

# Asset class insight: Fixed Income

An in-depth review of the Fixed Income investments held in PruFund. These reviews are updated every six months with the latest details available at the time of publishing.

## Introduction

This update from the M&G Treasury & Investment Office (T&IO) provides an insight into the characteristics of the fixed income portfolios within the PruFund range of funds.

This update covers the standard rather than Planet versions of PruFund.

We hope to highlight the key differentiators and strengths including;

- The global exposure
- The ability to adapt modelling to include new asset classes in public and private markets
- Creating segregated pools of assets or internal funds to best capture opportunities
- Use of well-resourced and skilled asset managers to put money into markets

Detail is provided on exposure across different areas of fixed income markets and the building blocks that make up the overall allocations. Information is also provided on M&G Investments that T&IO work with to create, manage and monitor many of the underlying building blocks.

## Characteristics of Fixed Income portfolios within the PruFund range of funds

- Globally diversified with new asset classes added as markets have evolved and our strategists have been able to adjust modelling and create new sleeves within the strategic asset allocation process
  - with relatively little exposure to developed market government bonds
  - reduced exposure to developed market corporate bonds over recent years although still the largest holding in % terms
  - exposure to higher yielding Asian and Emerging Market bonds has increased
  - exposure to Private Credit has increased leveraging the strength of specialist teams in M&G. Will continue to grow through new and future investments via M&G Catalyst, for example
- Underlying mandates and funds are actively managed by experienced teams in M&G Investments
- Fully hedged against movements in the major currencies
  - Sensible practice as currency movement can demonstrably affect risk adjusted returns

- A large percentage of assets held in segregated mandates/internal vehicles\* which has several benefits;
- Underlying fund managers work solely with T&IO as no other retail or institutional investors
- T&IO can work with the managers to set investment objectives and appropriate risk controls like stock and sector limits
- An underlying fund manager is unlikely to be a forced seller of assets
- Close and collaborative working relationships are formed with fund managers which provides market insights and new investment ideas
- The ability to create appropriate benchmarks and weights can help avoid a structural overweight to certain markets and help ensure money is allocated efficiently over time in less liquid markets
- Mandates can be adjusted as markets change and new ones evolve or if the broader macro environment changes such that overall portfolio duration can be adjusted, for example
- T&IO will seek to ensure that ongoing fund management costs are competitive

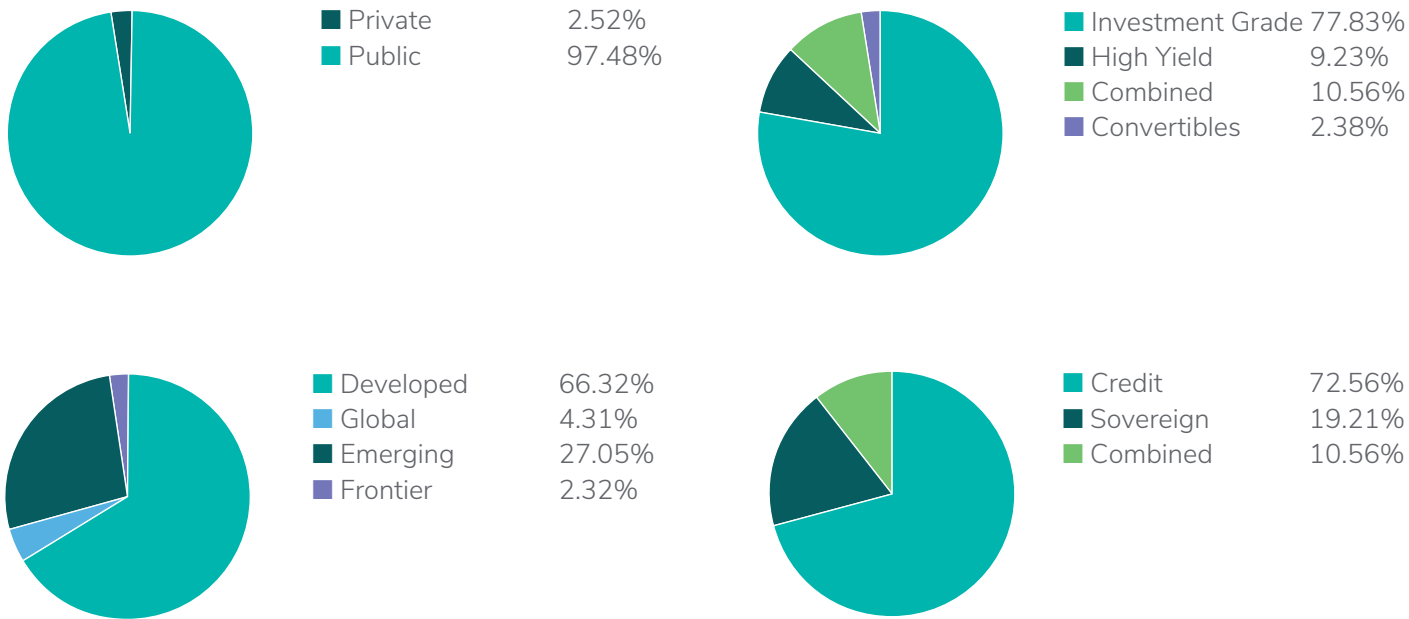
\* Some pooled vehicles are used – M&G Emerging Market Debt for example

- Geographic diversification and alternative sources of credit premium, different risk/return profiles and duration includes areas like;
  - **Asian bonds** – access to investment grade and sovereign debt with a higher potential yield
  - **Bridge loans** – generally investment grade, short duration bonds sourced in private markets that offer a higher return than an equivalent publicly traded bond
  - **Private credit** – now with a greater focus now on driving 'Impact and positive change in the global economy through investment innovation' through 'M&G Catalyst'
  - **High yield bonds** – positive credit spreads and often shorter duration
  - **Emerging markets debt** – higher yields and exposure to a diversified set of monetary and fiscal regimes

These more specialist asset classes now make up a meaningful part of PruFund portfolios as shown on the next page;

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Portfolio breakdown of PruFund Growth (source: T&IO, 30 June 2023)



\* Please note that these weightings are based on the predominate exposures of each underlying fund. The actual allocations can differ slightly from what is shown above due to the underlying managers having some mandate flexibility

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## Underlying building blocks of the PruFund Growth Fixed Income portfolio\*

To provide greater insight into PruFund portfolios the table below provides a breakdown of each sub asset class, the underlying vehicles and the asset manager.

Asset class	Mandate	Fund Name	Investment Style	Internally or Externally managed
UK (Investment Grade)	4 x segregated mandates 1 x bespoke mandate	M&G UK Investment Grade Mandate	Active	Internal
Europe (Investment Grade)		M&G European Investment Grade Mandate	Active	Internal
		M&G Collateral Fixed Income Mandate	Active	Internal
UK & Euro (High Yield)		M&G European/UK High Yield Mandate	Active	Internal
		M&G European Leveraged Loans Mandate	Active	Internal
UK Government**		M&G Gilt Mandate	Active	Internal
US (IG & HY)	3 x segregated mandates	M&G US Total Return Fixed Income Mandate	Active	Internal
US Treasury		M&G US Short Dated Fixed Income Mandate	Active	Internal
		M&G US Treasuries Mandate	Active	Internal
Asian Fixed Income	3 x pooled funds	M&G (Lux) Asian Corporate Bond Fund	Active	Internal
		M&G (Lux) Asian Local Bond Fund	Active	External
		ESI China Bond Fund	Active	External
Convertibles	1 x segregated mandate	M&G Global Convertibles Fund	Active	Internal
Lower Risk Private Credit	1 x bespoke mandate 1 x segregated mandate	M&G Catalyst – Credit Fund	Active	Internal
		Selection of M&G Private Credit Funds	Active	Internal
Global High Yield	1 x pooled fund	M&G Global High Yield Fund	Active	Internal
African Debt	1 x pooled fund	M&G Pan-African Bond Fund	Active	Internal
Emerging Market Debt	1 x pooled fund	M&G Emerging Market Debt Fund	Active	Internal

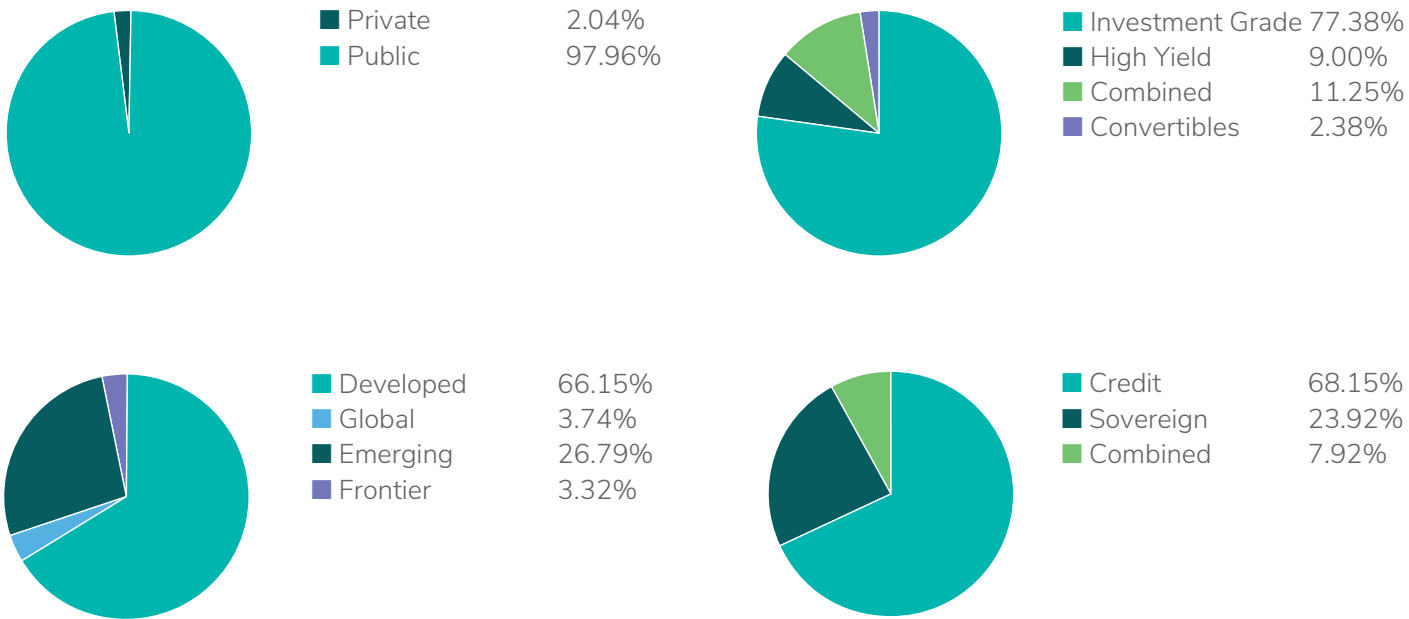
Source: T&IO as at 30.06.2023

\* The same building blocks are used across the entire PruFund range

\*\* For the 2023 PruFund Strategic Asset Allocation review, UK Government Bonds were added as allocations with PruFund Growth

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Portfolio breakdown of PruFund Cautious (source: T&IO, 30 June 2023)



\* Please note that these weightings are based on the predominate exposures of each underlying fund. The actual allocations can differ slightly from what is shown above due to the underlying managers having some mandate flexibility.

## Underlying building blocks of the PruFund Cautious Fixed Income portfolio\*

To provide greater insight into PruFund portfolios the table below provides a breakdown of each sub asset class, the underlying vehicles and the asset manager.

Asset class	Mandate	Fund Name	Investment Style	Internally or Externally managed
UK (Investment Grade)	4 x segregated mandates  1 x bespoke mandate	M&G UK Investment Grade Mandate	Active	Internal
Europe (Investment Grade)		M&G European Investment Grade Mandate	Active	Internal
UK & Euro (High Yield)		M&G Collateral Fixed Income Mandate	Active	Internal
		M&G European/UK High Yield Mandate	Active	Internal
European Leveraged Loans		M&G European Leveraged Loans Mandate	Active	Internal
UK Government**		M&G Gilt Mandate	Active	Internal
US (IG & HY)	3 x segregated mandates	M&G US Total Return Fixed Income Mandate	Active	Internal
US Treasury		M&G US Short Dated Fixed Income Mandate	Active	Internal
		M&G US Treasuries Mandate	Active	Internal
Asian Fixed Income	4 x pooled funds	M&G (Lux) Asian Corporate Bond Fund M&G (Lux) Asian Local Bond Fund ESI China Bond Fund	Active Active Active Active	External External External External
Convertibles	1 x pooled fund	M&G Global Convertibles Fund	Active	Internal
Lower Risk Private Credit	1 x bespoke mandate 1 x segregated mandate	M&G Catalyst – Lower Risk Selection of M&G Private Credit Funds	Active Active	Internal Internal
Global High Yield	1 x pooled fund	M&G Global High Yield Fund	Active	Internal
African Debt	1 x pooled fund	M&G South Africa Pan-African Bond Fund	Active	Internal
Emerging Market Debt	1 x pooled fund	M&G Emerging Market Debt Fund	Active	Internal

\* Source: T&IO as at 30.06.2023

\*\* For the 2023 PruFund Strategic Asset Allocation review, UK Government Bonds were added as allocations with PruFund Cautious

## Underlying Fixed Income managers for PruFund

T&IO is responsible for the strategic asset allocation of the PruFund range of funds as well as the selection and ongoing monitoring of the various investment managers. The underlying stock selection decisions are carried out by these investment managers who are selected by T&IO following a thorough due diligence process.

### M&G Investments

T&IO work very closely with M&G Investments who run most of the fixed income assets for PruFunds.

They are one of Europe's largest fixed interest investors and have a large established team of investment professionals that aim to deliver performance over the long-term across global government bonds, investment grade and high yield corporate debt.

As well as huge experience in public markets the institutional team also has a long heritage in private markets.

If you want to read more on M&G's thought leadership from their own fixed income investment specialists, visit their '**Bond Vigilantes**' page.

## Spotlight on Catalyst – Investment Example

Catalyst is a mandate within Private Credit, providing long-term flexible capital to companies with positive purposes at their core and delivering impact at scale.

### Green Norwegian Ferries

PruFund has gained exposure into the shipping and transportation sector via private senior secured debt investment by the Catalyst Mandate. Green Norwegian Ferries is Norway's biggest ferry operator that connects coastal communities and businesses. The company is leading the shift to zero emission ferry connections with around ~40% of its fleet being hybrid-electric. With further green ferries joining its fleet in the next couple of years, the company expects to have abated over 250,000 tonnes of CO<sub>2</sub>e since 2018.

The deal strengthens the company's balance sheet and strongly positions it to defend existing routes and bid for new tenders.

## Summary

Within the fixed income exposure of the PruFund range of funds, Developed market corporate bonds remain the largest holdings but in recent months and years T&IO have continued a two-pronged shift away from them in order to capture more differentiated sources of return that they believe will benefit portfolios in the future;

- By investing in more emerging market debt with higher yields and exposure to a diversified set of monetary and fiscal regimes, with more room to stimulate their economies,
- Accessing the credit and illiquidity premia available within private credit
- Have a globally diversified portfolio that offers multiple asset types with different characteristics, duration and risk/return profiles
- Utilise well-resourced and skilled active fixed income managers
- Source new and differentiated sub-asset classes
- Take a long-term view and see market downturns as an opportunity to acquire assets at compelling valuations

T&IO continue to believe the fixed income allocations within PruFunds are well-diversified and are continually evolving. They also feel that the fundamental, valuation and technical analysis carried out across the whole of M&G from both a top-down perspective and bottom-up stock level will continue to help capture market opportunities across a long-term investment horizon.

- As part of the 2023 PruFund Strategic Asset Allocation Review, UK Government Bonds were added within fixed income, due to much improved yields compared to any period in the last decade.

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