FLASH NOTE

18.11.2016

CARMIGNAC PORTFOLIO PATRIMOINE: WHAT NOW AFTER TRUMP'S ELECTION?

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Monetary policy can only do so much. Even after years of quantitative easing and rock-bottom interest rates, economic growth has almost everywhere been consistently disappointing for the past eight years. In country after country, every election seems to offer the opportunity to push a different economic agenda focused on more fiscal stimulus and, in some cases, less open borders.

Donald Trump's victory at the polls is therefore a symptom of broader failure; it attests to a rejection of the neoliberal globalisation "regime" that has speed up since the 2008 crisis. In a telling sign of the shift under way from monetary to fiscal support, industrial and cyclical stocks have bounced back from the lows hit in January and February to outperform stocks in other sectors, helped by cyclical stabilisation in the world economy. The election of Donald Trump has reinforced the trend. However, the populist rhetoric campaign of the President elected is actually accompanied by a program that is much less so. Although, a strong fiscal stimulus is foreseen, it is likely to be implemented as tax cuts, above all for companies, in addition to higher infrastructure spending and therefore rising budget deficits. Whatever the scepticism that can be expressed on all of these ambitions, they should lead to further yield widening on long term rates. We already have reduced, since this summer, the risk across all our Fixed Income portfolios and have initiated a short position on US Sovereign bonds. We have recently reinforced this positioning. On the equity side, the new "regime" will also mean further support for commodity stocks, stocks that benefit from infrastructure spending and domestic growth stocks in general. We have started a rebalancing of the equity portfolio in this direction; of course insufficiently given what has been a considerable acceleration of the trend since the US elections.

Equities

We keep managing the risk through a balanced portfolio.

CARMIGNAC PATRIMOINE :
A BALANCED EQUITY PORTFOLIO

« REFLATION » & EMERGING GROWTH STOCKS

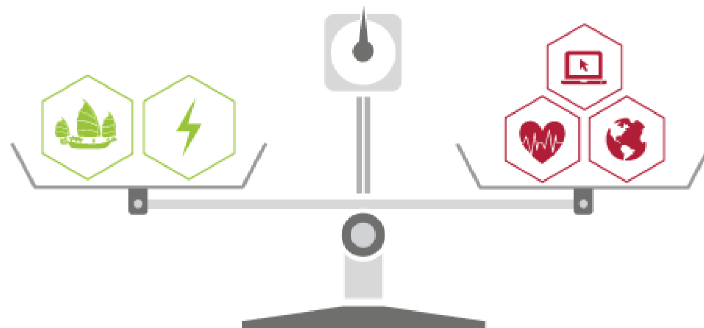
Active management of equity exposure

HIGH VISIBILITY STOCKS

«Reflation» Stocks

- Cement 1,7%
- Natural resources 8,7%
- Gold 3,3%
- European bank index

Emerging Growth 6,6%



Longevity 9,6%

Technology 9,0%

Millennials 7,0%

Source : Carmignac, 10/11/2016
Others : 0,6%

High visibility stocks

We continue to invest in equities with good earnings visibility that can generate rising returns in any macroeconomic environment. In our portfolio, those range from internet and tech stocks to healthcare stocks. Moreover, some of our profit-taking since the start of the year has involved stocks in those sectors, which have been buoyed by the low-yield, low-growth environment of the past several years. In the health care sector, investors breathed a sigh of relief after Hillary Clinton's defeat, as she had threatened to clamp down on pricing by drug companies. In contrast, Trump's protectionist rhetoric has proved punishing to the internet and tech space, with the sector's sound performance since the beginning of 2016 giving way to extreme profit-taking. However, this short-term volatility will have no impact on the long-term growth profile of our tech holdings.

Reflationary and emerging market growth stocks

Given that our portfolio is positioned around cyclical investment themes, we stand to benefit from fiscal stimulus programmes. Our exposure to commodities and cement manufacturers has accordingly been maintained and even gradually increased during the year.
Since the US election, we have continued with our efforts to rebalance our equity portfolio towards more cyclical companies, while keeping a close watch on the already high valuations for specific stocks and/or industries.

The prospect of fiscal stimulus accompanied by a reduction in corporate tax rates has stoked investor appetite for equities and conversely penalised the bond market. The resulting environment makes gold less attractive for the time being, and gold prices have already lost ground, but we are maintaining our exposure to gold stocks in order to manage the tail risk of diminished medium-term central bank credibility at a time of renewed inflation.

We will also continue to invest in emerging market equities. Since Trump was elected, emerging market assets have admittedly experienced high volatility, a reflection of mounting uncertainty and the threat of protectionist policies in the US. On the other hand, the noteworthy improvement in numerous emerging market fundamentals over the past few years has made those countries much less vulnerable to interest-rate hikes and a stronger dollar than the market seems to fear. In addition, the projected pick-up in private- and public-sector investment in the United States should work to the advantage of commodity producers as a whole. Lastly, the emerging world is more heavily influenced by developments in China than by the state of the US economy. A clear sign of this is that emerging economies have continued to benefit from the recent stabilisation brought about by the Chinese government's stimulus programme. With all that in mind, we will remain positive, but highly selective approach in an environment likely to remain volatile in the weeks to come.

Currencies

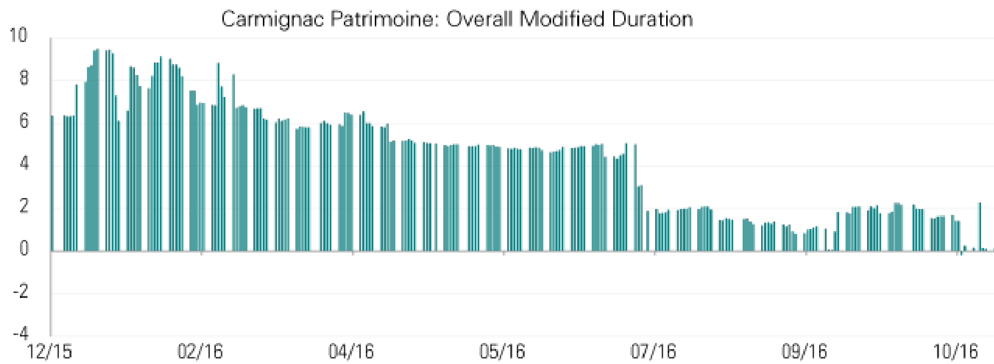
On the currency front, while we had reduced our exposure to the dollar ahead of the US elections, we have since then rebalanced our Dollar and Euro positions, at the expense of the Yen and the emerging currencies, so as to take into consideration the impact of Trump's programme on the greenback. (inflow of capital into the US that support the dollar, US rate hike).

Fixed income

Although the bond market has been rocked by Trump's victory and the ensuing expectations for a boldly reflationary policy in the US, the fixed income component of Carmignac Portfolio Patrimoine has stood its ground, thanks in part to strong reduction of the risk since the beginning of the summer. Historically low yields in the main developed countries were a tangible sign of complacency among bond investors, and that complacency left fixed income investments vulnerable to three key risks: 1) central banks might engineer an unprecedented shift to a less accommodating monetary policy stance; 2) the political agenda was in danger of heating up as anti-establishment movements gathered momentum; and 3) inflation was likely to pick up in the United States. In response, we moved as of July to gradually reduce the Fund's modified duration by shorting US Treasuries and German bunds, by taking profits on our various sources of bond performance (peripheral sovereign debt, commodity-related credit and credit to the financial sector and by adjusting our allocation to emerging market debt).

A Trump presidency, which includes a powerful fiscal stimulus programme, tax cuts and protectionist measures, can be seen as an accelerator of the trends we identified this past summer. We will therefore be maintaining our negative interest-rate sensitivity. At the same time, we will continue to actively manage allocation to our three key fixed income performance drivers, i.e., subordinate debt issued by European banks, European CLOs and emerging market debt, primarily from commodity-exporting countries (for which we have significantly reduced our foreign exchange risk).

REDUCED FIXED INCOME RISK IN CARMIGNAC PATRIMOINE



Source : Carmignac, 10/11/2016

Towards 2017: risks to monitor

As 2017 draws near, a number of unanswered questions call for special attention. First, the pace at which sovereign bond yields increase will have a determining impact on stock market trends. Equities could withstand a controlled rise in yields, but only if it takes place in anticipation of an economic upswing, rather than just as a reaction to monetary policy normalisation and to mounting budget deficits.

Second, the high level of global government debt is an issue that might make it hard for investors to gain a clear sense of how sustainable that government debt is.

Third, the protectionist measures championed by anti-establishment parties in various countries could eventually bring about a falloff in world trade that would penalise all exporting countries, first and foremost emerging markets.

Along with those specific risks, we will use the active management of both our exposure to equities and credit and the modified duration of our portfolio so as to support our primary performance drivers, based on how we view the risk curve going forward.

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