

GENERAL INVESTMENT CLIMATE

The Economy

The financial market turbulence and the fear of a recession in the US persisted during the second quarter of 2008. The American house market continued to deteriorate both in terms of prices and volumes. The number of new homes has fallen by 54% since the top of the market in the second half of 2008; also the sales of existing homes continue to decrease. Currently, 6.4% of mortgage borrowers are in arrears for more than a month, half of which are past due for more than three months. The number of foreclosures has more than doubled since the second quarter of 2007.

The American industry is still performing reasonably well, mostly due to increasing exports thanks to the low dollar. The decrease in order intake and increasing inventory levels, however, do not bode well for the future. Capacity utilization is also decreasing. The labour market continues to weaken: since the beginning of the year, there has been a net loss 564 000 jobs in the private sector. The final GDP growth figure for the first quarter was revised upward to 1%, predominantly caused by the consumer who continues to spend money despite his very low level of confidence. The index of consumer confidence of the University of Michigan has dropped to its lowest level since the oil crisis in the seventies. Analysts are also expecting a consumption-driven GDP growth in the second and third quarter. During the second quarter, all American taxpayers have received a cheque from the government. The total size of this gift from the government to the consumers is \$115 billion.

The fear of an economic slowdown is also increasing in Europe. This is clearly noticeable in the German sentiment driven indices ZEW (investors) and IFO (producers). Both indices increased unexpectedly during the first months of the year, but declined sharply in the second quarter. French sentiment indicators are down as well. In general, retail sales were disappointing in Europe, but this is partly caused by the lower number of working days. German unemployment stays at an extremely low level, but the number of outstanding vacancies has started to decrease. German industrial production was more or less constant at its high level compared to the same period last year.

In the UK, house prices continue to drop and the industry does not appear to taking advantage of the cheap pound. In Japan, there are strong signals of a slowdown: both industrial production and consumption have decreased in recent months. The Chinese economy on the contrary is still booming. While growth was originally mainly export-driven, the internal demand is becoming increasingly important. In May, domestic Chinese consumption has 22% higher compared to May 2007.

Commodity and energy prices were important themes in the market during the second quarter. Oil prices soared by 40% from \$100 per barrel at the end of the first quarter to \$140 at the end of the second quarter.

Money markets and exchange rates

During the first quarter of 2008, the American central bank intervened heavily in the money market. This slowed down in the second quarter with only one interest rate change. The benchmark rate was lowered from 2.25% to 2% at the end of April. The Fed continued to capture the attention of the markets, which was expecting further rate decreases down to 1.50%. The central bankers signalled however that the cut in

April would be the last of the series because the high energy prices are pushing up inflation. In May, producer prices increased by 7.2% compared to the same month last year. Considering these inflationary pressures, the expected date of the first rate increase has been brought forward. Currently, the market is already pricing in a first 25 basis point increase in September or October.

In Europe, consumer price inflation was 4% (year on year) in June while producer prices increased by 7.1%. In Belgium consumer prices were even up by 6%. The European Central Bank has repeatedly stressed that is very unhappy with this high level of inflation. On the 3rd of July, the ECB announced a “symbolic” 25 basis point rate increase from 4% to 4.25%. It is only a symbolic increase, because the ECB understands that it can not fight this oil price driven inflation with interest rate hikes. The central bank primarily wants to give the signal that it will do everything to prevent a wage-price spiral.

The short-term (3 month) interest rates in the US have increased by 9 basis points to 2.72%, while the European 3-month rate increased by 22 basis points to 4.95%. The spread between the European and the American rates thereby remains above 2%. Long-term rates increased both in the US and in Europe. In the US, the 10 year interest rate increased to 4.28% compared to 3.71% at the end of March. The European 10 year rate increased from 4.03% to 4.65%.

During the entire quarter, the dollar traded within the 1.5400 – 1.6000 trading range. Both levels have been tested several times, but have not been broken.

Stock Markets

After a strong drop in share prices during the first quarter of the year, the second quarter started with a general recovery of the stock markets. The AEX recovered from 442 at the end of March to 495 mid May. During the second half of the quarter, the index started declining again. On June 30th, the AEX closed the quarter at 425.93, down 3.7%. The DAX performed slightly better with a loss of only 1.8% because of the relatively good performance of the utilities.

Table 1.1 - General

	30/jun/08	31/mrt/08 - 3 mth	31/dec/07 - 6 mth	30/sep/07 - 9 mth	30/jun/07 - 12 mth
AEX	425,93	-3,73%	-17,42%	-21,27%	-22,31%
BEL20	3168,22	-14,82%	-23,24%	-26,75%	-31,71%
DAX	6418,32	-1,79%	-20,44%	-18,36%	-19,84%
EU50	3352,81	-7,59%	-23,79%	-23,48%	-25,32%
DJ	11350,00	-7,44%	-14,44%	-18,32%	-15,35%
SP500	1280	-3,23%	-12,83%	-16,16%	-14,86%
Nasdaq	2292,98	0,61%	-13,55%	-15,12%	-11,92%
EUR/USD	1,5755	-0,21%	7,98%	10,43%	16,34%
EUR 3 maanden	4,9470	0,2200	0,2630	0,1550	0,7720
EUR 10 jaar	4,8110	0,6880	0,4040	0,3920	0,2040

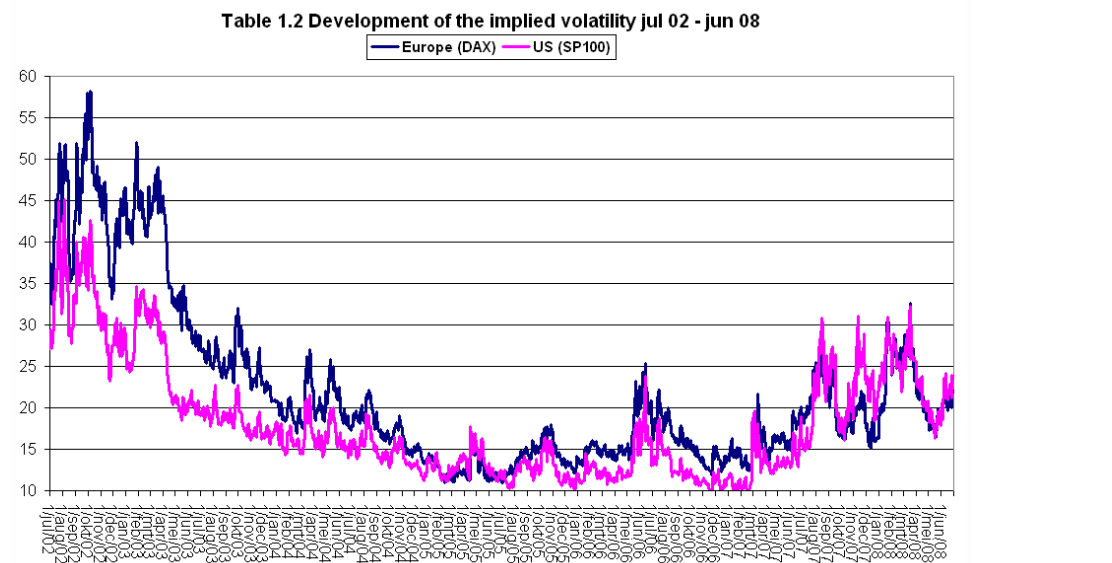
The small- and midcap indices also closed the quarter in red figures, with the exception of the MDAX which increased by 2.8%. This increase is however exclusively due to the

performance of the largest share in the index, K+S. The SDAX decreased by 5.5%, the AMX by 6.9% and the ASCX by 8.4%.

De American exchanges performed in line with the European markets. The Dow Jones declined by 7.4% and the S&P 500 by 3.2% while the Nasdaq went 0.6% higher. The BEL20 dropped 14.8% due to the high weighting of the financial sector in this index.

Implied volatility

The volatility of the stock market was very high at the end of the first quarter following the near-bankruptcy of Bear Stearns. After a brief recovery, the volatility increased again, but not to the same levels seen at the beginning of the year.



Long-term development

During the recovery in the first half of the second quarter, the 200-day trend line of the AEX was tested from below, but not broken. Subsequently, the AEX started a new decline. Because of the strong decline in share prices and unchanged or improved results, a number of companies have been very cheap.

