CPIC
Management Report
2nd Quarter 2006

Economic Development in the 2nd Quarter 2006

The world economy is in a robust state. All the important developed economies, as well as the principal emerging markets, have recorded high and even rising growth rates. During the first half of the year, the US economy started showing the first signs of a cyclical downturn. Growth in the Eurozone, Japan and Switzerland reached levels that have not been seen in recent years. The reason for the buoyant world economy is the expansive monetary policy of the last few years coupled with the fact that business cycles in the major economies are becoming increasingly synchronous, thereby boosting foreign trade.

The downside of the economic upswing is that central banks have become increasingly worried about price stability. They therefore felt that they could no longer maintain the high level of monetary expansion of the last few years. Once again it was the US Federal Reserve Bank that set the ball rolling. The Fed announced that it was not happy with the effects of its interest rate increases on price levels. As a result of the surprisingly sharp increase in inflation, a further increase in interest rates seemed inevitable in June. By contrast, the European, Swiss and Japanese central banks reacted as expected, that is to say that they either raised interest rates or made the necessary preparations to do so. In many emerging markets, too, interest rates returned to normal after having reached extremely low levels in previous years, especially in Asia.

Developments in Financial Markets

Equity markets
Equity markets in the 2nd quarter were characterized by significant price volatility. This was set against a background of investor uncertainty with regard to future US monetary policy. This caused many investors to reduce their risk positions. Towards the end of the quarter, stock prices rose significantly as uncertainty about monetary policy in the US diminished. In the 2nd quarter, all equity markets saw a fall in values expressed in Swiss francs. According to the MSCI indices, the Swiss equity market lost 3.4% while the world equity market fell by 6.6%. On the Swiss equity market, virtually all sectors and asset classes were hit by this downturn, with the exception of a few defensive stocks such as the insurance and food sectors. In the first half of the year, by contrast, the Swiss market rose by 2.8% and the world equity market by 3.2%. As a result, equity markets significantly outperformed bond markets.

Bond markets
All major bond markets were hostage to developments in the world economy and monetary policy. The biggest losses, which were essentially currency-related, were posted by Hungary, followed by Poland, the USA and Japan. Swedish bonds were the only ones to buck the trend and finished the period in slightly positive territory. As bond prices had also fallen during the 1st quarter, negative yield for the first half of the year was compounded.

The weakness of the US dollar
The weakness of the US dollar has also been unsettling to financial markets, although this was partially corrected towards the end of the quarter. Although a long-term depreciation of the dollar seems plausible as a result of major economic imbalances, the extent of the fall in value registered in May was certainly not justified. The fact is that the Federal Reserve restricted dollar supply, and a slightly weaker US economy produced a somewhat lower current account deficit. The value of the Swiss franc rose against most currencies in the 2nd quarter after showing some weakness in the previous period. The turnaround can be explained by uncertainties on international financial markets and the more restrictive monetary policy in Switzerland compared to that in other countries.

Performance of the share value
In the 2nd Quarter 2006, the value of the A-share has decreased by -0.46%, from CHF 234.11 to CHF 233.02, and in the same period the B-share has decreased by -0.95%, from CHF 209.45 to CHF 207.47.

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