M&G Global Dividend Fund
Sterling Class I – Accumulation shares

Quarterly Fund Review as at 30 September 2020

Fund manager(s) – Stuart Rhodes

For investment professionals only

Highlights

- The fund generated a positive return but lagged the fund's benchmark, the MSCI ACWI Index, with Imperial Brands leading the detractors.
- Not owning Apple and Tesla held back relative performance in a market led higher by 'new economy' stocks.
- Sector allocation detracted, not helped by the above-index exposure to energy.
- Methanex made the biggest positive contribution after the methanol producer's shares surged 35%. Pandora and Lowe's added value in consumer discretionary after reporting better-than-expected results.
- We bought three new holdings in the fund's 'quality' category: Coca-Cola, Novo Nordisk and Takeda Pharmaceutical. We sold LVMH and Constellation Brands in 'rapid growth' as well as Samsung Electronics in 'assets'. The number of stocks remained at 41.
- Technology holdings Microsoft and KLA Corp delivered dividend growth in the typical 5-15% range, alongside Lowe's in consumer discretionary. Imperial Logistics, Treasury Wine Estates and Motus reduced their payments, as expected, against a difficult operating backdrop.

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 holds a small number of investments, and therefore a fall in the value of a single investment may have a greater impact than if it held a larger number of investments.

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.

Fund performance

	3 months	YTD	1 year	3 years p.a.	5 years p.a.
Sterling I Accumulation	1.3%	-5.2%	-2.1%	4.3%	12.2%
MSCI ACWI Index	3.5%	4.3%	5.8%	9.0%	14.5%
Quartile ranking	2	2	2	2	1

Single year performance (5 years)

	2019	2018	2017	2016	2015
Sterling I Accumulation	19.4%	-7.1%	13.2%	40.7%	-6.8%
MSCI ACWI Index	22.4%	-3.3%	13.8%	29.4%	3.8%
Quartile ranking	2	3	1	1	4

Past performance is not a guide to future performance.

Benchmark= MSCI ACWI Index

Performance comparison: The fund is actively managed. The benchmark is a target which the fund seeks to outperform. The index has been chosen as the fund's target benchmark as it best reflects the scope of the fund's investment policy. The target benchmark is used solely to measure the fund's performance and income objective and does not constrain the fund's portfolio construction.

Source: Morningstar, Inc and M&G, as at 30 September 2020. Returns are calculated on a price to price basis with income reinvested.
Benchmark returns stated in GBP terms.

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Largest positive contributors 3 months %

	Relative weight	Absolute return	Contribution
Methanex Corporation	4.9	29.2	1.2
Pandora	2.4	26.9	0.5
Taiwan Semiconductor Manufacturing	1.1	35.1	0.3

Largest positive contributors YTD %

	Relative weight	Absolute return	Contribution
Pandora	2.2	75.9	1.0
Lowe's Companies	2.3	43.4	0.8
Microsoft	1.8	37.6	0.7

Largest negative contributors 3 months %

	Relative weight	Absolute return	Contribution
Imperial Brands	6.7	-9.7	-0.9
Standard Life Aberdeen	3.9	-13.1	-0.7
Apple	-3.7	21.6	-0.6

Largest negative contributors YTD %

	Relative weight	Absolute return	Contribution
Methanex Corporation	4.8	-33.6	-2.2
Imperial Brands	6.6	-21.6	-1.9
Gibson Energy	7.4	-15.5	-1.5

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
US	39.7	37.3	-2.5	57.4	-20.1
Canada	15.1	17.9	2.7	2.5	15.4
UK	14.2	13.9	-0.2	4.1	9.9
Switzerland	7.4	6.4	-1.0	2.8	3.5
Australia	5.4	5.5	0.1	1.8	3.7
Denmark	3.5	4.9	1.4	0.7	4.2
Japan	2.1	3.1	1.1	6.9	-3.7
Italy	0.0	2.1	2.1	0.5	1.6
Other	8.4	8.3	-0.1	23.3	-15.0
Cash	0.8	0.6	-0.2	0.0	0.5

Industry breakdown (%)

	Fund (Start)	Fund (End)	Change	Index	Relative weight
Consumer staples	18.0	17.9	-0.1	7.9	10.0
Health care	15.3	16.5	1.2	12.4	4.1
Information technology	19.0	15.8	-3.2	21.5	-5.7
Materials	13.2	15.4	2.1	4.7	10.7
Energy	10.9	12.1	1.1	2.8	9.2
Financials	12.7	11.9	-0.8	12.4	-0.5
Consumer discretionary	6.8	5.5	-1.3	12.7	-7.3
Utilities	2.5	3.8	1.3	3.1	0.7
Industrials	0.7	0.7	0.0	9.4	-8.7
Communication services	0.0	0.0	0.0	9.3	-9.3
Real Estate	0.0	0.0	0.0	2.6	-2.6
Other	0.0	0.0	0.0	1.1	-1.1
Cash and near cash	0.8	0.6	-0.2	0.0	0.5

Capitalisation breakdown (%)

	Fund (Start)	Fund (End)	Change	Index	Relative weight
Mega cap (> $50bn)	41.9	42.6	0.7	59.5	-16.9
Large cap ($10 - $50bn)	27.3	23.4	-3.9	32.1	-8.7
Mid cap ($2 - $10bn)	21.6	22.8	1.1	8.4	14.4
Small cap (< $2bn)	8.4	10.7	2.3	0.1	10.6
Cash	0.8	0.6	-0.2	0.0	0.5

Largest holdings (%)

	Fund	Index	Relative weight
Gibson Energy	7.5	0.0	7.5
Imperial Brands	7.2	0.0	7.1
Methanex	5.8	0.0	5.8
Keyera	4.6	0.0	4.6
Amcor	3.9	0.0	3.9
Standard Life Aberdeen	3.9	0.0	3.9
Roche	3.7	0.5	3.2
Trinseo	3.5	0.0	3.5
Microsoft	3.4	2.9	0.5
Bristol-Myers Squibb	3.3	0.3	3.1

Largest overweights (%)

	Fund	Index	Relative weight
Gibson Energy	7.5	0.0	7.5
Imperial Brands	7.2	0.0	7.1
Methanex	5.8	0.0	5.8
Keyera	4.6	0.0	4.6
Amcor	3.9	0.0	3.9
Standard Life Aberdeen	3.9	0.0	3.9
Trinseo	3.5	0.0	3.5
Roche	3.7	0.5	3.2
Bristol-Myers Squibb	3.3	0.3	3.1
ST Jamess Place	2.9	0.0	2.9

Largest underweights (%)

	Fund	Index	Relative weight
Apple	0.0	3.9	-3.9
Amazon	0.0	2.6	-2.6
Alphabet	0.0	1.7	-1.7
Facebook	0.0	1.2	-1.2
Alibaba Group Holding	0.0	1.1	-1.1
Johnson & Johnson	0.0	0.8	-0.8
Tencent Holdings	0.0	0.7	-0.7
Nestle	0.0	0.7	-0.7
Nvidia Corporation	0.0	0.6	-0.6
Tesla	0.0	0.6	-0.6

Commentary

Market review

Global equities extended their rally, with the MSCI ACWI Index reaching a peak in early September before giving back some of the gains towards the end of the quarter as 'new economy' stocks lost momentum. The US outperformed, with the S&P 500 Index and the Nasdaq Composite climbing to all-time highs. Emerging markets and Asia Pacific ex Japan delivered returns which were ahead of the MSCI AWI Index, but Japan fell short. Europe was the notable laggard as the UK weighed on returns from the region once more.

Consumer discretionary was the top-performing sector after Amazon.com ended the quarter with a 14% gain in US dollars, while technology benefited from Apple's 27% surge (neither stock is held by the fund). Cyclical sectors delivered mixed results, with materials and industrials outperforming in contrast to the weakness in energy and financials. Defensive stocks were left behind in a rising market, resulting in the underperformance of consumer staples, healthcare and utilities.

Performance commentary

The fund generated a positive return during the third quarter but trailed its benchmark, the MSCI ACWI Index. Stock selection added value but the positive contribution was offset by the negative effect of sector allocation. The overweight (relative to the benchmark) in energy provided the biggest drag on performance.

Imperial Brands (consumer staples) led the detractors as defensive stocks were out of favour in a market dominated by 'new economy' stocks. Roche (healthcare) was also among the leading laggards. Both stocks remain core holdings and we continue to believe that Imperial Brands in particular offers compelling value on a dividend yield of more than 10%.

Not owning Apple and Tesla held back relative performance in a market characterised by narrowness of leadership. Apple is a potential investment candidate because it has paid rising dividends in recent years, but we believe the valuation is demanding and we see more attractive opportunities elsewhere. Tesla does not pay a dividend and is therefore ineligible for our dividend growth approach.

Standard Life Aberdeen drifted lower in a lacklustre financials sector. We continue to believe that the asset manager's shares are extremely cheap and that the dividend yield of 9% is highly compelling. We support the company's decision to continue buying back shares at these distressed levels. We added to the holding on weakness.

Stock selection added value during the quarter with the strongest contributions from energy and materials stocks.

Not owning the oil majors such as Exxon Mobil helped relative performance. We continue to avoid the large integrated oil companies because of long-term growth concerns. The fund's energy holdings, Gibson Energy and Keyera, remain concentrated in energy infrastructure. Shares of the Canadian companies, which own and operate pipelines and storage terminals, ended the quarter broadly flat in local currency after strong performance in the second quarter. The midstream companies remain cash generative and continue to pay dividends. The shares remain attractively valued, in our view.

Methanex (materials) made the biggest positive contribution to performance after the methanol producer's shares surged 35%. Trinseo (chemicals) and Martin Marietta (building materials) also outperformed in the materials sector.

Pandora and Lowe's added value in consumer discretionary after reporting better-than-expected results. Taiwan Semiconductor Manufacturing Company (TSMC) was the top contributor in a strong technology sector.

Year-to-date performance

The fund trailed its benchmark, the MSCI ACWI Index, in the first nine months of 2020, with Methanex and Trinseo in the materials sector among the leading detractors. Gibson Energy and Keyera underperformed in a weak energy sector.

Pandora and Lowe's added the most value over the period after the consumer discretionary companies reported better-than-expected results. Microsoft and Tokyo Electron were also prominent among the top contributors in a buoyant technology sector, although not owning Apple and Amazon.com weighed heavily on relative performance.

Sector allocation detracted due to the above-index exposure to energy although positive stock selection in the sector mitigated the combined effect. Stock selection also added value in financials, helped by the positive contribution from Arthur J Gallagher.

Portfolio activity

There were three new purchases during the quarter matched by three complete sales – a level of turnover consistent with our typical time horizon of three to five years.

The new holdings were driven by a desire to strengthen the fund's income stream. All three purchases – Coca-Cola, Novo Nordisk and Takeda Pharmaceutical – belong to the fund's 'quality' category and we believe provide reliable growth in an environment of ongoing uncertainty. We continued to build our positions in the recent purchases of Procter & Gamble and Enel which we believe provide similar characteristics.

We also added to extreme value opportunities such as Standard Life Aberdeen (financials) and Keyera (energy). Both stocks belong to the fund's cyclical 'assets' category.

LVMH, Constellation Brands and Samsung Electronics were sold. All three stocks rebounded strongly from their lows in March and provided a source of cash for better ideas. We also took profits in strong performers including Microsoft and Lowe's which rose to all-time highs.

The number of holdings remained at 41, compared to our historic range of 40-50. Our cap remains 50 to ensure that every stock in the portfolio undergoes the detailed analysis we require. We want each holding to make a difference, with conviction behind each idea.

Fund positioning

The fund's exposure to 'quality' stocks rose to 42.2% following the new purchases of Coca-Cola, Novo Nordisk and Takeda. The defensive part of the portfolio remains at the lower end of our historic range of 40-60% because of the high multiples attached to many stocks associated with safety. The exposure to stocks in the fund's 'assets' category was higher at 40.2% after the strong performance of the fund's holdings in materials. The fund's cyclical component is above our historic range of 20-35%, reflecting the extreme valuation opportunities we see in a polarised market. The fund's weighting in 'rapid growth' fell to 14.8% after we sold LVMH and Constellation Brands. The typical range for the premium growth segment is 10-20%.

Looking at sectors, materials leapfrogged consumer staples as the fund's largest overweight, relative to the benchmark index, following the strong performance of Methanex, Trinseo and Martin Marietta. Energy remains an overweight position among the cyclical sectors, counterbalanced by a large underweight in industrials. The fund continues to have a small underweight in financials, with zero exposure to banks.

Consumer staples remained the largest overweight, relative to the benchmark, among the defensive sectors, although the absolute weighting was little changed from the previous quarter. The overweight in healthcare increased, helped by the addition of Takeda and utilities moved to an overweight after we bought more Enel to capture the long-term growth in renewable energy. The fund continues to have zero exposure to the bond proxies in communication services and real estate.

Technology moved from an overweight to underweight after we sold Samsung Electronics. Software moved to an underweight after we took profits in strong performers including Microsoft and Visa. The fund remains overweight in semiconductors and underweight in hardware.

Regional weightings were little changed, with North America continuing to account for the largest part of the portfolio at 57%. Europe ex UK was little changed at 15%, with Swiss stocks prominent among the exposure. The UK was stable at 14%. The weighting in Japan increased with the new purchase of Takeda, while the exposure to Asia Pacific ex Japan fell due to the sale of Samsung Electronics in South Korea.

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Company engagement

The assessment of environmental, social and governance (ESG) issues is an increasingly important consideration in the stock selection process and we remain committed to our longstanding practice of engaging companies on crucial aspects of corporate responsibility. We are keen to ensure that the companies in which we are invested adopt best practice to the benefit of all stakeholders, including employees, customers, shareholders and broader society.

The sale of Samsung Electronics during the quarter was a case in point and in keeping with our conscious effort to improve ESG standards across the portfolio. We have been monitoring the company closely: Samsung was the only holding in the portfolio which was potentially in breach of the United Nations Global Compact (UNGC) principles. The technology company is red-flagged due to the alleged involvement of its vice chairman in a bribery case, and we have engaged with the company on several occasions to ensure that appropriate changes are being made to both its culture and compliance so that such an incident does not happen again. While improvements in governance remain a work in progress, we feel the fund is better placed without Samsung. ESG was by no means the only reason for the sale, but it was certainly a contributing factor. The stock rebounded strongly from its March low to within touching distance of its all-time high, with little conviction in the valuation discount narrowing further. Since the initial purchase in February 2018, the shares had returned more than 30% in local currency.

ESG analysis is often associated with negative screening, but we are also keen to embrace its positive aspects and its ongoing development to create a more sustainable world. We are delighted that Gibson Energy, where we have been a cornerstone shareholder for many years, delivered on its promise of improving disclosure on greenhouse gas emissions as a direct consequence of our engagement with the company. We also welcome the creation of a Sustainability and ESG Board Committee to deliver on the company's sustainability strategy. We continue to have similar conversations with other holdings in the portfolio.

Dividend announcements

COVID-19 and its knock-on effect on the global economy continued to exert severe pressure on corporate cashflows and dividends. The environment remains challenging, but many of our holdings continued to deliver dividend growth in the core 5-15% range, reflecting the cash generative qualities of the underlying businesses and their confidence in long-term growth.

In technology, Microsoft raised its dividend by 10%. The industry bellwether was first added to the fund in 2008, since when the dividend has increased fivefold and the share price by a multiple of 11. KLA Corp, the US semiconductor equipment company, reported a 6% dividend increase. The global leader in process control is highly cash generative with a long track record of profitable growth which is reflected in consistently higher dividends.

Lowe's raised its dividend by 9% in consumer discretionary. The US home improvement retailer reiterated its commitment to capital discipline and shareholder returns as operating results continued to surprise on the upside.

Martin Marietta reported a 4% dividend increase. The US building materials company has an exemplary track record of dividend growth for a cyclical business, with the dividend rising every year since its stockmarket listing in 1994.

Novo Nordisk (healthcare) and AIA (financials) raised their interim dividends in the core 5-15% range. Both companies remained true to their commitment to return excess cash to shareholders in a sustainable manner.

The fund was not immune to dividend cuts, however, as the global pandemic had a more damaging effect on other holdings.

Treasury Wine Estates cut its final dividend for the financial year, in line with its policy of paying dividends determined by a payout ratio. We remain optimistic about the prospects for long-term dividend growth driven by the opportunity for higher wine consumption in China.

Imperial Logistics and Motus withdrew their final dividends as full-year results reflected the challenging circumstances presented by lockdown. The South African companies remained cash-generative, however, and their balance sheet remains strong. We continue to have confidence in the companies' long-term growth strategy and their commitment to reinstate dividends at the appropriate time.

While a dividend cut should never be taken lightly, these disappointments were outliers in a 41-stock portfolio. The majority of holdings continued to deliver stable or rising dividends in an extreme environment.

We are acutely aware of the reality that dividends will continue to be tested. It would be reasonable to expect more dividend cuts, if not dividend eliminations, as the year progresses. Being selective will be paramount. Balance sheet strength is therefore a key consideration in our company research to ensure that dividends are sustainable in the current climate. We take comfort from the fact that many of our holdings are carrying net cash.

We remain highly vigilant about the dividend outlook but continue to believe that the majority of our holdings can sustain dividend growth.

Outlook

The strength in equity markets continued to confound the sceptics, but focusing on market levels can be misleading given the narrowness of market leadership we have witnessed. The rally has been driven by a handful of 'new economy' stocks, many of which do not pay dividends, to the detriment of income-seeking investors who have been left behind in a rising market. The dominance of FAANG stocks has been a thorn in the side for dividend strategies owing to the fact that Facebook, Amazon.com, Netflix and Google have never paid a dividend between them. Newcomers such as Tesla and Salesforce.com are of a similar ilk. Apple is a dividend payer, but we believe the valuation is demanding for what is ultimately a cyclical business.

We are not averse to growth. We want to invest in growth companies to capture dividend growth over the long term, but we are not prepared to do so at any price. We continue to find what we consider attractive opportunities in fast-growing companies where dividends are an integral part of the company's capital allocation process, without the burden of a crippling valuation. We bought aggressively into companies such as Visa in the fund's 'rapid growth' category during the market downturn in March, but the subsequent rally has dampened our appetite to buy more. We would highlight the need to be selective and the importance of a valuation discipline.

From a valuation standpoint, we continue to have the greatest conviction in selected cyclical stocks, which despite the recent rebound, look attractively priced. That said, we have been tempering our enthusiasm for extreme value, taking into account portfolio construction issues. We have not allocated more capital to our 'assets' category in an active manner, conscious of the fact that the fund has enough exposure to this area already. We believe the fund has plenty of torque should the much touted 'V-shaped' recovery gather pace.

We are also acutely aware that growth is fragile in many parts of the global economy and therefore that dividends will continue to be tested in 2020. We cannot dismiss the potential for more dividend cuts, if not dividend eliminations, as the year progresses. With this reality in mind, we have made a conscious effort to strengthen the fund's income stream with what we believe is more reliable growth. It is not a coincidence that the three new purchases during the quarter – Coca-Cola, Novo Nordisk and Takeda – are all part of the fund's defensive 'quality' category.

We continue to believe that the majority of our holdings can sustain dividend growth at 5-15% over the long term and that the fund is well placed to build on its track record of providing a rising income stream. Income remains a key consideration in our decision making, but not at the expense of capital. We have confidence in the long-term growth prospects of our holdings and look to the future with optimism.

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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

The M&G Global Dividend Fund is a stand alone OEIC.

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