Special Report

Europe Capital Markets Newsletter – 1Q25

aranca

April 2025

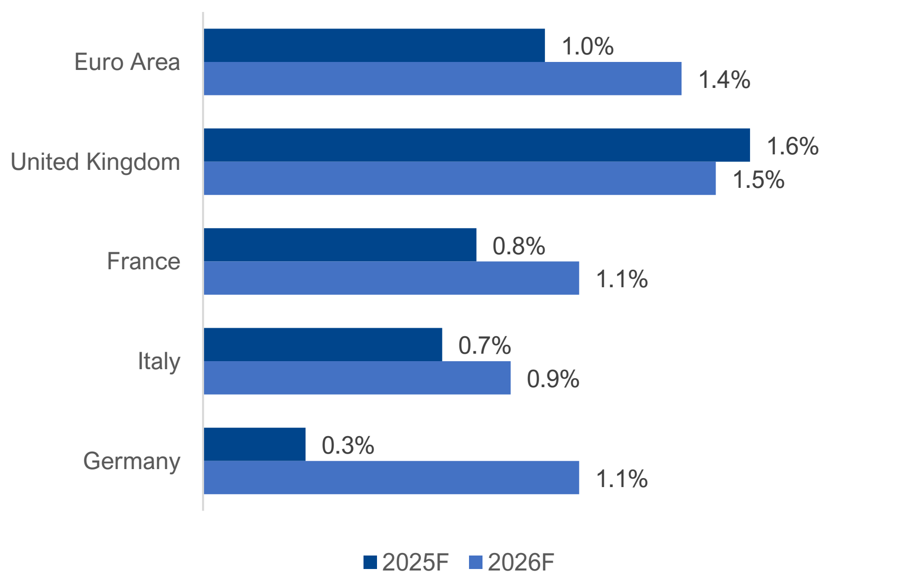
Executive Summary

Easing inflation and rate cuts offer limited relief as Europe’s growth outlook remains subdued	• Europe's economic recovery remains fragile, with only a modest pickup expected in 2026, led by marginal gains in household consumption and easing inflationary pressure. • While falling inflation and stable labor markets are creating room for interest rate cuts, manufacturing activity remains subdued.
Euro Gains Face Pressure from Yield Gap and Cautious ECB Stance	• The Euro has shown strong short-term gains but remains vulnerable to tariff related uncertainties and ECB’s cautious policy stance. • The persistent yield gap between the US and Europe reflects weaker inflation and growth expectations, which continues to exert downward pressure on the Euro.
Europe outperformed the broader US market in 1Q25	• In 1Q25, STOXX Europe 600 outperformed the S&P 500 by ~8.9%, driven by Germany’s EUR 500 billion fiscal stimulus and capital rotation amid US trade policy uncertainty. • Banks and defense stocks led Europe’s rally, while the UK markets were up due to strong performance of the energy sector. • Consumer stocks lagged across the region due to cautious sentiment and lower discretionary spending.
Europe’s global players likely to outperform local peers	• Europe’s economic growth has been relatively sluggish in recent years, and the outlook remains weak, with the IMF forecasting a lower GDP growth compared to other developed and emerging markets. • In this backdrop, companies with higher international revenue exposure are well positioned to outperform, benefiting from a relatively stronger global economy, a weaker Euro, and upcoming policy shifts by the ECB.

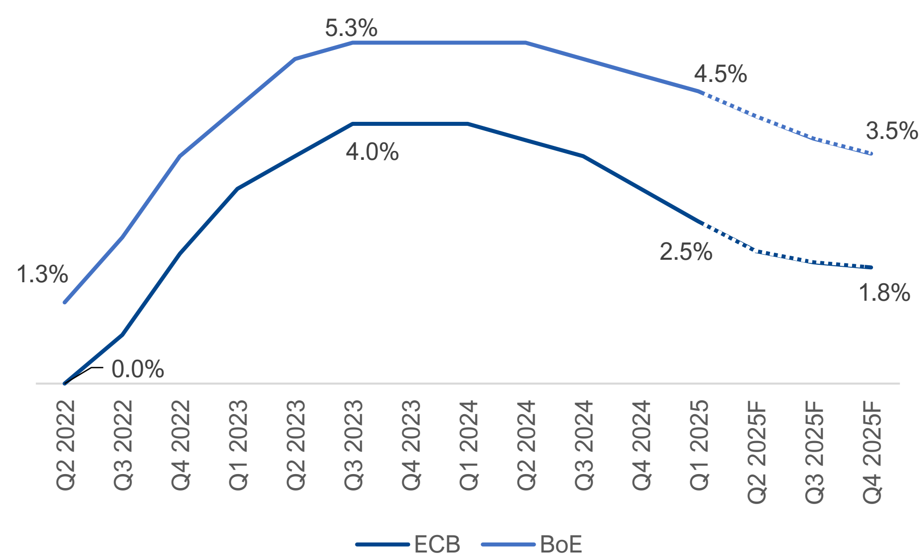
Modest GDP growth outlook amid rate cut expectations

- GDP growth is expected to pick up across most European economies in 2026, supported by easing inflation and a rebound in household consumption, especially in Germany and France.
- Elevated energy costs and geopolitical tensions, particularly in the Middle East, pose key threats to the recovery, potentially dampening external demand and raising inflation pressures.
- in the aftermath of the COVID-19 pandemic, both the ECB and BoE increased their policy rates that peaked in 2023 at 4.0% and 5.25%, respectively, marking the end of their tightening cycles.
- The market implied forecast assumes at least three further rate cuts beyond April by the ECB and BOE.

GDP Growth Forecast (IMF, 2025F–2026F)



Central Bank Policy Rate Trend (ECB & BoE)



Source: *IMF, Reuters Eikon, Aranca Research*

Eurozone inflation remained above 2% in 1Q25, while PMI improved

Inflation

Country	2024												2025		
	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	Jan	Feb	Mar
UK	4.0%	3.4%	3.2%	2.3%	2.0%	2.0%	2.2%	2.2%	1.7%	2.3%	2.6%	2.5%	3.0%	2.8%	NA
Eurozone	2.8%	2.6%	2.4%	2.4%	2.6%	2.5%	2.6%	2.2%	1.7%	2.0%	2.2%	2.4%	2.5%	2.3%	2.2%
Germany	3.1%	2.7%	2.3%	2.4%	2.8%	2.5%	2.6%	2.0%	1.8%	2.4%	2.4%	2.8%	2.8%	2.6%	2.3%
France	3.4%	3.2%	2.4%	2.4%	2.6%	2.5%	2.7%	2.2%	1.4%	1.6%	1.7%	1.8%	1.8%	0.9%	0.9%
Italy	0.9%	0.8%	1.2%	0.9%	0.8%	0.9%	1.6%	1.2%	0.7%	1.0%	1.5%	1.4%	1.7%	1.7%	2.1%

Manufacturing PMI

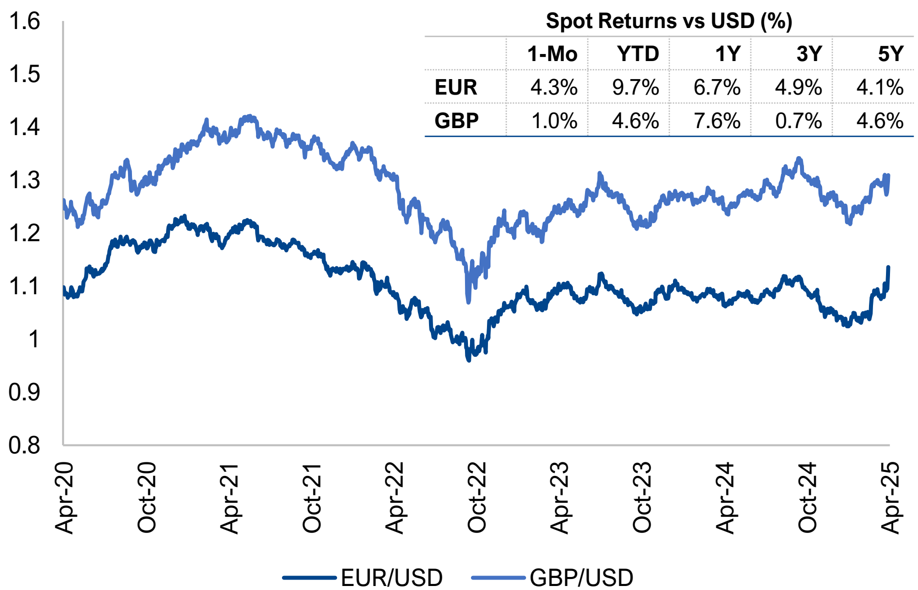
Country	2024												2025		
	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	Jan	Feb	Mar
Eurozone	46.6	46.5	46.1	45.7	47.3	45.8	45.8	45.8	45.0	46.0	45.2	45.1	46.6	47.6	48.6
UK	47.0	47.5	50.3	49.1	51.2	50.9	52.1	52.5	51.5	49.9	48.0	47.0	48.3	46.9	44.9
Germany	45.5	42.5	41.9	42.5	45.4	43.5	43.2	42.4	40.6	43.0	43.0	42.5	45.0	46.5	48.3
France	43.1	47.1	46.2	45.3	46.4	45.4	44.0	43.9	44.6	44.5	43.1	41.9	45.0	45.8	48.5
Italy	48.5	48.7	50.4	47.3	45.6	45.7	47.4	49.4	48.3	46.9	44.5	46.2	46.3	47.4	46.6

Source: *Eurostat, Aranca Research*

The Euro surged amid tariff-driven market volatility

- The Euro was highly volatile in 1Q25, recently reaching its three-year high against the US Dollar, driven by capital flight from the US assets amid trade tensions. The Euro's trajectory will largely depend on the ECB's monetary policy decisions and the broader global economic environment.
- Government bond yields in the Eurozone and the UK have come down since their 2023 highs, while the US yields remain high. The gap between the US and European yields points to weaker inflation and growth expectations in Europe. This difference is likely to continue through 2025, which could put renewed pressure on the Euro, especially if the ECB maintains a more cautious stance.

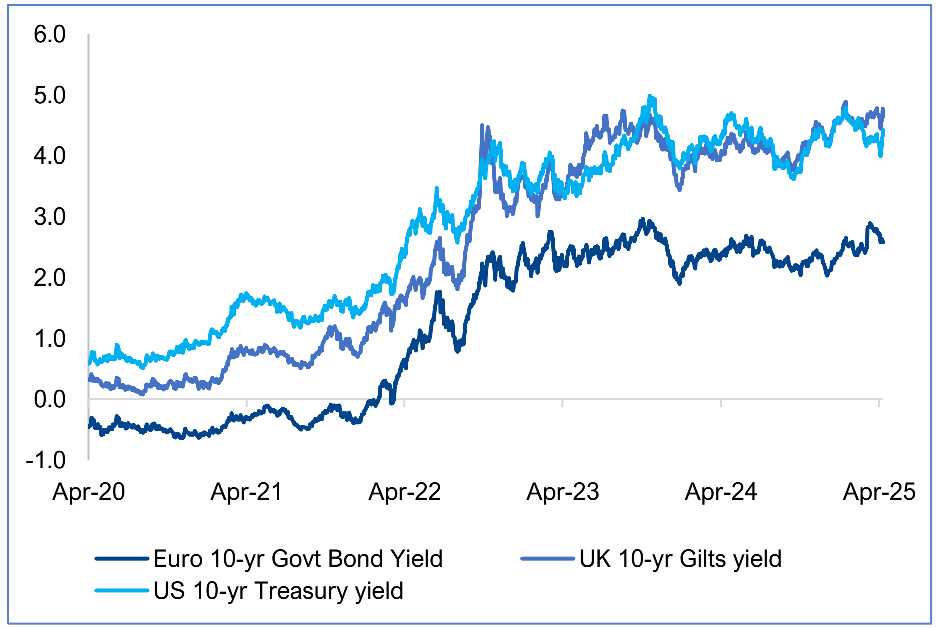
Currency Performance vs. the USD



Spot Returns vs USD (%)

	1-Mo	YTD	1Y	3Y	5Y
EUR	4.3%	9.7%	6.7%	4.9%	4.1%
GBP	1.0%	4.6%	7.6%	0.7%	4.6%

10-Year Government Bond Yields

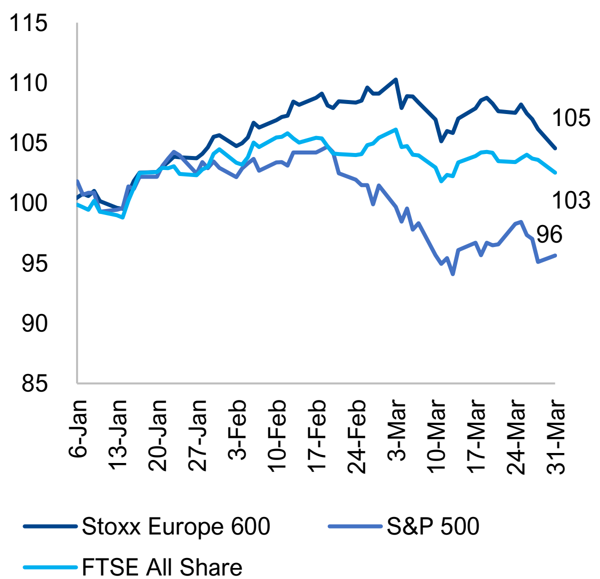


Source: *IMF, Reuters Eikon, Aranca Research*

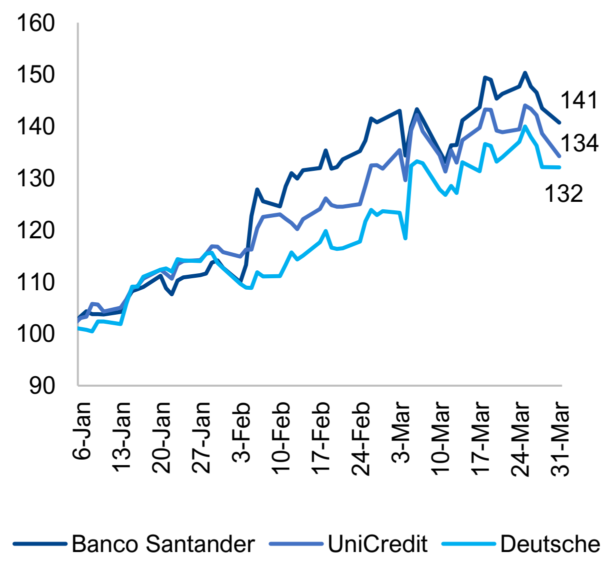
European markets significantly outperformed the US markets in 1Q25

- In 1Q25, STOXX Europe 600 outperformed the S&P 500 by ~8.9%, driven by attractive stock valuations and Germany's aggressive fiscal stimulus measures, including EUR 500 billion for infrastructure and an exemption from the constitutional debt brake to support increased defense spending.
- Defense stocks surged as investors bet for a long-term European rearmament and potential reconstruction efforts in Ukraine.
- Rheinmetall's share price rose by 119% in 1Q25, while Thales and Leonardo increased by 78% and 72%, respectively.

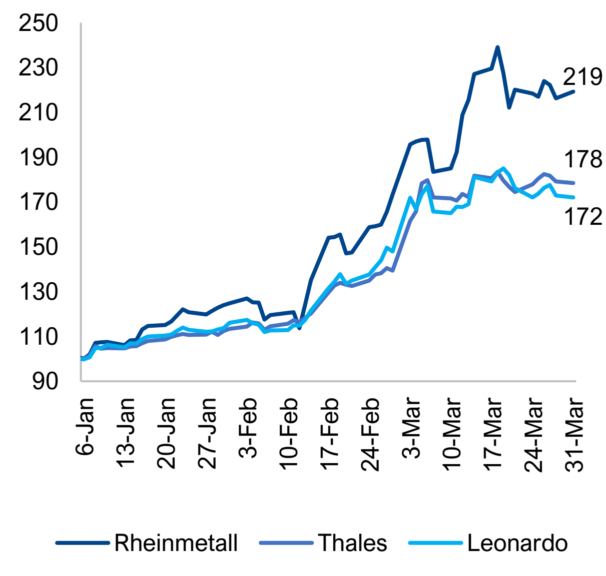
European Index Performance (1Q25)



STOXX Europe 600 Banks (Top 3)



STOXX Europe 600 Defense (Top 3)

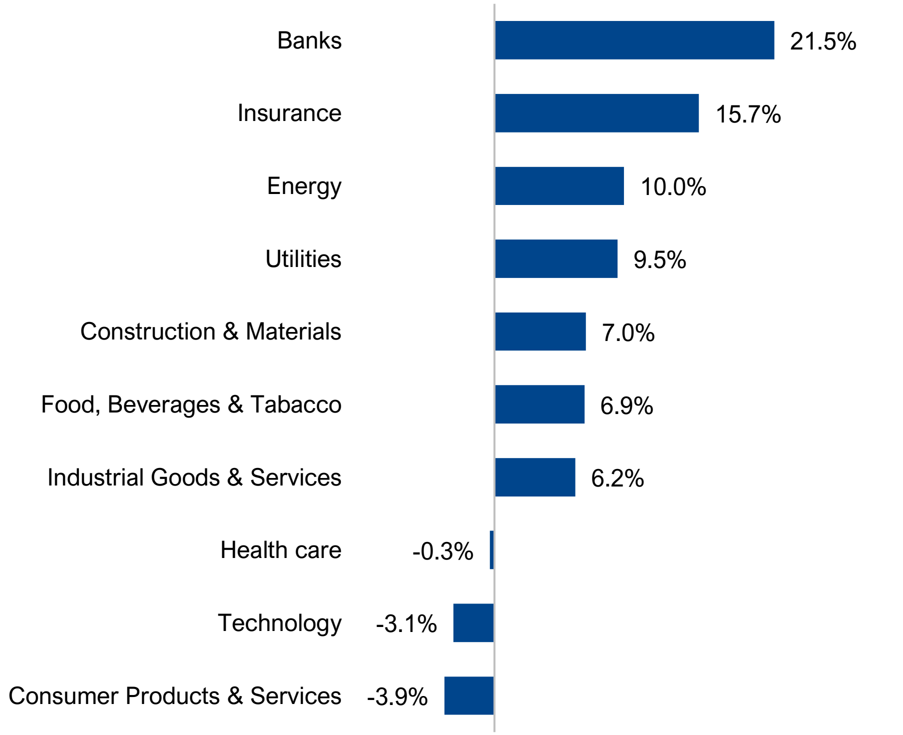


Source: *Bloomberg, Aranca Research; all charts rebased starting from January 1, 2025*

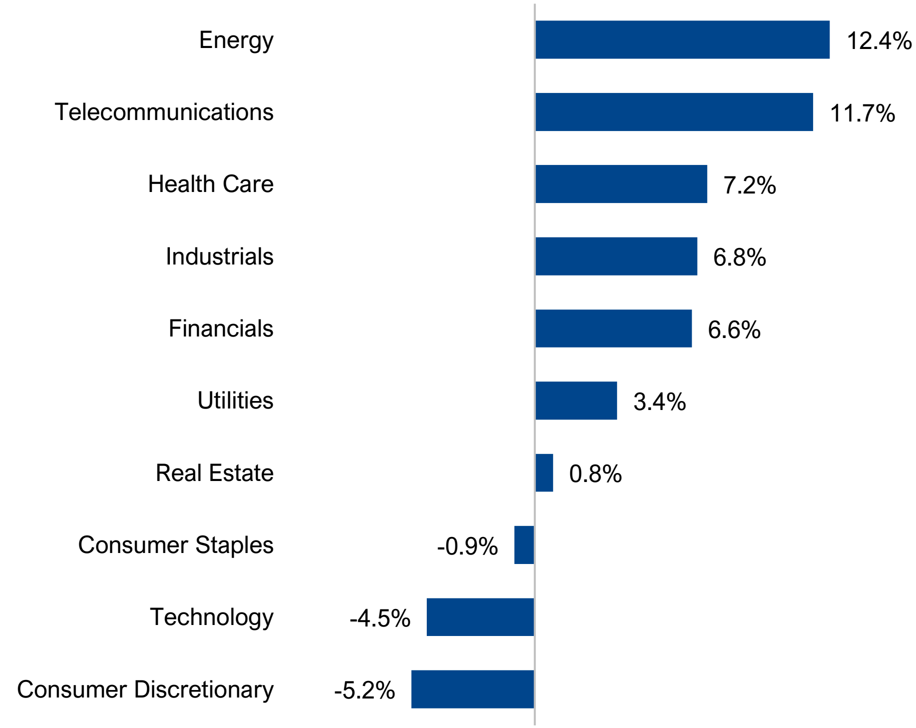
Diverging trends across indices: European gains led by banks, UK by energy

- Banks and insurance were the top performing sectors in Europe in 1Q25, while energy and telecom led in the UK.
- Banks posted strong earnings and were relatively insulated from trade tariff concerns.
- Defense, infrastructure, and energy sectors were other top performing sectors in Europe in 1Q25. Meanwhile, consumer stocks declined due to a cautious sentiment, lower discretionary spending, and a shift to cheaper options, despite steady incomes.

STOXX Europe 600

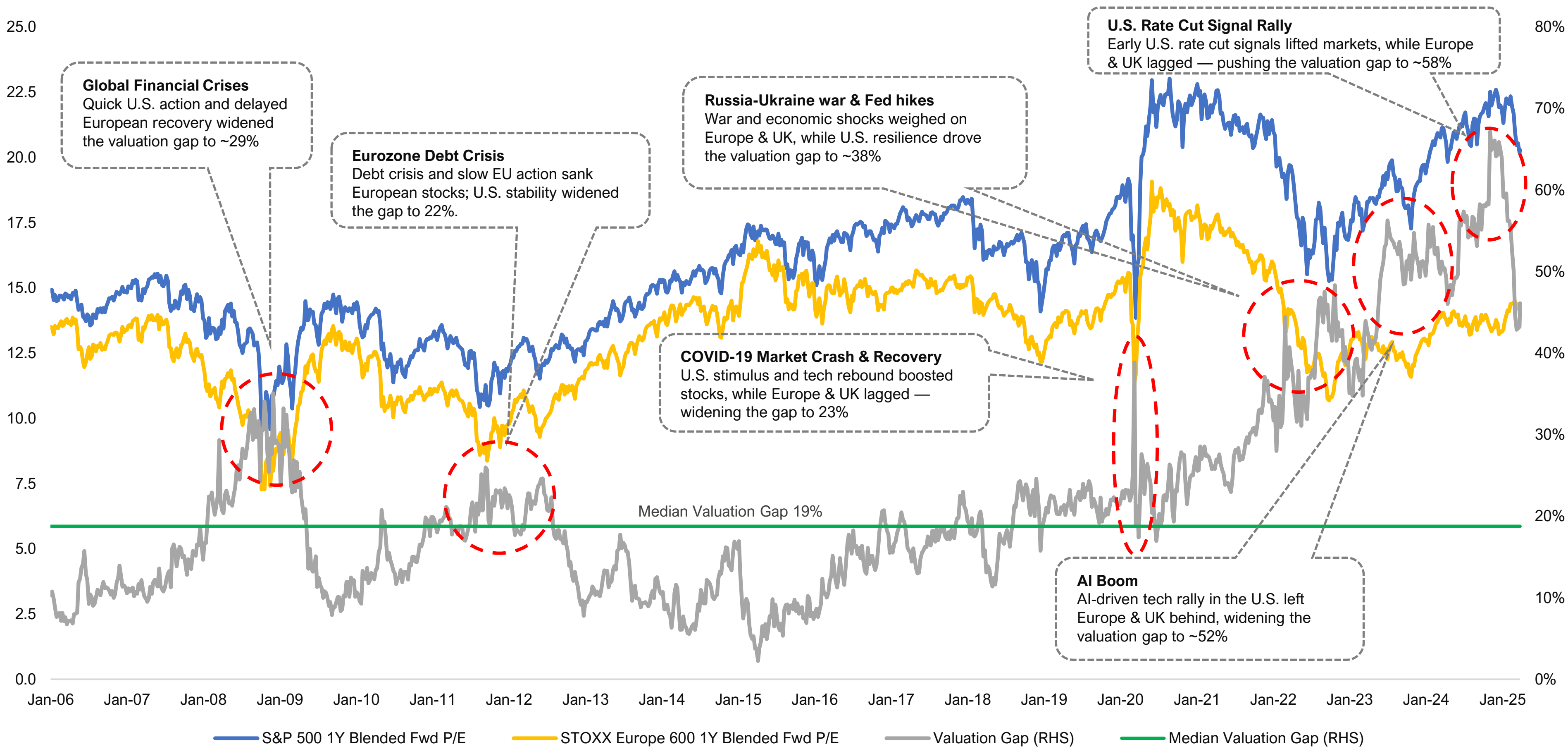


FTSE All-Share



Source: *Bloomberg, Aranca Research*

European Stocks Trade at a Long-Term Valuation Discount to US Markets

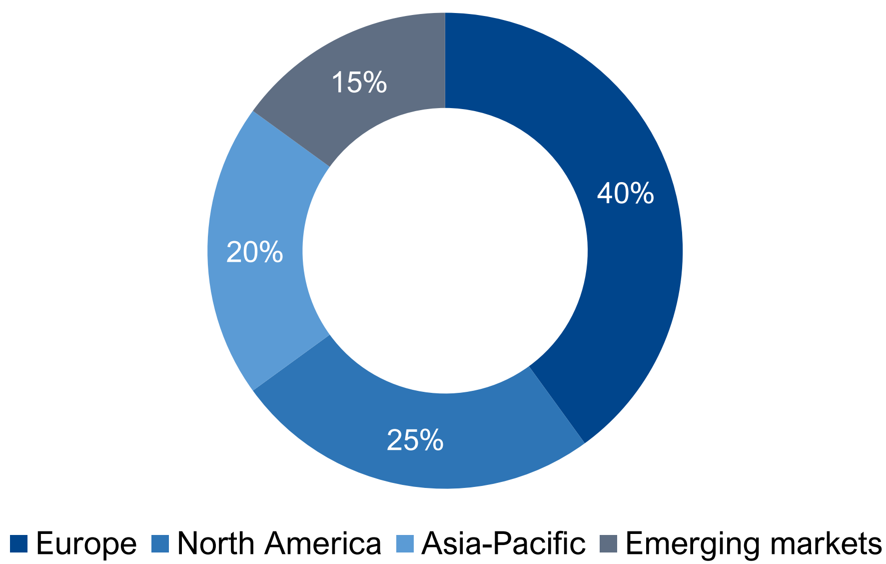


Source: *Bloomberg, Aranca Research*

European Companies Benefit from Significant International Sales Exposure

- European companies generate 60% of their revenues from international markets, significantly more than those based in Japan (40%), the US (30%), and emerging markets (25%). This extensive global footprint helps insulate them from weak domestic demand and allows them to benefit from high-growth markets within the global economy. Moreover, a weaker Euro and low relative valuations provide a supportive backdrop for Europe's globally oriented companies.
- North America accounts for 25% of total sales, with many European companies maintaining large manufacturing footprints in the US and integrating their supply chains tightly.
- Technology (79%), Health Care (77%), and Food & Beverage (75%) have the highest exposure to international markets.

STOXX Europe 600: Region-wise Sales



STOXX Europe 600: Sector-wise International Sales

Sector	International Sales
Technology	79%
Health Care	77%
Food, Beverage, and Tobacco	75%
Media	75%
Basic Resources	73%
Chemicals	68%
Industrial Goods and Services	66%
Personal Care, Drug, and Grocery	62%
Automobiles and Parts	60%

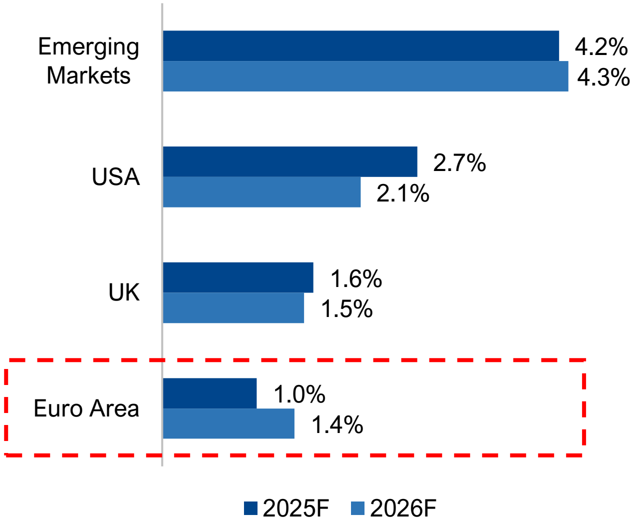
Note: *Europe represented by STOXX 600 Index, Japan by TOPIX, US by S&P 500, and emerging markets by MSCI Emerging Markets*

Source: *Aranca Research, Broker Reports*

Economic Growth Challenges & Monetary Policy Tailwinds for Globalized European Firms

Euro Area Economic Growth Lags Behind Peers

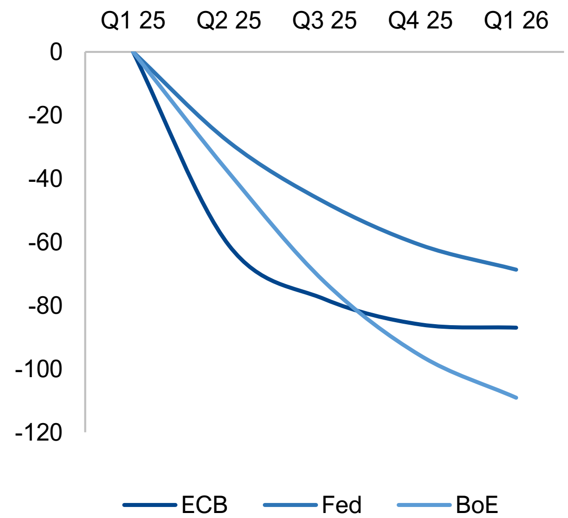
IMF Real GDP Growth Forecast



- The Euro Area GDP is expected to grow by 1.0% and 1.4% in 2025 and 2026, respectively, significantly lower than the US and emerging markets, suggesting limited domestic demand and slow corporate earnings growth.
- However, firms with a significant global revenue exposure will likely benefit from stronger growth outside Europe.

ECB's Aggressive Rate Cuts To Support International Earnings

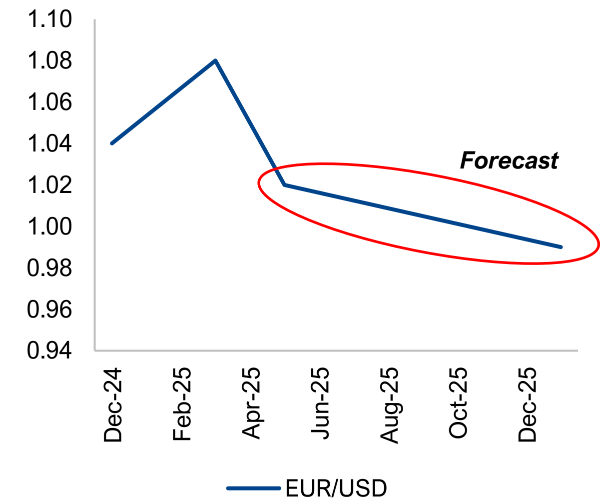
Policy Rate Expected Cuts (basis points)



- The ECB is set to cut rates more aggressively than the Fed, aiming to stimulate growth amid falling inflation.
- Low interest rates will provide further tailwinds to companies with a high international exposure due to weakening currencies, decreasing borrowing costs, and increasing earnings power.

Expected Weakness in Euro to Benefit Exporters

EUR/USD



- The Euro is expected to depreciate further amid rate cuts and economic softness.
- A weaker Euro benefits European exporters and multinational firms.
- Companies earning in stronger foreign currencies will benefit when repatriating profits.

Source: *IMF, Bloomberg, Aranca Research*

European Companies With High International Sales Exposure

- The companies listed below generate a large portion of their revenues outside Europe and will be key beneficiaries of strong global economies and falling Euro amid accelerated rate cut expectations.
- These companies are trading at a lower P/E multiple (a median percentile rank of 26) vs. their historical 5- and 10-year multiple. Given their low relative valuation and exposure to regions with a high growth potential, we believe these companies can outperform their local peers.

Company	Industry	Country	Market Cap (USD m)	Sales Exposure		P/E		NTM P/E Percentile Rank	
				Europe	International	FY25E	FY26E	5yr	10yr
Prudential	Insurance	UK	24,844	1%	99%	9.1x	7.9x	26	19
Standard Chartered	Banks	UK	29,140	2%	98%	6.4x	5.4x	42	21
ASML Holding	Technology	Netherlands	257,476	5%	95%	24.0x	20.2x	2	10
Rio Tinto	Basic Resources	UK	95,817	5%	95%	8.9x	8.9x	45	27
ASM International	Technology	Netherlands	20,985	6%	94%	21.5x	17.4x	14	57
Ashtead Group	Industrial Goods & Services	UK	21,626	8%	92%	13.6x	12.3x	3	25
Tenaris	Energy	Luxembourg	16,764	10%	90%	8.4x	8.2x	42	20
Epiroc AB	Industrial Goods & Services	Sweden	21,960	11%	89%	21.6x	19.5x	10	33
Experian	Industrial Goods & Services	UK	40,053	12%	88%	27.9x	24.9x	35	58
ACS	Construction and Materials	Spain	13,997	13%	87%	16.1x	13.9x	86	93
Telefonaktiebolaget LM Ericsson	Telecommunications	Sweden	24,091	14%	86%	12.2x	11.6x	44	26
VAT Group AG	Industrial Goods & Services	Switzerland	10,161	14%	86%	30.6x	25.1x	12	41
Anheuser-Busch InBev	Food, Beverage & Tobacco	Belgium	122,003	15%*	85%	16.2x	14.5x	22	15
InterContinental Hotels Group	Travel & Leisure	UK	15,733	15%*	85%	20.5x	18.1x	30	38
Pearson	Media	UK	10,058	17%	83%	17.5x	15.7x	62	79
Anglo American	Basic Resources	UK	30,979	18%	82%	17.6x	13.2x	97	94
Unilever	Personal Care, Drug & Grocery Store	UK	152,547	20%	80%	17.1x	16.1x	19	10
Novo Nordisk	Health Care	Denmark	283,367	21%*	79%	15.0x	12.2x	1	2
Hermes	Consumer Products & Services	France	271,901	24%	76%	49.1x	42.2x	41	71
Nestlé	Food, Beverage & Tobacco	Switzerland	268,020	24%	76%	18.5x	17.4x	18	9
LVMH	Consumer Products & Services	France	296,973	25%	75%	19.6x	17.6x	2	15
MEDIAN				**14%**	**86%**	**17.5x**	**15.7x**	**26**	**26**

** EMEA region – includes Europe, the Middle East, and Africa*

Source: *S&P Capital IQ, Koyfin, Aranca Research*

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