

The & Letter

Funds & Strategy

Number **101**
February 2011

SUMMARY

Editorial	1
Web site	2
Economic environment	3
A good first quarter in a shaky environment	
Core management	4-6
One swallow does not a summer make	
Money-market management	4
Upheaval in the monetary markets	
Fixed income management	5
Caution remains the order of the day	
Equity management	6
Rose-colored glasses as the year begins?	
Diversified management	7
Resisting the height(s)	
In the blink of an eye	8

Completed in February 16th 2011

EDITORIAL



Investment – together
under one roof

This spring season of risky assets bloomed early and vigorously. We don't (yet) think that signals a return to a normal cycle of seasons in the financial markets. This newsletter reports on the gray skies overhead. Now more than ever, selectivity and responsiveness are the watchwords that will help us weather the violent rotations among asset classes and within them – in particular, sectoral. More than ever, investors and asset managers must work together to find high-performing solutions to what is certain to be sustained instability. They share space under the same roof in this 'investment building' whose different rooms are close to each other. Moving from one room to another in that building is less a matter of entering new territory than it is finding – close by -- professional teams that hold true investment convictions, united around shared values.

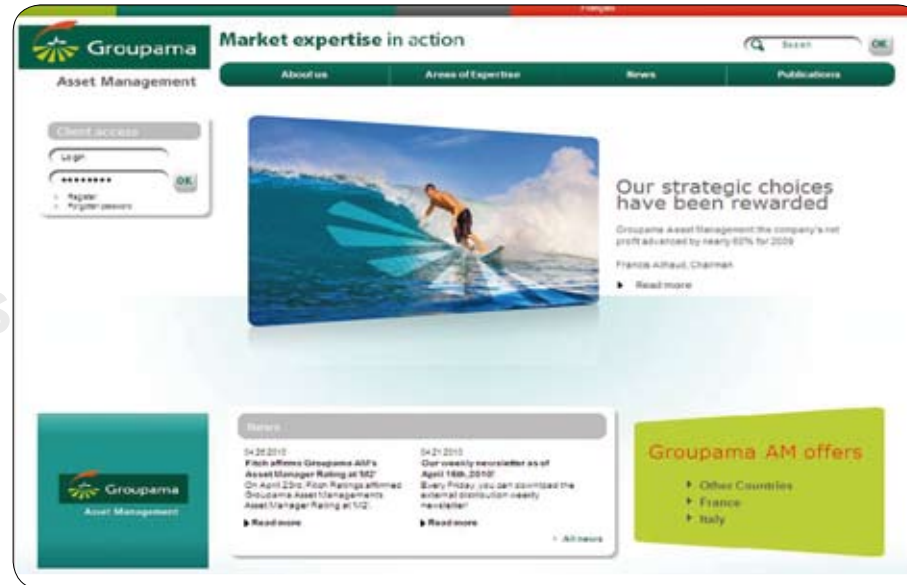
Antoine de Salins,
Chief Investment Officer
Groupama Asset Management

The Actively Responsible Asset Manager

Groupama Asset Management - Communication department:
58 bis, rue La boétie - 75008 Paris - Tel.: +33 (1) 44 56 79 18 • Fax: +33 (1) 56 59 40 93
www.groupama-am.fr • Numéro ISSN:1634-9032



Asset Management



Expertises
Performance
Economic analysis
Anticipation

Funds
Economic analysis
Tendance
Projection



Anticipation
Funds
Projection
Tendance

Projection
Tendance
Economic analysis
Anticipation

Find the full presentation of our products on our website www.groupama-am.com.

View the entire range of our funds, their presentation, features, and of course performances.

You will also find all the news and our downloadable publications.



United States

GROWTH STEADIES, STRUCTURAL CRISIS CONTINUES

Preliminary estimates of fourth-quarter growth place it at 3.2%, compared to 2.5% in the prior quarter, confirming the guiding principles of our scenario. The sharp reversal in the inventory cycle has been documented – occurring one quarter earlier than expected, it reduced growth by 3.4 points. Given overcapacity, the 3% contraction in company capacity spending should continue. Investment in information and communication technology (ICT) remains strong, increasing by 10% annually. As expected, residential investment has stabilised. Household consumption recorded its highest growth since early 2006 – 4.3% – while purchasing power has been treading water for four months. However, the one-point drop in the savings rate cannot continue. The real estate market remains in crisis, prices continue to fall and households still face tight financing constraints. Consumption should return to an average rate of 2%, compatible with the creation of 200,000 jobs, on average, per month. Last, the sharp contraction in the GDP deflator in the goods sector shows that fears of internal deflation are well-founded, even if overall inflation is rising again, impacted by energy prices. The first quarter should be solid, supported by world trade and the temporary build-up of restocked inventories, which had fallen too low.

Euro zone

SOVEREIGN DEBT CRISIS STIFLES EVERY SIGN OF RECOVERY IN DOMESTIC DEMAND

Growth, estimated at 0.3%, remained weak in the fourth quarter, punished by harsh weather and widespread weakness in consumer spending, except in France, where it was boosted by the scheduled end of the car-scrappage bonus program. The 0.5% contraction in GDP in the U.K. reflects these two developments: weather conditions, which caused GDP to fall 0.5%, and consumer spending, which headed up before the January hike in the VAT.

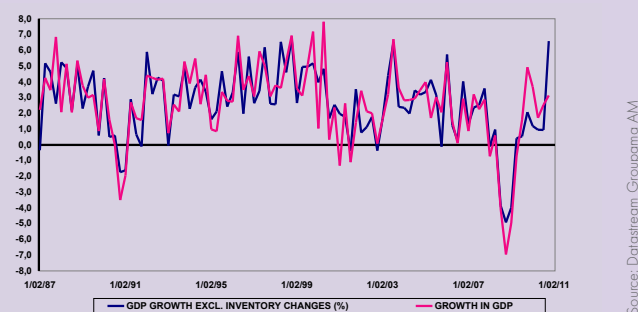
Growth should improve temporarily in the first quarter, catching up after the storms and thanks to the rebound in world trade. But beyond that, it will remain severely constrained by budget consolidation, increased unemployment – reaching historic highs in several peripheral countries – and the widespread worsening of employee purchasing power, resulting from rising energy prices. Continuing pressures on bond markets in the peripheral countries and continued rise of long-term interest rates in core countries remain a cause of considerable concern for growth. This has created a new hardening of credit conditions for households and the troubling slowdown in the Italian economy. Driven by energy and food prices, inflation in the Eurozone has risen to 2.4%. Underlying inflation remains stable and low.

Japan

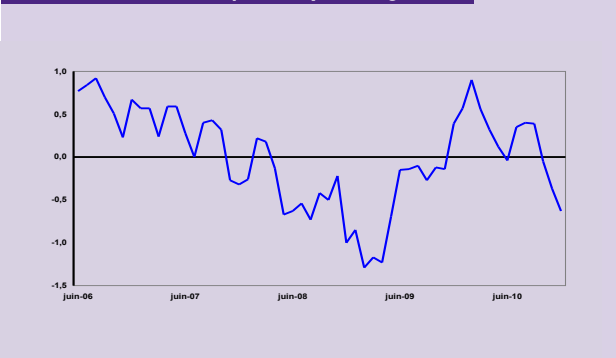
EXPORTS REBOUND BUT DOMESTIC DEMAND SHRINKS

Based on early estimates, GDP shrank 0.3% in the fourth quarter, affected by the correction in the automobile market. However, household consumption, which lost 0.4 points of growth, continues to fall. The reversal in late 2010 retail sales indicates a drop in household consumer spending that is much more sustained and fundamental than technical. Japanese households are experiencing declines in purchasing power due to a reversal in average compensation, while steady employment worsens. Companies are reducing payroll expenses after squeezing margins, an action intended to absorb the sharp appreciation in the yen. Facing this profitability shock, companies also had to reduce investment spending in the first quarter, as indicated by the recent drop in new domestic orders for capital goods and the fall in construction starts in the commercial real estate sector. Growth in the first quarter will thus continue to be affected by the general decline in components of domestic demand. However, as foreign trade continues to strengthen and the yen stabilises, Japan will return to growth.

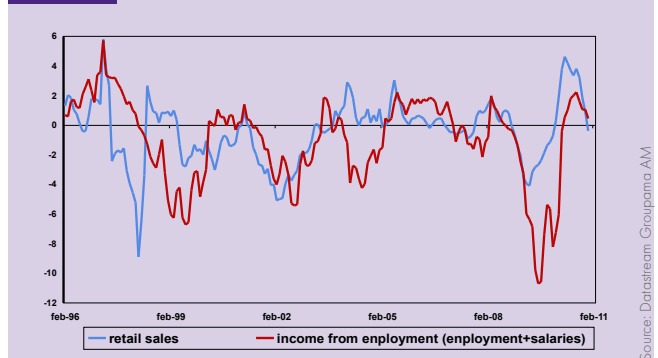
United States: growth excl inventory changes strengthens as a result of household consumption and sharp decline in imports (%)



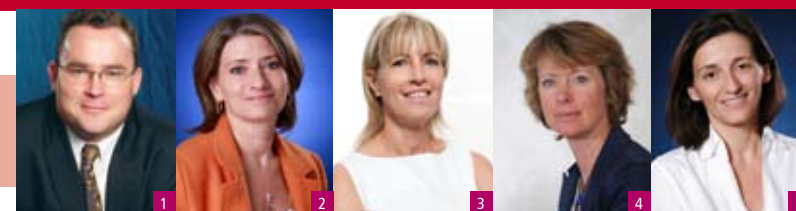
Euro zone: retail sales fall again for the first time since 2008 (retail sales, quarterly change, %)



Japan: retail sales relapse as a result of decline in earned income



CORE MANAGEMENT



Money Market Management

One swallow does not a summer make!

Pleasant surprises marked the beginning of this year: better-than-expected economic growth, bond issues from peripheral countries that are doing well and a Eurozone that appears better orchestrated. However, let's not be overly optimistic. Things are moving in the right direction, but it's too early to jump to conclusions. The issues have been successful because all steps were taken in advance to ensure that outcome and, while this may resolve the risk of illiquidity, it does not change anything in terms of insolvency. Banking sector financing has not been resolved and monetary normalisation has not been achieved. In brief, we can anticipate a sharp economic slowdown ahead. We thus take due note of this «improvement,» while maintaining an optimistic – but reasonable and prudent – position.

P-H.B

CENTRAL BANKS

■ Upheaval in the monetary markets.

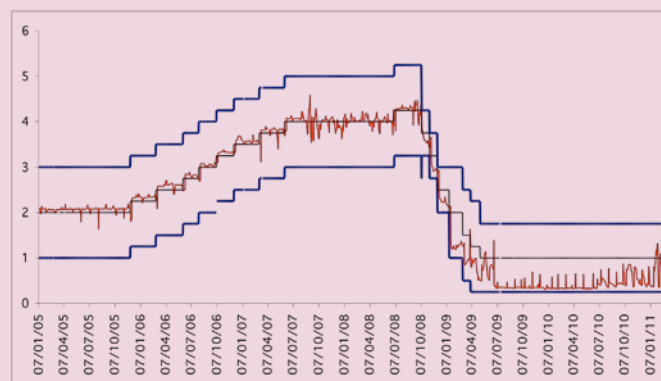
The monetary markets have experienced high volatility since the year began. The EONIA rate was around 0.40% during the first two weeks of January, headed to 0.70% - 0.80% levels, and subsequently crossed the 1% threshold, reaching a high of 1.318% on 1 February.

These pressures were primarily the result of a technical factor. The reserve maintenance period was exceptionally short – three weeks compared to six for the prior period and to four, in general. The banks thus relied heavily on the market. From our point of view, these pressures should not be confused with a normalization of the monetary markets. Don't forget that almost 15 banks are still completely dependent on the ECB for their refinancing.

While our scenario includes high volatility in the monetary markets, we do not expect refinancing rates to rise in the medium term. Against a backdrop of gradual «resolution» of Eurozone countries' debt crisis and the resumption of still-fragile growth, we remain relatively cautious. The combination of low rates and unlimited liquidity argues for an EONIA rate below the refinancing rate.

With an unemployment rate exceeding levels compatible with its mandate and an inflation rate that's below, the Fed says it's ready to pursue its accommodationist policy even if the economic situation improves.

Corridor, refinancing rate & EONIA
EONIA average capitalised over 2010: 0.43%



Source: Bloomberg

A WORD ABOUT THE INVESTMENT STRATEGY

■ Fund strategy.

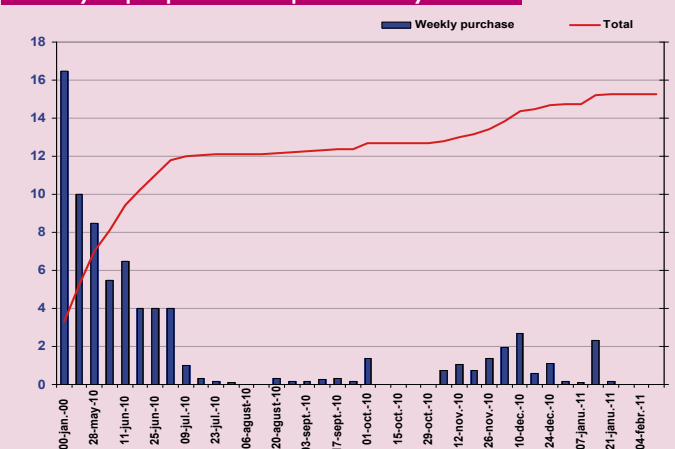
Tactically, we are maintaining a 50% fixed-rate allocation and a 50% floating rate allocation, which allows us to deal with the increasingly frequent pressures on the Eurozone interbank market. We believe that this positioning is appropriate, given current market conditions.

At the beginning of the year, several European banks returned to the short-term market for primary debt in FRNs, with maturity of one to two years.

We took advantage of them for our money market funds.

D.B

History of peripheral debt purchases by the ECB



Source: Groupama AM - Bloomberg

1- Philippe-Henri Burlisson

Core Management CIO

2- Diana Breton

Head of Money Market Management

3- Gaëlle Malléjac

Head of Fixed Income Management

4- Claire Chaves d'Oliveira

Head of Equity Management

5- Claire Bourgeois

Head of Equity & Fixed Income ALM



Summary

Fixed Income Management

LONG RATES

■ **The upward shift in rates continued at the start of the year on both sides of the Atlantic**, pulled by rising economic and inflation numbers.

What's new in 2011 is finding, in terms of debt, peripheral countries whose risk premiums have sharply deflated in favour of a changed perception in the markets regarding the sovereign debt crisis. This changed perception accentuated the rate increase in the «core» countries. Why did this change occur?

Last month, we focused on uncertainties in terms of refinancing in the Eurozone's peripheral countries. Subsequent bond issues were met with solid demand by investors and, it's true, considerable support from the ECB, which purchased securities on the secondary market.

Along with that boost, European officials increased their communication and their negotiations in support of a full range of measures seeking an overall resolution to the crisis and support for countries in difficulty (specifically, via modification of the current EFSF).

Details regarding the specifics of the measures currently under negotiation among the Eurozone countries are not yet available. However, the skies are clearing and the markets are increasingly recognising that the political will exists, thus easing the most extreme fears about the direction this crisis might take.

■ **Continued upturn in the economy over the coming months, both in the U.S. and the Eurozone**, together with rising inflation and continued improvement in market psychology in the peripheral countries argues for higher three-month rates. That's why we are revising our 10-year U.S. and French rates upward to 3.80%.

At one year, while the U.S. rate is expected to fall to 3.5% for fundamental reasons, the 10-year French rate should continue climbing to 4%, with the anticipated continuation of the transfer of the risk premium among the Eurozone countries.

CREDIT

■ **This changed perception of the sovereign debt crisis also greatly benefited private debt in the Eurozone.** They recorded a significant outperformance, with subordinated financial debt in the lead. The primary market has picked up again and the spreads have tightened, against a liquidity backdrop that, however, remains lower than normal. From a fundamental viewpoint, we remain cautious, particularly vis-à-vis regulatory uncertainties surrounding the banking sector and we remain neutral, tactically speaking.

INFLATION INDEXED

■ **Inflation-indexed bonds continue their strong progress, which began in late 2010, and have outperformed again.** Increasing in oil prices – upwards of \$100/barrel for the first time in two years – and publication of stronger-than-expected inflation figures in the Eurozone largely contributed to that performance. We still expect this trend to continue in the short term – positive for this asset class.

A WORD ABOUT THE INVESTMENT STRATEGY

■ **Our portfolios continue their slightly under-weight duration exposure**, still notably on the shortest maturities (expectation of upward revision of inflation forecasts). In the current environment, we are revising our country allocation and will reweight Spain's and Italy's share to neutral and over-weight. We remain under-weight in countries where budget ratios are not improving or that are facing solvency problems.

In terms of credit, we are staying cautious and continue to favour «core» countries' BBB-ranked corporate debt.

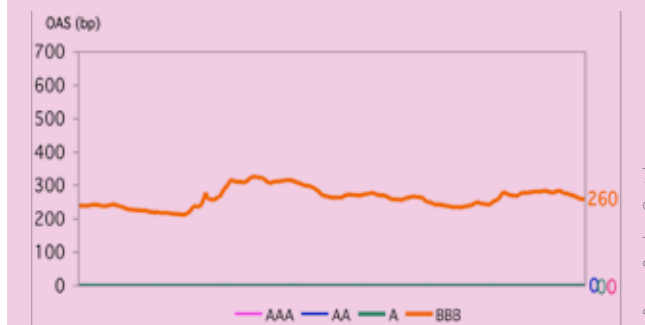
The inflation-indexed asset class should continue to benefit from a more buoyant environment in the coming weeks and so we are again increasing the indexed assets allocation in our aggregate portfolios.

G.M

Change in the short and long rates in the United States and the Eurozone



Change in risk premiums by rating



Equity Management

EARNINGS FORECASTS AND VALUATIONS

■ Trend still positive

• Having been supported by cost reductions, earnings growth is currently being fed by revived sales and boosted, for some companies, by operating leverage. However, the risk ahead is increased production costs.

■ Valuations: the stock markets, reassured, are catching up.

• In January, rising interest rates and, especially, markets drove a rebound in valuations, but they remain below the lower limit of 2003-2007 valuation levels.

OTHER FACTORS

■ Flows:

• Return of flows into equity funds, specifically from bond and monetary funds.
 • Record start of the year for M&As: The number of transactions is multiplying -- from Dupont de Nemours/Danisco to Duke Energy/Progress Energy. Coming up -- Sanofi/Genzyme and Sara Lee's future under heated debate.

■ Small Caps: painful sector rotation

• The harsh rotation at the start of the year was costly for the asset class (exposure to emerging countries and lack of bank shares)

• However, Small Caps should continue to perform well in 2011: mergers and acquisitions, strong growth.

■ Chart analysis: upward movement intensifies

Most of the indices remain in a positive trend on short-, medium- and long-term. Corrections could occur in the coming weeks but the basic trend should continue in 2011.

MARKET OUTLOOK

■ Rose-colored glasses as the year begins?

• Sector rotation, which is typical for January, proved to be extreme at the beginning of this year as a result of the combined effect of relief about the first sovereign debt refinancing in Eurozone countries (thus, the rebound in financial shares) and fears in terms of emerging countries (profit-taking on export stocks).

• Unsurprisingly, the results campaign is moving forward solidly. However, the outlook for 2011 depends on companies' ability to pass on increased costs. This is dependent on the end client (domestic or emerging, households or businesses), sector (beware of price wars) and, in particular, the leadership (or non-leadership) position.

• Capital flows confirm prior months' improvement, with investors clearly rebalancing in favour of U.S. and European equity markets. In addition, M&As are already underway, posting a record level

for a January.

• At last, encouraging news on the macroeconomic front and Europe's ability to manage the debt crisis during the first 2011 maturities lead us to revise our 12-month targets upward, with a preference for Europe, and a greater concern for emerging countries.

• However, we do not expect an increase at three months, as the markets have undoubtedly already anticipated a number of short-term positive elements.

A WORD ABOUT THE INVESTMENT STRATEGY

■ **Fears of pressure on margins in sectors unable to absorb price increases** lead us to be more watchful on consumer staples equities (food processing and food distribution). Similarly, we are taking profits on consumer durables and semiconductors. On the other hand, we are raising media, utilities and IT.

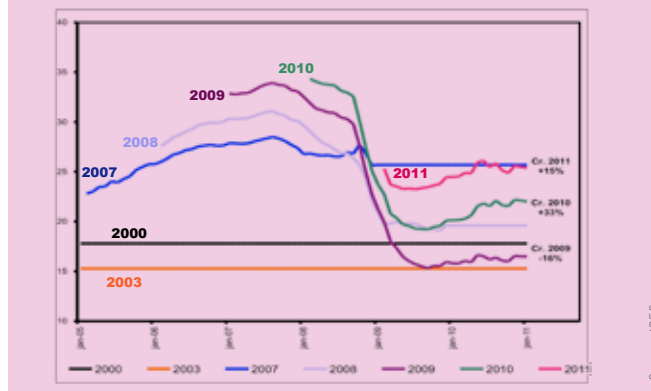
C.CO

Performance of the main indices since the start of the year

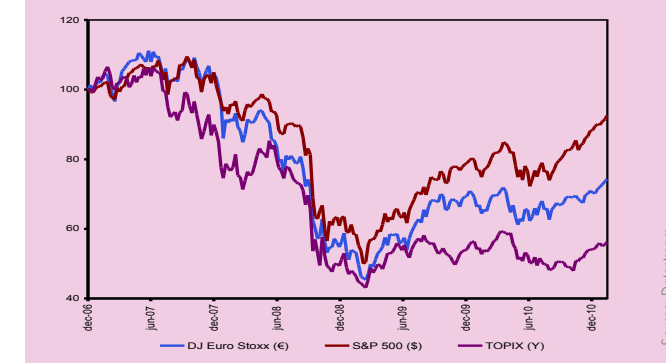
	09/02/11	Var. 2011 in euros
DJ Euro Stoxx 50	3032	8,5%
SBF 250	2993	6,9%
CAC 40	4091	7,5%
FTSE 100 (UK)	6052	3,3%
S&P 500	1321	2,8%
Nasdaq	2789	2,9%
Topix (Japon)	944	1,1%

Source: Datastream

Profits forecast by the consensus on Euro Stoxx



Performances of international stock market indices in local currency



GLOBAL BALANCED PORTFOLIO MANAGEMENT

Jean-Louis Autant,
Head of Global Balanced Management



Trend

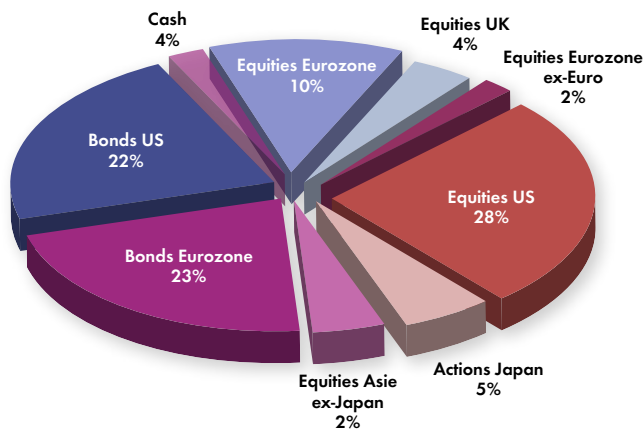
The world's leading stock markets continued their 2010 year-end launch, with some – often the most emblematic – managing to reach long-forgotten levels, as shown by the Nasdaq (highest since 2007), the DAX (the peak since 2008) and the Dow Jones, which reached its highest level in nearly 30 months.

However, the current heights, at the end of a steady climb without a regression phase, seem particularly difficult to traverse. Increasing geopolitical uncertainties (a danger that is obviously difficult to quantify) now supplement recurring fears about emerging countries – specifically, China. Incidentally, that adjective, «emerging,» seems less and less appropriate when describing an economic powerhouse that, aided by the Q4 2010 decline in Japanese GDP, claimed the envied and enviable title of the world's second-largest economic powerhouse.

What could carry the markets beyond their current resistance zone? Firstly, in terms of emerging economies and China, in particular, an easing of inflationary fears finally seems possible, especially if the rumours of change in the CPI calculation are confirmed. And secondly, on the «Old Continent,» news that Mr. Weber will not be a candidate to succeed J.C. Trichet should be welcomed positively by the participants. And lastly, on the other side of the Atlantic, the announcement of the much-awaited reform in residential housing financing clearly constitutes an initial important step toward the crucial improvement of the sector's situation.

While these developments could well play a favourable role in the medium term, for now, investors could well face a strong temptation to take fairly substantial profits.

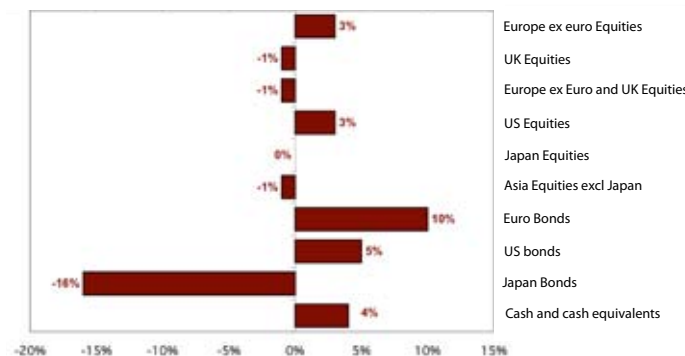
Model portfolio



Portfolio closed on 14/02/2011. Benchmark composed of 50% JPM global hedged + 50% MSCI world. Source: Groupama AM

% difference

BETWEEN BENCHMARK AND MODEL PORTFOLIO



Allocation

GLOBAL ALLOCATION

Equities 51% / Fixed Income 45% / Cash 4%: We are taking advantage of the stock markets' strong current performance worldwide to take part of our profits by reducing overexposure to equities. The assumption that a consolidation phase, expected to be fairly short, will occur is fairly likely. We will re-weight bonds at the margin (+1) at the same time.

EQUITY MARKETS (51%) -2

■ **USA (=):** US indices continue to flirt with very high levels. The earnings report period currently winding up was considered very encouraging, the fears associated with geopolitical risks – specifically, Egypt – appear to be fading. However, additional information that would contribute to surpassing the highest heights achieved recently is lacking. We're holding steady.

■ **Europe (=):** After enjoying a positive trend, the European indices are holding at levels close to solid resistance, which, here again, appear difficult to overcome. We're holding steady here, too.

■ **Asia (-2):** While we are maintaining neutral weight on Japanese equities, we are taking two points off Asia (excluding Japan). We are thus moving to underweight by taking advantage of the recent improvement in regional stock markets following positive information from China.

BOND MARKETS (45%)+1

■ **USA (=):** US bond markets are stabilising after strong recent pressure. Ben Bernanke's mention of a possible QE 3 (if necessary) may be favourable.

■ **Europe (+1):** The peripheral bond rally has ended for now, uncertainty regarding the future size of the stabilisation fund is again stressing the Eurozone's weak links and renewed ECB purchases will not compensate. We are resuming bond purchases – on the margin -- from «core» countries.

■ **Japan (=):** No interest.

MONEY MARKET +1

slight increase as a result of sales of Asian equities.

IN THE BLINK OF AN EYE

Our strategy

		Current level 08/02/11	Short-term objective	1 year objective
United States	Fed Funds	0,25	😊	😊
	10 yr T - bill	3,66	😞	😊
Eurozone	Refi rate	1,00	😊	😊
	10 yr OAT	3,62	😞	😞
Japan	BOJ rate	0,10	😊	😊
	10 yr JGB	1,31	😞	😞

Sources : Groupama AM, Bloomberg

Our model portfolio in € 08/02/11

BENCHMARK	EURO MTS GLOBAL
Sensitivity	😞
Inflation indexed allocation	😊
Curve choice	
1 - 3 yr	😞
3 - 5 yr	😞
5 - 7 yr	😊
7 - 10 yr	😊
10 - 15 yr	😞
15 yr +	😞

Sources : Groupama AM, Bloomberg

Conclusions of the equity markets committee 09/02/11

Indices	09/02/2011	Forecasts	
		Groupama Asset Management short term (< 3 months)	a 1 yr
France (CAC 40)	4 091	😊	😊
Euroland (DJ)	294	😊	😊
United-Kingdom (FTSE 100)	6 051	😊	😊
United-States (S&P 500)	1 319	😊	😊
Japan (Topix)	944	😊	😊
MSCI Asia free ex-japan	565	😊	😊

Sources : Groupama AM, Bloomberg

Sector Outlook

Energy	😊	Consumer Products - Cosmetics	😞
Basic Materials	😊	Health Care Equipment	😊
Capital Goods	😊	Pharmacy & Biotech	😞
Industrial and Commercial Services	😊	Banks	😊
Transportation	😊	Diversified Financials	😊
Automobile	😊	Insurance	😊
Consumer Durables	😊	Real Estate	😊
Hospitality & Leisure	😊	Software & Computer Services	😊
Media	😊	Technological Equipment	😊
Non-Food Retail	😊	Semiconductors	😊
Food Retail	😊	Telecoms Operators	😊
Food Processing	😊	Utilities	😊

Sources : Groupama AM

COMMERCIAL CONTACTS

😊😊 Positive 😊 Positive neutral 😐 Neutral 😞 Negative neutral 😞😞 Negative

📄 Summary

Groupama Asset Management
The Letter Funds and Strategy - N°101

8

Business Development Managing Director:
Jean-Marie Catala / 01 44 56 79 18 / jmcatala@groupama-am.fr
International Business Development Managing Director:
Arnaud Ganet / 01 44 56 56 61 / aganet@groupama-am.fr
Institutional Investor Relations:
Jacques Bontet / 01 44 56 57 76 / jbonnet@groupama-am.fr
Bruno de Solms / 01 44 56 75 43 / bdesolms@groupama-am.fr
Jérôme Guittet / 01 44 56 57 22 / jguittet@groupama-am.fr
Barbara Flogny / 01 44 56 75 62 / bflogny@groupama-am.fr

Valérie Rapoport / 01 44 56 56 45 / vrapoport@groupama-am.fr
Sandrine Louis-Sidney / 01 44 56 56 79 / slouissidney@groupama-am.fr
Gaspard Theyssset / 01 44 56 66 65 / gtheyssset@groupama-am.fr
External Distributor Relations:
Alexandre Jaeglé / 01 44 56 89 17 / ajaegle@groupama-am.fr
Anne-Laure Mugnier / 01 44 56 56 21 / almugnier@groupama-am.fr
Matthieu Painturaud / 01 44 56 77 72 / mpainturaud@groupama-am.fr
Jon Dubarbier / 01 44 56 71 45 / JDubarbier@groupama-am.com

Group Relations:
Corinne Foucoin / 01 44 56 79 07 / cfoucoin@groupama-am.fr
Eric Mathieu / 01 44 56 57 64 / emathieu@groupama-am.fr
Network Group Relations:
Luc de Corainville / 01 44 56 77 65 / ldecorainville@groupama-am.fr
Sabine Peter / 01 44 56 77 09 / speter@groupama-am.fr
Didier Oms / 01 44 46 66 74 / doms@groupama-am.fr
Jérôme Larsonneur / 01 44 56 56 20 / jlarsonneur@groupama-am.fr
SRI development:
Michel Lemonnier / 01 44 56 66 36 / mlemonnier@groupama-am.fr