



In this, our first investment news bulletin of the new year, we are taking the opportunity to look back at 2004 as a whole. We would also like to wish all of our readers a very happy and prosperous new year.

## Global Overview

- Global equity markets experienced further solid gains in 2004, consolidating and building on those achieved in 2003. The economic background provided strong support for equities, a vigorous economic expansion in the US and Far East, accompanied by a rather more luke-warm version in Europe, helping to produce strong growth in corporate earnings. Inflation remaining largely under control also helped, this despite sharply rising oil prices, driven by terrorism fears as well as supply/demand concerns. The price of oil rose to \$55 per barrel during the latter half of the year, before easing towards year-end. There was quite a wide dispersion in returns on equity markets during the year with Ireland, Australia and Asia (ex Japan) performing particularly well. Returns on a number of markets, while strongly positive in local currency terms, were more modest when converted back into euros.
- An underlying theme during the year was the long anticipated turn in US monetary policy. Interest rates remained at the historically low level of 1% until mid-year, when the Federal Reserve moved them upward by 0.25%, on 30th June. Four further increases, of 0.25% each, followed in the ensuing months, leaving the Fed Funds rate at 2.25% at year-end. Normally this could be expected to have an adverse effect on equity markets, but by the time the Fed moved on rates, the change in policy was widely anticipated and generally viewed as appropriate. Rates were also steadily increased in the UK but remained unchanged in the eurozone, at 2%, throughout the year.
- Economic expansion in the Far East was driven by China, which has taken over from Japan as the engine of growth in the region. With double-digit GDP growth a possibility, the authorities in China introduced some controls with a view to slowing the economy down, culminating in an interest rate rise of 0.27% at the end of October. China's seemingly insatiable appetite for raw materials also provided a significant boost to other neighbouring economies, notably Australia, with its resource-based economy.
- Eurozone bonds enjoyed an excellent year, the Merrill Lynch Euro Govt. > 5 Year Index growing 10.7% in the period. A major factor in the sustained strength of bond markets was that price inflation has been well behaved, despite strong US economic growth and soaring oil prices. This allowed the Federal Reserve to raise US rates at a 'measured pace', while the ECB held its base interest rate unchanged at 2%, worried about the fragile recovery in Germany, in particular. The ECB was also encouraged to leave rates on hold by a strengthening exchange rate which threatened eurozone growth prospects, though it did help negate the inflationary impact of higher oil prices. During the period, the euro rose 8% against the US dollar and 2% against its major trading partners. This had the knock-on effect of significantly reducing the return to eurozone investors from dollar-based markets.

Market	Index	% Return 31.12.03 to 31.12.04	
		Local Currency %	Euro %
US	S & P 500	9.0	1.0
US	NASDAQ	8.6	0.7
Europe	FT/S&P Europe Ex. U.K.	10.3	10.3
Ireland	ISEQ	26.0	26.0
UK	FTSE 100	7.5	7.1
Japan	Topix	10.2	7.0
Hong Kong	Hang Seng	13.2	4.8
Australia	S&P/ASX 200	22.8	18.4
Bonds	Merrill Lynch Euro over 5 year Govt.	10.7	10.7

## Global Outlook

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- Activity in the global economy remains reasonably strong, although the forward indicators suggest some slowdown over coming months. The effects of last year's one-third rise in oil prices seem limited to date, but policymakers will remain vigilant during 2005.
- The Federal Reserve raised rates from the emergency 1% level last year, ending the period at 2.25%. For 2005 it has promised further 'measured pace' increases, which have largely been anticipated by interest rate markets.
- In the eurozone, the ECB has kept rates flat at 2% for a prolonged spell now, notwithstanding currency strength and subdued to weaker economic data. Investors and the ECB still anticipate an upward bias to rates during the year but this will be subject to improvements in the economic numbers. Eurozone bonds performed very strongly in 2004, but the general investor consensus is much more cautious this year. Nonetheless, continued low rates and well-behaved inflation could continue to underpin bonds in 2005.
- Surveys of equity investors suggest that they have already moderated their expectations for growth in 2005, although they remain broadly positive on the overall outlook for equity markets. A strong fourth quarter means that total returns for last year were quite healthy. Corporate profit growth globally for 2005 is expected to be in the order of 10% and this is likely to underpin equity markets.
- Currently, the funds are overweight bonds and equities versus the manager average. Sector-wise the funds are overweight basic industries and financials, while underweight some of the more defensive sectors, such as pharmaceuticals. Resources and general industrials are at, or close to, neutral. In geographical terms, the funds continue to be neutral the UK and Japan while overweight the Pacific Basin and Europe. The US remains an underweight position.



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