



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

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

Interim Short Report September 2018

For the six months ended 30 September 2018

# Fund information

The Authorised Corporate Director (ACD) of M&G Investment Funds (10) presents its Interim 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 Interim Long Report and unaudited 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/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 20 April 2018, the Euro Class 'Z-H' (Accumulation) share class was launched in the M&G Absolute Return Bond Fund.

On 28 September 2018, the Depositary changed from National Westminster Bank Plc to NatWest Trustee & Depositary Services Limited.

## 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.

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 changed during this period. From 3 April 2018 to 19 April 2018 the risk number was 4.

**As at 1 October 2018, for the six months ended 30 September 2018**

### Performance against objective

Between 3 April 2018 (the start of the review period) and 1 October 2018, the M&G Absolute Return Bond Fund delivered a flat total return (the combination of capital growth and income), which was below 3-month GBP LIBOR + 2.5%, across all share classes. 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 condition and over any three-year period.\* LIBOR is the rate at which banks borrow money from each other.

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 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 Interim Long Report and unaudited 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. Calculated on a price to price basis with income reinvested.

Long-term performance				
	Six months 03.04.18 % <sup>[a]</sup>	Three years 01.10.15 % p.a.	Five years 01.10.13 % p.a.	Since launch % p.a.
<b>Sterling <sup>[b]</sup></b>				
Class 'A'	-0.1	n/a	n/a	+1.5 <sup>[c]</sup>
Class 'I'	+0.0	n/a	n/a	+1.7 <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

During the six-month review period, the fund delivered a flat return in an environment of considerable volatility in global financial markets, triggered by fears of a US-China trade war and political events in Italy and Turkey. Markets were also influenced by investors' focus on the likelihood of central banks finally being able to move towards more 'normal' monetary policy and gradually withdrawing the support they had been providing to financial markets for over a decade.

In the US, the Federal Reserve has continued to raise interest rates, taking its total number of rate increases since the end of the financial crisis to seven. Meanwhile, the European Central Bank announced in June it would halve its monthly bond purchases in September and end them altogether in December.

This contributed to muted performance from government bonds over the six months under review, despite the extent of stockmarket volatility. Yields on US Treasuries and UK government bonds (gilts) rose over the period, while German bunds were more resilient, as Italy's threats to leave the eurozone and the potential consequences

for its banking sector resulted in a 'flight to safety' on the continent. (Bond yields refer to the interest received from a fixed income security, which is usually expressed annually as a percentage based on the investment's cost, its current market value or its face value. Bond yields typically move in the opposite direction to bond prices.)

Performance from corporate bonds was generally weak overall, although July saw improved performance. US corporate bonds outperformed those from other regions, due partly to the country's stronger economic outlook and company earnings.

We placed a strong emphasis on minimising monthly losses and portfolio volatility during bouts of market turbulence in line with the fund's defensive mandate. We successfully kept these risk measures within our intended thresholds throughout the review period.

## Investment activities

The portfolio remains cautiously positioned in terms of its sensitivity to interest rate changes. This reflects our belief that a highly active approach is needed to manage interest rate risk in the current environment, as aforementioned moves expected by central banks to return to more 'normal' monetary policy pose a medium-term threat to government bond prices.

We actively adjusted our positions in credit default swaps to navigate periods of volatility, as these positions are designed to protect the portfolio when corporate bond (credit) markets perform poorly.

In credit, we were active in the primary market, taking opportunities to realise some gains from positions that had performed well and switching these for attractively valued new issues. New positions included Bayer, BASF, Goldman Sachs, Nationwide Building Society and UBS.

The fund has modest exposure to traditional 'safe-haven' currencies via the US dollar, Swiss franc and Japanese yen. We slightly increased exposure to the Japanese yen during the review period.

## Outlook

While global economic data remains positive, inflation measures in the US and Europe ended the review period modestly below expectations. We must therefore wait and see for tightness in the US labour market and wage pressures to filter through.

We remain cautious on emerging markets given that upcoming elections in Brazil and ongoing situations in Argentina and Turkey provide the potential for further volatility in the months ahead.

### 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

The table below shows the percentage holding per sector.

	% of fund as at	
	30.09.18	31.03.18
<b>FIXED INCOME</b>		
<b>Debt securities</b>		
'AAA' credit rated bonds	13.64	11.45
'AA' credit rated bonds	5.77	8.80
'A' credit rated bonds	12.46	15.08
'BBB' credit rated bonds	35.34	34.55
'BB' credit rated bonds	13.40	12.08
'B' credit rated bonds	3.78	3.99
'CCC' credit rated bonds	0.42	0.46
Bonds with no credit rating	13.87	12.28
<b>Debt derivatives</b>		
Credit default swaps	(0.25)	(0.45)
Interest rate swaps	0.05	0.05
Interest rate futures	0.27	(0.23)
<b>CURRENCY</b>		
Forward currency contracts	(0.07)	0.69
<b>CASH EQUIVALENTS</b>		
'AAA' rated money market funds <sup>[a]</sup>	1.18	0.75

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

### Portfolio transactions

for the six months to 30 September	2018	2017
Portfolio transactions	£'000	£'000
Total purchases	12,572	17,527
Total sales	10,629	9,307

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

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 sterling 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 Interim Long Report and unaudited 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

as at	30.09.18	31.03.18	31.03.17
	£'000	£'000	£'000
Fund net asset value (NAV)	35,854	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.

	Six months to 30.09.18 UK p	Year to 31.03.18 UK p	Year to 31.03.17 UK p
<b>Change in NAV per share</b>			
Opening NAV	102.58	100.87	100.00
Return before operating charges and after direct portfolio transaction costs	0.46	2.57	1.18
Operating charges	(0.47)	(0.86)	(0.31)
Return after operating charges	(0.01)	1.71	0.87
Distributions	(1.01)	(1.40)	(0.28)
Retained distributions	1.01	1.40	0.28
Closing NAV	102.57	102.58	100.87

<b>Direct portfolio transaction costs</b>	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
<b>Total direct portfolio transaction costs</b>	<b>0.00</b>	<b>0.00</b>	<b>0.00</b>

<b>Performance and charges</b>	%	%	%
Direct portfolio transaction costs <sup>[b]</sup>	0.00	0.00	0.00
Operating charges	0.92	0.85	1.04*
Return after operating charges	-0.01	+1.70	+0.87
Distribution yield	2.15	1.59	1.40
Effect on yield of charges offset against capital	0.00	0.00	0.00

### Other information

Closing NAV (£'000)	323	258	20
Closing NAV percentage of total fund NAV (%)	0.90	0.77	0.12
Number of shares	314,956	251,544	20,000
Highest share price (UK p)	103.13	103.61	101.38
Lowest share price (UK p)	101.99	101.32	99.89

\* The operating charge shown is an estimate of the charges, as the share class had 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.

	Six months to 30.09.18 UK p	Year to 31.03.18 UK p	Year to 31.03.17 UK p
<b>Change in NAV per share</b>			
Opening NAV	102.86	100.93	100.00
Return before operating charges and after direct portfolio transaction costs	0.46	2.57	1.18
Operating charges	(0.37)	(0.64)	(0.25)
Return after operating charges	0.09	1.93	0.93
Distributions	(1.11)	(1.63)	(0.34)
Retained distributions	1.11	1.63	0.34
Closing NAV	102.95	102.86	100.93

<b>Direct portfolio transaction costs</b>	<b>UK p</b>	<b>UK p</b>	<b>UK p</b>
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

<b>Performance and charges</b>	<b>%</b>	<b>%</b>	<b>%</b>
Direct portfolio transaction costs <sup>[b]</sup>	0.00	0.00	0.00
Operating charges	0.72	0.63	0.85*
Return after operating charges	+0.09	+1.91	+0.93
Distribution yield	2.37	1.79	1.60
Effect on yield of charges offset against capital	0.00	0.00	0.00

#### Other information

Closing NAV (£'000)	27,268	26,443	16,669
Closing NAV percentage of total fund NAV (%)	76.06	78.78	97.33
Number of shares	26,486,710	25,708,589	16,516,155
Highest share price (UK p)	103.46	103.86	101.42
Lowest share price (UK p)	102.32	101.38	99.89

\* The operating charge shown is an estimate of the charges, as the share class had 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.

The operating charges paid by each share class of the fund are shown in the following performance tables. 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	30.09.18	31.03.18	31.03.17	Average <sup>[a]</sup>
Indirect portfolio transaction costs	%	%	%	%
Average portfolio dealing spread	0.44	0.50	0.46	0.47

<sup>[a]</sup> Average of first three columns.

# Contact



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