EUROPE (4.0 STARS – VERY ATTRACTIVE)

1. GDP in the Eurozone managed to edge up slightly by 0.1% q-o-q in 1Q09, after a 0.1% growth in 4Q09. The growth is supported by further government spending and rising exports boosted by a weakening euro.
2. Investor sentiment deteriorated to 18.8 in Jun 10 after a 37.6 in May 10. This is a second consecutive month of decline following a sharp rebound from 37.9 in Mar 10 to 46.0 in Apr 10. The deterioration marks a less bullish view on the economy ahead as investors are worried that the series of cost cutting measures various governments have proposed to keep their debt under control may have a negative impact on economic activities.
3. PMI manufacturing index for Eurozone fell slightly to 55.6 in Jun 10, down from 55.8 in May 10 while PMI services index for Eurozone fell to 55.4 in Jun 10 from 56.2 in May 10. However, both indices continued to stay above the 50 mark since Oct 09, indicating continued expansion from both sectors.
4. Consumer prices remain below benign as prices measures by EU harmonised CPI index increased 1.6% y-o-y in May 10 after a 1.5% in Apr 10. On a m-o-m basis, prices increased by 0.1% in May 10 after a 0.5% increase in Apr 10.
5. With inflation rate below European Central Bank (ECB) long term target rate of 2.0% required for price stability, ECB continued to maintain their main refinancing rate at a suppressed level of 1.0%. They are likely to maintain the rate unchanged in the coming quarter as the present focus is to allow governments to clean up their balance sheet and to stimulate further growth.
6. In an unprecedented move, ECB injected liquidity into the market by buying government and private debts from markets which displayed dysfunctional behavior in an attempt to restore and maintain depth and liquidity in those markets. ECB also re-adopted fixed rate tender procedure and will conduct supplementary longer-term refinancing operations to inject liquidity to the market. Swap facilities with foreign nations were re-established so as to provide the European market with US dollar liquidity.
7. Capacity utilisation is picking up, rising for the third straight quarters after hitting a low of 69.6% in 3Q 2009. Presently, utilisation rate is at 75.2% in 2Q10, up from 72.3% in 1Q10. With the manufacturing sector showing continued expansion and capacity utilisation trending towards historical average, we believe this point towards a sustainable recovery within Eurozone. However, we remain cautious over the debt problems imminent in peripheral economies and will not surprised if some of these nations see a double dipping recession as a result of impair growth from their austerity measures to reduce debt.
8. ECB forecast of Eurozone GDP is revised downwards to 1.0% in 2010 and 1.2% in 2011. ECB believes that with the aggressive stance adopted by respective government in bringing down their budget deficit over the next couple of years, economic growth will be impaired and hence projected a slower growth rate than initially forecasted.
9. As of 30 June 2010, Stoxx 600 trades at a PE ratio 11.0 X and 9.2X forecasted 2010 and 2011 earnings. Earnings are expected to grow by 34.3% and 19.8% in 2010 and 2011 respectively. Valuations at this level suggest that Europe remains attractively priced among developed markets and we maintain Europe at a “Very Attractive” rating of 4 stars.