ROYAL LONDON GMAP CONSERVATIVE FUND

Quarterly Report 30 June 2021

For professional clients only, not suitable for retail investors

CONTENTS

ROYAL LONDON GMAP CONSERVATIVE FUND **3**

ROYAL LONDON GMAP CONSERVATIVE FUND

Fund data

	Fund
Fund size	£254.1m
Launch date	14.03.2016

Source: RLAM. Based on the M Inc share class.

Performance

	Fund (%) (M Acc)	Fund (%) (M Inc)	Benchmark (%)	Relative (%) (as compared to M Inc)
Q2 2021	**1.76**	**1.78**	**1.41**	**0.37**
Year-to-date	-0.86	-0.69	-1.89	1.21
Rolling 12 months	1.79	1.94	-0.69	2.64
3 years p.a.	4.05	4.12	3.42	0.70
5 years p.a.	3.51	3.58	2.86	0.72
Since Inception p.a. 14.03.2016	4.06	4.13	3.61	0.52

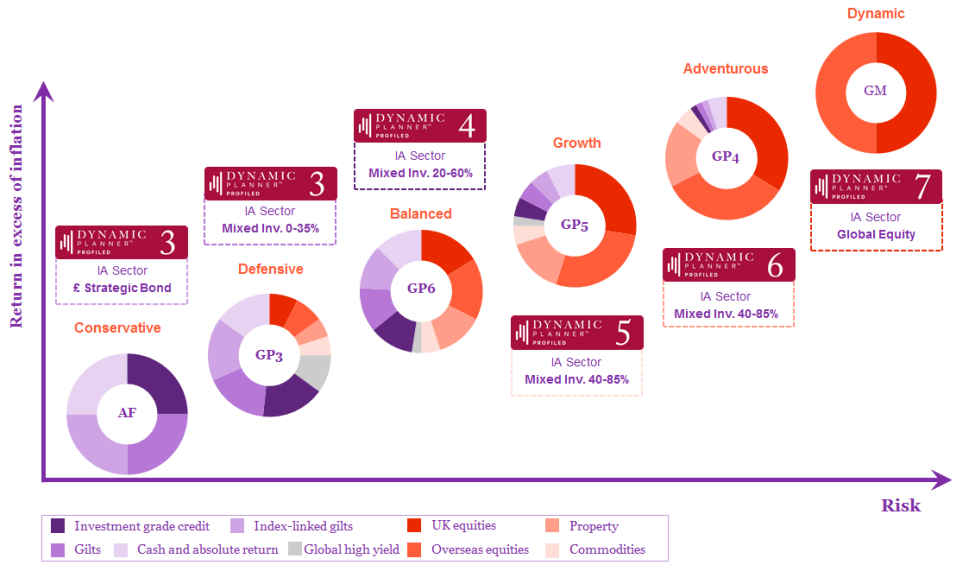
Past performance is not necessarily a reliable indicator of future performance. The value of investments and the income from them is not guaranteed and may go down as well as up and investors may not get back the amount originally invested.

Source: RLAM, based on the M share classes. Performance for the fund is calculated on a mid basis with income re-invested. All performance figures stated gross of fees and tax unless otherwise stated.

[1]GMAP Conservative Composite Benchmark. The benchmark has been designed with the aim of maximising long run return in excess of inflation for a given level of risk.

As of 6 April 2017, the UK Government announced that funds paying interest distributions (funds more than 60% in interest bearing assets, such as fixed income securities/bonds and cash) will be required to pay those distributions gross of tax. As a result, all performance figures provided within the quarterly report will conform to gross of tax, effective from this date onwards.

RL GMAP range

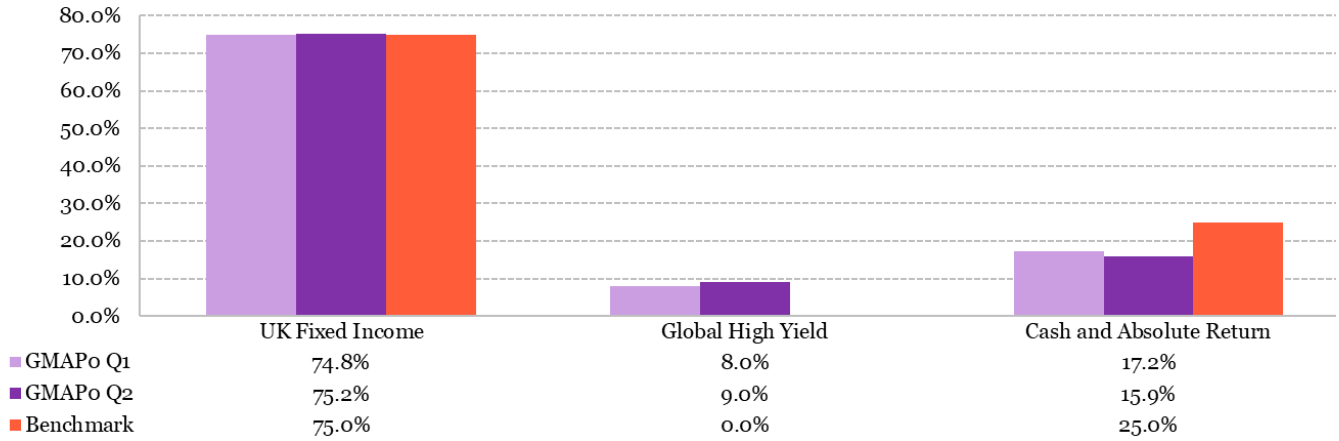


Risk rating is established by Distribution Technology (DT) and is out of 10. For illustrative purposes – reflects Strategic Asset Allocation weightings, may vary in accordance with tactical asset allocation.

Our GMAPs fund range is designed to span the risk return spectrum, with each fund aiming to maximise the long-term real return for its given level of risk through a broadly diversified portfolio of investments.

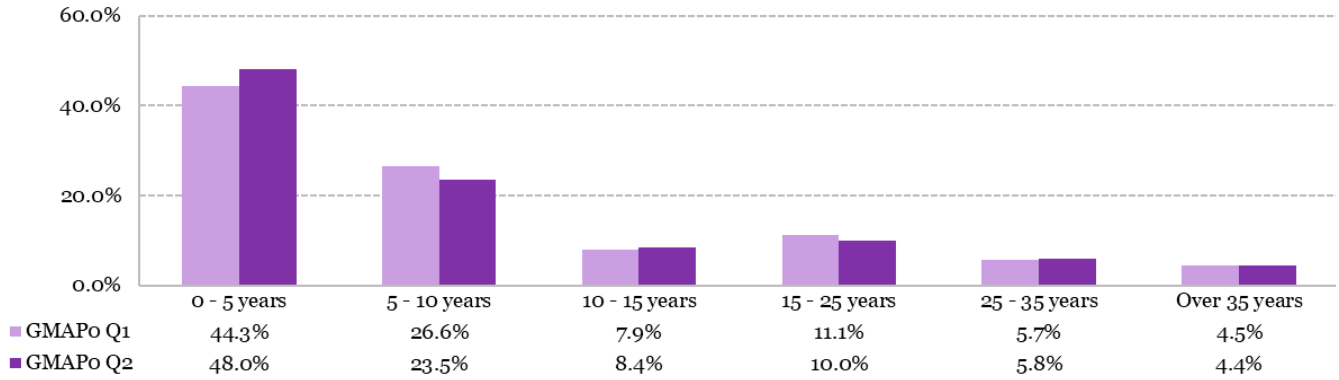
ROYAL LONDON GMAP CONSERVATIVE FUND

Asset split



Source: RLAM. We take a holistic approach to fixed income management and fund weights relative to their respective benchmarks may not reflect tactical exposures. Figures calculated on a 'look through' basis, reflecting underlying assets, not fund component weights.

Yield curve positions



Source: Figures calculated on a 'look through' basis, reflecting underlying assets, not fund component weights.

Largest holdings

	Asset type	Weighting (%)
RL UK Government Bond Fund	UK Fixed Income	22.6
RL Short Duration Global Index Linked Fund	UK Fixed Income	18.6
RL Sustainable Managed Income	UK Fixed Income	17.5
RL Ethical Bond Fund	UK Fixed Income	10.0
RL Enhanced Cash Plus Fund	Cash	7.0
RL Index Linked Fund	UK Fixed Income	6.2
RL Short Duration Global High Yield Bond Fund	High Yield	6.0
RL Absolute Return Government Bond Fund	Cash and Absolute Return	3.6
RL Global High Yield Bond Fund	High Yield	3.0
RL Short-Term Money Market Fund	Cash	3.0
Total		**97.5**

Source: RLAM. Information as at 30 June 2021 and correct at that date, unless otherwise stated. Total weight reflects rounding.

ROYAL LONDON GMAP CONSERVATIVE FUND

Executive summary

- Strong global economic data in the second quarter supported expectations of a sustained economic recovery and equity markets again provided strong returns, particularly in April and June, while May saw much greater volatility, driven weaker than expected US jobs data and investor concerns around potential future inflation and interest rate increases. We took profits in our equity position in April, moving to just a slight overweight that we maintained through the rest of the quarter. Although our overweight to equity was slight, it was beneficial to fund performance in the period.
- Central banks continued to support the global economy-in the second quarter. Although the Bank of England (BoE) began to taper its quantitative easing programme in May, slowing the pace of bond purchases, this had been expected by markets and had little impact on prices. The European Central Bank delayed any decision on tapering until a later date, and in the US, the Federal Open Market Committee (FOMC) now forecasts small increases in base rates during 2022 – a year earlier than their previous March forecasts showed – but their current view remains that inflation will be "transitory".
- We remained underweight government bonds given low nominal and negative real yields, as well as the prospect of higher inflation in the medium term.- We maintained our view that corporate credit will outperform government bonds as the global economy recovers. As such, we remained overweight credit, particularly global high yield bonds, and particularly short duration high yield, which was positive for performance of relevant GMAP funds.
- We participated in the ongoing rally in risk assets, remaining overweight in equities, global high yield bonds and commodities through the quarter. The strong global recovery helped high yield hold its position as the best performing asset class in fixed income and commodity prices to continue to be strong. Oil prices were up 50% year-to-date, reaching their highest levels since October 2018; the price of Brent crude oil rose by +18.2% to more than $76 a barrel in the period.
- As economies reopen further this year, we expect risk assets to continue their recovery, led by more cyclical assets. However, uncertainty regarding inflation, potential new virus variants and geopolitical risks remain; hawkish turns in policy or extensions to lockdown could be challenging for risk assets given current valuations.

GMAP fund	Q2 2021 performance (M class, Acc – net of fee)	GMAP custom benchmark	IA sector	IA sector average performance
Conservative	1.61%	1.41%	£ Strategic Bond	1.83%
Defensive	2.56%	2.59%	Mixed Investments: 0-35% shares	2.53%
Balanced	3.35%	3.65%	Mixed Investments: 20-65% shares	3.63%
Growth	4.79%	5.86%	Mixed Investments: 40-85% shares	5.01%
Adventurous	5.23%	5.86%	Mixed Investments: 40-85% shares	5.01%
Dynamic	5.59%	6.64%	IA Global	6.86%

Market overview

- The quarter began with further progress being made in reducing the spread of Covid-19, with the number of new cases falling and vaccine rollout programmes accelerating in most parts of the world, particularly in the US and Europe. A sharp rise in deaths in India and the importation of the 'Delta' variant from the country into the UK raised concerns about the potential for another further waves and lockdowns. However, evidence that the vaccine has significantly reduced the link between case numbers and deaths grew during the period, supporting market confidence regarding the reopening of economies.
- Global economic data remained strong in the second quarter but concerns about inflation were strengthened by a particularly strong US CPI figure (a measure of US inflation) of 4.2% which sent jitters through global equity markets. The US Federal Reserve reassured markets that inflation would be transitory, and that they were not yet 'talking about talking about tapering'. However, the Federal Open Market Committee (FOMC) forecasts showed base rates forecast to be around 0.6% at the start of 2023, pricing in two 25bps rate rises during 2022. In comparison, March forecasts had predicted no rate

rises over the same period. Meanwhile, in May, the Bank of England (BoE) began to taper its quantitative easing programme by slowing the pace of bond purchases – this had been expected by markets and had little impact on prices.

- The MSCI World Index posted healthy returns of 7.9% through the second quarter of 2021. Performance was strong throughout, although May was markedly more volatile. Regionally, Japan was the only market to post negative returns in sterling terms (-0.3%) while the US (8.9%) continued to lead major equity market returns, followed by Europe ex. UK (8.16%), the UK (5.8%), and emerging markets (5.1%).
- Growth returned as the main driver of performance in the quarter; the MSCI World Growth Index returned 10.94% for the quarter versus 4.9% for the MSCI World Value Index. The outperformance of growth was driven by the information technology sector, which grew by 10.6% in the quarter, leading global sector returns. Energy (9.6%) and healthcare (9.5%) were the next best performing sectors, while financials, the second strongest sector in the first quarter, was the sixth best of 11 MSCI sectors in the second quarter, providing returns of 6.42% to investors.
- Global government bonds were mixed in the quarter. The US led global markets with the 10-year US treasury yield falling by 27 basis points (bps) over the quarter to 1.47% (bond prices rise when yields fall, indicating easing concern about inflation and interest rates increases). The UK also performed well with the 10-year UK gilt yield falling by 13bps to 0.72%. Europe was the laggard of major global markets; in Germany the 10-year bund was up by 9bps to -0.21% reflecting the slower EU vaccination programme leaving the European economy opening more slowly than the US and UK.
- The average sterling investment grade spread (the average extra yield available from a corporate bond compared with government debt of equal maturity) ended the quarter 5bps tighter at 0.91%, while the sterling high yield spread ended 7bps tighter for the quarter with a spread of 1.5%. The Merrill Lynch Sterling Non-Gilt index delivered total returns of 1.71% for the quarter, while its sister Sterling High Yield Index returned 1.75% for the quarter, marginally outperforming gilts which returned 1.70% on an all maturities basis.
- The Brazilian real was the strongest currency in the quarter gaining 11.8% against the (US) dollar in the quarter, however major currencies were largely sedentary in comparison. The euro strengthened by 0.8% versus the dollar, while sterling saw no significant movement. The Australian dollar was the period's weakest currency, losing 1.61% against the USD for the quarter.
- Commodities extended their rally, leading cross-asset returns. Oil prices continued to recover strongly and were up 50% year-to-date, reaching their highest levels since October 2018 as the reopening trade sustained. The price of Brent crude oil rose by +18.2% to more than $76 a barrel in the quarter, while copper and gold also gained value; copper was up +7.2% for the quarter, and gold prices grew by 3.5% to $1,791/oz.

Asset allocation overview

- At the end of the quarter, and for the tenth consecutive month, our proprietary Investment Clock model remained in the 'Overheat' zone. This should be constructive for equities, industrial commodities, and corporate bonds, including global high yield. However, as macroeconomic drivers of momentum are beginning to peak, and taper talk is becoming more prevalent across global markets, we expect that the rate of change of recovery is likely to slow. At the close of the period we held a small equity overweight, having taken profits, favouring US and European markets following strong earnings revisions, and a large overweight in high yield bonds and commodities.

ROYAL LONDON GMAP CONSERVATIVE FUND

What we thought	What we did	What happened	Effect on portfolio
After the strong performance of stocks in H2 2020, we felt markets were likely to experience periods of greater volatility generated by the strong economic recovery leading to questions regarding the tapering of fiscal and monetary policy support to the global economy. Although value had performed well through the year-to-date and had driven strong financial and energy sector performance, we retain a constructive view on the resilience of technology sector growth prospects.	Given the dominant force in markets currently is the global growth recovery post-pandemic, we have remained overweight equities but took profits in April, moving from a moderate to a slight overweight that was maintained throughout the quarter. We took small relative positions with regard to sector tilts in Q2. We began the quarter in favour of value-oriented sectors and were overweight energy and financials. As the quarter developed (and concerns about interest rates receded), we added to our technology exposure, moving overweight from a prior held underweight. We stayed underweight consumer discretionary, consumer staples and utilities.	The MSCI World Index posted healthy returns of 7.9% through the second quarter of 2021. Performance was strong throughout, although May was markedly more volatile. Growth returned as the main driver of performance in Q2 as inflation and interest rate concerns eased; the MSCI World Growth Index returned 10.9% for the quarter versus 4.9% for the MSCI World Value Index.	Although we took profits in our equity position, remaining overweight proved marginally beneficial to performance. Our sector tilts were broadly neutral.
We took a positive view on the US, the UK and Europe in Q2 as global economic reopening continued post pandemic owing to successful vaccine rollouts; emerging markets and Japan are still lagging.	We were neutral/marginally overweight UK equities throughout Q2, and built on our overweight position in both the US and Europe into the close of the quarter. We were underweight in emerging markets, Japan, and Asia Pacific ex. Japan.	US equities returned 8.9% to sterling investors in the quarter, leading returns by major equity markets. Europe ex. UK (8.2%), the UK (5.8%), and emerging markets (5.1%). Japan posted negative returns to sterling investors (-0.3%).	Our regional tactical allocations in equity were beneficial across the board. Our US overweight was particularly beneficial.
We maintained our view that corporate credit will outperform government bonds as the global economy recovers strongly. High yield bonds have continued to provide strong returns relative to investment grade. The asset class has been supported by loose fiscal and monetary policy, which have made the default on debt less likely. Because of this, we still think that high yield credit spreads continue to overcompensate for their risks.	We remained overweight credit, particularly global high yield bonds, and particularly short duration high yield.	Gilts (all maturities) returned 1.70% in the period compared to 1.71% for the Merrill Lynch Sterling Investment Grade Index – the respective spread tightened by 5bps. Global high yield bonds continued to perform strongly over the quarter and the high yield spread tightened by a further 7bps. Global high yield funds returned 2.2%, for the quarter.	Staying underweight in government bonds and overweight in credit was positive for performance. The overweight allocation to global high yield was positive for performance.
As the recovery in the real economy continued, particularly in industrial production in China, we remained constructive on commodities.	We maintained our overweight in commodities throughout the quarter	Commodities rallied to a thirteen-year high, leading cross-asset returns, as oil continued its rebound.	The overweight exposure to commodities was positive for performance.
With the Covid economic shock to retail and hospitality, we believed UK commercial property would underperform, at least until there is a sustained economic recovery.	While recognising its diversifying benefits we maintained an underweight position in property through the quarter and increased this over the period.	Commercial property performed poorly over the quarter as lockdowns resumed and the retail and hospitality sectors continued to struggle.	Our underweight property position had a positive impact on performance.

Please note: This table details our main asset allocation decisions for the quarter across the GMAPs funds. Not all tactical allocations are relevant to the Conservative fund (fixed income-only) and Dynamic Fund (equity-only).

Outlook

- As economies reopen further this year, we expect risk assets to continue their recovery, led by more cyclical assets. However, uncertainty regarding inflation, new virus variants and geopolitical risks remain, and hawkish turns in policy or extensions to lockdown could be challenging for risk assets given current valuations. Our tactical overweight positioning in equites and

commodities added value over the period. We have taken some profits in equities but remain overweight global high yield bonds and underweight government bonds and property.

- For the latest views from the team, please see our Investment Clock blog at www.rlam.co.uk

ROYAL LONDON
ASSET MANAGEMENT

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