



CARNEGIE ASSET MANAGEMENT
FONDSMÆGLERSELSKAB A/S



Investment report
Fourth quarter 2009

A return to normality in 2010?

“Abnormal is so common, it is practically normal.”

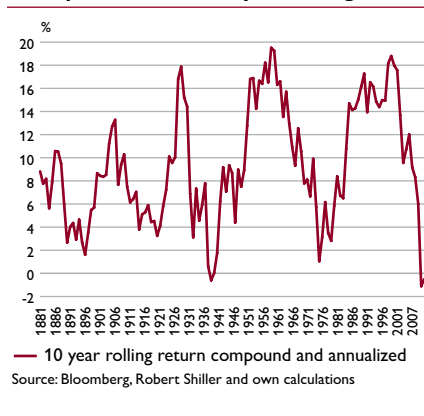
Nevertheless, it would be fair to ask whether 2010 will be a more stable year than 2009, which beat the breath out of most equity market participants. 2010 may very well turn out to be an equity year, in which returns will be close to normal levels of 5-8% in nominal terms. However, 2010 cannot be a normal year for the sole reason that we will see unexpected repercussions following the most extensive global monetary stimuli in world history.

The extraordinary conditions prevailing during the past couple of years have created a strong investment case for investors with a long-term horizon for equity investments. We will unveil this investment case in this quarterly report. Carnegie WorldWide/Global Equities is strongly exposed to this investment case, which we expect will provide us with a good start to the new decade.

2010 – on a razor’s edge

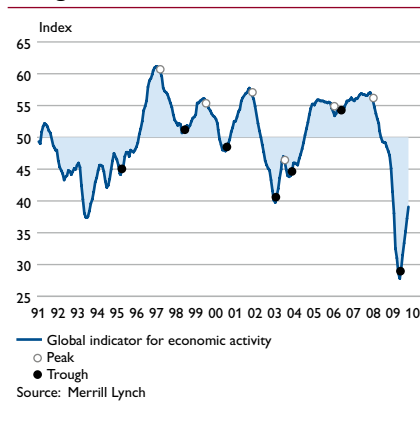
2010 will be an unusual year for the sole reason that the events of the upcoming year will be inextricably linked with the developments of the financial crisis of the past couple of years. 2010 will be a balancing act in which politicians and central banks will once again play leading roles the way they have for the past couple of years. Having hit an all-time low in March 2009 measured by ten-year returns on US equities, as shown in figure 1 below, the market rallied for the remainder of 2009.

Figure 1: US Equities return - 10 year rolling



The US federal reserve lowered short-term interest rates to close to 0%. Politicians took heed of the lessons learned from the 1930s in the USA, and short-term interest rates fell to all-time lows in most regions around the world. China aggressively stimulated the economy, and the country has such strong underlying dynamics that it, and not the USA, became the first country to emerge from the crisis. In other words, we have witnessed an unusual rescue action for the global economy. As shown in figure 2 below, which describes the health condition of the global economy in a

Figure 2: The global wave



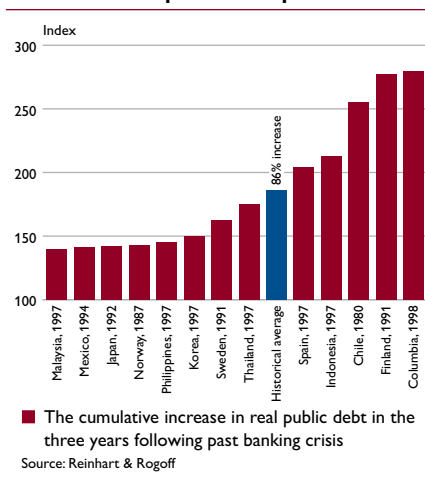
chart, the operation was successful. The patient is out of the emergency room but still needs very expensive and risky medicine – described by some sceptics as heroin. The medicine is slowly being withdrawn, and the first phase in which central banks reduce access to loans to the squeezed and vital banking sector has been initiated. However the nationalisation of the credit granting process is still in progress in the USA. In an announcement released on the day before Christmas, it was announced that the two major players in the US home financing market, Fannie Mae and Freddie Mac, which buy US home loans, will have unlimited access to federal aid for the next three years, whereas a cap previously applied to such funding. The next and difficult withdrawal phase involves hiking short-term interest rates. Individual countries such as Australia and Norway have already begun. There are some countries which already at the present stage need to tighten their fiscal reins quite dramatically, including Greece and Ireland. The rest of the western world, in particular, will follow suit with tighter public budget management when the local and global economies

are considered more stable. However, this is where the major challenges lie. How does one combine tighter public budget management with a world in which governments play an increasingly important role?

Governments as growth drivers

After the last couple of years, in which the otherwise well-tested model built on free markets malfunctioned, governments moved in to act as the saviour at the time of crisis. The predictable and typical outcome is that the global public systems dramatically push up debts. This is one of the themes of the recommendable book by Rogoff and Carmen “This Time is Different”. Figure 3 below shows that public debt after a financial crisis increases by 86% over a subsequent three-year period.

Figure 3: Increase in real public debt past crisis



As governments do not have any funds of their own, they need to borrow from today’s and tomorrow’s tax payers and savers to finance today’s public consumption. The government cannot and will not withdraw quickly as growth driver as described in previous quarterly reports. That by itself does not necessarily herald disaster for global growth. There are examples of how governments can sensibly allocate capital. China is a successful centralised example, while the Nordic countries have also performed well, in spite of heavy government involvement. However, a big state which also needs to act as a growth locomotive is expected to lead to weaker global growth trends for the next three to five

years, and greater fluctuations. In particular, growth will be weaker in countries that were financially weak before the crisis. Most of the industrialised world belongs in this category, whereas China and other selected countries are at a different point in their structural economic cycle and still have a strong platform for growth.

The risk arises only if the government finds difficulty in sourcing funds from savers and tax payers. As a result of the huge government deficits especially in the USA, both Japan, China and businesses, private individuals and banks will have to buy large quantities of government bonds to secure continued funding. So far, this appears to be sustainable, and especially the banking system held a relatively low proportion of government bonds in a historical perspective. We would refrain from buying a 10-year government bond at the current yield levels and keep it for ten years. However, most government bond buyers do not hold the bonds until maturity. They buy bonds for lack of a better alternative in a world in which cash carries close to 0% interest. Governments can only obtain funding at 2-4% as long as short-term rates remain much lower. That leads us to the all-important risk factor for 2010 and 2011; what will happen when short-term rates are hiked – how will it impact the global equity, bond and property markets?

The simple solution would be to merely continue keeping interest rates at the present, extremely low levels. However, we cannot continue to have short-term rates of close to 0% due to the high risk of new bubbles. If the cost of capital is too low, it may lead to sub-optimal investment behaviour. Too much cheap money in circulation increases the risk of inflation getting out of hand. So central banks need to tighten monetary policy and hike interest rates again at the right time. We expect that this could happen once the banking system has recovered and been appropriately recapitalised. We’re not quite there yet, but given the stabilisation of the property market and improvements in the more risky parts of the credit market, there is a strong probability that central banks will hike rates in 2010. The market should be able to cope with gradual rate hikes, but there is a high risk of instability.

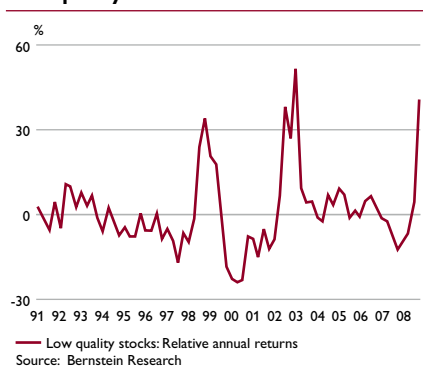
The global forex markets are experiencing an imbalance which is important to address politically as well financially. China still has a sky-high surplus on its trade balance and

current account, whereas the Anglo-Saxon economies, with the USA at the helm, have major deficits. Part of the solution to this imbalance is for China to start revaluing the Renminbi again. There are sound practical, political and market-psychology reasons for doing so. We would guess that the Chinese will re-launch the revaluation process initiated in the summer of 2005, with a monthly and gradual revaluation relative to the US dollar of 4-8% per annum. Failure by the Chinese to do this may create a basis for an escalating trade conflict and protectionism in an atmosphere marked by continuing high unemployment, especially in the USA. This would have a negative effect on global equity markets.

Quality on sale

High quality US companies had an unusually difficult period in the 2nd and 3rd quarters of 2009. According to US finance house Bernstein, these companies underperformed the market by as much as 23%, whilst companies with a lower credit rating outperformed the market by 56%. Over a longer period of time, figure 4 shows that low quality

Figure 4: Low quality stocks



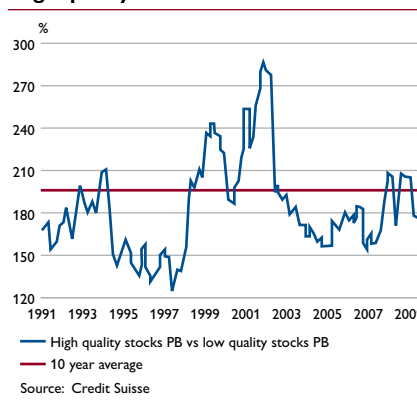
companies typically perform well during relatively short periods. The figure also shows that the strong additional returns of the past year match earlier periods during the late 1990s and 2002-2003. The reason is that investors with high risk profiles and short investment horizons have had access to extremely cheap funding. These investors play a very important role in an environment with easy access to cheap funding. They drive price developments in these more risky companies, causing lower quality companies to outperform.

2010 will most likely be the year in which we see some degree of normalisation of the very lenient monetary conditions. The consequence may well be that more fundamental and long-term investors will gradually take over price developments in the equity market.

It is important to note three factors in this respect:

- 1) The historical pattern is clear. After a year such as 2009 in which low quality strongly outperformed high quality, the pattern is the very opposite in the following year. Quality stocks thus perform 9% better on average in the following year.
- 2) Quality stocks can outperform the market even in strong market rallies. That has happened on a number of occasions.
- 3) Quality stocks are inexpensive. As shown in figure 5 below, these types of companies trade at attractive levels relative to history and relative to the category of lower quality.

Figure 5: High quality stocks Price/Book



In many ways, it feels like a sale in a furniture store that only sells designer furniture. High quality brands are on sale, and the sale may last for quite some time. As long as money comes cheap and is easily accessible, speculation will abound. People are queuing at the casino table, tempted by juicy investment categories with high returns, at high risk. If interest rates on government and credit bonds continue to fall, investors will continue to make bets.

Overall, we believe that long-term investors will make the most money. Now is a good time to buy quality stocks at

attractive prices. Therefore, we retain a strong overweight of these companies.

Quality pays in the long run

At Carnegie WorldWide, we focus on buying stocks and keeping them for many years. In our experience, this provides the best long-term return net of all costs. Consequently, we focus on the characteristics of a company that may generate a high long-term return. One such characteristic is quality. One of our long-standing customers once said, with a twinkle in his eye, that a quality stock to him was a stock that went up! The question remains for how long the price of the stock will rise and how big an overall return the company will yield.

Dividends are an important, but neglected, part of the return on stocks over longer periods. This is one of the arguments of Dimson, Marsh and Staunton's book "Triumph of the Optimists", in which the re-investment of dividends doubles the annual return on stocks. Some companies, however, are in a better position to pay dividend than others. These companies generate a high and stable return on their share capital, have low debt and a low investment level to maintain production of the goods and services they sell.

Over long periods of time, these companies on average outperform the market and at lower risk. For example, Bernstein found that the annual average additional return on US quality stocks from 1982 to 2009 was 1.6% per annum, whilst low-quality companies fluctuated far more and on average they underperformed by 1.6% per annum.

This simple historical fact based on common sense plays a pivotal role for the way in which Carnegie WorldWide builds its portfolios. We seek to optimise our portfolio over longer periods of time, and even though we could potentially profit from shifting from high to low quality in the short term, this could result in an unproductive and expensive discipline. We will continue to invest in companies that we believe offer long-term value.

Conclusion

We began this article by emphasising that the turbulence in the equity markets has opened up for sound investment



opportunities. Buying quality stocks and maintaining a long term investment horizon. In other words, invest instead of speculate. These are the values we emphasise and which have created strong results for our investors during the past 20 years.

2010 cannot be a normal year and should not be seen in isolation due to the extreme conditions in the fixed income markets and the recent financial crisis. Today, speculating is more the norm than investing. Investing with a short time horizon has become the normal thing to do rather than making long-term investments. In such a world, one should consider taking the advice of the successful US actress Jodie Foster: Normal is not something to aspire to, it is something to get away from!

Be abnormal, but stay logical and rational in your decision making. Buy quality. That is the opportunity available in the equity markets right now.



Carnegie Worldwide

Summary

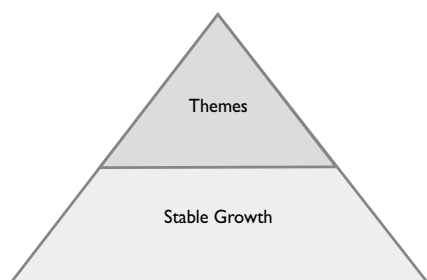
Global equities endured the most turbulent year in recent memory but ended on a positive note. Global Equities rose 5.7% (USD) during the quarter, while the market in general climbed 4.1% (USD). The year ended with an increase of 24.6% (USD), against a 30.0% (USD) increase in the global market. High-quality companies experienced a rough ride in 2009. The more financially sensitive equities proved to be the best performers, and especially March and August were characterised by a rally in higher-risk equities. The Carnegie Global Equities strategy only has exposure to these equities, as the portfolio is focused on more stable growth sectors. We believe that quality stocks are attractively priced and consequently have a diversified portfolio of companies with a high return on equity and low debt. Throughout the year, we increased our exposure to technology stocks, and we expect to see particularly strong growth in the use of mobile Internet services.

Strong finish to a turbulent year

The overall Q4 performance was an increase of 5.7% (USD). By comparison, the Morgan Stanley World Index gained 4.1% (USD). The quarter concluded a year of rising equity prices in the wake of successful political intervention, particularly in the financial sector. Peabody Energy was the year's best investment, gaining more than 100%. Peabody Energy was also the best Q4 performer. Google and Apple also contributed positively in Q4. As a new and hopefully lasting trend in the fourth quarter, the more stable companies finally made a positive contribution. For example, both Nestlé and Diageo were key contributors. No companies stood out negatively to any noteworthy extent. However, Bank of America experienced some difficulties and was a negative contributor in Q4 together with HDFC and Praxair without reporting any particularly negative corporate news. We added Bank of America during the year, whereas HDFC and Praxair were components of our portfolio all year, making a positive contribution to our full-year performance.

The fund's current investment strategy

Our investment strategy remains unchanged based on expectations of weak global economic growth with emerging markets offering the best growth prospects. It is still imperative that the debts of western economies are reduced from the current high levels, regardless of the dramatic initiatives by politicians to restore growth. Political initiatives increase the risk of inflation longer term. The enormous stimulus project for the global economy must be scaled down in 2010. This will stir uncertainty in the form of reduced access to cheap funding. We expect longer-horizon investors with a more fundamental stock-picking approach to drive the price of fundamentally strong companies. The fund has a high proportion of companies with substantial sales to emerging markets where the underly-



ing growth conditions continue to be the strongest. We foresee sustained strong growth in the virtual world which we access via our computer screens and the Internet. Particularly access to the parallel universe through so-called smartphones, such as Apple's iPhone, is expected to surge in the years ahead.

Change of benchmark

The benchmark for the Carnegie Worldwide Fund will change from the MSCI World Index to the AC World Index with effect from 1 January 2010. The AC World Index provides a broader and better picture of developments in the global equity markets. The MSCI World Index only to a very limited extent includes emerging markets, whereas the broader AC World Index has a higher weighting in these markets. Accordingly, the weighting of emerging markets is 13% (at 31 December 2009) in the AC World Index, as compared with 0% in the MSCI World Index. Conversely, the MSCI World Index has a higher weighting in the USA and Europe.

As the role of emerging markets in the global economy increases, more investors are expected to change their benchmark from MSCI World to AC World. As many investors are guided by the benchmark, we expect this change to have the effect of directing cash flows towards emerging markets.

However, the change of benchmark for the fund will have no impact on our portfolio. We will buy the maximum of 30 stocks we prefer, irrespective of the benchmark. We believe that this is the best way to achieve a long-term attractive return.

Portfolio changes

Funded by three smaller positions in **Nintendo**, **First Solar** and **Gazprom**, the purchase of **Apple** was the only major change during the quarter. Apple develops world-class products that are easy to use. In many ways, Apple is realising the dream from the turn of the millennium of easy access to the Internet via mobile phones. The great penetration value of iPod and iPhone has truly consolidated Apple's brand on a global scale. We expect a steady flow of new and exciting products from Apple, which will increase the company's still relatively limited market share, particularly within mobile telephony and PCs. The stock is reasonable priced relative to the strong growth rates, and we still expect positive surprises that may further drive up the stock.

Expectations for Carnegie Worldwide

Our expectations for 2010 are moderate.

We need to undergo a certain normalisation of the money market over the next couple of years. Otherwise, the risk of imbalances and new bubbles in the equity and bond markets will be too great. The return for the year depends on how this process is handled. We expect to generate a moderate return in the equity market, which, however, will be fully compatible with the return obtainable in the bond market. We expect Global Equities to slightly outperform the general trend in the global equity markets.

We expect major, stable quality stocks, which are currently attractively valued as compared with the rest of the market, to outperform in 2010, and we therefore maintain a high proportion of these stocks.

Investment philosophy

Carnegie WorldWide is a Sub-Fund of CARNEGIE FUND, an unincorporated open-ended collective investment fund registered in Luxembourg under Part 1 of the Law of December 20, 2002.

The investment objective of the fund is to achieve long-term capital growth exceeding the return of the market with a moderate risk profile as measured by standard deviation. The aim is to have a portfolio's standard deviation level at or below that of the market.

Our experience in managing focused portfolios has taught us that a concentrated portfolio of 25 to 30 high conviction stock picks ensures a sufficiently high risk diversification. The fund endeavours to understand and capitalize on the trends of the future. Most importantly though is to be optimally prepared for the future with a sturdy portfolio of unique stock picks.

The fund invests in equities listed on global stock exchanges and has no geographical or sectorial restrictions.

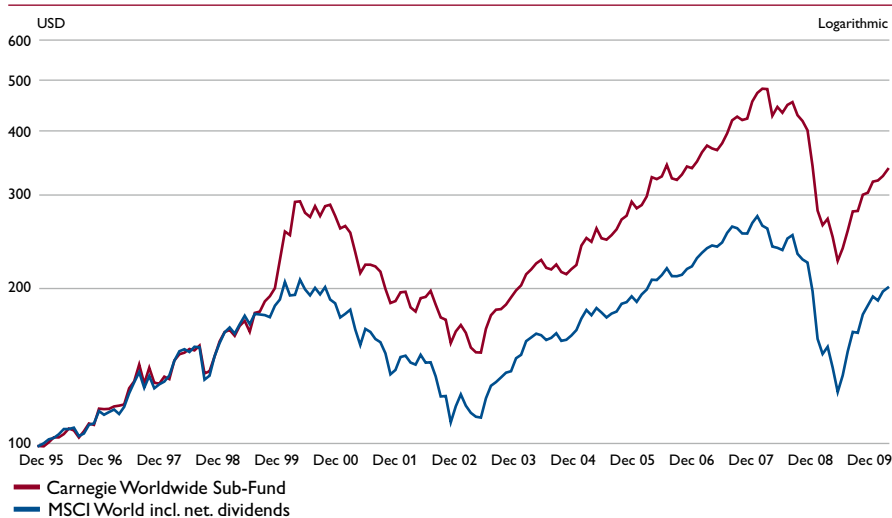
Key figures	31-Dec-09	30-Sep-09
NAV (1,000 USD)	2,759,408	2,507,582
NAV per share (USD)	68.00	64.35

ISIN	LU0086737722
Launch date:	15-Dec-95
Read more:	www.carnegieam.com/cw

Return/Excess return in %	1 year	3 years	5 years	10 years	Since launch
Return on Portfolio	24.6	-9.9	35.6	31.7	240.0
Return on Benchmark*	30.0	-16.0	10.5	-2.4	101.5
Active return (arithmetic)	-5.4	6.0	25.1	34.1	138.5

Risk	3 years	5 years	10 years	Since launch
SD Portfolio (%)	22.2	19.0	17.9	17.5
SD Benchmark (%)	22.1	18.0	16.9	16.2

Investment Performance Graph (Indexed)



Carnegie WorldWide as of 31 December 2009

	USA & Canada	UK & Ireland	Continental Europe	Japan	Pacific ex. Japan	Emerging Markets	Total	Benchmark*
Energy	Transocean 2.4 Peabody 3.2				Sinopec 2.6		8.2	10.9
Materials	Monsanto 2.9		Holcim 5.0				7.9	7.5
Industrials	Praxair 4.0		ABB 2.8				6.8	10.4
Consumer Discretionary							0.0	9.3
Consumer Staples	Lorillard 3.1	BAT 7.5 Diageo 2.5	Nestlé 7.5	Japan Tobacco 4.4			25.0	10.2
Health Care			Novartis 4.0 Roche 4.7				8.7	10.1
Financials	Bank of America 2.5	Standard Chartered 2.1	Allianz 4.6		HDFC 6.1 ICBC 3.4		18.7	20.6
Information Technology	Apple 2.5 Cisco Systems 3.6 Google 4.6			Canon 3.0			13.7	12.0
Telecommunication		Vodafone 2.6					2.6	4.4
Utilities	Exelon 2.5		E.ON 2.5				5.0	4.6
Others					Carnegie Asia 2.0	Carnegie East European 1.4	3.4	0.0
Total	31.3	14.7	31.1	7.4	14.1	1.4	100.0	-
Benchmark*	53.0	10.2	21.3	9.7	5.8	0.0	-	100.0

* The benchmark is MSCI World incl. net. dividends.
The number behind the name of the share states the percentage of the fund's holdings.



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