EAGLE STAR

Market Comment

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Overview

Caution was the order of the day among equity investors last week as worries about global economic growth continued to dog sentiment. The result was a good week for bonds and an extension of the previous week's price falls on equities.

In the US, the surprise jump in unemployment to 6% raised fears that the economy could slip back into recession, as did figures released on Thursday showing new jobless claims had risen from 355,000 to 441,000. The consumer sector showed continued resilience with November retail sales (ex autos) increasing 0.5% on the month. The University of Michigan index of consumer sentiment also beat forecasts, rising to 87 from 84.2 the previous month.

A policy meeting of the Federal Reserve on Tuesday, at which interest rates were left unchanged, had little impact, although the appointment of John Snow as Treasury secretary was expected to accelerate the passage of economy-boosting fiscal measures. Nonetheless, investors remained concerned that rising unemployment would make it more difficult for the consumer to continue spending.

In Europe, the slide in the German economy appeared to be finally having an impact on the ECB, which sharply revised down its growth forecasts for 2003 and, this morning (16th), announced that it is planning to reassess its 2% inflation target. Earlier in the week, Otmar Issing, the ECB's chief economist, indicated that the bank may cut interest rates further in the New Year.

Table 1 below shows the movements in the main markets since last week's comment.

Table 1

Market	Index	% Return 06/12/2002 to 13/12/2002	
		Local Currency	Euro
US	S&P 500	-2.5	-3.5
US	NASDAQ	-4.2	-5.2
Europe	FT/S&P Europe Ex. UK	-3.4	-3.4
Ireland	ISEQ	-4.5	-4.5
UK	FTSE 100	-3.4	-3.7
Japan	Topix	-2.9	-1.6
Hong Kong	Hang Seng	-2.5	-3.5
Bonds	Merrill Lynch Euro over 5 year	0.9	0.9

Equities

The October/November gains in equity markets were further eroded last week amid continuing economic worries and some negative corporate news. Technology stocks were hit by a warning from Nokia that sales of mobile handsets for the fourth quarter were likely to be weaker than expected. The European car sector weakened as monthly car figures showed a drop in sales of 6% over a year ago and Fiat struggled with changes in its top management structure, following the ousting of its chief executive. Trading volumes were generally light as investors awaited the start of the fourth quarter earnings reporting season later this week to give firmer guidelines on the strength, or otherwise, of the corporate sector.

Bonds

Eurozone bonds had a very good week, assisted by supportive comments on interest rate cuts by the ECB, combined with the weak state of the German economy. Dollar weakness also helped drive prices up as the euro rose to $1.0258, its highest level since January 2000. Euro strength (dollar weakness) is good for eurozone inflation and should make it easier for the ECB to cut interest rates further if economic conditions warrant further cuts.

Outlook

- Forward indicators for the major economies suggest that growth will remain relatively subdued into the New Year.
- With growth below trend in all the major economies, interest rates are likely to stay low in the US and the UK, and could fall further in the Eurozone.
- For further sustained rises in equities we need to see a more robust economic and

- earnings environment.
- Our overall portfolio remains neutral equities with a slight geographical bias towards Asian markets. Portfolios have become less defensive with overweight positions in financials, telecoms and healthcare. We have a preference for bonds over cash, given the low level of short term interest rates.