Royal London Fixed Income Funds

Fund Manager Commentary – November 2022

FOR PROFESSIONAL INVESTORS ONLY, NOT SUITABLE FOR RETAIL CLIENTS.

ROYAL LONDON
ASSET MANAGEMENT

Contents

Economic Developments 3
RLAM Credit Fund Performance 4
Credit Market Review 5
Royal London Corporate Bond Fund 6
Royal London Ethical Bond Fund 8
Royal London Global Bond Opportunities Fund 10
Royal London Investment Grade Short Dated Credit 12
Royal London Short Duration Credit Fund 14
Royal London Sterling Credit Fund 16
Royal London Sterling Extra Yield Bond Fund 18
RLAM Government Bond Fund Performance 20
Government Bond Market Review 21
Royal London Global Index Linked Bond Fund 22
Royal London Index Linked Bond Fund 23
Royal London Short Duration Global Index Linked Bond Fund 24
Royal London Short Duration Gilt Fund 25
Royal London UK Government Bond Fund 26
RLAM Global High Yield Fund Performance 27
Royal London Global High Yield Bond Fund 28
Royal London Short Duration Global High Yield Bond Fund 30

ROYAL LONDON ASSET MANAGEMENT

Economic Developments

- The new Chancellor's Autumn Statement involved significant fiscal tightening, albeit backloaded with measures to raise revenue/cut spending by £55bn annually by 2027-28. Supportive for households (and, arguably inflation) going into 2023 were decisions to continue energy bill support, although less generously than before; uprate pensions and benefits in line with inflation; and increase the minimum wage by 10%.
- With high inflation and a tight labour market in the UK, the Bank of England hiked interest rates 75bps to 3%. Inflation jumped to 11.1% in October, driven by the increase in energy prices; core inflation remained at 6.5%. The November PMI composite business survey indicator was broadly unchanged, but remained consistent with falling output.
- The US mid-terms resulted in the Republicans taking the House, though by a smaller margin than expected, while the Democrats retained control of the Senate. Monetary policy was tightened again with the FOMC raising the Fed Funds target range by 75bps to 3.75%-4%. Inflation fell more than expected in October to 7.7%. October non-farm payrolls came in stronger than expected, though the unemployment rate rose to a still low 3.7%. The November composite PMI business survey indicator sank further below the 50 'no growth' mark, signalling contracting private sector output.
- There was no European Central Bank meeting in October, but policymakers continued to indicate that more rate hikes were likely. Eurozone CPI fell to 10.0%, though core was stable at 5.0%. Timely survey indicators of economic activity remained downbeat, but did improve slightly. The composite PMI business survey measure rose to 47.8 from 47.3, reportedly helped by fewer supply constraints, but still below the 50.0 'no growth level', signalling a contraction in private sector activity.

ROYAL LONDON ASSET MANAGEMENT

RLAM Credit Fund Performance

	1 month (%)	Rolling 12 Months (%)
RL Corporate Bond Fund Z Inc	**4.52**	**-15.51**
IA Sterling Corporate Bond Sector	3.96	-16.63
iBoxx Sterling Non-Gilts All Maturities Index	3.39	-17.29
RL Ethical Bond Fund Z Inc	**3.89**	**-16.55**
IA Sterling Strategic Bond Sector	3.18	-10.68
iBoxx Sterling Non-Gilts All Maturities Index	3.39	-17.29
RL Global Bond Opportunities Fund Z Inc	**3.59**	**-7.06**
RL Investment Grade Short Dated Credit Fund Z Inc	**1.97**	**-7.79**
IA Sterling Corporate Bond Sector	3.96	-16.63
ICE BofA ML 1-5 year Sterling Non-Gilt All Stocks Index	1.26	-7.41
RL Short Duration Credit Fund Z Inc	**1.93**	**-7.07**
IA Sterling Strategic Bond Sector	3.18	-10.68
ICE BofA ML 1-5 year Sterling Non-Gilt All Stocks Index	1.26	-7.41
RL Sterling Credit Fund Z Inc	**5.15**	**-15.64**
IA Sterling Corporate Bond Sector	3.96	-16.63
iBoxx Sterling Non-Gilts All Maturities Index	3.39	-17.29
RL Sterling Extra Yield Bond Fund A Inc	**3.59**	**-5.60**
RL Sterling Extra Yield Bond Fund B Inc	**3.55**	**-6.08**
RL Sterling Extra Yield Bond Fund Y Inc	**3.63**	**-5.19**
RL Sterling Extra Yield Bond Fund Z Inc	**3.61**	**-5.36**
IA Sterling Corporate Bond Sector	3.96	-16.63
IA Sterling High Yield Sector	3.03	-9.32
IA Sterling Strategic Bond Sector	3.18	-10.68

PAST PERFORMANCE IS NOT A GUIDE TO FUTURE PERFORMANCE. THE VALUE OF INVESTMENTS AND THE INCOME FROM THEM IS NOT GUARANTEED AND MAY GO DOWN AS WELL AS UP AND INVESTORS MAY NOT GET BACK THE AMOUNT ORIGINALLY INVESTED.
SOURCE: RLAM AND FE, CORRECT AS OF 30 NOVEMBER 2022. RETURNS QUOTED ARE NET OF FEES.
ALL IA SECTOR PERFORMANCE SHOWN IS FOR THE MEDIAN.
[1]PLEASE NOTE THAT THE BENCHMARK PRICING IS END-OF-DAY AND ENTAILS NO CURRENCY CONVERSION.

Credit Market Review

Market highlights – sterling investment grade credit

- Government bond yields fell (and prices rose) in November as investors increasingly discounted a recession in 2023 following further increases in interest rates after the central bank meetings early in the month. Although these were widely expected, the tone around future guidance remained hawkish.
- The benchmark 10-year gilt yield decreased by 36 basis points (bps) to 3.16% over the month, with gilts returning 2.82% to investors (FTSE Actuaries) on an all-maturities basis. In comparison, sterling investment grade markets returned 3.39% (iBoxx). The average investment grade credit spread (the average extra yield available from a corporate bond compared with government debt of equal maturity) narrowed by 16bps to 1.70%.
- Credit sector returns were positive across the board, but dispersions in return were wide. Subordinated insurance, utilities, healthcare and real estate were the strongest sectors. Supranationals and covered bonds were the weakest sectors, with senior banks also underperforming the broad market. Duration was positive as longer-dated bonds notably outperformed shorter-dated issues. The A and BBB ratings bands were the strongest, outperforming higher-rated issues: however, the sterling high yield index outperformed all the investment grade ratings bands.
- With the end of the LDI crisis and the Autumn Statement helping to stabilise UK bond markets, sterling issuance hit £9.5bn in November, the busiest month since January 2020. Euro issuance also rebounded, reaching €70.6bn, the third busiest month of 2022. In both markets, issuance was dominated by banks, which were particularly active before year end. The euro market also saw significant issuance from real estate companies, suggesting that investors are less worried about the outlook for this sector after several challenging months.

ROYAL LONDON ASSET MANAGEMENT

Royal London Corporate Bond Fund

Portfolio commentary

- The fund significantly outperformed its benchmark, the iBoxx Sterling Non-Gilts All Maturities Index, in November, and has also outperformed for the year to date.
- Government bond yields fell (and prices rose) in November as investors discounted a recession in 2023 following the interest rate rises early in the month. Along with tighter credit spreads, this delivered positive absolute performance.
- The fund's relative performance was boosted by the significant underweight in supranationals, which underperformed, and the overweight allocations in subordinated insurance, structured, social housing and real estate. Stock selection within sectors was positive, driven by utilities and insurance –negative stock selection from structured bonds was insufficient to offset this. Duration was a small positive for performance, moving around a broadly neutral position through the month.
- With the sharp recovery in primary activity, we participated in 11 new issues – 10 of which were from issuers in the financials sectors. We bought senior banks issues by **NatWest**, **Santander UK**, **Morgan Stanley** and **Crédit Agricole** (non-prefs), and subordinated banks issues from **HSBC**, **Barclays**, **Swedbank**, **Investec** and **NatWest**. We also participated in a subordinated insurance issue from **ASR Nederland**. Otherwise, we bought a new issue by **GreenSquareAccord**, the social housing provider.
- In the secondary market, activity largely focused on managing cashflows and rebalancing the shape of the fund. Otherwise, we took advantage of higher yields in some sectors following the market volatility of recent months. In financials, other than participating in new issues (particularly subordinated banks), we sold a number of senior banks bonds (including **Goldman Sachs**, **NatWest Markets** and **Fidelity International**); against these, we increased our exposure to subordinated insurance by buying bonds of **Scottish Widows**, **Legal & General**, **Aviva**, **Prudential** and **esure**. In the structured sector, we sold bonds of **Westfield Stratford** and **Telereal** and bought bonds of **Ribbon Finance** and **Thames Water**, and switched between bonds of **Heathrow** on enhanced terms. We made similar intra-sector switches in social housing (selling bonds of **GB Social** and **Sunderland** in favour of **Guinness Trust** and **The Housing Finance Corporation**, and switching between issues of **Saxon Weald**). Lastly, we reduced exposure to a number of bonds that have performed well in the challenging conditions so far this year: these included bonds of **Volkswagen**, **Vodafone**, **Orsted** and **Apple**. Finally, we added to our holding in UK public transport operator **First Group**: the company has transformed following asset sales and appears cheap with low leverage.

Investment outlook

- Despite recent inflation data and signs of increasing wage pressures, we expect inflation to peak in the coming months. This is driven by our view that energy prices will moderate and that weaker GDP growth will reduce the tightness of the labour market. It is likely that UK interest rates will rise during the early part of 2023 as the Bank of England continues to focus on inflation control.
- We believe that higher interest rates will lead to a UK recession, impacting company earnings and leading to some increase in default rates. Nevertheless, it is our view that the current asset allocation in favour of sterling credit bonds is appropriate as the widening in credit spreads this year has taken valuations to very attractive levels, on both a relative basis compared to government bonds and in absolute terms. We consider that credit spreads discount a significant portion of bad news and that investors are being paid well to take credit over government bond risk. Against this background, we will maintain our focus on identifying companies with strong balance sheets, favouring issues with security and downside protection, and ensuring that portfolios are diversified across issuers and sectors.
- The 'all-in yield' on sterling investment grade credit (government yield plus credit spread) is at the most compelling level for years, particularly if inflation starts to fall as we expect. Although some further volatility is likely, our recent preference for short-dated credit bonds is gradually easing as we begin to take on more duration risk – albeit not at the ultra-long end of markets where all-in yields still look challenging. The fund has a significant targeted exposure to BBB rated bonds, but we believe that compensation for default risk remains most attractive in this rating band.

Key views within the fund

- Well diversified, with over 300 holdings, in order to improve overall portfolio liquidity and to reduce the effect on overall fund performance of any deterioration in the creditworthiness of an individual holding.
- A significant underweight in supranational bonds, as we expect corporate bonds to outperform over the medium term.
- Duration marginally shorter than the benchmark at month end.

- An overweight position in subordinated financial debt, where we believe yields are attractive.
- Orientated towards secured bonds in the asset-rich investment trust, property and social housing sectors, and towards structured bonds, which benefit from a claim on assets and cashflows.
- Environmental, social and governance (ESG) risk factors are fully integrated in the management of the portfolio. The WACI (weighted average carbon intensity) of the portfolio is below that of the index.

Shalin Shah
Senior Fund Manager

Matt Franklin
Fund Manager

Jonathan Platt
Head of Fixed Income

ROYAL LONDON ASSET MANAGEMENT

Royal London Ethical Bond Fund

Portfolio commentary

- Net of fees, the fund outperformed its benchmark, the iBoxx Sterling Non-Gilts All Maturities Index, in November, and has also outperformed over the year to date, three years and five years.
- Government bond yields fell (and prices rose) in November as investors discounted a recession in 2023 following the interest rate rises early in the month. Along with tighter credit spreads, this delivered positive absolute performance.
- The fund's relative performance was boosted by the significant underweight in supranationals, which underperformed, and the overweights in subordinated insurance, structured, social housing and real estate. Stock selection within sectors detracted from performance, driven by negative stock selection in the structured and social housing sectors; positive stock selection in utilities and insurance was insufficient to offset this. Duration was a small positive for performance, as it was marginally longer than the benchmark through the month.
- With the sharp recovery in primary activity, we participated in five new issues – four of which were from banks. We bought subordinated banks issues from **HSBC**, **Barclays**, **Commerzbank** and **Investec**. Otherwise, we bought a new issue by **GreenSquareAccord**, the social housing provider.
- In the secondary market, we took advantage of higher yields in some sectors following the volatility of recent months. In financials, other than participating in new issues, we bought an attractive subordinated insurance 'legacy bond' of **Aviva**, and switched between a subordinated and a senior bond of **HSBC** to reduce risk on favourable terms. We sold bonds of **Penarian Housing** against the **GreenSquareAccord** new issue, and bonds of **ENEL** to raise liquidity for the other new issues – this also lowered the carbon profile of the fund. We also sold several bonds following resilient performance through the recent turbulence, including subordinated banks bonds of **Rothschild**, structured debt of **Lunar**, and bonds of **AT&T** and **Severn Trent**.

Investment outlook

- Despite recent inflation data and signs of increasing wage pressures, we expect inflation to peak in the coming months. This is driven by our view that the impact of energy prices on inflation will moderate once the anniversary of the Russian invasion of Ukraine passes and that weaker GDP growth will reduce the tightness of the labour market. It is likely that UK interest rates will rise further during the early part of 2023 as the Bank of England continues to focus on inflation control.
- We believe that higher interest rates will lead to a UK recession, impacting company earnings and leading to some credit downgrades. Nevertheless, it is our view that the current asset allocation in favour of sterling credit bonds is appropriate as the widening in credit spreads this year has taken valuations to very attractive levels, on both a relative basis compared to government bonds and in absolute terms. We consider that credit spreads discount a significant portion of bad news and that investors are being paid well to take credit over government bond risk. Against this background, we will maintain our focus on identifying companies with strong balance sheets, favouring issues with security and downside protection, and ensuring that portfolios are diversified across issuers and sectors.
- The 'all-in yield' on sterling investment grade credit (government yield plus credit spread) is at the most compelling level for years, particularly if inflation starts to fall as we expect. Although some further volatility is likely, our recent preference for short-dated credit bonds is gradually easing as we begin to take on more duration risk. The fund has a significant targeted exposure to BBB rated bonds, but we believe that compensation for default risk remains most attractive in this rating band.

Key views within the fund

- The fund is diversified in order to improve portfolio liquidity and to reduce the effect on overall performance of any deterioration in the creditworthiness of an individual holding.
- The fund has a significant underweight position in supranational bonds, as we expect corporate bonds to outperform over the medium term.
- Duration broadly in line with the benchmark.

- The fund has an overweight position in subordinated financial debt, where we believe yields are attractive.
- The fund remains orientated towards secured bonds in the asset-rich property and social housing sectors, and towards structured bonds, which benefit from a claim on assets and cashflows.

CITYWIRE A

Eric Holt
Senior Fund Manager

ROYAL LONDON ASSET MANAGEMENT

Royal London Global Bond Opportunities Fund

Market highlights

Index	Total return (%)	Spread movement (basis points)
HY global non-financial corps **ICE BofA ML global non-financial high yield index**	3.33	-42
AT1 **ICE BofA ML contingent capital index**	4.17	-31
IG global non-financial hybrid corps **ICE BofA ML global hybrid non-financial corporate index**	4.69	-48
HY global non-financial hybrid corps **ICE BofA ML global hybrid non-financial high yield index**	2.39	-13
Dollar investment grade corporate bonds **ICE BofA ML US corporate index**	4.92	-24
Sterling investment grade corporate bonds **ICE BofA ML sterling corporate and collateralised index**	4.13	-23
Euro investment grade corporate bonds **ICE BofA ML euro corporate and Pfandbriefe index**	2.72	-36

Source: Bloomberg

- The US mid-terms resulted in the Republicans taking the House by a smaller margin than expected, while the Democrats retained control of the Senate. Monetary policy was tightened again with the FOMC raising the Fed Funds target range by 75 basis points (bps) to 3.75%-4%. Inflation fell more than expected in October to 7.7%, although October non-farm payrolls came in stronger than expected. There was no European Central Bank meeting in November, but policymakers continued to signal further rate hikes. Eurozone CPI fell to 10.0%, though core was stable at 5.0%. The new UK Chancellor's Autumn Statement involved significant fiscal tightening, albeit the measures were backloaded. With high inflation (11.1% in October) and a tight labour market in the UK, the Bank of England hiked interest rates again.
- The benchmark 10-year US treasury yield ended the month lower at 3.61% (a decrease of 44bps). Meanwhile, the equivalent bund yield decreased by 21bps to 1.93%. Credit spreads tightened across all relevant markets, but most notably in the high yield emerging markets as various measures were introduced by the state that will support the economy, including an easing of the 'zero Covid' policy that has led to civil unrest in many cities.
- Euro investment grade issuance rebounded, reaching €70.6bn. With UK bond markets stabilising, sterling issuance hit £9.5bn in November, the busiest month since January 2020. In both markets, issuance was dominated by banks, which were particularly active before year end. The euro market also saw significant issuance from real estate companies, suggesting that investors are less worried about the outlook for this sector after several challenging months. Similar to prior months in 2022, new issuance remained well below the levels seen in 2020 and 2021, and was limited to the dollar market.

Portfolio commentary

- The fund (Z, Acc) recorded a gross return of 3.63% (3.58% net) in November. This particularly strong monthly performance came from our exposure to parts of the market that performed well in the 'risk on' environment, such as subordinated financials, corporate hybrids and high yield bonds. Furthermore, the fund is constructed to deliver an attractive level of income: it remains our view that this income and the fund's sectoral biases will deliver outperformance over the medium term.
- With the sharp recovery in primary activity, we participated in nine new issues – eight of which were from issuers in the financials sectors. We bought senior banks issues by **NatWest** and **Crédit Suisse**, and subordinated banks issues from **Lloyds**, **BNP Paribas**, **Société Générale**, **Commerzbank** and **Investec**. We also participated in a subordinated insurance issue from **ASR Nederland**. Otherwise, we bought a new hybrid issue by French utility **EdF**.
- In the secondary market, we took advantage of the recovery in markets to take profits in some bonds: otherwise, activity mainly focused on managing cashflows and maintaining the shape of the fund. In the banks sector, we added to the

ROYAL LONDON ASSET MANAGEMENT

NatWest new issue in the secondary market. We also sold some existing subordinated bonds against the new issues, including those of **Permanent TSB**, **Lloyds**, **Barclays** and **Credit Suisse**. We also exited a position in **Nordea** subordinated bonds following the significant recovery in the bonds from their lows. We also sold a number of non-financials bonds, including debt of **TUI Cruises**, **Fluvius, Subsea**, **Bouygues** and **Techem Blitz**.

Investment outlook

- We expect inflation to peak in the coming months as the anniversary of the Russian invasion of Ukraine passes in late February – the impact of oil and gas price rises in 2022 will drop out through base effects, and weaker GDP growth will reduce tightness in labour markets. Nonetheless, interest rates have risen sharply and weaker GDP growth will impact the corporate sector, and we expect to see some increase in credit downgrades and default rates. We will maintain focus on identifying companies with strong balance sheets, favouring issues with security and downside protection, and ensuring that the fund remains well diversified across issuers and sectors.
- Despite this outlook, we believe that the widening in credit spreads this year has taken valuations to attractive levels, on both a relative basis compared to government bonds and in absolute terms. Credit spreads discount a significant portion of bad news, and investors are being paid well to take credit over government bond risk. The yields on gilts, sterling investment grade bonds, European sub-investment grade bonds and global sub-investment grade bonds have risen sharply this year Investment grade credit is still close to its most compelling level for nearly 10 years, particularly if inflation starts to fall: furthermore, the fund delivers a yield premium to the market.
- Following three quarters of weakness in government bond markets and negative returns, the high yield market is pricing in a severe recession and offers excellent value. Defaults are currently at record lows, yet the market is discounting a major recession and commensurate level of defaults. Yet this takes no account of the much higher quality and more robust nature of the high yield market today, compared to 2008/9; nor of the current financial state of issuers as we head towards the downturn. Most issuers are in a stronger position than normal at this stage of a cycle and default and recovery expectations remain extremely benign.
- The fund's unconstrained approach across a broad spectrum of fixed income opportunities – encompassing investment grade, sub-investment grade and unrated bonds in a wide range of credit markets – means that risks are diversified, while providing considerable opportunities. Furthermore, the short duration of the fund should limit the impact of the volatility that may continue to impact government bond markets.

CITYWIRE A

Eric Holt
Senior Fund Manager

CITYWIRE A

Rachid Semaoune
Senior Fund Manager

ROYAL LONDON ASSET MANAGEMENT

Royal London Investment Grade Short Dated Credit

Portfolio commentary

- Net of fees, the fund outperformed its benchmark, the ICE BofAML 1-5yr Sterling Non-Gilt All Stocks Index, in November It has marginally underperformed this benchmark over the rolling 12-month period, but strongly outperformed over three and five years.
- Government bond yields fell (and prices rose) in November as investors discounted a recession in 2023 following the interest rate rises early in the month. Along with tighter credit spreads, this delivered positive absolute performance.
- The overweight exposure to subordinated financial debt, substantial underweight in supranational bonds, and bias towards secured and structured issues remained the most noticeable features of sector positioning.
- The fund's relative performance was boosted by the significant underweight in supranationals, which underperformed, and the overweight allocations to the subordinated insurance and structured sectors. Stock selection within sectors was also positive, driven by banks, insurance and utilities –negative stock selection in the structured sector was insufficient to offset this. Duration was marginally positive for performance as the fund's duration was slightly longer than that of the benchmark through the month.
- With the sharp recovery in primary activity, we participated in seven new issues, all of which were from issuers in the banks sector. We bought senior issues by **NatWest**, **Santander UK**, **Nationwide** (non-prefs) and **Crédit Agricole** (non-prefs), and subordinated issues from **HSBC**, **Swedbank** and **Investec**.
- In the secondary market, we took advantage of higher yields in some sectors following the market volatility of recent months. In financials, other than participating in new issues in the banks sector, we bought subordinated banks bonds of **Jupiter Fund Management**. We sold senior insurance bonds of **New York Life** as they had held up well in the recent volatility as well as subordinated bonds of **RSA Insurance**, **Scottish Widows** and **Society of Lloyds**. In the structured sector, we bought bonds including **AA**, **Unite** and **Telereal**. We sold a number of bonds to manage cashflows, including **NBHA** in the social housing sector; utilities **Wessex Water**, **Western Power Distribution** and **Northern Ireland Electric**; **AT&T**; and **The Great Rolling Stock Co**. Finally, we added to our holding in UK public transport operator **First Group**: the company appeared cheap and has transformed following asset sales that have greatly improved its leverage.

Investment outlook

- Despite recent inflation data and signs of increasing wage pressures, we expect inflation to peak in the coming months. This is driven by our view that energy prices will moderate and that weaker GDP growth will reduce the tightness of the labour market. It is likely that UK interest rates will rise during the early part of 2023 as the Bank of England continues to focus on inflation control.
- We believe that higher interest rates will lead to a UK recession, impacting company earnings and leading to an increase in credit rating downgrades. Nevertheless, it is our view that the current asset allocation in favour of sterling credit bonds is appropriate as the widening in credit spreads this year has taken valuations to very attractive levels, on both a relative basis compared to government bonds and in absolute terms. We consider that credit spreads discount a significant portion of bad news and that investors are being paid well to take credit over government bond risk. Against this background, we will maintain our focus on identifying companies with strong balance sheets, favouring issues with security and downside protection, and ensuring that portfolios are diversified across issuers and sectors.
- The 'all-in yield' on sterling investment grade credit (government yield plus credit spread) is at the most compelling level for years, particularly if inflation starts to fall as we expect. Although some further volatility is likely, our recent preference for short-dated credit bonds is gradually easing as we begin to take on more duration risk – albeit not at the ultra-long end of markets where all-in yields still look challenging. The fund has a significant targeted exposure to BBB rated bonds, but we believe that compensation for default risk remains most attractive in this rating band.

Key views within the fund

- The fund is diversified, with almost 300 holdings, in order to improve general portfolio liquidity and to reduce the effect on overall performance of any deterioration in the creditworthiness of an individual holding.
- It has a minimal weighting in supranational bonds, as we expect corporate debt to outperform over the medium term.
- Fund duration is marginally longer than the benchmark.
- It has an overweight position in subordinated financial debt, where we believe yields are attractive.

ROYAL LONDON ASSET MANAGEMENT

- The fund remains orientated towards structured debt, which benefits from a claim on assets and cashflows; secured issues in the asset-rich property and social housing sectors; and covered bonds (i.e. senior bank debt benefiting from a first claim on a specified over-collateralised pool of assets).

Paola Binns
Head of Sterling Credit

ROYAL LONDON
ASSET MANAGEMENT

Royal London Short Duration Credit Fund

Portfolio commentary

- Net of fees, the fund outperformed its benchmark, the ICE BofAML 1-5yr Sterling Non-Gilt All Stocks Index, in November. It has also outperformed over the rolling 12-month period, and strongly outperformed over three and five years.
- Government bond yields fell (and prices rose) in November as investors discounted a recession in 2023 following the interest rate rises early in the month. Along with tighter credit spreads, this delivered positive absolute performance.
- The fund's relative performance was boosted by the significant underweight in supranationals, which underperformed, and the overweight allocations to the subordinated insurance and structured sectors. Stock selection within sectors was also positive, driven by banks, utilities and insurance –negative stock selection in the structured and general industrials sectors was insufficient to offset this. Duration was marginally negative for performance as the fund's duration was slightly shorter than that of the benchmark at the start of the month. It was, however, in line with the benchmark at month end.
- The overweight exposure to subordinated financial debt, substantial underweight in supranational bonds, and bias towards secured and structured issues remained the most noticeable features of sector positioning.
- With the sharp recovery in primary activity, we participated in 10 new issues, all of which were from issuers in the banks sector. We bought senior issues by **NatWest**, **Santander UK**, **Nationwide** (non-prefs) and **Crédit Agricole** (non-prefs), and subordinated issues from **HSBC**, **Barclays**, **Swedbank**, **Commerzbank**, **Investec** and **NatWest**.
- In the secondary market, we took advantage of higher yields in some sectors following the market volatility of recent months. In financials, other than participating in new issues in the banks sector, we bought senior banks bonds of **Royal Bank of Scotland**, and subordinated banks bonds of **Leeds Building Society**, **Yorkshire Building Society** and **BPCE**, and added to the **HSBC** new issue in the secondary market. We also increased our exposure to subordinated insurance by buying bonds of **AXA**. Otherwise, we sold senior insurance bonds of **New York Life** as they had held up well in the recent volatility. In the structured sector, we bought bonds including **AA**, **Summit Finance**, **Heathrow**, **ICSL** and **Meadowhall**. We also sold short-dated bonds of **Volkswagen** that have no spread duration.

Investment outlook

- Despite recent inflation data and signs of increasing wage pressures, we expect inflation to peak in the coming months. This is driven by our view that energy prices will moderate and that weaker GDP growth will reduce the tightness of the labour market. It is likely that UK interest rates will rise during the early part of 2023 as the Bank of England continues to focus on inflation control.
- We believe that higher interest rates will lead to a UK recession, impacting company earnings and leading to an increase in credit rating downgrades. Nevertheless, it is our view that the current asset allocation in favour of sterling credit bonds is appropriate as the widening in credit spreads this year has taken valuations to very attractive levels, on both a relative basis compared to government bonds and in absolute terms. We consider that credit spreads discount a significant portion of bad news and that investors are being paid well to take credit over government bond risk. Against this background, we will maintain our focus on identifying companies with strong balance sheets, favouring issues with security and downside protection, and ensuring that portfolios are diversified across issuers and sectors.
- The 'all-in yield' on sterling investment grade credit (government yield plus credit spread) is at the most compelling level for years, particularly if inflation starts to fall as we expect. Although some further volatility is likely, our recent preference for short-dated credit bonds is gradually easing as we begin to take on more duration risk – albeit not at the ultra-long end of markets where all-in yields still look challenging. The fund has a significant targeted exposure to BBB rated bonds, but we believe that compensation for default risk remains most attractive in this rating band.

Key views within the fund

- The fund is diversified, with more than 300 holdings, in order to improve overall portfolio liquidity and to reduce the effect on overall performance of any deterioration in the creditworthiness of an individual exposure.
- The fund has a significant underweight in supranational bonds, as we expect corporate debt to outperform over the medium term.

- The fund's duration was in line with that of the benchmark at month end.
- The fund has an overweight position in subordinated financial debt, where we believe yields are attractive.
- The fund remains orientated towards secured bonds in the asset-rich investment trust, property and social housing sectors, and towards structured issues, which benefit from a claim on assets and cashflows.

Paola Binns
Head of Sterling Credit

ROYAL LONDON ASSET MANAGEMENT

Royal London Sterling Credit Fund

Portfolio commentary

- Net of fees, the fund significantly outperformed its benchmark, the iBoxx Sterling Non-Gilts All Maturities Index, in November, and has also outperformed for the year to date.
- Government bond yields fell (and prices rose) in November as investors discounted a recession in 2023 following the interest rate rises early in the month. Along with tighter credit spreads, this delivered positive absolute performance.
- The fund's relative performance was boosted by the significant underweight in supranationals, which underperformed, and the overweight allocations in subordinated insurance, structured and social housing. Stock selection within sectors was also positive, driven by insurance, utilities and banks –negative stock selection from structured bonds was insufficient to offset this. Duration was neutral for performance as it was broadly in line with the benchmark through the month.
- The overweight exposure to subordinated financial debt, substantial underweight in supranational bonds, and bias towards secured and structured issues remained the most noticeable features of sector positioning.
- With the sharp recovery in primary activity, we participated in 13 new issues – 12 of which were from issuers in the financials sectors. We bought senior banks issues by **NatWest**, **Santander UK**, **Morgan Stanley**, **Nationwide** (non-prefs) and **Crédit Agricole** (non-prefs), and subordinated banks issues from **HSBC**, **Barclays**, **Swedbank**, **Commerzbank**, **Investec** and **NatWest**. We also participated in a subordinated insurance issue from **ASR Nederland**. Otherwise, we bought a new issue by **GreenSquareAccord**, the social housing provider.
- In the secondary market, we took advantage of higher yields in some sectors following the market volatility of recent months. In financials, other than participating in new issues (particularly in the banks sector), we bought senior banks bonds of **IG Group** and **Santander UK**, and subordinated banks bonds of **Royal Bank of Scotland** and **Lloyds**. Otherwise, we exited our position in **Nordea** subordinated bonds as they had rallied significantly from their lows. We also increased our exposure to subordinated insurance by buying bonds of **Legal & General**, **Aviva** and **AXA**. In the structured sector, we bought bonds of **Telereal**, **Arqiva** and **Juturna Euro Loan Conduit**. We made an intra-sector switch in social housing, selling bonds of **Sunderland** in favour of **Saxon Weald**. Finally, we added to our holding in UK public transport operator **Stagecoach**: the company appeared cheap and has better security over assets following its recent acquisition.

Investment outlook

- Despite recent inflation data and signs of increasing wage pressures, we expect inflation to peak in the coming months. This is driven by our view that energy prices will moderate and that weaker GDP growth will reduce the tightness of the labour market. It is likely that UK interest rates will rise during the early part of 2023 as the Bank of England continues to focus on inflation control.
- We believe that higher interest rates will lead to a UK recession, impacting company earnings and leading to an increase in credit rating downgrades. Nevertheless, it is our view that the current asset allocation in favour of sterling credit bonds is appropriate as the widening in credit spreads this year has taken valuations to very attractive levels, on both a relative basis compared to government bonds and in absolute terms. We consider that credit spreads discount a significant portion of bad news and that investors are being paid well to take credit over government bond risk. Against this background, we will maintain our focus on identifying companies with strong balance sheets, favouring issues with security and downside protection, and ensuring that portfolios are diversified across issuers and sectors.
- The 'all-in yield' on sterling investment grade credit (government yield plus credit spread) is at the most compelling level for years, particularly if inflation starts to fall as we expect. Although some further volatility is likely, our recent preference for short-dated credit bonds is gradually easing as we begin to take on more duration risk – albeit not at the ultra-long end of markets where all-in yields still look challenging. The fund has a significant targeted exposure to BBB rated bonds, but we believe that compensation for default risk remains most attractive in this rating band.

Key views within the fund

- Well diversified, with around 350 holdings, in order to improve overall portfolio liquidity and to reduce the effect on overall performance of any deterioration in the creditworthiness of an individual holding.
- A significant underweight in supranational bonds, as we expect corporate bonds to outperform over the medium term.
- Duration in line with the benchmark at month end.

ROYAL LONDON ASSET MANAGEMENT

- Orientated towards subordinated financial debt, where we believe yields are attractive.
- The fund remains orientated towards secured bonds in the asset-rich investment trust, property and social housing sectors, and structured bonds, which benefit from a claim on assets and cashflows.

Paola Binns
Senior Fund Manager

ROYAL LONDON ASSET MANAGEMENT

Royal London Sterling Extra Yield Bond Fund

Portfolio commentary

- In November, the fund posted returns of 3.59%, 3.55%, 3.63% and 3.61% for the A, B, Y and Z class shares, respectively. These bring 2022 year-to-date returns to -5.59%, -6.03%, -5.22% and -5.37%, respectively for these share classes.
- Sterling fixed interest markets continued their recovery in November after the sharp downturn spanning August and September. Gilts posted a 3.00% index return on the month, with yields on longer-dated gilts falling much more than short-dated bonds – yields on two-year gilts were virtually unchanged on the month, reflecting little change in the outlook for the path of the UK bank rate. Despite having lower average duration than gilts, sterling investment grade corporate bonds delivered a stronger index return in November of 3.40%, reflecting a narrowing of the average yield differential over reference gilts from 1.84% to 1.67% in the month. High yield markets also benefitted from the progressive recovery in bond markets, with European sub-investment grade bonds and global sub-investment grade bonds posting index returns of 3.72% and 3.24%, respectively, in November. Year-to-date returns for these four asset classes – gilts, sterling investment grade corporate bonds, European sub-investment grade bonds and global sub-investment grade bonds – were -21.60%, -16.30%, -10.82% and -11.75%, respectively, to the end of November.
- Unsurprisingly, the financial sectors of banking and insurance were particularly sensitive to the improving market conditions, with bonds of insurers **Aviva**, **Bupa**, **M&G** and **Scottish Widows** and of banks **Nationwide** and **Nordea** up around 10% in price on the month. Another area of particular strength was 'hybrid' bonds, where the issuer has optionality to extend maturity beyond the first call date, but at an increasingly penal interest cost – such bonds of French utility **EDF** in particular performed strongly in November, with a near 10% capital return. Other holdings posting strong positive performance were **REA Holdings**, the agriculture business that announced strong results and payment of preference share dividends deferred during the Covid period; offshore energy sector company **Boa**, whose secured bonds recovered strongly reflecting continued buoyancy in asset prices; commodities business **Metalcorp** addressing a short-term liquidity squeeze in the business; and long-dated secured bonds of **Swan Housing**, up over 20% in November reflecting both the decline in gilt yields in the month and recovery from the markdown in price on the downgrade to BB in October when the bonds were purchased. Performance was also enhanced by corporate activity, including offshore energy sector **Bluewater**'s early repayment of 2023 bonds refinanced with a new issue, and tenders by **HSBC** and **Investec** for 'old-fashioned' lower tier two bonds, now less efficient as regulatory capital also issuing new bonds. Such occasions typically provide both a fillip to the value of existing holdings and an opportunity to invest in the new issue.
- Much of the activity in the month was in the financial sectors, in part reflecting a flow of very attractively priced new issues into still potentially volatile and fragile markets. These included bonds of **Commerzbank**, **Investec**, **Santander UK** and **Societe Generale**. Most notable perhaps were new issues from **Barclays** and **HSBC**, each issued early in the month, each lower tier 2 capital with first calls at five years and seven years, respectively, with potential five-year extensions, with investment grade ratings and offering yields of 8.4% and 8.2%, respectively. All these new issues have performed strongly. A new issue of **NatWest** 6.375% five-year A rated senior bonds purchased in the month was subsequently sold, crystallising a 3% capital profit. Market purchases in the financial sectors in November included bonds of **Brit Insurance**, **Aviva**, **Axa** and **Jupiter Fund Management**, while sales included **Nordea** and **Zurich Insurance**. In other sectors, we purchased a new issue of energy sector business **M Vest Energy** – the company benefits from the very supportive Norwegian tax regime for energy companies and, while a small unrated issue, the bonds offered a yield of over 13% for their three-year term. Other purchases included secured bonds of pubs business **Fuller, Smith & Turner**, while sales included bonds of shipping business **Euronav** and of offshore services business **DOF Subsea**. Activity in the month in short-dated gilts reflected short-term cash management, with net sales of gilts in the month facilitating investment in the attractively priced new issues mentioned above.

Investment outlook

- Despite recent inflation data and signs of increasing wage pressures, we expect inflation to peak in the coming months. This is driven by our view that energy prices will moderate and that weaker GDP growth will reduce the tightness of the labour market. It is likely that UK interest rates will rise during the early part of 2023 as the Bank of England continues to focus on inflation control.
- We believe that higher interest rates will lead to a UK recession, impacting company earnings and leading to some increase in default rates. Nevertheless, it is our view that the current asset allocation in favour of sterling credit bonds is appropriate as the widening in credit spreads this year has taken valuations to very attractive levels, on both a relative basis compared to government bonds and in absolute terms. We consider that credit spreads discount a significant portion of bad news and that investors are being paid well to take credit over government bond risk. Against this

ROYAL LONDON ASSET MANAGEMENT

background, we will maintain our focus on identifying companies with strong balance sheets, favouring issues with security and downside protection, and ensuring that portfolios are diversified across issuers and sectors.

- The 'all-in yield' on sterling investment grade credit (government yield plus credit spread) is at the most compelling level for years, particularly if inflation starts to fall as we expect. Although some further volatility is likely, our recent preference for short-dated credit bonds is gradually easing as we begin to take on more duration risk – albeit not at the ultra-long end of markets where all-in yields still look challenging. The fund has a significant targeted exposure to BBB rated bonds, but we believe that compensation for default risk remains most attractive in this rating band.

Key views within the fund

- The fund's objective is to achieve a high level of income by seeking attractive investments across a broad spectrum of fixed income opportunities, encompassing investment grade, sub-investment grade and unrated bonds.
- The fund mitigates stock-specific risk by holding a diversified portfolio of investments, so that no individual investment can in isolation have an undue impact on overall performance. In addition, where possible within the yield objective of the fund, investments are focused on bonds where risk is mitigated by structure or a claim on assets or cashflows.

Rachid Semaoune
Senior Fund Manager

Eric Holt
Senior Fund Manager

ROYAL LONDON ASSET MANAGEMENT

RLAM Government Bond Fund Performance

	1 month (%)	Rolling 12 Months (%)
RL Global Index Linked Bond Fund Z Inc	**1.66**	**-16.38**
IA Global Bonds Sector	1.15	-12.82
Barclays World Government Inflation-Linked Bond Index (hedged)	2.54	-17.01
RL Index Linked Bond Fund M Inc	**2.82**	**-32.60**
IA UK Index Linked Gilts Sector	2.94	-34.97
FTSE Actuaries UK Index-Linked All Stocks Index	3.58	-33.89
RL Short Duration Gilt Fund Z Inc	**0.64**	**-3.68**
IA UK Gilts Sector	2.84	-22.72
FTSE Actuaries UK Conventional Gilts up to 5 Years Index	0.65	-4.45
RL Short Duration Global Index Linked Bond Fund Z Inc	**0.85**	**-4.57**
IA Global Bonds Sector	1.15	-12.82
RL Short Duration Global Index Linked Composite Benchmark[1,2]	1.59	-4.50
RL UK Government Bond Fund Z Inc	**2.87**	**-20.60**
IA UK Gilts Sector	2.84	-22.72
FTSE Actuaries UK Conventional Gilts All Stocks Index	2.82	-22.69

PAST PERFORMANCE IS NOT A GUIDE TO FUTURE PERFORMANCE THE VALUE OF INVESTMENTS AND THE INCOME FROM THEM IS NOT GUARANTEED AND MAY GO DOWN AS WELL AS UP AND INVESTORS MAY NOT GET BACK THE AMOUNT ORIGINALLY INVESTED.
SOURCE: RLAM AND FE, CORRECT AS OF 30 NOVEMBER 2022. RETURNS QUOTED ARE NET OF FEES.
ALL IA SECTOR PERFORMANCE SHOWN IS FOR THE MEDIAN.
1PLEASE NOTE THAT THE BENCHMARK IS PRICED END-OF-DAY.
2THE COMPOSITE BENCHMARK CONSISTS OF: 30% BLOOMBERG UK GOVERNMENT INFLATION LINKED BOND 1-10 YEAR INDEX, 70% BLOOMBERG WORLD GOVERNMENT INFLATION LINKED BOND (EX UK) 1-10 YEAR INDEX (GBP HEDGED).

ROYAL LONDON
ASSET MANAGEMENT

Government Bond Market Review

Market highlights

- Investors took a breath in November following a volatile few months. Gilts returned 2.82% to investors (FTSE Actuaries) on all-maturities basis. The positive return was driven by the belly of the curve (10-15 year maturity), as investors took heart from indications from the US Federal Reserve that it would slow its current pace of tightening. The benchmark 10-year gilt closed the period at 3.16%, falling from 3.52% at the start of November, and pulled back from a high of 3.64% during the month.
- Gilt yields were lower as the macroeconomic picture around the globe deteriorated and investors increasingly discounted a recession in 2023 following further increases in interest rates after the central bank meetings early in the month.
- The Bank of England hiked interest rates 75bps to 3%. Inflation jumped to 11.1% in October, driven by the increase in energy prices; core inflation remained at 6.5%. The November PMI composite business survey indicator was broadly unchanged, but remained consistent with falling output.
- The new Chancellor's Autumn Statement involved significant fiscal tightening, albeit backloaded with measures to raise revenue/cut spending by £55bn annually by 2027-28. Supportive for households (and, arguably inflation) going into 2023 were decisions to continue energy bill support, although less generously than before; uprate pensions and benefits in line with inflation; and increase the minimum wage by 10%.
- Gilt supply remains a headwind for the market. The Government is still planning to borrow around £200bn per year for the next five years, and while this is less than was needed under the Kwarteng plan, it remains historically high, particularly when the Bank of England is also committed to selling its gilt holdings into the market (quantitative tightening).

Index linked bonds

- UK index-linked gilt returns were 3.58% on an all-maturities basis (FTSE Actuaries) in November. Whilst they outperformed in total return turns, they underperformed conventional gilts on a breakeven basis, as breakeven (implied) inflation rates fell – the UK's 10-year breakeven rate fell by 12bps to 3.82%. The benchmark 10-year real yield fell by 49bps to -0.61%.
- The UK index-linked market outperformed the 2.58% return of the Barclays Global Index-linked Index. Real 10-year yields moved in similar directions, with 10-year real yields falling by 30bps to 1.24% in the US, and by 15bps to -0.37% in Germany – but breakevens rose by 11bps to 2.37% in the former and rose by 2bps to 2.29% in the latter.

Royal London Global Index Linked Bond Fund

Portfolio commentary

- Net of fund management fees, the fund returned 1.64% in November (M Inc share class), against benchmark returns of 2.54%. However, the comparison is distorted by the moves seen in the benchmark on the last day of November. On a like for like basis, the fund was slightly ahead of benchmark.
- Although real yields rallied on the first signs of weakening inflation and less hawkish central banks, two gilt syndications had a material impact on performance and activity over the month. It is rare to see two syndications in a single month, and the issue of a 2038 conventional gilt early in November and a 2073 index linked gilt later in the period caused short-term price movements both ahead of and following these syndications, giving us opportunities to add value.
- Our short duration position was a modest positive. With the end of QE, we expected syndications to be competitively priced, and moved short ahead of these, moving back to neutral afterwards. We ended the month with a small long position – gilts tend to perform well into year end and will be supported by the lack of issuance between now and Q2 2023. Yield curve positioning had little impact on performance, and we moved to a flattening bias over the month, notably adding the 2047 index linked gilt after this underperformed on falling out of the 25-year index.
- Cross-market positioning was the other positive of note. We added to Germany early in the month to move overweight, making a similar trade in US TIPS when the relative spread over UK equivalents reached 185bps. We took profits on the US position later in the month after the spread narrowed to 158. We ended the month with modest overweight positions in Australia and Germany, and flat in the UK after being underweight for most of the year.

Investment outlook

- The UK has now unwound all of the mini-budget sell-off, as the changes of Chancellor and Prime Minister led to a government U-turn on fiscal policies and the risk of significantly higher base rates receded. However, markets remain very volatile, the budget led a cut to the gilt issuance for the remainder of this fiscal year, however, UK supply will be at record levels post the financial crisis with gross issuance of just over £300bn for the next financial year, with quantitative tightening adding to market supply.
- With limited supply in December and seasonal demand expected for UK index link bonds we envisage staying close to home repatriating global positions back to the UK.
- Market volatility remains at elevated levels so we will continue to look for tactical opportunities, while generally sizing those positions smaller than normal to reflect that greater volatility. The lack of long dated supply should support a flatter curve and if UK inflation begins to fall we would also expect the 10 year part of the curve to underperform.
- For 2023 we still expect base rates to rise as we see no early fall in the level of inflation and as such, we expect the heavy supply next year to push yields higher – back into positive territory – and hence the portfolio will retain a bias towards a short duration stance.

Key views within the fund

- The fund has a small long duration position on a tactical basis, with our bias still to be short given our view that yields will move higher over the next year.
- The fund holds a modest flattening bias via an underweight in 20-year bonds relative to 30-year bonds.
- The fund is neutral on the UK, with an overweight in Germany and Australia, and underweight positions in France and Italy.

Paul Rayner
Head of Alpha Strategies

Gareth Hill
Fund Manager

Royal London Index Linked Bond Fund

Portfolio commentary

- Net of fund management fees, the fund returned 2.77% in November (M Acc share class), against benchmark returns of 3.58%. However, the comparison is distorted by the moves seen in the benchmark on the last day of November. On a like for like basis, the fund was 30 basis points ahead of benchmark.
- Although real yields rallied on the first signs of weakening inflation and less hawkish central banks, two gilt syndications had a material impact on performance and activity over the month. It is rare to see two syndications in a single month, and the issue of a 2038 conventional gilt early in November and a 2073 index linked gilt later in the period caused short-term price movements both ahead of and following these syndications, giving us opportunities to add value.
- Our short duration position was a modest positive. With the end of QE, we expected syndications to be competitively priced, and moved short ahead of these, moving back to neutral afterwards. We ended the month with a small long position – gilts tend to perform well into year end and will be supported by the lack of issuance between now and Q2 2023. Yield curve positioning had little impact on performance.
- Cross-market positioning was the other positive of note. We added to Germany early in the month, already having long positions in the US, France and Australia, and these positions outperformed gilt equivalents into the 2073 syndication. We then closed most of these ahead of the gilt market outperforming post syndication, to end the month with modest positions in France and Australia.
- Breakevens were a small positive. We used the 2038 syndication to take a small position in conventionals, selling these into the 2073 event later in the month to end the month with no breakeven positions.

Investment outlook

- The UK has now unwound all of the mini-budget sell-off, as the changes of Chancellor and Prime Minister led to a government U-turn on fiscal policies and the risk of significantly higher base rates receded. However, markets remain very volatile, the budget led a cut to the gilt issuance for the remainder of this fiscal year, however, UK supply will be at record levels post the financial crisis with gross issuance of just over £300bn for the next financial year, with quantitative tightening adding to market supply.
- With limited supply in December and seasonal demand expected for UK index link bonds we envisage staying close to home repatriating global positions back to the UK.
- Market volatility remains at elevated levels so we will continue to look for tactical opportunities, while generally sizing those positions smaller than normal to reflect that greater volatility. The lack of long dated supply should support a flatter curve and if UK inflation begins to fall we would also expect the 10-year part of the curve to underperform.
- For 2023 we still expect base rates to rise as we see no early fall in the level of inflation and as such, we expect the heavy supply next year to push yields higher – back into positive territory – and hence the portfolio will retain a bias towards a short duration stance.

Key views within the fund

- The fund has a small long duration position on a tactical basis, with our bias still to be short given our view that yields will move higher over the next year. The portfolio held a modest UK steepening bias via an overweight in 10- and 20-year bonds relative to 30-year bonds.
- The fund remains short the UK, with modest positions in global index linked markets, primarily Australia and France. The lack of gilt issuance in Q1 2023 should be supportive for gilts, so we would expect non-UK exposure to decrease further.
- The portfolio has no breakevens although continues to find tactical opportunities in this area.
- The fund's exposure to highly rated sterling corporate bonds was maintained as we believe the attractive yields these offer more than compensate for the credit risk given our view that spreads discount significant bad news.

Paul Rayner
Head of Alpha Strategies

Ben Nicholl
Fund Manager

ROYAL LONDON
ASSET MANAGEMENT

Royal London Short Duration Global Index Linked Bond Fund

Portfolio commentary

- Net of fund management fees, the fund returned 0.78% in November (M Acc share class), against benchmark returns of 1.59%. However, the comparison is distorted by the moves seen in the benchmark on the last day of November. On a like for like basis, the fund was broadly flat.
- Real yields rallied on the first signs of weakening inflation and less hawkish central banks, and while two gilt syndications had a material impact on longer indices, the maturity of the 2022 index linked gilt and the exit of the 2027 index linked gilt from the >5 year index were more significant to short duration investors.
- Duration had little impact on performance for the month, with the fund generally biased towards a short duration stance and real yields rallying over the period, but our tactical move towards a neutral stance mitigating this impact. We ended the month with a small long position – gilts tend to perform well into year end and will be supported by the lack of issuance between now and Q2 2023.
- Cross-market activity was a modest negative over the month – we remain underweight relative to global markets and short dated UK bonds performed strongly. We continue to feel this part of the UK index linked curve remains expensive. We reduced some of our underweight in short-dated US TIPS following weaker CPI data.
- A small breakeven position was positive for performance in November. We used the 2038 syndication to take a small position in conventionals at an attractive level, selling these later in the month as the market firmed to end the month with no breakeven positions.

Investment outlook

- The UK has now unwound all of the mini-budget sell-off, as the changes of Chancellor and Prime Minister led to a government U-turn on fiscal policies and the risk of significantly higher base rates receded. However, markets remain very volatile, the budget led a cut to the gilt issuance for the remainder of this fiscal year, however, UK supply will be at record levels post the financial crisis with gross issuance of just over £300bn for the next financial year, with quantitative tightening adding to market supply.
- With limited supply in December and seasonal demand expected for UK index link bonds we envisage staying close to home repatriating global positions back to the UK on any weakness of the UK.
- Market volatility remains at elevated levels so we will continue to look for tactical opportunities, while generally sizing those positions smaller than normal to reflect that greater volatility. The lack of long dated supply should support a flatter curve and if UK inflation begins to fall we would also expect the 10-year part of the curve to underperform.
- For 2023 we still expect base rates to rise as we see no early fall in the level of inflation and as such, we expect the heavy supply next year to push yields higher – back into positive territory – and hence the portfolio will retain a bias towards a short duration stance.

Key views within the fund

- The fund has a small long duration position on a tactical basis, with our bias still to be short given our view that yields will move higher over the next year.
- The fund remains short the UK, with an overweight in global index linked markets, notably euro markets through Germany and Australia, as we believe that the front end of the UK market looks expensive.

Paul Rayner
Head of Alpha Strategies

Gareth Hill
Fund Manager

ROYAL LONDON
ASSET MANAGEMENT

Royal London Short Duration Gilt Fund

Portfolio commentary

- Gross of fund management fees, the fund returned 0.66% in November (M Acc share class), broadly in line with the benchmark returns of 0.65%.
- The fund's small duration short hurt performance, but a curve flattening position was positive, as we had a 2-5 year bias. We saw 2026 bonds outperform shorter-dated gilts as the market started to price in rate cuts from 2024 onwards.
- Cross market exposure helped drive returns in the month, through a position in 2024 US treasuries, which outperformed 2024 gilts.
- On a relative value basis, the fund also sold July 2023 maturity gilts, buying six-month treasury bills with the same maturity for an attractive pick-up in yield of nearly 80bps.
- The fund held no exposure to UK inflation markets in the period.
- The fund's highly rated sterling credit holdings, focused on investment grade quality credits, had little performance impact in the period.

Investment outlook

- The perception of the third quarter was skewed by the market reaction to the mini-budget. Beyond this, we expect to see the trends of 2022 continuing for the rest of the year. Inflation is continuing to rise in the UK, reflecting higher raw material costs, energy price increases and tight labour markets. However, The Bank of England has been raising interest rates all year, and there are signs that this is starting to impact demand. It is likely inflation will peak at some point during Q4, but the key for central banks will be where inflation settles, and that remains a big unknown for markets.

Key views within the fund

- The portfolio's duration is shorter than the benchmark, including the impact of cash holdings on duration.
- The fund holds a small cross-market exposure in the US and will continue to look for opportunities to take such positions on a relative basis.
- The portfolio has allocations to high quality corporate bonds, which we expect to outperform gilts.
- The portfolio may look to tactically trade index-linked gilts to take advantage of mispricing opportunities, but had no exposure to UK inflation at the end of the month.

CITYWIRE AA

Craig Inches
Head of Rates and Cash

CITYWIRE AA

Ben Nicholl
Fund Manager

ROYAL LONDON
ASSET MANAGEMENT

Royal London UK Government Bond Fund

Portfolio commentary

- Gross of fund management fees, the fund returned 2.94% in November (M Acc share class), outperforming the benchmark returns of 2.82%.
- The fund's small duration short, about 0.3 years, was negative for performance during the month as yields fell, but we were able to mitigate this through tactical trading of the position.
- Cross market exposure added to performance, as we held US and later Australia bonds, which outperformed UK equivalents
- The fund's sterling credit exposure added to performance owing to credit spreads tightening.

Investment outlook

- The perception of the third quarter was skewed by the market reaction to the mini-budget. Beyond this, we expect to see the trends of 2022 continuing for the rest of the year. Inflation is continuing to rise in the UK, reflecting higher raw material costs, energy price increases and tight labour markets. However, The Bank of England has been raising interest rates all year, and there are signs that this is starting to impact demand. It is likely inflation will peak at some point during Q4, but the key for central banks will be where inflation settles, and that remains a big unknown for markets.

Key views within the fund

- The portfolio's duration is slightly short of the benchmark, including the impact of cash holdings on duration, although we continue to trade around this as market volatility provides opportunities to add value.
- The fund retains an exposure to steepening at the ultra long end of the curve, being underweight 50-year maturity gilts versus 30-year maturity bonds
- The fund has overseas exposure, mainly in dollar markets, and we continue to look for opportunities to take such positions on a relative basis.
- The portfolio has allocations to high quality corporate bonds which provide additional yield for the portfolio.

CITYWIRE AA

Craig Inches
Head of Rates and Cash

CITYWIRE AA

Ben Nicholl
Fund Manager

ROYAL LONDON
ASSET MANAGEMENT

RLAM Global High Yield Fund Performance

	1 month (%)	Rolling 12 Months (%)
RL Global High Yield Bond Fund M Inc	**2.94**	**-12.86**
RL Global High Yield Bond Fund Z Inc	**2.96**	**-12.63**
IA Sterling High Yield Sector	3.03	-9.32
ICE BofA ML BB-B Global Non-Financial High Yield Constrained Index	3.33	-10.82
RL Short Duration Global High Yield Bond Fund A Inc	**1.34**	**-3.40**
RL Short Duration Global High Yield Bond Fund M Inc	**1.37**	**-3.02**
RL Short Duration Global High Yield Bond Fund Z Inc	**1.38**	**-2.91**
IA Sterling High Yield Sector	3.03	-9.32
Sterling Overnight Index Average Rate (SONIA)[1]	0.23	1.14

PAST PERFORMANCE IS NOT A GUIDE TO FUTURE PERFORMANCE. THE VALUE OF INVESTMENTS AND THE INCOME FROM THEM IS NOT GUARANTEED AND MAY GO DOWN AS WELL AS UP AND INVESTORS MAY NOT GET BACK THE AMOUNT ORIGINALLY INVESTED.
SOURCE: RLAM AND FE, CORRECT AS OF 30 NOVEMBER. RETURNS QUOTED ARE NET OF FEES.
ALL IA SECTOR PERFORMANCE SHOWN IS FOR THE MEDIAN.
[1] BENCHMARK: SONIA. PLEASE NOTE THAT THIS CHANGED FROM 3-MONTH LIBOR, EFFECTIVE 15 DECEMBER 2020, AND IS REFLECTED IN THE RETURNS SHOWN ABOVE.

ROYAL LONDON
ASSET MANAGEMENT

Royal London Global High Yield Bond Fund

Portfolio commentary

- The fund (Z class) returned 2.96%, net of fees, in November, compared with 3.33% for the ICE BofA Merrill Lynch BB-B Global Non-Financial High Yield Constrained Index (100% GBP hedged). For the rolling 12-month period, the fund has returned -12.63% compared to -10.82% for the index.
- Global high yield spreads (BB-B index) were tighter on the month at 445bps (-34bps) and the government yield curve decreased by 31bps, leading to a monthly return of 3.33%. Price and income returns were 2.96% and 0.50%, respectively. Government bond yields fell (and prices rose) in November as inflation data released was lower than expected.
- The US default rate was unchanged in November at 0.01% – however, we expect an increase in defaults in the months to come as the global economy slows and particularly if the US slips into recession.
- Similar to prior months in 2022, new issuance remained well below the levels seen in 2020 and 2021.
- For the market as a whole, sector returns were widely dispersed, with real estate the standout performer. The leisure and utility sectors also had good showings. All regions posted positive returns: emerging markets had a particularly good month in November, while Europe outperformed the US and UK. Both BB and B rated bonds saw good returns, outperforming the CCC and below band by a wide margin. Longer-dated bonds generally outperformed their shorter-dated peers, although bonds in the three- to seven-year section of the curve were notably weak.
- The positive returns for the fund were broad-based across sectors, with all but media contributing positively to performance. The real estate, telecommunications, basic industry and capital goods sectors were the strongest contributors. The underperformance versus the benchmark arose from our overweight position in media, which underperformed. All regions contributed positively to the fund's performance, with Europe making the strongest contribution. BB rated bonds outperformed those rated B or CCC and below, but our B rated exposure made the strongest contribution to performance.
- Over the course of the month, the fund's exposure to CCC names was reduced. Exposure to investment grade credit was added to increase duration, given the outlook for lower inflation in 2023.
- At month end, the high yield market was yielding 8.02% (yield-to-worst) with duration of 4.16 years. The fund yield stood at 10.05% (yield-to-worst) with duration of 4.72 years.

*YIELD-TO-WORST REFERS TO THE REDEMPTION DATE THAT PRODUCES THE LOWEST RETURN.

Investment outlook

- We turned more defensive in March to navigate the remainder of 2022, de-risking our funds by reducing duration and increasing security. While the near term is relatively unthreatening and yields are undoubtedly attractive, the outlook for interest rates and economic growth remains unclear heading into 2023 and we will retain a defensive mindset until the prognosis for inflation is clearer.
- Following three quarters of weakness in government bond markets and negative returns, the high yield market is now pricing in a severe recession and we believe therefore offers excellent value. With spreads at over 519bps at the end of November, the implied five-year cumulative default rate is 22.5%. This compares to cumulative default rates of 25% during the Global Financial Crisis and 30%+ in the 1990s and early 2000s.The all-time high was 41% in the long and deep depression of the 1930s. So, while defaults are currently at record lows, the high yield market is discounting a major recession and commensurate level of defaults.
- Yet this implied default rate takes no account of the much higher quality and more robust nature of the high yield market today, compared to 2008/9; nor of the current financial state of issuers as we head towards the downturn. We believe that the future default cycle is unlikely to be as negative as prior cycles because the market composition has improved: the highest risk CCC rating band now only represents 9% of the market, compared to 17% in 2007; meanwhile, the BB rated band now accounts for 60% of the market. In addition, following the bumper issuance of 2020 and 2021 (and the strength of the energy sector in 2021 and the first half of 2022), most issuers are in a stronger position than normal at this stage of a cycle and default and recovery expectations remain extremely benign.
- While these figures are compelling, we don't feel that a higher-risk strategy is necessary. With yields at current levels and appealing potential returns, we will be paid sufficiently for maintaining a lower-risk position at least another quarter until there is more clarity about the outlook. Unlike equities, given the asymmetry of risks in credit investing, it doesn't pay to take excessive risks when heading into periods of more negative sentiment. The way through difficult markets is to focus on those risks that you can control and know what you own. We will keep duration low and focus on the quality

of issuers' financials, rather than relying on third-party ratings: at a sectoral level, cashflows are the key factor, so we need to know about on- and off-balance sheet leverage. We prefer not to wait for defaults as the recovery process can take time: however, should they occur, the key is to have an adequate solvency cushion.

Key views within the fund

- The fund's objective is to achieve a combination of capital growth and income. The fund seeks to achieve its investment objective by outperforming its benchmark, the BofA Merrill Lynch BB-B Global Non-Financial High Yield Constrained index, 100% hedged to sterling, by 1% per annum over rolling three-year periods.
- The fund seeks to mitigate stock-specific risk by holding a diversified portfolio of investments, so that no individual investment can, in isolation, have an excessive adverse impact on overall fund performance. Currency risk associated with holdings of bonds is hedged through the use of forward currency transactions.
- We expect market volatility to continue due to market expectations surrounding Federal Reserve monetary policy. As such, we believe bonds with near-term catalysts, which mitigate market risk, are an important attribute underpinning investment performance over the medium term. There seems little chance of a near-term resolution of the conflict in Ukraine – this also has significant implications for the global economy, particularly if ongoing higher energy prices and supply chain disruption exacerbate a global economic slowdown.

Azhar Hussain
Head of Global Credit

Stephen Tapley
Global Credit Fund Manager

ROYAL LONDON
ASSET MANAGEMENT

Royal London Short Duration Global High Yield Bond Fund

Portfolio commentary

- Net of fees, the fund (Z class) returned 1.38% in November, compared with 0.23% for SONIA. For the rolling 12-month period, the fund has returned -2.91% compared to 1.14% for the index.
- For context, global high yield spreads (BB-B index) were tighter on the month at 445bps (-34bps) and the government yield curve decreased by 31bps, leading to a monthly return of 3.33%. Price and income returns were 2.96% and 0.50%, respectively. Government bond yields fell (and prices rose) in November as inflation data released was lower than expected.
- The US default rate was unchanged in November at 0.01% – however, we expect an increase in defaults in the months to come as the global economy slows and particularly if the US slips into recession.
- Similar to prior months in 2022, new issuance remained well below the levels seen in 2020 and 2021.
- For the market as a whole, sector returns were widely dispersed, with real estate the standout performer. The leisure and utility sectors also had good showings. All regions posted positive returns: emerging markets had a particularly good month in November, while Europe outperformed the US and UK. Both BB and B rated bonds saw good returns, outperforming the CCC and below band by a wide margin. Longer-dated bonds generally outperformed their shorter-dated peers, although bonds in the three- to seven-year section of the curve were notably weak.
- By sector, the fund's positive performance was driven by capital goods and healthcare. Bonds rated BB outperformed those rated BBB and above and CCC and below, but B rated bonds were the strongest contributor to performance. By region, the US was the stronger contributor to performance.
- The fund's FX-adjusted expected yield decreased by 41 basis points to 7.98% from 8.39% with an expected duration of 1.72 years.

Investment outlook

- The outlook for interest rates and economic growth remains unclear heading into 2023 and we will retain a defensive mindset until the prognosis for inflation is clearer.
- Following three quarters of weakness in government bond markets and negative returns, the high yield market is now pricing in a severe recession and we believe therefore offers excellent value. With spreads at over 519bps at the end of November, the implied five-year cumulative default rate is 22.5%. This compares to cumulative default rates of 25% during the Global Financial Crisis and 30%+ in the 1990s and early 2000s.The all-time high was 41% in the long and deep depression of the 1930s. So, while defaults are currently at record lows, the high yield market is discounting a major recession and commensurate level of defaults.
- Yet this implied default rate takes no account of the much higher quality and more robust nature of the high yield market today, compared to 2008/9; nor of the current financial state of issuers as we head towards the downturn. We believe that the future default cycle is unlikely to be as negative as prior cycles because the market composition has improved: the highest risk CCC rating band now only represents 9% of the market, compared to 17% in 2007; meanwhile, the BB rated band now accounts for 60% of the market. In addition, following the bumper issuance of 2020 and 2021 (and the strength of the energy sector in 2021 and the first half of 2022), most issuers are in a stronger position than normal at this stage of a cycle and default and recovery expectations remain extremely benign.
- The fund's FX-adjusted expected yield was 7.98% at the end of November. All things being equal, an annual default rate of 13.30% (with 60% losses) would be required for an implied zero total return, at the current fund yield. This scenario is far in excess of both our own and market default expectations. It would equate to over a quarter of the fund defaulting over the next two years. It is worth recalling that the fund has never had any credit losses from defaults since inception.
- With yields at current levels and appealing potential returns, we will be paid sufficiently for maintaining a lower-risk position for at least another quarter until there is more clarity about the outlook. In keeping with the core focus of the strategy, we will keep duration low and focus on the quality of issuers' financials, rather than relying on third-party ratings. At a sectoral level, cashflows are the key factor and we continue to favour companies with contracted revenues. With regards to geography, our global outlook provides diversification away from country-specific risks.

Key views within the fund

- The fund's objective is to provide income. The manager seeks to achieve this by outperforming the benchmark, SONIA, by 2% per annum over rolling three-year periods.

- The fund is diversified in order to improve overall portfolio liquidity and to reduce the effect on overall fund performance of any deterioration in the creditworthiness of an individual holding.
- We expect market volatility to continue due to market expectations surrounding Federal Reserve monetary policy. As such, we believe bonds with near-term catalysts, which mitigate market risk, are an important attribute underpinning investment performance over the medium term. There seems little chance of a near-term resolution of the conflict in Ukraine – this also has significant implications for the global economy, particularly if ongoing higher energy prices and supply chain disruption exacerbate a global economic slowdown.

Azhar Hussain
Head of Global Credit

Stephen Tapley
Global Credit Fund Manager

ROYAL LONDON ASSET MANAGEMENT

IMPORTANT INFORMATION

FOR PROFESSIONAL CLIENTS ONLY, NOT SUITABLE FOR RETAIL CLIENTS. THE VIEWS EXPRESSED ARE THE AUTHOR'S OWN AND DO NOT CONSTITUTE INVESTMENT ADVICE.

THIS DOCUMENT IS A FINANCIAL PROMOTION. IT DOES NOT PROVIDE, AND SHOULD NOT BE RELIED ON FOR, ACCOUNTING, LEGAL OR TAX ADVICE, OR INVESTMENT RECOMMENDATIONS. FOR MORE INFORMATION ON THE FUND OR THE RISKS OF INVESTING, PLEASE REFER TO THE FUND FACTSHEET, PROSPECTUS OR KEY INVESTOR INFORMATION DOCUMENT (KIID), AVAILABLE VIA THE FUND INFORMATION PAGE ON WWW.RLAM.COM.

PAST PERFORMANCE IS NOT A GUIDE TO FUTURE PERFORMANCE. THE VALUE OF INVESTMENTS AND THE INCOME FROM THEM IS NOT GUARANTEED AND MAY GO DOWN AS WELL AS UP AND INVESTORS MAY NOT GET BACK THE AMOUNT ORIGINALLY INVESTED.

PORTFOLIO CHARACTERISTICS AND HOLDINGS ARE SUBJECT TO CHANGE WITHOUT NOTICE. THIS DOES NOT CONSTITUTE AN INVESTMENT RECOMMENDATION. FOR INFORMATION PURPOSES ONLY, METHODOLOGY AVAILABLE ON REQUEST. INFORMATION DERIVED FROM SOURCES OTHER THAN ROYAL LONDON ASSET MANAGEMENT IS BELIEVED TO BE RELIABLE; HOWEVER, WE DO NOT INDEPENDENTLY VERIFY OR GUARANTEE ITS ACCURACY OR VALIDITY.

ALL RIGHTS IN THE FTSE ALL STOCKS GILT INDEX, FTSE OVER 15 YEAR GILTS INDEX, FTSE A INDEX LINKED OVER 5 YEARS GILT INDEX AND FTSE A MATURITIES GILT INDEX (THE "INDEX") VEST IN FTSE INTERNATIONAL LIMITED ("FTSE"). ALL RIGHTS IN THE FTSE 350, FTSE ALL SHARE, FTSE 100, FTSE 250, FTSE 350 HIGHER YIELD AND FTSE SMALL CAP (THE "INDEX") VEST IN FTSE INTERNATIONAL LIMITED ("FTSE"). "FTSE®" IS A TRADE MARK OF THE LONDON STOCK EXCHANGE GROUP COMPANIES AND IS USED BY FTSE UNDER LICENCE. THE ROYAL LONDON FUNDS (THE "FUNDS") HAS BEEN DEVELOPED SOLELY BY ROYAL LONDON ASSET MANAGEMENT. THE INDEX IS CALCULATED BY FTSE OR ITS AGENT. FTSE AND ITS LICENSORS ARE NOT CONNECTED TO AND DO NOT SPONSOR, ADVISE, RECOMMEND, ENDORSE OR PROMOTE THE FUND AND DO NOT ACCEPT ANY LIABILITY WHATSOEVER TO ANY PERSON ARISING OUT OF (A) THE USE OF, RELIANCE ON OR ANY ERROR IN THE INDEX OR (B) INVESTMENT IN OR OPERATION OF THE FUND. FTSE MAKES NO CLAIM, PREDICTION, WARRANTY OR REPRESENTATION EITHER AS TO THE RESULTS TO BE OBTAINED FROM THE FUNDS OR THE SUITABILITY OF THE INDEX FOR THE PURPOSE TO WHICH IT IS BEING PUT BY ROYAL LONDON ASSET MANAGEMENT.

THE "SONIA" MARK IS USED UNDER LICENCE FROM THE BANK OF ENGLAND (THE BENCHMARK ADMINISTRATOR OF SONIA), AND THE USE OF SUCH MARK DOES NOT IMPLY OR EXPRESS ANY APPROVAL OR ENDORSEMENT BY THE BANK OF ENGLAND. "BANK OF ENGLAND" AND "SONIA" ARE REGISTERED TRADE MARKS OF THE BANK OF ENGLAND.

ALL CONFIDENTIAL INFORMATION RELATING TO ANY ROYAL LONDON GROUP COMPANY MUST BE TREATED BY YOU IN THE STRICTEST CONFIDENCE. IT MAY ONLY BE USED FOR THE PURPOSES OF ASSESSING THE PROPOSAL TO ENGAGE ROYAL LONDON ASSET MANAGEMENT LIMITED (RLAM). CONFIDENTIAL INFORMATION SHOULD NOT BE DISCLOSED TO ANY THIRD PARTY AND SHOULD ONLY BE DISCLOSED TO THOSE OF YOUR EMPLOYEES AND PROFESSIONAL ADVISERS WHO ARE REQUIRED TO SEE SUCH INFORMATION FOR THE PURPOSE SET OUT ABOVE. YOU SHOULD ENSURE THAT THESE PERSONS ARE MADE AWARE OF THE CONFIDENTIAL NATURE OF SUCH INFORMATION AND TREAT IT ACCORDINGLY. YOU AGREE TO RETURN AND/ OR DESTROY ALL CONFIDENTIAL INFORMATION ON RECEIPT OF OUR WRITTEN REQUEST TO DO SO.

ISSUED BY ROYAL LONDON ASSET MANAGEMENT LIMITED, FIRM REGISTRATION NUMBER: 141665, REGISTERED IN ENGLAND AND WALES NUMBER 2244297; ROYAL LONDON UNIT TRUST MANAGERS LIMITED, FIRM REGISTRATION NUMBER: 144037, REGISTERED IN ENGLAND AND WALES NUMBER 2372439; RLUM LIMITED, FIRM REGISTRATION NUMBER: 144032, REGISTERED IN ENGLAND AND WALES NUMBER 2369965. ALL OF THESE COMPANIES ARE AUTHORISED AND REGULATED BY THE FINANCIAL CONDUCT AUTHORITY. ROYAL LONDON ASSET MANAGEMENT BOND FUNDS PLC, AN UMBRELLA COMPANY WITH SEGREGATED LIABILITY BETWEEN SUB-FUNDS, AUTHORISED AND REGULATED BY THE CENTRAL BANK OF IRELAND, REGISTERED IN IRELAND NUMBER 364259. REGISTERED OFFICE: 70 SIR JOHN ROGERSON'S QUAY, DUBLIN 2, IRELAND.

ALL OF THESE COMPANIES ARE SUBSIDIARIES OF THE ROYAL LONDON MUTUAL INSURANCE SOCIETY LIMITED, REGISTERED IN ENGLAND AND WALES NUMBER 99064. REGISTERED OFFICE: 55 GRACECHURCH STREET, LONDON, EC3V 0RL. THE ROYAL LONDON MUTUAL INSURANCE SOCIETY LIMITED IS AUTHORISED BY THE PRUDENTIAL REGULATION AUTHORITY AND REGULATED BY THE FINANCIAL CONDUCT AUTHORITY AND THE PRUDENTIAL REGULATION AUTHORITY. THE ROYAL LONDON MUTUAL INSURANCE SOCIETY LIMITED IS ON THE FINANCIAL SERVICES REGISTER, REGISTRATION NUMBER 117672. REGISTERED IN ENGLAND AND WALES NUMBER 99064. FC RLAM ON 0332.