M&G North American Dividend Fund Sterling Class I – Accumulation shares

Quarterly Fund Review as at 30 September 2020

Fund manager(s) – John Weavers

For investment professionals only

Highlights

- The fund generated a positive return but lagged the S&P 500 Index.
- Sector allocation detracted, not helped by the overweight in energy.
- ONEOK led the detractors in a weak energy sector, while Lowe's added the most value after the home improvement retailer reported better-than-expected results.
- Not owning NVIDIA, Amazon.com and Salesforce.com weighed on relative performance in a narrow market led higher by 'new economy' stocks.
- We bought Activision Blizzard and American Tower, and sold Becton Dickinson. The number of holdings rose to 40.
- Tractor Supply, Microsoft and Mondelez were among the holdings that reported double-digit dividend increases. There were no dividend cuts.

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	3.6%	4.0%	4.5%	12.0%	18.1%
S&P 500 Index	4.1%	8.2%	9.8%	13.7%	17.8%
Sector	4.3%	8.0%	9.3%	12.0%	16.1%
Quartile ranking	3	3	3	3	1

Single year performance (5 years)

	2019	2018	2017	2016	2015
Sterling I Accumulation	26.1%	-0.6%	13.4%	41.5%	-0.7%
S&P 500 Index	26.4%	1.6%	11.3%	33.5%	7.3%
Sector	24.6%	-1.2%	10.5%	30.1%	4.5%
Quartile ranking	2	2	2	1	4

Past performance is not a guide to future performance.

Benchmark= S&P 500 Index

Sector= IA North America sector

Performance comparison: 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 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 fund 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.

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
Lowe's Companies	3.4	17.7	0.4
Methanex Corporation	1.4	29.0	0.3
Broadcom Pte	3.7	11.2	0.3

Largest positive contributors YTD %

	Relative weight	Absolute return	Contribution
Lowe's Companies	3.2	43.8	1.0
Tractor Supply Company	2.1	58.7	0.9
Progressive Corporation	1.8	38.4	0.6

Largest negative contributors 3 months %

	Relative weight	Absolute return	Contribution
Oneok	2.4	-23.1	-0.8
Apple	-4.2	21.8	-0.6
Nvidia	-1.0	36.2	-0.3

Largest negative contributors YTD %

	Relative weight	Absolute return	Contribution
Oneok	2.9	-62.8	-3.3
Amazon	-4.0	74.6	-1.9
Apple	-3.9	75.7	-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	96.1	96.8	0.7	98.5	-1.7
Canada	3.3	3.4	0.1	0.0	3.4
UK	0.0	0.0	0.0	0.8	-0.8
Ireland	0.0	0.0	0.0	0.6	-0.6
Switzerland	0.0	0.0	0.0	0.1	-0.1
Bermuda	0.0	0.0	0.0	0.0	0.0
Cash	0.6	-0.2	-0.8	0.0	-0.2

Industry breakdown (%)

	Fund (Start)	Fund (End)	Change	Index	Relative weight
Information technology	36.8	37.0	0.1	28.1	8.8
Health care	16.3	14.5	-1.8	14.2	0.3
Financials	11.6	12.0	0.4	9.6	2.4
Consumer discretionary	8.9	8.8	-0.1	11.5	-2.7
Consumer staples	6.6	6.7	0.1	7.0	-0.3
Industrials	5.8	6.1	0.2	8.0	-1.9
Energy	4.9	4.1	-0.8	2.0	2.1
Real Estate	2.1	3.5	1.4	2.5	1.0
Materials	3.0	3.4	0.4	2.6	0.8
Utilities	1.5	2.3	0.8	3.0	-0.6
Communication services	1.8	1.8	0.0	10.8	-8.9
Other	0.0	0.0	0.0	0.7	-0.7
Cash and near cash	0.6	-0.2	-0.8	0.0	-0.2

Capitalisation breakdown (%)

	Fund (Start)	Fund (End)	Change	Index	Relative weight
Mega cap (> $50bn)	69.6	70.7	1.1	75.9	-5.2
Large cap ($10 - $50bn)	26.5	23.8	-2.7	22.1	1.7
Mid cap ($2 - $10bn)	1.8	1.8	0.0	2.0	-0.1
Small cap (< $2bn)	1.4	3.8	2.3	0.0	3.8
Cash	0.6	-0.2	-0.8	0.0	-0.2

Largest holdings (%)

	Fund	Index	Relative weight
Microsoft	8.6	5.7	2.9
Visa	5.8	1.2	4.5
Broadcom PTE	4.5	0.5	4.0
Fidelity National Information Services	4.3	0.3	3.9
Lowes Companies	4.0	0.4	3.6
LAM Research Corporation	4.0	0.2	3.8
Unitedhealth Group	3.8	1.1	2.8
Anthem	3.8	0.2	3.5
Constellation Brands	3.7	0.1	3.6
Blackrock	3.2	0.3	2.9

Largest overweights (%)

	Fund	Index	Relative weight
Visa	5.8	1.2	4.5
Broadcom PTE	4.5	0.5	4.0
Fidelity National Information Services	4.3	0.3	3.9
LAM Research Corporation	4.0	0.2	3.8
Constellation Brands	3.7	0.1	3.6
Lowes Companies	4.0	0.4	3.6
Anthem	3.8	0.2	3.5
Blackrock	3.2	0.3	2.9
Microsoft	8.6	5.7	2.9
Harris Corporation	3.0	0.1	2.8

Largest underweights (%)

	Fund	Index	Relative weight
Apple	1.5	6.7	-5.1
Amazon	0.0	4.8	-4.8
Alphabet	0.0	3.1	-3.1
Facebook	0.0	2.3	-2.3
Berkshire Hathaway	0.0	1.5	-1.5
Johnson & Johnson	0.0	1.4	-1.4
Procter & Gamble	0.0	1.2	-1.2
Nvidia Corporation	0.0	1.2	-1.2
Home Depot	0.0	1.1	-1.1
Verizon Communications	0.0	0.9	-0.9

Market review

US equities extended their rally, with the S&P 500 Index and the Nasdaq Composite reaching all-time highs in early September before giving back some of their gains towards the end of the quarter as 'new economy' stocks lost momentum.

Consumer discretionary was the top-performing sector after Amazon.com (not held by the fund) ended the quarter with a 14% gain in US dollars, while technology benefited from Apple's 27% surge. Cyclical sectors delivered mixed results, with materials and industrials outperforming in contrast to the weakness in energy and financials. Consumer staples outperformed but was an outlier among defensive sectors as utilities and healthcare were left behind in a rising market.

Performance commentary

The fund participated in the market rally during the third quarter, but trailed the S&P 500 Index despite outperforming the benchmark in September as 'new economy' stocks retreated from their peak. Sector allocation held back performance during the quarter due to the fund's overweight relative to the S&P 500 Index in energy, which offset the positive contribution from the overweight relative to the benchmark in technology.

ONEOK led the detractors in a weak energy sector, having been one of the top positive contributors during the second quarter. Negative sentiment weighed on the sector once more, but ONEOK's fundamentals remained resilient. The midstream company remained cash-generative and continued to pay dividends. Unlike oil & gas producers, the cashflows generated by midstream companies, which own and operate pipelines and storage terminals, have limited exposure to the underlying commodity price. We continue to have confidence in our energy infrastructure holdings due to their exposure to some of the most prolific basins in North America.

Despite the pressure on ONEOK's share price, stock selection added value in the sector overall due to the fund's zero exposure to Exxon Mobil and Chevron. We continue to avoid the majors because of long-term growth concerns.

Automated Data Processing (ADP) and Visa were outliers in a strong technology sector after their results were given a lukewarm reception. ADP, the payrolls software company, provided a cautious outlook for the year ahead which overshadowed better-than-expected results for the previous quarter. Visa's earnings exceeded market expectations but the digital payments company did not provide guidance for the full year. Both stocks remain core holdings.

The fund's underweight relative to the S&P 500 Index in Apple held back fund performance, but the zero exposure to the laggards of Intel and Cisco Systems proved beneficial. We are increasingly wary of Apple's valuation after the stock's strong rally and we reduced the holding into strength.

Not owning NVIDIA in semiconductors also weighed on relative performance, although this negative effect was cancelled out by the positive contribution from its peers Broadcom and Lam Research.

The continued momentum in Amazon.com provided a headwind for dividend investors. The paragon of 'new economy' stocks continued to see strong demand, but the company is ineligible for our dividend growth strategy due to the lack of a dividend discipline. Salesforce.com, whose stock price jumped more than 30% during the quarter, is also out of scope for the same reason.

Lowe's made the biggest positive contribution to performance after the home improvement retailer's results continued to exceed market expectations. The shares returned more than 20% during the quarter and reached a record high.

Stock selection added value in materials after Methanex and Air Products and Chemicals ended the quarter with double-digit gains. Union Pacific, the railroads company, outperformed the S&P 500 Index in industrials.

Year-to-date performance

The fund generated a positive return in the first nine months of the year but underperformed its benchmark, the S&P 500 Index. Positive stock selection in financials (Progressive, S&P Global) and real estate (Equinix) was offset by negative contributions from technology (underweight relative to the S&P 500 Index in Apple, not owning NVIDIA) and healthcare (Anthem). ONEOK led the detractors in a weak energy sector; not owning Amazon.com provided the second-biggest drag on performance relative to the benchmark. Consumer discretionary (Lowe's, Tractor Supply) and technology (Microsoft, Broadcom) featured prominently among the top positive contributors.

Sector allocation also held back performance as the positive effect of the overweight relative to the S&P 500 Index in technology was cancelled out by the overweight relative to the benchmark in energy.

Portfolio activity

We bought two new holdings and exited one position during the quarter – a level of turnover consistent with our typical time horizon of three to five years.

Activision Blizzard (communication services) was the first new purchase in July. The publisher of interactive games is a market leader in a growth industry with a compelling growth trajectory over the long term. COVID lockdowns spurred an introduction to digital gaming for a huge number of potential new consumers globally, and with a suite of new games to be launched over the next two years, Activision Blizzard is well placed to capitalise on this expanded customer set. American Tower (real estate) was added to the portfolio in September to capitalise on the long-term growth in digital infrastructure. Despite its status as a real estate investment trust (REIT), the communications towers company should not be considered as a bond proxy. The US is on the cusp of meaningful spend of 5G roll out nationally, which should underpin attractive growth for American Tower for years to come. American Tower also has a broad geographic footprint with significant exposure to the structural growth in emerging markets driven by increasing wireless penetration and data usage.

Becton Dickinson (healthcare) was sold as a source of cash for better ideas. We also took profits in Tractor Supply (consumer discretionary) and reduced Comcast (communication services).

Following these transactions, the number of holdings rose to 40.

Fund positioning

The fund's exposure to 'quality' increased to 43.0% following the purchase of American Tower. 'Rapid growth' was little changed at 30.6% as the new holding in Activision Blizzard was offset by profit taking in Tractor Supply. The cyclical 'assets' category was higher at 26.6% after the strong performance of our semiconductor holdings Broadcom and Lam Research.

Technology remained the fund's largest overweight relative to the S&P 500 Index, with software accounting for the lion's share of the sector exposure. The weighting in semiconductors increased, while the hardware exposure fell as we reduced our holding in Apple. Communication services remained the largest underweight relative to the benchmark.

In cyclical sectors, the exposure to financials increased after we added to the holding in BlackRock. The fund remained overweight relative to the S&P 500 Index in the sector, with an overweight in insurance and an underweight in banks. Energy also remained an overweight relative to the benchmark.

Among the defensive sectors, the weighting in utilities rose as we continued to build our positions in the recent purchases of Sempra Energy and NextEra Energy. Healthcare remained an overweight relative to the S&P 500 Index although the weighting was lower after the sale of Becton Dickinson. Consumer staples continued to be a small underweight relative to the benchmark.

Dividend announcements

COVID-19 and its knock-on effect on the global economy continued to exert severe pressure on corporate cashflows and dividends paid by US companies. The environment remained 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. There were no dividend cuts.

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In technology, Lam Research and Microsoft raised their dividends by 13% and 10%, respectively, while Broadridge Financial Solutions and KLA Corp reported a 6% increase. Tractor Supply and Lowe's reported dividend growth of 14% and 9%, respectively, in consumer discretionary, while Mondelez boosted its payment by 11% in consumer staples.

Newcomer American Tower delivered the fastest growth, with a quarterly dividend which was 20% higher than the same period last year. Even in the unfashionable energy sector, ONEOK's quarterly dividend was up 5% compared to last year.

Not all of the fund's holdings reported dividend growth, however, as JPMorgan Chase (financials) and Union Pacific (industrials) held their dividends flat. JPMorgan has been required to maintain the dividend at the current level following the Federal Reserve's stress test. We fully expect Union Pacific to resume its dividend progression at the appropriate time.

We are encouraged that the majority of the fund's holdings continue to deliver stable and rising dividends, but we remain highly vigilant about the dividend outlook. We continue to believe that the fund is well placed to deliver on its objective of providing a rising income stream for investors.

Outlook

The strength in stockmarkets continued to confound the sceptics, but many uncertainties remain, not least the shape of the economic recovery following the devastating effects of the pandemic. Against this backdrop, we have been focusing our attention on seeking to identify potential winners in a post-COVID world.

Digital payments, for example, is an area where we have conviction that the structural growth is not only intact but accelerating due to permanent changes in consumer behaviour following life in lockdown. The long-run shift away from cash transactions towards card and digital payments shows no signs of abating. Visa and MasterCard are well placed to benefit from this multi-decade theme, in our view, as well as Fidelity National Information Services (FIS). We believe all three companies offer the potential for attractive growth without the burden of crippling valuations. Activision Blizzard (interactive games) and Lowe's (home improvement) are other potential winners we see in the 'new normal'.

The presidential election in November is a potentially market-moving event on the immediate horizon. We do not have a view on the likely election outcome, but we have been active in our search for potential beneficiaries of policy changes driven by the need to address long-term issues in the US economy.

Climate change is likely to attract increasing attention, in our view, with renewable energy providing an obvious avenue for long-term growth. Joe Biden in particular has been upfront about his green agenda and his commitment to clean energy. Our recent purchase of NextEra Energy is a potential beneficiary of this trend, in our view, due to its status as the US market leader in renewables.

Infrastructure spending is another topical subject, given its prominence in fiscal stimulus packages around the world. The desperate need to repair and modernise America's ailing infrastructure is not up for debate. The chronic underinvestment is so widely accepted that it has been one of the few areas of common ground between the Republicans and Democrats. Investment will not be confined to traditional infrastructure such as roads and bridges; there is a political desire for universal broadband access, including the rollout of 5G networks. Our holdings in the wireless towers companies Crown Castle and American Tower are well placed, we believe, to benefit from increased spending, regardless of which candidate wins the election.

Whatever the election result, there is a harsh reality that is unlikely to change: dividends are under pressure and are likely to remain so for the foreseeable future. It would be reasonable to expect more dividend cuts, if not more eliminations, in the months ahead. 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 cannot dismiss the potential for more dividend cuts, but we have an established process to cope with those scenarios in our endeavour to deliver a favourable outcome for our clients.

We continue to believe that the majority of our holdings can sustain dividend growth at 5-15% over the long term. The immediate outlook is more difficult to determine, but we continue to have confidence in the long-term prospects of the fund's holdings.

We remain undeterred in our pursuit of dividend growth and remain resolutely committed to its viability not only as a source of rising income, but also as a total return strategy in the US market over the long term.

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 fund originally launched on 18 December 1972 as the M&G American Fund. On 28 April 2015, the fund's name and objective changed and it is now called the M&G North American Dividend Fund and we are choosing to use this date as the launch date for this fund . Therefore the past performance shown before this change was achieved under circumstances that no longer apply.
The Fund changed its name and objective on 28 April 2015.

The M&G North American Dividend Fund is a sub-fund of M&G Investment Funds (1).

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