

European Equities Selling at a Discount to Historical Averages

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With the various issues plaguing Europe over the past few years, it isn't surprising that equity market valuations have been depressed. Yet given the general feeling that the worst of the European crisis may be behind us, allocations to Europe have been increasing and certain markets have experienced strong gains in 2013. Some may feel they missed the rally or that valuations are stretched. Yet if the earnings cycle is just starting to turn up, there could still be opportunities for growth in earnings as I discussed in a previous [blog post](#). To provide context for the current valuations, we compare both the [trailing](#) and estimated [price-to-earnings \(P/E\) ratio](#) for the 10 largest developed European countries to other regional indexes and their historical medians. **Figure 1: Regional and Country Price-to-Earnings Ratios**

Price-to-Earnings Ratio [1/31/1997–10/31/2013]				
Index	Historical Median	Current		Current Estimated Discount to Median
		Trailing	Estimated	
MSCI Emerging Markets	13.2x	12.2x	11.7x	-11.6%
MSCI Europe	18.3x	19.6x	14.6x	-20.1%
S&P 500	17.9x	16.7x	15.9x	-11.4%
Top 10 Countries of Europe				
MSCI Germany	14.7x	15.4x	13.3x	-9.5%
MSCI United Kingdom	18.5x	20.5x	13.4x	-27.5%
MSCI France	19.9x	22.2x	14.5x	-27.0%
MSCI Italy	18.6x	28.7x	15.0x	-19.2%
MSCI Netherlands	16.7x	21.8x	15.7x	-6.3%
MSCI Switzerland	19.6x	18.6x	16.3x	-16.8%
MSCI Spain	14.4x	62.2x	16.5x	14.5%
MSCI Sweden	16.7x	16.4x	17.0x	1.6%
MSCI Denmark	19.1x	19.0x	17.1x	-10.7%
MSCI Belgium	14.7x	13.5x	17.4x	18.2%

Sources: WisdomTree, Bloomberg (01/31/1997–10/31/13).
You cannot invest directly in an index. Subject to change. Past performance is not indicative of future results.

For definitions of indexes in the chart, please visit our [Glossary](#). • **Estimated Earnings Improvement Strong for Europe** – Of the major regional indexes, the MSCI Europe Index showed the largest improvement in the estimated P/E ratio, thus signaling the greatest expectations for earnings growth compared to the [S&P 500](#) and MSCI Emerging Markets indexes. • Within Europe, the best improvements in expected

earnings look to be in Italy and Spain, which have elevated P/E ratios on a trailing 12-month basis but see more normalized earnings and valuations in line with the rest of Europe. It is important for these two countries to begin normalizing, because they have provided some of the greatest headwinds for the European economy over the past six quarters. • **Europe Region with the Largest Discount to Its Own History** – Europe's estimated P/E ratio compared to its historical median showed a discount of 20%, greater than both the S&P 500 Index and the MSCI Emerging Markets Index. To be fair, the emerging markets have the lowest absolute valuation, but they have historically sold at a lower valuation compared to such developed markets as Europe or the United States. • **United Kingdom, Germany, France Lowest-Priced Markets** – Looking within the individual country markets we notice the United Kingdom and Germany leading the way with the lowest estimated P/E ratios—just above 13x earnings and about 10% lower than Europe's valuation as a whole. Both countries being among the region's top economies, it is interesting that they also have the lowest current valuations. If one looked for the highest discount to its historical median, France takes the second spot after the United Kingdom. France also happens to have the third-lowest estimated P/E ratio. **Implementation** Europe has been one of the primary risks for the global economy—with sluggish growth, over-leveraged countries and banks being a prime concern for many investors. With these concerns and risks, it may be no surprise that Europe looks attractive from a price-to-earnings perspective, compared to other regions and even its own history. If Europe's economy can expand upon its recent growth, it could be very supportive for future earnings growth and the regional equity markets. We feel there are different ways to play the European recovery theme, depending on one's conviction, and WisdomTree has designed many different Indexes to provide exposure: • **WisdomTree Europe SmallCap Dividend Index** – designed to provide exposure to the small-capitalization segment of the European dividend-paying market • **WisdomTree Europe Hedged Equity Index** – designed to provide exposure to large-capitalization European exporters while at the same time neutralizing the currency exposure • **WisdomTree United Kingdom Hedged Equity Index** – designed to provide exposure to global exporters listed in the United Kingdom while at the same time neutralizing the currency exposure • **WisdomTree Germany Hedged Equity Index** – designed to provide exposure to German exporters while at the same time neutralizing the currency exposure *Read the full research [here](#).*

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Foreign investing involves special risks, such as risk of loss from currency fluctuation or political or economic uncertainty. Investments focused in Europe are increasing the impact of events and developments associated with the region, which can adversely affect performance. Investments in currency involve additional special risks, such as credit risk and interest rate fluctuations. Investments focusing on certain sectors and/or smaller companies increase their vulnerability to any single economic or regulatory development. This may result in greater share price volatility.