ROYAL LONDON UK OPPORTUNITIES FUND

Quarterly Report 31 December 2020

For professional clients only, not suitable for retail investors

CONTENTS

ROYAL LONDON UK OPPORTUNITIES FUND

Asset split

	Fund (%)
Ashstead Group	6.0
Melrose Industries	5.3
Intermediate Capital Group	4.9
Rio Tinto	4.7
Prudential Plc	4.3
JD Sports	4.1
Synthomer	3.4
Berkeley Group	3.4
B&M	3.3
DCC	3.0
Total	**42.3**

Source: RLAM, based on the M Accumulation share class.

Fund data

	Fund
No. of stocks	35
Fund size	£830.8m
Launch date	31.07.2007

Performance

	Fund (%)	Benchmark[1] (%)	Relative (%)
Q4 2020	**20.40**	**12.62**	**7.78**
Year-to-date	-4.73	-9.82	5.08
Rolling 12 months	-4.73	-9.82	5.08
3 years p.a.	1.67	-0.91	2.59
5 years p.a.	4.38	5.14	-0.76
Since inception p.a. 31.12.2010	6.00	5.57	0.43

Past performance is not necessarily a reliable indicator of 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.

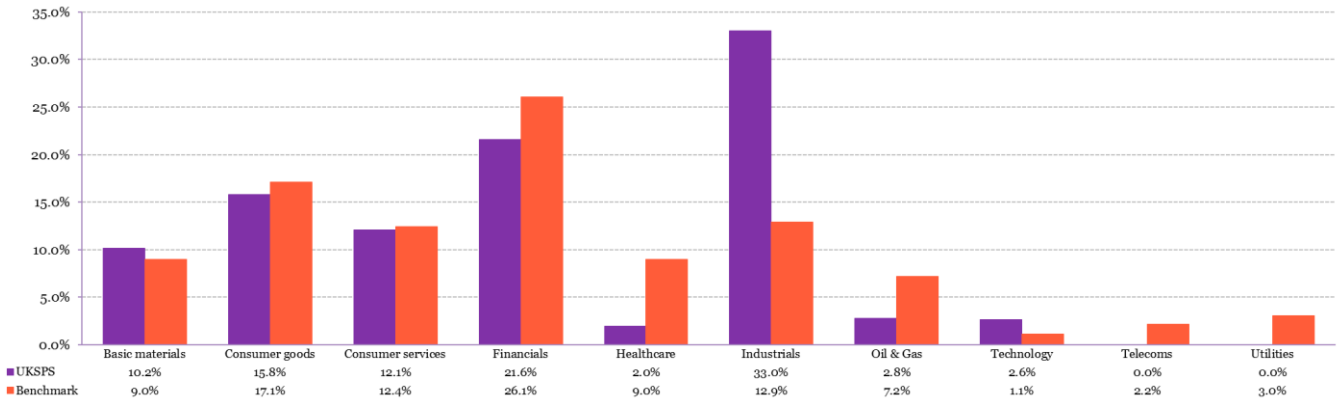
All performance figures stated gross of fees and tax unless otherwise stated.

Source: RLAM, as at 31 December 2020, based on the M Accumulation share class.

[1]Benchmark: FTSE® All Share Index.

As of 6 April 2017, the UK Government announced that funds paying interest distributions will be required to pay those distributions gross of tax.

Sector breakdown



Source: RLAM. Figures in relation to your portfolio exclude the impact of cash held.

ROYAL LONDON UK OPPORTUNITIES FUND

Background

- The market had a strong finish to the year as the last three months saw the FTSE All-Share add 12.6%. Interestingly, there was a definite change in market leadership as oils & gas, a consistent laggard in recent times, finally started to perform. Other strong performing sectors included financials, basic materials and telecommunications. Sectors such as technology and healthcare paused for breath and retreated on an absolute basis.
- There was a noticeable divergence between the performance of the FTSE 100 and that of the Mid 250 and Small Cap. The FTSE 100 Index returned 10.9%, whereas the FTSE 250 advanced 21.4% and the Small Cap leapt 30.9%.
- The two major announcements during the quarter were both positive, namely the successful conclusion of trade talks between the UK and EU, and the positive vaccination updates from Pfizer and Oxford/AstraZeneca. In the previous quarterly report, I wrote that if there was a positive conclusion to the talks, and a vaccine could be approved and rolled out, the market could be 'off to the races.'
- The fund outperformed its benchmark during the quarter, with its 20.4% return comparing to 12.6% from the FTSE All-Share index. The fund has also outperformed the benchmark over the year overall, with a -4.73% return versus -9.82% from the benchmark.

Performance review

The fund runs an 'all-cap' structure which allows us to find the most exciting investments across the market cap spectrum.

Positive contributors

- More than two thirds of the stocks held in the fund outpaced the market over the quarter leading to the strong performance experienced.
- The strongest performer was **Applegreen** (+66%) following an announcement that the founders of the business were looking to take the business private with the help of private equity firm Blackstone.
- **TI Fluid Systems** (+59%) rebounded strongly after releasing an upbeat trading statement showing the market was performing ahead of company expectations.
- **WH Smith** (+58%) was a major beneficiary of the successful vaccine trials. The market anticipated a revival of leisure and business travel following the rollout of Covid-19 vaccines in the first half of 2021.
- One of the fund's largest positions, **Melrose Industries** (+54%), increased materially after the company released a trading statement indicating its performance was at the top end of expectations.
- Challenger bank **One Savings Bank**, which is focussed on the buy-to-let space, was up 52%, while specialist asset manager **Intermediate Capital** was up 46%.
- Although this review is centred on the fourth quarter, it is also worth highlighting how strong some shares have rebounded from their lows in March. **Fevertree** (+183%), **Intermediate Capital** (+166%), **Ashtead** (+160%), **Synthomer** (+140%), **JD Sports** (+136%), **Applegreen** (+129%), **One Savings Bank** (+117%) and **Melrose** (+104%). These are worth highlighting because we are long-term holders in businesses trying to take advantage of short-term price dislocation. We have not deviated from our investment style, but continue to focus on business fundamentals. That has benefitted unitholders over the last nine months.

Negative contributors

- The poorest performer during the quarter was **DCC Group**, the international sales, marketing and support services group. The market seems frustrated that the company is currently running an inefficient balance sheet, many feel it should be acquiring in its chosen areas. Management is on the look-out for complementary acquisitions but will not overpay. The shares finished the quarter down 13%.
- **Experian**, the global leader in consumer and business credit reporting, saw some profit taking after a period of strong growth and finished the quarter down 5%. **Rentokil Initial**, the market-leading pest control and hygiene business also finished 5% lower. Both these companies come under the category of 'quality compounders' and businesses such as these lost ground against the market very recently.
- Other shares which ended the period in negative territory were pharmaceutical giant **GlaxoSmithKline** (-5%) and online wealth platform **Hargreaves Lansdown** (-2%).

ROYAL LONDON UK OPPORTUNITIES FUND

Portfolio activity

- At the end of the quarter the fund had 35 investments spread across a variety of market capitalisations. The active share, the percentage of holdings that deviate from the benchmark index, is currently 82%.
- The split of the investments was as follows:

	Weighting (%)
FTSE 100	66
FTSE 250	22
Small Cap/AIM	10
Cash	2

New holdings

- We added three new holdings during the quarter: **AstraZeneca**, **Computacenter** and **Tesco**.
- AstraZeneca is a global, science-led biopharmaceutical company. The business has changed markedly over the last decade and has transformed its pipeline and returned to growth. The company is focused on three main areas: oncology, cardiovascular and respiratory & immunology. The shares have performed very strongly, though recently weakened on the back of news that they are intending to buy US biotechnology company Alexion. This gave us an opportunity to buy into a long-term growth story at a sensible valuation.
- Computacenter is a leading provider of IT infrastructure services and advises organisations on their IT strategy and implementation of the most appropriate technology while optimising performance. The company has recently increased its position in the North American market with the acquisition of Pivot Technologies Solutions Inc. At present, margins earned in its North American division are roughly half those earned in the UK and the plan is to drive this higher, which would have a meaningful impact on earnings. On a multiple of around 17 times expected 2021 earnings, we are hopeful for future share price appreciation.
- We decided to buy into Tesco, the UK's leading supermarket chain, following the group's decision to exit the Asian market. Other than a small operation in central Europe, Tesco has retreated back to its home market. Using the proceeds received, management has plugged its pension deficit, reduced debt and will shortly return excess capital to shareholders. Its shares were trading on a forward free cashflow yield in excess of 10%, and we do believe the market has not fully appreciated this yet.
- The quarter was a much quieter time in terms of adding to existing positions. We only added to the fund's position sizes in **Hargreaves Lansdown** and **Lloyds Banking Group**.
- Both companies have struggled recently in terms of share price performance and offered us attractive levels to top up. Lloyds, in particular, had toiled as fears of a 'no deal Brexit' weighed heavily on investors' minds. After an upbeat meeting with the incoming Chairman of the Bank, we decided to increase our holding.
- Hargreaves Lansdown has failed to make meaningful progress in its share price for the last three years, but we believe the company is very well managed and in an attractive end market. We believe more potential clients will pivot towards wealth platforms as opposed to wealth managers, and Hargreaves Lansdown should be a major beneficiary of this.

Stocks sold

- The three stocks which exited the portfolio were **SSP Group**, **Compass Group** and **GlaxoSmithKline**.
- The rationale for selling both SSP and Compass was the same. We had been worried, given the continued restrictions being placed on the ability to travel and work from the office, about the time it would take for society to return to some form of normality. We were in the process of selling down the fund's stake in SSP when the news of the successful vaccines trials was announced. The shares immediately leapt in response and we took the opportunity to exit our position. We sold Compass Group just prior to the announcement. Given the further restrictions witnessed over the last month, the road to recovery still feels some way off.
- GlaxoSmithKline proved a disappointing investment for the fund. We were hopeful that after years of underperformance, the company would be able to turn the corner with the spin-off of its consumer division. Unfortunately, there is still a lack of earnings growth within the business and so we decided to recycle the proceeds into AstraZeneca where we see a much brighter future.
- Elsewhere, we took profits on three stocks during the quarter in order to control the position sizes in each. In addition, following the announcement of the bid to take **Applegreen** private, we started selling our position. The three stocks in

question were **Ashtead**, **JD Sports** and **Fevertree**. We are very keen on each of the companies and, indeed, both Ashtead and JD Sports are still top six positions within the portfolio

Outlook

- As we start the New Year, we once again look to the future with optimism. The world is certainly a much changed place from this time 12 months ago, but there is light at the end of the tunnel. It could be argued that it is currently two steps forward, one step back, but we are hopeful that with the successful rollout of the vaccines by this summer, life will return to normality. This means people once again going to their places of work, pubs and restaurants being open for business, and airlines welcoming people on board again.
- At present, the UK stockmarket feels well supported. Leaving aside Covid-19, the successful conclusion of trade talks with the EU gives us a feel good factor, together with the many implications of such a deal. There have been many international investors who have been sitting on the sidelines, unwilling to commit any capital to the market. This stance will very likely change and it is prudent to expect international investors to again allocate money into the UK market. This will likely prove beneficial for the larger, more liquid names initially, before trickling down to the mid-cap names.
- Private equity firms are currently sitting with huge war chests and we have already seen them acquire UK companies. Examples of names which have been bid for recently include William Hill, Entain, Signature Aviation, McCarthy & Stone, RSA and G4S. 2021 could be a bonanza in terms of M&A. We believe there is an incredible amount of latent value both within the companies we are invested in and within the market more generally.
- To conclude, we are confident the portfolio is well placed for the coming year, and indeed for a post-Covid world, whenever that may be. All it leaves me is to wish you a Happy New Year for the coming 12 months and thank you for your continued support.

ROYAL LONDON
ASSET MANAGEMENT

IMPORTANT INFORMATION

For professional clients only, not suitable for retail investors. The views expressed are the author's own and do not constitute investment advice.

This document is a financial promotion. It does not provide, and should not be relied on for, accounting, legal or tax advice, or investment recommendations. For more information on the fund or the risks of investing, please refer to the fund factsheet, Prospectus or Key Investor Information Document (KIID), available via the Fund Information page on www.rlam.co.uk.

Past performance is not a reliable indicator of future results. 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.

Portfolio characteristics and holdings are subject to change without notice. This does not constitute an investment recommendation. For information purposes only, methodology available on request. Information derived from sources other than Royal London Asset Management is believed to be reliable; however, we do not independently verify or guarantee its accuracy or validity.

All rights in the FTSE All Stocks Gilt Index, FTSE Over 15 Year Gilts Index, FTSE A Index Linked Over 5 Years Gilt Index and FTSE A Maturities Gilt Index (the "Index") vest in FTSE International Limited ("FTSE"). All rights in the FTSE 350, FTSE All Share, FTSE 100, FTSE 250, FTSE 350 Higher Yield and FTSE Small Cap (the "Index") vest in FTSE International Limited ("FTSE"). "FTSE®" is a trade mark of the London Stock Exchange Group companies and is used by FTSE under licence. The Royal London Funds (the "funds") have been developed solely by Royal London Asset Management. The Index is calculated by FTSE or its agent. FTSE and its licensors are not connected to and do not sponsor, advise, recommend, endorse or promote the fund and do not accept any liability whatsoever to any person arising out of (a) the use of, reliance on or any error in the Index or (b) investment in or operation of the fund. FTSE makes no claim, prediction, warranty or representation either as to the results to be obtained from the Funds or the suitability of the Index for the purpose to which it is being put by Royal London Asset Management.

All confidential information relating to any Royal London Group company must be treated by you in the strictest confidence. It may only be used for the purposes of assessing the proposal to engage Royal London Asset Management Limited (RLAM). Confidential information should not be disclosed to any third party and should only be disclosed to those of your employees and professional advisers who are required to see such information for the purpose set out above. You should ensure that these persons are made aware of the confidential nature of such information and treat it accordingly. You agree to return and/ or destroy all confidential information on receipt of our written request to do so.

Issued by Royal London Asset Management Limited, Firm Registration Number: 141665, registered in England and Wales number 2244297; Royal London Unit Trust Managers Limited, Firm Registration Number: 144037, registered in England and Wales number 2372439; RLUM Limited, Firm Registration Number: 144032, registered in England and Wales number 2369965. All of these companies are authorised and regulated by the Financial Conduct Authority. Royal London Asset Management Bond Funds Plc, an umbrella company with segregated liability between sub-funds, authorised and regulated by the Central Bank of Ireland, registered in Ireland number 364259. Registered office: 70 Sir John Rogerson's Quay, Dublin 2, Ireland.

All of these companies are subsidiaries of The Royal London Mutual Insurance Society Limited, registered in England and Wales number 99064. Registered Office: 55 Gracechurch Street, London, EC3V 0RL. The Royal London Mutual Insurance Society Limited is authorised by the Prudential Regulation Authority and regulated by the Financial Conduct Authority and the Prudential Regulation Authority. The Royal London Mutual Insurance Society Limited is on the Financial Services Register, registration number 117672. Registered in England and Wales number 99064. FQR RLAM EM 0972.