Letter from the President and the Fund managers
January 2008

After a very chaotic beginning of the year, the severity of the financial crisis stepped up another notch during September and October, and concerted efforts by various governments and central banks were necessary to avoid a failure of the banking system. Stock markets around the world were falling sharply at the end of October and saw their worst month since the crash of October 1997. The drop in the indexes would have been even more pronounced without intervention by the U.S. Federal Reserve. Faced with the market collapse, the Fed reduced its main key rate by half a point, to 1%, at the end of October. This was the ninth decrease since the beginning of the financial crisis in the summer of 2007. Several days earlier Jean-Claude Trichet, the president of the European Central Bank, had mentioned an upcoming decrease in the rates at a meeting of the Governing Council.

The markets, faced with a crisis that could turn out to be the worst since the 1930s, also received aid from the governments and the IMF in the form of emergency aid funds and loan programmes. As a result of this general mobilisation, signs of a lull appeared at the end of the month. The credit market saw a drop in interbank rates, which had soared to exceptionally high levels in early October, paralysing the market. And after the crashes of the preceding weeks, most stock markets were able to limit their retreat.

In this particular context, we are paying the closest possible attention to changes in the real economy and the extremely erratic development of the financial markets. The solvency of our partners, especially our banking partners, is also under close scrutiny because of the threat of bankruptcy that hangs over many international financial institutions. Our custodian bank, Lombard Odier Darier Hentsch & Cie, specialises in portfolio management and is not active in the loan or investment banking sectors, which are at the root of the current crisis. So our custodian bank is especially well protected from the bankruptcy risks currently threatening certain large universal banks, all the more so since it has twice as much equity capital as required by law, holds no toxic assets, and is involved only very little with the interbank market, since its assets are placed with central banks. Finally, it is worth remembering that even in the hypothetical and highly unlikely case of a failure of the custodian bank, the shares held by CPIC would not be part of the bankruptcy assets, and would remain the property of the pension fund.

In addition, our two portfolio managers make the quality of companies in which the assets are invested a top priority. In particular, shares in financial companies are greatly underrepresented in the portfolio, which contains none of the companies recently reported by the press as being at risk of failure, and no “risky” structured product from an issuer that might default. In these conditions, the portfolio consists of quality securities that should carry it through the current low point of the financial crisis and the coming economic slowdown.

Despite our prudent positioning and focus on the quality of the securities, we have of course not remained completely unscathed by the major fall in the value of assets, which affects in particular investment in shares. However, CPIC’s strategy of diversifying over the largest possible number of asset categories has tempered the overall drop. The fact that we kept significant exposure in Swiss francs (CHF) has also helped limit the damage since the beginning of the year. So in spite of a 16.86% depreciation in CHF since the beginning of the year, the growth segment (A shares) lost only 7.08% in EUR, which after all is a modest loss given the dramatic stock market adjustment. The conservative segment (B shares) played its role - of protecting capital - well: although it has fallen by -5.26 in CHF since the beginning of the year, its performance in EUR of +5.88 was very positive.

We have experienced a major crisis, but the systemic risk to the international banking system now seems to be receding. While the effects of the coordinated steps taken in early October by the governments and monetary authorities of a number of countries have not yet been fully felt, these actions are leading to the gradual return of trust between economic players and are re-establishing the conditions interbank lending and loans to businesses require. Although our two portfolio managers are still positioning themselves cautiously, they are continuously on the lookout to benefit from opportunities that will appear on the financial markets once the situation turns around.