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Royal London Sustainable Managed Growth Trust

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 Sustainable Managed Growth Trust. 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.

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The fund

Fund performance objective and benchmark

The fund's investment objective is to achieve a total return over the medium term (3-5 years) by investing mainly in sterling denominated bonds, with some exposure to the shares of UK companies, that are deemed to make a positive contribution to society. Investments in the fund will adhere to the Manager's ethical and sustainable investment policy.

The IA Mixed 0-35% Shares sector is considered an appropriate benchmark for performance comparison.

Fund value

	Total £m
30 September 2023	852.06

Asset Mix

	Holdings	Weight
Equity	49	25.53%
Fixed Income	248	74.47%

Fund analytics

	Fund
Fund launch date	4 December 2012
Base currency	GBP
Number of holdings	297

Performance and activity

Performance

	Fund (%)	IA Sector (%)	Relative (%)
Quarter	1.51	(0.51)	2.02
YTD	4.10	0.44	3.66
1 Year	10.55	2.44	8.11
3 Years (p.a.)	(1.69)	(0.85)	(0.84)
5 Years (p.a.)	2.47	0.59	1.88
10 Years (p.a.)	4.88	2.14	2.74
Since inception (p.a.)	5.02	2.26	2.76

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 Sustainable Managed Growth Trust (C Acc). Source: Royal London Asset Management; Gross performance; Since inception date of the shareclass is 4 December 2012.

Performance commentary

All issuers within our sustainable holdings offer a net benefit to society or show ESG leadership. As well as reducing risk, we seek out opportunities that are under-researched e.g., bonds that do not fall into mainstream indices or benchmarks and/or are unrated by ratings agencies. Importantly, the sustainable credit proposition provides access to critical sectors that most investors can't access via equity markets. Key themes in the funds include social housing, social & environmental infrastructure, community funding (regulated banks and building societies focused on SME and retail lending), financial inclusion & resilience (such as insurance products to support individuals through shocks) and the energy transition.

The fund produced a positive absolute return for the quarter, with the impact of rising gilt yields mitigated by a narrowing in credit spreads and the income on the portfolios.

In terms of performance effects, the outperformance of short-dated bonds relative to long-term equivalents was a headwind for performance. However, this was offset by our sector allocation – in particular our overweight in banks and significant underweight in supranationals. Within banks, our subordinated bonds (lower in the capital structure than senior bonds) were the main contributor, whilst our real estate allocation also proved to be beneficial. Early repayment and calls continue to be supportive, with the redemption of 2024 bonds from Go-Ahead at a premium to market pricing.

Exposure to floating rate notes (FRNs), where interest payments are linked to cash rates, has increased in recent quarters. This helps dampen interest rate risk and has boosted income receipts. Our holding in student loan provider ICSL is an example of this, where income payments are linked to Sterling Overnight Interbank Average (SONIA) rate; income on these securities has risen significantly over the time, reflecting higher SONIA rates.

The equity exposure within the fund saw negative returns over the quarter. Sector effects were the main headwind to performance. Not having exposure to the fossil fuel-based energy sector hurt performance as it was the best performing sector during the period. Higher quality and longer duration assets were also hurt by the rise in government bond yields.

Performance and activity

Top 10 holdings

	Weighting (%)
Aviva Plc 6.875% 20-may-2058	1.64
Hsbc Holdings Plc 8.201% 16-nov-2034	1.28
Legal & General Group Plc 5.5% 27-jun-2064	1.26
Investec Plc 1.875% 16-jul-2028	1.13
Prudential Plc 6.34% 19-dec-2063	0.96
RELX PLC	0.93
Lloyds Bank Plc 7.625% 22-apr-2025	0.91
Hsbc Bank Capital Funding (sterling 1) Lp 5.844% Perp	0.86
Standard Chartered PLC	0.86
Rentokil Initial plc	0.85
Total	10.68

Fund activity

Primary activity was relatively low over the quarter. As well as the seasonal lull usually seen over the summer, higher yields has discouraged issuance. In recent years companies have brought capital raising forward to take advantage of low yields, and we would therefore expect issuance to remain somewhat lower in the next few quarters.

Financials remain the largest part of the market and dominated market issuance and our new issue activity during the quarter. We had a bias towards senior new issues over the period, reflecting the fact that we felt spreads in these areas were very attractive. Early in the period we added a new issue from Principality Building Society, these five-year senior bonds coming to market at a healthy credit spread, meaning a total yield in excess of 8%, also adding further to this bond later in the quarter in the secondary market as the spread remained very attractive. We also added a new senior issue from One Savings Bank, which priced with an attractive yield of 9.5%. Furthermore, we added new issues of senior bonds from Nationwide and Virgin Money.

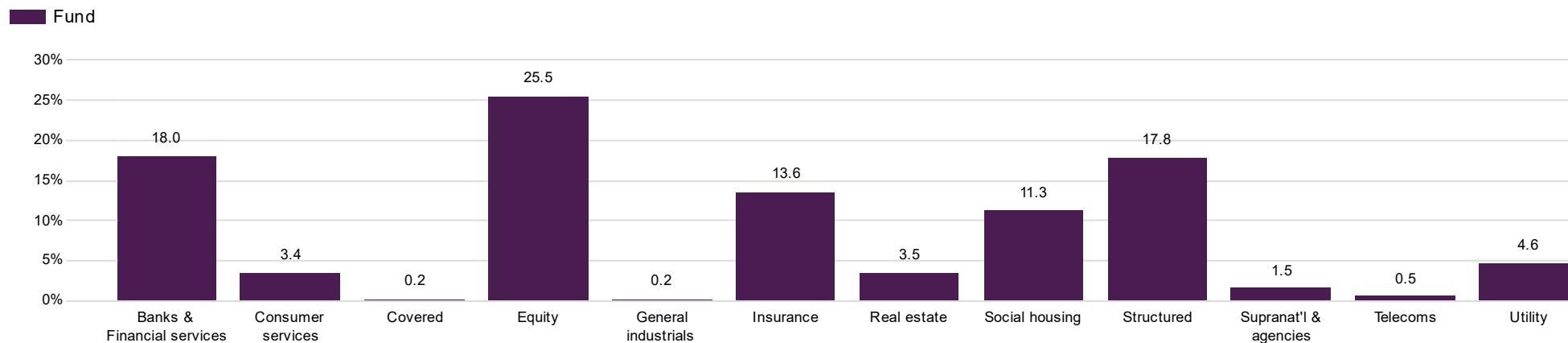
In the secured sector, we participated in a new issue from Last Mile Logistics – a commercial mortgage-backed security floating rate note backed by a portfolio of logistics assets across the UK with an attractive loan to value ratio and AAA rating.

In the structured area, primary issuance has been very limited, but we continue to see secondary market availability. During the quarter we added PFI bonds from Derby Health, and bonds from Meadowhall Finance, secured on the Sheffield shopping centre with good loan-to-value paying a very attractive credit spread.

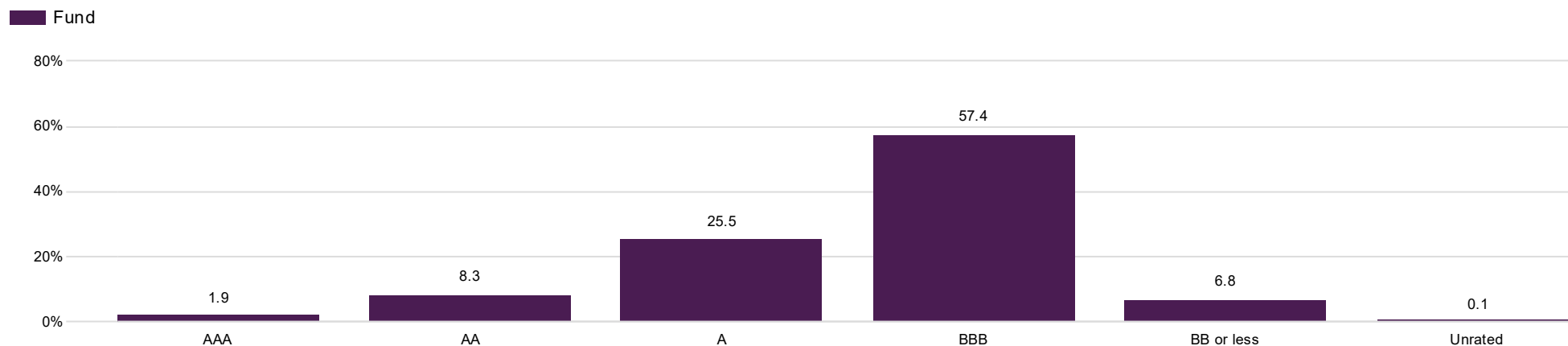
In the fund's equity exposure, we invested in HDFC Bank where we felt that a recent pull-back in the shares presented a compelling opportunity to get exposure to India's leading retail bank and to benefit from the structural growth trends of the Indian economy.

Fund breakdown

Sector weights



Credit ratings



Market commentary

Market overview

Markets made losses over the period under review on fears that interest rates will remain higher for longer than expected, which saw equities drop to their lowest levels since early June. The quarter also saw a market rotation with the best performing sector being the fossil fuel-based energy sector, which had underperformed in prior quarters, and the information technology sector giving back some gains, having been the best performing sector year-to-date. For the third quarter, the MSCI World and MSCI All Countries World Index (ACWI – which also includes 26 emerging markets) produced negative returns for the quarter in US dollar terms. Looking at national MSCI indices, the strongest market was Japan, while the weakest was Eastern Europe. In terms of style, the MSCI World Growth Index produced weaker returns versus the MSCI World Value Index.

The price of Brent crude oil soared by 24.7%, to \$92.20 a barrel. Copper futures also declined a further 1.5% in dollar terms on the back of warning signs emerging of a weakening in global demand as China's economic rebound stalls.

The US dollar appreciated by 3.1% against the yen, by 3% against the euro, and by 4% against sterling. On a translational basis, sterling's strength against the dollar impacts sterling investors in overseas assets as it lowers the returns over the quarter. However, the weaker dollar will benefit emerging markets countries and companies that have borrowed in dollars.

The third quarter was characterised by mixed data around the world, with central banks nearing the end of their rate hiking path, but with cuts still seemingly a while away. Economies have been more resilient than was expected 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 revival in headline inflation, other factors – including a weak economic 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.

Global government bond markets continued to see yields move higher (as prices decline) – 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. 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.

The sterling investment grade credit market (Non-Gilt) returned 2.26% over the quarter, as the negative impact of higher government bond yields was offset by tighter credit spreads and the greater proportion of short-dated bonds (which performed well relatively to longer-dated equivalents) in credit indices. 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 1.48% to 1.38% (iBoxx). Banks and insurance bonds performed strongly in the quarter while senior insurance debt also enjoyed an impressive quarter. No sector saw negative returns, but real estate was broadly flat, and healthcare and transportation lagged other sectors.

Outlook

As fund managers, we create our own investment identity which we imprint on markets. This identity can be a function of objective evidence as to what delivers performance in the long run, beliefs such as the importance of sustainability and the strengths and weaknesses of the people who are enacting it. Done thoughtfully and applied consistently, we believe this is the path to long-term investment success. Alongside this we are market observers. Each day there is messaging from within and across asset classes as to what is occurring in the global economy. Sometimes this is right, and sometimes this is wrong, but it is always worth paying attention to. What are the trends in the global economy markets are pointing to today?

The clearest messages we can see are that we are entering into something of a boom time for both the physical and digital worlds. In the last decade, the physical world has been somewhat left behind by the digitisation of large parts of the economy. This has created many of the technology giants we know so well. Investment in physical infrastructure has lagged, but this is changing.

The key trends in physical infrastructure include electrification, a consequence of a desire to decarbonise, and onshoring, which is a consequence of rising geopolitical tensions and a desire to have industrial and manufacturing capacity at home rather than abroad. We have seen this most prominently in the United States, where the Inflation Reduction Act (climate investment essentially) and CHIPS Act (semiconductor manufacturing) have created material incentives to invest in the physical world and those companies which help build it.

Market commentary

The strength in equity markets this year has been a positive surprise and has been a result of the view that we have reached and (potentially) passed peak inflation and interest rates while not seeing a meaningful slowdown in economic growth. In recent weeks however markets have increasingly priced in a higher-for-longer interest rate scenario as a result of more embedded and structural inflation than was previously expected. This has resulted in a weakness in both bond and equity markets while benefitting commodities. We believe the next six months will be crucial in determining the future path of inflation and whether developed economies such as the US and UK are able to avoid a recession.

Despite more challenging performance in September, we believe that 2023 is on track to be a good year for the Royal London Sustainable funds with our funds ahead of benchmarks and key peers. The macro environment remains complex and confusing, but we continue to have high conviction in the underlying drivers of the companies in which we are invested and in many cases find valuations to be undemanding. We consider our portfolios to be more diversified and lower risk than 18 months ago and would expect them to be relatively more resilient if we do enter a period of slowing economic growth or recession.

There is considerable uncertainty about the economic outlook for the remainder of 2023. In the US, the Federal Reserve has continued to raise interest rates in response to high inflation and many investors fear that this could tip the US into recession, although economic indicators remain broadly positive at this stage. The picture is potentially more problematic in the UK where inflation is higher and growth weaker. Europe is somewhere in the middle of these two outcomes. How inflation progresses from here, and how central banks respond, will be a key determinant of near-term returns.

In the long term, we believe that the trend towards sustainability remains a strong one, with all companies we meet with pointing to an acceleration both in recent years and since the start of the Ukraine war. Whilst this may seem counterintuitive given the strong performance of oil, energy security – as well as increased concerns about climate change – are resulting in an acceleration in the demand for renewable energy. Although innovation may be becoming more incremental in the consumer arena, recent developments in AI are driving significant advances in technology. Within healthcare innovation is accelerating as a greater understanding of the immune system as well as genetics, is resulting in a step change in cancer treatments, amongst other areas. The physical economy is also seeing a renaissance after many years of being overshadowed by the digital world. Electrification is a core part of path to a lower carbon economy and will require a significant investment in infrastructure over many years. These trends make us optimistic about the long-term outlook for sustainable investing.

Further Information

Please click on the links below for 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

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 October 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 Trust is an authorised unit trust scheme. The Manager is RLUM Limited, authorised and regulated by the Financial Conduct Authority, with firm reference number 144032.

For more information on the Trust 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.

The portfolio has no index as a comparison.

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.

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.

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 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.

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.

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.

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 30 September 2023

Cumulative (%)

	3 Month	6 Month	1 Year	3 Years	5 Years		
Fund (gross)	1.51	0.58	10.55	(4.99)	12.99	3 Years (p.a.)	5 Years (p.a.)
Fund (net)	1.34	0.25	9.84	(6.82)	9.39	(1.69)	2.47
						(2.33)	1.81

Annualised (%)

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
Fund (gross)	10.55	(19.71)	7.04	7.81	10.31
Fund (net)	9.84	(20.23)	6.35	7.12	9.59

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 RL Sustainable Managed Growth Trust (C Acc).

Glossary

Asset allocation

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.

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.

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 value

Total value of the fund as of the last business day of the calendar month. The fund value is as at close of business and 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.

Number of holdings

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

Performance

Performance is calculated using the daily end of day NAV per share produced by HSBC based on the mid price.

Sector breakdown

Breakdown of the fixed income assets, excluding derivatives and cash by RLAM's internal industry sector classification scheme. Figures are subject to rounding.

Top 10 holdings

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