Q2 2017

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Investment outlook

Playing the reflation game…

- Markets are giving the Trump-led reflation story the benefit of the doubt
- Global growth is edging up and corporate fundamentals are improving
- Bull market remains intact but is late stage and will be led by earnings growth
- As a result, stock calls will now matter more than sector calls
- Political and policy risks continue to remain elevated

Fidelity's outlook for equities, bonds and alternatives

Fidelity investment view

Playing the reflation game…

The reflation story is still intact, but we expect to see occasional volatility around it, as growth and inflation data wax and wane. Investors are waiting patiently for details and actions around President Trump's pro-growth policies (tax cuts and infrastructure spending). While the US president seems committed to delivering what he said he would, markets will increasingly demand evidence over platitudes and bluster.

Secular stagnation, by contrast, has taken a back seat. Yet the concept - a mainstay in recent years to explain slower growth and low rates - retains its supporters. Notably, there has been no damaging 'great' rotation out of bond markets. The bears argue that high debt levels, ageing demographics and low productivity have not gone away. Certainly, a sustained Trump-led growth trajectory will have to overcome some powerful headwinds.

Here, we reveal our views on the path of investment assets; these views are built on the fundamental research that we undertake on companies, governments, issuers, properties and tenants. We also reveal the regions and sectors we believe offer the most and least attractive growth and returns based on proprietary aggregate forecasts that are built from the ground up.

Contents

About the views

Note: This investment outlook provides a representative summary of the views of Fidelity International's investment teams. At Fidelity, individual portfolio managers have considerable flexibility and ultimately fiduciary responsibility for all investment decisions within their portfolios. Given this portfolio manager discretion, there may be differences between the broad, representative views shared here and the strategies applied within specific Fidelity funds.

Equities overview

Key Takeaways

- We remain in a firmly equity-friendly environment: equities will 'trump' bonds.
- Any progress on fiscal and infrastructure stimulus in the US will confirm the reflationary growth story and be positive for equity markets.
- We are entering a late stage within this extended equity bull market and US leadership will begin to fade.

Global aggregate forecasts	2017	2018
Earnings Growth	10.3%	9.1%
Return on Equity	13.0%	13.5%
Dividend Yield	2.6%	2.8%
P/E Valuation	15.6x	14.3x
P/B Valuation	2.0x	1.9x

Source: Fidelity Insights, Global Aggregate Forecasts in USD, March 2017. Our global aggregate forecasts are based on proprietary bottom-up research, and are the product of c.2500 individual company forecasts and 17,000 company meetings a year across all industry sectors and regions. Returns shown for a global USD investor.

Outlook

The bull market has momentum albeit we are entering a late stage

In 2017, equities will trump bonds. We are likely to see a move back towards an earnings-led market - indeed that has already begun - but we will also see the strength of US equity market leadership begin to fade. We are now eight years into an extended equity bull market that has been led by the US and driven by multiple expansion; developed markets have outperformed emerging markets; and we have seen a re-rating of intangible assets over hard assets in stark contrast to the previous bull phase of 2003-08.

This equity bull run still has strong momentum thanks to improving global activity and better corporate earnings growth backed by a strong reflationary narrative. Indeed, there is a chance that we could see a remarkably strong year for equities that, in itself, pushes us closer to the end of this bull market. Certainly, the 12-18 month outlook is strong, although it is worth recognising that we are now in the late stage, or the last quarter, of this bull market.

Most commentators are also bullish on the US dollar given the growth and interest rate differentials. However, dollar strength is likely to be capped if President Trump gets his way. If he does manage to enact aggressive fiscal stimulus and an ambitious infrastructure spending programme, it is likely that we will see the dollar bull run end at some point due to the impact of greater spending on the US fiscal account. While US equity market leadership is likely to wane given higher valuations, the scope for a re-rating in Europe, where valuations trade on a 20% discount to the US, is significant if we see benign political outcomes, for example, in the French election.

Corporate earnings growth is back

After a couple of years of disappointing corporate profits growth, we are now seeing a broad-based improvement in earnings. We are currently forecasting global earnings growth of 10.3% and a return on equity (ROE) of 13% in 2017, based on our proprietary fundamental earnings models for individual stocks. European earnings have lagged behind those of the US in recent years. However, we are now seeing a recovery in European corporate earnings.

Inflation is also coming back onto the radar

Financial cycles tend to produce their own grave diggers and this one is likely to be incrementally challenged by a familiar old foe as global growth picks up and monetary policy begins to normalise. Inflation is something we have barely had to worry about for a decade; the greater concern has been deflation. However, there is now a danger that financial markets will underestimate inflation. The reason is that all the major economies of the world are now operating at above-trend growth. This has not been the case for ten years. Spare capacity could get used up quite quickly, after which inflation could take hold. By the back-end of 2018, inflation could begin to cause some problems.

Hallmarks of recent bull markets

	2003-08	2009 - 2016
Main driver	Earnings growth	Multiple expansion
Leadership	China	US
Regional	EM>DM, weaker dollar	DM>EM, stronger dollar
Sector leadership	Hard assets, resources	Intangible assets, intellectual property
Investment focus	Rise of multi-asset, alternatives	Age of income investing

Source: Fidelity International.

What can we expect in 2017?

2017 >
Earnings growth-led
US market leadership will wane
US dollar bull run will peak
Less pronounced sector leadership Greater discrimination within sectors
Equities will 'trump' bonds Active management to perform better

Source: Fidelity International, March 2017.

US equities

Aggregate forecasts	2017	2018
Earnings Growth	10.3%	11.7%
Return on Equity	16.1%	17.2%
Dividend Yield	2.0%	2.2%
P/E Valuation	18.1x	15.9x
P/B Valuation	2.9x	2.7x

Source: Fidelity Insights, Global Aggregate Forecasts in USD, March 2017.

Outlook

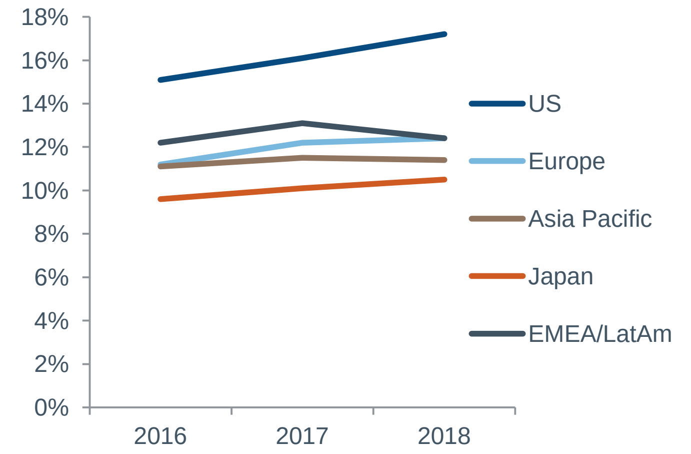
US dividend growth paints a positive market outlook

The S&P 500 index has been tracking the upward trend in US dividend pay-outs for the whole of this bull market. By the end of 2016, we reached just under $47 a share. Yet the pay-out ratio is still only 38%. Now with earnings growth accelerating again, the dividend pay-out could grow by four to five dollars per year. That would mean by the end of 2019, the S&P 500 would be distributing $60 a share, up from $25 at the peak of the last bull market in 2007. At $60 a share and a 2% dividend yield, this would indicate a market level for the S&P 500 of 3,000 by 2019. With interest rates going up however, this would argue for a dividend yield of 2.25% and a market level of 2,700. Either way, there could be a few hundred more points to go in this bull market.

Double-digit earnings growth in 2017

After a flat 2016, 2017 will see a double-digit recovery in profits growth, allowing market moves to be led by earnings rather than higher multiples. We are forecasting 10.3% earnings growth in 2017 and a return on equity of 16.1%, based on an aggregation of our analysts' forecast models for individual stocks. With S&P 500 companies harbouring an estimated $1 trillion in offshore earnings, the much-vaunted tax deal of the Trump administration to bring those dollars home could stimulate investment spending and future profits. However, there is a strong likelihood we will see much of this money returned to shareholders via dividends and buybacks. In 2017, buybacks could hit a record-breaking $780bn. Add this to an estimated $460bn in total dividends and we may be set for the most generous corporate handout in history.

US leads the way in returns on equity



Source: Fidelity Insights, Global Aggregate Forecasts in USD, March 2017. Note: 2018 are estimated projections.

European (incl. UK) equities

Aggregate forecasts	2017	2018
Earnings Growth	10.6%	8.4%
Return on Equity	12.2%	12.4%
Dividend Yield	3.4%	3.6%
P/E Valuation	15.9x	14.6x
P/B Valuation	1.9x	1.8x

Outlook

Politics has made sentiment very negative

Political uncertainty has clouded investor sentiment towards European stocks. The market has continued to see material outflows this year on top of $100 billion in outflows in 2016. Performance relative to the US recently hit a 40-year low - the kind of level historically associated with strong trend reversals. The stock market trades at a 21% discount to the US on a forward PE basis. On a Shiller PE basis, Europe has not been this cheap in a generation.

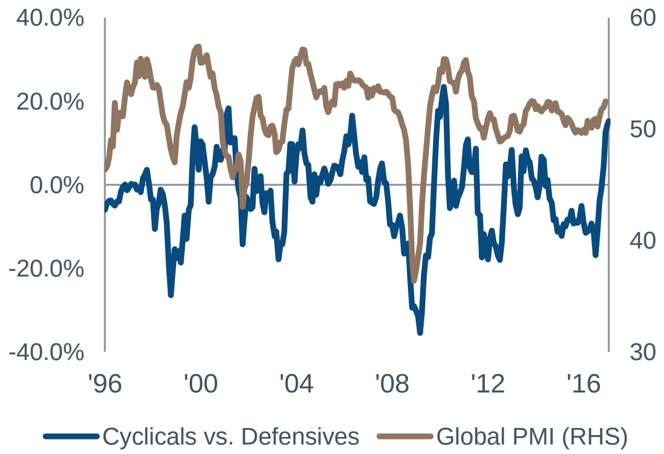
Yet economic and earnings growth is picking up

This valuation discount remains in place despite the fact we are seeing meaningful improvement in the European economy. Unemployment is falling and growth is solid, while credit and inflation are picking up. Critically, we are seeing a synchronised pickup in PMIs in both the core and periphery. Even the UK has been resilient, though formal Brexit negotiations present a headwind. We are also seeing a reasonable recovery in European earnings. Earnings revisions ratios haven't been this positive in 5 years, while the breadth of revisions is also at a 5-year high. Sector calls mattered much more than stock calls in 2016 - as cyclicals sharply outperformed defensives in H2 - but this is changing, with stocks that beat profit targets outperforming this earnings season.

A material re-rating is possible…if politics stay benign

If political events, such as the French election, are navigated without shocks, the potential for a re-rating of European equities is significant. There is ample scope for a catch-up in valuations to reflect better fundamentals.

Cyclicals have sharply outperformed defensives



Source: Goldman Sachs, February 2017. The dark blue line shows the YoY relative performance of cyclicals versus defensives, so when >0 cyclicals have outperformed over preceding 12m; when <0 defensives have outperformed over preceding 12m.

Asia Pacific (ex.Japan) equities

Aggregate forecasts	2017	2018
Earnings Growth	9.9%	7.2%
Return on Equity	11.5%	11.4%
Dividend Yield	3.0%	3.2%
P/E Valuation	13.1x	12.7x
P/B Valuation	1.5x	1.4x

Source: Fidelity Insights, Global Aggregates Forecasts in USD, March 2017.

Japanese equities

Aggregate forecasts	2017	2018
Earnings Growth	5.4%	8.6%
Return on Equity	10.1%	10.5%
Dividend Yield	2.1%	2.3%
P/E Valuation	14.2x	13.1x
P/B Valuation	1.4x	1.3x

Outlook

Grounds for optimism

There are grounds to be constructive on Asian equities. Markets have performed well relative to US equities, yet there is still scepticism among investors, and data shows that the average investor is still underweight Asia. Valuations are attractive relative to the US on a price-to-book basis (see below), and the earnings cycle appears to have turned. Since the 1980s, Asia - on average - comes out positively from rising US rate environments. But this has typically been the result of the stronger growth that tends to accompany higher interest rates.

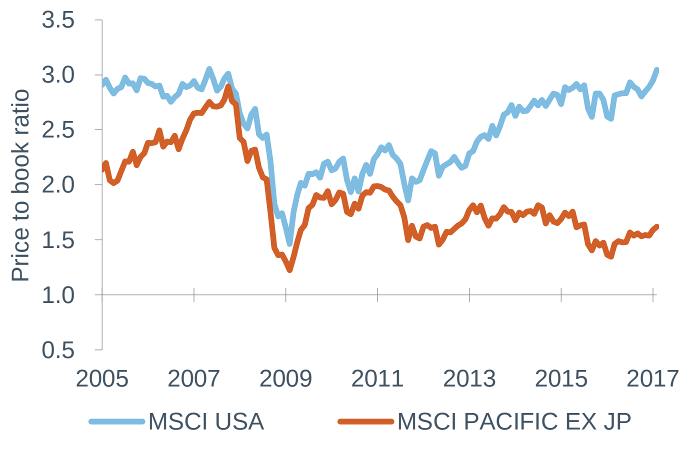
Is the traditional discount still justified?

Historically, Asian and emerging markets have traded at a discount to developed markets to reflect greater levels of political uncertainty. Yet with pronounced political risks in Europe and the US, it is worth considering whether such discounts are still warranted. Asia has been enjoying relatively stable politics. There are reforms underway in India and Indonesia, while China - the dominant power in the region - at least benefits from being a stable political construct. This autumn, the 19th National Congress of the CCP (twice a decade, last in 2012) will lay out another five-year plan that gives investors relatively good visibility on future government policy.

Protectionism is the key risk

Protectionism is the key concern for investors in Asia - a worry that is already hurting sentiment towards the region. Over the last two decades, every step has been towards free trade to the benefit of Asia and emerging markets. There is a risk that US-led protectionism could lower growth and stimulate cost-push inflation.

Asian equities trading at big price-to-book discount to US



Source: DataStream. Data as of 28 February 2017

Outlook

An improving macro picture

The Japanese economy is seeing a broad-based improvement. Fourth-quarter real GDP was 1.2% annualised, the fourth consecutive quarter of growth. Unemployment remains low at 3%, the lowest rate since 1995. With a healthy jobs-to-applicants ratio of 1.4, we saw steady growth in household incomes in 2016. Encouragingly, core CPI turned positive in January. Of course, the Bank of Japan is committed to a target of 2% so there is still some way to go. Certainly, if greater inflation were to come through, it could be a potential game-changer for the economy and stock market.

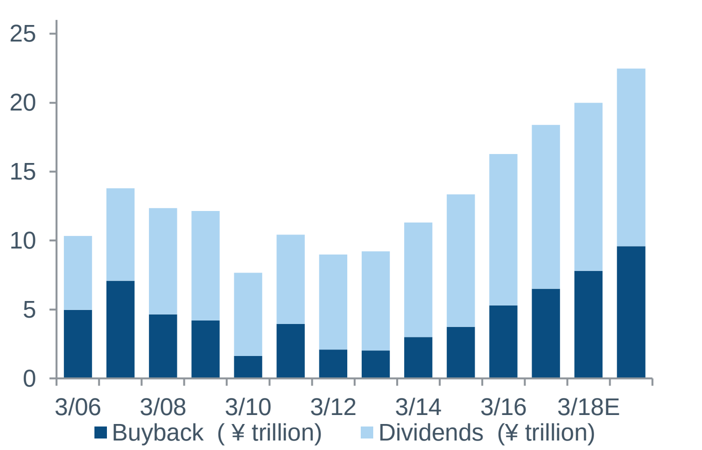
Better macro is feeding through to better earnings

The more positive global economic backdrop and the weaker yen have driven a turnaround in Japanese corporate earnings. We should see robust earnings growth and returns on equity in 2017. Many Japanese companies have high free cash flow levels so there is still scope for them to increase shareholder returns. Valuations are materially below those of the US market - with a market PE of 14 times forward earnings versus 18 times in the US. There is scope for a positive re-rating as investors reflect the improving macro and corporate environment in Japanese share prices.

Abe third term offers continuity on reform

Abe could become Japan's longest-serving prime minister after LDP party members voted to extend the terms that prime ministers can serve from two to three consecutive three-year terms. This would allow Abe - who has a high approval rating - to seek a third term in 2018. This would provide the political mandate to make further reform progress, which would support the equity market.

Improving shareholder returns and room to grow further



Source: Company data compiled by Goldman Sachs. Data as at 31 December 2016.

EMEA/Latin American equities

Aggregate Forecasts	2017	2018
Earnings Growth	16.7%	2.5%
Return on Equity	13.1%	12.4%
Dividend Yield	3.5%	3.8%
P/E Valuation	10.5x	10.1x
P/B Valuation	1.3x	1.2x

Source: Fidelity Insights, Global Aggregates Forecasts in USD, March 2017. EMEA is Emerging Europe, Middle East and Africa.

Outlook

Positive backdrop thanks to growth and commodity prices

Emerging markets have made a good start to 2017, outperforming developed markets. Improving global growth has been key, while higher commodity prices have helped exporters. Importantly, we are seeing greater supply-side discipline in China where the government has closed down steel and coal capacity. The Trump reflationary narrative is not as important for emerging markets as China. While there could be a pick-up from greater US infrastructure spending, China remains a much more significant driver of commodity pricing.

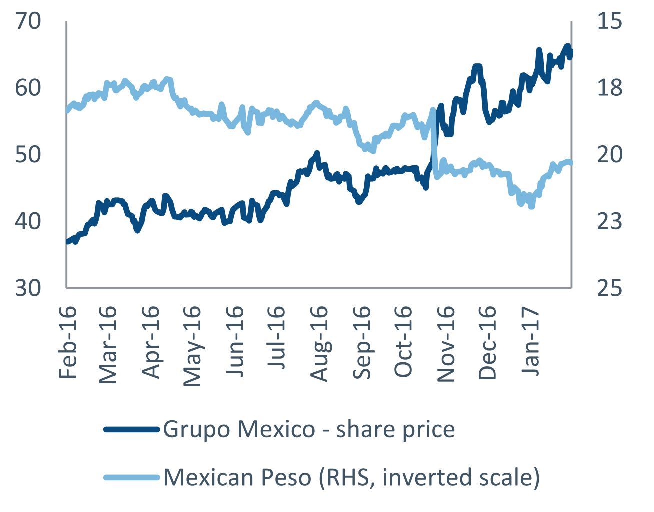
More positive on Russia

We are more positive on Russia as firmer oil prices feed through to the domestic economy. With Russian oil stocks suffering from heavy regulation and already discounting higher oil prices, we prefer to express our view via secondary beneficiaries of higher economic activity. We like Sberbank, which is the largest domestic bank and is well exposed to an upturn in the economy. Where we have materials exposure, it is focused on low-cost producers such as steel maker NLMK and fertiliser company Phosagro.

Mexican economy is struggling - but there are some winners

Mexico has perhaps suffered the most over concerns around President Trump's policies, given that around 80% of exports go to the US. There remains very little visibility but a lot of uncertainty. As a result, consumer confidence is turning over. Unfortunately, there was a fuel price hike of 20% in January, and the central bank has been raising interest rates (now at 6.25%) to offset peso weakness. We favour those companies that have costs in pesos but which can earn in foreign currencies, such as Grupo Mexico and MexiChem.

Mexican peso has been 'trumped' but there are winners



Source: Fidelity International, Bloomberg as at 17 February 2017. Reference in this document to specific securities should not be construed as a recommendation to buy or sell these securities, but is included for the purposes of illustration only.

Global equity sector views

Favoured sectors	Less favoured sectors
Technology	Property
Healthcare	Industrials
Energy	Utilities

Favoured and less favoured sectors by analyst rating

Outlook

Continue to favour technology stocks

We remain positive on technology stocks. Even though smartphone volume growth is flattening out, this does not mean innovation is fading. The ubiquity and mobility of smartphones will drive the creation of new platforms and applications which can sustain upgrade cycles for years. Moreover, the digitisation of other industries has only just begun. A good example of this is electric and autonomous cars, where we will see technology companies increasingly compete and collaborate with auto manufacturers.

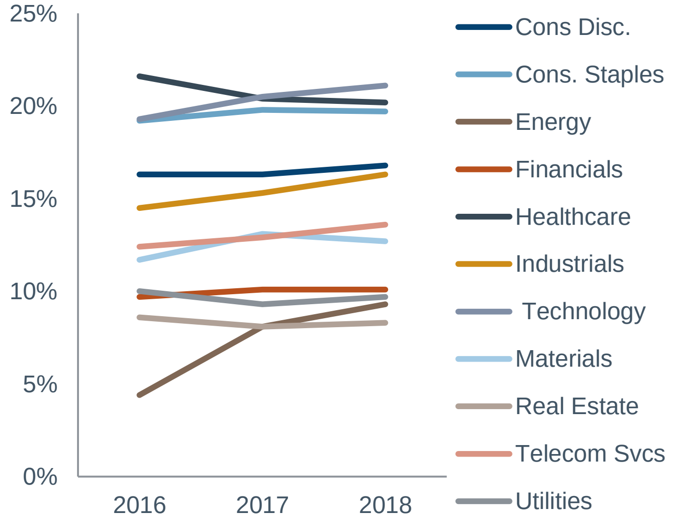
Remain positive on healthcare

We continue to favour healthcare stocks for their attractive long-term earnings potential, supported by a backdrop of structural demand. Strong R&D is delivering healthy pipelines of new drugs and innovative therapies, while there is also the potential for further M&A. In Europe, managers have reduced investments in those pharma stocks with the most significant exposure to US drug pricing due to concerns about price capping.

Industrials are priced for perfection

We think there is a bit too much optimism now baked into industrials. Our analysts are behind 'the Street' on earnings forecasts for 2017. Valuations are quite rich given we are at a late stage in the business cycle. Automobile companies are now late cycle everywhere with the exception of some emerging markets. Capital goods companies are late cycle everywhere except Europe, while construction is late cycle in both China and Japan.

Fidelity return on equity forecasts by industry sector



Source: Fidelity Insights, Fidelity International, March 2017.

Fixed income overview

Key takeaways

- Trump is not a watershed moment for the fixed income asset class. There are cyclical and secular forces which will mitigate upward pressure in Treasury yields.
- The focus is back on European politics, with investors nervously assessing the chance of a shock win for Marine Le Pen's Front National party in the French elections.
- The start of formal Brexit negotiations between the UK and EU is likely to weigh on the UK gilt market.

Current & forecast government bond yields

10yr yield	Current	Feb-18	Feb-21
US	2.43%	2.70%	3.12%
GER	0.27%	0.51%	1.17%
UK	1.19%	1.40%	2.03%

Source: Fidelity International, Bloomberg , 28 February 2017. The above forecasts are market implied forecasts.

Outlook

Focus is back on Europe

The changing political landscape in Europe and the US continues to impact fixed income markets. If 2016 was all about Trump and his campaign promises, in 2017 the focus moved firmly back to Europe and the upcoming French elections. As investors priced in a higher probability of a Le Pen victory, yields on French government bonds and on peripheral debt rose. However, our base case is that Ms. Le Pen is unlikely to succeed since the two-round electoral system in France presents a considerable hurdle to her victory. The ECB will remain actively engaged in the market, limiting any spillover from the political arena into government bonds that may impair their monetary policy transmission mechanism. Looking beyond the short term volatility and spread widening moves, we are therefore happy to take the other side of the latest market moves, with a constructive view on French government bonds and on eurozone peripheral debt more broadly.

Treasury investors have 'Trump-fatigue'

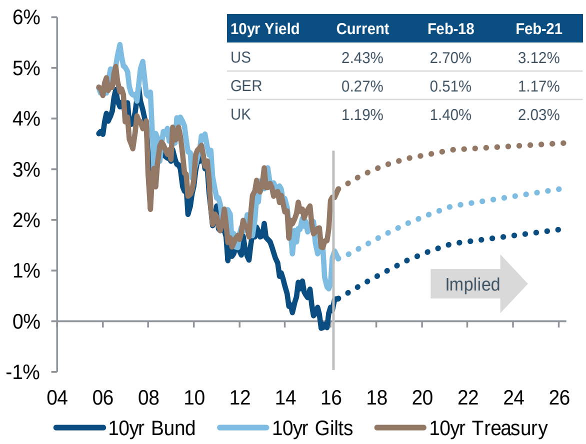
The US Treasuries market seems to be suffering from 'Trump-fatigue'. There are high expectations baked into prices, particularly around the promised fiscal stimulus, but investors are now patiently waiting for details and actions. US Treasuries have traded in a tight range since January, and the market has taken its cues from the Federal Reserve rather than Washington.

The March rate hike was navigated smoothly and the Fed is guiding for two more hikes this year. Looking ahead, however, the rise in yields and in the US dollar will gradually begin to weigh on financial conditions and on consumption. The scope for yields to increase much further from here may therefore be limited, particularly given the very optimistic scenario that is already priced in by the market. In addition, secular forces such as excess capital, high debt levels and ageing populations all continue to put downward pressure on yields.

Brexit 'phoney' war is over

The 'phoney' war is now over as the UK government begins formal negotiations to exit the European Union in April. Despite the uncertainty, capital flows to UK assets have been resilient since the EU referendum, supporting UK Gilts. Looking ahead, the scope for foreign capital to support UK Gilts appears limited, given the low level of yields on offer and the still challenging macro and political outlook. We therefore retain a cautious stance, and prefer to allocate capital to other regions.

10 year government bond yields



10yr Yield	Current	Feb-18	Feb-21
US	2.43%	2.70%	3.12%
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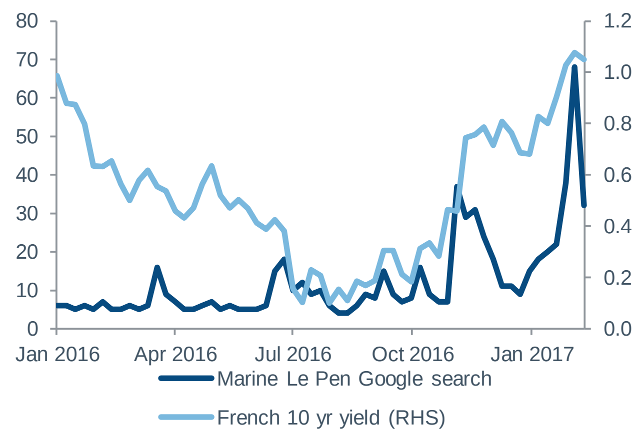
Source: Fidelity International, Bloomberg , 28 February 2017

France remains in the spotlight



Source: Fidelity International, Google Trends, Bloomberg. 17 February 2017.

Inflation linked bonds

Outlook

Constructive outlook for the asset class

With the OPEC supply deal appearing to support a stable oil price range, and evidence of inflationary pressures in various regions, we remain constructive on the outlook for inflation linked bonds in the medium term. Despite an uptick in recent inflation data, inflation-linked bonds have lagged their nominal counterparts due to a lack of clarity on US fiscal policy coupled with higher political uncertainty in Europe.

US inflation will remain a focus for investors

In the US, inflation expectations moderated slightly as markets await clarity on potential fiscal reforms. Labour markets remain tight with low unemployment and rising wages helping to boost consumer confidence. Strong headline and core CPI prints helped to maintain interest in the asset class and flows stand at over 3bn year to date, a trend we expect to continue as headline inflation moves above 2.5% in the coming months. We still see value in US inflation linked bonds and our long position also provides protection in the event of inflationary policies, such as trade barriers and border-adjusted taxation.

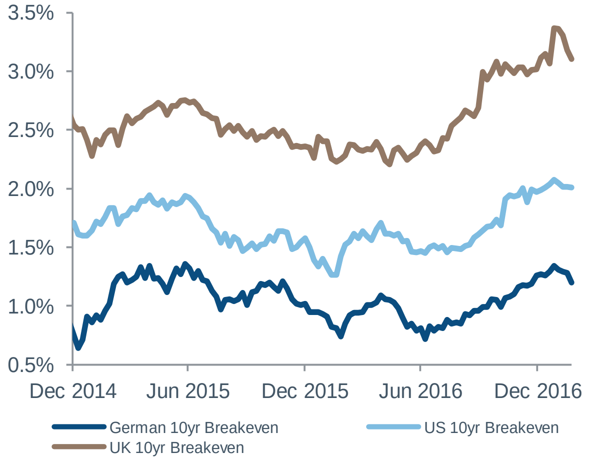
In Europe, there are opportunities in peripheral markets

Slack in European labour markets remains the biggest headwind to inflation, but we do expect the output gap in France, Italy and Spain to close, albeit slowly. Our outlook for core inflation is fairly stable, and we believe the ECB will remain accommodative in its bid to increase the level of core HICP. Political-induced weakness has made non-core inflation linked bonds attractive on a relative value basis and we retain a bias towards Italy. UK inflation linked bonds continue to look overvalued, in light of the headwinds that the economy is likely to face over the coming months. Given rich valuations and the political and macro hurdles that still lie ahead for the UK economy, we retain an underweight stance.

Emerging markets present a mixed picture

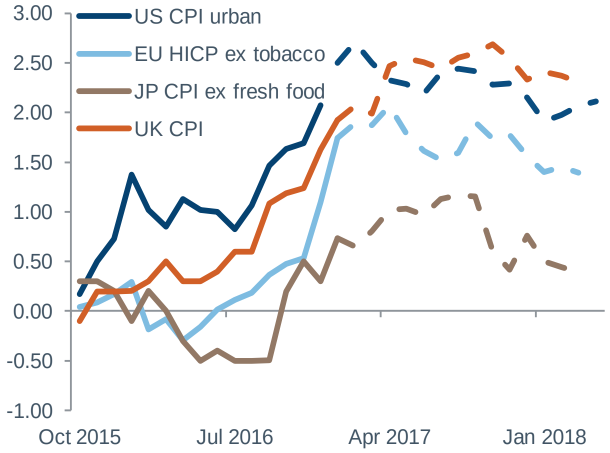
Inflation in emerging markets is generally coming in higher than expected, but at a regional level the picture is more nuanced as inflationary trends diverge. Deflationary forces are strong across much of Latin America as central banks have hiked rates to defend their currencies and mitigate inflationary pressures. However, Asia and parts of Central and Eastern Europe present the opposite picture where inflation is surprising to the upside as a result of tight labour market conditions and higher commodity prices.

Rise in breakevens led by higher nominal yields



Source: Fidelity International, Bloomberg, 28 February 2017.

Fidelity inflation forecasts



Source: Fidelity International, 28 February 2017.

Investment grade bonds

Outlook

A more neutral stance

At current levels, the case for additional spread compression in investment grade credit is less clear cut, and we have moved to a more neutral stance ahead of what is likely to be a very volatile period. We would not advocate, however, an underweight exposure to the asset class, given its defensive characteristics, solid fundamentals and ongoing support from central banks, particularly in Europe.

Risk and reward now more finely balanced for European credits

European investment grade bonds largely shrugged off the widening seen in European sovereign spreads, meaning corporate credit has outperformed government bonds by over 1.5% year to date. At 125 basis points, the yield differential between European investment grade credit and German Bunds is still far from the tightest levels that we have seen in the past. It is sensible, however, to take stock of the recent moves and of the risks ahead so we have moved to a neutral stance.

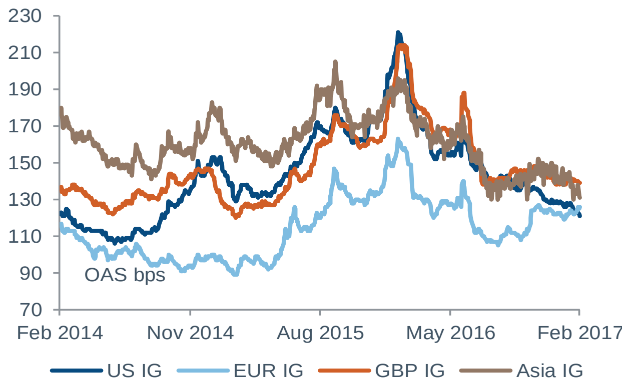
The Trump effect has left US credits fully priced

The 'Trump trade' has been a boon for US investment grade credits, with spreads tightening by 20 basis points since the US elections, and now trading tighter than European investment grade for the first time since 2013. Given how much good news is now priced in, however, we have a neutral but cautious stance towards the asset class. A busy supply schedule and the potential for disappointment on the policy front will limit the room for additional spread compression.

Asian investment grade also fully valued but currently sheltered from political storms

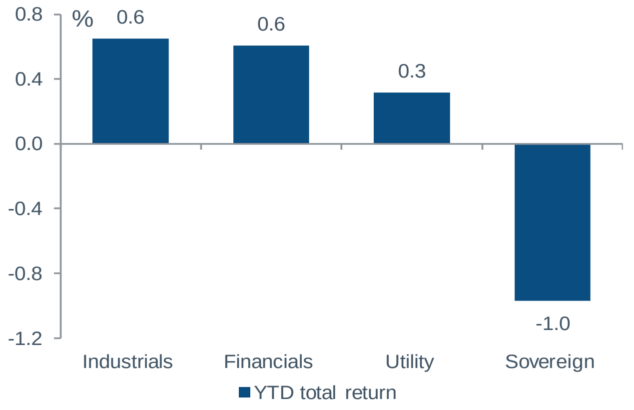
Asian USD-denominated investment grade credits face similar challenges to their US counterparts, with stretched valuations and spreads now in the 84th percentile since 2006. However, being far from the eye of the "political storm" in Europe and the US is a bonus for the asset class. Indeed, Asia investment grade credits have enjoyed healthy total returns, low volatility and low correlation to other markets thanks to the ongoing support from the domestic investor base. A neutral stance is warranted for now, although we will closely monitor valuations and political developments, with the latter likely to become a theme for Asian markets in the second half of the year.

Investment grade spreads



Source: Fidelity International, BofA Merrill Lynch, Bloomberg, 28 February 2017

Sovereign underperformance in Europe



Source: Fidelity International, BofA Merrill Lynch Indices (EMUL), 28 February 2017.

High yield bonds

Outlook

Priced for perfection?

Higher growth prospects, higher realised and expected inflation and ongoing demand for yield have so far been a perfect combination for the high yield market, allowing corporates to easily refinance debt and lower their cost of capital. Markets have been putting an extreme amount of faith (and capital) in the Trump reflation trade, pushing spreads tighter across the board. At current levels, markets seem to be priced for perfection, with implied default rates of only 1.5%, leaving little room for error.

Proceed with caution

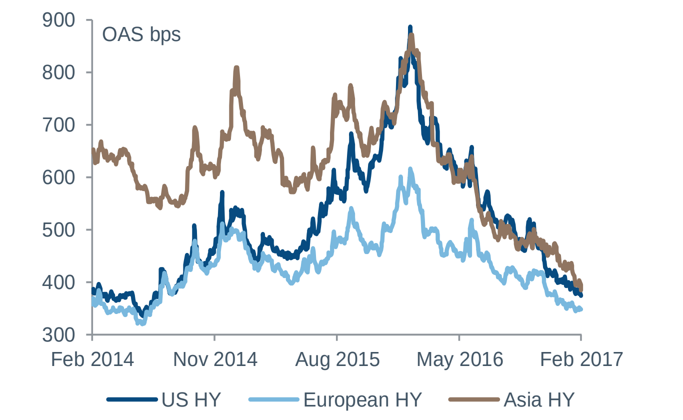
Looking beyond investors' exuberance, there are still plenty of ''known unknowns" that markets will soon have to deal with, including policy uncertainty and execution risk by the new US administration, potential monetary policy tightening both in the US and elsewhere and political hurdles in Europe. All of these require an additional risk premium and spread cushion that is currently not available in the High yield market, making us more cautious at current levels.

We are not arguing for an underweight stance just yet. Business and consumer confidence levels have been on the rise and can support risk appetite. Moreover, the ongoing financial repression by central banks in Europe and Asia will continue to fuel the search for income, limiting the upside for yields and spreads. High yield credit should also perform well in a reflationary environment, due to its short duration profile and the positive effect of higher inflation on the more leveraged corporates as they benefit from falling real debt burdens.

Neutral US and Europe, but underweight Asia

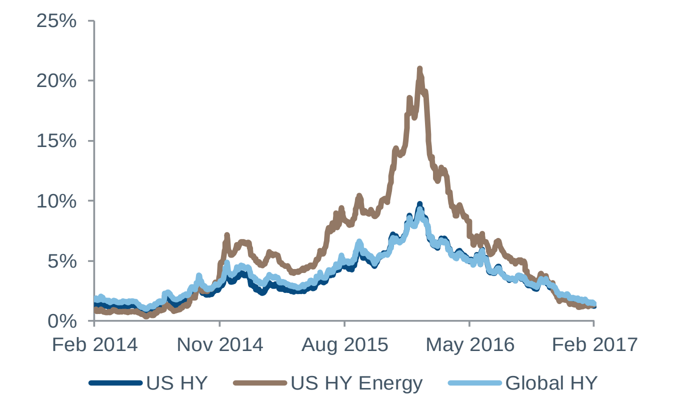
We have moved to a neutral position in US high yield in line with our European high yield exposure. We remain a little more cautious on Asia high yield, although valuations are gradually adjusting relative to the more liquid US market. With the spread differential between US and Asia still tight by historical standards, we still prefer the former to the latter, albeit less so than earlier in the year. We will look for opportunities to add to our Asian exposure should the differential between the two regions trade back to 50-100 basis points.

High yield credit spreads



Source: Fidelity International, BofA Merrill Lynch. 28 February 2017.

High yield implied default rates



Source: Fidelity International, 28 February 2017. The table shows an approximation of the default rate priced into OAS, with assumptions about required liquidity premium and recovery rates. Reference indices BofA Merrill Lynch Global HY (HW00), US HY (H0A0), US HY Energy (H0EN) index.

Emerging market debt

Outlook

Ongoing hunt for yield will support EMD as long as risk sentiment stays positive

Emerging market debt continues to benefit from positive risk sentiment and the hunt for yield that has driven returns since Trump's election. We have seen a welcome pick-up in EM economic growth momentum and credit quality is now stabilising after years of deterioration. While global growth indicators show a healthy picture overall, developed market activity is outpacing emerging market growth, a trend that could affect capital flows and EM returns in the coming months.

The outlook remains heavily dependent on the forward path of US rates and the US dollar as well as on the potential protectionist policies that the new US administration may choose to implement. Of these, the latter element in particular still hangs in the balance and could throw a spanner in the works of EM and global growth. Aside from these macro risks, certain countries will remain in the spotlight for domestic reasons. Leverage and weak growth in China, Venezuela's social unrest and dwindling foreign exchange reserves, and the increasing autocracy of the Turkish administration are some examples of areas we believe will capture more headlines this year.

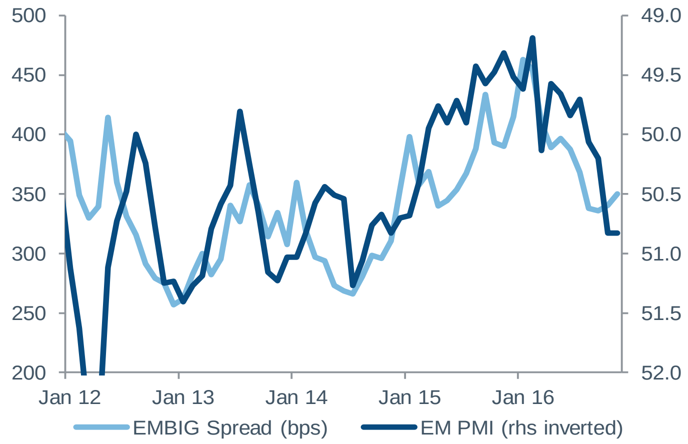
More optimistic on hard currency corporates

We retain a cautious stance towards EM hard currency sovereign debt, on the back of expensive valuations and stretched positioning. We prefer to allocate capital to EM hard currency corporates due to their higher quality, lower volatility and shorter duration characteristics, with a similar yield to what's on offer in the sovereign space.

EM local currency debt faces some headwinds, coming mainly from higher domestic inflation in some EM countries, and from the potential for further USD appreciation. Within the asset class, a higher allocation to inflation-linked bonds can help investors looking to remain engaged but who wish to diversify their sources of duration.

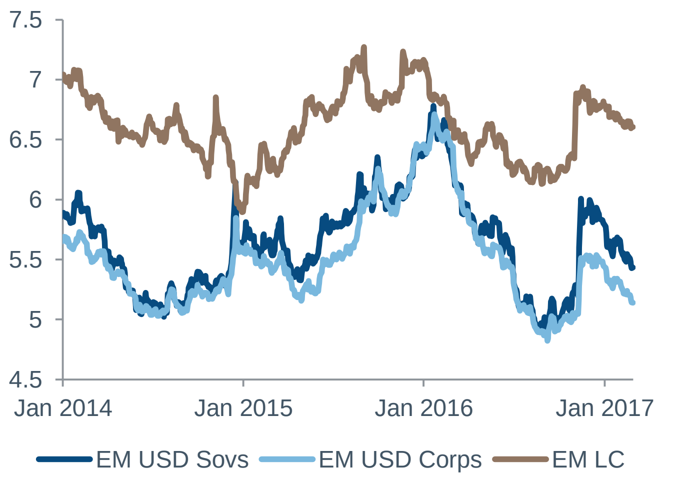
We also see opportunities in those markets where both the currency and rates have been particularly punished due to idiosyncratic reasons in the past few months. Countries like Turkey and Mexico, for example, have substantially underperformed the broader market due to macro and geopolitical concerns. While volatility in these markets will remain elevated, valuations have now adjusted considerably.

EMBIG spreads vs. EM PMI



Source: Fidelity International, Bloomberg, Markit, 28 February 2017

Yields across EM asset classes



Source: Fidelity International, Bloomberg, JP Morgan bond indices, 28 February 2017

Alternatives - Commercial Real Estate

Key Takeaways

- Underpinned by strong fundamentals and stable income returns, real estate remains an attractive investment, and we expect the ongoing growth in real estate allocations to continue
- The heavy weight of capital targeting real estate continues unabated. Cross-regional trends are becoming more complex due to the evolving global political scene
- Investors will continue to pursue lower-risk, income based strategies.

Fidelity Forecasts*	2017	5-Year
Europe market level total return	7.8% ± 2%	4.2 ± 3%
Market level total return	3.0% ± 3%	6.2% ± 3.5%

Source: Fidelity International Real Estate, JLL, March 2017.

* Synthetic prime all property return forecasts Western Europe (excl.UK) & expected variation from the base case scenario.

Commercial Real Estate: Continental Europe Outlook

Global politics - the new driving force

The ability of European real estate markets to cope with political uncertainty has been impressive so far, with France, Germany, Spain and the Netherlands gathering pace and delivering strong economic growth in Q4 2016. While a number of European elections are due to take place in 2017, we expect no further 'Brexit-like' event, with the Brexit negotiations and new US presidency remaining the two dominant political risks. Ironically, current global political uncertainty is likely to have a positive impact on European investment activity, diverting international capital towards less riskier markets, and the core Eurozone in particular. This is already starting to manifest itself, with Germany overtaking the UK as the largest European investment market in H2 2016, and we expect it to continue to gain market share in the near term, with a 25-30% market share becoming the 'new normal' (materially up on a long-term average of 19%[1]).

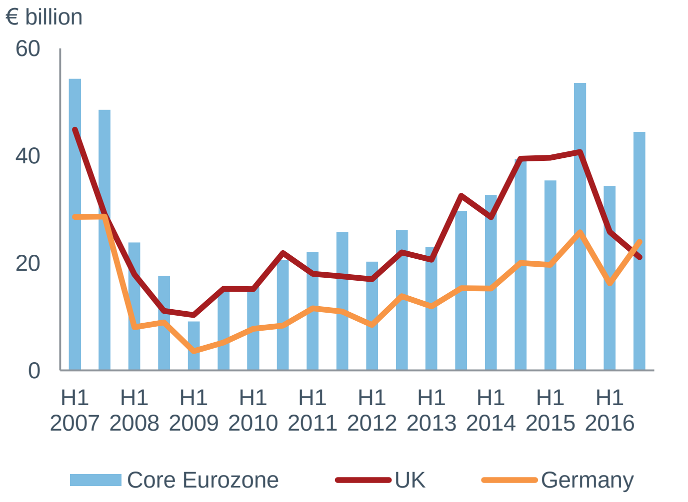
Strong fundamentals as we approach the next phase of the investment cycle

European real estate fundamentals are solid: (i) occupier demand is robust, exceeding the long-term average in many markets, (ii) vacancy levels are at structural lows, albeit development is picking up in places after a prolonged period of low construction activity, (iii) investor demand remains strong thanks to the attractions of an income-producing real asset class, which offers a partial inflation hedge. That said, if the recent uptick in economic growth continues to gather pace, the extension of the QE programme significantly beyond 2017 is unlikely. This raises our expectations that the Eurozone commercial real estate market is likely to move into the next phase of the investment cycle, where income return becomes the principal driver of performance. We expect this phase to start sometime in late 2018.

'Income watch' strategy - the key route to outperformance

Favourable near-term economic and occupier market conditions present a strong opportunity to maximise near-term returns through active asset management and selective development strategies. As we approach the next phase of the investment cycle, an 'income watch' strategy, based around an understanding of and an ability to diversify tenant exposure, will become pivotal to outperformance. This will lead to an uptick in 'core' strategies, with risk aversion and a focus on income sustainability driving investor decision-making.

Germany gains investment market share



Source: Fidelity International , Real Capital Analytics, January 2017

Fidelity forecasts*	2017	5-Year
Market level total return	7.8% ± 2%	4.2 ± 3%
Market level income return	3.8% ± 0.5%	3.8 ± 0.5%
Market level rental growth	2.5% ± 1%	1.6 ± 1.5%
Market level capital growth	4.0% ± 2%	0.4 ± 3%

* Synthetic prime all property return forecasts Western Europe (excl.UK) & expected variation from the base case scenario.

** MSCI IPD UK All Property Index return forecasts & expected variation from the base case scenario.

Source: Fidelity International Real Estate, JLL, RealFor, MSCI IPD March 2017.

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[1] Fidelity International , Real Capital Analytics, January 2017

Alternatives - Commercial Real Estate

Commercial Real Estate: UK
Outlook

A slow start to 2017, but further pricing volatility lies ahead

Political and economic uncertainty and currency fluctuations will remain the key challenges for the UK market in 2017. We have seen a significant weakening in sentiment as UK commercial real estate investment activity declined 35% year-on-year to £37.9 billion in 2016.[2] This led to several months of net outflows from the UK open-ended fund sector and an outward movement in yields, pushing the MSCI IPD UK All Property 2016 total return down to 2.6%, from 13.1% in 2015. After a slow start to 2017, and subject to Article 50 being evoked at the end of March, we expect further bursts of pricing volatility from Q2 2017 onwards. While the extent and direction will be difficult to predict until there is more clarity on the Brexit terms, the fact that Q4 2016 UK open-ended fund net inflows remained in negative territory (-£150 million[3]) may be an indicator of things to come.

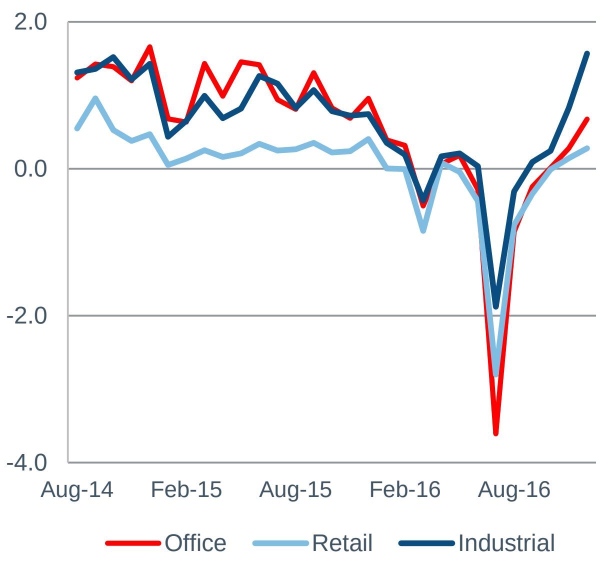
Brexit impact uneven

The UK economy, having held up well in 2016, is starting to soften, feeling the inflationary impact of weak sterling, rising import costs, a weaker job market and a potential slowdown in consumer spending. We expect the Brexit impact to be uneven, affecting some segments of the economy more than others and having a similarly mixed impact on occupational markets and real estate sectors. This will exaggerate the divergence in sector performance that emerged quite strongly last year. With the 2016 total return of 6.9%,[4] the industrial and logistics sector significantly outperformed (580 bps) offices and retail, being the only main commercial sector to report positive capital growth. Geographic differences may also become more pronounced.

Weight of money: a waiting game

As an income-generating investment class underpinned by a real asset, real estate remains an attractive investment choice in the medium-term, with secondary market segments offering a significant yield premium. In a higher inflation scenario, we expect further increases in capital allocations to real assets, including real estate. Furthermore, several sources of international capital are keeping a very careful watch on the UK market in the context of a weak pound, a need for geographic diversification and the recent corrections in pricing. That said, broad market sentiment is unlikely to pick up in a measurable way until late 2017 / early 2018 at the very earliest.

Capital growth: Sector divergence



Source: MSCI IPD UK All Property Monthly Index, February 2017

Fidelity forecasts**	2017	5-Year
Market level total return	3.0% ± 3%	6.2% ± 3.5%
Market level income return	4.8% ± 0.5%	4.8% ± 0.5%
Market level rental growth	0.4% ± 0.5%	1.3% ± 1%
Market level capital growth	-1.7% ± 3%	1.4% ± 3.5%

Source: Fidelity International Real Estate, RealFor, MSCI IPD, March 2017.

** MSCI IPD UK All Property Index return forecasts & expected variation from the base case scenario

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[2] Fidelity International , Real Capital Analytics, January 2017

[3] The Investment Association, February 2017

[4] MSCI UK Monthly Index, January 2017

Alternatives: commodities

Outlook

Still positive on oil based on global inventory picture

We remain modestly positive on commodities. The recent acceleration in global growth supports economically sensitive assets like industrial commodities and oil in particular. Despite the recent fall in the oil price below $50 a barrel, we retain a constructive view on the energy market.

While there has been concern this year on the build-up in US inventories, we believe that the picture is more nuanced. Part of the rise in US inventories is consistent with the typical seasonal pattern, as many refineries undergo maintenance at this time of the year. Additionally, there is evidence of a pull forward of demand before the OPEC cuts take effect. Overall, the rate of build in US inventories continues to slow, with the trend actually improving, as shown below.

Fundamentally, this is down to a broader rebalancing in the global oil market, as excess supply continues to be shut down. This is better reflected in the global data, with world oil inventories actually falling as shown in the second chart. As we head into the more oil-intensive driving season in the US, we would expect to start to see this impact US inventory numbers.

As well as focusing on US rather than global inventories, many commentators also tend to focus on US rather than global oil production. This has partly been driven by the emergence of shale drilling, with US oil production having risen by more than 40% in the past five years. Globally, however, US shale oil production remains a relatively small force, accounting for only 5% of global production. What happens with OPEC production is a more significant issue, particularly as we look to assess how the proposed production cuts are working over the next quarter.

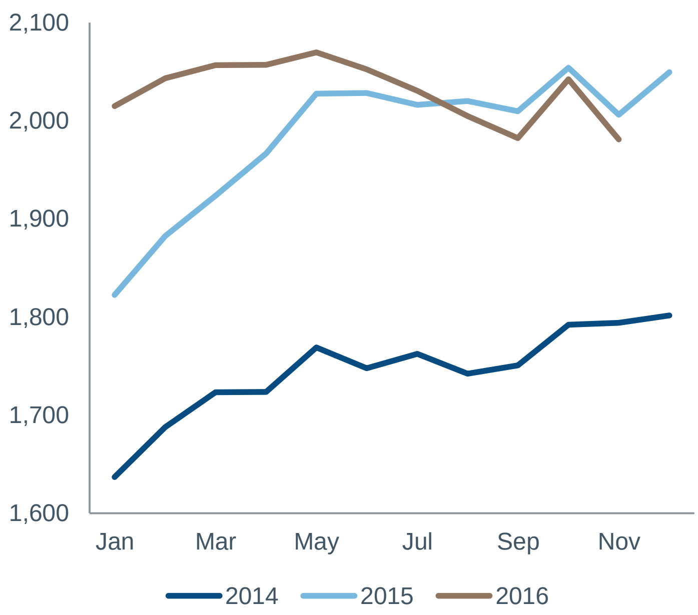
Global growth and supply interruptions supporting copper prices

We are also positive on the outlook for industrial metal prices. While there are potentially risks around the level of Chinese metal demand, stronger global growth supports the outlook over the short-to-medium term. In copper, there is the ongoing potential for industrial action to disrupt supply. Production rates at two of the world's largest copper mines - BHP Billiton's Escondida mine in Chile and Freeport McMoRan's Grasberg mine in Indonesia - have been hit by damaging strikes in recent months. The strike at Escondida has lasted for over 30 days. Given that the mine accounts for around 5% of global copper production, the strike has had a material impact on supply. Most significantly, 80% of net mined output growth in 2017 is expected to come from just four mines (Escondida and Grasberg included), leaving the copper market highly vulnerable to slipping into deficit in the event of any further extended production outages.

US oil inventory build is slowing…

Source: Fidelity International, IEA, EIA, JODI, Bloomberg. Feb 2017.

While global oil inventories are now falling…



Source: TR DataStream, as at February 2017.

Alternatives: infrastructure and loans

Outlook

Inflation and Trump should see infrastructure interest intensify

The structural popularity of infrastructure remains undimmed. Low yields and a resurgence in inflation have underlined the benefits of infrastructure to investors, while a relatively scarce supply of projects is amplifying the effect of strong demand. The result is that prices remain high, with a recent survey finding 53% of fund managers believe infrastructure valuations would be their biggest challenge over 2017. This has driven many of the managers we monitor to diversify their exposure away from the mature UK market or move higher up the risk spectrum into economic infrastructure, where assets are relatively better priced. Asian infrastructure is also an area of significant growth, though many vehicles are structured for growth rather than income. For US investors, the focus remains on the potential Trump effect. While promises of $1 trillion in spending have created greater coverage of infrastructure, the benefits are unlikely to be felt for another two to three years. For now, the best way to play increased spending may be through infrastructure groups (building the projects) rather than the listed vehicles that will run the concessions.

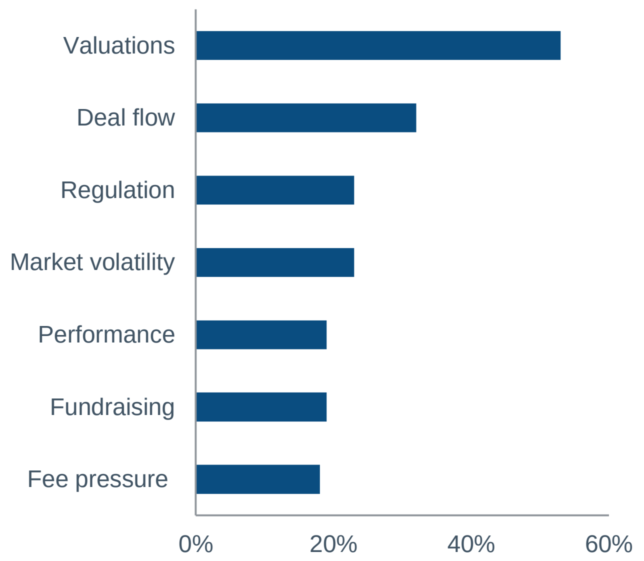
One of the most active infrastructure areas has been renewables, although the high volume of activity is offset by the low monetary value of many deals. While there is strong potential for increased spending to meet climate change targets, much of this could be small scale and unappealing to institutional investors. Where scale can be achieved, however, the depreciation in sterling and higher energy prices have helped to support the price of trust and listed infrastructure vehicles. Should the uptick in inflation continue, we expect investors' interest in infrastructure to intensify.

Loans remain attractive

Loans continue to offer attractive opportunities for investors, particularly in an environment where there are upside risks to inflation and central banks are beginning to tighten policy. Loans also offer a strong relative value argument at this stage in the cycle. While loans are higher up in the capitalisation structure, current spreads are attractive compared to high yield bond spreads. High yield bonds typically have higher capital upside, as they have better call protection versus loans but with the credit cycle relatively mature, loans can offer a steady income profile with better downside protection.

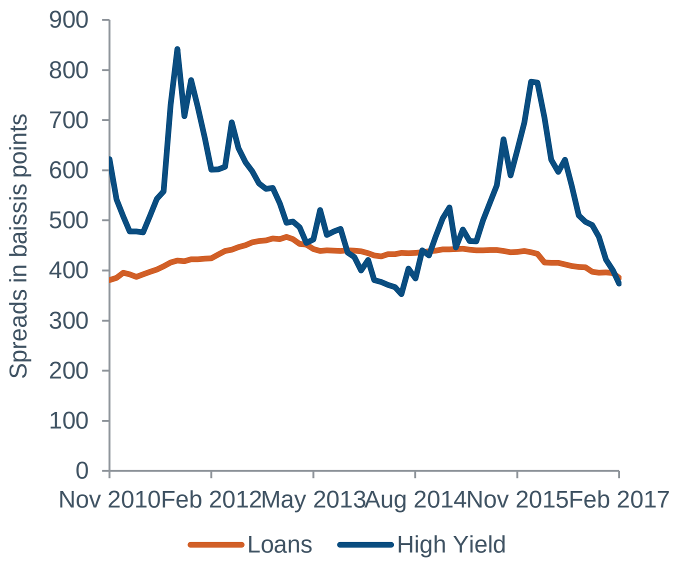
Loans are one of the few asset classes to offer an income roughly in line with pre-financial crisis levels. LIBOR, the benchmark on which yields are based, may have fallen, but spreads have risen. This is partly a reflection of banks being less willing to hold loans on their own balance sheets, thus increasing the amount of issuance available to general investors.

Challenges facing infrastructure managers



Source: Preqin Fund Manager Survey, November 2016

Loans more stable than high-yield bonds



Source: Fidelity International, Thomson Reuters DataStream, March 2017.

About Fidelity

Fidelity International offers world class investment solutions and retirement expertise. We are a privately owned, independent company, with the commitment and resources to provide the investment expertise, technology and service innovation needed to help our clients achieve their financial goals.

We invest USD $279 billion globally on behalf of clients in Asia Pacific, Europe, the Middle East, and South America.* Our clients range from pension funds, central banks, sovereign wealth funds, large corporates, financial institutions, insurers and wealth managers, to private individuals. For institutional clients, we offer tailored investment solutions design and full-service asset management outsourcing.

In addition to asset management, we provide investment administration and guidance services for workplace benefit schemes, advisers and individuals in several countries, with USD $83 billion in assets under administration.*

Established in 1969 as the international arm of Fidelity Investments, founded in Boston in 1946, Fidelity International became independent of the US organisation in 1980, and is today owned mainly by management and members of the original founding family.

*All data as at 31 Dec.16

Important Information

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