



## **M&G Global High Yield Bond Fund**

a sub-fund of M&G Investment Funds (2)

Annual Short Report May 2019

For the year ended 31 May 2019

The Authorised Corporate Director (ACD) of M&G Investment Funds (2) presents its Annual Short Report for M&G Global High Yield 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 (2), incorporating all the sub-funds and a Glossary of terms 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 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 28 September 2018, the Depositary changed from National Westminster Bank Plc to NatWest Trustee & Depositary Services Limited.

As a result of the Extraordinary General Meetings of Shareholders held on 4 October 2018, the non-sterling share classes of the M&G Global High Yield Bond Fund were merged into corresponding share classes of the equivalent sub-fund in M&G (Lux) Investment Funds 1. The effective date of the merger for the M&G Global High Yield Bond Fund was 9 November 2018. For further details of the Merger, please refer to [www.mandg.com/brexitmergerdocumentation](http://www.mandg.com/brexitmergerdocumentation).

Please note on 8 April 2019 the M&G Global High Yield Bond Fund launched the Sterling Class 'PP' (Accumulation) share class.

As per shareholder letter 17 June 2019, we are making changes to the way we charge for M&G funds based in the UK, starting on Thursday 1 August 2019. The annual charge should be simpler to understand and easier to compare with other fund charges. We are combining all the charges that make up the current ongoing charge figure (OCF) into a single annual charge. Only exceptional items such as unforeseen legal and tax expenses, also known as extraordinary expenses, will be excluded from the annual charge. To find out the new annual charge and the OCF on the KIID for the share class(es) you are invested in, visit our website [www.mandg.co.uk](http://www.mandg.co.uk).

### Investment objective

The fund aims to provide income and capital growth.

### Investment policy

At least 80% of the fund is invested in higher yielding corporate debt instruments which may be denominated in sterling, European currencies and other major global currencies, should the investment managers deem them to be appropriate investments. The fund's exposure to higher yielding corporate debt instruments may be gained through the use of derivatives and any currency exposures within the fund may be managed by currency hedges into sterling. Derivatives may also be used for efficient portfolio management. The fund may also invest in collective investment schemes, government and public securities and other transferable securities, cash, near cash, other money market instruments, warrants and other derivative instruments. More than 80% of the fund will be in sterling or hedged back to sterling.

### Investment approach

The fund manager concentrates on bottom-up analysis of individual bond issues while remaining aware of macroeconomic developments. Emphasis is placed upon investigating the ability of a company or government to meet its interest payments, especially during unfavourable economic conditions. Credit risk is constantly monitored and typically spread across a variety of countries and industrial sectors.

### Risk profile

The fund invests mainly in higher yielding fixed income securities, which may be denominated in sterling, European currencies and other major global currencies. It is, therefore, subject to the price volatility of the global bond market as well as the performance of individual issuers. In addition, the fund is subject to fluctuations in currency exchange rates.

The fund's focus on higher yielding debt securities implies that it may experience greater volatility than a fund that invests primarily in investment grade debt securities as higher risk assets could potentially experience a degree of illiquidity in times of market distress.

The fund's exposure to debt 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 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 (2).

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 June 2019, for the year ended 31 May 2019

### Performance against objective

Between 1 June 2018 (the start of the review period) and 3 June 2019, the M&G Global High Yield Bond Fund delivered a positive total return (the combination of income and growth of capital) for its sterling share classes.

Between 1 June 2018 and 9 November 2018, the fund's US dollar share class produced a small positive return, but its euro and Swiss franc share classes posted negative returns. On 9 November 2018 the fund's non-sterling share classes merged into the M&G (Lux) Global High Yield Bond Fund, a Luxembourg-authorized SICAV, which launched on that date.

In this reporting period, the fund has met its objective of providing income\* and capital growth, and it has also met its objective over three and five years and since launch.\*\*

\* The fund's distribution and distribution yield are as shown in the 'Specific share class performance' tables in the 'Fund performance' section of the Annual Long Report and audited Financial Statements for M&G Investment Funds (2). This fund provides a variable level of income.

\*\* For the performance of each share class, please refer to the 'Long-term performance by share class' table in the 'Financial highlights' section of the Annual Long Report and audited Financial Statements for M&G Investment Funds (2).

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. Calculated on a price to price basis with income reinvested.

Long-term performance				
	From 01.06.18 % <sup>[a]</sup>	From 03.06.16 % p.a.	From 03.06.14 % p.a.	Since launch % p.a.
<b>Sterling<sup>[b]</sup></b>				
Class 'A'	+1.5	+3.9	+2.4	+5.5 <sup>[c]</sup>
Class 'I'	+2.1	+4.5	+3.0	+5.1 <sup>[d]</sup>

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

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

<sup>[c]</sup> 1 October 2002, the launch date of the share class.

<sup>[d]</sup> 3 August 2012, the launch date of the share class.

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

The 12 months under review was a challenging period for high yield bond markets. (High yield bonds are loans paying fixed interest issued by companies with a low credit rating. Credit ratings are independent assessments of a borrower's ability to repay loans. Bonds from low-rated companies are considered riskier than those issued by companies with a high credit rating. They therefore pay a higher rate of interest than their higher rated counterparts, to compensate investors for the greater possibility that the issuer might be unable to meet its obligations, or in other words, default.)

After delivering solid investment returns throughout much of 2016 and 2017, high yield markets faced a more difficult market environment throughout much of 2018. A variety of factors weighed on sentiment during the year, including concerns over the negative impact of rising US interest rates, escalating trade war tensions between the US and China, and political turmoil in Europe and several emerging markets.

There was a change of fortune in 2019, with high yield markets recovering strongly in the first few months of the year. While global economic activity remained lacklustre, sentiment was boosted by the prospect that further US interest rate rises would be postponed for the time being. However, high yield bond markets experienced further weakness in May as a resurfacing of trade war tensions led to another period of risk aversion.

From a regional perspective, US high yield bonds outperformed other regions over the 12-month period, thanks in part to the continued resilience of the US economy. High yields bonds in Europe and emerging markets, however, endured a more challenging backdrop, with ongoing political uncertainty and slowing economic momentum weighing on returns.

The fund's sterling share classes delivered a small positive return over the review period, although they lagged the IA £ High Yield Sector. The fund's defensive sector positioning and modest exposure to emerging markets proved helpful overall, although this was more than offset by a bias towards European issuers and the financial sector, which generally underperformed.

## Investment activities

There were no significant changes to fund positioning and we maintain our preference for defensive companies that offer resilient cashflows irrespective of the economic environment, such as healthcare providers and cable operators.

In regional allocation terms, we maintain a slight preference for European high yield. We generally see more compelling value in the European high yield market, following its recent underperformance versus the US; we think investors can often capture a more attractive level of income relative to the risks being taken. Moreover, with the European economy at an earlier stage of the economic cycle, we believe European companies are still being conservatively managed and continue to maintain only modest levels of debt on their balance sheets.

We remain cautiously positioned in the energy and basic industry sectors, where in most cases we do not think investors are being adequately compensated for the risks. However, we will invest in these areas on a selective basis where we see compelling value, for instance purchasing an issue from oil & gas exploration company SM Energy.

We continue to find attractive opportunities in the primary market and we purchased newly issued bonds from a variety of companies, including US housebuilder Taylor Morrison and European telecom companies Altice and Ziggo. In terms of sales, we closed our positions in paper-based packaging company Smurfit Kappa and automaker Jaguar Land Rover after a strong run.

Fund duration (a measure of a bond fund's sensitivity to movements in interest rates) was broadly unchanged over the 12 months and stood at around 3.4 years as at the end of May. Given the relative strength of the US economy, we think further US interest rate rises could still be on the cards, and we prefer to maintain a cautious stance.

## Outlook

In the current environment where interest rates are low and many assets are generating a low prospective return, or yield, we think high yield bonds currently offer an attractive source of income. Following market weakness throughout much of 2018, we believe these assets look attractively priced against a backdrop of modest economic expansion and with the expectation that company default rates remain at historically low levels.

However, given where we are in the market cycle, we believe a cautious approach is still warranted and we maintain our preference for defensive businesses offering stable cashflows and healthy balance sheets. With heightened volatility likely to lead to a greater divergence in bond prices, we believe that careful individual bond selection and in-depth company analysis will become increasingly important to help identify the most attractive pockets of value.

In our view, high yield investing is as much about avoiding the losers as picking the winners. On this basis, we remain cautiously positioned in the retail sector. UK fashion retailers in particular have been experiencing higher input costs as a result of the depreciation in sterling, coupled with signs of a slowdown in consumer spending. The sector is also facing longer term structural headwinds as shoppers increasingly move towards online spending and away from traditional bricks-and-mortar stores. While some of these businesses will be able to adapt, we continue to be very selective in this space.

## Stefan Isaacs & James Tomlins

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 spread of investments

The table below shows the percentage holding per sector.

as at 31 May	% of fund	
	2019	2018
<b>EQUITIES</b>		
Equities	0.23	0.65
<b>FIXED INCOME</b>		
<b>Debt securities</b>		
'AA' credit rated bonds	4.87	6.08
'A' credit rated bonds	1.71	2.40
'BBB' credit rated bonds	10.23	10.17
'BB' credit rated bonds	48.24	45.84
'B' credit rated bonds	22.57	21.95
'CCC' credit rated bonds	3.01	2.63
'C' credit rated bonds	0.00	0.13
Bonds with no credit rating	2.34	3.58
<b>Debt derivatives</b>		
Credit default swaps	0.34	0.48 <sup>[a]</sup>
Asset swaps	(0.01)	0.02 <sup>[a]</sup>
Interest rate futures	(0.07)	(0.09)
<b>CURRENCY</b>		
Forward currency contracts	(2.97)	0.01
<b>CASH EQUIVALENTS</b>		
'AAA' rated money market funds <sup>[b]</sup>	6.31	4.16
<b>SHARE CLASS HEDGING</b>		
Forward currency contracts for share class hedging	0.00	(0.01)

<sup>[a]</sup> The comparative sector weightings have been re-analysed to reflect changes to the sector classifications.

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

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 charts 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 sterling share classes. Performance is shown after deduction of this charge. All UK 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 (2), 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 (2), 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

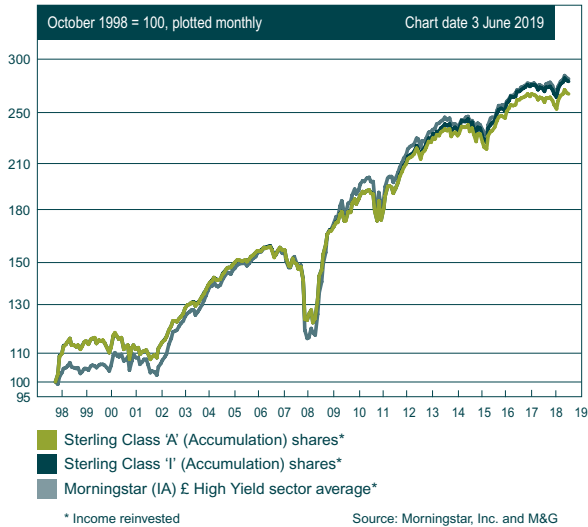
as at 31 May	2019 £'000	2018 £'000	2017 £'000
Fund net asset value (NAV)	1,058,635	1,172,791	1,185,263

# Financial highlights

## Fund performance

### Performance since launch

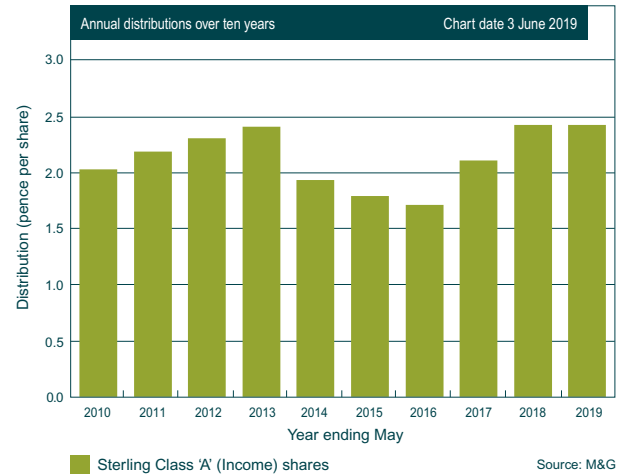
To give an indication of how the fund has performed since launch, the chart below shows total return of Sterling Class 'A' (Accumulation) shares and Sterling Class 'I' (Accumulation) shares.



The fund's Sterling Class 'I' (Accumulation) shares were launched on 3 August 2012. Performance data shown prior to this date is that of the fund's Sterling Class 'A' (Accumulation) shares.

### Distribution

The charts below show the annual distribution of Sterling Class 'A' (Income) shares over ten years and Sterling Class 'I' (Income) shares since launch.



# Financial highlights

## Fund performance

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 1 October 2002.

for the year to 31 May Change in NAV per share	2019 UK p	2018 UK p	2017 UK p
Opening NAV	130.02	129.44	117.38
Return before operating charges and after direct portfolio transaction costs	5.24	2.44	14.58
Operating charges	(1.86)	(1.86)	(1.75)
Return after operating charges	3.38	0.58	12.83
Distributions	(4.81)	(4.48)	(5.00)
Retained distributions	4.81	4.48	4.23
Closing NAV	133.40	130.02	129.44

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

Performance and charges	%	%	%
Direct portfolio transaction costs <sup>[b]</sup>	0.00	0.00	0.00
Operating charges	1.41	1.41	1.41
Return after operating charges	+2.60	+0.45	+10.93
Distribution yield	3.79	3.58	3.28
Effect on yield of charges offset against capital	0.00	0.00	0.00

#### Other information

Closing NAV (£'000)	250,671	259,871	247,752
Closing NAV percentage of total fund NAV (%)	23.68	22.16	20.90
Number of shares	187,906,510	199,863,410	191,398,631
Highest share price (UK p)	135.30	133.76	130.28
Lowest share price (UK p)	125.99	129.08	115.91

### Sterling Class 'I' Accumulation share performance

The share class was launched on 3 August 2012.

for the year to 31 May Change in NAV per share	2019 UK p	2018 UK p	2017 UK p
Opening NAV	1,365.39	1,351.18	1,219.04
Return before operating charges and after direct portfolio transaction costs	55.19	25.42	151.83
Operating charges	(11.27)	(11.21)	(10.48)
Return after operating charges	43.92	14.21	141.35
Distributions	(58.99)	(55.22)	(59.83)
Retained distributions	58.99	55.22	50.62
Closing NAV	1,409.31	1,365.39	1,351.18

Direct portfolio transaction costs	UK p	UK p	UK p
Costs before dilution adjustments	0.01	0.01	0.00
Dilution adjustments <sup>[a]</sup>	0.00	0.00	0.00
Total direct portfolio transaction costs	0.01	0.01	0.00

Performance and charges	%	%	%
Direct portfolio transaction costs <sup>[b]</sup>	0.00	0.00	0.00
Operating charges	0.81	0.81	0.81
Return after operating charges	+3.22	+1.05	+11.60
Distribution yield	4.39	4.18	3.88
Effect on yield of charges offset against capital	0.00	0.00	0.00

#### Other information

Closing NAV (£'000)	116,584	121,298	102,614
Closing NAV percentage of total fund NAV (%)	11.01	10.34	8.66
Number of shares	8,272,395	8,883,780	7,594,372
Highest share price (UK p)	1,429.11	1,401.66	1,359.96
Lowest share price (UK p)	1,327.60	1,348.33	1,204.20

<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.
- **Share class hedging:** Charge paid to M&G for currency hedging services to minimise exchange rate risk for the share class.
- **Oversight and other independent services:** Charges paid to providers independent of M&G for services which include depository, 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.

### 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 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 May	2019	2018	2017	Average <sup>[a]</sup>
Indirect portfolio transaction costs	%	%	%	%
Average portfolio dealing spread	0.84	0.79	0.65	0.76

[a] Average of first three columns.



# Contact



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