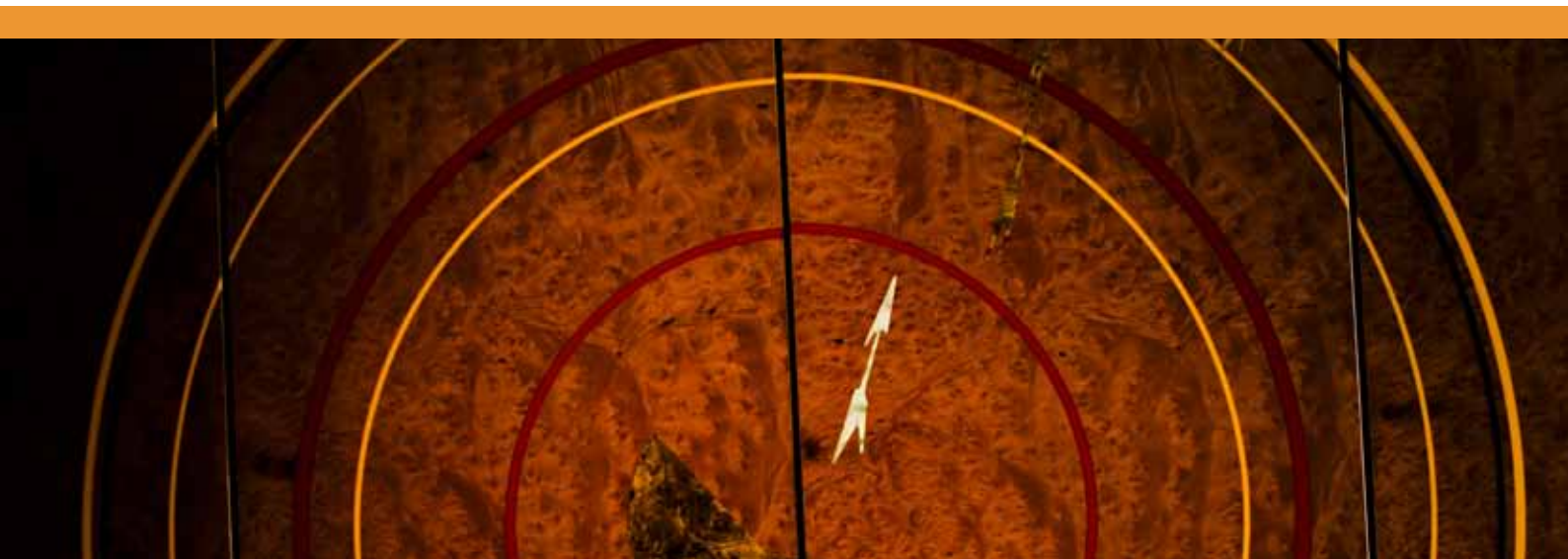
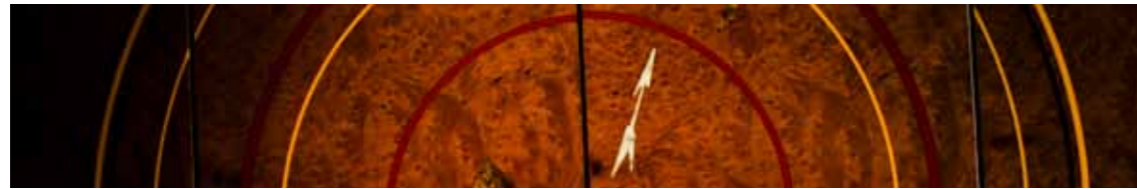


Trends



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Zuccotti Park

PATRICK SÉGAL

The tent city that has sprung up in Lower Manhattan deserves notice. Every day the protesters denounce the misdeeds inflicted on the real economy by a hypertrophic financial industry. The movement has spread to a number of financial centres, swollen with students who cannot find a job after borrowing to go to university and who now rail against the sizeable bonuses paid by firms that were largely to blame for the present crisis.

Little by little we are all growing indignant about the bewildering recklessness of some that threatens the health of our entire economies. Social strife cannot be far away in a situation where many young people have no future while a few others enjoy privilege. We are indignant about the squabbling and lack of vision of Europe's leaders, who only seem to care about getting re-elected. They refuse to do anything that might rub voters the wrong way, however reasonable the required decisions may be. A 27-headed hydra like the EU can have its whims, as illustrated entertainingly by Finland and Slovakia. But mostly it is just an absurd, hulking, hollow beast that balks when it has to make a move. We are indignant, too, about the incompetence of the bureaucrats in Brussels who failed to lift a finger while graft took hold in Greece and who continued instead to pay fat subsidies for non-existent farms.

We are indignant about the stand-off in the US between a president equally bent on re-election, who advocates additional spending to create jobs with a budget deficit near 10% of GDP, and a majority Republican opposition that opposes any rise in taxes. God has spoken to the Republicans, forbidding them from reforming America's indulgent tax regime. The Grand Old Party is so dogmatic that it has called for Bernanke's head after the Fed chairman dared to point out the need to raise taxes to reduce the deficit. The choice for a Republican candidate to run against President Obama next year currently pits a Mormon against an Evangelist, rather than focusing on pragmatic ways to rein in the US Treasury's galloping debt.

We are indignant at seeing how, two or three years after the Kerviel story, a young trader with four years' experience was able to create over CHF 10 billion of fictitious ETF positions and end up losing more than two and a half billion for UBS, a bank that prides itself on its risk control system. Watch out for ETFs.

Finally, we are indignant at seeing how incompetent and rabid management turned Dexia, a combination of two fine banks, Crédit local de France and Crédit communal de Belgique, into a monstrosity with €20 billion of Greek bonds in



Pressure on Europe



5

Indignant!



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its portfolio. Why would anyone, starting with two institutions that specialised in lending to local governments, pile into all kinds of new segments with no customers? And as if that weren't enough, why would anyone create derivatives for municipalities that end up bringing them to ruin by costing them 20% interest? Unfathomable.

With as many spills as thrills on this financial roller-coaster, confidence is gradually evaporating. Meanwhile the developed economies are barely moving and the emerging ones are flagging owing to weakness in their main export markets and tight credit conditions designed to fight inflation at home.

Yet it is difficult to foresee a run-of-the-mill recession taking hold in the US. Almost no-one in the economy is going overboard. Consumers, playing it safe, are saving more. Construction now accounts for a tiny (and incompressible) 3% of GDP, compared with a historical average of 10%. Capital investment has slowed sharply. The same pattern can be observed in Europe where governments play a greater role. So on the face of it severe slumps on either side of the Atlantic are unlikely, unless confidence collapses. We are

tuned to rumours and to the conflicting statements of ministers, government leaders, bank managers and moguls of finance and economics like George Soros and Nouriel Roubini. Until a solution to the banking crisis is found, confidence will remain shaky at best.

In early September we advised staying focused on gold and shares in large multinational companies that pay high dividends. Those recommendations are still valid as ways to weather the storm. For those who want yield, the discounted bonds of Europe's best insurance companies now offer a comfortable return.

PS: We have just come back from a trip to Canada and were pleasantly surprised to find a country in such fine financial shape, with full employment (incidentally requiring more immigration), low inflation, a strong currency, a healthy property market and what have you. An isle of prosperity in a sea of troubles. Why, you ask? For a simple reason: Canada's banking charter, like Australia's (both modelled on the British one), bars off-balance sheet liabilities and financing vehicles. The big Canadian banks have kept their AA ratings and the country is thriving—an ideal situation.

Time for politicians to stop looking for scapegoats

FRÉDÉRIC BINGGELI

The developed world is struggling to break out of a vicious circle. Living beyond their means has become the main problem of European governments. When the euro was created, the Continent did away with the borrower of last resort, i.e. with the central banks of sovereign states with a sovereign currency. Of course those currencies tanked when the governments concerned ran up large deficits, but the sovereign debt was paid back—admittedly in a depreciated currency but without defaulting (we are referring here to developed Europe). Requiring the euro zone members to comply with the Maastricht rules, it was believed, would provide enough convergence to ensure stability. The mistake was in accepting the lies, cheating and skewed national accounting. Companies, including banks, have to comply with strict accounting standards. Governments tried to put themselves above all that, and everybody knows what happened. Plenty of blame can be laid at the doorstep of politicians. By pledging benefits that they know full well they won't be able to deliver once in office, they buy people's votes (and thus engage in a form of clientelism). They spend their entire term worrying about getting re-elected and don't do a lick of work for the common good. They are like parents who promise their children extravagances while knowing that they already cannot make ends meet. Living in a world far removed from everyday cares and having no notion of how to budget since all their expenses are paid, they behave like mythomaniacs. Yet a

government is like a household: it may have more possibilities but it also has its limits, which though much greater still exist. And once they have been reached, either there is a collision or drastic steps have to be taken to avoid one. The inevitable result is a poorer country.

We will stick to the situation of Europe here, since that is our focus. It is saddening to hear what the EU politicians say. They would have their good citizens believe that the billions they need to balance their budgets are stashed away in banks. But banks are part of the system like everything else. The junk bonds of tottering states were issued by those same states, weren't they? Don't conclude from that that I defend the banking sector indiscriminately. In some ways it is a disaster, with mathematicians modelling risk that they have no practical knowledge of and with chains of command that lack a full understanding of the positions taken by traders or even of the products the bank sells. My views on politicians and banks run parallel when I think of Dexia, a hopeless case encapsulated in one of its business lines—selling fixed-income products denominated in Swiss francs to French municipalities that raise taxes in euros. Naturally it all backfired, since instead of maximising potential profit such formulas ended up maximising the so-called experts' incompetence. Dexia now has to be recapitalised by the Belgian government, though where the money will come from is anyone's guess.

One could argue that Dexia exemplifies yet again how banks are the source of all evil. Well it does not, because in life we all have our bit to play. It is the authorities' duty to provide a framework, to limit, prohibit or permit while bearing in mind the common good. It is the job of bankers, as businesspeople, to exploit the framework that they are given with a view to surviving in the face of competition. In exchange they pay high corporate and income taxes that ought to ensure a properly functioning state, which isn't the case in most countries nowadays.

It is high time Europe found new leaders like the visionary ones of the post-war era. A pan-European borrowing facility could only be set up by simultaneously integrating politically. In other words the EU would have to create a supranational body to oversee its members' public finances and budgets, i.e. their income and expenditure. Whether

Sarkozy has his hands full...



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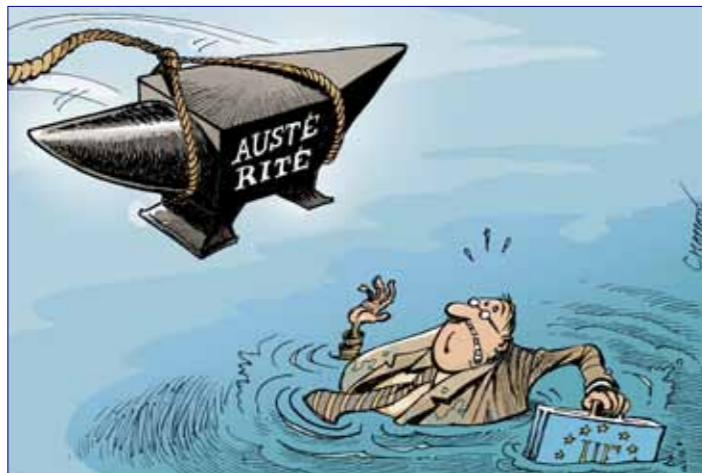


such a body starts with a small or a large number of countries is a procedural issue. At present Europe is buying time to avert an implosion of its financial system, which through payment transactions includes not only banks but also manufacturers and service providers of all kinds.

People often think that banks should be allowed to fail because, otherwise, taxpayers' money would have to be used to bail them out. The truth is quite the opposite. The authorities rush to the rescue of banks by printing money because, if they didn't, the whole population with its checking accounts, savings, pension funds and tax revenues (deposited in banks) would be swept away as if by a tsunami. Some would have us turn the clock back to avoid having to make such a choice. Do they really want to go back to barter or to the stone age, with all its trappings including high infant mortality?

There is an urgent need for citizens to search their souls and conscience before casting a ballot. We should think about our future, about what past generations have endured to bring us where we are now and about what sort of devastated landscape we will leave to the coming generations.

Europe going under...



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What we can do is make an effort so that there will indeed be a future. It is not by finding scapegoats that our problems will be solved. The past has shown us what extremes that can lead to and still not provide any solution. Politicians should do their job

as responsible men and women. And when they err, let the people democratically mete out retribution. Unrealistic policies, such as spending money that one does not have, should be debunked.

So how does Switzerland figure in all this? As an independent country in the heart of Europe, we are as real territorially as we are economically. Our franc is strong, ay ay too strong at present, but wouldn't a weak currency be a bigger shortcoming? Given our multilingual heritage, we have adopted English almost as a fifth national language. We have sound finances and a propensity for saving and moderation on a par with our neighbours' propensity to spend. Finally our political system, with its separation of powers at the municipal, cantonal and federal levels, means things can never get very far out of hand. Problems remain a manageable size. Politicians normally have to keep their ear to the ground. Only in Switzerland's two largest cities is the political class a bit disconnected from everyday realities. Struggling to make ends meet is unfamiliar to them, but as long as they are counterbalanced by countryside opinion we can stay on an even keel.

Is that an overly optimistic view? At all events it is how outsiders see us. We on the inside have the impression that our politicians and regulators at times ride roughshod over us and overstep their powers. Being out of touch, they take decisions that could cause considerable damage in terms of lost jobs and competitiveness in entire sectors. As guardians of the general interest our government should naturally defend Swiss manufacturers. But it should be standing up for the financial industry as well. We need a regulatory environment that is not only realistic but also provides scope for a constructive view on the future. It isn't a crime to inspire international confidence or to attract savings from around the world. Nor should it be wrong to develop expertise in wealth management or to overcome

the fiscal and regulatory obstacles that prevent our investment funds from being global players. With so many jobs at stake, it is important that Switzerland's government and market regulator be aware that we are counting on them. It would be unfitting to fall, in this area too, into the trendy trap of looking for scapegoats.

Debt makes the world go round

THANASSIS GONTIKAS

If anybody rewrote Liza Minnelli's most famous song these days, they would probably call it "Debt, debt" instead of "Money, money". Oh, yes—whether we like it or not, the global economy is all about debt.

Think about it for a second. Credit cards, leasing, mortgages, small or large project financing, even pension funds (as future payment obligations)—everything around us is debt. Government debt, consumer debt, corporate debt, institutional debt, debt that straddles our generation well into the next one...

When debt is used for productive and value-adding purposes, then the economy does fine. It grows and is able to repay what is owed. But if the debt is used to repay other debts or to fund non-productive projects, then its value diminishes and repayment becomes almost impossible. This is largely what is happening today on a global scale: debt is used to pay down debt. It's like a merry-go-round, with new players jumping on from time to time but with nobody jumping off. The contraption just keeps getting bigger and going around faster than anyone could have guessed. We are all so far in debt that every new-born child owes several thousand dollars when it takes its first breath.

And then of course comes the billion dollar question: is there a right amount of debt and, if so, how much? In the private sector I think the answer is simple. As long as a company can service its debt and still have enough money left over to continue operating profitably, then it will be alright. The problems really start when we try to apply this at the government level. Budget deficits are all too common these days; few countries run a surplus, and for those that do it is usually fuelled by royalties on abundant natural resources or by emerging growth.

Obviously there are exceptions, but let's focus on the rule. The US, France, Germany, Japan and the UK, to cite a few of the biggest names, are all running annual shortfalls with no sign of being able to balance their accounts in the next few years. So we know for sure that debt is here to stay. It could also be argued that, in the end, if everybody is issuing debt then it can't be so bad after all! But this



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again begs the question of what the right amount should be. Japan doesn't really show that it cares: it just keeps running up more debt and nobody blinks an eye. The US raised its debt ceiling this summer and will probably jack it up higher in the coming years. Meanwhile the EU is struggling to maintain some absurd rules on annual deficits and debt-to-GDP ratios. But those rules were grossly violated by its biggest members, paving the way for the undisciplined ones to really exaggerate and throw the ratios out of all proportion. They have been proved unrealistic and useless by political

If everybody is issuing debt then it can't be so bad after all!

necessity and economic reality, with no central decision-making process to control who gets what. They actually aggravate today's problems, making it impossible to apply them in the near future.

Why can't we have more than a 3% annual deficit? Why would it be so bad if the EU accepted a debt-to-GDP ratio exceeding 103% or 105% for a period of ten or more years? Technically speaking, these levels are well thought out and calculated



on the basis of averages during phases of healthy, steady economic growth. And that is exactly the point. When you run into periods of poor, choppy economic growth, if any, these rules should not apply and governments should be allowed above all to provide stimulus and protect the welfare of their citizens. Such is the approach to debt on the other side of the Atlantic. The US authorities are constantly creating mountains of debt in order to jump-start their economy and bring consumption back up to previous levels. Later on they will probably create some inflation to ...deflate their debt. Let's be clear about this: we should adamantly oppose bad budget practices and the kind of system abuse that we have seen in many cases. But to enforce unsustainable rules in an economic environment that simply cannot afford them is both difficult and dangerous.

As long as a country's debt is directly linked to the average citizen's standard of living, any government will have serious problems reducing it and, if it does so, will probably not survive beyond the next election. We have already seen this in Portugal and Spain, and I am afraid that many more examples are on the waiting list. Debt v. social unrest and/or stability is a very dangerous equation, especially in democratic societies where too much pressure is sure to result in a change of government. For any incumbent government it is a fine line balancing harsh debt-reduction measures against an electoral defeat, and that line is easily crossed. The EU's situation is a good illustration of this. Voters will react if they are asked to offer their tax euros to provide massive support to other indebted countries that do not appear to be pulling their weight. Likewise, voters in problematic countries will overthrow governments that try to adopt stringent fiscal policies on short notice. Fiscal discipline is a virtue that needs time to be vested and cannot change from one year to the next. It must be applied in a measure that proves effective against debt creation but is also socially acceptable.

The biggest risk facing Europe is not higher interest rates or debt; it is massive social unrest. The sooner the EU adopts a common fiscal policy for all its member states, the sooner we will be able to find effective, long-term ways to address the issue of debt. Debt pooling and a joint central policy are the only solutions for a truly united Europe that will be free from the spectre of debt, as well as from the spectre of social unrest and everything that goes with it. The sooner we understand this, the better off we will be in dealing with the problem. This requires a political solution and not just an economic one. EFSF, Eurobonds and a one-off wealth tax are likely ways to tame the European debt problem. But now we need to move fast.

Debt will continue to make the world go round and very much so. Imagine if debt were to freeze at some point in time. The bulk of economic activity would stop, trade would come to a standstill and debt securities would disappear from the financial markets. There would be total chaos. Throughout the history of Western societies, debt and credit have always been abundant. Actually that is what made capitalism succeed and allowed free economies to thrive and emerge as the leading system at the end of the 20th century.

Coming back to the question of what the right level of debt should be, I don't think there is a "right" one. What is enough in periods of strong growth and wealth creation is clearly little in recessionary periods. The Maastricht rules proved this point beyond a doubt. Actually the level of debt per se has nothing to do with fiscal discipline. I am a strong believer in very tight fiscal management, but at the same time I cannot see modern society reducing its level of debt at a fast pace. Countries that currently have huge debt burdens will have to shrink them to a sustainable size or face bankruptcy. This will have to be done at a much slower pace than we currently expect, and the way will be long and full of hurdles.



Beware a banking tsunami following the earthquake that has struck European finance

PHILIPPE LEDERREY

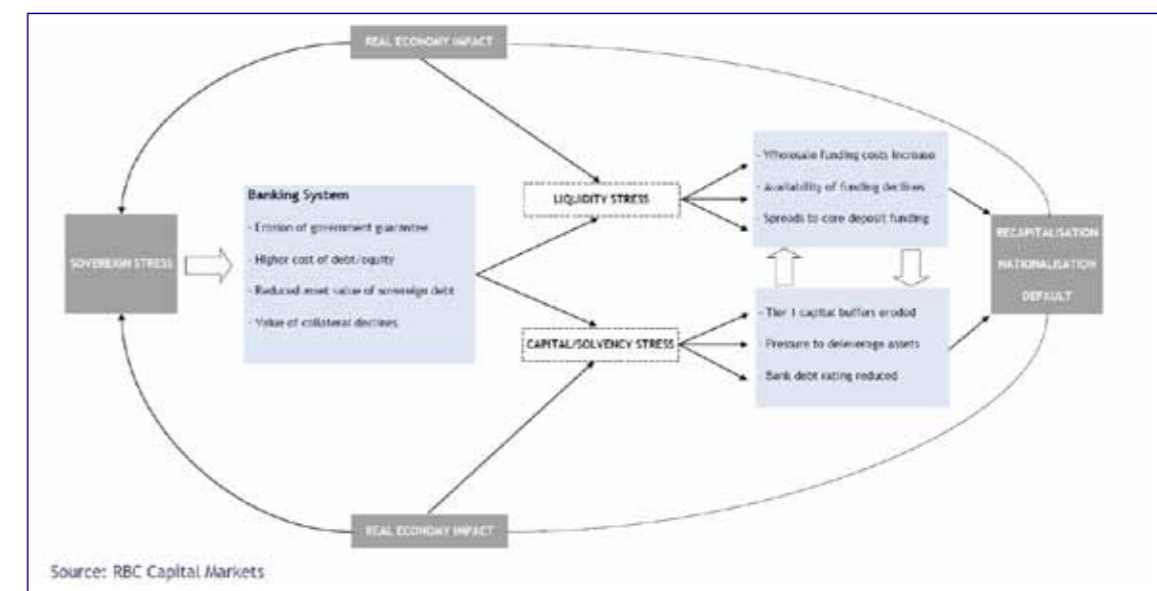
European banks caught in a vicious circle

Over the past eighteen months, eurozone decision-makers have certainly taken numerous decisions in an effort to resolve the crippling financial crisis. They have, for example, eased monetary conditions, changed banking regulations, imposed stress tests, and provided massive liquidity via the European Central Bank to those banks unable to tap the capital markets. These measures have unfortunately been unable to keep up with events. The leaders' inability to push through any real concrete measures has

given rise to a dangerous, self-feeding loop composed of sovereign risk and bank weakness and all their negative consequences on the real economy. As time goes by it becomes increasingly difficult to break out of this vicious circle. What is required at this stage is a credible resolution that will address all the problems simultaneously. And banks (some driven to the edge of bankruptcy in the wake of the subprime crisis) are unfortunately the weakest link in this fearsome chain.



The vicious circle between sovereign debt, banks and the real economy.



No miracle solution for banks in the short term

Developments since the end of July suggest that, in the absence of a workable solution to the financial quagmire in Greece, contagion to all the links deemed weak will accelerate. Even if the crisis can be effectively contained in the next few weeks – primarily a political challenge – European countries will still have to get their budgets in order and carry out structural reforms. In short, measures that will be necessarily painful for already wobbly economies. And banks will need to significantly reduce their balance sheets, which will unavoidably decrease potential revenues. This could well lead to a credit crunch.

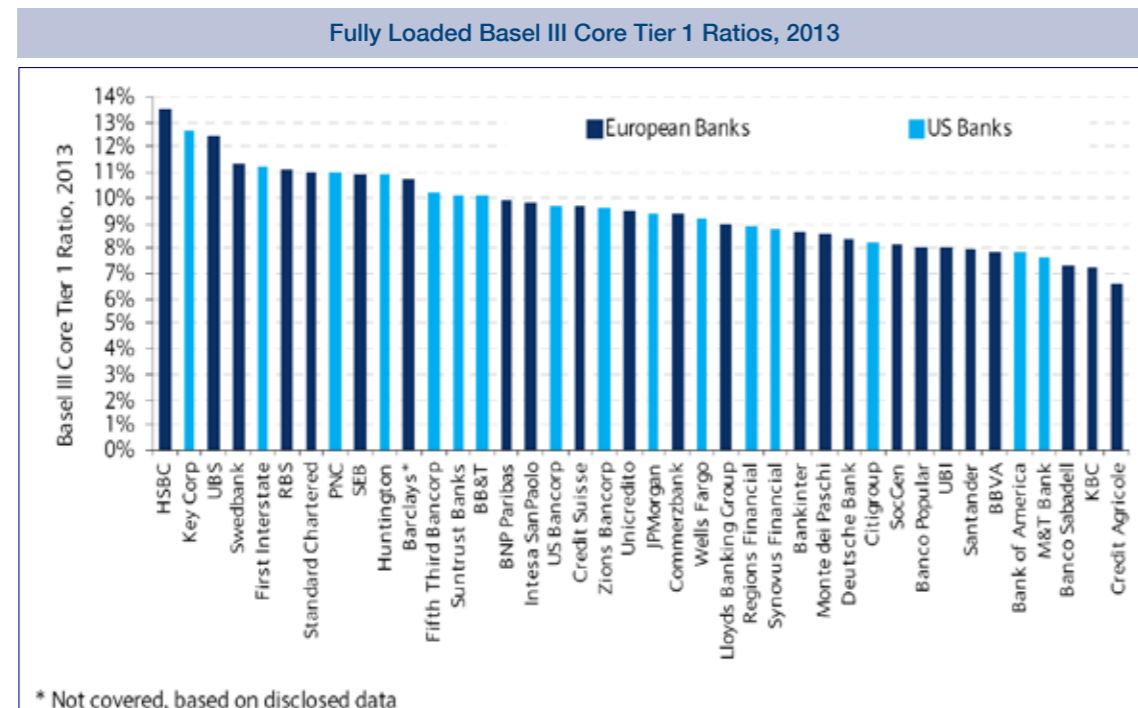
Do banks really need to recapitalise?

Based on the approach commonly used in Europe – which, under IFRS standards, weights assets as a function of their degree of risk – European banks’ solvency ratios are no worse off than those of American banks (leaving accounting technicalities aside). So recapitalisation may not really be necessary. The approach used in the USA leads to much lower ratios (because assets are not risk-weighted and are simply added, a mortgage loan to a creditworthy customer has the same weighting as a highly toxic derivative). But it would be incorrect to compare them. US banks employ the concept

of netting when booking assets or financial commitments (especially for derivatives), and their balance sheets are therefore much leaner than those of banks that use the principle of gross value. Deutsche Bank, for example, estimated that assets on its balance sheet that were worth € 1.5 trillion at the end of 2009 would have only been worth € 891 billion if the bank used the netting mechanism under GAAP standards.

Banks have little exposure to toxic sovereign debt, but that’s not the real problem

European banks have little exposure to the sovereign debt of the weakest countries (the PIIGS): for the entire sector, it amounts to around 1-2% of the core Tier 1 ratio. But focusing only on debt exposure is overly simplistic: Credit Agricole’s exposure to Greek debt, which is only a half billion euros, rises to nearly 25 billion euros if we include credit commitments to its Greek subsidiary (Emporiki). As was true during the subprime crisis – subprimes represented only a few percent of total assets – the main risk has to do with the contagion effect of this exposure: first the larger PIIGS (especially Italy), then contagion of the real economy itself, followed by a long-lasting economic slowdown that could weigh on the creditworthiness of customers and, finally, exposure to small businesses or individual customers crippled by a recession.



Is the problem related to capital levels? No, it's a liquidity problem!

Banks’ room for manoeuvre has definitely improved thanks to the liquidity made available by the ECB, but the system is under a nearly untenable level of stress. Any further capital required in this sector must at this point be considered the last recourse to allow banks to get the required liquidity and obtain financing (in order to carry out the traditional transformational role of the banking system). In other words, banks will first have to prove their solvency before being able to count on other forms of funding. At issue is thus not whether the implied losses on the PIIGS’ sovereign debt will be realised, but rather the need to ensure that European banks have enough capital to absorb potential major losses. The dismantling of Dexia demonstrates the low correlation between solvency and access to liquidity: the bank is well capitalised with a core Tier 1 ratio of 10.4%, but its deposits are far too low relative to loans.

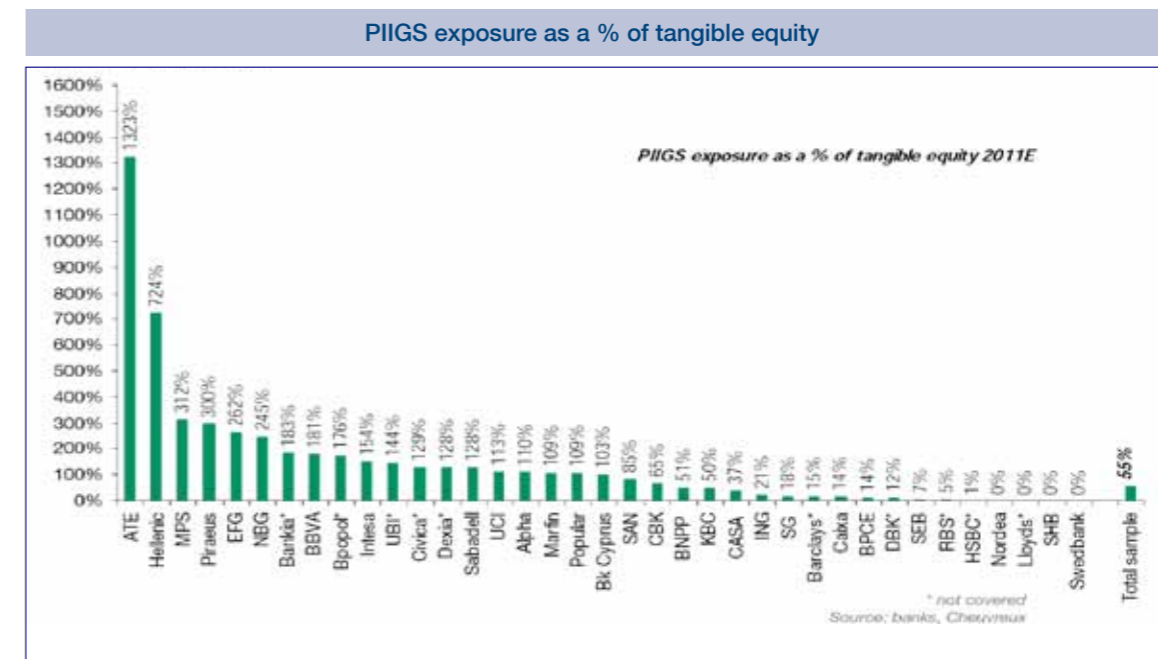
A “hard” restructuring of sovereign debts would cost several hundred billion euros

From an analytical perspective, even a very thorough restructuring of Greek debt would lead to manageable losses that would not have a

systemic impact on the sector (apart from Greek banks of course). Even assuming the sovereign debt of the other PIIGS were restructured (at a level equivalent to that of their CDSs), the theoretical loss would be around 250 billion euros (for the 91 banks included in the last stress test, i.e. excluding Swiss banks). Still, if there were a real systemic risk (which would be caused most likely by a disorderly Greek default or by some form of dislocation of the eurozone), the capital losses alone for these banks would amount to around 1.5 trillion euros. If we also take into account banks’ exposure to the resulting side effects on the economy, that figure would be doubled (at least). The necessary provisions would be too much for the banking system to bear.

In the financial sector we prefer insurers

We still feel that solid insurance companies can represent a less risky alternative than banks while also offering greater upside. The multiples are similar despite very different risk levels: no massive dilution following a capital increase, no chance of governments taking a stake in the capital, no drastic reduction in balance sheets following the forced reduction in leverage, potential additional taxes much lower, fewer regulatory risks, and so on. In addition, the life insurance sector would benefit if its top-quality bond exposure were to rise.



Indeed, when sovereign-risk fears ease, insurers' bond holdings (in this case massed in German bonds) pick up. That would also help ease fears about the return deficit on policies' long-term guarantees (on average 3% on existing business and 2.25% on new business).

The valuation of most European banking stocks defies logic: many of them are trading on only half of their (pre-dilution) book value. Volatility is extreme, however: even one of the safest bets in continental Europe is down more than 30% this year but has rebounded nearly 50% from its low in September – this is more akin to gambling than investing.

As long as the nature of the risks remains so asymmetric and credible political decisions (as opposed to the vague intentions we have seen so far) are not made, we feel that banks in the eurozone represent an overly risky asset class.



Economic forecasts

GDP growth and contributions to global expansion (BPER estimates)

Country	GDP 2010	GDP 2011 BPER Estimates	GDP 2012 BPER Estimates	Country weights	Contribution 2011
United States	2.8%	1.5%	2.2%	23.1%	0.51%
Canada (IMF estimates)	3.2%	2.1%	1.9%	2.5%	0.05%
Euro Area	1.8%	1.4%	0.0%	19.3%	0.00%
United Kingdom	1.4%	0.6%	-0.1%	3.6%	0.00%
Switzerland	2.7%	1.7%	0.2%	0.8%	0.00%
Russia	4.0%	4.7%	4.5%	2.3%	0.11%
Japan	3.9%	-0.5%	2.0%	8.7%	0.17%
China	10.3%	9.0%	8.0%	9.3%	0.75%
India	10.1%	7.5%	7.0%	2.7%	0.19%
Brazil	7.5%	3.5%	4.0%	3.3%	0.13%
Mexico	5.5%	4.0%	3.5%	1.6%	0.06%
Others (IMF estimates)	6.8%	6.8%	6.3%	22.6%	1.41%
WORLD	4.7%	3.5%	3.4%	100%	3.4%

Comments

- The GDP growth rates shown above are final for 2010. Projections for 2011 and 2012.
- Each country's weighting has been translated into US dollars and is based on the principle of purchasing power parity, which takes account of differences in prices and standards of living.
- The countries are ranked by the size of their economy, in decreasing order.
- Contributions to global growth are calculated as follows: the GDP growth of each country is multiplied by its size, with the total adjusted to the aggregate weighting of the countries listed. The sum of the contributions works out to 3.4%, a good estimate of global GDP growth for the current year.

Banque Privée Edmond de Rothschild SA issues a counter-proposal to the Swiss Federal Council's draft revision of the Collective Investment Schemes Act (CISA).

CISA recast by a practitioner

ALEXANDRE COL

The repercussions of the 2008 financial crisis could have a significant impact on Switzerland's investment funds industry.

Some people would find other topics more exciting, but I must admit that I have a passion for CISA. My ardour is at once intellectual and patriotic, the latter because this act provides a perfect illustration of how dependent we are in Switzerland on our ability to export. If we want to continue managing investment funds on European territory (a business that comes down to exporting our expertise in financial management), then under the EU's new Alternative Investment Fund Managers Directive (AIFMD) we will have to ensure that all fund managers operating in Switzerland are made subject to CISA by 2013.

For many years everyone in the Swiss financial industry knew that we were chafing under *lex americana*. Now we are about to submit to *lex europensis* as well. Globalisation, of which European integration is as much a consequence as a cause, has resulted in a balance of power that threatens to crush yet another realm of our treasured independence.

The Federal Council has therefore diligently undertaken a revision of CISA, and the draft bill has been submitted to the umbrella organisations of the financial industry for consultation until 7 October.

By definition, this type of process is defensive and reactionary. The Federal Council is urgently seeking to defend a sector of our economy and is merely reacting to the threat posed by AIFMD. Instead we should be taking advantage of this needed revision to make far-reaching changes to the law, based on the lessons learned from the 2008 crisis. Moreover, the revised CISA that the Federal Council is now trying to ram through will increase the number of constraints to which the funds industry is subject. In mathematics there are necessary and sufficient conditions; this two-pronged approach, while perhaps necessary, is far from sufficient. Offence is the best defence. We would like to see a much more thorough revision of CISA.

The first reason for this is that CISA in its present form has clearly failed. Let's take just one example: SICAVs (investment funds with a legal personality). Scope for their implementation was supposedly the main innovation of CISA, and yet only five or six SICAVs have been set up in Switzerland since the act came into force in 2007. Luxembourg introduced Specialised Investment Funds (SIFs) at the same time, and now there are hundreds of these. How can we contemplate continuing to function with such a law? By making it more restrictive on the one hand and adding a whole raft of European legislation to it on the other?

The funds market in Switzerland is a strange beast

Secondly, the draft revision does not take our competitors into account. Europe (which chiefly means Luxembourg and Ireland) has two laws governing funds: one covering UCITS (traditional funds) and one covering AIFs (vehicles such as hedge funds with more sophisticated structures and strategies). We have only CISA. Moreover, our European neighbours have been able to create three large families of funds: UCITS, funds incorporated under Part II of the Luxembourg law on UCITS, and SIFs. In Switzerland we have only two categories: "funds" and "other funds". How can we hold our own against such competition if our one and only law is unable to cope with the complexities that be?

Thirdly, the funds market in Switzerland is a strange beast. It combines the features of the inward-looking French market and the wide-open Luxembourg market with its appendage of particular and by no means insignificant traits, one being a very large foreign clientele with accounts held on Swiss territory. But unlike Luxembourg, whose national market is tiny in comparison with the number of foreign participants, Switzerland has a sizeable domestic investment community.

In this it resembles France, but unlike our much larger neighbour we manage numerous funds abroad so we have a far broader reach. And despite the threats to banking secrecy, our country manages very large sums on behalf of foreigners who come to us with the expectation of finding a globally oriented legal framework. Such clients, who could be from anywhere and whose assets are managed in Switzerland, will not accept an investment funds act that binds our country in a Eurocentric straitjacket.

Finally, we need a more thoroughgoing revision because Switzerland unwittingly strangled the development of Swiss funds by, among other things, maintaining some of the provisions of IFA (the act that preceded CISA) for longer than was reasonable. As a consequence most of the funds sold in Switzerland and managed by Swiss entities are incorporated abroad.

How can we avoid dealing a new blow to one of Switzerland's key export industries, i.e. finance, if we cling to the monolithic CISA? How can we boost our financial sector if we are happy with a defensive attitude? We should take the offensive by innovating. We should recapture the domestic funds market by promoting the creation of funds

under Swiss law. In a word, we should be patriotic.

But as I said at the beginning of this article, for me CISA is also an intellectual passion. The act has to take account of the extremely complex weave of our fund markets and foreign investors. It has to integrate EU requirements, protect Swiss investors and help us recover our domestic market. This can be done by fostering the development of Swiss-incorporated SICAVs, without hampering access to foreign investment funds. Revising CISA is an opportunity to ponder what specificities Switzerland has to offer in a world where we can no longer isolate ourselves as we have done in the past. Above all, though, the new act must resolve a contradiction that is very characteristic of Switzerland: we are a small country as measured by our domestic market and yet a large one in terms of our role in the global economy – especially in areas like finance.

We therefore call for a flexible, carefully crafted and sophisticated law. That is what prompted us to draft a full counter-proposal as our intellectual and patriotic contribution to this endeavour. Let's hope that it will inform and inspire the coming debate in parliament. ■



Tactical allocation (%)

CHF PORTFOLIO

Asset class	Switz.	Europe	UK	USA	Japan	Asia/other emerging regions	Commod.	Precious metals	Sundry or global	Total
Short-term	4									4
Fixed income	19	2								21
Equities	10	2		2	2	6				22
Directional hedge funds		5								5
Nondirectional hedge funds	25									25
Property	6								7	13
Commodities, Precious metals							0	10		10
Total	64	9	0	2	2	6	0	10	7	100

EUR PORTFOLIO

Asset class	Switz.	Europe	UK	USA	Japan	Asia/other emerging regions	Commod.	Precious metals	Sundry or global	Total
Short-term		10								10
Fixed income		19							2	21
Equities	6	7		2	2	5				22
Directional hedge funds		5								5
Nondirectional hedge funds		25								25
Property									7	7
Commodities, Precious metals								10		10
Total	6	66	0	2	2	5	0	10	9	100

USD PORTFOLIO

Asset class	Switz.	Europe	UK	USA	Japan	Asia/other emerging regions	Commod.	Precious metals	Sundry or global	Total
Short-term				10						10
Fixed income				21						21
Equities	6	2		8	2	4				22
Directional hedge funds				5						5
Nondirectional hedge funds				25						25
Property									7	7
Commodities, Precious metals								10		10
Total	6	2	0	69	2	4	0	10	7	100

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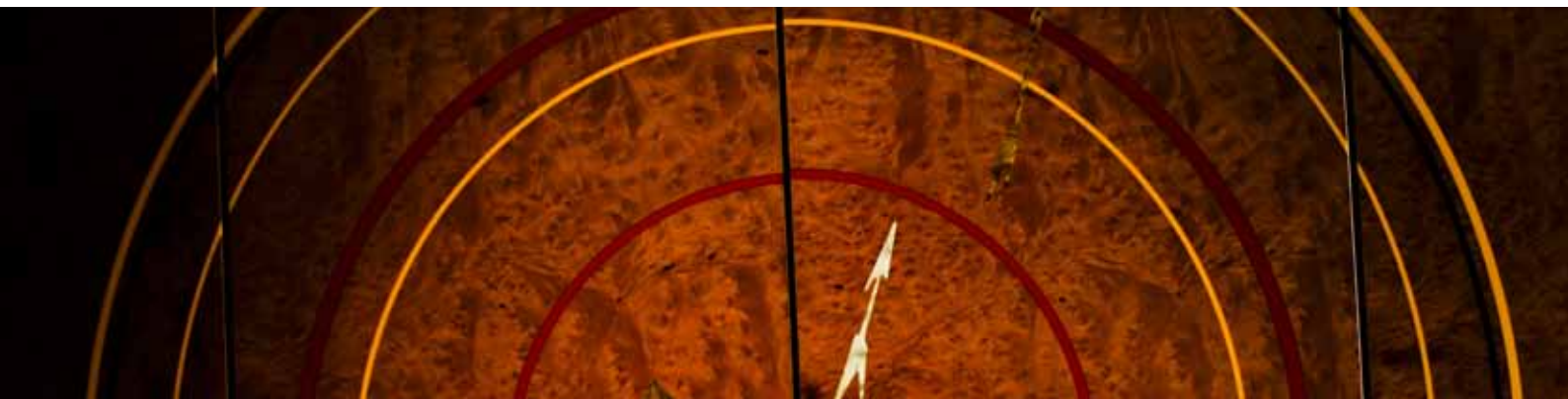
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