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Upward trends in Europe – growing investor interest?

European equities had been avoided for a long time by many investors, who rushed to buy US stocks instead. But now that dynamic is starting to shift: Attractive stock valuations, more positive news flow on the economy, and greater infrastructure and defense spending are generating fresh momentum for Europe and directing more investment capital toward the Continent. Read on to discover what makes Europe, European small- and mid-cap stocks in particular, so exciting today.

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Investor attention was clearly focused on US stocks during the past several years and this led to a significant valuation divergence between US and European equities. European small and mid caps in particular fell out of favor. Meanwhile US companies produced some stunning innovations, especially in the realm of AI, creating market giants with a dominant global position. A consensus quickly emerged that investors had to go long on Wall Street and stay away from European stocks, especially after the full-scale invasion of Ukraine. Stock valuations moved in opposite directions as a result, with US stocks occasionally trading at exorbitant premiums of up to 60% compared to their European counterparts. Stocks of smaller European companies languished the most.

Several years of underperformance have pushed valuations to historically low levels: European small caps are currently trading on a 12M forward P/E of 12.6x. The average multiple for European large caps is 14.5x and an even higher 19.4x for US small caps.

European equities have performed remarkably well during the opening months of 2025, however, advancing on average by about 10% to the middle of March – and not only the blue chips, but also the small- and mid-cap stocks. Could this mark the start of a longer-lasting change in trend? Has the investment case for Europe shifted to such an extent that investors will no longer focus nearly exclusively on US stocks?

Europe's economy is stabilizing – the US hits a soft patch

An important factor behind this trend reversal is the differing momentum of key macroeconomic variables in the US and Europe. The US economy is faced with uncertainty while Europe's economy is bottoming out after three years of meager growth. The Trump Administration's abrupt about-face on government spending and erratic tariff policy announcements are beginning to impact consumer confidence and capital expenditure in the US. The cautious tone that the US Federal Reserve has adopted, taking a "wait and see" approach in view of the new environment, does not help the situation in the US either. This contrasts with the situation in the eurozone, where the ECB is expected to lower its benchmark lending rate by 75 basis points by the end of 2025, which will boost demand for credit and economic growth. Leading indicators in Europe are finally heading in the right direction and this has led to upward revisions of both GDP and corporate earnings growth estimates despite the rumblings on the tariff front.

Europe's economy displays heterogeneity

Regional economic growth in Europe is heterogeneous. The consensus forecast for Spain's GDP growth in 2025 has risen from 2.2% to 2.5%, for example, fueled by the recent drop in unemployment to a 15-year low and by positive momentum in sectors ranging from banking and real estate to tourism, and the outlook for other countries such as Italy and Greece has also brightened. Meanwhile the forecast of France's GDP growth in 2025 was recently lowered to just 0.9% due to the country's domestic challenges. This striking heterogeneity within Europe calls for an active stock-picking approach in order to take full advantage of market opportunities as they arise. Investments in local champions account for about one-third of our portfolio positions.

US tariffs – less risk than expected for European equities

The overall impact of (potential) US tariffs is not as big as the market fears. While European companies do generate 26% of their total sales in the US, about half of those sales reflect services, which will not be affected by the proposed trade tariffs. In addition, about 11% of the reported sales of European manufacturers are protected from US import tariffs thanks to "local for local" strategies under which considerable production capacity has been transferred to the US since 2016, and even more so in the wake of the COVID pandemic. Ultimately, only about 7% of the total sales of European companies would actually be subject to potential trade tariffs. Certain sectors such as the auto or luxury industry are clearly much more exposed to US import tariffs than, say, the energy or defense industry. Stock selection should focus on companies that have strong market positions and pricing power and that could continue to operate successfully despite tariff-driven change.

Small and mid caps – value style also drives performance

The Bellevue Entrepreneur Europe Small (Lux) Fund (LU0631859229) takes a benchmark-agnostic, bottom-up stock-picking approach and invests in both growth and value. GARP, a strategy focusing on fast growth at a reasonable price, is a dominant element, accounting for about half of the invested fund assets. Value stocks are attractive for their stable dividend yields and low valuations, while high-growth companies offer strong sales and earnings growth. This mix fuels fund outperformance and creates opportunities across the interest rate cycle. There are particularly attractive opportunities in the small- and mid-cap space, and value stocks perform well in a market environment like today's.

An example here is Metso, a Finnish company in the fund's portfolio that provides equipment, technology and services to the mining, recycling, and minerals/metals processing industries. Metso is highly efficient and generates stable profits with an EBIT margin of 16%. Services account for 17% of its total sales.

Another example is Invisio, a Danish communication systems specialist that develops advanced communication headsets for military applications. By focusing on R&D and sales – while outsourcing most of the production to European contract manufacturers – Invisio operates with attractive margins and has successfully expanded its market share.

Both companies are good examples of how the fund managers target companies strong on innovation and growth in building a diversified portfolio.

Conclusion: Time for European small and mid caps

Attractive valuations, positive economic signals, active fiscal policies and innovative business models make a promising case for European small and mid caps. Investors with an active stock-picking approach can take advantage of today's enticing opportunities for diversification and long-term outperformance in this space.

Learn more on our website.

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