

IHB File No. FO/1511

<p style="text-align: center;">FINANCE COMMITTEE CIRCULAR LETTER No. 2/2003 4 April 2003</p>

INTERNAL RETIREMENT FUND

Reference: FCCL No. 6/2002 of 20 December 2002

Dear Hydrographer,

As we projected in the reference FCCL above, we have reviewed the current status of the Internal Retirement Fund (IRF) with the Finance Committee Officers at the 2 April 2003 biannual meeting. Unfortunately, we must report that the state of affairs with respect to the IRF continues to deteriorate.

Of greatest and immediate concern is the performance of the investments held by the IRF. As reported in the reference, the unrealized loss incurred by the investments in equities had reached €180,000 by the end of November 2002. This unrealized loss was in addition to the realized loss of nearly €145,000. At the 2 April 2003 review, the total loss had grown to over €415,000 (approximately €150,000 are currently unrealized losses). The last three years represent one of the worst investment climates in recent times. While the investment manager has clearly not performed brilliantly in these difficult conditions, he has been working within the investment strategy negotiated with the IHB in 1999. In this strategy, the IHB maintained about 50% of the IRF in bank accounts and the remainder was provided to the investment manager with a portfolio allocation of 55/25/20 between dynamic/diversified/conservative investments.

Although a pension plan can have a long-term perspective, it is clear to the Directing Committee and the Finance Committee Officers that the investment strategy initiated at the formation of the IRF is grossly inappropriate for its goals. We are now faced with a difficult decision. The Directing Committee and the Finance Committee Officers agree that the IRF should be invested in more conservative instruments. To do so will involve the liquidation of the current holdings in equities and the realization of the €50,000 loss. To not take this action, continues to place the IRF at the mercy of an uncertain investment climate. The Directing Committee has advised the investment manager to cease all transactions until further notice. We intend to begin the liquidation of the equity positions by the end of April 2003 and invest the proceeds in bonds and cash instruments. **We urgently request your comments no later than 30 April 2003 regarding this course of action.**

Two independent actuarial studies revealed that the IRF was underestimated by approximately €160,000. This increase in the corpus of the IRF to achieve a self-sustaining pension plan was largely due to a reduced rate of return assumed over the life of the fund. As the two studies were in basic agreement, we believe it prudent to seek this level of funding for the IRF. Since the population served by the IRF is not statistically significant we are taking measures to internally conduct yearly actuarial studies to maintain a close scrutiny of the IRF status. We also intend to verify these results with an independent, external actuarial study every five years or when significant changes occur.

The cumulative result of the investment losses and the updated actuarial study is an IRF under-funded by nearly €450,000. There are sufficient funds to meet all obligations for the foreseeable future but over the next few years the self-sustainability of the IRF must be reestablished. The currently approved five-year budget allows for the payment of pensions from the operating funds of the IHO. This action, in and of itself, reduces the draw down of the IRF, provides the opportunity for the recapitalization of the IRF through its investment interest and may be sufficient to return the IRF to self-sustainability over the next four years. In the interim, the IRF can be guaranteed, as it was in the past, through the working capital of the IHB. The Directing Committee proposes this initial course of action together with continued monitoring of the IRF status. We will provide updates as significant information is available and in conjunction with the next biannual meeting of the Finance Committee Officers scheduled for 25 November 2003.

On behalf of the Directing Committee
Yours sincerely,

(original signed)

Vice Admiral Alexandros MARATOS
President