QUARTERLY REPORT

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Carmignac Portfolio Emerging Patrimoine: Letter from the Fund Managers

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During the third quarter, **Carmignac Portfolio Emerging Patrimoine (A EUR ACC share class, ISIN LU0592698954[1])** returned -1.27% versus -1,59% for its reference indicator[2], taking its year-to-date performance to -15.00% versus -8.54% for its composite reference indicator.

Market Environment

The last quarter was driven by a continued volatility in the developed market rates with a pull and tug between the recession risk that would force the Federal Reserve (Fed) to stop their hiking and the fight against inflation that remains persistently high.

In this context emerging markets external debt has continued to trade under stress. We have seen values continue to drop in the index after a second round of volatility in US rates as the economic data was more robust than expected. The index's spread remains at very elevated levels close to the 600 spread peaks of Covid, and over the quarter a number of credits have gone to the IMF, such as Egypt, Ghana or Sri Lanka.

In local rates, the various EM central banks have continued to tighten their policies as the inflation pressure remains as well as an increased pressure on the FX. Towards the end of this quarter however we have seen more and more central banks truly pausing their hiking cycles notably the early hikers Brazil and Czechia, but also more recently Poland and Hungary. We note that local activity indexes in EM, for consumption, or lending are showing a significant deceleration showing the impact of the tightening.

In EM FX the USD continued to strengthen during the quarter thanks to the Fed's hawkish policy and generally risk-off sentiment. EM countries which had plentiful reserves started to defend their currencies, we can think of the INR or the CZK. In Asia, we have seen an unsustainable level of reserves burn over the quarter.

Finally, Emerging Equities continued to trend negatively this quarter due to the higher rates and a weak sentiment for Chinese equities from the continued zero covid policy and the economic slowdown. One exception to this was India's stock market which benefitted from strong IPOs and local participation boosting valuations.

What have we done in this context

In this difficult context the fund was able to contain losses to -75bps with the FX and the Credit books contributing positively against Equities and Rates contributing negatively.

In the **External Debt**, we managed to have a positive contribution despite the index volatility over the quarter with 177bps of positive contribution. This performance came from two sources, first the active management of our CDS protections to navigate the very volatile markets. The second source of performance was the distressed credits that we found attractive which have gone to the IMF and are making good progress on program negotiations such as Egypt or Tunisia.

In **Rates**, the fund lost 170bps from positioning the fund early for a turn of EM central banks. Indeed, the pressure of the USD has forced many to continue to hike, sometime very aggressively such as the Hungarian central bank. We did put in place a payer position in India from the large buildup of imbalances and the extreme use of reserves in order to defend the FX while having receiver positions in countries where the central banks were pausing.

On the **FX** side, we benefitted from a bias towards long USD vs Asian FX in the fund which helped generate 298bps of performance. For the Asian shorts we targeted countries which have more imbalances such as the Philippines or India. In the Central and Easter European region (CEE) we remained largely invested in the FX on the long side as these countries have high rates, notably we invested in CZK and on a more tactical basis in HUF.

The weak sentiment on Equities and China in particular, continued to weight on the equity performance of the fund with a 380bps loss. Over the quarter we have implemented short positions in Indices in order to protect the book and have remained lightly exposed.

Outlook for the next months

Going forward we continue to see the fight between the recession in the developed world and the need to fight inflation. Furthermore, we have seen some signs of financial instability such as the large sell-off of UK rates or rumors of default at Credit Suisse that are likely to make the Fed and the ECB more cautious in their tightening policies.

For **EM hard currency bonds**, a slowdown of the global economy and increasing stability in developed market rates would be a very positive driver for performance. Indeed, this segment of the market has been hit very hard and many bonds continue to trade at low cash prices usually indicative of stressed credits even in quality names. EM High yield segment has reached 2008 stress levels. We intend to retain a large amount of protection in the portfolio via CDS until we see enough signs of a slowdown that it would warrant a pivot from the Fed.

In **Local Rates** we have started to see a pause in the rate hikes from countries and we expect this movement to continue in LATAM and EMEA. Activity in those regions is slowing down, along with consumption which will prompt the local central banks to be cautious or cut rates, on top of that the effects of higher rates in developed markets is going to help EM fight inflation. In this space we are going to continue to hold on to our payer in India, and will be long Czech, Hungarian and Brazil rates.

For the **FX**, similarly to the Hard currency, we think that signs of slowdown in the US economy will be negative for the USD and thus help EM FX perform. We retain our preference for the high carry currencies in eastern Europe but would reduce the shorts in Asia should the weak dollar be confirmed. Another factor which will be important during the quarter is the announcement of the OPEC to reduce its production of oil by 2m barrels per day. The higher oil prices, that should result, will be negative for the balances of payment of oil importers notably India or Turkey.

For **Equities**, we will remain cautious with a high level of protection. We will reduce this protection as the Fed pivot occurs and have a more supportive environment. However, we do keep in mind that the pivot would occur in a recessionary context which is why we continue to be positioned on stocks that are trading at already significant discounts to their fundamentals.

Sources: Carmignac, Bloomberg, 30/09/2022

[1] Performance of the A EUR acc share class ISIN code: LU0592698954. Past performance is not necessarily indicative of future performance. The return may increase or decrease as a result of currency fluctuations. Performances are net of fees (excluding possible entrance fees charged by the distributor). From 01/01/2013 the equity index reference indicators are calculated net dividends reinvested.

[2] 40% MSCI Emerging Markets NR USD (Reinvested net dividends) + 40% JP Morgan GBI-EM Unhedged (EUR, Coupons reinvested) + 20% ESTER capitalised. Quarterly rebalanced.

Carmignac Portfolio Emerging Patrimoine

An all-inclusive, sustainable Emerging Market solution

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Carmignac Portfolio Emerging Patrimoine A EUR Acc

ISIN: LU0592698954

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.

INTEREST RATE: Interest rate risk results in a decline in the net asset value in the event of changes in interest rates.

CREDIT: Credit risk is the risk that the issuer may default.

EMERGING MARKETS: Operating conditions and supervision in "emerging" markets may deviate from the standards prevailing on the large international exchanges and have an impact on prices of listed instruments in which the Fund may invest.

The Fund presents a risk of loss of capital.