Chapter I – Financial Markets in 2003

After three years of steep decline, financial markets stabilised in 2003 and confidence began to return. This was reflected in a marked upturn in equity markets beginning in the spring, led chiefly by cyclical stocks and small and mid caps. Equity market volatility, meanwhile, fell to record lows. Despite this, business slowed on Euronext Paris, where turnover and initial public offerings (IPOs) were down on 2002. There was a sharp upturn in capital increases, but this was largely attributable to a handful of very large issues. Fixed-income markets, which had provided a safe haven during the downturn, underwent a correction from mid-June onwards as the business climate brightened. On the derivatives markets, trading on Euronext Liffe remained stable, while Eurex, the Chicago Mercantile Exchange (CME), the Chicago Board of Trade (CBOT) and the Chicago Board Options Exchange (CBOE) all reported double-digit growth.

French financial markets were also affected by a number of regulatory changes, which are described in Part II on this chapter.

Table 1:
MAIN TRENDS IN FRENCH FINANCIAL MARKETS (EUR billion)

	1998	1999	2000	2001	2002	2003
Issuance						
. equity securities (1) *(listed companies)*	**11.7**	**9.3**	**21.5**	**9.2**	**15.1**	**22.8**
. debt securities	**105.1**	**161.6**	**168**	**85.6**	**91.4**	**122.7**
Other issuers (2)	*52.8*	*117.8*	*120.5*	*33.1*	*38.0*	*55.5*
Government	*52.3*	*43.8*	*47.5*	*52.5*	*53.4*	*67.2*
French equity and bond markets						
Capitalisation (year-end)						
. equities	838.9	1,493.2	1,541.0	1,319.0	927.8	1,075.0
. bonds and non-voting shares	760.3	763.0	779.1	795.1	818.0	809.0
Total (EUR billion)	**1,599.2**	**2,256.2**	**2,320.1**	**2,114.1**	**1,745.8**	**1,884.0**
Transaction value (year) (3)						
. equities				1,111.0	1,002.4	877.8
. bonds				7.5	7.0	6.3
Total (EUR billion)				**1,009.9**	**1,118.0**	**884.1**
Number of listed companies	**962**	**967**	**965**	**936**	**873**	**816**
Premier Marché	513	484	453	425	395	368
Second Marché	368	372	354	347	325	312
Nouveau Marché	81	111	158	164	153	137
Collective investment (SICAVs + FCPs) (4)						
. Assets under management at 31 Dec. (5)	534.1	651.5	766.0	800.2	803.0	908.0
. Number of SICAVs and FCPs at 31 Dec.	6,274	6,511	7,144	7,603	7,791	7,906

(1) Includes issues for cash + exercises of options + exercises of equity warrants + stock dividends + reserved issues
NB: Previous annual reports counted issues for cash only.
(2) Includes French and international issuance of debt securities (bonds + all complex debt securities, cf. Appendix I p XX).
(3) Electronic order book transactions. Due to methodological changes, data are available only from January 2001.
(4) SICAV = Open-end mutual fund; FCP = Unincorporated mutual fund.
(5) Calculated on the basis of the last reported asset value.

I – A year of stabilisation on financial markets

A – EQUITY MARKETS REBOUND IN 2003

1 – Market indices return to July 2002 levels

Equity markets staged a recovery in 2003, after the sharp three-year correction that followed the bursting of the tech bubble. The main indices made substantial gains, especially in the USA. The Dow Jones put on 25.3% and the NASDAQ rose by 50% (Table 2). Europe's indices enjoyed more modest success, with the FTSE100 advancing by 13.6% and the CAC 40 by 16.1%. The top-performing index was Germany's DAX, which gained 37.1% to end the year at nearly 4,000 points. This mainly reflected a catch-up movement after the correction of 2002, when the DAX lost 44% and came last in Europe. The Nikkei also rebounded, rising by 24.5%.

Table 2: Change in the main world stock market indices

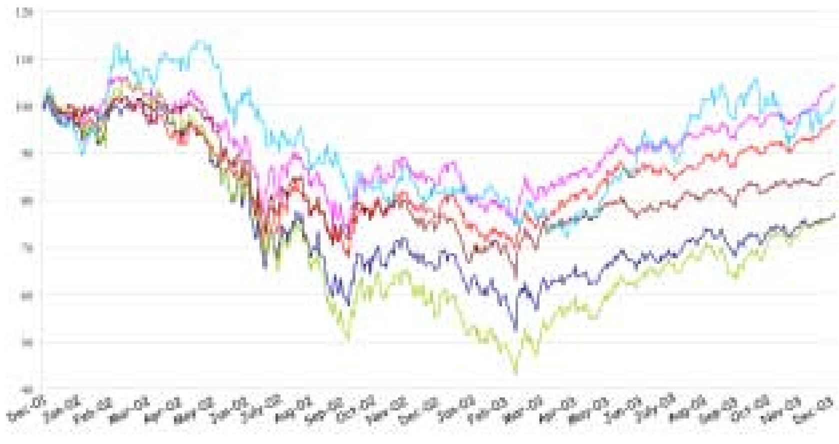
(Year-on-year change at year-end, %)

	CAC 40	DJ 30	NASDAQ.C	S&P 500	DAX 30	FTSE 100	MIB 30	Euro Stoxx 50	NIKKEI 225
2000	- 0.5	- 6.2	- 39.3	- 10.1	- 7.5	- 10.2	1.7	- 2.7	- 27.2
2001	- 22.0	- 7.1	- 21.1	- 13.0	- 19.8	- 16.2	- 26.2	- 20.2	- 23.5
2002	- 33.7	- 16.8	- 31.5	- 23.4	- 43.9	- 24.5	- 26.0	- 37.3	- 18.6
2003	16.1	25.3	50.0	26.4	37.1	13.6	11.8	15.7	24.5

National sources

By end-2003, the main indices had returned to their levels of July 2002 (Fig. 1).

Fig. 1: Main world stock market indices (31 December 2001 = 100)



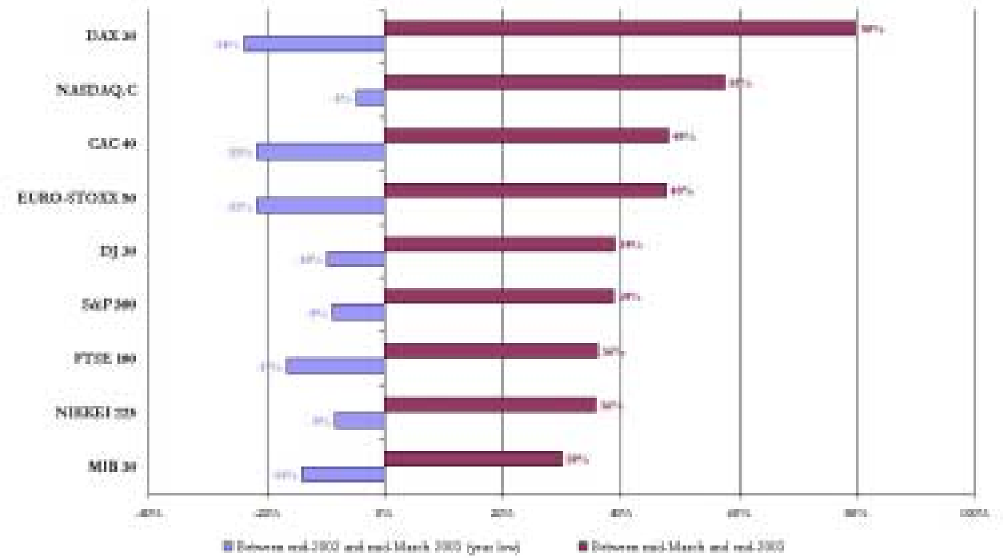
Source: Fininfo

a) The main stages of 2003: the rebound begins in the spring

Following on from late 2002, equity markets made a poor start to 2003, especially in Europe. Between early January and the low of 12 March 2003, the DAX and CAC 40 lost 24% and 21% respectively, while the main US indices gave up less than 10% and the Nikkei 7% (Fig. 2). By mid-March, the markets had hit historical lows, with the FTSE falling back to its level of August 1995, the DAX to its level of August 1996 and the CAC 40 to its level of April 1997. Volatility spikes also formed during this period. A combination of factors fuelled a mood of distrust towards stock markets in early 2003, including mounting geopolitical tensions in the lead-up to the Iraq conflict, uncertainties over the scope and strength of the US economic recovery, and a new spate of scandals adding to investors' doubts about the reliability of company accounts.

The trend then shifted into reverse. Equity markets were boosted by the toppling of Saddam Hussein's regime. Improving economic fundamentals in America also provided strong support, with signs of an upturn in activity, higher corporate profits and accommodative monetary and fiscal policies. The US markets began a strong rebound, pulling up the other exchanges in their wake. Between mid-March and end- 2003, the Dow Jones rose by 33.7%, ending the year just 10% off its record high in 2000. The Nikkei climbed 35.7%, although it was still 72% down on its 2000 high. The DJ Euro Stoxx 50 and the CAC 40 were both up by 48%, though both indices were also some 50% off their 2000 highs.

Fig. 2: The main stages of 2003



Source: Fininfo

b) The rebound was broad-based but varied in extent from region to region

In an economic context featuring firmer world growth, reduced geopolitical uncertainty and declining risk aversion from springtime onwards, equity prices rose across the board. However, the extent of the rebound varied from region to region. Measured by the Morgan Stanley Capital International (MSCI) indices in USD, equity markets worldwide rose by 30.8% in 2003. Emerging economies outperformed, climbing by 51.6%, compared with 29.9% in the developed countries (Table 3). Latin America and Eastern Europe did particularly well, putting on 67% and 57% respectively.

Table 3: MSCI Indices

(Annual % growth rate)

Geographical area	In local currency terms			In dollar terms		
	2001	2002	2003	2001	2002	2003
WORLD INDEX	**- 15.3**	**- 25.2**	**22.8**	**- 17.8**	**- 21.1**	**30.8**
Developed economies (G7)	**- 15.0**	**- 24.7**	**23.8**	**- 17.34**	**- 21.6**	**29.9**
North America	- 13.3	- 23.6	26.7	- 13.6	- 23.6	27.8
EFTA	- 17.5	- 27.5	17.4	- 22.6	- 17.5	35.3
Euro area	- 17.8	- 35.0	15.1	- 21.2	- 23.3	38.4
Europe	- 20.3	- 30.9	16.5	- 24.5	- 20.1	34.8
Pacific	- 17.1	- 18.3	19.7	- 26.2	- 10.4	36.3
o/w Far East (Japan, Hong Kong, Singapore)	*- 19.8*	*- 19.5*	*22.5*	*- 29.1*	*- 11.9*	*34.4*
Emerging economies	**5.1**	**- 9.1**	**42.3**	**- 4.9**	**- 8.0**	**51.6**
Asia	7.5	- 10.3	44.9	- 4.9	- 6.3	47.1
Far East (*o/w China, Indonesia, Thailand)*	12.8	- 11.6	43.0	9.5	- 7.1	44.5
Latin America	1.3	- 0.7	54.7	- 4.3	- 24.8	67.1
Middle East	-6.6	- 9.7	43.0	- 17.7	- 9.1	44.5
Eastern Europe	7.7	9.3	52.5	10.0	14.6	56.7

As in 2002, the US markets outperformed their main European counterparts. In local currency terms, the MSCI North America index rose by 26.7%, compared with just 15.1% for the MSCI euro area. However, currency effects were responsible for much of the outperformance: in dollar terms, European indices beat American indices. The dollar fell sharply in 2003 against the other main currencies, especially the euro and the yen. The euro/dollar reached a record high of 1.26 at end-December (Fig. 3). Meanwhile, the end of 2003 saw the dollar/yen return to its level of early 2001 despite repeated and large-scale intervention by the Bank of Japan on the currency market. The traditional determinants of exchange rate fluctuations failed to explain the movements in the euro/dollar exchange rate. The growth differential was largely in America's favour in 2003 and the yield spread between Europe and the USA narrowed in the second half. In fact, the dollar's slide in 2003 can be traced back to the USA's federal and current account deficits, which, at close to 5% of GDP, were well above the levels reached during the dollar's previous phases of depreciation in 1985 and 1995. Concerns over the sustainability of the US external deficit resurfaced in autumn when net capital inflows slowed.

Fig. 3: The dollar falls sharply in 2003

Source: Fininfo

The fact that European indices outperformed US indices in dollar terms should be seen in perspective, though, given that stocks in Europe suffered a series of severe corrections from Spring 2000 onwards.

c) Sector analysis: outperformance by cyclicals, especially tech stocks

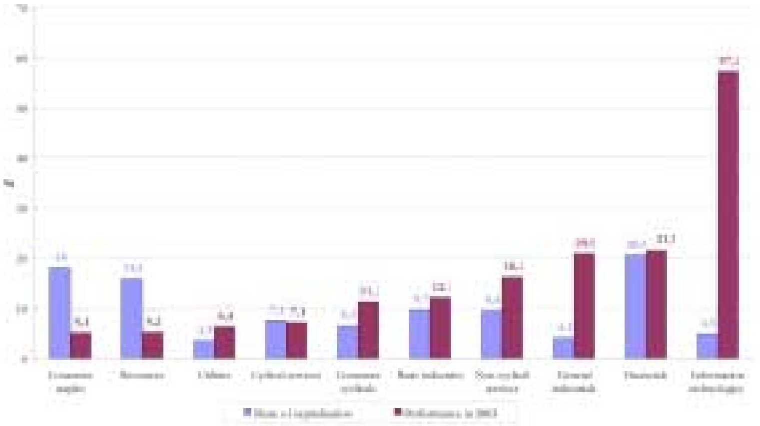
While all sectors benefited from the market rebound, cyclicals, and especially technology stocks, put in the best showing, buoyed by the economic upturn (Fig. 4). The stock market recovery was actually a correction of past falls, and tech and finance stocks had considerable upside after being hardest hit by the market crisis of 2001 and 2002.

Fig. 4: Catch-up effect as TMT stocks rebound

Source: MSCI

Climbing 57.16%, information technologies recorded the biggest increase on the CAC 40, followed by financials with 21.5%. Consumer staples and utilities, by contrast, posted far more modest gains, advancing by less than 5% (Fig. 5).

Fig. 5: Composition of the CAC 40: performance and share of total market capitalisation in 2003 (%)



Source: Euronext-Paris

d) Small and mid caps lead the market rebound in France

Small and mid cap indices – with the notable exception of the Nouveau Marché – show clearly that these stocks enjoyed stronger appeal than large caps last year (Fig. 6). Mid caps received support from a series of factors in 2003. First, cyclicals dominate the mid cap indices. Second, mid caps are less sensitive to dollar depreciation because they are more dependent on the domestic market. Third, mid caps were undervalued relative to large caps in 2003.

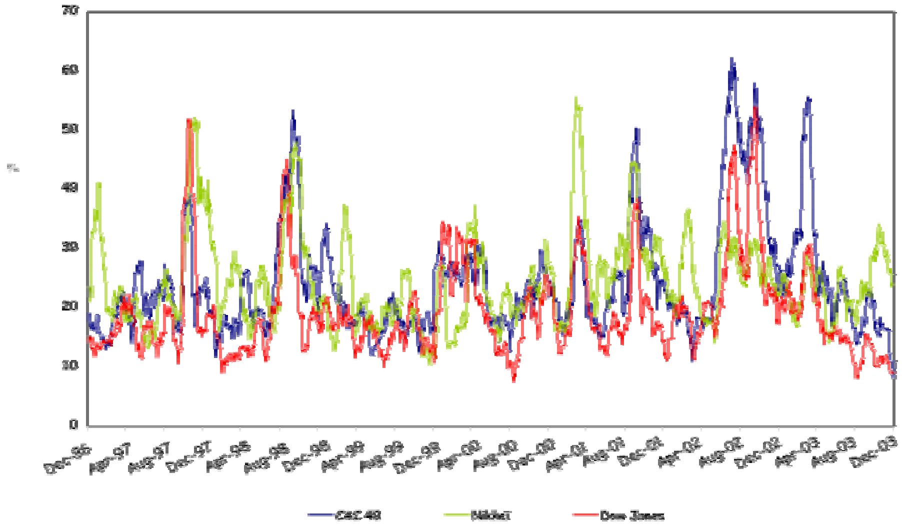
Fig. 6: Mid cap indices in 2003 (31 December 2002 = 100)

Source: Euronext Paris

e) Market volatility falls back to medium-term levels

After reaching record highs in 2002, stock market volatility eased considerably last year, returning to medium-term levels. Historical volatility on the CAC 40 and DJIA peaked in Spring 2003 on persistent economic and geostrategic uncertainties, but then fell back to historic lows by year's end (Fig. 7).

Fig. 7: Historical volatility (20-day) in 2003



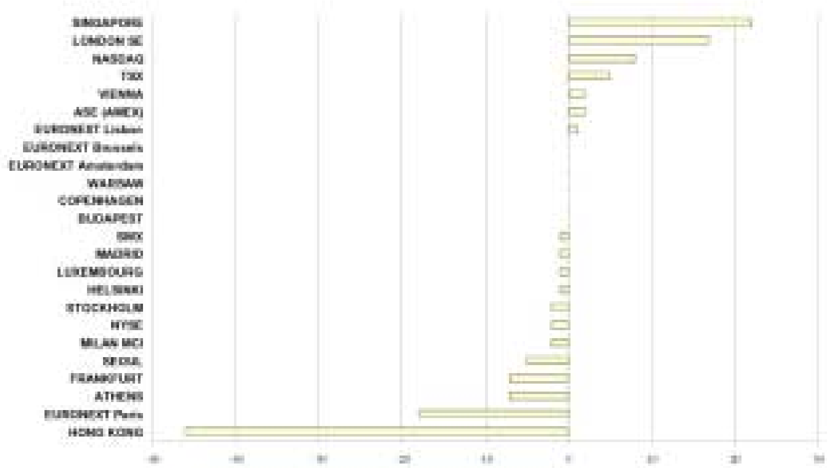
Source: Fininfo

2 –Equity market activity

a) Ongoing decline in the number of listed companies

IPO activity was sluggish in most financial centres in 2003. The situation was particularly worrisome in Europe, especially in Paris and Frankfurt (Fig. 8).

Fig. 8: Change in the number of IPOs between 2002 and 2003 on the main stock exchanges



Source: Fininfo

In France, there were fewer IPOs on Euronext Paris in 2003 than in 2002. Excluding exchange traded funds (ETFs) there were just three new listings on the regulated markets, compared with 11 the previous year. On the Marché Libre, there were 14 IPOs, after 23 in 2002 (Table 4), and there were no new listings on the Nouveau Marché or the Second Marché[1]. The ETF segment also experienced a slowdown, with six new listings in 2003 compared with 11 in 2002.

Table 4: New listings on regulated markets and Marché Libre of Euronext Paris (not counting ETFs or transfers)

	Premier Marché	**Second Marché**	**Nouveau Marché**	**Total, regulated markets**	**Marché Libre**	**TOTAL**
2000	16	16	49	**81**	55	**136**
2001	11	9	9	**29**	36	**65**
2002	2	7	2	**11**	23	**34**
2003	3	0	0	**3**	14	**17**

Source: Euronext Paris

As a result, following the delistings in 2003, the number of companies listed on regulated markets continued to decline, except in Japan (Table 5)[2].

Table 5: Number of listed companies on regulated markets, year-end data

	2002	**2003**			**Change**
	Total	**Total**	Domestic	Foreign	**2003/2002**
NASDAQ	3,649	**3,294**	2,951	343	**-9.7%**
NYSE	2,366	**2,308**	1,842	466	**-2.5%**
Deutsche Börse	934	**866**	684	182	**-7.3%**
Euronext	1,484	**1,392**	1,047	345	**-6.2%**
Borsa Italiana	294	**279**	271	8	**-5.1%**
London	2,824	**2,692**	2,311	381	**-4.7%**
Tokyo	2,153	**2,206**	2,174	32	**2.5%**

Source: World Federation of Exchanges

There were 817 companies listed on regulated markets in France in 2003, compared with 873 in 2002 (Table 6).

Table 6: Number of companies listed on Euronext Paris

	Premier Marché	Second Marché	Nouveau Marché	Total, regulated markets	Marché Libre	Total
Dec. 2000	453	354	158	965	218	1,183
Dec. 2001	425	347	164	936	239	1,175
Dec. 2002	395	325	153	873	258	1,131
Dec. 2003	368	312	137	817	254	1,071

Source: Euronext Paris/AMF

b) Upturn in market capitalisations

[1] The only new listings on the Second Marché were transfers from the Marché Libre.

[2] In France, most of the delistings (63 in 2003) were caused by squeeze-outs and, to a lesser extent, liquidations.

As share prices rebounded, the market capitalisation of the main stock exchanges increased, even though the number of listed companies continued to fall (Table 7).

Table 7: World ranking, market capitalisation of domestic equities at end-2003

Ranking	Exchange	Capitalisation (USD billion)	2003/2002 (%)
1	NYSE	11,329.0	26%
2	Tokyo	2,953.1	43%
3	NASDAQ	2,844.2	43%
4	London	2,425.8	36%
5	Euronext	2,076.4	35%
	-o/w Euronext Paris	*1,356.0*	*40%*
6	Deutsche Börse	1,079.0	57%
7	TSX Group	910.2	57%
8	Swiss Exchange	727.1	33%
9	Spanish Exchanges (BME)	726.2	57%
10	Hong Kong	714.6	54%
11	Borsa Italiana	614.8	29%

Source: World Federation of Exchanges

The upturn in capitalisation pushed up the market cap.-to-GDP ratio in the main developed countries. Measured by the size of its financial market, France occupies an intermediary position, well ahead of Japan and Germany, but far behind the UK and the USA (Table 8).

Table 8: Market capitalisation-to-GDP ratio

	1995	1999	2002	2003
UK	98%	195%	114%	**148%**
USA	78%	181%	106%	**134%**
France	35%	104%	68%	**93%**
Japan	81%	100%	52%	**74%**
Germany	28%	68%	35%	**54%**

National sources / World Federation of Exchanges

c) Equity issuance rose on Euronext Paris, but was concentrated in a handful of deals

According to estimates by Thomson Financial, equity issuance worldwide (excluding listed equity-related securities) climbed by 6% in 2003 to USD 220 billion, of which USD 79 billion in the USA and USD 52 billion in Europe.

Equity issuance on the Paris regulated markets rose strongly in 2003, amounting to almost EUR 23 billion, up 52% on 2002 and slightly higher than in 2000 (Table 9). As a comparison, total issuance in Europe was EUR 110 billion, according to Dealogic, a market information provider.

However, the number of issues fell 6%, with the result that the average size of each issue rose.

Table 9: Issuance of equity securities on the regulated markets of Euronext Paris

(EUR million)	2000	2001	2002	2003		
	Total	Total	Total	Total	% change	% of total
Regulated markets	21,323.7	9,035.9	15,032.2	22,840.7	52%	100%
Cash capital increase	11,508.3	2,938.7	3,204.5	4,154.9	30%	18%
Rights issues to staff	3,681.2	2,416.7	3,833.8	1,734.9	-55%	8%
Other reserved issues	1,516.6	75.0	4,134.8	49.0	-99%	0%
Stock dividends	339.6	316.0	972.7	339.8	-65%	1%
Exercises of equity warrants	745.0	1,979.9	1,965.4	15,631.7	700%	69%
Exercises of options	3,532.9	1,309.6	921.1	930.4	1%	4%

Source: Euronext Paris/AMF

However, this overall increase concealed differences according to the type of issue. Capital increases for cash were up 30%, while brisk growth in issuance from exercises of equity warrants had a particularly strong impact on the overall result. The France Télécom capital increase was key in this regard, accounting for 68% of the total amount issued in 2003. Reserved issues, by contrast, registered a steep decline. After their strong rise in 2002, they made up just 8% of the total amount issued in 2003.

Equity issuance was highly concentrated in 2003, with the five biggest deals accounting for over 80% of the amount issued in the year.

Furthermore, while issuance was up sharply on the Premier Marché, it contracted by 66% on the Second Marché and by 12% on the Nouveau Marché (Table 10).

Table 10: Equity security issuance, by market (EUR million)

	2000	2001	2002	2003	%
Premier Marché	17,420.3	8,119.5	13,824.9	22,331.8	62%
Second Marché	871.5	406.1	1,010.9	336.2	-66%
Nouveau Marché	3,032.0	510.3	196.4	172.7	-12%
Total, regulated markets	21,323.7	9,036.0	15,032.3	22,840.7	52%

Source: Euronext Paris/AMF

In all, net financing of the economy by the stock market was positive in 2003 at around EUR 13.8 billion: share buybacks amounted to some EUR 9 billion, compared with EUR 22.8 billion in gross equity issuance.

d) Trading volumes

Despite the market rebound, turnover was down on most exchanges in 2003 (Table 11).

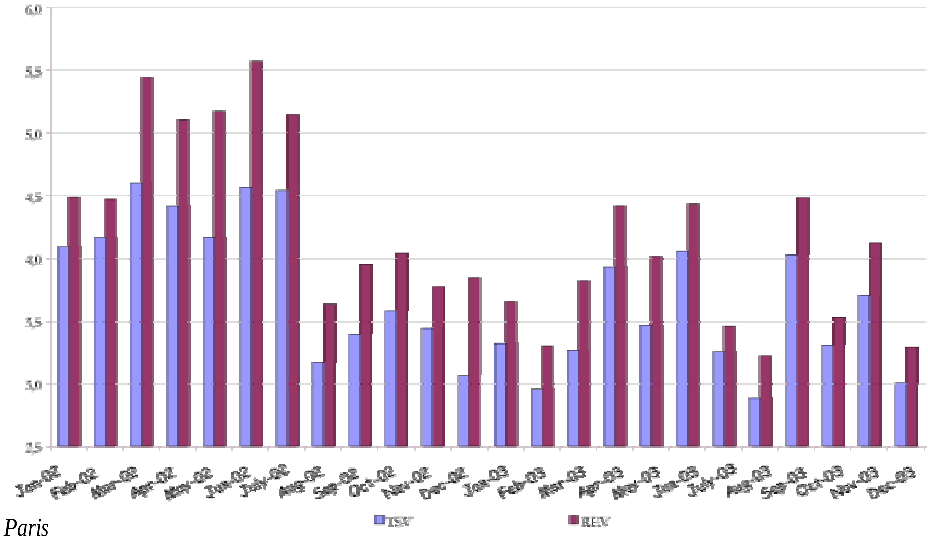
Table 11: Trading volumes in 2003 (EUR billion) [3]

	2002		2003		Change 03/02	
(EUR billion)	REV	TSV	REV	TSV	REV	TSV
NYSE		11,015.7		8,506.3		-22.8%
NASDAQ	7,709.2		5,920.5		-23.2%	
Tokyo		1,573.7		1,858.7		18.1%
London	4,227.0		3,273.4		-22.6%	
Euronext		1,574.3		1,359.4		-13.7%
Deutsche Börse		876.2		833.0		-4.9%
Swiss Exchange	650.8		541.6		-16.8%	
Spanish Exchange (BME)	628.9		820.5		30.5%	
Italian Exchange		688.8		667.0		-3.2%

Source: IEM Finance

In Paris, equity transactions handled by the central trading system, NSC, fell by 12% to EUR 878 billion, compared with EUR 1,002 billion in 2002. Although average daily turnover came out at EUR 3.8 billion, the pattern was relatively mixed over the year, with daily turnover falling from EUR 4.4 billion in April to EUR 3.3 billion in December (Fig. 9).

Fig. 9: Daily transaction value on Euronext Paris

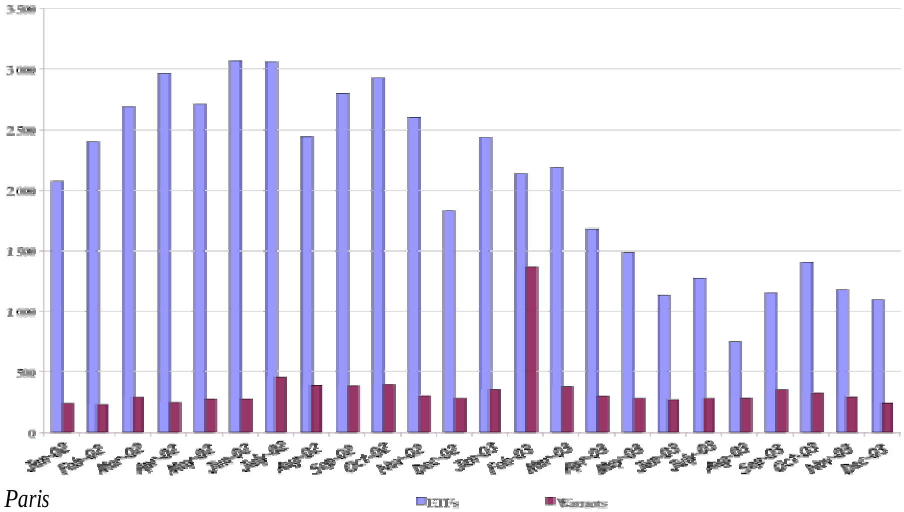


Source: Euronext Paris

[3] Because the markets have never managed to harmonise their trading statistics, the data should be compared with caution.
Exchanges use one of two approaches to compile trading statistics:
The Trading System View (TSV) counts only those transactions made directly through trading systems or floor trading;
The Regulated Environment View (REV) counts transactions included either in disclosures made by intermediaries to the market authority or in final settlement transactions performed by the subsystems.

Unlike in 2002, and in contrast with other European markets, the ETF segment posted one of the biggest contractions in 2003. Average daily turnover returned to 2001 levels, slipping from EUR 138 million in 2002 to EUR 90 million in 2003 (Fig. 10). Over the year as a whole, the aggregate value of these transactions totalled more than EUR 18 billion, down from EUR 31.6 billion in 2002. Robust equity markets had a highly positive impact on the market for warrants, more than 90% of which still consist of calls. Warrant trading volumes rose by 25% in 2003.

Fig. 10: ETF and warrant trading on Euronext Paris (EUR million)



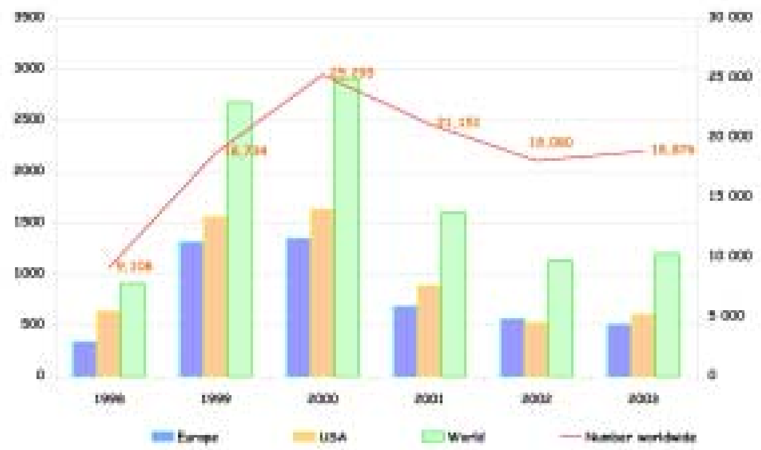
Source: Euronext Paris

e) Could the M&A downtrend be over?

Under way since 2000, the downtrend in the number of mergers and acquisitions (M&A) came to a halt in 2003 (Fig. 11). Aggregate M&A activity in 2003 rose to USD 1,200 billion worldwide, a 5% increase on 2002, though still well below the record USD 2,900 billion reached in 2000. The number of M&A deals completed worldwide increased by 4% from 18,080 in 2002 to 18,876 in 2003.
Although M&A activity stabilised worldwide, not all sectors of activity and geographical areas were affected identically.

The USA recorded a 14% increase in the aggregate value of M&A activity to USD 606 billion, while Europe posted a decline of 9.8% to EUR 510 billion. Europe captured 42.5% of the worldwide market in 2003, compared with the USA's 50.4%.

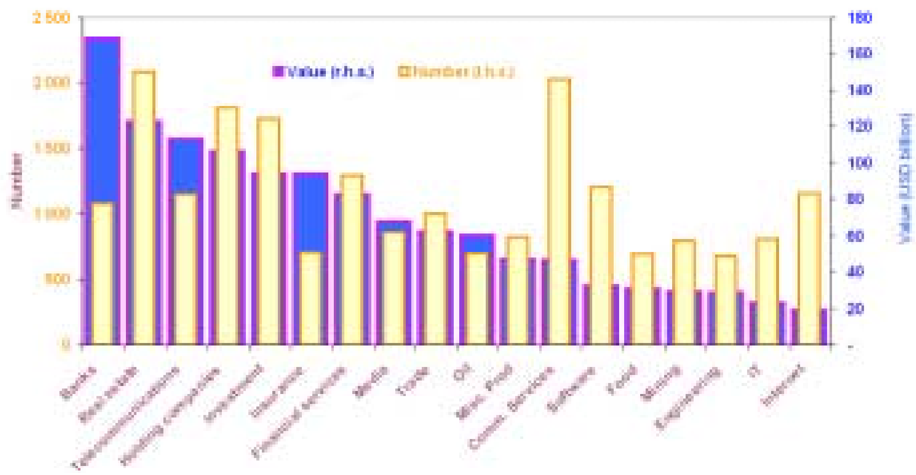
Fig. 11: Number and aggregate value of mergers and acquisitions



Source: Bloomberg

In terms of the aggregate value of worldwide M&A dealflow (Fig. 12), by far the leading sectors were banking with USD 166.8 billion, real estate with USD 120 billion, and telecommunications with USD 112 billion. M&A activity in insurance and financial services came to under USD 100 billion.

Fig. 12: Number and aggregate value of mergers and acquisitions worldwide, by sector



Source: Bloomberg

There were 69 public tender offers in France in 2003, fewer than in 2001 (95) or 2002 (87). In addition, their aggregate value decreased by 10%[4]. However, these data conceal disparities by transaction type:

- The biggest public tender offer of the year, and the third biggest worldwide (Table 12), was Crédit Agricole's combined cash and share offer for Crédit Lyonnais. At over EUR 4 billion[5], this dwarfed the next largest deal, Origny Naples SAS's combined cash and share offer for Beghin Say, worth almost EUR 396 million.
- The number of tender offers under simplified and standard procedures and standing offers fell sharply, from 38 to 24. Overall, though, their aggregate value declined by just 9% thanks to the Crédit Lyonnais/Crédit Agricole tie-up. As a result, the average bid size remained broadly stable, slipping from EUR 239 million to EUR 235 million.
- The number of all-share offers rose from three in 2002 to six in 2003 (compared with 14 in 2001).
- The aggregate value of mandatory buyout offers was down 57%, even though there were nine buyouts in 2003, compared with four in 2002.

Table 12: The ten largest acquisitions worldwide in 2003

Announced	Completed	Target company/Country	Acquiring company/Country	Amount (USD billion)
July 02	April 03	Pharmacia Corp/ USA	Pfizer Inc/USA	64,263.9
March 03	Aug. 03	Telecom Italia SPA/Old/ Italy	Telecom Italia SPA/ Italy	28,023.0
Dec. 02	June 03	Crédit Lyonnais SA/France	Crédit Agricole SA/France	16,636.6
June 03	Aug. 03	Resona Holdings Inc/ Japan	State/ Japan	16,635.4
Nov. 02	March 03	Household Intl Inc/ USA	HSBC Holdings PLC/UK	15,511.2
April 03	Oct. 03	Sibneft/ Russia	Yukos/ Russia	10,519.9
May 03	June 03	D/S 1912 -B-/ Denmark	A P Moller - Maersk A/S/Denmark	9,177.8
March 02	March 03	Sonera Oyj/Finland	Teliasonera AB/Switzerland	8,649.2
Dec. 01	April 03	Carnival PLC/UK	Carnival Corp/USA	8,168.4
Nov. 02	Feb. 03	Autostrade SPA/Old/Italy	Autostrade SPA/Italy	7,627.6
Sept. 01	Jan. 03	American Water Works Co Inc/ USA	RWE AG/Germany	7,495.5

Source: Bloomberg

B – FIXED-INCOME MARKETS

1 – The market rebound lessened the appeal of government bonds from the spring onwards

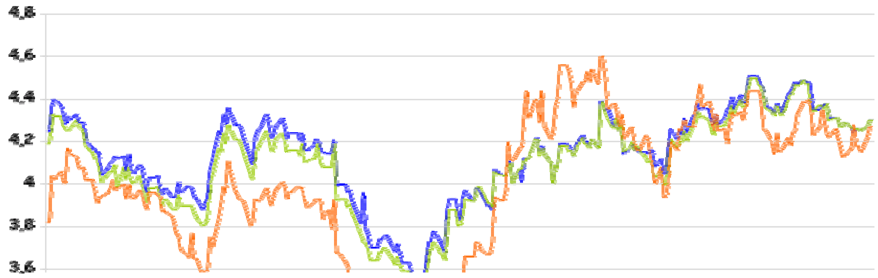
In 2001 and 2002, government bonds offered a safe haven to investors as equity markets collapsed, world growth slowed and monetary policies were loosened. In 2003, governments held up well amid the market rebound and economic recovery, although there were considerable intra-year fluctuations (Fig. 13). Over the first half-year, against the backdrop of an ongoing stock market correction and the introduction of highly accommodative monetary policies, bonds acted as a safe haven and benefited from a flight to quality and security. Government bond yields eased sharply to reach historically low levels by mid-June – around 3% for the 10-year T-Bond. An abrupt correction

[4] Offers whose results were published in 2003.

[5] The COB's statistics are based on traditional methodology, which does not value share exchange offers. However, for the purposes of cross-country comparisons, information providers value all-share offers at the opening price, i.e. EUR 12 billion in the case of the Crédit Agricole/Crédit Lyonnais tie-up.

followed over the summer, prompted by the improving economic climate and expectations of monetary tightening. By end-December, yields had returned to the levels of early 2003, i.e. around 4.20%.

Fig. 13: Contrasting intra-year trends in government bond yields



National sources

Unlike equity markets, bond markets remained highly volatile in 2003. This was especially true in the first quarter, when the stock market correction was still under way (Fig. 14). Bond market volatility spiked several times in the first half, notably in response to measures by central banks. Aside from the influence of interest rate cuts, the fixed-income markets reacted to the Fed's talk of using unconventional policy measures via purchases of government bonds. Bond volatility lessened in the second half, but remained at sustained levels.

Fig. 14: Bond market volatility was high in 2003

Source: Fininfo, AMF calculations