STRATEGY UPDATE

INVESTMENT CLOCK

STRATEGIC ASSET ALLOCATION REVIEW

November 2020

ROYAL LONDON ASSET MANAGEMENT

Royal London Asset Management manages £137.6 billion in life insurance, pensions and third party funds*. The multi asset team manages the Governed Range pension portfolios, as well as the Global Multi Asset Portfolios (GMAPs) and Multi Asset Strategies Fund (MAST) available on third party platforms.

*As at 30/09/2020

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We are increasing the strategic weights for high yield bonds by 2.5% at the expense of property in three of the GMAPs to increase diversification and improve liquidity.

Within equities we take the UK's strategic weight to just below 40% from 50%, while adding to the emerging markets and rest of world equities to increase exposure to faster growing countries and sectors.

We retain a broader mix of assets than many competitors and a deliberate bias in favour of assets expected to generate long term growth relative to UK inflation.

Please visit www.investmentclock.co.uk for our blog and information about our multi asset range. For product details, contact: multiassetsupport@rlam.co.uk

We are adjusting the strategic asset mix for our Global Multi Asset Portfolios following a periodic review. Changes increase international diversification and seek to improve expected returns while ensuring each fund remains well within its risk band. High yield bond weights go up funded out of property and a new blend within equities gives greater exposure to faster growing countries and sectors. Our deliberately broad asset mix lagged behind less diversified balanced funds in the deflationary shock of 2020 but it has similar long run returns and we expect it to do better over a wider range of future scenarios.

Changes to improve diversification and seek higher returns

We conduct a formal review of the strategic mix of the GMAP funds every three years to ensure they remain consistent with their risk targets, so we can adapt our approach as the investment backdrop evolves. Changes will increase international diversification and seek to improve expected returns. The new weightings will form the central position around which we will take our active tactical positions.

Implementation over the next couple of months

We do not need to sell property or buy high yield bonds as exposures in the relevant funds are already tilted in this direction. We plan to adjust equity exposures early in 2021 but have the flexibility to keep UK exposure close to previous levels, should we judge near term prospects to be improving on the back of vaccine deployment.

Multi asset for a more inflationary post-Covid recovery

The GMAPs were launched for sterling-based investors facing UK interest rate and inflation risks. We select an efficient strategic asset mix for each fund in order to maximise long run returns versus inflation for a given level of risk. Our mix with its broad asset class universe and greater exposure to UK assets lagged behind funds blending only global equities and bonds in 2020 but our line up offers good value and should do better over what could be a more inflationary post-Covid recovery.

Chart 1: New GMAP Strategic Asset Class Weights (%)

New Benchmark	GMAP Defensive	GMAP Balanced	GMAP Growth	GMAP Adventurous	GMAP Dynamic
UK Equities	5.6	12.1	20.5	25.2	37.4
Overseas Developed Equities	7.7	16.7	28.3	34.6	51.3
EM Equities	1.7	3.7	6.2	7.7	11.3
Property	5.0	10.0	12.5	15.0	0.0
Commodities	5.0	5.0	5.0	5.0	0.0
Global High Yield	10.0	5.0	5.0	2.5	0.0
UK IG Fixed income	50.0	35.0	15.0	5.0	0.0
Cash	15.0	12.5	7.5	5.0	0.0
Total	100.0	100.0	100.0	100.0	100.0

Change	GMAP Defensive	GMAP Balanced	GMAP Growth	GMAP Adventurous	GMAP Dynamic
UK Equities	-1.9	-4.2	-7.0	-8.5	-12.6
Overseas Developed Equities	0.9	1.9	3.3	3.9	5.8
EM Equities	1.0	2.2	3.7	4.7	6.8
Property		-2.5	-2.5	-2.5	
Commodities					
Global High Yield		2.5	2.5	2.5	
UK IG Fixed income					
Cash					
Total	0.0	0.0	0.0	0.0	0.0

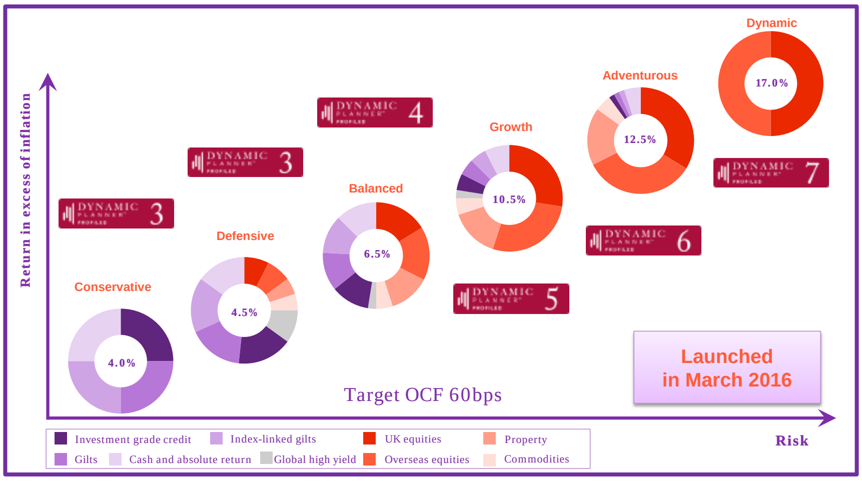
New benchmark details for each fund will be published in due course.

DESIGNED TO MAXIMISE RETURNS AFTER UK INFLATION

The GMAPs were launched for sterling-based investors facing UK interest rate and inflation risks. The strategic mix for each fund is designed to maximise long term return after inflation. We conduct formal reviews every three years to ensure the funds are consistent with their risk targets and so we can adapt our approach as the investment backdrop evolves.

Changes increase international diversification and seek to improve expected returns by raising high yield bonds out of UK property and shifting to a blend within equities that gives greater exposure to faster growing countries and sectors.

Chart 2: Royal London's GMAP range with long run risk targets



We diversify broadly, looking for assets with a proven track record in generating returns that can beat UK inflation or reduce risk.

Our asset mix lagged behind simple balanced funds blending only global equities and bonds in the deflationary Covid shock, as gilts rallied and US technology stocks led global equities higher. We expect our broader mix to do better over a wider range of future scenarios. Many of the 'losers' of 2020 are likely to rebound significantly as the Covid crisis comes to an end.

Chart 3: A wide spectrum of returns in 2020

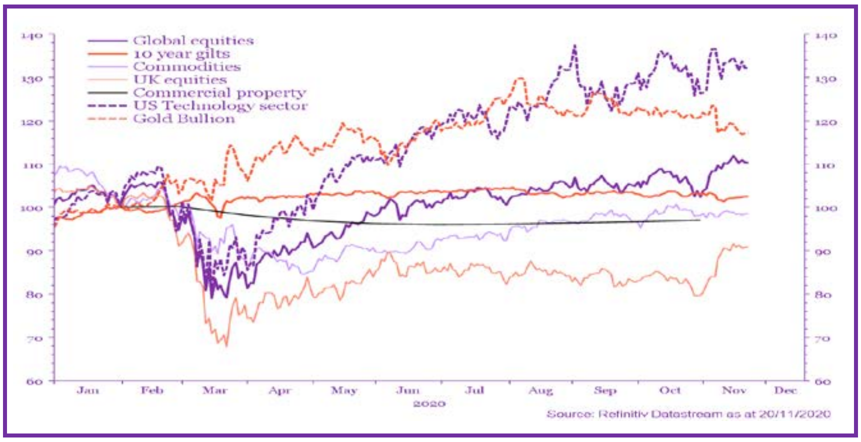


Chart 4: Annual Asset Class Returns for a UK Investor

Year	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	YTD
1	EM Stocks +37.4%	Gilts +12.8%	EM Stocks +62.5%	EM Stocks +23.6%	Gilts +15.6%	EM Stocks +12.8%	Global Stocks +21.2%	Property +19.5%	Property +13.9%	EM Stocks +35.4%	EM Stocks +21.1%	Property +7.5%	Global Stocks +22.6%	Global Stocks +10.7%
2	Commodities +14.3%	Cash +5.7%	UK Stocks +30.1%	Commodities +20.5%	Property +8.1%	UK Stocks +12.3%	UK Stocks +20.8%	Gilts +13.9%	Global Stocks +4.4%	Commodities +33.3%	Global Stocks +14.0%	Cash +0.6%	UK Stocks +19.2%	EM Stocks +9.2%
3	Global Stocks +11.2%	Commodities -10.9%	Global Stocks +20.6%	Global Stocks +17.2%	Cash +0.6%	Global Stocks +12.1%	**Multi Asset +12.1%**	Global Stocks +12.2%	**Multi Asset +2.5%**	Global Stocks +30.3%	UK Stocks +13.1%	Gilts +0.6%	EM Stocks +15.9%	Gilts +6.2%
4	Cash +6.0%	**Multi Asset -17.2%**	**Multi Asset +16.6%**	Property +14.7%	**Multi Asset +0.1%**	**Multi Asset +8.6%**	Property +11.0%	**Multi Asset +8.2%**	UK Stocks +1.0%	**Multi Asset +17.1%**	Property +11.2%	**Multi Asset -2.5%**	**Multi Asset +13.2%**	**Multi Asset +0.4%**
5	**Multi Asset +5.8%**	Global Stocks -18.5%	Commodities +5.9%	UK Stocks +14.5%	UK Stocks -3.5%	Gilts +2.7%	Cash +0.5%	EM Stocks +7.9%	Gilts +0.6%	UK Stocks +16.8%	**Multi Asset +9.4%**	Global Stocks -3.1%	Gilts +6.9%	Cash +0.3%
6	UK Stocks +5.3%	Property -22.6%	Property +1.9%	**Multi Asset +14.2%**	Global Stocks -6.9%	Property +2.3%	Gilts -3.9%	UK Stocks +1.2%	Cash +0.5%	Gilts +10.1%	Gilts +1.8%	Commodities -5.7%	Commodities +3.5%	Property -2.6%
7	Gilts +5.3%	UK Stocks -29.9%	Cash +1.0%	Gilts +7.2%	Commodities -12.7%	Cash +0.6%	EM Stocks -5.3%	Cash +0.5%	EM Stocks -10.3%	Property +2.6%	Cash +0.3%	EM Stocks -7.6%	Property +2.1%	Commodities -8.3%
8	Property -5.4%	EM Stocks -34.8%	Gilts -1.2%	Cash +0.6%	EM Stocks -18.4%	Commodities -5.4%	Commodities -11.2%	Commodities -11.8%	Commodities -20.3%	Cash +0.4%	Commodities -7.1%	UK Stocks -9.5%	Cash +0.7%	UK Stocks -12.2%

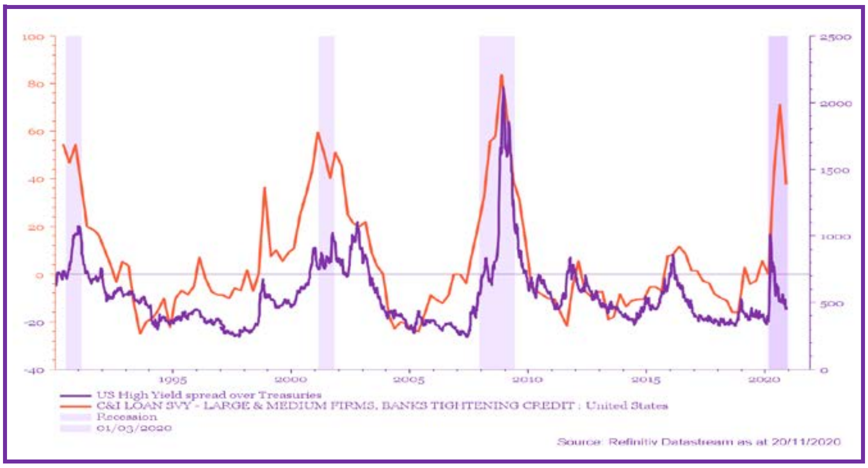
Source: RLAM, DataStream as at 20 November 2020; property as at October 2020. 'Multi Asset' returns are based on the benchmark weights of Royal London Global Multi Asset Portfolio (GMAP) Growth Fund / Governed Portfolio 5. Indices used are FTSE All World Ex-UK, FTSE All Share, FTSE British Govt Fixed All Stocks, JPM Cash UK 1 month Index, Bloomberg Commodity Index, MSCI UK Monthly Property Index and the FTSE Emerging Markets Index. Total returns in sterling terms.

INCREASING HIGH YIELD OUT OF PROPERTY

We are improving international diversification and liquidity by making a 2.5% increase to the strategic weight of sterling-hedged global high yield bonds in the GMAP Balanced, Growth and Adventurous funds while trimming property.

The high yield market has offered a good risk-adjusted return over the long run and downside risk in a crisis may be somewhat lower than in the past, judging by the speed with which the Federal Reserve intervened in credit markets in 2020. We have been tactically overweight the asset class.

Chart 5: High yield spreads and US senior loan officer survey

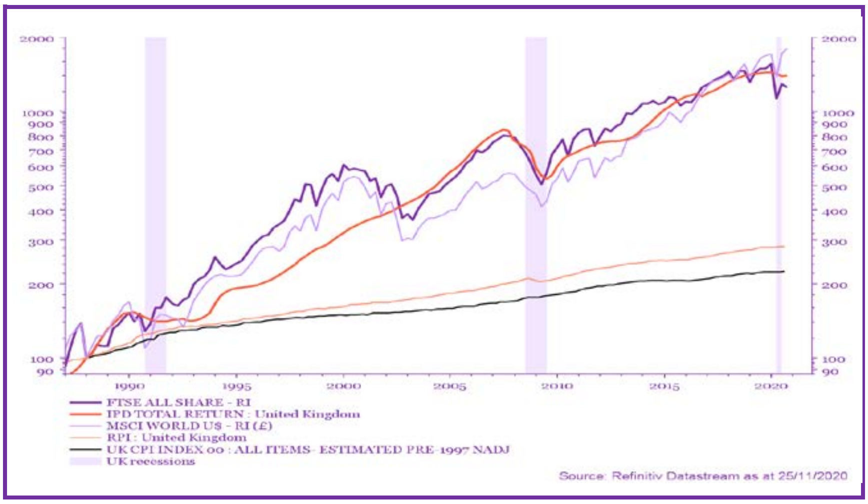


Source: RLAM and Refinitiv Datastream

Property has been impacted considerably by social distancing in 2020 and we have been tactically underweight.

While we are reducing its strategic weighting somewhat, we continue to see commercial property as a very important diversifier within the growth-seeking part of our portfolios. It has generated a similar inflation-beating return to UK and global equities over the long run but sometimes sails through equity bear markets unscathed. A good example is the dot com crash of 2001-3 when expensive global stock markets were de-rating but the UK economy and property markets stayed strong.

Chart 6: Long term property and equity returns versus inflation

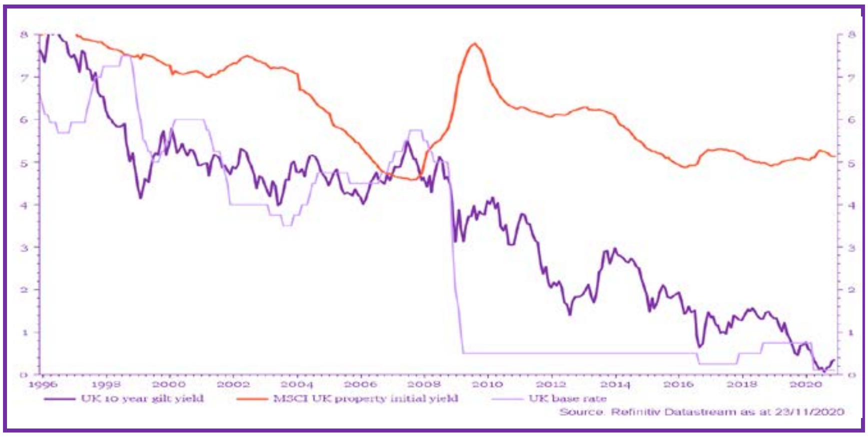


Source: RLAM and Refinitiv Datastream

The near term outlook for property is very uncertain but a re-opening of economies over 2021 should be positive and the most impacted sectors, such as high street retail, are a very small part of the market.

Rental yields of around 5% look very attractive in a low interest rate world, especially as rents tend to rise with inflation over the long run.

Chart 7: Property offers a high yield and is cheap versus bonds



Source: RLAM and Refinitiv Datastream

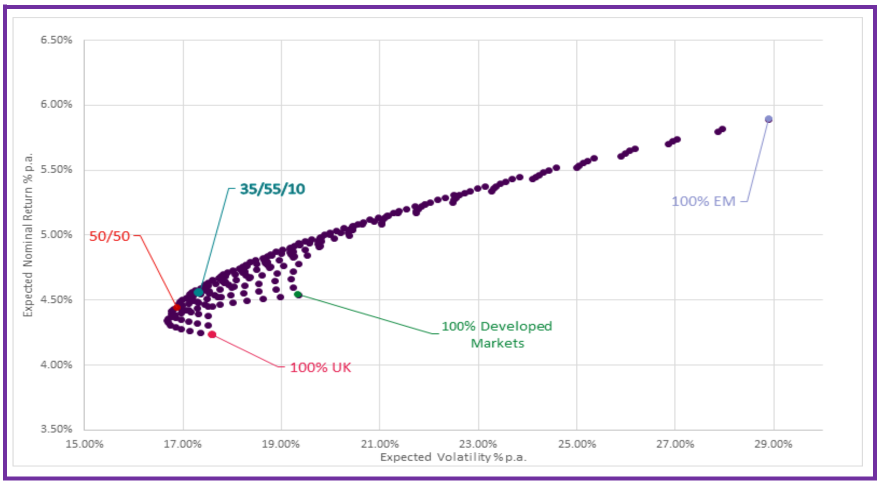
ACCESSING FASTER GROWING COUNTRIES AND SECTORS

Shifting property into high yield in the strategic allocation mix allows us to take more risk within equities which we are using to increase exposure to faster growing countries and sectors. The previous 50/50 split between UK and overseas equities moves to one that divides the allocation three ways.

The new blend is 35/55/10 for UK equities, global equities* and the emerging markets, accessing the latter using an ESG-screened index, as corporate and social standards can be lower.

* *including some additional UK exposure*

Chart 8: A higher risk/return position on the efficient frontier

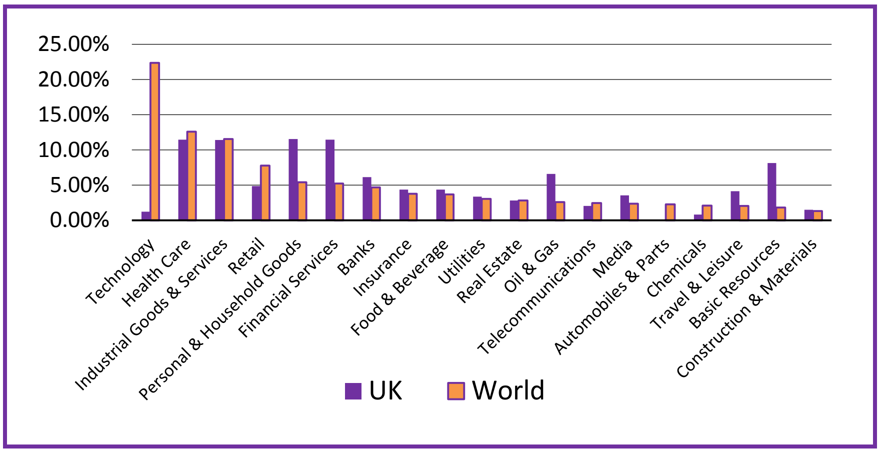


Source: Royal London, Moody's Analytics

Emerging economies, including China, make up 40% of the world economy but only a small proportion of global indices. An additional allocation here seeks to increase expected returns and reduces our exposure to the UK economy, which is likely to grow at a slower pace after the Brexit transition period ends.

By adding more to global equities, we also increase exposure to faster growing sectors like technology, which are under-represented in the UK market.

Chart 9: Sector breakdown for UK and world equities

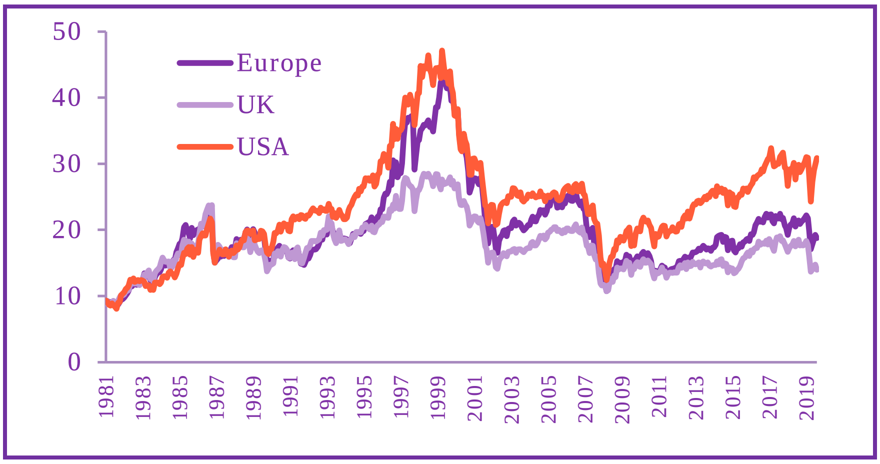


Source: RLAM and Refinitiv Datastream. FTSE indices.

While we are reducing its strategic weight, we maintain a deliberate bias towards UK equities. This gives us a more balanced sector exposure, lower currency risk and a closer linkage via domestically-generated profits and dividends to UK inflation trends.

We have the tactical flexibility to keep UK exposure in the funds close to previous levels, should we judge prospects to be improving during the post-Covid recovery. The UK equity market offers very good value whether compared to other markets, or its own history.

Chart 10: The UK is cheap versus other markets and history



Source: Barclays. Chart shows cyclically-adjusted price earnings ratios.

MORE DIVERSIFIED WITH A CLOSER LINK TO UK INFLATION

Our more diversified asset mix has generated a similar long run return when compared to balanced funds with the same level of risk but it has lagged in the Covid shock of 2020. Below we compare the long term performance and diversification characteristics of the GMAP Growth strategic mix to a notional balanced fund with 60% in global equities and 40% in UK investment grade bonds.

The Global Balanced Mix

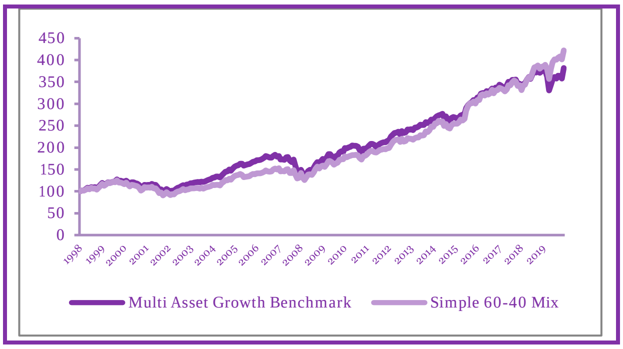
- Invests nearly 40% of its assets in US equities with expensive tech stocks dominating and around 30% in gilts vulnerable to a rise in yields; only 3% in UK real assets (equities) representing 7% of the income flowing into the fund; sterling exposure just over 40%

GMAP Growth Mix

- A more even asset class exposure investing almost 40% in UK real assets (UK equities, property and index-linked gilts), generating two-thirds of its income from these assets; sterling exposure c.60%

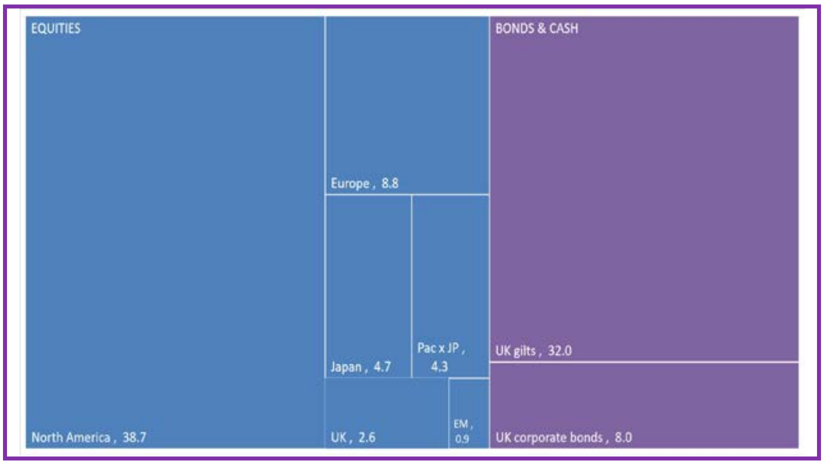
We believe our broader asset mix can provide good long run growth with greater resilience to the currency, interest rate and inflation risks facing UK investors over a wide range of future scenarios. We have a strong governance process and remain focused on these long term objectives.

Chart 11: Old GMAP Growth Mix vs "60/40"



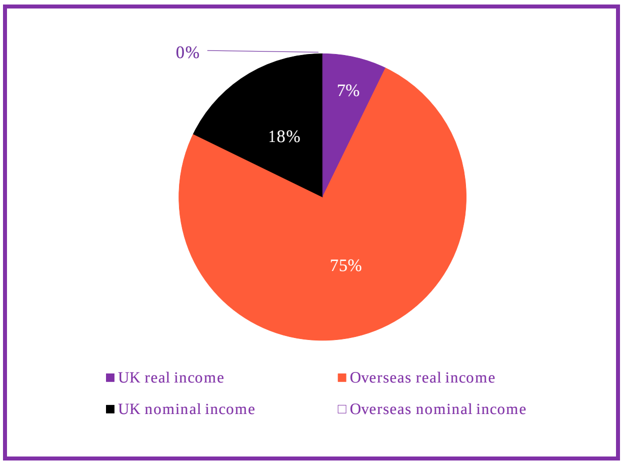
Source: RLAM, DataStream, as at 24 November 2020 Comparison of GMAP Growth strategic mix (prior to the current change) with a mix of 60% in global stocks and 40% in UK investment grade bonds.

Chart 12: 60/40 Balanced Fund strategic mix



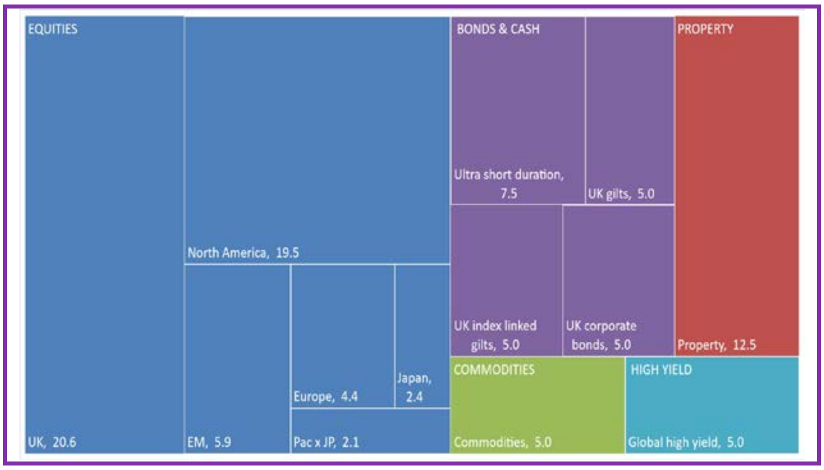
Source: RLAM. For illustration purposes only.

Chart 13: 60/40 fund income sources



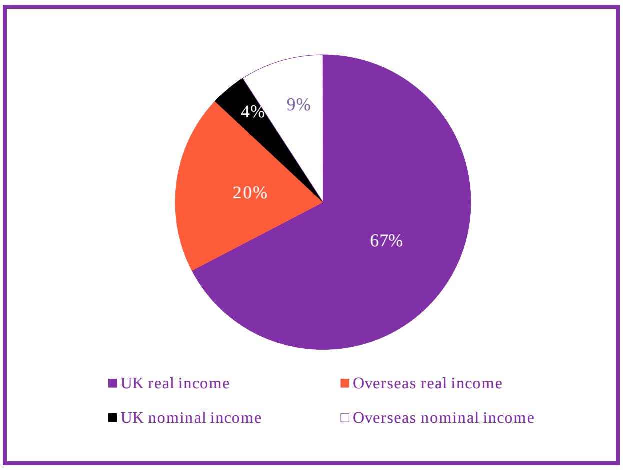
Source: RLAM. For illustration purposes only.

Chart 14: New GMAP Growth strategic mix



Source: RLAM

Chart 15: GMAP Growth income sources



Source: RLAM

Investment Risk: Past performance is not a guide to future performance. The value of investments and any income from them may go down as well as up and is not guaranteed. Investors may not get back the amount invested.

Credit Risk: Should the issuer of a fixed income security become unable to make income or capital payments, or their rating is downgraded, the value of that investment will fall. Fixed income securities that have a lower credit rating can pay a higher level of income and have an increased risk of default.

Derivative Risk: Derivatives are highly sensitive to changes in the value of the underlying asset which can increase both Fund losses and gains. The impact to the Fund can be greater where they are used in an extensive or complex manner, where the Fund could lose significantly more than the amount invested in derivatives.

Emerging Markets Risk: Investing in Emerging Markets may provide the potential for greater rewards but carries greater risk due to the possibility of high volatility, low liquidity, currency fluctuations, the adverse effect of social, political and economic instability, weak supervisory structures and accounting standards.

Exchange Rate Risk: Changes in currency exchange rates may affect the value of this investment.

Interest Rate Risk: Fixed interest securities are particularly affected by trends in interest rates and inflation. If interest rates go up, the value of capital may fall, and vice versa. Inflation will also decrease the real value of capital.

Liquidity Risk: In difficult market conditions the value of certain fund investments may be difficult to value and harder to sell, or sell at a fair price, resulting in unpredictable falls in the value of your holding.

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