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European stock markets in the front line. No vacation for profits.

Positive expectations for stock markets continue into the second half of the year. Surprise from the emerging markets.

by Sergio Carlin

2017 has been a very positive year so far for global stock markets. And according to managers, securities listings will continue to perform well in the coming six months, especially in Europe and in the emerging markets. Since January, the MSCI World index has gained over 11%, adding a further seven months of rises to a long cycle lasting since March 2009: the second most prolonged since the Second World War. Confidence in the international outlook for growth, the increase in company profits in all the major regions of the planet, expectations of a moderate resumption of inflation and over 1,000 billion dollars of quantitative easing (QE) injected throughout the globe since early 2017 have fuelled the stock exchange's lively performance.

The outlook

In the analysts' year-end reports for 2016 – thanks not least to the expansionary policy of the White House – the main bull market players were Wall Street and the bourses of Europe and Japan. Over the last six months the New York Stock Exchange (NYSE) may have lost the impetus of Trump's reflation trading. But it is now benefiting from the healthy results of American companies and investors betting on a less severe credit squeeze by the Fed than expected. It has lived up to expectations and continues to reach new record levels (+9.97% for S&P500 in mid-July), and in certain respects the stakes are getting higher. Europe and Tokyo have also done well (+6.61% for the Msci Europe and +5,26% for the Nikkei). But the real suprise, after the large-scale flight of capital in 2014-15, has been the recovery of the emerging markets. In less than seven months, thanks to the improvements in the outlook for the Chinese economy, the bounce-back by commodities and the struggling dollar, the MSCI EM index has climbed by about 21.5%, raising its capitalisation by nearly 890 billion euro.

The outlook

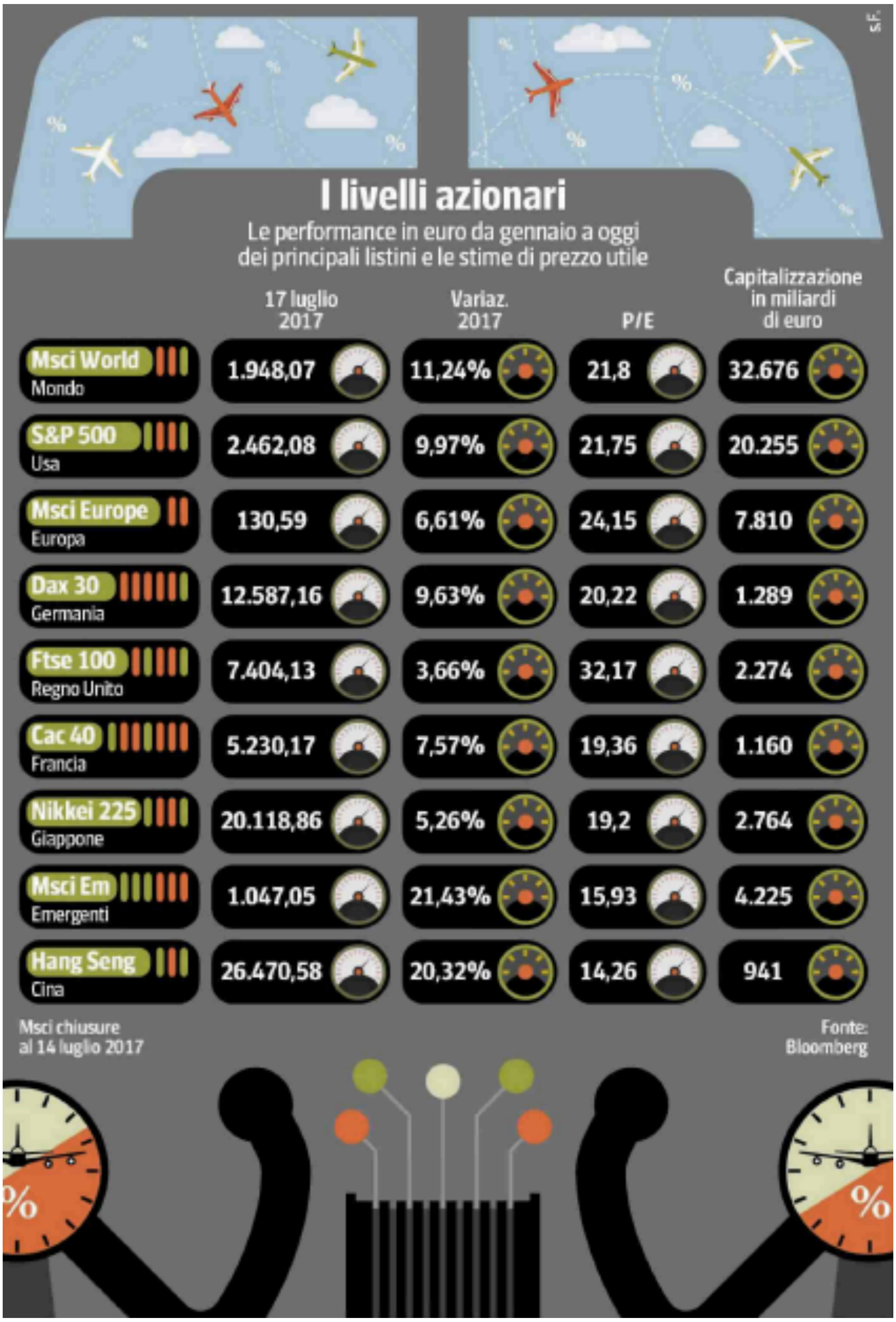
What will happen in the next six months? Will Wall Street continue to be bullish or will it give way to the feared adjustment? Most analysts are optimistic. If volatility too were to rise, however, that could provide excellent entry opportunities, with further rises in returns by the end of the year. In Europe in particular, where most fund managers are placing their bets, the structural framework will not change. The fuel will again be economic growth, better distributed than in the past, together with increased profits per share, which in the emerging markets will reach peaks of 20-25%. “The EU market is more interesting in terms of balance sheet results and potential returns, especially after the feared political outcomes didn’t materialise”, explains the shares team at Fidelity. “The moves in European profits are all in steadily positive territory and projections exceed those for the USA, including for growth in earnings”.

Lewis Grant, global equities portfolio manager at Hermes IM, also takes a more favourable view of investment in European stock markets. “Growth will be driven by consumption”, he predicts.

Grant advises investors to include European stocks like Adidas in their portfolios, along with shares which, after the Paris agreements, will benefit from the impetus provided by environmental sustainability measures. Three names come to the fore: Sweden’s Volvo, Spain’s Gamesa and Denmark’s Dong Energy. More prudent, in that he doesn’t expect “major movement on the absolute value of the indices, but varying sectoral dynamics”, is Angelo Meda, head of equities at Banor. Like many others, and in a climate of increasing deregulation, Banor’s asset manager advises investors to select US financial corporations like Goldman Sachs, a stock that at present is under-valued, and European oil companies like Total and Eni. The latter will benefit from a stabilisation of the price of crude at around 50 dollars. The analysts at Morgan Stanley, on the other hand, are keeping their focus on the East, predicting rises for Japan, which they view more favourably than Europe. In their view, a resumption of inflation and the propulsion effect of exports will underpin listings on the Nikkei.

Share levels.

Performance in euro since January 2017 of the main securities listings and price/earnings estimates



MSCI at close on 14 July 2017

Source: Bloomberg