

Market Comment

Issued on 28th April 2003

Overview

Equity markets failed to gather further momentum last week as the impact of the SARS virus escalated and the earnings reporting season continued. Many of the companies reporting beat market expectations; however these expectations are based on numbers that had been previously revised downward to reflect the weakness in the world economy.

The SARS virus continued to take a toll on financial markets. The World Bank cut 0.5 percentage points from its East Asian growth forecasts. The OECD also warned that the virus could unhinge growth in China, causing difficulties in the tourism and retail sectors.

In the US, Alan Greenspan, chairman of the Federal Reserve since 1987 is set for another term when his tenure is completed in June. The White House confirmed that George W. Bush is to nominate him again. Investors welcomed the news, as stability is important in the current economic climate. The Federal Reserve released its Beige Book survey of economic conditions on Wednesday. The overall picture was a downbeat one, however the housing market continues to hold up well. US gross domestic product grew by 1.6% in the first quarter. Economists had expected growth of 2.3%. A rise in US unemployment claims in April also weighed heavily on investor sentiment.

In the UK, the Bank of England's minutes from its last policy meeting showed that the members of its monetary policy committee voted 7-2 to keep interest rates on hold. This had largely been anticipated by the financial markets.

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

Market	Index	% Return 18/04/2003 to 25/04/2003	
		Local Currency	Euro
US	S&P 500	0.6	-0.8
US	NASDAQ	0.6	-0.8
Europe	FT/S&P Europe Ex. UK	-1.5	-1.5
Ireland	ISEQ	0.3	0.3
UK	FTSE 100	-0.5	-0.8
Japan	Topix	-1.1	-3.0
Hong Kong	Hang Seng	-2.0	-3.4
Bonds	Merrill Lynch Euro over 5 year	0.4	0.4

Equities

The corporate sector remained the focus of investor attention yet again last week as pharmaceutical, telecom and auto manufacturers announced results. In the US, pharmaceutical giants, Eli Lilly and Pfizer both beat expectations. Sprint, the long-distance telephone carrier reduced its 2003 earnings forecast. However, AT&T stock rose 18 per cent after it reported first-quarter profits that beat even the most optimistic estimates.

In Europe, German semiconductor maker, Infineon, fell after it said weak memory chip prices meant its quarterly losses widened. DaimlerChrysler, the maker of Mercedes cars, warned that deteriorating market conditions in the US would make it harder for it to achieve its earnings target for 2003.

Nissan Motor, the Japanese carmaker, has come from near bankruptcy to a zero debt position in three years. The company reported an operating margin of 10.8%, while its operating profit was up 50.7%.

Hong Kong fell to a four and half year low last week due to the deadly SARS virus.

News on Sunday that the virus may have peaked in most countries excluding China may help to alleviate some investor concerns. In Australia, the inflation rate came in at 2.1 percent for the first quarter. Analysts expect the central bank to hold its official cash rate at 4.75 % until the second half of 2003.

Bonds

Bond markets held their ground last week as equity markets stumbled and concerns over the SARS virus prevailed. Weak economic numbers on employment and output figures also helped US bonds despite large two-year issuance earlier in the week. Eurozone bonds were supported by the rise of the Euro, which broke through \$1.10. Low inflation data for April also helped bonds as it increases the possibility of an interest rate cut by the ECB.

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.
- ▶ 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. On a geographic basis, the funds continue to have a preference for the Pacific region on a valuation basis and as a low cost producer and the UK on valuation grounds. The funds are underweight in Europe due to deteriorating economic fundamentals. Within the Pacific region, a substantial part of the exposure had been moved from Hong Kong to Australia, prior to the SARS outbreak.

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