

Market Comment

Issued on 9th June 2003

Overview

Markets around the world made significant gains last week despite mixed signals on the world economy. The S&P 500 reached its highest level for eleven months, while the NASDAQ ended the week at levels not seen in over a year.

Comments from Alan Greenspan, the chairman of the US Federal Reserve were cautiously optimistic. He stated that it might be wise to lower US interest rates as an insurance against deflation, even though the economy looked likely to improve in the near term. The Institute of Supply Management manufacturing index showed an increase to 49.4 in May while its non manufacturing index registered a reading of 54.5, indicating growth and beating expectations. However, on Thursday there was a steep increase in US initial jobless claims and the unemployment rate rose to 6.1%.

In Europe, the week was dominated by the ECB decision on interest rates on Thursday. The committee cut the key interest rate by half a percentage point, a move that was widely anticipated by market participants. Wim Duisenburg, ECB president, also hinted at the prospect of further rate cuts in the eurozone.

On currency markets, the Euro continued its upward trend against the US dollar reaching \$1.19 early in the week before falling back to \$1.17 on Friday. On commodities markets, a lower than expected build up in US inventories lent support to oil prices.

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

Table 1			
Market	Index	% Return 30/05/2003 to 06/06/2003	
		Local Currency	Euro
US	S&P 500	2.5	3.0
US	NASDAQ	2.0	2.5
Europe	FT/S&P Europe Ex. UK	3.6	3.6
Ireland	ISEQ	3.7	3.7
UK	FTSE 100	2.5	4.6
Japan	Topix	3.8	4.9
Hong Kong	Hang Seng	2.2	2.7
Australia	S&P / ASX 200	1.3	3.1
Bonds	Merrill Lynch Euro over 5 year	0.4	0.4

Equities

The main news in the US was Oracle's unsolicited offer to buy rival PeopleSoft for about \$5.1 billion. The bid came after PeopleSoft earlier in the week said it would buy smaller rival J.D. Edwards for \$1.7 billion. This merger and acquisition activity helped to support markets globally.

European markets put in a strong performance last week as the long awaited interest rate cut from the ECB finally materialised. Financial stocks did well with Germany's Deutsche Bank rising following an upgrade to "buy" status from Merrill Lynch. SAP, the world's biggest maker of software to manage accounting and inventory tasks, rose sharply following the Oracle announcement in the US.

In the Far East, the Hong Kong market continued to benefit as the threat of the SARS virus receded and the weak US dollar supported exporting stocks. In Japan, the weaker currency helped exporting stocks such as Canon and Sony to extend their gains of last week.

Bonds

Eurozone bonds fell back early on in the week as equities moved ahead supported by better manufacturing data from the US. However they ended the week in positive territory following comments from the ECB president suggesting further interest rate cuts in addition to the 0.5% cut on Thursday. Inflation data released also supported bonds when it showed that the annual eurozone inflation rate has fallen to 1.9%, below the ECB's target of 2%.

Outlook

- ▶ Forward indicators for the major economies suggest that growth will remain relatively subdued for the rest of 2003.
- ▶ Central banks were anticipating a recovery in confidence post an Iraq war. Now they will be monitoring developments closely to see if economic activity stages even a partial rebound. Our central scenario remains that further rate cuts will be necessary, especially in Europe, even after last week's 0.5% reduction by the ECB.
- ▶ Given current valuation levels, a sustained rise in equities will need a more robust economic and earnings environment.
- ▶ Our current overall portfolio stance is overweight bonds and neutral equities versus the manager average. The funds are underweight in Europe due to deteriorating economic fundamentals and a strong currency and overweight Asia (ex-Japan) due to more attractive valuations and currency considerations.

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