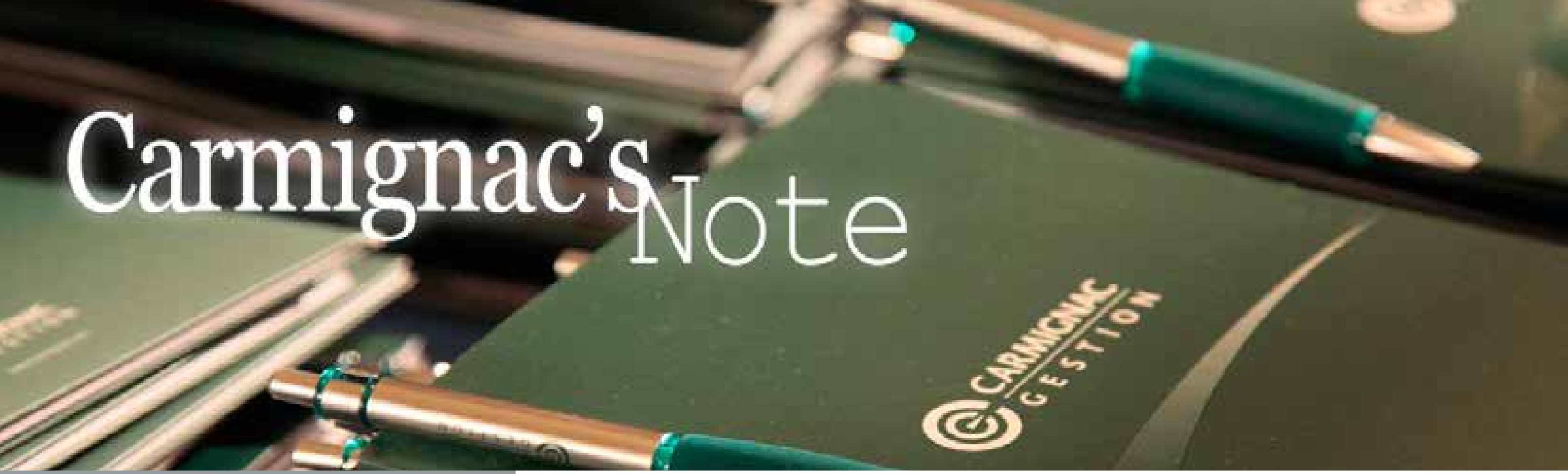

Carmignac's Note

DECEMBER 2014 // N°75

Lost in Stagnation

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Economic data published over the last two months in Europe, Japan, China and even the United States confirm the view that we summarised in our Newsletter on 3 October ("Our Concerns").

Albeit to varying degrees, the weakness of demand and consequently inflation and investment is forcing the main central banks to continue their intervention using the only means available: an accomodative monetary policy. The sudden equity market sell-off at the beginning of October, which European and Japanese central bankers quickly managed to reverse, is enlightening. Like a canary in a coal mine, this sudden concern warns of danger, which lies in the growing conflict between central banks' greater determination ("whatever it takes" from Tokyo to Frankfurt) and the clear limit on their ability to counteract a very weak economic cycle ("whatever they do"). Admittedly, a number of countries' efforts are making the medium-term outlook encouraging: this is the case in the United States but also India, the Philippines and China in Asia, Mexico, Peru and Colombia in Latin America, and Spain and Ireland in Europe. However, looking forward to 2015, pressure on the global economic cycle still appears to be underestimated and could fuel bouts of volatility. This justifies the pursuit of our investment strategy based on a global portfolio that very specifically targets high visibility growth stocks with a predominance of dollar-denominated assets and highly active management of levels of exposure to equity and bond markets alike.

"Low commodity prices, starting with energy, reflect the weakness of global demand."

The markets' performance thus far confirms our view that the world will continue to feel the effects of global deflationary pressures for some time

The main equity markets were quick to make up for most of their late-summer fall. However, looking more closely we see that this increased optimism is illusory. Since bottoming out on 16 October, quality low-risk stocks, which we group together in our style analyses as being suited to periods when the cycle slows, have continued to outperform lower-quality cyclical stocks. Overall, industrials for example are now lagging as far behind pharmaceuticals as they have at any time since 2011. At the

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same time, the German government bond yield has dropped further, from 1% to less than 0.70% in the space of two months, reflecting the ongoing appeal of such a safe haven asset. This market behaviour should be of no surprise as underlying macroeconomic trends remain unchanged: the OECD's leading indicator for G7 countries has been falling steadily since the beginning of the year, and purchasing managers indices are slowing too. Low commodity prices, starting with energy, reflect this weakness of global demand.

CARMIGNAC
GESTION

The US recovery casts a shadow of doubt as well

The US economy's resilience is key to global and especially European demand and its relative performance has hitherto been a godsend for the rest of the world. But despite an upward revision to the official GDP growth estimate for the third quarter, its apparent strength masks some signs of weakness, which make us question its upside potential. Indeed, several negative factors will now limit consumer spending growth in the United States: a stagnation of real income, a ratio of consumer debt to disposable income at an all-time high,

> *"It would be overoptimistic to rely on monetary creation alone to kick-start European growth."*

the beginnings of a rise in food prices and rents, and a savings rate that cannot go much lower. Meanwhile potential investment growth will be shackled by a dwindling production capacity utilisation rate after a negligible improvement, and by profit margins that are rising no more. As things stand, we are not heralding an imminent US economic downturn, merely highlighting the risks of disappointment which we feel a complacent consensus is underestimating. A further appreciation of the dollar in 2015 would naturally be another burden for US corporate earnings.

Europe still at the very beginning of its long walk

Matteo Renzi's and Manuel Valls' realisation of the pressing need for economic reform to increase long-term growth potential is to be welcomed. The former is currently reforming the labour market through his Jobs Act while the latter is preparing his own reforms in the future "Loi Macron". However, it has taken far too long to implement these reforms. Even in a best case scenario, it will be several years before we reap the benefits. Despite the progress already made in a few countries, nominal growth has already been slowing for nearly 12 months in the eurozone. Mario Draghi could possibly weaken the euro, bring down banks' borrowing costs even further and stem the slide of inflation expectations. That in itself would be quite a feat. But if consumer spending and investment fail to pick up, it would be overoptimistic to rely on monetary creation alone to kick-start European growth. Japan's misfortunes serve as a good example of this.

Japan, the testing ground in the fight against deflation

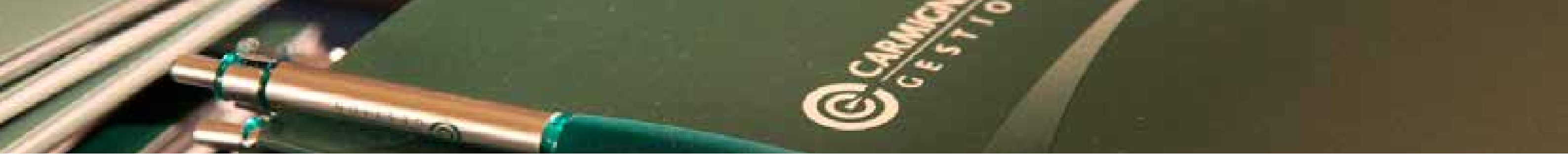
After 18 months of quantitative easing, raising VAT from 5% to 8% was all it took to plunge the Japanese economy back into recession. This is glaring confirmation that higher inflation and a cheaper currency are not enough to keep real growth at a steady pace without a parallel boost from demand. Japan's troubles embody the scale of the challenge that, to varying degrees, faces developed countries: how to stimulate demand when consumers are taking a wait-and-see approach, saving money for a rainy day, after years of overindebtedness that ultimately led to the mother of all credit crises. However, Japan is fortunate to have a resolute central bank whose balance sheet already equates to 60% of GDP. By comparison, we note that Mario Draghi's "bazooka", if actually fired, would swell the ECB's balance sheet to just 30% of the eurozone's GDP after six years of crisis.

China slowing controllably

The interest rate cut announced by the Chinese authorities in November confirms lingering pressures on growth and prices but equally the determination to be able to control the slowing of the economy. The long-term trajectory for the Chinese economy continues to improve under the influence of extensive reform, and the country remains "investable". We think it presents a number of opportunities, especially through its domestic equity market (A shares), which gives access to numerous service companies offering good visibility. In the immediate future, though, tackling corruption, reducing the size of the shadow banking industry and releasing some air from the property bubble will seriously limit growth, damaging countries that export to China.

Equity markets have lost much breadth in recent months, in the sense that the proportion of stocks outperforming their benchmarks has fallen considerably. This situation, which is affecting European more than US markets, is not insignificant. It reflects the shortage of convincing investment opportunities. This makes the challenge of stock-picking all the more acute and, given our concerns about the weakness of the economic cycle, highlights the importance of asset allocation and risk management to deliver a satisfactory return.

Drafting completed on 1 December 2014



INVESTMENT STRATEGY

CURRENCIES

The euro dropped further against the US dollar in November. From a level of 1.38 at the beginning of the year, the EUR/USD fell below 1.25 during the month. This constant slide since June made a significant contribution to our funds' performance. The divergence between monetary policies and economic momentum each side of the Atlantic will probably see this trend continue in 2015. We are therefore remaining long on the US dollar in our currency allocation. The other major event of the month was the depreciation of the yen as the Bank of Japan ramped up its quantitative easing. We temporarily hedged our exposure to the Japanese currency during this adjustment. However, we think a stabilisation is imminent as the negative effects of a weak yen on household purchasing power and the cost of SMEs' imports is gradually undoing the positive impact on inflation expectations.

RATES

The ECB's leaders have continued to discuss the possibility of using new instruments to fix inflation expectations in the eurozone. The prospect of a QE programme that includes buying government bonds from EMU Member States is drawing closer. In this context, we expect yield spreads between German and peripheral countries' bonds to converge further, which is why we are keeping our positions in the latter. For example, Spain's 10-year yield dropped below 2% during the month. US long rates did fall but not by as much. We are keeping a flexible, balanced approach to the US curve, seeking to benefit from any flattening as US monetary policy gradually returns to normal. We thus slightly increased our funds' modified duration during the month.

EQUITIES

The reduction in our equity exposure from the end of August allowed us to withstand the burst of volatility in September and October as the US Federal Reserve brought QE3 to a close. Equity markets have rallied since then, albeit with vast regional differences. Japan performed brilliantly (up by around 6%) and Europe solidly (more than 3%) in November, reflecting the key role that central banks still play in influencing equity market behaviour. Emerging markets were very mixed: India kept its forward momentum whereas the Russian market continued to suffer from geopolitical tension and falling oil prices. We still prefer structural growth investments offering good visibility and are avoiding cyclical stocks dependent on stronger growth. We opened positions in Visa and MasterCard during the month: these US companies, wrongly perceived as being exposed to the economic cycle through their credit card operations, are actually for the most part providers of payment solutions with highly recurrent business. They are stakeholders in the development of Apple's mobile phone payment system, a promising area. We also strengthened our holdings of pharmaceutical stocks by building a position in Shire, taking advantage of the temporary fall in its share price after the US group AbbVie abandoned a takeover plan. Lastly, we increased our equity exposure over the month to give a more balanced allocation, having been significantly underweight at the beginning of October.

COMMODITIES

Carmignac Portfolio Commodities' positioning, which was quite different to its reference indicator's, saw it safely through the commodity price drop of recent months. We increased our investments in oil companies whose cost structure will allow them to emerge from a period of depressed oil prices relatively unscathed. Suncor Energy, our Canadian tar sands company, is a notable example.

FUNDS OF FUNDS

Our funds of funds turned in a positive performance over the month. Pushing equity exposure towards its maximum allowed these funds to capture much of the markets' rally.

FUND PERFORMANCE

	NAV	2014	1 year	3 years	5 years
Carmignac Investissement A EUR acc	**1,100.71**	**9.15%**	**10.85%**	**34.82%**	**48.49%**
MSCI AC World NR (Eur)	-	*17.39%*	*18.00%*	*59.26%*	*81.72%*
Carmignac Portfolio Grande Europe A EUR acc	**172.03**	**9.46%**	**10.03%**	**42.78%**	**45.39%**
Stoxx 600 NR (Eur)		*8.59%*	*9.71%*	*52.80%*	*53.38%*
Carmignac Euro-Entrepreneurs A EUR acc	**252.58**	**5.85%**	**9.00%**	**57.30%**	**66.04%**
Stoxx 200 Small NR (Eur)		*3.40%*	*5.64%*	*57.54%*	*69.12%*
Carmignac Emergents A EUR acc	**772.59**	**8.96%**	**8.10%**	**20.76%**	**50.21%**
MSCI Emerging Markets NR (Eur)		*13.34%*	*10.37%*	*22.58%*	*33.15%*
Carmignac Portfolio Emerging Discovery A EUR acc	**1,204.86**	**12.05%**	**11.42%**	**30.34%**	**48.10%**
50% MSCI EM SmallCaps NR (Eur) + 50% MSCI EM MidCaps NR (Eur)		*13.65%*	*11.46%*	*29.13%*	*38.19%*
Carmignac Portfolio Commodities A EUR acc	**280.32**	**5.44%**	**7.24%**	**-13.52%**	**3.81%**
*Carmignac Commodities Index**		*-1.56%*	*-0.83%*	*-3.62%*	*8.48%*
Carmignac Patrimoine A EUR acc	**613.33**	**7.55%**	**8.49%**	**19.97%**	**27.43%**
50% MSCI AC World NR (Eur) + 50% Citigroup WGBI (Eur)		*14.05%*	*13.31%*	*31.50%*	*53.28%*
Carmignac Portfolio Emerging Patrimoine A EUR acc	**104.70**	**7.98%**	**6.45%**	**8.47%**	**-**
50% MSCI EM NR (Eur) + 50% JP Morgan GBI EM Global diversified		*12.07%*	*9.62%*	*17.96%*	-
Carmignac Euro-Patrimoine A EUR acc	**303.98**	**0.02%**	**0.08%**	**11.20%**	**18.13%**
50% EuroStoxx 50 NR (Eur) + 50% Eonia compounded		*3.67%*	*4.14%*	*22.62%*	*13.47%*
Carmignac Profil Réactif 100 A EUR acc	**188.62**	**5.53%**	**6.22%**	**28.19%**	**38.39%**
MSCI AC World NR (Eur)		*17.39%*	*18.00%*	*59.26%*	*81.72%*
Carmignac Profil Réactif 75 A EUR acc	**209.00**	**5.54%**	**5.73%**	**22.84%**	**30.13%**
75% MSCI AC World NR (Eur) + 25% Citigroup WGBI (Eur)		*15.73%*	*15.68%*	*45.05%*	*67.56%*
Carmignac Profil Réactif 50 A EUR acc	**173.01**	**5.45%**	**5.17%**	**14.83%**	**21.03%**
50% MSCI AC World NR (Eur) + 50% Citigroup WGBI (Eur)		*14.06%*	*13.32%*	*31.52%*	*53.30%*
Carmignac Portfolio Global Bond A EUR acc	**1,217.58**	**11.89%**	**12.65%**	**20.66%**	**34.08%**
JP Morgan Global Government Bond (Eur)		*11.68%*	*9.19%*	*6.62%*	*27.62%*
Carmignac Securité A EUR acc	**1,700.65**	**1.95%**	**2.20%**	**11.30%**	**14.49%**
Euro MTS 1-3 years		*1.77%*	*1.69%*	*9.81%*	*9.47%*
Carmignac Portfolio Capital Plus A EUR acc	**1,165.21**	**2.10%**	**2.29%**	**11.17%**	**14.65%**
Eonia compounded		*0.10%*	*0.12%*	*0.48%*	*1.79%*
Carmignac Court Terme A EUR acc	**3,767.35**	**0.18%**	**0.20%**	**0.86%**	**2.19%**
Eonia compounded		*0.10%*	*0.12%*	*0.48%*	*1.79%*

** 45% MSCI ACWF Oil and Gas NR (Eur), 5% MSCI ACWF Energy Equipment NR (Eur), 40% MSCI ACWF Metal and Mining NR (Eur), 5% MSCI ACWF Paper and Forest NR (Eur) and 5% MSCI ACWI Chemicals NR (Eur) as from 01/07/2013. Annually rebalanced as from 01/01/2012.*

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