Royal London Equity Funds

Fund Manager Commentary

May 2024

Contents

Royal London Asset Management Equity Performance

	1 month (%)	Rolling 12 Months (%)
RL UK Equity Income M Inc	**2.43**	**18.76**
IA UK Equity Income Sector	2.69	15.34
FTSE All Share Index	2.41	15.44
RL UK Dividend Growth Fund M Acc	**1.85**	**17.19**
IA UK All Companies Sector	2.70	13.97
FTSE All Share Index	2.41	15.44
RL UK Mid Cap Growth Fund M Acc	**5.95**	**13.37**
IA UK All Companies Sector	2.70	13.97
FTSE 250 ex-IT Index	5.48	17.15
RL UK Opportunities Fund M Acc	**2.94**	**11.83**
IA UK All Companies Sector	2.70	13.97
FTSE All Share Index	2.41	15.44
RL UK Smaller Companies Fund M Acc	**6.36**	**13.31**
IA UK Smaller Companies Sector	6.29	14.89
FTSE Small Cap ex-IT Index	6.71	20.85
RL Global Equity Select Fund M Acc	**1.68**	**29.75**
IA Global	1.18	15.54
MSCI World Net Index	2.74	21.60
Rl Global Equity Diversified Fund M Acc	**1.27**	**22.67**
IA Global	1.18	15.54
MSCI World Index	2.74	21.60

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 Morningstar, as at 31 May 2024. Returns quoted are net of fees. Please note that with effect from 1 February 2024 Royal London Asset Management 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.

Royal London UK Equity Income Fund

Portfolio Commentary

- During May the fund returned 2.43%, which was ahead of its benchmark, but behind the peer group median, ranking 57th percentile. Year to date the fund is slightly ahead of its benchmark and ranks 46th percentile.
- In the month the country found out that the next general election would be held on July 4. The prospect of a change of government, continued negative news flow around water companies and the launch of a £7bn equity issue by **National Grid** combined to make the utilities sector weak in the month. The oil sector was also down as the oil price drifted lower. Conversely, the financial sector was a strong performer, spurred on in part by a takeover offer for **Hargreaves Lansdown** – an offer which was rejected by the company. In other corporate activity news, the previously announced bid from **BHP** for **Anglo American** lapsed, after terms and a valuation for the mining mega-deal could not be agreed.
- The fund's outperformance of the index was driven by holdings in a diverse range of companies; **Intermediate Capital**, **Diploma**, **Marshalls**, **IMI** and **ITV**. The common theme across the stocks was that each had released reassuring trading statements or results. The holding in the software company **Sage** was a drag on performance after the company reported slightly slower sales growth than some had predicted.
- During the month holdings in **Astra Zeneca**, **Glencore**, **3i** and **Diploma** were reduced, on share price strength, with the proceeds used to add to existing holdings in **Sage**, **GlaxoSmithKline**, **DCC** and **Spectris**.

Investment Outlook

- We continue to feel that our approach of investing in a broad range of companies from different sectors and stages of their lifecycle is very appropriate and will allow performance to continue to be driven more by the success of our hunting for undervalued long term cashflows than by the prevailing winds of the macroeconomy, or factors such as growth or value styles being in vogue.

Richard Marwood

Head of Income Equities

Royal London UK Dividend Growth Fund

Portfolio Commentary

- During May the fund returned 1.85% and was behind the peer group median, ranking 72nd percentile. Year to date the fund is ahead of its benchmark and ranks 26th percentile.
- In the month the country found out that the next general election would be held on July 4. The prospect of a change of government, continued negative news flow around water companies and the launch of a £7bn equity issue by **National Grid** combined to make the utilities sector weak in the month. The oil sector was also down as the oil price drifted lower. Conversely, the financial sector was a strong performer, spurred on in part by a takeover offer for **Hargreaves Lansdown** – an offer which was rejected by the company. In other corporate activity news, the previously announced bid from **BHP** for **Anglo American** lapsed, after terms and a valuation for the mining mega-deal could not be agreed.
- The fund's outperformance of the index was driven by not holding any **National Grid** or water company stocks and by the holdings **Intermediate Capital**, **Watches of Switzerland**, **Barclays** and **Clarkson**. The holding in the software company Sage was a drag on performance after the company reported slightly slower sales growth than some had predicted.
- During the month holdings in **Glencore**, **3i**, **Sabre** and **Watches of Switzerland** were reduced, on share price strength, with the proceeds used to add to existing holdings in **Sage**, **BP** and **DCC**. A new position was also started in the Asia exposed insurance company **Prudential**.

Investment Outlook

- We continue to feel that our approach of investing in a broad range of companies from different sectors and stages of their lifecycle is very appropriate and will allow performance to continue to be driven more by the success of our hunting for undervalued long term cashflows than by the prevailing winds of the macroeconomy, or factors such as growth or value styles being in vogue.

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Richard Marwood

Head of Income Equities

Royal London UK Mid Cap Growth Fund

Portfolio Commentary

- The UK Mid Cap Growth fund returned 5.9% during the month, outperforming both the benchmark (FTSE 250 ex IT) and the IA UK All Companies peer group median by 1.9% and 3.2% respectively.
- In the UK, Prime Minister Rishi Sunak announced a general election to take place on 4th July. While the timing was earlier than many expected, financial markets have been anticipating a change of administration for some time and an early election is arguably a clearing event, removing the overhang of political uncertainty. To date both major parties have pledged fiscal stability, and the lack of significant moves amongst equity sectors or in bond markets has been telling. Macroeconomic data generally painted a positive picture for the UK with confirmation of GDP growth in Q1, activity surveys such as PMIs suggesting an improving trend in demand, and inflation reducing to 2.3% in April. This supports the market expectation for interest rate cuts in the second half of 2024. Within UK equity markets takeover activity continued to be a theme, with another flurry of companies announcing approaches including **Hargreaves Lansdown**, **Keywords Studios**, **XP Power**, **Wood Group** and **Capital & Regional**.
- **Integrafin** and **AJ Bell** were once again significant contributors to performance during the month, following their interim results announcements. Both businesses have benefitted from improving asset flows onto savings platforms – whether via financial advisors or directly from retail investors – as well as rising markets. Despite investing into improving their technology stacks or customers services, both companies experienced positive operating leverage as rising revenues outstripped cost investment. **FDM Group** was another positive contributor. Their share price rallied from very depressed levels, following a trading statement which highlighted that the business was seeing some early signs of improvement for customer demand.
- The significant detractors to relative performance were all companies within the FTSE250 index that the fund did not hold, such as **Hargreaves Lansdown** whose shares rallied c. 40% following a rejected takeover approach. Of the portfolio holdings, RS Group was a detractor despite announcing solid full year results. Management flagged that they would put additional cost into the business in the coming year to improve customer service and expand their product offering, diluting margins short term but supporting stronger long term profit growth.
- The fund initiated a position in **Shaftesbury Capital**, the real estate group comprised of a unique portfolio in London's West End. The REIT was formed following the merger of **Shaftesbury** and **Capital & Counties** in 2023, and management expect to deliver significant cost synergies as they realise benefits from the merger. Their portfolio benefits from already high occupancy rates and this, combined with an ongoing recovery in tourist numbers post COVID, should support compound growth in rental income. Despite the unique asset status of the portfolio and long-term valuation underpin that this provides, the shares are trading at a significant discount to asset value.

Henry Lowson

Head of UK Alpha Equities

Henry Burrell

Fund Manager

Royal London UK Opportunities Fund

Portfolio Commentary

- The Royal London UK Opportunities fund produced a return of 2.9% during the month, comfortably outperforming the FTSE All Share benchmark by 0.53%.
- In the UK, Prime Minister Rishi Sunak announced a general election to take place on 4th July. While the timing was earlier than many expected, financial markets have been anticipating a change of administration for some time and an early election is arguably a clearing event, removing the overhang of political uncertainty. To date both major parties have pledged fiscal stability, and the lack of significant moves amongst equity sectors or in bond markets has been telling. Macroeconomic data generally painted a positive picture for the UK with confirmation of GDP growth in Q1, activity surveys such as PMIs suggesting an improving trend in demand, and inflation reducing to 2.3% in April. This supports market expectations for interest rate cuts in the second half of 2024. Within UK equity markets takeover activity continued to be a theme, with another flurry of companies announcing approaches including **Hargreaves Lansdown**, **Keywords Studios**, **XP Power**, **Wood Group** and **Capital & Regional**.
- **Integrafin** and **Hill & Smith** were significant contributors to performance during the month. Integrafin updated the market with a solid set of results, benefitting from improving asset flows onto their savings platform – as well as rising markets. Despite investing into improving their technology stacks and customers services, the company has experienced positive operating leverage as rising revenues outstripped cost investment. **Hill & Smith's** trading update delivered an earnings upgrade for the full year, largely driven by strength in the group's US Galvanizing & Engineered Solutions divisions. The company continues to benefit from various US government acts which are stimulating industrial and infrastructure investment.
- The fund's underweight position in **HSBC** caused it to be a modest detractor to relative performance. The company updated issued a Q1 trading update at the end of April, where it revealed it had generated profits ahead of consensus expectations on an adjusted basis. The company also announced a new $3bn share buyback, which was higher than what analysts were expecting.

Royal London UK Smaller Companies Fund

Portfolio Commentary

- The UK Smaller Companies fund returned 6.4% during the month, performing in line with the benchmark (FTSE Small Cap ex IT) and slightly outperforming the UK Smaller Companies peer group median.
- In the UK, Prime Minister Rishi Sunak announced a general election to take place on 4th July. While the timing was earlier than many expected, financial markets have been anticipating a change of administration for some time and an early election is arguably a clearing event, removing the overhang of political uncertainty. To date both major parties have pledged fiscal stability, and the lack of significant moves amongst equity sectors or in bond markets has been telling. Macroeconomic data generally painted a positive picture for the UK with confirmation of GDP growth in Q1, activity surveys such as PMIs suggesting an improving trend in demand, and inflation reducing to 2.3% in April. This supports the market expectation for interest rate cuts in the second half of 2024. Within UK equity markets takeover activity continued to be a theme, with another flurry of companies announcing approaches including **Hargreaves Lansdown**, **Keywords Studios**, **XP Power**, **Wood Group** and **Capital & Regional**.
- **Johnson Service Group** and **Alpha Financial Markets Consulting** (**Alpha FMC**) were contributors to performance during the month. **Johnson Service Group** issued a first quarter trading update which confirmed strong sales growth within their hotel, restaurant & catering division. Management also indicated their confidence in operating margins expanding back to pre-Covid levels earlier than expected, a result of strong pricing activity, operational efficiencies, and lower energy costs. **Alpha FMC's** share price rose as the company confirmed it had received an indicative takeover offer from **Bridgepoint Advisers**. Other interested parties were also reported to be considering making an offer.
- The significant detractors to relative performance were all companies within the FTSE250 index that the fund did not hold, such as **XP Power** whose shares rallied c. 40% following a rejected takeover approach. Of the portfolio holdings, **Hollywood Bowl** was a modest detractor. The share price slightly declined on no material newsflow, after having had a strong run in the year to date.
- The fund recently initiated a position in soft drinks group AG Barr, which operates a portfolio of brands including **Irn-Bru**, **Rubicon**, **Moma** and **Boost**. While their flagship brand Irn-Bru is already well penetrated in its core markets, their other brands generally operate in faster growth segments of the market and the management team have shown themselves capable of driving brand growth. Last year operating margins remained below pre-Covid levels but with input cost inflation fading, and a number of self-help projects underway, the management team have levers to pull to drive operating leverage. The net cash balance sheet provides positive optionality to fund further brand acquisitions or shareholder returns.

Henry Lowson

Head of UK Alpha Equities

Henry Burrell

Fund Manager

Royal London Global Equity Select Fund

Portfolio Commentary

- Equity markets gained in May, seeing markets rally back towards their all-time highs. Earnings beats have been strong and well above average in the US, Japan and Europe.

Contributors

- **Sumitomo Mitsui Financial Group (SMFG)** is a leading Japanese financial institution offering banking, leasing, securities, and credit card services globally, currently in the mature phase of the corporate life cycle. During the period, **Sumitomo** announced positive quarterly results, beating analyst expectations and tracking well against our thesis milestones. The shares outperformed the market by a fair margin, but we still see a positive valuation payoff opportunity coupled with attractive wealth creation characteristics.
- **TSMC**, currently in the Compounding phase of the life cycle, is the largest global semiconductor foundry (essentially outsourced semiconductor manufacturing). TSMC manufactures semiconductors for its clients, who are usually fabless semiconductor design companies like **Qualcomm**, **NVIDIA**, **Broadcom**, and **AMD**. TSMC reported strong quarterly earnings in April as it continues to play its role in enabling the AI revolution, but it is important to note that it is not solely reliant on this sector. In light of the strong share performance this year, we still observe an attractive valuation payoff opportunity.
- **MercadoLibre** is an Accelerating business that operates an ecosystem of online commerce and financial services offerings in Latin America. The Latin American market, in which **MercadoLibre** competes, is in the initial stages of transitioning to e-commerce and digital payments. As a result, this large regional total addressable market (TAM) presents significant opportunities for future growth. The company reported quarterly results during the period, which were positively received by the market. Our investment thesis is that **MercadoLibre** can disrupt online commerce and financial services in Latin America during its transition to e-commerce and a digital economy. We are still in the early stages of this transition, but the company is tracking well thus far.

Detractors

- **Old Dominion Freight Line (ODFL)** is a pure play less than truck load (LTL) US trucking company in the Slowing & Maturing stage of the Life Cycle. **ODFL** reported quarterly results in April which were not so well received by the market. The results reflect a weaker macro-economic environment as opposed to a stock specific issue. We remain confident in the company's combination of Wealth Creation characteristics and valuation pay-off.
- **Dollar General**, in the Slowing and Maturing stage of the life cycle, is the largest discount retailer in the US with over 20,000 stores in 47 states. The company offers a wide range of merchandise, including consumables, packaged food, health and beauty products, home products, and more. **Dollar General** announced its quarterly results towards the end of the period. The market initially reacted harshly, with shares trading down 8% on the day, but they have since recovered. While concerns of a weakening US consumer are widespread, we remain positive about the Wealth Creation characteristics of the business and the valuation opportunity it presents.
- **Tyson Foods** is a leading US meat and prepared food business in the Turnaround phase of the Life Cycle. Operating across the beef, chicken, pork, and prepared foods markets, the business experiences varying degrees of cyclicality depending on its level of integration into these markets. Tyson reported Q1 results during the period, which were in line with consensus, but the outlook for the remainder of the year may have unsettled the market. We remain focused on **Tyson's** long-term ability to generate returns above its cost of capital, which the market is currently discounting.

ALPHA MANAGER 2024
Mike Fox

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Head of Sustainable Investments

Royal London Global Equity Income Fund

Portfolio Commentary

- Equity markets gained in May, seeing markets rally back towards their all-time highs. Earnings beats have been strong and well above average in the US, Japan and Europe.
- During the month the fund underperformed the benchmark and its peer group.
- The fund is having a lower exposure to US stocks than the benchmark (US benchmark weight is 71%, the fund is 57%), and this was the most significant regional factor driving performance. On a stock basis not holding **Nvidia**, which pays a negligible yield and as such is unsuitable for this mandate, was the main stock detractor from relative performance. The main positive contributor was the holding in the US paper company **Sylvamo** which reported strong results in the month.
- During the month the holdings in **Doosan Bobcat**, **Maersk**, **Halma** and **Aperam** were exited, and new holdings established in, among others, **Aviva**, **Bucher Industries**, **Volvo**, **Pepsico** and **CME**.

Piers Hillier

Chief Investment Officer

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Richard Marwood

Head of Income Equities

Matt Burgess

Head of Passive and Quantitative Equities

Royal London Global Equity Diversified Fund

Portfolio Commentary

- Equity markets gained in May, seeing markets rally back towards their all-time highs. Earnings beats have been strong and well above average in the US, Japan and Europe.

Contributors

- Two of the greatest contributors to performance this past month were stocks we did not own, **Tesla**, and **Salesforce**. An expected outcome of running a diversified portfolio with a high allocation to stock specific risk is that performance will come from an array of idiosyncratic stock picks as opposed to one or two names.
- **Sprouts Farmers Market**, **Inc**. is a US-based grocery chain that offers fresh, natural, and organic food products. Sprouts leverages its scale to deliver a 'Farmers Market' experience to all consumers, focusing on providing fresh foods at good value. Sprouts reported Q1 2024 earnings at the beginning of May which were extremely well received by the market as they beat analyst expectations and raise guidance for FY 2024. Management appears to be executing on sensible strategy for a Compounding business whilst the market values the company as it if were Slowing & Maturing, presenting a valuation opportunity.

Detractors

- **Carl Zeiss** (**CZ**) is a leading provider of medical equipment specialising in innovative solutions for the diagnosis and treatment of eye diseases. The company is currently in the Slowing & Maturing phase of the corporate Life Cycle. CZ announced H1 2024 results during the period which were heavily impacted by destocking in their Chinese sales channel. They have cut guidance to their 2024 outlook, but we remain comfortable with our investment thesis and believe CZ continues to offer an attractive valuation pay-off opportunity.
- **Shell** is a prominent Oil & Gas company in the Turnaround phase of the Life Cycle. Shell detracted from performance in May as the shares fell approx. -1% versus a strong market. Shell announced a good set of results during the period, but the shares were dragged down in a broad sell off in the O&G sector as global oil prices begin to struggle this year by some measures (WTI Crude Oil USD). Our assessment of Shell's Wealth Creation characteristics has not changed.
- **Tyson Foods** is a leading US meat and prepared food business in the Turnaround phase of the Life Cycle. Operating across the beef, chicken, pork, and prepared foods markets, the business experiences varying degrees of cyclicality depending on its level of integration into these markets. Tyson reported Q1 results during the period, which were in line with consensus, but the outlook for the remainder of the year may have unsettled the market. We remain focused on Tyson's long-term ability to generate returns above its cost of capital, which the market is currently discounting.