

Fixed income and credit management

Investment Strategy 2010

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INVESTMENT MANAGERS

Our forecasts for 2010 :

Spreads and interest rates:

	Current levels	In 6 months	Expected volatility	Performance 2009	Performance 2010 e	Our Convictions (risk/return)
5 year Euro Bond	2.4%	2.1%	High	3.5%	2-3%	=
Inflation-linked Bonds	1.5%	1,50%	High	8.3%	2.5-3.5%	- -
Investment Grade Credit	132 (Asset Swap, bp)	100 (Asset Swap, bp)	Low	14%	5-7%	+ +
High Yield Credit	611 (Asset Swap, bp)	580 (Asset Swap, bp)	High	60%	9-12%	+ +
Emerging Market Debt	291 (Asset Swap, bp)	250 (Asset Swap, bp)	Average	20%	9-12%	+ +

Source : EdRIM Gestion. Data at 06/01/2010. Figures refer to previous years. Historic data is not a reliable indicator of future figures.

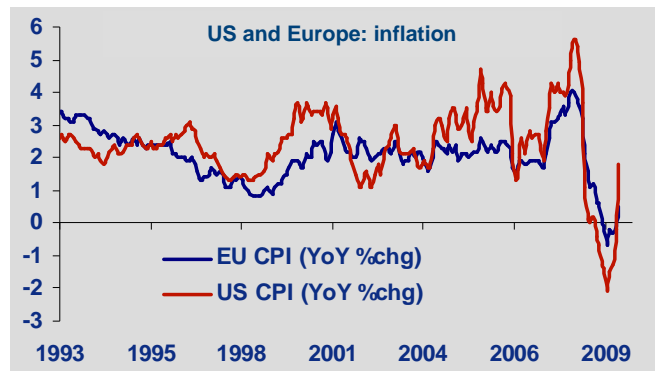
Governments saved the economy in 2008 & 2009
but what will have to be financed in 2010?

Macroeconomic environment: *The equation today is...*

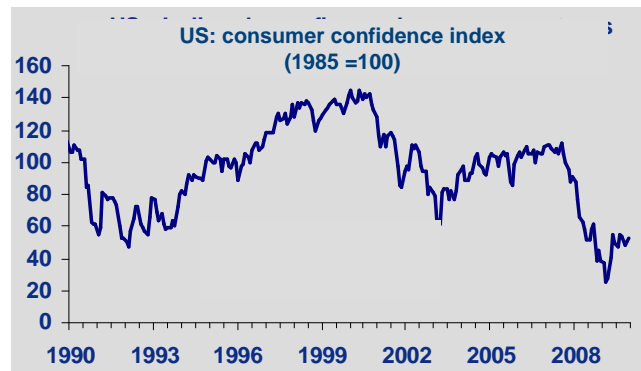
zero inflation...



... doubts on growth rates



Source : Bloomberg – Edrim Gestion – data at end November 2009



Source : Bloomberg – Edrim Gestion – data at end December 2009



Source : Bloomberg – Edrim Gestion – data at end November 2009

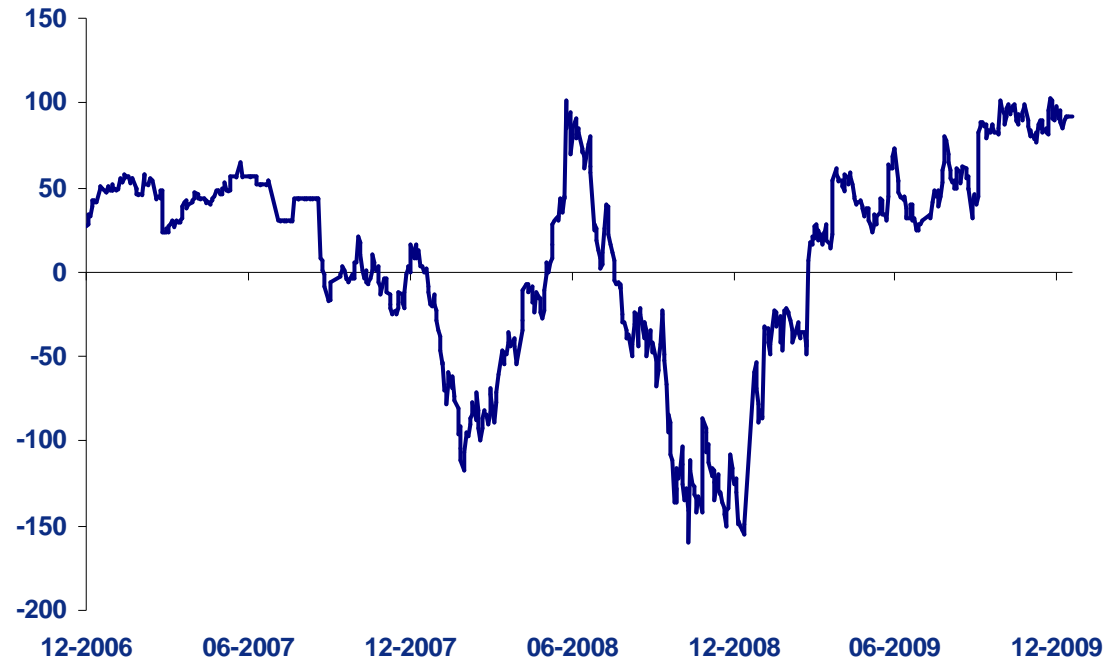
= returns



Credit is the asset class for this environment

Main refinancing rates: *Focus on Europe*

Expected trend in interest rates in 12 months (bp)



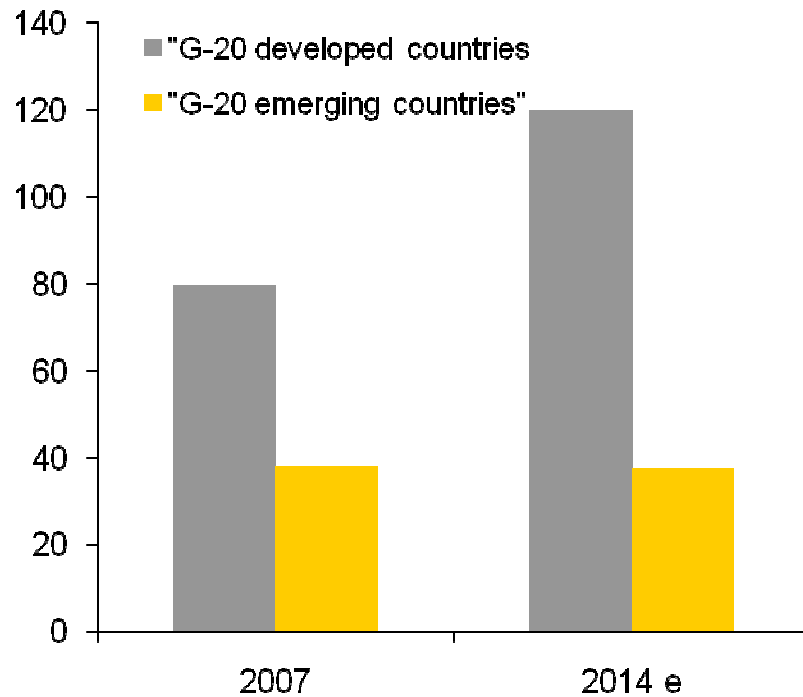
Source: Bloomberg, Crédit Suisse, EDRIM Gestion, données au 29/12/2009

Main refinancing rates expected to rise by 100bp in 2010

Risks to watch out for in 2011-2012:

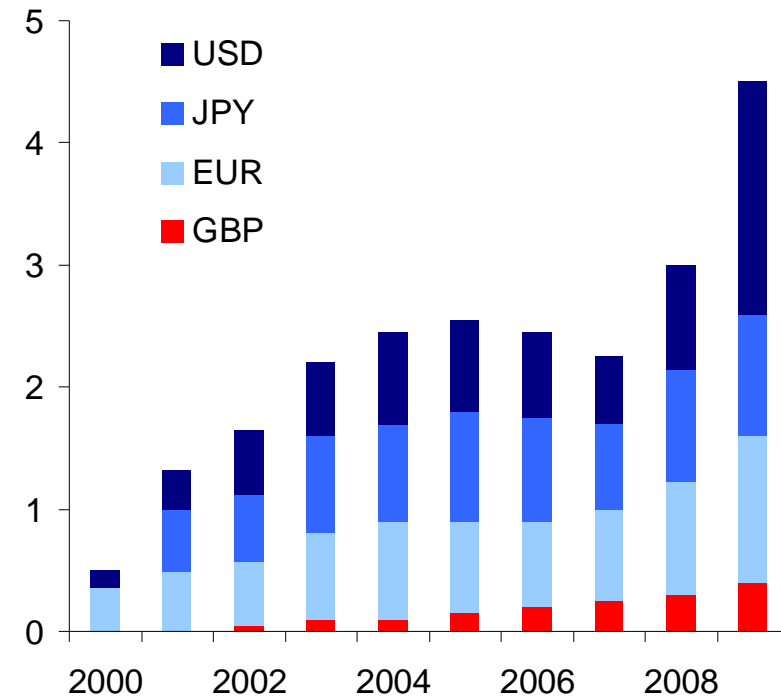
Increase in sovereign debt in developed countries (1/2)

Gross sovereign debt % GDP



Source : IMF World Economic Outlook. 2014 = IMF projection

Gross issuance of sovereign debt 2009 YTD, \$tn



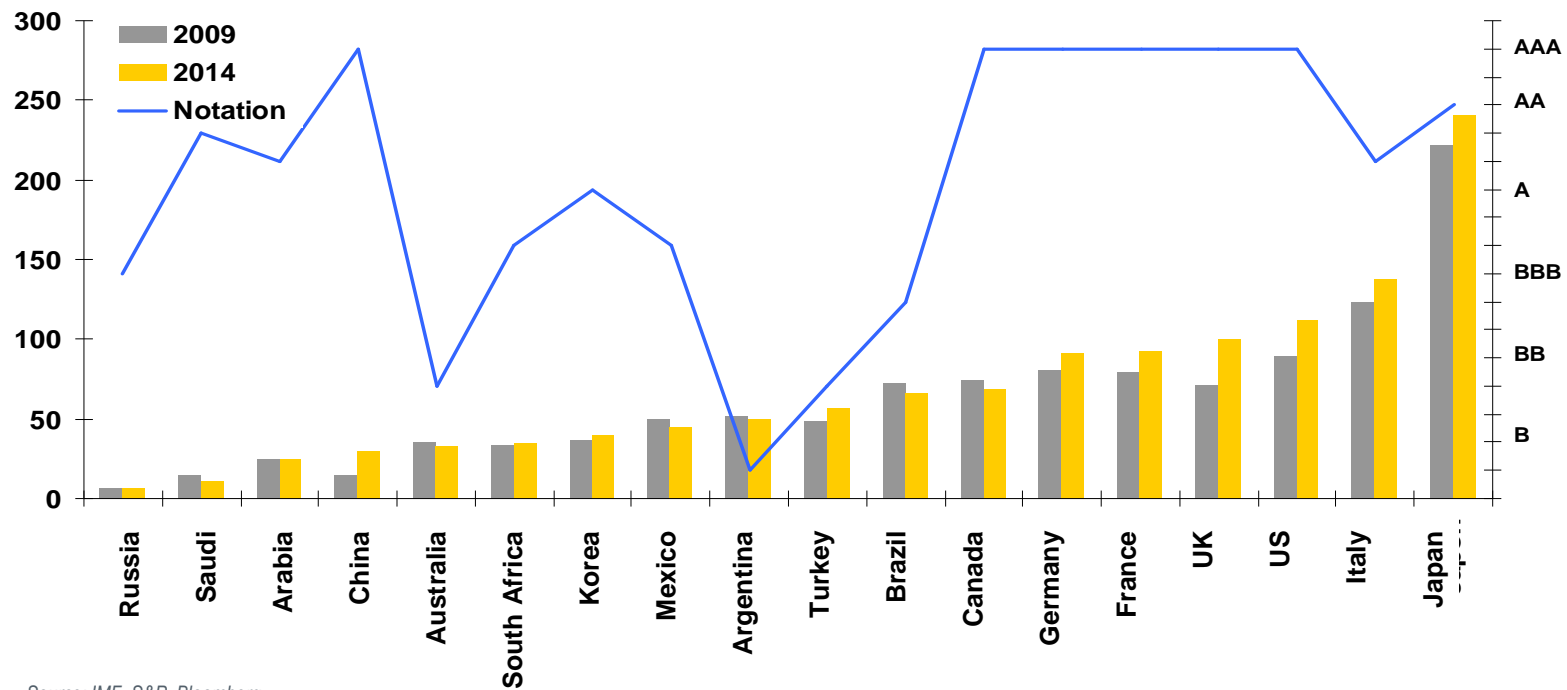
Source : Dealogic

Higher sovereign credit risk in developed countries compared to emerging countries

Risks to watch out for in 2011-2012:

Increase in sovereign debt in developed countries (2/2)

Gross sovereign debt (%GDP) vs S&P rating



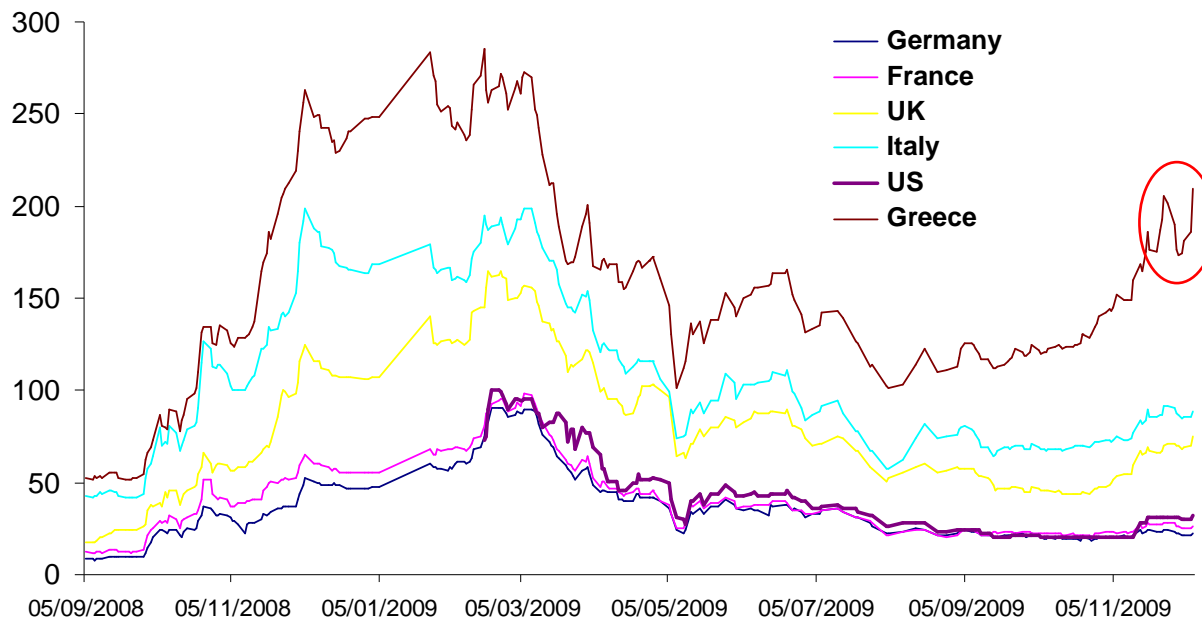
Source: IMF, S&P, Bloomberg

Potential for very unstable ratings as the most debt-laden countries have the highest ratings

Early warning signs

- Fitch downgraded Greece from A- to BBB+ on December 8. The Credit Default Swap on the 5-year maturity went from 186 to 209 bps on the news.

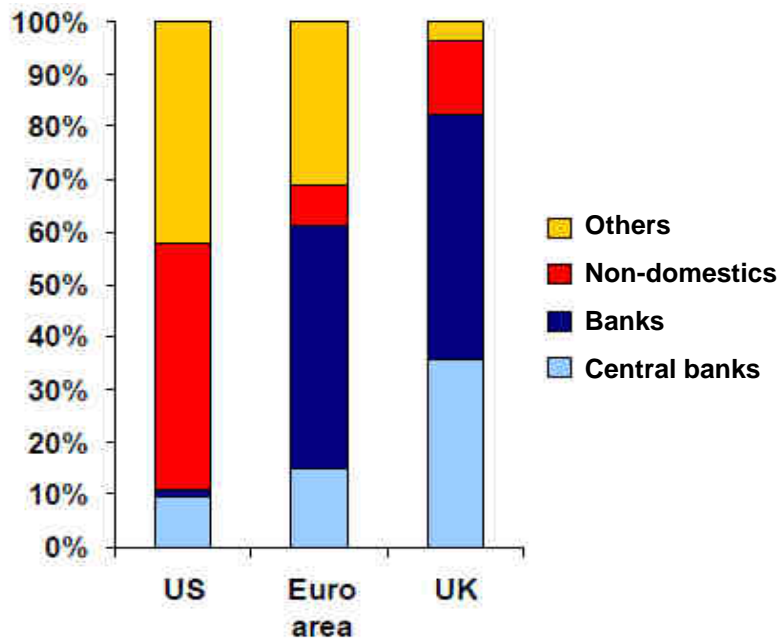
Sovereign Credit Default Swap, 5 year maturities



Source: Bloomberg, EDRIM, données au 08/12/2009

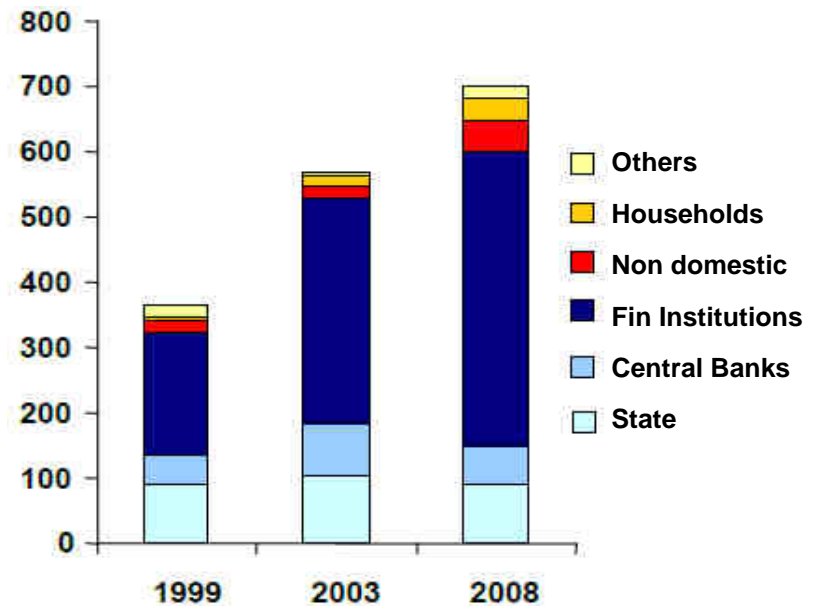
Government bonds: Who's buying?

Government bond buyers:
Q2 08, Q2 09, % net issues



Source: Federal Reserve, ECB, Bank of England.

Japan:
Japanese government bonds (JPYtn)



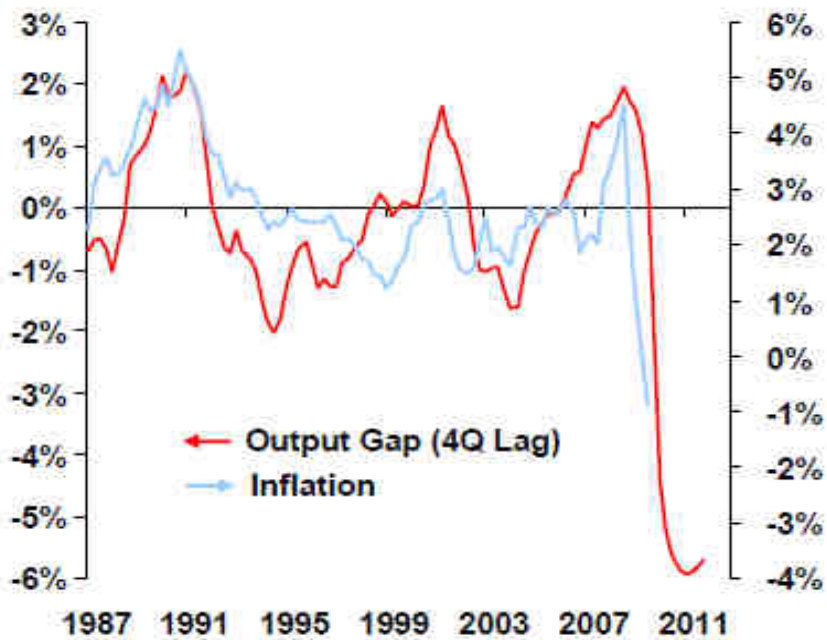
Source: Bank of Japan.

* Postal Savings classified as a financial institution even prior to privatization to ensure

Banks will continue to buy significant amounts of government bonds

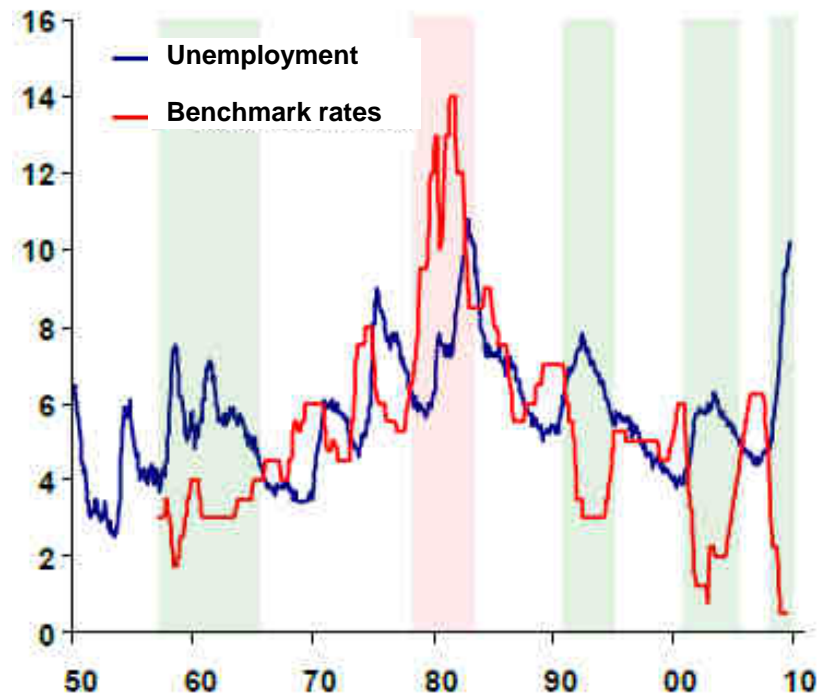
Risks to watch out for in 2011-2012: *Inflation*

Inflation & output gap



Source: OECD, Reuters Ecowin.







Benchmark rates vs unemployment (%)



Source: Reuters Ecowin.

The output gap means we are not worried about inflation reviving in 2010

Fixed income markets: outlook

Macroeconomy	
Inflation	
ECB	
Technical factors	
Value	
Score Change in market price	

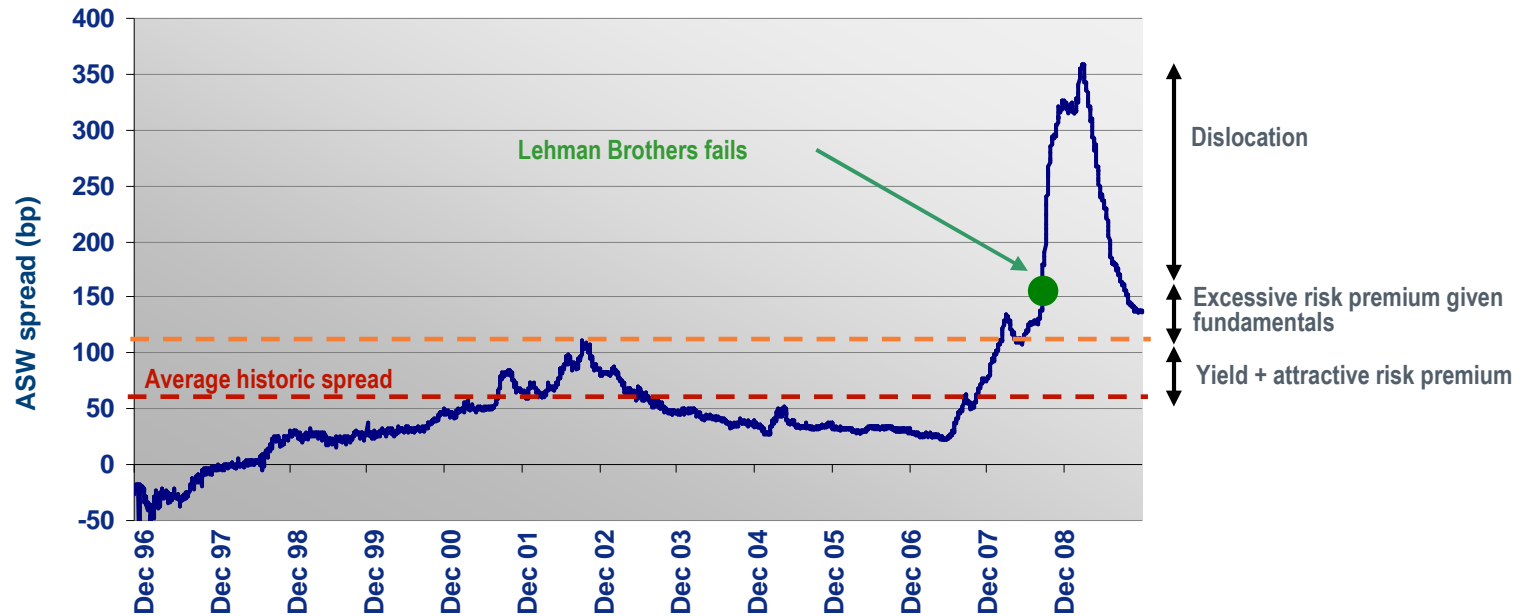
- **Improvement in the economy:**
Commercial bank buying will compensate for the scheduled end to central bank quantitative easing
- **Inflation should not be a problem in 2010:**
Output gap
High unemployment (10%) in developed countries
- **ECB main refinancing rate should remain low coupled with a steep yield curve**
We expect a bull flattening
- **Fund flows will provide support:**
Regulatory and prudential rules force some institutionals to continue investing in government bonds
- **EONIA abnormally low, below benchmark rates for some months to come**

*Macroeconomic picture improving thanks to counter-cyclical fiscal and monetary policies.
Inflation should not return before 2011*

Investment Grade credit: *Market still attractive after excellent performance in 2009*

→ Corporate issuers still offering high premiums of around 150bp

Investment Grade Euro Corporate index (1998 -2009)

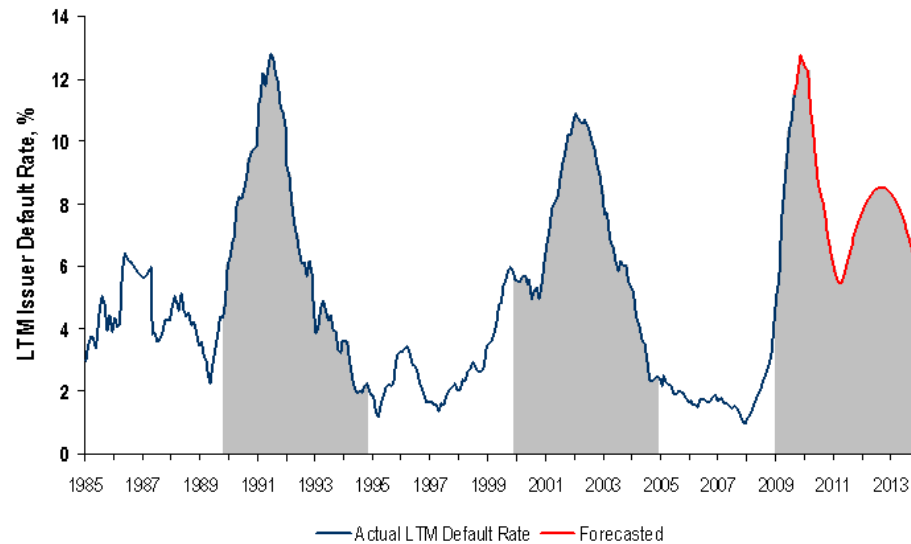


Sources : Merrill Lynch – EdRIM, données au 31/12/2009

Current premium far higher than average historic Investment Grade spread of 60bp

High Yield credit: *Peak default rates now behind us*

HY default rate (Moody's)









Forecasts 2009 (Moody's)

<i>End 2009 estimates</i>	<i>Moody's</i>
<i>World</i>	<i>12.50%</i>
<i>Europe</i>	<i>11.40%</i>
<i>US</i>	<i>13.20%</i>

- ➔ **Defaults:** Mecachrome, LyonDellBasell, Belvedere, Escada
- ➔ **Coupon non-payment:** Akerys, IT Holding, Thomson SA, Hellas
- ➔ **Distressed exchange :** TNTLOG (Ceva Logistics)

*Estimates of default rates in 2010
have fallen significantly*

Credit market outlook

Macroeconomy		
Fundamentals		→ Company fundamentals are no longer deteriorating Companies have repaired balance sheets
Value		→ High Yield defaults forecast for 2010 have gone below the 4% level (source: Moody's).
Market sentiment		→ The market environment is pushing investors towards credit (Investment Grade)
Technical factors		→ After a record 2009, the primary market in 2010 should slow in Investment Grade, but still remain strong. The High Yield segment is expected to be particularly active.
Score Change in market price		→ We expect Investment Grade credit to yield 2 to 3% more than government bonds. High Yield credit is expected to return around 10%.

Less directional performance that will be balanced between capital gains from spreads narrowing and carry

Saint-Honoré Bond Allocation

A multi strategies bond fund

Objectives

- Outperform the composite index of 50 % Barclays Capital Euro Aggregate Corporate Total Return / 50% Barclays Capital Euro Aggregate Treasury Total Return
- Preserve capital over a medium to long term horizon

Key points

- Conviction-based management with a large tracking-error; a concentration of the best ideas of the Fixed Income and Credit team
- Important diversification of assets, strategies and sectors across all bond markets
- Modified duration is managed within a large spread (-2 ; +8)
- A product adapted to all market contexts thanks to dynamic allocation across all bond assets

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SAS à Directoire et Conseil de Surveillance au capital de 3.000.000 Euros

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