EAGLE STAR

Market Comment

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Overview

It was a good week for equity markets which responded positively to first quarter earnings reports which were generally ahead of expectations. It is worth bearing in mind, however, that these expectations were drastically reduced over recent months in the face of weak economic numbers.

The economic signals remained mixed last week. In the US, April consumer confidence and March factory orders were stronger than expected. The Conference Board index of consumer confidence rose nearly 20 points from a downwardly revised 61.4 in March. The timing of the survey which determines the index is significant as the previous one was taken just after the start of the war with Iraq when oil prices were at a peak and there was intense uncertainty as to how the conflict would progress. The most recent results were obtained around the period of the fall of Baghdad when the coalition victory was secure. Nonetheless, the turnaround could signal a recovery in US consumer spending, although it would need to be underpinned by improving labour market conditions and this is not yet apparent. Indeed, the figures on initial jobless claims released on Thursday were higher than expected and the Institute of Supply Managers index of manufacturing activity was lower, as was spending in the construction sector

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

Table 1

Market	Index	% Return 25/04/2003 to 02/05/2003	
		Local Currency	Euro
US	S&P 500	3.5	1.8
US	NASDAQ	4.8	3.0
Europe	FT/S&P Europe Ex. UK	2.2	2.2
Ireland	ISEQ	2.1	2.1
UK	FTSE 100	2.1	1.3
Japan	Topix	2.9	2.2
Hong Kong	Hang Seng	4.8	3.0
Australia	S&P / ASX 200	-0.9	-0.4
Bonds	Merrill Lynch Euro over 5 year	0.3	0.3

Equities

In the US, the technology sector drove the rally in equities last week, with the NASDAQ rising almost 5%. Telecoms, materials and financials also performed well, while defensive sectors underperformed.

Healthcare stocks helped support the UK market. AstraZeneca rose 5.3% as Q1 earnings beat expectations. The company has also just received approval from the US Food and Drug Administration for its new cancer drug, Iressa. European insurers gained from the positive impact of recent gains in equity markets on the value of their reserves, with the giant German insurer, Allianz, rising over 15% as its €4.4bn. rights issue was successfully placed.

In Hong Kong, the SARS outbreak was reported to have peaked with the number of new cases declining and this underpinned a 4.8% rally in the Hang Seng index. The defensive Australian market underperformed on the week.

Bonds

Despite the continued gains on equities, bond prices held steady on the week as investors remained unconvinced that the US economy has turned the corner. Eurozone bonds were supported by further signs of economic weakness as France revised down its growth rate for the final quarter of last year to an annualised fall of 0.2%. In Germany, the Ifo purchasing managers' index for April recorded a sharp drop and the Reuters index of eurozone manufacturing activity fell to its lowest level for 15 months. The bad news helped sustain expectations of a cut in interest rates, as did a further rise to 1.12 in the euro/dollar rate, although the consensus view is that no cut will be forthcoming at this week's meeting of the ECB.

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. The funds are underweight in Europe due to deteriorating economic fundamentals and a strong currency.