EAGLE STAR

Market Comment

Issued on 24th November 2003

Overview

Strong economic fundamentals were overtaken by other events last week, causing pressure on equity markets and boosting bond prices. Most of the decline in equities could be attributed to profit taking after strong advances in recent months. However, sentiment was also hit by the revival of terrorism fears following bombing attacks in Turkey, together with concerns of a possible trade war following the US imposition of quotas on some Chinese textile imports. Investor confidence was also shaken by a fall in the dollar which pushed the euro to $1.20, its highest level since the single currency launch in 1999.

On the economic front, US economic indicators continued to point to a robust cyclical recovery. On Monday, the Empire manufacturing Index, which measures manufacturing activity in New York State, rose to 41 from an upwardly revised 34.1 in October and was well ahead of expectations. Later in the week, October housing statistics revealed increases in housing starts and building permits as well as upward revisions to the previous month's figures. Initial jobless claims and continuing claims were also lower than in the previous week.

Movements in the main markets since last week's comment

Market	Index	% Return 14/11/2003 to 21/11/2003	
		Local Currency	Euro
US	S&P 500	-1.4	-2.8
US	NASDAQ	-1.9	-3.2
Europe	FT/S&P Europe Ex. UK	-2.7	-2.7
Ireland	ISEQ	-3.0	-3.0
UK	FTSE 100	-1.8	-2.0
Japan	Topix	-3.2	-5.0
Hong Kong	Hang Seng	-3.0	-4.4
Australia	S&P/ASX 200	-1.0	-1.8
Bonds	Merrill Lynch Euro over 5 year	0.4	0.4

Equities

Profit-taking and dollar weakness were the main influences on equity markets during the week, with the largest declines occurring in those regions, such as Asia, and sectors, such as technology, which had risen fastest during the upturn. This was despite strong prospects for economic growth in Asia and positive results from some leading technology stocks. Analog Devices, which makes computer chips, increased its profits on better orders, while Hewlett Packard announced its strongest results since its purchase of Compaq last year.

Currency movements hit European equities in particular. Export-oriented European stocks such as autos and pharmaceuticals were hit by the negative impact of a stronger euro on earnings. In Europe, too, insurance stocks weakened on renewed terrorism fears, together with the negative effect of lower equity values on their reserves.

The UK market held up somewhat better thanks to a strong performance from Vodafone which rose 3.5% on the week on better than expected results.

Bonds

Bond markets had a good run on the week, notwithstanding stronger signals on the US economy. Instead, investors focussed on the longer term impact of a potential trade war, safe haven considerations as terrorism fears resurfaced, and on the impact of a weaker dollar. The Merrill Lynch >5 year index of Eurozone bonds gained 0.4%.

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.
- Interest rates have been kept low for some time, but markets have already priced for both the Federal Reserve and ECB beginning to increase rates next year.
- 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 remains overweight equities and underweight bonds versus the manager average. The funds continue to be underweight 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 continue to have a sectoral bias toward cyclical stocks although some defensive sectors such as pharmaceuticals have been moved from underweight to neutral.