KRAEMER, SCHWAB & CO. AG

Investment Management

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"In bull markets, people have faith; in bear markets, doubt. The other way around might be more profitable." *James Grant*

Investors around the world anxiously wonder how deep the present crisis will develop. At first it looked like a localised correction in one area of financial markets, i.e. US real estate, which had undergone excessive speculation for some time. But the crisis has grown deeper and deeper in a crescendo of staggering losses, financial failures and bankruptcies, up to the present point where some financial markets no longer function; widespread fear and distrust reign so that the ultimate lenders, the Central Banks, have had to provide liquidity repeatedly to avoid collapses. This is very likely one of the worst crisis since the depression. And we don't know how much worse it will get or how long it will last. Such circumstances spread scare, fear and panic among investors. Financial markets have crashed, exerting additional pressure and anxiousness on unsettled participants.

How does a thoughtful investor react to these changed circumstances; how does he behave in a bear market? The most important rule is: don't let the market infect you with fear and panic; stand firm against pessimism and don't succumb to the feeling of doom. We are not leveraged, we don't have to act since we don't need the money soon and therefore we should simply disregard ridiculous price swings. Even the best investors like Buffett can't really predict markets, only boasters can do it. Masters too have bought into weak markets and temporarily suffered big losses. Their strength is that they know when prices are low and they build up positions when everybody else is going into cash to preserve his capital. In addition they are very patient and perseverant. As long as their companies, in which they have invested, do well, they don't mind living with losses on paper and they don't waver even under extreme market pressure.

In the last century there has been one bear market, which has tested investors to the ultimate extent and which is always somehow in our minds: the Great Depression. Then and now the cause of the crash was leverage, over-betting with borrowed funds, which requires a huge unwinding and deleveraging. However, Governments and Central Banks have reacted quite differently in 1929 versus 2007. In the last century they introduced austerity measures; all public authorities tried to reduce deficits and to limit international trade and finance. This led to a disastrous collapse and widespread unemployment. Today Governments and Central Banks are relentlessly working to bring liquidity back into markets and to keep credit available, despite the general insecurity, mistrust and suspicion. De-leveraging the financial system will take time and lead to huge losses, there is no doubt. General irresponsibility, carelessness and brashness have led to unbelievable excesses, which come to light now.

The correction will be painful and take time. Nevertheless, it would be a grave mistake in our opinion to succumb to doom now. Economic history and the study of crashes show, that eventually economic activity picks up again and resumes growth; along with it markets will recover. As Bernard Baruch, a veteran of the Great Depression wrote: "Bears don't own houses on Park Avenue." Fear creates opportunities; this is a great time for good purchases. We are staying with high quality companies and this will help us in tough times.

The crisis is also a reminder that excessive expectations and greed lead to losses. This time around it is the financial sector, which has sinned the most against the law of moderation and now has to bear the brunt of the losses. We hope the companies involved have been taught a lesson, which they will take to heart and will hopefully follow sounder business principles in the future.

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