December 7, 2018

Parisian riots: an illustration of Europe's wider political risk

As the US business cycle ages (albeit gracefully), normally investors would see this as an opportune moment to start looking further afield, perhaps diversifying into European equities, given that the continent is at an earlier stage in the cycle. This is something that has been discussed at length by our experts, yet so far, we have been unable to shake our reluctance for this asset class, given the seemingly unending political risk that European equity investors must contend with.

This week it was France that grabbed headlines, with an estimated 136,000 citizens protesting on Saturday. The protests predominantly played out in the ritzier districts of Paris, where the Arc de Triomphe was vandalised and cars were set a-light by the so-called 'gilet jaunes'– a group wearing hi-vis yellow vests, a mandatory safety requirement in all French vehicles. The movement was initially against rising fuel costs and the prospect of a new fuel eco-tax to be rolled out in January, but morphed into a wider movement expressing frustration about costs of living and inequality. The spreading protests are not aligned with any political party, but share a solidarity against a raft of Macron's policies.

The scenes became so alarming that the French Prime Minister announced that the introduction of the taxes - designed to improve France's environmental credentials – would be postponed for six months. But the additional taxes seem to just be one more layer in a mille-feuille of discontent that has built up over the years, layer-by-layer. France's much needed structural reforms are still to materialise, whilst its budget deficit is almost touching the 3% limit imposed on euro zone members, and its public debt pile stands at almost 100% of GDP. It is increasingly felt amongst the people that the system is failing and somewhere, online expressions of anti-elite resentment have evolved into a physical protest movement. It remains to be seen whether the movement can maintain momentum in the long term, but the fact that is a leaderless movement also means that negotiation is mostly wishful thinking.

It seems that there is a growing resentment with traditional political systems at large, and a collapse of the left-right paradigm. According to reporting by the Guardian newspaper, protestors interviewed did not express allegiance to any politician: most said politics disgusted them. A poll for Harris Interactive conducted after the weekend scenes, found that 72% of French people continued to support the gilets jaunes, even if 85% said they disagreed with the violence in Paris.

And what is happening in France is just a microcosm of what is happening across Europe where populist ideals are gaining ground. Whilst France may have a mille-feuille of issues, Slovakia's finance minister - Peter Kazimir - has a similar analogy for broader Europe: a lasagne of evil, with each layer representing a different part of society that has failed to curb growing unrest — the media, politicians, corporations, even religion. As he said, now we are being forced to eat the lasagne – for example with Britain's departure from the EU and Italy's new government's reluctance to play ball with the EU over its budget. At a European level, growing polarisation in national politics makes it even harder for the EU's 28 governments to make decisions.

And we do not see political risk fading throughout 2019. On 29th March, the UK is scheduled to leave the EU. In Germany, Merkel will not go up for re-election, marking a weakening of Germany's centre-left party – the SDP. And in May there will be the European elections which will be a real litmus test of the true strength of populist sentient across the bloc. Without stellar fundamentals eclipsing the political scene, the investment case for Europe is simply not there at the moment.

Disclaimer

All financial data and/or economic information released by this Publication (the "Publication"); (the "Data" or the "Financial data and/or economic information"), are provided for information purposes only, without warranty of any kind, including without limitation the warranties of merchantability, fitness for a particular purpose or warranties and non-infringement of any patent, intellectual property or proprietary rights of any party, and are not intended for trading purposes. Banque Internationale à Luxembourg SA (the "Bank") does not guarantee expressly or impliedly, the sequence, accuracy, adequacy, legality, completeness, reliability, usefulness or timeless of any Data. All Financial data and/or economic information provided may be delayed or may contain errors or be incomplete. This disclaimer applies to both isolated and aggregate uses of the Data. All Data is provided on an "as is" basis. None of the Financial data and/or economic information contained on this Publication constitutes a solicitation, offer, opinion, or recommendation, a guarantee of results, nor a solicitation by the Bank of an offer to buy or sell any security, products and services mentioned into it or to make investments. Moreover, none of the Financial data and/or economic information contained on this Publication provides legal, tax accounting, financial or investment advice or services regarding the profitability or suitability of any security or investment. This Publication has not been prepared with the aim to take an investor's particular investment objectives, financial position or needs into account. It is up to the investor himself to consider whether the Data contained herein this Publication is appropriate to his needs, financial position and objectives or to seek professional independent advice before making an investment decision based upon the Data. No investment decision whatsoever may result from solely reading this document. In order to read and understand the Financial data and/or economic information included in this document, you will need to have knowledge and experience of financial markets. If this is not the case, please contact your relationship manager. This Publication is prepared by the Bank and is based on data available to the public and upon information from sources believed to be reliable and accurate, taken from stock exchanges and third parties. The Bank, including its parent,- subsidiary or affiliate entities, agents, directors, officers, employees, representatives or suppliers, shall not, directly or indirectly, be liable, in any way, for any: inaccuracies or errors in or omissions from the Financial data and/or economic information, including but not limited to financial data regardless of the cause of such or for any investment decision made, action taken, or action not taken of whatever nature in reliance upon any Data provided herein, nor for any loss or damage, direct or indirect, special or consequential, arising from any use of this Publication or of its content. This Publication is only valid at the moment of its editing, unless otherwise specified. All Financial data and/or economic information contained herein can also quickly become out-of- date. All Data is subject to change without notice and may not be incorporated in any new version of this Publication. The Bank has no obligation to update this Publication upon the availability of new data, the occurrence of new events and/or other evolutions. Before making an investment decision, the investor must read carefully the terms and conditions of the documentation relating to the specific products or services. Past performance is no guarantee of future performance. Products or services described in this Publication may not be available in all countries and may be subject to restrictions in some persons or in some countries. No part of this Publication may be reproduced, distributed, modified, linked to or used for any public or commercial purpose without the prior written consent of the Bank. In any case, all Financial data and/or economic information provided on this Publication are not intended for use by, or distribution to, any person or entity in any jurisdiction or country where such use or distribution would be contrary to law and/or regulation. If you have obtained this Publication from a source other than the Bank website, be aware that electronic documentation can be altered subsequent to original distribution.

As economic conditions are subject to change, the information and opinions presented in this outlook are current only as of the date indicated in the matrix or the publication date. This publication is based on data available to the public and upon information that is considered as reliable. Even if particular attention has been paid to its content, no guarantee, warranty or representation is given to the accuracy or completeness thereof. Banque Internationale à Luxembourg cannot be held liable or responsible with respect to the information expressed herein. This document has been prepared only for information purposes and does not constitute an offer or invitation to make investments. It is up to investors themselves to consider whether the information contained herein is appropriate to their needs and objectives or to seek advice before making an investment decision based upon this information. Banque Internationale à Luxembourg accepts no liability whatsoever for any investment decisions of whatever nature by the user of this publication, which are in any way based on this publication, nor for any loss or damage arising from any use of this publication or its content. This publication, prepared by Banque Internationale à Luxembourg (BIL), may not be copied or duplicated in any form whatsoever or redistributed without the prior written consent of BIL 69, route d'Esch ı L-2953 Luxembourg ı RCS Luxembourg B-6307 ı Tel. +352 4590 6699 ı www.bil.com.