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Management Report
4th Quarter 2008

Trend on the financial markets in the 4th quarter of 2008

In the 4th quarter equities posted dramatic price losses all over the world. They were preceded by trends that escalated in September 2008 when no end was in sight to the marked price decreases on the US real-estate market. The two leading semi-government-owned US mortgage banks Fannie Mae and Freddie Mac had to be completely nationalized, the investment bank Lehman Brothers filed for bankruptcy and the investment bank Merrill Lynch was taken over by Bank of America. In addition, the US central bank had to save the insurance group AIG from bankruptcy by extending a number of loans. Above all, the bankruptcy of the investment bank Lehman Brothers had an extremely dramatic impact on the international securities markets as the bank was not saved by the US Ministry of Finance – unlike other banks – yet was important as a counterparty.

The government rescue packages were then feverishly put together for the financial industry all over the world; the central banks, for their part, made available enormous sums in loans and reduced their interest rates aggressively in some cases. Furthermore the central banks began to directly buy up toxic securities. Although the government rescue packages made it look as though the fundamental problems relating to the stability of the banking system had been defused, the stock markets expected a sharp recession as a consequence of the disruption to lending. This was all the more true in that the rescue packages had first to be implemented. The defensively oriented Swiss market suffered least of all, followed by the US market.

The price losses concerned all sectors, but to varying extents. The defensive sectors of non-cyclical consumer goods and health performed best. The commodities and finance sectors ranked at the bottom of the list.

The performance of the most important government bonds in local currency terms benefited from the global financial crisis because government bonds offer a high level of issuer security. Bond prices rose and interest rates fell accordingly. Currency risk played a great role in the case of investments in foreign government bonds, however. Thus foreign bonds were only profitable for a Swiss-franc investor in individual cases. US dollar and yen bonds generated clearly positive yields in Swiss francs. On the other hand, the very sharp correction of the British pound led to severe losses in sterling bonds. The clear-cut gains on government bonds in euros were almost completely eaten up for a Swiss franc-based investor by the negative trend in the exchange rate of the euro.

The trend in corporate bonds was completely different. The escalating financial crisis massively increased investors' risk aversion so that corporate bond prices fell on a broad front, and interest rates rose. The interest-rate differential between US corporate and government bonds, which serves as a risk indicator, widened to an above-average extent.

Hedge funds also suffered once again significantly in the fourth quarter and sustained a further double-digit percentage loss on average.

The commodity markets posted very severe losses owing to the abruptness and extreme severity of the incipient global downturn in the economy. The crude oil price suffered nothing less than a collapse, plummeting by 63% in Swiss francs in the fourth quarter alone. In this very unfavourable environment gold was able to prove itself as a safe haven and maintained its price level.

In the 4th quarter 2008, the value of the A-share decreased by 11.42%, from CHF 227.51 to CHF 201.52, and in the same period the B-share decreased by 2.07%, from CHF 210.62 to CHF 206.26. For the whole year 2008, the A-share has decreased by 19.79% and the B-share by 3.12%.

This report was prepared by René Exenberger, Vontobel Asset Management, Zurich

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