Royal London Fixed Income Funds

Fund Manager Commentary

February 2024

ROYAL LONDON
ASSET MANAGEMENT

Contents

Economic Developments

- As expected, the Bank of England kept rates on hold at their February meeting. Although one committee member voted for a rate cut, two still voted for a hike. Data released in February again painted a mixed picture of economic activity, while inflation remained above the central bank's 2% target. Year-on-year January CPI inflation remained at 4.0% and core inflation was also steady on the month at 5.1%; both figures were lower than expected, as was services CPI. Fourth quarter GDP fell 0.3% quarter-on-quarter, weaker than expected and meaning that the UK recorded a technical recession in the second half of 2023.
- In the US, Federal Reserve speakers continued to signal rate cuts this year, but without signalling urgency and while reiterating the need for more confidence in the path of inflation first. Inflation data was mostly stronger than expected. January CPI came in a touch stronger than expected at 0.3% versus the previous month, core inflation rose 0.4% on both PCE and CPI measures and so-called 'super-core' inflation rose further above 0.2% on both CPI and PCE measures. January nonfarm payrolls were much stronger than expected and the unemployment rate remained 3.7% rather than rising a tenth as expected. However, quite a large proportion of the activity data over the month disappointed.
- Several European Central Bank speakers mentioned that they see a first cut as possible/likely in the summer/June. President Christine Lagarde reiterated that upcoming wage data would be important in their analysis. January CPI fell to 2.8% year-on-year after 2.9%, a touch above expectations. Core CPI fell slightly, but annual services CPI again remained at 4.0%. Activity data released over the month were mixed.

Royal London Asset Management Credit Fund Performance

	1 month (%)	Rolling 12 Months (%)
RL Corporate Bond Fund Z Inc	**-0.28**	**8.06**
IA Sterling Corporate Bond Sector	-0.70	5.77
iBoxx Sterling Non-Gilts All Maturities Index	-0.66	5.56
RL Ethical Bond Fund Z Inc	**-0.27**	**6.79**
IA Sterling Strategic Bond Sector	-0.48	6.40
iBoxx Sterling Non-Gilts All Maturities Index	-0.66	5.56
RL Global Bond Opportunities Fund Z Inc	**0.44**	**7.94**
IA Global Mixed Bond Sector	-0.39	3.67
RL Investment Grade Short Dated Credit Fund Z Inc	**-0.19**	**6.53**
IA Sterling Corporate Bond Sector	-0.70	5.77
ICE BofA ML 1-5 year Sterling Non-Gilt All Stocks Index	-0.38	5.19
RL Short Duration Credit Fund Z Inc	**0.51**	**7.83**
IA Sterling Strategic Bond Sector	-0.48	6.40
ICE BofA ML 1-5 year Sterling Non-Gilt All Stocks Index	-0.38	5.19
RL Sterling Credit Fund Z Inc	**-0.21**	**8.04**
IA Sterling Corporate Bond Sector	-0.70	5.77
iBoxx Sterling Non-Gilts All Maturities Index	-0.66	5.56
RL Sterling Extra Yield Bond Fund A Inc	**0.99**	**8.46**
RL Sterling Extra Yield Bond Fund B Inc	**0.95**	**7.90**
RL Sterling Extra Yield Bond Fund Y Inc	**1.04**	**8.93**
RL Sterling Extra Yield Bond Fund Z Inc	**1.02**	**8.74**
IA Sterling Corporate Bond Sector	-0.70	5.77
IA Sterling High Yield Sector	0.28	9.35
IA Sterling Strategic Bond Sector	-0.48	6.40

Past performance is not a guide to 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: Royal London Asset Management and FE, as at 29 February 2024. Returns quoted are net of fees. Please note that with effect from 1 February 2024 RLAM are using peer group comparisons provided by Morningstar. Prior to this peer comparison were provided by Lipper so there may be some differences compared to the data provided historically.

All IA sector performance shown is for the median.

Credit Market Review

Market highlights – sterling investment grade credit

- The sterling investment grade market (iBoxx) produced another negative return in February, marking two straight down months to start 2024, with a return of -0.66%. However, this was driven entirely by higher underlying government bond yields, with the average investment grade credit spread (the average extra yield available from a corporate bond compared with government debt of equal maturity) tightening to 1.07% from 1.13%.
- In UK investment grade markets, rising yield levels meant the negative returns over the month were broad based across all sectors. The worst performing sectors, however, were supranationals and telecommunications, while structured, insurance and subordinated banking bonds were the best relative performers. By rating, only the sterling high yield market saw positive returns, with investment grade bonds struggling, particularly A rated assets. By maturity, shorter-dated bonds outperformed their longer-dated counterparts.
- After a strong showing in January, sterling issuance slumped to £2.7bn in February, a far way off the £8.3bn seen the prior month. This month's issuance was the slowest February since 2016. Once again, issuance was led by financials, at £1.6bn. Euro issuance was strong in February, at €66.7bn, which was down from January's €92.0bn but well ahead of the €50.6bn seen in the same period a year prior. The levels were supported by buoyant issuance from non-financials.
- February was another weak month for global government bonds, with the strong run in late 2023 and tempered rate cut expectations leading to higher yields. US treasury 10-year yields rose to 4.25% from 3.88%, while German bund 10-year yields climbed to 2.41% from 2.15%. In the UK, the benchmark 10-year gilt rose to 4.12% at the end of February, from 3.75% at the start of the month, reversing around half of the falls seen in the final two months of 2024, meaning the FTSE UK Conventional Gilt All-Stocks index returned -1.11% for the month.

Royal London Corporate Bond Fund

Portfolio commentary

- The fund outperformed its benchmark, the iBoxx Sterling Non-Gilts All Maturities Index, in February. On a year-to-date basis, the fund has posted negative total returns but is well ahead of the benchmark.
- UK government bond yields moved higher in February, while credit spreads were lower. The sterling credit market outperformed gilts over the month, helped by the lower duration of credit markets compared to government bonds.
- For February, the combination of sector and stock selection was the main driver of positive relative returns, while our curve positioning detracted. The sector allocation returns were driven by our overweighting in structured bonds and insurance, as well as our significant underweight position in supranationals. By stock selection, our banking and insurance bonds stood out.
- Our primary market activity was relatively light in February, and was led by financials, in particular subordinated financials as the AT1 market continued to re-open. We added AT1 bonds from French bank **BNP Paribas** and specialist lender **Investec**, with the latter issue coming with a yield above 10%. We also added to our position in Investec senior paper in the secondary market, where we felt yields were attractive relative to other bank senior bonds.
- Outside of financials, we picked up a new 2036 euro-denominated issue from Dutch telecommunications company **KPN,** funding a tender for an existing bond held by the fund.
- Market dynamics and inefficiencies continue to provide opportunities to make switches where we can improve credit quality, yield or spread, with several examples during the month. In particular, we switched between **Southern Water** bonds, where for a modest extension in maturity we were able to pick up around 40bps in additional spread, which we felt more than compensated for the additional maturity risk.
- Another switch we enacted was moving into **Tesco Property** from **Motability Operations**. The move saw a pickup in spread and issuer diversity, while adding security given the assets backing these bonds.
- Also in the secondary market, we added to our position in **Annington Funding**, a property firm focused on leasing properties to the Ministry of Defence. It is a firm where we see good cashflow visibility and are paid an attractive credit spread for risk.

Investment outlook

- Inflation came down significantly in 2023 but remains above the Bank of England's target, and now does not have the 'easy' wins of base effects to push this lower. In our view, wage inflation is the key metric to watch: we believe that the Bank will find it hard to start cutting rates if wages continue to rise at 5-6% per annum. Although the economic data remain very mixed, we still believe that higher interest rates will contribute to a slowdown in the UK. This could impact company earnings and lead to some increase in pressure on credit markets. However, consumer resilience has been greater than expected in both the UK and globally, which has helped support growth and prevent a sharp recession.
- We expect supply to weigh on credit markets in the first quarter but think that underlying fundamentals will limit spread widening. Overall, we believe that the all-in yield on sterling investment grade credit remains attractive. This is reflected in the significant asset allocation in favour of credit bonds. In recent months the magnitude of this position has been reduced, as credit spreads have contracted.
- Given the potential economic challenges, we remain focused on identifying companies with strong balance sheets, favouring issues with security and downside protection. Over the medium term the superior yields available on credit bonds and the credit risk mitigation undertaken through sector and issuer diversification should support further outperformance.

Key views within the fund

- Well 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 slightly longer than the benchmark, which has been increased as yields have risen. Interest rate sensitivity is broadly neutral when factoring in a number of bonds which have theoretical duration but are not as interest rate sensitive.
- An overweight position in subordinated financial debt, where we believe yields are attractive.
- 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.
- Environmental, social and governance (ESG) risk factors are fully integrated in the management of the portfolio. The WACI (weighted average carbon intensity) of the portfolio is below that of the index.

CITYWIRE AA

Shalin Shah
Senior Fund Manager

Matt Franklin
Fund Manager

Royal London Ethical Bond Fund

Portfolio commentary

- The fund outperformed its benchmark, the iBoxx Sterling Non-Gilts All Maturities Index, in February. On a year-to-date basis, the fund has posted negative total returns but is well ahead of the benchmark.
- UK government bond yields moved higher in February, while credit spreads were lower. The sterling credit market outperformed gilts over the month, helped by the lower duration of credit markets compared to government bonds.
- For February, the combination of sector and stock selection was the main driver of positive relative returns, while our curve positioning detracted. The sector allocation returns were driven by our overweighting in structured bonds and insurance, as well as our significant underweight position in supranationals. By stock selection, our banking and insurance bonds stood out. Our duration positioning was a slight positive, with the fund short of the benchmark, so was aided by a shift upwards in the UK government yield curve.
- Our primary market activity was relatively light in February, with a new 2028 issue from Norwegian company **Scatec** – a firm that specialises in renewable energy systems – the highlight.
- One switch we enacted during the month, was moving into more senior bonds in **Close Brothers**. The switch helped de-risk the position as we moved into operating company debt from holding company debt.

Investment outlook

- Inflation came down significantly in 2023 but remains well above central bank targets, and now does not have the 'easy' wins of base effects to push this lower. Although the economic data remain very mixed, we still believe that higher interest rates will contribute to a slowdown in economic growth. This could well impact company earnings and lead to some increase in pressure on credit markets. However, consumer resilience has been greater than expected across most major economies, particularly in the US, which has helped support growth and prevent a recession. How this continues into 2024 could prove critical.
- As we came into 2024, we felt that the all-in yield on investment grade credit was still attractive, despite the falls in yields in November and December. January's moves reversed around half of the falls seen in those final months of 2024. Our credit strategy focuses on three sources of return: underlying government bond yields, market credit spreads, and the additional credit spread we generate over credit benchmarks. Further, the additional yield embedded in our credit strategies, over that available from credit benchmarks, gives us confidence in our ability to deliver long-term outperformance.
- Although recent outperformance means that the relative attractiveness of credit bonds has reduced, we still favour holding them compared to government debt as credit spreads remain at levels that more than compensate for the credit risk across both investment grade and high yield markets. Given the potential challenges in the outlook, we remain focused on identifying companies with strong balance sheets, favouring issues with security and downside protection, and ensuring that portfolios are diversified across issuers and sectors.

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.
- Duration is broadly in line with 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 property and social housing sectors, and towards structured bonds, which benefit from a claim on assets and cashflows.

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CITYWIRE A

Eric Holt
Senior Fund Manager

CITYWIRE AA

Paola Binns
Head of Sterling Credit

Royal London Global Bond Opportunities Fund

Market highlights

Index	Total return (%)	Spread at end of month (basis points)	Spread change over month (basis points)
HY global non-financial corps **ICE BofA ML global non-financial high yield index**	0.46	359	-43
AT1 **ICE BofA ML contingent capital index**	0.34	345	-29
Emerging market **ICE BofA ML**	1.42	437	-111
HY global non-financial hybrid corps **ICE BofA ML global hybrid non-financial high yield index**	0.26	269	-26
IG global non-financial hybrid corps **ICE BofA ML global hybrid non-financial corporate index**	-0.13	214	-16
Dollar investment grade corporate bonds **ICE BofA ML US corporate index**	-1.40	100	-2
Sterling investment grade corporate bonds **ICE BofA ML sterling corporate and collateralised index**	-0.54	125	-8
Euro investment grade corporate bonds **ICE BofA ML euro corporate and Pfandbriefe index**	-0.90	117	-9

Source: Bloomberg

- In the US, Federal Reserve speakers continued to signal rate cuts this year, but without signalling urgency and while reiterating the need for more confidence in the path of inflation first. Inflation data was mostly stronger than expected. January CPI came in a touch stronger than expected at 0.3% versus the previous month, core inflation rose 0.4% on both PCE and CPI measures and so-called 'super-core' inflation rose further above 0.2% on both CPI and PCE measures. January nonfarm payrolls were much stronger than expected and the unemployment rate remained 3.7% rather than rising a tenth as expected. However, quite a large proportion of the activity data over the month disappointed.
- Several European Central Bank speakers mentioned that they see a first cut as possible/likely in the summer/June. President Christine Lagarde reiterated that upcoming wage data would be important in their analysis. January CPI fell to 2.8% year-on-year after 2.9%, a touch above expectations. Core CPI fell slightly, but annual services CPI again remained at 4.0%. Activity data released over the month were mixed.
- As expected, the Bank of England kept rates on hold at their February meeting. Although one committee member voted for a rate cut, two still voted for a hike. Data released in February again painted a mixed picture of economic activity, while inflation remained above the central bank's 2% target. Year-on-year January CPI inflation remained at 4.0% and core inflation was also steady on the month at 5.1%; both figures were lower than expected, as was services CPI. Fourth quarter GDP fell 0.3% quarter-on-quarter, weaker than expected and meaning that the UK recorded a technical recession in the second half of 2023.
- February was another weak month for global government bonds, with the strong run in late 2023 and tempered rate cut expectations leading to higher yields. US treasury 10-year yields rose to 4.25% from 3.88%, while German bund 10-year yields climbed to 2.41% from 2.15%. In the UK, the benchmark 10-year gilt rose to 4.12% at the end of February, from 3.75% at the start of the month, reversing around half of the falls seen in the final two months of 2024, meaning the FTSE UK Conventional Gilt All-Stocks index returned -1.11% for the month.

- US, euro and sterling investment grade markets produced more negative returns in February, marking two straight down months to start 2024. However, this was driven entirely by higher underlying government bond yields, with the average investment grade credit spread (the average extra yield available from a corporate bond compared with government debt of equal maturity) tightening slightly in all three markets.

Portfolio commentary

- The fund recorded a net return of 0.44% (Z Acc share class) in February. This was a pleasing result in a month where government and investment grade bond markets saw negative or flat returns, and was driven by our broad-based exposure across areas such as high yield and At1 bank bonds.
- Following an active January, February again saw a number of opportunities to add to attractively priced new issues. With the AT1 market more active, we added bonds from preferred banks including US dollar bonds from **Standard Chartered**, **BNP Paribas** and **ING**, as well as euro AT1 bonds from **ABN Amro**, all at very attractive yields. Elsewhere in financials, we added a US dollar subordinated bond new issue from **NatWest**, and preference shares from **CitiGroup**.
- Away from financials, we added a new issue from Norwegian renewable-focused utility Scatec, as well as a new issue from offshore oil shuttle tanker provider **Altera**.
- Secondary market was limited given the value on offer in the new issue space, but we did add to the recent new issue of secured bonds from **Husky Technologies** yielding over 9%, as well as **Lloyds** AT1 bonds with a call date in 2025.

Investment outlook

- Inflation came down significantly in 2023 but remains well above central bank targets, and now does not have the 'easy' wins of base effects to push this lower. Although the economic data remain very mixed, we still believe that higher interest rates will contribute to a slowdown in economic growth. This could well impact company earnings and lead to some increase in pressure on credit markets. However, consumer resilience has been greater than expected across most major economies, particularly in the US, which has helped support growth and prevent a recession. How this continues into 2024 could prove critical.
- As we came into 2024, we felt that the all-in yield on investment grade credit was still attractive, despite the falls in yields in November and December. Moves higher in January and February have reversed much of this. Whilst 10-year bund yields at around 2.5% are obviously are not as attractive as the levels seen in October, we feel that the yield available across investment grade and high yield credit overcompensates for default risk. Further, the yield embedded in the fund gives us confidence in our ability to deliver positive long-term returns.
- Given the potential challenges in the outlook, we remain focused on identifying companies with strong balance sheets, favouring issues with security and downside protection, and ensuring that portfolios are diversified across issuers and sectors.

Eric Holt
Senior Fund Manager

Rachid Semaoune
Senior Fund Manager

ROYAL LONDON
ASSET MANAGEMENT

Royal London Investment Grade Short Dated Credit Fund

Portfolio commentary

- The fund outperformed its benchmark, the ICE BofAML 1-5yr Sterling Non-Gilt All Stocks Index, in February. On a year-to-date basis, the fund has posted negative total returns but is well ahead of the benchmark.
- UK government bond yields moved higher in February, while credit spreads were lower. The sterling credit market outperformed gilts over the month, helped by the lower duration of credit markets compared to government bonds.
- For February, the combination of sector and stock selection was the main driver of positive relative returns, while our curve positioning detracted. The sector allocation returns were driven by our overweighting in structured bonds and insurance, as well as our significant underweight position in supranationals. By stock selection, our banking and insurance bonds stood out.
- Our primary market activity was relatively light in February, with a new five-year sterling issue from French cooperative bank **Credit Mutuel** the highlight. Another new issue of note was a six-year green bond from German management consultant **P3 Group**.
- In the secondary market, we took advantage of some inflows to add to existing positions in senior banking paper. In particular, we added to our holdings in **HSBC**, **Investec** and **UBS**. We also increased our exposure to short-dated subordinated issues from **Credit Agricole** and **Societe Generale**.
- One switch we enacted during the month, was moving into more senior bonds in **Close Brothers**. The switch helped de-risk the position as we moved into operating company debt from holding company debt.

Investment outlook

- Inflation came down significantly in 2023 but remains above the Bank of England's target, and now does not have the 'easy' wins of base effects to push this lower. In our view, wage inflation is the key metric to watch: we believe that the Bank will find it hard to start cutting rates if wages continue to rise at 5-6% per annum. Although the economic data remain very mixed, we still believe that higher interest rates will contribute to a slowdown in the UK. This could impact company earnings and lead to some increase in pressure on credit markets. However, consumer resilience has been greater than expected in both the UK and globally, which has helped support growth and prevent a sharp recession.
- We expect supply to weigh on credit markets in the first quarter but think that underlying fundamentals will limit spread widening. Overall, we believe that the all-in yield on sterling investment grade credit remains attractive. This is reflected in the significant asset allocation in favour of credit bonds. In recent months the magnitude of this position has been reduced, as credit spreads have contracted.
- Given the potential economic challenges, we remain focused on identifying companies with strong balance sheets, favouring issues with security and downside protection. Over the medium term the superior yields available on credit bonds and the credit risk mitigation undertaken through sector and issuer diversification should support further outperformance.

Key views within the fund

- The fund is well diversified 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.
- It has a minimal weighting in supranational bonds, as we expect corporate debt to outperform over the medium term.
- Fund duration was marginally longer than the benchmark at month end.
- 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
Head of Sterling Credit

Royal London Short Duration Credit Fund

Portfolio commentary

- The fund strongly outperformed its benchmark, the ICE BofAML 1-5yr Sterling Non-Gilt All Stocks Index, in February. On a year-to-date basis, the fund has posted strong total returns and is well ahead of the benchmark.
- UK government bond yields moved higher in February, while credit spreads were lower. The sterling credit market outperformed gilts over the month, helped by the lower duration of credit markets compared to government bonds.
- For February, the combination of sector and stock selection was the main driver of positive relative returns, while our curve positioning detracted. The sector allocation returns were driven by our overweighting in structured bonds and insurance, as well as our significant underweight position in supranationals. By stock selection, our banking and insurance bonds stood out.
- Our primary market activity was relatively light in February, and was led by financials, in particular subordinated financials with the AT1 market continuing to re-open for business. We added AT1 bonds from French bank **BNP Paribas, Standard Chartered** and **Investec**, with the Investec issue coming with a yield above 10%. We also added to our position in Investec senior paper in the secondary market, where we felt yields were attractive relative to other bank senior bonds.
- Outside of financials, we picked up a new 2028 issue from Norwegian company **Scatec**. The firm specialises in renewable energy systems. Another new issue of note was a six-year green bond from German management consultant **P3 Group**.
- In the secondary market, we were able to enact a switch during the month, moving into more senior bonds in **Close Brothers**. The switch helped de-risk the position as we moved into operating company debt from holding company debt.

Investment outlook

- Inflation came down significantly in 2023 but remains above the Bank of England's target, and now does not have the 'easy' wins of base effects to push this lower. In our view, wage inflation is the key metric to watch: we believe that the Bank will find it hard to start cutting rates if wages continue to rise at 5-6% per annum. Although the economic data remain very mixed, we still believe that higher interest rates will contribute to a slowdown in the UK. This could impact company earnings and lead to some increase in pressure on credit markets. However, consumer resilience has been greater than expected in both the UK and globally, which has helped support growth and prevent a sharp recession.
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Key views within the fund

- The fund is well diversified, 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.
- The fund's duration slightly below that of the benchmark at month end.
- 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 AA

Paola Binns
Senior Fund Manager

Royal London Sterling Credit Fund

Portfolio commentary

- The fund outperformed its benchmark, the iBoxx Sterling Non-Gilts All Maturities Index, in February. On a year-to-date basis, the fund has posted negative total returns but is well ahead of the benchmark.
- UK government bond yields moved higher in February, while credit spreads were lower. The sterling credit market outperformed gilts over the month, helped by the lower duration of credit markets compared to government bonds.
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- Outside of financials, we picked up a new 2036 euro-denominated issue from Dutch telecommunications company **KPN**. The company has strong ESG credentials, and the bonds came at an attractive yield premium to the market. We also took part in a euro-denominated 20-year issue from **Siemens Financier**.
- Market dynamics and inefficiencies continue to provide opportunities to make switches where we can improve credit quality, yield or spread, with several examples during the month. In particular, we switched between **Southern Water** bonds, where for a modest extension in maturity we were able to pick up around 40bps in additional spread, which we felt more than compensated for the additional maturity risk.
- Another switch we enacted was moving into **Tesco Property** from **Motability Operations**. The move saw a pickup in spread and issuer diversity, while adding security given the assets backing these bonds.
- Also in the secondary market, we added to our position in **Annington Funding**, a property firm that refurbishes homes previously owned by the Ministry of Defence and then sells or rents them. It is a firm where we see good cashflow visibility and are paid a material yield premium to the market.

Investment outlook

- Inflation came down significantly in 2023 but remains above the Bank of England's target, and now does not have the 'easy' wins of base effects to push this lower. In our view, wage inflation is the key metric to watch: we believe that the Bank will find it hard to start cutting rates if wages continue to rise at 5-6% per annum. Although the economic data remain very mixed, we still believe that higher interest rates will contribute to a slowdown in the UK. This could impact company earnings and lead to some increase in pressure on credit markets. However, consumer resilience has been greater than expected in both the UK and globally, which has helped support growth and prevent a sharp recession.
- We expect supply to weigh on credit markets in the first quarter but think that underlying fundamentals will limit spread widening. Overall, we believe that the all-in yield on sterling investment grade credit remains attractive. This is reflected in the significant asset allocation in favour of credit bonds. In recent months the magnitude of this position has been reduced, as credit spreads have contracted.
- Given the potential economic challenges, we remain focused on identifying companies with strong balance sheets, favouring issues with security and downside protection. Over the medium term the superior yields available on credit bonds and the credit risk mitigation undertaken through sector and issuer diversification should support further outperformance.

Key views within the fund

- Well diversified, with around 350 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.
- Fund duration was broadly in line with the benchmark at month end.
- Orientated towards 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.

CITYWIRE AA

Paola Binns
Senior Fund Manager

Royal London Sterling Extra Yield Bond Fund

Portfolio commentary

- After the robust start to 2024 achieved in January, the fund posted a broadly similar level of return in February; 0.99%, 0.95%, 1.03% and 1.02% respectively for the A, B, Y and Z class shares. These bring 2024 year to date returns to 2.08%, 1.99%, 2.16% and 2.13% respectively for these share classes.
- January's partial reversal of fixed interest market strength in the final two months of 2023, triggered primarily by growing expectations that interest rates had peaked and would soon start a progressive decline, continued in February. The yield of the bellwether 10-year gilt rose from 3.79% at the end of January to 4.12% by the end of February – it had dipped to a low of 3.43% in the final days of 2023 - with gilts posting an index return of -1.22% in February. Sterling investment grade corporate bonds fared better, with index performance of -0.56% in the month, with the impact of higher gilt reference yields partially mitigated both by their shorter average duration than gilts and by a narrowing of the average yield differential over gilts, from 1.11% to 1.03% in the month. European and Global sub-investment grade indices posted positive index returns in February, +0.35% and +0.45% respectively, reflecting their lower sensitivity to the rise in yields and their stronger rate of income accrual. 2024 year to date index returns to end February for these four asset classes, gilts, sterling investment grade corporate bonds, European and global sub-investment grade bonds are -3.59%, -1.55%, 1.18% and 0.86% respectively.
- Despite the rise in government bond yield in February, more than approximately half the holdings in the fund rose in price in February, with the strong level of income accrual further enhancing their returns, while mitigating wholly or in part the decline in price of other holdings. There were only three holdings which were notably weak in the month; **Close Brothers Group**, the financial services business, down 5% in price on news of a regulatory review of past car finance business which triggered a sharp drop in the company's share price; **Thames Water** holding company bonds, down 7% from a subdued level as the tensions around capital provision for the company ahead of the upcoming 5 year pricing review; and **Bayport**, the developing country microfinance business down 10% on challenging operational performance. In contrast there were several areas of positive performance; AT1 bonds of **Investec**, the financial services company, were up 7% in price on news of an early tender for the bonds accompanying a new AT1 bond with a 10½% coupon until first call in 2029 and up 2% in price from issue by end February – thus the fund benefitted from uplift in the prices of both the old and new bonds; holdings in property companies **MPC** – specialising in healthcare assets – and **Metrocentre** – owner of the Tyneside shopping complex – were each up over 5% in price in February as the very negative sentiment to the sector abated; some investments in the energy sector such as **BlueNord**, **Enquest**, **Floatel** and **Mvest** delivered performance around 4% in the month. By far the most marked performance is the energy sector was the 17% rise in the price of shares in **DOF Group**, the specialist vessel owner and subsea services provider, which were received as part of a bond restructuring in June last year, since when their share price has more than doubled delivering equity like rather than bond like returns to the investment.
- The fund participated in the flow of new issues in the month, including financials **Investec** mentioned above, together with **BNP** and **ING** and **Standard Chartered**, each US$ denominated AT1 bonds with BB/BBB credit ratings and offering yields at or near 8%, **Altera Shuttle Tankers** 9% bonds 2028, unrated but benefitting from long term contracts and business with major international energy companies, and Scatec, the European renewable energy business which issued Norwegian Krone 2028 floating rate bonds at an initial yield of 9%. Market purchases included bonds of financial companies **Abrdn** and **Co-operative Bank**, the later now subject to acquisition by Coventry Building Society. Sales in the month included bonds of **Ping Petroleum**, at par ahead of redemption in July and as part of a tender process by the company, **Aviva** Tier 2 bonds which had performed relatively well in recent months, and the repayment of **Altera Shuttle Tankers** October 2024 bonds in an above par tender process related to their new issue. Finally activity in short-dated gilts reflected liquidity management.

ROYAL LONDON ASSET MANAGEMENT

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.

CITYWIRE A

Rachid Semaoune
Senior Fund Manager

CITYWIRE A

Eric Holt
Senior Fund Manager

Royal London Asset Management Government Bond Fund Performance

	1 month (%)	Rolling 12 Months (%)
RL Global Index Linked Bond Fund Z Inc	**-0.84**	**1.44**
Global Inflation Linked Bond Sector	-0.62	1.51
Bloomberg World Government Inflation-Linked Bond Index – Total Return (GBP Hedged)	-0.61	1.57
RL Index Linked Bond Fund M Inc	**-0.93**	**-3.08**
IA UK Index Linked Gilts Sector	-0.91	-3.77
FTSE Actuaries UK Index-Linked All Stocks Index	0.37	-1.51
RL Short Duration Gilt Fund Z Inc	**-0.63**	**3.71**
IA UK Gilts Sector	-1.35	0.39
FTSE Actuaries UK Conventional Gilts up to 5 Years Index	-0.53	3.34
RL Short Duration Global Index Linked Bond Fund Z Inc	**-0.94**	**3.66**
Global Inflation Linked Bond Sector	-0.62	1.51
RL Short Duration Global Index Linked Composite Benchmark[1]	-0.79	3.76
RL UK Government Bond Fund Z Inc	**-1.67**	**1.00**
IA UK Gilts Sector	-1.35	0.39
FTSE Actuaries UK Conventional Gilts All Stocks Index	-1.11	1.07

Past performance is not a guide to 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: Royal London Asset Management and FE, correct as of 29 February 2024. Returns quoted are net of fees. Please note the fund returns are based on mid-day pricing, and benchmark returns are priced at end of day. Please note that with effect from 1 February 2024 RLAM are using peer group comparisons provided by Morningstar. Prior to this peer comparisons were provided by Lipper so there may be some differences compared to the data provided historically.

All IA sector performance shown is for the median.

[1] The composite benchmark consists of: 30% Bloomberg UK government Inflation Linked Bond 1-10 year index, 70% Bloomberg World Government Inflation Linked Bond (Ex UK) 1-10 year index (GBP Hedged).

Government Bond Market Review

Market highlights

- The sell off in Global Fixed Income markets continued in February, with UK government bond yields rising throughout the month. The sterling credit market outperformed conventional government bonds due to the lower duration of credit indices and a tightening of credit spreads.
- The benchmark 10-year gilt yield rose to 4.12% at the end of February, from 3.75% at the start of the month, meaning the FTSE UK Conventional Gilt All-Stocks index returned -1.11% for the month. Year to date, yields have reversed around half of the falls seen in the final two months of 2024.
- As expected, the Bank of England kept rates on hold at their February meeting. Although one committee member voted for a rate cut, two still voted for a hike. Data released in February again painted a mixed picture of economic activity; Labour market data was broadly stronger than expected, with a surprise fall in the unemployment rate to 3.8%; the market had been forecasting a rise to 4.0%. Average weekly earnings also surprised to the upside at 5.8%, despite falling from 6.5% previously. January CPI inflation remained at 4.0% year on year and core inflation was also steady on the month at 5.1%; both figures were lower than expected, as was services CPI. Fourth quarter GDP fell 0.3% quarter-on-quarter, weaker than expected and meaning that the UK recorded a technical recession in the second half of 2023. The February PMI business survey composite measure fell, though still signalled moderate private sector activity growth at 51.4.
- In the US, Federal Reserve speakers continued to signal that rate cuts were likely to commence this year, but without signalling urgency and while reiterating the need for more confidence in the path of inflation first. Inflation data was mostly stronger than expected. January CPI came in a touch stronger than expected at 0.3% versus the previous month, core inflation rose 0.4% on both PCE and CPI measures and so-called 'super-core' inflation rose further above 0.2% on both CPI and PCE measures. January nonfarm payrolls were much stronger than expected and the unemployment rate remained 3.7% rather than rising a tenth as expected. However, quite a large proportion of the activity data over the month disappointed. The February PMI business survey composite measure fell, though still signalled moderate private sector activity growth at 51.4.
- Several European Central Bank speakers mentioned that they see a first cut as possible/likely in the summer/June. President Christine Lagarde reiterated that upcoming wage data would be important in their analysis. January CPI fell to 2.8% year-on-year after 2.9%, a touch above expectations. Core CPI fell slightly, but annual services CPI again remained at 4.0%. Activity data released over the month were mixed. December retail sales fell, but industrial production rose and by more than expected. The February composite PMI rose to 48.9 from 47.9, a touch stronger than expected but still consistent with falling private sector activity (i.e., below 50).
- The sterling investment grade market (iBoxx) produced another negative return in February, marking two straight down months to start 2024, with a return of -0.66%. However, this was driven entirely by higher underlying government bond yields, with the average investment grade credit spread (the average extra yield available from a corporate bond compared with government debt of equal maturity) tightening to 1.07% from 1.13%.

Royal London Global Index Linked Bond Fund

Portfolio commentary

- Net of fund management fees, the fund returned -0.84% in February (Z Inc share class), against benchmark returns of -0.61%. It should be noted that returns can be distorted by the differing valuation points of the fund and index. On a like-for-like basis, the fund outperformed the index over the month.
- After weakness in January, yields rose in early February, pushed higher by the stronger US employment data and worse-than-expected inflation data. This led to decreased hopes of early rate cuts, and led to higher breakevens and a flatter yield curve. There was a modest rebound later in the month on softer UK inflation numbers and increased LDI demand.
- Our duration position was positive for returns over the month. We were slightly underweight early in the month, benefiting from the rise in yields, before going slightly long later in the month when yields rallied, before taking profits to end the month flat once more
- Cross-market positioning was a small positive over the month. Our underweight in Italy was helpful as these underperformed and we took profits on the position, while tactical trading of US TIPs relative to the UK added value as the spread between the two markets remained volatile. We also bought 30-year French and US bonds late in the month, selling UK equivalents that we believe will struggle into the syndication in March.
- Breakeven and curve positioning had no meaningful impact on performance over the month.

Investment outlook

- We believe that inflation will continue to drift lower in 2024, although it is likely to remain above target in most economies by the end of the year, particularly so in the UK, which appears more at risk of inflation becoming more embedded and persistent, than other G10 economies. Shallow recessions are possible but are unlikely to be deep enough at this stage to ease the excessive tightness seen in labour markets. Central banks are at peak rates, and markets are preparing themselves for cuts, but are now pricing these for the second half of 2024, having previously expected these to begin earlier.
- We expect yields to remain volatile around economic data, central bank meetings and ongoing geopolitical issues. We will look for opportunities to re-build a long duration stance, looking to benefit from supply events and a large UK index extension.
- Supply will be an issue for government bond markets over the next few years, with record supply in many with the notable exception of Australia. We expect these to provide opportunities, for instance the 30-year UK syndication in March, and will look to take tactical positions around these.

Key views within the fund

- The portfolio has a neutral duration position, after significant movements over the last three months.
- The fund has no strategic curve position, but on a tactical basis, is underweight the 30-year area relative to 15-year and 40-year due to the expected impact of the March syndication.
- The fund has no strategic breakeven positions, but we will look for tactical opportunities to sell breakevens as we move through 2024.
- The fund is underweight in the UK relative to global markets given the negative outlook from supply. Within global, we are underweight in Japan due to the expected end of the Bank of Japan's negative interest rate policy, and overweight the US.

CITYWIRE A

Paul Rayner
Head of Alpha Strategies

CITYWIRE AA

Gareth Hill
Fund Manager

ROYAL LONDON
ASSET MANAGEMENT

Royal London Index Linked Bond Fund

Portfolio commentary

- Net of fund management fees, the fund returned -0.93% in February (M Inc share class), against returns of 0.37% for benchmark. It should be noted that returns can be distorted by the differing valuation points of the fund and index. On a like-for-like basis, the fund slightly underperformed the index.
- After weakness in January, yields rose early in February, pushed higher by the stronger US employment data and worse-than-expected inflation data. This led to decreased hopes of early rate cuts, and led to higher breakevens and a flatter yield curve. There was a modest rebound later in the month on softer UK inflation numbers and increased LDI demand.
- Our duration position was positive for returns over the month. We were slightly underweight early in the month, benefiting from the rise in yields, before going slightly long later in the month when yields rallied, before taking profits to end the month flat once more
- Cross-market positioning was mixed over the month. Tactical trading of US TIPs relative to the UK added value as the spread between the two markets remained volatile, although our overseas exposure did hurt performance late in the month when the UK market performed well. We bought 30-year French and US bonds late in the month, selling UK equivalents that we believe will struggle into the syndication in March.
- Breakeven had no meaningful impact on performance over the month, while our curve positioning was negative.

Investment outlook

- We believe that inflation will continue to drift lower in 2024, although it is likely to remain above target in most economies by the end of the year, particularly so in the UK, which appears more at risk of inflation becoming more embedded and persistent, than other G10 economies. Shallow recessions are possible but are unlikely to be deep enough at this stage to ease the excessive tightness seen in labour markets. Central banks are at peak rates, and markets are preparing themselves for cuts, but are now pricing these for the second half of 2024, having previously expected these to begin earlier.
- We expect yields to remain volatile around economic data, central bank meetings and ongoing geopolitical issues. We will look for opportunities to re-build a long duration stance, looking to benefit from supply events and a large UK index extension.
- Supply will be an issue for government bond markets over the next few years, with record supply in many with the notable exception of Australia. We expect these to provide opportunities, for instance the 30-year UK syndication in March, and will look to take tactical positions around these.

Key views within the fund

- The portfolio has a neutral duration position, after significant movements over the last three months.
- The fund has no strategic curve position, but on a tactical basis, is underweight the 30-year area relative to 15-year and 40-year due to the expected impact of the March syndication.
- The fund has no strategic breakeven positions, but we will look for tactical opportunities to sell breakevens as we move through 2024.
- The fund is underweight in the UK relative to global markets given the negative outlook from supply.

Paul Rayner
Head of Alpha Strategies

Ben Nicholl
Fund Manager

Royal London Short Duration Global Index Linked Bond Fund

Portfolio commentary

- Net of fund management fees, the fund returned -0.94% in February (Z Inc share class), compared to benchmark returns of -0.79%. It should be noted that returns can be distorted by the differing valuation points of the fund and index. On a like-for-like basis, the fund slightly underperformed the index over the month.
- After weakness in January, yields rose early in February, pushed higher by the stronger US employment data and worse-than-expected inflation data. This led to decreased hopes of early rate cuts, and led to higher breakevens and a flatter yield curve. There was a modest rebound later in the month on softer UK inflation numbers and increased LDI demand.
- Our duration position was positive for returns over the month. We were slightly underweight early in the month, benefiting from the rise in yields, before going slightly long later in the month when yields rallied, before taking profits to end the month flat once more
- Cross-market positioning was a small negative over the month. Our underweight in Italy was helpful as these underperformed and we took profits on the position, while tactical trading of US TIPs relative to the UK added value as the spread between the two markets remained volatile. However, exposure to US was negative later hurt performance due to the market pricing out rate cuts in the first half of 2024.
- Breakeven and curve positioning had no meaningful impact on performance over the month.

Investment outlook

- We believe that inflation will continue to drift lower in 2024, although it is likely to remain above target in most economies by the end of the year, particularly so in the UK, which appears more at risk of inflation becoming more embedded and persistent, than other G10 economies. Shallow recessions are possible but are unlikely to be deep enough at this stage to ease the excessive tightness seen in labour markets. Central banks are at peak rates, and markets are preparing themselves for cuts, but are now pricing these for the second half of 2024, having previously expected these to begin earlier.
- We expect yields to remain volatile around economic data, central bank meetings and ongoing geopolitical issues. We will look for opportunities to re-build a long duration stance, looking to benefit from supply events and a large UK index extension.
- Supply will be an issue for government bond markets over the next few years, with record supply in many with the notable exception of Australia. We expect these to provide opportunities, for instance the 30-year UK syndication in March, and will look to take tactical positions around these.

Key views within the fund

- The portfolio has a neutral duration position, after significant movements over the last three months.
- In terms of curve positioning, the fund has a bias towards 10-year bonds over five-year equivalents, with the latter expected to underperform as the March 2029 issue drops out of longer indices, which we expect to lead to selling pressure.
- The fund has no strategic breakeven positions, but we will look for tactical opportunities to sell breakevens as we move through 2024.
- The fund is neutral in terms of UK vs global markets. Within global, we remain overweight in short dated Japanese bonds due to the attractive carry available on Japanese bonds hedged back into sterling. However, we are underweight longer dated Japanese bonds as yields are expected to rise as negative interest rate policy is ended.

CITYWIRE A

Paul Rayner
Head of Alpha Strategies

MORNINGSTAR Bronze

CITYWIRE AA

Ben Nicholl
Fund Manager

Royal London Short Duration Gilt Fund

Portfolio commentary

- Net of fees, the fund was behind its benchmark in February but it should be noted that returns can be distorted by the differing valuation points of the fund and index. On a like-for-like timing basis, the fund outperformed the index.
- The main story dominating headlines, and the attention of investors, during the month was interest rates. In particular, the chatter was centred around when, and how many, cuts we can expect to see in base rates.
- Yields were broadly higher, a trend seen in the UK, US and across Europe. The rise in yields was seen most at the front-end of the curve, with 30-year yields rising less sharply – resulting in a flattened curve.
- The sell-off at the front-end was driven by the economic data coming in the month being generally stronger than expected. As a result, the market started to pull back on its base rate expectations. At the start of the month, in the UK, markets had priced base rates to be 4.0% at year-end, but this had risen to 4.5% at the end of February.
- With this shift, the market now expects the Bank of England's first cut to come in August.
- The fund started the month slightly long relative to the benchmark and added duration, ending the period about 0.3 of a year long. We decided to add duration as yields rose, with our duration coming from 2029 gilts.
- The fund's duration position remains focused in the 5-year portion of the curve, which was the main detractor from performance during the month but we tactically traded around market volatility – which helped offset some our strategic position.
- We started adding duration when 5-year yields hit the 4% mark – which was around the middle of the month – and we did not see yields rise much further from that position.
- The fund remains overweight in the two-to-three part of the curve – which was broadly neutral for performance.
- Our relative-value positioning was flat for performance. The large overweight position in certain 2025 and 2027 bonds we hold have seen strong performance versus neighbouring bonds.
- During the period, the fund added 6-month UK Treasury bills, with the yield on them coming in 25-30bps higher than 5-year gilts.
- The fund has no inflation exposure.

Investment outlook

- We believe that inflation will continue to drift lower in 2024, although it is likely to remain above target in most economies by the end of the year, particularly so in the UK, which appears more at risk of inflation becoming more embedded and persistent, than other G10 economies. Shallow recessions are possible but are unlikely to be deep enough at this stage to ease the excessive tightness seen in labour markets. As we enter 2024, central banks are at peak rates, and markets are preparing themselves for cuts, starting in the first half of 2024.
- In the UK, the market is now assuming base rates have peaked at 5.25%, with the first cut priced in for the first half 2024 and falling to a terminal level of around 3.25% by late-2026. At one point in early July the market was pricing peak rates closer to 6.5%. Government bond markets have moved a long way during the last few months, particularly in the UK where five-year gilts have fallen significantly from their summer peak.
- Supply will be an issue for the market over the next few years, with around £200bn per annum forecast over each of the next five years. Alongside quantitative tightening (where the BoE is selling its gilt holdings back into the market), this will represent a headwind for gilts. However, when considering gilts in a global context, we believe the gilt market is somewhat priced for this.

Key views within the fund

- The portfolio’s duration is long of the benchmark, including the impact of cash holdings on duration.
- The portfolio has allocations to high quality corporate bonds, which we expect to outperform gilts.

Paul Rayner
Head of Alpha Strategies

Ben Nicholl
Fund Manager

Royal London UK Government Bond Fund

Portfolio commentary

- Net of fees, the fund was behind its benchmark in February but it should be noted that returns can be distorted by the differing valuation points of the fund (12:00) and index (16:15). On a like-for-like timing basis, the fund outperformed the index.
- The main story dominating headlines, and the attention of investors, during the month was interest rates. In particular, the chatter was centred around when, and how many, cuts we can expect to see in base rates.
- Yields were broadly higher, a trend seen in the UK, US and across Europe. The rise in yields was seen most at the front-end of the curve, with 30-year yields rising less sharply – resulting in a flattened curve.
- The sell-off at the front-end was driven by the economic data coming in the month being generally stronger than expected. As a result, the market started to pull back on its base rate expectations. At the start of the month, in the UK, markets had priced base rates to be 4.0% at year-end, but this had risen to 4.5% at the end of February.
- With this shift, the market now expects the Bank of England's first cut to come in August.
- The fund started the month slightly long relative to the benchmark and added duration, ending the period about 0.4 of a year long. We decided to add duration as yields rose, with our duration addition being focused in the 15-year part of the curve.
- The funds duration position marginally detracted from performance during the month but we tactically traded around market volatility – which helped offset our strategic position.
- Our curve position was broadly neutral for performance. Our steepening bias in 5/10s (overweight 5-year maturity gilts and underweight 10-year maturity gilts) detracted from performance, but this was offset by our heavy overweight in 15-year maturity gilts, and a flattening bias in longer maturity bonds.
- Our cross-market positioning was also broadly flat for performance. We had retained a small residual position in Australia but took profit on the position during the month, selling 30-year Aussie bonds when yields were flat to 30-year maturity gilts.
- The fund had a small inflation exposure through a holding in linker 2051s. We took profit on this at the start of February as index linked bonds outperformed and break-evens rose.
- Finally, as credit spreads on corporate bonds tightened, we took the opportunity to sell out of long-dated credit positions in the fund – namely Oxford University, State of Jersey and Church Commissioners of England. Spreads on these bonds were at near all-time lows. A small portion of the fund is still invested in high-quality credit, but it is now focused in sub-5-year bonds.

Investment outlook

- We believe that inflation will continue to drift lower in 2024, although it is likely to remain above target in most economies by the end of the year, particularly so in the UK, which appears more at risk of inflation becoming more embedded and persistent, than other G10 economies. Shallow recessions are possible but are unlikely to be deep enough at this stage to ease the excessive tightness seen in labour markets. As we enter 2024, central banks are at peak rates, and markets are preparing themselves for cuts, starting in the first half of 2024.
- In the UK, the market is now assuming base rates have peaked at 5.25%, with the first cut priced in for the first half 2024 and falling to a terminal level of around 3.25% by late-2026. At one point in early July the market was pricing peak rates closer to 6.5%. Government bond markets have moved a long way during the last few months, particularly in the UK where five-year gilts have fallen significantly from their summer peak.
- Supply will be an issue for the market over the next few years, with around £200bn per annum forecast over each of the next five years. Alongside quantitative tightening (where the BoE is selling its gilt holdings back into the market), this will represent a headwind for gilts. However, when considering gilts in a global context, we believe the gilt market is somewhat priced for this.

Key views within the fund

- The portfolio's duration is slightly long versus the index, including the impact of cash holdings on duration, although we continue to trade around this as market volatility provides opportunities to add value.
- The fund retains an exposure to steepening via its overweight in 5-year maturity bonds versus 10-year maturity bonds, but then a flattening bias thereafter due to an overweight in 15- and 30-year maturity bonds. The fund remains underweight 50-year maturity gilts versus 30-year maturity bonds.
- The fund holds no overseas government bonds.
- The fund holds no index linked bonds currently.
- The portfolio has allocations to high quality corporate bonds which provide additional yield for the portfolio.

CITYWIRE A

Paul Rayner
Head of Alpha Strategies

MORNINGSTAR Bronze

CITYWIRE AA

Ben Nicholl
Fund Manager

Royal London Asset Management Global High Yield Fund Performance

	1 month (%)	Rolling 12 Months (%)
RL Global High Yield Bond Fund M Inc	**0.11**	**8.01**
RL Global High Yield Bond Fund Z Inc	**0.14**	**8.22**
IA Sterling High Yield Sector	0.28	9.35
ICE BofA ML BB-B Global Non-Financial High Yield Constrained Index	0.27	9.82
RL Short Duration Global High Yield Bond Fund A Inc	**0.21**	**6.77**
RL Short Duration Global High Yield Bond Fund M Inc	**0.24**	**7.21**
RL Short Duration Global High Yield Bond Fund Z Inc	**0.25**	**7.32**
IA Sterling High Yield Sector	0.28	9.35
Sterling Overnight Index Average Rate (SONIA)[1]	0.40	4.87

Past performance is not a guide to 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 Morningstar, correct as of 29 February 2024. Returns quoted are net of fees. Please note that with effect from 1 February 2024 RLAM are using peer group comparisons provided by Morningstar. Prior to this peer comparisons were provided by Lipper so there may be some differences compared to the data provided historically.

All IA sector performance shown is for the median.

Royal London Global High Yield Bond Fund

Portfolio commentary

- The fund returned 0.11% (M Inc), net of fees, in February, which was behind the benchmark, the ICE BofA Merrill Lynch BB-B Global Non-Financial High Yield Constrained Index (100% GBP hedged), return of 0.27%. Against the fund's objective, outperforming its benchmark by 1% per annum over rolling thee-year periods, it is slightly behind of the benchmark, gross of fees (-0.10% versus -0.06%).
- The global high yield market produced a GBP-hedged monthly return of +0.27% in February to mark four months in a row with positive returns. This return came from carry and spread tightening as global high yield spreads (BB-B index) tightened 35bps during the month with the government yield curve widening by 38bps during the month. The high yield market is now yielding 7.1% (YTW) with a duration of 3.6 years.
- The fund's yield, FX-adjusted, stood at 7.3% (YTW) at the end of February, with a duration of 4.1 years.
- The month of February saw a continuation of the strong amount of high yield new issuance at $26.5bn, down $6bn from January but still higher than any other month since January 2022. The issuance was split 40% BB, 52% single B rated and 8% CCC rated companies.
- The US high yield default rate was unchanged in February, sitting at 2.3%. February's rate means the default rate in the US high yield market has not exceeded 3% since May 2021, and never topped 2.5% in 2023. For comparison, during the GFC the default rate was seen over 20% and it was over 7% during the pandemic. The global high yield rate inched higher, however, nudging upward to 2.8% from 2.7% but is lower than the 4.0% seen in February last year.
- These default levels would be entirely normal in an historic context, but the nature of the economic backdrop and strong company balance sheets means we expect default rates to grind higher, instead of sharply spiking.
- In the fund, the main contributors to our performance was our energy, leisure and telecommunications holdings. Relative to the benchmark, telecommunications was also a strong outperformer with our media bonds outperforming too. Lagging the benchmark, were our capital goods, retail and technology & electronics holdings – with all three also seeing negative total returns. By rating, both our BB and B rated bonds were behind the benchmark but our preference for single B rated bonds contributed strongly to performance. While outside the benchmark, our BBB & Above holdings recorded negative total returns but this was offset by our CCC& Below bonds. Regionally, our European holdings was the standout performer, relatively and in terms of total return. Our UK holdings also contributed, while our US and RoW holdings saw a poor relative return versus the benchmark.
- For the market, all regions produced positive returns during the month with the RoW relatively outperforming. With respect to sectors, only media and technology & electronics produced negative returns. Real estate was the outperformer on a relative basis.

*YIELD-TO-WORST REFERS TO THE REDEMPTION DATE THAT PRODUCES THE LOWEST RETURN

Investment outlook

- Our focus will remain on the Fed. With inflation expected to fall back towards the long-term target, the levels that the Fed is happy with and when it then begins to lower rates will be the key factor for the upcoming year. The resiliency of the economy has led to the narrative that interest rates will now stay 'higher-for-longer'. With monetary policy lags appearing longer than they used to be there is some recognition by central banks that policy tightening needs time to work and that the impacts of policy tightening are still feeding through. This is causing spreads to tighten as investors are now convinced the fallout won't be coming until late 2024 or early 2025.
- Current default rates are very low at around 2-3% and while we expect this to track to 3%-5% over the course of 2024. These levels would be entirely normal in an historic context, but the nature of the economic backdrop and strong company balance sheets means we expect default rates to grinding higher over this period, instead of sharply spiking. Even if default rates creep higher than our target range we don't see this as particularly worrying as it won't change the fundamentals of the high yield market and will only come about from Fed monetary policy, which has been priced into corporate valuations, instead of, as of yet, unknown increased economic hardship.
- With this in mind, we believe 2024 should play out similarly to 2023: maturity wall concerns being overplayed; companies holding high liquidity; private debt markets eating the bottom cohort of public markets; public markets remaining open, with solid issuance levels. As long as public markets stay open, any maturity wall concerns will be swept away. And, as long as private markets are taking away the weakest parts of public markets, defaults should stay low.

- In our view, the way through difficult markets is to focus on those risks that you can control and know what you own. We will keep spread duration low and focus on the quality of issuers' financials, rather than relying on third-party ratings: at a sectoral level, cashflows are the key factor, meaning we need to know about on- and off-balance sheet leverage. We prefer not to wait for defaults as the recovery process can take time: however, should they occur, the key is to have an adequate solvency cushion.

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.
- 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 market volatility to continue due to market expectations surrounding 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. There seems little chance of a near-term resolution of the conflict in Ukraine – this also has significant implications for the global economy, particularly if ongoing higher energy prices and supply chain disruption exacerbate a global economic slowdown.

Azhar Hussain
Head of Global Credit

Stephen Tapley
Global Credit Fund Manager

Royal London Short Duration Global High Yield Bond Fund

Portfolio commentary

- The monthly return was 0.24% (M Inc) on a net basis, while the benchmark returned 0.40% in February.
- The global high yield market produced a GBP-hedged monthly return of +0.27% in February to mark four months in a row with positive returns. This return came from carry and spread tightening as global high yield spreads (BB-B index) tightened 35bps during the month with the government yield curve widening by 38bps during the month. The high yield market is now yielding 7.1% (YTW) with a duration of 3.6 years.
- The fund's GBP-expected FX-adjusted yield increased by 44bps to 6.69% with an expected duration of 1.2 years.
- The month of February saw a continuation of the strong amount of high yield new issuance at $26.5bn, down $6bn from January but still higher than any other month since January 2022. The issuance was split 40% BB, 52% single B rated and 8% CCC rated companies.
- The US high yield default rate was unchanged in February, sitting at 2.3%. February's rate means the default rate in the US high yield market has not exceeded 3% since May 2021, and never topped 2.5% in 2023. For comparison, during the GFC the default rate was seen over 20% and it was over 7% during the pandemic. The global high yield rate inched higher, however, nudging upward to 2.8% from 2.7% but is lower than the 4.0% seen in February last year.
- These default levels would be entirely normal in an historic context, but the nature of the economic backdrop and strong company balance sheets means we expect default rates to grind higher, instead of sharply spiking.
- For the market, all regions produced positive returns during the month with the RoW relatively outperforming. With respect to sectors, only media and technology & electronics produced negative returns. Real estate was the outperformer on a relative basis.
- Decomposing the funds' assets: UK and European assets outperformed on a relative basis, but with RoW and US assets still producing positive returns. By rating, the fund's single B rated assets relatively outperformed with the fund's BB rated assets still producing a positive return. By sector, leisure and telecommunications relatively outperformed, with media and financial services underperforming relatively, and also producing a negative return.
- Asset composition by region and rating were both broadly unchanged on the month.
- Following the high amount of new issuance in the market in January, several companies used those proceeds to redeem outstanding debt. As a result, the fund's holdings in **Ball**, **Caesars**, **Cirsa, Ineos**, and **Transdigm** were redeemed during February.
- Overall, the cash level was 5.6% at end of the month.

*FX ADJUSTED YIELD IS THE GROSS RATE OF RETURN TO THE EXPECTED MATURITY ADJUSTED FOR HEDGING AND INCLUSDES THE IMPACT OF CASH

Investment outlook

- Our focus will remain on the Fed. With inflation expected to fall back towards the long-term target, the levels that the Fed is happy with and when it then begins to lower rates will be the key factor for the upcoming year. The resiliency of the economy has led to the narrative that interest rates will now stay 'higher-for-longer'. With monetary policy lags appearing longer than they used to be there is some recognition by central banks that policy tightening needs time to work and that the impacts of policy tightening are still feeding through. This is causing spreads to tighten as investors are now convinced the fallout won't be coming until late 2024 or early 2025.
- Current default rates are very low at around 2-3% and while we expect this to track to 3%-5% over the course of next year. These levels would be entirely normal in an historic context, but the nature of the economic backdrop and strong company balance sheets means we expect default rates to grinding higher over this period, instead of sharply spiking. Even if default rates creep higher than our target range we don't see this as particularly worrying as it won't change the fundamentals of the high yield market and will only come about from Fed monetary policy, which has been priced into corporate valuations, instead of, as of yet, unknown increased economic hardship.
- With this in mind, we believe 2024 should play out similarly to 2023: maturity wall concerns being overplayed; companies holding high liquidity; private debt markets eating the bottom cohort of public markets; public markets remaining open,

with solid issuance levels. As long as public markets stay open, any maturity wall concerns will be swept away. And, as long as private markets are taking away the weakest parts of public markets, defaults should stay low.

- In our view, the way through difficult markets is to focus on those risks that you can control and know what you own. We will keep spread duration low and focus on the quality of issuers' financials, rather than relying on third-party ratings: at a sectoral level, cashflows are the key factor, meaning we need to know about on- and off-balance sheet leverage. We prefer not to wait for defaults as the recovery process can take time: however, should they occur, the key is to have an adequate solvency cushion.
- With yields at current levels and appealing potential returns, we will be paid sufficiently for maintaining a lower-risk position for at least another quarter until there is more clarity about the outlook. In keeping with the core focus of the strategy, we will keep duration low and focus on the quality of issuers' financials, rather than relying on third-party ratings. At a sectoral level, cashflows are the key factor and we continue to favour companies with contracted revenues. With regards to geography, our global outlook provides diversification away from country-specific 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 market volatility to continue due to market expectations surrounding 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. There seems little chance of a near-term resolution of the conflict in Ukraine – this also has significant implications for the global economy, particularly if ongoing higher energy prices and supply chain disruption exacerbate a global economic slowdown.

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