Confidence must be earned

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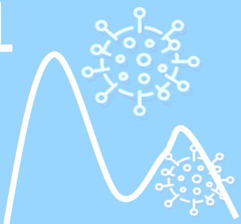
Time to play a cyclical recovery in European equity

Investment Insights | Market Stories

Five themes supporting European equities

1



Pandemic under control

Europe **is ahead in the virus cycle**: the most acute phase of the crisis is over, contagion curve has flattened.

2

Cyclical recovery underway

After the lockdown, **high frequency economic indicators have posted a strong rebound**. Europe should lead GDP growth in 2021 among DM.

3

Benign fiscal and monetary conditions

Europe is in a new phase, with **the end of fiscal austerity** and massive monetary support that is gradually transferring to the real economy.

4

Easing geopolitical risk/ Recovery Fund

The geopolitical risk that has been one of the causes of underperformance of EU equities **should fade**. The approval of the Recovery Fund could benefit EU equities in relative terms.

5

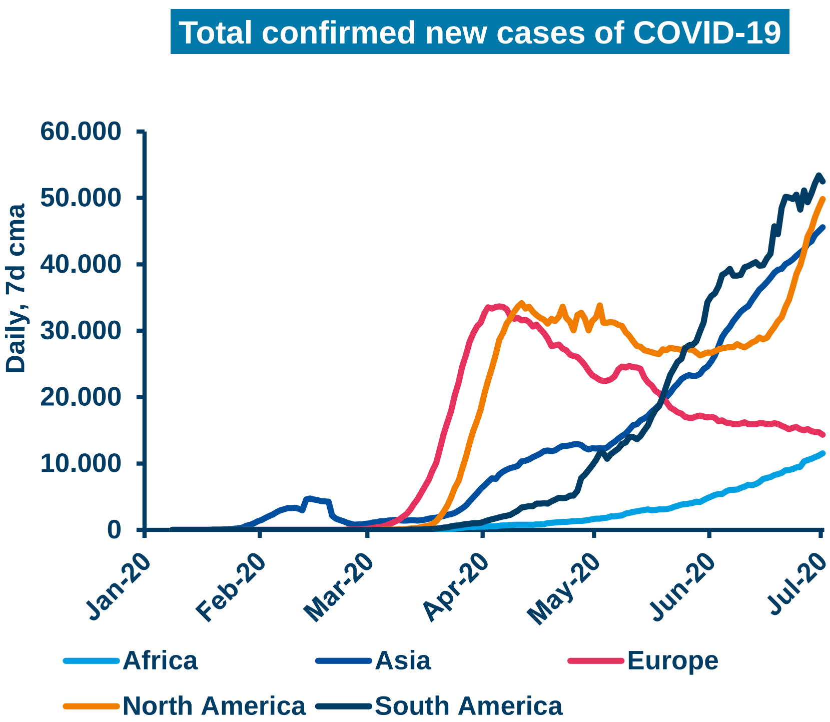
A more attractive market

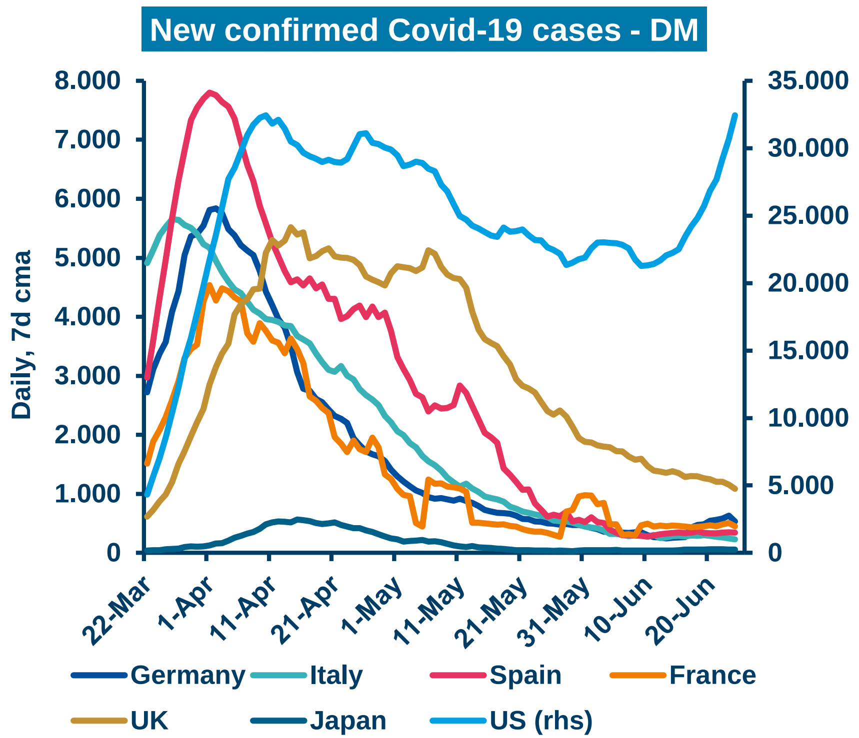
The EU markets has transformed and **the weight of most challenged sectors has reduced in favour of the most dynamic part** of the economy.

» Cyclical conditions are turning more positive for Europe. Easing geopolitical risk and the prospect of massive fiscal resources (national and EU-wide) and monetary support could support a recovery in 2021. The improved sentiment could benefit European assets, equities in particular, that have been a laggard due to the pandemic. This could lead to a catch up of EU equities in relative terms vs other markets.

Source : Amundi, as of 30 June 2020.

Covid-19 situation in Europe is under control





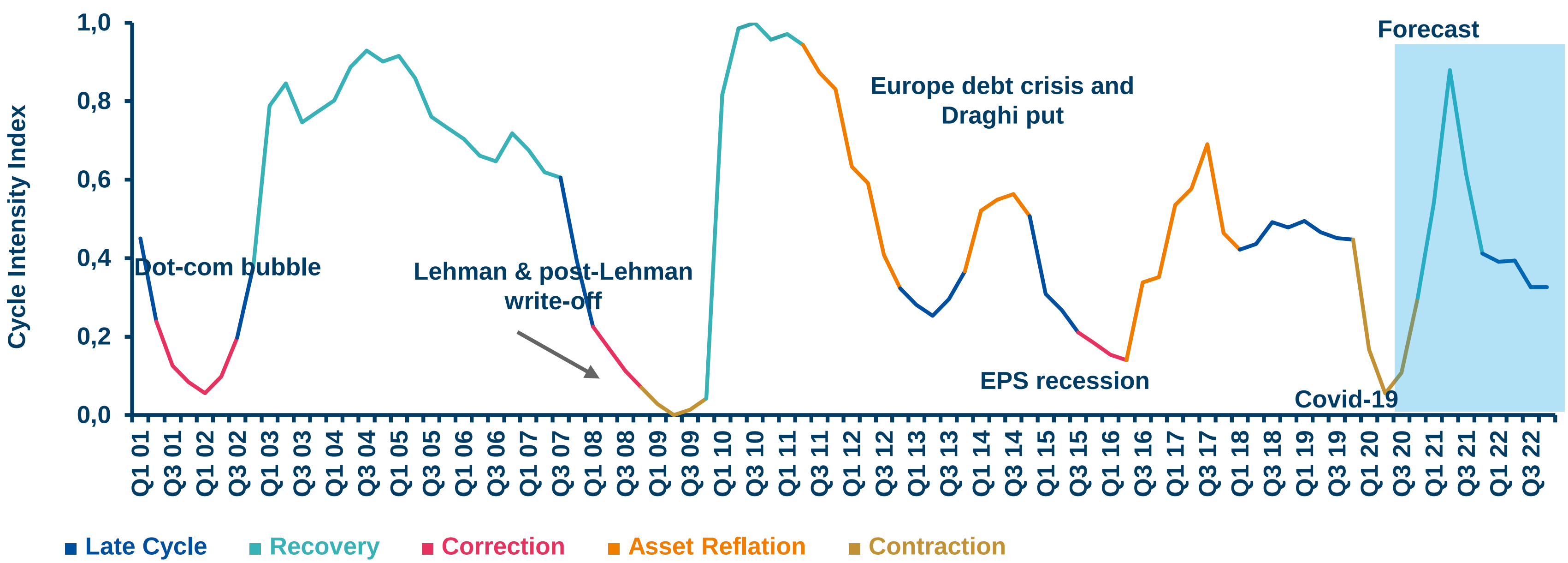
Compared to the rest of the world, infection rate in European countries fell. Most European countries have already reinforced their healthcare systems and policies to fight a possible second wave that we expect to be more contained vs the first one.

Source: Amundi elaborations on Worldometers data. As of 1 July 2020.

Source: Amundi elaborations on Worldometers data. As of 24 June 2020.

After a strong contraction, we expect a recovery in the economic cycle

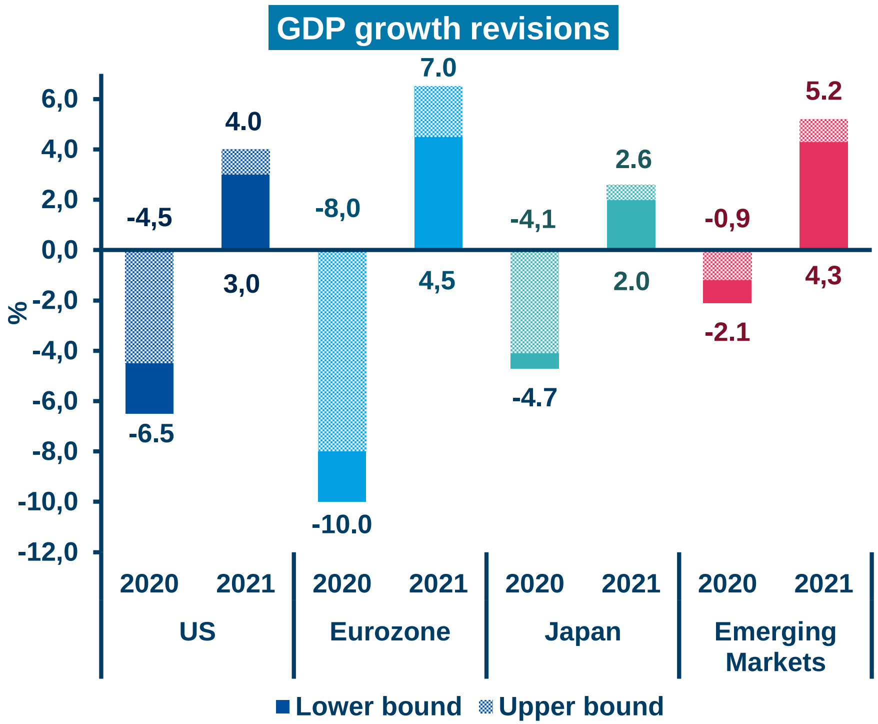
Advanced Investment Phazer: A contraction followed by a recovery recovery

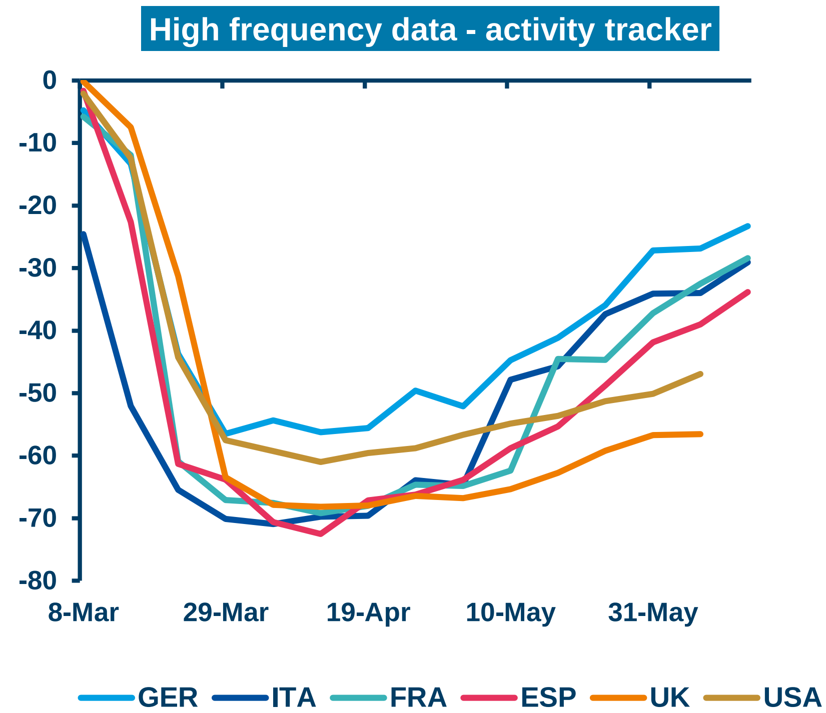


Our current base scenario foresees a deep recession, massive support from central banks and governments and rising unemployment. A subsequent gradual recovery from the H1 2020 economic freeze would see activity retracing at varying speeds across different regions.

Source: Amundi Research as of 29 May 2020. Advanced Investment Phazer.

A recovery already started





Some signs of economic recovery are already visible in the PMI and in high frequency data. According to our estimates, Europe should witness the highest rate of growth in 2021, and 2020 bad numbers should be already priced in the market.

Source: Amundi Research as 30 June 2020. Proprietary indicator including Covid new cases, Lockdown stringency index, travel to retail and leisure, travel to workplace, travel to transport stations, restaurant reservation, Airlines passengers, UK cargo ships and tankers. WEI Fred eco activity, a composite of 10 weekly economic indicators: Redbook same-store sales.

Source: Amundi Research, GDP growth forecast estimates as of 18 June 2020.

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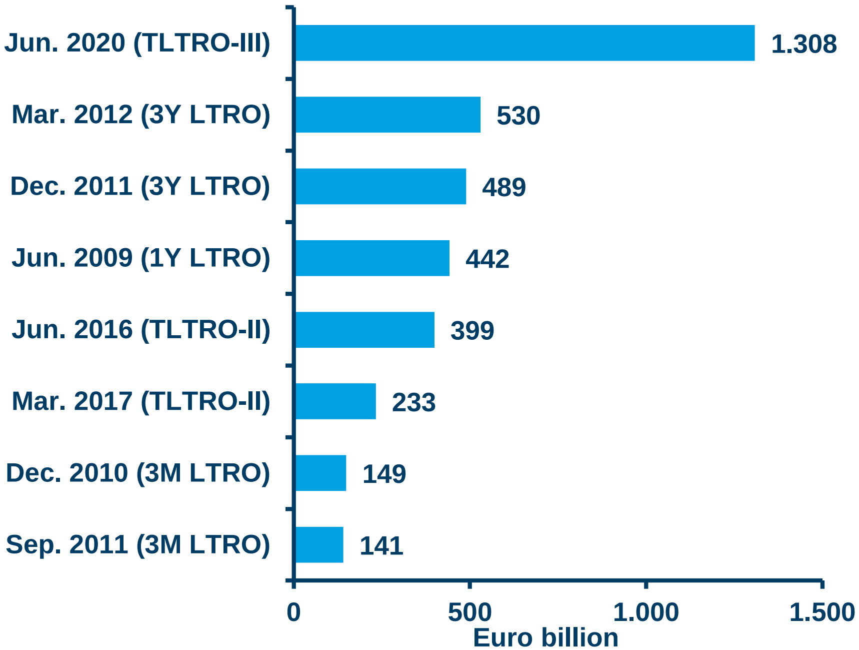
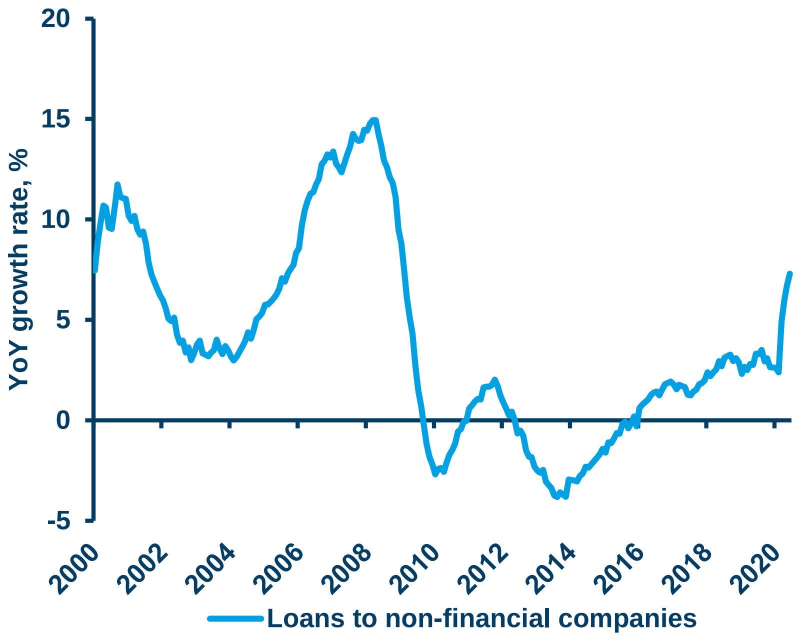
ECB support is benefitting the real economy

ECB's Longer-Term Refinancing Operations



Euro-area corporate loans

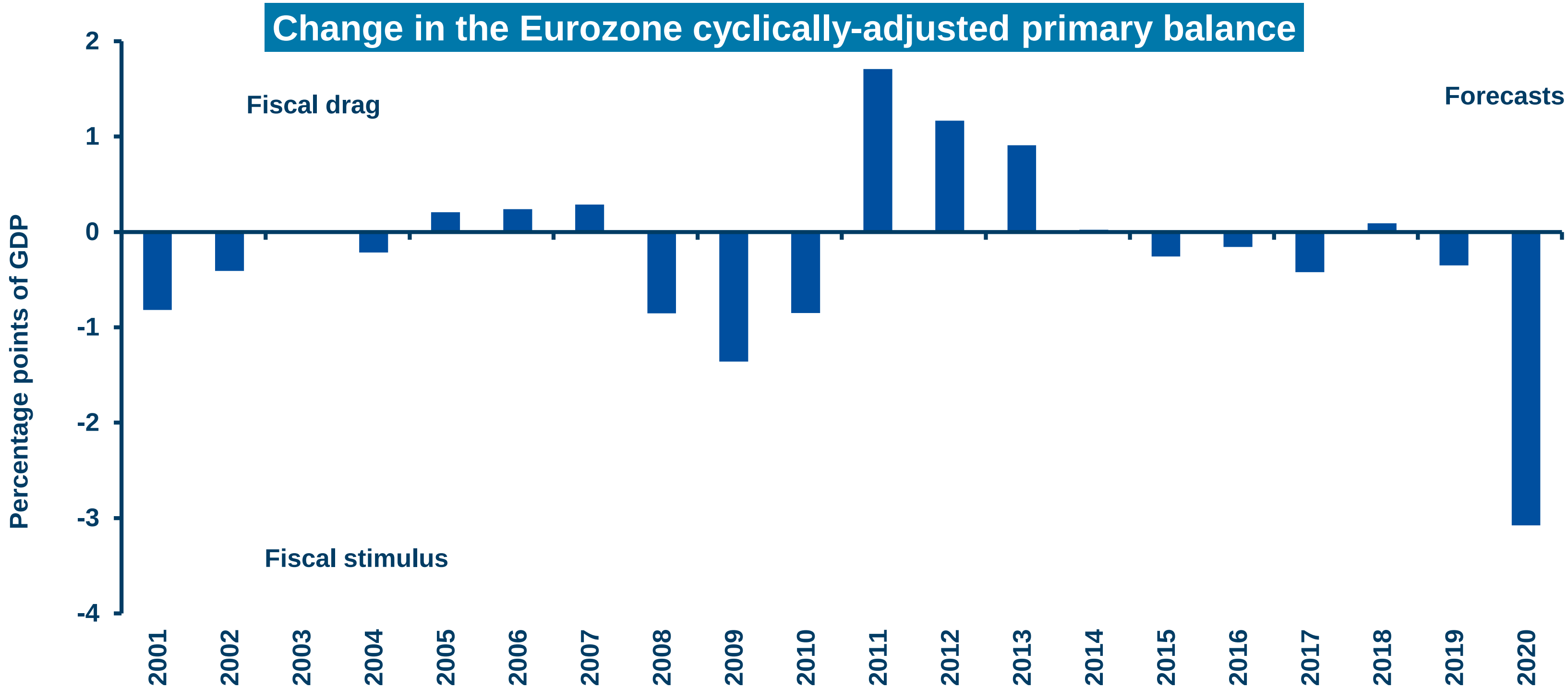


Since the outbreak of the Covid-19 crisis, more than €1 trillion has been injected into the system by the ECB through long-term financing (TLTRO). The massive liquidity injected has been benefitting non-financial corporations that gained access to cheap loans through this facility.

Source: Amundi, ECB. Data as of 19 June 2020.

Source: Amundi, European Central Bank. Data as of 6 July 2020.

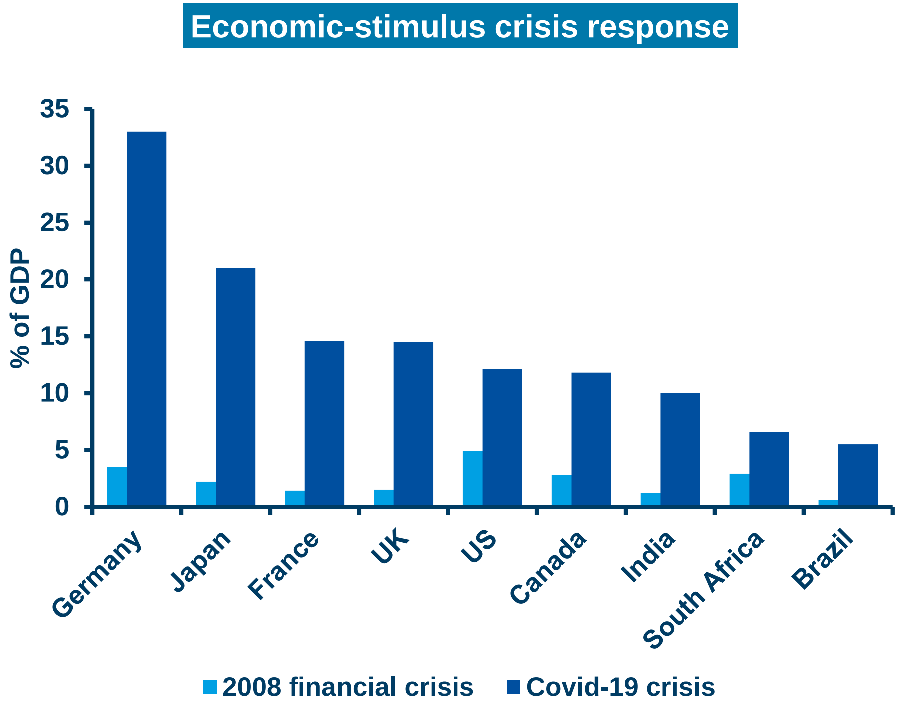
The era of austerity is over

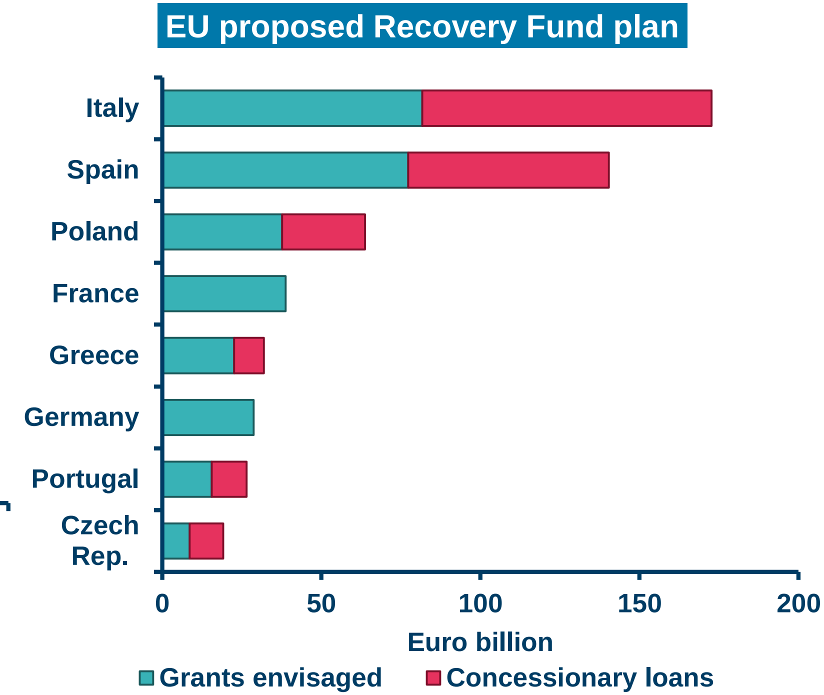


» The Eurozone has learnt its lesson from the debt crisis: the approach to the current crisis is different and the era of fiscal austerity seems to be over, with huge fiscal stimulus expected in 2020. Primary deficit is also expected in 2021.

Source: Amundi, Datastream as of 6 July 2020. Forecasts are by the European Commission.

Unprecedented economic-stimulus responses



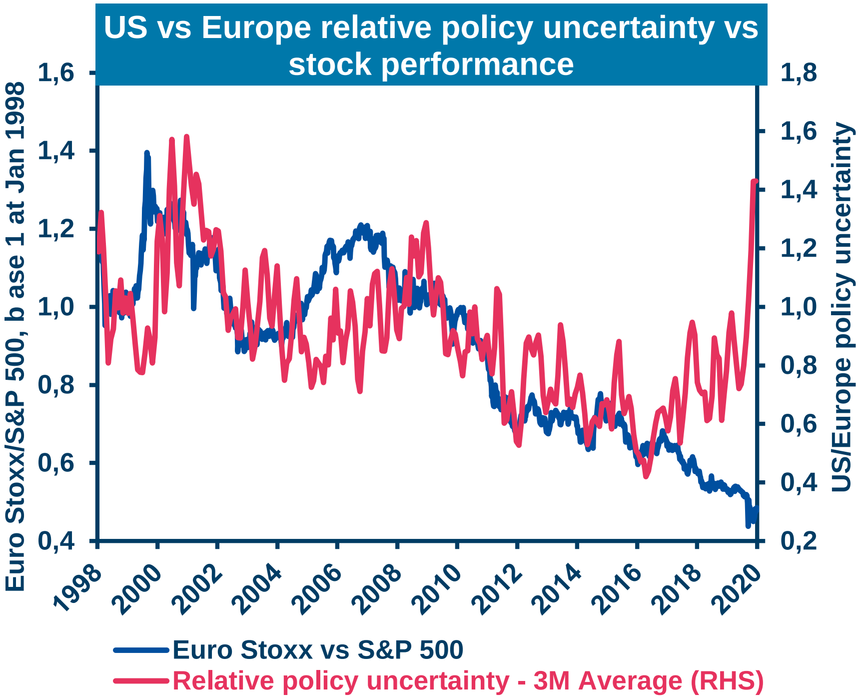


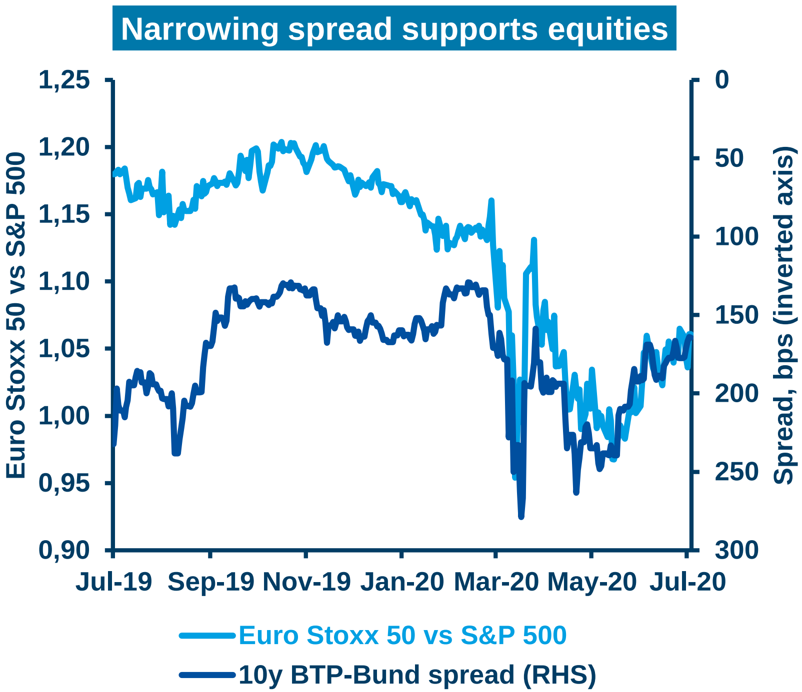
» Governments have responded with fiscal measures to keep economies afloat. Economic stimulus responses to the Covid-19 crisis outsize those to the 2008 financial crisis. The EU Commission has proposed a €750 billion recovery fund, with up to €500 billion available as grants and the remaining €250 billion as loans.

Source: Amundi, McKinsey & Company, IMF. As of 5 June 2020.

Source: Amundi. European Commission. As of 22 June 2020.

Easing political risk and falling spreads are supportive



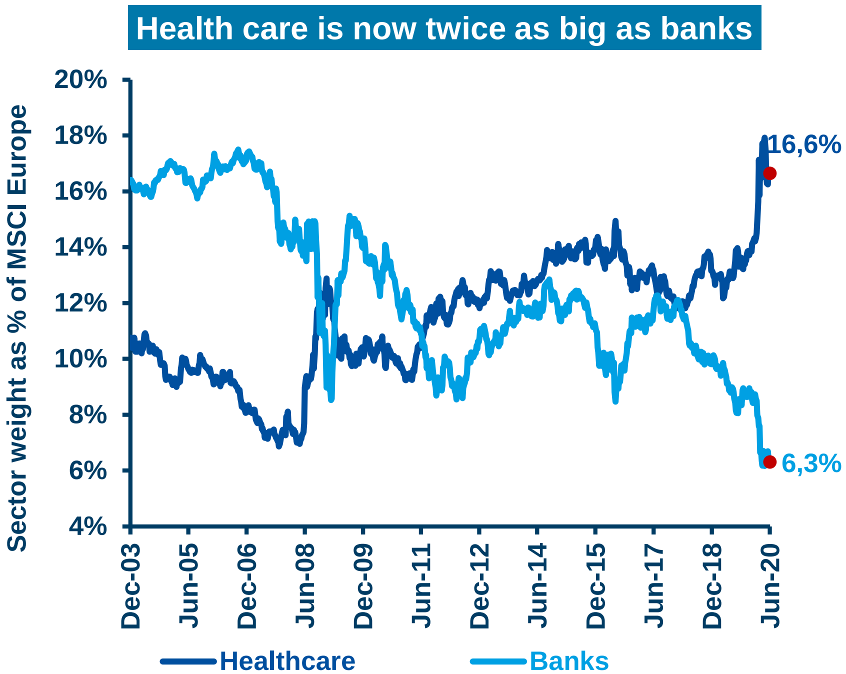


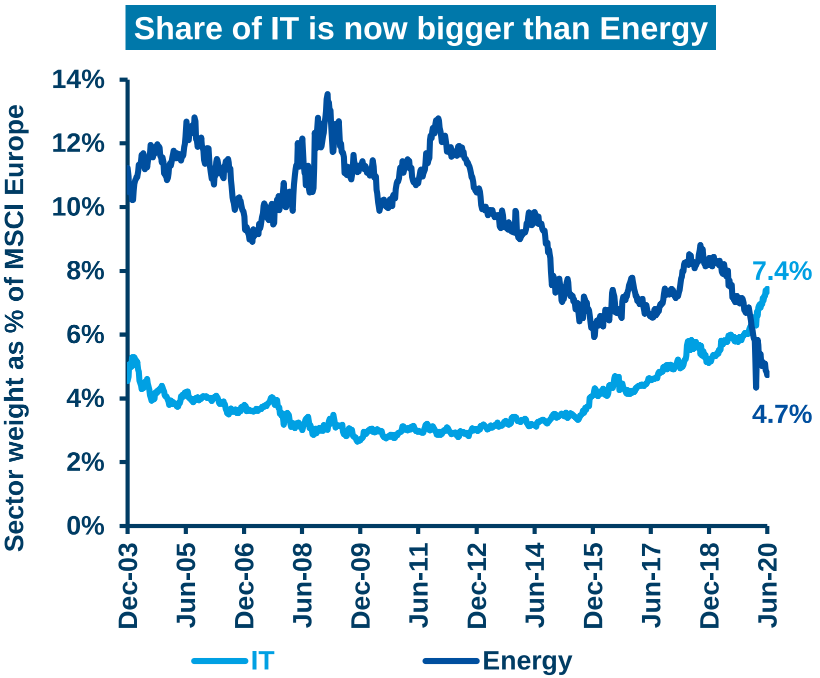
A reduction in political risk premium in Europe should be positive for European equities. Investors should look for businesses with strong balance sheets and cyclical names exposed to a recovery.

Source: Amundi, Policyuncertainty.com, Monthly data as on 30 June 2020. Relative policy uncertainty = US Policy uncertainty index/European policy uncertainty index.

Source: Amundi, Bloomberg, as of 3 July 2020.

EU market is becoming more attractive



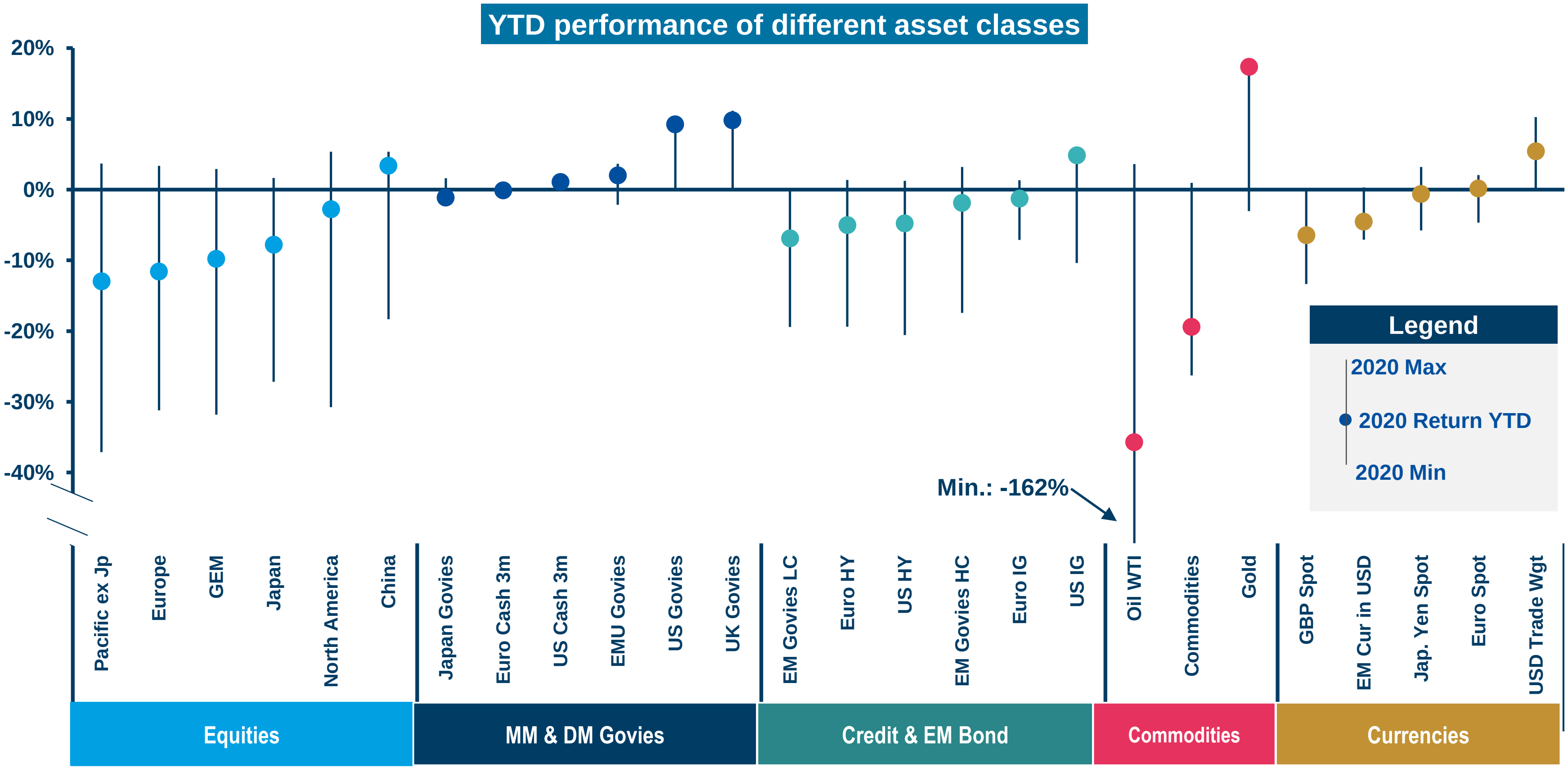


» European markets have evolved over the years, and the weight of challenged sectors, including energy, is falling amid a bent towards a greener economy. The most dynamic part of the market such as IT is growing. This evolution makes the EU market more attractive.

Source: DataStream, Amundi Research, on MSCI Europe index. as at 1 July 2020.

Source: DataStream, Amundi Research, on MSCI Europe index. as at 1 July 2020.

Risk assets rebounded, still room for Europe to catch-up



Source: Bloomberg, analysis by Amundi of 26 asset classes (and FX). Data as of 30 June 2020. Index providers: cash, government bond and EM bond indices are from JPMorgan; corporate bond indices are from BofA; equity indices and EM currency indices are from MSCI; commodities indices are from Bloomberg Barclays. All indices used to represent asset classes are in local currency. **Past performance is no guarantee of future results**.

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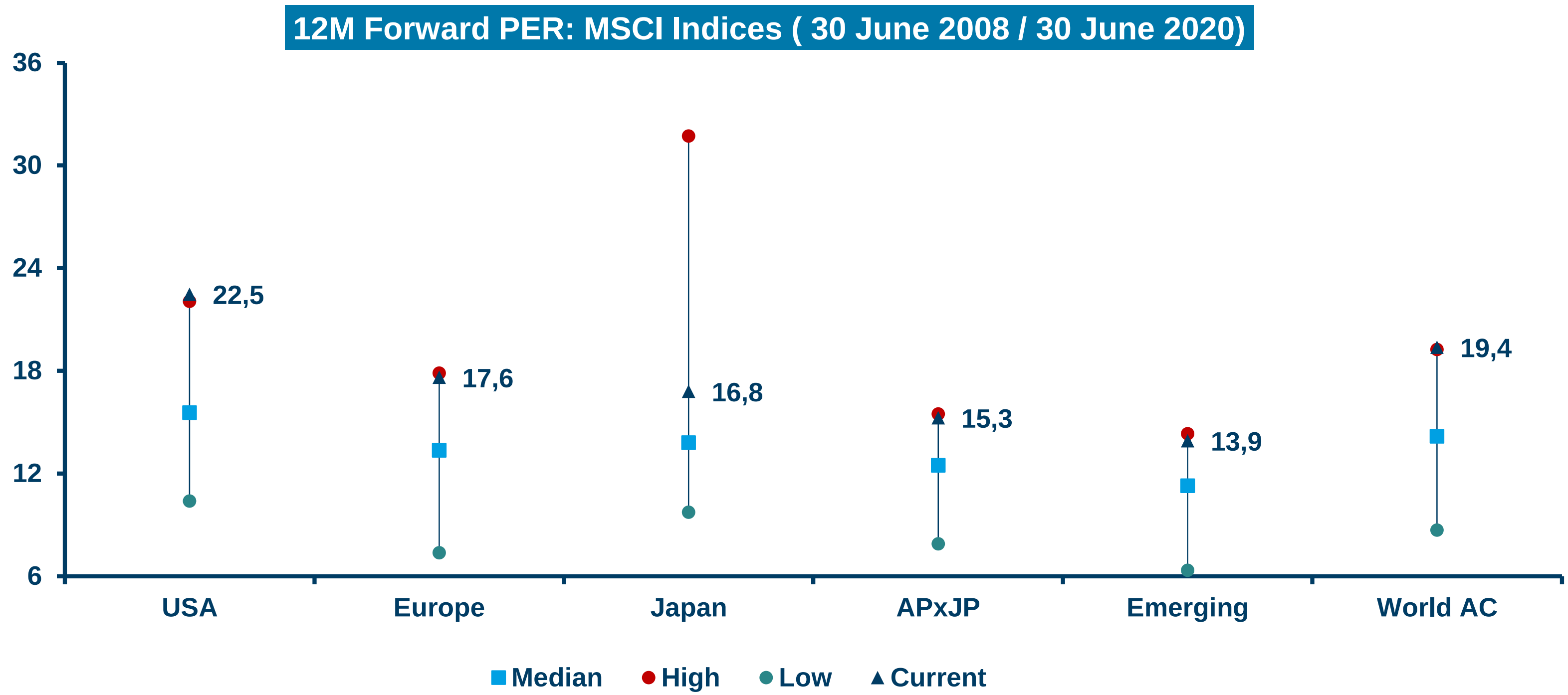
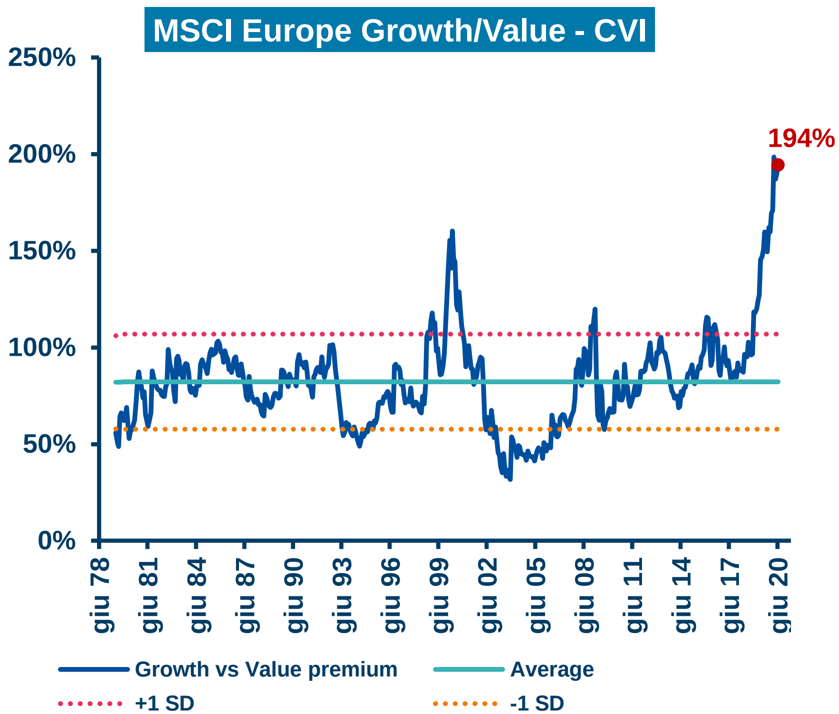
With tight valuations globally, look at areas of rotation

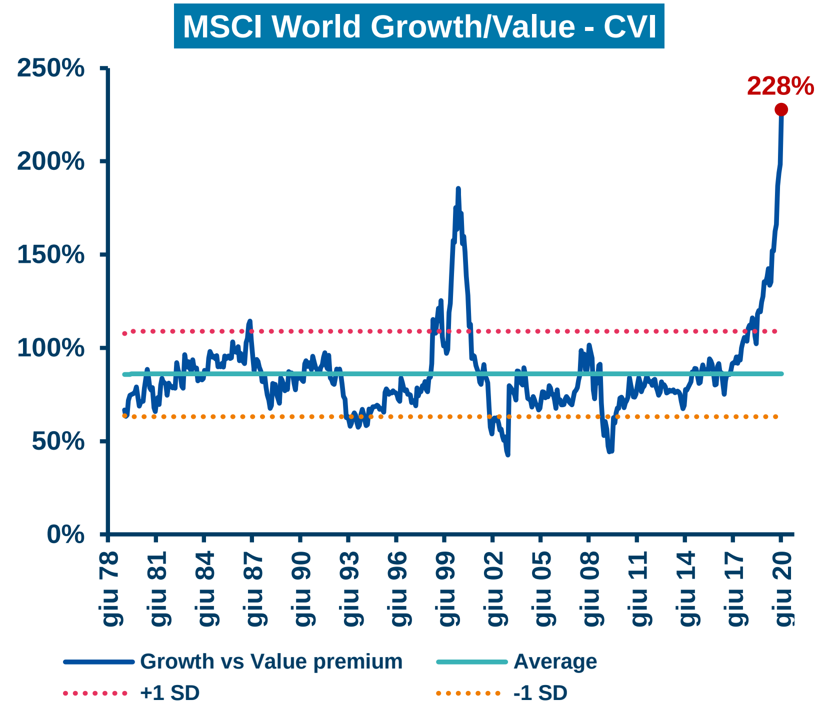


After falling sharply in March, equities recovered on the back of central bank support and expectations that the virus cycle is over. Current valuations are not particularly compelling, and therefore, focus on earnings will be key for the remainder of the year.

Source: MSCI, Amundi Research. Data as of 23 June 2020.

Growth/Value at historical high, some reversal expected but better to be balanced

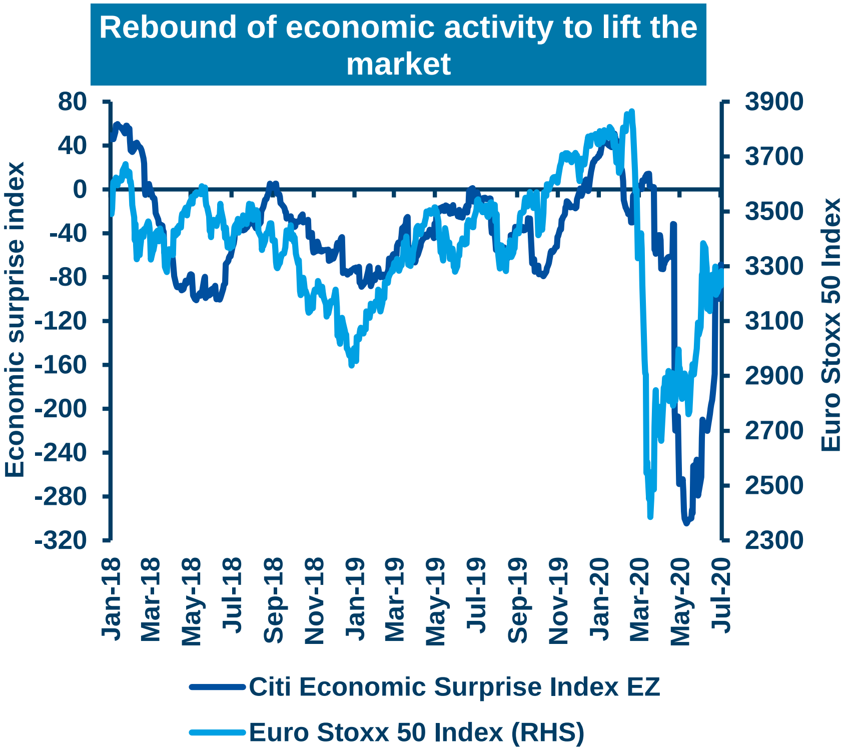


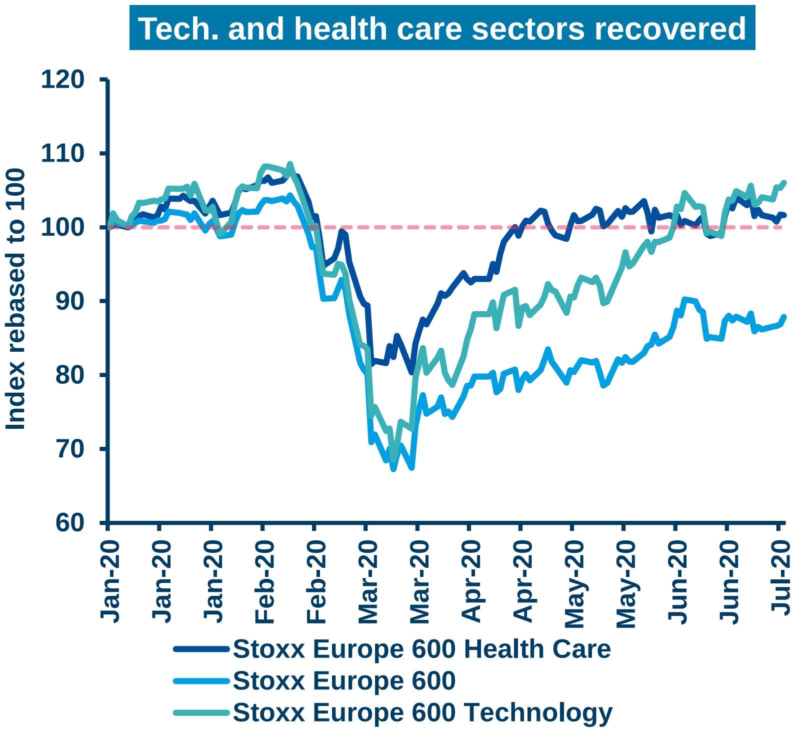


» Growth vs value premium is historically at a high level, particularly in Europe. A correction is due, especially with a PMI rebound that could support Value, Beta plays and Laggards. However, the Covid-19 crisis has accelerated the shift toward digitalization and rates are likely to stay low to finance huge deficits. The leaders of the next cycle could well be the same as in the previous cycle. A balanced positioning makes sense.

Source: DataStream, Amundi Research, as at 30 June 2020. Composite Valuation Indicator (CVI): Based on a basket of criteria in absolute terms – Trailing Price to earnings (PE), Price to book value (P/BV) and Dividend yield (DY), and ranked in percentile from 0 to 100% the percentage of time this basket was cheaper since 1979 (0% never been cheaper; 100% never been more expensive).

Play the cyclical rebound



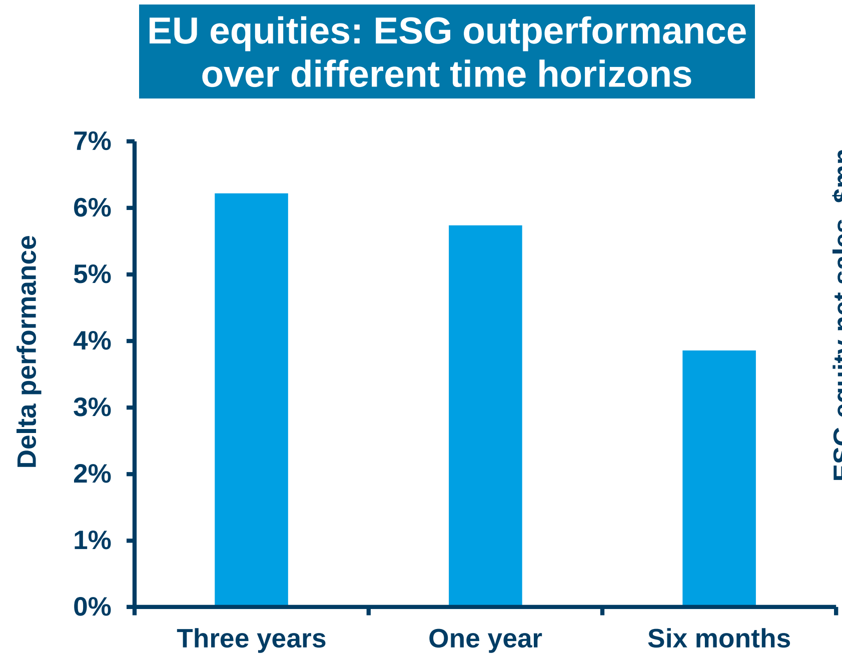


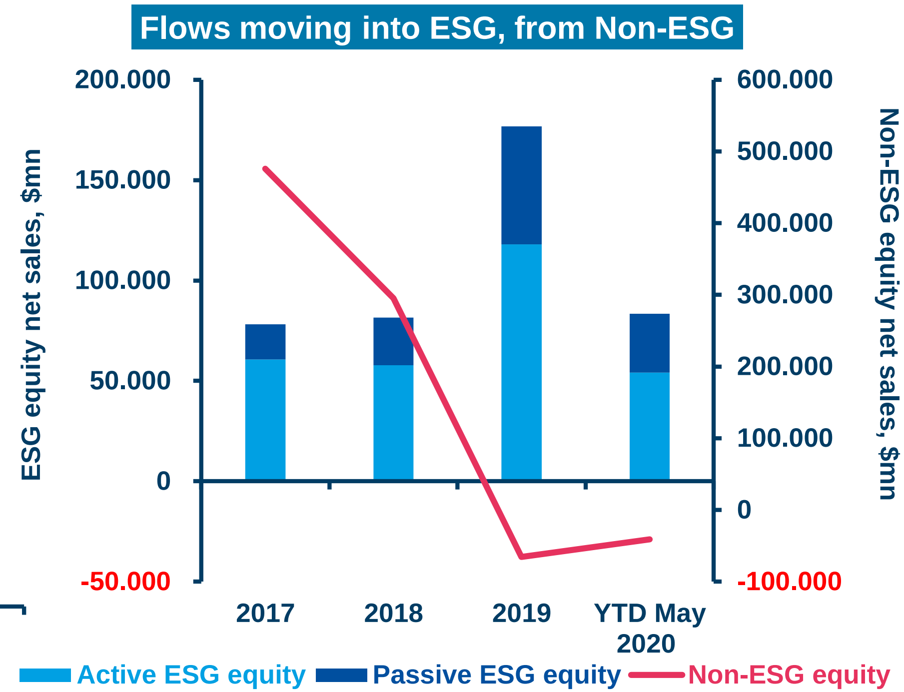
» Investors should play the rotation towards cyclical sectors in Europe as these tend to benefit the most from an economic recovery. This approach should be balanced with exposure to areas most resilient to the pandemic.

Source: Amundi, Bloomberg, 2 July 2020.

Source: Amundi, Bloomberg, 2 July 2020.

ESG investing becoming mainstream





» Covid-19 is foremost a health crisis and investors are carefully watching how companies respond to the needs of their stakeholders such as employees, suppliers and the broader society. In addition, ESG is a good indicator of idiosyncratic risks of companies.

Source: MSCI Europe and MSCI Europe ESG Leaders, Amundi on Bloomberg data as of 6 July 2020..

Source: Broadridge, worldwide open-ended funds. Latest monthly data as at 2 July 2020.

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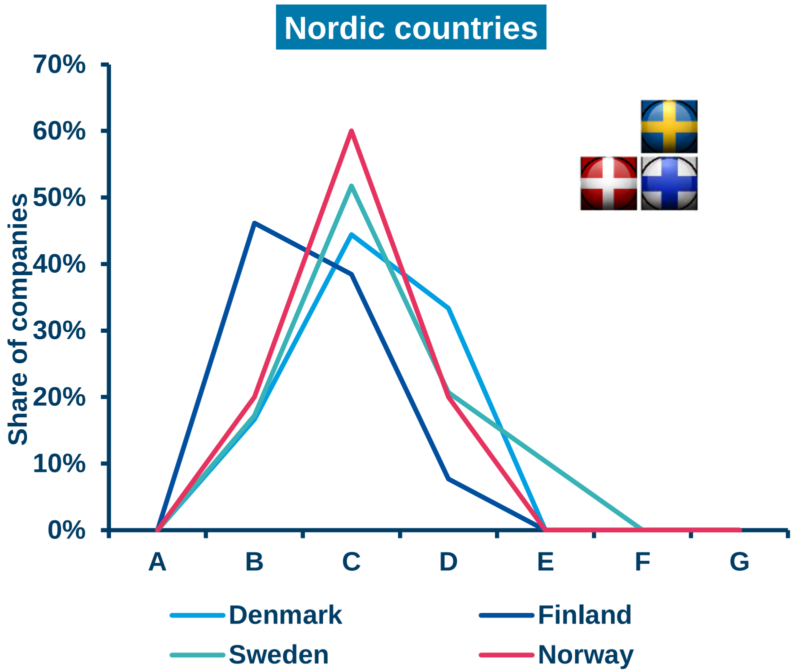
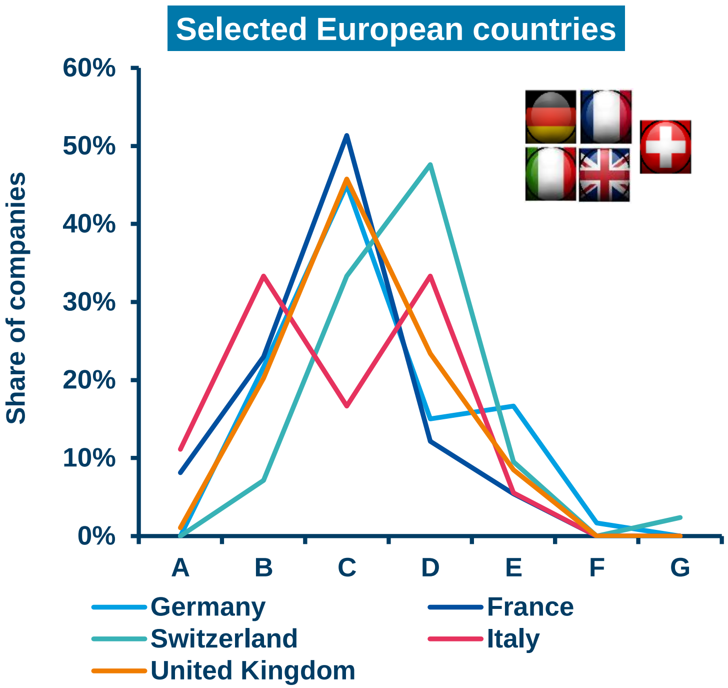
Opportunities to play the “improvers” theme





» Europe stands ahead in terms of climate policies, renewable energy and de-carbonisation. Governance is also generally strong. However, the distribution of ESG ratings is uneven across European countries, with Nordic countries being the ESG leaders and a high number of highly-rated companies. But rest of Europe shows a more diverse ESG profile, with more room for improvement. This leaves scope for scouting investment opportunities across the region.

Source: Amundi as of 3 July 2020.

Amundi View: Current and H2 perspective

Current view

EQUITIES	
US	-/=
Europe	-/=
Japan	=
EM	=

H2 perspective

EQUITIES	
US	=
Europe	=/ +
Japan	+
EM	=

We favour a balanced strategy, looking for some cyclicality in the short term but long-term winners as a core position. The cyclical recovery could drive some catch up of the beta markets such as EU and Japan. Some rotation favouring cyclical value, could also be on the cards. However, investors need to be selective and focus on companies with strong balance sheets. This view depends on our main scenario of a gradual normalization of economic conditions, continued policy actions, implementation of the recovery fund and no aggressive second wave of the pandemic.

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Negative View Neutral Positive View

Source: Amundi, as of 26 June 2020.

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