

## Market Comment

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### Overview

There was some disquiet on equity markets over the last week, largely generated by concerns that the US economic recovery expected for 2002 would be slow and sluggish. New releases of economic indicators were slightly worse than expected. Retail sales figures, though ahead of expectations overall, were more disappointing when adjusted for motor sales which were buoyed by cheap financing deals and heavy discounting. Industrial output and capacity utilisation figures were also worse than forecast.

On the positive side, inflation remained subdued, helped by downward pressure on oil prices, and this should allow scope for a further interest rate cut, already hinted at by the Federal Reserve chairman, Alan Greenspan.

### Market Performance

Table 1 below shows the movements in selected markets since the beginning of the new year.

Table 1

Market	Index	% Return 08/01/2002 to 16/01/2002		% Return 01/01/2002 to 16/01/2002	
		Local Currency	Euro	Local Currency	Euro
US	S&P 500	-2.9	-1.9	-1.8	-0.9
US	NASDAQ	-5.4	-4.4	-0.3	0.6
Europe	FT/S&P Europe Ex. UK	-3.1	-3.1	-4.2	-4.2
Ireland	ISEQ	-0.2	-0.2	-1.5	-1.5
UK	FTSE 100	-2.3	-1.7	-1.7	-2.1
Japan	Topix	-4.3	-2.9	-4.3	-3.9
Hong Kong	Hang Seng	-6.4	-5.4	-3.8	-3.0
Euro Bonds	Merril Lynch Euro over 5 year	0.7	0.7	1.9	1.9

### Bonds

The more cautious stance on the economic front was positive for bond markets and prices of long-dated stocks moved ahead as investors took the view that the interest rate cycle may not yet have reached its bottom. Falling interest rates normally result in higher bond prices and, conversely, higher interest rates cause bond prices to fall. Towards the end of last year, bond prices fell on the expectation that an early economic recovery would bring an end to the round of interest rate cuts, but this expectation has now receded allowing bond prices to move forward again. The Eagle Star Active Fixed Income Fund, which invests in government and high quality corporate bonds, has gained 2.5% in the month to 16th January.

### Equities

Equity markets faltered in the face of the weaker economic numbers, combined with disappointing corporate news. The highlight of corporate announcements was Intel, the giant microchip maker, which reported stronger 2001 results than analysts had expected, yet experienced a fall in its share price. This was due to the fact that the stock has had a very strong run since late September, advancing by 70%, and its valuation is now at a level where investors need to see strong growth in future earnings to have a further appetite for the stock. Last year's results were accompanied by a downbeat statement from the Intel chief executive on future economic prospects and its own capital expenditure plans. This resulted in a more cautious assessment of the level of valuations generally, particularly in the technology sector. Nonetheless, the sector continues to hold its post-September gains, as evidenced by the NASDAQ Index, which rose 40% from its bottom on 24th September up to the end of the year, and is largely unchanged month to date. Over the period from close of business on 21st September 2001 to close of business on 16th January 2002, Eagle Star's Top Tech 100 fund is up over 41%.

### 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; moves which were possible due to subdued inflation pressures globally.
- Cutting interest rates will help to reflate the major economies but as a policy instrument interest rate cuts act slowly. The recovery could also appear patchy at first, as many sectors still have an overhang of capacity built up during 1999/2000.

- In 2002, investors are watching economic data to ascertain where we are in this global downturn/recovery cycle; currently it is felt that we are at the low point for the global economy and close to lows on interest rates.
- Given the extent of the stimulus we have seen, especially in the US, equity investors should sit through negative earnings' reports in anticipation of a recovery in corporate profits in the second half of 2002.

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