

Economic Situation and Strategy

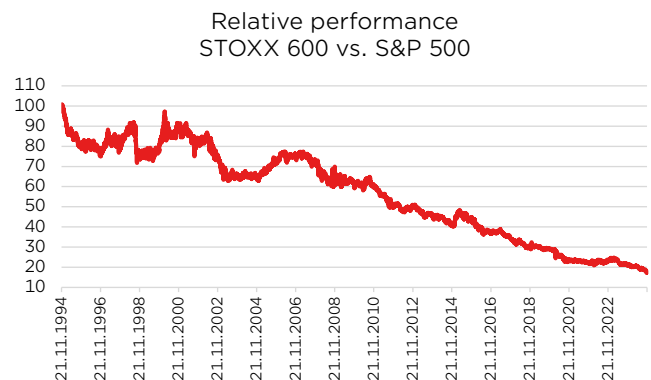
22 November 2024

European equities: endless under-performance?

Anyone who would have invested in the S&P 500 30 years ago could consider themselves lucky today. Because the calculated performance (in US\$ and excluding dividends) is a staggering 1180%! If dividends are also taken into account, the performance in US\$ increases to an astonishing 2150%. This is not a miscalculation, but the result of a good p.a. performance in combination with a relentless compound interest effect. Anyone who had alternatively bought European equities (measured by the STOXX 600) would also have been pleased with the remarkable performance; however, the result is more modest compared to US equities. From a fundamental point of view, this result is understandable - economic value creation in the USA has grown faster than in Europe over the last 30 years, and profits in the USA have also been more abundant than in Europe. In addition, the hope of future profits has caused valuation levels to rise more strongly in the USA than in Europe, which also explains part of the performance difference.

Looking at the relative performance of the STOXX 600 compared to the S&P 500, it is noticeable that Europe's systematic underperformance began roughly between 2006 and 2010. This is also understandable to a certain extent, as Europe was hit harder by the financial crisis than the USA in economic terms, recovered more slowly and was additionally slowed down by the burdens of the debt crisis. A less developed capital market (particularly in the area of private equity) meant that the capitalisation of many smaller companies in Europe developed less dynamically than in the USA. It is also fair to say that significantly more disruptive technologies were ready for the market in the USA from this period onwards than in

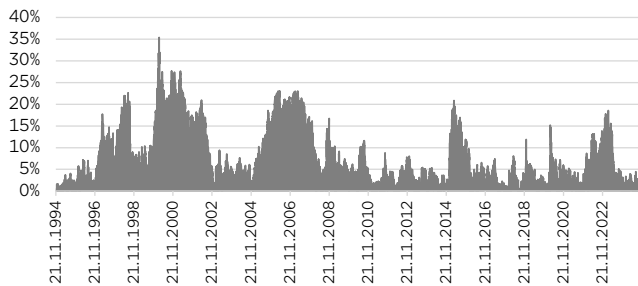
the Eurozone. Excessive European bureaucracy and higher taxes probably contributed to the fact that European equities were nowhere near the performance of their US competitors.



Therefore, the chart above suggests that you would have made a huge mistake from 2010 at the latest if you had still held European equities in your portfolio at all. While this is true in retrospect, it cannot be generalised for individual periods. The seemingly linear trajectory of under-performance somewhat obscures the fact that there have been periods when a good tactical allocation to overweight European equities could have actually added to performance.

To analyse this in more detail, we have calculated how the European STOXX 600 has performed against the S&P 500 after reaching a new historical low (in each case) in the relative performance of the STOXX 600 to the S&P 500. This shows that there have indeed always been phases in which European equities were able to outperform US equities for some time. The magnitude of this relative outperformance has been around 20% in two cases since 2010, with values of 5% being achieved very frequently.

Relative performance of the STOXX 600 after reaching a (new) low in relative performance to the S&P 500



However, it is also a fact that you have to be pretty quick and good at timing these tactical allocation decisions in order to be able to utilise these time windows for your portfolio. It often only takes a few months from reaching a relative low to reaching a (local) relative high. In addition, since the stock market does not ring a bell, it is likely that even an investor with an extremely good sense of timing will only be able to realize half of the possible outperformance by temporarily overweighting European equities.

The logical question now is whether this might be the right time to try your luck with European equities. On November 13, the relative performance of the STOXX 600 to the S&P 500 hit an all-time low, and since that low we have moved more or less sideways in terms of relative performance. In such situations in the past, the probability of a mean reversion was somewhat higher than that of a further deterioration in relative performance. However, is this in itself a good reason to change horses and bet on European equities from a more technical perspective?

Actually, we don't think that's the case. Of course, short-term reversals can never be ruled out and are even likely, but in the coming months there is still more to be said in favor of the US and less in favor of Europe. In particular, Trump's victory has shifted the balance back in favor of the US. No matter how you feel about an 'America First' policy, it initially favors the US economy and puts Europe at a disadvantage. In the USA, taxes and energy

prices will tend to fall. At the same time, bureaucracy and regulation will probably be reduced. Tariffs on European products are likely to rise, and Europe will have to bear higher burdens within NATO. Moreover, there is no reason why the valuation ratios of US equities should suffer under these conditions. In fact, the opposite is more likely to be the case. The expected future profits are likely to be even higher and thus justify even higher valuation ratios, which seems hardly conceivable given the current price/earnings ratios.

However, valuation ratios such as the P/E ratio or the price-to-book ratio at index level obscure the fact that not all shares have reached very high valuation levels. In fact, the S&P 500 appears so expensive primarily because some very large and highly weighted companies in the index are valued comparatively expensively. However, if our hypothesis that the economy as a whole should benefit from Trump's economic policy is correct, the profits of medium-sized and small companies should also receive a systematic boost in the coming years. This in turn would be a good reason for the capital markets to reconsider the fundamental valuation level of small and medium-sized companies and trigger a so-called 'multiple expansion' here too. As a result, equities across the market would also benefit from this development, possibly ending the phase in which primarily the very large US equities were able to achieve a very good performance. From this perspective, one would be well advised to focus tactically not on European equities, but rather on smaller U.S. equities as a complement to the large caps still in the portfolio. There are several ways to reflect this idea in portfolios. In addition to individual investments, ETFs could be purchased that track the performance of dedicated small- and mid-cap indices. Alternatively, ETFs could be purchased that track broad market indices via an equal weighting of stocks. Unfortunately, we lack the imagination to see Europe outperform.

Dr. Christian Jasperneite

Market data

Stock marketes	As of	Change versus				
	22.11.2024	15.11.2024	21.10.2024	21.08.2024	21.11.2023	29.12.2023
	10:56	-1 week	-1 month	-3 months	-1 year	YTD
Dow Jones	43870	1,0%	2,2%	7,3%	25,0%	16,4%
S&P 500	5948	1,3%	1,6%	5,8%	31,1%	24,7%
Nasdaq	18972	1,6%	2,3%	5,9%	33,6%	26,4%
DAX	19061	-0,8%	-2,1%	3,3%	19,9%	13,8%
MDAX	25871	-2,0%	-4,7%	3,8%	-0,3%	-4,7%
TecDAX	3337	-0,5%	-1,6%	-0,1%	7,3%	0,0%
EuroStoxx 50	4731	-1,3%	-4,3%	-3,2%	9,2%	4,6%
Stoxx 50	4271	0,2%	-4,2%	-4,4%	8,2%	4,3%
SMI (Swiss Market Index)	11616	-0,1%	-5,3%	-5,2%	7,7%	4,3%
Nikkei 225	38284	-0,9%	-1,7%	0,9%	14,8%	14,4%
Brasilien BOVESPA	126922	21257,6%	20884,5%	-7,0%	1,0%	21018,4%
Indien BSE 30	79150	6858,6%	6858,6%	-2,2%	20,1%	7205,2%
China CSI 300	3866	67,8%	72,6%	16,4%	7,9%	90,7%
MSCI Welt	3754	1,2%	0,4%	3,4%	25,1%	18,4%
MSCI Emerging Markets	1085	0,0%	-5,5%	-1,4%	9,8%	6,0%
Bond markets						
Bund-Future	132,48	3700	3702	-231	122	3632
Bobl-Future	119,14	-1306	-1402	111	225	-1808
Schatz-Future	106,99	-1162	-1204	68	188	-1229
3 Monats Euribor	3,00	206	206	-66	-97	207
3M Euribor Future, Dec 2024	2,83	#WERT!	#WERT!	-15	-21	#WERT!
3 Monats \$ Libor	3,17	0	-25	#WERT!	#WERT!	-72
Fed Funds Future, Dec 2024	4,52	172	169	4	2	222
10 year US Treasuries	4,39	-6	21	60	-3	53
10 year Bunds	2,25	-11	-3	10	-27	25
10 year JGB	1,08	1	15	20	38	46
10 year Swiss Government	0,38	-686	-675	-1	-59	-673
US Treas 10Y Performance	565,63	0,4%	-0,1%	-8,7%	-1,3%	0,0%
Bund 10Y Performance	106,83	0,0%	0,0%	-81,2%	-80,3%	0,3%
REX Performance Index	452,90	-94,9%	-95,2%	0,4%	4,2%	-94,6%
IBOXX AA, €	3,03	3	4	-10	-69	-4
IBOXX BBB, €	3,49	3	2	-15	-102	-26
ML US High Yield	7,42	-8	9	-13	-131	-37
Commodities						
MG Base Metal Index	416,03	-0,8%	-4,6%	-0,2%	8,7%	6,4%
Crude oil Brent	74,31	2,9%	0,7%	-3,9%	-9,9%	-4,4%
Gold	2703,58	5,1%	-0,6%	7,9%	35,0%	30,9%
Silver	3370,40	1,2%	3,1%	11309,6%	14013,9%	13,3%
Aluminium	30,73	1,4%	-8,8%	-98,8%	-98,6%	26,7%
Copper	2599,60	-1,0%	1,6%	-71,5%	-68,9%	10,8%
Iron ore	102,02	-77,4%	-77,5%	3,7%	-21,3%	-77,2%
Freight rates Baltic Dry Index	1576	-11,7%	1,9%	-10,4%	-12,2%	-24,7%
Currencies						
EUR/ USD	1,0413	#DIV/0!	#DIV/0!	-6,3%	-4,9%	#DIV/0!
EUR/ GBP	0,8319	-21,4%	-23,3%	-2,3%	-4,6%	-24,7%
EUR/ JPY	160,80	19176,0%	19194,5%	-0,9%	-0,5%	18456,3%
EUR/ CHF	0,9252	-99,4%	-99,4%	-2,6%	-4,4%	-99,4%
USD/ CNY	7,2490	-92,9%	-93,1%	1,6%	1,5%	-94,7%
USD/ JPY	154,54	0,1%	2,4%	6,4%	4,1%	9,5%
USD/ GBP	0,80	644370,1%	664721,0%	4,4%	0,2%	617965,9%

Source: Refinitiv Datastream

Carsten Klude
+49 40 3282-2572
cklude@mmwarburg.com

Dr. Rebekka Haller
+49 40 3282-2452
rhaller@mmwarburg.com

Martin Hasse
+49 40 3282-2411
mhasse@mmwarburg.com

Dr. Christian Jasperneite
+49 40 3282-2439
cjasperneite@mmwarburg.com

Simon Landt
+49 40 3282-2401
mlandt@mmwarburg.com

Jan Mooren
+49 40 3282-2992
jmooren@mmwarburg.com

This article does not constitute an offer or an invitation to submit an offer but is solely intended to provide guidance and present possible business activities. This information does not purport to be complete and is therefore not binding. The information provided should not be considered a recommendation to purchase financial instruments individually but serves only as a proposal for a possible asset allocation. The opinions expressed herein are subject to change without notice. Where statements were made with respect to prices, interest rates or other indications, these solely refer to the time when the information was prepared and do not imply any forecasts about future development, particularly regarding future gains or losses. In addition, this information does not constitute advice or a recommendation. Before completing any deal described in this information, a product-specific consultation tailored to the customer's individual needs is required. This information is confidential and exclusively intended for the addressee described herein. Any use by parties other than the addressee is not permissible without our approval. This particularly applies to reproductions, translations, microfilms, saving and processing in electronic media as well as publishing the entire contents or parts thereof.

This article is freely available on our website.