CARMIGNAC
INVESTING IN YOUR INTEREST

LETTER FROM EDOUARD CARMIGNAC

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EDOUARD CARMIGNAC'S LETTER

Edouard Carmignac writes on current economic, political and social issues each quarter.

CARMIGNAC
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Paris, October 1, 2015

Dear Investor,

Yet another year with no summer break for the financial markets. More to the point: the gyrations they experienced in August wiped out a large chunk of the gains made by a number of our funds since the start of 2015.

Quite frankly, our active management style should have averted such a loss of value. And it wasn't as if our staff spent the summer sunbathing, either. The slowdown in China – now widely recognised as what triggered the market turmoil – certainly didn't catch us off guard. Nor did the slackening pace of global economic growth. In fact, that was what prompted us as far back as summer 2014 to start overweighting defensive stocks.

What did come as a surprise was the depreciation of the Chinese currency. Now, 3.5% against the dollar isn't a big decline, but it was enough to raise the spectre of a substantial contraction in global liquidity. Chinese investors – already rattled by a slowing economy – began to fear a major devaluation of the yuan and set off large-scale capital flight (an estimated $180 billion in August alone) that drove the People's Bank of China to defend the currency by scaling back its forex reserves, which consist mainly of government bonds from developed countries. And it's the threat of a plummeting yuan, combined with worries over an impending rate hike in the United States, that has sparked such serious doubts about global liquidity.

As October gets under way, we feel that the risk of dwindling liquidity will remain manageable. Capital outflows from China should taper off as long as the yuan holds reasonably steady; Europe and Japan will likely maintain their ultra-loose monetary policies; and a flagging US economy will make it harder for the Fed to raise its key interest rates.

Of much greater concern to us is the ongoing slowdown in the world economy. Zero interest-rate policies in the advanced world won't provide an adequate firewall against the deceleration under way in emerging markets. While current signs indicate that our growth stocks with good visibility will continue to hold their ground, we intend to be extremely cautious in the upcoming period of turbulence so as to sustain our enviable long-term track record and protect your capital in the event of a severe market correction.

Sincerely,

Edouard Carmignac