European Equities

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US investors pile into European equities

By David Oakley, Investment Correspondent

US investors have pumped more money into European equities than at any time since 1977 in a big vote of confidence for the region and its ability to recover from the sovereign debt crisis.

Pension funds and other big US groups invested $65bn in European stocks in the first six months of 2013, the highest in 36 years over that time period, according to research compiled by Goldman Sachs' European strategy team from US Treasury data.

Early signs of economic recovery and rising business confidence have restored the faith of US investors in Europe as hopes grow that markets can rally further on a wave of stronger earnings in the second half of the year.

Eddie Perkins, chief investment officer of international equity at Goldman Sachs Asset Management, said: "The economic story makes Europe a good bet. We expect European equities to keep rising as the continent recovers."

Robert Parkes, equity strategist at HSBC, added: "We see earnings surprising on the upside, which will act like a tailwind for European equities."

HSBC says that European stocks are still 15 per cent undervalued compared with the long-term average. This is the case despite the big rise in European equities since July 2012 when Mario Draghi, European Central Bank president, pledged to do "whatever it takes" to save the euro. European stocks have risen 27 per cent since June 4, 2012.

However, equity markets still face substantial risks. A possible US military strike against Syria, worries about emerging markets instability and a renewed flare-up of the eurozone crisis could prevent further gains.

The poor performance of emerging markets, in particular, is a worry as European companies derive about a third of their revenues from that region. A further setback in emerging markets would hit their profits and revenues.

Despite the risks, the fact European stocks remain cheap is encouraging more US funds to put money into the market, say strategists and investment managers. HSBC's cyclically adjusted price earnings multiples are running at 11.4 times compared with an historical average of 14.8 times.

Sectors that are favoured by Goldman Sachs and HSBC are financials, telecoms and utilities as these have underperformed because of the eurozone debt crisis in the past few years.

European banking stocks, in particular, are back in vogue as the success of financials tends to depend on an improving economy. Expectations of more mergers and acquisitions activity in areas such as telecoms is also seen as positive for stocks.

Mr Parkes said: “There are still a lot of pessimists out there, but the cheapness of stocks makes them attractive. The risks are outweighed by the positives and I think European stocks can definitely move higher.”