



M&G Episode Allocation Fund

a sub-fund of M&G Investment Funds (4)

Interim Short Report April 2019

For the six months ended 30 April 2019

The Authorised Corporate Director (ACD) of M&G Investment Funds (4) presents its Interim Short Report for M&G Episode Allocation 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 (4), 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

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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 8 April 2019, the Sterling Class 'PP' (Accumulation) shares were launched across all four sub-funds of M&G Investment Funds (4).

Investment objective

The fund aims to deliver a total return (the combination of capital growth and income) of at least 5% per annum above the 3-month GBP LIBOR rate, before any charges are taken, over any five-year period.

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

Investment policy

The fund is a multi-asset fund that invests across a range of asset classes, including equities, fixed income securities, convertibles, cash and near cash. Exposure to these assets may be gained either directly or indirectly via collective investment schemes or derivatives. The fund may also invest indirectly via collective investment schemes or derivatives in other asset classes such as property and gold.

The currency exposure of the fund will be actively managed, seeking to enhance returns, with a minimum of 30% of the fund exposed to sterling and a minimum of 60% in developed market currencies (including sterling).

Derivatives may be used for investment purposes, efficient portfolio management and hedging.

Investment approach

The fund managers have a flexible top-down approach to the allocation of capital between different types of assets in response to changes in economic conditions and asset values. This approach combines in-depth research to work out the value of assets over the medium to long term, with analysis of market reactions to events to identify investment opportunities. In particular, the managers seek to respond when asset prices move away from a reasonable sense of 'fair' long-term value due to market reactions to events.

The fund seeks to manage risk by investing globally across multiple asset classes, sectors, currencies and countries. The fund will typically invest 20-60% of its assets in equities and convertibles, 30-75% in fixed income securities or cash, and up to 20% in other assets. These allocations reflect the net exposure of the portfolio.

The fund will typically take investment positions at index or sector level, but it may also take positions in individual shares or bonds. The fund's investment strategy may involve the use of derivatives to take long or short positions.

Risk profile

The fund invests globally in a broad range of assets, including company shares (equities), fixed income securities (bonds), currencies and other assets such as property shares and convertible bonds. The fund is, therefore, subject to the price volatility of global financial and currency markets. Exposure to the different asset classes 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.

The fund adopts a flexible approach to the allocation of capital between asset classes in response to changes in economic conditions and the valuation of assets, and the managers will seek to maximise portfolio diversity wherever possible. However, in cases where the managers believe that the opportunities are limited to a few areas, there may be a higher-than-usual concentration of asset or market exposure. Such strategies may result in higher volatility of the fund's short-term performance.

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 not changed during this period.

As at 1 May 2019, for the six months ended 30 April 2019

Performance against objective

Between 1 November 2018 (the start of the review period) and 1 May 2019, the M&G Episode Allocation Fund produced a positive total return (the combination of income and growth of capital) which was above 3-month LIBOR + 5.0% across all of its share classes. The fund's returns were also ahead of the average return of its peer group, the IA Mixed Investment 20-60% Sector.

The fund's objective is to achieve a total return of at least 5% per annum above the 3-month GBP LIBOR rate, before any charges are taken, over any five-year period. LIBOR is the rate at which banks borrow money from each other. Over five years, the fund has met its objective; the annualised five-year return before any charges was 7.1% versus three-month LIBOR + 5.0% of 5.6%.*

* 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 (4).

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 01.11.18 % ^[a]	Three years 03.05.16 % p.a.	Five years 01.05.14 % p.a.	Since launch % p.a.
Sterling^[b]				
Class 'A'	+5.5	+7.5	+5.4	+5.3 ^[c]
Class 'I'	+5.8	+8.2	+6.0	+6.8 ^[d]

^[a] Absolute basis.

^[b] Price to price with income reinvested.

^[c] 16 February 2007, the launch date of the fund.

^[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

It was a case of contrasting fortunes for financial markets during the period under review. The last two months of 2018 – November and December – were particularly challenging. Risk assets such as global equities (company shares) fell out of favour with investors because of fears of an economic slowdown and tensions surrounding trade tariffs between the US and China. Concerns that US interest rates would continue to rise added to the volatility and put pressure on the price of many assets. In fact, December was notably gloomy for virtually all asset classes, with even US equities – generally robust until now – sold off by investors.

The new year triggered stronger demand for risk assets, however. This led to higher prices in areas such as European and Asian equities and the fund's basket of diversified global equities did well as a result. The main reason for this turnaround in investor sentiment was the easing of expectations that US interest rates would rise in the coming months. The US Federal Reserve cautioned against being too hasty with rate hikes in its January meeting, which set the tone for many other central banks to voice similar 'dovish' statements in the months that followed.

Of the few laggards that detracted from fund performance during the period under review, a small loss was incurred in our allocation to Turkish equities. This market suffered from bouts of risk aversion during the six months, as uncertainty over fiscal and monetary policies unsettled investors. Exposure to Japanese equities also dragged on returns, mostly in December, as doubts about a lack of economic growth and below-par company earnings dampened investor sentiment.

Contributions from the fund's bond positions were positive, particularly among emerging market issuers. (Bonds are loans that are extended by an investor to an issuer – such as a company or government – usually 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'.) Mexican and South African government bonds added to fund performance during the period because emerging market debt typically performs well in an environment of low US interest rates.

Holdings in corporate bonds issued by UK mining companies provided a small source of positive returns, while the fund's exposure to convertible bonds detracted slightly. A holding in the M&G Property Portfolio, a UK commercial property fund, weighed on returns as investors generally saw the lack of progress in Brexit negotiations as a negative for 'bricks and mortar' in 2019.

Investment activities

December 2018 was the only time within the six-month period under review when we made any tactical changes. We switched the fund's holding in short-dated Mexican government bonds into the same bonds but with 30-year tenures. This is because bonds with longer tenures typically pay a higher interest rate, or yield, to the investor. However, by holding longer dated bonds, there is a greater risk that higher inflation could reduce the value of payments, and also the greater risk that higher overall interest rates could cause the bond's price to fall. In this context, we think the risks in Mexico of both higher inflation and higher interest rates are fairly low.

The fund's pro-equity positioning was unchanged over the six months (and remains close to the 60% maximum equity allocation). However, 'no change' is an active decision, given the temptation to make small portfolio adjustments often on the back of lots of 'noise' and short-term volatility in the market. We are more inclined to make more significant shifts in asset allocation should valuations change more materially, as we did in October 2018 when the price of equities fell sharply.

Outlook

We continue to have a broad pro-equity bias in our portfolio, preferring Asian and European equities. Outside equities, we still favour long positions in emerging market government bonds, select corporate bonds, and peripheral government bond issuers such as Italy.

Investors are generally pessimistic about global growth, which means equity markets still have further scope to rise, should we see even a modest lift in sentiment. For instance, Asian economies with strong links to China have yet to show a material turnaround in their fortunes, despite China's recent stimulus measures. By contrast, bank lending in China showed an unexpected rise in transactions in March, which we believe bodes well for efforts to shore up its sluggish economy.

For now, however, major central banks have certainly turned accommodative in their monetary policies, in light of slower economic growth and softer inflation so far in 2019. First, the US Federal Reserve indicated that it would be patient with future interest rate hikes. This was followed by other central banks such as the European Central Bank and recently the Bank of Japan and Bank of Canada stating that low interest rates were going to carry on for longer. We believe this is good news for all asset classes.

Tony Finding & Juan Nevado

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.

	% of fund as at	
	30.04.19	31.10.18
EQUITIES		
United Kingdom		
UK equities	0.76	0.61
Europe		
European equities	2.41	2.18
North America		
North American equities	4.74	4.64
Other		
Other equity futures	0.89	(0.98)
EQUITY PORTFOLIOS		
United Kingdom	5.40	4.57
Europe	0.41	0.32
Asia Pacific (ex Japan)	1.35	1.04
Other	5.93	6.11
FIXED INCOME		
United Kingdom		
UK Government bonds	12.02	11.33
UK investment grade corporate bonds	0.86	0.73
Europe		
European Government bonds	5.62	4.76
North America		
North America Government bonds	32.14	37.96
North America investment grade corporate bonds	0.85	0.74
North America below investment grade corporate bonds	0.82	0.71
Global		
Global fixed income funds	4.66	4.68
Other		
Other Government bonds	6.16	5.56
Other investment grade corporate bonds	1.34	1.17
PROPERTY		
United Kingdom	7.23	6.65
CURRENCY		
Forward currency contracts	(0.28)	0.51
CASH EQUIVALENTS		
'AAA' rated money market funds ^[a]	4.29	1.40

^[a] 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 April	2019	2018
Portfolio transactions	£'000	£'000
Total purchases	397,989	665,070
Total sales	471,694	400,333

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

Financial highlights

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 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.

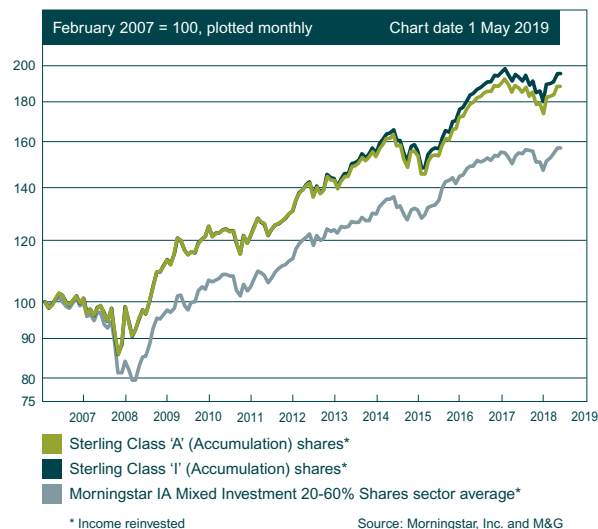
The fund is available for investment in different share classes, each with varying levels of charges and minimum investments; please refer to the Prospectus for M&G Investment Funds (4), which is available free of charge either from our website at www.mandg.co.uk/prospectuses or by calling M&G Customer Relations. For the specific performance tables of all share classes, please refer to the Interim Long Report and unaudited Financial Statements for M&G Investment Funds (4), 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			
	30.04.19	31.10.18	31.10.17
as at	£'000	£'000	£'000
Fund net asset value (NAV)	544,816	609,767	550,233

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.

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 period are calculated as at 10 May 2019.

Sterling Class 'A' Accumulation share performance

The share class was launched on 16 February 2007.

	Six months to 30.04.19 UK p	Year to 31.10.18 UK p	Year to 31.10.17 UK p
Change in NAV per share			
Opening NAV	177.65	188.23	166.10
Return before operating charges and after direct portfolio transaction costs	11.06	(7.56)	25.10
Operating charges	(1.49)	(3.02)	(2.97)
Return after operating charges	9.57	(10.58)	22.13
Distributions	(1.22)	(1.52)	(1.12)
Retained distributions	1.22	1.52	1.12
Closing NAV	187.22	177.65	188.23
Direct portfolio transaction costs	UK p	UK p	UK p
Costs before dilution adjustments	0.01	0.04	0.01
Dilution adjustments ^[a]	(0.01)	0.00	(0.01)
Total direct portfolio transaction costs	0.00	0.04	0.00
Performance and charges	%	%	%
Direct portfolio transaction costs ^[b]	0.03	0.02	0.01
Operating charges	1.59	1.61	1.64
Return after operating charges	+5.39	-5.62	+13.32
Historic yield	1.21	0.85	0.60
Effect on yield of charges offset against capital	0.00	0.00	0.00

Other information

Closing NAV (£'000)	165,734	152,423	129,924
Closing NAV percentage of total fund NAV (%)	30.42	25.00	23.61
Number of shares	88,521,794	85,800,043	69,023,967
Highest share price (UK p)	188.61	193.87	188.99
Lowest share price (UK p)	171.45	176.14	161.91

Sterling Class 'I' Accumulation share performance

The share class was launched on 3 August 2012.

	Six months to 30.04.19 UK p	Year to 31.10.18 UK p	Year to 31.10.17 UK p
Change in NAV per share			
Opening NAV	1,462.83	1,540.63	1,351.36
Return before operating charges and after direct portfolio transaction costs	90.18	(64.55)	202.56
Operating charges	(6.76)	(13.25)	(13.29)
Return after operating charges	83.42	(77.80)	189.27
Distributions	(14.48)	(21.64)	(17.99)
Retained distributions	14.48	21.64	17.99
Closing NAV	1,546.25	1,462.83	1,540.63
Direct portfolio transaction costs	UK p	UK p	UK p
Costs before dilution adjustments	0.11	0.35	0.07
Dilution adjustments ^[a]	(0.07)	(0.03)	(0.05)
Total direct portfolio transaction costs	0.04	0.32	0.02
Performance and charges	%	%	%
Direct portfolio transaction costs ^[b]	0.03	0.02	0.01
Operating charges	0.84	0.86	0.89
Return after operating charges	+5.70	-5.05	+14.01
Historic yield	1.81	1.47	1.17
Effect on yield of charges offset against capital	0.00	0.00	0.00
Other information			
Closing NAV (£'000)	297,776	340,028	287,826
Closing NAV percentage of total fund NAV (%)	54.66	55.76	52.31
Number of shares	19,257,904	23,244,607	18,682,329
Highest share price (UK p)	1,557.72	1,589.05	1,546.81
Lowest share price (UK p)	1,413.02	1,450.31	1,317.31

^[a] In respect of direct portfolio transaction costs.

^[b] 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.

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				
	Six months to 30.04.19	Year to 31.10.18	Year to 31.10.17	Average ^[a]
Direct portfolio transaction costs ^[b]	%	%	%	%
Broker commission	0.01	0.01	0.01	0.01
Taxes	0.01	0.01	0.00	0.00
Costs before dilution adjustments	0.02	0.02	0.01	0.01
Dilution adjustments ^[c]	0.01	0.00	0.00	0.00
Total direct portfolio transaction costs	0.03	0.02	0.01	0.01
as at	30.04.19	31.10.18	31.10.17	Average ^[a]
Indirect portfolio transaction costs	%	%	%	%
Average portfolio dealing spread	0.58	0.50	0.43	0.50

^[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.

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