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Management Report
2nd Quarter 2008

Economic Developments during the Second Quarter of 2008

In spite of the dramatic rise in energy costs, a sharp spike in inflation, and a serious and continuing bank crisis, the world economic climate has not deteriorated as badly in 2008 as was initially expected. In fact, the US economy even grew by 1% during the first quarter, driven by a sharp cut in interest rates by the Federal Reserve and a booming export sector. Developments were less uniform during the second quarter.

The economies of Europe and Japan fared a little better, although the latest developments show that the situation has taken a serious turn for the worse. High petrol and food prices have made consumers far more pessimistic about the immediate future.

At the beginning of the second quarter, the US authorities undertook a number of actions which included a bailout of the investment bank Stearns, a loose monetary policy, as well as a package of measures to bolster the economy. As a result, it was hoped that the situation for US consumers would improve quickly. These hopes were, however, soon dashed by the massive hike in oil prices and a sharp rise in inflation.

Developments on financial markets

During the first six months of the year, commodities recorded their best performance of the last 50 years, whereas shares, and to a lesser extent bonds, performed extremely poorly during this period.

Because of strong inflationary trends, interests rates on international bond markets recorded a substantial increase, which translated into negative bond yields. In spite of this, most currencies appreciated somewhat against the Swiss franc in the second quarter, which helped to contain bond losses expressed in Swiss francs. At the end of June, the

annual performance of foreign currency bonds expressed in Swiss francs slipped well into negative territory.

On equity markets, however, the situation turned out to be much worse. Although the second quarter saw only minor losses, the first six months were the worst in 26 years. And yet the second quarter had initially seemed so promising. A rally that started in mid-March gave equity markets a significant fillip. But then came a toxic cocktail of sky-rocketing energy prices, a further round of gigantic write-offs at banks, rising interest rates, higher inflation, a poor economic outlook, falling real estate prices and a downward revision of profit forecasts by analysts. International equity markets lost over 8% in June alone. The Dow Jones Industrial index recorded its worst June performance since 1930. All the major markets suffered double-digit losses in June. Equity markets in Euroland fell by 11.7%. Swiss shares performed somewhat less badly, losing 7.5%. Emerging markets, with some minor exceptions, did not fare much better either. On an annualised basis, performance in the different sectors varied widely: energy and commodities did extremely well on the back of increasing raw material prices, whereas stock prices in other sectors were hit by a highly negative performance. The worst performers, and by a long margin, were the stocks of financial institutions which suffered from the disastrous effects of the collapsing US housing market.

In the 2nd quarter 2008, the value of the A-share increased by 0.6%, from CHF 232.56 to CHF 234.03, and in the same period the B-share increased by 0.9%, from CHF 207.20 to CHF 209.16.

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