

## **M&G Absolute Return Bond Fund**

a sub-fund of M&G Investment Funds (10)

Annual Short Report March 2018

For the year ended 31 March 2018

The Authorised Corporate Director (ACD) of M&G Investment Funds (10) presents its Annual Short Report for M&G Absolute Return Bond Fund which contains a review of the fund's investment activities and investment performance during the period. The ACD's Annual Long Report and audited Financial Statements for M&G Investment Funds (10), incorporating all the sub-funds and a Glossary of terms is available free of charge either from our website at [www.mandg.co.uk](http://www.mandg.co.uk) or by calling M&G Customer Relations on 0800 390 390.

### ACD

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(Authorised and regulated by the Financial Conduct Authority.  
M&G Securities Limited is a member of the Investment Association  
and of the Tax Incentivised Savings Association.)

### Important information

On 27 April 2018, share class Euro 'Z-H' Accumulation was launched in the M&G Absolute Return Bond Fund.

### Investment objective

The fund aims to achieve a total return (the combination of income and capital growth) of at least 2.5% per annum above the 3-month GBP LIBOR rate, before any charges are taken, in any market conditions and over any three year period. LIBOR is the rate at which banks borrow money from each other.

The fund aims to achieve this while seeking to minimise the degree to which the value of the fund fluctuates over time (volatility), while also seeking to limit monthly losses. Managing the fund in this way reduces its ability to achieve returns significantly above 3-month GBP LIBOR plus 2.5%.

There is no guarantee that the fund will achieve a positive return over three years, or any other period, and investors may not get back the original amount they invested.

### Investment policy

The fund invests at least 70% in fixed and variable rate securities (including, but not limited to, corporate bonds and government and public securities), currencies, cash, near cash and deposits. These may be from anywhere in the world and denominated in any currency.

The fund's exposure to these investments may also be gained through the use of derivatives, which are financial contracts whose value is derived from an underlying asset. The fund may take short positions (holding derivatives with the aim of delivering a positive return when the assets they are linked to fall in value) in markets, currencies, securities, and groups of securities. The fund also has the flexibility to gain exposure to investments exceeding the net asset value of the fund in order to increase potential returns in both rising and falling markets.

Derivatives may be used to meet the fund's objective and for efficient portfolio management purposes. The fund may also invest in other funds.

### Investment approach

The fund managers take a flexible approach, investing across a broad range of fixed income and currency markets according to where they identify value. A dynamic investment approach is followed, allowing the fund managers to change the blend of duration, credit and currency exposures based on their outlook. The fund will typically aim to have a high level of diversification in individual credit selection and across investment themes and sources of return. The managers will aim to achieve the performance objective while managing the fund's volatility and limiting losses during difficult market conditions.

### Risk profile

The fund is a flexible bond fund which invests in a range of fixed income securities and in currencies. The fund is therefore subject to the price volatility of global bond markets and fluctuations in currency exchange rates.

The fund's exposure to fixed income securities may be gained through the use of derivatives. In association with the use of derivatives, including those instruments not traded through an exchange, collateral is deposited in order to mitigate the risk that a counterparty may default on its obligations or become insolvent.

Portfolio diversification is key in managing liquidity and default risks as well as reducing market risk. The blend of assets held in the fund is regularly adjusted depending on where the managers see the most value and to manage risks, including liquidity, credit, currency and market risks. The fund's risks are measured and managed as an integral part of the investment process.

Please note that the risk management policies are set out in full in the financial statements and notes sections of the Annual Long Report and audited Financial Statements of M&G Investment Funds (10).

The following table shows the risk number associated with the fund and is based on Sterling Class 'A' shares.



The above number:

- is based on the rate at which the value of the fund has moved up and down in the past and is based on historical data so may not be a reliable indicator of the future risk profile of the fund.
- is not guaranteed and may change over time and the lowest risk number does not mean risk free.
- has not changed during this period.

As at 3 April 2018, for the year ended 31 March 2018

### Performance against objective

Between 3 April 2017 (the start of the review period) and 3 April 2018, the M&G Absolute Return Bond Fund delivered a positive total return (the combination of capital growth and income), albeit slightly less than 3-month GBP LIBOR + 2.5%. The fund's objective is to achieve a total return of at least 2.5% per annum above the 3-month GBP LIBOR rate, before any charges are taken, in any market conditions and over any three-year period.\*

The M&G Absolute Return Bond Fund is a flexible, multi-strategy bond fund that targets steady positive returns, with a specific focus on minimising volatility and monthly losses in difficult market conditions. As a highly diversified portfolio, the fund provides exposure to a broad range of fixed income strategies across global corporate bond, government bond and currency markets. (Bonds are loans that are extended by an investor to an issuing entity – such as a company or government – in exchange for regular interest payments. Bonds issued by companies are referred to as 'corporate bonds', while those issued by governments are called 'government bonds'.)

The fund draws on the best ideas of M&G's Retail Fixed Interest team, giving investors access to an extensive range of investment knowledge across global bond markets. The team has long-running experience in managing flexible bond strategies, and has demonstrated the ability to manage risk during periods of heightened volatility, such as during the global financial crisis and the eurozone debt crisis. (Volatility is the extent to which asset prices fluctuate over time.) A disciplined investment process, combining macroeconomic analysis, stock selection and robust risk management, is adopted.

The fund also holds a modest allocation to asset-backed securities (ABS), a type of bond whose income is derived from a pool of underlying assets, such as mortgages, credit cards or student loans. ABS typically pay a variable rate of income and therefore provide an element of protection against rising interest rates.

\* For the performance of each share class, please refer to the 'Long-term performance by share class' table in the 'Fund performance' section of the Annual Long Report and audited Financial Statements for M&G Investment Funds (10).

To give an indication of the performance of the fund, the following table shows the compound rate of return, per annum, over the period for Sterling Class 'A' (Accumulation) shares and Sterling Class 'I' (Accumulation) shares after the ongoing Charges figure has been taken. Calculated on a price to price basis with income reinvested.

Long-term performance				
	One year 03.04.17 % <sup>[a]</sup>	Three years 02.04.15 % p.a.	Five years 03.04.13 % p.a.	Since launch % p.a.
<b>Sterling<sup>[b]</sup></b>				
Class 'A'	+1.5	n/a	n/a	+2.2 <sup>[c]</sup>
Class 'I'	+1.8	n/a	n/a	+2.4 <sup>[c]</sup>

<sup>[a]</sup> Absolute basis.

<sup>[b]</sup> Price to price with income reinvested.

<sup>[c]</sup> 13 December 2016, the launch date of the fund.

Please note past performance is not a guide to future performance and the value of investments, and the income from them, will fluctuate. This will cause the fund price to fall as well as rise and you may not get back the original amount you invested.

## Investment performance

After an extended period of calm, volatility returned to financial markets in early 2018. The previous year saw strong performance for higher risk assets such as corporate bonds, as the global economy continued to deliver positive growth surprises. However, this appears to have led to fears of inflationary pressures in the US, where markets appear sensitive to the idea that the US central bank could raise interest rates faster than previously indicated.

Prospective returns on US government bonds subsequently rose to their highest levels in several years in February, which influenced price movements across many other types of asset. Corporate bond prices generally fell sharply. Markets also appear to have regained sensitivity to political developments after a resilient prior year. Towards the end of the review period, government bond yields reversed slightly, as further volatility prompted investors to retreat to perceived safe-haven assets.

Against this backdrop, the fund's cautious positioning helped to mitigate some of the effects of recent market volatility, which resulted in overall performance remaining positive for the review period.

## Investment activities

The fund is currently positioned cautiously with a low sensitivity to movements in interest rates, as we believe that expected moves by central banks towards 'normal' monetary policy for the first time since the global financial crisis pose a medium-term threat to government bonds.

We have continued to find what we believe are attractive opportunities in selected corporate bonds. We have also invested in bonds with shorter maturities, as these assets are typically less sensitive to interest rate movements. (Maturity is the length of time until the initial investment amount – the 'principal' of a fixed income security – is due to be repaid to the holder.)

The fund has held modest exposure to traditional 'safe-haven' currencies such as the US dollar, Swiss franc and Japanese yen. Recently, we also added some exposure to emerging market currencies from Colombia, Mexico and Russia, as we believe these assets offer attractive value.

## Outlook

We believe that market volatility is likely to remain higher in 2018, as business and financial cycles mature and asset prices that have been supported by the low interest rate environment potentially correct. In Europe, we also expect the European Central Bank to take further steps towards normalising monetary policy if the eurozone economy continues to strengthen. As such, we will continue to position the portfolio cautiously with a view to minimising the effects of further potential market volatility and rate rises.

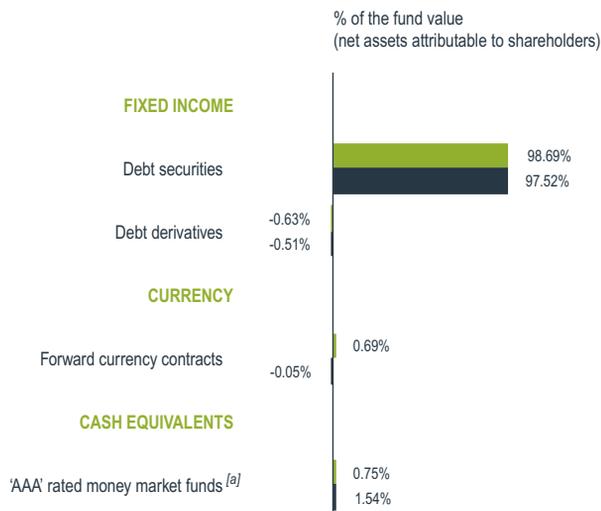
### Jim Leaviss & Wolfgang Bauer

Co-fund managers

Employees of M&G Limited which is an associate of M&G Securities Limited.

Please note that the views expressed in this Report should not be taken as a recommendation or advice on how the fund or any holding mentioned in the Report is likely to perform. If you wish to obtain financial advice as to whether an investment is suitable for your needs, you should consult a Financial Adviser.

### Classification of investments



<sup>[a]</sup> Uncommitted surplus cash is placed into 'AAA' rated money market funds with the aim of reducing counterparty risk.

■ 31 March 2018  
■ 31 March 2017

Source: M&G

Please note past performance is not a guide to future performance and the value of investments, and the income from them, will fluctuate. This will cause the fund price to fall as well as rise and you may not get back the original amount you invested.

The following chart and tables show the performance for two of the fund's share classes – Sterling Class 'A' (Accumulation) shares and Sterling Class 'I' (Accumulation) shares.

We show performance for these two share classes because:

- The performance of the Sterling Class 'A' (Accumulation) share is what most individuals investing directly with M&G have received. It has the highest ongoing charge of all the share classes. Performance is shown after deduction of this charge. All investors in the fund therefore received this performance or better.
- The performance of the Sterling Class 'I' (Accumulation) share is the most appropriate to compare with the average performance of the fund's comparative sector. It is the share class used by the Investment Association in the calculation of the comparative sector's average performance. This share class is available for direct investment with M&G subject to minimum investment criteria, or via third parties who may charge additional fees. The performance shown takes the deduction of the ongoing charge for this share class into account but it does not take account of charges applied by any other party through which you may have invested.

The fund is available for investment in different share classes, each with varying levels of charges and minimum investments; please refer to the Prospectus for M&G Investment Funds (10), which is available free of charge either from our website at [www.mandg.co.uk/prospectuses](http://www.mandg.co.uk/prospectuses) or by calling M&G Customer Relations. For the specific performance tables of all share classes, please refer to the Annual Long Report and audited Financial Statements for M&G Investment Funds (10), which is available free of charge either from our website at [www.mandg.co.uk/reports](http://www.mandg.co.uk/reports) or by calling M&G Customer Relations.

### Fund level performance

#### Fund net asset value

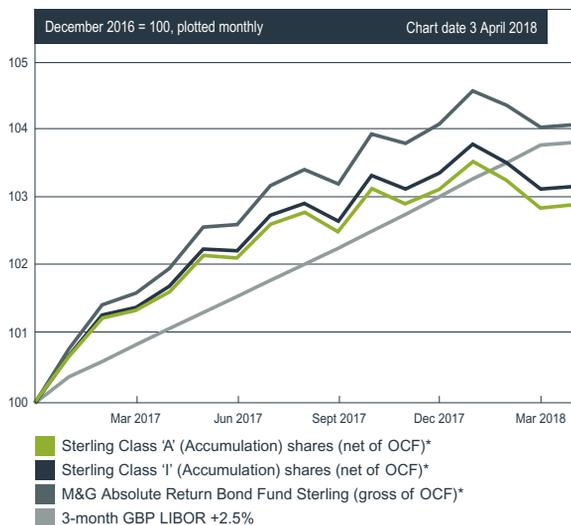
	2018 £'000	2017 £'000
as at 31 March		
Fund net asset value (NAV)	33,565	17,126

# Financial highlights

## Fund performance

### Performance since launch

To give an indication of how the fund has performed since launch, the chart below shows total return of Sterling Class 'A' (Accumulation) shares and Sterling Class 'I' (Accumulation) shares.



\* Income reinvested

The past performance shown here is for both gross returns (before the ongoing charges figure is taken) in line with the objective of the fund and net returns (after the ongoing charges figure has been taken) to illustrate how charges affected the performance. Investors should note that the net return is what they would receive and is therefore the more relevant figure.

Source: Morningstar, Inc. and M&G

To give an indication of how the fund has performed during the period the tables below show the performance of Sterling Class 'A' (Accumulation) shares and Sterling Class 'I' (Accumulation) shares.

All 'Performance and charges' percentages represent an annual rate except for the 'Return after operating charges' which is calculated as a percentage of the opening net asset value per share (NAV). 'Dilution adjustments' are only in respect of direct portfolio transaction costs.

### Sterling Class 'A' Accumulation share performance

The share class was launched on 13 December 2016.

for the year to 31 March Change in NAV per share	2018 UK p	2017 UK p
Opening NAV	100.87	100.00
Return before operating charges and after direct portfolio transaction costs	2.57	1.18
Operating charges	(0.86)	(0.31)
Return after operating charges	1.71	0.87
Distributions	(1.40)	(0.28)
Retained distributions	1.40	0.28
Closing NAV	102.58	100.87

Direct portfolio transaction costs	UK p	UK p
Costs before dilution adjustments	0.00	0.00
Dilution adjustments <sup>[a]</sup>	0.00	0.00
Total direct portfolio transaction costs	0.00	0.00

Performance and charges	%	%
Direct portfolio transaction costs <sup>[b]</sup>	0.00	0.00
Operating charges	0.85	1.04*
Return after operating charges	+1.70	+0.87
Distribution yield	1.59	1.40
Effect on yield of charges offset against capital	0.00	0.00

### Other information

Closing NAV (£'000)	258	20
Closing NAV percentage of total fund NAV (%)	0.77	0.12
Number of shares	251,544	20,000
Highest share price (UK p)	103.61	101.38
Lowest share price (UK p)	101.32	99.89

\* The operating charge shown is an estimate of the charges, as the share class has not been in existence for a full financial year.

# Financial highlights

## Fund performance

### Sterling Class 'I' Accumulation share performance

The share class was launched on 13 December 2016.

for the year to 31 March Change in NAV per share	2018 UK p	2017 UK p
Opening NAV	100.93	100.00
Return before operating charges and after direct portfolio transaction costs	2.57	1.18
Operating charges	(0.64)	(0.25)
Return after operating charges	1.93	0.93
Distributions	(1.63)	(0.34)
Retained distributions	1.63	0.34
Closing NAV	102.86	100.93

Direct portfolio transaction costs	UK p	UK p
Costs before dilution adjustments	0.00	0.00
Dilution adjustments <sup>[a]</sup>	0.00	0.00
Total direct portfolio transaction costs	0.00	0.00

Performance and charges	%	%
Direct portfolio transaction costs <sup>[b]</sup>	0.00	0.00
Operating charges	0.63	0.85*
Return after operating charges	+1.91	+0.93
Distribution yield	1.79	1.60
Effect on yield of charges offset against capital	0.00	0.00

#### Other information

Closing NAV (£'000)	26,443	16,669
Closing NAV percentage of total fund NAV (%)	78.78	97.33
Number of shares	25,708,589	16,516,155
Highest share price (UK p)	103.86	101.42
Lowest share price (UK p)	101.38	99.89

\* The operating charge shown is an estimate of the charges, as the share class has not been in existence for a full financial year.

<sup>[a]</sup> In respect of direct portfolio transaction costs.

<sup>[b]</sup> As a percentage of average net asset value.

# Financial highlights

## Operating charges and portfolio transaction costs

We explain below the payments made to meet the ongoing costs of investing and managing the fund, comprising operating charges and portfolio transaction costs.

### Operating charges

Operating charges include payments made to M&G and to providers independent of M&G:

- **Investment management:** Charge paid to M&G for investment management of the fund (also known as Annual Management Charge).
- **Administration:** Charge paid to M&G for administration services in addition to investment management – any surplus from this charge will be retained by M&G.
- **Oversight and other independent services:** Charges paid to providers independent of M&G for services which include depositary, custody and audit.
- **Ongoing charges from underlying funds:** Ongoing charges on holdings in underlying funds that are not rebated.

Operating charges do not include portfolio transaction costs or any entry and exit charges (also known as initial and redemption charges). The charging structures of share classes may differ, and therefore the operating charges may differ.

Operating charges are the same as the ongoing charges shown in the Key Investor Information Document, other than where an estimate has been used for the ongoing charge because a material change has made the operating charges unreliable as an estimate of future charges.

For this fund there is no difference between operating charges and ongoing charges figures, unless disclosed under the specific share class performance table.

# Financial highlights

## Operating charges and portfolio transaction costs

### Portfolio transaction costs

Portfolio transaction costs are incurred by funds when buying and selling investments. These costs vary depending on the types of investment, their market capitalisation, country of exchange and method of execution. They are made up of direct and indirect portfolio transaction costs:

- **Direct portfolio transaction costs:** Broker execution commission and taxes.
- **Indirect portfolio transaction costs:** 'Dealing spread' – the difference between the buying and selling prices of the fund's investments; some types of investment, such as fixed interest securities, have no direct transaction costs and only the dealing spread is paid.

Investments are bought or sold by a fund when changes are made to the investment portfolio and in response to net flows of money into or out of the fund from investors buying and selling shares in the fund.

To protect existing investors, portfolio transaction costs incurred as a result of investors buying and selling shares in the fund are recovered from those investors through a 'dilution adjustment' to the price they pay or receive. As the fund invests mainly in fixed interest securities, the direct transaction costs paid on other investments are too small to be reflected in the table below. To give an indication of the indirect portfolio dealing costs the table below shows the average portfolio dealing spread.

Further information on this process is in the Prospectus, which is available free of charge on request either from our website at [www.mandg.co.uk/prospectuses](http://www.mandg.co.uk/prospectuses) or by calling M&G Customer Relations.

Portfolio transaction costs			
as at 31 March	2018	2017	Average <sup>[a]</sup>
Indirect portfolio transaction costs	%	%	%
Average portfolio dealing spread	0.50	0.46	0.48

[a] Average of first two columns.

# Contact



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\*\* Please remember to quote your name and M&G client reference and sign any written communication to M&G. Failure to provide this may affect your ability to transact with us.

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