

Market Comment

Issued on 16th February 2004

Overview

Investors took heart last week from Federal Reserve Chairman, Alan Greenspan's, Report to Congress on the US economy and pushed bond and equity markets further ahead.

The G7 meeting of leading industrial nations ended last weekend with little market impact. The press release from the meeting warned against excessive volatility in exchange rates (European view of recent €/£ strength) but also said that more exchange rate flexibility was desirable (aimed at the Chinese currency peg).

Mr. Greenspan stated on Wednesday that the economy was recovering well but "with inflation very low and substantial slack in the economy, the Federal Reserve can be patient in removing its current policy accommodation". While he sounded a warning note on slack fiscal policy, investors responded well to the benign scenario of a strengthening economy and continued low interest rates and pushed markets ahead. Some profit-taking occurred towards the end of the week as US economic statistics showed an unexpectedly sharp fall in consumer confidence and a significant widening in the trade deficit in December.

Movements in the main markets since last week's comment			
Market	Index	% Return 06/02/2004 to 13/02/2004	
		Local Currency	Euro
US	S&P 500	0.3	0.1
US	NASDAQ	-0.5	-0.7
Europe	FT/S&P Europe Ex. UK	0.8	0.8
Ireland	ISEQ	-1.2	-1.2
UK	FTSE 100	0.2	2.0
Japan	Topix	1.2	1.0
Hong Kong	Hang Seng	3.2	3.1
Australia	S&P/ASX 200	1.9	4.2
Bonds	Merrill Lynch Euro over 5 year	0.4	0.4

Equities

Optimism on Mr. Greenspan's benign statement kept the S&P 500 slightly positive on the week, although the Nasdaq Index was down, reflecting the more demanding level of valuations in the technology sector. Merger and acquisition activity also sustained market momentum as communications giant Comcast announced a \$45.6bn hostile bid for Walt Disney & Co. and there was anticipation of a \$35 billion bid by Vodafone for AT&T, the third biggest US mobile phone company. Disney rose 14% on the announcement of the news on Wednesday, while AT&T gained 1.8% on the week.

In Europe, the banking sector was boosted by strong results from UBS, the largest Swiss bank. The French bank, Societe Generale, reported better than expected earnings late in the week, but the share price failed to benefit. Mining stocks were boosted by rising metals prices and economic optimism and the UK company, BHP Billiton, gained 6.8% on the week. Also in the UK, British Airways gained 8% on strong earnings and following European Commission approval for a merger between Air France and the Dutch airline KLM, which is expected to encourage further consolidation in the sector.

The strongest advances of the week were on Far East markets. Japan recovered some of the previous week's losses as banking stocks rose on prospects of a strengthening economy. Exporters were marked down, however, as the weakening dollar is expected to hit sales. The Hong Kong market gained from strong earnings from the fashion retailer, Esprit, and general economic optimism. Australia was supported by buoyancy in resource stocks and a rising Australian dollar.

Bonds

The prospect that US interest rates would remain low for the foreseeable future boosted bond markets. Eurozone bonds were further supported by expectations that the euro's gains will be sustained, despite ongoing verbal "intervention" by the ECB, indicating unease with recent sharp movements in the currency.

Outlook

- The global economy, led by the US, continues to display strong momentum.
- Investors have begun to anticipate the turn (upwards) in the US and Eurozone interest rate cycle, although the strength of the euro may keep the ECB on hold for longer. The Fed is using low inflation as justification for maintaining US interest rates at their current ultra-low levels.
- This environment is one in which bonds should remain less favoured than equities, despite the relatively supportive inflationary background currently being experienced.
- The economic picture remains a more positive one for equity markets, although valuations are once more an issue in certain markets and sectors. Historically, equity markets have continued to be supported even in the initial stages of tighter monetary policy.
- Our current stance is overweight equities and neutral bonds versus the manager average. The funds continue to be overweight Asia due to more

attractive valuations and better economic growth potential. The funds are also overweight Europe on valuation grounds. The funds have overweight sectoral positions in financials and general industrials.

© Copyright 2004 Eagle Star Life, Eagle Star House, Frascati Road, Blackrock, Co. Dublin.

Eagle Star Life Assurance Company of Ireland Limited is regulated by the Irish Financial Services Regulatory Authority.