

Highlights

- Government bond yields slightly repriced in December, while investment grade credit spreads continued their seemingly inexorable move tighter. Against this backdrop, the fund rose.
- Fund Manager Stefan Isaacs slightly reduced duration in December, ending the year at 4.3 years.

Risks associated with this fund

For any past performance shown, please note that past performance is not a guide to current or future performance and the performance data does not take into account any entry and exit charges incurred on the purchase and sale of shares but does take into account the ongoing charge.

The value of investments and the income from them will rise and fall. This will cause the fund price, as well as any income paid by the fund, to fall as well as rise. There is no guarantee the fund will achieve its objective, and you may not get back the amount you originally invested.

The fund may use derivatives with the aim of profiting from a rise or a fall in the value of an asset (for example, a company's bonds). However, if the asset's value varies in a different manner, the fund may incur a loss.

Changes in currency exchange rates will affect the value of your investment.

The value of the fund may fall if the issuer of a fixed income security held is unable to pay income payments or repay its debt (known as a default).

Further risk factors that apply to the fund can be found in the fund's Key Investor Information Document (KIID).

Single year performance (5 years ending December)

From To	01.01.17 31.12.17	01.01.16 31.12.16	01.01.15 31.12.15	01.01.14 31.12.14	01.01.13 31.12.13
Euro A Acc	3,2%	4,4%	-1,4%	7,2%	3,8%

Performance over 5 years



Fund performance

	1 month (%)	3 months (%)	YTD (%)	1 year (%)	3 years (%) p.a.	5 years (%) p.a.	Since tenure (%) p.a.	Since inception (%) p.a.
Fund	-0,2	+0,7	+3,2	+3,2	+2,0	+3,4	+4,5	+4,1
Index	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Sector	-0,3	+0,6	+2,5	+2,5	+2,0	+3,3	+3,9	+3,9
Ranking	27/105	32/105	24/103	24/103	40/99	30/86	10/50	13/33
Quartile ranking	1	2	1	1	2	2	1	2

Past performance is not a guide to future performance.

Things you should know

The fund allows for the extensive use of derivatives.

Key information

Fund manager	Stefan Isaacs
Fund manager tenure from	30 March 2007
Deputy fund manager	Wolfgang Bauer
Launch date	13 January 2003
Launch of share class	13 January 2003
Fund size (millions)	€1.983,45
Fund type	OEIC, incorporated in the UK
Comparative sector	Morningstar EUR Corporate Bond sector
Number of issuers	204
Distribution yield (Acc)	0,99%
Distribution yield (Inc)	2,14%
Underlying yield (Acc)	0,99%
Underlying yield (Inc)	0,99%
Yield to expected maturity*	0,95%
Modified duration (years)	4,3
Spread duration (years)	5,47
Average maturity (years)	6,17
Average coupon	2,49
Volatility†	3,47%
Average credit rating	A-
Share type	Acc & Inc
Ongoing charge	1,16%

*Source: Morningstar, three-year annualised volatility, as at 31 December 2017

The distribution yield reflects the amounts that may be expected to be distributed over the next 12 months as a percentage of the share price, as at the date shown. It is based on a snapshot of the portfolio on that day. It does not include any preliminary charge and investors may be subject to tax on distributions. It is the fund's policy to offset certain charges against income for accumulation share classes and to offset certain charges against capital for income share classes. These charges include the annual management charge, administration fee and share class hedging fee (where applicable). As a result, yield figures for income and accumulation share classes may differ significantly. The underlying yield reflects the annualised income net of expenses of the fund (calculated in accordance with relevant accounting standards) as a percentage of the mid-market price of the fund as at the date shown. It is based on a snapshot of the portfolio on that day. It does not include any preliminary charge and investors may be subject to tax on distributions. For the fund's income share classes, the distribution yield is higher than the underlying yield only because a portion of the fund's expenses are charged to capital. This has the effect of increasing distribution(s) for the year and constraining the fund's capital performance to an equivalent extent.

* The yield to expected maturity is calculated gross of fund expenses and includes effects from derivative instruments and currency forwards. It is calculated at fund level in the valuation currency of the fund. A fund may hold callable bonds whose yields are calculated on the basis of expected maturity.

Fund ratings

Overall Morningstar rating ★★★★
Morningstar Analyst rating Bronze

Source of Morningstar ratings: Morningstar, as at 30 November 2017

Ratings should not be taken as a recommendation.

Asset breakdown (%)

	Physical	CDS short	CDS long	Net
Government bonds	10,6	0,0	0,0	5,6
Investment grade corporate bonds	72,0	-6,4	10,9	76,5
Fixed rate	68,7	0,0	2,4	71,2
Floating rate	3,2	0,0	0,0	3,2
Index linked	0,0	0,0	0,0	0,0
Credit default swap indices	0,0	-6,4	8,4	2,1
High yield corporate bonds	7,8	0,0	0,0	7,8
Fixed rate	7,6	0,0	0,0	7,6
Floating rate	0,3	0,0	0,0	0,3
Index linked	0,0	0,0	0,0	0,0
Credit default swap indices	0,0	0,0	0,0	0,0
Securitised	6,2	0,0	0,5	6,7
Cash	3,4	0,0	0,0	3,4

CDS short: bought protection (short credit exposure); CDS long: sold protection (long credit exposure)

The columns may not always add up when reading across as physical bond holdings and/or cash are sometimes used as collateral for CDS exposure.

Credit rating breakdown (%)

	Physical	CDS short	CDS long	Net
AAA	14,5	0,0	0,0	9,5
AA	7,6	0,0	0,0	7,6
A	25,1	0,0	4,7	29,8
BBB	41,5	-6,4	6,7	41,9
BB	6,8	0,0	0,0	6,8
B	1,0	0,0	0,0	1,0
CCC	0,0	0,0	0,0	0,0
CC	0,0	0,0	0,0	0,0
C	0,0	0,0	0,0	0,0
D	0,0	0,0	0,0	0,0
No rating	0,0	0,0	0,0	0,0
Cash	3,4	0,0	0,0	3,4

CDS short: bought protection (short credit exposure); CDS long: sold protection (long credit exposure)

The columns may not always add up when reading across as physical bond holdings and/or cash are sometimes used as collateral for CDS exposure.

Where a security has not been rated by Standard & Poor's, Fitch or Moody's, we may use M&G's internal credit rating. Based on a comparison of all available ratings for each security, the most conservative rating (S&P, Fitch, Moody's or M&G's internal rating) is taken into consideration. The ratings so identified are then expressed or converted into M&G's ratings format to obtain uniform information for all securities in the portfolio.

Industry breakdown (%)

	Physical	CDS short	CDS long	Net
Banking	24,5	0,0	0,0	24,5
Telecommunications	7,9	0,0	0,3	8,2
Healthcare	5,8	0,0	0,0	5,8
Utility	5,7	0,0	0,0	5,7
Energy	4,9	0,0	0,8	5,6
Insurance	5,6	0,0	0,0	5,6
Sovereign	10,6	0,0	0,0	5,6
Real Estate	4,0	0,0	0,0	4,0
Consumer Non-Cyclical	3,7	0,0	0,0	3,7
Asset Backed	3,1	0,0	0,5	3,6
Capital Goods	3,4	0,0	0,0	3,4
Financial Services	3,1	0,0	0,0	3,1
Mortgage Backed	3,0	0,0	0,0	3,0
Technology & Electronics	2,8	0,0	0,0	2,8
Basic Industry	1,2	0,0	0,9	2,0
Services	2,0	0,0	0,0	2,0
Automotive	0,9	0,0	0,5	1,4
Finance & Investment	1,4	0,0	0,0	1,4
Consumer Cyclical	1,3	0,0	0,0	1,3
Media	0,9	0,0	0,0	0,9
Quasi & Foreign Government	0,8	0,0	0,0	0,8
Investment grade indices	0,0	-6,4	8,4	2,1
High Yield indices	0,0	0,0	0,0	0,0
Cash	3,4	0,0	0,0	3,4

CDS short: bought protection (short credit exposure); CDS long: sold protection (long credit exposure)

The columns may not always add up when reading across as physical bond holdings and/or cash are sometimes used as collateral for CDS exposure.

Country breakdown (%)

	Physical	CDS short	CDS long	Net
US	27,9	0,0	0,3	28,1
France	14,3	0,0	0,0	14,3
UK	9,4	-6,4	9,0	12,0
Germany	12,9	0,0	0,5	8,4
Spain	6,1	0,0	0,8	6,9
Switzerland	5,4	0,0	0,9	6,3
Italy	5,0	0,0	0,0	5,0
Netherlands	4,2	0,0	0,0	4,2
Ireland	2,8	0,0	0,0	2,8
Belgium	1,7	0,0	0,0	1,7
Other	6,9	0,0	0,0	6,9
Cash	3,4	0,0	0,0	3,4

CDS short: bought protection (short credit exposure); CDS long: sold protection (long credit exposure)

The columns may not always add up when reading across as physical bond holdings and/or cash are sometimes used as collateral for CDS exposure.

Currency breakdown (%)

	Pre-hedge	Post-hedge
Euro	92,4	98,7
British pound	3,9	0,9
US dollar	3,7	0,3
Swiss franc	0,0	0,0

Maturity breakdown (%)

	Physical
0 - 1 years	2,1
1 - 3 years	12,8
3 - 5 years	21,5
5 - 7 years	20,4
7 - 10 years	25,0
10 - 15 years	8,1
15+ years	6,7
Cash	3,4

Duration breakdown by currency and asset class

	Physical	Futures	Swaps	Net
Euro	4,8	-0,5	0,0	4,3
US dollar	0,2	-0,2	0,0	0,0
British pound	0,1	-0,1	0,0	0,0
Total	5,2	-0,9	0,0	4,3

Largest issuers (excluding government bonds and CDS indices, %)

	Fund
Johnson & Johnson	2,4
Intesa Sanpaolo	1,9
Goldman Sachs	1,9
AT&T	1,6
UBS	1,6
Bank of America	1,6
Morgan Stanley	1,6
Verizon Communications	1,5
JP Morgan	1,5
Wells Fargo	1,4

Commentary

Sentiment in financial markets remained generally well supported by an encouraging global economic outlook as 2017 drew to a close. However, the US Federal Reserve confirmed another 0.25% rise in interest rates in December and returns were mixed in global bond markets during the month.

Also in the US, President Trump achieved possibly the most notable success so far of his presidency, by signing the Tax Cuts & Jobs Act of 2017 in late December. While the minutiae of its implications will take time to be fully understood, the legislation is expected to benefit US businesses through a significantly lower tax burden on their domestic earnings and an even larger reduction in tax levied on offshore earnings that are subsequently repatriated.

Markets were largely unmoved by the success of pro-independence parties in Catalan elections in securing a renewed parliamentary majority. Although the pro-union centre-right Citizens party won the biggest share of the vote, the result was nonetheless a blow to Spanish Prime Minister Mariano Rajoy.

While the performance of risk assets generally benefited from the prospect of synchronised global economic growth as 2017 progressed, the caution of tighter monetary policy and the possibility of firmer inflation also remained key themes as the year ended.

The fund's short duration position cushioned it from the worst of an upward move in European government yields in December.

Key changes

Duration ended the year at 4.3 years, slightly shorter than one month earlier, and around 0.9 years short of a comparable index.

Stefan continues to keep a close eye on the fund's exposure to financials, following strong performance from the sector in 2017. However, he still finds financials more attractive than non-financial credit that isn't eligible for purchase under the ECB's corporate bond buying programme. Furthermore, he thinks both of these categories are more attractive than credit that has been affected by the ECB scheme.

If credit spreads continue to tighten further, Stefan will move the fund gradually closer to a neutral spread duration position. Spread duration ended the year at 5.5 years (versus neutral of 5.2 years).

The fund's risk-free allocation increased modestly in December. Stefan will reinvest the capital into the corporate bond market as opportunities arise.

Fund codes and charges

Share class	ISIN	Bloomberg	Annual management charge	Ongoing charge	Minimum initial investment	Minimum top up investment
Euro A Inc	GB00B959HG95	MGECEBAE LN	1,00%	1,16%	€1.000	€75
Euro A Acc	GB0032178856	MGECEBEA LN	1,00%	1,16%	€1.000	€75
Euro C Acc	GB0032179045	MGECEBEC LN	0,50%	0,66%	€500.000	€50.000
Euro C Inc	GB00BK6MBH38	MGECECEI LN	0,50%	0,66%	€ 500.000	€50.000

The ongoing charge figures disclosed above include direct costs to the fund, such as the annual management charge (AMC), administration charge and custodian charge, but does not include portfolio transaction costs. They are based on expenses for the period ending 30 June 2017.

Please note that not all of the share classes listed above might be available in your country.

Important information

Cash may be held on deposit and/or in the Northern Trust Cash Funds, a range of collective investment schemes.

Source of performance data: Morningstar, Inc., as at 31 December 2017, Euro Class A shares, gross income reinvested, price to price basis. Past performance is not a guide to future performance. All other statistics from M&G internal sources, as at 31 December 2017 unless indicated otherwise. The Morningstar Overall Rating based on the fund's Euro Class A shares. Copyright © 2018 Morningstar UK Limited. All Rights Reserved. Ratings should not be taken as recommendation.

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