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The Milan Bourse is a wager

Managers divided over the future

BTPs attracting greater confidence

by Andrea Gennai

The question is simple, and affects the average investor very closely. In a globalised financial world, how much "Italy" should they include in their portfolios, on both the equity and the bond side? The world of bonds is strongly influenced by zero yields and central banks manoeuvres. The question of equity seems less complex, and here Milan is feeling the effects of a difficult decade. Credit Suisse has analysed the "weight" of Italian stocks: they currently represent 6.81% of the MSCI EMU index (euro area) and 0.77% of the MSCI World index. Ten years ago, the figures were 11.67% and 1.8% respectively. Over the decade, the proportion has halved and this has a strong impact on the decisions of major – and other – investors.

As Francesco Fonzi, strategist at Credit Suisse, explains, "our bank is more heavily weighted on the euro area but we're under-weighted on Italy. We prefer situations like France. In Italy there are too many political uncertainties and the economic picture shows marked contrasts. On the bonds side we're more constructive and have a significant presence of BTPs [Italian government bonds] in our portfolio; the spread ensures at least a minimum return, which has become the preserve of just a few peripheral products".

The stock market is feeling the distortive effect of financial products, which alone represent 34% of the list. This means that the valuation of these sectors seems to have a higher "weight" with respect to the real economy. In Fonzi's view, "Italy is still a work in progress and it will be important to understand what happens in October, with the constitutional referendum. Another problem that remains to be solved is growth, which isn't recovering".

At Allianz Global Investors, they're more optimistic. According to Massimiliano Maxia, fixed income product specialist, "the stock market has recently been penalised by the presence of financial sector securities but we believe that there are companies with excellent fundamentals in other sectors. Selecting the right securities is therefore the key element of any investment: in the portfolio as a whole we reckon 3-5% is appropriate. As for the bond market, Italian government bonds in the euro area still offer interesting returns, especially for longer maturities and if compared with other countries' bond products. In a global portfolio we can allocate about 10%".

The wager on Italy strongly depends on solving the banks' problems. As Luca Riboldi, chief investment officer at Banor SIM, comments, "what has happened in this first part of 2016 is exemplary. Wall Street is up 2% since the start of the year in dollars and practically zero in euro. In Italy, if we disregard the just under 40% of financial products in the index, we obtain the same performance, i.e. zero. It's clear that it's the financial products that are weighing on the entire index in Milan. I think that the solution to the senior management issue at UniCredit, the probable capital increase, and a solution for MPS, will mean that the major problems of the Italian banking system have been solved and we'll be able to make a clean start. Our inclination is to go heavy on Europe. We think that for the average retail client the weighting for Italy should be about 20% in a portfolio concentrating on Europe, and 2 or 3% in a global portfolio".

There is no lack of questions still to be solved, including at the economic level. "The Italian stock market", says Giuseppe Sersale, strategist at Anthilia Capital Partners, "is still weighed down by a series of structural problems, including a stagnant economy, an overly high tax burden and excessive red tape, which doesn't favour investment. To all of that we can add the high proportion of financial products in the index, which affects its performance. Before structurally increasing their weight in Italian equity, I'd wait for signals, for example the result of the constitutional referendum in October. That said, in the short term a number of factors can act to the advantage of Italian assets, such as the new TLTRO operations which the ECB is about to launch and which should favour, in particular, Europe's peripheral countries and their banks".

ITALY'S ROLE ON THE STOCK MARKETS

0.77%: ITALY'S WEIGHT IN MSCI WORLD

The weight of the Italian stock market on the MSCI World index has fallen to 0.77%. Ten years ago it represented 1.8%. Then, after the 2007 crisis, and then the debt crisis in 2011, the Italian bourse gradually lost ground with respect to the other global stock markets. The strong incidence of financial securities (now around 34%), which weighed down the list as a whole in a period of major tensions for the entire segment, played a decisive role.