

## Market Comment

Issued on 28th October 2003

### Overview

The third quarter reporting season continued in earnest last week. Almost 70% of the companies in the S&P 500 have now released results, the majority beating expectations. However, investors have already priced in much of this improvement in the equity market rally that began in mid-March. This resulted in some consolidation last week and only stocks with exceptionally good results made gains.

It was a quiet week for economic data. In the US, the Conference Board's September index of leading economic indicators fell 0.2%. It had been expected to rise marginally. The OECD released a cautious report on market trends, citing higher oil prices and the strengthening euro as possible dangers to financial markets. However, weekly unemployment data from the US showed further signs of stability in the labour market.

On currency markets, the dollar was lower. John Snow, the US treasury secretary reiterated the "strong dollar" policy of the US government. However, the consensus remains that the US administration favours a weaker dollar, particularly against Asian currencies. The US feels that Asian governments have kept their currencies artificially weak by pegging or manipulating them in order to support their export oriented industries.

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

Movements in the main markets since last week's comment			
Market	Index	% Return 17/10/2003 to 24/10/2003	
		Local Currency	Euro
US	S&P 500	-1.0	-2.8
US	NASDAQ	-2.5	-4.3
Europe	FT/S&P Europe Ex. UK	-2.3	-2.3
Ireland	ISEQ	-1.1	-1.1
UK	FTSE 100	-2.4	-2.8
Japan	Topix	-6.4	-7.8
Hong Kong	Hang Seng	-2.6	-4.5
Australia	S&P/ASX 200	-1.2	-1.6
Bonds	Merrill Lynch Euro over 5 year	0.3	0.3

### Equities

Positive third quarter results from a majority of companies failed to impress investors last week and there was profit-taking in evidence on markets around the world. Asian markets, which have outperformed in recent months, suffered the greatest falls. Japan had a particularly bad day on Thursday, when the Topix index ended the day 5.3% lower.

In the US, equities fell back despite good news from numerous companies. Citigroup reported a 20% rise in earnings, citing strong growth in investment banking and consumer lending as reasons. JP Morgan also announced rising profits. Lucent Technologies, the telecommunications equipment maker, reported its first profitable quarter for three years. Microsoft stock fell, despite raising its full year earnings guidance. The company warned that corporate spending on IT remained weak and investors focused on this aspect of their report.

In Europe, poor results from Electrolux, the home appliance maker, and Unilever, the home products producer, led the market lower. Electrolux reported a steep fall in US sales, while Unilever lowered its sales growth forecasts.

### Bonds

Bond prices held up well last week driven mainly by profit-taking in global equity markets. Eurozone bonds gained as the euro strengthened against the US dollar. While US bonds received a boost due to a bout of profit-taking on US equity markets. The release of the minutes of the last Bank of England Monetary Policy Committee meeting showed that four of the nine members had voted for an increase in interest rates. This was negative for UK bonds and has heightened the prospect of rising UK interest rates in the coming months. The over 5 year eurozone bond index rose 0.3% on the week.

### Outlook

- Economic activity has strengthened in the US and investors have begun to anticipate a synchronised global recovery; inflation pressures remain low.
- Equity markets have risen sharply since mid-March; increased growth optimism could extend this rally further although valuations are a constraint in certain sectors and markets. Additionally, investors still have some concerns about the sustainability of growth improvements.
- Central banks have re-stated their commitment to keeping interest rates low and recent inflation data have supported this stance.
- Ultimately, however, a successful reflationary effort by global policymakers would mean a negative environment for bond markets and a more positive

one for equities.

- Our current overall portfolio stance is overweight equities and underweight bonds versus the manager average. The funds remain underweight in the UK equity market due to its defensive characteristics and overweight Asia and Latin America due to more attractive valuations and better economic growth potential.

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