COMMENTARY

May 12, 2017

Dear clients and colleagues,

Following in the footsteps of the Netherlands in March, Macron's victory in France has, at least for now, contained the populist trend and the possibility of a Frexit while easing political risk in Europe. The focus will now turn to the June parliamentary elections.

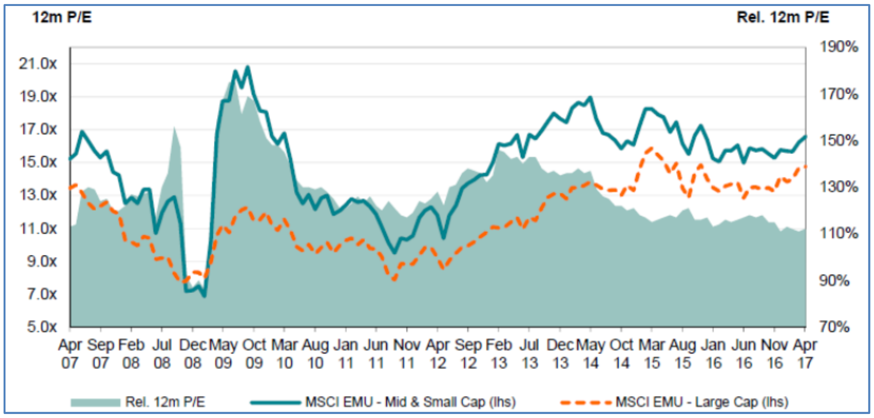
Given the level of fragmentation seen during the French presidential election, at this point in time estimating what the composition of parliament will be is difficult. Although "En Marche", Macron's centrist party, should be the most favored by voters, we cannot rule out the formation of a coalition government with the right wing Republican Party as both parties have similar economic platforms. Below are some of Macron's economic programs that could positively transform France:

- Lowering the corporate tax from 33% to 25% to line-up with the European average.
- Liberalizing the labour market by simplifying the labour code and encouraging negotiations at sector and company levels.
- Reducing employers' social contribution and payroll taxes.
- Improving public finances by reducing public expenditure to 52% of GDP.
- Lowering capital gain and dividend taxes to 30%.
- Proposing an investment plan of €50B over 5 years.

With the passing of some of these measures, we believe France's positioning within Europe will be greatly reinforced. A more business-friendly environment would benefit several companies in industries such as consumer and construction, thanks to fiscal stimulus and lower personal taxes they should do particularly well.

Overall, we continue to believe that stocks will benefit from an improved risk sentiment towards Europe. The positive momentum built over the years should continue to support small cap stocks. The Euro Stoxx companies that have already released their Q1 earnings numbers, have confirmed this trend by exceeding street estimates 80% of the time while average EPS growth has been robust at 18% over the same period last year.

Continuing to be attractive, Eurozone small cap equities, shown below, are reasonably priced versus their larger counterparts but they do not factor in the higher earnings growth potential they can offer.



Source: Exane BNP

Have a good weekend.

The Global Alpha Team