SHINING A LIGHT ON……
M&G GLOBAL HIGH YIELD BONDS

At a glance

In this update we spoke to James Tomlins. James is the co-manager of the Global High Yield Bond Fund and Manager of the Global Floating Rate High Yield Bond Fund. The High Yield Bond Fund was launched in October 1998 and Floating Rate High Yield Bond Fund in September 2014. James has 10 years working with high yield bonds and 5 years' experience with M&G.

There is a lot of uncertainty in the bond market and in particular high yield and this makes investors nervous. There are two factors, firstly interest rates and how in a rising environment bond funds could return negatively, and secondly especially with high yield a creeping default rate. Despite these concerns investors continue to turn to bonds because of the low volatility compared to equities.

We started by talking about the market today. James explained that at the start of the year the markets were very volatile with big falls and then in mid-February there was a big snap back driven by the oil price rally and QE. What has been clear is that calling the right sector has been really important. Some might argue that holding energy stocks would have benefited investors especially with the snap back came however the sector is still down 20% over twelve months, so even with the rise it hasn't captured all the loses.

If we take this a step further the default rates globally have been increasing and are now at 4.3%, however energy is at 15.9%. Taking out commodities the default rate drops to 2.3%. This further highlights the need to be selective.

James added that regionally there are dispersions on yield with Europe seen as a safe haven with yields around 4% but elsewhere global yields are at over 6% as are US yields.

With the need to be selective James added that this has happened before with the tech bubble. Between 1999 and 2002 high yield defaults peaked at over 10% and much of this was driven by the tech sector. However, investing in the sector as a whole between January 2001 and October 2004 would have returned 45%, if you took out the telco sector the return was 60%.

It is no different today, James feels it is about avoiding the energy sector and that sector positioning will drive returns. Getting this right he feels will deliver double digit returns over the medium term.

Talking in general terms James added that there is some exposure in the funds to energy but it is small and selective. We discussed defaults on holdings and he explained that the sector average is 13.51% whereas the fund is 4.92%. In 2015 there were 89 defaults and the fund suffered 3, and 2014 it was 51 and the fund suffered 2.

Talking about the differences between the funds the Global High Yield Fund has a greater exposure to the US and is overweight Banking, Media and Capital Goods. It is underweight Energy, Basic Industry and Utilities. The Floating Rate Fund is more diversified geographically between the US, UK and Europe. It is overweight Telecommunications, Media, Financial Services and underweight Banking, Energy and Healthcare. The Floating Rate Fund has lower volatility which ensures it provides downside protection but on the flipside doesn't fully participate in any upside.

The High Yield Fund carries interest rate risk with duration at 3.4% whereas and Floating Rate Fund carries no interest rate risk with zero duration. The yield on the High Yield Fund is slightly higher at 5.85% whereas on the Floating Rate Fund it is 5.22%.

In summary these are well managed funds. The Floating Rate Fund has a shorter track record and this may deter investors. However, in its first full year in 2015 it displayed its ability to protect on the downside, and then in 2016 (to date) it hasn't full participated in the upside (effectively doing what it says it sets out to do). The Global High Yield Bond has a longer tracker record but we have just shown since the launch of the ETF index in 2012 to provide a comparison for potential investors. Over 1 and 3 years and since 2012 it has demonstrated its ability to outperform the index. High yield bonds carry great risk because the higher yield is paid as there is deemed a greater risk of default, investors need to be aware of this risk and be happy to take this. If they are, then these funds may be something to consider.

Fund performance

Global High Yield Fund

Performance from launch of ETF benchmark (15 November 2012) to 23 May 2016:

	2012	**2013**	**2014**	**2015**	**2016**
M&G Global High Yield Bond Fund	2.76%	8.86%	1.87%	-1.58%	4.73%
iShares Global High Yield Corporate Bond ETF	2.28%	0.71%	-0.42%	-6.43%	5.15%

12 months, 3 years and since launch of ETF:

	1 Year	**3 Years**	**Since launch of ETF**
M&G Global High Yield Bond Fund	-1.01%	8.85%	17.19%
iShares Global High Yield Corporate Bond ETF	0.51%	-10.14%	0.93%

Global Floating Rate High Yield Fund

Performance from launch (11 September 2014) to 23 May 2016:

	2014	**2015**	**2016**
M&G Global Floating Rate High Yield Bond Fund	-0.72%	1.06%	2.20%
M&G Global High Yield Bond Fund	-1.58%	-1.58%	4.73%
iShares Global High Yield Corporate Bond ETF	-0.42%	-6.43%	5.15%

12 months, and since launch

	1 Year	**Since launch**
M&G Global Floating Rate High Yield Bond Fund	-0.49%	2.70%
M&G Global High Yield Bond Fund	-1.01%	1.64%
iShares Global High Yield Corporate Bond ETF	0.51%	-1.02%

You should note that past performance is not a reliable indicator of future returns and the value of your investments can fall as well as rise. The total return reflects performance without sales charges or the effects of taxation, but is adjusted to reflect all on-going fund expenses and assumes reinvestment of dividends and capital gains. If adjusted for sales charges and the effects of taxation, the performance quoted would be reduced.

The source of information in this note has been provided by M&G and is correct as at May 2016. These are notes from meeting the fund manager or representative and should not be seen as a recommendation to purchase any fund mentioned. Any reference to shares is not a recommendation to buy or sell. Should you wish to make a decision based on these notes we cannot take responsibility for this and you should carry out your own research before making a decision. You should note that past performance is not a reliable indicator of future returns and the value of your investments can fall as well rise.