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Royal London Short Term Fixed Income Fund

Quarterly Investment Report

31 December 2024

Quarterly Report

The fund as at 31 December 2024

The purpose of this report is to provide an update on the Royal London Short Term Fixed Income Fund. The report has been produced by Royal London Asset Management. The report starts with a summary dashboard showing key information about the fund. A glossary is located at the end of the report covering the description of some of the more technical terms used within the report. All data is as at the report date unless otherwise stated.

Contents

ROYAL LONDON
ASSET MANAGEMENT

The fund

Fund performance objective and benchmark

The Fund's investment objective is to achieve a total return over rolling 12-month periods by primarily investing (at least 70% of its assets) in Short Term Fixed Income Securities. The Fund's comparator benchmark is the Bank of England Sterling Overnight Interbank Average (SONIA) plus 0.5%. For the most appropriate comparison, this should be considered on a 'before the deduction of fees' basis. SONIA is the average overnight interest rate UK banks pay for unsecured transactions in sterling. It is considered to be an appropriate benchmark as it is a widely recognised approach to benchmarking short-term money market and fixed income funds.

Benchmark: SONIA (Sterling Overnight Index Average)

Fund value

	Total £m
31 December 2024	3,953.00

Fund analytics

	Fund
Fund launch date	15 June 2011
Duration (years)	0.15
Number of issuers	45
Gross redemption yield (%)	5.01

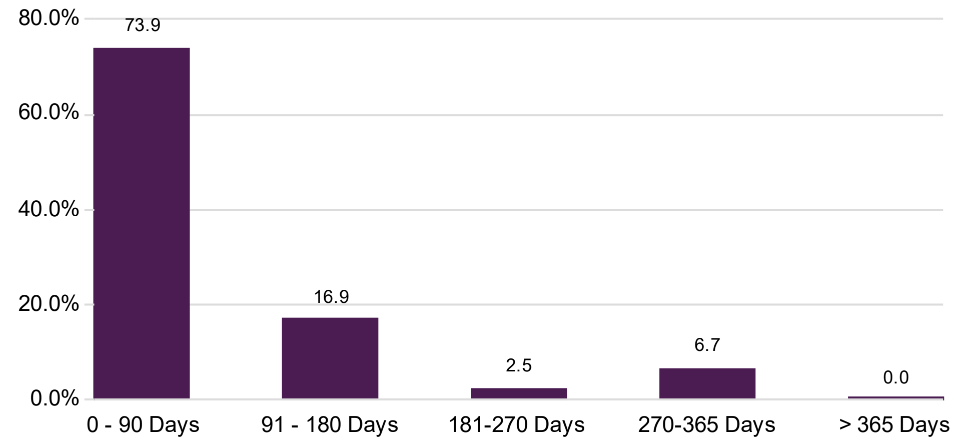
Performance and activity

Performance

	Fund (%)	Benchmark (%)	Relative (%)
Quarter	1.26	1.19	0.07
1 Year	5.73	5.07	0.66
3 Years (p.a.)	3.97	3.67	0.30
5 Years (p.a.)	2.62	2.24	0.38
10 Years (p.a.)	1.68	1.30	0.38
Since inception (p.a.)	1.55	1.11	0.44

Past performance is not a guide to future performance. Please refer to the Glossary for the basis of calculation and impact of fees. Performance and since inception date based on Z Inc GBP. Source: Royal London Asset Management; Gross performance; Since inception date of the share class is 21 May 2012.

Duration profile

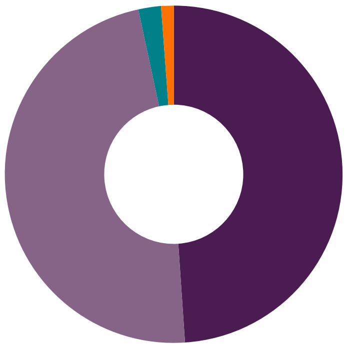


Performance commentary

Performance was positive over the quarter compared to the SONIA benchmark. At a portfolio level, we had built up a yield premium to the benchmark. Covered bonds still account for the majority of non-money market exposure and were the main drivers of returns over the quarter given the premium these pay over SONIA. Money market exposure was also positive for returns, helped by the high level of diversification across both fixed and floating exposure and having avoided excessive lengthening of maturities when those rates had been poorer value earlier in the year.

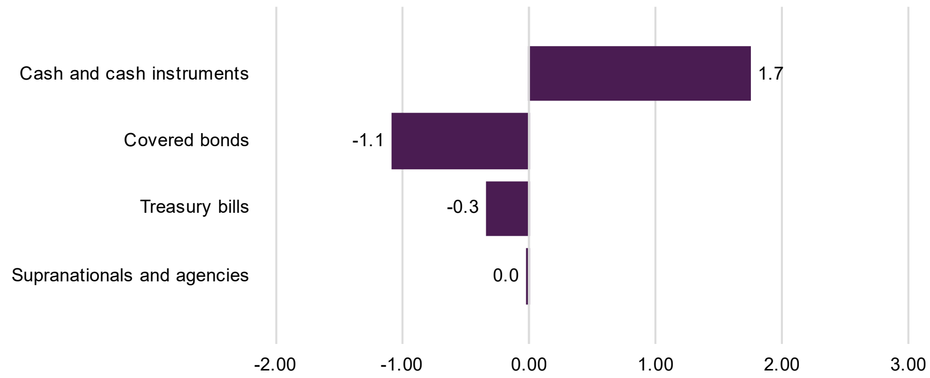
Performance and activity

Asset allocation profile

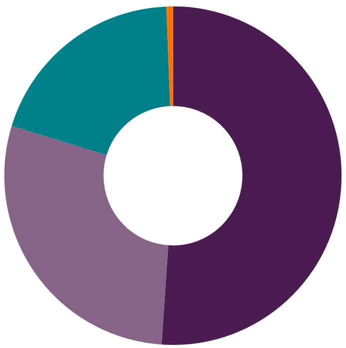


Cash and cash instruments	48.9%
Covered bonds	47.7%
Treasury bills	2.2%
Supranationals and agencies	1.2%

Change since last quarter (asset allocation) %

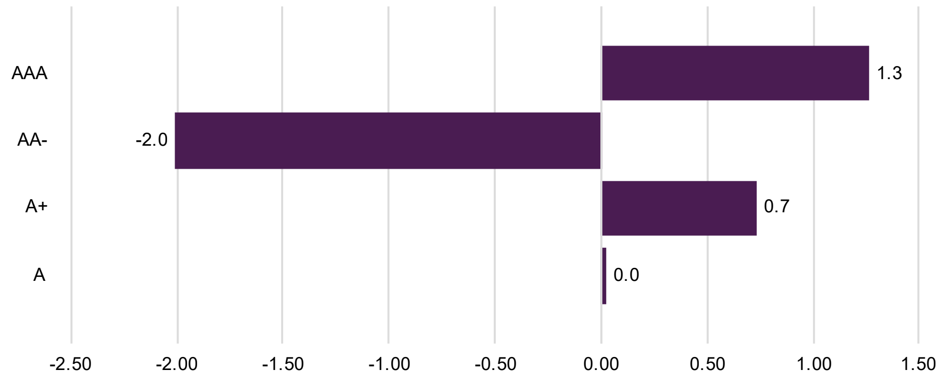


Credit rating profile



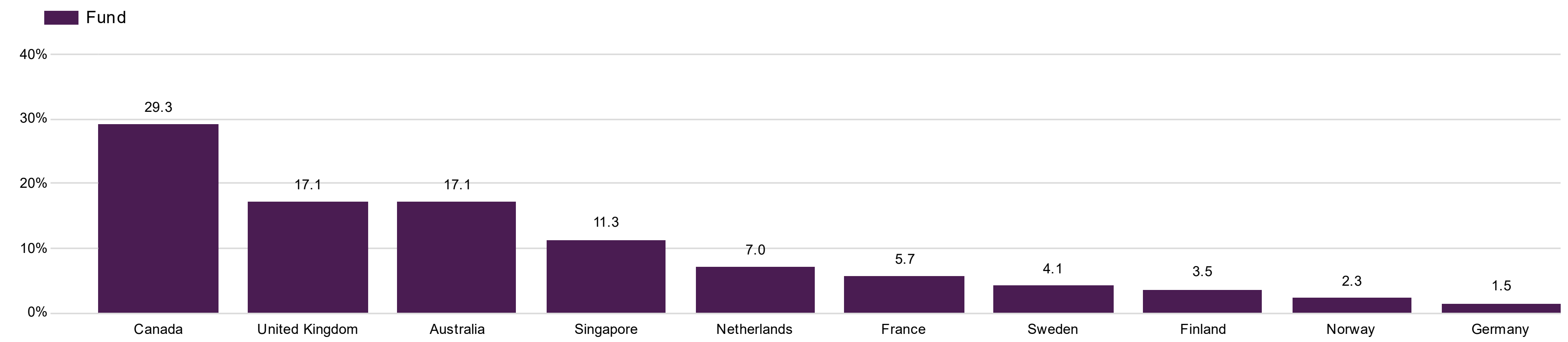
AAA	51.1%
AA-	28.7%
A+	19.6%
A	0.6%

Change since last quarter (rating) %

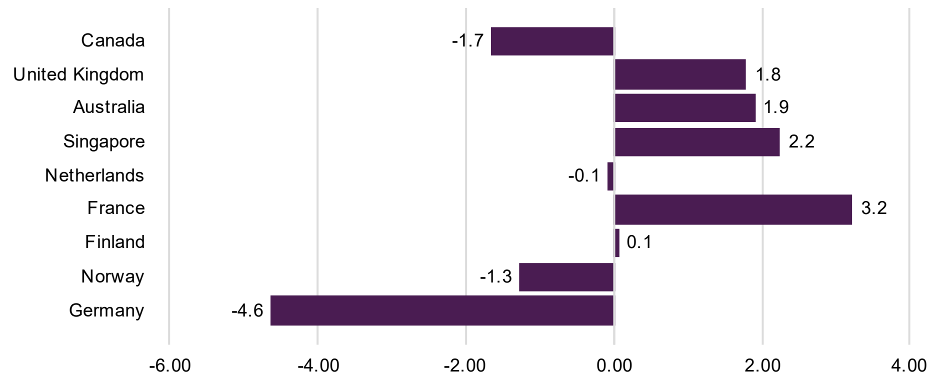


Performance and activity

Top ten geographic allocation (ex gilts) %



Change since last quarter (geographic) %



Performance and activity

Fund activity

Activity was generally in overnight deposits, as well as CDs – where we looked to add attractive yield levels into next year. In particular, we looked to take advantage of elevated longer yields, including six-month CDs from BNP Paribas, Goldman Sachs and one-year paper from Swedbank and Standard Chartered, all highly rated issuers in our universe. We were happier to add more to longer maturity paper later in the period with yields on offer looking more realistic compared to earlier in the year.

Covered bonds from favoured issuers are always attractive for fund, and remain a significant part of the portfolio. Issuance remain light, but we add new issue covered bonds from Commonwealth Bank of Australia and Canadian Imperial Bank of Commerce, both offering an attractive premium of more than 50bps over SONIA. We took profits on several names that had performed strongly, including Royal Bank of Canada and United Overseas Bank, where the premiums had shrunk to around 40bps over SONIA, reinvesting in covereds from Westpac Banking and TSB Bank at higher levels.

Market commentary

Market overview

Markets were volatile during the fourth quarter – with the US elections and the potential for central bank rate cuts the main causes of uncertainty. With the election of Donald Trump as US President, and the Republicans having a majority in both the Senate and House of Representatives, markets moved to price in potentially higher US deficits.

Alongside political events, attention remained on the Federal Reserve, European Central Bank and Bank of England to see if expected rate cuts would materialise. However, with inflation remaining higher than central bankers would like, expectations for rate cuts in 2025 were revised down. This backdrop pushed government bond yields higher, leading to negative absolute returns for most investment grade credit markets despite credit spreads tightening and credit excess returns over government bonds being positive, while equities ended a strong 2024 with another positive quarter, with US stocks – notably the 'magnificent seven' – leading the way.

At its final meeting of 2024, and as expected, the Bank of England kept rates on hold at 4.75%. Meanwhile, according to the minutes, "a gradual approach to removing monetary policy restraint remains appropriate." November CPI inflation rose to 2.6% year-on-year as expected on 'base effects'. Pay growth was stronger than expected. October GDP shrank month-on-month after falling in September, with this contraction (and subdued business surveys since) raising the risk of a mild GDP contraction in the fourth quarter. Away from economic data, the new Labour government presented its first budget. This was less obviously a budget for growth than one for public services repair with a substantial proposed increase in day-to-day fiscal spending and net investment. Public spending was increased substantially, but at the cost of a big increase in taxes. Since the Budget, business optimism has dropped, and firms are indicating a mix of responses to the rise in National Insurance contributions including hiring less and raising prices.

The Federal Reserve cut rates 50bps over the quarter to a 4.25% - 4.5% target range. They signalled fewer cuts for 2025 than previously indicated, indicating only 50bps cuts for 2025 (100bps previously). In November, Donald Trump was elected US President for the second time. A Trump presidency will likely bring a change in both policy making style and substance. It was a clean sweep for the Republicans, winning the White House, Senate and House of Representatives, increasing the prospects of Trump getting his fiscal policies through.

Government bond yields rose over the quarter, as central banks continued to struggle to bring inflation back to target levels and amid ongoing political volatility with elections across Europe and the US. In the US, 10-year treasury yields rose to 4.57% from 3.78%, while German 10-year bunds similarly saw yields rise to 2.36% from 2.06%. Benchmark 10-year gilt yields increased to 4.57% from 4.01%.

UK money market rates were flat for the first half of 2024, reflecting that attention was on the Bank of England and a first rate cut in this cycle. After the rate cut in August, SONIA started the fourth quarter at 4.95%, falling to 4.7% following the November rate cut. Two-year gilts, often seen as a proxy for market expectations of BoE rates, started at 4.00% but trended higher throughout the period – reflecting the potential increase in gilt supply under the new government, as well as lower expectations of rate cuts.

Outlook

Market pricing of UK interest rates in 2025 has changed over the past quarter. Having priced in year-end rates of 4% at the start of October, the market is now expecting base rates of 4.25% by December 2025. In our view, expectations have been overly optimistic throughout 2024, but now appear more realistic – in simple terms, the low growth backdrop gives the Bank of England scope to cut rates, but with inflation still lurking, that scope is limited. As we laid out in our end of year Outlook, while stagnant growth and high inflation are termed Stagflation, we see more of a 'Bambi' inflation scenario, with unexciting growth and sticky inflation.

With rate expectations now more realistic, and relatively few cuts priced in for 2025, we retain a cautious stance in the funds in terms of duration. These funds are more cautious than other areas anyway, but even within that remit, we do not feel market rates are at levels that make extending maturities attractive. As a result, we are focused more on maintaining attractive overall yields rather than implementing a rate 'view', making use of floating rate exposure to help manage volatility in rate expectations.

In general, we have been cautious for most of 2024 on both maturities and credit risk. We remain comfortable with this approach, given our view that credit risk within the very short-dated space is not particularly well rewarded, and are therefore to have higher than normal exposure to areas such as treasury bills or gilts.

Our liquidity and short term fixed income funds do not have specific ESG objectives, but we continue to incorporate assessment of ESG risks into our holdings. While the primary consideration in looking at a bank will be assets and cashflows, ESG risks are also material. In addition, we believe that our exposure to covered bonds also helps manage risk, with these being regulated instruments and exempt from bail-in, so if a bank does get into difficulty, these assets are not bailed into the wind-up process.

Further Information

Please click on the links below for further information:

Stewardship and responsible investment at RLAM

Royal London Sterling credit ESG analysis

TCFD climate report

Find out more

In an uncertain geopolitical and economic environment, we recognise the importance of keeping our clients updated on our current investment thinking.

Articles, videos, podcasts and webinars giving the latest views of our investment experts can be found in the Our Views section of www.rlam.com, including regular updates from our Fixed Income, Global Equity, Sustainable and Multi Asset teams.

Disclaimers

Important information

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Issued in January 2025 by Royal London Asset Management Limited, 80 Fenchurch Street, London EC3M 4BY. Authorised and regulated by the Financial Conduct Authority, firm reference number 141665. A subsidiary of The Royal London Mutual Insurance Society Limited.

The Fund is a sub-fund of Royal London Bond Funds ICVC, an open-ended investment company with variable capital with segregated liability between sub-funds, incorporated in England and Wales under registered number IC000797.

The Authorised Corporate Director (ACD) is Royal London Unit Trust Managers Limited, authorised and regulated by the Financial Conduct Authority, with firm reference number 144037.

For more information on the fund or the risks of investing, please refer to the Prospectus or Key Investor Information Document (KIID), available via the relevant Fund Information page on www.rlam.com.

The "SONIA" mark is used under licence from the Bank of England (the benchmark administrator of SONIA), and the use of such mark does not imply or express any approval or endorsement by the Bank of England. "Bank of England" and "SONIA" are registered trademarks of the Bank of England.

Risks and Warnings

Investment risk

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.

EPM techniques risk

The Fund may engage in EPM techniques including holdings of derivative instruments. Whilst intended to reduce risk, the use of these instruments may expose the Fund to increased price volatility.

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. Unlike the income from a single fixed interest security, the level of income (yield) from a fund is not fixed and may go up and down. Bond yields (and as a consequence bond prices) are determined by market perception as to the appropriate level of yields given the economic background.

Counterparty risk

The insolvency of any institutions providing services such as safekeeping of assets or acting as counterparty to derivatives or other instruments, may expose the Fund to financial loss.

Government and public securities risk

The Fund can invest more than 35% of net assets in different Transferable Securities and Money Market Instruments issued or guaranteed by any EEA State, its local authorities, a third country or public international bodies of which one or more EEA States are members.

Inflation risk

Where the income yield is lower than the rate of inflation, the real value of your investment will reduce over time.

Performance to 31 December 2024

Cumulative (%)

	3 Month	6 Month	1 Year	3 Years	5 Years
Fund (gross)	1.26	2.74	5.73	12.41	13.82
Fund (net)	1.25	2.73	5.70	12.31	13.65

Annualised (%)

	3 Years (p.a.)	5 Years (p.a.)
Fund (gross)	3.97	2.62
Fund (net)	3.94	2.59

Year on year performance (%)

	31/12/2023 - 31/12/2024	31/12/2022 - 31/12/2023	31/12/2021 - 31/12/2022	31/12/2020 - 31/12/2021	31/12/2019 - 31/12/2020
Fund (gross)	5.73	5.29	0.98	0.22	1.03
Fund (net)	5.70	5.26	0.95	0.19	1.00

Past performance is not a guide to future performance. The impact of fees or other charges including tax, where applicable, can be material on the performance of your investment.

Source: RLAM as at 31 December 2024. All figures are mid-price to mid-price for the Royal London Short Term Fixed Income Fund Z Inc GBP share class.

Glossary

Asset allocation

Breakdown of the assets by asset classes. Based on RLAM asset classification scheme.

Duration

Measure of sensitivity of a Fixed Income instrument to changes in interest rates, indicating the potential impact of interest rate fluctuations on the value of the investment.

Fund value

Total value of the fund as of the last business day of the calendar month. The fund value is as at close of business and on a mid-price basis.

Gross redemption yield

Gross redemption yield is the rate of discount at which a bond's future obligations of interest and capital payments equates to its current price. The gross redemption yield shown for the fund is the average for its individual holdings, weighted by their current value, net of relevant fund management costs and gross of tax.

Number of issuers

Number of unique issuers of all assets held by the Fund, excluding cash, currency and derivatives.

Performance

Performance is calculated using the daily end of day NAV per share produced by HSBC based on the mid price.