INVESTMENT FOCUS

EUROPEAN EQUITIES: **UPSIDE POTENTIAL DESPITE HIGH VOLATILITY** OVER THE SHORT TERM

Fund flows rather than fundamentals are **influencing today's environment**

European equities returned +8.22% in 2015 but this performance masked increased asset price fluctuations. Trading was very choppy with several swings of between 15-20%. Strong rises gave way to steep falls. For example, the MSCI Europe (NR) in EUR gained 21.6% between January 1st and April 15 2015 but then suffered a maximum drawdown of 17.6% (between mid- April and the end of August[1]) before rallying in the subsequent months and finishing the year 8.22% higher.

In this much rockier environment, the question is therefore how to benefit from the potential rerating of European equities. Answering the question means taking the investment horizon into account.

VOLATILITY IS STILL RISING

Since the beginning of 2016, ongoing risks from oil prices, China's exchange rate policy and the question of monetary policy efficiency have led to persistently high volatility. Markets seem to be taking the most pessimistic assumptions for granted in an environment which is influenced more by fund flows than fundamentals, but Edmond de Rothschild Asset Management (France) believes that European equities now have significant upside because of the continent's underlying economic resilience.

There are four main reasons why equity market volatility has been high since April 2015.

First, historic performance drivers have weakened while sensitivity to economic surprises is now more acute. This is due to slowing productivity gains in major developed nations and a change in China's growth model.

Lack of central bank coordination has also fuelled volatility while surplus liquidity on global markets has led to potentially massive capital flows and increasingly large fluctuations in fundamental equity valuations.

Geopolitical risk has also resurfaced both in Europe, which is now facing the risk of the United Kingdom leaving Europe (Brexit) and Catalonia's aspirations for independence, and in the rest of the world with serious tension between Saudi Arabia and Iran for example.

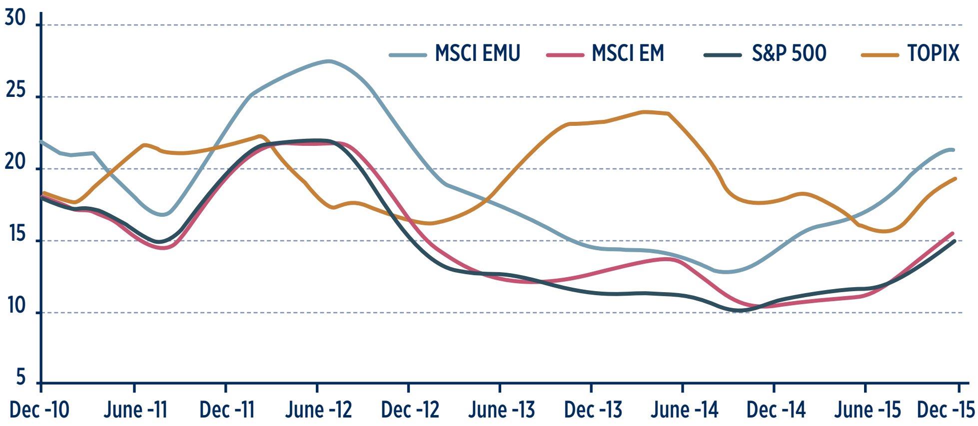
European equities have been particularly badly hit by this turbulence in spite of strong support factors and Europe's resilient economy: over a year, the Eurostoxx 50 has seen a record 23% in volatility, even higher than the

1. MSCI Europe (NR) in EUR from 15/04/2015 to 29/09/2015. Source: Edmond de Rothschild Asset Management (France).

16% seen in emerging countries (currencies unhedged)[2].

This has led to a disconnect between company fundamentals and economic reality with the oil price becoming a new source of risk. But any stabilisation in the oil price could trigger a move back to valuations that would be more in tune with the eurozone's genuine economic prospects.

MAJOR GLOBAL EQUITY INDICES: 250 DAY VOLATILITY



Source: Edmond de Rothschild Asset Mangement (France) – December 2015.
Figures refer to previous years. Past performance is not necessarily a guide to future returns.

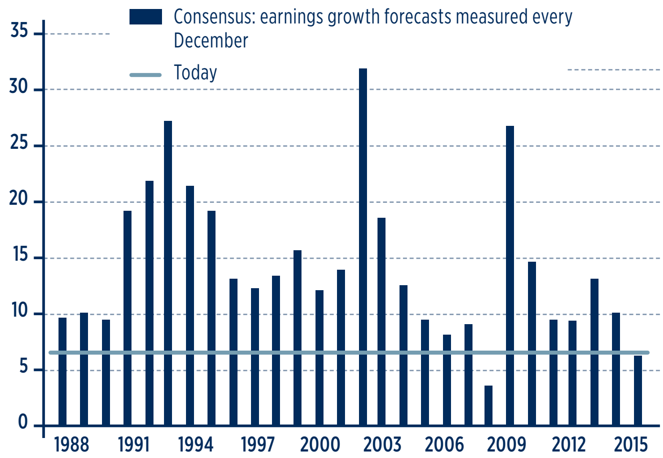
EUROPEAN EQUITIES: UPSIDE IS STILL INTACT

European companies and especially those in the eurozone have been hit by this volatile environment. And yet they offer, according to Edmond de Rothschild Asset Management (France), significant upside as they still have better visibility than other geographical zones. The weak euro, recovering growth, falling unit labour costs and very cheap commodities are all providing support to eurozone equity performance. France, for example, has benefited in full from lower oil prices as almost half (0.4%) of the 1.1% in growth seen in 2015 can be attributed to the oil price slump[3]. In another positive indication, Germany posted a record trade surplus of EUR 248bn in 2015 thanks to exports rising more than 6%[4]. Looking beyond these favourable points, eurozone companies have pressed on with the restructuring that first started during the 2008 financial crisis. This has allowed them to optimise structures and balance sheets and should help them boost any additional growth especially as earnings expectations for 2016 are particularly cautious.

There seems to be **greater visibility** on **European companies**

But Europe is not an island and its companies are necessarily impacted by international factors. This leaves investors in a paradoxical situation: European equities appear to offer significant upside but are also highly volatile.

FORECAST EARNINGS GROWTH



Source: Barclays Equity Strategy – December 2015.

European stocks boast **optimised structures** and **balance sheets**

As a result, investors have to include two essential points in their investment processes: an asymmetrical performance target (capturing part of equity market rises while cushioning any market declines) and the strategy's investment horizon. This is the approach adopted by Edmond de Rothschild Fund Europe Flexible, which tactically manages equity market exposure, and Edmond de Rothschild Fund Europe Value & Yield which modulates allocation to its performance drivers.

2. Source: Edmond de Rothschild Asset Management (France) – data at end January 2016.
3. Source: INSEE.
4. Source: Federal Statistical Office - Germany.

INTERVIEW

EDMOND DE ROTHSCHILD FUND EUROPE FLEXIBLE : **A FLEXIBLE, RESPONSIVE STRATEGY**

Michaël Nizard
LEAD MANAGER, ASSET ALLOCATION MANAGER

Flexible, tactical allocation over the **short to medium terms**

YOU RUN EDMOND DE ROTHSCHILD FUND EUROPE FLEXIBLE[5]. HOW DOES THE FUND TACKLE MARKET UNCERTAINTY?

Edmond de Rothschild Fund Europe Flexible is a flexible fund which seeks to participate in positive European equity market momentum while limiting downside in highly volatile periods[6]. To do so, we combine two approaches: (i) our group's expert stock selection to create long term value and (ii) active management of equity exposure between 0% and 100% via flexible tactical allocation over the short to medium terms.

Thanks to the fund's active management of market exposure, it is particularly well suited to investors looking to invest in equities but without their volatility and all associated risks.

GIVEN THE VOLATILITY SEEN IN 2015, YOUR INVESTMENT APPROACH WAS REALLY PUT TO THE TEST. HOW DID YOU MANAGE YOUR PORTFOLIO?

2015 was overall a positive year for European equities but it was a very 12 months with a succession of favourable periods and severe market shocks. There were many factors driving volatility and we had to remain very flexible to actively manage our market exposure.

For example, we kicked off 2015 with an upbeat stance on equities and around 75% market exposure due to attractive valuations and the economic recovery in Europe.

After two good months, we started to reduce exposure significantly, taking it down to 35% after observing some risk factors and taking consensus views on board; that helped us significantly cushion the market retreat after April. Following the market capitulation over the summer due to the Asian shock, we raised exposure to its maximum 100% level as we considered the market had bottomed out. That helped us benefit in full from the rebound up to the end of November.

The ECB had proved unusually proactive at the end of November when it argued in favour of further easing but we took the view that there was a high risk of disappointment and so preferred to cut portfolio risk ahead of the actual ECB meeting. Once again, that helped us limit downside as markets fell back in December.

We eventually ended the year 10.4% higher which placed the fund in the first quartile of its Morningstar category. In comparison, the DJ Eurostoxx 50 and the MSCI Europe (NR) gained 6.4% and 8.9% respectively while posting much higher volatility and drawdown[7]. Note that the composite index 50% Eonia - 50% MSCI Europe, with which the fund may be compared, ended the year 4.5% higher.

WHAT DO YOU RECOMMEND FOR 2016?

Volatility will remain high and our strategy will be to deploy a resolutely tactical investment approach in line with our convictions and our medium term outlook. We were rather early in spotting the shift in the market's volatility regime in 2015 and thus able to significantly cushion the downward trend after

We will continue to **actively manage exposure** to **avoid the full impact of market shocks**

April 2015 and we are now looking to increase exposure ahead of the market's next upward cycle. Experience shows that periods of excessive pessimism, where fund flows and sentiment dictate the trend, create excellent investment opportunities as markets always ended up returning to fundamentals.

Generally speaking, Edmond de Rothschild Fund Europe Flexible's strategy seeks to help the portfolio weather turbulent phases and then capture some of the gains in bullish periods.

The subfund was a French-regulated FCP up to 22/01/2016. Past performance is not necessarily a guide to future returns.

5. Edmond de Rothschild Fund – Europe Flexible is a sub fund of the Luxembourg-regulated SICAV which is approved by the CSSF and approved for marketing in France and Luxembourg. The fund manager may change during the product's life.

6. Wrong assumptions may mean that investors do not totally benefit from rising phases on the various markets to which the fund is exposed.

7. Data from 31/12/2014 to 31/12/2015 (A share).

Source Edmond de Rothschild Asset Management (France). Performance since launch (31/01/2009): +47.91% (+126.4% for the MSCI Europe NR, +46.07% for the Eurostoxx 50 and +45.4% for the fund's benchmark, the "50% Eonia – 50% MSCI Europe"). Morningstar ratings are not market ratings and cannot be interpreted as recommendations to buy, sell or hold units or shares in mutual funds managed by Edmond de Rothschild Asset Management (France). Reference to a ranking or award given to this fund is not an indication of future performance by these funds or the fund manager.

KEY POINTS

- Two complementary strengths: European stock picking and flexibility
- Equity risk is managed on a dynamic and permanent basis
- A strategy that can adapt to all market environment
- Targeted returns over a complete economic cycle in return for a capital loss risk
- Active conviction-driven investing on European equity markets

SUBFUND INFORMATION*

Inception date: 30/01/2009, transfer date to the SICAV EDRF: 22/01/2016

ISIN Codes
'A' Share: LU1160352602
I Share: LU1160353089

Maximum management charges
'A' Share: 1.70%/I Share: 0.75% max.

Variable management fees
15% of performance in excess of the benchmark

Minimum initial subscription
'A' Share: 1 share
I Share: EUR 500,000

Front load charge: 4.5 % max.

Redemption charges: None

Benchmark
50% MSCI Europe dividends reinvested (EUR) and 50% capitalised EONIA

Recommended investment horizon
> 3 years

* Share classes described herein are the main euro-denominated share classes. The fund also has USD, GBP and CHF share classes. Please ask your sales contact for any further information.

PRINCIPAL INVESTMENT RISKS

Edmond de Rothschild Fund – Europe Flexible is a sub fund of the Luxembourg-regulated SICAV which is approved by the CSSF and approved for marketing in France, Austria, Belgium, Switzerland, Germany, Spain, England, Italy, Netherlands and Luxembourg.

The fund is a category 5 (on a scale of 1-7) or high risk/return fund profile which reflects its ability to have equity market exposure of between 0% and 100%.

The risks described below are not exhaustive: it is the responsibility of investors to analyse each investment's risk and to come to their own opinion.

Capital loss risk: as the sub fund does not have any guarantee or protection, the capital initially invested might not be restituted in full even if subscribers hold their shares over the recommended investment horizon.

Discretionary management risk: discretionary management depends on anticipating future trends on equity and bond markets. There is a risk that the sub fund might not always be invested in the best performing stocks. The same applies to its exposure to one asset class rather than another. The sub fund's performance may fall short of its investment objective and the fall in its net asset value may lead to negative performance.

Equity risk: The sub fund may be exposed to equity markets through direct investments in shares and/or through financial contracts and/or mutual funds. Equity market fluctuations may entail changes in the fund's net valuation and might have a negative impact on the sub fund's performance. If equity markets fall, the sub fund's NAV might also fall. The sub fund may have a risk and volatility profile that might entail larger price fluctuations than for the overall equity market. The use of financial contracts to reduce the portfolio's exposure to equity risk is likely to modify the sub fund's risk profile.

Interest rate risk: this might entail a capital loss from rising yield curve movements. Bond prices move in opposite directions to bond yields. The impact of a move in interest rates is measured by the sub fund's sensitivity. Sensitivity measures the possible impact on the sub fund's NAV of a change in interest rates. For example, if rates rise by 1% and the sub fund's sensitivity is +4, the fixed income assets in the sub fund will fall by 4%. The sub fund's NAV may also decline if its sensitivity is negative and the yield curve falls.

Credit risk: the main risk is issuer payment default on interest payments and/or on reimbursement of the capital. Credit risk also concerns issuer downgrades. Subscribers are warned that the sub fund's net asset value could fall should a total loss be incurred on a transaction due to counterparty default. Any private company debt held directly by the portfolio or through the sub fund exposes the sub fund to changes in the issuing company's credit rating.

Liquidity risk: Low liquidity in underlying markets could make them sensitive to significant buying or selling.

Counterparty risk: a default by a market participant could prevent the participant respecting its commitments to your portfolio.

INTERVIEW

EDMOND DE ROTHSCHILD FUND EUROPE VALUE & YIELD IS A **LONG TERM EQUITY STRATEGY**

Philippe Lecoq
LEAD MANAGER

Our main objective is to **select companies with inherent upside**

EDMOND DE ROTHSCHILD FUND EUROPE VALUE & YIELD IS A LONG TERM EQUITY STRATEGY. BUT HOW ARE YOU MANAGING THE POTENTIAL IMPACT OF TODAY'S VOLATILITY ON THE FUND'S SHORT TERM PERFORMANCE?

Stock picking is the main source of added value in this European equity fund. We strive to roll out conviction-driven investing and that could entail wide sector and geographical deviations with indices. For us, this is a key source of protection. For example, we are currently heavily underweight banks (2% for Edmond de Rothschild Fund Europe Value & Yield vs. 11% our benchmark, the MSCI Europe NR). Our prime objective is to select companies with inherent upside and which are to some extent uncorrelated with index moves. Our stock selection also reflects our investment horizon of above 5 years which means we have fairly low stock rotation.

HOW IS THIS REFLECTED IN YOUR INVESTMENT PROCESS?

We have two performance drivers:
- discounted stocks with strong rerating potential (Value) which help capture equity market rises.
- stocks selected because of the size and sustainability of their dividends (Yield). These are expected to provide some protection if markets fall and also help rein in volatility.

Thanks to this dual approach and allocation which varies in line with market conditions, we can aim at an asymmetrical performance profile. In 2015, we focused on the portfolio's Value envelope.

While steering clear of "deep-value"[8], we sought out companies undergoing restructuring which had strong enough catalysts to trigger reratings. The strategy paid off as the fund outperformed by 4.3% in 2015[9], rising 12.5% vs. 8.2% for its benchmark, the MSCI Europe NR. For 2016 we have turned more cautious. We have taken some profits on the Value envelope and switched to companies with more sustainable dividend payouts. Active in sectors with higher visibility, these companies have a stable payout track record and help protect the portfolio against excessive surges in volatility. Typical examples would be telecoms and healthcare.

WHICH STOCKS DO YOU LIKE AT THE MOMENT?

In the Value envelope, we like domestic plays. According to Edmond de Rothschild Asset Management (France) they have interesting upside because of their exposure to European growth. Restructuring plays, where we have identified catalysts, should also benefit from the multiplier effect of an economic recovery. A good example is Nokia which has excellent prospects both in terms of valuations and yield. The group, which is trading at a discount, is in the process of acquiring Alcatel, the final stages of its drive to refocus its businesses around network infrastructure and research and development. With around 30,000 patents, mostly in telephony, the value of Nokia's assets is not yet reflected in its share price. The group also has large amounts of cash which could be paid out to shareholders in coming years. Another

We favor **domestic value**

example is Peugeot, the car manufacturer with the biggest exposure to the recovering European autos market. Its new CEO, Carlos Tavares, a sector specialist, has successfully completed the restructuring plan and the group should now be able to catch up on the margins posted by its European peers.

Yield stocks generally benefit from a highly visible economic model and robust finances.
This envelope, which we are currently focusing on, seeks to cushion market downswings while curbing volatility. Terna is a good example. Europe's largest specialist in electricity transmission is underpinned by its monopoly in Italy, its home market, and by the fact that this is a non-cyclical business operating within a regulated environment. Terna contrasts with electricity generation companies which are sensitive to shifting commodity prices and its dividend should remain stable as its revenue streams enjoy strong visibility.

Edmond de Rothschild Fund – Europe Value & Yield is a sub fund of the Luxembourg-regulated SICAV which is approved by the CSSF and approved for marketing in France and Luxembourg. The fund managers featured in this document may change during the product's life. Information on stocks may not in any way whatsoever be construed as an opinion of Edmond de Rothschild Asset Management (France) on future price trends in the said companies, nor, where applicable, on the likely price trend of the financial instruments that these companies might issue. Any information herein cannot be interpreted as a solicitation to buy or sell these stocks. **Past performance is not a reliable indication of future returns and is not constant over time.**
8. Deep value stocks are viewed as significantly undervalued and their market capitalisation may be inferior to revalued assets.
9. 'A' share performance of the sub fund Edmond de Rothschild Fund Europe Value & Yield. Performance at end January since inception (02/09/1999): an annualised +5.08 % vs. 3.08 % for the MSCI Europe NR index.

KEY POINTS

- An equity strategy which is particularly adapted to today's market conditions
- An investment approach geared to providing a particularly attractive risk/return profile
- Capital loss risk on equity exposure
- An investment team renowned for its European market expertise

SUBFUND INFORMATION*

Inception date: 02/09/1999, transfer date to the SICAV EDRF: 22/01/2016
ISIN Codes
'A' Share: LU1103283468 / I Share: LU1103284433
Maximum management charges
'A' Share: 1.70% / I Share: 0.75% max.
Minimum initial subscription
'A' Share: 1 share / I Share: EUR 500,000
Front load charge: Maximum 4.5%
Redemption charges: None
Benchmark: MSCI Europe (EUR) (NR)
Recommended investment horizon: > 5 years
Eligible for the PEA (French equity savings scheme): Yes

* Share classes described herein are the main euro-denominated share classes. The fund also has USD, GBP and CHF share classes. Please ask your sales contact for any further information.

PRINCIPAL INVESTMENT RISKS

Edmond de Rothschild Fund – Europe Value & Yield is a sub fund of the Luxembourg-regulated SICAV which is approved by the CSSF and approved for marketing in France, Austria, Belgium, Switzerland, Germany, Spain, England, Italy, Finland, Netherlands, Sweden, Taiwan and Luxembourg.

The sub fund is a category 5 (C, D and I shares) or high risk/return fund profile which reflects its ability to be up to 110% exposed to equity markets. Investments made by the fund are subject to market trends and fluctuations. Investors may not recover the amount originally invested.

The risks described below are not exhaustive: it is the responsibility of investors to analyse each investment's risk and to come to their own opinion.

Capital loss risk: as the sub fund in this document does not have any guarantee or protection, the capital initially invested might not be restituted in full.

Equity risk: share prices may move in line with factors specific to the issuing company but they may also react to external political and economic factors. Equity market fluctuations may entail changes in the sub fund's net asset value and might have a significantly negative impact on its performance. The fund's performance will depend on the companies selected by the asset management company.

Exchange rate risk: this may exist when stocks or investments are denominated in a different currency than that of the sub fund. If the currency of portfolio holdings falls against the sub fund's reference currency, the euro, the fund's NAV could also fall.

Interest rate risk: funds holding debt securities and money market instruments are exposed to fluctuations in interest rates. The risk is as follows: rising interest rates cause bond valuations to fall and thus a decline in the sub fund's net asset valuation.

Credit risk: valuations of debt securities and other financial instruments are influenced by the issuing company's credit rating. As a result, their capital value fluctuates according to the market's perception of the financial health of their issuers and this may entail a fall in the sub fund's NAV if the outlook turns negative. Credit risk corresponds to the risk that an issuer of bonds or money market instruments might not be able to honour his commitments.

February 2016. Non-binding document. This document is for information only.

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