

INVESTMENT HORIZONTE

INVESTMENT PUBLICATION ISSUED BY MAERKI BAUMANN & Co. AG

APRIL 2010

**Dear Client,**

Four months have passed since we presented you with our first edition of *Investment Horizonte*. We were very pleased to receive positive feedback and suggestions for improvement from many of you and would like to thank you for your input. Numerous forecasts contained in the last edition have materialized over the past months. This applies to the feared equity market correction, but also to national economies, which remain unstable. In addition to an in-depth market review and outlook, we will examine opportunities for investing in emerging countries and the Norwegian krone, which are, in our opinion, particularly attractive at the moment. In the "Point of View" section, we look at the topic of public debt, which is likely to be an issue for some time to come.

We wish you enjoyable reading.

Yours sincerely,

A handwritten signature in blue ink that reads "A. Homberger".

Dr. Andreas Homberger
Chief Investment Officer

MARKETS AT A GLANCE

Caught up by the Truth

As feared at the end of last year, global equity markets experienced a correction at the beginning of 2010. After losing between 5% and 10% in January, they rallied again somewhat in February and March. Commodities were also slightly negatively impacted. The US dollar recovered sooner than we predicted, or more precisely, it benefited from the distinct weakness of the euro. Bond yields increased moderately during this period.

Economic development continues to be positive and most analysts have revised their growth estimates upward. The pace of development, however, has slackened, and the stabilizing effects of measures taken by governments and central banks are abating significantly, despite the prolongation of the individual support measures. We still believe that industrialized countries will experience rather modest growth in comparison to recoveries seen after previous recessions. As a result, labor markets and consumption will remain under pressure and central banks will not significantly raise interest rates at present. For emerging countries the situation looks significantly better. The Chinese government has restricted lending and in India, the short-term interest rates were increased as per end of March 2010 in light of inflationary risks.

In the meantime, the topics of government deficits and national debt have taken on increased importance. In Europe, the issues with Greece have resulted in doubts about the monetary union and a weakening of the euro.

Within the monetary union there is only a single monetary policy and fiscal flexibility is limited given the Maastricht criteria. As a result, an individual country in crisis has only two options: either to save or to seek external help. Despite occasional rhetoric to the contrary, the EU has not abandoned Greece. Big problems are coming to the fore not only in Greece, however, but also in Portugal, Spain and Ireland. Further to the debt problems, the not-so-well-thought-out attempts to regulate banks as well as the critical questioning of the independence of central banks are weighing on financial markets.

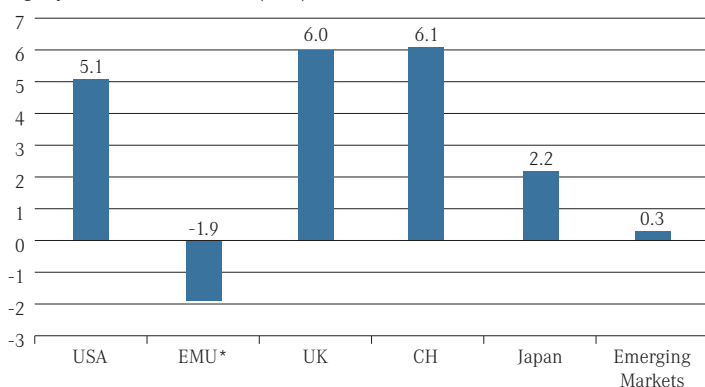
Our financial market outlook remains slightly cautious. Many of the problems that have arisen from the financial crisis have been deferred, but not resolved. We therefore do not anticipate significant short-term price increases in equity and commodity markets. With regard to bonds, gradual interest rate increases are likely to continue and central banks in emerging countries could soon increase interest rates. In this scenario, the US dollar is likely to remain strong.

Market Review for the First Quarter of 2010

Equity Markets

The initial euphoria arising from the strong trading days at the beginning of the new year has made a substantial retreat. Market participants have become significantly more nervous. This is visible, among other things, in the increased range of share price fluctuation, that is to say, in the volatility. The earnings season on the other hand, was predominantly positive. In the US, over 70% of companies met the profits and sales estimates. After some initial small gains, global equity markets began a more volatile downward trend. In recent weeks, however, prices trended slightly stronger and the MSCI World Index is now 2.8% in positive territory.

Equity Market Performance (in %)



* European Monetary Union

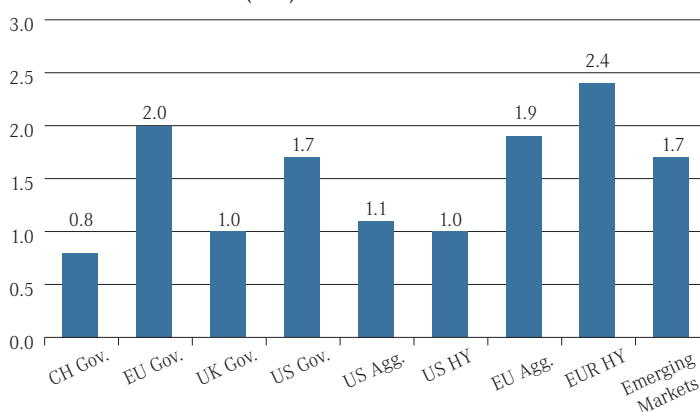
Source: Bloomberg, period 1.1-23.3.2010

With regard to countries and regions, we are beginning to see a reversal of trends, with last year's winners becoming the losers. Emerging countries were the financial market winners last year, but have been unable to maintain the trend this year. Certain peripheral countries, such as the Baltic States, Romania or Nigeria, that experienced a strong negative impact as a result of the financial and economic crisis, were able to demonstrate signs of a recovery. The difference in performance in developed markets, however, remained relatively small. Switzerland was once again able to prove its strength as a defensive market, whereas Europe, according to the STOXX 50 Index, was one of the losers. Since the beginning of the year, Japan has moved slightly into positive territory. Among emerging countries, China and India in particular have shown bigger equity market decreases. Signs of a tendency toward overheating of the real economy are becoming visible in both countries. On a sector level, the global tendency was to seek out rather defensive sectors such as pharmaceuticals, telecommunications and stable consumers. Predominantly cyclical sectors were avoided. The energy and utilities sectors brought up the rear.

Bonds

The trends that emerged last year in bond markets have continued into 2010. Generally speaking, highest grade government bonds have benefited from the "flight to quality." In Europe, countries considered uncertain and with a high level of indebtedness were punished with increased risk premiums. The catchword PIIGS, an acronym for Portugal, Ireland, Italy, Greece and Spain, was often mentioned in this context.

Bond Market Performance (in %)



Source: Bloomberg/Barclays, period 1.1-23.3.2010

It is interesting to note that certain market segments remained exempt from the generally increasing risk premiums, for example in the case of high-yield bonds and local debtors in emerging countries. Accordingly, no correction took place.

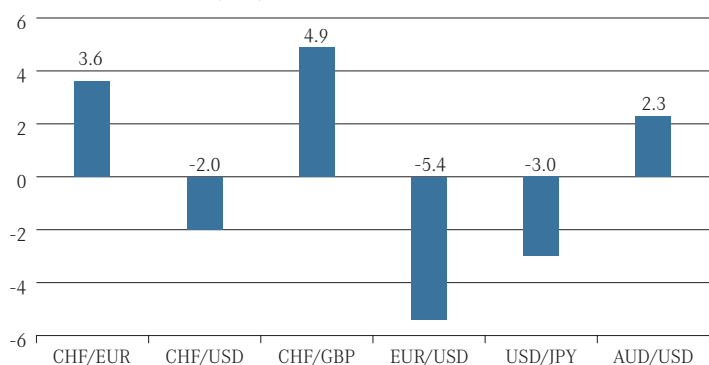
Currencies

In December 2009, a "revival" of the US dollar was already taking place, after having been almost written off. This trend has continued into the new year, and can be attributed to the once again slightly decreasing risk appetite. This manifests itself in the fact that higher risk investments, for example in currencies of commodities-producing countries, were sold and often exchanged against US dollars and Swiss francs. The catalyst for this was the discussion surrounding the indebtedness of individual countries within the Eurozone, which resulted in a significant weakening of the euro against several currencies such as the Swiss franc and the US dollar.

Greece in particular was the source of strong concern in this regard and put pressure on the euro against the Swiss franc and the US dollar. An appreciating Swiss franc has a negative impact on exports.

For this reason, the Swiss National Bank has suspended open interventions on the foreign exchange market. With the exception of the Japanese yen, Asian currencies appreciated versus Western currencies such as the US dollar, the British pound, the euro and the Swiss franc.

Currency Performance (in %)



Source: Bloomberg, period 1.1-23.3.2010

Commodities

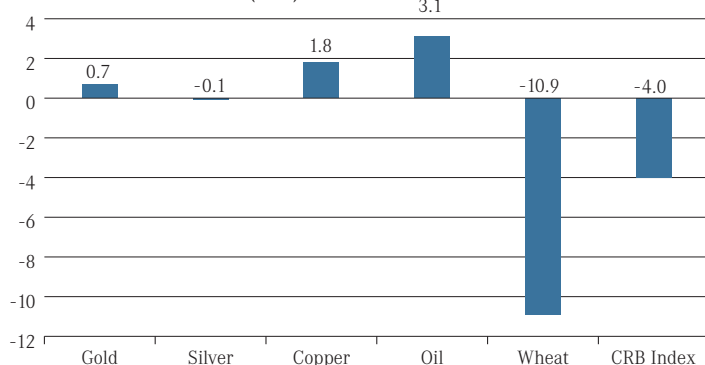
Developments in commodities markets have once again been heterogeneous. The CRB (Commodity Research Bureau), a broad index, lost approximately 4%. At the beginning of the new year, a price increase was still generally expected, but when risk appetite declined, commodity prices followed in line with equity markets – in a few instances quite significantly so. As an illustration: The zinc price, one of the leading economic indicators, decreased by 13%.

In terms of precious metals, silver underwent a short correction phase around mid-January with strong price movements of up to 20%. Overall, the silver price has changed very little since the beginning of January. During the same period, the price of gold increased by 1%.

The agricultural sector in contrast, developed unevenly. Positive trends were seen in pork bellies (+3%) and feeder cattle (+11%), while wheat (-11%), soy (-14%) and corn (-13%) experienced negative movement.

The Baltic Dry Index, an important leading indicator for economic activity, measures the various transportation costs for dry bulk traffic. The index rose by approximately 9% in the first months of the new year, which suggests that international trade is now slowly stabilizing.

Commodities Performance (in %)

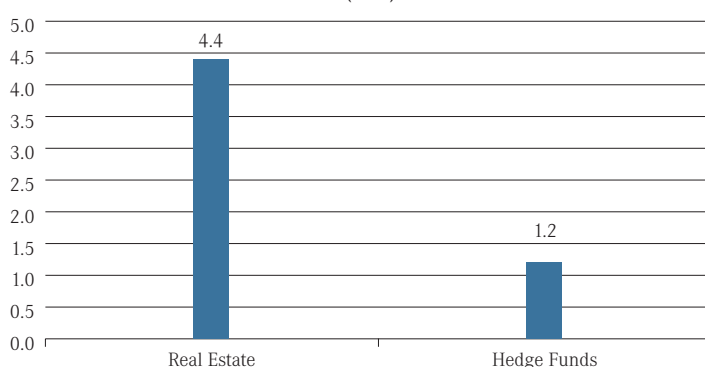


Source: Bloomberg, period 1.1-23.3.2010

Alternative Investments

Global real estate investments benefited from the current low interest rate environment and rose by approximately 4%. Since the beginning of the year, hedge fund performance has remained practically flat. In terms of single strategies, only convertible bond arbitrage has demonstrated exceptional performance, with a gain of 16%. The macro-manager strategy, which was very successful last year, only increased by approximately 2% year-to-date.

Alternative Investments Performance (in %)



Source: Bloomberg, period 1.1-23.3.2010

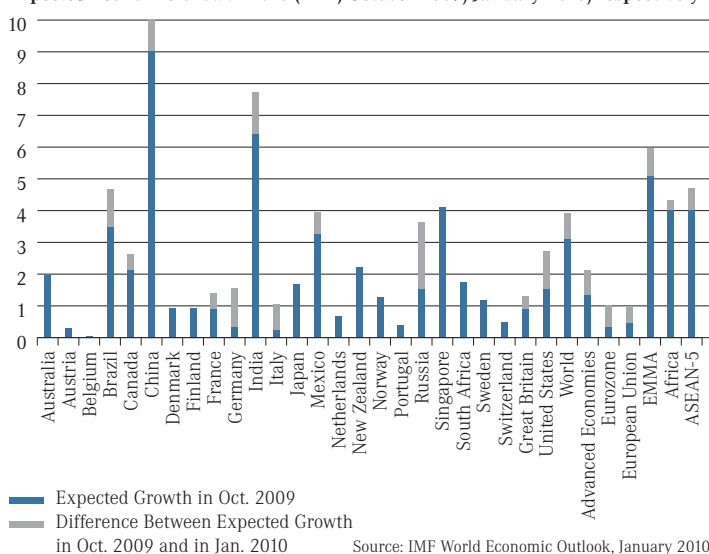
Outlook for the Second Quarter of 2010

Economy

The global economy has developed better than we expected since the last issue of *Investment Horizonte*, with momentum arising in particular as a result of growth in emerging countries. This momentum, however, is now already subsiding somewhat, as China and India in particular are aiming to slow growth via interest rate increases and limitation of credits and as the impact of fiscal measures introduced in the industrialized countries is waning. With regard to the latter, a self-sustained recovery is not in sight.

The International Monetary Fund (IMF) revised its 2010 growth forecast upward by 0.8 percentage points to 3.9% and for 2011, by 0.1 percentage points to 4.3%. For industrialized countries, the forecast was also increased by 0.8 percentage points to 2.1%, while growth in emerging countries is now being estimated at 6% (+0.9 percentage points). The enormous strength of consumption in the US and the restocking of inventories are important drivers behind the better-than-expected growth.

Expected Economic Growth 2010 (in %) October 2009, January 2010, respectively



On a country level, the US and Germany have seen the strongest adjustments: +1.2 percentage points for both countries. The current growth forecasts are 3.9% and 1.5% respectively. In emerging countries, expectations for Russia and India had the strongest upward revision, with increases of 2.1 and 1.3 percentage points respectively. The growth forecast for Japan remains unchanged at 1.3% despite a large, recently launched stimulus package. The forecast for England was increased by 0.4 percentage points to 1.3%, while Switzerland remained unchanged at 0.5%.

Even though growth rates look better than they did at year-end, the key problems have barely been addressed and have clearly not been resolved. Employment markets have not recovered and despite increased growth rates, reducing unemployment rates is likely to take a significant amount of time. Outside of the US, consumption and investment levels remain very low.

The subject of public debt is becoming increasingly important. Europe in particular is currently facing significant headwind in this regard. The PIIGS countries are all carrying enormous budget deficits of between 6% and 10% of aggregate output and national debt is in the range of 66% (Spain) and 125% (Greece). Unemployment rates are between 10% and 20%. Due to the unified monetary policy, these countries cannot bring momentum into their economies with cheap money. The fiscal scope is also very restricted – on the one hand due to budget deficits and indebtedness which are already too high and, on the other hand, due to the EU debt criteria. The solid growth of key countries Germany and France further compounds the issue of monetary policy. The European Central Bank is likely to gear its fiscal policy toward the key countries and therefore likely to increase interest rates toward year-end.

The problem is most acute in Greece, which was only granted entry into the EU as a result of dressed-up figures and did not follow a sustainable fiscal policy. Greece is overindebted and is dangerously close to insolvency. In the second quarter of 2010 alone, Greece is obliged to refinance over EUR 50 bn. This will be possible only at very unfavorable conditions, if at all. Greek government bonds have a yield of approximately 6% at present, almost double that of Germany. The agreed austerity program, although acceptable, has not found resonance with the population, the result of which is general strikes. Nevertheless, Greece and the other countries will remain in the EU. Increasing national debt, rising unemployment and a premature reduction of stimulus measures are the biggest risk factors for the global economy. In the “Point of View” section, we examine the subject of national debt in detail (see page 11).

Economic Data PIIGS Countries

	Budget Deficit*		Public Debt*		Unemployment Rate
	2009	2010	2009	2010	January 2010
Portugal	8.0	8.0	77.4	84.6	10.5%
Ireland	12.5	14.7	65.8	82.9	13.8%
Italy	5.3	5.3	114.6	116.7	8.3%
Greece	12.7	12.2	112.6	124.9	10.6%
Spain	11.2	10.1	54.3	66.3	18.8%

* in % of aggregate output

Source: EU Commission, various statistics

Inflation is still not a central issue in industrialized nations. In emerging countries, the situation is different, in particular for India, Russia and China where rising inflation is becoming apparent. Should these countries respond by introducing measures that are too drastic, the result could be a considerable slowing of the global economy.

Geopolitical Situation

In our view, the current overall geopolitical climate remains relatively stable. Several conflict areas including Afghanistan, Iran, Israel, North Korea and Pakistan should, however, be observed closely.

There is also potential for an increase in political stress tests within the Eurozone. The deficit problems in the PIIGS countries pose large challenges for the entire European economic area. It is relatively unlikely at this time, however, that negative effects arise through a forthcoming agricultural or energy shortage.

It is as yet too early to give the all-clear with regard to the swine flu (H1N1 virus). This conclusion was reached by the World Health Organization (WHO) after consulting with various experts. The WHO is maintaining its highest warning level, particularly since new cases of swine flu have emerged in West Africa. In addition, the winter season in the Southern hemisphere is soon to begin.

Equities

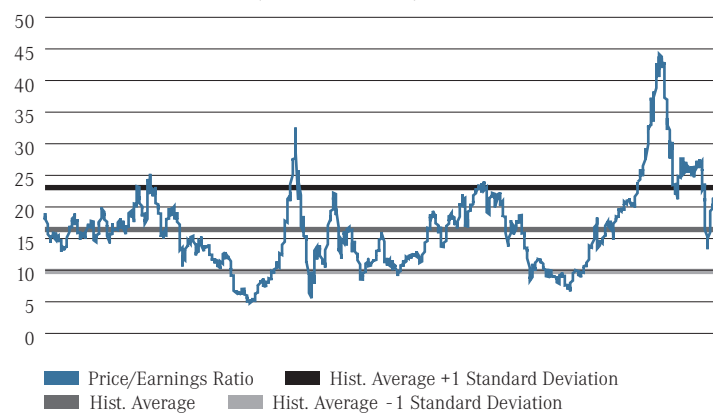
Although we expect moderate economic growth overall, we do foresee a relatively dynamic increase in corporate profits for this year. The drastic efficiency measures introduced by companies (optimizing of inventory management, layoffs, launching of cost reduction programs, etc.) were successful and will result in a slow increase in profit margins.

We still do not view equities on a global basis as cheap, however. According to the Shiller Price/Earnings Ratio (Shiller P/E Ratio), an important valuation indicator, the S&P 500 Index for 2010 currently stands significantly over 20. The long-term average since 1881 is 16.4. The Shiller P/E Ratio takes into account the inflation-adjusted average earnings of the last ten years in relation to the stock market price, which results in a smoothing out of the economic cycle fluctuations in earnings performance. Historically, Shiller P/E Ratios under 10 constitute good entrance opportunities. Ratios over 20, however, are a signal to sell. Equity markets in the US are forecasting earnings expectations that exceed analyst predictions and imply economic growth of 4-5%. Taking this view, the US equity markets are no lon-

ger attractive, which suggests a valuation adjustment in the long-term. The situation for the Swiss market is similar.

Equity valuations for emerging markets are also no longer as attractive. The price-to-book ratio compared to industrialized nations has increased by 1.2x. This was only ever exceeded in 1995, by a ratio of 1.35x. Adjusted by the price-turnover ratio, the number is currently 1.7x, compared with a higher valuation in mid-2008 (2x) and end of 2000 (over 2x). The higher the price-turnover ratio is, the less attractive the valuation of equity markets.

Equity Market Assessment (P/E Development)



Source: Robert Shiller, data for US equity market as of 23.3.2010

An increasing number of investors have reallocated their portfolios to these markets in the hope of stronger growth rates. Although we also expect higher GDP-growth rates in emerging countries, this does not necessarily mean that these markets will overperform in comparison to established equity markets.

We are therefore cautious with regard to equities in emerging countries at present. We would use a correction of 10%, however, as an opportunity to enter these markets. Increasing nervousness can result in a sudden correction in equity markets. We reduced this risk some time ago by under-allocating exposure to equities.

Equities remain attractive versus bonds. In the medium term, we consider equity markets to be interesting. In order for share prices to rise sustainably, however, company revenues must continue to grow.

Against this backdrop, we prefer investments with a thematic orientation, such as investments in the agricultural or energy sectors. We also favor companies that generate high and sustainable dividends.

Outlook for the Second Quarter of 2010

Bonds

In our view it is appropriate that the issues of indebtedness of certain countries have moved to the center of economic discussions. In the case of Greece, for example, which must restructure its debts, the refinancing need this year alone is over EUR 50 bn. Raising capital on the financial markets is becoming more and more expensive as market participants demand increasingly higher risk premiums. But not only Greece and the other PIIGS countries are experiencing problems. Even Germany is facing a certain expansion of risk premiums. A further issue is that although the most recently published GDP figures demonstrate a small growth for the Eurozone (GDP growth in the fourth quarter of 2009: +0.1% compared to the previous quarter), various individual countries had negative growth in the fourth quarter of 2009.

Interest rate increases are therefore undesirable at this time. We believe that the European Central Bank (ECB) will keep the base rate unchanged at 1% into the fourth quarter of 2010. In the US, we expect to see a base rate increase at the earliest by mid-year. The discount rate for bank loans was already raised by 0.25 percentage points to 0.75% in the first quarter of 2010. For the Swiss market, we expect an increase sometime between the increase of the US and European base rates. Such a decision also depends on the further development of the EUR/CHF exchange rate. In order not to further compound the negative effects of appreciation by increasing base rates, the Swiss National Bank will have to act carefully.

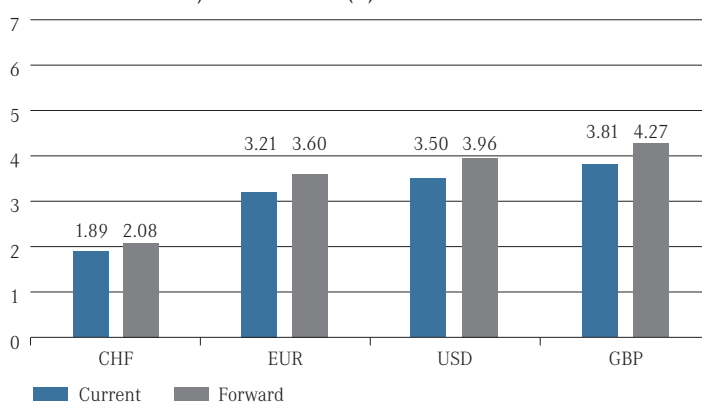
China, on the other hand, is battling with the increasingly evident problem of a real estate bubble. According to statements from observers, half of the new commercial buildings, for example in the Beijing region, are empty. Apartment prices in Hong Kong have reached the highest level of all active real estate markets in the world. China's official growth rate is around 11% and therefore significantly above the 8% national target. As a result, China has moved to a restrictive lending policy. This is not likely to change in the medium-term. Despite these adverse factors, we see entrance opportunities for the medium term in China.

Against the backdrop of a somewhat improved economic environment, we expect to see slightly increasing long-term interest rates. In the short term (i.e. over the coming three months), however, we see virtually no changes on the interest rate front.

In our view, the premiums on corporate bonds and emerging market bonds are still attractive. Government bonds, on the other hand, are generally priced expensively. Last year's global bond market performance will therefore be near-impossible to attain.

Norwegian and Emerging Market bonds are promising investment themes in our view, not least due to foreign exchange considerations and interest rate advantages, as compared to the Swiss franc and the euro (see the "Investment Recommendations" section on page 10).

Interest Rate Outlook, Ten-Year Bonds (%)



Source: Bloomberg, 23.3.2010 and Maerki Baumann calculations

Currencies

Considering the significant problems of indebtedness in the Eurozone and the clear trend toward overheating in China, it is not surprising that the US dollar is becoming increasingly sought after as a reserve currency. Additionally, numerous risk positions, not least in emerging markets, are being sold and converted back into US dollars. Postulations for depreciation of the US dollar have subsided again in past weeks.

We view the movement of the US dollar less as a reflection of strength of the greenback and more as a consequence of the weakness of the euro. The fundamental value, measured in terms of the purchase power parity, implies further upward potential for the US dollar. In particular, the US should play a leading role when it comes to the cycle of raising interest rates.

The appreciation of the Swiss franc is becoming an increasing burden on the Swiss export sector. The Swiss National Bank (SNB) has emphasized numerous times that it will not allow the franc to appreciate too strongly. We therefore assume that we will see further interventions on the part of the SNB. We also expect to see "peripheral" currencies such as the Norwegian krone appreciate. Furthermore, we believe select currencies in emerging countries to be undervalued, including the Chinese and Indian currencies.

We are cautious with regard to the British pound. The UK economy was particularly hard-hit last year by the financial crisis, resulting in a 5% decrease in economic output. Consumption continues to show signs of weakness, which also applies to price developments in the real estate market. However, based on the purchase power parity, the British pound is undervalued 18% as compared to the Swiss franc. Small signs of an economic recovery could result in a reversal of this trend.

The weakness of the euro is placing an increasing burden on the Swiss franc. Since the beginning of the year, the euro has depreciated by 3.80% against the Swiss franc (by 5.60% since December 2009, however), and against the US dollar by 10.90%. The SNB wishes to prevent an overly strong franc and thus last intervened when the rate reached EUR/CHF 1.48. This was only successful for a short time, however. As of mid-December last year, the euro depreciated again and slid to under EUR/CHF 1.43. According to voices in the market, the SNB has already intervened in the market four times this year.

The Norwegian krone is attractive due to the fact that Norway has navigated the economic crisis very well from a fundamentals perspective. Its public debt is one of the lowest worldwide. Unemployment is below 3%. Norway is one of the few countries in Europe with a growing population. With its rich oil reserves, the country has funded a USD 380 bn sovereign wealth fund, one of the largest worldwide. In terms of risk, the possibility of a strong decline in crude oil prices is worth mentioning, as this would have negative repercussions on the economy.

In addition, economic factors such as deep indebtedness paired with strong economic growth and high productivity speak for investments in various emerging country currencies such as the Brazilian real, the Turkish lira or the Mexican peso. Additionally, such currencies show a positive interest rate differential, a so-called carry, which means that an investment is made in a currency that yields higher interest on a relative basis. Because we believe that these trends will continue for the medium term, we remain positive for the next 2-3 years.

Commodities

Markets currently assume that the International Monetary Fund (IMF) wishes to sell the second tranche of gold directly in the market. However, priority will once again be given to interested central banks in order to avoid strong price movements in the market. A total of 191 tons are to be sold, which equals USD 7.2 bn at the current

market price. Should the central banks purchase this gold directly from the IMF, this would be a very positive indicator for the further development of the gold price.

One way to determine the relative attractiveness of commodities is to look at the important gold/silver ratio. Currently this ratio indicates a relative attractiveness of silver.

Gold also has interesting qualities. To a great extent, it is viewed as a currency and an investment that protects against inflation. Furthermore, gold benefits from a "flight to quality" mentality. Several of these points also apply to silver, although in the case of silver, industrial demand should also be listed.

Approximately 50% of the demand for silver relates to industrial use compared to only 11% for gold. Should industrial growth increase even slightly, we expect that the price of silver would increase relative to gold. We believe that both silver and gold make good additions to a portfolio.

Market participants appear to be content with a price range of USD 75-85 for oil. We still do not see any immediate factors that would result in the price of oil breaking through the upper end of the price range. We believe that we will see further stock reduction over the coming six months.

The annual price negotiations for iron ore deliveries between big producers such as BHP Billiton, Rio Tinto and Vale were recently concluded. In the process, a fundamental change was made to the price-determination practice: While over the past 40 years prices were fixed for the coming 12 months, going forward, they will be negotiated every three months and will be based on spot market prices. Price increases of up to 90% for iron ore are currently being achieved.

Our outlook for agricultural commodities remains unchanged. We anticipate higher prices for corn, soy and wheat in 2010/2011. The global discrepancy between supply and demand will widen significantly should it not be possible to augment the area of arable land. It is becoming increasingly difficult for China to be self-sufficient. Inventory is therefore being increased. As a result, we also see the possibility of a bottleneck on the supply side. This year's crops are difficult to predict, as they are heavily dependent on weather conditions.

Most commodities are still in so-called contango, meaning that the prices for future delivery are higher than prices for present delivery. Very few commodities are physically available, with the result

Outlook for the Second Quarter of 2010

that investments are generally made in commodities futures. These must be renewed, or “rolled over” before reaching maturity. In this process, new, comparatively more expensive futures are purchased. This leads to so-called roll-over losses which can reduce the total return significantly.

Maerki Baumann: Asset Allocation

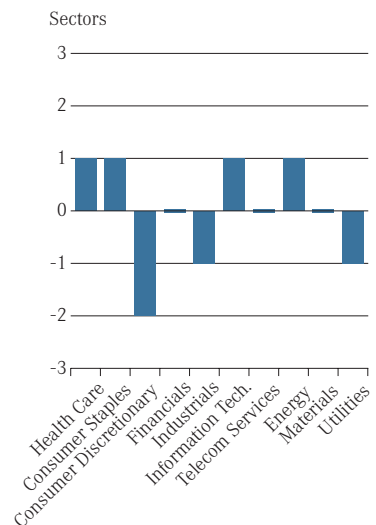
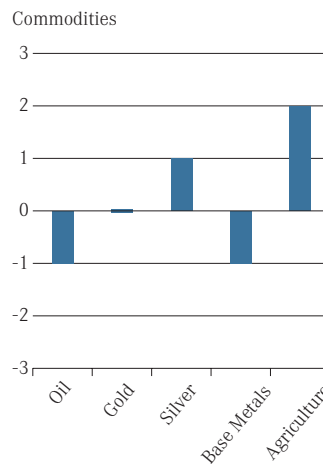
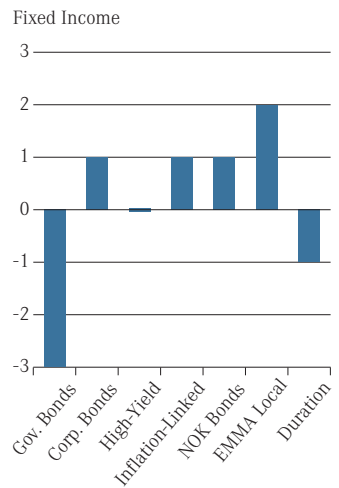
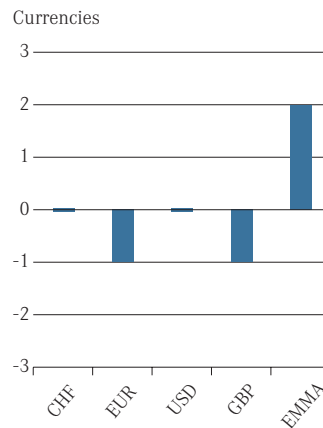
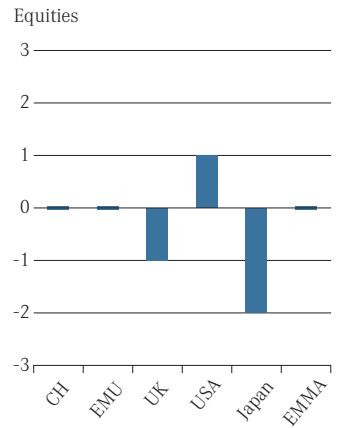
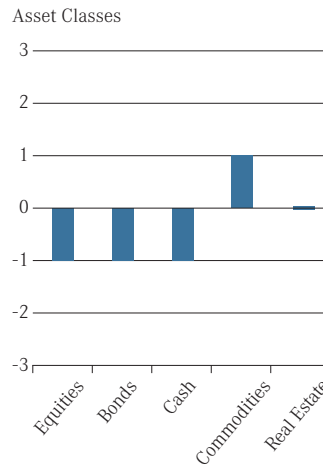
At present, we are underweight in equities. Equity markets rose approximately 60% in one year and valuations have increased accordingly. Based on fundamental factors, we no longer consider equity markets as cheap. The current earnings season is showing good results overall in terms of operating profits and sales trends, thus corresponding with the current share prices.

On a sector basis in Europe we are overweight in technology, energy and pharmaceuticals and underweight in consumer discretionary and industrials.

Our sector strategy for the US is very similar. Due to the structural differences between the US-American and European telecommunications sector, we are underweight in the US. In terms of special themes, we currently favor energy, agricultural commodities, gold and silver, as well as global infrastructure and inflation-protected bonds.

Looking at currencies, we are overweight in the respective local markets as well as overall for emerging countries. For CHF investors this translates into an overweight in Swiss francs, for EUR investors in euros and for USD investors in US dollars. We are underweight in euros and British pounds.

Asset Class Weightings



+/-3: strongly overweight/underweight
 +/-2: moderately overweight/underweight
 +/-1: slightly overweight/underweight
 0: neutral

Source: Maerki Baumann as of 25.3.2010

Updated Economic and Financial Market Scenarios 2010

Bull Scenario	Maerki Baumann Scenario	Bear Scenario
↗ Global economy grows by around 4-5%	↗ Global economy grows by around 3-4%	➔ Global economy grows by around 1.5-2%
↗ US economy grows by around 3-4%, Europe by around 2.5%, China by > 10%	↗ US economy grows by around 1.5-2.5%, Europe by around 0.5-1.5%, China by around 9%	➔ US economy grows by around 0.5-1.5%, Europe by around 0-1%, China by > 7-8%
↗ Central banks remain expansive and interest rates rise	➔ Central banks remain expansive and interest rates remain constant	↘ Central banks remain expansive and interest rates fall
↗ Unemployment decreases and new jobs are created	➔ Unemployment remains unchanged and a limited number of new jobs are created	↘ Unemployment continues to rise
↗ Consumer confidence recovers	➔ Consumer confidence does not recover completely	↘ Consumer confidence further declines
↗ Stock markets rise by about 20% and return to old record levels	↗ Stock markets rise by between 0% and 10%; high level of volatility	↘ Stock markets trend sideways or downward between -10% and 0%; high volatility
↗ Commodity prices increase markedly, gold price falls	➔ Commodity prices increase slightly, gold price may rise	↘ Commodity prices fall, gold price may rise
↗ Yield curves remain steep or become even steeper	↗ Yield curves remain as steep as at present	↘ Yield curves become flatter
↗ US dollar appreciates	➔ US dollar remains stable or appreciates somewhat	↘ US dollar depreciates
Probability: 15%	Probability: 70%	Probability: 15%

Investment Recommendations

Emerging Market Bonds (Local Currencies)

The growth outlook for 2010 for emerging countries that have historically shown substantially faster growth than developed countries and have also better weathered the financial crisis is significantly higher than for industrialized nations. The IMF forecasts a growth of 6.0% for emerging countries compared to 2.1% for developed countries. Based on these figures, emerging countries will account for approximately two thirds of global economic growth in 2010. This growth will not only be the result of exports, but also due to domestic consumption and investments.

The positive developments in emerging markets are also identifiable in the corresponding bonds. Emerging market bonds were historically high-yield vehicles with an average rating of BB or B. Today they are often rated BBB (so-called investment grade) or higher. This means that rating agencies assess these bonds as having a low probability of default, which is comparable to the levels of traditional corporate bonds.

A further improvement in ratings can be expected, which means that henceforth, credit spreads lower than in 2009 are possible and the opportunity for a positive return on this basis remains intact. Furthermore, we believe that some central banks will increase interest rates in 2010, which will have a negative effect on bonds issued in local currencies; however, interest rate increases will also strengthen the currencies and overcompensate the losses on bonds. Further reasons to invest in emerging market bonds in local currencies are the returns, which are higher than for the US dollar, the diversification effect and the limited correlation to other investment classes.

Maerki Baumann approaches this investment theme through the Pictet Funds (LUX)-Emerging Local Currency Debt. This fund invests in local currency-denominated bonds. In a first step, a top-down approach is applied to define the global risk environment and coupled with a bottom-up approach for the selection of the individual countries. In a second step, the attractiveness of the interest rates and currencies of the individual countries is ascertained in order to reach the final investment decision.

Pictet Funds (LUX)-Emerging Local Currency Debt-I-EUR

Swiss security no: 2 840 759

Fees (total expense ratio): 0.96%

Performance (as per 22.3.2010):

- Year-to-date: 11.29%

- 1 year: 35.47%

- 3 years: 41.04%

Bonds in Norwegian Krone (NOK)

Norway, much like Switzerland, has weathered the financial crisis well. This can be attributed to good fiscal and monetary policy as well as the importance of the oil industry, which had a stabilizing effect on the economy. In addition, Norway's public debt is one of the lowest in Europe and, as a result, the country was less affected by recession than the G-10 countries. Norway is thus the country with the highest capacity utilization.

After declining in the first quarter of 2009, gross domestic product (GDP) climbed steadily for the remainder of the year. Ultimately, it only decreased by 1.5% in 2009 (Eurozone: -3.8% for the same period). Norway expects a GDP growth of 1.5% for 2010, 1.9% for 2011 and 2.1% for 2012, while the expected growth rate for the Eurozone is 0.8% for 2010, 1.5% for 2011 and 2.0% for 2012. The growth drivers in Norway are strong private and public spending, the continuing global economic recovery and the rising price of oil.

Thanks to these factors, the Norwegian krone has advanced to become the strongest currency compared with the G-10 currencies and has been able to continue the trend of appreciation against the euro that began in 2009. The Norwegian central bank's monetary policy gave the currency a further boost, as it was the first European central bank to increase interest rates. The interest rate, which is now at 1.75%, will reach a level of 3% by the end of 2010, according to analyst estimates. The difference in interest rates to the Eurozone further supports the currency and is likely to result in a currency appreciation of 7.5% for the NOK/EUR exchange rate.

As in the case of emerging market currencies, we conclude that due to the appreciation of the Norwegian krone and the interest rate advantage of 1.5%-2.5% relative to the euro and the Swiss franc, an investment in Norwegian krone is attractive. We recommend bonds in Norwegian krone with average durations of 3-5 years, issued, for example, by Rabobank Nederland, with a 3.75% coupon and maturity in 2014.

Bonds: Rabobank Nederland

Swiss security no: 10 815 991

Coupon: 3.75%

Maturity: 21.1.2014

Rating: AAA

Point of View. National Debt

The state of government budgets has significantly worsened in recent years. In 2007, national debt in industrialized countries measured against economic output still averaged 73%. According to estimates by the IMF, this figure could increase to 109% by 2014. As a result of the financial crisis, budget deficits and national debt have become even more central issues. Both have reached unprecedented heights in industrialized countries and a reversal of this trend is not in sight.

Causes

For cyclical reasons, national debts have risen substantially over the last two years. Around the globe, countries have had to support their economies in order to lessen the effects of the financial crisis, or rather of the ensuing recession, with the result that national support and stimulus packages accounted for several percent of the respective gross national products.

Basics

The best measure of national debt is the value of all publicly held government bonds. The variation in national debt is primarily determined by the primary balance (difference between national expenditure and tax income), the servicing of public debt and the real growth of the economy. As a general rule, national debt rises when a primary deficit arises and when the real interest rate is higher than the economic growth. In such a case, the process of incurring debt becomes explosive, meaning that without measures to the contrary, the national debt in relation to the gross national product grows continuously. Generally speaking, however, a country cannot go bankrupt if it is able to print money. In a worst-case scenario, a country would print so much money that it could pay back a part of its debts in cash. This would, however, have disastrous side effects such as inflation, weakening of the exchange rate, increased interest rates, etc.

Looking at it from a macroeconomic perspective, the following interdependencies apply:

1. A larger national deficit can be refinanced by way of increased private savings (and the resulting reduction in consumption). The investors will, as a rule, request a credit spread for the additional savings.
2. Alternatively, investments can be reduced. The consequence thereof is slower growth of productivity and the overall economy in the medium term.
3. The budget deficit can be financed from abroad. High interest paid on additional capital attracts foreign investors and the currency appreciates in the short term. As a result thereof, more foreign rather than national goods are consumed which in turn leads to increased trade deficits and therefore slower growth.

4. Taxes can be raised in parallel or at a later stage.

The macroeconomic repercussions of budget deficits crucially depend on the creation of expectations in the markets. If the so-called Ricardian Equivalence applies, i.e., economic participants interpret the national deficit as an additional future tax, then national deficits have no effect other than that future consumption takes place today instead. If the interpretation diverges from this theory and participants feel more prosperous, it is possible that positive effects arise. According to the Keynesian school of thought, national deficits lead to many more positive effects: As a result of government spending, unused resources get activated and multiplier effects occur.

Consequences

Experts are somewhat divided with regard to the consequences of high budget deficits and national debt. Some generally applicable statements can however be formulated:

- Big deficits and debt levels limit the possibility of introducing further financial policy measures because more and more funds are put toward debt servicing. In the US, for example, debt servicing is estimated to rise to USD 500 bn between 2010 and 2019. This is equivalent to the yearly budget of the US for education, health, inland security as well as for the wars in Iraq and Afghanistan. High national debts lead to lower credit ratings and tend to result in higher interest rates. Assuming that national debts increase by 40% for all industrialized nations over the coming years, this would imply an increase in interest rates of 2 percentage points. In addition, the refinancing costs for private loans would rise given the fact that they are derived from the interest level of government bonds. As a result, investments become less attractive and economic growth slows down.
- In order to reduce national debt and budget deficits, it is necessary to save and to raise additional taxes. Economic growth also slows down.
- Should central banks be required to purchase government bonds as a result of insufficient demand from financial markets, then inflation and hyperinflation become latent dangers. This is because central banks need to print money in order to pay for the government bonds.
- High public indebtedness financed by foreign investors can lead to a debt and currency crisis. If investors lose confidence and sell the government bonds with the intent to convert the proceeds into their local currency, then this can have catastrophic consequences for a highly indebted nation. In this scenario, the country would have to raise interest rates quickly and introduce a significant cost-cutting program. The consequence is that the national economy falls into a deep recession.

Point of View. National Debt

Options for Decreasing National Debt

There are three options for decreasing national debt. All options correspond de facto to a levy tax or to an expropriation:

1. Reduction of the primary deficit: The government can save, i.e., spend less money. Given the fact that such measures can jeopardize the re-election of politicians, it is a difficult path to follow and was not successful historically, as it is not very practicable. The other possibility, namely increasing taxes, is not popular and has negative repercussions on consumption and investments.
2. Inflation: National debts can be monetized through the printing of money which is akin to an inflation tax. Given that newly printed money circulating within the economy has inflationary effects, the intrinsic value of the government debt (which is nominally fixed) is reduced. This method is very interesting for governments, because as a general rule, no centrally coordinated opposition arises. In addition, it is quite an efficient tool for reducing the problem of debt. Having said that, in the case of government

bonds with short maturities, this approach has its limitations because higher interest rates will have to be paid on government bonds issued in the future.

3. Repudiation: Not recognizing debt is an easy solution, however not a practicable or realistic one in the Western economies.

Summary

It is easy for countries to go into debt and enjoy political support in doing so. The beneficial effect is felt short-term but the negative repercussions will be felt later and all the more strongly. In order to mitigate the future implications, all countries that are currently significantly increasing national debt must have concrete plans in place for reducing this debt. As good as these plans may be, they will as a consequence slow economic growth and result in tax increases. In the years to come we will have to pay the price for benefits we enjoy today.

“Countries don’t go bust.”

(Walter Wriston, CEO Citigroup, 1967 - 1974)

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