M&G (Lux) European Strategic Value Fund
Euro Class A – Accumulation shares

M&G Investments

Quarterly Fund Review as at 31 December 2020

Fund manager(s) – Richard Halle

For investment professionals only

Highlights

- The fund rallied in the fourth quarter and outperformed the MSCI Europe Net Return Index. Robust performance from holdings in cyclical areas such as financials contributed to relative performance.
- European equities ended a tumultuous year on a high as optimism about COVID-19 vaccines fuelled a global stockmarket rally. Value as a style outperformed.
- We identified a number of new opportunities during the quarter including UK retailer Tesco and French telecoms firm Orange. The stake in BIC was sold.

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 can be exposed to different currencies. Movements in currency exchange rates may adversely affect the value of your investment.

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

Things you should know

The fund invests mainly in company shares and is therefore likely to experience larger price fluctuations than funds that invest in bonds and/or cash.

Performance is stated in the share class currency, which may differ from your domestic currency. As a result, the return may rise or fall due to currency movements.

Fund performance

	3 months (%)	YTD (%)	1 year (%)	3 years (%) p.a.	5 years (%) p.a.
Euro A Accumulation	13,7%	-8,3%	-8,3%	-2,2%	1,4%
Benchmark	10,8%	-3,3%	-3,3%	3,1%	4,6%
Sector	14,0%	-7,5%	-7,5%	-1,4%	1,6%
Quartile ranking	3	2	3	3	2

Single year performance (5 years)

	2020	2019	2018	2017	2016
Euro A Accumulation	-8,3%	19,3%	-14,4%	10,7%	3,5%
Benchmark	-3,3%	26,0%	-	-	-
Sector	-7,8%	20,8%	-14,4%	9,3%	3,2%
Quartile ranking	2	3	2	2	2

Past performance is not a guide to future performance.

Benchmark= MSCI Europe Net Return Index

Sector= Morningstar Europe Large-Cap Value Equity sector

The benchmark is a comparator against which the fund's performance can be measured. It is a net return index which includes dividends after the deduction of withholding taxes. The index has been chosen as the fund's benchmark as it best reflects the scope of the fund's investment policy. The benchmark is used solely to measure the fund's performance and does not constrain the fund's portfolio construction.

The fund is actively managed. The investment manager has complete freedom in choosing which investments to buy, hold and sell in the fund. The fund's holdings may deviate significantly from the benchmark's constituents.

Fund performance prior to 20 September 2018 is that of the EUR Class A Accumulation of the M&G European Strategic Value Fund (a UK-authorised OEIC), which merged into this fund on 7 December 2018. Tax rates and charges may differ.

Benchmark prior to 31 December 2011 is the FTSE World Europe. From 1 January 2012 to 19 September 2018, it is the MSCI Europe Index, all stated as Gross Return. From 20 September 2018, the benchmark is the MSCI Europe Net Return Index.

Source: Morningstar, Inc and M&G, as at 31 December 2020. Returns are calculated on a price to price basis with income reinvested. Benchmark returns stated in EUR terms.

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Largest positive contributors 3 months %

	Relative weight	Absolute return	Contribution
Bank Of Ireland	1,6	108,4	1,1
Aperam	2,7	43,8	0,8
Whitbread	2,2	47,9	0,7

Largest positive contributors YTD %

	Relative weight	Absolute return	Contribution
William Hill	3,0	34,0	2,1
Aperam	2,3	27,3	0,7
Maersk	1,3	45,0	0,6

Largest negative contributors 3 months %

	Relative weight	Absolute return	Contribution
Hornbach Holding	2,6	-21,0	-1,0
UCB	2,5	-13,0	-0,7
William Hill	3,8	-1,7	-0,5

Largest negative contributors YTD %

	Relative weight	Absolute return	Contribution
BP	1,8	-44,7	-0,9
Deutsche Lufthansa	1,0	-34,0	-0,8
Lloyds Banking	1,4	-44,9	-0,7

Source: M&G and BlackRock Solutions®, preliminary data. Performance contribution includes both stocks held and not held relative to the fund's comparative index.

Country breakdown (%)

	Fund (Start)	Fund (End)	Change	Index	Relative weight
UK	30,0	31,6	1,7	20,5	11,1
Germany	14,0	13,3	-0,8	14,9	-1,6
France	9,9	11,3	1,5	17,3	-6,0
Switzerland	8,7	6,7	-1,9	16,0	-9,2
Finland	5,0	5,2	0,1	1,9	3,2
Netherlands	4,9	4,9	0,1	7,8	-2,9
Belgium	4,0	4,0	0,0	1,5	2,6
Luxembourg	0,0	4,0	4,0	0,4	3,6
Other	15,9	18,1	2,3	19,7	-1,6
Cash	3,4	0,8	-2,6	0,0	0,8

Industry breakdown (%)

	Fund (Start)	Fund (End)	Change	Index	Relative weight
Health care	21,0	17,5	-3,5	14,4	3,1
Industrials	12,9	15,7	2,8	14,5	1,2
Financials	11,2	15,0	3,8	15,5	-0,6
Consumer discretionary	17,0	13,1	-3,8	11,3	1,8
Energy	8,5	9,8	1,3	4,4	5,4
Materials	9,7	9,4	-0,2	8,2	1,2
Consumer staples	5,8	7,6	1,8	13,5	-5,9
Utilities	4,3	4,1	-0,3	5,0	-0,9
Communication services	3,3	3,9	0,6	3,9	0,0
Information technology	3,0	3,2	0,2	7,8	-4,6
Real Estate	0,0	0,0	0,0	1,4	-1,4
Cash and near cash	3,4	0,8	-2,6	0,0	0,8

Capitalisation breakdown (%)

	Fund (Start)	Fund (End)	Change	Index	Relative weight
> €50 billion	24,0	21,3	-2,7	43,4	-22,1
€25 - €50 billion	11,3	16,4	5,0	24,5	-8,2
€5 - €25 billion	24,1	26,2	2,0	31,6	-5,4
€2.5 - €5 billion	16,8	18,1	1,3	0,5	17,7
< €2.5 billion	20,4	17,3	-3,1	0,0	17,3
Cash and near cash	3,4	0,8	-2,6	0,0	0,8

Largest holdings (%)

	Fund	Index	Relative weight
Novartis	4,1	2,1	2,0
Total	3,8	1,1	2,7
UPM-Kymmene	3,3	0,2	3,1
Aperam	2,9	0,0	2,9
Glaxosmithkline	2,6	0,9	1,7
William Hill	2,6	0,0	2,6
Securitas	2,5	0,1	2,4
UCB	2,4	0,1	2,3
Hornbach Holding AG & Kgaa	2,3	0,0	2,3
Tesco	2,3	0,3	2,0

Largest overweights (%)

	Fund	Index	Relative weight
UPM-Kymmene	3,3	0,2	3,1
Aperam	2,9	0,0	2,9
Total	3,8	1,1	2,7
William Hill	2,6	0,0	2,6
Securitas	2,5	0,1	2,4
Hornbach Holding AG & Kgaa	2,3	0,0	2,3
UCB	2,4	0,1	2,3
Whitbread	2,2	0,1	2,1
Bank of Ireland Group	2,1	0,0	2,1
Novartis	4,1	2,1	2,0

Largest underweights (%)

	Fund	Index	Relative weight
Nestle	0,0	3,4	-3,4
ASML	0,0	2,1	-2,1
LVMH	0,0	1,8	-1,8
Unilever	0,0	1,6	-1,6
SAP	0,0	1,4	-1,4
Novo Nordisk	0,0	1,2	-1,2
Sanofi	0,0	1,1	-1,1
Siemens	0,0	1,1	-1,1
HSBC	0,0	1,1	-1,1
Allianz	0,0	1,0	-1,0

Commentary

European equities rose in the fourth quarter to round off a tumultuous year on a high. The upbeat mood was largely due to news of effective COVID-19 vaccines and optimism about a potential rebound in global economic growth in 2021. This contributed to the performance of the Value style, which benefited the fund. The election of Joe Biden as US president and the avoidance of a no-deal Brexit also lifted investor sentiment.

These developments outweighed concerns about rising coronavirus infections around the world, further lockdowns, as well as new strains of the disease.

In this upbeat environment, the MSCI Europe Index rose 10.8% (in euros). Despite the large decline in March due to the coronavirus-driven fears, the index ended the year down 2.8% largely due to the recent rally.

During the quarter there was a powerful style rotation to value. For most of the year, value stocks had been shunned as many of them are in economically sensitive areas that were hardest hit by coronavirus. During the quarter, especially in the period following the positive vaccine news in November and the prospect of a return to normal, investors shifted their focus to stocks that had previously been weak.

This reversal helped cyclicals outperform defensives in the fourth quarter. Consumer discretionary, energy and financials were the stand-out performers. In contrast, consumer staples and healthcare were notable laggards.

Against this background, the fund delivered a positive return ahead of the benchmark index, driven by robust gains due to our value style of investing.

In economically sensitive financials, our holdings in Irish lender Bank of Ireland and UK financial group NatWest were among the leading contributors. Bank of Ireland's share price more than doubled in the period, reversing some of its fall in March. Investors were encouraged by a positive trading update and government support for the housing market.

As investors focused on stocks that might benefit from the post-COVID 19 recovery, hotel and restaurant operator Whitbread, low-cost airline easyJet and UK coach firm National Express added value. All three UK stocks rallied on hopes that demand for travel would rebound once the vaccine was rolled out.

Luxembourg-based stainless steelmaker Aperam also made a significant contribution. The company has demonstrated resilience in this crisis and the market is starting to appreciate Aperam's strong cashflow and good execution of its strategic plan.

On the other hand, some of the fund's more defensive holdings where performance had been strong prior to the period failed to participate in the market's rise. In healthcare, drugmakers GlaxoSmithKline, Ipsen and UCB were a drag on relative performance but we remain comfortable with these holdings.

Dutch supermarket operator Ahold Delhaize and German home improvements retailer Hornbach both retreated after good share price performance earlier in the year. We believe that Hornbach is a well-managed company that is growing market share and remains very attractively valued.

Activity and positioning

There were five new holdings and one complete sale in the quarter. In the UK, we identified three new opportunities: pub chain JD Wetherspoon, food retailer Tesco and coach operator National Express.

The coronavirus pandemic has hit National Express's business hard, but we believe that it could recover to previous levels when it was considered a stable business.

In relation to Tesco, we think concerns about the growth of less profitable online shopping and the threat from discount supermarkets are overblown. The company is selling its Thai business to focus on the UK and plans to reduce its pension deficit with the proceeds.

We also started positions in Belgium-based biotechnology firm Galapagos. In our view, the company has an interesting drug discovery platform (in collaboration with Gilead) and some promising new medicines in the pipeline, which could deliver significant sales.

The final newcomer was French telecoms firm Orange, which we believe is trading at a very attractive valuation. In our view, Orange could see capital expenditure fall in the next few years as the roll-out of fibre completes, the French market could grow, and it could potentially sell some of its infrastructure assets. We think investors are underappreciating the possible benefits of these factors.

In terms of sales, we sold the stake in French stationery firm BIC. We also took some profits from stocks that have performed well recently, including UK bookmaker William Hill, which received a takeover bid, Danish shipping container firm AP Moller Maersk and French drug maker Roche.

The fund continues to have large weightings, relative to the benchmark, in healthcare, as well as consumer discretionary and energy. In contrast, consumer staples is a significant below-index position on valuation grounds. Information technology and financials are also underweights.

Outlook

The development of effective working COVID-19 vaccines has given investor confidence a significant boost. For the time being, optimism about the process of 'normalisation' and potential stimulus measures is outweighing worries about rising coronavirus cases.

While we recognise that the process of rolling out vaccines is challenging, we believe that this development could bring a welcome end to the cycle of lockdowns and enable the market to look forward to a post-COVID world.

In our view, this environment could be very positive for value stocks, which have struggled in the pandemic. As we saw in November following the positive news of Pfizer's vaccine, an economic rebound could encourage investors to rotate towards sectors that have been weakest. These include travel and leisure, general retail, oil and gas and financials, which are mainly found at the value end of the market.

In addition to the catalyst of the vaccines, we believe there are several factors that could potentially drive a shift to value, including rising inflation expectations, an end to the decline in bond yields and increased regulatory pressure on mega cap tech stocks. After more than a decade of underperformance, we believe the value style has a long way to recover, even after the strong rebound at the end of 2020.

As dedicated value investors, we have waited patiently for value to return to favour and we believe the fund is well positioned to benefit from any style reversal. However, we recognise that we have had false starts before and a value recovery might not be a straight line. Therefore, we remain selective and continue to focus on company fundamentals, particularly financial health, to try and avoid cheap stocks that have material risks and might be unable to weather the current crisis.

ESG Integrated funds

Funds that integrate financially material ESG data into the risk management and decision-making process, as well as our company-wide exclusions (cluster munitions and anti-personnel mines). Some strategies may have some additional ESG exclusions.

Approach to responsible investment

	Yes	No	N/A
ESG integration	✓		
Additional ESG specifications		✓	
Exclusions	✓		
Cluster munitions & anti personnel landmines	✓		
Other exclusions or restrictions		✓	
Voting	✓		
Engagement	✓		

Please see glossary for further explanation of these terms.

ESG Standard Glossary

Additional ESG specifications: In the context of M&G, these are funds managed with an explicit ESG objective, outcome or in accordance with specific ESG criteria, and will have a number of minimum exclusions in place.

Engagement: Interaction with company management on various financial and non-financial, including ESG, issues. Engagement allows investors to better understand how a company is undertaking its operations and how it is interacting with its stakeholders, as well as advising on and influencing company behaviour and disclosures where appropriate.

ESG integration: Describes the explicit and systematic inclusion of Environmental, Social and Governance factors in investment analysis and investment decisions. It underpins a responsible investment approach, and allows investors to better manage risk and generate sustainable, long-term returns.

Exclusions: The exclusion or restriction of investments based on the sector in which they operate, the products or services they provide or for other specific criteria, i.e. they are deemed to be in breach of the United Nations Global Compact principles on human rights, labour the environment and anti-corruption.

Voting: As the partial owners of a company, shareholders have the right to vote on resolutions put forward at a company's annual general meeting. These resolutions include the re-election of directors, executive remuneration and business strategy, among others, and may include resolutions put forward by shareholders.

Important information

On 7 December 2018 the non-sterling assets of the M&G European Strategic Value Fund, a UK-authorised OEIC which launched on 2 January 2008, merged into the M&G (Lux) European Strategic Value Fund, a Luxembourg-authorised SICAV, which launched on 18 September 2018. The SICAV is run by the same fund manager, applying the same investment strategy, as the UK-authorised OEIC.

The past performance for the fund and the index includes recoverable withholding tax which may not be applicable to the SICAV.

The M&G (Lux) European Strategic Value Fund is a sub-fund of M&G (Lux) Investment Funds 1.

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This information is not an offer or solicitation of an offer for the purchase of investment shares in one of the Funds referred to herein. Purchases of a Fund should be based on the current Prospectus. The Instrument of Incorporation, Prospectus, Key Investor Information Document, annual or interim Investment Report and Financial Statements, are available free of charge from the Luxembourg paying agent: Société Générale Bank & Trust SA, Centre operational 28-32, place de la Gare L-1616 Luxembourg.

Before subscribing investors should read the Prospectus, which includes a description of the investment risks relating to these funds.

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