

Picking up the baton

BlackRock®

September 2021

The global restart has broadened beyond the US and China, with Europe benefiting from a pickup in activity.

Accommodative policy and attractive valuations support the case for European equities. Despite recent positive sentiment and a pickup in flows, Europe remains under-owned in investor portfolios.

Investors seeking a more selective approach may consider differentiating their Europe allocation through country, sector, and factor index exposures, or through alpha solutions.

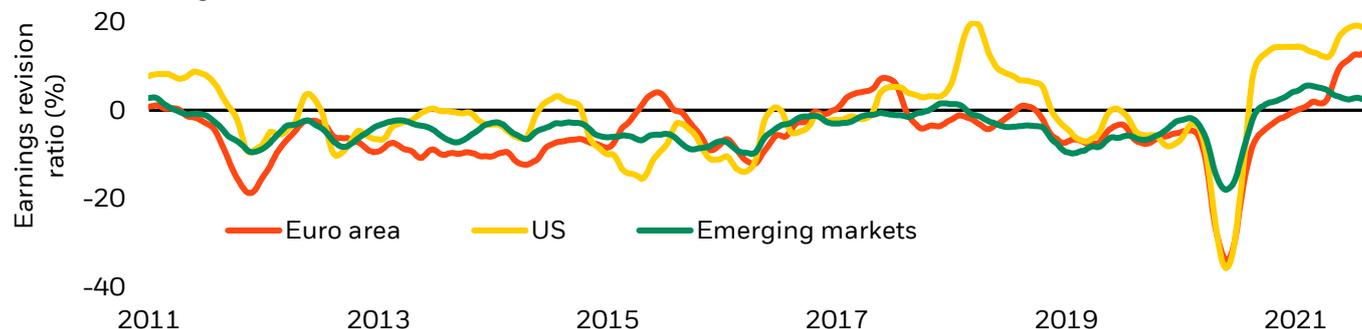
We recently upgraded European equities to overweight on a tactical basis: we see Europe as being well-positioned to catch up with other regions, while tailwinds such as attractive valuations and accommodative policy should provide further support. In this paper, we discuss the case for increasing allocations to European equities.

Strong tailwinds, but still under-owned

After a slow start, Europe's vaccine rollout picked up speed in May, leading to an accelerating activity restart.

Eurozone economic data and confidence indicators have remained robust, and earnings revision ratios are still improving in the region while stalling elsewhere (see chart 1). Our Fundamental European Equity team notes that alongside the supportive macro backdrop, attention has come back to company fundamentals after strong Q1 and Q2 earnings seasons that saw many companies deliver beats and upgrades. Rising virus cases could pose a risk, yet vaccines have so far proven effective against new variants and hospitalisations remain well below previous peaks. Should this continue, any rise in cases would likely be a temporary bump in the path of the overall restart.

Chart 1: Earnings revision ratios: Euro area vs. US and EM, 2011–2021



Sources: BlackRock Investment Institute, with data from Refinitiv Datastream and Bloomberg, 26 August 2021. Notes: The chart shows a three-month moving average of earnings revisions ratios – or the ratio of corporate earnings upgrades to downgrades for each region shown. The three markets are represented by the MSCI EMU Index, MSCI USA Index and MSCI Emerging Markets Index.

Policy support remains accommodative. The European Central Bank (ECB) has suggested that rates are likely to remain at or below current levels until inflation can persistently and durably reach the central bank's new 2% symmetrical target for the medium term. This is in line with our [new nominal](#) theme, which flags a more muted monetary policy response than in the past to higher inflation expectations and actual inflation, keeping nominal long-term yields low and real yields negative – a supportive environment for risk assets. As the ECB's most-recent inflation forecasts highlighted, inflation is expected to fade after a boost from temporary factors, reaching only 1.5% in 2023.¹ Even with pandemic support measures such as the Pandemic Emergency Purchase Program (PEPP) winding down, we expect the ECB to introduce additional easing measures in 2022 given that inflation remains well below its 2% symmetric target. Fiscal spending has also ramped up, with the EU Recovery Fund beginning to distribute its €750B of loans and grants to help drive growth and investment. Ample monetary and fiscal support should help to sustain the restart and provide a tailwind for European equities.

The pickup in macro data and policy support have already provided a significant boost for sentiment, with \$16.7B added to European equity ETPs globally since the start of May, bringing total inflows to \$26.0B YTD – nearly 4x last year's total (\$7.2B).² However, cumulative inflows have only just recovered to highs last seen in 2018, and after many years of muted buying, Europe remains under-owned, in our view.³ Beneath the surface, the shift to sustainability has been a key theme, as investors replace their core portfolio holdings with sustainable equivalents. So far this year, global inflows into sustainability-focused European equity ETPs have reached a record \$7.5B vs. \$6.6B for the whole of 2020.⁴ This trend is even more apparent at a regional level, with c.70% of inflows into EMEA-listed European equity ETPs this year being allocated to sustainable products.⁵

1 European Central Bank as of 9 September 2021. **2,3,4,5** BlackRock and Markit, as of 31 August 2021. All flows are global and in USD unless stated otherwise. **1**

Chart 2: eurozone equity risk premium, 2000-August 2021

Source: Refinitiv Datastream, MSCI, Federal Statistical Office, Germany, as of 31 August 2021. Notes: the equity risk premium is calculated by deducting the German 10-year real bund yield from MSCI Eurozone earnings yield.

Despite the recent rerating, European equity valuations – as measured by the equity risk premium – remain attractive and cheaper than their historic average (see chart 2). Over the longer term, our [Capital Market Assumptions](#) forecast European equities to deliver the highest returns out of any public equity market over five and 10-year horizons.⁶ Combined with the restart and Europe's high sensitivity to global growth, we believe this positions European equities as an attractive investment in the current environment.

SAEU iShares MSCI Europe ESG Screened UCITS ETF	SAUM iShares MSCI EMU ESG Screened UCITS ETF	MESLU BGF European Fund	MEREMAA BGF Euro-Markets Fund
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Taking a selective approach

We see European equities fulfilling multiple roles in portfolios. Investors can adopt a selective approach to access structural growth themes, adjust their factor tilts, or gain exposure to particular countries in Europe.

Tech stands out



The European tech sector has been the single largest contributor to returns for the region this year, due largely to its high exposure to semiconductors, which are benefiting from restricted supply and increased demand amid accelerated technology adoption. Recent semiconductor shortages have highlighted the fragility of supply chains, leading to targeted policy support, with the EU announcing plans to boost investment in the space.⁷

ESIT iShares MSCI Europe Information Technology Sector UCITS ETF
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Facing fact(ors)



European equities were historically thought of as being a 'value' market, given an index composition that was heavily weighted to banks and 'old economy' industries. More recently, market structure has shifted, and quality characteristics such as high profitability and low leverage can help to balance out exposure to the value factor, potentially boosting portfolio resilience. Our Factor Rotation Model favours momentum, quality and value in Europe, due to attractive valuations, a supportive economic backdrop and buying trends. Factor allocations can be built through direct factor strategies, as well as sectors. For example, the STOXX 600 Europe Basic Resources Index provides exposure to quality and value characteristics, which could help it benefit from the economic restart, with an element of resilience via companies with higher profitability, according to our Equity Product Prism framework.

IEFM iShares Edge MSCI Europe Momentum Factor UCITS ETF	IEFQ iShares Edge MSCI Europe Quality Factor UCITS ETF	IEVL iShares Edge MSCI Europe Value Factor UCITS ETF	SXPPEX iShares STOXX Europe 600 Basic Resources UCITS ETF (DE)
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Tour of Europe



We see France and Germany continuing to benefit from the broadening restart. France's equity market is heavily tilted towards cyclicals, such as consumer discretionary stocks, which benefited from the cyclical rotation earlier this year and could continue to be supported as the restart broadens. German macro data has continued to come in strongly for both services and manufacturing, and German equities could be well positioned to benefit from policy support and improving restart dynamics. Peripheral eurozone countries like Italy could also present opportunities. Italian macro data has remained robust, especially in manufacturing. Italian equities have heavy weightings to financials (c.30% of the MSCI Italy Index), which could benefit from easy monetary and fiscal policy, and lifting of dividend restrictions by the end of September.⁸

IFRE iShares MSCI France UCITS ETF	DAXEX iShares Core DAX UCITS ETF	IMIB iShares FTSE MIB UCITS ETF
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⁶ BlackRock Capital Market Assumptions, as of 31 March 2021. Returns refer to Europe equities mean expected return in EUR currency over a five and ten year horizon. ⁷ 'EU says its ready to invest 'significant' funds in chip sector', Reuters. 20 May 2021. ⁸ ECB Banking Supervision, as of 23 July 2021.

BlackRock's European equity platform

For investors wishing to outsource granular decision making to alpha managers, BlackRock's leading Fundamental European Equity team can help.

BlackRock's Fundamental European Equity team manages 12 strategies, covering a range of client needs for fundamental high-conviction European equity, and uses a robust and repeatable investment process designed to deliver durable alpha over the long term. The platform benefits from:



Scale: the large investment team is able to cover a lot of ground finding attractive investment ideas across the breadth of the European equity market. The team also benefits from global connectivity with BlackRock investors across asset classes and thought leaders in areas such as macroeconomics, sustainability, and risk management.



Innovating to stay ahead: the team's use of alternative data brings unique proprietary insights, while a focus on correcting unconscious biases within the investment team, in partnership with behavioural scientists, helps to unlock opportunities for incremental performance gains. Elsewhere, the team's partnership with the BlackRock Capital Markets team can help to provide access to IPOs and placements.



Conviction through differentiated insights: the team manages 12 strategies across a variety of styles including flexible, income, value, and absolute return (long/short equity), meaning analysts are incentivised to find a wide range of alpha opportunities. Having expertise in shorting also benefits our long-only portfolios, where we are comfortable allocating capital to our best ideas – and with the large over/underweights this creates versus the benchmark – thanks to the strength of conviction built from our analysis for short ideas. As bottom-up driven managers, the team focuses on company-specific fundamentals within portfolios to take a selective approach in European equities. This year, this approach has unearthed opportunities in digitisation, green transition, healthcare, and consumer demand for goods and services, in particular.

A range of strategies to suit client needs



MESLU

BGF European Fund

For investors seeking a flexible approach

The BGF European Fund offers a flexible portfolio of winning franchises and opportunistic value ideas across the pan-European market. The fund is focused towards businesses and management teams that have: a clear strategy to deliver shareholder value and a strong track record of value creation; sustainable high returns on capital explained by durable competitive advantages; opportunities to invest in growth and deploy cash at high incremental rates of return; and strong cashflow generation that indicates self-funded value creation.

The Fund is actively managed, and the Investment Adviser (IA) has discretion to select the Fund's investments. In doing so, the IA will refer to the MSCI Europe Index (the "Index") when constructing the Fund's portfolio, and also for risk management purposes to ensure that the active risk (i.e. degree of deviation from the Index) taken by the Fund remains appropriate given the Fund's investment objective and policy. The IA is not bound by the components or weighting of the Index when selecting investments. The IA may also use its discretion to invest in securities not included in the Index in order to take advantage of specific investment opportunities. However, the geographical scope of the investment objective and policy may have the effect of limiting the extent to which the portfolio holdings will deviate from the Index. The Index should be used by investors to compare the performance of the Fund.



MLVLU

BGF European Value Fund

For investors seeking a value exposure to hold across the market cycle

The BGF European Value Fund focuses on finding attractively-valued assets through a fundamental assessment of future cashflows. The fund dynamically allocates between 'Stable Value' companies less sensitive to the cycle, 'Cyclical Value' companies that are cash generative and at the upturn stage of their end-market, and 'Turn-around Value' where company-specific restructuring can lead to realising value. The strategy also recognises that price alone is not an indication of a value opportunity, and that having a low valuation multiple does not necessarily mean a company is undervalued.

The Fund is actively managed, and the IA has discretion to select the Fund's investments. In doing so, the IA will refer to the MSCI Europe Value Index (the "Index") when constructing the Fund's portfolio, and also for risk management purposes to ensure that the active risk (i.e. degree of deviation from the Index) taken by the Fund remains appropriate given the Fund's investment objective and policy. The IA is not bound by the components or weighting of the Index when selecting investments. The IA may also use its discretion to invest in securities not included in the Index in order to take advantage of specific investment opportunities. However, the geographical scope of the investment objective and policy may have the effect of limiting the extent to which the portfolio holdings will deviate from the Index. The Index should be used by investors to compare the performance of the Fund.

References to specific investments are for illustrative purposes only and are not intended and should not be interpreted as recommendations to purchase or sell such investments.


**BGF European
Equity Income
Fund**
For investors seeking resilience and income

The BGF European Equity Income Fund is designed to seek a premium dividend yield and growth in distributions over time, with portfolio resilience and long-term outperformance. The portfolio is split into three buckets: 'High Yield' companies that help to deliver a premium yield; 'Steady Growth' companies that provide portfolio resilience; and 'Unique Franchises' with high growth prospects to help drive long-term outperformance and dividend growth.

The Fund is actively managed and the Investment Adviser (IA) has discretion to select the Fund's investments. In doing so, the IA may take into consideration the MSCI Europe Index (the "Index") when constructing the Fund's portfolio, and also for risk management purposes to ensure that the active risk (i.e. degree of deviation from the Index) taken by the Fund remains appropriate given the Fund's investment objective and policy. The IA is not bound by the components or weighting of the Index when selecting investments. The IA may also use its discretion to invest in securities not included in the Index in order to take advantage of specific investment opportunities. However, the geographical scope of the investment objective and policy may have the effect of limiting the extent to which the portfolio holdings will deviate from the Index. The Index should be used by investors to compare the performance of the Fund.


**BGF European
Sustainable
Equity Fund**
For Investors seeking sustainable solutions

The BGF European Sustainable Equity Fund aims to deliver long-term outperformance and measurable sustainable outcomes including a higher ESG score and lower carbon emission intensity relative to the benchmark. The team looks for sustainable business models that focus on all stakeholders, and actively engages with companies to encourage better disclosures and accelerate the adoption of best practices. Mapping revenues to UN Sustainable Development Goals (SDGs) helps the team to identify companies that have sustainability at their core and can potentially outgrow the market in the long term.

The Fund is actively managed. The Investment Adviser (IA) has discretion to select the Fund's investments and is not constrained by any benchmark in this process. The MSCI Europe Index (Index) should be used by investors to compare the performance of the Fund. The ESG Policy reduces the investment universe of the Fund compared to the Index by at least 20%.

References to specific investments are for illustrative purposes only and are not intended and should not be interpreted as recommendations to purchase or sell such investments.

Risk Warnings

Capital at risk. The value of investments and the income from them can fall as well as rise and are not guaranteed. Investors may not get back the amount originally invested.

Past performance is not a reliable indicator of current or future results and should not be the sole factor of consideration when selecting a product or strategy.

Changes in the rates of exchange between currencies may cause the value of investments to diminish or increase. Fluctuation may be particularly marked in the case of a higher volatility fund and the value of an investment may fall suddenly and substantially. Levels and basis of taxation may change from time to time.

BlackRock has not considered the suitability of this investment against your individual needs and risk tolerance. The data displayed provides summary information. Investment should be made on the basis of the relevant Prospectus which is available from the manager.

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Product Risks

iShares Core DAX® UCITS ETF (DE)

Concentration Risk, Counterparty Risk, Equity Risk

iShares MSCI EMU ESG Screened UCITS ETF

Concentration Risk, Counterparty Risk, Equity Risk, Environmental, Social and Governance (ESG) Risk

iShares MSCI Europe ESG Screened UCITS ETF

Concentration Risk, Counterparty Risk, Credit Risk, Equity Risk, Environmental, Social and Governance (ESG) Risk

iShares Edge MSCI Europe Momentum Factor UCITS ETF EUR (Acc)

Counterparty Risk, Equity Risk, Factor Focus Risk, Index Methodology Risk

iShares Edge MSCI Europe Quality Factor UCITS ETF EUR (Acc)

Counterparty Risk, Equity Risk, Factor Focus Risk, Index Methodology Risk

iShares Edge MSCI Europe Value Factor UCITS ETF EUR (Acc)

Counterparty Risk, Equity Risk, Factor Focus Risk, Index Methodology Risk

iShares FTSE MIB UCITS ETF EUR (Acc)

Concentration Risk, Counterparty Risk, Equity Risk

iShares MSCI Europe Information Technology Sector UCITS ETF EUR (Acc)

Concentration Risk, Counterparty Risk, Equity Risk, Investment in Technology Securities Risk

iShares MSCI France UCITS ETF EUR (Acc)

Concentration Risk, Counterparty Risk, Equity Risk

iShares STOXX Europe 600 Basic Resources UCITS ETF (DE)

Concentration Risk, Counterparty Risk, Equity Risk, Investments in Natural Resources Risk

BGF Euro-Markets Fund

Counterparty Risk, Equity Risk

BGF European Equity Income Fund

Counterparty Risk, Currency Risk, Equity Risk, Erosion to Capital

BGF European Fund

Counterparty Risk, Equity Risk

BGF European Sustainable Equity Fund - Aggregate

Counterparty Risk, Equity Risk

BGF European Value Fund

Concentration Risk, Counterparty Risk, Equity Risk

Description of Product Risks

Concentration Risk – iShares

Investment risk is concentrated in specific sectors, countries, currencies or companies. This means the Fund is more sensitive to any localised economic, market, political or regulatory events.

Concentration Risk – BGF

Investment risk is concentrated in specific sectors, countries, currencies or companies or because the Fund has only a small number of investments. This means the Fund is more sensitive to any localised economic, market, political or regulatory events. Concentrated investment exposure by the Fund could magnify the other risks to which the Fund is exposed.

Counterparty Risk – iShares

The insolvency of any institutions providing services such as safekeeping of assets or acting as counterparty to derivatives or other instruments, may expose the Share Class to financial loss.

Counterparty Risk – BGF

The insolvency of any institutions providing services such as safekeeping of assets or acting as counterparty to derivatives or other instruments, may expose the Fund to financial loss.

Credit Risk

The issuer of a financial asset held within the Fund may not pay income or repay capital to the Fund when due.

Currency Risk

The Fund invests in other currencies. Changes in exchange rates will therefore affect the value of the investment.

Environmental, Social and Governance (ESG) Risk

The benchmark index only excludes companies engaging in certain activities inconsistent with ESG criteria if such activities exceed the thresholds determined by the index provider. Investors should therefore make a personal ethical assessment of the benchmark index's ESG screening prior to investing in the Fund. Such ESG screening may adversely affect the value of the Fund's investments compared to a fund without such screening.

Equity Risk

The value of equities and equity-related securities can be affected by daily stock market movements. Other influential factors include political, economic news, company earnings and significant corporate events.

Erosion to Capital

This Share Class may pay dividends or take charges from capital. While this may allow more income to be distributed, it may reduce the value of your holdings and impact the potential for long term capital growth.

Factor Focus Risk

Indices with a factor focus are less diversified than their parent index because they have predominant exposure to a single factor rather than the multiple factor exposure of most indices. Therefore they will be more exposed to factor related market movements. Investors should consider this fund as part of a broader investment strategy.

Index Methodology Risk

Although the Benchmark Index was created to select securities within the Parent Index for their recent price increases on the assumption that such increases will continue, there is no guarantee this objective will be achieved.

Investment in Technology Securities Risk

Investments in the technology securities are subject to absence or loss of intellectual property protections, rapid changes in technology, government regulation and competition.

Investments in Natural Resources Risk

Investments in natural resources securities are subject to environmental concerns, taxes, government regulation, price and supply fluctuations.

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