The case for active management in UK index linked gilts

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UK index-linked gilts (linkers) are designed to provide investors with exposure to real interest rates while helping to mitigate the effects of inflation. After a prolonged period of financial repression, real yields in the UK have reset meaningfully higher and now sit at levels that we believe look attractive on a long term historical basis. With the direction of travel for interest rates increasingly downwards, linkers offer the potential for capital gains through falling real yields, supported by a favourable supply backdrop and continued macro and geopolitical uncertainty. In this environment, dispersion across maturities, breakevens and markets is elevated, reinforcing the case for active management.

UK index linked gilts are UK government bonds whose principal and coupon payments rise in line with inflation. Investors therefore earn a real yield (a yield after inflation), rather than a nominal yield. Returns are driven by real yields, the main driver of price sensitivity, as well as inflation accrual via the index uplift, and inflation expectations which are reflected in breakeven inflation versus nominal gilts.

Role of linkers within portfolios

For many investors, linkers serve several distinct purposes. Linkers provide a direct hedge against inflation outcomes that exceed expectations, making them a natural component of portfolios with inflation-sensitive liabilities or real return objectives. By separating nominal rate risk from real rate risk, linkers diversify traditional gilt exposure and can behave differently to nominal bonds during periods of inflation volatility. Linkers retain the convexity and duration benefits of long-dated government bonds, while offering protection against upside inflation risks.

Historically attractive real yields

Following the sharp global tightening cycle of 2022–2024, UK real yields have moved decisively higher. Across the curve, real yields are now positive and sit towards the upper end of their long-term historical ranges. Long-dated UK real yields are close to levels last seen prior to the global financial crisis and in our view, screen attractively relative to their post 2008 history.

From a valuation perspective, this represents a markedly different starting point to much of the past decade, when real yields were persistently negative. In our view, higher starting real yields can seek to improve prospective long-term returns and provide a stronger cushion against adverse scenarios.

Potential for future downward pressure on interest rates

While inflation has tapered from the highs we saw post-Covid, prolonged sticky inflation, coupled with limited demand, can lead to fragile growth dynamics. Policy rates remain largely restrictive by historical standards and central banks will be mindful of this when considering their next policy moves, and we therefore believe the asymmetry for long duration assets is therefore improving. For linkers, prices are sensitive to changes in real yields which can be associated with increases in capital values. Long-dated index linked gilts exhibit significant sensitivity to real yield movements, meaning even modest declines in real yields can generate meaningful price appreciation. In our view, high starting real yields, and the option to benefit from rate cuts, create a compelling combination.

Supportive supply backdrop

The UK debt management office has adjusted its issuance strategy in response to market conditions. Recent and forward looking issuance plans show a reduced emphasis on long dated supply, a trimming of index linked issuance relative to history, and greater flexibility in the maturity profile of new issuance. With structural demand from pension schemes lower than in the past, these supply adjustments matter. Lower net supply of long-dated and index linked gilts reduces the amount of duration risk the market needs to absorb, providing technical support to valuations, particularly at the long end of the real yield curve.

Current environment: Heightened macro and geopolitical uncertainty

The ongoing global macro environment remains unsettled. Geopolitical risks, fiscal uncertainty and divergence in global monetary policy continue to drive volatility in both nominal and real yields. In such environments, inflation expectations and real rates can move independently, creating opportunities but also risks for passive investors. Linkers provide a degree of stability against unexpected inflation outcomes while retaining the defensive characteristics of sovereign bonds during risk-off episodes.

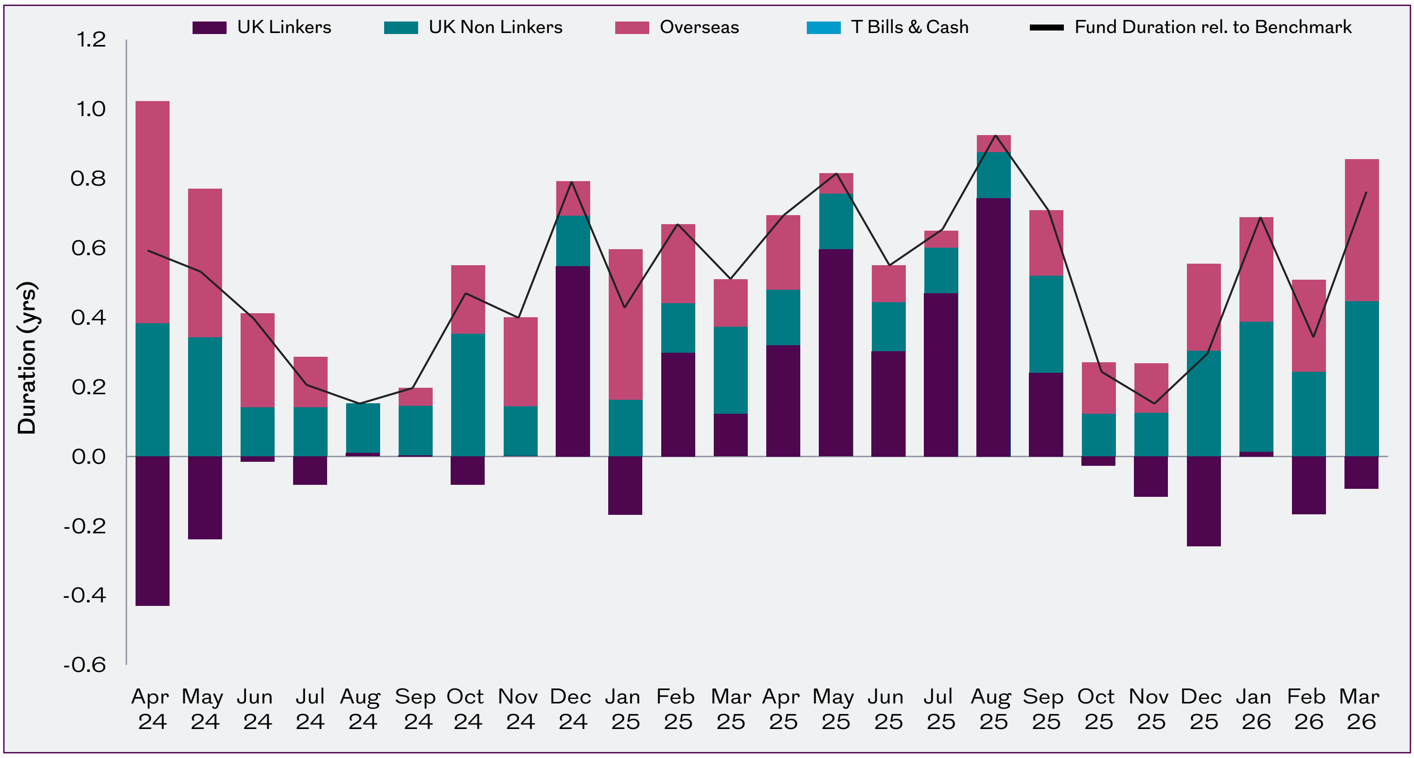
More specifically the recent escalation in tensions around Iran, adds an additional layer of uncertainty to the inflation and growth outlook. While the immediate market focus tends to be on energy prices and near-term inflation risks as higher input costs, tighter financial conditions and weaker confidence begin to bite.

In this scenario, inflation may prove stickier than central banks would like, even as growth momentum fades. We believe that the combination likely points to falling real yields over time, reinforcing the case for duration, while index linked bonds offer valuable protection against upside inflation risks should energy driven pressures persist for longer than expected.

Opportunity for active value

Although index linked gilts are often perceived as a buy and hold asset class, in practice they offer opportunity for active value add, particularly in the current environment. Supply dynamics, pension demand and technical factors can lead to persistent mispricings along the curve. Inflation expectations can become disconnected from underlying fundamentals, particularly during periods of energy price volatility or geopolitical stress. Switching between nominal gilts and linkers can add value when real yields and breakevens move out of line with economic realities. Global differences in inflation dynamics, fiscal policy and central bank reaction functions create opportunities to allocate real rate exposure selectively. Elevated volatility increases the opportunity set (see figure 1) for active managers with the resources and experience to navigate these markets.

Figure 1: RL Index Linked Fund relative positions



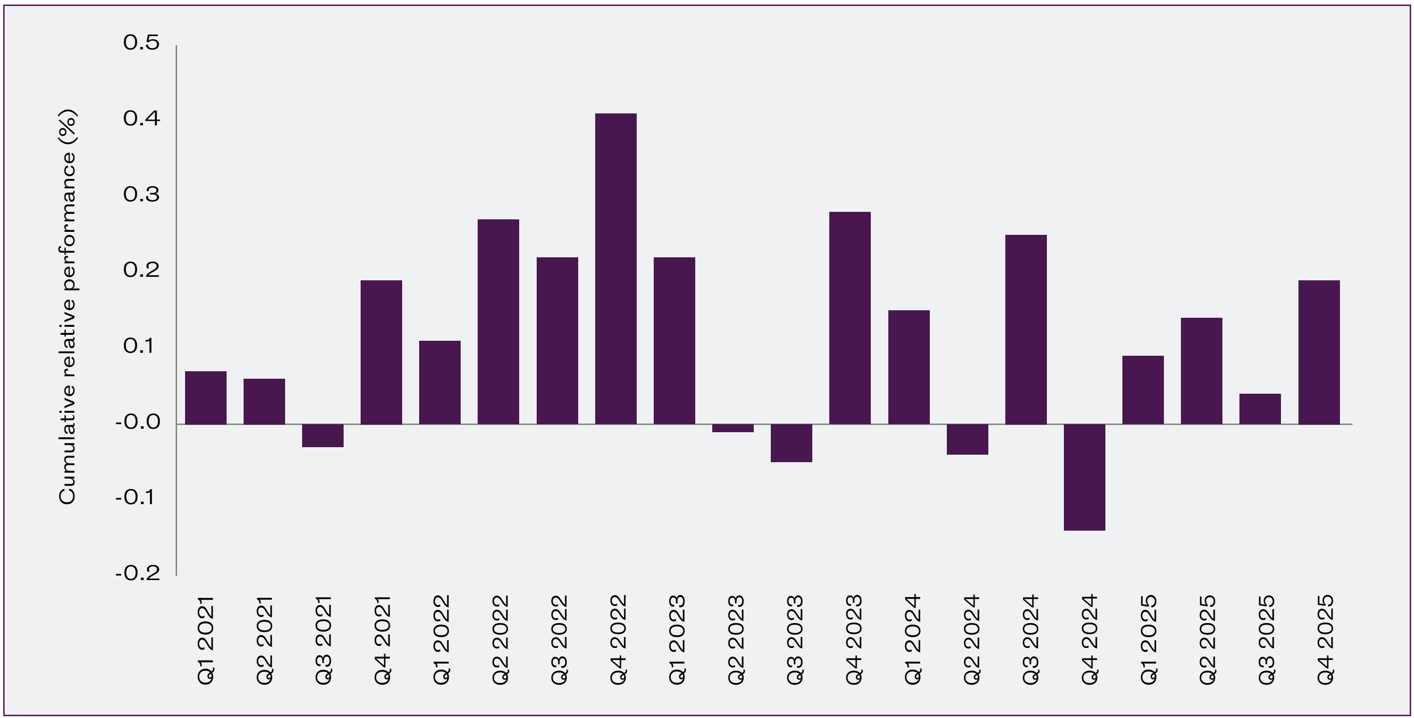
Past performance is not a guarantee or reliable indicator of future returns. Portfolio characteristics and holdings are subject to change without notice. This does not constitute an investment recommendation. For information purposes only.

Source: RLAM as at 31 March 2026.

Our approach

Royal London Asset Management has a long and established track record in global government bond markets, including index linked gilts (figure 2). The RL Index Linked Fund aims to provide a return greater than that of FTSE Actuaries UK Index Linked Gilts (All Stocks) Total Return GBP Index over rolling 5-year periods, through a combination of capital growth and income, after the deduction of charges. Our approach is characterised by deep expertise in rates and inflation markets, supported by an experienced dedicated team, an active investment process focused on real yield, breakeven and curve based opportunities, and strong integration of macro, valuation and technical analysis. Our teams have proven ability to manage risk through different market regimes, including periods of extreme volatility. In an environment where starting valuations matter, supply dynamics are supportive and dispersion is elevated, we believe our active management approach to index linked gilts offers investors a valuable option.

Figure 2: RL Index Linked fund quarterly relative returns since start of 2021



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Source: RLAM as at 31 December 2025. The index for the Fund is UK Index-Linked All Stocks Index.

Year on year performance %

RL Index Linked Fund	31/03/2025 - 31/03/2026	31/03/2024 - 31/03/2025	31/03/2023 - 31/03/2024	31/03/2022 - 31/03/2023	31/03/2021 - 31/03/2022
Share class	3.27	(7.08)	(5.84)	(25.14)	4.19

Source: RLAM as at 31 March 2026. **Past performance is not a guarantee or reliable indicator of future returns. 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.** Share class performance is based on mid-day prices, net of fees and gross of taxes, with gross income reinvested unless otherwise stated. Benchmark performance is priced at close of business, gross of fees and taxes. 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 your investment. Rolling performance data shown using month end returns. Share class referenced is M Inc GBP.

Investment risks

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.

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.

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.

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.

Government and Public Securities Risk: The Fund can invest more than 35% of net assets in different Transferable Securities and Money Market Instruments issued or guaranteed by any EEA State, its local authorities, a third country or public international bodies of which one or more EEA States are members.

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