LOMBARD ODIER

LOMBARD ODIER DARIER HENTSCH

CIO Flash Bulletin

Swiss small and mid-caps at an all-time high: a sustainable rise?

Investment Solutions **November 2017**

Buoyed by strong earnings growth, Swiss small and mid-caps have outperformed large caps by over 11.8% year-to-date. This trend has also been observed in the European markets, and has recently started in the United States. Here, we analyse the potential of this important sector of the Swiss economy.

By Stéphane Monier, Chief Investment Officer Lombard Odier Private Bank

The burning question for investors interested in equities is whether they should continue to invest capital in this asset class when the markets seem expensive at their current levels. The S&P 500 is trading at close to 21.8x the price/earnings ratio, the Stoxx Europe 600 at 21.3x, the SMI at 24.7x and the SPI at 17.3x[1]. Some commentators would put the figure for the SMI higher, given that its performance was penalised by the decline in the three heavyweights that make up 60% of the index: Novartis, Nestlé and Roche. Does a historic multiple equal an expensive asset class? Not necessarily. There are two aspects to an equity valuation. The first, future earnings growth, allows listed shares to enter into a prolonged rise for as long as companies can maintain sustained earnings growth. The second is relative valuation. Compared with the expected return on other asset classes, the return on equities is appealing. In Switzerland, the dividend yield is 3.2% for the SMI, 2.9% for the SPI and 2.1% for the SPI Extra[2], attractive levels in the universe of low returns on financial assets. In the current macroeconomic environment, and based on the global economic outlook, it would therefore seem that the equity markets are not overheating but have achieved a cruising speed in sync with global growth. For investors attracted by Swiss securities, the small and mid-cap segment looks particularly interesting.

The outperformance of listed small and mid-caps stands out in the developed markets. In Switzerland, they have been outpacing large caps by 11.8% year-to-date[3]. The same trend can be seen in the Eurozone, where the performance of the 200 smallest companies in Stoxx Europe 600 has exceeded that of the 200 largest by 7.3%[4]. In the United States, companies with a market value of less than USD 2 billion are embarking on a cycle of outperformance buoyed by expectations about future tax reform. This should help them navigate with the wind at their backs in the medium term.

Stéphane Monier
Chief Investment Officer, Lombard Odier Private Bank

Key takeaways

- Small and mid-caps have outperformed large caps in Switzerland and in the Eurozone year-to-date. This trend has also started in the United States.
- Swiss small and mid-caps represent a high-quality sector, exposed to structural transformation resulting from the fourth industrial revolution, and well placed to benefit from the solid fundamentals supporting global economic growth.

---

[1] The SMI (Swiss Market Index) measures the performance of 20 star-performing listed Swiss stocks. The SPI (Swiss Performance Index) includes all Swiss companies listed on the SIX Swiss Exchange and some primary listed foreign companies (source: SIX Swiss Exchange). Figures as at 3 November 2017, Bloomberg.

[2] SPIEX – SPI Extra, the Swiss Stock Exchange index that measures the performance of small and medium-sized enterprises (companies that are not included in the SMI).

[3] SPIEX versus SMI, figures as of 31 October 2017, Bloomberg.

[4] A performance of 15.57% for the 200 smallest companies versus 8.27% for the largest companies year-to-date. Source: Bloomberg.

Important information: Please see important information at the end of this document.
Monthly publication of Lombard Odier – Contacts: Investment Solutions, CP-INVESTMENT@lombardodier.com
Data as of 6 November 2017 unless otherwise stated.

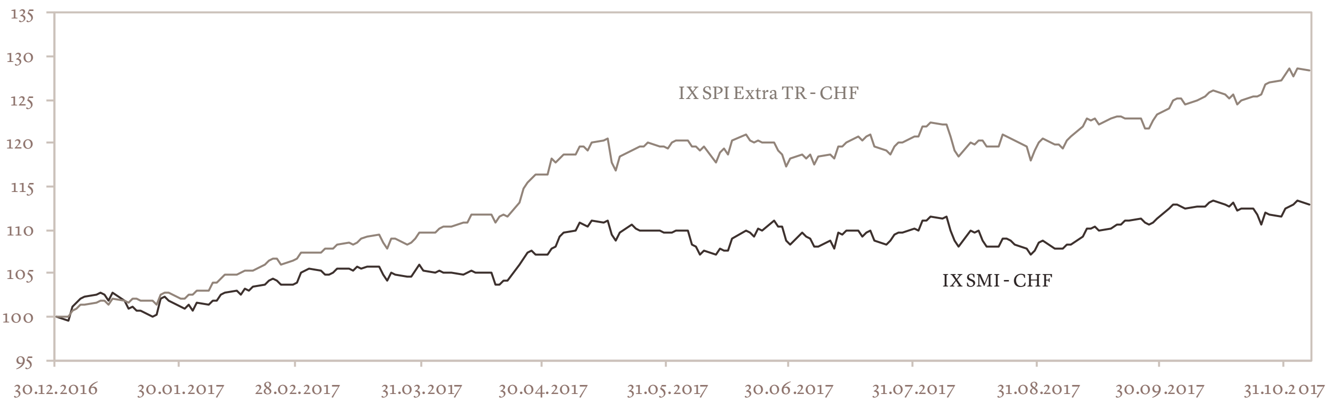
Small and medium enterprises (SMEs)[5] make up the backbone of the Swiss economy. Most of the listed SMEs are export firms. For these companies, external market growth sets the pace for their earnings outlook. And they have good reason to be optimistic. For the first time since the financial crisis in 2008, the global economies have engaged this year on a path of a synchronised and stable recovery. Balanced growth, subdued inflation and an affordable cost of capital are the hallmarks of this "soft goldilocks" economic environment. Our contacts confirm that the economic recovery in Europe and the rest of the world is clearly setting the pace for the performance of Swiss small and mid-caps. While most of them are reluctant to publicly disclose too many details about the expected figures – as traditional conservatism dictates – they are quietly confident about their future activities. In terms of sectors, companies operating in construction materials are mainly counting on the Eurozone's economic recovery and a constructive tone emanating from China. Names associated with the automotive industry continue to benefit from the positive trends in Europe. In the oil and gas industry, although the firms appear cautious, their order books are stabilising. Companies in the agricultural sector are holding up well. Overall, Swiss companies continue to fund innovative products and implement pioneering business models in the health, technology, automation and supply chain optimisation sectors, and many more.

Admittedly, Switzerland's growth rate is currently more modest than that of the Eurozone and the United States. To boost growth, economic players cannot afford to shy away from making crucial investments as savings excesses could stifle domestic growth. Nevertheless, the country does have some major advantages. Switzerland is top of the World Economic Forum (WEF) competitiveness index, and is consequently very well placed to benefit from the fourth industrial revolution. This ranking attests to its sophisticated economic activity, efficient labour market and innovation capacity. The WEF describes Switzerland as one of the world's most fertile innovation ecosystems, and identifies the SME sector as a part of the economy that is very active in innovation and well known for the quality of its products and services[6]. Switzerland nurtures companies with global reach and has historically produced leaders in numerous industries, while its innovation has stimulated economic growth. Growth supported by advances in technology – i.e. structural forces rather than cyclical factors – is particularly desirable, as it is by nature defensive. It tends to protect corporate earnings when the economy enters a cyclical downturn. The small and mid-cap segment is well placed on this path of structural transformation: the technology sector now represents 11% of the SPI Extra, and the industrial sector 26%.

The global economies and markets are still vulnerable to certain risks, and investors would be well advised to look closely at those that might jeopardise the global economic upturn: deteriorating global financial conditions, inflation no longer under control and geopolitical risks that weigh on a number of markets. While the Swiss stock market is trading at high levels in the short term, we think that there are pockets of opportunities in the small and mid-cap segment, a high-quality sector that is well placed to benefit from the solid fundamentals supporting the global economic upturn.

Performance of the SPI Extra versus the SMI

Year-to-date 2017



Source: Bloomberg

[5] 99% of Swiss companies are SMEs. Source: Swiss Confederation https://www.eda.admin.ch/aboutswitzerland/en/home/wirtschaft/uebersicht/wirtschaft---fakten-und-zahlen.html (last updated 18 August 2017).

[6] The Global Competitiveness Report 2017-2018, K. Schwab, World Economic Forum, 26 Sept. 2017.

Important information: Please see important information at the end of this document.

Important information

This is a marketing communication issued by Bank Lombard Odier & Co Ltd or an entity of the Group (hereinafter "Lombard Odier"). It is not intended for distribution, publication, or use in any jurisdiction where such distribution, publication, or use would be unlawful, nor is it aimed at any person or entity to whom it would be unlawful to address such a document.

This marketing communication is provided for information purposes only. It does not constitute an offer or a recommendation to subscribe, to purchase, sell or hold any security or financial instrument. It contains the opinions of Lombard Odier, as at the date of issue. These opinions and the information contained herein do not take into account an individual's specific circumstances, objectives, or needs. No representation is made that any investment or strategy is suitable or appropriate to individual circumstances or that any investment or strategy constitutes a personal investment advice to any investor. Tax treatment depends on the individual circumstances of each client and may be subject to change in the future. Lombard Odier does not provide tax advice. Therefore, you must verify the above and all other information provided in the marketing communication or otherwise review it with your external tax advisors.

Investments are subject to a variety of risks. Before entering into any transaction, an investor should consult his/her investment advisor and, where necessary, obtain independent professional advice in respect of risks, as well as any legal, regulatory, credit, tax, and accounting consequences. The information and analysis contained herein are based on sources considered to be reliable. Lombard Odier make its best efforts to ensure the timeliness, accuracy, and completeness of the information contained in this marketing communication. Nevertheless, all information and opinions as well as the prices, market valuations and calculations indicated herein may change without notice.

Past performance is no guarantee of current or future returns, and the investor may receive back less than he/she invested. The value of any investment in a currency other than the base currency of a portfolio is subject to foreign exchange rate risk. These rates may fluctuate and adversely affect the value of the investment when it is realised and converted back into the investor's base currency. The liquidity of an investment is subject to supply and demand. Some products may not have a well-established secondary market or in extreme market conditions may be difficult to value, resulting in price volatility and making it difficult to obtain a price to dispose of the asset.

European Union Members: This document has been approved for use by Lombard Odier (Europe) S.A., in Luxembourg and by each of its branches operating in the following territories: **Belgium**: Lombard Odier (Europe) S.A. Luxembourg • Belgium branch; **France**: Lombard Odier (Europe) S.A.• Succursale en France; **Italy**: Lombard Odier (Europe) S.A. • Italian Branch; **Netherlands**: Lombard Odier (Europe) S.A. • Netherlands Branch; **Spain**: Lombard Odier (Europe) S.A. • Sucursal en España; and **United Kingdom**: Lombard Odier (Europe) S.A. • UK Branch.

Notice to investors in the United Kingdom: Lombard Odier (Europe) S.A. • UK Branch is authorised in the UK by the Prudential Regulation Authorities (PRA) and is subject to limited regulation by the Financial Conduct Authority ('FCA') and the Prudential Regulation Authority ('PRA'). **Details of the extent of our authorisation and regulation by the PRA and regulation by the FCA are available from us on request. UK regulation for the protection of retail clients in the UK and the compensation available under the UK Financial Services Compensation Scheme does not apply in respect of any investment or services provided by an overseas person.**

In addition, this document has also been approved for use by the following entities domiciled within the European Union: **Gibraltar**: Lombard Odier & Cie (Gibraltar) Limited; **Spain**: Lombard Odier Gestión (España) S.G.I.I.C., S.A.U.

Switzerland: This document has been approved for issue in Switzerland by Bank Lombard Odier & Co Ltd Geneva, a bank and securities dealer authorized and regulated by the Swiss Financial Market Supervisory Authority (FINMA).

United States: Neither this document nor any copy thereof may be sent, taken into, or distributed in the United States of America, any of its territories or possessions or areas subject to its jurisdiction, or to or for the benefit of a United States Person. For this purpose, the term "United States Person" shall mean any citizen, national or resident of the United States of America, partnership organized or existing in any state, territory or possession of the United States of America, a corporation organized under the laws of the United States or of any state, territory or possession thereof, or any estate or trust that is subject to United States Federal income tax regardless of the source of its income.

SWITZERLAND

GENEVA
Bank Lombard Odier & Co Ltd[1]
Rue de la Corraterie 11 · 1204 Genève · Suisse
geneva@lombardodier.com
Lombard Odier Asset Management (Switzerland) SA
Avenue des Morgines 6 · 1213 Petit-Lancy · Suisse
Support-Client-LOIM@lombardodier.com
Management Company regulated by the FINMA.

FRIBOURG
Banque Lombard Odier & Cie SA · Bureau de Fribourg[1]
Rue de la Banque 3 · 1700 Fribourg · Suisse
fribourg@lombardodier.com

LAUSANNE
Bank Lombard Odier & Co Ltd[1]
Place St-François 11 · 1003 Lausanne · Suisse
lausanne@lombardodier.com

VEVEY
Banque Lombard Odier & Cie SA · Agence de Vevey[1]
Rue Jean-Jacques Rousseau 5 · 1800 Vevey · Suisse
vevey@lombardodier.com

ZURICH
Bank Lombard Odier & Co Ltd[1]
Utoschloss · Utoquai 29-31 · 8008 Zürich · Schweiz
zurich@lombardodier.com

EUROPE

AMSTERDAM
Lombard Odier (Europe) S.A. · Netherlands Branch[2]
Herengracht 466 · 1017 CA Amsterdam · Nederland
amsterdam@lombardodier.com
Credit institution supervised in the Netherlands by De Nederlandsche Bank (DNB) and Autoriteit Financiële Markten (AFM).

BRUSSELS
Lombard Odier (Europe) S.A. Luxembourg · Belgium branch[2]
Avenue Louise 81 · Box 12 · 1050 Brussels · Belgium
brussels@lombardodier.com
Credit institution supervised in Belgium by the Banque nationale de Belgique (BNB) and the Financial Services and Markets Authority (FSMA).

GIBRALTAR
Lombard Odier & Cie (Gibraltar) Limited
Suite 921 Europort · P.O. Box 407 · Gibraltar
gibraltar@lombardodier.com
Authorised and regulated by the Gibraltar Financial Services Commission (FSC) to conduct banking and investment services business.

[1] *Private bank and securities dealer authorised and regulated by the Swiss Financial Market Supervisory Authority (FINMA).*

[2] *Branch of Lombard Odier (Europe) S.A., a credit institution based in Luxembourg, authorised and regulated by the Commission de Surveillance du Secteur Financier (CSSF) in Luxembourg.*

LONDON
Lombard Odier (Europe) S.A.[2]
Queensberry House · 3 Old Burlington Street · London W1S 3AB · United Kingdom
london@lombardodier.com
The Bank is authorised and regulated in the UK by the Prudential Regulation Authority (PRA) and subject to limited regulation by the Financial Conduct Authority (FCA) and the PRA. Details of the extent of our authorisation and regulation by the PRA and regulation by the FCA are available from us on request. Registered in Luxembourg No. B169907.
Lombard Odier Asset Management (Europe) Limited
Queensberry House · 3 Old Burlington Street · London W1S 3AB · United Kingdom
london@lombardodier.com
Investment firm authorised and regulated by the Financial Conduct Authority (FCA register No. 515393).

LUXEMBOURG
Lombard Odier (Europe) S.A.
291, route d'Arlon · 1150 Luxembourg · Luxembourg
luxembourg@lombardodier.com
Credit institution authorised and regulated by the Commission de Surveillance du Secteur Financier (CSSF) in Luxembourg.
Lombard Odier Funds (Europe) S.A.
291, route d'Arlon · 1150 Luxembourg · Luxembourg
luxembourg@lombardodier.com

MADRID
Lombard Odier (Europe) S.A. · Sucursal en España[2]
Paseo de la Castellana 66 · 4ª Pl. · 28046 Madrid · España · madrid@lombardodier.com
Credit institution supervised in Spain, by the Banco de España and the Comisión Nacional del Mercado de Valores (CNMV).
Lombard Odier Gestión (España) S.G.I.I.C, S.A.U.
Paseo de la Castellana 66 · 4ª Pl. · 28046 Madrid · España · madrid@lombardodier.com
Management Company supervised by the Comisión Nacional del Mercado de Valores (CNMV).

MILAN
Lombard Odier (Europe) S.A. · Succursale in Italia[2]
Via Santa Margherita 6 · 20121 Milano · Italia
milano-cp@lombardodier.com
Credit institution supervised in Italy by the Commissione Nazionale per le Società e la Borsa (CONSOB) and la Banca d'Italia.

MOSCOW
Bank Lombard Odier & Co Ltd · Representative Office Moscow
82 Sadovnicheskaya Street · 115 035 Moscow · Russian Federation · moscow@lombardodier.com
Under the supervisory authority of the Central Bank of the Russian Federation.

PARIS
Lombard Odier (Europe) S.A. · Succursale en France[2]
8, rue Royale · 75008 Paris · France.
RCS PARIS B 803 905 157 · paris@lombardodier.com
Credit institution supervised in France by the Autorité de contrôle prudentiel et de résolution (ACPR) and by the Autorité des Marchés Financiers (AMF) in respect of its investment services activities. Business permit No. 23/12. Registered in Luxembourg No. B169 907.
Insurance intermediary authorised by the Commissariat aux Assurances (CAA) No. 2014 CM002. The registration with the CAA can be verified at www.orias.fr.

MIDDLE EAST | AMERICAS | ASIA | PACIFIC

BERMUDA
Lombard Odier Trust (Bermuda) Limited
3rd Floor, Victoria Place · 31 Victoria Street · Hamilton HM 10 · Bermuda · bermuda@lombardodier.com
Licensed to conduct Trust and Investment Business. Supervised by the Bermuda Monetary Authority (BMA).

DUBAI
Bank Lombard Odier & Co Ltd · Representative Office Dubai
Conrad Business Tower · 12th Floor · Sheikh Zayed Road · P.O. Box 212240 · Dubai · UAE
dubai@lombardodier.com
Under the supervisory authority of the Central Bank of the UAE.

HONG KONG
Lombard Odier (Hong Kong) Limited
3901, Two Exchange Square · 8 Connaught Place · Central · Hong Kong · hongkong@lombardodier.com
A licensed entity regulated and supervised by the Securities and Futures Commission in Hong Kong.

ISRAEL
Israel Representative Office · Bank Lombard Odier & Co Ltd
Museum Tower, 7th floor · 4 Berkowitz Street · Tel Aviv 6423806 · Israel · telaviv@lombardodier.com
Israel Representative Office of Bank Lombard Odier & Co Ltd is not supervised by the Supervisor of Banks in the Bank of Israel, but by Swiss Financial Market Supervisory Authority which supervises the activities of Bank Lombard Odier & Co Ltd.

MONTREAL
Lombard Odier & Cie (Canada), Limited Partnership
1000 Sherbrooke Street West · Suite 2200 · Montreal (Quebec) · Canada H3A 3R7
montreal@lombardodier.com
Regulated by the Autorité des Marchés Financiers du Québec.

NASSAU
Lombard Odier & Cie (Bahamas) Limited
Goodman's Bay Corporate Centre · West Bay Street · P.O. Box N-4938 · Nassau · Bahamas
nassau@lombardodier.com
Supervised by the Central Bank of the Bahamas and the Securities Commission of the Bahamas.

PANAMA
Lombard Odier & Cie (Bahamas) Limited · Representative Office in Panama
Oceania Business Plaza Torre 2000 · Oficina 38-D · Blvd. Pacifica · Urb. Punta Pacifica · Corregimiento de San Francisco · Panamá · panama@lombardodier.com
Supervised by the Central Bank of the Bahamas and the Superintendencia de Bancos de Panamá.
Lombard Odier (Panama) Inc.
Oceania Business Plaza Torre 2000 · Oficina 38-D · Blvd. Pacifica · Urb. Punta Pacifica · Corregimiento de San Francisco · Panamá · panama@lombardodier.com
Supervised by the Superintendencia del Mercado de valores de Panamá. License to operate as an Investment Adviser. Res. SMV No. 528-2013.

SINGAPORE
Lombard Odier (Singapore) Ltd.
9 Raffles Place · Republic Plaza #46-02 · Singapore 048619 · singapore@lombardodier.com
A merchant bank regulated and supervised by the Monetary Authority of Singapore.

TOKYO
Lombard Odier Trust (Japan) Limited
Izumi Garden Tower 41F · 1-6-1 Roppongi, Minato-ku · Tokyo 106-6041 · Japan
tokyo@lombardodier.com
Regulated and supervised by the Financial Services Agency (FSA) in Japan. It holds a trust business license (FSA No. 208) and is registered with Kanto Local Finance Bureau for Financial Instruments Business Operator (No. 470).