Monthly Newsletter

Schroder ISF# Global High Yield

Index data	YTW	OAS	YTD TR	MTD TR
GHY Corporate Index*	7.50	+535	4.82	(1.13)
Pan-European HY	8.23	+577	4.22	(1.80)
U.S. HY	7.32	+525	4.97	(0.97)
Cross-Over	5.66	+332	5.46	(1.00)
BB	6.07	+396	5.06	(0.75)
B	7.32	+525	4.51	(0.92)
CCC	9.71	+774	5.73	(1.28)
CC / C / D	12.98	+1066	5.70	(4.04)

Basic fund statistics	Fund	Index	Diff
Yield (YTW)	7.33	7.50	(0.17)
Duration (OAD)	4.18	4.36	(0.18)
Number of Issuers	249	1157	
Number of Bonds	365	2311	
Fund Size (US$ million)	6006.2		

Quality composition	Fund	Index	Diff
Cash	4.5	0.0	+4.5
- Net single-name CDS	-3.6	0.0	(3.6)
Governments	0.0	0.0	+0.0
Asset-Backed	0.3	0.0	+0.3
Cross-Over & Inv Grade	9.2	6.9	+2.3
BB	16.0	30.5	(14.6)
B	48.2	43.9	+4.3
CCC	23.5	16.0	+7.5
CC / C / D	1.1	2.3	(1.2)
NA / NR	0.7	0.4	+0.3

Regional composition	Fund	Index	Diff
North America	74.1	74.1	(0.1)
Europe	16.3	17.0	(0.7)
U.K.	6.2	4.6	+1.6
Asia	2.3	4.0	(1.7)
EEMEA	0.2	0.2	+0.1
South America	0.9	0.1	+0.8

Currency composition	Fund	Index	Diff
USD	82.1	81.0	+1.0
EUR	13.5	16.1	(2.7)
GBP	4.3	2.7	+1.6
other	0.2	0.2	+0.0

Total returns	SI	12 Mo	YTD	MTD
Fund – USD I shares[1]	74.05	16.42	4.38	(1.69)
Fund – USD A shares[2]	59.00	14.97	3.75	(1.76)
Benchmark*	83.84	15.05	4.82	(1.13)

Figures reflect periods through month-end 30 June 2011
Sources: Barclays Capital, Schroders FIA

[1] Schroder ISF Global High Yield USD I shares (ticker SCHHYDI)
[2] Schroder ISF Global High Yield USD A shares (ticker SCHHYDA)

* The benchmark for the Fund is Barclays Capital Global High Yield Corporate 2% Issuer Capped Bond Index, US$ Hedged

 # Schroder International Selection Fund is referred to as Schroder ISF throughout this document

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Market review: Macro uncertainties drive market volatility

The global high yield index* posted a total return of -1.13% in June, as weaker-than-expected economic data and concerns over a possible Greek default put pressure on risk assets generally. The yield on the global high yield benchmark peaked intra-month at 7.67% (higher by 67 basis points from May 31st), but a month-end rally brought yields back to 7.50%. On a spread basis, the move was even more dramatic given the volatility in underlying Treasuries, so that in the end, the OAS versus Treasuries widened 35 bps in June to +535, well inside of the intra-month wide mark of +572. Much of the late June spread narrowing resulted from a sell-off in Treasuries following improving prospects for Greece to be able to stave off an imminent default; the yield on the 10-year Treasury note rose 30 bps to 3.16% during the last week in June. Both the yield and the spread of the global high yield index now approximate the levels at which the year began (7.64% and +540, respectively, at 31 December 2010).

Consistent with the typical flight-to-quality pattern, US high yield outperformed Pan-European high yield and higher-rated credit uniformly outperformed lower quality – with CCCs posting a return of -1.28% for June. With the exception of emerging markets (+0.67%), most asset classes delivered negative returns in June as leveraged loans (-0.42%), the investment grade credit index (-0.73%), and even the US Treasury index (-0.34%) all lost ground given shifting investor sentiment. Major equity indices posted negative returns for June but they experienced a material bounce near month-end as did high yield – unlike commodities which was particularly hard hit and ended June with a -5.69% total return.

The CDS indices outperformed cash in June, as the CDX HY on-the-run index had a +0.15% return, compared to the -0.97% return on the US high yield bond index.

REITS, Consumer Non-Cyclical, Consumer Cyclical, Energy, and Communications were among the best performing sectors for the month, although all produced negative returns. The worst performers were Banking, Insurance, Other Industrial, and Capital Goods. (See table on page 2 for specific returns.)

Of the top performing industries, only restaurants produced a positive return for the month of June (a mere +0.06%). Other outperforming industries included refining, lodging, railroads, and airlines (all of which produced slight losses for the month that clustered between -0.09% and -0.23%). After banking, which was the worst performer for the second month in a row, other underperformers included packaging, life insurance and transportation services, all with returns slightly below -2%.

Among the 100 largest issuers in the index, the best performers were BB-rated issuers in more defensive industries such as healthcare, cable and media. In healthcare, Fresenius (+0.81%) and Community Health (+0.46%) were among the top performers, while cable and media credits Charter Communications (+0.40%) and Quebecor Media (+0.37%) also outperformed. The worst performers among the top 100 issuers included Commerzbank (-3.77%) and Royal Bank of Scotland (-3.21%) in the banking sector, as well as cyclical issuers such as Weyerhaeuser (-3.29%) and Reynolds Group (-4.31% and the worst performer in the top 100) in paper and packaging, and chemical producer Ineos Group (-2.97%).

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Index data	YTW	OAS	YTD TR	MTD TR
Basic Industry	6.97	477	4.02	(1.29)
Capital Goods	7.19	491	3.52	(1.45)
Communications	7.41	526	4.60	(0.89)
Consumer Cyclical	7.06	507	3.90	(0.80)
Consumer Non-Cyclical	6.93	491	4.25	(0.64)
Energy	7.08	490	5.28	(0.84)
Technology	8.07	589	6.80	(0.90)
Transportation	7.61	565	2.09	(1.29)
Other Industrial	7.45	533	2.16	(1.65)
Banking	12.36	958	7.26	(3.99)
Brokerage	9.07	739	6.11	(1.44)
Finance Companies	6.65	488	4.78	(1.13)
Insurance	10.84	811	10.99	(2.10)
REITS	5.95	410	5.45	(0.62)
Other Financial	8.16	614	5.01	(0.51)
Electric	9.20	668	7.92	(0.95)
Natural Gas	5.73	338	7.14	(1.15)
Total	7.50	+535	4.82	(1.13)

Sector breakdown	Fund	Index	Diff	
Basic Industry	9.0	8.4	+0.5	o/w
Capital Goods	6.7	8.8	(2.2)	
Communications	18.8	15.6	+3.2	o/w
Consumer Cyclical	16.9	18.7	(1.8)	
Consumer Non-Cyclical	5.4	11.2	(5.8)	
Energy	8.8	7.2	+1.6	o/w
Technology	8.1	5.2	+3.0	o/w
Transportation	2.8	2.7	+0.2	o/w
Other Industrial	0.3	1.9	(1.6)	
Banking	5.0	4.4	+0.6	o/w
Brokerage	0.0	0.2	(0.2)	
Finance Companies	6.2	5.5	+0.7	o/w
Insurance	2.5	1.2	+1.3	o/w
REITS	0.4	1.0	(0.6)	
Other Financial	0.4	0.6	(0.3)	
Electric	4.2	4.8	(0.6)	
Natural Gas	2.9	2.6	+0.3	o/w
Other Utility	0.3	0.1	+0.2	o/w
Total	98.6	100.0	(1.4)	
European ABS	0.3			
Cash & US Treasuries	4.5			

Credit default swap exposure (in %)	Fund
Single-name CDS longs	+3.8
Single-name CDS shorts	(0.2)
CDS index longs (CDX, iTraxx)	+0.0
CDS index shorts (CDX, iTraxx)	(2.1)
total gross exposure	+6.1
total net exposure	+1.5

Figures reflect periods through month-end 30 June 2011
Sources: Barclays Capital, Schroders
* The benchmark for the Fund is the Barclays Capital Global High Yield Corporate 2% Issuer Capped Bond Index
Please refer to the footnotes on the last page

Portfolio positioning

The Fund underperformed its benchmark* in June primarily due to our credit quality tilt. Industry exposure, issue selection, and yield curve positioning also detracted slightly from performance. An overweight to single-B and CCC-rated credits (where we think there is more deleveraging to come) at the expense of being very underweight low-yielding BBs, was the primary contributor to the Fund's underperformance amid the flight-to-quality trend in June. Currency exposure added slightly to relative returns, given the Fund's underweight to EUR bonds, which performed worse than USD or GBP high yield credit.

Given our view that much of the recent economic slowdown was attributable to temporary shocks, we consider interest rate risk to be a greater threat than default risk to fixed income returns over the next 12-18 months. We expect economic growth to be only modest in the 2nd half of 2011 and in 2012 but we still expect default risk to remain quite benign. We also expect bonds of several CCC issuers we own to be upgraded in the next year. While investor sentiment may temporarily turn cautious, at it did in May-June, we believe that higher-yielding lower-rated credits which are still on a deleveraging trajectory will outperform lower-yielding BBs over the next 6-12 months.

Our trading activity was lighter than usual during June, given limited liquidity during the market's most volatile periods, our view that the correction would prove to be a temporary setback and not the start of a bear market, and our desire to preserve cash. We allowed outflows to diminish our cash balance by 3% during the month as we anticipate a market turn soon. We continue to be extremely selective in participating in the new issue market, although we did participate in a number of higher quality deals across a diversified mix of industries – most of them more defensive in nature. Some of the new issues we bought included the 10-year B1/BB-rated notes of electric utility AES Corp at a 7.375% yield, the 8-year notes rated Ba3/BB- of Endo Pharmaceutical Holdings at a 7.0% yield, and the B1/B+ 8-year unsecured notes of Arch Coal Inc also at a 7.0% yield.

There were few changes to our sector weights during the month, although we did increase exposures in the Communications and Energy sectors modestly. After spread widening driven by concerns about a Greek sovereign default, we also added to our European banking exposure in select Tier 1 and Lower Tier 2 debt of top credit picks. Given our expectation for moderate growth in the second half of 2011, we have maintained exposures in those industries that will do well even in a slow growth environment including Communications, Technology and Energy; whereas, we remain cautious regarding consumer sectors and more cyclical industries facing growing headwinds with respect to input costs. Hence we sold or trimmed several positions such as JC Penney 7.40% Apr'37 unsecured bonds, Gymboree 9.125% Dec'18 and Jo-Ann Stores 8.125% Mar'19 – all retailers facing a weak US consumer and, in the case of Gymboree, getting pressured by rising cotton costs. In addition, we trimmed several high priced, low-yielding credits with little further capital appreciation potential, such as the unsecured notes of telecom provider Digicel Group Ltd 10.50% Apr'18 rated Caa1/B- at $114 for a 6.69% yield, and a recent USD new issue by European beverage producer Pernod-Ricard 5.75% Apr '21 notes rated Ba1/BB+ at $106 for a 4.95% yield (which had appreciated nearly $7 in less than 3 months).

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Key issues driving high yield valuations

Changes in the risk premium have once again been the primary driver of high yield valuations. Credit fundamentals have remained broadly positive, but investors continued to price in greater uncertainty associated with macro risks in June. Among the key issues facing the high yield market: weaker-than-expected global economic data, increased concern surrounding a potential Greek default, political posturing by leaders in Washington relating to the US debt ceiling, and the spillover effect of the Fed's attempts to auction off securities from its "Maiden Lane II" mortgage-backed portfolio. The sale of this portfolio, purchased from AIG at the height of the financial crisis, put technical pressure on risk markets as dealers and other traders sought to hedge against Fed-induced securitized spread widening via other more liquid markets.

Importantly, a number of these headwinds have been addressed, if only temporarily, leading to June's month-end market bounce. With respect to economic data, the latest ISM surveys have shown some improvement and there is growing evidence of a bounce back in Japanese production. While the data are likely to remain mixed near term, we believe the economy is poised to post moderate growth in the second half as temporary dislocations are resolved. Also, the recent approval of an austerity program in Greece paves the way for additional aid. Although we do not believe the current program addresses the long term insolvency issues, the probability of a near-term default is diminished. Finally, the Fed announced last week that further liquidations of its Maiden Lane II portfolio will be put on hold indefinitely.

A market correction – such as the one we are currently experiencing – can be healthy for the high yield market since it causes new issue volumes to slow down, investors to push back more on terms of the deals that do get priced, and it injects sobriety to the mindset of underwriters, issuers, and private equity firms. That was very evident during the month of June as new issue volumes fell dramatically from May's record levels, as a number of transactions were either cancelled or postponed and slightly less than $20bn in new issues priced globally.

Just as market volatility caused dislocation in the new issue market, high yield mutual funds were impacted as well, with redemptions rising to record levels. According to JP Morgan, June's outflow for high yield bond funds totaled -$6.1bn and included the largest weekly outflow on record. Nevertheless, net inflows still exceed +$4.7bn year-to-date. By quarter end, fund flows appeared to have stabilized, and demand from institutional investors such as insurance companies and pension funds began to surge again.

Against this challenging macro and technical backdrop, fundamental credit trends remain solid. Default risk remains benign, with forecasts for 2011 defaults centered around 1.5%. Once again during June, there were more rising stars upgraded to investment grade than there were fallen angels (triple-Bs downgraded to high yield), and there were also more upgrades than downgrades across the entire high yield universe (for the 22nd month in a row).

Market outlook

Despite the recent volatility, we continue to hold a positive outlook for the high yield sector for the full year, and believe that the market can continue to bounce back from the most recent correction. In fact, at the midway mark, the 2011 total return for the global high yield index (+4.82% ytd) is right on pace with our expected return of +10% for the full year.

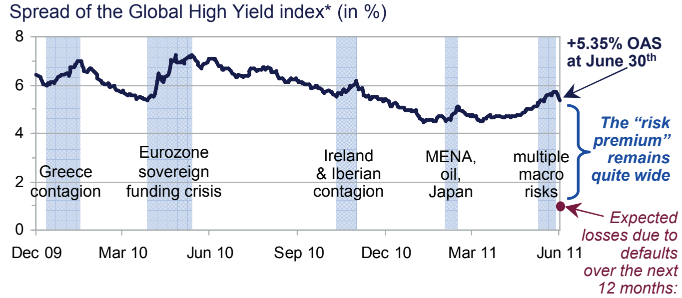
In our view, recent softness in economic data was magnified by temporary dislocations related the earthquake in Japan and production rebounds will likely provide a boost to growth soon. However, given remaining macro headwinds, growth will remain sluggish in the second half and the Fed will maintain its accommodative stance. This is constructive since economic growth of about 2% to 2.5% combined with ultra-low short-term rates is a supportive backdrop for high yield. The technical equation has started to come back into balance in recent weeks as supply has slowed, institutional demand has recently begun to pick up at wider spread levels, and cash is accumulating among investors from coupon payments and maturities. At the same time, valuations – which by April had started to become a constraint on further price appreciation – have already reset to levels where material upside is again possible. As the graph below illustrates, macro concerns drove risk premiums wider in May and June, but also led the snap back at the very end of the month as concerns eased and the flight to quality dissipated.[1]

Within the high yield market itself, credit fundamentals are supportive of valuations. Default risk is benign at this point in the credit cycle. We expect global high yield defaults to remain well below 3% for at least the next 2 years even if economic growth slows, since so many companies have been proactive in recent months in refinancing future bank loan and bond maturities. Liquidity and profit margins are at record levels and, while 2nd quarter earnings reports may begin to show margin compression from rising input costs for some companies, we expect that earnings releases overall could serve as a positive catalyst for the high yield market.

While European sovereign credit risk and debate relating to the US federal debt ceiling will continue to be sources of volatility, we believe that investors will gain more clarity on these issues as summer wears on, and risk markets will rally again before year-end.

Déjà vu: Macro risks triggered a correction in High Yield, for the fifth time in 18 months. During this downdraft, the GHY index yield rose 87 bps & the OAS widened 122 bps[1]

Spread of the Global High Yield index* (in %)



Source: Schroders, Barclays Capital; daily data through 30 June 2011

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*The benchmark for the Fund is the Barclays Capital Global High Yield Corporate 2% Issuer Capped Bond Index, US$ Hedged. Prior to November 2008, the benchmark was branded under Lehman Brothers, and prior to 1 August 2005, the unconstrained version of that index was used. A change in the Fund's benchmark to the 2% issuer capped index was made subsequent to the downgrade to high yield of General Motors and Ford Motor bonds in mid-2005, since those two issuers alone comprised more than 13% of the unconstrained index. In November 2008, all Lehman Brothers fixed income indices were rebranded under the Barclays Capital Indices.

Fund data reflects the Schroder ISF Global High Yield Class I USD Shares. Since Inception figures are since 16 April 2004, when the Fund commenced operations. Schroder International Selection Fund is referred to as Schroder ISF.

The source for all fixed income index data is Barclays Capital. The source for the total returns for Schroder ISF Global High Yield is from the NAV pricing of the Fund (as calculated by JPM Luxembourg and as published on Bloomberg). The source for all other Fund data is Schroders *Fixed Income Analytics*. Please note that there can be a slight difference between the portfolio composition break-down and other fund statistics reported in this publication when compared to final month-end fund publications – this is due to the one-day time lag between trades executed on the New York trading desk and reported by the Fund's accounting book of record versus the positions reported by the Fund's custodian domiciled in Luxembourg. (For example, if we trade on the last day of the month, statistics in this publication will be impacted whereas the reports generated by the custodian will not reflect such trading activity for month-end reports.) Also, please note that there is a timing difference between daily pricing of the NAV of the Fund in Luxembourg and the pricing of the index in the afternoon in New York; when there is material intra-day market volatility, this can have a meaningful impact on the return of the Fund compared to the index over a very short horizon.

The quality composition classification of bonds by rating in the table on the first page of this publication is based on the methodology of the *lower* of the ratings by either Moody's or S&P; whereas, the month-end Factsheet and other similar publications base ratings classifications on the higher rating of the three rating agencies, Moody's, S&P and Fitch. For example, a bond rated B1/BB- by Moody's and S&P, respectively, would be included in the single-B quality tier in this *High Yield Update* publication, whereas the Fund Factsheet would treat it a double-B. In both sets of publications, the quality tier classification is consistent in treatment for both the Fund and the benchmark. "NA / NR" refers to bonds with ratings not available or bonds not rated. Please note that since March 2010, we display a line item on the quality composition table that shows the net single-name CDS exposure as an offset against cash so that we can show the effect of CDS positions on the credit quality classifications and other portfolio composition lists. For example, if the Fund held a 3.7% net long risk position in singe-name CDS, then a –3.7% offset would be shown against the cash position, so that the percentage notional CDS held can be classified under each respective ratings category for the individual single-name CDS positions.

[1] A standard valuation framework with which to assess whether the high yield market is rich or cheap is based on the notion that investors need to be compensated in excess of the risk-free rate by an amount sufficient to cover expected losses due to defaults plus a healthy risk premium. The equation under this framework is that the High Yield OAS = ((1 - Expected Recovery Rate) * Expected Default Rate) + Risk Premium. Using current levels of the OAS on the global high yield index* of +5.35% versus Treasuries, an expected default rate of approximately 1.5% over the next 12 months, and an expected recovery rate in the range of 50% on the bonds that default, then current market valuations imply a risk premium of approximately 4.6%. The risk premium for high yield bonds has historically ranged between 1% and 5%, with only very brief episodes outside of that range; such levels have served as good contrarian sell and buy signals, respectively. Given the multiple macro risks present today, an elevated risk premium is understandable (to compensate for uncertainty in forecasts, mark-to-market price volatility, and an illiquidity premium in yield to compensate for the lower liquidity in the high yield market compared to Treasuries). The blue shaded regions in the graph on page 3 represent high yield market corrections since 2010.

Glossary of terms used in this document

Option-adjusted-spread (OAS) is the spread of a high yield bond relative to risk-free government bonds (US Treasuries), incorporating the value of any embedded call options in the high yield bond using a bond options pricing model. The OAS for the index or for the fund is just the weighted average OAS of the individual bonds comprised therein. OAS is expressed in basis points (hundredths of a percentage point).

Yield-to-worst (YTW), is similar to the yield-to-maturity (YTM) for a bond, but is a more appropriate statistic for callable bonds (where the issuer holds the option to call the bond at a date earlier than the final maturity, based on the bond's specific call schedule). More than half of the global high yield bond universe is comprised of callable bonds. Using YTW is a more conservative approach for investors to evaluate and compare bond yields, since the YTW will always be equal to or less than the YTM.

Option-adjusted duration (OAD) is the duration on the Fund, based on the weighted average duration of the portfolio of high yield bonds, calculated using Barclays Capital's options pricing model.

"TR" = total return; "YTD" = year-to-date; "MTD" = month-to-date. "S.I." = Since Inception total returns, for the period since 16 April 2004, which was the commencement date of the Fund. "Cross-Over" reflects bonds of issuers which have split ratings between investment grade and high yield by the three major rating agencies, Moody's, S&P, and Fitch. "IG" denotes investment grade rated bonds, which have ratings of Baa3/BBB-/BBB- or higher by Moody's, S&P, and Fitch, respectively. "Leveraged loans" returns reflect the Barclays Capital U.S. High Yield Loan Index. "CDS" are credit default swaps. "o/w" denotes those industry sectors in which the Fund is overweight versus the index.

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