

Annual Short Report May 2013
For the year ended 31 March 2013

M&G UK Inflation Linked Corporate Bond Fund

a sub-fund of M&G Investment Funds (10)

How to contact us



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* For security purposes and to improve the quality of our service, we may record and monitor telephone calls. You will require your M&G client reference. Failure to provide this will affect your ability to transact with us.

** Please remember to quote your name and M&G client reference and sign any written communication to M&G. Failure to provide this may affect your ability to transact with us.

† Please note that information contained within an email cannot be guaranteed as secure. We advise that you do not include any sensitive information when corresponding with M&G in this way.

AUTHORISED CORPORATE DIRECTOR'S REPORT

Investment objective of the M&G UK Inflation Linked Corporate Bond Fund

The Fund aims to protect the value of capital and income from inflation by generating a return consistent with or greater than UK inflation over the medium to long term.

Investment policy of the M&G UK Inflation Linked Corporate Bond Fund

The fund invests mainly in investment grade corporate bonds, including inflation-linked corporate bonds, floating rate notes (including asset backed securities) and other fixed income instruments (including bonds not linked to inflation). Derivatives may be used in pursuit of the fund objective and for efficient portfolio management purposes. Corporate bond exposure may be achieved either directly or by investing in a combination of assets, including government securities and credit derivatives. Inflation strategies may, at times, result in a return profile different to that of corporate bonds not linked to inflation. If deemed appropriate by the investment manager, the associated currency risks may be hedged.

The fund may also invest in other assets including collective investment schemes, other transferable securities and debt instruments (including high yield debt, convertible and preference stocks), cash and near cash, deposits, warrants and money market instruments.

Investment approach

The M&G UK Inflation Linked Corporate Bond Fund invests in a range of fixed interest securities that should perform well when inflation is high or rising. The fund will be mainly exposed to investment grade credit but can also invest in inflation-linked government bonds, floating rate notes (FRNs), senior secured loans, conventional corporate and government bonds, cash and derivatives such as credit default swaps (CDS). The fund managers may also form assets out of a combination of government bonds and derivatives, whose returns behave in a similar way to inflation-linked corporate bonds. The aim of the fund is to provide returns that are consistent with or exceed inflation, as measured by the Consumer Prices Index (CPI) over the medium to long term.

Risk and reward profile*



- The above risk number is based on the rate at which the value of the Fund has moved up and down in the past.
- This risk number is based on simulated historical data and may not be a reliable indicator of the future risk profile of the Fund.
- The risk number shown is not guaranteed and may change over time.
- The lowest risk number does not mean risk free.

The Fund has the above risk number because of the effect of the following risks:

- The value of stockmarket investments, and the income from them, will fluctuate. This will cause the Fund price to fall as well as rise and you may not get back the original amount you invested.
- Any investment in international companies means that currency exchange rate fluctuations will have an impact on the Fund.
- **Derivatives** – The Fund may use derivatives for the purposes of meeting the Fund's objective, and protecting the capital value from risk. We anticipate that the use of derivatives will not materially alter the risk profile of the Fund or increase price fluctuations, in comparison to equivalent funds that cannot invest in derivatives.

The Fund may take short positions through the use of derivatives which are not backed by equivalent physical assets. Short positions reflect an investment view that the price of the underlying asset is expected to fall in value. Accordingly, if this view is incorrect and the asset rises in value, the short position could involve greater risk due to the theoretical possibility of an unlimited rise in its value.

Some derivative transactions may be entered into directly with an eligible person or institution (a "counterparty"). There is a risk that the counterparty may not meet its obligations or becomes insolvent which could cause the Fund to incur a loss.

- **Fixed income securities** – The fund manager may use derivatives with the aim of producing a capital gain if interest rates rise. Normally, if interest rates increase, the capital value of fixed income securities will fall. However, if the fund manager's view is incorrect and interest rates fall, the Fund will experience a loss.

The value of the Fund will fall if the issuer of a fixed income security held is unable to pay income payments or repay its debt (known as a default). A default, expected default, or downgrading will make a fixed income security harder to sell as its value and income are likely to fall. Fixed income securities that pay a higher level of income usually have a lower credit rating because of the increased risk of default. The higher the rating the less likely it is that the issuer will default, but ratings are subject to change.

- The Fund invests mainly in one geographic region or country. It is therefore more vulnerable to the market sentiment of that specific geographic region or country. This type of fund can carry a higher risk and can experience larger than average price fluctuations when compared to a fund with a broader investment universe.
 - In low or zero inflation conditions there is a risk that the Fund's expenses may exceed the income earned. Should this occur any shortfall will be taken from the Fund's capital, there will be no income and the capital growth will be reduced.
 - This Fund is subject to effective yield accounting which means that a proportion of the capital inflation protection will be distributed to the holders of income shares. As a result, income shareholders will, in effect, be withdrawing part of the capital protection element.
- * Please note that this 'Risk and reward profile' section is based on Sterling Class 'A' shares, the nominated share class.

INVESTMENT ACTIVITIES OVER THE REPORT PERIOD

As at 2 April 2013, for the year ended 31 March 2013

In May 2012, we increased the fund's duration (a measurement of the fund's sensitivity to changes in bond prices) based on our view that the economic situation in the eurozone was likely to deteriorate. However, as investor sentiment improved in the second half of the year, we re-established the portfolio's short duration position. We believe this is a prudent stance for the fund to take as yields ^[a] on high quality bonds ^[b] issued by governments remain at historically low levels and offer little long-term value in our view.

In contrast, we see good value in debt issued by high quality companies. Over the review period, we invested further in some of our preferred businesses, including retailer Tesco, energy company National Grid and Severn River Crossing, the company responsible for the operation of the Severn Bridges.

We reduced the fund's position in high yield corporate bonds, which are loans issued by companies that pay relatively high rates of interest to compensate investors for the greater risk that they might default, that is, fail to repay the money they have borrowed. These instruments have performed very well over the past 12 months and continue to provide an attractive level of income, although we believe they now offer less potential for further significant capital gains.

While Europe still suffers from weak growth and rising unemployment, we have a more positive outlook for the US economy and its strengthening housing market. Although we reduced the fund's US exposure ahead of the country's difficult fiscal negotiations at the end of 2012, we have maintained a significant allocation to this region.

We remain cautious regarding banks, due to their high levels of indebtedness, and the fund's financial exposure was scaled back throughout the review period. However, we view some of the stronger US banks more favourably and invested further in quality names such as Wells Fargo.

Jim Leaviss & Ben Lord

Co-fund managers

Jim Leaviss & Ben Lord are employees of M&G Limited which is an associate of M&G Securities Limited.

^[a] The interest received from a bond as a percentage of its investment cost, current market value or face value.

^[b] Bonds are loans that are extended by an investor to an issuing entity – private sector firms in the case of corporate bonds and governments in the case of government bonds – in exchange for regular interest payments. The issuer promises to pay the holder the initial value of the loan at the end of the bond's life.

Please note that the views expressed in this Report should not be taken as a recommendation or advice on how the fund or any holding mentioned in the Report is likely to perform. If you wish to obtain financial advice as to whether an investment is suitable for your needs, you should consult a Financial Adviser.

FUND SUMMARY

DISTRIBUTION DATES AND FUND FACTS

Distribution type	xd	payment
Interim	01.10.13	30.11.13
Final	01.04.14	31.05.14

	Final distribution		Ongoing Charges Figure ^[b]	
	Inc 31.05.13 ^[a]	Acc 02.04.13 ^[a]	31.03.13	31.03.12
Sterling	p	p	%	%
Class 'A'	0.0000	0.0000	1.17	1.17
Class 'I'	0.2224	0.1884	0.66	0.67
Class 'R'	0.0000	0.0000	0.92 ^[c]	n/a

[a] The date on which the final distribution will be paid to Income shareholders and credited to Accumulation shareholders.

[b] The Ongoing Charges Figure is the ratio of the relevant annualised total disclosable costs of each share class from the most recent reporting period to the average net asset value for that share class over the same period.

[c] The Ongoing Charges Figure shown here is an estimate of the charges, as the share class has not been in existence for a full financial year.

Income accrued from interest-bearing securities is distributed on an effective yield basis.

FUND PERFORMANCE

	Net asset value per share as at 31.03.13		Net asset value per share as at 31.03.12		Net asset value % change	
	Inc	Acc	Inc	Acc	Inc	Acc
	p	p	p	p	%	%
Sterling						
Class 'A'	110.51	112.13	104.68	105.65	+5.57	+6.13
Class 'I'	110.82	113.32	104.96	106.34	+5.58	+6.56
Class 'R'	105.54	105.67	n/a	n/a	n/a	n/a

PRICES

	Calendar year	Income shares		Accumulation shares	
		Highest	Lowest	Highest	Lowest
Sterling (net)		p	p	p	p
Class 'A'	2010 ^[a]	101.56	100.00	101.56	100.00
	2011	105.51	100.37	106.08	101.29
	2012	108.18	102.39	109.70	103.33
	2013 ^[b]	111.78	107.96	113.35	109.48
Class 'I'	2010 ^[a]	101.63	100.00	101.66	100.00
	2011	105.68	100.39	106.48	101.66
	2012	108.51	102.51	110.73	103.85
	2013 ^[b]	112.23	108.31	114.52	110.52
Class 'R'	2012 ^[c]	103.30	100.00	103.38	100.00
	2013 ^[b]	106.78	103.10	106.87	103.18

^[a] From 16 September 2010 (the launch date of the fund).

^[b] To 2 April 2013.

^[c] From 3 August 2012 (the launch date of the share class).

Past performance is no indication of current or future performance and the performance data does not take account of the commissions and costs incurred on the issue and redemption of shares.

The price of shares and the income from them may go down as well as up, and you may get back less than you invested.

INCOME

Interest income per share

	Calendar year	Final	Distributed		Reinvested
			Interim	Total	
Sterling (net)		p	p	p	p
Class 'A'	2011	0.5540	0.3520	0.9060	0.9104
	2012	0.0000	0.5400	0.5400	0.5452
	2013 ^[a]	0.0000	-	0.0000	0.0000
Class 'I'	2011	0.7660	0.5600	1.3260	1.3300
	2012	0.0000	0.7540	0.7540	0.7628
	2013 ^[a]	0.2224	-	0.2224	0.1884
Class 'R'	2012	n/a	0.1020	0.1020	0.1008
	2013 ^[a]	0.0000	-	0.0000	0.0000

^[a] Up to final: ex-distribution date 2 April 2013;
payment date 31 May 2013.

MAJOR HOLDINGS

The top ten holdings at the end of this year and the previous year end are shown below.

	% of sub-fund as at 31.03.13		% of sub-fund as at 31.03.12
Treasury 2.5% IL 2013 (£)	29.21	Treasury 2.5% IL 2016 (£)	29.38
Treasury 2.5% IL 2016 (£)	29.05	Treasury 2.5% IL 2013 (£)	10.28
Tesco 4% IL 2016 (£)	3.37	Tesco 4% IL 2016 (£)	4.16
Toyota Motor Credit 2.413% IL 2017 (£)	3.20	Toyota Motor Credit 2.413% IL 2017 (£)	3.47
Severn River Crossing 6.125% IL 2013 (£)	2.03	Severn River Crossing 6.125% IL 2013 (£)	3.05
JPMorgan Chase Bank 5.375% 2016 (£)	1.80	JPMorgan Chase 5.375% 2016 (£)	2.41
		Rabobank Nederland 2.324% IL 2013 (£)	2.05
Wells Fargo Bank 5.25% 2023 (£)	1.64		
US Bank National Association Var. Rate 2017 (£)	1.48	National Grid Gas 4.1875% IL 2022 (£)	2.03
Bank of America 5.3% 2017 (£)	1.48	Wells Fargo 5.25% 2023 (£)	1.98
National Grid Gas 4.1875% IL 2022 (£)	1.08	Anglian Water Services Financing 4.125% IL 2020 (£)	1.69

CLASSIFICATION OF INVESTMENTS

The table below shows the percentage holding per sector.

	% of sub-fund as at 31.03.13	% of sub-fund as at 31.03.12
'AAA' credit rated bonds	60.26	42.46
'AA' credit rated bonds	3.39	7.61
'A' credit rated bonds	17.05	29.47
'BBB' credit rated bonds	6.78	6.38
'BB' credit rated bonds	0.48	2.06
'B' credit rated bonds	1.65	1.24
Bonds with no credit rating	6.76	8.74
Credit default swaps	(0.84)	(0.16)
Forward currency contracts	0.05	0.03
Interest rate futures contracts	(1.05)	0.03
'AAA' rated money market funds ^[a]	0.88	0.54

^[a] Uncommitted surplus cash is swept into 'AAA' rated money market funds with the aim of reducing counterparty risk.

OTHER INFORMATION

The information in this report is designed to enable shareholders to make an informed judgment on the activities of the sub-fund during the period covered by the report and the results of those activities at the end of the period. For more information about the activities and performance of the sub-fund during this and the previous period, please contact the Authorised Corporate Director (ACD).

Short Reports

This Short Report is issued in accordance with the requirements of the Collective Investment Schemes sourcebook as issued (and amended) by the Financial Conduct Authority. This Short Report does not contain the Financial Statements of the M&G UK Inflation Linked Corporate Bond Fund, and it is unaudited.

Investment Report and Financial Statements

A copy of the ACD's Annual Investment Report and Financial Statements for M&G Investment Funds (10), which incorporates the sub-fund's annual investment report and audited financial statements is available free of charge on request from our website at www.mandg.co.uk/reports or by calling M&G Customer Relations on 0800 390 390.

Regulatory changes affecting sub-funds

UK law has been changed in order to segregate each sub-fund's assets and liabilities. This means that each sub-fund is responsible for meeting its own debts and its assets may not be used to pay the debts of the other sub-funds. As a result of the change in regulation sub-funds are also permitted to invest in other sub-funds in the same umbrella under specific conditions. The prospectus has been updated to reflect these changes.

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Co-fund managers

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M&G is a member of the Investment Management Association and of
the Tax Incentivised Savings Association.

The Instrument of Incorporation can be inspected at our offices or at
the office of the Depositary.

M&G Securities Limited is authorised and regulated by the Financial Conduct Authority
and provides investment products. The company's registered office is Laurence
Pountney Hill, London EC4R 0HH. Registered in England number 90776.