EAGLE STAR

Market Comment

Issued on 24th February 2003

Overview

Equity markets recorded a second consecutive week of modest gains, largely in response to some analyst upgrades. On the US economic front, the important feature of the week was the announcement of the country's largest ever trade deficit of $44 billion. The figure had been expected to come in at around $39 billion and the overrun is indicative of the weak economic state of the main trading partners of the US, notably Europe and Japan. The dollar took a further slide in response to the news. Jobless claims were also higher than expected although, more positively, housing starts and building permits were ahead of expectations. Tomorrow's release of consumer confidence figures will be keenly awaited as an indicator of the health of the consumer sector which accounts for 70% of the US economy.

In Europe, industrial production recorded a drop of 1.5% in December, the worst fall on record, while the German economics minister announced that the country may have slipped into a recession, further fuelling expectations of an early cut in eurozone interest rates.

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

Table 1			
Market	**Index**	**% Return 14/02/2003 to 21/02/2003**	
		Local Currency	**Euro**
US	S&P 500	1.6	1.4
US	NASDAQ	3.0	2.8
Europe	FT/S&P Europe Ex. UK	0.0	0.0
Ireland	ISEQ	1.2	1.2
UK	FTSE 100	3.2	1.4
Japan	Topix	-2.1	-0.9
Hong Kong	Hang Seng	0.5	0.4
Bonds	Merrill Lynch Euro over 5 year	0.5	0.5

Equities

The UK was the best performing region as it continued to rally from deeply oversold positions in late January. It was helped by its high exposure to oil stocks, which have been gaining from increased oil prices. On the downside, the insurance sector was hit by concerns on pensions deficits. Eagle Star stepped up its exposure to the UK market during the early February downturn when stock prices fell to attractive levels. We are now overweight the market relative to competitors.

At a sectoral level, technology stocks recorded strong gains, helped by a positive research report from Merrill Lynch. Healthcare stocks also performed well, with earnings results beating expectations in many cases. Sanofi-Synthelabo, the French pharmaceuticals group, rose 9% on Wednesday on announcing a 29% rise in earnings per share.

In Asia, Singapore and South Korea rose by 3% and 5% respectively, mainly due to the strong performance in technology stocks. Japan was hit by further significant weakness in the banking sector.

Bonds

The negative news on the German economy, allied with expectations of lower interest rates and a rise in the euro against the dollar, gave a further boost to eurozone bond prices. The market is discounting an early interest rate cut of 0.5% and some commentators anticipate that it could be as much as 1%. Since year end, the over 5 year eurozone bond index is up 2.7%.

Outlook

- Forward indicators for the major economies suggest that growth will remain relatively subdued, particularly in the first half of 2003.
- Renewed geo-political tensions have seen oil prices rise by 35% since the low of last November. If sustained at these levels, economic growth forecasts could be reduced

further.

- With growth below trend in all the major economies, interest rates are likely to stay low in the US and should fall further in the Eurozone.
- The US dollar will remain under scrutiny in 2003 with further downward pressure likely.
- For sustained rises in equities we need to see a more robust economic and earnings environment. But in the near term, the Iraq crisis continues to impact negatively on market sentiment.
- Our current overall portfolio stance is overweight bonds and neutral to slightly underweight 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. The funds are underweight in Europe due to deteriorating economic fundamentals.