### Key themes and their investment implications for Q3 2022

# Asset **Allocation**

#### **Equities**

## Fixed income

#### **Private** markets

#### Real estate

#### Hard or crash landing

- · Defensively positioned, underweight equities and credit. Hawkish CBs and stubbornly high inflation suggests further volatility is probable.
- Preference for government bonds vs credit in anticipation of focus shifting to growth downturn and to offset credit UW.
- Overweight USD on rate differentials and safe-haven characteristics. OW euro vs sterling also on rate differentials.
- Equity volatility likely to stay high at least until inflation begins to moderate and CBs dial down the hawkishness, Selected opportunities for stock pickers amonast oversold names.
- Rising real yields have led to rotation to value from growth. Investors may benefit from value exposure, especially if inflation remains elevated. Value continues to be relatively cheap
- Growing risk of a hard landing not yet fully priced into fixed income markets. We believe that capital preservation in Q3 will be essential. Further CB tightening could move spreads wider.
- We believe that CBs are unlikely to tighten as much as market currently expects -providing opportunities in US and EU core government bonds.
- · Prefer IG over HY. We consider that Euro IG is attractively valued and has repriced too far.
- from company transportation networks, supply chains and inventory build, are likely to become fully visible in earnings over the next 12-18 months. Could see an abrupt slowdown, but severity is hard to gauge.

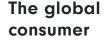
A number of pressures, ranging

- Expect risks at the lowest end of the ratings scale (CCC) to increase; however, default rates should remain below previous
- There tends to be a long lag between changes in interest rates and real estate values.
- Low transaction volumes this year reflect a nervous investment market. There appears to be a 'sellers' strike' underway, as buyers digest a rapidly rising cost of debt.
- Index-linked leases that are more prominent in Continental Europe offer some inflation protection. These will drive rents and support values to some degree as yields shift outwards

### China recovery

- Constructive view on China equities, given improving fundamentals and attractive valuation and technical factors.
- Preference for EM equities vs Europe, where we believe recession remains likely. China's emergence from lockdown supportive of EM.
- Positive long-term case for Chinese equities as valuations are around historical lows.
- Some caution in the short term as much depends on Covid developments and level of stimulus.
- Japan equities could provide a DM diversification option with relatively high exposure to China's recovery. Exporters are attractive after a sharp fall in
- On a real yield basis, China more attractive relative to other markets; Neutral on CGBs short term but CGB yields could rise in 2023 on more fiscal support and limited monetary easing.
- · Asian HY could be attractive for risk takers but it will continue to be a bumpy road.

- Consumer squeeze will challenge growth supporting underweight to risk assets.
- · Cost of living challenges and the rising cost of capital are major headwinds; the US consumer is showing cracks, which we are monitoring.
- We are focused on companies that offer margin protection, given inflationary pressures.
- Balance sheets are still healthy and credit card spend remains strong, but US consumers are starting to feel the pressure, with savings rates declining and real wages turning negative.
- Expectation is for a sudden deterioration in labour markets, putting additional pressure on consumer spending. Credit markets still underprice this risk, especially in US high yield.
- Not yet clear where the consumer's breaking point will be. Historical assumptions on companies' cost pass through ability may not hold given double digit inflation. Borrowers may need to find alternative levers to
- · Evidence of food retail consumers trading down.
- In the near term, strong pent-up demand for some Covid impacted
- Weak consumer spending is likely to dampen demand for high street and shopping centre retail space, limiting rental growth from recently re-based rents.
- There is increased risk of a slowdown in logistics demand as a result of an overall reduction in sales volumes and a return to multi-channel sales





#### Important Information

This document is issued by FIL Responsible Entity (Australia) Limited ABN 33 148 059 009, AFSL No. 409340 ("Fidelity Australia"). Fidelity Australia is a member of the FIL Limited group of companies commonly known as Fidelity International.

Prior to making an investment decision, retail investors should seek advice from their financial adviser. This document has been prepared without taking into account your objectives, financial situation or needs. You should consider these matters before acting on the information. This document has not been specifically produced for an Australian audience and may include general commentary on global market activity, sector trends or other broad-based economic or political conditions that should not be taken as investment advice. Information stated herein about specific securities is subject to change. While the information contained in this document has been prepared with reasonable care, no responsibility or liability is accepted for any errors or omissions or misstatements however caused. This document is intended as general information only. The document may not be reproduced or transmitted without prior written permission of Fidelity Australia. The issuer of Fidelity's managed investment schemes is FIL Responsible Entity (Australia) Limited ABN 33 148 059 009. © 2022 FIL Responsible Entity (Australia) Limited. Fidelity International and the Fidelity International logo and F symbol are trademarks of FIL Limited.

