Royal London Multi Asset Credit Fund

Quarterly Investment Report

30 September 2023

Quarterly Report

The fund as at 30 September 2023

The purpose of this report is to provide an update on the Royal London Multi Asset 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 with the report. All data within this report is at the report date unless otherwise stated.

Contents

The fund

Fund performance objective and benchmark

The fund will seek to outperform its benchmark, SONIA, by 4-6% per annum over rolling three year periods (gross of fees).

Benchmark: SONIA (Sterling Overnight Index Average)

Fund value

	Total £m
30 September 2023	819.90

Fund analytics

	Fund
Fund launch date	3 July 2017
Base currency	GBP
Duration to worst (years)	2.94
FX adjusted yield (%)	8.37

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

Performance and activity

Performance

	Fund (%)	Benchmark (%)	Relative (%)
Quarter	1.18	1.25	(0.06)
YTD	5.56	3.27	2.29
1 Year	8.89	3.97	4.92
3 Years (p.a.)	2.17	1.57	0.61
5 Years (p.a.)	2.51	1.20	1.31
10 Years (p.a.)	-	-	-
Since inception (p.a.)	2.48	1.11	1.37

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 Multi Asset Credit Fund (Z Inc). Source: Royal London Asset Management; Gross performance; Since inception date for the share class is 9 October 2017.

Performance commentary

The fund was slightly behind its Sterling Overnight Index Average Rate (SONIA) benchmark in the quarter with short-dated leverage loans aiding performance. Year-to-date, the fund is considerably ahead of its benchmark.

The benefit of the loan book in the portfolio includes the high carry, the short interest rate duration risk and convexity (as most high-quality loans trade below par) so there is optionality on a refinancing in a defensive instrument.

Performance and activity

Top 10 holdings

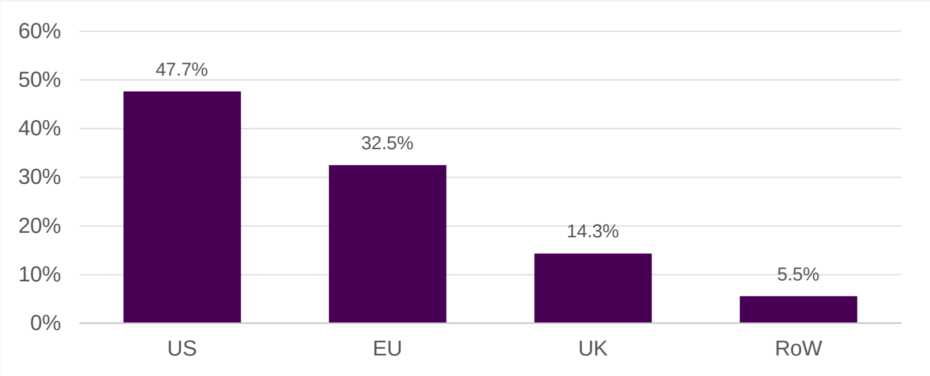
	Weighting (%)
Sprint Llc 7.625% 15/02/2025	1.25
Palmer Square European Loan Fundi Frn 15/07/2031	1.03
Eircom Tl 1l EUR 3% Loan 15/05/2026	0.98
Transdigm Inc 6.25% 15/03/2026	0.93
Dryden 56 Euro Clo 2017 Dac Frn 15/01/2032	0.93
Techem Blitz F 6% 30/07/2026	0.91
Gems Menasa Cayman Ltd Gems Ed 7.125% 31/07/2026	0.89
Tenet Healthcare Corp 4.875% 01/01/2026	0.89
Actina Tl B3 1l Loan 6.875999928 30/09/2028	0.88
Rollsroyce Plc 5.75% 15/10/2027	0.87
Total	**9.54**

Fund activity

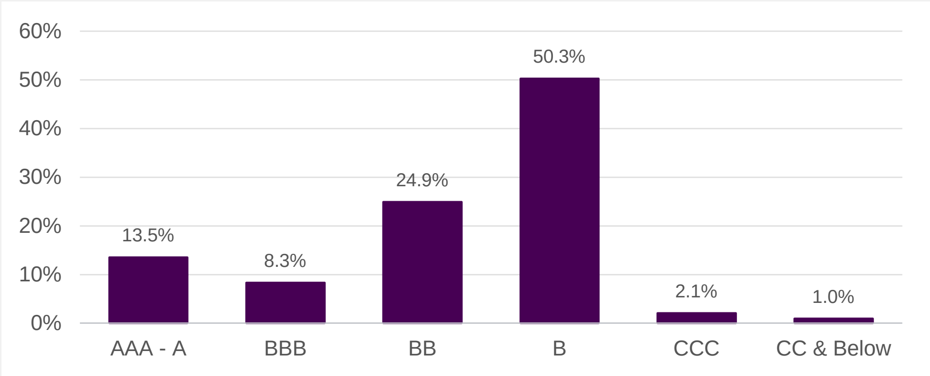
Spreads tightened in the quarter, hitting their tightest levels year-to-date as government bond yields moved higher. We are seeing spreads come in as contrary to consensus, high yield and leveraged loan markets are doing better than investment grade or government markets and default rates continue to be very benign in public markets running at just 2% in the US high yield market (and 1% and 3% in Europe and emerging markets, respectively). In fact, the last 12-month rate actually dropped to 2.0% during the third quarter as last August's lumpy defaults fell out of the calculation but then picked up and was 2.5% in September.

Asset allocation

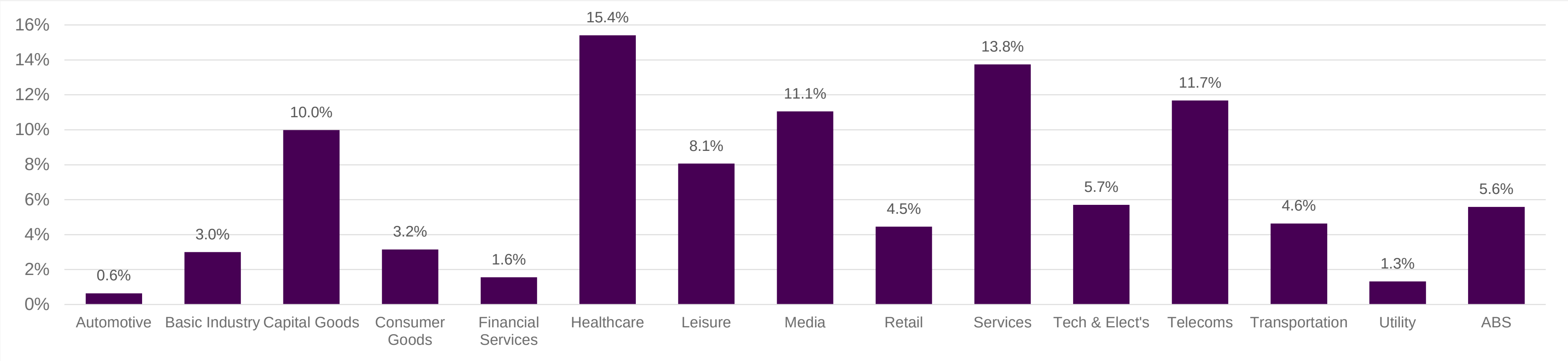
Regional profile



Credit ratings



Sector allocation



Market commentary

Market overview

The third quarter was characterised by mixed data around the world, with central banks coming towards the end of their rate hiking path, but with cuts still seemingly a while away. The global economic picture is rosier now than it was at the start of the year, but global growth is spluttering again amid a disappointing bounce in China activity, slow-to-no growth in Europe and against a backdrop of restrictive monetary policy. The US still looks at risk of recession too, even if activity data to date has been fairly robust.

Inflation has fallen significantly and, although higher energy prices threaten a widespread revival in headline inflation, other factors – including a soggy economic activity backdrop – should pull inflation lower still. With taming inflation still the priority for central banks, there is still a possibility of further rate hikes from the Federal Reserve (Fed), European Central Bank (ECB) and Bank of England (BoE), but peak rates look to be near, with real rates now well into positive territory.

In the US, the real economy has been surprisingly resilient in the face of tighter credit conditions. However, the fourth quarter looks set to see a few growth challenges, monetary policy is restrictive and employment growth has slowed. A number of recession indicators are still flashing. Business survey data paints a mixed picture, with PMIs consistent with flattish growth while ISM surveys look more upbeat. Employment gains have slowed on the non-farm payrolls data and job openings have fallen a long way from their highs consistent with a less tight labour market. Housing-related activity remain subdued.

The Fed continued to hike rates over the quarter against a still resilient labour market backdrop, to help ensure inflation returns sustainably to target. Over the third quarter, the Fed raised the Fed Funds target range by another 25bps to 5.25-5.50%. As of their September meeting, the mean forecast of participants still had one more rate increase in it for the rest of 2023, but removed some of the rate cuts that participants had pencilled in for 2024. Over the quarter, CPI inflation rose to 3.7% year-on-year by August, from 3.0% in June driven by higher energy inflation, but with core continuing to drift lower over the period. The core PCE measure of inflation fell over the quarter and month-on-month was only 0.1% in August. Second quarter GDP recorded a steady-ish 2.1% quarter-on-quarter annualised. More timely economic activity indicators were mixed over the quarter. The government shutdown stand-off was eventually resolved at the last minute, but with a stop-gap measure that will fund the government only through to mid-November 2023.

The euro area economy may already be in mild recession and forecasts continue to pencil one in. Business surveys have deteriorated and look consistent with falling private sector output. Tighter monetary policy will still be feeding through to the real economy. Bank lending conditions have tightened and loan growth has slowed. High domestically driven inflation continues to point to the balance of risks being in the direction of further hikes.

Over the third quarter, the ECB again raised rates 50bps. At the September meeting, they signalled that current levels would potentially mark the peak, while leaving the door open for further rate hikes if necessary. Euro area CPI fell to 4.3% year-on-year in September from 5.5% in June. Core CPI fell over the same period too and showed a clearer downward trend than over the previous quarter. The euro area economy grew (only) 0.1% on a quarterly basis in the second quarter - the same outcome as seen in the first three months of the year. However, business surveys signalled a deterioration in activity into more recessionary territory by the end of the quarter.

UK data released in the third quarter painted a picture of slower economic activity, with high but falling inflation albeit featuring still-strong domestic inflationary pressure. Second quarter GDP grew 0.2% quarter-on-quarter in real terms. Upward back revisions to GDP over the quarter showed Q2 GDP as 1.8% above pre-pandemic levels (0.2% previously), with the bulk of revisions from before 2022. The data showed that the UK economy experienced a less-bad pandemic in GDP terms than first estimated. Meanwhile, inflation fell, and tended to surprise on the downside at headline level: year-on-year CPI inflation fell from 8.7% for the May release to 6.7% for the August release. Core inflation fell from 7.1% to 6.2% over the same period. Consistent with a somewhat looser-looking labour market and lower than expected inflation, the Bank of England raised rates another 25bps in August to 5.25% but chose to keep rates on hold at their September meeting.

The outlook is still lacklustre in the UK. A technical recession is still assumed for the UK in the next 12 months, but a modest one. There are still risks from the housing sector and consumer spending has yet to respond fully to tighter monetary policy. GDP growth has been weak since late 2021 and PMI business surveys point to deterioration, falling into recessionary territory over the summer. Inflation should fall significantly at headline level, but domestically driven inflation continues to look strong, despite higher interest rates. The labour market is starting to look less tight and lead indicators of wage growth suggest some slowing ahead but so far, pay growth remains much too strong to be consistent with hitting a 2% inflation target.

In the high yield market, the ICE BofAML (BB-B) Global Non-Financial High Yield Index benchmark returned 0.47% in the quarter as spreads tightened to 376bps. At the end of the period, the index's yield-to-worst stood at 8.29%, rising from 8.20% at the start of the year. In the broader-based high yield index, which includes CCC rated bonds, spreads tightened to 438bps, with a yield-to-worst of 8.90%.

Market commentary

Global corporate bond markets saw similar underlying influences over the third quarter, with differing overall results. All markets faced the headwind of rising government bond yields, but with this mitigated by ongoing additional carry, and tighter credit spreads as corporates continued to perform well in spite of the higher interest rate environment. In the US, the impact of higher government bond yields dominated returns, leading to a negative return over the quarter, the ICE BofAML US Corporate Index returning -2.70%, while in the eurozone and UK, larger spread tightening and smaller government bond yield increases meant positive returns, with the ICE BofAML Euro Corporate & Pfandbrief Index and iBOXX Sterling Non-Gilt indices returning 0.28% and 2.26% respectively.

Global government bond markets continued to see yields move higher – a trend that started in mid-2020, reflecting market views that rising inflation would necessitate higher interest rates and that the central banks and governments would ultimately have to withdraw the support measures put in place during the global financial crisis and then used further to help mitigate the economic impact of Covid. With the end of the rate rising cycle possibly in sight, but issuance expected to remain high, markets have become more volatile. In the US, 10-year treasury yields rose to 4.57% from 3.84%, hitting heights not seen in fifteen years, while in Germany the 10-year bund yield increased to 2.84% from 2.39%.

UK government bonds struggled, being impacted by the higher-than-expected inflation print. Gilts delivered a -0.63% return (FTSE Actuaries) over the third quarter with the benchmark 10-year gilt yield rising to 4.44% from 4.39% but pulled back from a 4.75% high seen in mid-August. There was a marked difference in maturities, with short-dated bonds materially outperforming longer-dated bonds, as expectations that rates may be at a peak helped short-dated bonds start to anticipate cuts in late 2024, while longer-dated bonds remained weak due to concerns about the long-term inflation environment and significant gilt supply.

Outlook

In our view, the banking turmoil towards the end of the first quarter means a global recession is closer than anticipated at the start of the year. Banks will look to be more cautious with lending, leading to a broad credit contraction that we would expect to push the global economy into recession towards the end of this year or early 2024. Our focus will remain on the Fed. With inflation expected to fall back towards the long-term target, the levels that the Fed is happy with and when it then begins to lower rates will be the key factor for the upcoming year.

In this higher rate environment, we are beginning to see a disconnect between yields and valuations. The longer yields stay higher, there will be a realisation that higher costs of capital are here to stay so valuations will need to be adjusted. This supports our move into investment grade names as some of the longer duration, high quality, low single A, high BBB, and longer duration debt offer good value with 5% plus yields. If the rates environment starts to turn you also get some yield compression which gives you some good convexity.

Current default rates are very low at around 2-3% and while we expect this to track to 3% over the course of this year. These levels would be entirely normal in an historic context, but the nature of the economic backdrop and strong company balance sheets means we expect default rates to grinding higher over this period, instead of sharply spiking.

It is also worth mentioning implied default rates take 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 our default and recovery expectations remain extremely benign. We are seeing yields at their highest rates in 10 years or more, so we feel comfortable handling the predicted rise in defaults to come as our cushion is more substantive.

In our view, the way through difficult markets is to focus on those risks that you can control and know what you own. We will keep spread 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, meaning 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.

ROYAL LONDON ASSET MANAGEMENT

Further information

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.

Notable publications in the third quarter include our annual Climate Report, as well as our annual Assessment of Value reports, available from the home page of www.rlam.com.

Disclaimers

Important information

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Issued in October 23 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 Investment Funds ICAV, an Irish collective asset-management vehicle authorised by the Central Bank of Ireland pursuant to the Irish Collective Asset-management Vehicles Act 2015 and the AIFM Regulations, and has been established as an umbrella fund with segregated liability between Funds.

It is not a recognised scheme under the Financial Services and Markets Act 200.

The Management Company is FundRock Management Company SA, Registered office: 33 rue de Gasperich L-5826 Hespergange, 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 available via the relevant Fund Information page on www.rlam.com.

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

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.

CIBOR (Copenhagen Interbank Offered Rate) is owned and administered by Danish Financial Benchmark facility (DFPF). The use of CIBOR does not imply or express any approval or endorsement by DFBF.

Risk 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.

Concentration Risk

The price of Funds that invest in a reduced number of holdings, sectors, or geographical areas may be more heavily affected by events that influence the stockmarket and therefore more volatile.

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.

Leverage Risk

The Fund employs leverage with the aim of increasing the Fund's returns or yield, however it also increases costs and its risk to capital. In adverse market conditions the Fund's losses can be magnified significantly.

Derivative Risk

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 purpose of meeting the investment objective, protecting the risk to capital, duration and credit management, as well as 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 the these derivatives will be within the parameters allowed for linked funds by the Financial Conduce Authority and Prudential Regulation Authority.

Efficient Portfolio Management (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 form 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.

Counterparty Risk

The insolvency of any institutions providing services such as safekeeping of assets or acting as counterparty to derivatives or other instruments, may expose the Fund to financial loss.

Performance to 30 September 2023

Cumulative (%)

	3 Month	6 Month	1 Year	3 Years	5 years
Funds (gross)	1.18	2.29	8.89	6.66	13.20
Fund (net)	1.16	2.25	8.82	6.44	12.93

Annualised (%)

3 Years (p.a.)	5 years (p.a.)
2.17	2.51
2.10	2.46

Year on year performance (%)

	30/09/2022 – 30/09/2023	30/09/2021 – 30/09/2022	30/09/2020 – 30/09/2021	30/09/2019 – 30/09/2020	30/09/2018 – 30/09/2019
Funds (gross)	8.89	(10.88)	9.92	0.95	5.14
Fund (net)	8.82	(10.95)	9.84	0.91	5.14

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 September 2023. All figures are mid-price to mid-price in GBP for the Royal London Multi Asset Credit Fund (Z Inc).

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 the Fitch rating.

Duration

Measure of sensitivity of a Fixed Income instrument to charges 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 excludes 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.

Performance

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

Sector breakdown

Breakdown of the fund assets, excluding derivatives 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.