



Dear Reader,
 dear Investor,

Within the last couple of weeks global financial markets were dominated by chaos and fear and almost daily we were getting more and more bad news. Therefore we decided to postpone to send out our newsletter until we see some sort of market resilience. We feel that we are experiencing a normalization of global financial markets but expect volatility to stay relatively high for quite some time.

When I started my career as an asset manager in 1987, I was only in the job for 3 months before the 1987 stock market crash took place. This experience made a lasting impression on me and knowing how quickly markets can fall, helped shape my vision of a globally diversified investment strategy, which would include various asset classes that have some offsetting risk characteristics. In my view the current crisis has been the most serious one since the stock market crash in 1929 and certainly of much more concern than the crash of 1987 and other crisis such as the LTCM collapse.

The finance sector is clearly the most important industry and its key role for a proper functioning economy is obvious. The ongoing deleveraging process marks a turning point in the history of ever increasing debt burden of private households and businesses. Especially financial companies have been able to grow profits very strongly because of the increasing amount of leverage and risk that they took on. Also, most of the banks were not able to manage their risks. This fact, combined with a lack of regulation, helped building this house of cards. The bailout package that has been put together will help to ease the pain, at least in the short-term. Longer-term we need to see some real changes and clearer regulation of financial companies, therefore addressing the problems created by an ever increasing appetite for credit, leverage and profit maximization. I am worried, that the longer-term impact of the current crisis results in overregulation of finance companies, therefore creating another problem. I am a strong believer in free markets but realize the need for proper regulation, especially among sectors that have a critical role for the whole economy. Clearly, financial companies are the most important in this regard, banks need to provide the overall economy with liquidity and credit, which are critical for solid economic growth of every country. The problem with the current crisis is that it hits exactly this part of the market, sending shock waves to others markets and industries. This has far reaching consequences, not only for banks and insurance companies, but also for almost every business around and it will also have a severe impact on consumption. Consumers have been hit hard by falling housing prices and a rapid increase in commodity prices. Now they are also going to face the consequences of the 700 billion rescue package. This is a heavy burden on tax-payers and hard to take, both financially and psychologically. Consumers now face a situation where the ability and willingness to consume is very low. Realizing that household consumption is the most important contributor to GDP growth, makes it hard to believe that we will see any positive development soon.

The far reaching implications of the current crisis can be felt globally, but most severely in the U.S. Over-simplified, one could say that the value of the U.S. Dollar could be seen as the share price of the U.S., we find it hard to believe that we are going to see any significant advances considering the current situation. Actually, it is quite the opposite, we believe that all the factors have fallen into place which point to a prolonged period of structural U.S. Dollar weakness. This outlook makes it more important than ever to hedge the U.S. Dollar exposure and to diversify assets globally. The latest recovery of the U.S. Dollar was caused by the unwinding of existing investment positions and a lot of money went back into the U.S. Dollar. This development has come to an end and we expect the market to focus on fundamentals again and these things look bad for the U.S.

Furthermore, gold has not been a safe haven during this crisis with prices falling quite substantially. We continue to be optimistic for the longer-term outlook for gold. In our view the recent price weakness was caused by a huge liquidation of commodity investments. It seems that a lot of big players in the market were offloading these exposures to create liquidity. We see this as an attractive entry point as the speculative component of the price has been removed. We expect once the global economy recovers a few quarters from now, there will be significant upward pressure on prices, which will lead to higher inflation. This outcome would be very positive for gold in our opinion.

We expect that stocks will stay relatively weak and continue to trade in a volatile manner. The current recovery from very oversold levels is therefore just a sign that things are going back to normal. However, we see only very limited potential in the next 12 months for the broad market but believe there will be significant return spreads among the various sectors. We have been heavily underweighting financial stocks since spring 2007 and are not yet planning to increase our exposure. We like industries and companies that are able to generate real organic earnings growth, benefit from longer-term structural changes and the value drivers created thereof.

There is no question, the current market level is challenging but we also realize that there are a lot of bargains right now. Therefore, we are making use of these opportunities and try to purchase the most promising long-term investments.

Daniel Zurbrügg, Managing Partner

The US Treasury's sweeping plan to stabilize the financial system and dramatic efforts by the Fed to support money markets promise to reduce the downside risks to the economy and will likely have significant implications for investors, financial institutions and monetary policy. Of course there is no guarantee that it will work. After a long political debate, the plan finally passed the Senate and the House of Representatives. The plan must be quickly enacted, and authorities must use their new powers aggressively to underpin markets and restore confidence. Moreover, it will not quickly reverse the global economic slowdown that is now underway. The plan, if well executed, should be positive for risky assets by reducing risk premiums, creating balance sheet capacity for lenders, alleviate the credit crunch, narrow credit spreads and promote expectations of lower risks and an eventual rebound in earnings.

Legislation gave the Treasury an initial USD 250bn to buy distressed assets, but we think the plan does not do enough to solve the real problem, namely the prevention of destruction of bank capital and the resulting reduction in lending and economic activity. We think a direct injection of capital into the banking system would have a substantial impact for a fraction of the overall cost.

We are not convinced that the longer term bear market has ended yet, particularly given the risks remaining in relation to the financial system and the growth outlook. Once risk premiums normalize, the market should refocus on earnings. As the latter has declined, we have been looking for a washout in sentiment accompanied by high volume selling in order to get a confirmation that equity markets have bottomed. This was evidenced three weeks ago by a couple of signs as e.g. a spike in the VIX volatility index, significant widening in credit spreads, a collapse in Treasury Yields, a collapse in emerging market and commodity-related equities and high volume broad based selling. The S&P 500 is now down 35% from its 4Q07 high, with selling pressures broadening and stretching well beyond the Financials. Eight of the ten S&P 500 sectors have crossed into bear market territory during the sell-down - only Consumer Staples and Healthcare are down less than 20% from their peak. We remain concerned that the earnings downgrade cycle is far from complete. Credit market weakness will continue to weigh on the financial sector and hamper the speed at which asset deleveraging and balance sheet repair can take place. Additionally, the lending standards will remain tight and this will be negative for business and consumer spending going forward. By traditional measures, e.g. the forward P/E ratios, the European markets don't appear cheap, despite the hefty correction.

Within the last two weeks the stock markets reached such an oversold level, measured by almost every valuation and fear indicator metric, that it was quite obvious the market was overdue for a major bounce. This actually happened last week with the main indices gaining over 10%. We believe, despite harsh economic indicators - especially in the US, that the worst selloffs are over. A good sign therefore is that bad economic news are being countered by buying orders. Other signs are a decreasing VIX, an easing of the LIBOR market and of the government CDS. Additionally, the technical momentum indicators are in oversold territory, but have found their way upwards. Going forward there will still be plenty of setbacks, but we recommend investors to add some positions of very good companies at these attractive levels.

Notwithstanding the euro-zone's unexpectedly strong start to the year, there are clear signs that the economy is slowing. GDP growth will slow from 2.6% last year to zero, or even a contraction this year, with the divergence between different countries set to widen further. For the US economy we fear a relapse towards the end of the year as the fiscal boost begins to fade and further signs of the financial crisis will appear. The economic imbalances in the UK are at least as severe as those in the US. The longer inflation worries prevent the Bank of England from cutting rates, the deeper and longer the slowdown will be. The latest surveys evidence that GDP growth has come to a halt and that a recession is looming. China's economy has continued to perform well despite a large fall in the contribution from net trade and a (food-led) surge in headline inflation. Nonetheless, we believe that the growth rates will decrease there as well. We believe central banks will continue to lower their interest rates in order to respond to further slowing activity.

Market update

PRICES AS PER NOVEMBER 4TH 2008

Global Equity Indices	Last Close	YTD %
Swiss Market Index	6277.4	-26.01
Swiss Performance Index	5156.9	-25.54
Eurostoxx 50	2715.1	-38.29
German DAX Index	5214.1	-35.37
FTSE 100	4553.0	-29.49
CAC40 Paris	3606.6	-35.76
Standard & Poors 500	1005.8	-31.51
Dow Jones Industrials	9625.3	-27.44
Nasdaq 100	1780.1	-32.88
Nikkei	9521.2	-37.80
Topix	966.9	-34.48
Hang Seng	14840.2	-46.64
All Ordinaries	4336.6	-31.60

Government Bond Yields 10Y	Last Close	YTD %
USA	3.8	-6.29
EUROPE	3.8	-11.73
U.K.	4.5	-0.84
SWITZERLAND	2.9	-5.74
JAPAN	0.8	-2.57

Libor 3 Months	Last Close	YTD %
USA	2.51	-46.70
EUROPE	4.66	-0.45
U.K.	5.68	-5.23
SWITZERLAND	2.60	-5.62
JAPAN	0.80	-7.27

Exchange Rates	Last Price	YTD %
US Dollar / Swiss Franc	1.1690	-3.13
Euro / US Dollar	1.2878	11.73
US Dollar / Japanese Yen	98.9600	11.45
Euro / Swiss Franc	1.5053	8.98
Pound Sterling / Swiss Franc	1.8583	17.41

Commodities	Last Price	YTD %
Crude Oil	68.36	-24.85
Gold	754.83	-9.48

Alternative Investments	Last Price	YTD %
Tremont Hedgeindex	391.02	-9.87
Goldman Sachs Commodities	455.503	-25.35
LPX Private Equity	741.24	-43.53
Global Property	189.52	-27.50

Macroeconomic and Market perspectives

October and September were stamped with a sentiment of apocalypse within the global financial markets, which culminated with the rescue of Fannie Mae and Freddie Mac, the insolvency of Lehmann Brothers and the US Government taking over American International Group (AIG). Additionally Merrill Lynch was forced to sell itself to Bank of America only to be followed by the announcement that the last investment banks Morgan Stanley and Goldman Sachs agreed to become bank holding companies in a move to survive a deepening financial storm. Morgan Stanley and Goldman Sachs sought shelter with the Federal Reserve in a move that effectively ends the Wall Street investment banking model of the past two decades. The United States addressed the turbulence alternatively with brave reservation and hefty interventions culminating with the biggest financial bailout in U.S. history with an amount of USD 700 Billion of taxpayer money to take the worst of Wall Street's assets off its books.

The causes of the financial crisis are rapidly identified. Starting point was the run up in the U.S. housing market, which ended in a bubble. This was due to the overly generous money supply by the Fed, state run promotion of residential building and a problematic refinancing trend. This bubble was nurtured by an alignment of human characteristics such as greed, exorbitance, pretentiousness and incompetence, not only on Wall Street but also at the government, the authorities and the media. Maybe it is worthwhile to look back at 2004 when the SEC loosened the capital resources for the 5 biggest investment banking firms. Due to this regulation change the investment banks doubled their debt positions. This decision was like a starting point for the ongoing securities engineering.

The consequences of this financial turmoil are especially severe and painful for the U.S. The creditworthiness of the American state will come under pressure. The US budget deficit now amounts to 3% of GDP. At least a doubling of this figure will result thereof. Furthermore, in the aftermath the U.S. needs finally to start to save, not only private households but the state as well. This will be pretty painful as U.S. citizens were accustomed to living beyond their means. If this correction doesn't happen, the next crisis will be pre-programmed. Furthermore, an overlap of the real economy is inevitable, because the financial and the real economy are linked. Another consequence of the financial crisis will without doubt be an increase of regulations, the first one to be the interdiction of naked short selling. A lot of things have been written over the government bailout plan. Instead of discussing whether it was the right thing to do, we would like to elaborate on the implications of the plan. Obviously it helped the market by preventing a complete meltdown in the financial sector. Even if financial conditions do now improve, the availability of credit is only one dimension of the collapse in the housing markets and the economic backdrop is continuing to deteriorate. The bottom line is that the financial and economic imbalances have taken years to build up and may well take years to unwind. Equity markets are therefore likely to remain weak at least until the US economy shows signs of bottoming out. The impact of the increased supply of bonds needs to be seen in the context of the outlook for the economy, inflation and interest rates. The US economy is facing a prolonged period of stagnation and heightened risk aversion, inflation is set to fall sharply and short-term interest rates may well be cut again. Indeed the US GDP figures have been constantly revised down to zero growth or even worse showing signs of a contraction. The FED lowered its interest rates just last week and even further cuts are expected going forward and leaving them at this level throughout 2010. Under these circumstances the increased supply of bonds should be met with increased demand without yields having to rise.

The impact of deterioration in the government fiscal balances on the current account deficit is likely to be at least partly offset by an increase in household savings over the coming years, as consumers look to rebuild their finances in the wake of the destruction of housing wealth. Falling oil prices will also help reduce the trade deficit. Indeed, increased domestic savings could largely finance the increase in government borrowing without additional calls on overseas investors.

With regard to the dollar, we believe it benefited from the long-term credit-worthiness of the United States, its stability suggests that the US is still viewed as a safer risk. Eventually, the USD will reflect foreign concerns about the deteriorating U.S. economy and the huge trade deficit and resume its downward course once the financial crisis has calmed down.

Our most probable scenario for the developed economies calls for a recession or at least for a significant growth deceleration. Real estate prices in the US, UK, Spain etc. continue to fall while consumption slumps. Corporations try to save and cut costs. Banks continue to write down and/or sell assets and some banks are taken over by the government. The real economy ceases to grow and many countries enter into a prolonged phase of decelerated growth. The consensus growth GDP figures have been sharply revised downwards lately. This is evidenced by the euro-zone PMI survey, which showed that the economy contracted for the second quarter. Additionally the latest German Ifo Survey exhibited that business confidence continues to deteriorate. The only light at the end of the tunnel is the recent improvement in the inflation outlook following the sharp declines in global commodity prices. As well as easing (though not reversing) the pressure on household and corporate budgets, this will clearly give central banks a freer hand to support the real economy. We do believe, that prices regarding oil, gold and other commodities will return upwards after a phase of economic slowdown and value correction due to the structural demand/supply situation and due to the strong demand of the emerging countries e.g. China and India. The developments of the oil price are likely to be pivotal for other commodities and in particular agricultural concerns, given oil's importance as a production cost (via fuels and fertilisers) and the growing diversion of crops to the production of bio-fuels. ■

