



M&G Episode Growth Fund

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

Interim Short Report April 2019

For the six months ended 30 April 2019

Fund information

The Authorised Corporate Director (ACD) of M&G Investment Funds (4) presents its Interim Short Report for M&G Episode Growth 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 higher total return (the combination of capital growth and income), net of the ongoing charge figure, than that of a composite index comprising two thirds global equities and one third global bonds*, over any five-year period.

* As measured by the MSCI ACWI and Bloomberg Barclays Global Aggregate Index respectively.

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 25% of the fund exposed to sterling and a minimum of 50% 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 40-85% of its assets in equities and convertibles, 15-50% in fixed income securities and cash, and up to 10% 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.¹

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 Growth Fund delivered a positive total return (the combination of income and growth of capital) across all of its share classes*. Over this period, the fund was ahead of its comparative index, which returned 6.0%. The comparative index, made up of two thirds global company shares (as measured by the MSCI ACWI Index) and one third global bonds (as measured by the Bloomberg Barclays Global Aggregate Index), was introduced at the end of August 2018 when the fund's objective and policy were changed.

The fund's returns were also ahead of the average return of its peer group, the IA Mixed Investment 40-85% Sector.

* 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'	+6.5	+8.9	+5.5	+7.9 ^[c]	
Class 'I'	+6.9	+9.7	+6.3	+7.9 ^[d]	

^[a] Absolute basis.

^[b] Price to price with income reinvested.

^[c] 1 October 2002, the launch date of the share class.

^[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 like 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 which detracted from fund performance during the period under review, a small loss was incurred through our allocation to Canadian equities – principally from our holding in methanol producer Methanex. 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 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 Indonesian government bonds added to fund performance during the period because emerging market debt can typically perform well in an environment of low US interest rates.

Pleasingly, exposure to Italian government bonds (we added these to the fund in May 2018) was an important source of positive return in the period. These bonds have continued to outperform in the face of some challenging conditions for the Italian economy and also the political environment generally.

Investment activities

We were fairly active in making changes to the portfolio in the review period, mainly taking profits on some of our equity holdings following a strong rally in prices. For example, we reduced the exposure to selected banks in January, and a month later, sold the shares we held in a mining company. In April, and in response to gains in UK and Russian stockmarkets, we reduced our positions in these risk assets. The fund remains skewed towards equities, however, with about 74% of assets invested across a range of stockmarkets.

Within bonds, we added a small 'short' position on German bunds, with the view that yields on German government debt were far too low – and therefore prices too high. (Yields refer to the interest received from a fixed income security and are usually expressed annually as a percentage based on the investment's cost, its current market value or its face value. Bond prices move inversely to their yields.) We saw the movement in yields as the outcome of investors' behaviour being broadly inconsistent with the fundamentals of the German economy and Europe overall (that is, still growing). By taking a short position, we are expecting that the price of these bonds will fall in the future.

Outlook

Despite market volatility and heightened pessimism – which has abated in recent months as investors' mood has lightened – we continue to believe that large parts of the global equity universe, particularly Asian and European stockmarkets, are still attractively valued compared to most developed market government bonds. The fact that we concluded the first quarter of 2019 by initiating a short position on German bunds demonstrates the view that negative/low-yielding Western bonds offer little prospect of positive real returns (returns above the inflation rate) in the current environment.

Meanwhile, major central banks have certainly turned accommodative in their monetary policies. 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.

Jenny Rodgers & Eric Lonergan

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	
	30.04.19	31.10.18 ^[a]
EQUITIES		
Equity portfolios		
United Kingdom ^[b] ^[c]	8.87	16.10
France	0.00	3.00
United States	1.16	1.14
Luxembourg	0.00	1.62
Japan ^[b] ^[c]	3.92	4.46
Asia pacific ^[b] ^[c]	4.14	3.85
South Korea	4.48	4.52
Turkey	1.79	2.56
China	0.00	7.32
Other	9.39	9.49
Equities		
United Kingdom	1.57	1.63
Ireland	0.88	1.04
Italy	4.46	4.18
Spain	0.88	1.09
United States	11.66	11.53
Japan	2.56	3.08
Australia	0.00	0.79
Russia	2.55	3.33
Equity derivatives		
Equity index futures	0.46	(0.29)
FIXED INCOME		
Bond portfolios		
Other ^[c]	1.15	1.13
Government bonds		
United Kingdom	23.94	0.00
Italy	5.13	5.00
Mexico	4.23	4.13
Indonesia	2.16	2.03
Turkey	1.59	1.74
Debt derivatives		
Interest rate futures	0.06	0.00
CURRENCY	0.20	(0.47)
Forward currency contracts	0.20	(0.47)
CASH EQUIVALENTS	0.00	3.77
'AAA' rated money market funds ^[d]	0.00	3.77

^[a] The portfolio has been reclassified to more appropriately reflect how the fund is managed. 31.10.18 comparatives have been restated to reflect this.

^[b] All holdings in M&G collective investment schemes are in Sterling Class 'A' (Income) shares unless otherwise stated.

^[c] Related parties.

^[d] 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	417,005	142,948
Total sales	398,351	131,217

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			
as at	30.04.19 £'000	31.10.18 £'000	31.10.17 £'000
Fund net asset value (NAV)	890,399	854,877	969,437

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 'X' (Income) 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 1 October 2002.

	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	78.63	84.86	71.79
Return before operating charges and after direct portfolio transaction costs	6.32	(4.71)	14.49
Operating charges	(0.72)	(1.52)	(1.42)
Return after operating charges	5.60	(6.23)	13.07
Distributions	(0.39)	(0.87)	(0.67)
Retained distributions	0.39	0.87	0.67
Closing NAV	84.23	78.63	84.86

Direct portfolio transaction costs	UK p	UK p	UK p
Costs before dilution adjustments	0.01	0.02	0.05
Dilution adjustments ^[a]	0.00	0.00	0.00
Total direct portfolio transaction costs	0.01	0.02	0.05

Performance and charges	%	%	%
Direct portfolio transaction costs ^[b]	0.02	0.03	0.06
Operating charges	1.73	1.81	1.79
Return after operating charges	+7.12	-7.34	+18.21
Historic yield	1.33	1.10	0.79
Effect on yield of charges offset against capital	0.01	0.01	0.01

Other information

Closing NAV (£'000)	54,565	42,404	44,001
Closing NAV percentage of total fund NAV (%)	6.13	4.96	4.54
Number of shares	64,780,672	53,929,963	51,849,542
Highest share price (UK p)	84.84	88.57	84.86
Lowest share price (UK p)	73.69	77.23	69.95

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	1,552.94	1,663.67	1,397.43
Return before operating charges and after direct portfolio transaction costs	123.92	(95.04)	280.93
Operating charges	(7.49)	(15.69)	(14.69)
Return after operating charges	116.43	(110.73)	266.24
Distributions	(13.61)	(30.44)	(25.08)
Retained distributions	13.61	30.44	25.08
Closing NAV	1,669.37	1,552.94	1,663.67

Direct portfolio transaction costs	UK p	UK p	UK p
Costs before dilution adjustments	0.19	0.48	0.92
Dilution adjustments ^[a]	0.00	(0.08)	(0.05)
Total direct portfolio transaction costs	0.19	0.40	0.87

Performance and charges	%	%	%
Direct portfolio transaction costs ^[b]	0.02	0.03	0.06
Operating charges	0.88	0.96	0.94
Return after operating charges	+7.50	-6.66	+19.05
Historic yield	2.13	1.94	1.56
Effect on yield of charges offset against capital	0.01	0.01	0.01

Other information

Closing NAV (£'000)	52,221	55,169	46,664
Closing NAV percentage of total fund NAV (%)	5.86	6.45	4.81
Number of shares	3,128,184	3,552,534	2,804,861
Highest share price (UK p)	1,681.14	1,739.91	1,664.34
Lowest share price (UK p)	1,456.95	1,525.23	1,361.88

^[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	0.02	0.02	0.05	0.03
Taxes	0.00	0.01	0.01	0.01
Costs before dilution adjustments	0.02	0.03	0.06	0.04
Dilution adjustments ^[c]	0.00	0.00	0.00	0.00
Total direct portfolio transaction costs	0.02	0.03	0.06	0.04
as at	30.04.19	31.10.18	31.10.17	Average ^[a]
Indirect portfolio transaction costs	%	%	%	%
Average portfolio dealing spread	0.08	0.12	0.11	0.10

^[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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