M&G (Lux) Optimal Income Fund
Euro Class A – Accumulation shares

Monthly Fund Review as at 30 September 2019

For investment professionals only

Highlights

- Weak US manufacturing data stokes volatility, despite Fed and ECB rate cuts.
- We took further advantage of a pricing mismatch in inflation breakevens.
- We maintain our very underweight duration position of around 1.6 years.

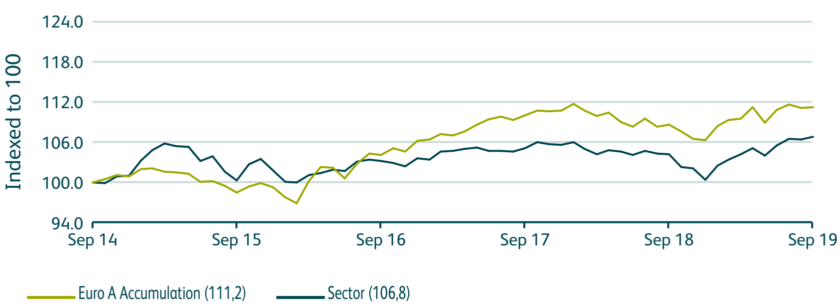
The main risks associated with this fund

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.
Investments in bonds are affected by interest rates, inflation and credit ratings. It is possible that bond issuers will not pay interest or return the capital. All of these events can reduce the value of bonds held by the fund.
High yield bonds usually carry greater risk that the bond issuers may not be able to pay interest or return the capital.
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 is exposed to different currencies. Derivatives are used to minimise, but may not always eliminate, the impact of movements in currency 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
Euro A Accumulation	-4,0%	4,3%	7,0%	-1,6%	4,7%
Sector	-4,9%	2,1%	1,9%	0,8%	5,3%

Performance over 5 years



Fund performance

	1 month (%)	3 months (%)	YTD (%)	1 year (%)	3 years (%) p.a.	5 years (%) p.a.
Euro A Accumulation	0,1%	0,4%	4,7%	2,4%	2,2%	2,2%
Sector	0,4%	1,3%	6,4%	2,5%	1,2%	1,3%

Past performance is not a guide to future performance.

Performance prior to 7 September 2018 is that of the EUR Class A-H Accumulation of the M&G Optimal Income Fund (a UK-authorised OEIC), which merged into this fund on 8 March 2019. Tax rates and charges may differ.

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

Key information

Fund manager	Richard Woolnough
Fund manager tenure from	20 April 2007
Deputy fund manager	Stefan Isaacs
ISIN	LU1670724373
Launch date of fund	05 September 2018
Launch of share class	07 September 2018
Fund size (millions)	€ 19.836,56
Fund type	SICAV
Comparative index	1/3 Bloomberg Barclays Global Agg Corp EUR Hedged, 1/3 Bloomberg Barclays Global High Yield EUR Hedged, 1/3 Bloomberg Barclays Global Treasury EUR Hedged Index
Comparative sector	Morningstar EUR Cautious Allocation - Global sector
Number of issuers	271
Underlying yield	0,87%
Average credit rating	A-
Modified duration (years)	1,56
Average coupon	3,13
Spread duration (years)	6,3

'Manager tenure' includes the period when managing an equivalent UK-authorised OEIC. Please see 'Important information' at the end of this document for further details.

Charges

Entry charge	4,00%
Ongoing charge	1,46%

Duration by currency and asset class

	Fund	Futures	Swaps	Net
Euro	1,4	-1,3	0,0	0,2
British pound	2,1	-0,6	-0,7	0,8
US dollar	3,4	-3,0	0,0	0,3
Other	0,2	0,0	0,0	0,2
Total	7,1	-4,8	-0,7	1,6

Things you should know

The fund allows for the extensive use of derivatives.

Fund ratings

Morningstar Analyst rating — Silver

Overall Morningstar rating ★★★★★

Source of Morningstar ratings: Morningstar, as at 30 September 2019

Ratings should not be taken as a recommendation.

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Asset breakdown (%)

	Physical	Short (via CDS)	Long (via CDS)	Net
Government bonds	**32,9**	**-4,9**	**0,0**	**27,9**
Investment grade corporate bonds	**49,7**	**-2,5**	**1,7**	**48,9**
Fixed rate	41,6	0,0	0,0	41,5
Floating rate	8,1	0,0	0,0	8,1
Index linked	0,0	0,0	0,0	0,0
Credit default swap indices	0,0	-2,5	1,7	-0,8
High yield corporate bonds	**8,1**	**0,0**	**0,0**	**8,1**
Fixed rate	7,0	0,0	0,0	7,0
Floating rate	1,1	0,0	0,0	1,1
Index linked	0,0	0,0	0,0	0,0
Credit default swap indices	0,0	0,0	0,0	0,0
Securitised	**2,7**	**0,0**	**0,0**	**2,7**
Equities	**4,7**	**0,0**	**0,0**	**4,7**
Cash	**1,9**	**0,0**	**0,0**	**1,9**
Other	**0,0**	**0,0**	**0,0**	**0,0**

Credit rating breakdown (%)

	Physical	Short (via CDS)	Long (via CDS)	Net
AAA	30,3	0,0	0,0	30,3
AA	7,2	0,0	0,0	7,2
A	6,3	0,0	0,0	6,3
BBB	40,2	-3,0	1,7	38,9
BB	7,7	-4,5	0,0	3,3
B	1,3	0,0	0,0	1,3
CCC	0,2	0,0	0,0	0,2
CC	0,1	0,0	0,0	0,1
C	0,0	0,0	0,0	0,0
D	0,0	0,0	0,0	0,0
No rating	4,7	0,0	0,0	4,7
Cash	1,9	0,0	0,0	1,9

Country breakdown (%)

	Physical	Short (via CDS)	Long (via CDS)	Net
Germany	30,9	0,0	0,0	30,9
US	27,7	0,0	0,0	27,7
UK	18,4	0,0	0,0	18,4
France	8,0	0,0	0,0	8,0
Italy	2,7	0,0	0,0	2,7
Belgium	1,9	0,0	0,0	1,9
Netherlands	1,8	0,0	0,0	1,8
Japan	1,7	0,0	0,0	1,7
Other	5,1	-1,6	0,0	3,5
Investment Grade indices	0,0	-2,5	1,7	-0,8
Cash	1,9	0,0	0,0	1,9
Other	0,0	-3,3	0,0	-3,3

Largest issuers (%)

	Fund
AT&T	3,1
Microsoft	2,7
Anheuser Busch	1,9
Altria Group	1,8
Bank of America	1,5
Verizon Communications	1,3
Lloyds Banking Group	1,2
Vodafone Group	1,2
Orange	1,1
Citigroup	1,1

Maturity breakdown (%)

	Physical
0 - 1 years	7,6
1 - 3 years	14,4
3 - 5 years	13,3
5 - 7 years	9,1
7 - 10 years	16,6
10 - 15 years	8,0
15+ years	29,1
Cash	1,9

Currency breakdown (%)

	Pre-hedge	Post-hedge
Euro	42,3	99,5
US dollar	31,2	0,3
British pound	24,6	0,2
Swiss franc	0,2	0,0
Japanese yen	1,7	0,0
South African rand	0,0	0,0
Singapore dollar	0,0	0,0

Industry breakdown (%)

	Physical	Short (via CDS)	Long (via CDS)	Net
Sovereign	31,0	0,0	0,0	31,0
Banking	10,0	0,0	0,0	10,0
Telecommunications	9,9	0,0	0,0	9,9
Consumer goods	5,9	0,0	0,0	5,9
Technology & electronics	4,3	0,0	0,0	4,3
Automotive	3,2	0,0	0,0	3,2
Asset backed	3,0	0,0	0,0	3,0
Insurance	2,8	0,0	0,0	2,8
Basic industry	2,8	0,0	0,0	2,8
Healthcare	2,6	0,0	0,0	2,6
Media	2,1	0,0	0,0	2,1
Utility	2,1	0,0	0,0	2,1
Energy	1,9	0,0	0,0	1,9
Foreign Sovereign	1,8	-1,6	0,0	0,2
Covered Bonds	1,6	0,0	0,0	1,6
Real Estate	1,4	0,0	0,0	1,4
Commercial Mortgage Backed	1,4	0,0	0,0	1,4
Retail	1,3	0,0	0,0	1,3
Mortgage backed	0,8	0,0	0,0	0,8
Transportation	0,6	0,0	0,0	0,6
Financial services	0,5	0,0	0,0	0,5
Services	0,5	0,0	0,0	0,5
Leisure	0,5	0,0	0,0	0,5
Capital goods	0,4	0,0	0,0	0,4
Supranational	0,4	0,0	0,0	0,4
Agency	0,3	0,0	0,0	0,3
Government Guaranteed	0,1	0,0	0,0	0,1
Quasi & foreign government	0,0	-3,3	0,0	-3,3
Investment Grade indices	0,0	-2,5	1,7	-0,8
Other	4,7	0,0	0,0	4,7
Cash	1,9	0,0	0,0	1,9

Commentary

September was an active month for markets as investors focused on a series of interest rate moves from major central banks. Both the Federal Reserve and the European Central Bank cut interest rates, while the Bank of England held rates (at 0.75%) although it did include 'lower for longer' language on the rising risk of a 'no deal' Brexit. Volatility continued too, driven by the prospect of the latter and, more significantly, concerns over the US economy – its manufacturing sector showing signs of increasing weakness despite continued accommodative policy from the Fed. Oil prices spiked on rising tensions in the Middle East, which added to investor unease in the month.

However, against this uncertainty core government bond yields failed to behave as they did in August, rallying higher in the first half of the month. This perhaps was an indication that expectations for further monetary loosening had been extremely high. Subdued data towards the end of the month put downward pressure on yields again. Credit initially rallied on the ECB's announcement of 'QE infinity', but heavy supply from the primary corporate bonds market subsequently weighed heavily on spreads.

The fund generated a small positive return in September, supported by its cautious duration position. Being short rates exposure meant we offset price falls in German bunds and US Treasuries particularly early in the month. On the other hand, the fund benefited from its equity exposure, which admittedly remains low/steady at around 5% of asset allocation. As yields trended higher, banks' securities had a good month as earnings expectations rose. The fund also received a boost from the marginal compression in spreads, notably in US dollar-denominated investment grade corporates (the area we prefer) as they outperformed both sterling and euro credit in period under review.

Key changes

It has been a very active month for the fund, as we harness the full flexibility of Optimal Income's investment approach. Within the government bond space and in areas that performed well in the last few months, we continued to reduce our exposure to long-dated French bonds (OATs) and started to trim exposure to Italian government bonds (BTPs) issued in sterling (last month we sold BTPs issued in euros).

A key tactical play for us recently has centred around taking advantage of a mismatch in how the market is pricing inflation expectations over the coming years. Similar to August's bet, we bought more Japanese and eurozone inflation-linked bonds, given they are attractively-priced against a backdrop of negative-to-zero inflation expectations. In a reverse move, we have initiated a short position on UK inflation through 10-year swaps. In our view, UK inflation is looking expensive and, arguably, fully discounting a fall in sterling post Brexit. In addition, the development in attempts to reform the retail price index (RPI) could add pressure on mid-to-long-dated linkers, as at some juncture (2025 onwards) they might reference the consumer price index plus housing costs (CPIH). At last count, this index was around 0.9 percentage points below RPI.

Within corporate credit, we continued to trim banks – a theme for the fund in 2019 - and added some exposure to asset-backed securities. In this regard, with spreads tightening, we have been buying some more defensive and high-rated ABS. These instruments' yields also have a 0% floor, which is quite useful to have in this environment of negative-yielding debt elsewhere.

Exposure to high yield remained steady in September, but well below the fund's neutral exposure of 33.3% as we believe it has less value than the favoured investment grade universe. We continue to favour modest holdings of BB rated bonds over lower-rated names.

Within equities, in response to higher asset prices in the month we sold Italian bank securities, while adding Imperial Tobacco on compelling yields of around 10%.

On the long-held view that the global economy remains on a solid footing, although with some signs of weakness, we maintain a very underweight duration of around 1.6 years versus a neutral 6.1 years. Most of this duration still comes from sterling assets.

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Fund codes and charges

Share class	ISIN	Bloomberg	Currency	Launch date of fund	Ongoing charge	Distribution yield	Underlying yield	Minimum initial investment	Minimum top up investment
Euro A Acc	LU1670724373	MGOIEAA LX	EUR	07/09/2018	1,46%	-	0,87%	€1.000	€75
Euro A Inc	LU1670724456	MGOIEAD LX	EUR	07/09/2018	1,46%	2,33%	0,87%	€1.000	€75
Euro B Acc	LU1670724530	MGLOEBA LX	EUR	07/09/2018	1,96%	-	0,37%	€1.000	€75
Euro B Inc	LU1670724613	MGLOEBD LX	EUR	07/09/2018	1,96%	2,33%	0,37%	€1.000	€75
Euro C Acc	LU1670724704	MGOIECA LX	EUR	07/09/2018	0,96%	-	1,37%	€500.000	€50.000
Euro C Inc	LU1670724886	MGOIECD LX	EUR	07/09/2018	0,96%	2,33%	1,37%	€500.000	€50.000
Euro CI Acc	LU1797814339	MOIECIA LX	EUR	07/09/2018	0,92%	-	1,41%	€500.000	€50.000
Euro CI Inc	LU1797814412	MOIECID LX	EUR	17/12/2018	0,93%*	2,33%	1,42%	€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 do not include portfolio transaction costs. They are based on expenses for the period ending 31 March 2019. Any ongoing charge figure with * indicates an estimate. The fund's annual report for each financial year will include details of the exact charges.

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

On 8 March 2019 the non-sterling assets of the M&G Optimal Income Fund, a UK-authorised OEIC which launched on 8 December 2006, merged into the M&G (Lux) Optimal Income Fund, a Luxembourg-authorised SICAV, which launched on 5 September 2018. The SICAV is run by the same fund manager, applying the same investment strategy. as the OEIC.
Comparative Index: 1/3 Bloomberg Barclays Global Agg Corporate Index EUR Hedged; 1/3 Bloomberg Barclays Global High Yield Index EUR Hedged; and 1/3 Bloomberg Barclays Global Treasury Index EUR Hedged.

Performance prior to 7 September 2018 is that of the EUR Class A-H Accumulation of the M&G Optimal Income Fund (a UK-authorised OEIC), which merged into this fund on 8 March 2019. Tax rates and charges may differ.

It is 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.
For 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 M&G (Lux) Optimal Income Fund is a sub-fund of M&G (Lux) Investment Funds 1.

Sector: Morningstar category averages represent the average return of funds within their category over time. The category averages are created by using the average daily total return index series, or TRI, as well as monthly, quarterly, and annual averages of return and non-return data. Morningstar applies a fractional weighting methodology whereby, on the last day of each month, the funds are equally weighted and the share classes within each fund are equally weighted. Fractional weighting ensures that funds with multiple share classes do not dominate and skew the returns of the average, thus presenting the peer group performance in a fair and consistent manner.

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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The M&G Investment Funds are registered for public distribution under Art. 15 of Act 35/2003 on Collective Investment Schemes as follows: M&G Investment Funds (1) reg. no 390, M&G Investment Funds (2) reg. no 601, M&G Investment Funds (3) reg. no 391, M&G Investment Funds (5) reg. no 972, M&G Investment Funds (7) reg. no 541, M&G Investment Funds (9) reg. no 930, M&G Investment Funds (12) reg. no 1415, M&G Investment Funds (14) reg. no 1243, M&G Global Dividend Fund reg. no 713, M&G Global Macro Bond Fund reg. no 1056, M&G Optimal Income Fund reg. no 522 and M&G (Lux) Investment Funds 1 reg. no 1551.

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 Allfunds Bank, Calle Estafeta, No 6 Complejo Plaza de la Fuente, La Moraleja, 28109, Alcobendas, Madrid.

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

The information contained herein is not a substitute for independent investment advice.

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