anchor our responses. While we are transparent in the provision of this information, it comes heavily caveated as to my knowledge at least there is no framework than can perfectly foresee the future and numbers are just that even though they do tend to take on a life of their own. We produce these numbers to help us systematically assess different information in a world that has an endless amount of "noise" with the end game to help us develop a portfolio. The reason we build portfolios after all is to manage through this uncertainty. If we had perfect foresight then a single asset portfolio would be fine.

I raise this seemingly obvious point to highlight the current debate about bonds and their worth to investors in a world where yields are still very low. The "why hold bonds when rates are low" argument has some intuitive appeal and we certainly have not been champions for the cause of ever increasing duration of bond benchmarks given the heavy distortions caused by deep pocketed central banks as they seek to reflate the global economy. But as portfolio constructors, operating in a world of perpetual uncertainty, the merits of bonds remain tantamount to robust portfolio construction. If you're a bond sceptic, then you should take a look at the numbers for May. The Bloomberg Composite Bond Index returned almost 1.2%, whereas Australian equities returned -2.75% for the same period (a difference in performance terms of almost 4%). Likewise, for 2017 so far Australian bonds have marginally outperformed Australian equities with volatility less than 1/6th the volatility of equities over that period. None of this is to say that we won't see periods where bonds are a drag on returns, but avoiding exposure because this might happen is a big risk.

2017 is interesting as the growth and inflation backdrop globally has erred on the reflationary rather than deflationary side (certainly compared to the start of 2016). What happens if deflationary fears resurface? Notwithstanding yields are still relatively low (and we'd argue below levels consistent with the pace of economic fundamentals), sovereign bonds will rally their socks off (as they did at the start of 2016), and equities will fall. Bonds will outpoint equities in this scenario by a significant margin.

Post-fee performance of other Real Return products offered by Schroders

	1 mth	3 mths	6 mths	1 yr	3 yrs p.a.	mFund Code
Schroder Real Return CPI Plus 3.5% Fund Wholesale*	0.23	1.39	2.77	4.97	N/A	SCH12
Schroder Real Return CPI Plus 5% Fund Wholesale*	0.12	1.80	3.57	6.14	4.80	SCH11

*Both funds on offer are unlisted. An application into these funds 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 Real Return CPI Plus 3.5 % Fund (Wholesale Class) is 0.60% and for the Schroder Real Return CPI Plus 5% Fund (Wholesale Class) is 0.90%.

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Outlook and strategy continued

To be clear this is not our central scenario, but as I pointed out above, we build portfolios because we don't have perfect foresight and will the world still inherently unstable this is not a scenario that can be discounted. And, even if the opposite scenario unfolds and bond yields do eventually normalise, the impact on portfolio returns from holding bonds themselves is likely to be small (even if moderately negative).

Consistent with the theme of ensuring downside protection we remain relatively defensively positioned in broad asset allocation terms. Our position in "risk" assets, defined as equities and global high yield credit is now around 28%, while cash (as our preferred "store of value") is just over 30%. The one change to the Portfolio worth noting in May was the addition of a cross market, interest rate position linked to an expected narrowing of the gap between very low yielding German Bunds and US Treasury bonds. This position continues the strategy of exploiting mispricing opportunities at a sub asset class level to help achieve our return objectives.

Investment style

Our approach to inflation plus (or real return) investing is to choose the portfolio that has the highest probability of achieving the required return objective over the investment horizon with the least expected variability around this objective. The Fund employs an objective based asset allocation framework in which both asset market risk premium, and consequently, the asset allocation of the portfolio are constantly reviewed. The portfolio will reflect those assets that in combination are most closely aligned to the delivery of the objective.

Fund details

ASX Code	GROW
Fund size (AUD)	$33,257,057
ASX Quoted Price	$3.6488
Fund inception date	August-2016
Management costs	0.90%
Distribution frequency	Normally twice yearly - June and December

Unless otherwise stated figures are as at the end of May 2017

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