GLOBAL OVERVIEW

World Equity Markets

Despite the World Index ending the fourth quarter with a moderate gain, 2002 is likely to be remembered as being the third year in succession when equity markets experienced declines, a phenomenon not seen since the beginning of the Second World War.

The collapse in earnings seen in many of the world's major corporations has been almost without precedent, as the excesses which accompanied expansion during the mid to late 1990's during the Internet boom have been systematically wrought from company valuations. Accompanying this collapse has been a dramatic rise in Geopolitical risk, stemming from the September 2001 attacks, and a renewed focus, with increasing legal backing, on the veracity of corporate governance.

United States

The S&P 500 Index showed a gain of approximately 10% during the fourth quarter, lead by a rebound, albeit from very low levels, in the value of many major technology companies, as investors searched for corporations amongst the sector who would likely benefit from the early stages of economic recovery.

Oil shares also continued to profit from a rise in the underlying commodity price, as tensions grew over the likely long term result of the UN weapons inspectors arrival in Iraq. As the likelihood of military action in the gulf remains, there seems little prospect of lower oil prices, and whilst supply concerns exist, we do not believe that a return to mid USD$ 25 price levels is likely in the short term.

From a purely financial aspect, the key to positive returns being sustained into 2003 is a continuation in positive earnings surprises from major US corporations. Economic activity in the US continued to rebound during the fourth quarter from last year's recession, however the pace of the recovery remains modest and uneven. Further evidence that companies are seeing real earnings growth will therefore be required to underpin the recent rise in share prices.

Europe

The economic landscape in Euroland has been bleak for some time, and there has been little evidence over the fourth quarter of 2002 that the Central Bank's decision to keep interest rates on hold for much of the year has been correct. Indeed the Bank's decision to cut interest rates by 50 basis points at their December meeting is indicative of the depth of concern within the region at the economic outlook for 2003.

Against this largely negative background however, equity markets managed to show a positive return over the quarter, as once again, investors searched for companies which would likely weather the current economic conditions, and would prosper from any US lead global recovery.

Of the top ten largest gainers within the S&P Euro 50 Index over the quarter, four (France Telecom, Alcatel, Deutsche Telekom and Vivendi Universal) were at the forefront of the 1990's telecommunications boom and each of whom has seen their share prices decimated over the past three years. The remaining six companies are all major financial institutions, providing some insight into investor thinking over the period.

United Kingdom

The economic environment in the United Kingdom over the last five years has been characterised by weak manufacturing output, strong consumer spending and a housing boom. There are signs that this may be about to change. Consumers have built up debt aggresively in recent years, and although low interest rates have eased debt service costs, the real value of these debts is becoming a considerable burden.

With increasing social security payments being introduced in April 2003, the Bank of England has become increasingly concerned at the build up of debt, and the risk that this will lead to a hard landing. This is the principal reason that they have resisted reducing interest rates as other central banks have done.

Despite these concerns, the benchmark FTSE 100 index showed a modest 5% gain over the fourth quarter of 2002, as a number of positive earnings surprises from major UK companies (including Vodafone and British Airways) spurred investor interest. The index's high energy weighting (British Petroleum, Shell etc.) was also of benefit, as continuing middle east tensions saw oil prices approach USD$ 30 per barrel once again.

Japan

Following a surprise 3% annualised growth in GDP during the third quarter, expectations for a modest recovery in the Japanese economy were diminished during the latter stages of 2002 as export growth suffered a 25% decline, reflecting the weak global economic picture.

Japanese equities continued their seemingly relentless decline, the Nikkei Index falling by approximately 9% over the quarter as the previous stalwarts of the economy, the electronics and auto manufacturers, saw business levels tail off as exports declined.

The Japanese government has continued to attempt to introduce stability to the fragile economy, with new policies on non-performing loan assistance, and a planned 5 Trillion Yen spending program for 2003. However with domestic consumption remaining in the doldrums, there seems little likelihood of any meaningful equity recovery in the short term.

Global Bonds

Following declines early in the fourth quarter as expectations for an improvement in global economic conditions saw interest rate pressure rise slightly, global bonds staged a recovery to close the quarter on a firmer note, with small net gains being seen in each of the major currency areas.

Short dated bonds continued to see gains, as both the Federal Reserve and European Central Bank cut key interest rates in response to continuing global economic weakness. The largest gains within the major currency area were seen in Euro denominated issues, despite the Euro member states' decision to expand membership to include former Eastern Bloc states in forthcoming years, and the funding issues this is likely to raise.

Global Currencies

The strongest of the major currencies over the fourth quarter was the Euro, which gained approximately 6% against the Dollar and approximately 3% against the Pound in the three month period. Continuing yield premiums over the US currency, and demand for fixed interest assets in Europe and the UK contributed to the Dollar's decline, reversing the usual maxim of the US currency being seen as a safe haven in times of geopolitical uncertainty.

Despite domestic economic concerns, the Japanese Yen also showed limited strength against the Dollar, gaining approximately 3% against the weaker US currency.

Summary

Whilst economic conditions undoubtedly remain difficult worldwide, we have, with the exception of Japan, been encouraged by global equity markets ability to show positive returns during the quarter under review.

Corporate earnings in the US, still the world's foremost economy, have generally fared better than most analysts expectations, and if these improvements can be sustained, then this bodes well for the country's main trading partners.

Equity valuation levels have generally retreated to more reasonable levels, and the balance sheets of companies which have weathered the recession are in reasonable shape as a result of cost cutting and much reduced inventory levels.

The tensions in the Middle East have undoubtedly weighed heavily upon investors minds during the last year, however, if the situation escalates into full conflict, we do not expect this to be protracted. If one reviews the behaviour of markets following the gulf war, one can see that the greatest stock market declines were seen prior to, rather than after, the conflict began. We believe that the gradual deterioration in confidence as a result of the escalation may well prove to mirror this historical precedent.

We therefore look forward to a continuation of the recent market performance as we head into 2003, albeit that, with interest rates remaining at near record low levels, growth expectations for world stock markets have been reduced to more realistic, long term average, levels.