Royal London Asset Management

Equity Funds

Fund Manager Commentary

January 2024

FOR PROFESSIONAL CLIENTS ONLY, NOT SUITABLE FOR RETAIL CLIENTS.

Contents

Royal London Asset Management Equity Performance

	1 month (%)	Rolling 12 Months (%)
RL UK Equity Income M Inc	**-0.79**	**5.40**
IA UK Equity Income Sector	-1.29	2.16
FTSE All Share Index	-1.32	1.90
RL UK Dividend Growth Fund M Acc	**-0.57**	**5.31**
IA UK All Companies Sector	-0.90	2.13
FTSE All Share Index	-1.32	1.90
RL UK Mid Cap Growth Fund M Acc	**-1.57**	**2.19**
IA UK All Companies Sector	-0.90	2.13
FTSE 250 ex-IT Index	-1.48	1.69
RL UK Opportunities Fund M Acc	**-1.68**	**1.44**
IA UK All Companies Sector	-0.90	2.13
FTSE All Share Index	-1.32	1.90
RL UK Smaller Companies Fund M Acc	**0.39**	**2.36**
IA UK Smaller Companies Sector	-0.38	-2.34
FTSE Small Cap ex-IT Index	-2.20	2.61

Past performance is not a guide to future performance. The value of investments and the income from them is not guaranteed and may go down as well as up and investors may not get back the amount originally invested.

Source: RLAM and FE, as at 31 January 2024. Returns quoted are net of fees.

Royal London UK Equity Income Fund

Portfolio Commentary

- During January the fund returned -0.79%, which was better than its benchmark and ahead of the peer group median, ranking 28th percentile.
- Data continues to suggest that inflation is past its peak and that interest rates could be eased at some point this year. However investor expectations continue to be somewhat at odds with policy makers, expecting cuts to be both deeper and sooner than the monetary authorities are guiding to. The month saw a lot of consumer related trading statements. Comments from Marks & Spencer, Sainsbury, Tesco and Cranswick suggested that spending on food was robust over Christmas, but other retail areas were more mixed. JD Sports, Watches of Switzerland and Burberry (none of which is held in the fund) all released notably weak updates and saw their share prices hit.
- The main contributors to the fund's outperformance were the holdings in **Hikma** and **Clarkson**. There was no specific news on Hikma, but Clarkson shares were strong after releasing a strong trading statement. **Close Brothers** shares were a drag performance after regulators announced a review of financing in the motor financing market. This review is likely to drag on, but our view is that the hit to Close Brothers shares represents something of an overreaction.
- During the month the main trades were to trim the holdings **Sage**, **Hikma** and **RELX**.

Investment Outlook

- We continue to feel that our approach of investing in a broad range of companies from different sectors and stages of their lifecycle is very appropriate and will allow performance to continue to be driven more by the success of our hunting for undervalued long term cashflows than by the prevailing winds of the macroeconomy, or factors such as growth or value styles being in vogue.

Richard Marwood

Head of Income Equities

Royal London UK Dividend Growth Fund

Portfolio Commentary

- During January the fund returned -0.57%, which was better than its benchmark and ahead of the peer group median, ranking 32nd percentile.
- Data continues to suggest that inflation is past its peak and that interest rates could be eased at some point this year. However investor expectations continue to be somewhat at odds with policy makers, expecting cuts to be both deeper and sooner than the monetary authorities are guiding to. The month saw a lot of consumer related trading statements. Comments from Marks & Spencer, Sainsbury, Tesco and Cranswick suggested that spending on food was robust over Christmas, but other retail areas were more mixed. JD Sports, Watches of Switzerland and Burberry (none of which is held in the fund) all released notably weak updates and saw their share prices hit.
- The main contributors to the fund's outperformance were the holdings in **Clarkson** and **Cranswick**, both of whom released strong trading statements. **Close Brothers** shares were a drag performance after regulators announced a review of financing in the motor financing market. This review is likely to drag on, but our view is that the hit to Close Brothers shares represents something of an overreaction.
- During the month the fund trimmed the holding **Clarkson**, into the strength in the share price and also exited the small position in the building products company **Marshalls**. Clarkson remains the largest position relative to the stock's index weighting within the fund.

Investment Outlook

- We continue to feel that our approach of investing in a broad range of companies from different sectors and stages of their lifecycle is very appropriate and will allow performance to continue to be driven more by the success of our hunting for undervalued long term cashflows than by the prevailing winds of the macroeconomy, or factors such as growth or value styles being in vogue.

CITYWIRE +

Richard Marwood

Head of Income Equities

CITYWIRE +

Niko de Walden

Fund Manager

Royal London UK Mid Cap Growth Fund

Portfolio Commentary

- The UK Mid Cap Growth fund returned -1.57% during the month, broadly performing in line with the benchmark (FTSE 250 ex IT) return of -1.48%.
- Following a strong performance of the UK equity market in November and December last year, January by contrast was somewhat more subdued. Expectations for interest rate cuts by central banks were paired back during the month, following higher-than-expected inflation data in the UK & US, and comments made by the chair of the US Federal Reserve. At a high level, market expectations aren't much changed – multiple rate cuts are still expected through 2024 – but a little later than anticipated a month ago. The usual flurry of January trading updates by companies revealed winners and losers from the Christmas period – the larger grocers, food producers and consumer staples companies generally did better, while fashion retailers, online retailers and luxury goods companies had a tougher time of it including a number of profit warnings. However this appears to be more of a change in consumer spending rather than wholesale reduction, as pubs, restaurants and travel operators all reported sustained demand.
- **Cranswick, Bodycote** and **Intermediate Capital Group** were contributors to performance during the month. Cranswick issued a robust trading statement, their third upgrade to profits guidance of the financial year, driven by both better sales volumes as well as operating margin improvements. Bodycote announced the acquisition of a US heat treatment business, and kicked off a £60m share buyback programme. Intermediate Capital Group issued its Q3 results which revealed better-than-expected fundraising activity, led by two of its flagship strategies, Senior Debt Partners & Strategic Equity.
- **Watches of Switzerland Group** and **WH Smith** were detractors to performance. Watches of Switzerland downgraded profits guidance for the full year, blaming a deterioration in Christmas trading and particularly within lower to mid-tier luxury watches and jewellery. The UK performance was weaker than that in the US, where they still posted reasonable sales growth, which was somewhat reassuring of the ongoing supply and demand dynamics in their key growth market. While margins compressed, the business remains highly profitable and cash generative, with a significant net cash balance sheet to fund growth or shareholder returns. WH Smith released a mildly disappointing trading update where their InMotion stores in the US – which mostly sell personally technology products such as Apple headphones – showed sales declines. Nevertheless their larger US retail operation, MRG, performed better and results from the UK and Rest of World were robust. They continue to win significant new contracts to operate travel concessions and that will drive sales and profit growth over the medium term.
- Trading activity was quiet during the month. The fund added to a range of holdings including **Genus**, **Grafton** and **Integrafin**.

ALPHA MANAGER 2022
Henry Lowson

Henry Lowson

Head of UK Alpha Equities

Royal London UK Opportunities Fund

Portfolio Commentary

- The RLAM UK Opportunities fund produced a return of -1.68% during the month, underperforming the benchmark (FTSE All Share) return of -1.32%.
- Following a strong performance of the UK equity market in November and December last year, January by contrast was somewhat more subdued. Expectations for interest rate cuts by central banks were paired back during the month, following higher-than-expected inflation data in the UK & US, and comments made by the chair of the US Federal Reserve. At a high level, market expectations aren't much changed – multiple rate cuts are still expected through 2024 – but a little later than anticipated a month ago. The usual flurry of January trading updates by companies revealed winners and losers from the Christmas period – the larger grocers, food producers and consumer staples companies generally did better, while fashion retailers, online retailers and luxury goods companies had a tougher time of it including a number of profit warnings. However this appears to be more of a change in consumer spending rather than wholesale reduction, as pubs, restaurants and travel operators all reported sustained demand.
- **Intermediate Capital Group** and **Grafton** were contributors to performance during the month. Intermediate Capital Group issued its Q3 results which revealed better-than-expected fundraising activity, led by two of its flagship strategies, Senior Debt Partners & Strategic Equity. Grafton's full year update revealed that operating profits for its full year are expected to be slightly ahead of consensus expectations. This is primarily driven by its cost reduction measures and a positive performance from its Irish division.
- **Watches of Switzerland** and **Lloyds Banking Group** were detractors during the month. Watches of Switzerland downgraded profits guidance for the full year, blaming a deterioration in Christmas trading and particularly within lower to mid-tier luxury watches and jewellery. The UK performance was weaker than that in the US, where they still posted reasonable sales growth, which was somewhat reassuring of the ongoing supply and demand dynamics in their key growth market. While margins compressed, the business remains highly profitable and cash generative, with a significant net cash balance sheet to fund growth or shareholder returns. Lloyds' shares fell as investors grew cautious about the implications of the newly announced FCA review on the historical use of commissions in motor finance arrangements.
- In terms of trading activity, the fund trimmed its exposure to **Lloyds Banking Group** (prior to the FCA announcement) and started a new position in **HSBC**. From a portfolio construction perspective, this maintains the fund's exposure to the banking sector whilst providing additional diversification. From a stock specific perspective, we believe HSBC should benefit from the restructuring of its non-core divisions and it should generate good growth from its wealth management and insurance arms. HSBC also trades on a compelling valuation at below 1x price-to-tangible book value, and a mid-single digit price earnings ratio.

Royal London UK Smaller Companies Fund

Portfolio Commentary

- The UK Smaller Companies fund returned 0.39% during the month, placing 25th percentile compared to the UK Smaller Companies peer group and significantly outperforming the benchmark (FTSE Small Cap ex IT) by 2.59%.
- Following a strong performance of the UK equity market in November and December last year, January by contrast was somewhat more subdued. Expectations for interest rate cuts by central banks were paired back during the month, following higher-than-expected inflation data in the UK & US, and comments made by the chair of the US Federal Reserve. At a high level, market expectations aren't much changed – multiple rate cuts are still expected through 2024 – but a little later than anticipated a month ago. The usual flurry of January trading updates by companies revealed winners and losers from the Christmas period – the larger grocers, food producers and consumer staples companies generally did better, while fashion retailers, online retailers and luxury goods companies had a tougher time of it including a number of profit warnings. However this appears to be more of a change in consumer spending rather than wholesale reduction, as pubs, restaurants and travel operators all reported sustained demand.
- **Boku** and **Craneware** were contributors to performance during the month. Boku issued its full year update which outlined revenue and profit growth ahead of consensus expectations. Whilst both its Local Payment Method and Direct Carrier Billing divisions grew well, the former grew exceptionally strongly and this was despite very little contribution from its significant new partner, Amazon, which will support revenue growth in future years. Craneware's first half trading update showed accelerating new sales growth, and positive profit growth ahead of analyst expectations. Pleasingly the headwinds which Craneware faced in the US healthcare industry during the last few years seem to be abating as US hospitals re-started investment into system upgrades and software procurement. It also may be the case that Craneware's new sales structure and product portfolio reorganisation is demonstrating early results.
- **Inspecs** and **Focusrite** were detractors to performance during the month. Inspecs revealed weaker-than-expected revenues as a result of lower demand and delayed orders in. Whilst the update was disappointing, the medium to long-term opportunity to take market share remains significant – Inspecs should be able to achieve this as it remains one of few players in the industry who are vertically integrated & have a portfolio of strong brands. Focusrite announced a trading update which highlighted challenging trading conditions in its end markets. Whilst the group did however hold its profit guidance for the full year, this will likely be achieved with a second half weighting.
- The fund initiated a position in **Norcros**. The group owns a portfolio of bathroom & kitchen brands, which are typically the market leader in their niche with a track record of innovation. The new management team have taken significant positive steps to restructure the group, closing loss-making subsidiaries and there remain further 'self-help' opportunities. The business generates good margins and returns on capital, which have scope to significantly improve thanks to the new strategy; the shares currently trade on an attractive mid-single digit price earnings multiple. The position was funded by the disposal **Mattioli Woods**.

ALPHA MANAGER 2022
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IMPORTANT INFORMATION