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Royal London Global Sustainable Credit Fund

Quarterly Investment Report

31 December 2023

ROYAL LONDON
ASSET MANAGEMENT

Quarterly Report

The fund as at 31 December 2023

The purpose of this report is to provide an update on the Royal London Global Sustainable Credit Fund. The report has been produced by Royal London Asset Management. The report starts with a summary dashboard showing key information about the fund. A glossary is located at the end of the report covering the description of some of the more technical terms used within the report. All data is as at the report date unless otherwise stated.

Contents

ROYAL LONDON
ASSET MANAGEMENT

The fund

Fund performance objective and benchmark

The fund's investment objective is to outperform the Bloomberg Barclays Global Aggregate Corporate Total Return Index Hedged USD (the "Benchmark") by 0.75% per annum over rolling three year periods (gross of fees). The Benchmark is being used by the Fund for performance comparison purposes only and the Fund does not intend to track it.

Benchmark: Bloomberg Barclays Global Aggregate Corporate Total Return Index Hedged USD

Fund value

	Total $m
31 December 2023	468.85

Asset allocation

	Fund (%)	Benchmark
Conventional credit bonds	98.97%	100.00%
Securitised	1.03%	-

Fund analytics

	Fund	Benchmark
Fund launch date	10 February 2021	
Base currency	USD	
Duration (years)	6.88	6.07
Gross redemption yield (%)	5.22	4.73
Number of holdings	266	15,909
Number of issuers	165	2,805

Performance and activity

Performance

	Fund (%)	Benchmark (%)	Relative (%)
Quarter	8.27	7.53	0.74
1 Year	9.33	9.10	0.23
3 Years (p.a.)	-	-	-
5 Years (p.a.)	-	-	-
10 Years (p.a.)	-	-	-
Since inception (p.a.)	(2.43)	(2.22)	(0.21)

Past performance is not a guide to future performance. Please refer to the Glossary for the basis of calculation and impact of fees. Performance and since inception date based on RL Global Sustainable Credit Fund (Z Acc) (USD). Source: Royal London Asset Management; Gross performance; Since inception date of the shareclass is 10 February 2021.

Performance commentary

The fund outperformed the index over the quarter (M Acc USD). Performance over the period was driven by a combination of tighter credit spreads and the additional yield built into the portfolio. In addition, given the levels that yields reached in the late summer of 2023, we were more inclined to add long-dated bonds in the expectation that yields would come down and long-dated bonds would see a greater benefit that short-dated equivalents. This effect was marked during November and December, and we took profits on this stance as we came into the year end, meaning we start 2024 with a neutral duration stance.

Sector positioning was broadly neutral over the period, but stock selection was another positive for the fund. Exposure to selected subordinated banking bonds was particularly helpful, as were holdings in the communications sector such as AT&T and Orange.

Performance and activity

Top 10 holdings

	Weighting (%)
LLOYDS BANKING GROUP PLC 7.953000000 2033-11-15	1.32
XYLEM INC 2.250000000 2031-01-30	0.97
LLOYDS BANKING GROUP PLC 4.582000000 2025-12-10	0.96
REPUBLIC SERVICES INC 2.300000000 2030-03-01	0.95
HSBC HOLDINGS PLC 7.390000000 2028-11-03	0.94
NN GROUP NV 4.625000000 2048-01-13	0.93
LEGAL & GENERAL GROUP 5.250000000 2047-03-21	0.91
ECOLAB INC 2.125000000 2032-02-01	0.88
PRUDENTIAL FINANCIAL INC 5.375000000 2045-05-15	0.88
AVISTA CORP 4.350000000 2048-06-01	0.84
Total	**9.58**

Fund activity

We continued to invest in bonds that meet both our demanding financial and sustainable criteria, and which fit into the sustainable themes that we think will endure and offer long-term solutions to the challenges that the world faces. We also aim to construct the fund to ensure that it yields more than the benchmark index. We believe that this positioning will be beneficial in the medium term, given the current valuation of credit markets and attractive opportunities we see.

The additional sustainable criteria we use mean that our portfolio will tend to have certain differences with the benchmark index. For instance, while it will have significant exposure to the banking sector, this is typically much lower in US banks than the index, reflecting the higher weighting of investment banks that typically do not score well on our criteria. In addition, the portfolio will usually have much lower exposure to China and India, where issuers may look attractive in financial terms, with many offering significant yield premia, but again do not score well on our criteria.

Financials remain the largest part of the market with issuance in 2023 skewed similarly. We continued to find opportunities across the financial sector, adding new senior issues from BPCE and Santander early in the period, also adding an AT1 subordinated new issue from Close Brothers at a yield in excess of 11%.. This market, having been very quiet since the Credit Suisse rescue, has been active with investors now confident that such debt will rank higher than equity holders in US dollar, euro and sterling markets.

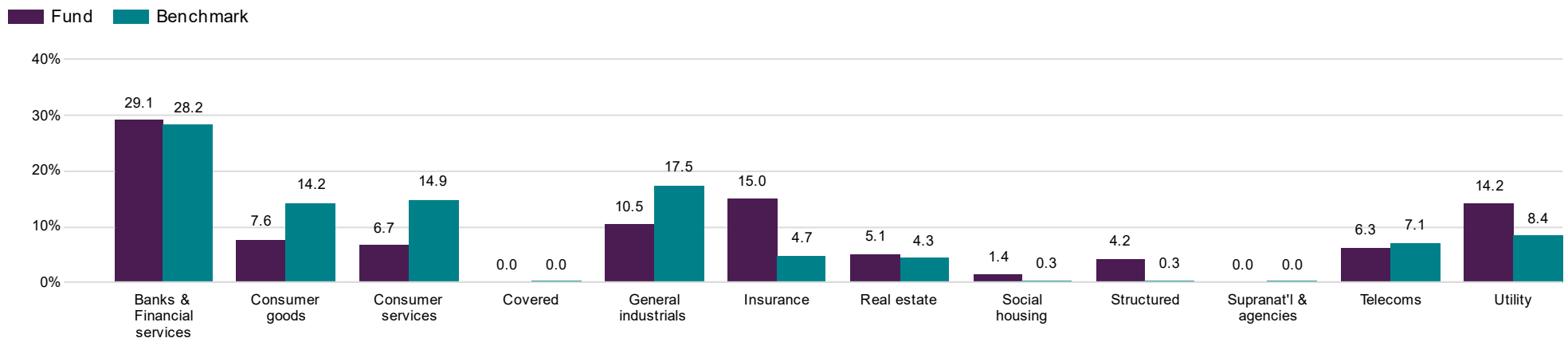
Social housing remains a key area for our sterling credit strategies. During the quarter a new issue of 2041 bonds from Places for People. The company owns and manages 240,000 properties across the UK and the bonds came at an attractive spread premium to the market.

There were noteworthy new issues in the structured sector as well. We added a five-year new issue from the RAC, these bonds yielding over 8%, with the bonds backed by cashflows of the operating company.

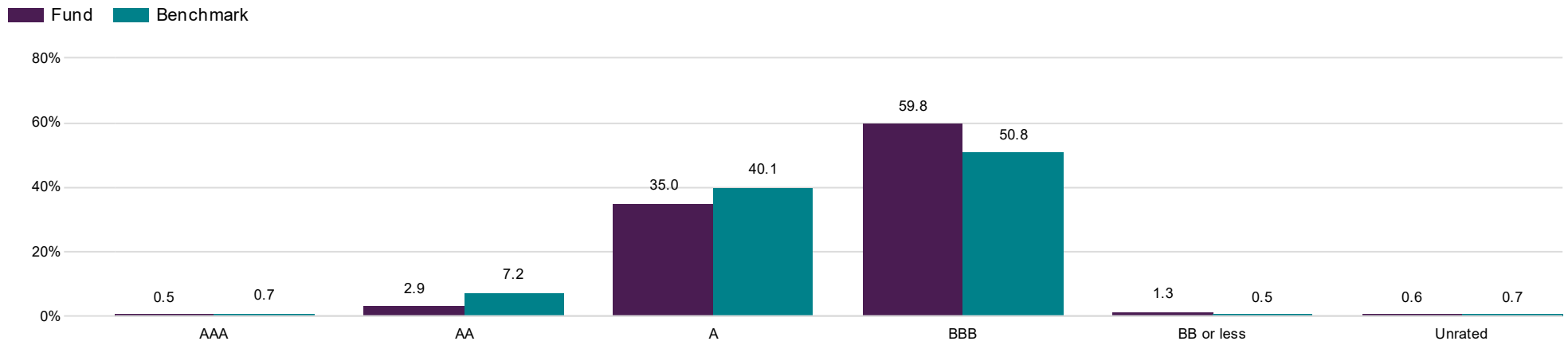
During the quarter secondary market activity was used opportunistically to reduce our exposure to senior financials, recycling monies raised into subordinated bonds where we felt that yields were very attractive given the current outlook. Examples included a senior to subordinated switch in bonds from Nationwide, BNP Paribas, Lloyds and Metropolitan Life. We also looked to reduce exposure to US dollar bonds from pharmaceuticals where spreads were very tight, adding to the telecoms sector where bonds looked more attractive, selling AstraZeneca and GlaxoSmithKline into AT&T and Telefonica respectively.

Fund breakdown

Sector breakdown

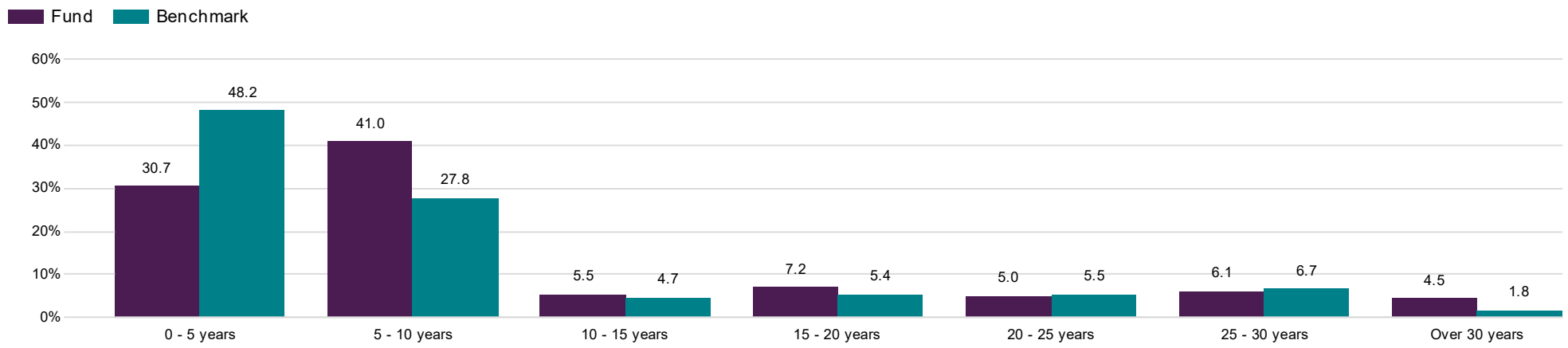


Credit ratings



Fund breakdown

Maturity profile



Characteristics and climate

ESG characteristics rationale

The Fund focuses on the sustainability of the products and services of the companies it invests in, as well as their standards of environmental, social, governance ("ESG") management, alongside financial analysis. The investment approach is fundamentally based on positive screening; identifying companies that are making a positive contribution towards a cleaner, healthier, safer and more inclusive society, through assessing both what a company does and how it does it, and through active engagement to encourage continual improvement. The fund will not invest in companies that undertake business activities deemed to be detrimental to society and that breach our Do No Significant Harm principle. Further details of the Funds Sustainable Investment process can be found in the ethical and sustainable investment policy at www.rlam.com

ESG characteristics

	Yes	No
ESG integration	✓	
Promotes environmental or social characteristics	✓	
Sustainable fund objective	✓	
Additional exclusions	✓	

Additional exclusions

Exclusion criteria that make sure a fund does not invest into a specific service or product. Royal London Asset Management has a controversial weapons exclusion across all investments.

Adult entertainment	✓	High environmental impact	✓
Alcohol	✓	Human rights issues	✓
Animal welfare	✓	Nuclear power	✓
Armaments	✓	Nuclear weapons	✓
Controversial weapons	✓	Tobacco	✓
Fossil fuels	✓		
Gambling	✓		

Climate metrics

	Fund	Benchmark	Difference (%)
Financed emissions (tCO2e)	12,348	n/a	n/a
Financed emissions coverage	74.47%	n/a	n/a
Carbon footprint (tCO2e/$M invested)	26.87	68.43	(60.73)
Carbon footprint coverage	74.47%	89.35%	(16.66)
Weighted average carbon intensity (tCO2e/$M sales)	115.76	194.48	(40.47)
Weighted average carbon intensity coverage	97.07%	96.43%	0.67

All climate metrics presented above are for Scope 1-2 emissions. Unless specified in the objective, the data is for information only and should not be taken to mean they are being managed to/controlled.

Implied temperature rise

	Fund (%)	Benchmark (%)	Difference (%)
Implied temperature rise (ITR) coverage	72.90	87.14	(16.34)
% of portfolio below 2°C ITR	59.28	62.02	(4.43)
% of portfolio below 1.5°C ITR	39.86	34.38	15.94

SBTi net - zero

	Fund (%)	Benchmark (%)	Difference (%)
SBTi Net-Zero committed	20.05	18.82	6.55
SBTi Near-Term committed	15.13	9.62	57.32
SBTi Near-Term targets set	27.52	27.81	(1.04)

Fund Engagement

Engagement definition

Engagement is active dialogue with investee companies (or other entities). There are two types: engagement for information, which is dialogue as part of investment research or ongoing monitoring, without specific objectives for change, and engagement for change, which is purposeful dialogue to influence positive change, with defined objectives and demonstrable outcomes.

Engagements

Engagement activity	Fund 3 months	Fund 12 months
Number of entities engaged	14	30
Number of engagements	23	73

This is an estimate. Some engagements at the issuer level may not have been attributed to the specific bond held in the fund, resulting in a lower number of engagement activities.

Total engagements by theme and topic

Climate	**4**
Climate - Transition Risk	4
Governance	**4**
Remuneration	2
Board	1
Corporate Governance	1
Health	**1**
Health - Community	1
Social & Financial Inclusion	**13**
Social & Financial inclusion	7
Just transition	5
Labour & Human Rights	1
Technology, Innovation & Society	**3**
Cybersecurity	3

Engagement focus

Firm-wide engagement activity is centred around six themes which we have identified in consultation with our clients. These are: climate change; biodiversity; health; governance and corporate culture; social and financial inclusion; innovation, technology and society. Portfolio level engagements are not thematic and are focussed on issues specific to managing the portfolio and meeting the investment objective.

Engagement data represents all engagements undertaken at both firm and portfolio level across Royal London Asset Management, and may not be limited to those undertaken solely for the purpose of managing the fund.

Fund Engagement

Engagement outcomes

E.ON SE

Purpose:

As co-leads of the CA100+ initiative, we facilitated a meeting between NGO Influence Map and E.ON to provide feedback on the company's lobbying disclosures.

Outcome:

E.ON welcomed the feedback and agreed to update its disclosures with greater transparency on its direct engagement and a complete list of its trade associations. However, the company disagreed with the criteria used to assess the alignment of trade associations and its own positions with the goals of the Paris Agreement, citing methodological inaccuracies. E.ON agreed to connect Influence Map with the Federation of German Industries (BDI) for further discussion.

National Grid Plc

Purpose:

Following the release of National Grid's Responsible Business Charter update, we engaged in a meeting with the Chief Sustainability Officer to offer feedback and suggest further enhancements to their climate transition plans.

Outcome:

National Grid was receptive to the majority of our feedback and sought additional guidance on their Just Transition plans. We positively acknowledged the company's improved emission reduction target and renewed emphasis on biodiversity. The company will be improving its lobbying disclosures and developing a Climate Transition Plan. However, it was unable to provide further clarity on forward looking expenditures and maintained that gas will continue to play a vital role in balancing the grid and, most notably, in their heating retail business in the US.

Standard Chartered

Purpose:

In a collaborative engagement on cybersecurity led by Royal London Asset Management, we engaged with Standard Chartered about its performance against our investor expectations. We used the opportunity to further understand its cybersecurity governance and risk management to assess whether it aligns with best practice.

Outcome:

Our conversation with Standard Chartered was positive and the company welcomed our feedback on how its practices and disclosures could be improved. Standard Chartered demonstrate best practice on the governance and risk management processes surrounding cybersecurity. We were satisfied that appropriate improvements have been made following a 2021 fine for failure to report breaches and encouraged related public disclosures. The security of the information perimeter is another area for improvement, and we gained comfort that the company was focused on this area.

Market commentary

Market overview

Economic attention over the quarter has been on inflation. At the start of the quarter investors focussed on the persistence of large price increases and central bank messaging on rates being held higher for longer. Yet, as headline inflation fell, sentiment swung dramatically towards the end of the quarter, pushing markets to price in interest rate cuts in 2024. The Federal Reserve (Fed), European Central Bank (ECB) and Bank of England (BoE) all left rates unchanged over the quarter, maintaining official rates at multi-year highs. The Fed has now held rates unchanged at its last three meetings. There has however been a significant shift in messaging, with the US central bank now indicating that it expects to cut rates by 0.75% in 2024. The ECB has similarly kept rates steady at its two most recent meetings, but central bankers in the eurozone said that no rate cuts have yet been discussed.

Global government bond yields started the quarter continuing the rising trend that started in mid-2020. This reflected market views that rising inflation would necessitate even higher interest rates and the mantra of higher for longer. Yet, with inflation starting to come down, expectations of rate cuts in 2024 contributed to significant falls in bond yields fell in November and December. The fall in yields was such that yields along the length of the curve ended the quarter lower than they started, and closed 2023 at roughly the same levels as they started. In the US, 10-year treasury yields fell from 4.57% to 3.88%, falling back from 15-year highs to reverse virtually all of the rise seen in the prior quarter. German 10-year bunds similarly saw material falls in the fourth quarter, falling from 2.84% to 2.01%.

The final couple months of 2023 saw very strong returns with a stunning magnitude of reversal in yields with spreads and rates substantially tighter. November ended up being the best month in 38 years for investment grade bonds, while it was simply the best month since last summer for the high yield market. Investment grade bonds did well relative to high yield due to the higher duration of these assets which was beneficial in a falling yield environment.

Global corporate bond markets saw a strong rally into year-end but this could limit performance from spreads in 2024. December continued in a similar vein to November with spreads and rates continuing their declines leading to another month of healthy returns – allowing 2023 to report double digit returns. Over the fourth quarter, the ICE BofAML US Corporate Index returned 7.91%, while in the euro zone and UK, the ICE BofAML Euro Corporate & Pfandbrief Index and iBoxx Sterling Non-Gilt indices returned 5.49% and 7.35% respectively.

Outlook

Inflation has come down significantly in 2023 but remains well above central bank targets, and now does not have the ‘easy’ wins of base effects to push this lower. Although the economic data remain very mixed, we still believe that higher interest rates will contribute to a slowdown in economic growth. This could well impact company earnings and lead to some increase in pressure on credit markets. However, consumer resilience has been greater than expected across most major economies, particularly in the US, which has helped support growth and prevent a recession. How this continues into 2024 could prove critical.

As we came into November 2023, we felt that the all-in yield on investment grade credit was looking very attractive, having risen significantly since the start of the year. The falls in government bond yields since then have largely reversed those rises. Our sterling credit strategy focuses on three sources of return: gilt yields, market credit spreads, and the additional credit spread we generate over credit benchmarks. Whilst ten-year bund yields of 2% are not as attractive as the 3% seen in October, we feel that the excess yield available on investment grade and high yield credit overcompensates for default risk. Similarly, we expect supply to weigh on credit markets in the first quarter but believe that underlying fundamentals will limit spread widening. Further, the additional yield embedded in our credit strategies, over that available from credit benchmarks, gives us confidence in our ability to deliver long-term outperformance.

Although recent outperformance means that the relative attractiveness of credit bonds has reduced, we still favour holding them compared to government debt as credit spreads remain at levels that more than compensate for the credit risk. Given the potential challenges in the outlook, we remain focused on identifying companies with strong balance sheets, favouring issues with security and downside protection, and ensuring that portfolios are diversified across issuers and sectors.

Further Information

Please click on the links below for further information:

Stewardship and responsible investment at RLAM

Responsible investment at RLAM

TCFD climate report

Royal London voting and engagement

Find out more

Royal London Asset Management's Outlook 2024 document and podcasts are both available on our website. In this year's Outlook document, our fund managers assess the challenges and opportunities in their respective asset classes for 2024. With an environment of falling inflation and modest recession, the benefits or risk for equities or credit is not so clear cut and knowing your companies is key. We analyse the areas of concern and potential growth within this environment.

In our Outlook 2024 podcast, Piers Hillier, CIO, looks ahead to 2024 and discusses the issues he believes will be prominent over the next 12 months, and where the key investment risks and opportunities may lie.

Articles, videos and webinars explaining our investment thinking can be found in the Our Views section of www.rlam.com, including regular updates from our Fixed Income, Global Equity, Sustainable and Multi Asset teams.

Disclaimers

Important information

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Issued in January 2024 by Royal London Asset Management Limited, 80 Fenchurch Street, London EC3M 4BY. Authorised and regulated by the Financial Conduct Authority, firm reference number 141665. A subsidiary of The Royal London Mutual Insurance Society Limited.

The Fund is a sub-fund of Royal London Asset Management Funds plc, an open-ended investment company with variable capital (ICVC), with segregated liability between sub-funds.

Incorporated with limited liability under the laws of Ireland and authorised by the Central Bank of Ireland as a UCITS Fund. It is a recognised scheme under the Financial Services and Markets Act 2000.

The Management Company is FundRock Management Company SA, Registered office: 33 rue de Gasperich, L - 5826 Hesperange, Luxembourg and is authorised and regulated by the Commission de Surveillance du Secteur Financier (CSSF).

The Investment Manager is Royal London Asset Management Limited.

For more information on the Fund or the risks of investing, please refer to the Prospectus or Key Investor Information Document (KIID), available via the relevant Fund Information page on www.rlam.com.

Most of the protections provided by the UK regulatory system, and the compensation under the Financial Services Compensation Scheme, will not be available.

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Risks and Warnings

Investment Risk

The value of investments and any income from them may go down as well as up and is not guaranteed. Investors may not get back the amount invested.

Credit Risk

Should the issuer of a fixed income security become unable to make income or capital payments, or their rating is downgraded, the value of that investment will fall. Fixed income securities that have a lower credit rating can pay a higher level of income and have an increased risk of default.

EPM Techniques

The Fund may engage in EPM techniques including holdings of derivative instruments. Whilst intended to reduce risk, the use of these instruments may expose the Fund to increased price volatility.

Exchange Rate Risk

Changes in currency exchange rates may affect the value of your investment.

Interest Rate Risk

Fixed interest securities are particularly affected by trends in interest rates and inflation. If interest rates go up, the value of capital may fall, and vice versa. Inflation will also decrease the real value of capital. Unlike the income from a single fixed interest security, the level of income (yield) from a fund is not fixed and may go up and down. Bond yields (and as a consequence bond prices) are determined by market perception as to the appropriate level of yields given the economic background.

Liquidity Risk

In difficult market conditions the value of certain fund investments may be difficult to value and harder to sell, or sell at a fair price, resulting in unpredictable falls in the value of your holding.

Emerging Markets Risk

Investing in Emerging Markets may provide the potential for greater rewards but carries greater risk due to the possibility of high volatility, low liquidity, currency fluctuations, the adverse effect of social, political and economic instability, weak supervisory structures and accounting standards.

Responsible Investment Risk

The Fund can only invest in holdings that demonstrate compliance with certain sustainable indicators or ESG characteristics. This reduces the number securities in which the Fund can invest and there may as a result be occasions where it forgoes more strongly performing investment opportunities, potentially underperforming non-sustainable funds.

Performance to 31 December 2023

Cumulative (%)

	3 Month	6 Month	1 Year	3 Years	Since Inception
Fund (gross)	8.27	6.02	9.33	-	(6.86)
Fund (net)	8.16	5.80	8.89	-	(7.93)

Annualised (%)

3 Years (p.a.)	Since Inception (p.a.)
-	(2.43)
-	(2.82)

Year on year performance (%)

	31/12/2022 - 31/12/2023	31/12/2021 - 31/12/2022	31/12/2020 - 31/12/2021	31/12/2019 - 31/12/2020	31/12/2018 - 31/12/2019
Fund (gross)	9.33	(14.74)	-	-	-
Fund (net)	8.89	(15.08)	-	-	-

Past performance is not a guide to future performance. The impact of fees or other charges including tax, where applicable, can be material on the performance of your investment.

Source: RLAM as at 31 December 2023. All figures are mid-price to mid-price in GBP for the RL Global Sustainable Credit Fund (Z Acc) (USD); Since inception date 10 February 2021.

Glossary

Asset allocation

Based on RLAM's holistic approach to fixed income management and fund weights relative to their respective benchmarks. May not reflect tactical exposures.

Carbon footprint

Exposure to high emitters in the portfolio, expressed in tCO2e/$M invested. Financed emissions (explained above) are divided by the portfolio value, the same approach for listed companies and private issuers is applied in this metric.

ESG Integration

The systematic and explicit inclusion of environmental, social and governance (ESG) factors into investment analysis and investment decisions.

Exclusions

Explicitly prohibits investing in a particular company, sector, business activity, country or region.

Financed emissions

The emissions from activities in the real economy that are financed through lending and investment portfolios, expressed in tCO2e. Emissions are attributed to a portfolio based on the portion of the company's value the portfolio holds, and using different accounting values for public and private corporates. We provide financed emissions for scope 1 and 2 emissions.

Fund restrictions definitions

Adult Entertainment: Companies which own or produce adult entertainment services, or engage in the distribution or sale of adult entertainment services.
Alcohol: Companies which have involvement in brewing, distillation or sale of alcoholic drinks.
Animal Welfare: Companies that conduct animal testing (other than for purposes of human or animal health and/or where it is required by law or regulation).
Armaments: Companies who manufacture armaments or nuclear weapons or associated products.
Controversial Weapons: Weapons which have an indiscriminate and disproportional impact on civilians or weapons that are illegal and prohibited by international conventions and treaties.
Fossil Fuels: Companies involved in the exploration, extraction or refining of oil, or gas, or coal, plus any activity relating to thermal coal.
Gambling: Companies who promote irresponsible gambling which includes betting shops, casinos or amusement arcades.
High Environmental Impact: Companies which have a high environmental impact, and which have 'no evidence' of appropriate environmental management systems.
Human Rights Risks: Companies with a strategic presence operating in countries of concern and which have 'no evidence' of policies or systems to manage human rights risks.
Nuclear Power: Companies who generate energy from Nuclear Power.
Nuclear Weapons: Companies that manufacture, nuclear; or are involved in the production of intended-use parts, whole weapons systems, or exclusive delivery platforms.
Tobacco: Companies which are growing, processing or selling tobacco products.

Gross redemption yield

Gross redemption yield is the rate of discount at which a bond's future obligations of interest and capital payments equates to its current price. The gross redemption yield shown for the fund is the average for its individual holdings, weighted by their current value, net of relevant fund management costs and gross of tax.

Implied temperature rise (ITR)

ITR aims to measure the global warming outcome from the emissions trajectory of a company, if the whole economy followed the same trajectory.

Number of holdings

Total number of unique holdings of the Fund excluding cash, currency and derivatives.

Number of issuers

Number of unique issuers of all assets held by the Fund, excluding cash, currency and derivatives.

Promotes environmental or social factors

An ESG Fund promotes, among other characteristics, environmental or social characteristics, or a combination of those characteristics, provided that the companies in which the investments are made follow good governance practices.

SBTi

The Science-Based Targets initiative is a consortium of organisations that set up the definition and promotion of science-based target setting.

Glossary

Sustainable fund objective

A product that has sustainable investment or a reduction in carbon emissions as its objective.

Top 10 holdings

Top 10 assets held by market value, excluding derivatives and cash.

Weighted Average Carbon Intensity (WACI)

Portfolio's exposure to carbon-intensive companies, expressed in tCO2e / $M revenue. Scope 1 and scope 2 GHG emissions are divided by companies revenues, then multiplied based on portfolio weights (the current value of the investment relative to the current portfolio value). The WACI is calculated as a weighted average sum of the holdings with carbon intensity coverage.