Schroder Real Return Fund
ASX: GROW

A smarter way to invest. An easier way to grow your wealth.

Monthly Report - July 2017

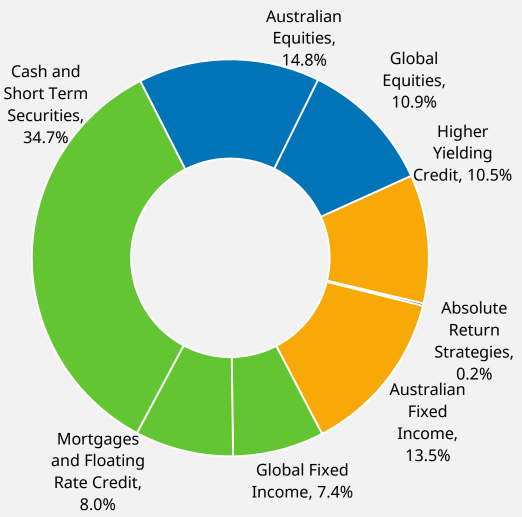
For more information about the Fund visit www.schroders.com.au/grow

Total return %	1 mth	3 mths	1 yr	3 yrs p.a.	5 yrs p.a.	Inception p.a.
Schroder Real Return Fund (Managed Fund) (pre-fee)	-0.13	-0.15	-	-	-	5.13
Schroder Real Return Fund (Managed Fund) (post-fee)*	-0.20	-0.38	-	-	-	4.22

Portfolio inception 09/08/2016, 0 years and 11 months

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

Asset allocation



* Includes floating rate notes, term deposits, negotiable certificate of deposits, cash and other cash equivalents.

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 30 June 2017

3 months	0.51%
1 year	1.84%
3 years. p.a.	1.91%
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 July 2017

Portfolio review

The Real Return Fund (ASX: GROW) returned -0.2% (post-fee) in July. We continue to position the portfolio with a defensive / downside risk focus against a backdrop of low yields, narrow credit spreads and extended equity valuations. In the near term, we don't expect the environment to get any easier and our capital preservation objectives remain in focus.

From a market perspective risk assets generally ground higher in July, with equities eking out modest gains and credit spreads contracting from already narrow marks. There was more action in currencies though with a weaker USD and hawkish minutes from the RBA sparking a 4% rally in the AUD while GBP was also weaker amid concerns about the economy and post the election result. Our currency positions were the most noteworthy drag on the strategy's returns in July.

Outlook and strategy

In recent reports I've discussed the appropriateness of the return objectives in the current environment and restated our view that it remains appropriate. Clearly "appropriate" and "easy to achieve" are not the same thing and getting there will be challenging. I've also highlighted the non-linearity of our return estimates – which in plain English means the potential for low / negative returns as markets restore (at some point) an appropriate risk premium. This challenge was evident in our July performance and I expect to remain evident until some sense / normality returns.

I was recently discussing our thoughts on the current investment environment with a client. I suggested that if all you knew about the state of the world were market valuations, you'd be ultra-defensive, have very little aggregate market exposure and mostly hold cash (well I would anyway). Alternatively, I suggested that if you knew nothing about valuations but was simply told that the global economy was chugging along at trend or above, that inflation was low and that while central banks were tinkering at the margin with rates and their rhetoric around policy settings, monetary policy was highly stimulatory and likely to remain so, you'd be likely long equities and risk assets more broadly. At the moment (and certainly in the most recent past) the cycle dynamics are winning out in the hearts, minds and investment preferences of the marginal price setters in the market. The challenge is that if you know both the valuation and the cyclical story you are faced with some difficult choices.

For perspective (and inspiration) I subsequently went back to some of the reports that I'd written in August 2007 (the dim, dark days pre- Global Financial Crisis (GFC))) to be clear what our thinking and positioning was in the fog that preceded the GFC proper. It was instructive and reminded me that 2007 was actually a good year for investors. Between January and October 2007 for example the Australian equity market had returned investors around 24% despite the fact that sub-prime crisis was starting to unravel. However in the August 2007 report for our Balanced Fund (virtually 10 years to the day of writing) I noted that the consensus (indeed our global house view) was that "*Fed easing, global economic resilience and a still healthy corporate sector mean a US recession can be averted*". Sound familiar? Not a great indictment for the consensus or our global house view for that matter! For the record, the Balanced Fund at the time had adopted a different position – significantly underweight risk assets and significantly overweight cash. On cash it was noted that "*The Fund is overweight defensive assets. We have raised cash reflecting both concern about equity valuations …. The Schroder Fixed Income Fund also has a relatively high cash weighting for similar reasons. We are looking for an opportunity to re-invest in riskier assets but believe that volatility will remain elevated in the near term and that with cash rates high it is prudent to be cautious.*"

Mark Twain is famously quoted "History doesn't repeat itself, but it often rhymes". To be clear, I'm not suggesting that GFC Mark II is imminent, but what I am suggesting is that there are enough parallels to be alert. Narrow credit spreads (and risk premium generally), overconfidence in the ability of Central Banks to steer the steady course and growing evidence of what I'd describe as "late cycle" behaviour on the part of investors (such as leverage and the ignoring of fundamental risk) top the parallels list.

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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*	-0.07	-0.05	1.33	3.83	N/A	SCH12
Schroder Real Return CPI Plus 5% Fund Wholesale*	-0.20	-0.37	1.60	4.62	4.21	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

On the other hand the financial sector is arguably in better shape and economic imbalances seem less evident. From a market perspective cash rates and yields generally are much lower – meaning the alternative to taking "risk" does not offer much incentive. But, when markets are correcting, a low positive return from a very liquid asset is still significantly more attractive.

The bottom-line is that we don't ultimately know what the future will bring, nor do we know what event or combination of events would cause markets to rethink their current course. We do know that valuations tell us there is very little "juice" left in the tank. Investors have the choice of holding on and riding the cyclical impulse or recognising that the risks around returns aren't stacking in favour of the investor in most assets.

With this in mind its worth highlighting that the Real Return Fund (ASX: GROW) has two objectives. The one that gets the most focus is returns. The other is a risk objective, and in particular the avoidance of downside risk. In late cycle investors often disregard the latter, just at the time when it's most important.

Fund details

ASX Code	GROW
Fund size (AUD)	$38,715,390
ASX Quoted Price	$3.5961
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 July 2017

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.

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