Monthly Strategy Update – 3 November 2003

GET READY FOR INTEREST RATE RISES

So much for those who were looking for difficult equity markets in October! The result was a world index rise of close to 6% as Wall Street continued to cheer investors with third quarter results coming in much better than expected. On top of this economic news was positive whilst the American Federal Reserve emphasised a continuation of its favourable monetary policy. Throw in a resurgence of corporate activity and you have a powerful cocktail to keep equity momentum. Elsewhere, Fixed Interest markets were weaker as yields rose to reflect a realisation of stronger economic growth and a growing expectation that the UK would be the first major economy to raise interest rates. A combination of record consumer borrowing and renewed strength in the UK property market seems to make a rise inevitable.

Our defensive yield curve positioning has sheltered us from the difficulties in Fixed Interest markets. In International portfolios we have tactically reduced our Canadian Dollar exposure by half and invested in the Australian Dollar, which we consider will continue to benefit from a cyclical upturn in commodity prices. In our International Sterling portfolio we are looking to increase our Euro exposure into further short term sterling strength. There is also potential for a short-term technical rally in the UK Bond market, given its recent weakness and an imminent move to a European calculation of inflation. This could present us with a temporary trading opportunity of which we would take advantage.

To properly reflect our short term confidence in equities we raised our equity allocation by 10% and reduced our Fixed Interest weighting by an equivalent sum. To provide immediate exposure to world equity markets in an efficient manner we bought our own Sterling and US Dollar Strategist aggressive equity Funds. It also gives us the flexibility to cut the position swiftly and cost effectively if we feel it is right to move to a less active equity position in the future. The Sterling Aggressive Fund has outperformed the average fund during the last three years and its year to date performance leaves it in the top decile of its peer group.

Within our direct equity portfolios we have sold **Marsh and McLennan**, as we were concerned about its relative valuation and the weaker performance stemming from its Fund Management arm, Putnam Investments. Additionally, we have also sold **Met Life** following the disclosure that the Securities and Exchange Commission has launched a formal investigation into one of its subsidiaries. With the proceeds we have concentrated on **American International Group** where the shares stand at a 20% discount to the major American market index for 2004. We expect the shares to outperform others in the Insurance peer group, as they are technically and fundamentally attractive.

In the short run we expect the cyclical stock market recovery in equities to continue and have positioned our “Managed” and “Growth” portfolios accordingly. Whilst we recognise there are some disturbing imbalances in the world economy we consider that there is sufficient “blue sky” to be more active. In particular we believe that forecasts for fourth quarter profits are too low and will, like the third quarter, surprise on the upside.

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