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Royal London Absolute Return Government Bond Fund

Quarterly Investment Report

31 December 2024

Quarterly Report

The fund as at 31 December 2024

The purpose of this report is to provide an update on the Royal London Absolute Return Government 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 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

The fund

Fund performance objective and benchmark

The investment objective of the fund is to target absolute positive capital growth and the fund will seek to achieve its objective on an active basis. The Fund seeks to achieve its investment objective by outperforming its benchmark, the Sterling Overnight Index (the "Benchmark") on an annual basis by 2.5% over rolling three year periods and aims to provide positive performance over 12 month periods. The Benchmark is an index which tracks overnight funding rates in the Sterling market. The Benchmark is being used by the Fund for performance comparison purposes only and the Fund does not intend to track the Benchmark.

Benchmark: SONIA (Sterling Overnight Index Average)

Fund value

	Total £m
31 December 2024	1,238.05

Asset allocation

	Fund (%)
Conventional credit bonds	48.79
Money Market Instruments	35.37
Conventional gilts	5.70
Index linked foreign sovereigns	5.57
Conventional foreign sovereigns	2.58
Index linked gilts	1.58
Index linked credit bonds	0.41

Fund analytics

	Fund
Fund launch date	17 November 2014
Base currency	GBP

Performance and activity

Performance

	Fund (%)	Benchmark (%)	Relative (%)
Quarter	1.71	1.19	0.52
1 Year	6.63	5.07	1.56
3 Years (p.a.)	5.28	3.67	1.61
5 Years (p.a.)	3.69	2.24	1.46
10 Years (p.a.)	2.37	1.35	1.02
Since inception (p.a.)	2.33	1.34	1.00

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 Z Acc GBP. Source: Royal London Asset Management; Gross performance; Since inception date of the share class is 17 November 2014.

Performance commentary

The fund posted a strong return over the quarter, outperforming its cash benchmark, and remains significantly ahead of benchmark over one and three years. Year to date the fund has achieved higher returns than all government bond indices, reflecting the higher yield on the fund and shorter duration

The largest contributor to performance was again from the core holdings of sterling money market instruments. These assets yielded above 4.75% and benefited from expectations that UK rates would be cut over the next 12 months.

Duration positions added value, particularly through tactically trading the volatility seen in markets as economic data continued to be mixed. Long positions in the US and Australia were the main positives for the portfolio. A short duration position in Germany also added value.

Curve positions were mixed steepening positions in the US and Europe added value whilst the curve flattener in Japan detracted as the curve continued to steepen.

Inflation positions added value particularly a short position in the UK relative to the US and Europe and the long held position in Japanese breakevens.

Cross market positions were mixed with the long UK vs Europe particularly detracting from performance after the poorly received UK budget.

Performance and activity

Return Contribution

	Quarter	1 year	Target return (of live trades)
Inflation	29.33	88.32	306.98
Curve	(2.53)	40.51	6.84
Duration	20.47	81.21	212.93
Relative Value	2.77	2.49	9.92
Cross Market	(0.62)	(7.41)	187.06
FX Hedges	0.00	0.00	0.00
Cash	104.99	421.68	865.50
Total	**154.42**	**626.81**	**1,589.23**

Top Contributors

	Strategy	Q4 Contribution (bps)
Cash	Cash	104.00
Inflation	Japan	19.00
Duration	UK	9.00
Duration	US	9.00
Inflation	US	7.00

Bottom Contributors

	Strategy	Q4 Contribution (bps)
Cross Market	UK/EUR	(11.00)
Inflation	UK	(5.00)
Curve	UK	(5.00)
Curve Japan	US	(4.00)

Performance and activity

Portfolio Exposure

Trades	Position size	Net duration exposure	Market beta	Target return (bps)
Inflation				
Long Japanese Breakeven	0.10	0.00	(0.03)	2.00
Long US 30y Break even	0.20	0.00	(0.06)	1.00
Curve				
Japan 10-30 Flattener	0.40	0.00	0.00	20.00
Cross Market				
Long Germany France	0.10	0.00	0.00	2.00
Long UK vs Europe (7y swap)	0.10	0.00	0.05	10.00
Relative Value				
Long 30 year Gilt Asset Swap	0.60	0.00	0.00	10.00
Short 30 year Iota	0.20	0.00	0.00	5.00
Duration				
Long UK 10 and 30y	0.15	0.15	0.20	10.00
Long UK 1y1y	0.20	0.20	0.14	3.00
Long 10y Italy	0.05	0.05	0.00	2.00
Long 5y BTP Italia	0.05	0.05	0.00	2.00
Long 10y Germany	0.10	0.10	0.03	2.00
Long 10y Norway	0.10	0.10	0.03	5.00
Long UK 30y Ry	0.20	0.20	0.10	5.00

Performance and activity

Portfolio Exposure

Trades	Position size	Net duration exposure	Market beta	Target return (bps)
Duration				
Long US 30y Ry	0.10	0.10	0.05	5.00
Cash				
Cash	0.20	0.15	-	450.00
Overall Net Duration Position	**2.85**	**1.10**	**0.51**	**534.00**

Performance and activity

Asset allocation – duration

	0 -2 yrs	2 -7 yrs	7 - 12 yrs	12 - 17 yrs	17 -22 yrs	22 -27 yrs	>27 yrs	Total
Australia	0.02	0.00	0.00	0.00	0.00	0.00	0.00	0.02
Canada	0.04	0.00	0.00	0.00	0.00	0.00	0.00	0.04
European Union	0.03	(0.08)	(0.12)	0.00	0.00	0.00	0.00	(0.16)
Finland	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
France	0.01	(0.01)	(0.09)	0.00	0.00	0.00	0.00	(0.09)
Germany	0.01	0.01	0.19	0.00	0.00	0.00	0.00	0.21
Italy	0.00	0.06	0.09	0.00	0.00	0.00	0.00	0.14
Japan	(0.01)	0.06	(0.41)	0.02	0.02	0.07	0.24	0.00
Netherlands	0.01	0.00	0.00	0.00	0.00	0.00	0.00	0.01
Norway	0.02	0.00	0.06	0.00	0.00	0.00	0.00	0.08
Singapore	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Spain	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Supranational	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Sweden	0.03	0.00	0.00	0.00	0.00	0.00	0.00	0.03
Switzerland	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
United Kingdom	(0.15)	0.48	0.16	0.00	0.01	0.01	0.28	0.79
United States	(0.00)	0.00	(0.01)	0.00	0.00	(0.01)	0.11	0.08
Total								1.15

Performance and activity

Asset allocation - inflation

	0 -2 yrs	2 -7 yrs	7 - 12 yrs	12 - 17 yrs	17 -22 yrs	22 -27 yrs	>27 yrs	Total
Australia	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Canada	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
European Union	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Finland	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
France	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Germany	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Italy	0.00	0.05	0.00	0.00	0.00	0.00	0.00	0.05
Japan	0.00	0.07	0.00	0.00	0.00	0.00	0.00	0.07
Netherlands	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Norway	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Singapore	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Spain	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Supranational	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Sweden	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Switzerland	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
United Kingdom	0.00	0.00	0.00	(0.00)	0.00	0.10	0.00	0.10
United States	0.00	0.00	0.00	0.00	0.00	0.20	0.00	0.30
Total								0.52

Performance and activity

Stand alone risk contribution

	Quarterly Vol (%)	Annual Vol (%)
Inflation	(0.00)	(0.01)
Curve	0.01	0.02
Duration	0.39	0.78
Relative Value	0.03	0.06
Cross Market	0.05	0.09
FX Hedges	0.02	0.04
IOTA	(0.00)	(0.00)
Cash	0.12	0.23
Overall Volatility	**0.61**	**1.22**

Risk Model Factor Risk Breakdown

	Standalone Risk Portfolio (bp)	Risk Contribution Portfolio (bp)	% of overall risk
Rates	114.61	111.75	91.87
Inflation	21.58	(0.76)	(0.62)
Spreads	21.12	10.96	9.01
Foreign Exchange	2.12	(0.31)	(0.26)
Time	0.00	-	-
Other	0.00	-	-
Total	**159.44**	**121.63**	**100.00**

Diversification across Risk Factors (%)	**(24)**

Performance and activity

Fund activity

The fund began the quarter around 0.5 years long, and gradually increased duration over the first half of the period – predominantly buying Australian, UK and Spanish bonds – to leave the fund 1.5 years long in November. With yields falling after the US election, we reduced duration, notably through selling the overweight position in Australia, reducing exposure to the UK and selling French bonds. Towards the end of the quarter, as yields in the US and UK rose on supply fears, we increased the duration position again to end the year 1.1 years long.

During the first part of the quarter we reduced inflation exposure as breakevens rose prior to the US election, selling US and UK breakevens. Towards the end of the year we increased inflation exposure, predominantly buying UK and US long-dated real yields at levels not seen since the Truss debacle.

During the quarter we tactically traded the France/Germany spread and also added to the long UK / Europe trade. After strong performance we also closed the Canada/US position.

Curve positions in the US and Europe were traded actively. With curves steepening early in the quarter, we closed both the US and European steepeners but added to the flattening position in Japan.

We added to our long gilts relative to swaps and short 30-year cash breakevens vs inflation swaps.

We used supply events across the globe to add duration when new issue premia were again attractive, taking part in syndications in the UK and Spain.

Market commentary

Market overview

Markets were volatile during the fourth quarter – with the US elections and the potential for central bank rate cuts the main causes of uncertainty. With the election of Donald Trump as US President, and the Republicans having a majority in both the Senate and House of Representatives, markets moved to price in potentially higher US deficits.

Alongside political events, attention remained on the Federal Reserve, European Central Bank and Bank of England to see if expected rate cuts would materialise. However, with inflation remaining higher than central bankers would like, expectations for rate cuts in 2025 were revised down. This backdrop pushed government bond yields higher, leading to negative absolute returns for most investment grade credit markets despite credit spreads tightening and credit excess returns over government bonds being positive, while equities ended a strong 2024 with another positive quarter, with US stocks – notably the 'magnificent seven' – leading the way.

At its final meeting of 2024, and as expected, the Bank of England kept rates on hold at 4.75%. Meanwhile, according to the minutes, "a gradual approach to removing monetary policy restraint remains appropriate." The new Labour government presented its first budget. This was less obviously a budget for growth than one for public services repair with a substantial proposed increase in day-to-day fiscal spending and net investment. Public spending was increased substantially, but at the cost of a big increase in taxes. Since the Budget, business optimism has dropped, and firms are indicating a mix of responses to the rise in National Insurance contributions including hiring less and raising prices.

The Federal Reserve cut rates 50bps over the quarter to a 4.25% - 4.5% target range. They signalled fewer cuts for 2025 than previously indicated, indicating only 50bps cuts for 2025 (100bps previously). Donald Trump was elected US President for the second time. A Trump presidency will likely bring a change in both policy making style and substance. It was a clean sweep for the Republicans, winning the White House, Senate and House of Representatives, increasing the prospects of Trump getting his fiscal policies through. Business optimism on the PMI survey rose, hitting a two and a half year high in December, "reflecting growing optimism about business conditions under the incoming Trump administration," though manufacturers flagged concerns about tariffs (where Trump has promised increases) and inflation.

As widely expected, the European Central Bank's final decision of the year saw another 25bps rate cut, taking the deposit rate to 3.00%. The bank continues to note that domestic inflation remains high, "mostly" attributable to wages and prices in certain sectors, and acknowledge that they are "still adjusting to the past inflation surge with a substantial delay." The picture for activity outside Germany and France was somewhat better than for those two economies, with both France and Germany affected in recent months by political/policy uncertainty. France's finance minister was replaced after Barnier's budget failed to pass and Germany will now have early elections in the first quarter of 2025. CPI inflation rose on data released over the quarter, reaching 2.3% in November.

Government bond yields rose over the quarter, as central banks continued to struggle to bring inflation back to target levels and amid ongoing political volatility with elections across Europe and the US. In the US, 10-year treasury yields rose to 4.57% from 3.78%, while German 10-year bunds similarly saw yields rise to 2.36% from 2.06%. Benchmark 10-year gilt yields increased to 4.57% from 4.01%.

Index linked markets saw similar moves, with this a poor quarter for index link bonds as real yields globally ended the year at their highest levels for the year. Despite rate cuts during the quarter the prospect of substantial cuts across the globe in 2025 were priced out of valuations after the election of Trump, the poorly received UK budget and sticky inflation data.

Outlook

We expect markets to remain volatile around economic data and supply points. Towards the end of the year future rate cut expectations were pared back and fears of a surge in supply in January saw yields rise to their highest level in over a year.

Valuations in certain markets look very attractive and we will use supply events in January to add duration.

We do expect further rate cuts across the globe and more than is priced by markets now supporting a long duration stance. However markets will remain choppy particularly around inflation data which still looks to be unacceptably high.

Inflation is now more fairly valued in Japan and any further tightening of monetary policy could impact break evens. We will use strength to reduce this position further. Breakeven rates in the UK look stretched and we will look to sell breakeven rates particularly with a 30-year auction in January.

The Bank of Japan is expected to raise short-term rates further. We expect the Japanese curve to flatten – this is currently the steepest amongst G10 nations

The UK market has sold of relatively on fears of a large increase in supply following the budget in late October. We believe this to be overdone and have begun to increase the overweight in the UK.

Further Information

Please click on the links below for further information:

Stewardship and responsible investment at RLAM

TCFD climate report

Find out more

In an uncertain geopolitical and economic environment, we recognise the importance of keeping our clients updated on our current investment thinking.

Articles, videos, podcasts and webinars giving the latest views of our investment experts 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.

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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: Airport Center Building, 5 Heienhaff, L-1736 Senningerberg, Luxembourg and is authorised and regulated by the Commission de Surveillance du Secteur Financier (CSSF).

The Investment Manager is Royal London Asset Management Limited.

The Prospectus and Key Investor Information Document (KIID) are available in English via the relevant Fund Information page on www.rlam.com. A summary of investor rights is also available in English, and can be accessed at www.rlam.com/uk/policies-and-regulatory

RLAM may terminate the arrangements made for marketing of the fund pursuant to Article 93a of Directive 2009/65/EC.

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.

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 risk

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.

Performance to 31 December 2024

Cumulative (%)

	3 Month	6 Month	1 Year	3 Years	5 Years
Fund (gross)	1.71	3.22	6.63	16.72	19.91
Fund (net)	1.64	3.07	6.31	15.60	17.79

Annualised (%)

3 Years (p.a.)	5 Years (p.a.)
5.28	3.69
4.95	3.33

Year on year performance (%)

	31/12/2023 - 31/12/2024	31/12/2022 - 31/12/2023	31/12/2021 - 31/12/2022	31/12/2020 - 31/12/2021	31/12/2019 - 31/12/2020
Fund (gross)	6.63	6.40	2.88	0.90	1.82
Fund (net)	6.31	6.08	2.51	0.48	1.41

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 2024. All figures are mid-price to mid-price for the Royal London Absolute Return Government Bond Fund Z Acc GBP share class.

Glossary

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.

Performance

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

VaR

VaR is a statistical measure of the level of financial risk within the fund over a specific time.