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# French Presidential Election: A Market-Friendly Outcome, But Issues Remain

The outcome of the French Presidential election will no doubt be greeted by investors with a sigh of relief. Emmanuel Macron, the market's preferred candidate, has won Sunday's vote. In this note, our Head of Europe, Australasia and Far East (EAFE) Equities David Hussey examines if Mr. Macron's victory could put to bed lingering fears about the outlook for European equities.

It's interesting that the French political system appears to be following what I call the 'US Election Playbook'. The old guard of the Gaullist right and socialist/communist left wing parties have been replaced by the populist movement, which is often perceived as being against globalization, and a market-savvy political newcomer offering a fresh approach. So what's going on and do we care?

Well it seems that in France, as in the US, electorates are tired with the old guard and want a new direction. Mr. Macron promises to introduce economic reform and modernize the French economy – just like many of his predecessors. But I believe there is a more than fair chance that he will not ultimately have the mandate or power to do that. If history repeats itself, little will change in reality.

So should his victory over Ms. Le Pen be viewed as 'green light' for large transfers of funds from US stocks into European risk assets given that the perennial bear point of political risk has supposedly been put to bed? In the short-term, I believe it is likely to encourage investors to move into Europe. After all, the continent does boast a relatively attractive narrative - better valuations, positive earnings growth and economic momentum[1].

From a longer-term perspective, however, should Mr. Macron fail in his efforts to reform the economy and create new jobs, and the anti-globalization forces grow in strength in the wake of a weaker global economy, it is more than likely that the populist parties will be back. In my view, political risk will remain around the western democracies until the wages and jobs situation improve. And this will translate into persistent uncertainty and volatility for the markets.

That being said, the European equities market has had a reasonable start to the year rising nearly 7.1% in euro terms, matching the return from the S&P 500 index[2]. However, this belies an early sell-off in more value-biased stocks as bond yields tightened on disappointment regarding the US administration's initial inability to garner enough support to push through healthcare reforms. It has also cast some doubt on the administration's ability to introduce tax reform and infrastructure spending.

We believe the outlook generally for the rest of this year should be reasonably positive for more 'value opportunities' versus the defensive and often expensive growth names. As ever,

[1] Bloomberg, as of May 2, 2017
[2] FactSet, as of April 30, 2017

we believe those who have invested their time and resources on quality research should benefit. We continue to see value in energy, mining and financial companies – the more traditional value sections of the market.  Companies we favor typically have healthy free cashflow yields and dividend yields that are higher than market levels.

In summary, Mr. Macron's election will not signal the end of European political uncertainty. But investor interest in Europe equities will likely rise – where free cashflow yields can appear attractive relative to their peers and economic momentum could see margins as well as earnings expand in 2017 and beyond.