

## Flash Economics

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### European equities and the euro have an upside potential

We can now see that the valuation of European equities is weak, but not very weak; and that the euro's exchange rate is weak, but not very weak.

Yet, the net open position on the euro is very short and non-residents are massive sellers of European equities: investors are therefore behaving as if they expected a recession in the euro zone.

However, the euro-zone economy is resilient as demand is clearly being stimulated: once investors revise their expectations for euro-zone growth, equity valuation will be raised and the euro will appreciate.

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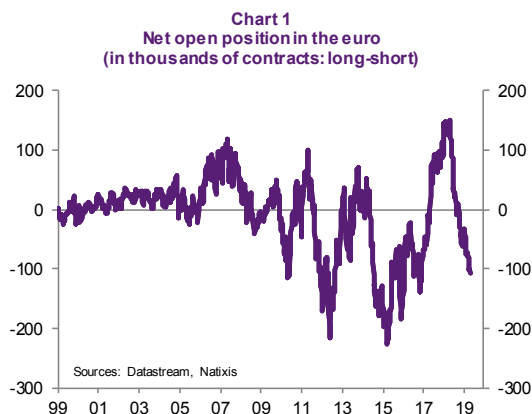
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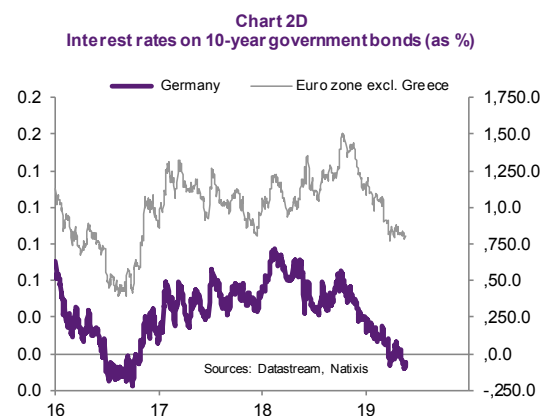
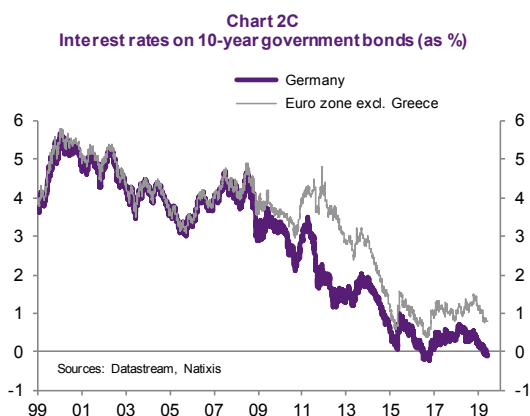
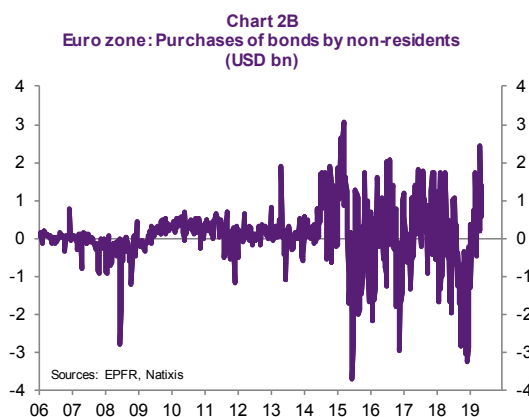
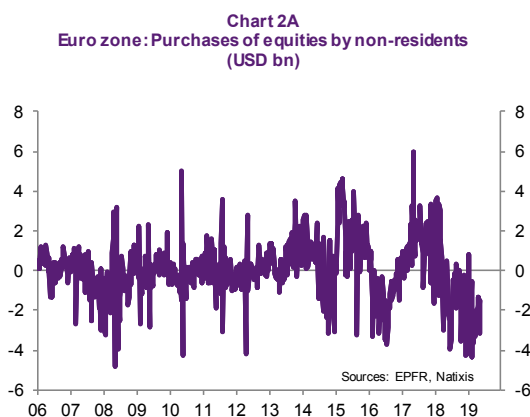
## The valuation of euro-zone equities and the euro's exchange rate are not very weak despite capital outflows

We are now seeing:

- Short-term capital outflows from the euro zone, given the net open position in the euro (Chart 1);



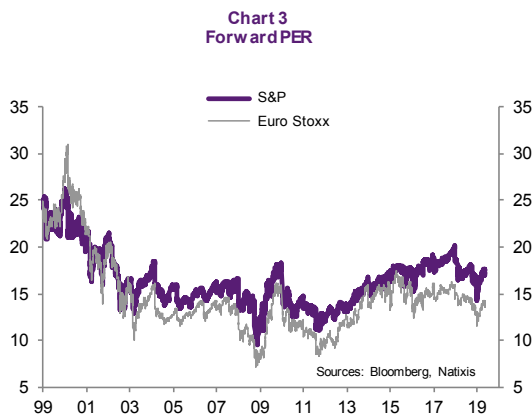
- Sales of euro-zone equities by non-residents (Chart 2A) who are, furthermore, buyers of bonds (Chart 2B), which explains the very low level of long-term interest rates (Charts 2C and D).



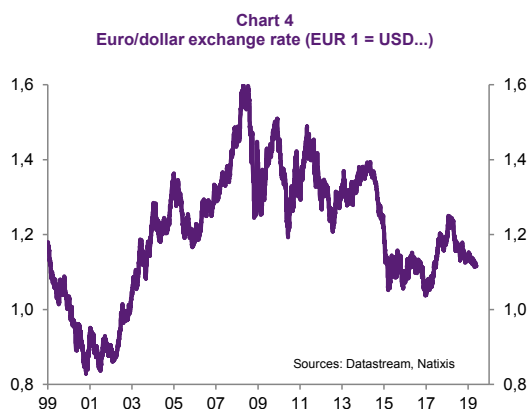
So investors show that they expect a recession in the euro zone.

Yet:

- While valuation of euro-zone equities is weak, it is not very weak (Chart 3);



- While the euro is weak, it is not very weak (Chart 4).

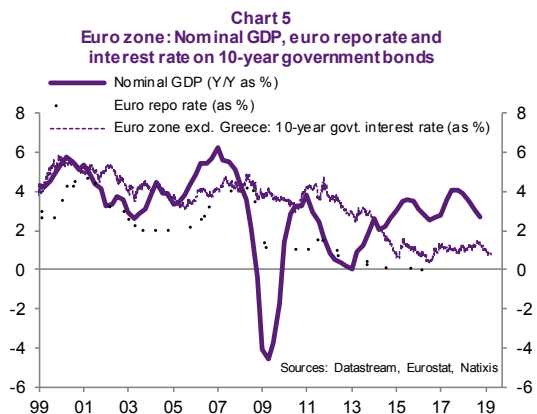


Euro-zone equity valuation and the euro's exchange rate are therefore resilient despite the expectations of a recession.

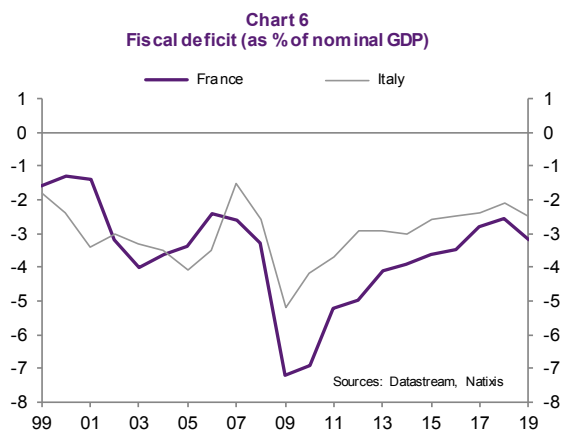
## But the euro-zone economy is resilient

But in reality, the euro-zone economy is resilient and the euro zone is not sliding into recession, due to the stimulation of demand via:

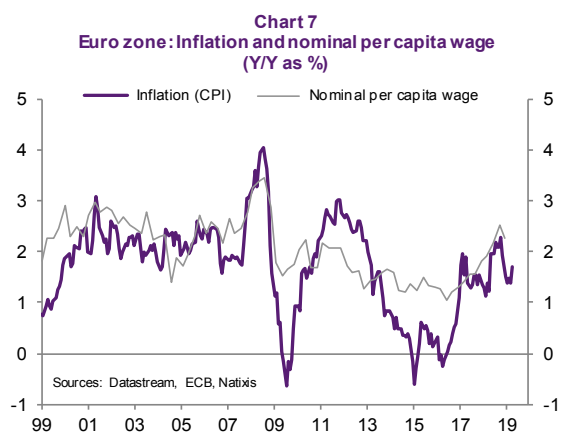
- The expansionary monetary policy (Chart 5);



- The expansionary fiscal policy in France and Italy (**Chart 6**);

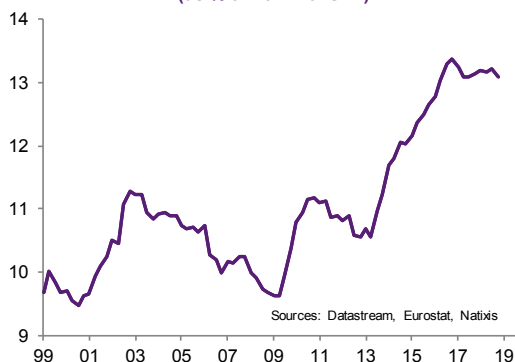


- The decline in inflation that increases real wages (**Chart 7**);

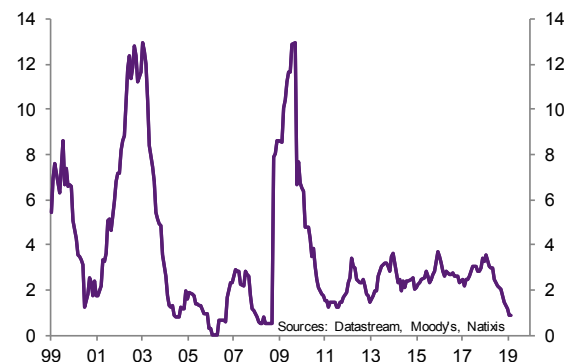


- The high level of corporate profitability (**Chart 8A**) and the fall in defaults (**Chart 8B**).

**Chart 8A**  
Euro zone: Profits after tax, interest and dividends  
(as % of nominal GDP)



**Chart 8B**  
Euro zone: High Yield default rate (as %)



**Conclusion: As a result, an upside potential for the valuation of European equities and an appreciation of the euro**

Even though investors currently expect a recession in the euro zone, and the valuation of euro-zone equities and the euro's exchange rate are weak, they are not very weak.

This shows that we can expect a quite high valuation of equities and a quite strong exchange rate for the euro once investors understand that the euro-zone economy is resilient and that no recession is coming.

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