Market Comment

Issued on 22nd April 2003

Overview

It was a positive week on most equity markets as investors focused on corporate earnings reports for the first quarter and looked beyond the war in Iraq. The majority of results were from the technology and financial sectors and were in line with forecasts or better than expected. However, there are suggestions that these earnings results are due to cost cutting measures by corporations rather than price or volume increases and this is causing concern about employment levels. The earnings reporting season will continue this week when pharmaceutical and telecommunications companies release their reports.

There were mixed data on the economic front. In the US, business inventories climbed to their highest level since September 2001, while US industrial production for March was worse than expected. There was positive news on US housing which rebounded in March, helped by low mortgage rates. The Philadelphia Federal Reserve also released its outlook, which remained relatively subdued. In the UK, disappointing data regarding the retail sector served to underscore speculation about the slowdown in the UK economy, which had held up relatively well.

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

Table 1

Market	Index	% Return 11/04/2003 to 18/04/2003	
		Local Currency	Euro
US	S&P 500	2.9	1.7
US	NASDAQ	4.9	3.7
Europe	FT/S&P Europe Ex. UK	2.9	2.9
Ireland	ISEQ	2.7	2.7
UK	FTSE 100	2.1	0.9
Japan	Topix	1.1	0.6
Hong Kong	Hang Seng	-0.8	-1.9
Bonds	Merrill Lynch Euro over 5 year	0.5	0.5

Equities

Investors turned their attention to the corporate sector last week. In the US, shares in Citigroup rose after the financial services group announced its first-quarter profits rose by 18 percent. IBM reaffirmed full-year earnings estimates, while Microsoft reported better than expected earnings. Intel also met its financial targets. However, both Microsoft and Intel cautioned that demand is likely to remain subdued in the medium term.

In Europe, the big news of the week came from Nokia, the telecommunications equipment maker. First quarter earnings per share came in at 18 cents, well above market expectations and ahead of the company's own guidance range. The company also predicted that sales would climb between 4% and 12% in the second quarter. Adecco, the giant Swiss recruitment agency, jumped more than 15% when it produced net profits which almost doubled market expectations.

Asian markets under-performed their European and US counterparts. In Japan, there was further selling by corporate pension funds. Pension funds are poised to return a portion of their poorly performing assets to the state later this year. Many pension fund trustees are choosing to return cash and this is exerting downward pressure on the Japanese equity market.

Hong Kong has continued to falter due to the threat of the deadly SARS virus. Reports that the Chinese authorities had understated the level of infection in the territory led to the resignation of the health minister. This contributed further to investor jitters and the Hang Seng index lost ground on the week.

Bonds

Bond markets traded in a range last week as equity markets rose and expectations of further interest cuts in the Eurozone receded. Comments by Wim Duisenberg, president of the European Central Bank, that Eurozone interest rates remain appropriate and that easing monetary policy would not necessarily reduce the uncertainties brought about by the war, dampened expectations of a further rate cut. However, the ECB has been known to alter its views quite quickly in the past, when necessary. Bond markets were helped by inflation data in the US. The Consumer Price Index, excluding food and energy, was flat during March.

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. 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 and the UK on valuation grounds. The funds are underweight in Europe due to deteriorating economic fundamentals. Within the Pacific region, a substantial part of the exposure had been moved from Hong Kong to Australia, prior to the SARS outbreak.