M&G Episode Macro Fund
Sterling Class T-H – Accumulation shares

Monthly Fund Review as at 30 September 2019

For investment professionals only

M&G INVESTMENTS

Highlights

- Major markets generally reversed the rapid moves seen in August.
- Equity markets rallied and developed market government bonds weakened.
- In response to these moves, we reduced long exposure to equities and US corporate credit.

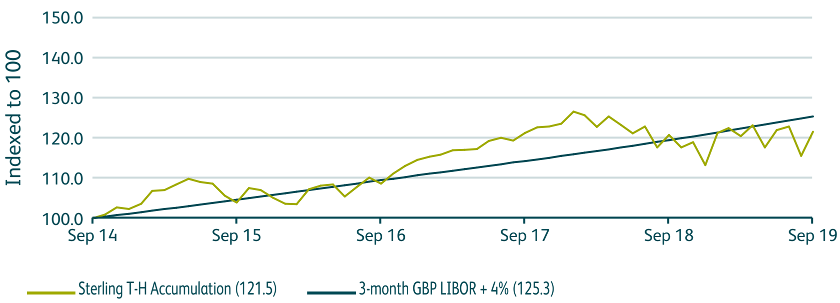
The main risks associated with this fund

For any past performance shown, please note that past performance is not a guide to future performance.
The value and income from the fund's assets will go down as well as up. This will cause the value of your investment to fall as well as rise. There is no guarantee that the fund will achieve its objective and you may get back less than you originally invested.
The fund may use derivatives to profit from an expected rise or fall in the value of an asset. Should the asset's value vary in an unexpected way, the fund will incur a loss. The fund's use of derivatives may be extensive and exceed the value of its assets (leverage). This has the effect of magnifying the size of losses and gains, resulting in greater fluctuations in the value of the fund.
The fund may be highly concentrated at times in a limited number of investments or areas of the market, which could result in large price rises and falls.
The fund can be exposed to different currencies. Movements in currency exchange rates may adversely affect the value of your investment.
The hedging process seeks to minimise, but cannot eliminate, the effect of movements in exchange rates on the performance of the hedged share class. Hedging also limits the ability to gain from favourable movements in exchange rates.
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)

	2018	2017	2016	2015	2014
Sterling T-H Accumulation	-8.3%	7.8%	8.9%	2.7%	8.6%
3-month GBP LIBOR + 4%	4.7%	4.3%	4.6%	4.6%	4.6%

Performance over 5 years



Fund performance

	1 month (%)	3 months (%)	YTD (%)	1 year (%)	3 years (%) p.a.	5 years (%) p.a.
Sterling T-H Accumulation	5.2%	-0.3%	7.4%	0.7%	3.8%	4.0%
3-month GBP LIBOR + 4%	0.4%	1.2%	3.7%	4.9%	4.6%	4.6%

Past performance is not a guide to future performance.

Performance comparison: The fund is actively managed. The benchmark is a target which the fund seeks to achieve. The rate has been chosen as it is an achievable performance target given the fund's investment policy. The target benchmark is used solely to measure the fund's performance and does not constrain the fund's portfolio construction.

Source: Morningstar, Inc and M&G, as at 30 September 2019. Returns are calculated on a price to price basis with income reinvested.
Benchmark returns stated in GBP terms.

Key information

Fund manager	David Fishwick, Eric Lonergan
Fund manager tenure from	04 June 2010
ISIN	GB00B5LCW587
Launch date of fund	03 June 2010
Launch of share class	03 June 2010
Fund size (millions)	£ 109.79
Benchmark	3-month GBP LIBOR + 4-8%
Benchmark type	Target
Number of companies	21
Historic yield	0.24%
Average credit rating	A+
Modified duration (years)	-4.60
VaR	6.75
Average coupon	1.28
Payment dates	Feb
Ex-dividend dates	Jan

Charges

Entry charge	0.00%
Ongoing charge	0.93%
Performance fee	20.00%

Things you should know

The fund may invest more than 35% in securities issued by any one or more of the governments listed in the fund prospectus. Such exposure may be combined with the use of derivatives in pursuit of the fund objective. It is currently envisaged that the fund's exposure to such securities may exceed 35% in the governments of Australia, Austria, Belgium, Canada, Denmark, Finland, France, Germany, Italy, Japan, Netherlands, New Zealand, Singapore, Sweden, Switzerland, UK, USA although these may vary subject only to those listed in the prospectus.
The fund may be very concentrated at times which could result in greater fluctuations in the fund's short-term performance.
The fund allows for the extensive use of derivatives.

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Leverage and volatility

	Fund
Volatility	8.2%
Net leverage	0.1x
Gross leverage	1.3x

Credit rating breakdown (%)

	Net exposure
AAA	0.0
AA	-32.4
A	-29.7
BBB	0.0
BB	6.7
B	6.4
CCC	0.0
CC	0.0
C	0.0
D	0.0
No rating	0.0

Asset breakdown (%)

	Long exposure	Short exposure	Net exposure
Equity	**46.4**	**0.0**	**46.4**
UK	2.3	0.0	2.3
Europe	9.6	0.0	9.6
US	13.9	0.0	13.9
Japan	5.8	0.0	5.8
Asia Pacific ex Japan	12.3	0.0	12.3
Global equity funds	0.0	0.0	0.0
Other	2.6	0.0	2.6
Government bonds	**13.0**	**-62.1**	**-49.0**
UK	0.0	-29.7	-29.7
Europe	0.0	-32.4	-32.4
US	0.0	0.0	0.0
Japan	0.0	0.0	0.0
Asia Pacific ex Japan	3.3	0.0	3.3
Other	9.7	0.0	9.7
Corporate bonds	**0.0**	**0.0**	**0.0**
Investment grade	0.0	0.0	0.0
High yield	0.0	0.0	0.0
Global bond funds	**8.9**	**0.0**	**8.9**
Convertible bonds	**0.0**	**0.0**	**0.0**
Property funds	**0.0**	**0.0**	**0.0**

Commentary

After performance weakness in August – and the decision to add to long equity and emerging market bond exposure at the end of that month – the fund recovered well in September. Long equity exposures were the main source of positive return, alongside gains from government bond and currency themes. In response to the extent of the recovery in risk assets, we reduced long exposure to equity and high yield credit during the month.

In August, we thought that price actions in many areas looked somewhat episodic, and indeed, weakness in many equity markets proved to be short-lived. There were strong rebounds in Japan, Turkey, and Europe in September, and also gains from the fund's largest equity position in the US banking sector. August's decision to add exposure to a basket of basic resources stocks (from 2.5% to 7.5%) proved beneficial, with that position being the second largest contributor to return among equity positions.

With regards to government bonds, the correlated behaviour between long equity and short developed market bonds that manifested itself in August persisted as that episode partially unwound. The main source of gains from fixed income during September was short exposure to German government bonds. However, the broader bond selloff did reverse somewhat into the end of the month, and the return from a short position in UK gilts was flat overall.

Long exposure to a basket of emerging market bonds (which had been increased from 15% to 22.5% at the end of August) also generated a positive return, though a little less than that from the short bunds.

Currency exposures in the portfolio also generated a positive return, primarily driven by appreciation in long positions in high-yielding emerging market currencies. The Turkish lira, where the fund maintains a 12% position, was the primary contributor.

Key changes

In response to the rapid moves in September, aggregate equity exposure was scaled back mid-month to the lowest level since April this year (prior to the bouts of market volatility in May and August). As part of this reduction, a position in the pan-European Eurostoxx index was reduced from 7.5% to 2.5%, Italian and Turkish equity halved to 2.5% each, the basic resources position cut from 7.5% to 5%, and a 2% position in Taiwan closed.

At the same time, we closed an 18.5% long exposure to US high yield credit (selling protection via a credit default index) following the unwinding of that tactical opportunity and tightening of spreads capital. There were no changes to government bond positions and currency exposures during the month.

The year to date can be characterised as one in which the unwinding of the episode of December 2018, combined with the support for asset valuations provided by falling US rates, was the main source of return in the first four months of the year. Since then there have been two notable bouts of volatility: first in May, and subsequently in August. We have been able to respond to these tactical opportunities by adding long equity and/or credit exposure in response to market weakness, and reducing exposure as prices have recovered.

This positive environment for the approach has been partially offset by the trend for lower bond yields over the year. Since long exposure to US Treasuries was closed in early June, short positions in bunds and gilts have detracted from returns. The nature of these yield declines had not looked episodic (with the possible exception of August) and we did not respond to market moves by increasing short exposures. This judicial element of the approach has helped to contain losses from this theme in the third quarter.

Low developed market bond yields are partly justified by the environment: some weakness in macro data and policy easing around the world have been key themes of the year. However, as investors, we need to consider the extent to which asset prices have gone to extremes in extrapolating known trends. Our sense is that, while tactical opportunities have been less in evidence in bonds than they have in equity markets, a longer-term perspective suggests that prevailing yields are very vulnerable to even modest changes in either the economic backdrop, or investor sentiment. In this respect, the environment resembles that of the first half of 2016, when embedded investor pessimism and a belief that bond yields could never rise set investors up for poor subsequent returns.

It therefore seems appropriate to maintain short bond positions, reflecting two central considerations. First, it is often very difficult to try to forecast when such long-term value signals will work in one's favour. The idea of searching for 'catalysts' can frequently lead to being too late to capture major market moves, which can occur without obvious drivers. Second, though it seems hard to picture today, a rising rate environment can represent a real threat to long equity exposures, as was the case in 2018. While short bond positions may look highly correlated with long equities in phases of short-term volatility such as we have just seen, gaining access to such portfolio diversification properties with value on one's side can be very useful.

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Fund codes and charges

Share class	ISIN	Bloomberg	Currency	Share class launch date	Ongoing charge	Historic yield	Minimum initial investment	Minimum top up investment
Sterling S-H Acc	GB00B5T6XP91	MGMESHS LN	GBP	03/06/2010	1.93%*	-	£500	£100
Sterling T-H Acc	GB00B5LCW587	MGMETHS LN	GBP	03/06/2010	0.93%*	0.24%	£500,000	£50,000

Any ongoing charge figure with * indicates an estimate. The ongoing charge figure may vary from year to year and excludes portfolio transaction costs. The charges are mostly, if not exclusively, the Annual Charge which may be discounted depending on the size of the fund. For further details, please see the fund's Key Investor Information Document (KIID). The fund's annual report for each financial year will include details on the exact charges made.
Please go to www.mandg.co.uk/literature to view the Costs and charges illustration which contains information on the costs and charges applicable to your chosen fund and share class.
Please see the Important Information for Investors document and the relevant Key Investor Information Document for more information on the risks associated with this fund and which share classes are available for which product and which investor type.

Important information

The fund's physical holdings include a significant proportion of cash or cash equivalents, which are used as backing for the derivatives positions.
The fund's neutral currency positioning is 100% in US dollars. Deviations from this figure, therefore, represent long/short exposure.
The fund changed its objective and investment policy, and introduced a benchmark on 14 June 2019. The past performance before this date was achieved under circumstances that no longer apply. The performance of the benchmark before this date is for information purposes only.

Performance fees - The investment manager is entitled to receive a performance fee. Performance fees may be considered to create an incentive for the investment manager that may increase the risk profile of the fund. Please note that this fund comes with further risks that are explained in the Key Investor Information Document.
On all positive returns above the hurdle and above the high water mark (HWM). The HWM is the highest level that a fund's NAV (net asset value) has reached at the end of any 12-month accounting period. In this context, a hurdle is a value to surpass before the performance fee can be levied. Each day, the hurdle will increase (or decrease) by the hurdle rate (three-month LIBOR for the currency in which the relevant share class is denominated).
Due to the nature of this fund, we strongly recommend that you seek financial advice before deciding whether to invest.

The M&G Episode Macro Fund is a sub-fund of M&G Investment Funds (5).

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.

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