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BIZ INSIGHT

Looming political clouds can't rain on European equities

SPECIAL TO THE NATION

WITH POLITICAL uncertainty looming around Europe, it naturally makes investors a little anxious.

As of right now, European equities are far more attractive compared to the current low bond yields. Yet, the market seems vulnerable given upcoming elections in a few major countries, Brexit and Greece's debt situation. Certainly, the political risk cannot be ignored, but not all stocks are affected the same way. Despite these clouds, leading gauges were resilient in January. The composite PMI suggested a healthier economic condition which resulted in a surge in Euro-zone economic sentiment.

Accordingly, BlackRock altered its European equity outlook from neutral to overweight, due to them believing that equities will benefit in a reflation scenario.

Together with a depreciating Euro that is expected to fuel export growth, both factors are indicating the European market cannot be ignored.

The European market offers several opportunities. Their price/forward earnings ratio of roughly 15x is equivalent to an 8 per cent discount to global developed stocks and about a 15 per cent discount to US stocks.

For instance, consider European chemicals and energy industries. The chemical industry is positioned to benefit from an increase in global supply and demand such as polyethylene, which is used in plastics.

In the energy sector, some major companies are still attractive even after a 2016 rally, and companies that cut costs substantially during the oil price slump should enjoy a more profitable run in the short term.

Lastly, domestic industries should not hesitate as European brands with global exposure could pick up if consumer spending does.

It is ordinary to factor in political risks when weighing investment decisions. However, in today's world there's political uncertainty everywhere, from Washington, DC to China. Therefore, Europe's current political factors should not be considered a greater risk than other parts of the world.

This does not mean that headlines will be amusing and optimistic over the coming months, but as seen in the market rally following the US election, there are still equities that do not depend on regional stability for long-term success.

In conclusion, overall Europe's economic prospects remain encouraging. Growth seems to be robust in 2017, but slower than 2016's 1.7 per cent (source: FocusEconomics as of February 1). The labour market is improving and the ultra-easy monetary policy should drive domestic growth.

Furthermore, rising inflation and higher oil prices will reduce pressure on consumption as they reduce tailwinds against household incomes. FocusEconomic suggests the Euro zone will grow 1.5 per cent in 2017 and the same in 2018 (source: FocusEconomics as of February 1).

However, investors practising timing strategy and closely monitoring markets are still key. For those who are looking to generate returns on Europe's growing equity, but may lack the time to monitor market conditions, seeking a professionally managed European equity mutual fund is highly recommended.

Investment contains risk. The investors should thoroughly study prospectuses, product features, return conditions and risk before investing.

Contributed by Asset Plus Fund Management