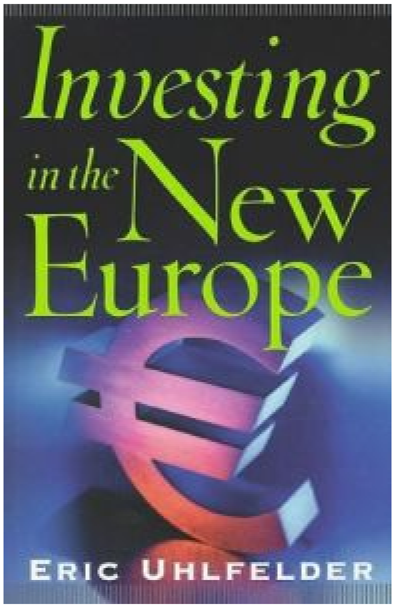

Book Investing in the New Europe

Eric Uhlfelder
Bloomberg Press, 2001

Recommendation

Eric Uhlfelder’s book could be titled "Europe 101: An Introduction for Americans." European readers will not gain much by reading this work, which is filled with the very basic basics of Europe’s politics, economies and companies. But for Americans looking to diversify their newly constructed stock portfolios, it is a valuable resource, profiling the EU and the economic strengths and weaknesses of EU and non-EU countries. The book also profiles key companies, such as Nokia, SAP, Adecco and others, and discusses which individual stocks and mutual funds you should acquire. *BooksInShort* recommends this interesting primer to Yankee readers, who might be surprised to learn how fast Ireland is growing, how much Austria’s fling with the far right cost the country and how a French utility firm is positioned to take over the world.

Take-Aways

- The European Union is comparable in size and GNP to the United States.
- The EU is still a great investment opportunity, despite the lagging euro.
- Many European countries aren’t part of the EU, including the United Kingdom, Switzerland, Norway and Denmark.
- The uniform rules of the EU have forced countries to become more competitive.
- A close look at Europe reveals the existence of five distinct investment regions.
- These regions are The Core, The Tigers, The Independents, The Latent Reformers and The Emerging Markets.
- Ireland and Portugal are among the fastest growing countries in the EU.
- The German multinational SAP is the world’s third-largest software company.
- Each country has fiscal strengths and weaknesses.
- You can look at European investment by sector regions, such as banking.

Summary

The Promise of Europe

Investors should buy European stocks for two reasons. First, continental companies are superb investments and, second, improving corporate fundamentals are driving up European earnings. Europe encompasses 19 major markets, each with its own resources. Despite the continuous decline of the euro, the big news is the government and corporate restructuring that's been going on for nearly a decade.

> "Europe has started to shed its government influenced, border-conscious, structurally rigid style of doing business and is increasingly committed to competing in the global marketplace."

The "new Europe" is attracting the United States' largest banks and investment houses and the big money is betting that Europe is poised for success. European companies are becoming increasingly Americanized. Systemic change makes European investment attractive not only as a way to diversify your portfolio, but as a way to lock in strong returns. The common currency has fueled progressive change including improved macroeconomic conditions, market deregulation and the increased efficiencies of more open competition. "The bottom line is that you can find Microsofts, Baby Bells and ExxonMobils in bourses across Europe."

Some Pretty Heady Numbers

Western European equity markets, which have been on a tear, rose collectively in 1999 by nearly 28% in local terms, led by Finland (up 193.7%), Sweden (up 87.4%) and France (up 50%). Stocks within the Eurozone performed even better, rising 37.5%. This favorable comparison with the U.S. market goes further. Eurozone returns between 1996 and 1998 matched the performance of U.S. stocks. Half a dozen bourses beat the Dow. These numbers may surprise some, but for the first time, many European countries are focused on profitability.

> "Europe has made a stunning turnaround from the not-so-distant past, when it was common to see governments push businesses to effect social policy (jobs created, taxes paid and pensions funded) and for large corporations to be more focused on serving this agenda rather than return on investments."

European economic and monetary union is one of the most significant global changes since the end of World War II. The European Monetary Union (EMU) created dramatic improvements by forcing countries to:

- Reduce national debt to no more than 60% of gross domestic product (GDP).
- Allow government deficits of no more than three percent of GDP.
- Keep domestic inflation and interest rates within 1.5 percentage points of the average of the three best-performing economies within the Eurozone.
- Create stable foreign exchange rates.

> "Supported by a wide range of European Union directives seeking to open up markets and competition, economic and monetary union has helped unleash a more effective form of capitalism rippling across the entire continent."

Common currency has forced governments to get their houses in order and - in combination with European Union (EU) directives seeking to open up both markets and competition - has created a more effective form of capitalism. The EU has generated a number of positive developments: the privatization and deregulation of major industries, key mergers and acquisitions, a focus on shareholder value, a new cost harmonization between nations, pension reform and an increase in productivity.

European Investment Geography

The Eurozone, which is comprised of 11 countries, is the most recognizable investment region in Europe. These initial participants in EMU are Austria, Belgium, Finland, France, Germany, Ireland, Italy, Luxembourg, the Netherlands, Portugal and Spain. Greece was added in 2001. The Eurozone is a broken landmass ranging from Finland in the northeast, Ireland in the northwest, Portugal in the southwest, and Greece in the southeast. The Eurozone population is roughly the same as the United States and has a GDP that's nearly 80% of the U.S. GDP.

> "Europe is realizing its traditional economic formulas can't be sustained, because the global marketplace in which it's competing plays by a far less restrictive set of rules."

A more refined look at Europe beyond Eurozone borders reveals the existence of five distinct investment regions. Inspect these regions to gain a better understanding of European finance. These regions are called The Core, The Tigers, The Independents, Latent Reformers and Emerging Markets.

The Core

Germany, France and Italy comprise nearly two-thirds of the Eurozone's wealth. Switzerland and the United Kingdom, which are not currently part of the EMU, had the least to gain during the phase-in of common currency. Except for Italy, currencies in these core countries have been Europe's most stable and their public finances are the region's soundest. Their strong private sectors are home to some of the world's best-run companies. As the monetary union adds to economic integration, companies based in the large core countries should enjoy increased market share across Europe, especially through mergers and acquisitions. The Euro should also allow those same countries to reach beyond the Eurozone to less developed countries, such as Portugal, Greece and Hungary, with less risk.

The Tigers

Europe's tiger economies, Ireland, Spain, Portugal and the Netherlands, lie on the continent's periphery. Common currency has allowed these countries to grow at twice the rate of Europe's core economies. A sense of legitimacy and the prospect of monetary convergence with the core countries have encouraged these smaller, less developed economies to clean up their fiscal acts. Furthermore, their governments' willingness to tackle structural reform - including more flexible labor laws, wage restraint and the privatization of prized national assets - has "triggered rapid expansion of foreign direct investment within their borders."

The Independents

The Nordic region is one of the most prosperous economic zones in the world. In a mark of the region's independence, only Finland decided to join the EMU. Remaining suspicious of Brussels and EU policy, the other Nordic countries decided to maintain their own fiscal and monetary sovereignty. Nordic currencies, such as the Swedish krona and the Norwegian krone, held up fairly well in 1999, depreciating only slightly against the dollar. Strong market ties between the Scandinavian and Eurozone economies ultimately will dictate equity performance. The region offers investors a non-euro alternative to participating in European growth. However, pending public referendums on joining EMU could change the region's policy toward Eurozone membership over the next several years.

Latent Reformers

Belgium and Austria have been under-performing the rest of the Eurozone because of their slower pace of structural reform. Their core businesses have not kept up with their neighbors' rapid growth, and they will find it difficult initially to benefit from common currency. Substantial unemployment, high tax rates and government spending have stifled competitiveness in Belgium and many of its blue chips have become acquisition targets. The Austrian market is far more commodities-oriented, however, it lacks the telecoms and technologies that have driven growth in other European markets. The nepotistic Austrian political system has hurt the development of a pro-business culture. Jorg Haider, an ultra right-winger who has been compared to Hitler, didn't help Austria either. His political ascension translated into EU sanctions against Austria. Greater liberalization should come to both economies as restrictive domestic policies give way to EU reform.

Emerging Markets

Three of Europe's four core emerging markets - Poland, Hungary and the Czech Republic - lie just east of Germany and Austria, and are defined by their low levels of income per capita. However, these countries are enjoying an influx of investment from foreign corporations in search of cheap labor and low production costs. They also share the additional advantage of proximity to Western Europe's central markets.

> "Systemic change is making European investments not only an effective way to diversify a portfolio but a smart bet for locking in strong returns."

Greece is also a part of Europe's emerging markets. All four of these economies offer potential investors rapid growth. The risk is that these countries are still learning the realities of capitalism. Their economic infrastructures are still evolving and corruption remains a significant concern. Exchange-rate stability is also a major concern. This instability is due to higher inflation and interest rates, proximity to Russia and the need for additional structural reform.

The Sectoral Approach

Sector-based investing is a reflection of European integration and globalization, key factors that are driving stocks. Domestic performance is no longer a measure of a particular stock's appeal. So while economic policy and product specialization still have national faces, policy shaping Europe's investment environment is increasingly defined by its industry sectors. Findings in each sector indicate:

> "Sector-based investing is a reflection of European integration and globalization, key factors that are driving stocks. In fact, one would be hard-pressed to find a stock whose appeal is primarily based on domestic performance."

Banking - Industry deregulation and more liberal markets have made firms more efficient, bank stocks have soared by nearly 31% and banks are deriving an increasing flow of their profits from asset management. Insurance - European insurers are among the largest in the world and the life industry is widely recognized as the sector's fastest growing profitable segment. Retail - There is a major trend toward consolidation, there have been extensive acquisitions and Wal-Mart's entry is triggering significant restructuring and consolidation. Telecommunications services - Deregulation and the breakup of state-run monopolies have transformed telecommunication services into one of Europe's top-performing sectors where growth is being driven by the demand for data and Internet access. Utilities - Privatization and market liberalization are turning utility stocks into good investments, utilities are beginning to benefit from moves into the new economy. Tremendous demand for improved water distribution will drive industry growth worldwide.

Model Stocks, Model Companies

The Continent's most prominent growth stories represent a wide array of investment opportunities in the New Europe. Focused operations are a common feature among all these stocks - No highly diversified conglomerates here. Every company has achieved significant market share in its respective industry.

> "Although economic policy and product specialization still have national faces, Europe's investment environment is increasingly being defined in terms of sectors."

Nokia has the technology and marketing acumen to exploit the industry's increasingly open standards and geometric expansion. Nokia is one of Europe's top growth stocks and has become one of the globe's largest manufacturers of mobile phones, but its high proportion of institutional ownership and sky-high valuation exposes shares to substantial volatility.

> "The easiest way to profit from Europe is through funds invested across the Continent. Because they are able to shift assets freely from one end of Europe to the other, gaining exposure to the full offering of various industries, these funds have notched the best long-term returns."

The German multinational SAP is the world's largest manufacturer of enterprise resource planning software (ERP), with a 39% market share. Spawned and spurned by IBM, SAP is now the third-largest software company in the world and the company's CEO is known as the charismatic European equivalent of Larry Ellison or Bill Gates.

> "The one theme that characterizes investing in the new Europe is change. It is occurring at a cosmic pace, and at any given time, events can turn askew even the most basic investment assumptions."

Suez Lyonnaise des Eaux is a France-based multinational utility that competes for services not only in Europe, but also throughout the world. The company is poised to exploit the world's expanding utility needs. Its stock is defined as "defensive-growth" and the company is expanding into telecom by moving into mobile and cable services. It offers a likelihood of sustained, long-term growth.

About the Author

Eric Uhlfelder has been covering international markets as a writer and analyst for more than 10 years. His work is featured in *Business Week,* Euromoney's *Global Investor, Individual Investor, Mutual Funds* and *Fidelity Focus* magazines.