ROYAL LONDON FIXED INCOME

Fund Manager Commentary – October 2020

For professional clients only, not suitable for retail investors

CONTENTS

ECONOMIC DEVELOPMENTS

Economic developments

- Covid-19 cases spiked in Europe and the UK, leading to renewed national lockdowns; albeit with reduced restrictions compared to those in the spring. US case numbers also rose sharply across a number of states.
- In the UK, the furlough scheme was extended as the lockdown resumed. Labour market data revealed fragility, not least the claimant count, which rose to 2.7m in September. High-frequency data releases suggest UK retail/recreation trends peaked in late August. While the EU summit failed to produce an agreement, Brexit talks continued and entered a more intensive phase.
- US GDP rose 33.1% annualised in the third quarter, leaving output just 2.9% below a year ago. That being said, monthly data indicated that growth had slowed by July and high-frequency data weakened. Congress again failed to agree an extended support package. President Trump continued to question the validity of postal ballots. Joe Biden maintained his national poll lead, although this was less clear cut in key battleground states.
- Euro area GDP rose 12.7%Q (9.6%Q expected) after stronger-than-expected growth in France, Germany and Italy. Annualised GDP growth is -4.3%, still weak heading into a challenging period. Google mobility and OpenTable data revealed deteriorating consumer trends pre-lockdown. The ECB indicated that more easing is on the way in December and ECB president Lagarde confirmed that there would be a package of measures to recalibrate its approach.

RLAM CREDIT FUND PERFORMANCE

Fund performance

	1 month (%)	Rolling 12 months (%)
RL Corporate Bond Fund Z Inc	**0.46**	**4.25**
IA Sterling Corporate Bond Sector	0.20	4.39
iBoxx Sterling Non-Gilts All Maturities Index	0.11	4.34
RL Ethical Bond Fund Z Inc	**0.42**	**4.65**
IA Sterling Strategic Bond Sector	0.32	3.35
iBoxx Sterling Non-Gilts All Maturities Index	0.11	4.34
RL Global Bond Opportunities Fund Z Inc	**0.54**	**0.38**
RL Investment Grade Short Dated Credit Fund Z Inc	**0.10**	**2.50**
IA Sterling Corporate Bond Sector	0.20	4.39
ICE BofA ML 1-5 year Sterling Non-Gilt All Stocks Index	0.21	2.41
RL Short Duration Credit Fund Z Inc	**0.39**	**2.63**
IA Sterling Strategic Bond Sector	0.32	3.35
ICE BofA ML 1-5 year Sterling Non-Gilt All Stocks Index	0.21	2.41
RL Sterling Credit Fund Z Inc	**0.42**	**3.99**
IA Sterling Corporate Bond Sector	0.20	4.39
iBoxx Sterling Non-Gilts All Maturities Index	0.11	4.34
RL Sterling Extra Yield Bond Fund A Inc	**0.64**	**-3.00**
RL Sterling Extra Yield Bond Fund B Inc	**0.58**	**-3.49**
RL Sterling Extra Yield Bond Fund Y Inc	**0.67**	**-2.58**
RL Sterling Extra Yield Bond Fund Z Inc	**0.66**	**-2.76**
IA Sterling Corporate Bond Sector	0.20	4.39
IA Sterling High Yield Sector	0.49	-0.25
IA Sterling Strategic Bond Sector	0.32	3.35

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.

Source: RLAM and FE, correct as of 31 October 2020. Returns quoted are net of fees.

[1]Please note that the benchmark pricing is end-of-day, and entails no currency conversion.

CREDIT MARKET REVIEW

Market highlights

Sterling Investment Grade Credit

- The benchmark 10-year gilt yield increased from 0.23% to 0.26% in October. Sterling investment grade corporate debt returned 0.11%, outperforming UK government bonds (-0.53%). The average sterling investment grade credit spread (the average extra yield available from a corporate bond compared with government debt of equal maturity) narrowed from 1.29% to 1.23%.
- Total returns were generally positive across sterling credit sectors. Bonds in the banking sector outperformed the broad market, while those in the insurance sector were weak; subordinated insurance was the worst performing sector over the month. Secured and structured bonds encompassed a broad spectrum of returns: real estate and asset-backed securities lagged the wider market, whereas covered bonds outperformed. The strongest returns came from medium-dated bonds and the worst came from long-dated issues. Lower-rated bonds outperformed higher-rated issues, with supranationals marginally lagging the broad market.
- Credit issuance eased in the sterling and euro credit markets, in line with seasonal trends but nevertheless below levels prevalent a year ago. There was a fairly even spread of financial and industrial issuers.

ROYAL LONDON CORPORATE BOND FUND

Portfolio commentary

- Net of fees, the fund delivered a return of 0.46% in October (Z class, Income), outperforming the iBoxx Sterling Non-Gilts All Maturities Index, which returned 0.11%, and the 0.21% average return for its peer group (IA Sterling Corporate Bond).
- Total returns were generally positive across sterling credit sectors. Banks outperformed, including subordinated banks, although this was offset by underperformance in subordinated insurance. Covered bonds also outperformed, which marginally benefitted performance. Conversely, secured and structured bonds were relatively weak, with real estate markedly underperforming, which adversely affected performance. Supranationals marginally underperformed the broad market, which supported performance given our significant underweight in this large sector. Lower-rated bonds (BBB and below) strongly outperformed higher-rated issues, which was particularly positive for performance given our overweight positions in BBB rated, sub-investment grade and unrated bonds.
- Overweight exposure to insurance, a substantial underweight in supranational bonds, and a bias towards secured issues (such as social housing) are the most noticeable features of sector positioning.
- We participated in six new issues, including subordinated insurance issues from **Just Group** and **Pension Insurance Corporation**. Otherwise, we bought bonds from hotels operator **InterContinental Hotels (IHG)** and packaging and PPE supplier **Bunzl**, and a structured bond of **Heathrow**. Lastly, we participated in the issue of short-dated 'payment-in-kind' bonds by **The Metrocentre Partnership** that are secured against the shopping centre in the North East.
- Secondary market activity mainly focused on buying bonds in the financials and structured sectors. We bought senior bonds of **Handelsbanken**, the Swedish bank, and bonds of **Barclays** and **Leeds Building Society**, as well as short-dated covered bonds of **Leeds Building Society**. We also bought structured bonds of **Southern Water**, which is an attractive regulated water utility with lower transition risk, and short-dated bonds of utility **Western Power Distribution** and **Orange**, the mobile telecoms company. Against this activity, among other trades, we sold bonds of **Bank of Scotland** and covered bonds of **TSB**, and structured bonds of **Logicor** and **Southern Water** as both had performed well.
- Bonds of Dutch bank **Rabobank** were repurchased from the portfolio by the issuer on attractive terms for investors.

Investment outlook

- The UK's economic recovery, which had already been slowing during the summer, may be jeopardised by recent lockdown measures and rising unemployment seems likely. Even if the measures succeed in curtailing the spread of Covid-19 and society can return to more normal conditions, the economy is likely to be compromised over the medium term given the surge in government debt. Interest rates look set to remain at very low levels over the next two or three years, with yield curves heavily managed by governments.
- We continue to believe that portfolio diversification is important and a focus on bonds supported by stable income streams and structural enhancements should provide protection in times of market turbulence.
- While the economic impact of the virus will have a detrimental impact on corporate profitability, we consider that the current credit spread offers sufficient compensation for default and other risks (e.g. liquidity and rating migration). We expect investment grade credit bonds will outperform UK government securities over the next three years.

Key views within the fund

- The fund is diversified, with over 300 holdings, in order to improve overall portfolio liquidity and to reduce the effect on overall fund performance of any deterioration in the creditworthiness of an individual holding.

ROYAL LONDON CORPORATE BOND FUND

- A significant underweight in supranational bonds, as we expect corporate bonds to outperform over the medium term.
- Duration marginally below benchmark.
- An overweight position in subordinated financial debt, where we believe yields are attractive.
- The fund remains orientated towards secured bonds in the asset-rich investment trust, property and social housing sectors, and towards structured bonds, which benefit from a claim on assets and cashflows.

Shalin Shah
Senior Fund Manager

Jonathan Platt
Head of Fixed Income

ROYAL LONDON ETHICAL BOND FUND

Portfolio commentary

- The fund's Z class delivered a return, net of fee, of 0.42% in October. This compares to the 0.11% return of the iBoxx Sterling Non-Gilts All Maturities Index and the average returns recorded for the Investment Association (IA) Sterling Strategic Bond sector and the IA Sterling Corporate Bond sector of 0.32% and 0.20% respectively. The fund is a constituent of the former sector because its weighting in investment grade sterling corporate bonds has frequently been less than 80%, predominantly as a result of the holdings of unrated secured debt; however, in the context of its investment grade benchmark, the fund's performance relative to the more homogenous Sterling Corporate Bond sector is also relevant.
- The fund's bias towards lower-rated bonds (BBB and below) was helpful over the month, with the significant underweight exposure to supranationals also contributing to performance. Within financial sectors, the fund benefitted from its overweight exposure to subordinated banking issues, but its overweight insurance allocation detracted from relative returns. The fund's overweight holdings of secured and structured bonds were detrimental during the month, given that real estate and asset-backed securities lagged the wider market.
- Overweight exposure to subordinated financial debt, a substantial underweight in supranational bonds and a bias towards secured and structured issues remained the most noticeable features of sector positioning.
- The fund participated in several new issues over the month. Within the financial sectors, subordinated insurance bonds were added of **Just Group** and **Pension Insurance Corporation**, as well as a senior bond from **Barclays**. In the consumer services sector, additions included bonds from **InterContinental Hotels** and distribution company **Bunzl**. With regard to structured debt, purchases included a new issue of **Heathrow**, floating-rate commercial mortgage-backed securities from the affordable housing provider **Sage**, and an issue of short-dated 'payment-in-kind' bonds by **The Metrocentre Partnership**, ranking by agreement ahead of the company's existing secured debt, with a 'super-senior' claim on the shopping centre in the North East.
- Secondary market activity primarily involved buying bonds in the financial and structured sectors. Within the financial sectors, purchases included subordinated bonds of **Credit Agricole**, **Leeds Building Society** and **Virgin Money**, as well as a senior bond of **TP ICAP** and a covered bond of **Clydesdale Bank**. Among structured issues, a notable addition was long-dated debt of **Progress Health**, which featured an attractive balance of risk and return given that its sector was likely to be less impacted by economic weakness caused by the Covid-19 pandemic. Elsewhere, short-dated structured debt of **Gatwick** and **Heathrow** was also added.

Investment outlook

- The UK's economic recovery, which had already been slowing during the summer, may be jeopardised by recent lockdown measures and rising unemployment seems likely. Even if the measures succeed in curtailing the spread of Covid-19 and society can return to more normal conditions, the economy is likely to be compromised over the medium term given the surge in government debt. Interest rates look set to remain at very low levels over the next two or three years, with yield curves heavily managed by governments.
- We continue to believe that portfolio diversification is important and a focus on bonds supported by stable income streams and structural enhancements should provide protection in times of market turbulence.
- While the economic impact of the virus will have a detrimental impact on corporate profitability, we consider that the current credit spread offers sufficient compensation for default and other risks (e.g. liquidity and rating migration). We expect investment grade credit bonds will outperform UK government securities over the next three years.

Key views within the fund

- The fund is diversified, with more than 400 holdings, in order to improve portfolio liquidity and to reduce the effect on overall performance of any deterioration in the creditworthiness of an individual holding.
- The fund has a significant underweight position in supranational bonds, as we expect corporate bonds to outperform over the medium term.

ROYAL LONDON ETHICAL BOND FUND

- Duration moderately below the benchmark.
- The fund has an overweight position in subordinated financial debt, where we believe yields are attractive.
- The fund remains orientated towards secured bonds in the asset-rich investment trust, property and social housing sectors, and towards structured bonds, which benefit from a claim on assets and cashflows.

FE ALPHA MANAGER 2019 ERIC HOLT

CITYWIRE +

Eric Holt
Head of Credit

ROYAL LONDON GLOBAL BOND OPPORTUNITIES FUND

Executive summary

- The fund's Z class recorded a return, net of fee, of 0.54% in October. It was an unusual month for corporate bond markets, reflecting divergence in the performance of underlying government bond markets. High yield debt broadly outperformed investment grade issues, but regional differences proved a significant factor. At the sector level, strong performances were seen in the banking sector, while the consumer and energy sectors were generally more subdued. The fund delivered a very strong relative return in this context, ahead of all of its comparator indices bar one, reflecting the strong income generation of the portfolio. The fund has recovered strongly so far this year and is well positioned going forward.
- Distributions payable at the end of November were 1.31p.

Market highlights

Index	Total return (%)	Spread movement (basis points)
Euro investment grade corporate bonds **ICE BofA ML euro corporate and Pfandbriefe index**	0.75	-1
AT1 **ICE BofA ML contingent capital index**	0.44	1
HY global non-financial corps **ICE BofA ML global non-financial high yield index**	0.39	-5
HY non-financial emerging markets **ICE BofA ML emerging markets high yield ex. subordinated financial index**	0.30	-7
Sterling investment grade corporate bonds **ICE BofA ML sterling corporate and collateralised index**	0.15	-5
HY global non-financial hybrid corps **ICE BofA ML global hybrid non-financial high yield index**	0.00	13
IG global non-financial hybrid corps **ICE BofA ML global hybrid non-financial corporate index**	-0.01	10
Dollar investment grade corporate bonds **ICE BofA ML US corporate index**	-0.17	-10

Source: Bloomberg

- The performance of corporate bond markets in October was somewhat unusual. There was significant day-to-day volatility, with the bellwether 30-year benchmark gilt trading across a price range of over 5%. There was also considerable dispersion in performance by region, in part reflecting movements in underlying government bond markets. While government bond yields declined in Europe, they rose slightly in the UK and significantly in the US. Consequently, although dollar investment grade corporate bonds saw the greatest average spread contraction, they constituted the worst performing comparator index from a total return perspective. Similarly, while high yield bonds generally outperformed investment grade debt, euro investment grade bonds performed best on a total return basis.
- The general outperformance of global risk assets was supported by expectations, based on polling, of a 'blue sweep' in the upcoming US elections, whereby both Biden would become President and the Democrats would take control of the Senate. Such an outcome would be likely to result in a larger US stimulus package, given that the Democrats had sought a $2.2tn package during the month, whereas Trump had offered $1.8tn. On the other hand, a significant resurgence of Covid-19 cases prompted renewed lockdowns in Europe, albeit with less economic impact than earlier in the year due to policy support from governments and central banks. That supported less risky assets in the region.

Portfolio commentary

- The relatively muted market backdrop in October provided a number of influences on segments of the fund's portfolio, without any being particularly significant, while a substantial part of the fund's overall performance reflected its robust income generation. The prospect of a second wave of Covid-19 infection, and the prospect of lockdown constraints, affected holdings related to the consumer sector, notably bonds of **Heathrow** and pub operator **Mitchells & Butlers**. Holdings in the banking sector generally did better, with bonds of **Lloyds**, **Rabobank**, **Santander** and **Standard Chartered** moving up in price on the month. The brief period of oil price weakness towards the end of the month resulted in subdued sentiment in the energy sector, with the prices of **DNO**, **Ithaca Energy**, **ShaMaran Petroleum** and the offshore

ROYAL LONDON GLOBAL BOND OPPORTUNITIES FUND

contractor **Vantage Drilling** down moderately in price. In contrast, bonds from several companies that provide services to the oil & gas sector performed strongly, such as **Beerenberg** after the successful early refinancing of its 2021 notes.

- Activity in the month included participation in new issues of Danish multinational power company **Ørsted** (a short-dated hybrid with a high reset), shopping centre owners **Metrocentre Partnership** (short-dated 'payment-in-kind' bonds, ranking by agreement ahead of the company's existing secured debt, with a 'super-senior' claim on the shopping centre in the North East), and **Rolls Royce** (BB rated, offering 5¾% income for seven years and contingent on the company's £2 billion equity raise). Sales during the month included bonds from the banks **Barclays**, **Lloyds** and **UBS**, energy company **Santos**, shipping companies **Songa Container** and **Teekay Shuttle Tankers**, and telecommunications businesses **Bharti Airtel**, **Eutelsat** and **INWIT**. Bonds from the exploration and production company **Aker BP** and the international banking group **BNP Paribas** were called away from the portfolio during the month at favourable terms.

Investment outlook

- Global economies may be jeopardised by recent lockdown measures and rising unemployment seems likely. Even if the measures succeed in curtailing the spread of Covid-19 and societies can return to more normal conditions, many economies are likely to be compromised over the medium term given the surge in government debt. Interest rates look set to remain at very low levels over the next two or three years, with yield curves heavily managed by governments.
- We continue to believe that portfolio diversification is important and a focus on bonds supported by stable income streams and structural enhancements should provide protection in times of market turbulence.
- While the economic impact of the virus will have a detrimental impact on corporate profitability, we consider that the current credit spread offers sufficient compensation for default and other risks (e.g. liquidity and rating migration).

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Rachid Semaoune
Senior Fund Manager

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Eric Holt
Head of Credit

MONEY OBSERVER RATED FUND 2019

ROYAL LONDON INVESTMENT GRADE SHORT DATED CREDIT FUND

Portfolio commentary

- The fund recorded a net return of 0.10% (Z class, Income) in October, against the 0.21% gross return of the ICE BofA Merrill Lynch 1-5 Year Sterling Non-Gilt Index and the 0.21% average return of the wider all-maturities sector (IA Sterling Corporate Bond).
- Total returns were generally positive across sterling credit sectors. Banks outperformed, including subordinated banks, although this was offset by underperformance in subordinated insurance. Covered bonds also outperformed, which benefitted performance. Conversely, secured and structured bonds were relatively weak, adversely affecting performance. Supranationals marginally underperformed the broad market, which supported performance given our significant underweight in this large sector. Lower-rated bonds (BBB and below) strongly outperformed higher-rated issues, which was particularly positive for performance given our overweight position in BBB rated bonds.
- The minimal weighting in supranational bonds, overweight holding of financial debt and bias towards secured and structured issues remained the fund's most notable sector characteristics.
- We participated in three new issues, including a senior banks issue from **Barclays** and a structured bond of **Thames Water.** Otherwise, we bought bonds of hotels operator **InterContinental Hotels**.
- Secondary market activity focused on managing cash inflows. We mainly bought bonds in the financials and structured sectors, including senior bonds of **Lloyds Banking Group**, **3i** and **Investec**; subordinated insurance bonds of **Aviva**, **Liverpool Victoria** and **PGH Capital**; and short-dated structured bonds of **Heathrow** and **Gatwick**. Otherwise, we bought bonds of mobile telecoms operator **Orange** and **A2d Funding**, the social housing group.
- Bonds of **Walgreens Boots Alliance** were called away from the portfolio in the month.

Investment outlook

- The UK's economic recovery, which had already been slowing during the summer, may be jeopardised by recent lockdown measures and rising unemployment seems likely. Even if the measures succeed in curtailing the spread of Covid-19 and society can return to more normal conditions, the economy is likely to be compromised over the medium term given the surge in government debt. Interest rates look set to remain at very low levels over the next two or three years, with yield curves heavily managed by governments.
- We continue to believe that portfolio diversification is important and a focus on bonds supported by stable income streams and structural enhancements should provide protection in times of market turbulence.
- While the economic impact of the virus will have a detrimental impact on corporate profitability, we consider that the current credit spread offers sufficient compensation for default and other risks (e.g. liquidity and rating migration). We expect investment grade credit bonds will outperform UK government securities over the next three years.

Key views within the fund

- The fund is diversified, with almost 300 holdings, in order to improve general portfolio liquidity and to reduce the effect on overall performance of any deterioration in the creditworthiness of an individual holding.
- It has a minimal weighting in supranational bonds, as we expect corporate debt to outperform over the medium term.
- Duration is slightly lower than that of the benchmark.
- It has an overweight position in subordinated financial debt, where we believe yields are attractive.
- The fund remains orientated towards structured debt, which benefits from a claim on assets and cashflows; secured issues in the asset-rich property and social housing sectors; and covered bonds (i.e. senior bank debt benefiting from a first claim on a specified over-collateralised pool of assets).

CITYWIRE A

Richard Nelson
Senior Fund Manager

CITYWIRE A

Paola Binns
Senior Fund Manager

ELITE PROVIDER
rated for bonds by FundCalibre.com

ROYAL LONDON SHORT DURATION CREDIT FUND

Portfolio commentary

- The fund's Z class delivered a return, net of fee, of 0.39% in October, against the 0.21% return of the ICE BofA Merrill Lynch 1-5 Year Sterling Non-Gilt All Stocks Index and the 0.32% return of the IA Sterling Strategic Bond sector.
- The fund's bias towards lower-rated bonds (BBB and below) was helpful over the month, with the significant underweight exposure to supranationals also contributing to performance. Within financial sectors, the fund benefitted from its overweight exposure to subordinated banking issues, but its overweight insurance allocation detracted from relative returns. The fund's overweight holdings of secured and structured bonds were detrimental during the month, given that real estate and asset-backed securities lagged the wider market.
- Overweight exposure to subordinated financial debt, a substantial underweight in supranational bonds and a bias towards secured and structured issues remained the most noticeable features of sector positioning.
- We participated in several new issues over the month. Within the financial sectors, we bought subordinated bonds from **Just Group** and **RBS**, as well as a senior bond from **Barclays**. In the consumer services sector, we added debt from **InterContinental Hotels** and pub group **Fuller's**. With regard to structured debt, we purchased floating-rate commercial mortgage-backed securities from the affordable housing provider **Sage**, and participated in the issue of short-dated 'payment-in-kind' bonds by **The Metrocentre Partnership** that are secured against the shopping centre in the North East.
- Secondary market activity primarily involved buying bonds in the financial and structured sectors. Within the financial sectors, we bought subordinated bonds of **Wells Fargo** and **Yorkshire Building Society**, as well as of **Nationwide Building Society** as part of an attractively-priced 'rump issue'. Additionally, we bought senior bonds of **Lloyds Bank** and **3i Group** that appeared modestly priced. Among structured issues, we added short-dated debt of **Gatwick** and **Heathrow**, and we increased our holdings of **Delamare Finance**, bonds backed by Tesco operational property and leases, and of **Cold Finance**, which are secured on cold storage facilities.

Investment outlook

- The UK's economic recovery, which had already been slowing during the summer, may be jeopardised by recent lockdown measures and rising unemployment seems likely. Even if the measures succeed in curtailing the spread of Covid-19 and society can return to more normal conditions, the economy is likely to be compromised over the medium term given the surge in government debt. Interest rates look set to remain at very low levels over the next two or three years, with yield curves heavily managed by governments.
- We continue to believe that portfolio diversification is important and a focus on bonds supported by stable income streams and structural enhancements should provide protection in times of market turbulence.
- While the economic impact of the virus will have a detrimental impact on corporate profitability, we consider that the current credit spread offers sufficient compensation for default and other risks (e.g. liquidity and rating migration). We expect investment grade credit bonds will outperform UK government securities over the next three years.

Key views within the fund

- The fund is diversified, with more than 300 holdings, in order to improve overall portfolio liquidity and to reduce the effect on overall performance of any deterioration in the creditworthiness of an individual exposure.
- The fund has a significant underweight in supranational bonds, as we expect corporate debt to outperform over the medium term.
- Fund duration longer than the benchmark, as central banks adopt more dovish policy stances.
- The fund has an overweight position in subordinated financial debt, where we believe yields are attractive.
- The fund remains orientated towards secured bonds in the asset-rich investment trust, property and social housing sectors, and towards structured issues, which benefit from a claim on assets and cashflows.

Paola Binns
Senior Fund Manager

ROYAL LONDON STERLING CREDIT FUND

Portfolio commentary

- The fund's Z class recorded a return, net of fee, of 0.42% in October. This compares with 0.11% for the iBoxx Sterling Non-Gilts All Maturities Index and 0.20% for its sector (IA Sterling Corporate Bond).
- The fund's bias towards lower-rated bonds (BBB and below) was helpful over the month, with the significant underweight exposure to supranationals also contributing to performance. Within financial sectors, the fund benefitted from its overweight exposure to subordinated banking issues, but its overweight insurance allocation detracted from relative returns. The fund's overweight holdings of secured and structured bonds were detrimental during the month, given that real estate and asset-backed securities lagged the wider market.
- Overweight exposure to subordinated financial debt, a substantial underweight in supranational bonds and a bias towards secured and structured issues remained the most noticeable features of sector positioning.
- We participated in several new issues over the month. Within the financial sectors, we bought subordinated insurance bonds from **Just Group** and **Pension Insurance Corporation**, and we bought a senior bond from **Barclays**. In the consumer services sector, we added debt from **InterContinental Hotels** and distribution company **Bunzl**. With regard to structured debt, we participated in a new issue of **Heathrow** and added short-dated floating rate notes of the shopping centre **MetroCentre**.
- In the secondary market, our activity was focused on the structured and financial sectors. With respect to structured issues, we added debt from **Progress Health** and **Derby Healthcare**, attracted by the balance of risk and return they offered given that they are likely to be less impacted by economic weakness caused by the Covid-19 pandemic. For similar reasons we also added structured debt from **Aspire Defence**, which provides accommodation to soldiers as part of one of the largest private finance initiatives ever contracted by the Ministry of Defence. Elsewhere, we added short-dated structured debt of **Gatwick**. In the financial sectors, we bought a number of bonds that featured attractive yields and risk-return dynamics, such as from **Lloyds Bank**, **Rothschild & Co** and **Santander**.
- Bonds of **Aker BP** and **Barclays** were called away from the portfolio during the month.

Investment outlook

- The UK's economic recovery, which had already been slowing during the summer, may be jeopardised by recent lockdown measures and rising unemployment seems likely. Even if the measures succeed in curtailing the spread of Covid-19 and society can return to more normal conditions, the economy is likely to be compromised over the medium term given the surge in government debt. Interest rates look set to remain at very low levels over the next two or three years, with yield curves heavily managed by governments.
- We continue to believe that portfolio diversification is important and a focus on bonds supported by stable income streams and structural enhancements should provide protection in times of market turbulence.
- While the economic impact of the virus will have a detrimental impact on corporate profitability, we consider that the current credit spread offers sufficient compensation for default and other risks (e.g. liquidity and rating migration). We expect investment grade credit bonds will outperform UK government securities over the next three years.

Key views within the fund

- The fund is diversified, with around 400 holdings, in order to improve overall portfolio liquidity and to reduce the effect on overall performance of any deterioration in the creditworthiness of an individual holding.
- A significant underweight in supranational bonds, as we expect corporate bonds to outperform over the medium term.

ROYAL LONDON STERLING CREDIT FUND

- Duration in line with the benchmark. We believe the level of gilt yields is challenging over the longer term. However, our level of conviction is low regarding their short-term direction.
- An overweight position in subordinated financial debt, where we believe yields are attractive.
- The fund remains orientated towards secured bonds in the asset-rich investment trust, property and social housing sectors, and structured bonds, which benefit from a claim on assets and cashflows.

Paola Binns
Senior Fund Manager

ROYAL LONDON STERLING EXTRA YIELD BOND FUND

Portfolio commentary

- The value of the A, B, Y and Z class shares rose 0.64%, 0.58%, 0.67% and 0.66% respectively in October, extending the progressive recovery from the depths of the market in March, bringing the year-to-date returns to -4.23%, -4.64%, -3.89% and -4.02%, respectively.
- While financial markets maintained a significant degree of volatility in the month, with the bellwether 30-year benchmark gilt trading across a price range of over 5%. In some contrast its yield over the month ranged from 0.69% to 0.89% p.a. The overall returns for the month somewhat belie this day-to-day volatility. Gilts posted an index return of -0.56%, reflecting a modest move up in yields after the significant fall in gilts yields earlier in the year. Sterling investment grade corporate bonds performed better, posting a 0.11% return as the improvement in sentiment and the attraction of incremental yield more than offset the rise in gilt yields, while European and global sub-investment grade indices posted 0.24% and 0.42% returns, again reflecting the attraction of yield and improving market sentiment. 2020 year-to-date index returns to end October for these four asset classes are 7.54%, 4.73%, -2.31% and 0.19%, reflecting the decline in government yields and the more challenging environment for corporate bonds, albeit corporate bond markets have progressed significantly from the low point in March.
- This relatively muted market backdrop in October produced a number of influences on segments of the overall portfolio, without any being particularly significant, while a substantial part of the fund's overall performance reflected its robust income generation. The prospect of a second wave of Covid-19 infection, and the prospect of lockdown constraints, affected holdings related to the consumer sector, including bonds of retailer **Intu**, pub operator **Mitchells & Butler**, leisure business **Center Parcs** and **Heathrow**. Holdings in the banking sector generally did better, with bonds of **Barclays**, **Lloyds**, **NatWest**, **Santander** and **Standard Chartered Bank** moving up in price on the month. The brief period of oil price weakness towards the end of the month resulted in subdued sentiment in the energy sector, with the prices of **DNO**, **Independent Oil & Gas** and **Norwegian Energy** down moderately in price. In contrast, strong individual performances were recorded by shipping company **Songa Container**, developing economy microfinance business **Bayport**, Irish property group **Yew Grove**, specialist lender **Together Group** and fund management group **Jupiter**, perhaps reflecting the smaller, lower-profile nature of such holdings and their slower response to improving market sentiment.
- Activity in the month included participation in new issues of **Aggregated Micro Power** (unrated, increasing issue size to £155m and funding expansion of its renewable energy and UK electricity grid integrity assets), **Rolls Royce** (BB rated, offering 5¾% income for seven years and contingent on the company's £2 billion equity raise), insurers **Just Group** and **Pension Insurance** (each BBB rated but callable and 'bullet' respectively, with 7% income to a 2025 call date and 3⅝% income to 2032 – both have performed very well in the early weeks of trading), and **InterContinental Hotels** (BBB rated 3⅜% 2028 bonds of the predominantly US domestic hotel business). Sales in the month included insurers **Direct Line** and **Legal & General**, bonds of **Leeds Building Society**, banking groups **Credit Agricole**, **Rothschild**, and **Standard Chartered** – generally reducing exposure to longer-dated bonds after recent strong performance, while a capital gain of over 6% was crystallised by the sale of **BP** hybrid US dollar bonds bought at issue in June. A further feature of the month was disinvestment, broadly proportional and across the range of investments in the fund, as an investor in the fund moved to investment in segregated assets within the same strategy – this disinvestment left the fund's characteristics effectively unchanged. Finally, activity in short-dated gilts reflected efficient liquidity management during the month.

Investment outlook

- The UK's economic recovery, which had already been slowing during the summer, may be jeopardised by recent lockdown measures and rising unemployment seems likely. Even if the measures succeed in curtailing the spread of Covid-19 and society can return to more normal conditions, the economy is likely to be compromised over the medium term given the surge in government debt. Interest rates look set to remain at very low levels over the next two or three years, with yield curves heavily managed by governments.
- We continue to believe that portfolio diversification is important and a focus on bonds supported by stable income streams and structural enhancements should provide protection in times of market turbulence.
- While the economic impact of the virus will have a detrimental impact on corporate profitability, we consider that the current credit spread offers sufficient compensation for default and other risks (e.g. liquidity and rating migration). We expect investment grade credit bonds will outperform UK government securities over the next three years.

ROYAL LONDON STERLING EXTRA YIELD BOND FUND

Key views within the fund

- The fund's objective is to achieve a high level of income by seeking attractive investments across a broad spectrum of fixed income opportunities, encompassing investment grade, sub-investment grade and unrated bonds.
- The fund mitigates stock-specific risk by holding a diversified portfolio of investments, so that no individual investment can in isolation have an undue impact on overall performance. In addition, where possible within the yield objective of the fund, investments are focused on bonds where risk is mitigated by structure or a claim on assets or cashflows.

FE ALPHA MANAGER 2019 ERIC HOLT
CITYWIRE +

Eric Holt
Head of Credit

FE ALPHA MANAGER 2019 RACHID SEMAOUNE
CITYWIRE +

Rachid Semaoune
Senior Fund Manager

MONEY OBSERVER RATED FUND 2019

RLAM GOVERNMENT BOND FUND PERFORMANCE

Fund performance

	1 month (%)	Rolling 12 months (%)
RL Global Index Linked Bond Fund Z Inc	**0.00**	**7.23**
IA Global Bonds Sector	0.01	4.43
Barclays World Government Inflation-Linked Bond Index (hedged)	0.04	6.10
RL Index Linked Bond Fund M Inc	**0.28**	**9.34**
IA UK Index Linked Gilts Sector	0.36	9.33
FTSE Actuaries UK Index-Linked All Stocks Index	0.65	6.69
RL Short Duration Gilt Fund Z Inc	**0.00**	**1.20**
IA UK Gilts Sector	-0.52	5.69
FTSE Actuaries UK Conventional Gilts up to 5 Years Index	-0.05	1.25
RL Short Duration Global Index Linked Bond Fund Z Inc	**-0.09**	**3.80**
IA Global Bonds Sector	0.01	4.43
RL Short Duration Global Index Linked Composite Benchmark[1 2]	-0.22	2.92
RL UK Government Bond Fund Z Inc	**-0.49**	**6.18**
IA UK Gilts Sector	-0.52	5.69
FTSE Actuaries UK Conventional Gilts All Stocks Index	-0.53	4.77

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.

Source: RLAM and FE, correct as of 31 October 2020. Returns quoted are net of fees.

[1]Please note that the benchmark is priced end-of-day.

[2]The composite benchmark consists of: 30% Barclays UK Government Inflation Linked Bond 1-10 year index, 70% Barclays World Government Inflation Linked Bond (ex UK) 1-10 year index (GBP hedged).

GOVERNMENT BOND MARKET REVIEW

Market highlights

- There was wide variety in the performance of government bond markets in October. While yields generally declined in European markets, they rose slightly in the UK and significantly in the US and Canada. The risk-off sentiment in Europe reflected a backdrop of renewed national lockdowns amid surging Covid-19 case numbers. Although cases also increased sharply in a number of US states, treasury yields rose due to expectations of a 'blue sweep' in the upcoming US elections and better-than-expected economic news. In particular, US GDP jumped 33.1% annualised in the third quarter, leaving output just 2.9% below a year ago. The UK gilt market fluctuated over the month on changing headlines around the Brexit negotiations. Despite the failure to produce an agreement by the EU summit, which had been Prime Minister Johnson's deadline, gilt yields ended the month slightly higher after Brexit talks restarted with an ambition for a deal by mid-November.

Gilts

- The yield on 10-year UK government bonds increased by 3 basis points (bps) to 0.26%. Longer-dated gilts (>15 years) underperformed shorter-dated issues (<5 years). Overall, gilts returned -0.53%, behind sterling investment grade corporate debt (which returned 0.11%). The average sterling investment grade credit spread (the average extra yield available from a corporate bond compared with government debt of equal maturity) narrowed by 6bps to 1.23%.
- Gilts underperformed European government bond markets during the month. This reflected optimism that progress was being made towards a Brexit deal by the end of the year, in spite of volatile headlines and political posturing.
- The yield curve steepened over the month as yields sold off at longer maturities, while the shortest-dated gilts remained relatively pinned where they were.

Index linked gilts

- Index-linked UK government bonds returned 0.65%, outperforming conventional gilts (-0.53%). Returns were strongest for long-dated issues and weakest at shorter maturities. The yield on five-year index-linked gilts declined 4bps to -2.91%, while 10- and 30-year yields increased 3bps and 5bps to -2.96% and -2.24%, respectively.
- The 10-year breakeven (implied) inflation rate increased 6bps to 3.12%. Data releases for September showed that CPI rose from 0.2% to 0.5% annualised and RPI rose from 0.5% to 1.1%. Air fares and second hand car prices contributed to the rise. Most inflation categories contributed negatively, however, and inflation remains well below the Bank of England's target. Brent crude oil dropped 11.25% to around $37 a barrel.

Overseas

- European markets performed relatively strongly over the month versus global bond markets, as yields fell. Renewed national lockdowns in Europe continued to cast doubt over the state of economic recoveries in the region, the European Central Bank (ECB) indicated that it would unveil more easing in December and ECB president Lagarde confirmed that there would be a package of measures to recalibrate the Bank's approach. Additionally, the European Commission announced that it would issue EU SURE 'social bonds' of up to €100bn, giving the proceeds to Member States to alleviate the impacts of the Covid-19 pandemic.
- For a third consecutive month, the US was the worst performing major overseas market, with 10-year treasury yields rising 19bps to 0.87% and the curve steepening. A key driver was the potential, according to polling, of both Biden becoming President and the Democrats taking control of the Senate. Such events were likely to result in a larger stimulus package, driving yields higher, particularly at the longer end. The Democrats had sought a package of $2.2tn during the month, whereas Trump had offered $1.8tn.
- US real yields increased again during the month, after hitting record lows in August, and inflation (as measured by breakevens) continued to recover. 10-year US real yields increased 12bps to -0.84% and the 10-year breakeven rate rose 8bps to 1.71%.

ROYAL LONDON GLOBAL INDEX LINKED BOND FUND

Portfolio commentary

- Net of fees, the fund (M Class, Income) delivered a return of 0.00% in October, apparently marginally underperforming its benchmark (Barclays World Govt Inflation Linked Bonds - £ Hedged), which returned 0.04%. However, the performance of the fund and the index are calculated at different times of day, which affects the comparison. On a like-for-like basis, the fund returned 0.10%, outperforming the benchmark by six basis points (bps). For the year to date, the fund has returned 7.74% on the same like-for-like basis, outperforming the index by 41bps.
- In the UK, index linked gilts (0.65%) outperformed conventional gilts, which returned -0.53%, driven by strong returns for long-dated issues. The main movement was to the curve as higher demand for LDI hedging supported the longer end of the market, while hopes of a Brexit deal supported sterling and weighed on the front end of the market. Breakevens rose modestly across the month particularly at the long end.
- On a cross-market basis, Italy was the strongest market, driven by the surprise move to upgrade its credit outlook from negative to stable, whereas some commentators had expected a downgrade. France and Germany modestly outperformed the UK, while the US underperformed as expectations rose of a Biden presidency and clean sweep by the Democrats.
- Cross-market positions contributed positively to relative performance. We traded tactically, taking positions in Italy, France and the US during the month. French bonds were subsequently sold, but cross-market positions were maintained in the US and Italy. After strong performance, profits were taken in Australian bonds prior to the Reserve Bank of Australia meeting early in November.
- The portfolio's bias to benefit from flatter curves also added value.
- Duration positioning was positive for performance. We traded duration tactically between 0.25 short and 0.25 long.
- No breakeven positions were taken during the month.

Investment outlook

- With intraday volatility remaining high around supply and buyback events and non-market risk events, we will continue to position the fund with a more tactical bias.
- As a result, the fund is positioned close to neutral duration with only a small underweight in the UK. The fund is overweight in European and Japanese bonds as it benefits from hedging these bonds back into sterling.
- Given recent curve flattening and the meeting of the BoE's Monetary Policy Committee in early November, curve positions have been reduced with only a small flattening position. In addition, speculation about a decision on RPI reform in the UK has grown with the announcement of a spending review on 25 November. Our base case is still for change to occur in 2030 with no compensation to investors, but this could keep pressure on the UK market over the next few weeks.
- We still believe UK bonds are relatively expensive, but as we approach the extended deadline for the trade talks between the UK and Europe there is potential for the UK to outperform as investors hedge the risk of 'no deal'. We would anticipate increasing global exposure into any significant widening of spreads.
- The outcome of the US elections will be crucial to treasuries and TIPS. A clean sweep by the Democrats with a majority in the Senate would likely result in a larger stimulus package, driving yields higher, particularly at the longer end. The Democrats had sought a package of $2.2tn during the month, whereas President Trump had offered $1.8tn.
- Otherwise, we are mindful of the strategy review that is currently being undertaken by the ECB. Following the increased flexibility around inflation adopted by the Fed in its revised monetary strategy, we expect the ECB to take a similar approach. We anticipate further currency volatility over coming months, even before the wildcard of the negotiations regarding a post-Brexit trade deal.

Key views within the fund

- Activity remained tactical, given the volatility around Covid-19 lockdowns, the expected extension of the BoE's quantitative easing programme, potential RPI reform and ongoing Brexit talks and the imminent US elections. It centred on tactically trading duration between 0.25 short and 0.25 long, ending the month marginally long.
- Given the sharp flattening of the 25- to 35-year area of the yield curve, we sold shorter into the 10- and 15-year area, where UK index linked 2036s will be auctioned in early November.

ROYAL LONDON GLOBAL INDEX LINKED BOND FUND

- Activity remained tactical, given the volatility around Covid-19 lockdowns, the expected extension of the BoE's quantitative easing programme, potential RPI reform and ongoing Brexit talks and the imminent US elections. It centred on tactically trading duration between 0.25 short and 0.25 long, ending the month marginally long.
- Given the sharp flattening of the 25- to 35-year area of the yield curve, we sold shorter into the 10- and 15-year area, where UK index linked 2036s will be auctioned in early November.

Paul Rayner
Head of Alpha Strategies

Gareth Hill
Fund Manager

ROYAL LONDON INDEX LINKED BOND FUND

Portfolio commentary

- Net of fees, the fund delivered a return of 0.28% in October (M Class, Acc), apparently underperforming the FTSE Actuaries UK Index Linked All index, which returned 0.65%. However, the performance of the fund and the index are calculated at different times of day, which affects the comparison. On a like-for-like basis, the fund returned 0.76%, outperforming the benchmark by 10 basis points. For the year to date, the fund has returned 10.87% on the same like-for-like basis, outperforming the index by 46 basis points.
- Index linked UK government bonds (0.65%) outperformed conventional gilts, which returned -0.53%, driven by strong returns for long-dated issues. This supported the fund's positive absolute returns in October.
- Cross-market positions contributed positively to relative performance. We traded tactically, taking positions in Italy, France and the US during the month.
- The portfolio's bias to benefit from flatter curves also added value.
- Duration positioning was positive for performance. We traded duration tactically between 0.25 short and 0.25 long through the month.
- No breakeven positions were taken during the month.

Investment outlook

- With intraday volatility remaining high around supply and buyback events and non-market risk events, we will continue to position the fund with a more tactical bias.
- As a result, the portfolio is positioned close to neutral duration with limited overseas exposure. Given recent curve flattening and the meeting of the BoE's Monetary Policy Committee in early November, curve positions have been reduced with only a small flattening position – we are short 15-year index linked bonds ahead of the 2036 auction and long 20 years. The fund is also underweight ultra-long bonds relative to the 40-year area.
- In addition, speculation about a decision on RPI reform in the UK has grown with the announcement of a spending review on 25 November. Our base case is still for change to occur in 2030 with no compensation to investors, but this could keep pressure on the UK market over the next few weeks.
- We still believe UK bonds are relatively expensive, but as we approach the extended deadline for the trade talks between the UK and Europe there is potential for the UK to outperform as investors hedge the risk of 'no deal'. We would anticipate increasing global exposure into any significant widening of spreads.
- Otherwise, we are mindful of the strategy review that is currently being undertaken by the ECB. Following the increased flexibility around inflation adopted by the Fed in its revised monetary strategy, we expect the ECB to take a similar approach. We anticipate further currency volatility over coming months, even before the wildcard of the negotiations regarding a post-Brexit trade deal.

Key views within the fund

- Activity remained tactical, given the volatility around Covid-19 lockdowns, the expected extension of the BoE's quantitative easing programme, potential RPI reform and ongoing Brexit talks and the imminent US elections. It centred on tactically trading duration between 0.25 short and 0.25 long, ending the month marginally long.
- Given the sharp flattening of the 25- to 35-year area of the yield curve, we sold shorter into the 10- and 15-year area, where index linked 2036s will be auctioned in early November.
- French, Italian and US index linked bonds were purchased as global spreads widened early in the month. French bonds were subsequently sold, but cross-market positions were maintained in the US and Italy.

Paul Rayner
Head of Alpha Strategies

Craig Inches
Head of Rates and Cash

ROYAL LONDON SHORT DURATION GLOBAL INDEX LINKED BOND FUND

Portfolio commentary

- Net of fees, the fund (M Class, Income) delivered a reported return of -0.18% in October, marginally outperforming its benchmark, which returned -0.22%. However, the performance of the fund and the index are calculated at different times of day, which can affect the comparison. On a like-for-like basis, the fund returned -0.17%, outperforming the benchmark by five basis points (bps). For the year to date, on the same like-for-like basis the fund has returned 3.98%, outperforming the index by 66bps.
- In the UK, index linked gilts (0.65%) outperformed conventional gilts, which returned -0.53%, driven by strong returns for long-dated issues. The main movement was to the curve as higher demand for LDI hedging supported the longer end of the market, while hopes of a Brexit deal supported sterling and weighed on the front end of the market. Breakevens rose modestly across the month particularly at the long end. Higher yields at the short end led to negative absolute returns for the fund.
- On a cross-market basis, Italy was the strongest market, driven by the surprise move to upgrade its credit outlook from negative to stable, whereas some commentators had expected a downgrade. France and Germany modestly outperformed the UK, while the US underperformed as expectations rose of a Biden presidency and clean sweep by the Democrats.
- Cross-market positions contributed positively to relative performance. We traded tactically, taking positions in Italy, France and the US during the month. French bonds were subsequently sold, but cross-market positions were maintained in the US and Italy. After strong performance, profits were taken in Australian bonds prior to the Reserve Bank of Australia meeting early in November.
- Curve trading was light, although we switched longer-dated bonds shorter as the UK curve flattened.
- Duration positioning was positive for performance. We traded duration tactically between 0.25 short and 0.25 long.
- No breakeven positions were taken during the month.

Investment outlook

- With intraday volatility remaining high around supply and buyback events and non-market risk events, we will continue to position the fund with a more tactical bias.
- As a result, the fund is positioned close to neutral duration with only a small underweight in the UK. The fund is overweight in European and Japanese bonds as it benefits from hedging these bonds back into sterling.
- Given recent curve flattening and the meeting of the BoE's Monetary Policy Committee in early November, curve positions have been reduced with only a small flattening position. In addition, speculation about a decision on RPI reform in the UK has grown with the announcement of a spending review on 25 November. Our base case is still for change to occur in 2030 with no compensation to investors, but this could keep pressure on the UK market over the next few weeks.
- We still believe UK bonds are relatively expensive, but as we approach the extended deadline for the trade talks between the UK and Europe there is potential for the UK to outperform as investors hedge the risk of 'no deal'. We would anticipate increasing global exposure into any significant widening of spreads.
- The outcome of the US elections will be crucial to treasuries and TIPS. A clean sweep by the Democrats with a majority in the Senate would likely result in a larger stimulus package, driving yields higher, particularly at the longer end. The Democrats had sought a package of $2.2tn during the month, whereas President Trump had offered $1.8tn.
- Otherwise, we are mindful of the strategy review that is currently being undertaken by the ECB. Following the increased flexibility around inflation adopted by the Fed in its revised monetary strategy, we expect the ECB to take a similar approach. We anticipate further currency volatility over coming months, even before the wildcard of the negotiations regarding a post-Brexit trade deal.

Key views within the fund

- Activity remained tactical, given the volatility around Covid-19 lockdowns, the expected extension of the BoE's quantitative easing programme, potential RPI reform and ongoing Brexit talks and the imminent US elections. It centred on tactically trading duration between 0.25 short and 0.25 long, ending the month marginally long.
- Curve trading was light, although we switched longer-dated bonds shorter as the UK curve flattened.

ROYAL LONDON SHORT DURATION GLOBAL INDEX LINKED BOND FUND

- French, Italian and US index linked bonds were purchased as global spreads widened early in the month. French bonds were subsequently sold, but cross-market positions were maintained in the US and Italy.
- After strong performance, profits were taken in Australian bonds prior to the Reserve Bank of Australia meeting early in November.

Paul Rayner
Head of Alpha Strategies

Gareth Hill
Fund Manager

ROYAL LONDON SHORT DURATION GILT FUND

Portfolio commentary

- Short-dated gilts remained relatively pinned during the month owing to the accommodative policies of the Bank of England. Yields fell for gilts dated less than four years, while they rose at longer maturities. We held a small short duration position in the fund, starting the month around 0.3 years short relative to the FTSE Actuaries UK Conventional Gilts up to five years index and ending around 0.1 years short, which slightly added value overall.
- The fund's curve positioning had little overall effect on relative returns.
- We were underweight gilts on a cross-market basis through our holdings of French and Spanish government bonds. Both outperformed gilts during the month, and therefore the positions were positive for performance. We subsequently took profits on both holdings.
- We tactically traded Australian government debt during the month. We had bought five-year bonds at the end of September which performed well. We then switched them into 10-year Australian government debt which had not done as well, which subsequently outperformed. We held the position thinking that the Reserve Bank of Australia would cut interest rates and extend quantitative easing across the curve at its November meeting.

Investment outlook

- We expect global government bond yields to rise gradually from current levels. In the short-term we think that economic growth will be kept in check by uncertainty around the coronavirus, but already-announced fiscal and monetary policy globally should see economic activity recover over the medium term.
- We continue to look for opportunities to take both tactical and strategic positions in overseas government bonds, where appropriate to the fund's risk and return objectives.
- We continue to believe that both gilt and index-linked real yields do not reflect longer-term fundamentals, and as such, we will maintain a strategic short duration position relative to the benchmark.

Key views within the portfolio

- The portfolio currently has a short duration position relative to its benchmark. We expect a gradual rise in UK government bond yields as the year progresses.
- The fund is positioned for higher yields and slight curve flattening.
- The fund had no overseas exposure at month end, but we continue to look for opportunities to take such positions on a relative basis.
- The portfolio has an allocation to high-quality corporate bonds, which we expect to outperform gilts in a low-yielding environment.
- The portfolio may look to tactically trade index-linked gilts to take advantage of mispricing opportunities. The fund held no exposure to UK inflation over the month.

Craig Inches
Head of Rates and Cash

Ben Nicholl
Fund Manager

ROYAL LONDON UK GOVERNMENT BOND FUND

Portfolio commentary

- There was significant divergence in the performance of global bond markets during October. US treasury yields rose markedly and the curve steepened, driven by expectations of a 'blue sweep' in the upcoming US elections which would be likely to result in higher levels of fiscal stimulus. By contrast, yields dropped and curves flattened in Europe, and peripheral spreads outperformed despite worsening news regarding the spread of Covid-19. The UK gilt market's performance was in between these markets, as the economic fallout from coronavirus, alongside significant event risk in the form of Brexit and RPI reform, continue to weigh on the market.
- In recent months we have shied away from taking a large strategic duration position in the fund, in part due to the significant market event risks that lie ahead in the fourth quarter. These include the US election, the global coronavirus pandemic, Brexit and UK RPI reform. Instead we have looked to tactically trade market volatility, which has been high as a result of these event risks. The fund's relative duration traded around neutral, within a range of 0.25 years short to 0.25 years long relative to the FTSE Actuaries UK Conventional Gilts All Stocks index, ending the month 0.25 years long relative to the benchmark. While the fund's strategic duration positioning did not have a significant effect on performance, given that it was broadly neutral, our tactical trading was a key value driver for the month.
- With regard to yield curve positioning, we held a marginal flattening bias throughout the fund. This had a small detrimental impact upon returns as the yield curve steepened over the month. While longer-dated gilts sold off, front-end gilts remained relatively pinned due to the accommodative policies of the Bank of England.
- We benefitted from the gilt market's underperformance by being slightly underweight gilts on a cross-market basis, having entered the month with a long-held position in Japanese inflation-indexed bonds, as well as holding nominal Italian government bonds. We traded the Italian bonds tactically during the month, which added value. Similarly, we benefitted from buying and selling Spanish government bonds and EU SURE bonds. The latter were issued by the European Commission as 'social bonds', with the proceeds being given to EU members to alleviate the impacts of Covid-19. Finally, we bought 10-year Australian government bonds late in the month based on our view that the Reserve Bank of Australia would cut interest rates, and extend its quantitative easing programme at its November meeting; this neither added nor detracted value during the month.

Investment outlook

- We expect global government bond yields to rise gradually from current levels. In the short term we think that economic growth will be kept in check by uncertainty around the coronavirus, but already-announced fiscal and monetary policy globally should see economic activity recover over the medium term.
- We continue to look for opportunities to take both tactical and strategic positions in overseas government bonds, where appropriate to the fund's risk and return objectives.
- We continue to believe that both gilt and index-linked real yields do not reflect longer-term fundamentals. However, uncertainty remains high and markets are volatile. As such we look to keep overall duration relatively neutral, but add value through trading markets tactically in the short term.

Key views within the fund

- The portfolio's duration is currently 0.25 years long relative to the benchmark, including the impact of cash holdings on duration. This is a short-term tactical view based on overseas holdings, as we expect UK government bond yields to gradually trend higher into year end.
- The fund holds a marginal flattening bias.

ROYAL LONDON UK GOVERNMENT BOND FUND

- The fund has a small overseas exposure, and we continue to look for opportunities to take such positions on a relative basis.
- The portfolio has allocations to high-quality corporate bonds, which we expect to outperform gilts in a low-yielding environment.
- The portfolio may look to tactically trade index-linked gilts to take advantage of mispricing opportunities, but had no exposure to UK inflation at the end of the month.

Craig Inches
Head of Rates and Cash

Paul Rayner
Head of Alpha Strategies

RLAM GLOBAL HIGH YIELD FUND PERFORMANCE

Fund performance

	1 month (%)	Rolling 12 months (%)
RL Global High Yield Bond Fund M Inc	**0.23**	**0.35**
RL Global High Yield Bond Fund Z Inc	**0.23**	**0.59**
IA Sterling High Yield Sector	0.49	-0.25
ICE BofA ML BB-B Global Non-Financial High Yield Constrained Index	0.42	1.72
RL Short Duration Global High Yield Bond Fund A Inc	**0.11**	**-1.60**
RL Short Duration Global High Yield Bond Fund M Inc	**0.15**	**-1.20**
RL Short Duration Global High Yield Bond Fund Z Inc	**0.15**	**-1.10**
IA Sterling High Yield Sector	0.49	-0.25
3 month LIBOR	0.00	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.

Source: RLAM and FE, correct as of 31 October 2020. Returns quoted are net of fees.

GLOBAL HIGH YIELD MARKET REVIEW

Market highlights

- The global high yield market returned 0.42% in October. BB rated bonds outperformed lower-rated issues, with their 0.54% average return comparing to respective returns of 0.21% and -0.09% for B rated debt and bonds rated CCC and lower. Returns were strongest for longer-dated bonds.
- The global high yield market produced a positive return in October. Risk appetite was supported by markets cheering the possibility of a 'blue sweep' in the upcoming US elections, whereby both Biden would become President and the Democrats would take control of the Senate. Such an outcome would likely result in a larger stimulus package, given that the Democrats had sought a $2.2tn package during the month, whereas Trump had offered $1.8tn.
- A significant global resurgence in Covid-19 cases prompted renewed lockdowns in Europe. However, the economic impact of the lockdowns has been less significant than earlier in the year due to policy support from governments and central banks. Consequently, we have not significantly altered our default rate expectations.
- Returns were generally positive across sectors and regions. The automotive sector was the best performer, while basic industry contributed the most to the positive market returns due to its greater weighting. Leisure was the worst performer sector, and the main detractor from market returns. With respect to regions, the UK was the outperformer though contributed the least due to its relatively low weighting, while Europe saw the worst returns.
- Issuance in the high yield market, while down from September, remained at a historically elevated level. The majority of the issuance continued to be BB or B rated and came primarily from the US market.
- The US default rate remained broadly unchanged, which had also been the case the previous month, with the energy and telecommunications sectors still the primary sources. The majority of the defaults were rated CCC and below.

ROYAL LONDON GLOBAL HIGH YIELD BOND FUND

Portfolio commentary

- The fund's Z class returned 0.23%, net of fee, in October, compared with 0.42% for the ICE BofA Merrill Lynch BB-B Global Non-Financial High Yield Constrained Index (100% GBP hedged).
- Index performance during the month was influenced by a positive income return of 0.45%, while the price and hedging returns were -0.02% and -0.01%, respectively.
- The yield-to-worst* on the benchmark ended October at 5.07%, compared with 5.04% at the beginning of the period. The fund yield stood at 6.22% at month end, excluding the impact of cash, and its duration was longer than that of the index.
- The global high yield market produced a positive return in October. Risk appetite was supported by markets cheering the possibility of a 'blue sweep' in the upcoming US elections, whereby both Biden would become President and the Democrats would take control of the Senate. Such an outcome would likely result in a larger stimulus package, given that the Democrats had sought a $2.2tn package during the month, whereas Trump had offered $1.8tn.
- A significant global resurgence in Covid-19 cases prompted renewed lockdowns in Europe. However, the economic impact of the lockdowns has been less significant than earlier in the year due to policy support from governments and central banks. Consequently, we have not significantly altered our default rate expectations.
- Returns were generally positive across sectors and regions. The automotive sector was the best performer, while basic industry contributed the most to the positive market returns due to its greater weighting. Leisure was the worst performer sector, and the main detractor from market returns. With respect to regions, the UK was the outperformer though contributed the least due to its relatively low weighting, while Europe saw the worst returns.
- Issuance in the high yield market, while down from September, remained at a historically elevated level. The majority of the issuance continued to be BB or B rated and came primarily from the US market.
- The fund's overweight exposure to the **Telecommunications** sector was the primary driver of performance at the sector level, while the overweight allocation to **Media** was the biggest drag. **Media** remained the fund's leading overweight sector allocation relative to the benchmark, while **Real Estate** was the main underweight.
- The biggest contributor to the fund's performance was the oil & gas exploration company **Tullow Oil**, which added approximately 7 basis points. The largest detraction from relative performance came from telecommunications conglomerate **Sinclair Broadcast Group**, costing around 14bps.

**Yield-to-worst refers to the redemption date that produces the lowest return.*

Investment outlook

- There is a high level of uncertainty around the global economic growth outlook and the corresponding monetary and fiscal policy responses to be taken. As a result, we expect ongoing volatility in markets, with corporate default rates set to rise.
- However, we continue to believe that global high yield bonds are attractive on a spread basis and that they overcompensate for default risk, while their level of income generation is also appealing on a relative basis.

Key views within the fund

- The fund's objective is to achieve a combination of capital growth and income. The fund seeks to achieve its investment objective by outperforming its benchmark, the BofA Merrill Lynch BB-B Global Non-Financial High Yield Constrained index, 100% hedged to sterling, by 1% per annum over rolling three-year periods.

ROYAL LONDON GLOBAL HIGH YIELD BOND FUND

- The fund seeks to mitigate stock-specific risk by holding a diversified portfolio of investments, so that no individual investment can, in isolation, have an excessive adverse impact on overall fund performance. Currency risk associated with holdings of bonds is hedged through the use of forward currency transactions.
- We expect bouts of market volatility due to market expectations surrounding US Federal Reserve monetary policy. As such, we believe bonds with near-term catalysts, which mitigate market risk, are an important attribute underpinning investment performance over the medium term.

Azhar Hussain
Head of Global High Yield

Stephen Tapley
Global High Yield Senior Fund Manager

ROYAL LONDON SHORT DURATION GLOBAL HIGH YIELD BOND FUND

Portfolio commentary

- The fund's Z class returned 0.15%, net of fee, in October, compared with 0.00% for three-month sterling LIBOR.
- The global high yield market produced a positive return in October. Risk appetite was supported by markets cheering the possibility of a 'blue sweep' in the upcoming US elections, whereby both Biden would become President and the Democrats would take control of the Senate. Such an outcome would likely result in a larger stimulus package, given that the Democrats had sought a $2.2tn package during the month, whereas Trump had offered $1.8tn.
- A significant global resurgence in Covid-19 cases prompted renewed lockdowns in Europe. However, the economic impact of the lockdowns has been less significant than earlier in the year due to policy support from governments and central banks. Consequently, we have not significantly altered our default rate expectations.
- Returns were generally positive across sectors and regions. The automotive sector was the best performer, while basic industry contributed the most to the positive market returns due to its greater weighting. Leisure was the worst performer sector, and the main detractor from market returns. With respect to regions, the UK was the outperformer though contributed the least due to its relatively low weighting, while Europe saw the worst returns.
- Issuance in the high yield market, while down from September, remained at a historically elevated level. The majority of the issuance continued to be BB or B rated and came primarily from the US market. In keeping with the strategy of the fund, we did not participate in any primary issuance, though we view it as a clear indicator of market health.
- The biggest relative contributor to the fund's performance was the pharmaceutical company **Nidda Healthcare**, which added approximately 3 basis points, while the largest detractor was the US pet superstore chain **PetSmart**, which cost around 2 basis points.
- At month-end, the expected yield on the fund was 4.00% (4.02% on an FX-adjusted basis), with an expected maturity of 1.13 years.

Investment outlook

- There is currently a high level of uncertainty around the global economic growth outlook and the corresponding monetary and fiscal policy responses to be taken. As a result, we expect ongoing volatility in markets, with corporate default rates set to rise.
- We continue to believe that short duration global high yield bonds are attractive on a relative and absolute basis and overcompensate for the associated default, illiquidity and volatility risks.

Key views within the fund

- The fund's objective is to provide income. The manager seeks to achieve this by outperforming the benchmark, three-month sterling LIBOR, by 2% per annum over rolling three-year periods.
- The fund is diversified in order to improve overall portfolio liquidity and to reduce the effect on overall fund performance of any deterioration in the creditworthiness of an individual holding.
- We expect bouts of market volatility due to changing market expectations surrounding monetary policy worldwide. As such, we believe companies with strong liquidity characteristics are an important element in underpinning investment performance over the medium term.

Azhar Hussain
Head of Global Credit

Stephen Tapley
Global Credit Fund Manager

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