

REGIONAL MARKETS UPDATE

EUROPE (2.5 STARS – NEUTRAL)

EUROZONE AGGREGATE

- Advance reading of Eurozone PMI composite at 58.6 in Jan 18, as compared to a finalised 58.1 in Dec 17
- Advance Consumer Confidence at 1.3 in Jan 18, up from a finalised 0.5 reading in Dec 17
- Retail sales rose 2.8% y-o-y in Nov 17, up from a downward-revised 0.2% y-o-y gain in Oct 17
- ZEW survey (expectations) at 31.8 in Jan 18, up from 30.9 in Dec 17
- Sentix Investor Confidence came in at 32.9 in Jan 18, up from 31.1 in Dec 17

GERMANY

- Advance composite PMI at 58.8 in Jan 18, down from a finalised 58.9 in Dec 17
- Factory orders rose 8.7% y-o-y in Nov 17, after an upward-revised 7.2% rise in Oct 17
- ZEW readings rose for both the current situation and expectations surveys in Jan 18
- IFO surveys for current assessment and business climate surveys rose, but expectations survey fell in Jan 17

FRANCE

- Preliminary PMI composite at 59.7 in Jan 18, up from a finalised 59.6 in Dec 17
- Industrial production rose 2.5% y-o-y in Nov 17, down from a 5.5% rise in Oct 17
- Bank of France business sentiment at 110 in Dec 17, INSEE business confidence at 110 in Dec 17

UNITED KINGDOM

- Preliminary PMI Composite at 54.9 in Dec 17, up from 54.8 in Nov 17
- Retail sales ex auto fuel rose 1.3% y-o-y in Dec 17, down from a 1.5% change in Nov 17
- Retail sales ex auto fuel fell -1.6% m-o-m in Dec 17, down from a downward-revised 1.1% rise in Nov 17

MARKET OUTLOOK

European companies on aggregate (as represented by the benchmark Stoxx 600 Index) saw minor upgrades over the first month of 2018, with 2018's and 2019's earnings estimates both raised by 0.3% respectively (as of 29 January 2018). On a sector basis, European oil and gas firms saw earnings estimates bumped up over the month on the back of rising crude oil prices. The basic resources sector once again saw earnings estimates revised higher across both FY 2018 and FY 2019, while the automobile industry also saw earnings upgrades as a whole. European financial services, chemicals and travel and leisure-related companies also continued to enjoy earnings upgrades, reinforcing the trend seen in cyclically-orientated sectors as external demand continues to improve.

In terms of economic data, trends in the labour markets across Europe remain constructive, with continued job gains and unemployment generally improving (with the periphery seeing a faster rate of recovery than the core). Leading indicators have been particularly strong, with composite PMIs of the major European countries on a firm uptrend and sentiment supported by an improving outlook. Consumer confidence has also continued to improve, lending support to the outlook for domestic consumption. Hard data is also starting to reflect this development, contributing to overall GDP on the continent. While political events (i.e. current Brexit talks and upcoming general election in Italy) may or may not adversely impact business confidence depending on the outcomes, we believe that the increasingly entrenched recovery across Europe is a positive development that is difficult to ignore.

In political developments, European asset markets breathe a sigh of relief as Germany's Social Democrats (SPD) announced that they will start formal coalition talks with incumbent Chancellor Merkel's conservative party. A rerun of a conservative-SPD 'grand coalition' appears to be what market participants had hoped for, as both parties have been weakened by the rise of Germany's far right in the recent Federal elections last year.

In its latest policy update, the European Central Bank (ECB) made no changes to its benchmark policy rates, reiterating that asset purchases at the monthly pace of EUR 30.0 billion "are intended to run until the end of September 2018", until the path of inflation is consistent with its policy target. The ECB affirmed that economic momentum is robust, and that economic slack has reduced, capacity utilisation has risen and "private consumption is supported by rising employment". When asked if interest rates will only be raised well past the end of net asset purchases during the press conference, ECB President Mario Draghi responded that "based on data, on today's data and today's projection, I think I see very few chances at all that interest rates could be raised this year." We expect the ECB to normalise monetary policy moving forward, albeit in a gradual and measured way, which could be communicated during their projections and policy update later in March.

Since the start of 2018, European equity indexes (DAX, CAC, IBEX, AEX, FTSEMIB) across the continent has rallied strongly as investors increasingly acknowledge that growth is increasingly entrenched in the Euro-region. The benchmark Stoxx 600 Index rose 2.7% in EUR terms (3.7% in SGD terms as the EUR rallied broadly) as of 29 January 2018. Some of the top performing stocks include GKN PLC, Fiat, Logitech International and Unione di Banche Italiane, while Suez, Pandora and Burberry Group can be found at the bottom of the performance table. The European equity market thus trades at 15.4X and 14.2X 2018's and 2019's estimated earnings respectively, as compared to its fair PE ratio of 13.5X, indicating that valuations are currently premium to where we deem them to be fair. European companies are projected to see their earnings grow by 8.4% in 2018 and by 8.7% in 2019, which is fairly reasonable given that various indicators and data points suggest that the ongoing recovery is increasingly entrenched (barring any unforeseen adverse political developments). **We maintain a 2.5 Stars "Neutral" rating for Europe, and advocate investors to remain an underweight exposure to European equities in their portfolios.**