Intermonte

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Italian Equity Research – Strategy Report

Italian Equity Strategy Monthly

Lower Visibility Requires Higher Intra-Sector Selection

by Intermonte Research Team

Italian Equity Market

- **Market outlook.** The performance in July was quite a rollercoaster. Despite markets posting modest gains overall, the underlying performance of stocks and sectors was quite divergent. A lot of cyclical stocks and tech suffered set-backs for different reasons: cuts to estimates in the first case and profit taking for the latter. Best performers were financials and utilities, benefitting from solid 2Q prints and the benign environment.
- **Investment strategy.** August is usually a month of limited newsflow and low volumes. We expected a slowdown in earnings momentum after a buoyant 2023, also due to a challenging comparison base, and this is definitely happening in some sectors. Markets were polarized on some sectors like AI-driven stocks, but we think that some relatively defensive and higher visibility stocks like utilities and financials can still provide positive opportunities. We also believe that intra-sector stock picking will be relevant in order to perform in markets with lower visibility.
- **Corporate.** 2Q reporting is in full swing right now but various large caps have already reported. As anticipated, it is shaping out as a pretty interesting reporting season, as shown by the volatile stock reactions to indications. We have revised estimates significantly downward for some industrial stocks penalized by de-stocking and soft pricing, while the picture is totally different for banks, with further estimate upgrades on continuation of a favourable scenario for NII and cost of risk. Other financial sector stocks (insurance and asset managers) are also reporting positive indications, along with utilities. The mixed picture for consumers, luxury and healthcare very much depends on their market positioning and pricing power. Summing up these divergent trends has led to a slightly negative revision, with financials' EPS estimates up and industrials / energy down.
- **Portfolio selection**: Our portfolio reported a slightly positive relative performance last month, taking outperformance YTD to ~200bps. We are making some changes to our long stocks selection by adding ones that are well positioned in our view in their respective sectors like Mediobanca, Brunello Cucinelli and Recordati, and taking profit from Intesa Sanpaolo, which reported positive indications on 2Q trends. In general, we are keeping an overweight bias on utilities and selectively adding stocks that we think offer good protection in terms of earnings momentum and relative valuations. On the underweight side, we are adding Prysmian, a very good company but now becoming less compelling on valuation grounds, and removing Stellantis, which posted a highly negative performance and has suffered a massive level of estimate downgrades.

  As a recap, our changes to the stock selection for August are the following:

  Large caps to overweight: Adding Mediobanca, Brunello Cucinelli and Recordati, removing Intesa Sanpaolo and confirming A2A, Enel, Eni, Saipem among utilities and energy, Banca Mediolanum and Unipol among financials, and Iveco among industrials.

  Mid/small caps to overweight: We are not making changes this month as we think our selection remains valid for the months ahead.

  Stocks to underweight: we add back Prysmian following the strong recent performance.

Italian Equity Market - Asset Allocation by Sector

Positive	Neutral	Negative
UTILITIES	BANKS	CONSUMERS
ASSET MANAGEMENT	MEDIA	INDUSTRIALS
ENERGY	TELECOM	
	INSURANCE	

Source: Intermonte SIM

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GUIDE TO FUNDAMENTAL RESEARCH

The main methods used to evaluate financial instruments and set a target price for 12 months after the investment recommendation are as follows:

- Discounted cash flow (DCF) model or similar methods such as a dividend discount model (DDM)
- Comparison with market peers, using the most appropriate methods for the individual company analysed: among the main ratios used for industrial sectors are price/ earnings (P/E), EV/EBITDA, EV/EBIT, price /sales.
- Return on capital and multiples of adjusted net book value are the main methods used for banking sector stocks, while for insurance sector stocks return on allocated capital and multiples on net book value and embedded portfolio value are used
- For the utilities sector comparisons are made between expected returns and the return on the regulatory asset base (RAB)

Some of the parameters used in evaluations, such as the risk-free rate and risk premium, are the same for all companies covered, and are updated to reflect market conditions. Currently a risk-free rate of 4.0% and a risk premium of 5.5% are being used.

Frequency of research: quarterly.

Reports on all companies listed on the S&PMIB40 Index, most of those on the MIDEX Index and the main small caps (regular coverage) are published at least once per quarter to comment on results and important newsflow.

A draft copy of each report may be sent to the subject company for its information (without target price and/or recommendations), but unless expressly stated in the text of the report, no changes are made before it is published.

Explanation of our ratings system:

BUY: stock expected to outperform the market by over 25% over a 12 month period;

OUTPERFORM: stock expected to outperform the market by between 10% and 25% over a 12 month period;

NEUTRAL: stock performance expected at between +10% and – 10% compared to the market over a 12 month period;

UNDERPERFORM: stock expected to underperform the market by between –10% and -25% over a 12 month period;

SELL: stock expected to underperform the market by over 25% over a 12 month period.

Prices: The prices reported in the research refer to the price at the close of the previous day of trading

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Intermonte SIM is authorised by CONSOB to provide investment services and is listed at n° 246 in the register of brokerage firms.

As at 30 June 2024 Intermonte’s Research Department covered 116 companies. Intermonte’s distribution of stock ratings is as follows:

BUY:	23.97 %
OUTPERFORM:	49.59 %
NEUTRAL:	25.61 %
UNDERPERFORM	00.83 %
SELL:	00.00 %

The distribution of stock ratings for companies which have received corporate finance services from Intermonte in the last 12 months (49 in total) is as follows:

BUY:	38.78 %
OUTPERFORM:	51.02 %
NEUTRAL:	10.20 %
UNDERPERFORM	00.00 %
SELL:	00.00 %

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