

THEMA

Which sustainable alternative to develop ?



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Social responsibility and sustainable development are foremost among today's most serious concerns.

It seems only natural to assess manufacturing companies from these two standpoints in such fields as agriculture or industry, environment or energy. However, they become less relevant in analysing financial institutions.

Yet social responsibility and sustainable development have taken on considerable importance in each section of today's society, and the financial community cannot ignore them. One by one, it has taken to heart each of the major issues involved.

Investment products specialised in business sectors and companies that comply with these criteria now form part of the investments offered by any financial institution.

But some financial institutions have gone further still, incorporating these criteria into their own corporate governance and the way they function internally. They examine each financial project for its risks to society and the environment.

Innovest, a social and environmental rating agency, awarded its AAA rating to the Crédit Agricole Group in 2007 for incorporating social responsibility and sustainable development criteria in all its business lines and entities. In addition, the banking sector's leading magazine, *The Banker*, named the Group "Bank of the Year".

While the Group's approach and its progress have been recognised, we should view these events as encouragement to go further in the same direction.



All set for a sluggish summer?

Following the property slump and credit crisis, the market's fears have now turned towards inflation,

which is being driven up by the soaring oil price. This factor has further overshadowed an already very bleak macroeconomic scenario :

- first, through its negative impact on companies' margins, whose historically high levels appear increasingly unsustainable against the backdrop of a widespread slowdown and higher costs ;
- next, by paralysing the central banks, whose room for manoeuvre is now severely hampered ;
- lastly, by further penalising consumers, who are already under intense pressure and are having to contend with tougher conditions in the labour market as well as a negative wealth effect on their property assets.

Keeping a very close watch on the inflationary risk

In the US, the idea of a V-shaped scenario has been completely abandoned, the question now being whether or not the US economy will manage to avoid sinking into recession. Admittedly, with intervention rates at 2%, the Federal Reserve has conducted a highly expansionary policy and a plan to stimulate growth via tax incentives has been put in place. Nevertheless, it is difficult to see how these measures could offer lasting benefits for the property market, this being the very origin of the crisis. Given the latest figures on housing starts (at their lowest level in more than 15 years) and the vacancy rate (rising), this sector seems to be sinking into recession. The most recent manufacturing output statistics, which showed a decline, further darken

the picture. On top of all this comes the impact of the soaring oil price over which the US central bank is unable to exert any real influence.

While inflation is a threat in the US, in Europe it is making the economic headlines. In May, it reached a record level of 3.6%, still fuelled by oil and food prices (stripping out these two components, inflation remains below the 2% mark). Economic prospects are weakening. Germany's business sentiment index fell sharply in June and consumption, a major growth engine, is sluggish in most countries. There is now a risk that the Eurozone could slide into recession as well as the UK, where the pick-up in inflation (3.3% in May) is now preventing the Bank of England from pursuing its policy of a monetary easing.

V, W, U, and L scenarios. A language full of imagery...

When a sharp economic decline (or even a recession) is followed by a rapid and sustainable rebound, economists talk about a V scenario. If this rebound is followed by a fresh decline, it becomes a W scenario while a less rapid rebound will make for a U scenario. If there is no rebound at all, then the economic scenario will take the shape of a letter L.

The ECB's more aggressive rhetoric in terms of inflationary risks has further boosted the euro against the dollar. Due to these inflationary fears, bond yields are continuing to rise on both sides of the Atlantic. Lastly, the equity markets have plummeted again and are now back at their mid-March levels, while all macroeconomic indicators are in the red. A sombre mood is setting in as we move into the summer period ...



Asian inflation moving at two speeds

The weak inflation which has prevailed over the past fifteen years was the result of the world economy's increasing globalisation, rapid expansion in trade and high productivity gains. Now a new era appears to be getting under way, marked by rising inflation, growing protectionism and more moderate productivity gains. The inflationary threat is from steadily rising commodity prices, most of all for oil and food. Asia is set to take this shock head on. Whereas the cost of energy and food accounts for 25 % of household spending in the US and the EMU, this ratio is more than doubled in South East Asian countries.

Inflationary pressures started appearing in mid-2007 in Asia, before picking up alarming speed at the start of this year. As frequently happens, the first alarm was sounded in China. Between 1997 and mid-2007, average inflation in China kept below 4 %, but it suddenly spiralled to an 8.7 % high in February. Inflation exceeded 7 % in the Asian region in April for the first time in ten years, and cuts in fuel subsidies suggest that this rise is not over.

Asian inflation is moving ahead at two speeds. Inflation appears to have peaked in China, which forecasts a level of 5 % at the end of 2008. Of this surge in inflation, 80 % is from a spike in food prices, almost exclusively in the price of pork. The country's pork shortage is due to cyclical factors (bluetongue disease and severe winter storms in 2007) as well as structural factors (chronic underinvestment because of depressed prices), but which are currently being resolved. Energy is not a significant factor in Chinese household spending, accounting for less than 5 %, and no signs have yet appeared of inflation pushing up wages or the prices of manufactured goods

and services. Beijing considers the situation under control and has the tax resources needed to continue its policy of subsidising food and fuels.

Share of the food budget in household spending

Africa – Middle East	45 %
Asia	44 %
Eastern Europe	35 %
South America	29 %
Developed countries	15 %

Source: US Dept of Agriculture (USDA)

In other South East Asian countries, however, inflation is clearly on the rise, fuelled by the structure of household spending. Food accounts for 47 % and 57 % of the respective price indices in the Philippines and India, where the weight of energy products is twice as high as in China. More worrying still, inflation is spreading fast to many products in some countries, such as the Philippines.

Highly sensitive to inflation, the People's Bank of China has taken a proactive stance. It will not raise interest rates, however, except as a last resort, preferring such measures as increasing reserve requirements for banks. Were it to raise its target rates, an already appreciating renminbi would be pushed up higher than intended, attracting still more "hot money". Instead, Beijing's aim is to curb the country's abun-

dant liquidity. In the rest of South East Asia, central banks are still playing a waiting game. The spectre of inflation brings back painful memories, frightening the money markets, and currencies are coming under pressure. Huge government subsidies weigh heavily on government coffers. Consumers are now raging as these subsidies are being cut. Yet acting rapidly and decisively looks like the only way out, since the entire system could seize up very quickly, jeopardising the area's macroeconomic stability.

Evolution of Thai rice price



Source: Bloomberg

panorama

Asset Allocation of Crédit Agricole Luxembourg as of 30/06/2008

Bond Investment

Given the rather sluggish outlook for the second half, we had increased our bond positions during May, taking advantage of the rebound in long rates caused by inflation expectations. However, this increase was modest, particularly for sovereign bonds, as they still offered lower yields than cash lines. In June, we maintained these positions without increasing them any further. In the short term, pressures on the yield curves cannot be ruled out with central bankers alluding to monetary tightening. Over the medium term, however, the bond markets could come back into favour with investors as growth reaches its low point. With this in mind, we are more positive on EUR long rates than USD long rates. Current equity market volatility calls for prudence in the convertible bond market, in which we have reduced our portfolio holdings. Likewise for corporate and high-yield issues.

Equity Investment

All manner of ills seem to be afflicting the equity markets. The sharp rise in interest rates in May reduced the equity markets' appeal. These markets were also penalised by the general downward trend in revisions to earnings forecasts. However, these revisions did not affect all sectors in the same manner, with earnings revised downwards for financial stocks and upwards for energy and staple goods. Valuation levels are also historically low overall but will probably improve given that profit margins remain high and are most likely unsustainable. Our view on these markets is negative over the short to medium term, particularly as regards Europe. Our positions are focussed more on the US, traditionally more defensive, and Asia, especially Japan (which seems to be emerging at last from a long period of deflation). Overall, our portfolios are under-invested in the equity markets.

Alternative & Currency Investment

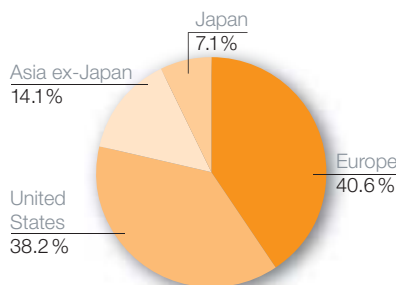
The high volatility in the equity markets and renewed risk aversion are boosting the appeal of alternative investments. We have increased the alternative investment holdings in our portfolios, especially as the risk of a systemic crisis seems to have been ruled out. At the same time, we have extended the range of strategies in which we are invested. We are continuing to hedge our USD positions against the EUR at 25% and our GBP positions against the EUR at 100%.

Asset Allocation

	Prudent	Balanced	Growth
Equities	7.5%	24.9%	43.0%
Bonds	42.3%	30.3%	16.8%
Alternative	19.8%	17.7%	11.3%
Monetary Funds	20.6%	15.9%	22.8%
Cash	9.8%	11.2%	6.1%
Total	100.0%	100.0%	100.0%

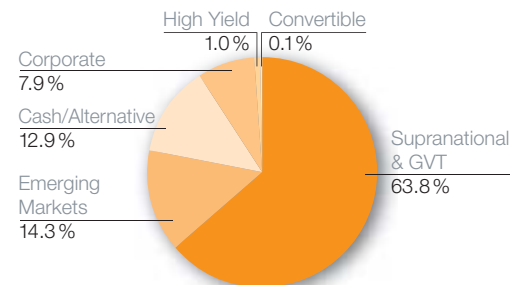
Equity Portfolio

Geographical breakdown



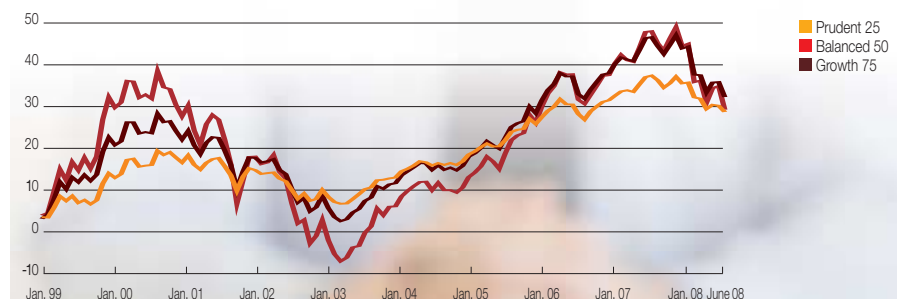
Bond Portfolio

Breakdown by product type



Performance as of 30 June 2008

Performances euro	YTD 2008	2007	2006	2005	2004	2003	2002	2001	2000
Prudent 25	-5.20%	2.40%	2.84%	8.28%	4.19%	5.80%	-5.70%	-1.58%	2.32%
Balanced 50	-8.36%	2.98%	4.73%	12.96%	4.69%	7.57%	-10.36%	-3.67%	-0.39%
Growth 75	-10.93%	3.32%	5.56%	16.80%	5.33%	10.94%	-17.23%	-7.65%	-3.49%



Performance as of 30 June 2008

CRÉDIT AGRICOLE LUXEMBOURG

Managed Fund Portfolio Best Select (MFP) EUR	Currency	NAV	YTD%	1 year %	5 years %
PRUDENT 25	EUR	-	-2.50	-3.98	n.a.
BALANCED 50	EUR	-	-6.22	-10.12	n.a.
GROWTH 75	EUR	-	-9.22	-15.70	n.a.
DYNAMIC 100	EUR	-	-11.98	-20.03	n.a.
Managed Fund Portfolio Robeco (MFP) EUR					
PRUDENT 25	EUR	-	-4.07	-6.40	n.a.
BALANCED 50	EUR	-	-6.95	-11.29	n.a.
GROWTH 75	EUR	-	-10.31	-16.72	n.a.
DYNAMIC 100	EUR	-	-13.21	-21.29	n.a.
Managed Fund Portfolio Best Select (MFP) USD					
PRUDENT 25	USD	-	-2.05	-1.38	n.a.
BALANCED 50	USD	-	-5.42	n.a.	n.a.
GROWTH 75	USD	-	-8.41	n.a.	n.a.
DYNAMIC 100	USD	-	-9.86	n.a.	n.a.

CREDIT AGRICOLE LUXEMBOURG FUNDS

Money Market and Short Term Funds					
Lion Intergestion - Monétaire Euro -P-	EUR	1238.49	1.97	3.87	12.07
International Multi-Manager Court Terme Dynamique	EUR	1064.24	-2.64	-2.94	n.a.
Asset Allocation Funds					
LIS Income - SRI	EUR	1146.43	-1.16	-0.29	6.01
LIS Prudent - SRI	EUR	1132.04	-4.82	-6.53	10.96
LIS Balanced - SRI	EUR	1056.42	-8.42	-11.47	14.76
LIS Growth - SRI	EUR	966.70	-11.32	-15.08	21.67
LIS Dynamic - SRI	EUR	778.66	-15.30	-19.57	24.72
Multi-Manager Funds					
International Multi-Manager 50	EUR	1325.47	-6.46	-6.92	28.36
International Multi-Manager 75	EUR	1345.31	-9.26	-9.80	34.17
International Multi-Manager 100	EUR	1334.04	-12.47	-13.73	38.99

FUNDS SELECTED LIST

Money Markets						
EUR	CAAM Funds Euro Reserve	EUR	12.00	2.04	3.90	11.52
USD	CAAM Interinvest Short Term USD	USD	112.29	1.33	3.55	n.a.
	CAAM Funds US Dollar Reserve -C-	USD	11.94	1.36	3.65	14.04
Fixed Income						
GLOBAL	CAAM Obligations Internationales	EUR	101.36	-2.86	-9.12	n.a.
	CAAM Funds Global Bond	USD	18.65	1.75	7.74	33.98
	Rorento	EUR	42.90	-1.58	0.16	8.94
EUROPE	CAAM Obligations 1-3 Euro	EUR	21495.00	-0.53	1.51	9.31
	CAAM Cr�dit 1-3 Euro	EUR	22845.07	-0.32	0.23	10.68
	CAAM Oblig Etat Euro	EUR	4437.35	-1.35	1.61	10.42
	Morgan Stanley European Curr H/Y Bond Fund	EUR	11.62	-3.73	-6.29	27.27
EMERGING DEBT	JPMF Emerging Markets Bond Fund	USD	281.15	-0.10	2.37	65.81
CONVERTIBLES	Morgan Stanley Global Convertible Bond Fund	EUR	32.95	-6.95	-6.05	24.81
ABSOLUTE RETURN	CAAM Invest VaR2 EUR	EUR	1068.55	1.27	1.15	n.a.
Equities						
GLOBAL	Fidelity Funds World	EUR	10.57	-15.98	-20.17	47.17
	JPMF Europe Small Cap Fund	EUR	13.13	-17.00	-30.82	n.a.
EUROPE	Oyster European Opportunities	EUR	288.38	-17.60	-23.47	88.80
	ING (L) Invest Europe High Dividend	EUR	276.17	-21.58	-29.29	n.a.
	Fidelity European Aggressive Growth	EUR	11.49	-6.43	-4.88	n.a.
USA	UBAM Neuberger Berman US Equity	USD	855.55	-5.55	-10.04	86.33
	Fidelity American Growth	USD	10.24	-11.80	-7.66	n.a.
	SGAM US Equities Relative Value	EUR	68.17	-21.07	-35.49	n.a.
ASIA PACIFIC X JAPAN	Aberdeen Global Asia Pacific	USD	52.14	-13.97	-2.54	191.94
	Comgest Magellan	EUR	1315.21	-17.67	-9.56	188.13
EMERGING MARKETS	JPMF Eastern Europe Equity Fund	EUR	23.45	-9.95	3.35	n.a.
	CAAM Funds Latin America Equities	USD	677.47	8.63	25.56	631.45
	Fidelity ASEAN Fund	USD	15.18	-9.91	4.55	n.a.
	SGAM Fund Equities MENA	EUR	98.64	n.a.	n.a.	n.a.
	JAPAN	Axa Rosenberg Japan Equity	JPY	965.02	-8.42	-25.44
Thematic funds						
AGRICULTURE	Parvest Agriculture	EUR	141.31	16.22	41.86	n.a.
WATER	SAM Sustainable Water Fund	EUR	145.42	-15.48	-20.17	73.30
NATURAL RESSOURCES	JPMF Global Natural Resources Fund	EUR	23.03	-4.52	-2.08	n.a.
INFRASTRUCTURE	Clariden Leu Infrastructure Fund H Eur	EUR	115.14	-17.33	-12.96	n.a.
REAL ESTATE	Morgan Stanley Asian Property	USD	15.44	-20.62	-18.65	157.33
BIOTECH	Pictet Fund Biotech HP Eur hedged	EUR	256.97	-0.31	9.36	n.a.

MARKET INDICES

Dow Jones Euro Stoxx 50	EUR	3352.81	-23.79	-25.32	38.57
Dow Jones Industrial Average	USD	11350.01	-14.44	-15.35	26.32
MSCI World CR	USD	1402.13	-11.75	-12.50	60.97
Nikkei 225 CR	JPY	13481.38	-11.93	-25.67	48.42
MSCI EM (Emerging Markets) CR	USD	1087.12	-12.72	2.59	226.77
EFFAS Euro Govt All	EUR	145.84	-0.73	2.74	14.29
JP Morgan United States GBI	USD	424.62	2.25	10.61	21.09
JP Morgan Global GBI	USD	417.67	4.76	16.72	35.36

Capitalisation shares. Sources : Lipper Hindsight, CAL, Bloomberg.

This document is not a prospectus and does not constitute an offer to sell or buy any security, including shares of the funds featured. Shares of these funds are offered on the basis of their respective prospectuses only. The past performance of investments is not necessarily a guide to future returns. Changes in rates of exchange and other factors may cause the value of an investment to go up or down. Additional risk factors are described in the fund prospectuses. The Alternative Investment Funds are invested in "non-traditional" investment funds, whose managers have the flexibility to hold short positions, to invest in non-transferable securities or to use substantial leverage in addition to holding traditional long side investments. Alternative investment funds may also hold illiquid securities which result in difficulties establishing a fund's net asset value.

Investing in alternative asset management and choosing the CAAM Master Alternative fund

The financial crisis linked to property and credit, pressures on consumption and the recent rise in inflation make the market environment unfavourable for traditional asset classes in 2008. This is particularly the case for equities, whose valuations no longer seem to provide reasonable protection against a market downturn. With today's highly volatile markets, investors have increasingly become adverse to risk.

These conditions call for the use of alternative asset management, particularly arbitrage strategies and those involving undervalued securities. Uncertainty

investment opportunity. CAAM Master Alternative's investment managers actively pick alternative funds

A selection of alternative strategies offering the best growth potential over the medium term.

out of a universe of more than 9 500, clearly many more than just those managed by Crédit Agricole Group.

CAAM Master Alternative offers several attractions. It is diversified, invested in both multi- strategy and mono-strategy funds, and its volatility is well under control. In the alternative funds universe, it also stands out for its weekly liquidity.



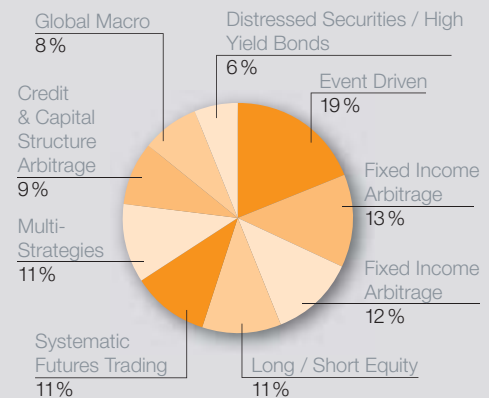
about the size of the economic slowdown should lead to highly dispersed performances on the equity markets, depending on the sectors, geographic areas and market capitalisations concerned. Arbitrage strategies will also take advantage of opportunities in the bond markets. As yield curves steepen in both the US and Europe, rising volatility and widening spreads offer attractive possibilities in the credit market. Forecast rises in the default rate, mainly in the automotive, property and construction sectors, could benefit fund managers holding undervalued securities. In alternative asset management, shrewd strategy selection is every bit as important as in the management of other asset classes.

This makes the **CAAM Master Alternative** fund of funds the right choice for investors seeking an

The management team's first task is to pinpoint the alternative strategies with the greatest potential for medium term growth. The aim is to focus on uncorrelated management techniques, geographic areas and asset classes in order to reduce the portfolio's overall risk. The investment managers then put together a diversified portfolio using a number of strategies, balancing one risk against another. For each of these strategies, the only funds chosen are those able to inspire the managers' genuine conviction. Meanwhile, investments in money-market funds make for better control over risk while ensuring the fund's liquidity.

With its four year investment horizon, CAAM Master Alternative aims at realising an annual performance more than 3% higher than the capitalised Eonia rate.

CAAM Master Alternative - P



Portfolio breakdown as of 31 May 2008



patrimonial

Group and sustainable development, a commitment cited by the social and environmental rating agency Innovest

Innovest awarded its AAA rating to the Group in 2007, in its "global banks" category. This recognition is an encouragement to pursue our efforts to deal with current and future social and environmental issues. Crédit Agricole Group has implemented a policy of social and environmental responsibility for several years.

Each of the Group's entities has adopted this approach. Corporate and investment bank Calyon now factors social and environmental risks into its project financing. Similarly, Crédit Agricole Asset Management is committed to a responsible voting policy at the 2 800 shareholders' meetings it attends each year. The international private banking entities, including Crédit Agricole Luxembourg, offer their clients certified socially responsible investment funds. Last February, in partnership with Professor M. Yunus, 2006 Nobel Peace Prize winner, Crédit Agricole S.A. set up the "Grameen – Crédit Agricole Microfinance Foundation".

Interview with Greg Larkin

senior banking analyst at Innovest, New York



How do you go about analysing a bank ?

First we look at the Innovest ratings of all the companies the bank has helped finance in any way, either through loans or investments, or by acquiring shares. We also look at the impact of the bank's business on low-income populations, i.e. does it make responsible loans? Then comes the hardest part: determining how the banking group as a whole manages environmental and social risks.

What must a bank do to receive an AAA rating ?

Very few banks are able to withstand the pressure of market expectations without sacrificing long-term risk management. Yet this is precisely what we want from them.

Moreover, every employee who has the power to allocate funds to third parties must be able, at his or her level, to incorporate environmental and social risks into decision-making process. We also appreciate banks that are not simply trying to be philanthropic but that they are really looking for ways to draw profit from sustainable development. The banks with AAA ratings are those that have really thought this through, at the highest levels of management, and not just by the communications department.

This year we awarded four global banks our AAA rating, one of which was later downgraded. Indeed, nothing is written in stone: the banks must prove themselves year after year.

Which ESG risks threaten to have the biggest impact on the banking sector ?

Of course, banks will have to think about ways to make responsible loans to low-income/high-risk demographics: we are still in the midst of the subprime crisis. At Innovest, we are also starting to worry about a carbon crisis in the United States, which could affect companies with the biggest carbon emissions. This could also affect banks which finance these companies, through loans and market performances.

But doesn't this also mean new opportunities for banks ?

Absolutely. There is a huge and growing demand for banks to provide their clients with environmental risk management solutions, especially in carbon intensive/sensitive sectors. Furthermore, tighter carbon regulations would fuel greater demand for alternative energy and new carbon management technology. Companies that meet their energy needs while limiting carbon emissions will be a real advantage.

Social and environmental rating agencies

These agencies assess and rate companies' social and environmental responsibility policies on the basis of non financial criteria. Their ratings are based on public documents, specific questionnaires and meetings with executive officers.

Each agency develops a methodology of its own. They meet a demand from private and institutional investors for transparency regarding the ethical purposes of their investments.

The ECB celebrates its tenth birthday



The European Central Bank (ECB) turned ten on 1 June. Back in 1998, this new institution with its head office in Frankfurt replaced the European Monetary Institute, created by the Maastricht treaty to pave the way for a transnational central bank with a common monetary policy.

The ECB's prime task remains price stability. More specifically, it seeks to keep inflation below a threshold of 2 % over the medium term. Second, the ECB has a duty to contribute to the achievement of the Union's economic objectives, namely high employment and sustainable, non-inflationary growth.

Thus the ECB's duties are clearly prioritised. Its US counterpart, the Federal Reserve (the Fed), has three objectives, all of which rank equally: maximum employment, stable prices and moderate interest rates over the long term. This difference has sometimes resulted in the ECB having the reputation of being uncompromising about interest rates compared with the Fed, which is perceived as more pragmatic and quicker to react to changing conditions.

The ECB must be credited though with the introduction of the euro on 1 January 1999, and now the second most important world currency, behind the dollar. In 2007, 25 % of world reserves were denominated in euros compared with 18 % in 1999. The adoption of a single currency de facto did away with currency risk and stimulated intra-European trade, which now accounts for a third of the Eurozone's GDP compared with only a quarter ten years ago. The successive devaluations of the '80s and '90s are no more, and inflation, though the focal point of current worries, is far below its levels in the '70s and '80s, when it sometimes went into double digits.

The ECB has been compared with its US opposite number throughout the past ten years. In terms of communication, whereas the Fed publishes the minutes of its meetings, the ECB gives only a press conference and time for questions, a style which is sometimes deemed excessively laconic. The second, and more important, comparison has to do with its support of economic growth. Statements by the ECB frequently deal only with

inflation, in line with its key assignment. Does this necessarily mean that the ECB pays less attention to growth than the Fed? The European Central Bank likes to argue that stable prices are the best guarantee of high employment and medium term growth. Yet looking back over the past ten years, both central banks have in fact charted fairly similar policies: restrictive until 2001, then more accommodating policies until 2006 followed by a neutral phase. In the past few months, the Fed's repeated cuts in interest rates have once again stood out against the ECB's attachment to the status quo. It is, however, worth noting that the Fed's proactive policy has not prevented the US economy from slowing down sharply, whereas the ECB has not really hurt European growth by keeping its key interest rate at 4 % during one year.

The moment of truth may still be to come. Both central banks are faced with a new economic configuration: strong inflation due to spiralling oil and raw material prices instead of domestic factors. Such external causes give them no real levers with which to act.

news

Withholding tax increased from 15 % to 20 % as of the 1st July 2008

The withholding tax taken by Luxembourg, Austria and Belgium on interest payments made to residents of other Member States has been increased to 20 % since 1st July 2008, in accordance with the European agreement on the taxation of savings.

As of the 1st July 2011, it will be carried to 35%.

Content and Production

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