PRIVATBANKIERS
REICHMUTH & CO
INTEGRAL INVESTMENT MANAGEMENT

CHECK-UP

CLIENT INFORMATION OF PRIVATBANKIERS REICHMUTH & CO, INTEGRAL INVESTMENT MANAGEMENT

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EDITORIAL

Crises are unfortunately an integral part of the capitalist system, just like periods of euphoria. However, there is no better system for ensuring long-term prosperity. Markets always exaggerate, on the upside as well as on the downside. Markets under tight state control may well do so to a lesser extent, but they inevitably lead to erroneous trends. The state can provide security over the short term so that people are not paralyzed by fear during a crisis and can eventually get back on their feet. Yet prices are ultimately determined by the markets, not by the state - and the markets have bounced back from every financial crisis in the past.

Just in time for the spring, we are seeing the first signs of stabilization on financial markets. These will be followed by a recovery in the real economy in about a year's time. We take a closer look at this scenario in the historical context on the final page of this issue of Check-Up.



Karl Reichmuth
General Partner

NO DEPRESSION LIKE IN THE THIRTIES

PROTRACTED PHASE OF STAGFLATION LIKELY

«This financial crisis is now hitting the real global economy with full force…the current situation is exceptionally serious.» Such unequivocal words from the Swiss National Bank are both startling and disconcerting. Are there even nastier surprises in store? Will the crisis plunge us into a depression like that seen in the 1930s?

Mountains of debt cannot be cleared with new debts

We are not expecting a 1930s-style depression. There are considerable differences in both the background and the responses to the current problems. The main cause of the present malaise is excessive debt. Especially the US, have lived beyond our means on credit. These debts have to be scaled back to sustainable levels, which is no easy task. The failures we have witnessed to date - especially in the banking sector with the collapse of Lehman Brothers - have destroyed a lot of confidence. Governments and central banks alike want to avoid further cases of this kind at all costs. Tools at their disposal are expansive monetary and fiscal policy. This means governments creating new debts in an attempt to reduce the burden of the existing debt mountain.

Inflation is the friend of all debts

Conversely, deflation is the worst enemy of all debts and must be averted. Deflation means falling prices, and the anticipation of further falls causes consumers to hold off from making purchases. Debts are a twofold burden in a deflationary environment. It would be easier if inflation were making debts more bearable for borrowers. If this were the case, the debts would continue to stand in nominal terms, but the inflation would reduce their value in real terms. Of course, this would entail real losses for creditors, but the system would be able to absorb these, and they would be less harmful than outright bankruptcies. Deleveraging, i.e. the reduction of debt, has already decimated asset values and thus resulted in a slump in economic output. This downward spiral will continue if deflation cannot be effectively combated. The real debt burden will increase, and with it the number of firms going bankrupt.

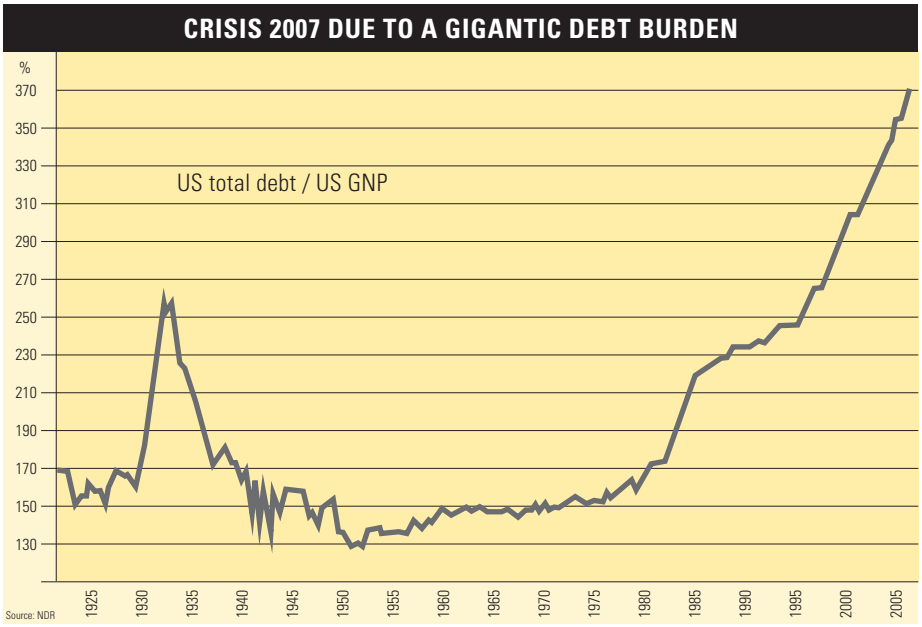
How can we create trust?

Trust only builds up slowly. A stable financial system is an essential prerequi-

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site. In addition, the end of the economic downturn has to be in sight. This should be the case from the fourth quarter of 2009 onward. The economic downturn did not come about until the final quarter of 2008, prior to which economies had been performing very well indeed. We will have to wait until toward the end of the year for a weak year-back comparison base. This basis effect will then help to produce positive growth figures.

How much debt can the state create?

Provided a government can take on debt in its own currency, which it can print itself, there is theoretically no limit. This holds true as long as buyers can be found for the debts. This is still the case in the US, yet not in Ireland or Spain. The latter two countries belong to the euro zone and can no longer print their own money. The central bank can also buy up government debts to a certain extent. Newly printed money is being used to finance government debts, which is economically questionable and will probably depress the currency's external value.

How do we put money into consumers' pockets?

This is currently the big question, and it remains unanswered for now. The financial system will be saved, whatever the cost. To date, however, the new money has only served to fill the gaps in the banks' balance sheets - it has not helped to create new demand. Cutting costs and reducing capacities is the order of the day in the real economy for the time being. This is causing unemployment to rise. While unemployment insurance has a stabilizing effect, it is not enough for a sustainable upswing. The economy must first bottom out, and this will take a long time.

What does this mean for currencies?

Printing new money to finance government debts is only economically viable in a crisis situation. It means that the currency has to depreciate. However, the question amid the current problems in the global financial system is this: against what? All the major currency regions are now printing money - Switzerland included. In fact, the frequency and scale of interventions by governments and central banks are increasing, and they are unpredictable. It is therefore impossible to make economic forecasts over the short term.

Protecting against currency effects

How can investors protect themselves against losses in the value of currencies? This is only possible if you draw a distinction between preserving money and preserving value. This is explained schematically on page 6. Value can only be preserved by investing in assets with solid long-term earnings power. Money is not such an asset at the moment, but the stock of a globally active firm like Nestlé is. Central banks' decisions are only of secondary importance to such firms. Nestlé produces and sells worldwide and thus has a global cost and income base. Large-cap companies of this kind serving day-to-day needs like food, medicine or energy are more suited than cash to a portfolio geared to value preservation.

How do you preserve your assets in this environment?

Rather than a depression, we are expecting a lengthy phase of weak economic growth with gradually rising inflation. We are viewing equities more positively than we were six months ago. Stock markets are much quicker to react than the real economy. They are driven by supply and demand. Over the past few months, fear has prompted investors to offload their stocks on the market. This oversold situation is likely to ease, perhaps even turn around. Sudden, sharp increases in stock prices are normal in phases like this, but the real economic outlook is not yet positive enough to support a new multi-year bull run.



Christof Reichmuth
General Partner

THE BIG PICTURE

OUR SCENARIO ANALYSIS IN A NUTSHELL

CONSENSUS	CYCL. DEFLATION	DEPRESSION	STAGFLATION	GROWTH
The financial crisis has peaked but is still far from over. The real economic downturn continues. The central banks maintain extremely expansionary stances, and government finances are increasingly problematic. Inflation is not an issue.	The financial crisis persists, and the real economic downturn worsens. Bankruptcies increase, and unemployment becomes a serious social problem. Despite all the central banks' efforts, temporary deflation is unavoidable as commodity and real estate prices fall further.	Governments and central banks fail to restore trust. The economic crisis spreads. Pension systems collapse. Bankruptcies and unemployment take on massive dimensions. The deflationary spiral accelerates. Investments are avoided wherever possible.	The central banks' extremely expansionary monetary policies keep core inflation rates above zero despite the worsening economy. Confidence in the central banks and the value of money evaporates. The economy only recovers slowly. Over time, the inflationary spiral begins to gather pace.	The financial crisis is overcome, and the real economy starts to recover. Central banks drain back excess liquidity. Inflation picks up slightly but remains modest.
INVESTMENT IDEAS Diversified money market Corporate bonds ETFs in high-yield bonds Dividend stocks with low valuations	INVESTMENT IDEAS Diversified money market Bonds from firms with a stable business Dividend stocks with no debt Inflation-linked bonds	INVESTMENT IDEAS Government bonds Stocks of crisis-resistant firms Farms with land	INVESTMENT IDEAS Inflation-linked bonds High-yield real estate Dividend stocks with high debt Gold	INVESTMENT IDEAS Short government bonds ETFs in high-yield bonds Cyclically sensitive stocks and emerging markets
High Yield Spreads: 1200	High Yield Spreads: 1800	High Yield Spreads: 3000	High Yield Spreads: 800	High Yield Spreads: 300
Probability 6 months: 25%	Probability 6 months: 40%	Probability 6 months: 10%	Probability 6 months: 20%	Probability 6 months: 5%
Probability 24 months: 10%	Probability 24 months: 20%	Probability 24 months: 10%	Probability 24 months: 50%	Probability 24 months: 10%

IS THE BANKING SYSTEM STABILIZED?

A LONG RECOVERY PERIOD TO BE EXPECTED

Credit Default Swaps (CDSs) serve as a good indicator for the situation of the banking system. For a given debtor, CDSs reflect the costs implied for a default insurance of a five-year bond. In our analysis we follow the development of CDSs very closely and define the banking system as stable whenever these rates fall below 100 basis points. Until the start of the financial market crisis two years ago, these rates were much lower. Taking the example of the CDSs for UBS one can clearly recognize the three most pronounced periods of that crisis. At hindsight, whenever these rates reached a peak, they also indicated a short-term trough of the stock price. Consequently: whenever the stock price rises, CDSs sink and vice versa. It is still too early to call for an enduring stabilization of the banking system – yet, from a short-term view it seems that the situation has slightly mitigated. And, should the CDS curve continue its descent – which is what we expect – then we can assume that the banking system has stabilized.

UBS 5-YEAR CREDIT DEFAULT SWAP STILL TOO HIGH



INVESTMENT POLICY
MAY 2009

BASIS	CH	EU	USA	J	CHINA
Purchasing Power Parities					
Ned Davis Research		1.52	1.16	1.11	
GDP Growth					
actual	-0.6%	-1.5%	-0.8%	-4.3%	6.1%
6 months	↘	↘	↘	→	→
3 years	↗	↗	↗	↗	↗
Inflation					
actual	-0.4%	0.6%	-0.4%	-0.1%	-1.2%
6 months	↘	↘	↘	↘	→
3 years	4.0%	5.0%	6.0%	3.0%	7.0%
Stock Markets	**SPI**	**DAX**	**S&P 500**	**TOPIX**	**HSCEI**
Price/Sales	1.1	0.5	0.9	0.4	1.3
Dividend Yield	2.8	5.6	3.3	2.3	3.2
Price/Book	1.5	1.3	1.9	1.0	1.8
Price/Earnings actual	30	18	13	30	13
Price/Earnings estimate	12	12	15	37	12

FORECAST	CH	EU	USA	J	CHINA
Money Markets (3 months)					
actual	0.4%	1.4%	1.1%	0.6%	1.2%
6 months	↘	↘	↘	↘	→
Swap Rates (10 years)					
actual	2.4%	3.5%	3.1%	1.3%	5.9%
6 months	→	→	→	→	n.a.
3 years	↗	↗	↗	↗	n.a.
Currencies					
actual		1.51	1.14	1.18	6.0
6 months		→	→	→	→
3 years		↘	↘	↗	↗
Stock Markets	**SPI**	**DAX**	**S&P 500**	**TOPIX**	**HSCEI**
actual	4'325	4'580	865	830	8'700
6 months	→	→	→	→	→
3 years	↗	↗	↗	↗	↗
Real Estate Market	→	→	→	→	→

Legend: ↗ = increasing → = neutral ↘ = decreasing as of: April 27, 2009

MARKET OUTLOOK
2nd TRIMESTER 2009

CURRENCIES

Currency rates remain volatile, yet move only slightly. The currencies that were strong during 2008, the CHF and the JPY, have weakened.

The cooperation and coordination among central banks has created a climate of relatively stable currency rates. In some countries, for example Eastern European countries, the worldwide financial crises has lead to massive disequilibriums in the balance of payments. Hence, sharp currency devaluations could not be avoided, yet the overall financial situation of those countries has remained under control thanks to generous support by the IMF and the leading central banks. In Switzerland and Japan market participants were convinced by the authorities that the strong appreciation of their respective currencies would not be accepted anymore, and, hence, a weaker CHF and JPY were accepted. The disequilibriums in the current accounts have become smaller, in particular the deficit of the USA. Yet, these must be reduced substantially more in order to bring currencies back into stable conditions in the long-run. At least, inflation rates have aligned and, hence, there are no longer any major deviations from the point of view of purchasing power parity. Consequently, short-term relatively stable currency rates are to be expected. In the long-run the USD will probably continue its descent, especially against Asian currencies. The EUR will probably fall slightly against the CHF to a level below CHF 1.50.

INTEREST RATES

Money market rates have continued to weaken and are close to zero. Long-term rates have stabilized at very low levels.

Under the pressure of the on-going financial market crises central banks have continued with their policy of lowering base rates. This policy was accompanied by unconventional measures such as «quantitative easing». Only the ECB remains with a potential for further cuts in the base rates and it is to be expected that it will soon make use of this. Base rates in other countries are already close to zero. Since the economies continue to be weak there is no inflationary impulse due to the massive increase in the money supply. Yet, long-term, the danger of an inflation wave can only be avoided if central banks decide to drain such money supply massively and timely. From today's perspective it is unclear whether they will succeed in this taking the expected huge political pressures; because interest rates will probably have to be raised when unemployment starts to peak.

Long-term yields have moved only slightly and remain at historically low levels; yield curves have steepened somewhat. When and by how much long-term rates will start to rise will be a function of inflation expectations by market participants. For the moment the tendency towards deflation remains in place. The example of Japan demonstrates that an economy can remain in a deflation for many years despite a massive increase in the money supply and an extremely expansionary fiscal policy. Hence, a sudden and massive rise in interest rates seems currently improbable.

Credit spreads for corporate bonds for many sectors, and in particular for the financial sector, have diminished sharply from their highs. As it seems the culmination of the worldwide financial crises is behind us. Yet the slowdown in the real economy continues and the large wave of defaults is still to come. Consequently, the market for corporate bonds will continue to be volatile. A skillful selection of securities in this sector is promising, even if rates start to rise.

STOCK MARKETS

The year 2009 started on a bad footing; yet, in the last few weeks an emerging recovery was able to recoup some of the large losses.

Will the recovery of the last weeks continue or was it only a correction of the oversold situation that was driven by fear? For the moment being, we believe the latter and, therefore, expect a sideways market characterized by large volatility. Stock prices are a function of supply and demand and, for the moment, the strong selling pressure seems to have abated. Short-term investors try to take advantage of such swings by entering the market, e.g. via an index, and simultaneously implementing stop-loss orders. For longer-term investors we recommend to gradually increase stock positions. From a fundamental point of view stocks are attractive despite lowered earnings expectations. Since the economic outlook remains very unclear we continue to focus our attention on defensive sectors, e.g. firms with a solid capital base and stable free cash flows in the pharmaceutical, non-cyclical consumer or utility sector.



Dr. Max Rössler

MODULAR CONCEPT «PORTFOLIO OF THE FUTURE»

MIX OF PORTFOLIOS GEARED TO DEFLATION AND INFLATION

We currently view the portfolio as comprising two extremes. One is geared to deflation, the other to the phase of inflation which we are anticipating. At present, we advise holding as much cash as you will need over the next two years. The rest, in other words the long-term portfolio, should be gradually shifted over the next 12-18 months toward the inflation portfolio, which aims to preserve value with a higher weighting of equities and a lower weighting of fixed-income paper. Our Portfolio of the Future is a mix of these two extreme portfolios. Diversification continues to take precedence in terms of asset classes, individual investments and currencies. We expect the asset allocation of this model portfolio to shift more toward the inflation portfolio over the coming 12 months. We will be happy to compile suitable proposals for you as a basis for discussion.

PORTFOLIO FOR AN ENVIRONMENT OF DEFLATION/DEPRESSION

ALLOC.	WHAT
80-100%	**Fixed Income** Cash Money market Government Bonds Bonds from toop issuers
0-10%	**Dividend stocks**
0-10%	**Precious Metals** Gold / Silver physical

Expected return: 1-3%, expected volatility approx. 3-5%

Expectations for the next 3-year average – no guarantee

VALUE-PRESERVING PORTFOLIO FOR AN INFLATIONARY FUTURE

ALLOC.	WHAT
0-20%	**Fixed Income** Inflation-linked Bonds Corporate Bonds
20-80%	**Equities** Solid balance sheets, stable cash flows Utilities, energy, food, pharma, infrastructure, commodities
0-20%	**Alternative Investments** Distressed and Global Macro Strategies
5-20%	**Precious Metals** Gold / Silver physical
5-20%	**Real Estate** With long-term financing

Expected return: 6-9%, expected volatility approx. 10-14%

Expectations for the next 7-year average – no guarantee

«PORTFOLIO OF THE FUTURE» - ADAPTED TO THE MARKET ENVIRONMENT

ALLOC.	WHAT	IMPLEMENTATION	RETURN*	VOLATILITY*
40%	Fixed Income	Money market Short-term bond from companies with stable cash flows EUR inflation-linked government bonds	2-4%	4%
25%	Equities	Scale-in / Scale-out concept Stocks with no or little debt Food, health care, energy, and electricity infrastructure	6-12%	15%
5%	Structured products	Asia FX against EUR and USD	10-15%	8%
20%	Alternative Investments	Reichmuth Matterhorn and diversified fund of hedge funds Reichmuth Himalaja	8-10% 10-15%	< 5% < 10%
5%	Real Estate	1/2 Switzerland, 1/2 Asia Reits	5-10%	15%
5%	Precious Metals	Gold / Silver physical (ETF ZKB or Julius Bär)	8-10%	10%
		Total	**5-8%**	**approx. 6-8%**

*Expectations for the next 5-year average – no guarantee

INTEGRAL INVESTMENT MANAGEMENT

IMPLEMENTATION WITH A MODULAR CONCEPT

Integral investment management is central to our corporate mindset and the services we offer. Investment management can only be integral if it is based on a consolidated overview of the assets concerned and a detailed knowledge of the client's personal circumstances. The question of where the assets are deposited with is only of secondary importance. They may be with our private bank, with another bank, or split between the two. We call this flexible approach our dual business model, i.e. clients are free to choose where they deposit their investment assets for safekeeping. It is of course always advisable to maintain a consolidated overview of the assets as a whole with a view to setting a strategic course for the future.

Our modular concept can be adapted to a changing environment

As regards implementation, we have been working with our proven modular concept for years. We diversify the modules in terms of more than just stocks and bonds. Precious metals, alternative investments, structured products, and real estate stocks are also included in the mix. In line with our future expectations, we give the most promising modules higher weightings than the others. This active weighting of the individual building blocks is based on our future-oriented approach and has been the decisive success factor of our investment concept over the last decade.

Tobias Pfrunder

A NEW START FOR REICHMUTH MATTERHORN

NEW LAUNCH OF A SUCCESSFUL AND PROVEN CONCEPT

FACTS AND FIGURES PER DECEMBER 31, 2008

Performance in USD	1 Year	5 Years	10 Years	15 Years
MSCI World	-42.0%	-11.2%	-20.0%	+53.8%
HFRI Fund of Funds	-21.4%	+9.9%	+67.7%	+126.8%
Reichmuth Matterhorn	-18.9%	+32.0%	+108.2%	n.a.

At the start of this year the fund management company had to decide on the dissolution and the new launch of the successful fund of hedge funds Reichmuth Matterhorn. As a consequence of redemptions caused by the financial crisis and the fraud case of Bernard Madoff the portfolio structure would have shifted unfavorably and no longer conform to the targets over time. This strong step was the only way to assure the absolute principle of an equal treatment of all investors. The dissolution is being conducted as planned and by the end of April 2009 approximately half of the fund volume has been returned to the investors, as scheduled.

Good Performance – bad Press

It is during periods of crises that one bethinks oneself about things that one believes to know. In particular, hedge funds are once again in the forefront of critics – despite the fact that the origins of the current crisis lie in the most regulated market sector, i.e. banks and brokers. An objective performance comparison speaks a clear language: hedge funds performed considerably better than equities, irrespective whether the analysis is short or long-term.

Building block in a diversified Portfolio

Alternative investments were and continue to be an attractive building block in a diversified portfolio. Since a fund of hedge funds is further diversified, lump risks at the level of the building block, the strategy and of a single investment can be avoided.

Very promising Strategies

Our new fund of hedge fund program is based on our long-term and proven track record and our experienced team. With our new solution we want to provide our clients with an opportunity to invest in this attractive building block – a module that can continue to take advantage of the various promising hedge fund strategies that we can no longer take advantage from with our existing fund in dissolution. The following table gives an overview of some promising topics for the new start. We would be happy to explain some of these investment ideas in our next dialogue with you.

Dr. Ricardo Cordero

PROMISING TOPICS FOR SPECIALISTS

TOPIC	STRATEGY
PROBLEMS DUE TO CYCLICAL DEFLATION	
■ Currency devaluation (e.g. Eastern Europe)	Global Macro
■ Danger of a state collapse	Global Macro, Short Strategies
■ Default of Corporate Bonds	Global Macro, Short Strategies
■ Mis-pricing due to selling pressure	Relative Value
OPPORTUNITIES DUE TO LONG-TERM INFLATION	
■ New currency system	Global Macro
■ Increasing demand for commodities	Global Macro, Long/Short Equity
■ Saving/recovery of the banking system	Long/Short Equity, Event Driven
■ Infrastructure programs	Long/Short Equity
■ Emerging Markets with good fundamentals	Long/Short Equity
OPPORTUNITIES DUE TO RESTRUCTURINGS	
■ Strategic take-over of firms	Event Driven
■ Restructuring of balance sheets	Distressed

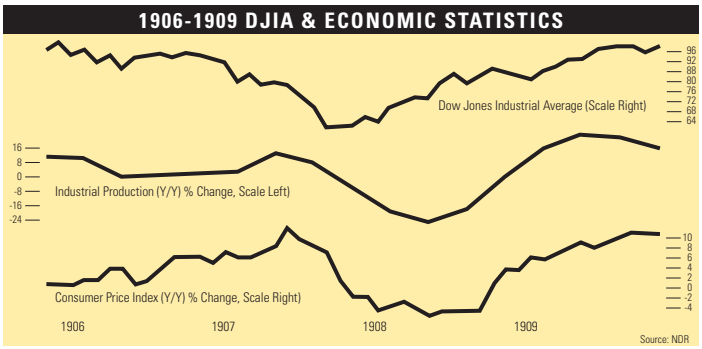
LESSONS LEARNED FROM PAST CRISES

EQUITIES TURN AROUND FIRST, THEN THE ECONOMY, THEN INFLATION

Past experience from seven financial crises since the year 1900 give grounds for optimism. Six were turned around within two years, with only the Great Depression from 1929 to 1936 lasting longer. The three biggest crises are outlined in brief below:

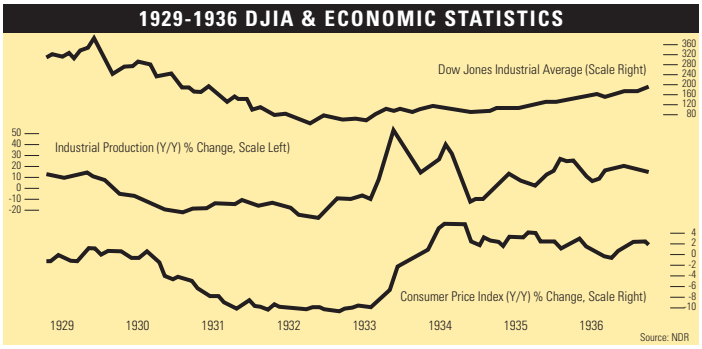
The financial crisis 1907-1909

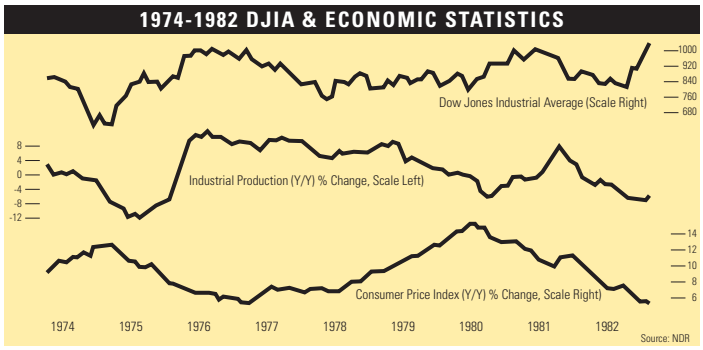
Following several bullish years, the stock market fell by 44.1% between January 1906 and November 1907. Real gross domestic product (GDP) contracted by 10.8% in 1908. Consumer prices decreased by 3.2%, and unemployment hit a high of 16.4% in 1909. However, the stock market rebounded by 89% as early as 1908 after J.P. Morgan and other bankers ensured a massive increase in the money supply.



The Great Depression of 1929-1936

Amid a crisis in the global economy, the stock market slumped by almost 90% between September 1929 and July 1932. Real GDP fell by more than a quarter up to 1933. In a deflationary environment, consumer prices came under heavy pressure, dropping by about 25%, and unemployment had risen to 25% by 1933. Nevertheless, an upturn began on the stock market in 1933, when stocks gained 110% until the end of 1934. The turning point came with the newly elected President Roosevelt's «New Deal» at the end of 1932, which served to significantly expand the money supply.





The recession years of 1974-1982

Between 1974 and 1975 GDP fell by 2.5% (and by more than 6% in Switzerland in 1975). The trend in consumer prices was atypical compared with other crises. Driven by high oil prices, they rose by 30% between 1973 and 1975. The US budget deficit, forced up by higher government spending, peaked at 4.2% of GDP in 1976. Unemployment rose to 9% in May 1975. The USD depreciated against the CHF from 4.30 to 2.35 in the period from 1973 to 1975. The stock market lost some 45%, only to post a gain of 76% in mid-1975.

The financial crisis of 2007-?

Between its high in October 2007 and its erstwhile low in March 2009, the stock market lost more than 50% of its value. Real GDP was down 1.8% in the second half of 2008 and is set to fall further. Inflation is on the slide and already in negative territory in some cases. The US budget deficit is likely to reach 12.3% in 2009, higher than it has been since the Second World War. Unemployment is rising and has already reached 8.5% in the US. When will the financial markets turn around this time?

What we have learned

None of the comparison periods offer precise points of reference. The only thing we can be certain of is that spring always comes around. What we can learn from the past is that stock markets preempt a recovery in the real economy by 12 to 18 months and that inflation becomes an issue again once this recovery sets in. We remain convinced that 2009 will be a year of cyclical (i.e. temporary) deflation without a slide into depression. We thus expect a trend toward stagflation in the next year to two years and advise broad diversification with a successive restructuring of the portfolio in favor of inflation protection, meaning more real assets instead of nominal ones.



Karl Reichmuth
General Partner