



In a rising rate environment, where is the sweet spot in fixed income?

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Strong Economic Recovery Scenario

Economic growth is intensifying as the roll-out of the COVID-19 vaccination program progresses and economies reopen. Global growth is expected to reach +5.9% in 2021 according to the latest IMF projections. The outlook on defaults on High Yield (HY) debt remains very favorable, particularly in Europe and the United States, thanks to the economic recovery following the health crisis and the support of central banks (FED, ECB, BOE, etc.). The financial situation of companies has clearly improved with leverage ratios (net leverage, interest coverage ratio etc.) that have returned to the pre-Covid level. Finally, corporate liquidity has never been so strong in the face of very limited bond maturities: in Europe approx. 13% of the stock of HY debt is due in 2022 and 2023 versus a cash position of 30% of gross debt; in the US less than 8% of the stock of HY debt is due in 2022 and 2023 versus a cash position of 16% of gross debt. However, the situation is somewhat different and less favorable in emerging markets.

Though the FED and ECB have been cautious, considering inflationary pressures as “transitory”, they are nevertheless preparing markets for a decrease in asset purchases (i.e., tapering). We believe tapering could create more volatility in the markets. However, in our opinion, it does not constitute a disruptive element that could cause a significant widening of credit spreads and a sudden increase in defaults. Moreover, any curve steepening should benefit the banking sector.

La Francaise AM believes in a strong economic recovery scenario, judging by the positive trends in corporate fundamentals and contained default rates. In our view, the greatly feared consequences of the end of state aid in Europe and the US on the solvency of companies will be limited.

A flexible asset allocation

In today's environment with upward inflationary pressures and the prospect of future interest rate hikes by central banks, **La Francaise AM offers a pure credit strategy with limited exposure to interest rate sensitivity, La Francaise Carbon Impact Floating Rates.** As its name implies, the fund invests in Floating Rate Notes (FRN).

FRN are bonds issued by corporate issuers and banks. They exhibit very limited interest rate sensitivity as the coupon is based on a margin over a benchmark rate (i.e., Euribor 3M, SOFR...).

Furthermore, the volatility of FRNs is more limited than fixed rate bonds: the volatility of the Euro Investment Grade FRN index is close to 80% lower than the Euro Investment Grade Fixed index, which is a clear benefit to a diversified asset allocation in the fixed income universe. La Francaise Carbon Impact Floating Rates is primarily invested in FRN (approx. 74% of assets as at end of September 2021) and thanks to the attractive features of FRNs is able to generate a limited modified duration of 0.31 and a 1-year weekly volatility of 0.77%.

The fund allows for a flexible and global asset allocation (Investment Grade and High Yield, geographic and sectoral positioning) and given the current exposure of the fund to the financial sector (approx. 60%), should benefit from curve steepening movements as bank fundamentals should improve. The fund's exposure (minimum 50% of IG and maximum 50% of HY) seeks to capitalize on La Francaise AM's credit expertise and strongest credit convictions through investments in Floating Rates Notes, the systematic hedging of foreign exchange risks and a long-term diversification objective of approximately 130 issuers.

Bond selection is subject to a variety of financial and extra financial filters. First, La Française AM's exclusion policy, which covers controversial weapons, companies from blacklisted countries etc., and ESG filters are applied to the initial investment universe of over 4 500 companies. Approximately 2 000 companies remain and are thereafter subject to a four-step credit analysis:

- fundamental approach,
- solvency and liquidity analysis,
- profitability analysis,
- country approach: influence of macro data on the issuer and its sector)

and to "ESG" and "Carbon Transition" analyses. Only then, does the fund management team proceed with portfolio construction, selecting from what is now an investable universe of only 600 companies, while keeping sight of the overall **investment objective of achieving a carbon footprint at least 50% lower than the composite benchmark (50% Bloomberg Barclays Global Aggregate Corporate Index + 50% ICE BofAML BB-B Global High Yield Index).**

La Francaise AM believes that the inclusion of ESG and Carbon criteria in the fund's investment strategy can only have a positive impact on its credit profile due to an even more stringent selection process. Companies that embark on the transition have demonstrated their ability to adapt to their environment. They are generally more agile and less sensitive to climate risks. Likewise, if the impact is positive on the quality of the fund's issuers, it could also have a positive impact on the fund's volatility. Within the Bloomberg Euro Floating Rate Notes index (LEF1TREU), the volatility of the 25% of issuers with the best ESG ratings have a one-year volatility (as at end of Sept. 2021) of 0.2% compared to 0.3% for 25% with the worst ratings.

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Associated risks: risk of capital loss, interest rate risk, default risk relating to issuers of debt securities, risk associated with investments in "speculative securities" counterparty risk, liquidity risk, risk relating to subordinated debt securities, risk related to contingent convertibles, risk associated with holding convertibles bonds, risk arising from techniques such as derivatives, liquidity risk related to performance swaps (TRS), exchange risk, discretionary risk, potential risk of conflict of interest, ESG investment risk, sustainability risk. Please refer to the Prospectus for full details of the risks.

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La Française Carbon Impact Floating Rates is a compartment of the SICAV La Française (SICAV de droit français). The Autorité des Marchés Financiers approved the compartment La Française Global Floating Rates (renamed La Française Carbon Impact Floating Rates) on 13/08/2019. The integration of ESG criteria into the investment strategy was not subject to AMF approval. Investors were informed of said modifications by means of a letter to investors. The changes took effect as of 06/10/2021.

In relation to the investment strategy mentioned in this document, the latest prospectus, the KIID and the annual and semi-annual reports (whose latest versions are available free of charge on www.la-francaise.com or from your local paying agent) have been published containing all the necessary information about the product, the costs and the risks which may occur.

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