For professional clients only, not suitable for retail clients.

# RLPPC Over 5 Year Corporate Bond Fund

## Quarterly Investment Report

## 30 June 2023

# Quarterly Report

## The fund as at 30 June 2023

The purpose of this report is to provide an update on the RLPPC Over 5 Year Corporate Bond 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 of terms is located at the end of the report covering the principles by which this report has been constructed and descriptions of some of the more technical terms used within the report. All data within this report is as at the report date unless otherwise stated.

# Contents

# The fund

## Fund performance objective and benchmark

To outperform its benchmark by +0.50% per annum net of fees (on a rolling three year basis). The RLPPC Over 5 Year Corporate Bond Fund invests in sterling credit bonds, including sub-investment grade bonds. The fund also invests in UK government bonds and non-sterling bonds.

Benchmark: iBoxx Sterling Non-Gilt 5+ Index

## Fund value

| | Total £m |
|---|---|
| 30 June 2023 | 154.44 |

## Asset split

| | Fund (%) | Benchmark |
|---|---|---|
| Conventional credit bonds | 97.26% | 96.80% |
| Sterling conventional gilts | 2.45% | 0.42% |
| Foreign conventional sovereign | 0.29% | 2.78% |

## Fund analytics

| | Fund | Benchmark |
|---|---|---|
| Fund launch date | 2 July 2007 | |
| Base currency | GBP | |
| Duration (years) | 7.84 | 8.56 |
| Gross redemption yield (%) | 6.59 | 6.05 |
| Number of securities | 255 | 701 |
| Number of issuers | 191 | 353 |

Past performance is not a guide to future performance. Please refer to the glossary for a description of the yield used.

# Performance and analytics

## Performance

| | Fund (%) | Benchmark (%) | Relative (%) |
|---|---|---|---|
| Quarter | (3.59) | (4.42) | 0.83 |
| YTD | (0.73) | (1.46) | 0.73 |
| 1 Year | (8.30) | (10.05) | 1.75 |
| 3 Years (p.a.) | (6.71) | (9.10) | 2.39 |
| 5 Years (p.a.) | (1.08) | (2.58) | 1.51 |
| Since inception (p.a.) | 5.52 | 3.64 | 1.87 |

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 RLPPC Over 5 Year Corporate Bond Fund (Acc). Source: Royal London Asset Management; Gross performance; Since inception date of the shareclass is 2 July 2007.

## Performance commentary

The portfolio produced a negative return for the quarter, with the impact of rising gilt yields mitigated by a narrowing in credit spreads. On a relative basis, the portfolio performed well, outperforming the index. By sector, our overweight in insurance and significant underweight in supranationals were both positive, with stock selection the main driver of outperformance over the quarter.

The main driver for outperformance over the quarter was security selection in banks and insurance. The two sectors saw a strong rebound following the first quarter's sell-off in response to the Credit Suisse collapse and ultimate takeover from Swiss peer UBS. In both banking and insurance, capital restructuring was helpful, as legacy bonds were called at significant premia to prevailing market prices. In insurance our Legal & General 2064 bonds and Axa 2054 bonds benefitted from this. Towards the end of the period, Aviva paid a 16% consent fee to bondholders to allow them to bring the terms and conditions of their bond into compliance with current Solvency II requirements.

One issuer of note was Thames Water. Towards the end of the quarter, the CEO unexpectedly resigned, leading to significant focus on the utility's debt levels. The portfolio owns Thames Water bonds, with most exposure at the operating company level. We believe that operating company debt remains protected by the regulatory framework and the criticality of the infrastructure. The portfolio also held a smaller position in holding company debt (Thames Water Kemble 4.625 2026, rated B1 / B by Moodys and Fitch). This bond is secured on the equity of the operating company and is dependent on dividends from it to service debt. This lending is more subordinated and therefore carries greater credit risk. In aggregate, while the impact from exposure to Thames Water was negative for the portfolio, the effect was mitigated by portfolio's significant diversification.

# Performance and analytics

## Top 10 holdings

| | Weighting (%) |
|---|---|
| HSBC HOLDINGS PLC 8.201000000 2034-11-16 | 2.03 |
| HOME GROUP LTD 0.000000000 2027-05-11 | 1.39 |
| M&G PLC 6.340000000 2063-12-19 | 1.38 |
| FIN FOR RESID SOC HOUS 8.369000000 2058-10-04 | 1.28 |
| E.ON INTL FINANCE BV 6.125000000 2039-07-06 | 1.27 |
| ANNES GATE PROPERTY PLC 5.661000000 2031-06-30 | 1.25 |
| BARCLAYS PLC 6.369000000 2031-01-31 | 1.22 |
| EXCHEQUER PARTNERSHIP NO 5.396000000 2036-07-13 | 1.22 |
| DALI CAPITAL 29 4.799240000 2037-12-21 | 1.19 |
| UNITED KINGDOM GILT 3.750000000 2053-10-22 | 1.18 |
| **Total** | **13.41** |

## Portfolio activity

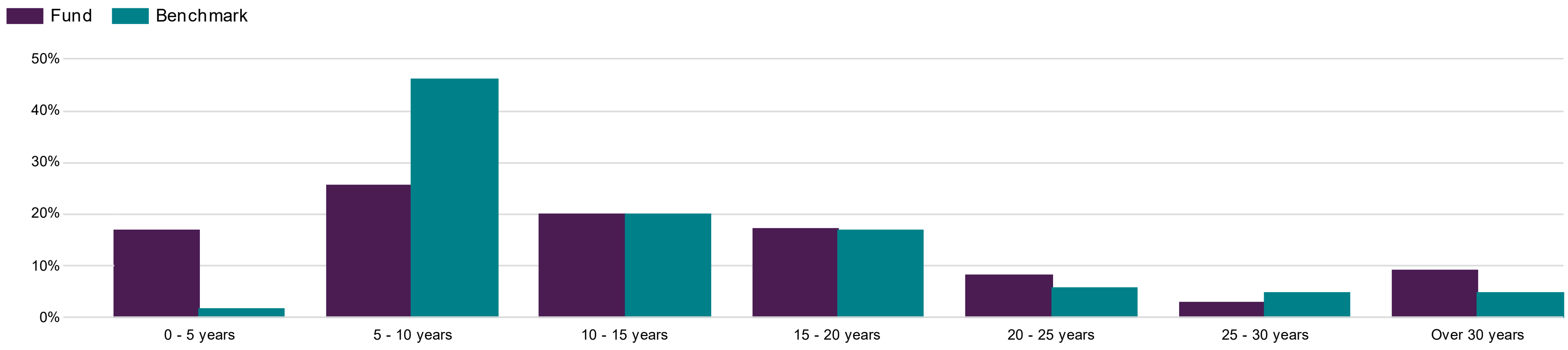
Financials remains an active area for new issues and with spreads attractive, we participated in a number of these, including senior bonds from interdealer broker TP ICAP, Close Brothers and Yorkshire Building Society at above-market premia to gilts – which combined with the rise in underlying gilt yields provide attractive all-in yields for the portfolio.

In the structured area, a key component of the portfolio, we added a new of 2039 bonds from Anglian Water – these bonds issued out of the operating company and hence benefit from being part of a regulated utility with good cashflow visibility.

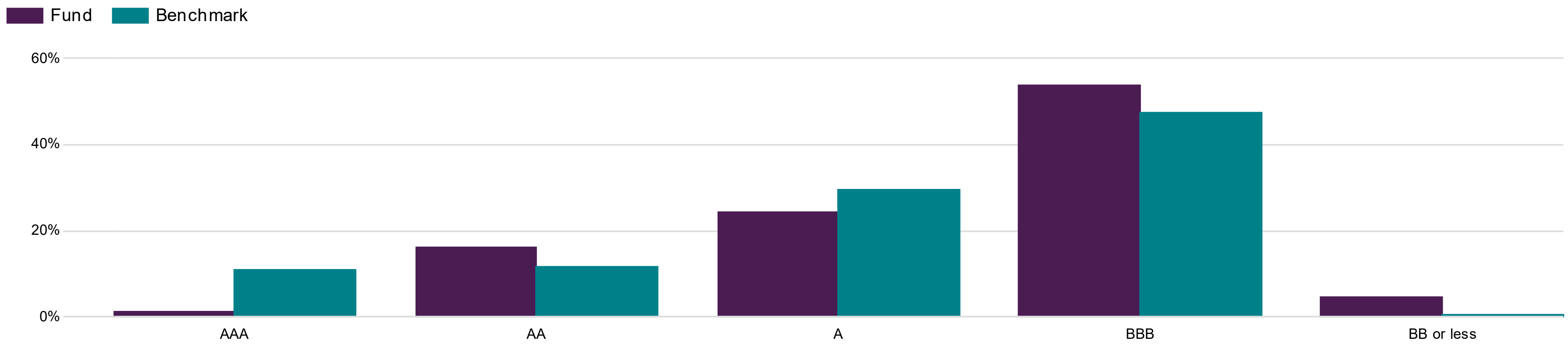
Finally we bought new sterling-denominated hybrid bonds from Vodafone and in the utilities sector, we added a new 10-year issue from National Grid.

# Asset allocation

## Maturity profile

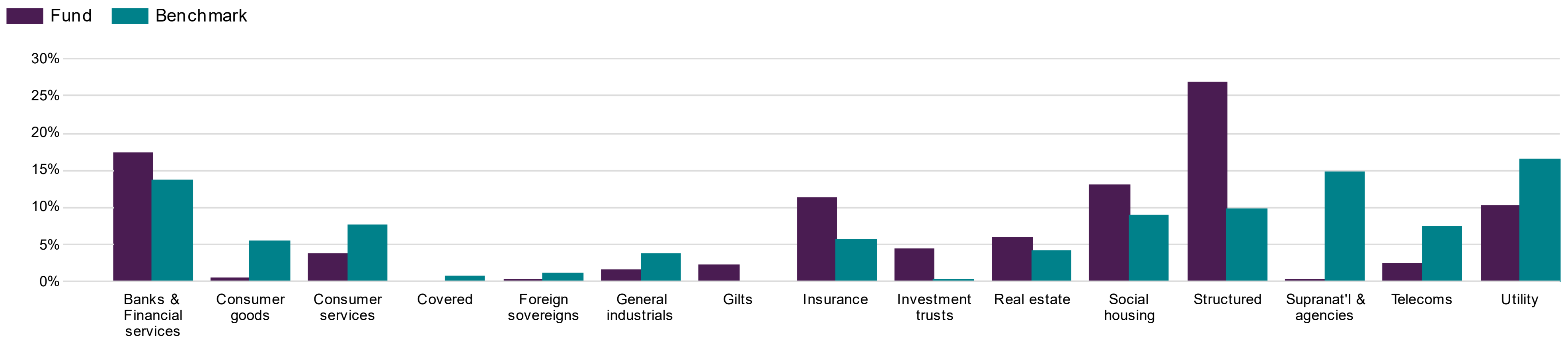



## Credit ratings



# Asset allocation

## Sector breakdown



# Market commentary

## Economic and market overview

Central bank interest rate rises have been the story of the second quarter. For the major central banks of the Federal Reserve (Fed), European Central Bank (ECB) and Bank of England (BoE), after more than 12 months of tightening monetary policy, market attention has turned towards expectations of when and at what level rates will peak. In contrast to 2022, when all three were expected to continue hiking, the changing growth and inflation picture in the US, euro zone and UK means that expectations have become more differentiated.

Despite the emerging divergent paths, the major central banks are on, they continued their rate hiking route. The Fed, ECB and BoE all pushed rates higher in the quarter. The BoE increased rates the most, with hikes of 0.25% and 0.50% in May and June respectively, while the ECB hiked 0.25% at its two meetings and continued to talk future rate rises. In contrast, after hiking rates by 0.25% in May, the Fed left rates unchanged in June. Despite market hopes that this may be the end of the tightening cycle, Fed officials pencilled in a further two interest rate hikes over the coming quarters as well as revising up their expectations for inflation, citing a strong labour market and persistent 'stickier' core inflation.

Since the start of the current cycle the Fed has increased rates by 5.00% over the course of ten rises since March 2022. The BoE started the cycle at 0.1% but has moved rates higher 13 times since the end of 2021, now sitting at 5.00%, while the ECB on the other hand has only increased its main refinancing operation rate eight times to 4.00%. The ECB has indicated that a hike in July is likely and said that "inflation has been coming down but is projected to remain too high for too long". For the BoE, inflation also means more hikes are likely, with the market now pricing in a peak of 6-6.25%.

The level of UK GDP remains little changed since late 2021. Meanwhile, inflation remained strong, and surprised on the upside: year-on-year CPI inflation fell less than expected on data released over the quarter from 10.1% year-on-year for the March release to 8.7% for May release. Meanwhile, annual core inflation did not fall at all, rising to 7.1% in May from 6.2% in March. Regular pay growth data also rose on the data released during the quarter, reaching 7.2% for the three months to April.

In the US, CPI inflation fell further to 4.0% year-on-year in May, with core inflation now higher than headline at 5.3%. Core CPI inflation rose 0.4% on the previous month in the May data, although the equivalent core PCE measure of inflation was softer at 0.3%. Economic activity indicators looked consistent with positive activity growth in the second quarter, including strong payroll gains in April and May, although the unemployment rate rose in May. The debt ceiling stand-off was eventually resolved in a deal that suspended the debt ceiling until January 1 2025.

Euro area CPI fell to 5.5% year-on-year over the second quarter. However, core inflation did not show a clear downward trend. Meanwhile, back revisions showed the euro area economy in a technical recession over the turn of the year.

UK government bonds struggled, being impacted by the higher-than-expected inflation print. Gilts delivered a -5.42% return (FTSE Actuaries) over the second quarter with the benchmark 10-year gilt yield rising 90 basis points to 4.39%. Shorter-dated bonds outperformed longer-dated bonds, with the ultra-short end of the curve the only area able to eke out a positive performance in the three-month period. In the US, 10-year treasury yields rose to 3.84% from 3.47%, while in Germany the 10-year bund yield increased to 2.39% from 2.29%.

The sterling investment grade credit market (Non-Gilt) returned -3.39% over the quarter, struggling as gilt yields increased and gave back all gains made in the previous quarter. The average sterling investment grade credit spread (the average extra yield available from non-gilt bonds compared with government debt of equal maturity) tightened from 1.61% to 1.48% (iBoxx). Following the tough end to the first quarter for subordinated bank debt, tier 1 bonds were the best performing sector in the second quarter, despite posting a small negative return. The losses were broad based, but utilities were particularly hard hit, as were telecoms and real estate.

Primary credit activity picked up through the quarter after a particularly slow April. Sterling issuance was £17.2bn over the quarter, which was behind the £23.7bn issued in the first quarter but ahead of the £11.1bn seen in the same period a year prior.

# Market commentary

## Outlook

We expect that inflation has peaked. This is driven by our view that energy prices will moderate and that weaker GDP growth will reduce the tightness of the labour market. Nonetheless, UK interest rates are likely to rise further as the BoE continues to focus on bringing inflation under control.

Although the economic data remain very mixed, we still believe that higher rates will lead to a slowdown in the UK, impacting company earnings and leading to some increase in credit rating downgrades and default rates. Nevertheless, it is our view that an asset allocation in favour of sterling credit bonds is appropriate as credit spreads remain at reasonably 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) remains attractive, particularly if inflation starts to fall as we expect. Our strategies generally have a material yield premium to the market, which we feel will support performance both in absolute terms and relative to the market. Our strategies typically have a significant targeted exposure to BBB rated bonds, but we believe that compensation for default risk remains most attractive in this rating band.

# Further Information

## Please click on the links below for further information:

- Stewardship and responsible investment at RLAM
- Royal London Sterling credit ESG analysis
- Royal London voting and engagement

## Find out more

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

For professional clients only, not suitable for retail clients.

This is a financial promotion and is not investment advice.

Telephone calls may be recorded. For further information please see the Privacy Policy at www.rlam.com.

Issued in July 2023 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.

iBoxx indexes and data are an intellctual property of Markit North America, Inc., Markit Indices GmbH, Markit Equities Limited and/or its affiliates iBoxx and has been licensed for use in connection with the fund (or other investment vehicle) or securities referenced herein.

The Index provided by IHS Markit is subject to disclaimer currently available here (and as updated by IHS Markit from time to time): https://ihsmarkit.com/Legal/disclaimers.html and/or in the prospectus for the Fund.

# Risks and Warnings

**General Risks**

The degree of investment risk depends on the fund you choose.
The prices of units can go down as well as up.
The return from your investment is not guaranteed; therefore, you may get back less or more than shown in the illustrations.
You may not get back the amount that you originally invested.
Past performance is not a guide to future return.
Inflation may, over time, reduce the value of your investments in real terms.
There may be a variation in performance between funds with similar objectives owing to the different assets selected.
Funds aiming for relatively high performance can incur greater risk than those adopting a more standard investment approach.
The use of derivatives in pursuit of a fund's objective may cause its risk profile to change and this may be material.

**Fixed interest security 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. Key determinants include economic growth prospects, inflation, the government's fiscal position, short-term interest rates and international market comparisons. The returns from bonds are fixed as at the time of purchase. Therefore the fixed coupon payable and the final redemption proceeds are known at the outset. This means that if a bond is held until its redemption date, the total return that could be expected is unaltered from its purchase date, subject to counterparty default (see 'Credit risk' below). However, over the life of a bond, the yield priced by the market (as opposed to actual fixed coupons payable) at any given time will depend on the market environment at that time. Therefore, a bond sold before its redemption date is likely to have a different price to its purchase price and a profit or loss may be incurred.

**Credit risk**

The value of a fixed interest security will fall in the event of the default or reduced credit rating of the issuer. Generally, the higher the rate of interest, the higher the perceived credit risk of the issuer. This fund may invest a percentage of it's assets in sub-investment grade bonds. Such bonds have characteristics which may result in higher probability of default than investment grade bonds and therefore higher risk.

**Overseas markets risk**

Funds investing in overseas securities are exposed to, and can hold, currencies other than Sterling. As a result, overseas investments may be affected by the rise and fall in exchange rates.

**Derivatives risk for Efficient Portfolio Management:**

Derivatives may be used by this Fund for the purpose of efficient portfolio management. This restricts the use of derivatives to the reduction of risk and the reduction of cost. Such transactions must be economically appropriate and the exposure fully covered.

**Derivatives risk for investment purposes:**

This fund may undertake transactions in derivatives and forward transactions (both on exchange and over the counter (OTC)). These may include interest rate swaps and interest rate futures for the purposes of meeting the investment objective, protecting the risk to capital, duration and credit management, as well as for hedging. While the discerning use of derivatives can be beneficial, derivatives also involve specific risks. These risks relate specifically to market risk, management risk, credit risk, liquidity risk, the risk of mispricing or improper valuation of derivatives and the risk that derivatives may not correlate perfectly with underlying assets, interest rates and indices. The use of derivative instruments may from time to time alter the economic exposure of the fund causing it to deviate significantly from the performance of the market as a whole. The use of these derivatives will be within the parameters allowed for linked funds by the Financial Conduct Authority and Prudential Regulation Authority.

# Performance to 30 June 2023

## Cumulative (%)

| | 3 Month | 6 Month | 1 Year | 3 Years | 5 Years |
|---|---|---|---|---|---|
| **Fund (gross)** | (3.59) | (0.73) | (8.30) | (18.81) | (5.27) |
| **Fund (net)** | (3.60) | (0.74) | (8.31) | (18.83) | (5.80) |

## Annualised (%)

| 3 Years (p.a.) | 5 Years (p.a.) |
|---|---|
| (6.71) | (1.08) |
| (6.72) | (1.19) |

## Year on year performance (%)

| | 30/06/2022 - 30/06/2023 | 30/06/2021 - 30/06/2022 | 30/06/2020 - 30/06/2021 | 30/06/2019 - 30/06/2020 | 30/06/2018 - 30/06/2019 |
|---|---|---|---|---|---|
| **Fund (gross)** | (8.30) | (15.65) | 4.97 | 8.07 | 7.96 |
| **Fund (net)** | (8.31) | (15.66) | 4.96 | 7.83 | 7.64 |

**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 30 June 2023. All figures are mid-price to mid-price in GBP for the RLPPC Over 5 Year Corporate Bond Fund (Acc).

# Glossary

### Asset split
Breakdown of the assets by asset classes. Based on RLAM asset classification scheme.

### Credit ratings
Credit ratings are based on RLAM composite ratings which uses a hierarchy of S&P, Moody's and then the Fitch rating.

### Credit spread
Credit spread is the difference in yield between two debt securities of the same maturity but different credit quality.

### Distribution yield
The distribution yield reflects the amounts that may be expected to be distributed over the next 12 months. It is calculated net of standard management charges. It reflects RLAM's current perception of market conventions around timing of bond cash flows.

### Duration
Measure of sensitivity of a Fixed Income instrument to changes in interest rates, indicating the potential impact of interest rate fluctuations on the value of the investment.

### FX adjusted yield
FX adjusted yield is the gross rate of return to the expected maturity adjusted for hedging and includes the impact of cash.

### Fund analytics
All figures exclude cash. Credit bonds include non-sterling bonds and CDs where held within the fund or benchmark.

This is applicable to the following sections: fund Asset Allocation, Duration, Yield curve, Sector breakdown, Financial holdings, Credit ratings.

### Fund size
Total value of the fund as of the last business day of the calendar month. The valuations are based on signed off prices and are on a mid-price basis.

### 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.

### Internal ratings
Internal ratings are derived using RLAM's credit rating methodology. Applicable for bonds that are not rated by the external rating agencies (S&P, Moody's and Fitch).

### Performance
Performance is calculated using the signed off NAV per share. The impact of fees or other charges including tax, where applicable, can be material on the performance of your investment. The impact of fees reduces the return.

### Rating changes - downgrades
Directly held credit bonds downgraded from investment grade to sub-investment grade based on the RLAM composite rating during the quarter.

### Rating changes - upgrades
Directly held credit bonds upgraded from sub-investment grade to investment grade based on the RLAM composite rating during the quarter.

### Real yield
Real yield shows the inflation-adjusted redemption yield for the underlying fund and therefore does not include the impact of fees. For share class level yields, please see the latest factsheet.

### Sector breakdown
Breakdown of the fund assets, excluding derivativs and cash by RLAM's internal industry sector classification scheme.

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

### Yield to worst
Yield to worst is a measure of the lowest possible yield that can be received on a bond that fully operates within the terms of its contract without defaulting.