Carmignac Portfolio Grande Europe: Letter from the Fund Manager

Author(s)
Mark Denham

Published
October 17, 2022

Len

-3.9%

Carmignac Portfolio Grande Europe's performance

in the 3rd quarter of 2022 for the A EUR Acc Share class

-4.3%

Reference indicator's performance

in the 3rd quarter of 2022

+6.3%

Annualised performance of the Fund

since Mark Denham started managing it (17/11/2016) versus +4.9% for the reference indicator

During the third quarter of 2022, the return of Carmignac Portfolio Grande Europe (A EUR Acc share class) was a decline of -3.9%, however, this was above the reference indicator which fell -4.3%.

Quarterly Performance Review

Throughout the quarter, European markets continued to face several headwinds. On the one side, inflation remains resilient at a level much higher than central banks' targets, resulting in upward pressure on interest rates and rising bond yields.**On the other side, the war in Ukraine** – and the resulting suspension of Russian gas supplies to the region –**has kept energy prices high and increases the likelihood of rationing in 2023. Both these dynamics are likely to place a material burden on consumers and companies in Europe, resulting in downside risks to profit forecasts for next year** (a deeper deceleration from that already factored in).
Additionally, at least in the first half of 2023, we also expect negative GDP growth. Nevertheless, it is true that fiscal actions are mitigating some of these headwinds (i.e. energy price caps), but they require funding which, in turn, limits governments' ability to maneuver and boost growth. A dramatic example of this was the new UK government's U-turn in recent days on their own proposed tax cuts.

How is the fund positioned?

In July, markets initially rose on the false hopes of a fast decline in US inflation. These prospects were firstly dashed by hawkish commentary from policymakers, and successively by strong employment reports and higher inflation prints. These data confirmed the persistent strength in the labour market and so-called core inflation (which excludes energy and food). Nonetheless, as of today, we still expect the dominant headwind to change soon as **investors' focus will shift from valuation multiple compression, due to rising rates, to growing fear over the impact of rising costs on economies and companies' profits. This transition will create an environment more conducive to the kind of stocks we have in our portfolio: companies with higher visibility and sustainability of sales and profits which are thus less economically sensitive.** Q2 reporting season in Europe was broadly uneventful, with an unusually high proportion of companies beating estimates. Full year forecasts were broadly maintained, as the impact of the above-mentioned headwinds were yet to materialise. However, investors considered these numbers to be backward looking as the risks remain ahead of us.

In the last three months, all sectors performed negatively with energy and commodities more muted. This backdrop weighed on the fund as our exposure to these two sectors is virtually zero. However, our stock selection was positive, and helped us to modestly beat the reference indicator. Support came from our Healthcare allocation which, in recent months, we have increased. This area is now a strong focus of the fund as we like the visibility that many of the underlying names provide in a tough environment. Additionally, we believe that these stocks have been unduly punished by valuation compression due to rising interest rates. As well as having added new names earlier in the year such as Alcon (ocular lenses), Genmab (biotech) and Straumann (dental), in Q3 we also added Lonza, a contract drug manufacturer. Latest results – and the company business model – has shown particularly visible profit streams owing to the long-term nature of its contracts, as well as growth in demand primarily driven by the use of biologic drugs, and gene and cell therapies such as RNA mechanisms. Having lost significant value this year, we took advantage of an excellent entry point. **Novo Nordisk, our largest holding, has been volatile in the period** After reacting badly this summer to news that recommencement of the supply of their weight loss drug, Wegovy, was to be deferred again to the end of Q4, the name recouped value quickly after a pipeline product delivered market leading efficacy on weight loss. Quarterly numbers were also strong, and the company increased full year guidance, primarily due to the relentless growth in their leading once-weekly diabetes injectable, Ozempic. The product has been on the market for a few years already, but growth has followed an exponential trajectory owing to strong efficacy and convenience, with prescriptions in the US rising more than 80% in the quarter versus the previous year.

Good performance came from contract caterer Compass Group whose stock rose in Q3 as they continued to recoup their losses, including those due to the pandemic. This reopening name has made steady progress, rising significantly since we added it at the start of the Covid crisis. As a result, it has now reached our target price and we have cut the holding down to almost zero. **LVMH – the luxury goods company – has also been a strong performer** on the back of Q2 reporting numbers which underlined the strength of their brands (organic growth and no signs of slowdown). Again, we have cut this holding back after strong relative performance as we currently prefer competitor Hermes. We initiated in the latter in July after a significant fall created a wonderful entry opportunity. Since then, the name has already recovered some of the value lost. **On the negative side, we saw a pronounced weakness in names with higher sensitivity to economic activity, such as Puma (sportswear) and Kingspan (building materials). Wind energy players Orsted and Vestas were also weak** after quarterly results confirmed the tough operating environment caused by volatile energy prices, supply chain disruption, and logistic cost pressure. We have added to Orsted, as the long-term outlook is favourable on the back of high growth in installed wind farms for decades to come.

What is our outlook for the coming months?

All year, the market environment has been a difficult one for us, both in absolute terms and relative to our reference indicator. However, **we have an investment horizon of 5 years, and we will stick to our process of focusing on profitable companies with high returns on capital, reinvesting for future growth**. We believe these companies will continue to deliver the most attractive long-term returns for investors. This is why the dramatic pullbacks in prices of these types of companies are opportunities for us: they provide excellent entry points in great businesses – as shown by the examples mentioned above.

Reference indicator: Stoxx Europe 600 (NR, EUR). From 01/01/2013 the reference indicator is calculated net of dividends reinvested. Source: Company website, Bloomberg, Carmignac, September 2022

Carmignac Portfolio Grande Europe

A high conviction, sustainable European equity strategy

Discover the fund page

Carmignac Portfolio Grande Europe A EUR Acc

ISIN: LU0099161993

Recommended minimum investment horizon

Lower risk Higher risk

1	2	3	4*	5	6	7

Main risks of the Fund

EQUITY: The Fund may be affected by stock price variations, the scale of which is dependent on external factors, stock trading volumes or market capitalization.

CURRENCY: Currency risk is linked to exposure to a currency other than the Fund's valuation currency, either through direct investment or the use of forward financial instruments.

DISCRETIONARY MANAGEMENT: Anticipations of financial market changes made by the Management Company have a direct effect on the Fund's performance, which depends on the stocks selected.

The Fund presents a risk of loss of capital.