Market Comment

Issued on 12th January 2004

Overview

Financial markets had a positive start to the New Year, with equities continuing to make ground on better economic and earnings expectations. Bond prices picked up further after the release of surprisingly weak US employment data.

The technology sector was particularly buoyant, underpinned by positive earnings guidance from Nokia, the world's largest mobile phone maker, which helped the NASDAQ Index gain 4% on the week. Economic data was less buoyant than recent releases; weaker US employment figures raised concerns about the pace of job creation. Non-farm payrolls increased by only 1,000 in December, surprising market commentators, who had been expecting an increase of 150,000. The previous month's figure of 57,000 new jobs was also revised downwards to 43,000.

The jobs data caused the dollar to weaken further, falling to 1.28 against the euro, while oil prices went higher to just under $32 per barrel as harsh weather in the US pushed up demand. These factors would normally be negative for equities, but market momentum and good corporate news helped sentiment remain fundamentally positive.

Movements in the main markets since last week's comment			
Market	**Index**	**% Return 02/01/2004 to 09/01/2004**	
		Local Currency	**Euro**
US	S&P 500	1.2	-0.7
US	NASDAQ	4.0	2.0
Europe	FT/S&P Europe Ex. UK	0.5	0.5
Ireland	ISEQ	2.4	2.4
UK	FTSE 100	-1.0	0.0
Japan	Topix	2.1	0.6
Hong Kong	Hang Seng	4.6	2.6
Australia	S&P/ASX 200	0.0	0.5
Bonds	Merrill Lynch Euro over 5 year	1.5	1.5

Equities

The technology sector was the main focus of attention with Nokia announcing on Thursday that Q4 profits and revenues would be higher than previously forecast due to improving sales on the networking side of the business and better selling prices achieved by handsets. Nokia shares closed over 18% higher on the week. The sector was also supported by reports of a 26% rise in global chip sales in November, which helped Samsung Electronics, the Korean-based chip maker, gain 8% on the week, while Intel, the world's largest chip manufacturer, added 3%.

Telecom stocks also had a good week with Vodafone gaining 6%, pushing it back into the largest capitalisation position in the FTSE 100 Index. The overall index fell 1% however as oil stocks were badly hit by a shock 20% reduction by Royal Dutch Shell of its estimated proven reserves. The weighting of oil giants such as Shell and BP in the FTSE Index caused it to underperform on the week

In Asia, strong economic expectations pushed the Hong Kong market up 4.6% with property stocks particularly strong and China Mobile gaining from interest in telecom stocks with a rise of 12%.

Bonds

Bonds bounced during the week, helped by weak US employment data, which caused investors to push back their expectations of higher interest rates. Prior to the release of the US non-farm payroll figures, consensus expectations were for US interest rates to rise by 25 basis points around mid-year. A strong labour market is considered essential for sustained economic growth and the latest statistics convinced commentators that the Federal Reserve would maintain its accommodative stance until there is a clear improvement in the jobs market, particularly as inflation remains at low levels.

Outlook

- The global economy, led by the US should continue to expand fairly strongly during 2004.
- As confidence in the global economy has improved, 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.
- This environment is one in which bonds will 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 and Latin America due to more attractive valuations and better economic growth potential and underweight in the UK equity market due to its defensive characteristics. The funds are also overweight Europe on valuation grounds. The funds continue to have a sectoral bias toward cyclical stocks although some defensive sectors have been increased with pharmaceuticals being moved from underweight to neutral.