

## VIVE LA DIFFÉRENCE

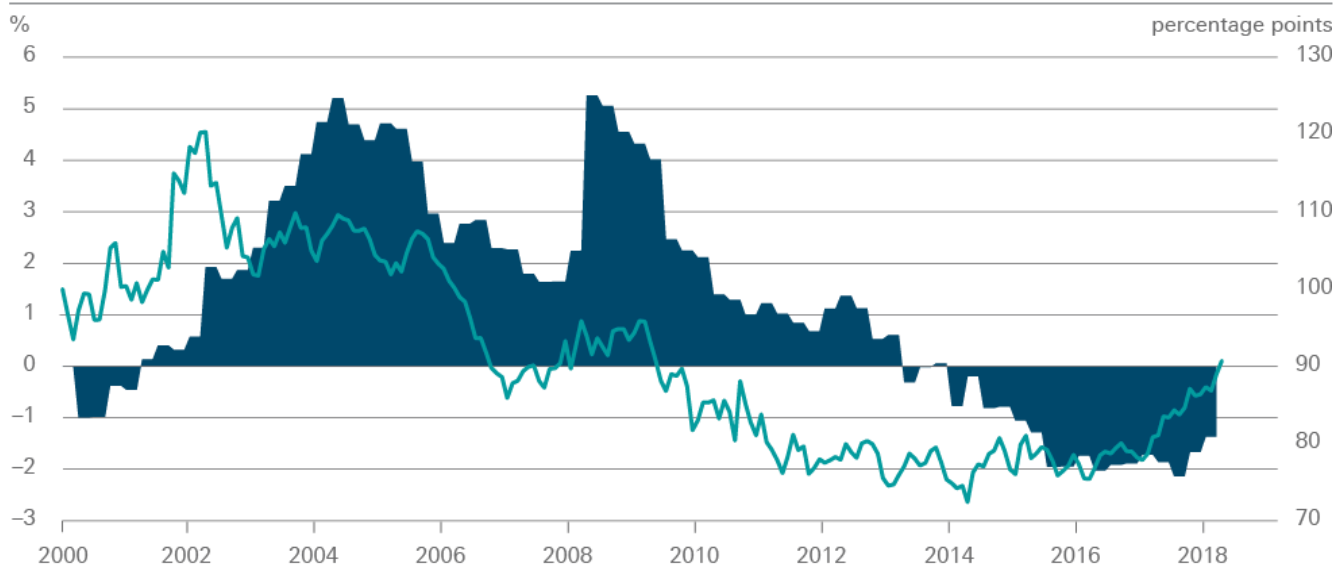
What might a Eurozone slowdown mean for equity markets? A closer look at France and Germany over the past 20 years reveals some interesting patterns.

Casual observers like to draw a direct link between a country's economic growth rates and the likely returns its equity market might offer. Reality often turns out a lot more complicated. For one thing, investors care about company earnings more than whole economies. Even domestically, earnings can grow – or shrink – more than an economy as a whole, depending on how company profitability develops. That is especially true at cyclical turning points. At the late stages of the economic cycle, it is not uncommon, for example, for low unemployment rates to create wage pressures, which companies might struggle to pass on. The economy might continue to grow – even overheat – for a little longer, but earnings growth might stall. Another issue concerns the growth of multi-national companies, which tend to make the bulk of their revenues and earnings outside their home country. And of course, national equity markets can differ a lot in terms of their sector composition.

For illustration of all these factors, our "Chart of the Week" shows the gross-domestic-product (GDP) growth rates and equity markets of France and Germany over the past 20 years. After 2002, France grew more quickly than Germany, but experienced a comparative slowdown from 2005 on-

wards. France was better able to cope with the Great Recession in 2009. Germany finally managed to catch up and surpass France in 2014. By contrast, French equities (as measured by both countries' MSCI indices) outperformed until late 2006, before taking a long and lasting nose-dive. That trend only began to sharply reverse over the past two years, just as the French economy began to outpace the German one.

The patterns in both countries' equity markets reflects the sources of both economic and earnings growth. Germany's economy and stock market are much more dependent on cyclical export goods, with heavy weightings for industrials, carmakers and materials such as chemicals. Financials also remain quite heavily weighted in Frankfurt when compared to the Paris stock exchange. The French market is arguably more balanced and defensive, with larger weightings for higher-margin consumer goods, thanks to strong French brand names. These tend to be much in demand in times of looming economic slowdowns. It goes to show that investors need to be careful when extrapolating from economic growth rates to any country's stock-market performance.



■ GDP France vs. Germany, cumulative growth differential since 2000

■ MSCI France Index vs. MSCI Germany Index (right axis)

Sources: Bloomberg Finance L.P., DWS Investment GmbH as of 4/11/19

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Source: DWS Investment GmbH

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CRC 066759 (04/2019)

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## GLOSSARY

### Equity market

A **market** in which **equities** (stocks) are traded. The term can be used to refer to an actual market (e.g. the New York Stock Exchange) or to general trends in equity trading. Equities are securities which certify rights of ownership of (parts of ) a company.

### Great Recession

The **Great Recession** refers to the prolonged economic downturn in much of the world after the financial crisis of 2007-08.

### Gross domestic product (GDP)

The **gross domestic product (GDP)** is the monetary value of all the finished goods and services produced within a country's borders in a specific time period.

### MSCI

**MSCI** is a company providing indices and other analytical tools for investors.

### MSCI France Index

The **MSCI France Index** tracks the performance of French stocks.

### MSCI Germany Index

The **MSCI Germany Index** tracks the performance of German stocks.

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