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EUROPE: THE BULL-BEAR FIGHT RUMBLES ON

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Laurence Taylor
Portfolio Specialist, Global Equities

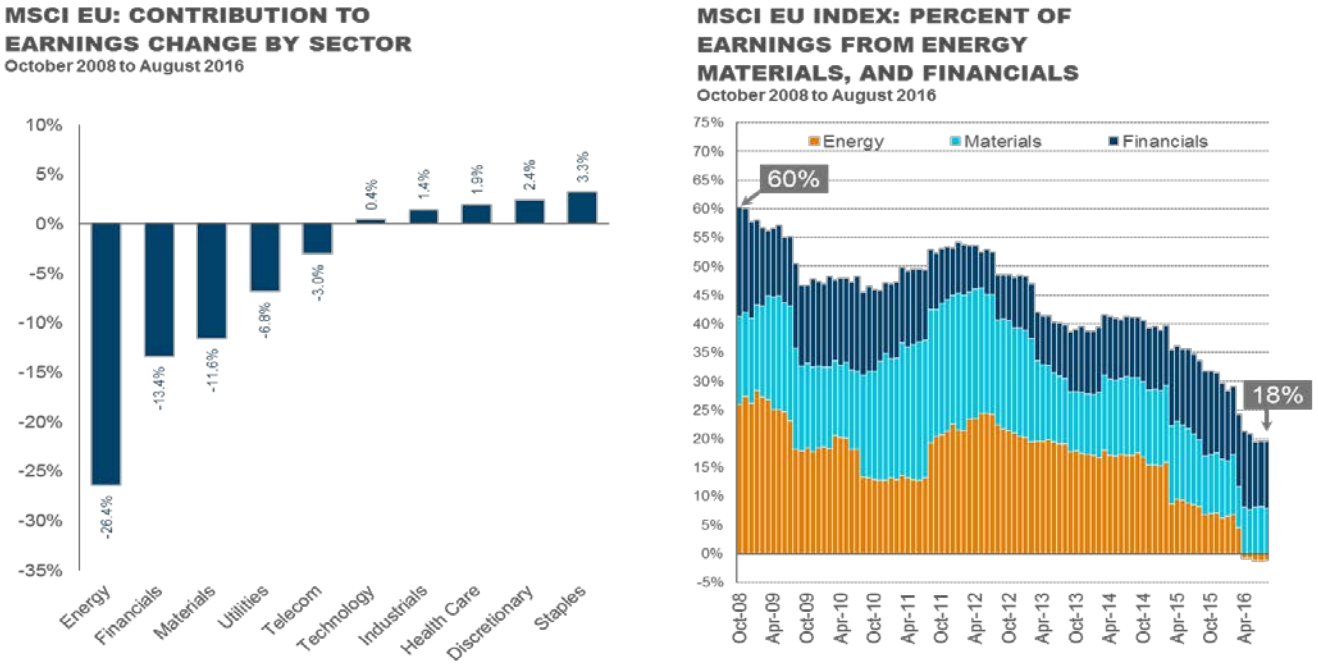
A bull and bear fight that is getting very feisty, US inflation rising to a three year high in 2017, Europe's market cap falling to a 25 year low, global profits potentially ticking up ending a two year recession and Value outperforming Growth for the first time in eight years. There is a lot to talk about in markets today and I haven't even mentioned the word 'Trump'!

To ensure we maintain a focus away from events in the US that are righty attracting so much interest, here's a succinct case against and then for European equities as investors ponder their asset allocation into 2017.

THE CASE AGAINST EUROPEAN EQUITIES

Europe's profitability has changed dramatically due to structural reasons – oil, materials and financials have seen profits collapse, some of which is permanent and should impact investors' perception of future earnings power/growth and be priced into valuations.

Figure 1: European Profits – Why So Bad?

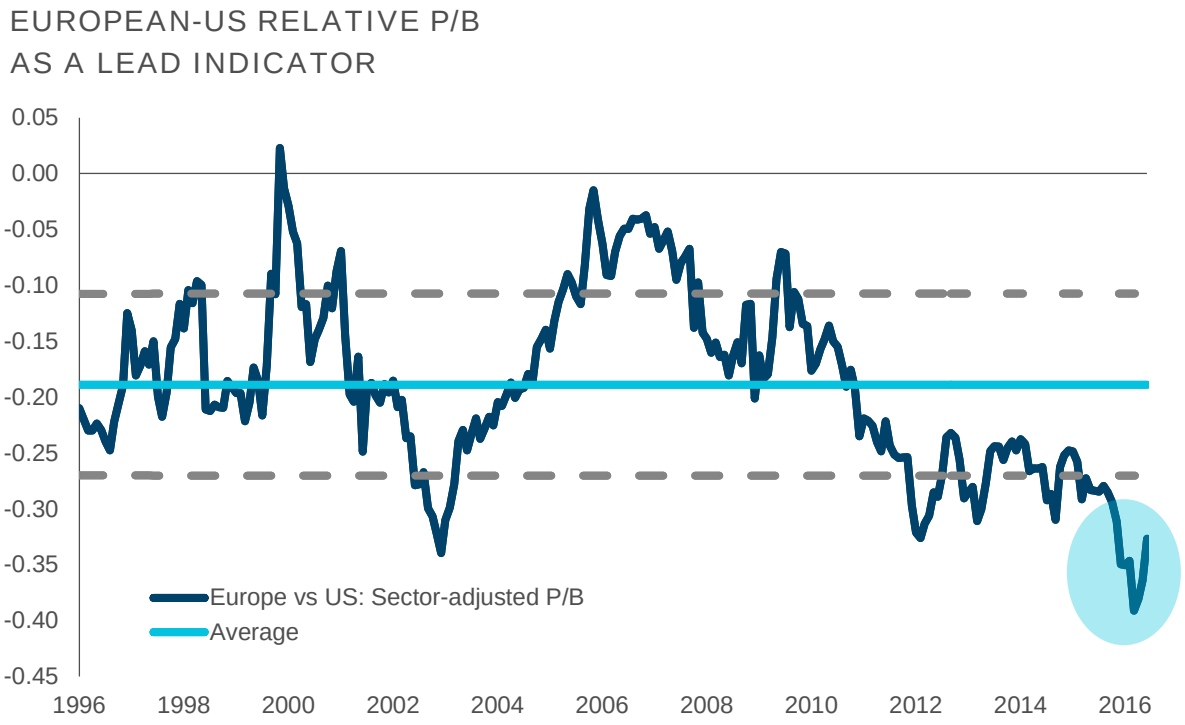


Past performance is not a reliable indicator of future performance.
Chart is shown for illustrative purposes only and does not represent the performance of any specific security.
Sources: FactSet, MSCI.

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But when you look at European valuations versus the US, levels have clearly reached an extreme point and this measure has turned during the summer. If you're a cyclical believer (a prolonged turn usually coincides with global economic growth accelerating – think late 90's, mid 2000's) or a mean-reversionist (given valuations look so cheap on a relative basis), Europe no doubt offers real opportunity today. Given the challenges ahead, however, the need to stay selective is as important as ever.

Figure 2: Europe – Inflection or Relief?



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Source: FactSet.

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