ROYAL LONDON FIXED INCOME

Fund Manager Commentary – January 2021

For professional clients only, not suitable for retail investors

CONTENTS

ECONOMIC DEVELOPMENTS

Economic developments

- While more transmissible variants of Covid-19 led to tighter restrictions, case numbers generally declined across the US, UK and Europe, as lockdown measures started to prove effective. Meanwhile, the UK vaccination programme made good progress, despite friction with the EU over vaccine exports.
- The extended lockdown impacted UK economic activity with business surveys suggesting a contraction in January with the flash PMI at only 40.6. High frequency data look consistent with a contraction worse than November, but not as deep as April. Following the trade deal with the EU, feared queues at Dover failed to materialise, but there were reports of hold-ups and issues in some sectors. January house prices fell and the RICS survey signalled weaker housing activity levels.
- In the US, the Democrats gained control of Congress, albeit only with a casting vote from Vice President Harris. Markets assumed that greater short-term fiscal support will be offset by higher taxes and more regulation down the line. President Biden proposed a $1.9tn stimulus package, although even some Democrats baulked at the size. US GDP growth slowed to 4.0%Q annualised in the fourth quarter, giving -3.5% GDP growth for 2020.
- In Europe, economic activity was softer again in the fourth quarter with GDP falling 0.7%Q, leaving full-year 2020 GDP growth at -6.8% (-5.0% in Germany, -8.3% in France). Surveys indicated weaker activity in January as some national lockdowns were extended, notably in Germany. The Italian prime minister resigned, which initially worried investors. However, a new government is the most likely outcome, rather than early elections.

RLAM CREDIT FUND PERFORMANCE

Fund performance

	1 month (%)	Rolling 12 months (%)
RL Corporate Bond Fund Z Inc	**-0.36**	**5.07**
IA Sterling Corporate Bond Sector	-0.76	4.28
iBoxx Sterling Non-Gilts All Maturities Index	-0.91	3.99
RL Ethical Bond Fund Z Inc	**-0.49**	**4.61**
IA Sterling Strategic Bond Sector	-0.17	3.87
iBoxx Sterling Non-Gilts All Maturities Index	-0.91	3.99
RL Global Bond Opportunities Fund Z Inc	**0.82**	**2.83**
RL Investment Grade Short Dated Credit Fund Z Inc	**-0.10**	**2.72**
IA Sterling Corporate Bond Sector	-0.76	4.28
ICE BofA ML 1-5 year Sterling Non-Gilt All Stocks Index	-0.03	2.50
RL Short Duration Credit Fund Z Inc	**0.19**	**3.04**
IA Sterling Strategic Bond Sector	-0.17	3.87
ICE BofA ML 1-5 year Sterling Non-Gilt All Stocks Index	-0.03	2.50
RL Sterling Credit Fund Z Inc	**0.14**	**4.92**
IA Sterling Corporate Bond Sector	-0.76	4.28
iBoxx Sterling Non-Gilts All Maturities Index	-0.91	3.99
RL Sterling Extra Yield Bond Fund A Inc	**1.04**	**0.12**
RL Sterling Extra Yield Bond Fund B Inc	**1.00**	**-0.39**
RL Sterling Extra Yield Bond Fund Y Inc	**1.07**	**0.56**
RL Sterling Extra Yield Bond Fund Z Inc	**1.07**	**0.39**
IA Sterling Corporate Bond Sector	-0.76	4.28
IA Sterling High Yield Sector	0.29	3.67
IA Sterling Strategic Bond Sector	-0.17	3.87

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 January 2021. 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 0.20% to 0.33% in January. Sterling investment grade corporate debt returned -0.93%, outperforming UK government bonds (-1.70%). The average sterling investment grade credit spread (the average extra yield available from a corporate bond compared with government debt of equal maturity) tightened 1 basis point from 0.99% to 0.98%.
- Total returns were negative for nearly all sterling credit sectors. Covered bonds outperformed the broad market, along with the wider banks and insurance sectors. Otherwise, supranational bonds outperformed as sentiment turned more cautious. While sub-investment grade bonds delivered positive returns, there was no particular shape to the returns from different ratings as AAA and BBB rated bonds outperformed their AA and A rated peers. However, shorter-dated issues clearly outperformed longer-dated bonds.
- Credit issuance increased sharply in the sterling and euro markets in January following the seasonal slowdown in December and generally lower issuance in the fourth quarter, but was below the levels of a year ago. Issuance came more from the financial sectors in both markets.

ROYAL LONDON CORPORATE BOND FUND

Portfolio commentary

- Net of fees, the fund delivered a return of -0.36% in January (Z class, Income), outperforming the iBoxx Sterling Non-Gilts All Maturities Index, which returned -0.91%, and the -0.76% average return for its peer group (IA Sterling Corporate Bond).
- Total returns were negative for nearly all sterling credit sectors. The outperformance of covered bonds and the insurance sector, particularly subordinated insurance, was positive for performance. The strong returns from the portfolio's sub-investment grade bonds were also beneficial .
- 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 during the month. We bought senior bonds from **MetLife** and **New York Life**, the US life insurance companies; subordinated bonds of **Zurich Insurance**; and a 10-year senior issue from **BNP Paribas**. We also bought a longer-dated bond from **Great Places**, a housing association with over 19,000 homes mostly in North West England, and a tap of a structured issue from **Thames Water**.
- Our secondary market activity primarily focused on managing liquidity and switching between different bonds of issuers to enhance terms, mainly to longer-dated bonds. We switched holdings in **Barclays**, **HSBC**, **Intercontinental Hotels Group** and structured bonds of **Gatwick Airport**. We also sold senior **RBS** debt to fund the **BNP Paribas** new issue. Otherwise, we added to holdings of **Tesco Property** structured bonds and **Vodafone**. To raise liquidity, we reduced our holding of APT Pipelines, which also lowered the carbon intensity of the fund, and sold bonds of **Digital Stout** following good performance as we prefer secured bonds in the real estate sector.
- No bonds were called away or tendered from the portfolio.

Investment outlook

- Viral mutations and extended lockdown measures have jeopardised the economic recovery in the short term and rising unemployment seems likely. Against this, the positive start for the UK vaccination programme raises hopes of a return to more normal social and economic conditions later this year. However, 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 central banks.
- 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 still 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, although the magnitude of this outperformance is expected to be lower than our previous projections.

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.
- 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

- Net of fees, the fund (Z class, Income) delivered a return of -0.49% in January. This compares to the -0.91% 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 -0.17% and -0.76%, 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.
- Total returns were negative for nearly all sterling credit sectors. The outperformance of the financials sectors, particularly subordinated banks and insurance, was positive for performance. The strong returns from the portfolio's sub-investment grade bonds were also beneficial.
- 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 six new issues during the month. We bought senior bonds from **MetLife** and **New York Life**, the US life insurance companies. We also bought a longer-dated bond from **Great Places**, a housing association with over 19,000 homes mostly in North West England; a tap of a structured issue from **Thames Water**; a tap of **Retail Charity Bonds** in the social housing sector, which provides unsecured loan finance for charities; and bonds of **Deutsche Bahn**, the public transport operator.
- Secondary market activity focused on the banks, insurance, social housing and structured sectors. Purchases included senior debt of **Deutsche Bank**, **BNP Paribas** and **3i**, and additional tier 1 bonds of **HSBC**. We also bought subordinated debt of **Virgin Money** and **Wells Fargo** in the banks sector, and **M&G** and **JRP Group** in the insurance sector. We also switched between different bonds of **Legal & General** to enhance terms. In social housing, we bought bonds of **London and Quadrant** and **A2Dominion**, and sold bonds of **Clarion Funding**; and bought commercial mortgage-backed securities of **Cold Finance** in the structured sector. Other notable trades included buying bonds of **GE Capital**, **Eversholt Capital** and **SSE**, and selling bonds of **GlaxoSmithKline**.

Investment outlook

- Viral mutations and extended lockdown measures have jeopardised the economic recovery in the short term and rising unemployment seems likely. Against this, the positive start for the UK vaccination programme raises hopes of a return to more normal social and economic conditions later this year. However, 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 central banks.
- 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 still 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, although the magnitude of this outperformance is expected to be lower than our previous projections.

Key views within the fund

- The fund is diversified 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. We believe the level of gilt yields will be challenging over the longer term.
- 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.

ALPHA MANAGER 2020
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 0.82% in January. Returns across the credit universe generally flat or slightly negative, driven more by weakness in government bond yields than credit spread movements. Fund performance was aided by short duration positioning as well as its exposure to the energy sector, which performed well.
- Distributions payable at the end of February were 1.35p.

Market highlights

Index	Total return (%)	Spread movement (basis points)
AT1 **ICE BofA ML contingent capital index**	0.11%	-4
HY global non-financial corps **ICE BofA ML global non-financial high yield index**	0.14%	-6
HY global non-financial hybrid corps **ICE BofA ML global hybrid non-financial high yield index**	-0.10%	6
HY non-financial emerging markets **ICE BofA ML emerging markets high yield ex. subordinated financial index**	-0.32%	10
IG global non-financial hybrid corps **ICE BofA ML global hybrid non-financial corporate index**	-0.14%	6
Dollar investment grade corporate bonds **ICE BofA ML US corporate index**	-1.23%	-1
Sterling investment grade corporate bonds **ICE BofA ML sterling corporate and collateralised index**	-1.05%	0
Euro investment grade corporate bonds **ICE BofA ML euro corporate and Pfandbriefe index**	-0.13%	0

Source: Bloomberg

- While more transmissible variants of Covid-19 led to tighter restrictions, case numbers generally declined across the US, UK and Europe, as lockdown measures started to prove effective. In the US, the Democrats gained control of Congress, albeit only with a casting vote from Vice President Harris. Markets assumed that greater short-term fiscal support will be offset by higher taxes and more regulation down the line. President Biden proposed a $1.9tn stimulus package, although even some Democrats baulked at the size.
- The global high yield market produced a flat return in January. Spreads were largely unchanged for the overall index, but the positive impact from the carry on high yield bonds was offset by increased government bond yields over the month. Returns were mixed across market index sectors. The energy sector, the largest in the high yield universe, produced negative returns over the month, as did real estate, while other major sectors such as healthcare, media and telecoms produced positive returns. Generally speaking, lower rated debt such as CCC rated bonds outperformed higher rated BB and B rated debt. UK was the strongest performing region, with modest gains for both the US and Europe, while emerging market high yield saw negative returns.
- Issuance in the high yield market was relatively buoyant in January and significantly higher than during the same month in 2020. The majority of issuance continued to be BB or B rated, with an even split between the two. Issuance came overwhelmingly from the US market, with European high yield issuance materially lower, albeit also higher than the same month last year.

Portfolio commentary

- In a month where index performance was driven more by underlying government bond weakness than credit spread movements, the fund's duration positioning was positive for returns. The fund's weighted average duration is just 3.4 years. In terms of credit exposure, our exposure to energy was positive, as our holdings in oil-related companies saw gains on back of WTI rising from $48 to $52 – names such as **Sand Hill Petroleum** and offshore drilling contractor **Vantage Drilling** performing well.
- Activity in the month was relatively light. The fund participated in new US dollar issues of **Standard Chartered Bank** and **Zurich Insurance** - the former sold shortly after purchase at a modest profit, as well as a new issue from **Nippon**

ROYAL LONDON GLOBAL BOND OPPORTUNITIES FUND

Life at an attractive yield. Short dated unsecured bonds of shipping company **Golar LNG** were sold after recent strong performance, while we also took profits on utilities **Edison International** and **Drax**.

Investment outlook

- Global economies may be jeopardised by recent lockdown measures and rising unemployment seems likely. While the positive developments regarding a vaccine rollout may allow societies to return to more normal conditions next year, 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 central banks.
- 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).

CITYWIRE +

Rachid Semaoune
Senior Fund Manager

ALPHA MANAGER 2020
Eric Holt

CITYWIRE +

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 January, against the -0.03% gross return of the ICE BofA Merrill Lynch 1-5 Year Sterling Non-Gilt Index and the -0.76% average return of the wider all-maturities sector (IA Sterling Corporate Bond).
- Total returns were negative for nearly all sterling credit sectors. The outperformance of covered bonds and the financials sectors, particularly subordinated insurance and banks, was positive for performance. The strong returns from the portfolio's lower-rated bonds (BBB) were also beneficial.
- 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 two new issues during the month, buying senior bonds from **MetLife** and **New York Life**, the US life insurance companies.
- Our secondary market activity primarily focused on managing liquidity and switching between different bonds of issuers to enhance terms, mainly to longer-dated bonds. We switched between senior issues of **Barclays** and **Lloyds Banking Group**, and otherwise bought senior bonds of of **CYBG** (the holding company of Clydesdale Bank), **Royal Bank of Scotland**, **Investec**, **Wells Fargo**, **BFCM** and **3i**. We also bought senior bonds of **Yorkshire Building Society** and **Coventry Building Society** as well as lower tier 2 (LT2) bonds of **Leeds Building Society**. We also added to our holding of short-dated covered bonds of **Co-operative Bank**. In the insurance sector, we bought LT2 bonds of **Legal & General** and **Aviva**, and tier 1 bonds of **AXA**. We also bought bonds in the social housing sector (**A2d Funding** and **Haven Funding**) and structured bonds of **Heathrow Funding** and **Lanark Master Issuer**. Other notable purchases included attractively-priced bonds of **Volkswagen Financial Services** and a new position in **E.On International Finance** to diversify further the portfolio. Against these purchases, we sold only some LT2 bonds of **Direct Line Insurance**, taking profits following strong performance.
- Bonds of **Friary No 3** were called away from the portfolio.

Investment outlook

- Viral mutations and extended lockdown measures have jeopardised the economic recovery in the short term and rising unemployment seems likely. Against this, the positive start for the UK vaccination programme raises hopes of a return to more normal social and economic conditions later this year. However, 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 central banks.
- 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 still 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, although the magnitude of this outperformance is expected to be lower than our previous projections.

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.

ROYAL LONDON INVESTMENT GRADE SHORT DATED CREDIT FUND

- Duration is in line with 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).

Paola Binns
Senior Fund Manager

ROYAL LONDON SHORT DURATION CREDIT FUND

Portfolio commentary

- Net of fees, the fund delivered a return of 0.19% in January (Z class, Income), outperforming the ICE BofA Merrill Lynch 1-5 Year Sterling Non-Gilt All Stocks Index, which returned -0.03%, and the -0.17% average return for its peer group (IA Sterling Strategic Bond sector).
- Total returns were negative for nearly all sterling credit sectors. The outperformance of covered bonds and the insurance sector, particularly subordinated insurance, was positive for performance. The strong returns from the portfolio's sub-investment grade bonds also benefited relative performance.
- 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 three new issues during the month. We bought senior bonds from **MetLife**, the US life insurance company; a tap of a structured issue from **Thames Water**; and a tap of **Retail Charity Bonds** in the social housing sector, which provides unsecured loan finance for charities.
- In the secondary market, we added to our financials exposure by buying senior bonds of **Intermediate Capital Group**, additional tier 1 bonds of **Barclays** and lower tier 2 bonds of **Investec Bank**. We also added to our holding of short-dated covered bonds of **Co-operative Bank**. We switched between senior issues of **Lloyds Banking Group** to extend the term by a year and enhance the yield. Otherwise, we added to **Scottish American Investment Trust** and bought short-dated bonds in **First Hydro**, the hydro-electric utility, while selling bonds of **Northern Ireland Electricity**.

Investment outlook

- Viral mutations and extended lockdown measures have jeopardised the economic recovery in the short term and rising unemployment seems likely. Against this, the positive start for the UK vaccination programme raises hopes of a return to more normal social and economic conditions later this year. However, 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 central banks.
- 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 still 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, although the magnitude of this outperformance is expected to be lower than our previous projections.

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 slightly 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.

CITYWIRE A

Paola Binns
Senior Fund Manager

Rayner Spencer Mills R RATED FUND

ROYAL LONDON STERLING CREDIT FUND

Portfolio commentary

- Net of fees, the fund delivered a return of 0.14% in January (Z class, Income), outperforming the iBoxx Sterling Non-Gilts All Maturities Index, which returned -0.91%, and the -0.76% average return for its peer group (IA Sterling Corporate Bond).
- Total returns were negative for nearly all sterling credit sectors. The outperformance of covered bonds and the insurance sector, particularly subordinated insurance, was positive for performance. The strong returns from the portfolio's sub-investment grade bonds also benefited relative performance.
- 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 six new issues during the month. We bought senior bonds from **New York Life**, the US life insurance company; additional tier 1 (AT1) bonds of **Standard Chartered**; subordinated bonds of **Zurich Insurance**; and a 10-year senior issue from **BNP Paribas**. We also bought a longer-dated bond from **Great Places**, a housing association with over 19,000 homes mostly in North West England, and a tap of a structured issue from **Thames Water**.
- Our secondary market activity primarily focused on managing liquidity and duration. We also switched between issues to longer-dated bonds of **Intercontinental Hotels Group** to enhance terms. We added to the AT1 holding of **CYBG**, the holding company of Clydesdale Bank, and bought short-dated bonds of **SGSP (Australia)**, which owns energy and utility infrastructure assets in Australia. Otherwise, to raise liquidity, we reduced our holdings of **GlaxoSmithKline**, **Equinor**, **Credit Agricole** and **Scottish Hydro**. We also sold bonds of **Digital Stout** following good performance as we prefer secured bonds in the real estate sector; and sold **Global Switch** real estate bonds.
- No bonds were tendered or called away from the portfolio.

Investment outlook

- Viral mutations and extended lockdown measures have jeopardised the economic recovery in the short term and rising unemployment seems likely. Against this, the positive start for the UK vaccination programme raises hopes of a return to more normal social and economic conditions later this year. However, 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 central banks.
- 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 still 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, although the magnitude of this outperformance is expected to be lower than our previous projections.

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.
- Duration moderately below the benchmark. We believe the level of gilt yields will be challenging over the longer term.
- 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 A, B, Y and Z class shares recorded returns of 1.04%, 1.00%, 1.07% and 1.06% respectively in January.
- After the sharp fall in gilt yields in 2020, with the all maturities index yield falling from 0.95% to 0.33% – the main influence behind 2020's high index returns for gilts and sterling investment grade corporate bonds of 8.84% and 7.96% respectively, there was a partial reversal in January. The gilt all maturities index yield rose from 0.33% to 0.44% in the month, corresponding to a -1.76% index return in January. Sterling investment grade corporate bonds held up better, with an index return of -0.92% in the month, reflecting their shorter average duration than gilts – the average yield differential between the asset classes was 0.99% at the start and end of the month. Within sterling investment grade corporate bonds the financial sectors of banks and insurance held up relatively well, in part reflecting their higher yields, with the bank 'Tier 1' index, comprising the most junior tier of bank capital, the sole sector in the asset class to post a positive return in the month, of +0.78%. Similarly the European and global sub investment grade indices posted returns of 0.42% and 0.19% in January, being fairly immune to the rise in government bond yields and benefitting from income generation – the yields on these two indices being 2.78% and 4.28% respectively at end January.
- There were a number of influences supporting the overall performance of the fund in January. The fund has relatively modest exposure to the uptick in gilt yields in the month, and while a number of holdings in the fund edged lower in price in the month, this was partially or wholly offset by robust income accrual. Financials generally held up very well, with holdings of banks **Barclays** and **Santander** posting returns of 2% and 3% respectively, bonds of building societies **Nationwide** and **Skipton** up 2% and 3% respectively – the former up 11% in price since issue last June, insurer **Just Group** up 4% and bonds of asset management business **Jupiter** up 3%. Secured bonds in shipping, mostly issued in 2017 when assets and financing was migrating from banks to new owners financing in bond markets, performed well in January as shipping rates improved – bonds of **Borealis**, **Eagle Bulk**, **MPC Containerships** and **Songa Container** each posted returns of 2-3% in the month, while still offering yields around 7% on these secured bonds. Finally the rise in the oil price, extending its recent upward trend and increasing from $51.8 to $55.9 in January, supported the prices of many of the fund's investments in the energy sector. For example the prices of bonds of **Independent Oil & Gas** and **Siccar Point Energy**, each operating in the highly regulated UK North Sea sector, were up 8% and 5% respectively in the month.
- Activity in the month was relatively light. The fund participated in new US dollar issues of **Standard Chartered Bank** and **Zurich Insurance** - the former sold shortly after purchase at a modest profit, and in a new sterling denominated, secured bond of specialist mortgage lending business **Together**. Short dated unsecured bonds of shipping companies **Golar LNG** and **Stolt Neilsen** were sold after recent strong performance. Finally, activity in short dated gilts reflected efficient liquidity management in the fund during the month.

Investment outlook

- Viral mutations and extended lockdown measures have jeopardised the economic recovery in the short term and rising unemployment seems likely. Against this, the positive start for the UK vaccination programme raises hopes of a return to more normal social and economic conditions later this year. However, 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 central banks.
- 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 still 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, although the magnitude of this outperformance is expected to be lower than our previous projections.

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.

Rachid Semaoune
Senior Fund Manager

Eric Holt
Head of Credit

RLAM GOVERNMENT BOND FUND PERFORMANCE

Fund performance

	1 month (%)	Rolling 12 months (%)
RL Global Index Linked Bond Fund Z Inc	**-0.41**	**5.70**
IA Global Bonds Sector	-0.69	4.03
Barclays World Government Inflation-Linked Bond Index (hedged)	-0.74	5.32
RL Index Linked Bond Fund M Inc	**-2.66**	**3.36**
IA UK Index Linked Gilts Sector	-2.76	3.42
FTSE Actuaries UK Index-Linked All Stocks Index	-3.05	3.38
RL Short Duration Gilt Fund Z Inc	**-0.10**	**0.96**
IA UK Gilts Sector	-1.64	2.89
FTSE Actuaries UK Conventional Gilts up to 5 Years Index	-0.13	1.09
RL Short Duration Global Index Linked Bond Fund Z Inc	**0.45**	**4.32**
IA Global Bonds Sector	-0.69	4.03
RL Short Duration Global Index Linked Composite Benchmark[1 2]	0.35	3.60
RL UK Government Bond Fund Z Inc	**-1.59**	**3.29**
IA UK Gilts Sector	-1.64	2.89
FTSE Actuaries UK Conventional Gilts All Stocks Index	-1.70	2.80

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 January 2021. 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

- While yields rose across all leading bond markets in January, there was some divergence in performance. Yields rose more significantly in the UK, US and Canada. The UK made good progress with its vaccination programme, raising hopes of a route out of lockdown by April or May. The relative lack of disruption from a 'no deal' Brexit or extensive delays at borders was also a positive, despite weak hard data.
- In the US, the Democrats gained control of Congress following the Georgia Senate runoffs, albeit only with a casting vote from Vice President Harris, driving up treasury yields to their highest level since March 2020. Investors inferred that greater fiscal support in the short term will be offset by higher taxes and more regulation down the line. President Biden proposed a $1.9tn stimulus package.
- The risk-off sentiment in Europe reflected extended national lockdowns with new strains of Covid-19, but without the optimism of a fast rollout of vaccination programmes. Matteo Renzi's resignation from the Italian government was followed by Prime Minister Conte's resignation. While a new government remains the most likely outcome, rather than early elections, investors initially reacted negatively to the return of political uncertainty. However, the spread between Italian and German government bonds narrowed again by month end.

Gilts

- The yield on 10-year UK government bonds increased by 13 basis points (bps) to 0.33%. Longer-dated gilts (>15 years) underperformed shorter-dated issues (<5 years). Overall, gilts returned -1.70%, lagging sterling investment grade corporate debt (which returned -0.93%). 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 1bp to 0.98%.
- Gilts underperformed European government bond markets during the month as the UK made good progress with its vaccination programme, raising hopes of a route out of lockdown by April or May. In contrast, the EU's programme seems less well coordinated and has struggled to source vaccine supplies.
- 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 -3.05%, underperforming conventional gilts (-1.70%). Returns were positive for short-dated issues (<5 years), but negative for longer-dated issues. The yield on five-year index-linked gilts declined 19bps to -3.02%, while 10- and 30-year yields increased 1bp and 17bps to -2.89% and -2.15%, respectively.
- The 10-year breakeven (implied) inflation rate increased 11bps to 3.11%. UK headline CPI inflation rose to 0.6%Y from 0.3%Y in December. However, there isn't much evidence of an inflation trend yet, and some of the more noisy elements of CPI were behind the rise (e.g. clothing). VAT is set to rise again on 1 April. Headline inflation will also get a mechanical boost from positive energy price base effects as Brent crude oil rose 8.8% to nearly $56 a barrel.

Overseas

- While yields rose, European markets were relatively strong over the month versus global bond markets. Extended national lockdowns in Europe, notably in Germany, continued to cast doubt over the state of economic recoveries in the region. Economic activity was softer in the fourth quarter with GDP falling 0.7%Q, leaving full-year 2020 GDP growth at -6.8% (-5.0% in Germany and -8.3% in France). Business surveys indicated weaker activity in January.
- The US was again one of the weaker major overseas markets, with 10-year treasury yields rising 15bps to 1.07%. Victory in the Georgia Senate runoffs gave the Democrats control of Congress. Investors believe this will lead to greater stimulus in the short term offset by higher taxes in future, along with more regulation.
- US real yields increased again during the month, after hitting record lows last August, and inflation expectations (as measured by breakevens) continued to rise. The 10-year US real yield increased to -1.04% (+5bps) and the 10-year breakeven rate rose 12bps to 2.10%.

ROYAL LONDON GLOBAL INDEX LINKED BOND FUND

Portfolio commentary

- Net of fees, the fund delivered a return of -0.41% in January (M Class, Income), outperforming its benchmark (Barclays World Govt Inflation Linked Bonds - £ Hedged), which returned -0.74%. 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 outperformed by 11 basis points, returning -0.63%.
- Yields rose sharply during the month through a combination of increased confidence that Covid-19 vaccines will lead to a strong recovery in the second half of 2021, and the Georgia Senate runoffs leading to expectations of more fiscal stimulus in the US.
- Cross-market positions made a positive contribution to performance. The UK underperformed other global markets because the legacy of the trade deal negotiations with the EU hung over the market, sterling strength put pressure on UK relative real yields and expectations of increased linker supply in 2021. We were overweight global markets against the UK.
- The yield curve marginally detracted from performance as the curve steepened against our slight bias towards flattening.
- Duration was tactically traded around flat as we feel there is still some uncertainty around the shorter-term impact of vaccines, while markets have generally embraced the global reflation trade. Duration made a small positive contribution.
- With the 2051 index linked syndication coming, we started to sell index-linked 2046s into conventional 2046s to take advantage of the impact of additional supply. This started with the 2046 conventional syndication during the month. However, breakeven positions made a minimal contribution to performance.

Investment outlook

- We believe that UK real yields remain expensive on a legacy Brexit basis. However, these factors could be sustained for some time if cross-border frictions (such as paperwork and VAT issues) affect imports and pension industry technical factors continue to drive the market. On a global basis, following the Georgia Senate runoffs, US bond markets are discounting higher inflation with US breakevens rising to three-year highs, having reached just 20bps in the initial crisis last year.
- The success of vaccine programmes may be less definitive than seems to be the case, however, with new strains of the virus emerging and the ongoing challenges of rolling out mass vaccination programmes. Similarly, while the balance of power in the Senate has shifted, we feel that the need for pragmatism will limit more radical spending and reforms.
- The first half of 2020 will remain volatile due to the conflict between extended lockdowns and the successful rollout of the vaccine, and this volatility could be amplified by base effects compared to 2020. We believe yields are likely to be higher by the end of the year and will use any strength to reduce duration in the funds and to increase global index linked exposure.
- 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. ECB president Christine Lagarde has openly discussed average inflation targeting. The euro was notably strong against the dollar last quarter and, although this reversed somewhat in January, we anticipate further currency volatility over coming months.

Key views within the fund

- Activity remained fairly tactical, given the volatility around new strains of Covid-19, high expectations of vaccination programmes, the impact of post-trade deal frictions on supply chains and US political developments.
- While derisking into year end with the uncertainty around the UK-EU trade talks, we remained overweight in global markets against the UK. The UK looked vulnerable because the legacy of the trade deal negotiations with the EU hung over the market with supply chain concerns, sterling strength put pressure on UK relative real yields and expectations of increased linker supply in 2021. Early in the month, we bought Spain, Italy, Canada and Germany against the UK. Having taken profits in Italy (with the political volatility) and some in Canada, we remain long Germany , Spain and Canada; and also have a small short in the US, where we feel inflation now looks expensive having bounced so far from last year's lows.

ROYAL LONDON GLOBAL INDEX LINKED BOND FUND

- Despite our concerns about the UK, we bought very short-dated linkers (2022s and 2024s) at the start of the month as we feel there is a risk of higher short-term inflation through import disruptions and oil price base effects. These were the only UK linkers where the prices rose over the month.
- We maintained a slight bias towards a flattening of the yield curve.
- Duration was tactically traded around neutral as we feel there is still some uncertainty around the shorter-term impact of vaccines, while markets have generally embraced the global reflation trade.
- On breakevens, with the 2051 index linked syndication coming, we started to sell linker 2046s into conventional 2046s to take advantage of the impact of additional supply. This started with the 2046 conventional syndication during the month.

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 -2.66% in January (M Class, Inc), outperforming the FTSE Actuaries UK Index Linked All index, which returned -3.05%. 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 -2.98%, outperformance of 7 basis points.
- Yields rose sharply during the month through a combination of increased confidence that Covid-19 vaccines will lead to a strong recovery in the second half of 2021, and the Georgia Senate runoffs leading to expectations of more fiscal stimulus in the US.
- Cross-market positions made a positive contribution to performance. The UK underperformed other global markets because the legacy of the trade deal negotiations with the EU hung over the market, sterling strength put pressure on UK relative real yields and expectations of increased linker supply in 2021. We were overweight global markets against the UK.
- The yield curve marginally detracted from performance as the curve steepened against our slight bias towards flattening.
- Duration was tactically traded around flat as we feel there is still some uncertainty around the shorter-term impact of vaccines, while markets have generally embraced the global reflation trade. Duration made a small positive contribution.
- With the 2051 index linked syndication coming, we started to sell index-linked 2046s into conventional 2046s to take advantage of the impact of additional supply. This started with the 2046 conventional syndication during the month. However, breakeven positions made a minimal contribution to performance.

Investment outlook

- We believe that UK real yields remain expensive on a legacy Brexit basis. However, these factors could be sustained for some time if cross-border frictions (such as paperwork and VAT issues) affect imports and pension industry technical factors continue to drive the market. On a global basis, following the Georgia Senate runoffs, US bond markets are discounting higher inflation with US breakevens rising to three-year highs, having reached just 20bps in the initial crisis last year.
- The success of vaccine programmes may be less definitive than seems to be the case, however, with new strains of the virus emerging and the ongoing challenges of rolling out mass vaccination programmes. Similarly, while the balance of power in the Senate has shifted, we feel that the need for pragmatism will limit more radical spending and reforms.
- The first half of 2020 will remain volatile due to the conflict between extended lockdowns and the successful rollout of the vaccine, and this volatility could be amplified by base effects compared to 2020. We believe yields are likely to be higher by the end of the year and will use any strength to reduce duration in the funds and to increase global index linked exposure.
- 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. ECB president Christine Lagarde has openly discussed average inflation targeting. The euro was notably strong against the dollar last quarter and, although this reversed somewhat in January, we anticipate further currency volatility over coming months.

Key views within the fund

- Activity remained fairly tactical, given the volatility around new strains of Covid-19, high expectations of vaccination programmes, the impact of post-trade deal frictions on supply chains and US political developments.
- While derisking into year end with the uncertainty around the UK-EU trade talks, we remained overweight in global markets against the UK. The UK looked vulnerable because the legacy of the trade deal negotiations with the EU hung over the market with supply chain concerns, sterling strength put pressure on UK relative real yields and expectations of increased linker supply in 2021. Early in the month, we bought Spain, Italy, Canada and Germany against the UK. Having taken profits in Italy (with the political volatility) and some in Canada, we remain long Germany , Spain and Canada.

ROYAL LONDON INDEX LINKED BOND FUND

- Despite our concerns about the UK, we bought very short-dated linkers (2022s and 2024s) at the start of the month as we feel there is a risk of higher short-term inflation through import disruptions and oil price base effects. These were the only UK linkers where the prices rose over the month
- We maintained a slight bias towards a flattening of the yield curve.
- Duration was tactically traded around neutral as we feel there is still some uncertainty around the shorter-term impact of vaccines, while markets have generally embraced the global reflation trade.
- On breakevens, with the 2051 index linked syndication coming, we started to sell linker 2046s into conventional 2046s to take advantage of the impact of additional supply. This started with the 2046 conventional syndication during the month.

Paul Rayner
Head of Alpha Strategies

Ben Nicholl
Fund Manager

ROYAL LONDON SHORT DURATION GLOBAL INDEX LINKED BOND FUND

Portfolio commentary

- Net of fees, the fund delivered a reported return of 0.45% in January (M Class, Income), outperforming its composite benchmark, which returned 0.35%. 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 outperformed by 6 basis points, returning 0.41%.
- Yields rose sharply during the month through a combination of increased confidence that Covid-19 vaccines will lead to a strong recovery in the second half of 2021, and the Georgia Senate runoffs leading to expectations of more fiscal stimulus in the US.
- Cross-market positions made a positive contribution to performance. The UK underperformed other global markets because the legacy of the trade deal negotiations with the EU hung over the market, sterling strength put pressure on UK relative real yields and expectations of increased linker supply in 2021. We were overweight global markets against the UK.
- The yield curve marginally detracted from performance as the curve steepened against our slight bias towards flattening.
- Duration was tactically traded around flat as we feel there is still some uncertainty around the shorter-term impact of vaccines, while markets have generally embraced the global reflation trade. Duration made a small positive contribution.
- No breakeven positions were held during the month.

Investment outlook

- We believe that UK real yields remain expensive on a legacy Brexit basis. However, these factors could be sustained for some time if cross-border frictions (such as paperwork and VAT issues) affect imports and pension industry technical factors continue to drive the market. On a global basis, following the Georgia Senate runoffs, US bond markets are discounting higher inflation with US breakevens rising to three-year highs, having reached just 20bps in the initial crisis last year.
- The success of vaccine programmes may be less definitive than seems to be the case, however, with new strains of the virus emerging and the ongoing challenges of rolling out mass vaccination programmes. Similarly, while the balance of power in the Senate has shifted, we feel that the need for pragmatism will limit more radical spending and reforms.
- The first half of 2020 will remain volatile due to the conflict between extended lockdowns and the successful rollout of the vaccine, and this volatility could be amplified by base effects compared to 2020. We believe yields are likely to be higher by the end of the year and will use any strength to reduce duration in the funds and to increase global index linked exposure.
- 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. ECB president Christine Lagarde has openly discussed average inflation targeting. The euro was notably strong against the dollar last quarter and, although this reversed somewhat in January, we anticipate further currency volatility over coming months.

Key views within the fund

- Activity remained fairly tactical, given the volatility around new strains of Covid-19, high expectations of vaccination programmes, the impact of post-trade deal frictions on supply chains and US political developments.
- While derisking into year end with the uncertainty around the UK-EU trade talks, we remained overweight in global markets against the UK. The UK looked vulnerable because the legacy of the trade deal negotiations with the EU hung over the market with supply chain concerns, sterling strength put pressure on UK relative real yields and expectations of increased linker supply in 2021. Early in the month, we bought Spain, Italy, Canada and Germany against the UK. Having taken profits in Italy (with the political volatility) and some in Canada, we remain long Germany , Spain and Canada; and also have a small short in the US, where we feel inflation now looks expensive having bounced so far from last year's lows.

ROYAL LONDON SHORT DURATION GLOBAL INDEX LINKED BOND FUND

- At the start of the month, we were overweight the 0-5 years area of the curve in the US and Germany. This section of the curve really benefitted from the global reflation story, so we took profits and shifted to underweight 5-year US and 3-year Germany, buying 10-year Germany and US.
- Despite our concerns about the UK, we bought very short-dated linkers (2022s and 2024s) at the start of the month as we feel there is a risk of higher short-term inflation through import disruptions and oil price base effects. These were the only UK linkers where the prices rose over the month.
- We maintained a slight bias towards a flattening of the yield curve.
- Duration was tactically traded around neutral as we feel there is still some uncertainty around the shorter-term impact of vaccines, while markets have generally embraced the global reflation trade.

Paul Rayner
Head of Alpha Strategies

Gareth Hill
Fund Manager

ROYAL LONDON SHORT DURATION GILT FUND

Portfolio commentary

- Gilt yields rose and curves steepened with the selloff being led by bonds with a maturity over 10 years. Vaccination programmes increased market confidence in a route out of lockdowns by April or May and markets sought to price in the potential for an economic recovery in the second half of the year. In addition, the Democrats' success in the Georgia Senate runoffs suggested increased fiscal support for the US economy, albeit with the risk of higher taxes and increased regulation down the line. This added momentum to the global reflation trade, which had already been evidenced by increased supply-chain costs, and with positive base effects as oil prices continue to rise.
- We ran duration 0.25 years short relative to the benchmark, which was beneficial for performance in a rising yield environment. In addition to this, the fund switched from a long-held flattening position into a 2/5 steepener (i.e. underweight 5-year and overweight 2-year maturity bonds) during the middle of the month.
- The fund was also heavily overweight the lowest coupon bonds in each maturity bucket. The lowest coupon bonds were issued last year at a yield premium to surrounding bonds. With many of these bonds approaching the end of their issuance cycle, they have started to outperform.
- In cross-market positions, we bought 10-year Spain against 5-year gilts.
- Late last year the fund bought T-bills, as they offered a better yield than very short-dated (<12m) gilts. While T-bills have risen a little in yield, very short dated gilts have risen by more so this has been beneficial to the fund. Overall the fund has around 6% in T-bills
- The fund's highly-rated sterling credit exposure, which we hold primarily as a means of enhancing the portfolios yield continues to be run close to its maximum limit of 5%. These positions are predominantly AAA rated, secured, floating rate notes and should provide the fund with some additional protection in a rising yield environment.

Investment outlook

- We expect global government bond yields to rise further from current levels. In the short term, economic growth will be kept in check by uncertainty around new strains of Covid-19 and the ongoing success of the vaccination programmes, but global fiscal and monetary policy should see economic activity recover sharply 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, so these effects could be sustained for some time. 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 currently has a short duration position relative to its benchmark. We expect a rise in UK government bond yields as the year progresses.
- The fund is positioned for higher yields and curve steepening as the curve had become far too flat at the front end.
- The fund has limited overseas exposure at month end through 10-year Spain against 5-year gilts and 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

- Gilt yields rose across the curve over the month, particularly for longer maturity bonds as curves steepened. Vaccination programmes increased market confidence in a route out of lockdowns by April or May and markets sought to price in the potential for an economic recovery in the second half of the year. In addition, the Democrats' success in the Georgia Senate runoffs suggested increased fiscal support for the US economy, albeit with the risk of higher taxes and increased regulation down the line. This added momentum to the global reflation trade, which had already been evidenced by increased supply-chain costs, and with positive base effects as oil prices continue to rise.
- At the start of the year, the fund's duration was 0.25 years shorter than the FTSE Actuaries UK Conventional Gilts All Stocks Index. We added duration as yields rose, actively trading volatility around neutral. We took advantage of supply events in Italy early in the month and subsequent renewed political tensions to trade duration. The fund's duration at month end was 0.1 years short. With regard to yield curve positioning, we had a steepening bias throughout the fund, so the steepening of the curve was positive for performance.
- Cross-market trading was positive for performance. We traded US treasuries and Spanish government bonds against gilts, ending the month with a long position in Spain.
- The fund's modest highly-rated sterling credit exposure, which we hold primarily as a means of enhancing yield in the fund, marginally added to returns as credit spreads (the average extra yield available from corporate bonds compared with government debt of equal maturity) tightened slightly.

Investment outlook

- We expect global government bond yields to rise further from current levels. In the short term, economic growth will be kept in check by uncertainty around new strains of Covid-19 and the ongoing success of the vaccination programmes, but global fiscal and monetary policy should see economic activity recover sharply 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, so these effects could be sustained for some time. 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 slightly shorter than the benchmark, including the impact of cash holdings on duration.
- The fund holds a steepening bias.
- 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

Ben Nicholl
Fund Manager

RLAM GLOBAL HIGH YIELD FUND PERFORMANCE

Fund performance

	1 month (%)	Rolling 12 months (%)
RL Global High Yield Bond Fund M Inc	**0.14**	**5.74**
RL Global High Yield Bond Fund Z Inc	**0.15**	**6.07**
IA Sterling High Yield Sector	0.29	3.67
ICE BofA ML BB-B Global Non-Financial High Yield Constrained Index	-0.01	4.77
RL Short Duration Global High Yield Bond Fund A Inc	**0.07**	**-0.31**
RL Short Duration Global High Yield Bond Fund M Inc	**0.10**	**0.09**
RL Short Duration Global High Yield Bond Fund Z Inc	**0.12**	**0.20**
IA Sterling High Yield Sector	0.29	3.67
Sterling Overnight Index Average Rate (SONIA)[1]	0.00	0.24

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 January 2021. Returns quoted are net of fees.

[1] Benchmark: SONIA. Please note that this changed from 3-month LIBOR, effective 15 December 2020, and is reflected in the returns shown above.

ROYAL LONDON GLOBAL HIGH YIELD BOND FUND

Portfolio commentary

- The fund's Z class returned 0.15%, net of fee, in January, compared with -0.01% 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 0.42%, while the price return was -0.42%.
- The yield-to-worst* on the benchmark ended January at 3.81%. The fund yield stood at 4.75% 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 flat return in January. Spreads were largely unchanged for the overall index, but the positive impact from the carry on high yield bonds was offset by increased government bond yields over the month.
- While more transmissible variants of Covid-19 led to tighter restrictions, case numbers generally declined across the US, UK and Europe, as lockdown measures started to prove effective. In the US, the Democrats gained control of Congress, albeit only with a casting vote from Vice President Harris. Markets assumed that greater short-term fiscal support will be offset by higher taxes and more regulation down the line. President Biden proposed a $1.9tn stimulus package, although even some Democrats baulked at the size.
- Returns were mixed across market index sectors. The energy sector, the largest in the high yield universe, produced negative returns over the month, as did real estate, while other major sectors such as healthcare, media and telecoms produced positive returns. Generally speaking, lower rated debt such as CCC rated bonds outperformed higher rated BB and B rated debt. UK was the strongest performing region, with modest gains for both the US and Europe, while emerging market high yield saw negative returns.
- Issuance in the high yield market was relatively buoyant in January and significantly higher than during the same month in 2020. The majority of issuance continued to be BB or B rated, with an even split between the two. Issuance came overwhelmingly from the US market, with European high yield issuance materially lower, albeit also higher than the same month last year.
- The fund's underweight allocation to **energy**, one of its leading underweight positions relative to the benchmark, was the primary driver of performance at the sector level. The fund's overweight exposure to **services** was also positive.
- The biggest contributor to the fund's performance was the cinema operator **AMC Entertainment**. The largest detraction from relative performance came from the Mexican energy giant **Pemex**.
- **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 Credit

Stephen Tapley
Global Credit Fund Manager

ROYAL LONDON SHORT DURATION GLOBAL HIGH YIELD BOND FUND

Portfolio commentary

- The fund's Z class returned 0.12%, net of fee, in January, compared with 0.00% for SONIA.
- The global high yield market produced a flat return in January. Spreads were largely unchanged for the overall index, but the positive impact from the carry on high yield bonds was offset by increased government bond yields over the month.
- While more transmissible variants of Covid-19 led to tighter restrictions, case numbers generally declined across the US, UK and Europe, as lockdown measures started to prove effective. In the US, the Democrats gained control of Congress, albeit only with a casting vote from Vice President Harris. Markets assumed that greater short-term fiscal support will be offset by higher taxes and more regulation down the line. President Biden proposed a $1.9tn stimulus package, although even some Democrats baulked at the size.
- Returns were mixed across sectors. The energy sector, the largest in the high yield universe, produced negative returns over the month, as did real estate, while other major sectors such as healthcare, media and telecoms produced positive returns. Generally speaking, lower rated debt such as CCC rated bonds outperformed higher rated BB and B rated debt. UK was the strongest performing region, with modest gains for both the US and Europe, while emerging market high yield saw negative returns.
- Issuance in the high yield market was relatively buoyant in January and significantly higher than during the same month in 2020. The majority of issuance continued to be BB or B rated, with an even split between the two. Issuance came overwhelmingly from the US market, with European high yield issuance materially lower, albeit also higher than the same month last year.
- The biggest relative contributor to the fund's performance was the satellite operator **Intelsat**. There were no material detractors from performance, with both US fibre provider **Zayo Group** and aerospace components supplier **Transdigm** small negatives for the fund.
- At month-end, the expected yield on the fund was 2.77% (2.76% on an FX-adjusted basis), with an expected maturity of 1.02 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, SONIA, 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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