

EUROPEAN MIDCAPS: FOCUSING ON MACRO TRENDS



Marion Casal and Olivier de Royère
Portfolio Managers

The under performance of the Euro zone mid-caps over the last year is a rare event that investors should take advantage of. Over the long run the asset class benefits from a stronger growth profile than their large cap counterparts, leaner business models and less efficient market behavior. They represent a very deep -2500 stocks- and diversified playground both in terms of sectors and styles.

LIFESTYLE

Consumer sectors will be totally transformed by the rising of the Chinese Millennials, representing 415 million customers (more than the working population of all Europe and the US): they will buy mostly online and will allocate a much larger share of "having fun" spending than their parents. In the consumer goods sector, some brands such as SMCP are focusing their expansion in Asia and intensifying their physical and online presence, which allow them to deliver more than 20% growth at constant currency in the region.

The rising of Millennials

Consumers will accelerate the trend of "Casual Wear" on a global basis: athletic brands are becoming dominant in all consumer products categories and they will keep-on expanding market share.

BETTER LIFE

In 1998 21% of Europeans were aged 65 years or older: they will be 47% in 2030. This demographics earthquake will provide a structural tailwind for care services -such as nursing homes- drugs and pharmaceutical devices. Given the record number of compounds authorized by the FDA in 2018, the midterm prospects for the pharma sector are excellent provided the pressure on US prices remain under control. But our Better Life theme goes beyond that and reflects the desire of people to take care of their well-being throughout their lives. Millennials who live in dense urban areas are thriving to increase their Fitness activities, providing a powerful kick to the Sport related businesses like Technogym.

SMART ENERGY

Europe Energy Revolution is under way and the newly elected European Parliament will even accelerate the course. In 2000 less than 10% of the energy production came from renewable sources: this share will be 35% by 2030. Wind but even more solar are replacing fossil fuel, thus making electrification a transformative force all over the

sectors of the economy: Transports, Buildings and Manufacturing. A major wave of investments in grids should deliver organic growth of 4.5% per year through 2050. Growth will be strong; our challenge is to find companies that have healthy returns such as the biomass and solar electricity producer Albioma who benefits from contracts with secured margins.

DIGITAL IMPACT

We focus on specific themes (payments, SMACS, Automation) that are growing much more than traditional market. The price of a small robot has fallen below the annual cost of an assembly worker in China in 2016: this level of cost advantage opens up huge opportunities for growth. European companies such as Kion are specialized in automated solutions for warehouses, business that is expected to grow high single digit this year. Overall, the market of industrial robots is expected to grow at a sustained 5-6% per year over the next decade.

The weakness of the economy is currently impacting small caps more than the rest of the market because they anticipate recoveries less than large caps. It gives us investment opportunities in a segment which has the highest potential. Some cyclical companies can weather the downturn better than market thinks thanks to their involvement in structural growth themes.