EAGLE STAR

Market Comment

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Overview

Equity markets moved forward last week supported by positive economic data and earnings reports. The US Federal Reserve met on Tuesday and as expected left interest rates unchanged. The eagerly awaited accompanying statement from the Board restated that interest rates are likely to stay low for "a considerable period". Economic growth in the US surged to its highest level since 1984. Gross domestic product for the third quarter expanded by 7.2% annualised, beating even the most optimistic of expectations. Other US economic data was also good. The housing market in the US continues to hold up remarkably well. Labour data was also positive and improved consumer confidence figures reflected the upbeat economic picture.

The earnings-reporting season winded down last week with the majority of companies having achieved much improved figures. Overall, average earnings are 17 per cent higher than this time last year. However, there have been some cautious outlooks from a number of companies.

In currency markets, the Japanese Ministry of Finance announced, it had sold approximately $25 billion of domestic currency in October. This is the fifth highest monthly intervention in the last 12 years. The aim of the authorities is to weaken the yen against the US dollar to protect Japans export oriented stocks. The US Treasury Secretary, John Snow, reiterated the US strong dollar policy but stressed his belief that market forces should be allowed to determine exchange rates.

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 24/10/2003 to 31/10/2003	
		Local Currency	Euro
US	S&P 500	2.1	4.3
US	NASDAQ	3.6	5.8
Europe	FT/S&P Europe Ex. UK	3.2	3.2
Ireland	ISEQ	2.4	2.4
UK	FTSE 100	1.2	3.1
Japan	Topix	1.8	3.2
Hong Kong	Hang Seng	3.9	5.9
Australia	S&P/ASX 200	0.5	3.6
Bonds	Merrill Lynch Euro over 5 year	-0.1	-0.1

Equities

Equity markets in the US received a boost by the emergence of some fresh merger activity in the financial sector. Bank of America announced on Monday that is is paying $47 billion in stock for Fleet-Boston Financial to create the second largest US bank measured in asset terms. Bank of America fell 10% on the announcement and ended the week 7.9% lower.

European markets ended the week in positive territory. The German market performed particularly well. The Ifo index of business confidence rose from 92.0 in September to 94.2 this month. This is the sixth consecutive rise in the reading.

Hong Kong continued its upward trend driven by the positive economic data from the US. Financials and Chinese "H" share stocks performed particularly well.

Bonds

Bond prices fell back last week driven mainly by the emergence of very strong GDP data. Eurozone bonds struggled as the positive data from Germany favoured equities. In the UK, investors are now expecting an early rate rise due to strong consumer spending and robust house prices. This may even happen this week. The over 5 year eurozone bond index fell 0.1% 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.
- Central banks have re-stated their commitment to keeping interest rates low. However, markets are beginning to question the longevity of this commitment.
- Ultimately, 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. The funds have a sectoral bias toward cyclical stocks.

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