



# Fixed Income and Macro Views

**Stefan Isaacs, Deputy Head of Retail Fixed Interest**  
**September 2018**

# Agenda

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2018 in review

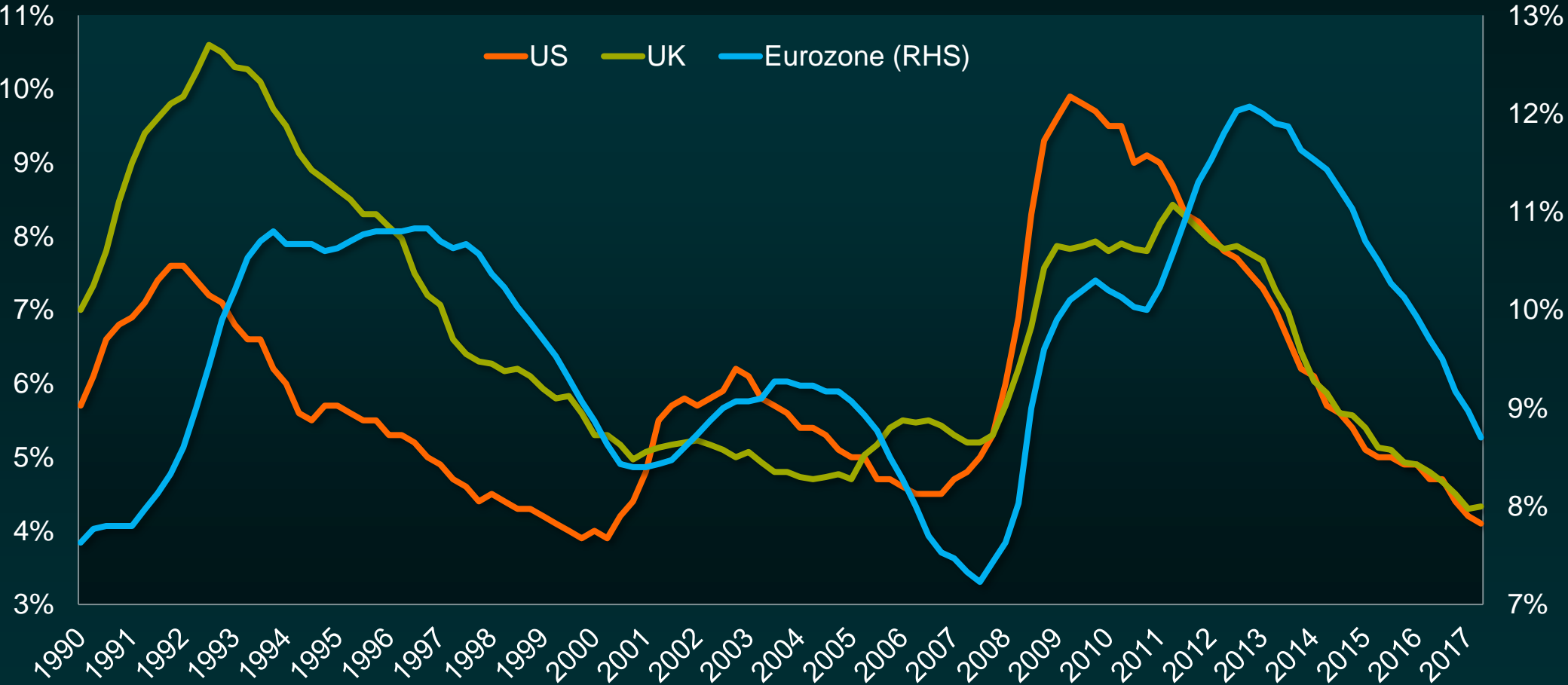
Challenges to the view

Where does that leave us?

M&G Optimal Income Fund and M&G Global Floating Rate High Yield Fund

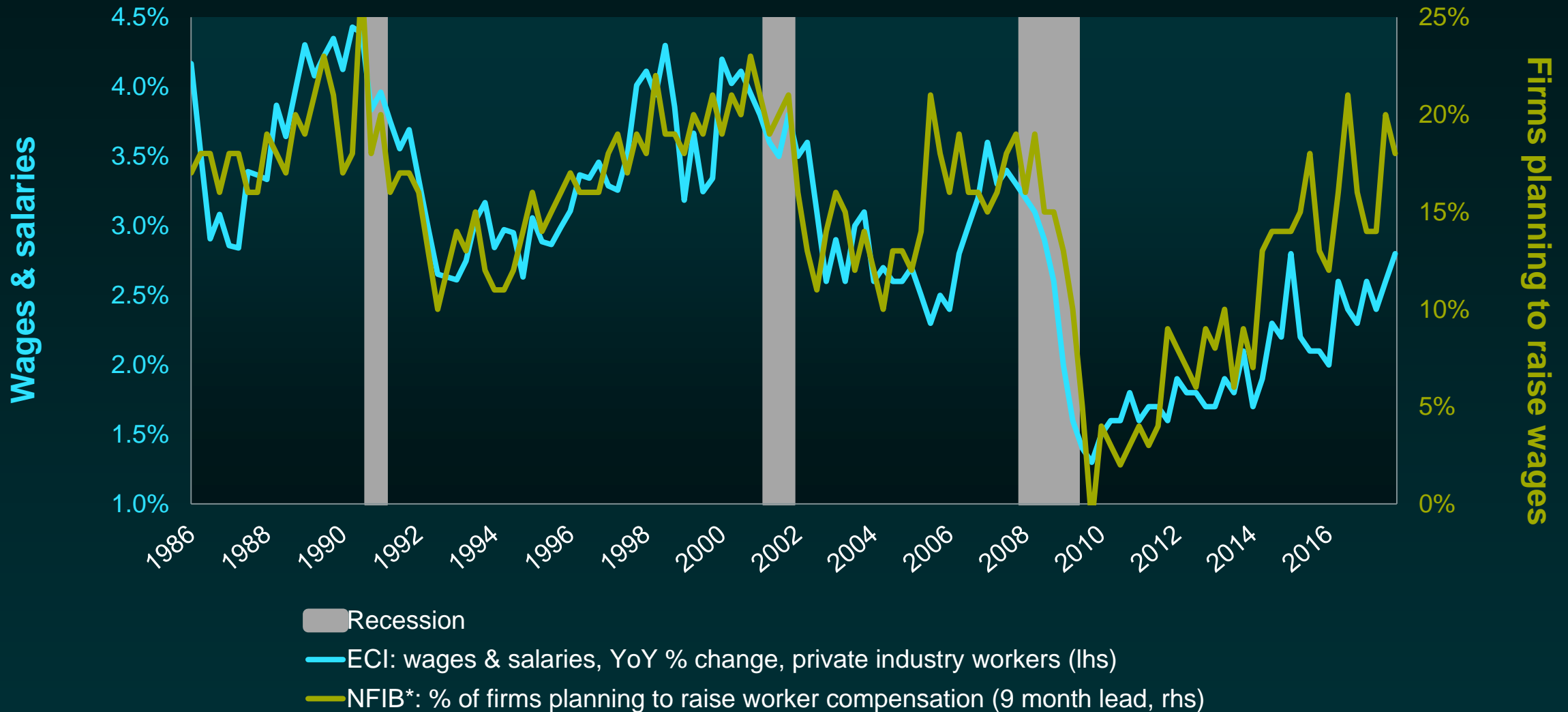
# Monetary policy worked

## Unemployment rates continued to fall



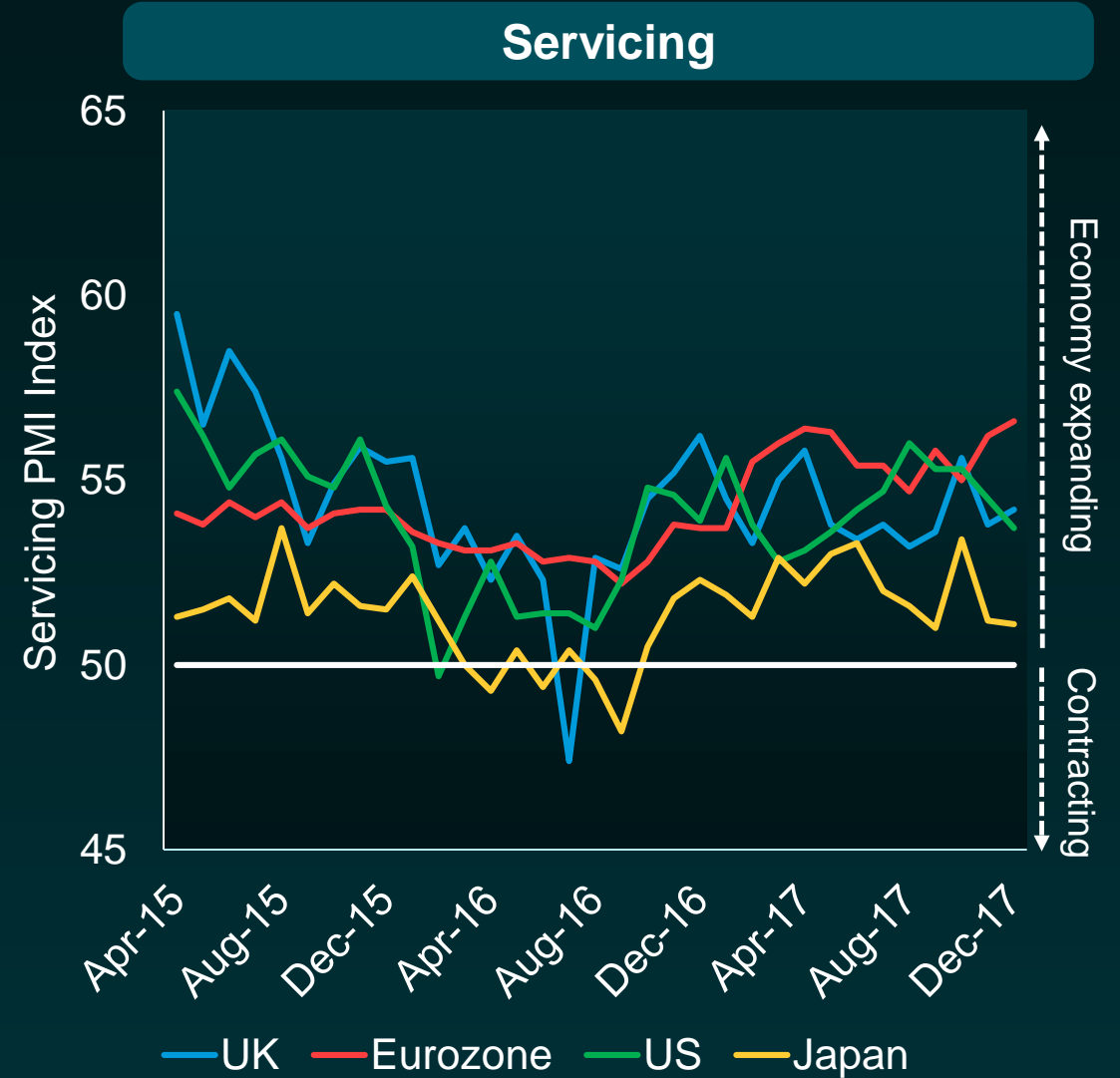
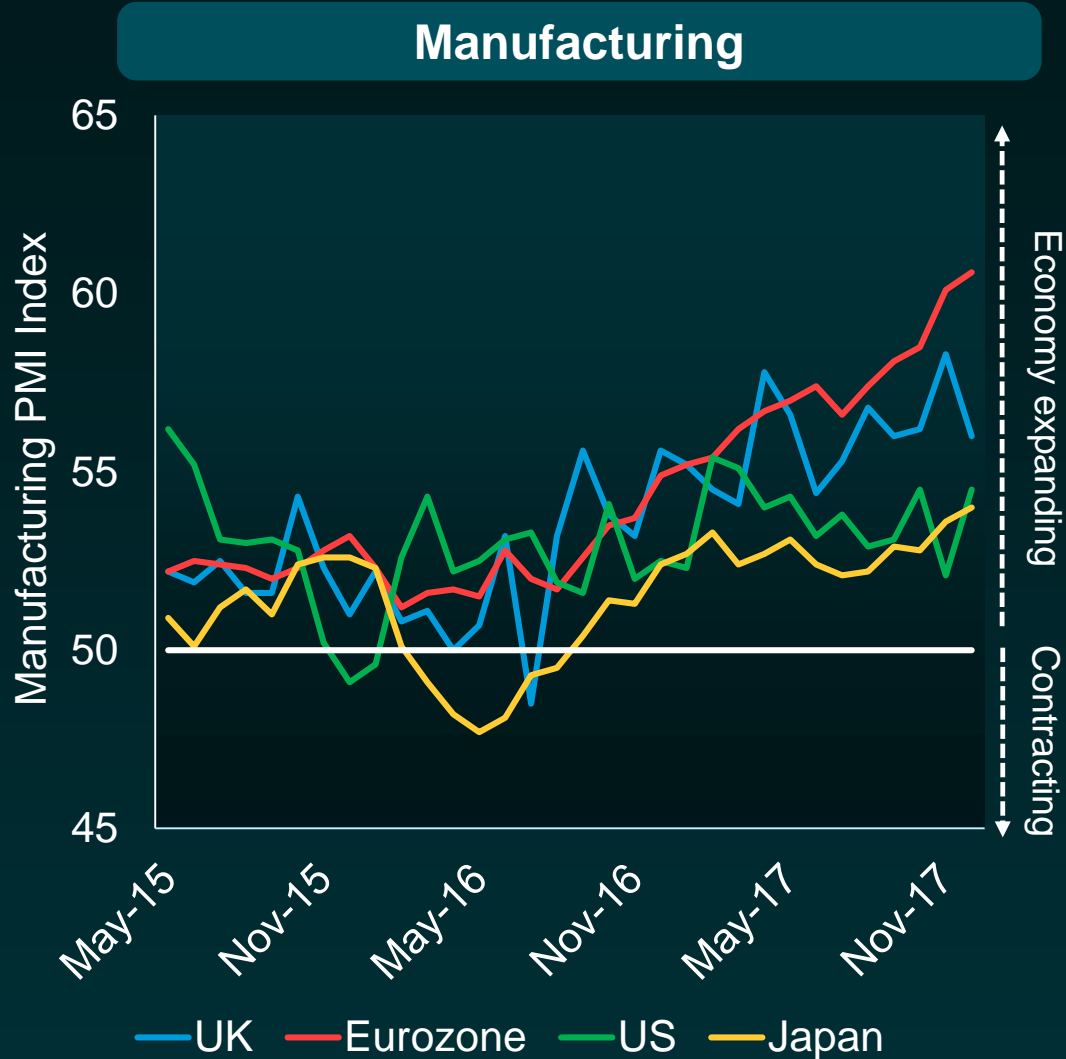
# Where's wage growth going?

## Into end 2017, wage growth subdued but rising



# What was the data telling us?

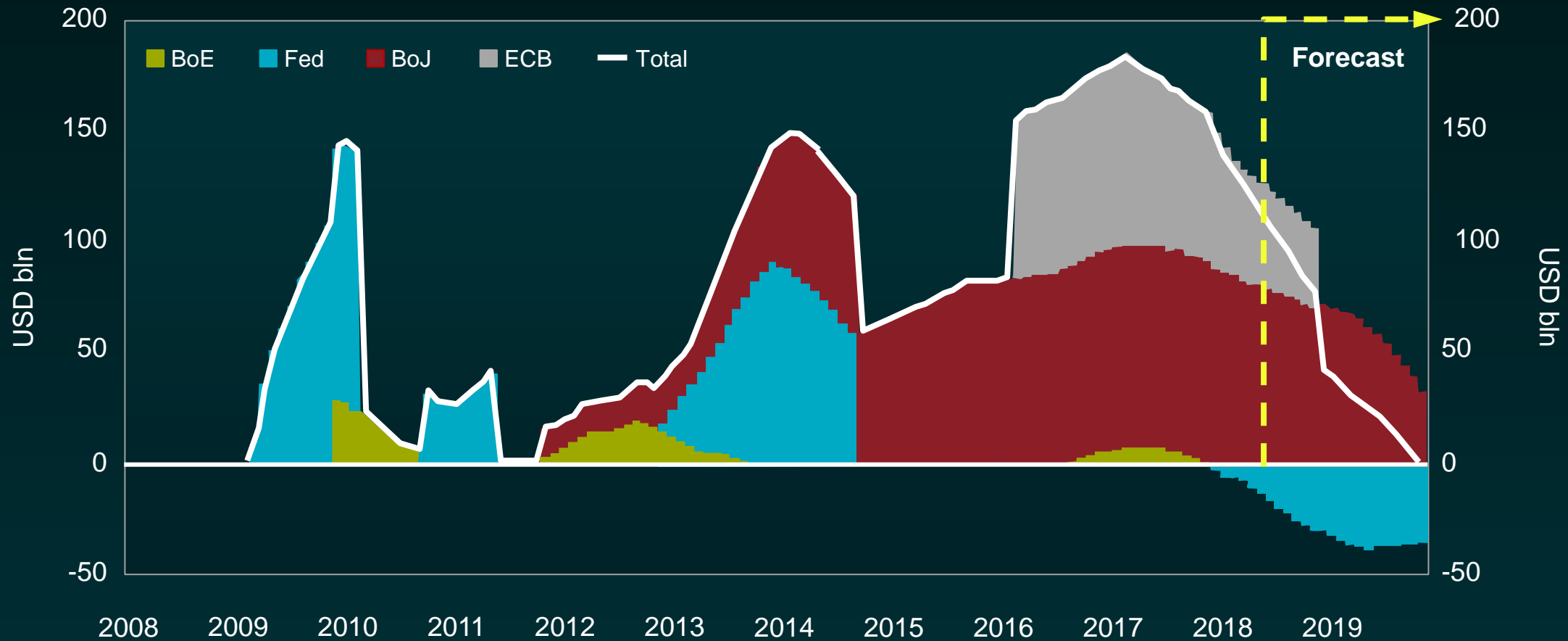
Synchronised global growth had been the theme supported by global data



# Declining central bank liquidity with further tightening expected

## The upside risk to global rates look significant in 2018

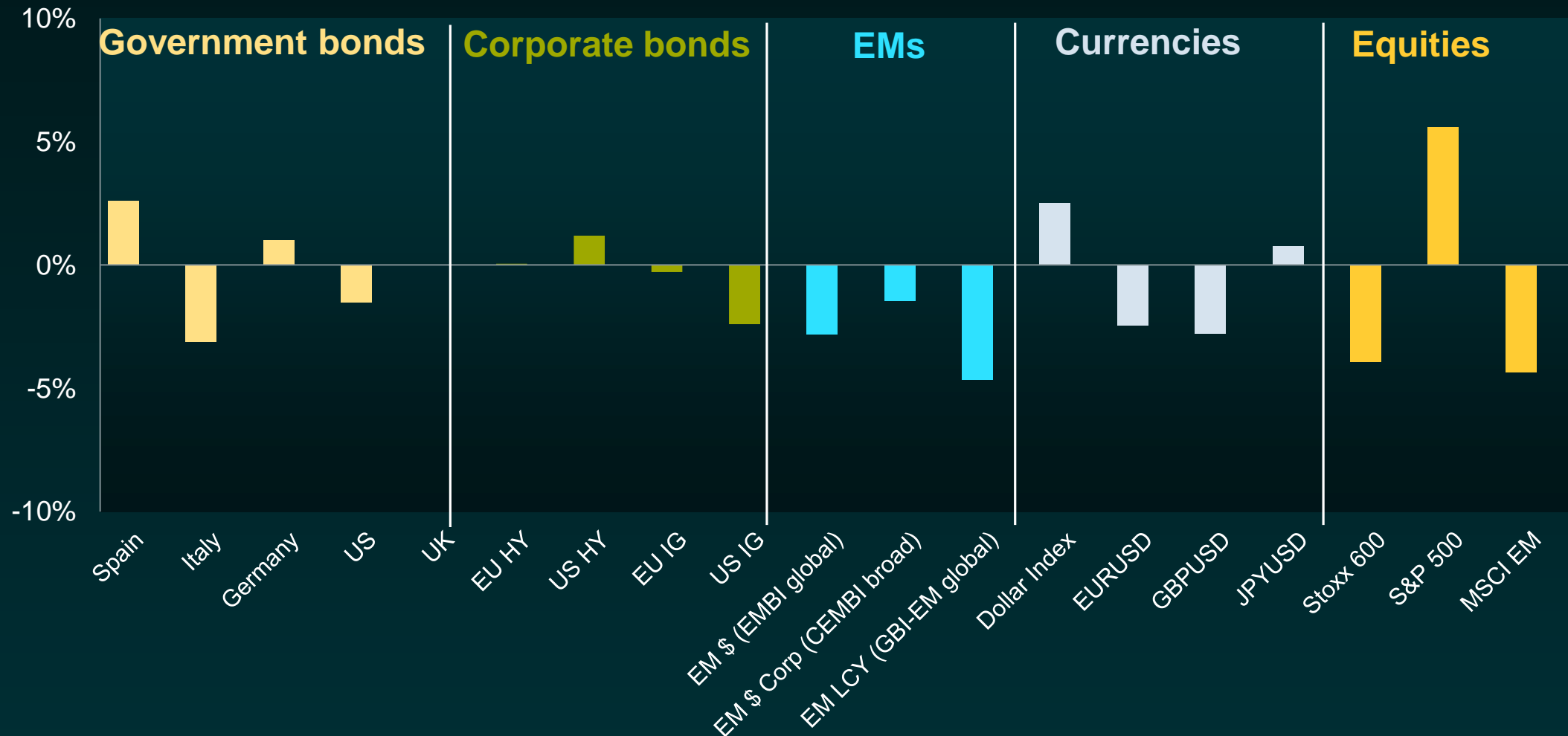
Monthly flow of G4 central bank assets purchases (MA)\*



\*Notes and assumptions: Data are 12m MA, assumptions. Fed will redeem maturing assets as per the announced cap during the September decision. ECB will cut buying to EUR 30 billion per month from January 2018 and eventually end the process by September 2018. BoE assumed not to begin reducing balance sheet in the medium term. BoJ's monthly purchase of JGBs assumed to be 8 trln Yen per month and is expected to continue purchases in the medium term.

# YTD 2018 Performance

9 months later markets have changed tack



Past performance is not a guide to future performance

Source: M&G, Bloomberg, Bank of America Merrill Lynch, JP Morgan, 31 August 2018

# Agenda

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2018 in review

**Challenges to the view**

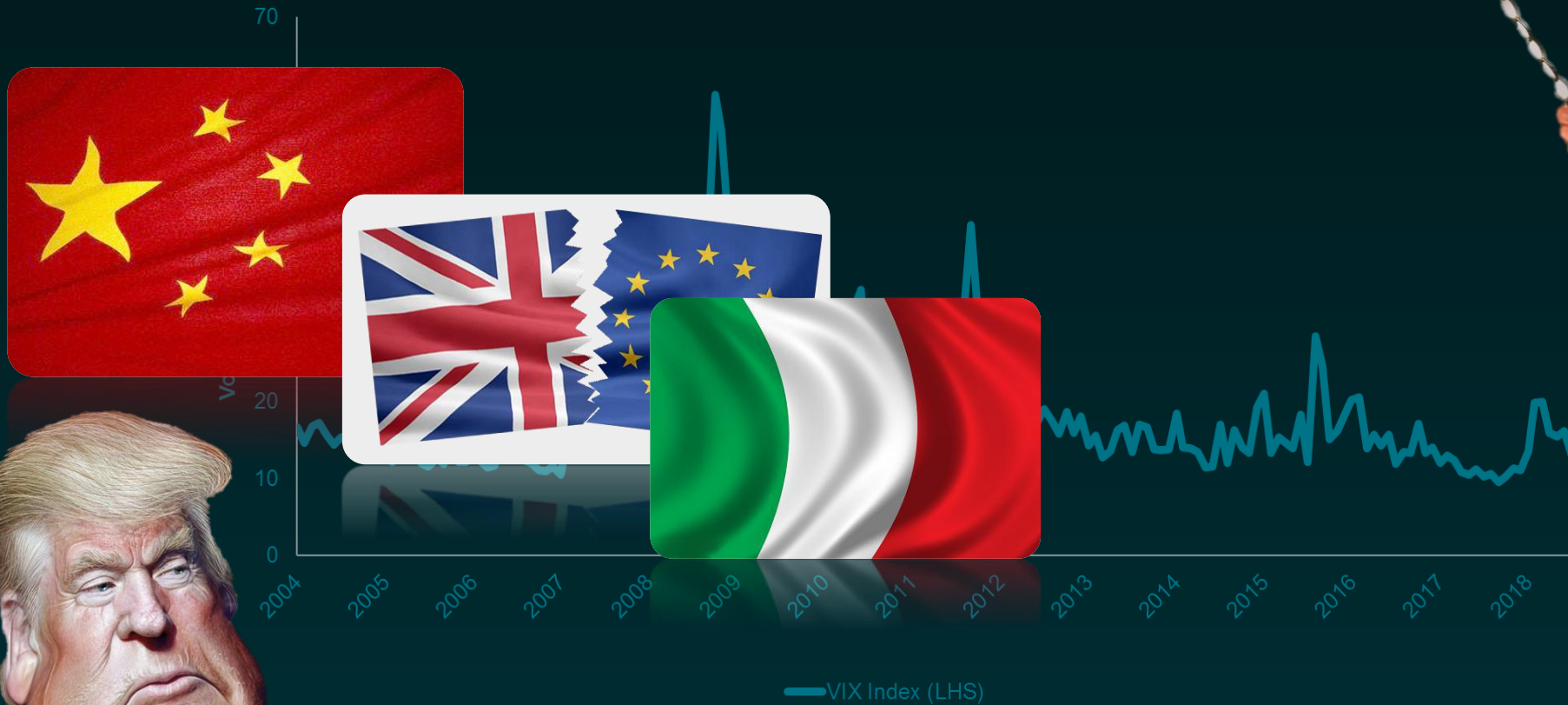
Where does that leave us?

M&G Optimal Income Fund and M&G Global Floating Rate High Yield Fund



# What events have challenged the views we held?

2018 has been largely a risk-off year with politics dominating markets



# Markets have watched the US curve flatten

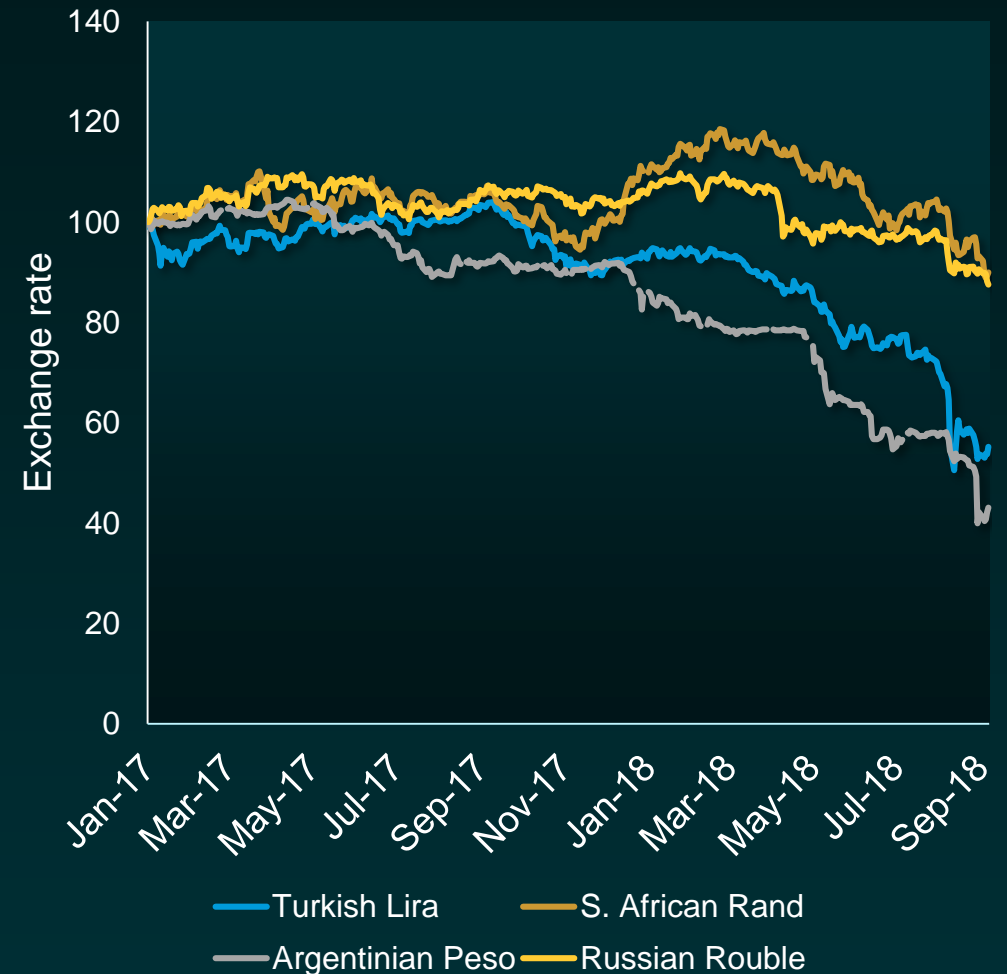
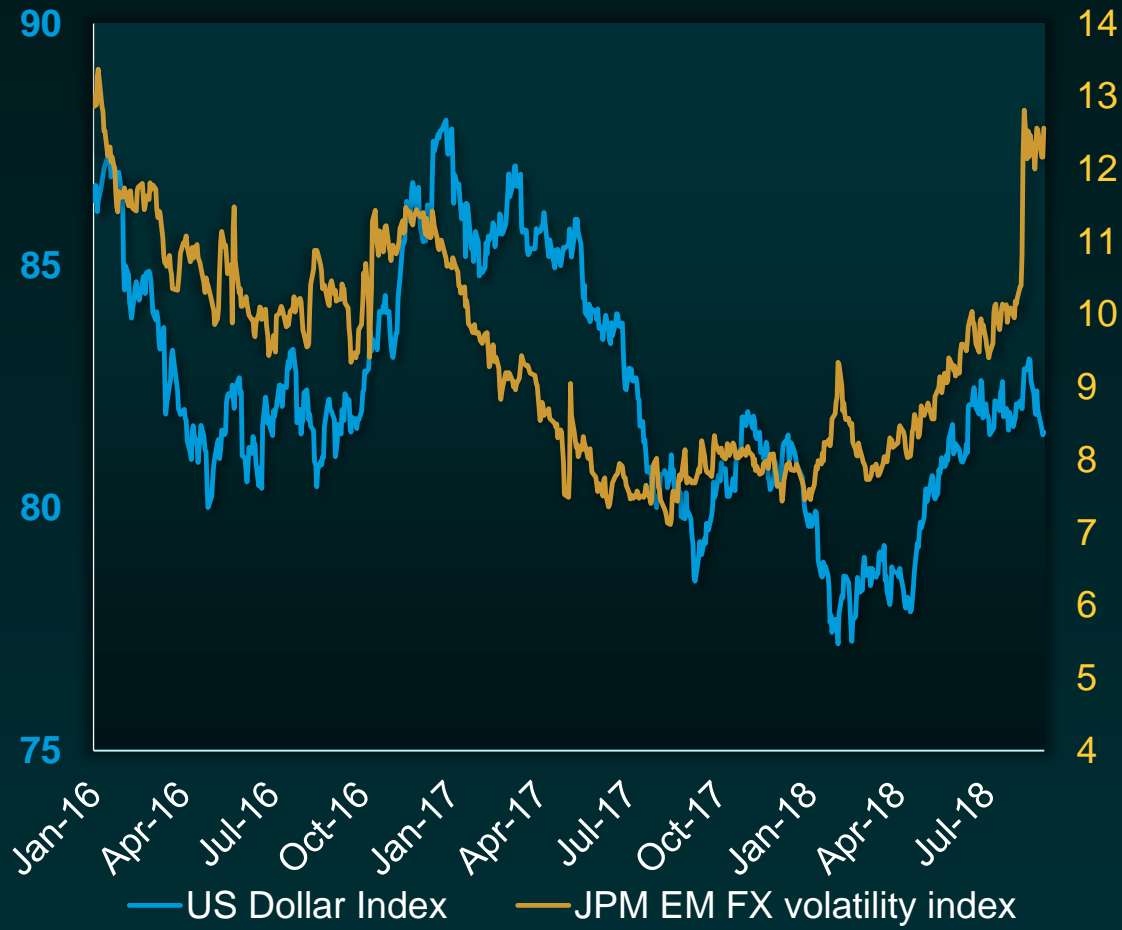
**Inversion has historically signalled recession, but we are not there yet**

US 10yr Govt bond – US 2yr Govt bond



# Is US Dollar strength the cause of EM weakness?

EM risks are contained to a few economies, at least for now



# Agenda

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2018 in review

Challenges to the view

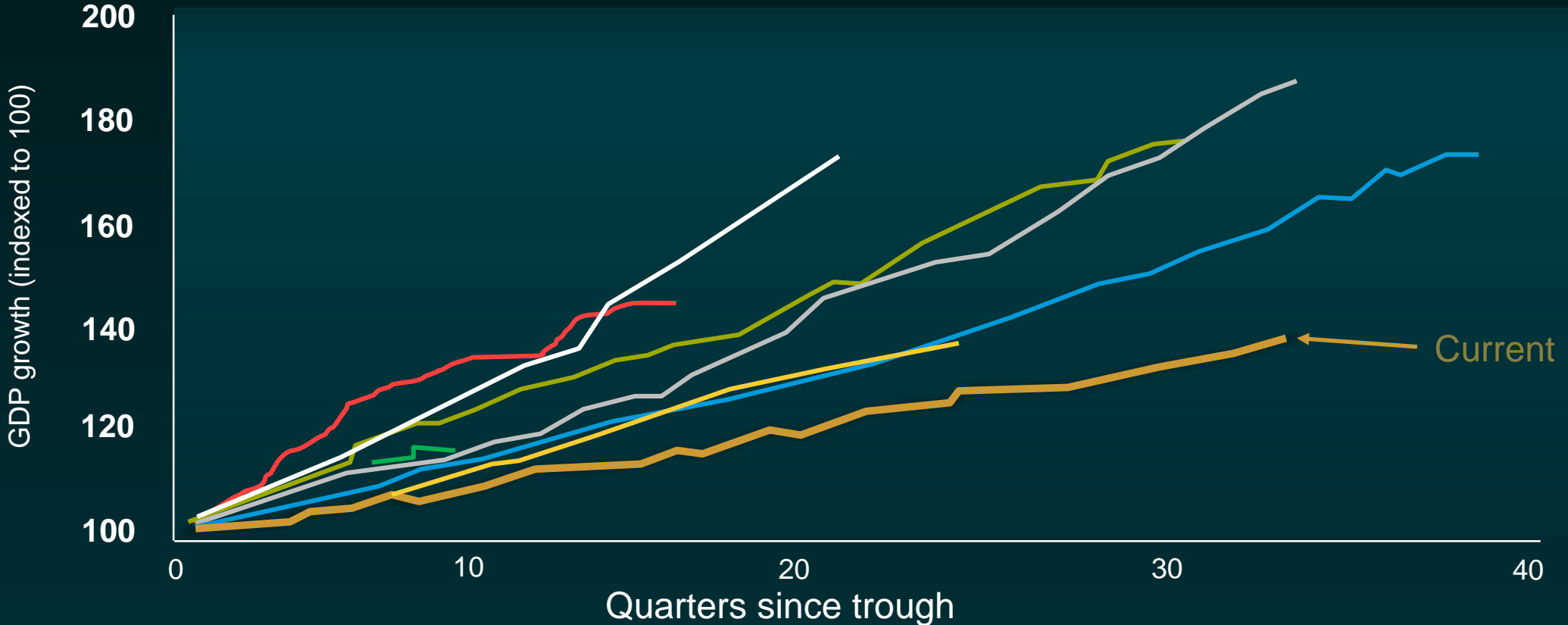
**Where does that leave us?**

M&G Optimal Income Fund and M&G Global Floating Rate High Yield Fund

# Global growth remains on an upward trajectory despite recent volatility

## Are we due a recession?

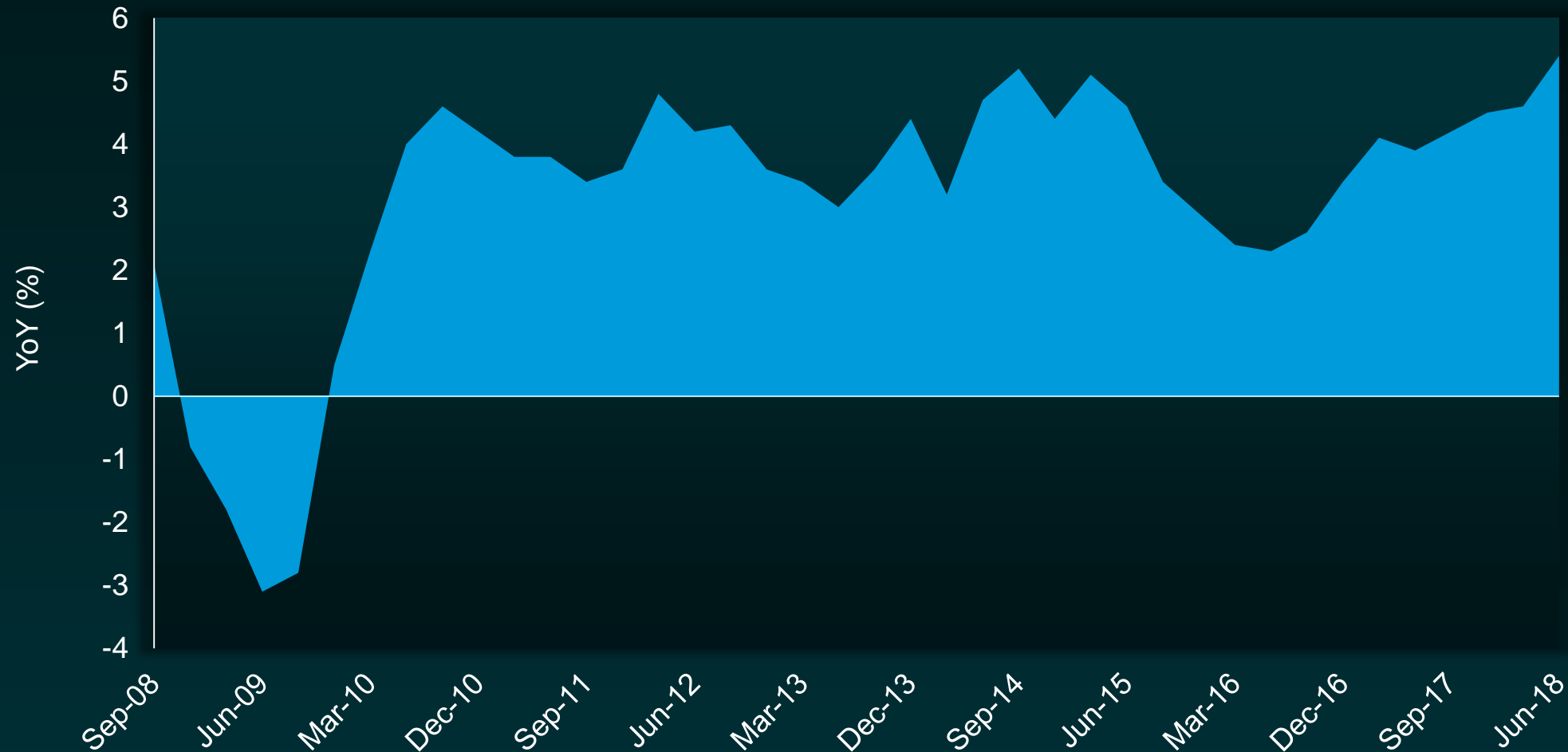
Cumulative GDP growth post-recessions



# US economy firing on all cylinders with economic activity accelerating

We see little evidence of economic weakness here

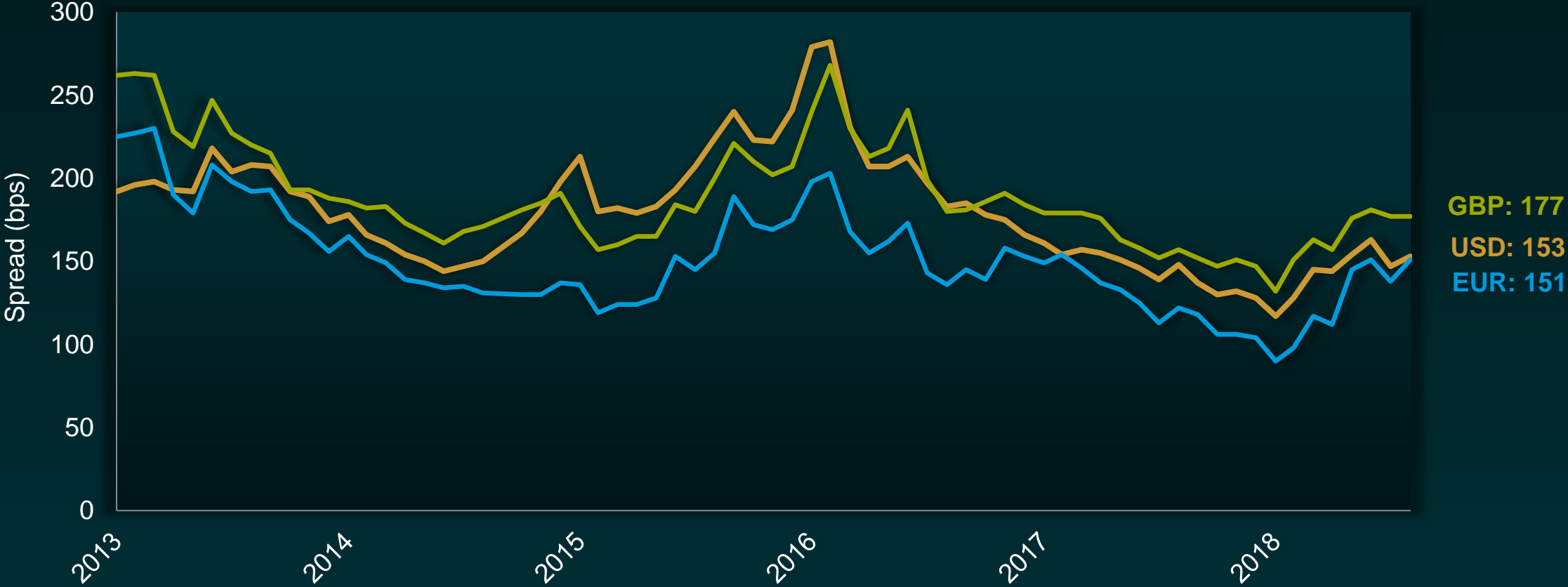
US nominal GDP



# Entry point appears better than it has for some time

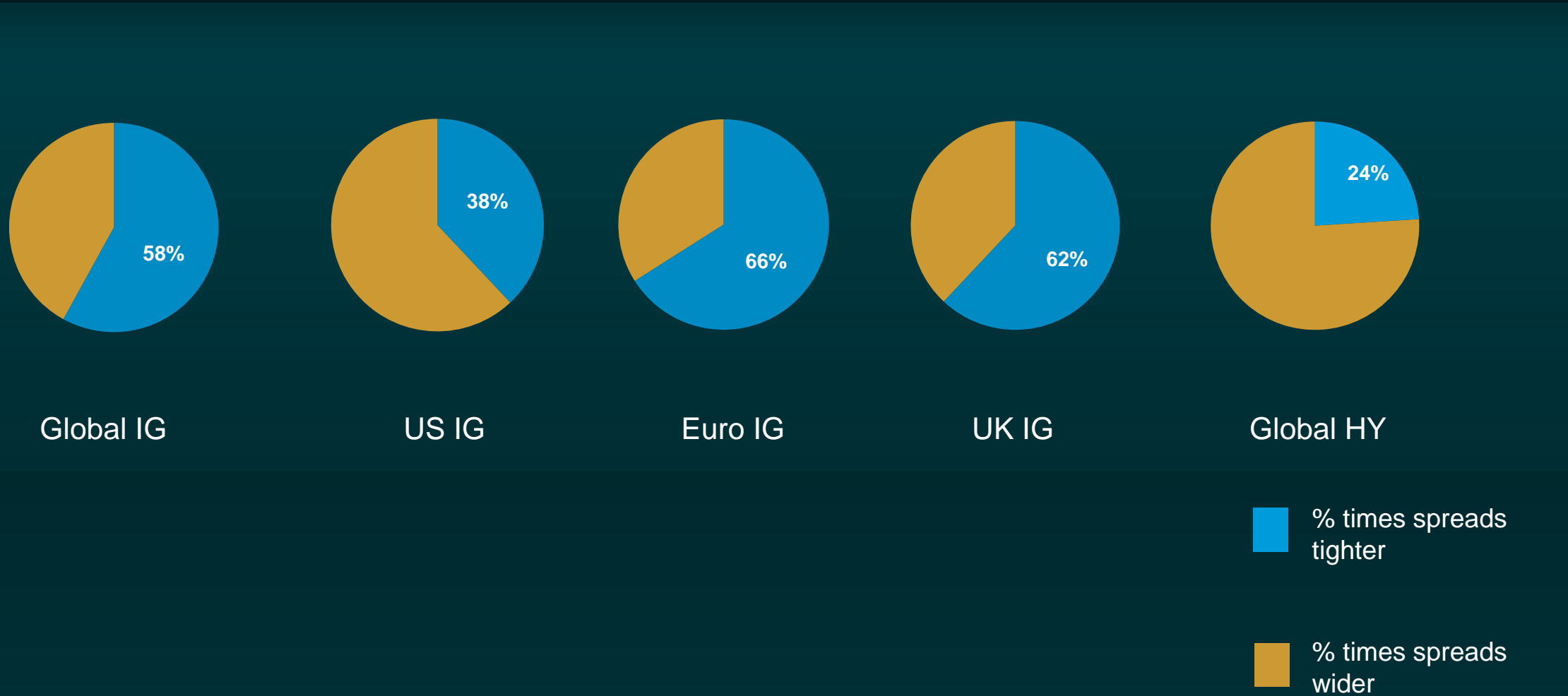
## BBB corporates

BBB corporate spreads over governments



# Valuations look more attractive following some recent repricing

**We believe spreads now offer a better entry point**





# Government bond markets have been a bit mixed

We see better value in US treasuries, although we think bunds remain expensive



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2018 in review

Challenges to the view

Where does that leave us?

**M&G Optimal Income Fund and M&G Global Floating Rate High Yield Fund**

# M&G Optimal Income Fund

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## Risks associated with this fund

The value of investments and the income from them will rise and fall. This will cause the fund price, as well as any income paid by the fund, to fall as well as rise. There is no guarantee the fund will achieve its objective, and you may not get back the amount you originally invested.

When interest rates rise, the value of the fund is likely to fall.

The value of the fund may fall if the issuer of a fixed income security held is unable to pay income payments or repay its debt (known as a default).

The fund may use derivatives to gain exposure to investments exceeding the value of the fund (leverage). This may cause greater changes in the fund's price and increase the risk of loss.

The fund may use derivatives with the aim of profiting from a rise or a fall in the value of an asset (for example, a company's bonds). However, if the asset's value varies in a different manner, the fund may incur a loss.

Changes in currency exchange rates will affect the value of your investment.

Where market conditions make it hard to sell the fund's investments at a fair price to meet customers' sale requests, we may temporarily suspend dealing in the fund's shares.

Some transactions the fund makes, such as placing cash on deposit, require the use of other financial institutions (for example, banks). If one of these institutions defaults on their obligations or becomes insolvent, the fund may incur a loss.

Wherever a reference or indication of past performance is shown, please note, past performance is not a guide to future performance.

## It is also important to note that:

The Fund allows for the extensive use of derivatives

# M&G Global Floating Rate High Yield Fund

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The fund invests mainly in one type of asset. This type of fund can experience larger-than-average price changes when compared to a fund which invests in a broader range of assets.

Changes in currency exchange rates will affect the value of your investment.

Hedged share classes aim to mirror the performance of another share class. We cannot guarantee that the hedging objective will be achieved. The hedging strategy will limit holders of the hedged share class from benefiting if the hedged share class currency falls against the US dollar.

The fund will invest in emerging markets which are generally smaller, more sensitive to economic and political factors, and where investments are less easily bought and sold. In exceptional circumstances, the fund may encounter difficulties when selling or collecting income from these investments, which could cause the fund to incur a loss. In extreme circumstances, it could lead to the temporary suspension of dealing in shares in the fund.

When interest rates rise, the value of the fund is likely to fall.

Where market conditions make it hard to sell the fund's investments at a fair price to meet customers' sale requests, we may temporarily suspend dealing in the fund's shares.

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The Fund allows for the extensive use of derivatives

# Fund facts

## M&G Optimal Income Fund

Fund name	M&G Optimal Income Fund
Fund manager:	Richard Woolnough
Deputy Fund Manager	Stefan Isaacs
Launch date (manager tenure):	December 2006 (since launch)
Fund size:	£23.8 billion
Investment objective:	The fund aims to provide a total return (the combination of income and growth of capital) to investors based on exposure to optimal income streams
YTM gross of ongoing charges	2.8%
Comparative sector:	IA £ Strategic Bond Sector
Valuation currency:	GBP
Fund structure:	UK OEIC – UCITS
Pricing/dealing frequency:	Daily



Ratings as at 30.06.2018. The Morningstar Overall Rating based on the fund's Sterling Class I shares. Copyright © 2018 Morningstar UK Limited. All Rights Reserved. The Morningstar Analyst Rating™. © 2017 Morningstar. All Rights Reserved. Neither Morningstar nor its content providers are responsible for any damages or losses arising from any use of this information. Ratings should not be taken as recommendation. FE Crown Fund Ratings based on the fund's Sterling I Acc shares. FE Crown Fund Ratings do no constitute investment advice offered by FE and should not be used as the sole basis for making any investment decision. All rights reserved.

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**Past performance is not a guide to future performance**

Source: M&G, 31 July 2018

# Calendar year performance in sterling

## M&G Optimal Income Fund

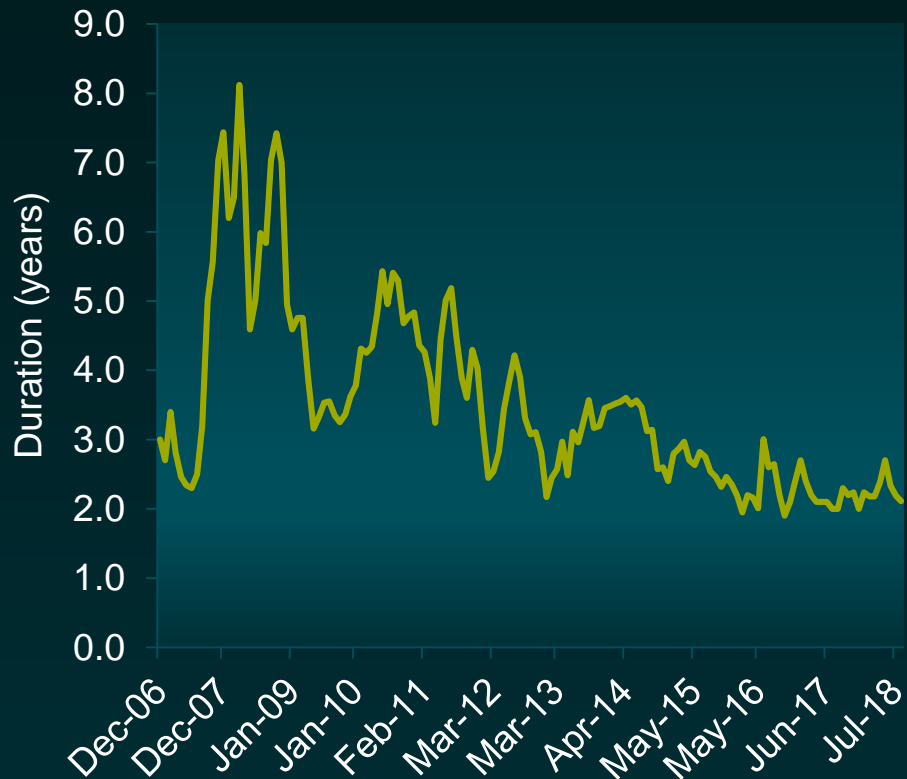
	YTD %	2017 %	2016 %	2015 %	2014 %	2013 %
M&G Optimal Income Fund	-1.1	5.8	8.1	-0.9	5.2	7.7
IA STER Strategic Bond sector average	-1.0	5.6	7.4	0.2	6.5	3.5

Past performance is not a guide to future performance.

# Duration evolution

## M&G Optimal Income Fund

### Duration movements



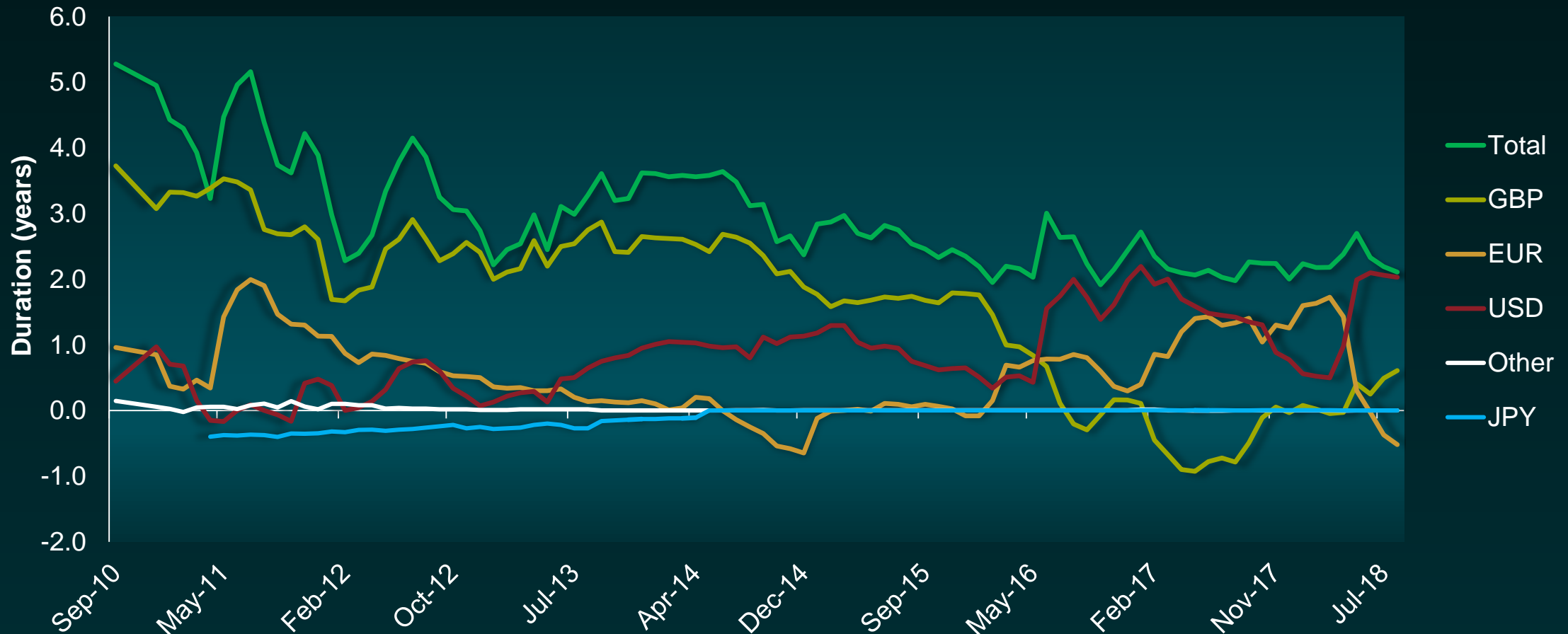
### Contribution to duration by currency



## Actively managing duration

# Duration contributions

## M&G Optimal Income Fund



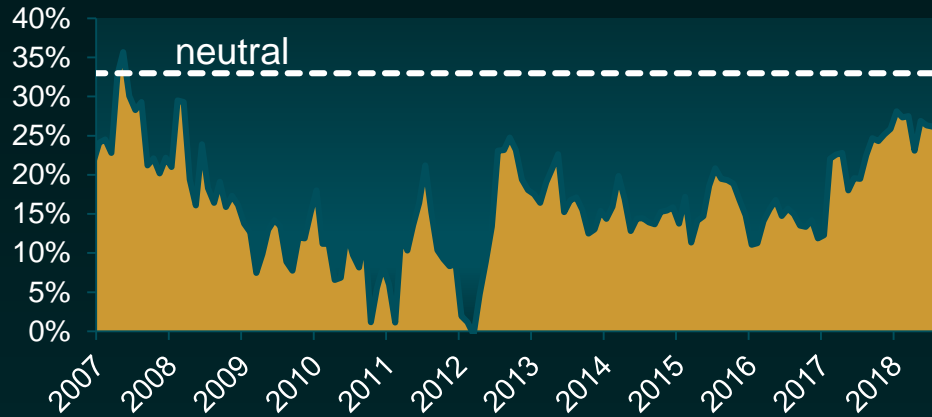
**Actively managing duration across markets**



# Asset allocation over time

## M&G Optimal Income Fund

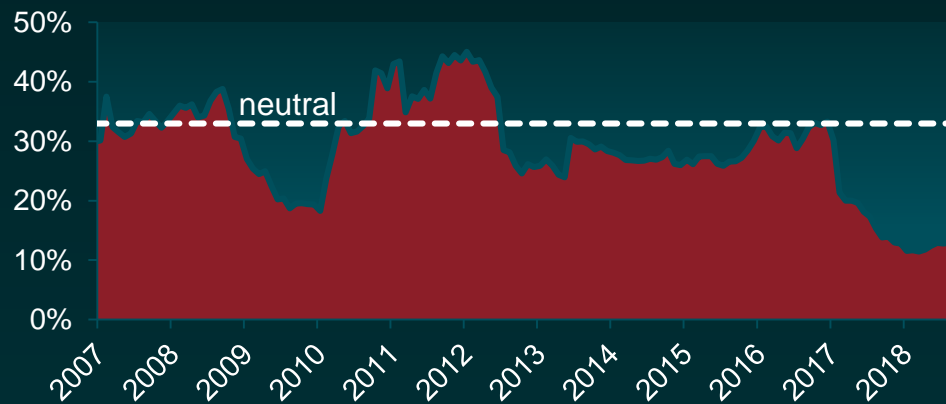
### Govt bonds (and cash)



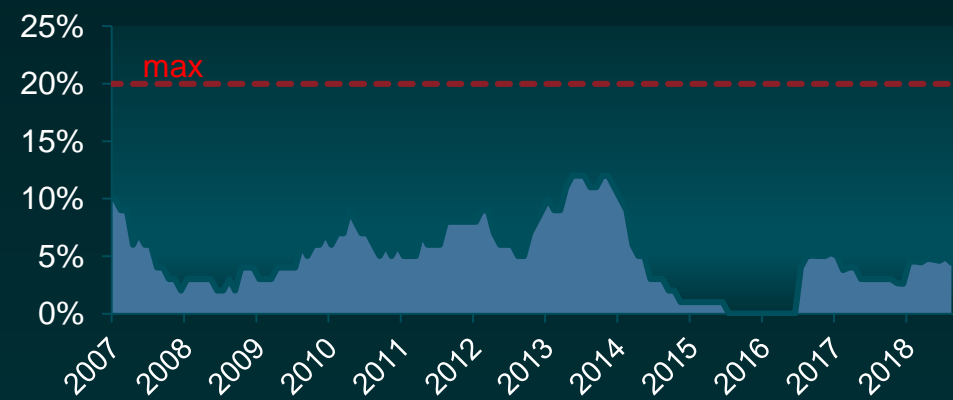
### IG corporate



### HY corporate



### Equity



# Average credit risk over time

## M&G Optimal Income Fund



# Fund facts

## M&G Global Floating Rate High Yield Fund

Fund name	M&G Global Floating Rate High Yield Fund
Fund manager:	James Tomlins
Deputy Fund Manager	Stefan Isaacs
Launch date (manager tenure):	September 2014 (since inception)
Fund size:	£3674 million
Investment objective:	The Fund is designed to maximise total return (the combination of income and growth of capital).
YTM gross of ongoing charges	5.29%
Comparative sector:	IA £ High Yield Bond
Valuation currency:	USD
Fund structure:	UK OEIC – UCITS
Pricing/dealing frequency:	Daily



Ratings as at 30.06.2018. The Morningstar Overall Rating based on the fund's Sterling Class I shares. Copyright © 2018 Morningstar UK Limited. All Rights Reserved. Neither Morningstar nor its content providers are responsible for any damages or losses arising from any use of this information.

**Ratings should not be taken as recommendation**

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# Calendar year performance in sterling

## M&G Global Floating Rate High Yield Fund

	YTD %	2017 %	2016 %	2015 %	2014 %	2013 %
M&G Global Floating Rate High Yield Fund	1.2	3.1	7.3	0.3	NA	NA
ICE BofAML Global Floating Rate High Yield 3% Constrained (GBP Hedged) Index*	1.3	3.6	12.1	-0.2	NA	NA

Past performance is not a guide to future performance

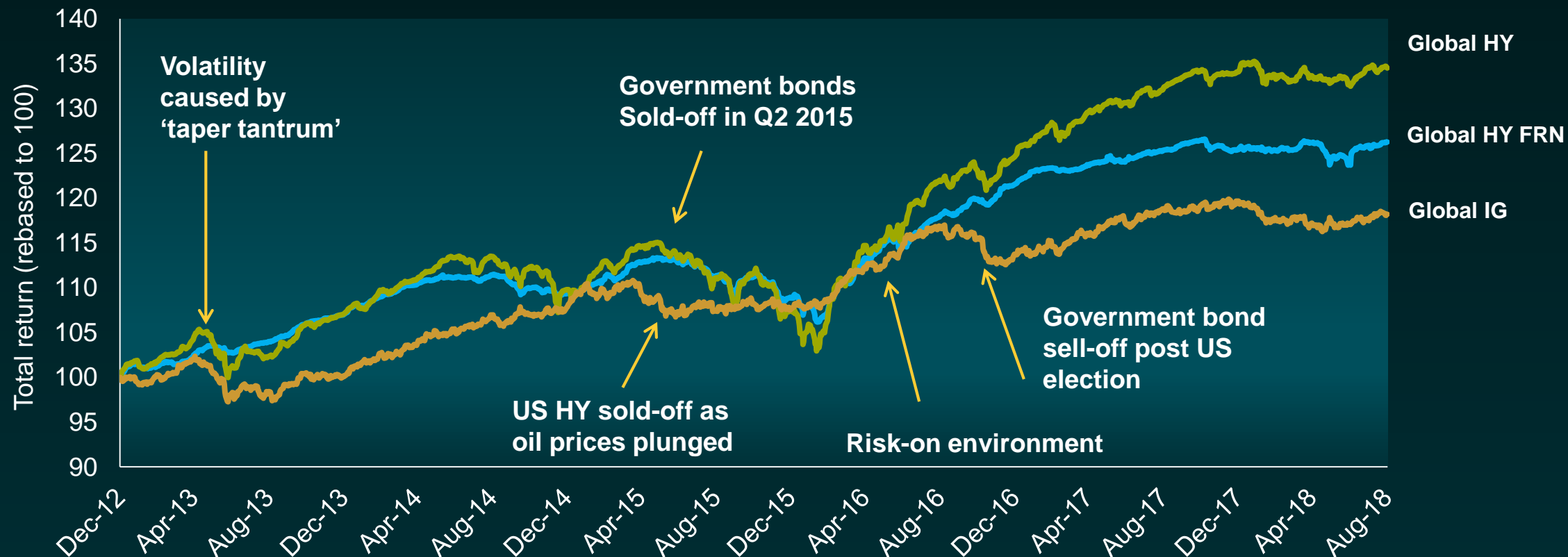
*Source: Morningstar Inc., UK database, 31 July 2018, sterling I-H share class, income reinvested, price to price. On 1 April 2016, the fund's performance comparator changed.*

*\*Past performance shown from 11 September 2014 to 31 March 2016 is the ICE BofAML Global Floating Rate High Yield (GBP Hedged) Index. Past performance shown from 1 April 2016 is the ICE BofAML Global Floating Rate High Yield 3% Constrained (GBP Hedged) Index*

# Comparing fixed income asset classes

High yield FRN has delivered lower volatility while generating income

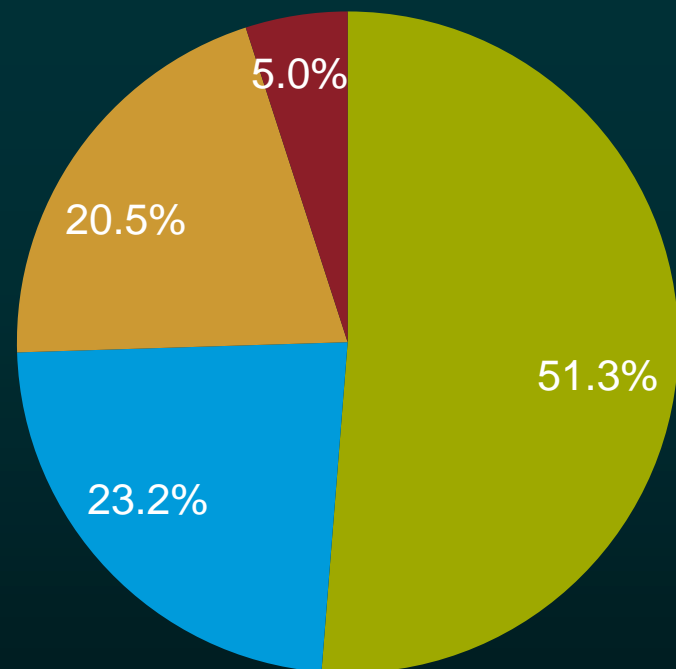
## Performance of global IG, global HY and global HY FRN



# Fund positioning

## M&G Global Floating Rate High Yield Fund

### Asset allocation



- Physical FRN
- Credit Default Swaps
- Fixed rate bonds + interest rate swaps
- Government Bonds and Cash

Spread duration:

3.5 years

Duration:

0.6 years

### Top 10 holdings – net of CDS collateral

1	CDX.NA.HY	18.90%
2	WIND TRE SPA	3.83%
3	PICARD GROUPE SAS	2.99%
4	REYNOLDS GROUP	2.88%
5	GARFUNKELUX HOLDCO 3 SA	2.70%
6	MATTERHORN TELECOM SA	2.24%
7	SYNLAB BONDCO PLC	2.22%
8	ITRX.XO	1.91%
9	ICELAND BONDCO PLC	1.88%
10	ARDAGH PACKAGING FINANCE PLC	1.62%

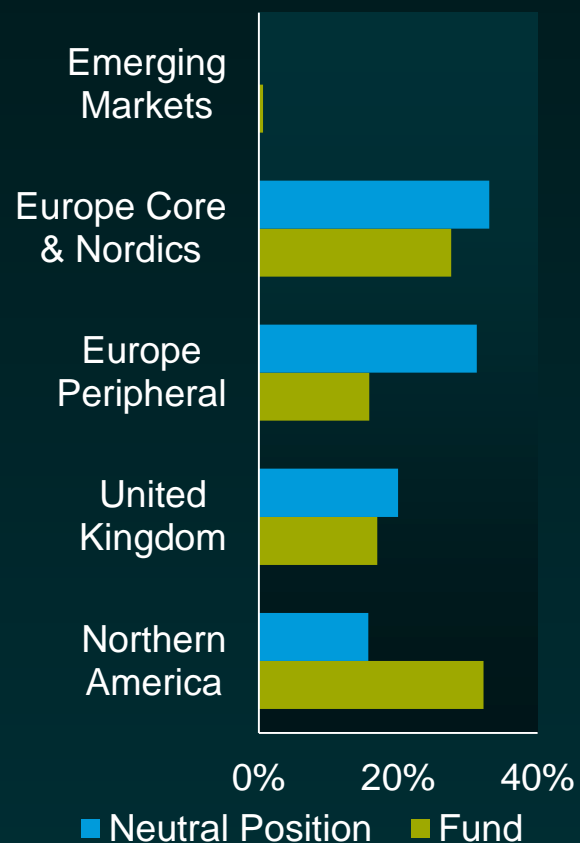
Source: M&G, 31 July 2018. Please note, portfolio data is based on internal sources, is unaudited and may differ from information as shown in the Monthly Fund Review.

\*Net using cash first as collateral

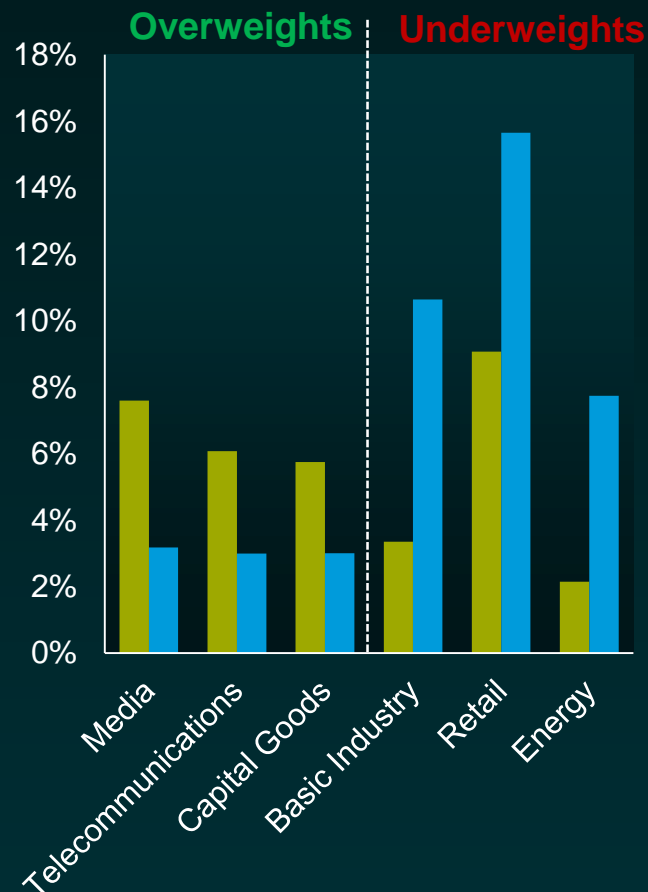
# Fund Positioning

## M&G Global Floating Rate High Yield Fund

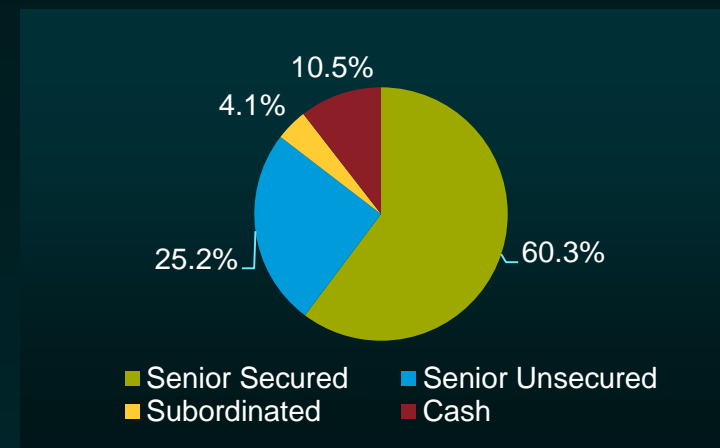
### By region



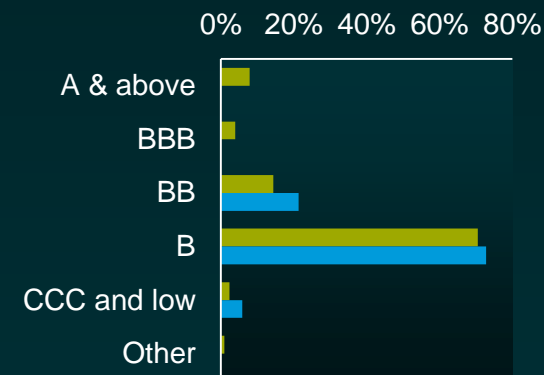
### By sector



### By financial tier



### By rating\*



Source: M&G, as of 31 July 2018. \*Includes derivative positions. Please note, portfolio data is based on internal sources, is unaudited and may differ from information as shown in the Monthly Fund Review

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# Q&A

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