

## Market Comment

Issued on 21st March 2002

### Overview

Economic statistics released during the week continued to point to a recovery in the US economy. Businesses cut production severely in the fourth quarter of 2001 and met demand from inventories. This process has now stopped and this will give a significant boost to recorded GDP in the first quarter of 2002. Other positive indicators included figures showing industry working at a higher capacity and greater numbers of new houses being started. The University of Michigan Index of business confidence also showed a strong upswing to 95%, from 90.7% in the previous month, well ahead of expectations.

With evidence that the economy has resumed growth, it is not surprising that the Federal Reserve at its monthly meeting on Tuesday shifted its earlier stance that weakness posed the greatest risk to the economy. Instead it took a neutral stance, leaving interest rates unchanged on the grounds that, while the economy is growing, there are few signs of inflation picking up. However, it put down markers for a future rate increase in its upbeat comments on the economy, stating "the information that has become available since the last meeting of the Federal Reserve indicates that the economy, bolstered by a marked swing in inventory investment, is expanding at a significant pace".

The more positive economic outlook is reflected in an upturn in equity markets and a weaker performance from bonds over the last few weeks. Table 1 below shows the movements in the main markets since last week's comment and in the month to date

### Market Performance

Table 1

Market	Index	% Return 13.03.2002 to 20.03.2002		% Return 28.02.2002 to 20.03.2002	
		Local Currency	Euro	Local Currency	Euro
US	S&P 500	-0.2	-1.1	4.1	2.1
US	NASDAQ	-1.6	-2.5	5.9	3.9
Europe	FT/S&P Europe Ex. UK	1.3	1.3	3.9	3.9
Ireland	ISEQ	1.2	1.2	3.5	3.5
UK	FTSE 100	-0.1	-0.1	3.3	2.1
Japan	Topix	2.1	-0.6	8.3	8.1
Hong Kong	Hang Seng	-1.6	-2.5	5.3	3.3
Bonds	Merrill Lynch Euro over 5 year	0.0	0.0	-1.4	-1.4

### Equities

Equity markets in Europe made further gains during the last week, responding well to the US economic upturn and to signs of stronger growth in Europe. The US market was more muted as the shift in the Fed's policy stance led to some profit taking, and the technology sector weakened in the face of negative analyst comments on semi-conductor stocks. Valuations of many companies in the US technology sector are high relative to expectations of earnings increases in those companies and relative to their equivalents in Europe, so they are more vulnerable to any negative comment. On the month to date all markets have made solid gains, confirming that the market recovery begun in September last year is again underway.

### Bonds

European bond prices were unchanged over the week, while in the US prices of shorter dated issues came under some pressure as the Fed announcements on the economy confirmed the view that a rise in interest rates is not far away. The main support for bond prices is a lack of any inflationary pressure, which should allow monetary policy makers to sustain their low interest rate stance longer than would normally be expected in a scenario of rising economic growth.

### Market Outlook

- The Federal Reserve performed a dramatic easing of monetary policy during 2001, with interest rates cut to below 2%, a forty-year low. Other central banks also lowered rates in a global effort to counteract recessionary conditions.
- The cuts in interest rates have helped to reflate the major economies. However, the recovery could be moderate in nature compared to previous rebounds.

- With companies in general unable to increase prices, partly due to an overhang in capacity, inflationary pressures will likely remain subdued.
- A slightly overweight stance in equities is warranted at present given the improving news concerning global economic recovery. However, concerns remain regarding the degree and sustainability of the economic upturn, the opaque corporate earnings picture and high valuations in the US technology sector.

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