EAGLE STAR

Market Comment

Issued on 3rd June 2003

Overview

In a short trading week interrupted by bank holidays in the US and UK on Monday, and in Europe on Thursday, currency movements were a dominant feature of the markets. The euro rose to an all-time high of 1.193 against the dollar on Tuesday, further fuelling expectations of an early eurozone interest rate cut of 0.5%. Some of the euro's gain was given up by the end of the week when better US economic data underpinned a small dollar recovery which ended the week at 1.176 against the euro.

On the economic front, investors responded well to a rise in the US consumer confidence index from 81 in April to 83.8 in May and an upward revision in Q1 GDP from 1.6% to 1.9%. The good news was compounded on Friday with the release of the Chicago Purchasing Managers' Survey which jumped from 47.6 to 52.2, well above an expected level of 49. Even in Europe, there was a glimmer of an improvement with the German Ifo business climate index rising from 86.6 in April to 87.6 in May. However, not all the news was positive and investor sentiment was dampened down by disappointing US durable goods orders and higher than expected jobless claims. Overall, though, equity markets made solid gains on the week while eurozone bonds gave up a little of their recent advance.

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

Table 1

Market	Index	% Return 23/05/2003 to 30/05/2003	
		Local Currency	Euro
US	S&P 500	3.3	3.6
US	NASDAQ	5.7	6.0
Europe	FT/S&P Europe Ex. UK	1.7	2.1
Ireland	ISEQ	-1.2	-1.2
UK	FTSE 100	1.7	2.1
Japan	Topix	1.4	-0.4
Hong Kong	Hang Seng	2.0	2.3
Australia	S&P/ASX 200	0.4	-0.1
Bonds	Merrill Lynch Euro over 5 year	-0.7	-0.7

Equities

Strong gains were registered in the US market in response to better consumer confidence. Technology stocks were particularly strong and the NASDAQ Index rose almost 6%. Globally, technology stocks gained from a statement by ST Microelectronics, the world's fourth largest chipmaker, that it expected capital expenditures to rise substantially in the second half of the year. Other chipmakers, such as Intel, which is due to give a mid-quarter update this week, also rose on the news.

The prospect of a rise in US consumer demand and a retreat in the euro gave a much needed boost to European car-makers which had flagged recently on a downturn in demand and on the impact of the stronger euro on their export earnings. European pharmaceuticals also received a boost from the weaker euro.

In the Far East, the Hong Kong market extended its recovery of last week as the SARS threat receded and the weak US dollar supported exporting stocks. In Tokyo, the efforts of the Bank of Japan to push down the Yen began to pay off and the weaker currency helped exporting stocks such as Canon to make significant gains.

Bonds

The Eurozone over 5 year bond index slipped back slightly as hopes revived of a stronger US economy and the euro gave up some of its gains against the dollar. The ECB is due to meet this week and an interest rate cut of 50 basis points is widely expected by market forecasters.

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. The funds are underweight in Europe due to deteriorating economic fundamentals and a strong currency.