

Carmignac *views*

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2012, a very rock 'n' roll year?

We are prepared for it. Even if it is necessary to desert (all) long-term financial assets. We don't think so, but the question is even more legitimate as 2011 was one of the more disastrous years, and sometimes far from in keeping with the macroeconomic environment. Here are three examples: If someone had told me in January 2011 that the euro zone would go through the most serious crisis of its history and that the very foundations of the single currency would be shaken, I would have expected to see the euro 15% lower against the dollar than at the start of the year, and not just 3% as occurred. If someone had told me in January 2011 that the Chinese economy would show growth of 9% while a recession would be on the horizon for Europe, I would have expected a net outperformance of Chinese equities against the European indices, and not the reverse, though this is what happened. Finally, if someone had told me in January 2011 that the price of a barrel of oil would increase by 14% and an ounce of gold by almost 9%, I would have expected positive performance in the oil services and gold-mining sectors and not declines in these stocks, which reached 12% and 8.5% respectively.

So over a 2011 full of uncertainties and changes, many of which were political, the only correct reading of the macroeconomic map proved to be inadequate. Risk management dominated, and managed to counter the fall in the markets and, even though this prudence led to several upside points being lost in the technical rebounds of the markets, we are confident that in the long term it is a major plus point of our management.

Does this year promise to be better? Despite the still uncertain economic prospects, the two main themes of reduction of western countries' debt and growth in emerging markets' domestic consumption could constitute an environment that is favourable for the markets, especially as the world outside Europe is not doing so badly. There is significant upside potential for our



assets. However, as this new year starts, we consider risk management to be the priority, first and foremost due to the European situation.

The future of the euro is far from guaranteed. Those who dreamt it up imagined it as the first step on the road to true European economic and political union. Their successors were lax or complacent,

and put off the necessary structural reforms, hiding behind the illusory protection of a currency that brought them stability and a low refinancing rate. The day of reckoning has been approaching since 2010. And the response made in the many "last-chance" summits has failed to satisfy or reassure anyone. Only Germany's economic performance is exceptional and in this European context deserves to be saluted. Can this performance continue while its main commercial partners are in recession and the global economy is slowing down? Probably not in absolute terms, but in relative terms the German situation remains enviable. It is the only country in the euro zone whose 10-year refinancing is at rates below inflation.

At the same time Italy must pay 7% to its 10-year creditors, which is untenable. The ECB's mandate must be extended, to provide a solid defence, giving the countries time to restructure. In any case, for 2012, euro zone base rates must fall again and the euro must be weakened. The structural reforms needed in the euro zone require devaluation first, which would at least enable the weakest countries to regain competitiveness.

In this scenario, bonds would be supported by the presence of a primary buyer and a buyer of last resort, exporting companies by the weakening of the euro, and global assets by a decline in fears of a systemic risk which threatens to contaminate the global economy.

Despite a domestic political crisis and initial contamination from the European crisis, the US economy has shown great resilience. The recovery in the Japanese production chain has led to a significant burst of activity in recent months. Likewise, household consumption, although at the price of a burden on their savings (from 5% in late June to 3.5% in late November), has been a positive surprise since the end of summer. Despite a contraction in the public sector, the US economy therefore still seems to have some traction. However, the forces that contributed to this burst of activity are fragile. On the other hand, the reduction from 4.34% to 2.90% in 30-year government bond yields over the last 12 months could constitute a positive factor for the real estate sector, which is still moribund. The main risk for the US economy is political. The electoral battle has begun in earnest, and in this context any hope of reform seems to be out of the question. Any monetary support from the Fed appears to be ruled out at least for the first half of the year.

Interest rates should therefore remain low and anticipated inflation moderate. A context that favours equities valued around 13x 2011 earnings remains attractive. The main risk would be an increase in the dollar, which would hit the corporate sector. Bear in mind that 45% of S&P 500 revenues are generated outside the United States. In this sense exposure to the dollar is a means of partially offsetting this risk.

China and all the emerging countries must negotiate their soft landing with skill. The western context should favour this soft landing. China's anticipated growth will, however, remain close to 6%. Autumn saw

the publication of significant information on the bursting of China's real estate bubble and the consequences for its financial system. The slowdown in the Chinese economy and the government's difficulty managing the excesses caused by the colossal deflation plan announced in November 2008 are a reality. The Shanghai and Hong Kong equity



markets failed to live up to expectations because of an excess of credit expansion, a sometimes doubtful or inappropriate allocation of capital, and inflationary pressures which have lasted much longer than we expected and which have required significant monetary tightening.

Rather than deny these problems, on the contrary we consider that they can now be overcome. **What seems to be important, and is perhaps difficult to conceive from Europe, is that in China these problems will be resolved by growth and not by an accumulation of austerity measures.** In 2012, nominal GDP growth should be close to 14% and growth in outstanding credit should be similar, between 7.5 and 8 trillion yuans. This will therefore be an economy that is going to continue to create wealth, at a sustained rate, but without excessive escalation of global debt. As regards real estate, we should remember that the government orchestrated this consolidation of the sector. Furthermore, we should not forget that China is still, and has been for many years, facing a housing shortage. The government has logically taken into account this present and future shortage and plans to build 10 million homes a year, prioritising and subsidising social housing. The construction sector is therefore not going to collapse and the best players in the sector will get out while the going is good.

The redirection of emerging economies towards domestic demand and household consumption will continue and accelerate. Moreover, these countries have large margins of manoeuvre concerning monetary and fiscal support. Finally, the fall in

currencies in the second part of the year and lower stock exchange valuations than those of developed markets are other factors which make both bond and equity investments in these countries particularly attractive.

2012 will therefore be a rock 'n' roll year, during which risk management will retain all its importance, but it is a year when our international management of equities, diversified securities and bonds will have powerful performance engines that we will exploit with enthusiasm and passion. But I first wish you all the best for 2012.

Eric Le Coz

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Currencies : the advantages of a weaker euro

We had to wait until late October and the climax of the Greek tragedy and the miserable G20 summit in Cannes to see the euro weaken significantly against the dollar (down 9% in two months). The decline in the single currency is set to continue in 2012, with Europe entering recession and the ECB lowering base rates to levels close to zero. This weakening will be a plus point for our exporting companies, on which the European equity team is focusing all its attention. This decline is

also a plus point for our international management, whether bonds or equities, due to its ability to benefit from the appreciation of other currencies against the euro. Emerging currencies have suffered from repatriation of international capital as risk aversion spreads. However, they now seem to be globally undervalued, except maybe for the Indian rupee in the short term.

Fixed income : bond management holding steady

The safe haven effect and the prospect of a sharp slowdown have benefited German government bonds which, with 10 years to maturity, still lost 45 basis points in December to end the year yielding 1.83%. Over the same period, yields on 10-year US Treasuries lost 19 basis points to stand at 1.88% at the year-end. The heightened sensitivity of our bond portfolios was therefore profitable in December. In the same month, yields on Italian 10-year government bonds remained stable at around 7%. Italy is one of the countries with the highest refinancing needs in the euro zone in 2012, particularly in the first quarter. Who could reasonably believe that Italian finances are going to recover by forcing the country to refinance at such punitive rates? These levels

clearly show that stabilisation of the euro zone situation has not been achieved. Our bond management got out while the going was good, demonstrating great prudence and diversifying its assets into robust corporates and bonds issued by countries with healthy economic fundamentals. Annual performances of 0.8%, 1.6% and 9.5% over the year enjoyed respectively by **Carmignac Sécurité**, **Carmignac Cash Plus** and **Carmignac Global Bond** must be welcomed in this difficult context. The current yields of our bond portfolios (and those of our diversified funds **Carmignac Patrimoine** and **Carmignac Emerging Patrimoine**), the basis of their future performance, are now particularly attractive.

Equities : management of net exposure to equity risk is a point in our favour

Despite a reasonably fair macroeconomic reading, our global management has not managed to outperform its performance indicators. The main reason for this is too high an allocation in emerging equities, which are severely (and often unjustly) hit by persistent inflationary pressures and then by fear of a marked economic slowdown. The corollary of this excessive emphasis on emerging economies has been considerable underweighting in US stocks, which have largely outperformed all major global equity indices (with stable performance

of the S&P 500 in dollars). Nevertheless, in a global context that is unfavourable for this asset class, management of the net exposure was very helpful, making it possible to contain the erosion linked to falling equity markets. The best example of this is **Carmignac Euro-Patrimoine**, which with something like a long-short strategy, and with a maximum exposure to equity risk of 50%, lost only 1.2% over the year, and over three years, with a rise of 16%, is doing twice as well as the Euro Stoxx 50 index (dividends reinvested).

Commodities : chinese growth will remain strong

Despite a substantial recovery over the last quarter, our management of these sectors suffered in 2011. No safe haven was really possible, due to UCITS legislation which forbids direct indexing to physical commodities. In fact, over the year as a whole, in dollars, the Brent price was up 14% and gold up 8.8%. At the same time the index of oil services stocks fell 11.8% and the gold mine index was down 8.5%. Commodity prices held up under the effect of ever-growing demand, even though

growth was less steep than at the peak of the cycle, or under the effect of geopolitical tensions. China, India, Brazil and Indonesia will continue to grow, however, and their growth will continue to be intensive in natural resources. It therefore seems that the stocks of companies we hold in our global portfolios and in **Carmignac Commodities** offer very significant catch-up potential, which will bear fruit if risk aversion declines owing to any resolution of the European crisis.

Funds of Funds : asset allocation

This has been a difficult year for the absolute and relative performances of our funds of funds, hit like global funds by too high an allocation in emerging countries. Duly noted. Management of the net exposure to equities remains a point in our favour and guarantees the flexibility needed for the coming year. As regards emerging equities,

as stated in this newsletter's leading article, we feel they offer the best potential in terms of equities. Holding them should enable us to quickly catch up on time lost this year.

// FUND PERFORMANCE

	NAV	2011	3 years	5 years
Carmignac Investissement A	8103,51	-9,95%	51,12%	24,36%
Carmignac Investissement E	123,54	-10,62%	46,39%	17,04%
<i>MSCI All Countries World Free (Eur)</i>		-6,39%	43,97%	-17,28%
Carmignac Investissement GBP	86,76	-12,19%	28,85%	54,12%
<i>MSCI All Countries World Free (GBP)</i>		-8,74%	22,68%	2,56%
Carmignac Grande Europe A	122,79	-14,47%	29,23%	-20,98%
Carmignac Grande Europe E	70,89	-15,12%	26,41%	-
<i>DJ Stoxx 600</i>		-11,34%	24,20%	-33,05%
Carmignac Grande Europe GBP	82,2	-16,84%	9,90%	-2,32%
<i>DJ Stoxx 600 (GBP)</i>		-13,57%	5,83%	-17,00%
Carmignac Euro-Entrepreneurs	163,02	-12,97%	46,69%	-18,56%
<i>DJ Stoxx 200 Small</i>		-17,52%	52,37%	-29,99%
Carmignac Emergents A	644,36	-12,09%	98,03%	5,04%
<i>MSCI Emerging Markets Free (Eur)</i>		-17,75%	76,48%	2,00%
Carmignac Emergents GBP	84,96	-14,07%	69,35%	30,56%
<i>MSCI Emerging Markets Free (GBP)</i>		-19,82%	50,38%	26,45%
Carmignac Emerging Discovery A	948,88	-19,12%	112,51%	-
<i>Index CARMIGNAC Emerging Discovery (Eur)</i>		-24,34%	94,54%	-
Carmignac Emerging Discovery GBP	77,92	-21,17%	81,17%	-
<i>Index CARMIGNAC Emerging Discovery (GBP)</i>		-26,24%	65,77%	-
Carmignac Innovation	206,12	-8,53%	20,26%	-34,06%
<i>Index CARMIGNAC Innovation (Eur)</i>		3,27%	52,91%	1,70%
Carmignac Commodities A	321,75	-21,12%	95,38%	15,09%
<i>Index CARMIGNAC Commodities (Eur)</i>		-13,26%	59,00%	7,26%
Carmignac Commodities GBP	76,23	-23,16%	66,73%	42,74%
<i>Index CARMIGNAC Commodities (GBP)</i>		-15,44%	35,48%	32,99%
Carmignac Patrimoine A	5224,8	-0,76%	25,45%	36,22%
Carmignac Patrimoine E	133,95	-1,25%	23,10%	30,71%
<i>50% MSCI AC World Free (Eur) + 50% Citigroup WGBI (Eur)</i>		1,76%	34,69%	16,46%
Carmignac Patrimoine GBP	95,08	-3,77%	6,41%	67,93%
<i>50% MSCI AC World Free (GBP) + 50% Citigroup WGBI (GBP)</i>		-0,80%	14,77%	44,39%
Carmignac Emerging Patrimoine A	98,1	-	-	-
Carmignac Emerging Patrimoine E	97,94	-	-	-
<i>50% MSCI EM Free (Eur) + 50% JPM GBI EM (Eur)</i>		-	-	-
Carmignac Emerging Patrimoine GBP	92,79	-	-	-
<i>50% MSCI EM Free (GBP) + 50% JPM GBI EM (GBP)</i>		-	-	-
Carmignac Emerging Patrimoine USD	89,98	-	-	-
<i>50% MSCI EM Free (USD) + 50% JPM GBI EM (USD)</i>		-	-	-
Carmignac Euro-Patrimoine	276,77	-1,19%	16,06%	-4,20%
<i>50% DJ Euro Stoxx 50 + 50% Eonia Capitalisé</i>		-8,08%	-0,82%	-16,52%
Carmignac Market Neutral A	1023,35	-6,62%	-1,29%	2,33%
<i>Eonia Capitalisé</i>		0,88%	2,07%	10,41%
Carmignac Market Neutral GBP	93,46	-6,14%	-10,54%	31,48%
<i>Eonia Capitalisé (GBP)</i>		0,88%	2,07%	10,41%
Carmignac Profil Reactif 100	150,59	-11,76%	34,34%	-11,44%
<i>MSCI All Countries World Free (Eur)</i>		-6,39%	43,97%	-17,28%
Carmignac Profil Reactif 75	174,28	-8,66%	25,47%	-2,30%
<i>75% MSCI AC World Free (Eur) + 25% Citigroup WGBI (Eur)</i>		-2,31%	39,49%	0,32%
Carmignac Profil Reactif 50	154,54	-4,29%	19,83%	6,19%
<i>50% MSCI AC World Free (Eur) + 50% Citigroup WGBI (Eur)</i>		1,76%	34,69%	16,46%
Carmignac Global Bond A	1066,26	9,47%	1,86%	-
<i>JP Morgan GGB</i>		10,81%	25,48%	-
Carmignac Global Bond GBP	105,32	6,62%	-13,21%	-
<i>JP Morgan GGB (GBP)</i>		8,02%	6,92%	-
Carmignac Securite	1545,44	0,81%	13,59%	21,24%
<i>Euro MTS 1-3 Y</i>		0,54%	5,65%	16,93%
Carmignac Cash Plus A	10536,29	1,62%	3,99%	-
<i>Eonia Capitalisé</i>		0,88%	2,07%	-
Carmignac Cash Plus GBP	4953,8	-0,21%	-10,67%	-
<i>Eonia Capitalisé (GBP)</i>		-1,65%	-13,02%	-

Source : Morningstar as at 30/12/2011.

Please note that past performance is not a guarantee of future returns and that it may fluctuate over time.



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