M&G UK Select Fund

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

Annual Short Report May 2019
For the year ended 31 May 2019

M&G INVESTMENTS

Fund information

The Authorised Corporate Director (ACD) of M&G Investment Funds (2) presents its Annual Short Report for M&G UK Select 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 or by calling M&G Customer Relations on 0800 390 390.

ACD

M&G Securities Limited,
10 Fenchurch Avenue, London EC3M 5AG
Telephone: 0800 390 390
(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 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.

Investment objective and policy up to 28 February 2019

The fund invests principally in the equities of UK companies with high growth potential with the sole objective of capital growth. The fund may at any time be concentrated in a limited number of equities. Income considerations are ignored.

Investment approach up to 28 February 2019

The fund manager employs a bottom-up stockpicking approach, driven by the fundamental analysis of individual companies. He seeks to invest in companies with sustainable competitive advantages that have the opportunity to reinvest their capital at high rates of return. A company's strategy around capital allocation is central to the investment process. The fund manager focuses on companies which recognise the importance of dividends, which in turn instils capital discipline and ensures that the highest-returning growth projects are prioritised. Rising free cashflow is expected to result in dividend growth of the fund's holdings being higher than that of a broad index of UK equities over the long term. This premium dividend growth is expected to drive the fund's long-term capital growth and growth in the fund's income distributions. The fund will hold less than 50 stocks, with a long-term investment view and a typical holding period of three to five years.

Investment objective from 1 March 2019

The fund aims to provide a higher total return (the combination of capital growth and income), net of the ongoing charge figure, than that of the FTSE All Share Index over any five-year period.

Fund information

Investment policy from 1 March 2019

At least 80% of the fund is invested directly in equity securities and equity-related securities of companies across any sectors and market capitalisations, that are incorporated, domiciled, listed or do most of their business in the United Kingdom.

The fund usually holds a concentrated portfolio of fewer than 50 companies.

The fund may also invest in other transferable securities directly and via collective investment schemes (including funds managed by M&G).

The fund may also hold cash and near cash for liquidity purposes.

Derivatives may be used for efficient portfolio management and hedging.

Investment approach from 1 March 2019

The fund employs a disciplined approach to investment which concentrates on the analysis and selection of individual companies.

The investment approach seeks to identify UK companies that have sustainable competitive advantages leading to high return on invested capital. Each company's strategy around capital allocation is central to the investment process.

The fund manager focuses on companies which recognise the importance of dividends, which in turn instils capital discipline and ensures that the highest returning growth projects are prioritised.

Rising cashflow, and over time, rising dividends, for the fund's holdings are expected to drive the long-term total return of the fund.

Risk profile

The fund invests in the shares of UK-listed companies and is, therefore, subject to the price volatility of the UK stockmarket and the performance of individual companies. The fund typically holds around 50 stocks and this relatively concentrated profile requires the fund manager to have strong conviction in each and every holding. However, the fund is mainly invested in the shares of large and medium-sized companies, which are normally traded with relative ease.

Diversification is key in managing liquidity risk and 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.

Low risk ← → High risk

Typically lower rewards — Typically higher rewards

1	2	3	4	**5**	6	7

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 fund delivered a negative total return (the combination of income and growth of capital) across all share classes. The total return by the fund's Sterling Class 'A' (Accumulation) shares of -3.5% was broadly in line with the FTSE All-Share Index, a comparative index, which returned -3.3%, while the fund's Sterling Class 'I' (Accumulation) shares returned -2.8%.

On 1 March 2019 the fund's objective changed to aiming to provide a higher total return (the combination of capital growth and income), net of the ongoing charge figure, than that of the FTSE All Share Index over any five-year period. Prior to this date, the fund's aim was to invest principally in the equities of UK companies with high growth potential, with the sole objective of capital growth. Income considerations were ignored.

The fund has not achieved its new objective over five years. The total returns by the fund's Sterling Class 'A' and 'I' (Accumulation) shares of 4.1% and 4.9% per annum respectively were behind the FTSE All-Share Index return of 5.3% per annum.*

* 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 (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

	One year 01.06.18 % [a]	Three years 03.06.16 % p.a.	Five years 03.06.14 % p.a.	Since launch % p.a.
Sterling [b]				
Class 'A'	-3.5	+6.9	+4.1	+9.5 [c]
Class 'I'	-2.8	+7.7	+4.9	+8.0 [d]

[a] Absolute basis.

[b] Price to price with income reinvested.

[c] 17 December 1968, the end of the initial offer period of the predecessor unit trust.

[d] 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 period of contrasts, with marked declines in UK and many global stockmarkets in the second half of 2018, before a significant rally in the early months of 2019. These moves resulted in the UK stockmarket recording a modest decline over the period.

Late 2018 saw a continuation of previous weakness on concerns about slowing US growth, just as the effect of President Trump's tax cuts was beginning to wane. Rising US protectionism and the prospect of higher interest rates added to investors' worries. However, risk appetite improved dramatically in the new year, after the US Federal Reserve indicated a pause in interest rate hikes due to concerns about their economic impact, the sharp increase in market volatility and muted domestic inflation. In addition, investors were encouraged by some better-than-expected corporate results, signs of progress in the US-China trade talks, and news that China's central bank was boosting lending in the Chinese economy in response to slowing growth. There was a brief setback in March when some business sentiment data in the US and Europe disappointed, before equity markets, the UK included, resumed their upward trajectory, with the US reaching a new all-time high. However, in the final month of the fund's year, investor sentiment deteriorated sharply as the US president surprised everyone by escalating his disputes over trade, initially with China but later taking aim at Mexico and India.

In the UK, Brexit increasingly dominated the headlines. Prime Minister Theresa May secured a withdrawal agreement with the EU, but MPs rejected the deal three times, along with a number of indicative votes on alternative options put forward by MPs. The original 29 March 2019 deadline for Brexit came and went after the EU agreed to extend the process. With the aim of avoiding a departure with no deal in place on 12 April, the Prime Minister secured agreement to a new deadline of 31 October 2019, before announcing that she would step down as party leader on 7 June when she accepted that she had insufficient support for her deal in Parliament, kick-starting the contest to find her replacement and a new Prime Minister.

Sterling experienced a volatile 12 months, mainly in response to Brexit developments. The currency stood at around US$1.33 at the start of the period, and passed lows of around US$1.25 in December as investors contemplated the possibility of a messy outcome or a general election. It then recovered to US$1.33 as 'no deal' appeared less likely in February, before settling at US$1.26 by the end of May 2019 in the wake of the prime minister's resignation.

All company size categories declined over the 12 months, reflecting the market sell-off in 2018. Larger companies were more resilient overall, assisted by sterling weakness in 2018. However, medium-sized companies have outperformed so far in 2019. Currency has been a big driver, with sterling weakness last year boosting the overseas revenues of UK multinationals, while sterling strength since the start of 2019 has brought down import costs for more domestically focused medium-sized and smaller companies.

Sector performance was mixed, reflecting the mid-term market volte-face, with mining, oil & gas producers, consumer staples, pharmaceuticals, media, fixed line telecoms, water utilities, non-life insurance and technology companies outperforming, while oil services, chemicals, industrials, tobacco, healthcare equipment, consumer services, mobile telecoms, financials and electricity generators underperformed. Notably, consumer staples (excluding tobacco) companies attracted support, reflecting their steady earnings growth characteristics. Technology was helped by the strength of the US sector, but it is a very small part of the UK market. The energy sector was lacklustre, as the oil price ended the 12-month period down slightly at US$66, although this disguised a rise to above US$86 in October, followed by a steep fall to US$50 by the end of 2018, before supply constraints and US sanctions caused the trend to reverse.

Against this background, there was a positive contribution to the fund's performance from stock selection within large and medium-sized stocks held in the portfolio, especially in mining, general retailers, financials, healthcare and software companies. Sector allocation also added value, primarily through holding above-market positions in personal goods and software, versus below-market positions in banks and mobile telecoms.

Some performance was surrendered, however, as the fund had a below market position in larger companies, which outperformed, helped by sterling weakness against the US dollar, and an above-market position in medium-sized companies, which underperformed amidst concerns about the impact of Brexit on the economy. In addition, the fund has a small overseas exposure that lagged the domestic market.

The main individual contributors to the fund's performance included wealth manager AJ Bell, software firm Micro Focus, soft drinks manufacturer A.G. Barr, household goods and food producer Unilever, plus electronic exchange NEX. AJ Bell, which was only floated on the market in December, was a very strong performer as it benefited from the market rally in 2019. Micro Focus' latest results showed it is beginning to recover from last year's acquisition of HP Enterprise's software business. Consumer staples remained in demand over the 12 months and this was reflected in strong performances from AG Barr and Unilever. NEX was taken over in the second half of 2018 by CME (the Chicago Mercantile Exchange).

The principal individual detractors included paper and packaging manufacturer DS Smith, online travel company On The Beach, pizza delivery business Domino's Pizza and medical equipment manufacturer ConvaTec. DS Smith was affected by concerns about a supply glut and the debt required to fund the US$2 billion acquisition of rival Europac. On The Beach consolidated with the rest of the travel industry as a result of the hot weather across Europe and concerns about Brexit suppressing demand for foreign holidays. Domino's Pizza's international performance was worse than expected; however, the majority of its business is in the UK and Ireland, which generated an increase in revenues. ConvaTec's results were disappointing in 2018 and the chief executive has been replaced; the company, which makes colostomy bags and wound dressings, is under margin pressure from lower priced rivals, and in response has launched a US$150 million, three-year turnaround strategy.

In addition, the fund's overseas exposure lagged due to stock-specific issues, as PrairieSky Royalty and Methanex in Canada were affected by weaker energy prices, and Ireland's newly privatised AIB (Allied Irish Bank) succumbed to the Brexit uncertainty and worries about core profitability.

Investment activities

The main purchases over the 12-month period included London Stock Exchange (LSE), engineering group Rotork, cyber security firm GB Group and wealth manager AJ Bell.

LSE was added to the portfolio following the takeover of NEX. The exchange has been restructuring its business around revenue streams that are generated independently of market moves. Today only circa 20% of LSE's earnings are linked to the overall volume and price level of capital markets. The business has two highly moated businesses in LCH Clearnet and FTSE Russell Indices. The LSE purchase coincided with a market sell-off in October where Brexit became what was believed to be a mispriced concern.

Rotork is one of the highest quality companies in the global engineering sector. Through its control valve actuator – a device that takes a process signal and controls a valve – Rotork has established market leadership where brand, service and a reliable reputation have been built up over more than 60 years of actuator development. Actuators are sold into process industries, with core markets in oil and gas, waste water and power. The cost of an actuator is very low in the context of a new build refinery or waste water treatment facility, and consequently Rotork has strong pricing power.

GB's products and services are largely software solutions that use third-party data banks to help businesses validate and verify the location and identity of their consumers. The structural growth in these markets is highly attractive given the digitisation trends and increase in security concerns as more and more businesses and consumers move online. GB's organic growth has run between 10-15% per annum as the group focuses on expanding existing products into new geographies.

AJ Bell was added to the portfolio via a market flotation in December 2018. The company operates platforms used by financial advisers and DIY investors, and is one of two DIY platforms that is profitable in a fragmented market. The business has now reached scale and should continue to drive +10% profit growth as market share grows (4% on DIY and 5% on the adviser platform) on costs that are largely fixed. The business is net cash, requires negligible capital to continue growing and is expected to pay out 65% of its earnings to shareholders via dividends.

The main sales over the 12-month period included mezzanine finance specialist Intermediate Capital (ICG), Irish construction materials firm CRH, office space developer Workspace and the UK's leading pet-and-vet retailer Pets at Home.

Investors in ICG have been well rewarded with outperformance and the business has enjoyed the benefit of margin expansion as assets have grown. The decision to sell was based upon performance whereby the shares appeared to be fully valued and the funds raised could be put to use in investments with greater upside.

Confidence was lost in the CRH investment case for two reasons. The first was that although CRH has an outstanding long-term dividend record, it was felt that the growth of the dividend was of secondary importance to driving acquisitive growth. The second reason was due to the number of large acquisitions the company seemed to be pursuing.

The Workspace holding was sold because of growing concerns about supply additions and increased competition in temporary offices led by the growth of providers such as WeWork, which appears more than happy to run at a loss as it grows market share. The fund's position in Workspace had been trimmed previously due to valuation concerns, although the decision to exit was taken when the company issued equity to bolster its balance sheet for further acquisitions. However, the shares had delivered good performance during the time they were held in the portfolio.

The decision to buy Pets at Home in 2017 was predicated on the strength of the Vets franchise, which, it was believed, would drive growth at higher rates of return than the business was generating in the conventional retail operation. However, the Vets operation has struggled to grow profitability in line with expectations, and in some cases has been forced to receive loans from Pets at Home to cover losses within the Vets clinic. This meant that more of Pets At Home's capital was tied up in the Vets clinic than anticipated and, as it was felt that earnings and dividend growth would not materialise as expected, the holding was sold.

A number of companies also exited the portfolio due to takeovers and these included drugmaker Shire, Zoopla owner ZPG and electronic exchange NEX.

Outlook

The UK equity market has proved to be remarkably sanguine so far this year, notwithstanding a deterioration in the economic outlook at home and abroad, an increase in trade tensions between the US and its major trading partners, and concerns around Brexit, which is effectively on hold until the Conservative Party finds a new leader and prime minister.

The main reasons behind the market's support have been the Bank of England's maintenance of a low interest rate policy, together with the low level of bond yields. Another factor, however, has been a remarkably resilient consumer, helped by unemployment at a 44-year low and wage growth that has finally overtaken inflation. In addition, UK equities began 2019 looking relatively cheap as investors reacted to the increased uncertainty over Brexit. Despite this year's rally, the UK equity market still represents fair value compared to other equity markets, but it is likely to remain at a discount to them until the Brexit imbroglio has run its course.

Sterling has tended to be more immediately reflective of the Brexit outlook and it is expected to rally strongly if 'no deal' is avoided, and sell off sharply in the wake of a hard Brexit. A deal would also support the equity market, especially domestic stocks, and may potentially reduce the risk of a Labour government, worries about which have also acted as a restraint on the market's upward progress. But even in the circumstances of a no deal scenario, with 75% of FTSE 100 companies' earnings derived from overseas, the market should find some support. Longer term, UK companies' balance sheets are well capitalised, and earnings and dividend growth supportive, assisted by the Bank of England's stimulative monetary policy.

With the M&G UK Select Fund, we are trying to create a concentrated and high-conviction portfolio of great investments that combine to minimise any macroeconomic exposure. So whether we see events such as a no-deal Brexit, a Trump impeachment, China/US trade negotiations sour or global economic growth grind to a halt, we aim to outperform over the longer term.

Rory Alexander
Fund manager

An employee of M&G Limited which is an associate of M&G Securities Limited. At the start of the review period Sam Ford was the fund manager.

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.

Portfolio statement

as at 31 May Holding		2019 £'000	2019 %	2018 [a] %
	EQUITIES	**560,471**	**96.44**	**98.39**
	Software & computer services	**30,878**	**5.30**	**3.25**
1,900,000	GB	11,704	2.01	
1,550,000	Sage	11,532	1.98	
1,847,746	Sophos	7,642	1.31	
	Technology hardware & equipment	**2,341**	**0.40**	**0.00**
3,021,026	IQE	2,341	0.40	
	Telecommunication service providers	**0**	**0.00**	**1.35**
	Medical equipment & services	**20,519**	**3.53**	**4.28**
4,963,382	ConvaTec	6,976	1.20	
810,000	Smith & Nephew	13,543	2.33	
	Pharmaceuticals & biotechnology	**35,566**	**6.11**	**9.09**
492,400	AstraZeneca	28,668	4.93	
230,000	Dechra Pharmaceuticals	6,293	1.08	
27,902	Hutchison China MediTech ADR	605	0.10	
	Banks	**52,724**	**9.07**	**7.39**
2,676,472	HSBC	17,303	2.98	
34,000,000	Lloyds Banking	19,482	3.35	
2,335,000	Standard Chartered	15,939	2.74	
	Investment banking & brokerage services	**74,049**	**12.75**	**5.94**
3,200,000	AJ Bell	13,312	2.29	
751,139	Burford Capital	12,394	2.13	
1,400,000	IntegraFin	5,501	0.95	
902,160	Liontrust Asset Management	6,044	1.04	
480,000	London Stock Exchange	25,027	4.31	
8,058,002	Man	11,771	2.03	
	Life insurance	**25,345**	**4.37**	**7.35**
520,000	Prudential [b]	8,226	1.42	
1,650,000	St. James's Place	17,119	2.95	
	Non-life insurance	**13,423**	**2.31**	**2.39**
820,000	Hiscox	13,423	2.31	
	Real estate investment trusts	**0**	**0.00**	**1.25**
	Household goods & home construction	**32,941**	**5.66**	**5.21**
4,075,000	Countryside Properties	12,404	2.13	
325,000	Reckitt Benckiser	20,537	3.53	
	Leisure goods	**0**	**0.00**	**0.46**

Portfolio statement (continued)

as at 31 May Holding		2019 £'000	2019 %	2018 [a] %
	Personal goods	**39,673**	**6.83**	**7.32**
227,844	Burberry	3,872	0.67	
740,000	Unilever	35,801	6.16	
	Media	**25,188**	**4.33**	**3.43**
2,989,896	Ascential	11,750	2.02	
2,034,174	Moneysupermarket.com	7,425	1.28	
1,070,000	Next Fifteen Communications	6,013	1.03	
	Retailers	**21,845**	**3.76**	**4.07**
1,110,000	WH Smith	21,845	3.76	
	Travel & leisure	**10,735**	**1.85**	**3.70**
2,375,000	On the Beach	10,735	1.85	
	Beverages	**4,740**	**0.82**	**2.47**
500,000	A.G. Barr	4,740	0.82	
	Food producers	**17,523**	**3.02**	**1.26**
640,000	Cranswick	17,523	3.02	
	Tobacco	**17,843**	**3.07**	**5.34**
640,000	British American Tobacco	17,843	3.07	
	Construction & materials	**2,341**	**0.40**	**1.27**
545,179	Polypipe	2,341	0.40	
	General industrials	**19,695**	**3.39**	**5.84**
1,165,949	DS Smith	3,651	0.63	
1,120,000	Smiths	16,044	2.76	
	Industrial engineering	**25,430**	**4.38**	**1.81**
160,000	Kone	6,904	1.19	
6,560,036	Rotork	18,526	3.19	
	Industrial support services	**27,040**	**4.65**	**1.89**
1,909,069	Essentra	7,640	1.31	
499,685	Experian	11,843	2.04	
143,075	Intertek	7,557	1.30	
	Industrial transportation	**2,762**	**0.48**	**0.00**
114,130	Clarkson	2,762	0.48	
	Industrial metals & mining	**0**	**0.00**	**1.58**
	Chemicals	**17,572**	**3.03**	**2.86**
328,643	Methanex	11,306	1.95	
320,000	Victrex	6,266	1.08	
	Non-renewable energy	**40,298**	**6.93**	**7.59**
7,500,000	BP	40,298	6.93	

Portfolio statement (continued)

as at 31 May Holding		2019 £'000	2019 %	2018 [a] %
	Unquoted / unlisted	**0**	**0.00**	**0.00**
770,825	Izodia [c]	0	0.00	
Portfolio of investments		**560,471**	**96.44**	**98.39**
	CASH EQUIVALENTS	**45,048**	**7.75**	**1.99**
	'AAA' rated money market funds [d]	**45,048**	**7.75**	**1.99**
45,048,168	Northern Trust Global Fund - Sterling	45,048	7.75	
Total portfolio		**605,519**	**104.19**	**100.38**
Net other assets / (liabilities)		**(24,352)**	**(4.19)**	**(0.38)**
Net assets attributable to shareholders		**581,167**	**100.00**	**100.00**

All securities are on an official stock exchange listing except where referenced.

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

[b] Related party to the fund.

[c] Suspended.

[d] Uncommitted surplus cash is placed into 'AAA' rated money market funds with the aim of reducing counterparty risk.

Top ten portfolio transactions

for the year to 31 May 2019

Largest purchases	**£'000**
London Stock Exchange	22,722
Rotork	20,392
HSBC	17,721
GVC	17,421
Cranswick	12,743
Burford Capital	12,233
Ascential	11,846
Experian	11,782
British American Tobacco	10,933
BP	9,249
Other purchases	166,202
Total purchases	**313,244**

Largest sales	**£'000**
ZPG	20,670
NEX	18,761
Prudential [a]	17,184
Imperial Brands	16,924
Shire	16,217
DS Smith	14,721
Burberry	14,604
A.G. Barr	14,574
Rio Tinto	14,431
Intermediate Capital	12,878
Other sales	153,321
Total sales	**314,285**

[a] Related party to the fund.

Purchases and sales exclude the cost and proceeds of 'AAA' rated money market funds.

Fund performance

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 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 or by calling M&G Customer Relations.

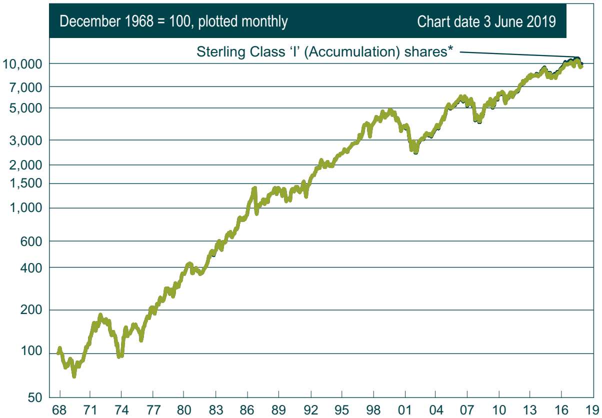
Fund level performance

Fund net asset value

as at 31 May	2019 £'000	2018 £'000	2017 £'000
Fund net asset value (NAV)	581,167	601,265	624,276

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.

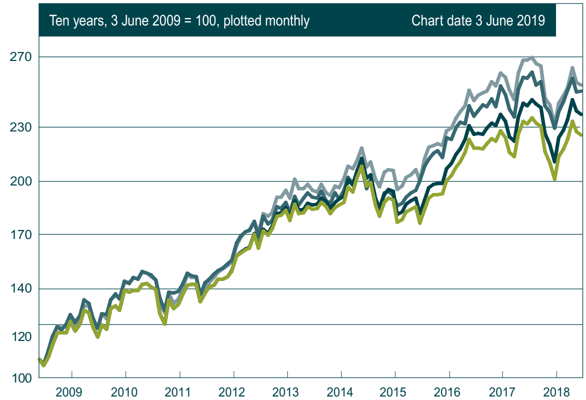


Sterling Class 'A' (Accumulation) shares*
Sterling Class 'I' (Accumulation) shares*

* Income reinvested   Source: Morningstar, Inc. and M&G

Ten-year performance

Please note that comparative data is not available from fund launch. Therefore a ten-year comparable performance chart is shown below.



Sterling Class 'A' (Accumulation) shares*
Sterling Class 'I' (Accumulation) shares*
FTSE All-Share Index
Morningstar (IA) UK All Companies sector average*

* Income reinvested   Source: Morningstar, Inc. and M&G

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.

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.

Historic yields for the current year are calculated as at 14 June 2019.

Sterling Class 'A' Accumulation share performance

The share class was launched on 17 December 1968.

for the year to 31 May Change in NAV per share	2019 UK p	2018 UK p	2017 UK p
Opening NAV	4,809.42	4,598.26	3,819.83
Return before operating charges and after direct portfolio transaction costs	(80.52)	286.79	845.98
Operating charges	(76.36)	(75.63)	(67.55)
Return after operating charges	(156.88)	211.16	778.43
Distributions	(73.22)	(52.09)	(45.73)
Retained distributions	73.22	52.09	45.73
Closing NAV	4,652.54	4,809.42	4,598.26
Direct portfolio transaction costs	**UK p**	**UK p**	**UK p**
Costs before dilution adjustments	11.87	7.84	14.75
Dilution adjustments [a]	(1.67)	(0.26)	(0.63)
Total direct portfolio transaction costs	10.20	7.58	14.12
Performance and charges	**%**	**%**	**%**
Direct portfolio transaction costs [b]	0.22	0.16	0.34
Operating charges	1.66	1.66	1.66
Return after operating charges	-3.26	+4.59	+20.38
Historic yield	1.56	1.08	1.02
Effect on yield of charges offset against capital	0.00	0.00	0.00
Other information			
Closing NAV (£'000)	180,828	203,795	221,522
Closing NAV percentage of total fund NAV (%)	31.11	33.89	35.48
Number of shares	3,886,649	4,237,421	4,817,512
Highest share price (UK p)	4,884.05	4,872.93	4,596.70
Lowest share price (UK p)	4,081.30	4,306.59	3,446.72

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	1,733.34	1,644.85	1,356.20
Return before operating charges and after direct portfolio transaction costs	(28.66)	103.40	301.43
Operating charges	(15.26)	(14.91)	(12.78)
Return after operating charges	(43.92)	88.49	288.65
Distributions	(38.96)	(30.98)	(27.14)
Retained distributions	38.96	30.98	27.14
Closing NAV	1,689.42	1,733.34	1,644.85
Direct portfolio transaction costs	**UK p**	**UK p**	**UK p**
Costs before dilution adjustments	4.31	2.82	5.09
Dilution adjustments [a]	(0.61)	(0.09)	(0.22)
Total direct portfolio transaction costs	3.70	2.73	4.87
Performance and charges	**%**	**%**	**%**
Direct portfolio transaction costs [b]	0.22	0.16	0.34
Operating charges	0.91	0.91	0.91
Return after operating charges	-2.53	+5.38	+21.28
Historic yield	2.29	1.79	1.68
Effect on yield of charges offset against capital	0.00	0.00	0.00
Other information			
Closing NAV (£'000)	88,570	50,251	45,357
Closing NAV percentage of total fund NAV (%)	15.24	8.36	7.27
Number of shares	5,242,643	2,899,075	2,757,523
Highest share price (UK p)	1,762.73	1,755.90	1,644.30
Lowest share price (UK p)	1,477.29	1,549.92	1,224.41

[a] In respect of direct portfolio transaction costs.

[b] As a percentage of average net asset value.

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.

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. The table below shows direct portfolio transaction costs paid by the fund before and after that part of the dilution adjustment relating to direct portfolio transaction costs. To give an indication of the indirect portfolio dealing costs the table also 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 or by calling M&G Customer Relations.

Portfolio transaction costs

for the year to 31 May Direct portfolio transaction costs [b]	2019 %	2018 %	2017 %	Average [a] %
Broker commission	0.04	0.03	0.09	0.05
Taxes	0.22	0.14	0.27	0.21
Costs before dilution adjustments	0.26	0.17	0.36	0.26
Dilution adjustments [c]	(0.04)	(0.01)	(0.02)	(0.02)
Total direct portfolio transaction costs	0.22	0.16	0.34	0.24

as at 31 May Indirect portfolio transaction costs	2019 %	2018 %	2017 %	Average [a] %
Average portfolio dealing spread	0.12	0.09	0.06	0.09

[a] Average of first three columns.

[b] As a percentage of average net asset value.

[c] In respect of direct portfolio transaction costs. Please see the section above this table for an explanation of dilution adjustments.

Contact

Customer Relations*

0800 390 390

Write to us at:**

M&G Securities Limited
PO Box 9039
Chelmsford
CM99 2XG

Our website:

www.mandg.co.uk

Email us with queries:†

info@mandg.co.uk

* For security purposes and to improve the quality of our service, we may record and monitor telephone calls. You will require your M&G client reference. Failure to provide this will affect your ability to transact with us.

** 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.

† Please note that information contained within an email cannot be guaranteed as secure. We advise that you do not include any sensitive information when corresponding with M&G in this way.

58243_SR_310720