



# Unlocking Value in DC pensions – why active fixed income matters

Lee Hollingworth, Retirement & DC Solutions Director, explores the future adequacy problem facing the UK DC system, and how an active approach to fixed income investing could help improve retirement outcomes.



## Framing the challenge

**The UK faces a pension adequacy issue: simply put, pension pots are going to be too small to meet the retirement needs of UK savers. This is especially true of workplace Defined Contribution (DC) schemes, where the auto-enrolment rates are set at a level unlikely to meet the needs of most savers.**

**In our view, there are only two solutions to this challenge: save more or invest to look to achieve higher net returns. The mandatory minimum rates are unlikely to be raised in the near future; therefore, in our view, greater attention should be paid towards looking to generate higher returns. However, to date deployment of potential solutions have been stymied by the low-cost environment. We believe this is likely to change.**

The regulatory environment is undergoing significant transformation. With the introduction of new Value for Money (VFM) requirements and a government backed push toward Productive Finance, there are two distinct imperatives that, if implemented correctly, can grow pension pots. First, through VFM, schemes will be expected to demonstrate not just cost efficiency, but genuine value delivered through stronger, more resilient long term outcomes. In addition, via the Mansion House accord, the addition of less liquid “productive assets”, could enhance returns if implemented well.

Whilst asset managers cannot make savers save more, they can contribute to the solution of insufficient pensions pots by seeking to increase the growth rates of those pots, with VFM and Mansion House being two separate sources of impetus – the former asking for reliable and cost-effective alpha, and the latter being productive assets that are also return enhancing.

Against this backdrop and in a series of two articles, we will describe how Royal London Asset Management is approaching this challenge. In this first piece, we examine the role of actively managed fixed income assets and the ability to improve outcomes through targeted portfolio construction, and how the use of active

fixed income strategies are potentially the most immediate way of looking to achieve improved and cost-effective outcomes of the VFM requirements.

Later this year, we will describe the way that illiquid assets are used within Royal London Asset Management’s pension range and how they meet the twin commitments of aiming to enhance savers’ returns while allocating to UK productive assets.

At a time when some are questioning the purpose of active management, most obviously demonstrated by the flows of assets to passive strategies, we believe the challenge of improving the lives of UK pensioners is a material way that the asset management industry can demonstrate its value.



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## New world order

The introduction of VFM regulations represent a significant catalyst for change in DC investing. Today, DC defaults lean heavily on public equities and bonds due to their liquidity, simplicity, and low cost. But under the new VFM framework, a cost first mindset is being actively rebalanced toward a clearer focus on aiming to achieve long-term net returns, investment quality, and member outcomes.

Workplace DC schemes will increasingly compete based on investment performance metrics, incentivising schemes to seek out areas that can potentially deliver higher net returns - for example, active fixed income and private markets. These assets, while potentially more expensive, offer the prospect of enhanced investment returns and improved member outcomes when used appropriately.

VFM regulations will require providers to publish consistent and comparable performance metrics, particularly around net investment returns, enabling employers, advisers and governance committees to directly benchmark schemes against peers. This shift - from judging schemes primarily on charges to judging them on value delivered after costs - creates strong competitive pressure. Low fee strategies will no longer be sufficient where they fail to deliver sustainable real returns. As noted in the FCA consultation and related internal summaries, schemes that fail to demonstrate VFM will face mandatory remediation actions, including potential removal from the market if underperformance persists.

Securing additional return in a pension portfolio could improve member outcomes and of course allocations to private markets is a topical example following these changes. However, it is not the only option. We believe that there are easier, more cost-effective routes available that are worth exploring first. A key element of that for Royal London Asset Management is actively managed fixed income. In our view, under this regime, active fixed income becomes attractive for several structural reasons:

- Inefficiencies in credit markets (mispricing, complexity premia, covenant dispersion) that skilled managers can look to exploit.
- Flexibility to rotate across sectors, regions and credit quality as conditions evolve.

This is reflected in our own active credit approach, which emphasises security selection, structural protections and risk aware positioning. These characteristics align directly with the VFM requirement to evidence sustained value, not simply low fees.

On top of that, schemes must now evidence downside mitigation – an area where active fixed income can often be superior. Active fixed income looks to demonstrably reduce downside risk by:

- Adjusting duration more quickly than passive indices.
- Allocating away from deteriorating credit.
- Using off benchmark sectors (such as ABS, secured finance) that could offer better risk-adjusted outcomes. This fits the growing emphasis on resilience and aiming to smooth return paths as members approach retirement. Under VFM, this risk management benefit becomes more valuable because drawdowns directly worsen a scheme's published metrics.

Active management is not about aggressively pursuing short term gains or stretching risk budgets. Rather, it is rooted in disciplined, research driven management: making intentional allocation decisions, diversifying thoughtfully across complementary sources of return, and identifying investments with the potential to outperform through cycles. It requires a robust investment philosophy, deep analytical insight, and a long term perspective.

As the VFM rules embed, schemes will increasingly need to demonstrate not just low cost – but better net performance, risk adjusted returns and evidence of high quality investment. Consultation outcomes also emphasise that providers will compete on long term value rather than price alone, reinforcing this shift.



**The next generation of DC portfolios will be defined by their ability to justify value, demonstrate performance and deliver stronger outcomes for members in a more transparent, data-driven environment.**



## Trends in asset allocation

Together, these dynamics mean that diversification is no longer simply an innovation trend. It is becoming a regulatory driven imperative. The next generation of DC portfolios will be defined by their ability to justify value, demonstrate performance and deliver stronger outcomes for members in a more transparent, data driven environment.

Default fund design typically divides into three distinct phases: the Growth phase; the Consolidation phase; and the Retirement phase. This provides a useful framework to illustrate the evolution:

- **Growth phase:** typically, DC members with over 15 years to their retirement age. The primary objective here is generating real returns investing in growth assets through passive equities. Today the trend is towards greater exposure to private equity and venture capital with the aim of improving the net return.
- **Consolidation phase:** typically, DC members with less than 15 years to retirement. The objective here is to introduce an increased focus on managing downside risk, through greater diversification and allocations to fixed income. How this is achieved can vary between asset owners. For example one may implement through passive management while another uses active management. Going forward we expect to see less emphasis on passive and increasing allocations to private credit and infrastructure, but active fixed income stands out to us as an opportunity for value. This phase is about building resilience and smoothing returns as members approach retirement.
- **SPA (Secure Pension Arrangement) phase:** typically, DC members with less than three years to their retirement age. Bonds now form the majority of the portfolio, integrated with longer-term decumulation design. In this defensive phase, private credit and infrastructure, as well as selectively chosen active fixed income, are likely to be key components in future designs, supporting income and risk management.

## Practical approaches to improve portfolios

Within this environment, Royal London's position is distinctive, as its dual role as both a provider of workplace pensions and an investment manager offers a level of insight into the DC market. Operating on both sides of the value chain gives Royal London Asset Management direct visibility of how regulatory pressures, governance requirements and member behaviours interact in real time. This vantage point allows the organisation to design 'DC-ready' investment strategies - portfolios built not only to satisfy regulatory scrutiny, but to meet the practical needs of employers, trustees and members navigating each stage of the retirement journey.

This integrated perspective means we can tailor our diversified solutions based on deep understanding of how DC schemes operate. The result is a suite of investment approaches crafted specifically for DC savers, both today and as the landscape continues to shift.

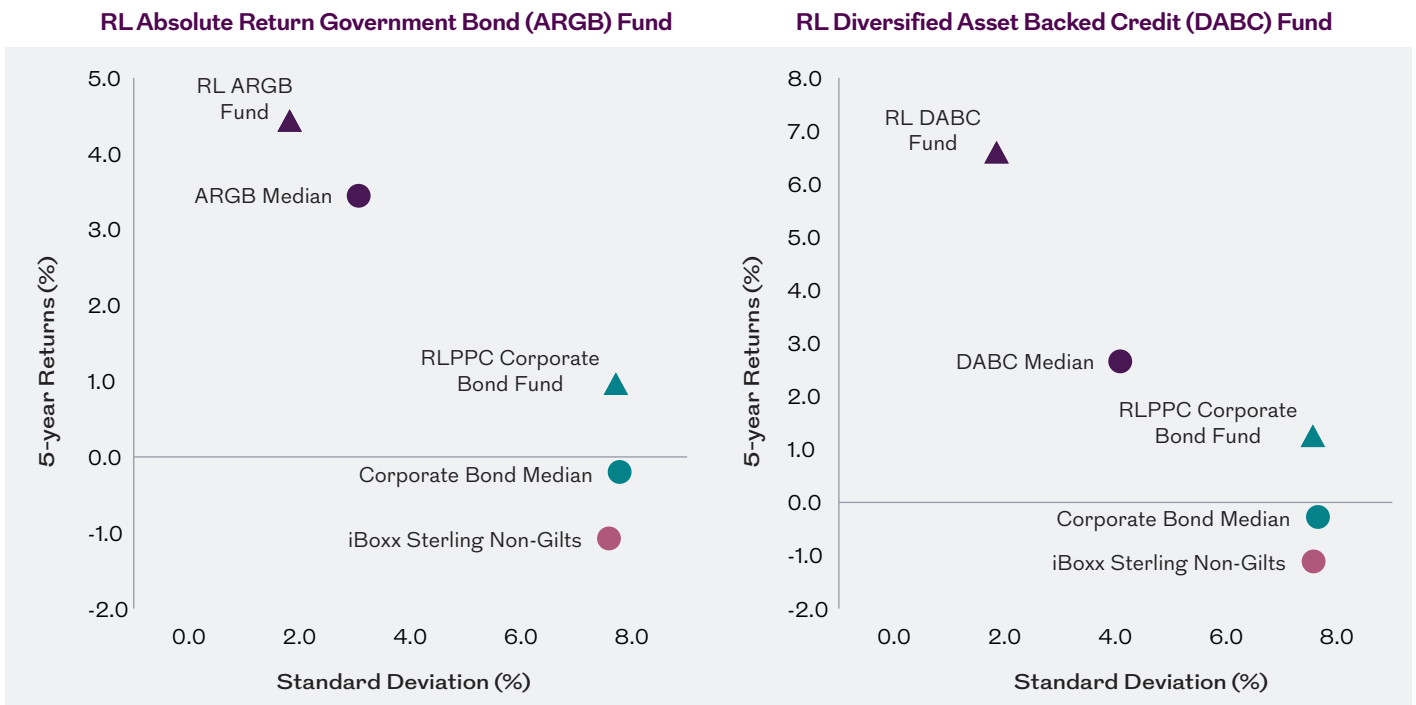
Adding alpha is about making the fund work harder for members, seeking to add excess return generated by active management. Royal London Asset Management can support these aims with a range of fixed income funds that look to take advantage of market conditions.

## Supporting the DC lifecycle

Royal London Asset Management is able to offer comprehensive solutions offering a range of outcomes, with strategies that play a different role at each stage of the DC journey, from early accumulation to retirement. Their core attributes of seeking to provide capital stability, strong liquidity, conservative volatility, and incremental yield over cash can make them especially useful under the VFM framework, where downside risk and net returns are both under scrutiny.

### Figure 1: The potential risk/return profile in passive and active fixed income investing

The chart looks at passive investing, represented here by the iBoxx Sterling Non-Gilt index, and how that fares against active fixed income investing, the Corporate Bond median, and then Royal London Asset Management's Corporate Bond Fund and select funds.



Past performance is not a guarantee or reliable indicator of future returns.

Source: RLAM, eVestment as at 24 March 2026. Performance figures are shown net of fees.

Royal London Absolute Return Government Bond Fund year on year performance (%) - M Acc GBP					
	2026	2025	2024	2023	2022
M Acc GBP	4.22	6.59	6.30	4.01	-0.15
Benchmark	3.95	4.84	5.06	2.51	0.19
RLPPC UK Corporate Bond Fund year on year performance (%) - I Inc GBP					
	2026	2025	2024	2023	2022
I Inc GBP	4.67	7.02	6.40	-7.01	-6.62
Benchmark	3.21	5.64	4.27	-7.70	-8.37
Royal London Diversified Asset-Backed Credit Fund year on year performance - Z Acc GBP					
	2026	2025	2024	2023	2022
Z Acc GBP	7.41	7.08	10.10	3.82	1.52
Benchmark	3.95	4.84	5.06	2.51	0.19

Past performance is not a guarantee or reliable indicator of future returns. Share class performance is based on close of business prices, net of fees and gross of taxes, with gross income reinvested unless otherwise stated.

Source: RLAM as at 30 April 2026.

While passive fixed income can play an important role within DC portfolios, it typically tracks market exposures and therefore can suffer in periods of rising yields, widening credit spreads and elevated volatility. In practice, this can translate into larger drawdowns and a less predictable return profile at precisely the point when schemes are increasingly focused on outcomes and the member experience.

By contrast, actively managed fixed income is intended to manage these risks more deliberately, through a combination of security selection and active portfolio construction - adjusting duration and credit exposure, repositioning across sectors as conditions change, and seeking to capture opportunities in dislocated markets. In that context, Royal London Asset Management's Absolute Return Government Bond (ARGB) and Diversified Asset Backed Credit (DABC) strategies (see Figure 1) can be positioned as building blocks, with the objective of seeking to generate absolute positive capital growth, in the case of ARGB, and excess return over SONIA, for DABC, while aiming to manage volatility.

Royal London Asset Management's fixed income solutions range is designed to support DC savers throughout their full retirement journey. At the early and mid-life stages of DC saving, lower-risk options such as Short Term Fixed Income Enhanced and Senior ABS strategies look to provide SONIA-plus returns with low interest rate duration and high credit quality, helping schemes manage liquidity and reduce cash drag while aiming to deliver dependable incremental yield.

As members move toward consolidation, diversified options such as the RL Absolute Return Government Bond Fund and the RL Short Duration Global High Yield Bond Fund look to offer higher return targets (up to SONIA + 2%) with controlled duration and measured credit exposure, helping support smoother return paths and minimising sequencing risk. In the later stages - pre-retirement and drawdown - strategies like the RL Global Mezzanine ABS Fund, the RL Diversified Asset-Backed Credit Fund, and the RL Multi-Asset Credit Fund can provide attractive yields and stable, collateral-backed cashflows while sustaining income needs (ranging from SONIA + 2.25% up to +6%).

Together, this carefully structured suite looks to allow DC schemes to flex risk levels over time, maintain strong liquidity, and help deliver consistent, evidence-based value - helping members achieve more stable outcomes at every stage of their retirement journey.

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## Investment risks

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.

**Government & 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.

**EPM Techniques:** The Strategy may engage in EPM techniques including holdings of derivative instruments. Whilst intended to reduce risk, the use of these instruments may expose the Strategy to increased price volatility.

**Exchange Rate Risk:** Investing in assets denominated in a currency other than the base currency of the Strategy means the value of the investment can be affected by changes in exchange rates.

**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.

**Liquidity Risk:** In difficult market conditions the value of certain strategies 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 Strategy to financial loss.



## Contact us

For more information about our range of products and services, please contact us.

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The Prospectus and Key Investor Information Document (KIID) are available in English. A summary of investor rights is also available in English. RLAM may terminate the arrangements made for marketing of the fund pursuant to Article 93a of Directive 2009/65/EC.

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