Royal London Equity Funds

Fund Manager Commentary – October 2022

FOR PROFESSIONAL INVESTORS ONLY, NOT SUITABLE FOR RETAIL INVESTORS.

Contents

RLAM Equity Performance

	1 month (%)	Rolling 12 Months (%)
RL UK Equity Income M Inc	**5.63**	**-1.31**
IA UK Equity Income Sector	3.44	-5.07
FTSE All Share Index	3.11	-2.78
RL UK Dividend Growth Fund M Acc	**3.95**	**-10.43**
IA UK All Companies Sector	2.99	-10.20
FTSE All Share Index	3.11	-2.78
RL UK Mid Cap Growth Fund M Acc	**5.74**	**-26.95**
IA UK All Companies Sector	2.99	-10.20
FTSE 250 ex-IT Index	5.63	-22.48
RL UK Opportunities Fund M Acc	**4.42**	**-23.39**
IA UK All Companies Sector	2.99	-10.20
FTSE All Share Index	3.11	-2.78
RL UK Smaller Companies Fund M Acc	**1.80**	**-32.71**
IA UK Smaller Companies Sector	2.12	-30.37
FTSE Small Cap ex-IT Index	0.75	-22.90
RL Global Equity Income Fund M Inc	**4.16**	**6.15**
IA Global Equity Income	2.39	0.91
MSCI All Countries World Index	2.81	-4.70
RL Global Equity Select Fund M acc	**3.62**	**8.11**
IA Global	2.07	-7.95
MSCI World Net Index	3.92	-2.94

PAST PERFORMANCE IS NOT NECESSARILY A RELIABLE INDICATOR OF 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 31 OCTOBER 2022. RETURNS QUOTED ARE NET OF FEES.

Royal London UK Equity Income

Portfolio Commentary

- During the month the fund returned +5.63%, ahead of the benchmark and the peer group median, placing 12th percentile in the month and 35th percentile year to date.
- The volatility of politics and markets that we saw in September carried on into October, in what was another extraordinary month. Following the very poorly received mini-budget in September, the prime minister fired the Chancellor of the Exchequer, and the planned unfunded tax cuts were cancelled. These moves received a positive reception, causing the pound to rally and gilt yields to reduce. However that was not enough to save Liz Truss's position as Prime Minister and she resigned later in the month, being replaced by Rishi Sunak. With slightly improved sentiment towards the UK economy, the small and mid-sized companies of the FTSE 250 performed better than the larger and generally more international businesses of the FTSE 100.
- A wide range of stocks drove the fund's performance: **Investec**, **Close Brothers** and **Paragon** in financials; tobacco company **Imperial Brands**; retailer **Dunelm** and engineering businesses **Spectris** and **IMI**.
- During the month the fund continued to add to the relatively new holding in **HSBC** and trimmed the holding in **BP**, where the fund now holds a position broadly in line with the benchmark weight.

Investment Outlook

- The new government is seen as slightly more stable and economically responsible which has helped sterling rally and reduced bond yields to some degree. However, there is little doubt that the UK economy faces a tough period. Inflation remains very high, interest rates have increased, and taxes may well have to rise to help to pay for the energy cost cap.
- In this tricky background we feel that our approach of investing in a broad range of companies from different sectors and stages of their lifecycle is very appropriate and will allow performance to continue to be driven more by the success of our hunting for undervalued long term cashflows than by the prevailing winds of the macroeconomy, or factors such as growth or value styles being in vogue.

CITYWIRE A

Richard Marwood

Head of Income Equities

Royal London UK Dividend Growth Fund

Portfolio Commentary

- During the month the fund returned +3.95%, ahead of both the benchmark and peer group median, placing 25th percentile in the month and 49th percentile year to date.
- The volatility of politics and markets that we saw in September carried on into October, in what was another extraordinary month. Following the very poorly received mini-budget in September, the prime minister fired the Chancellor of the Exchequer, and the planned unfunded tax cuts were cancelled. These moves received a positive reception, causing the pound to rally and gilt yields to reduce. However that was not enough to save Liz Truss's position as Prime Minister and she resigned later in the month, being replaced by Rishi Sunak. With slightly improved sentiment towards the UK economy, the small and mid-sized companies of the FTSE 250 performed better than the larger and generally more international businesses of the FTSE 100.
- A range of stocks drove the fund's performance: equipment rentals company **Ashtead**, food producer **Cranswick**, engineer **Spectris**, tobacco company **Imperial Brands** and retailer **Dunelm**.
- During the month trading activity was relatively light, with the most noteworthy trades being increasing our holdings in **Close Brothers** and **Drax**.

Investment Outlook

- The new government is seen as slightly more stable and economically responsible which has helped sterling rally and reduced bond yields to some degree. However, there is little doubt that the UK economy faces a tough period. Inflation remains very high, interest rates have increased, and taxes may well have to rise to help to pay for the energy cost cap.
- In this tricky background we feel that our approach of investing in a broad range of companies from different sectors and stages of their lifecycle is very appropriate and will allow performance to continue to be driven more by the success of our hunting for undervalued long term cashflows than by the prevailing winds of the macroeconomy, or factors such as growth or value styles being in vogue.

CITYWIRE A

Richard Marwood

Head of Income Equities

CITYWIRE A

Niko de Walden

Fund Manager

Royal London UK Mid Cap Growth Fund

Portfolio Commentary

- During the month of October, the fund returned 5.7% which compared to 5.6% from the benchmark (FTSE 250 ex-IT index) and 3.2% from the IA All Companies peer group.
- October was another volatile month for the UK and was largely dominated by political news and events. After a series of U-turns on September's mini-budget and the firing of her chancellor Kwasi Kwarteng, Liz Truss resigned as the UK's Prime Minister. A leadership contest ensued, and Rishi Sunak was subsequently announced as the new Prime Minister in relatively swift succession. Markets reacted positively following the roll back of policies announced in the mini-budget, the installation of Jeremy Hunt as chancellor and the commencement of Rishi Sunak's premiership. Following the improved sentiment towards the UK economy during the month, the FTSE 250 index, which comprises of more domestically focused mid-sized businesses, outperformed the FTSE 100 index, which comprises of more internationally focused larger-sized businesses.
- **Telecom Plus**, the asset light utility company, was a significant contributor to performance of the fund during the period. The company issued a positive trading update which highlighted significant growth in its customer base, further progressing toward achieving its growth target of adding 1 million customers in the next 4-5 years. As a result, the company now expects profits for the financial year to be materially ahead of current market expectations. In addition to the trading update, the company also announced it had entered into an improved and extended wholesale agreement with its broadband provider, which should further Telecom Plus' competitive offering in this area. **AJ Bell**, the investment platform provider, was also a significant contributor to performance. The company released a trading update during the month highlighting growth in its total customers as well as net inflows across both its financial advisor and retail business divisions. Considering the difficult market backdrop, we believe the results produced by AJ Bell evidence the strength of its business model.
- **GB Group**, the identity verification specialist, was a detractor to performance. The share price fell during the month following news that Private Equity firm GTCR was no longer considering making an offer for the company, as well as after the publication of a trading update. With regards to the latter, despite GB Group announcing strong growth within its Location and Fraud divisions, investors grew concerned by the performance within the larger Identity division. Although the shares have been disappointing more recently, in the long term we continue to believe that the business is well positioned to benefit from the secular market growth in online ID verification and fraud detection in areas such as e-commerce, social media and financial services.
- In terms of trading activity, the fund initiated a position in **Safestore**, the real estate investment trust focused on providing self-storage to both businesses and consumers. Safestore is the largest self-storage business in the UK and operates a total of 178 sites across the UK and Europe. Self-storage is an attractive sub-sector within Real Estate and has high barriers to entry in the form of a structural lack of supply of suitable locations, together with an increasing penetration of corporates and consumers using self storage in Europe and consistent rental growth. International expansion is a further potential revenue driver as the company develops further sites in Paris, Spain and other territories. The fund also added to a range of existing positions during the month, including **JTC**, the provider of fund administration services.

ALPHA MANAGER 2022
Henry Lowson

Henry Lowson

Head of UK Alpha Equities

Royal London UK Opportunities Fund

Portfolio Commentary

- During the month the fund returned 4.42%, ahead of both the benchmark and peer group median, placing 19th percentile over the month.
- October proved to be another momentous month when it came to British politics. The United Kingdom saw its third Prime Minister in three months with the resignation of Liz Truss and the internal coronation of Rishi Sunak. It became clear Truss' position was unsustainable following the disastrous 'mini-budget' presided over by her (ex) Chancellor Kwarteng. The decision made by Conservative MPs to install Sunak has calmed the markets and the thought is he will be a safe hand on the tiller, alongside Jeremy Hunt as Chancellor, as the UK navigates choppy waters in the months ahead. With slightly improved sentiment towards the UK economy, the small and mid-sized companies of the FTSE 250 performed better than the larger and generally more international businesses of the FTSE 100.
- This month's top performer was again **Dunelm**, up 19% as investors took stock following solid results in September. The general retail sector has had a torrid year but with ratings having materially dropped, there is more interest being shown. Another retail stock, **Watches of Switzerland Group**, added 15%. Other stocks which performed robustly included **Integrafin** and **Melrose**, up 15% and 14% respectively.
- On the downside, **Marshalls** unsurprisingly issued a profit warning citing conditions in the private landscaping market. What did surprise however was the share reaction. Shares had already fallen materially during the year but finished October another 12% weaker. We continue to believe management are first class and are well positioned to weather the downturn. Prudential fell 9% as concerns surrounding China's tough covid stance resurfaced once again. Other stocks which fell included Future and Rio Tinto, both off 8%.
- The fund had a very quiet month in terms of trading with only the positions in **MJ Gleeson** and **St James Place** added to.

Investment Outlook

- Consumers are facing a significant cost of living squeeze, as inflation is currently at its highest level for decades. Likewise, companies are battling to defend margins, as their own input costs increase significantly. We believe our approach of investing in a broad range of companies who are in control of their own fates, irrespective of market conditions is the right one. As well as looking for durable businesses, a willingness to look through short-term extremes of sentiment and buy stocks when they are out of favour, or take profits when sentiment becomes exuberant should drive longer-term performance.

Craig Yeaman

Senior Fund Manager

Royal London UK Smaller Companies Fund

Portfolio Commentary

- During the month of October, the fund returned 1.8% which compared to 0.8% from the benchmark (FTSE Small Cap ex-IT index) and 2.2% from the IA UK Smaller Companies peer group. The fund's relative outperformance to the benchmark was driven largely by stock selection within the Industrials sector, as well as due to an underweight position in the Real Estate sector.
- October was another momentous month for the UK and was largely dominated by political news and events. After a series of U-turns on September's mini-budget and the firing of her chancellor Kwasi Kwarteng, Liz Truss resigned as the UK's Prime Minister. A leadership contest ensued, and Rishi Sunak was subsequently announced as the new Prime Minister in relatively swift succession. Markets reacted positively following the roll back of policies announced in the mini-budget, the installation of Jeremy Hunt as chancellor and the commencement of Rishi Sunak's premiership.
- **Cerillion**, the software provider for telecommunication companies, was a significant contributor to performance following the announcement of a strong update where the firm noted positive trading for the full financial year. As a result, management now expect that profit before tax to be materially ahead of market expectations. The company's short-term outlook also looks strong, as management note that new business opportunities from both existing and new customers remains buoyant. **DiscoverIE**, the designer and manufacturer for customised electronic components, was another contributor to performance following the announcement of its H1 results. The company revealed strong organic sales growth across both of its divisions, a record level in its order book and that it remains on track to deliver full year earnings in line with expectations.
- **GB Group**, the identity verification specialist, was a detractor to performance. The share price fell during the month following news that Private Equity firm GTCR was no longer considering making an offer for the company, as well as after the publication of a trading update. With regards to the latter, despite GB Group announcing strong growth within its Location and Fraud divisions, investors grew concerned by the performance within the larger Identity division. Although the shares have been disappointing more recently, in the long term we continue to believe that the business is well positioned to benefit from the secular market growth in online ID verification and fraud detection in areas such as e-commerce, social media and financial services.
- In terms of trading activity during the month, the fund trimmed its position in **Ergomed**, the pharmaceutical services group, to reduce the position below the 3% individual stock limit, and disposed of its holding in **XP Power**, the power supply specialist. With regards to XP Power, we were concerned about the company's balance sheet after receiving an unexpectedly large fine, the deterioration in cashflow over the year, evidence of a weakening semi-conductor market and elevated analyst earnings expectations for 2023. The fund also added to a range of existing positions during the month, including **Porvair**, **Treatt and Yougov**.

ALPHA MANAGER 2022
Henry Lowson

Henry Lowson

Head of UK Alpha Equities

Henry Burrell

Fund Manager

Royal London Global Equity Income Fund

Portfolio Commentary

- The Royal London Global Income fund returned +6.09% in October (vs +2.81% MSCI ACWI). Year to date, the fund has returned +1.61% (vs -7.23% MSCI ACWI).
- The fund performed well during October with strong stock picking across all sectors apart from energy and information technology. We benefited from two of the fund's largest active positions, **Steel Dynamics** and **Gilead**, both being up more than 20%. Steel Dynamics surprised the market with the strength of their forward orderbook within high margin, pre-fabricated products, whilst Gilead exhibited strong performance in its core HIV franchise as well as nascent signs of success within their oncology pipeline. We continue to believe that both stocks have highly attractive risk rewards, but have taken some profit in both, to avoid active positions becoming too large.
- During the month, we continued to add to new holding, **Applied Materials**, a company which has been very weak this year due to China and cyclical concerns, but one which we believe can continue to generate high returns on investment through their strong market position in cutting edge machines which help semiconductor companies fit ever more transistors onto chip. We also added to **Adidas**, who have been hit by every storm at sea in the last couple of years, but operate within highly attractive, consolidated markets, and with valuation at levels which assume little success in turning the company around, we took the opportunity to add to our now small position.

Investment Outlook

- With geopolitical issues with China and Russia, combined with central bank tightening, continuing to drive markets we continue to try hard to achieve balance by Region, Sector and Life Cycle within the fund, so that it is our stock picking that drives the majority of relative performance, rather than the outcomes to these various issues.

CITYWIRE A

Niko de Walden

Fund Manager

Royal London Global Equity Select Fund

Portfolio Commentary

- Global equity markets rallied during October posting strong positive absolute returns. There was no Federal Reserve monetary policy meeting in October, but a Wall Street Journal article gained market attention suggesting that while a 75bp hike was likely in November (as expected by most economists), officials were "likely to debate then whether and how to signal plans to approve a smaller increase in December. In the UK, Prime Minister Truss resigned after less than 50 days in office and a shorter than usual selection process saw former Chancellor Rishi Sunak become PM. The ECB meanwhile hiked rates again by 75bp against a continued high inflation backdrop. The statement accompanying the decision indicated that the Governing Council expected to hike rates further, but also that they have "made substantial progress in withdrawing monetary policy accommodation."

Contributors to performance:

- **Steel Dynamics**, the steel manufacturer in the 'Slowing & Maturing' category of the corporate Life Cycle, outperformed over the month as steel prices remain elevated. Though steel prices have come down from the peaks of last year, they remain well above the long-term average. While steel prices have declined over 50% from their 2021 highs, they remain above the long-term average and the industry has reduced excess capacity. Quarterly results also highlighted record steel shipments for the company, with some pressure on the operating margin, though the fabrication of raw steel provided upside. The new plant in Sinton Texas continues to ramp up production and the company's valuation pay-off remains attractive. **Reliance Steel** the metals distributor 'Slowing & Maturing' outperformed during the month. The company has benefited from inflation – as the demand situation normalises the business should release working capital and generate significant cash flows. The company is using excess cash to repurchase shares, a strategy that we support for this company at this stage of the Life Cycle. **HCA Healthcare**, the hospital giant in the Compounding phase, during the period has actively managed higher labour costs which have represented a headwind for the business. Recent results show the challenges of labour shortages in healthcare, which is manifesting itself in lower patient admissions due to supply constraints and higher costs. We believe that HCA is better placed than competitors to manage these challenges and that the long-term demand outlook remains attractive.

Detractors from performance:

- Online retail giant **Amazon** in the Slowing & Maturing category underperformed during the month as quarterly results were taken badly by the market – a slowdown in the AWS cloud business growth was a notable concern as was guidance for Q4. We continue to view the business as having strong competitive advantages and an attractive valuation pay-off. **Lithia Motors** in the Slowing and Maturing category of the Life Cycle has faced concerns about declining second hand car values and the continued shortage of new cars associated with supply chain disruption. The North American car dealership network had a challenging quarter for earnings. Having enjoyed high prices for used cars in recent years, supply chains are normalising and putting downward pressure on sales and margins. Our analysis suggests that the valuation pay-off remains attractive as while short-term trends are negative, the shares are pricing in an excessively negative scenario. In the 'Accelerating' category, **TSMC**, the semiconductor manufacturing business, was hit as the US imposed restrictions on sales of advanced semiconductors to China. This will impact TSMC as China accounts for approximately 10% of sales. Our assessment is that the valuation pay-off remains attractive given the technological advantage that TSMC retains in semiconductor manufacturing.

CITYWIRE AAA

Head of Equities

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James Clarke

Senior Fund Manager

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Senior Fund Manager