

## **Third quarter 2009**

### **Carmignac Gestion**

## **Economic outlook and investment strategy**

### **I – Economic outlook**

- ▶ Confirmation of the global economic recovery, but the gap between developed countries and emerging countries is widening

Although IMF economists have confirmed that developed countries will return to growth in 2010 (+1.6% in the United States and Japan and +0.3% in Europe), the developed world as a whole has been slow to provide solid evidence of this. In fact, despite the bailout plans, this return to growth is mainly due to an improvement in trade balances (linked with the fall in imports) and by better-than-expected consumption. Yet the robustness of final demand relies on factors that could prove fragile. Apart from the classic kickbacks from support measures such as the cash for clunkers allowance in the US, consumption has benefited from the fall in consumer prices (-1.5% year-on-year). The mechanical effects of this fall in terms of more purchasing power will be difficult to replicate in the coming period, largely due to the fall in hourly wages.

- ▶ Emerging countries, not least China, have posted healthy growth forecasts

This situation is in sharp contrast to the remarkable resilience demonstrated by emerging countries. Efficient bailout plans have enabled China to return to growth of almost 9%, while India is witnessing growth of more than 6% and Brazil too is making a vigorous recovery. The momentum of the Chinese economy is widely benefiting its most export-dependent neighbours: both Taiwan and South Korea have seen exports contribute significantly to growth in the wake of their powerful neighbour. Korea, for example, is now only 6% off its pre-Lehman Brothers export levels. The strength of Chinese demand is also benefiting countries that produce commodities, which have reported enviable growth rates.

► Governments must continue their support for developed economies

At a time when the economic rebound in developed countries is still not guaranteed, it seems essential that governments maintain their budgetary and monetary support policies. Paradoxically, the greatest risk to our scenario would be if the economic recovery were perceived as too sharp, justifying a premature normalisation of monetary policy in the most strategic countries for the global economic balance. If the Federal Reserve abandoned its quantitative easing measures, bond rates would inevitably shoot up and money supply would shrink. So in our view, the major advanced economies will have to continue with their accommodating policies, putting off the inevitable adjustments of the withdrawal of liquidity and more importantly the restoration of public finances. The slow process of deleveraging must be allowed to continue in order to allow debt to continue to be transferred from the private sector to the public sector at financing rates that governments can cope with.

## II – Investment strategy

### I – International equities

► The market context still favours the equity markets and justifies our aggressive positioning

Our hopes in the previous quarter for the continued rebound of the equity markets were not let down, and the developments of recent months justify beyond any doubt our structural exposure to the themes of improving living standards in emerging countries, and its corollary, the shortage of commodities. The resilience of equity markets in developed countries in the face of a wave of disappointing economic figures from the US in late September and early October seems, moreover, to support our decision to maintain high exposure to the equity markets. In fact, the sluggish growth of developed economies has the advantage of postponing what have become known as "exit strategies" from expansionary monetary and budgetary policies. With interest rates at close to zero and money supply more than abundant, we believe that this set of factors will augur well for the equity markets.

► The markets do not seem overvalued

Despite the fact that after the rally this summer, US firms are valued at 17.5 times their average earnings over the last 10 years, or almost 10% above their median valuation for the last 20 years, the estimated earnings multiple of 14.8 times for 2010 is still reasonable, largely due to current productivity gains. Cost-cutting by firms in spite of the fall in activity, combined with lower debt servicing due to deleveraging, are both highly conducive to business profitability. As for emerging companies and commodity producers, they are still discounted at an average of 20% compared with advanced country indices, despite their recent growth and more promising outlook.

- ▶ We have continued to invest in the theme of improving living standards in emerging countries and in commodities.

In the higher beta segment of the Carmignac Investissement portfolio (70%), the theme of improving living standards in emerging countries made up 26.2% of assets. The crisis has proved to be a driving force for global rebalancing, which will benefit developing countries. The normalisation of monetary policy allowed by the sharp economic upturn in the major emerging countries is delivering extra momentum for the rise in emerging currencies against leading international currencies, providing an added incentive to invest in the emerging world. Meanwhile, commodities represent 23.7% of the assets of Carmignac Investissement. The robustness of demand for commodities in emerging countries, combined with the fact that demand seems to have sunk to a low point in developed countries, gives us confidence in the medium-term outlook.

- ▶ We are maintaining a defensive component equivalent to 30% of Carmignac Investissement

Alongside the 70% invested in growth themes, Carmignac Investissement has a defensive segment representing 30% of assets, consisting of defensive stocks (healthcare, non-cyclical consumption, etc.) and gold. Representing 13.2% of Carmignac Investissement, gold continues to offer the best hedge against the risk of inflation or deflation materialising.

## II – Bond performance drivers

- ▶ We are pursuing our strategy aimed at benefiting from the fall in corporate bond premiums

On the whole, corporate bonds have benefited in recent months from the reduction of risk premiums owing to the improvement in the economic climate. We believe that this trend is set to continue, albeit with the riskiest bonds outperforming safer investments. Taking account of the more favourable economic climate, we have rotated the portfolio by disposing of bonds with premiums of less than 80 basis points to focus on (for 40% of the corporate portfolio) more generous premiums of 2% or more for bonds offering an attractive risk/return. Corporate bonds represent 30% of the assets of Carmignac Patrimoine.

- ▶ Emerging strategies have been increased

The macroeconomic divide observed between developed markets and emerging markets has helped emerging currencies to rise. Risk premiums on foreign debt declined during the quarter, particularly taking into account the upgrading of Brazil's sovereign debt rating to investment grade. Meanwhile, local debt has benefited from the fall in inflation indices, allowing central banks to continue their accommodating policy. In this context, we have reinforced our emerging strategies, both in local and foreign debt and currencies. This item now represents 10.5% of the assets of Carmignac Patrimoine.

- ▶ Government bonds offer a relatively unattractive risk/return

Even in our scenario of a slow recovery in developed countries, government debt in those countries offers an unattractive risk/return. We do not believe that the fall in rates witnessed this quarter will last. Government debt in Carmignac Patrimoine was therefore trimmed from 15% to 10% of assets.

- ▶ We remain positioned in US inflation-indexed bonds

On the other hand, we have deemed it prudent to increase our investments in US inflation-indexed bonds because, although wage inflation is set to remain virtually non-existent, taking into account the weakness of the job market, nominal inflation should rise over the next few months due to the low inflation numbers dropping out of the series. US inflation linked bonds represent 9% of the assets of Carmignac Patrimoine.

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***About Carmignac Gestion***

Founded in 1989 by Edouard Carmignac, Carmignac Gestion is one of the leading independent asset management companies in Europe today. The company's shares are held entirely by its managers and staff. In this way, the company's long-term viability is ensured by a stable shareholding structure, reflecting its spirit of independence. This fundamental value ensures the freedom required for its successful and renowned portfolio management.

Managing nearly €30 billion of assets, Carmignac Gestion has developed a range of 19 funds across all asset classes, including equity funds and balanced funds, as well as a mandate offering.

Our funds are actively distributed in eight European countries: France, Luxembourg, Switzerland, Belgium, Italy, Germany, Spain and the Netherlands. As a platform for its international development, the company has had a subsidiary in Luxembourg since 1999. In 2008 it opened representative offices in Madrid and Milan.