

- ▼ EU: Non-euro country presides Council
- ▼ Gov't bonds: China and Japan buy euro debt
- ▼ Long-term: Energy and water are trends

part

partners' view

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|-----------------|------------------|---------------|---------------|-------------|--------------|--------------|----------------|-------------------|------------------|-------------------|-------------------|
| January
1/11 | February
2/11 | March
3/11 | April
4/11 | May
5/11 | June
6/11 | July
7/11 | August
8/11 | September
9/11 | October
10/11 | November
11/11 | December
12/11 |
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Politics and business

US labor market gains momentum.

Cyclical expenditures rise. Non-euro nation assumes EU Council presidency.

At 2.2 percent, inflation in the Eurozone climbed to the highest level since October 2008 (see chart). This is not necessarily the outcome of a flourishing economy but is based on the effect of a weak currency. In some instances, imported goods from outside Euroland, such as commodities, became much more expensive because of the anemic euro. The flip side of a weak currency is increased exports because in the customers' currencies (yen, Swiss franc, US dollar, etc.), goods become cheaper. As the classic world champion in exports, Germany is one of the main beneficiaries of this equation. Additionally, the heterogeneous composition of the eurozone makes it difficult to pursue a fiscal and monetary policy in the interest of the entire Union.

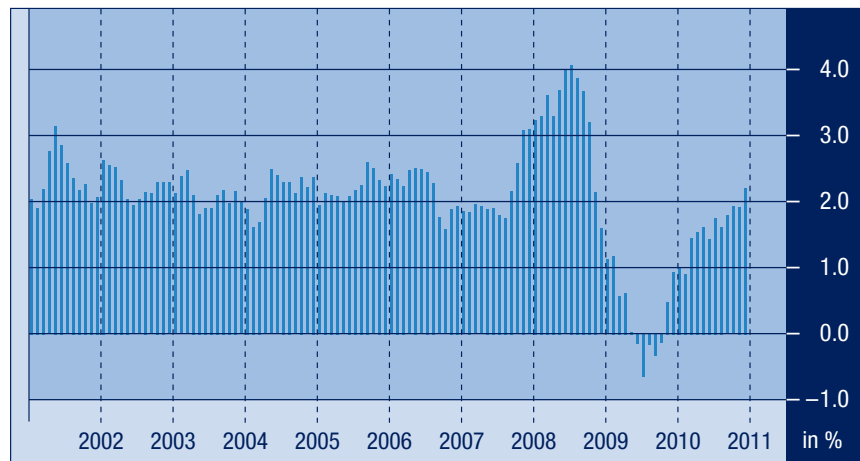
Convincing US metrics

Economic data from the USA remains surprising in the positive sense. Core unemployment, for example, fell from 9.8 to 9.4 percent, the lowest value since May 2009. Even cyclical consumer spending, with car sales at the front lines, looks good. The ISM Manufacturing Index (purchasing managers index) climbed to 57.0 points, the highest level in seven months.

Hungary presides over EU

Effective January 1, 2011, Hungary started its half-year tenure as the presiding entity of the EU Council. Thus, in year 1 after the beginning of the big euro crisis (Greece, Ireland),

Eurozone inflation in % YoY



Source: Eurostat

a country that hasn't even introduced the euro (and for the time being will not be eligible to do so) stands at the helm of the European Union. In half a year, Hungary will pass the baton on to Poland and in early 2012, Denmark will take the wheel... neither is a euro country. They will be followed in six-month intervals by Cyprus, Ireland, Lithuania, and Greece. It is hard to imagine that this function is anything beyond a prestige post and might actually have some impact. After all, agenda-setting is ultimately the prerogative of the "strong" countries like Germany and France.

The full time president of the EU, Herman Van Rompuy, flamboyantly praised the Hungarian government on the occasion of his official visit, although a highly controversial media law was ratified on the same day. While Van Rompuy politely overlooked this circumstance, EU

member nations were quick to criticize the law as censorship and a violation of freedom of the press, urging Hungary to respect EU standards. The sore lack of coordination in this particular issue is yet another impressive demonstration of the political incoherence of the European Community. Apart from the disputable media law, Hungary's "crisis tax" and the nationalization of private pension funds are also causing irritation and disbelief within the European Union. In fact, the EU Commission must now investigate if the new tax is commensurate with EU law or whether it might even discriminate against major European corporations.

Currencies and interest rates

China seeks alternatives to US dollar for foreign exchange reserves. Successful auctions held in Spain and Portugal for bond floats.

Just before the end of the year, the Norwegian krone finally started its long-awaited appreciation versus the euro and the Swiss franc. Within a short period of time, it gained six percent versus the single currency (see graph). The Norwegian currency is likely to profit from further uncertainties in Europe, even though the euro briefly gained momentum when short positions were closed (see further below).

Good news ...

In January, the euro generated good news and bad news. Apart from China's financial involvement in Greece, Spain is the beneficiary of a Chinese liquidity injection as well. Additionally, Japan also wants to pitch in and help solve the euro debt crisis now. For this purpose, Nippon is participating in the next placement of euro-denominated government bonds. In return, apart from very attractive interest rates, Japan now also has the option of swapping its overvalued yen against euro. This is a double blessing for Japan's economy. For one thing, it helps stop the euro's weakness and second, it cushions the crisis in a major market (Eurozone). China's motivations are similar, with the added side-effect that it can diversify its predominantly dollar-denominated foreign currency reserves of currently 2,850,000,000,000 (2.85 trillion) US dollars. The management of China's forex reserves that originate from trade balance surpluses could also have an influence on

interest rates in the USA, because although China is America's largest lender with over 900 billion US dollars worth of US government bonds, Beijing is actively looking for diversification options outside the dollar arena.

... and bad news

On the negative euro news pages, we certainly have the speculations regarding Portugal's financial problems and the potential vulnerabilities of Spain. One of the downsides of the euro – the financial weakness of the southern periphery – is that it has also triggered enormously strong countermovements versus the US dollar and the Swiss franc. Because the government bond auctions in Portugal, Italy, and Spain were very successful (thanks to China and Japan), and the debt service of the new

bonds turned out to be lower than expected, many short positions were closed down. This resulted in a fast and furious reaction that is rarely observed on the currency markets. According to the US Treasury, the USA's official debt ceiling of 14.3 trillion US dollars will be reached in the next three months. If Congress, with its Republican majority, fails to endorse an increase, it will become difficult to finance public-sector spending (wages, investments, etc.).

Norwegian krone versus euro



Financial markets

Equities remain in the limelight in 2011. Recognizing long-term megatrends helps investors make profitable choices.

For investors, it is interesting to know where the masses are moving and which assumptions are behind their decisions. If projections turn out to be false, favored investments will automatically be exposed to considerable contractions. Customarily, large financial institutions publish their lists of favorites and their estimates around year-end. In a nutshell: bonds, especially government bonds, are out. Asia (India, China, Indonesia) is the global economy's growth engine. Shares are favorably valued relative to solid earnings growth. Both the euro and the US dollar remain under pressure.

Megatrends

Investors who recognize and ride a long-term trend stand a good chance of earning money on the capital markets. The global technology trend (Internet, PCs) and mobility are examples from the past in which early trend-riding paid off. The dominant themes of the coming years are water, food, and energy. Water was nicknamed "blue gold" because of its increasing scarcity combined with population growth. In July 2010, the UN declared that availability of clean water was a human right. Companies in the water value chain include Geberit (water efficiency), Georg Fischer (piping), or Veolia and RWE (processing and distribution).

Less agricultural land

The world's population growth also has an impact on food production. Additionally, popula-

tions are spreading, turning arable land into industrial or residential zones. The increasing demand for staples (rice, wheat, corn) must be addressed with continually shrinking agricultural plots. The value chain includes companies such as Caterpillar (machines), Syngenta (seeds, herbicides), Kali & Salz (fertilizer), or Nestlé (production and distribution). "Energy production" as mentioned in the last issue of partners' view is also a long-term theme. The clean and continuous production of electricity will require huge investments, resulting in substantial revenues and profits for the leading providers in this industry. China's five-year plan went into effect on January 1, 2011, releasing government investments in the magnitude of 1500 billion US dollars in key sectors such as renewable energy and information technologies. China is not alone, because when Barack Obama was elected President, the USA also embarked on a new era with respect to environmental pollution control. Obama received unexpected support when the oil disaster occurred in the Gulf of Mexico. This value chain includes automakers (Toyota) as well as solar and wind technology and energy generation (ABB, Siemens).

Last but not least

"Everything is different this time – the five most expensive words on the stock market."

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