Fidelity INTERNATIONAL

From the desk of

James Abela and Maroun Younes

Portfolio Managers, Fidelity Global Future Leaders Fund

March 2021

The perfect recipe for a strong recovery?

It's been an eventful start to the year so far in global financial markets – so much for waving goodbye to 2020. The vaccine rollout is progressing nicely in many countries around the world, and there is a sense of optimism around the level of pent-up demand at the consumer level. Governments remain committed to keeping their foot on the accelerator, global liquidity remains high and rates remain low. This all sounds like the perfect recipe for a strong recovery.

Beneath the seemingly tranquil surface, though, there are some concerns building. Over the last few weeks, we've seen the market start to express some scepticism around the ability of central bankers to keep inflation under control. To be clear, no one is calling for an immediate surge in inflation right away. However, comments by central banks about pushing out their expectations for rate rises are causing questions to be asked around whether the central banks will ultimately allow inflation to run away from them before acting. And what we've seen is a sell-off in the long end of the yield curve, which is pushing up long-term interest rates.

In our previous 'From the desk of...', we spoke about this as a key theme to watch out for in 2021, and it's begun to play out almost immediately. Long-duration growth stocks have benefited disproportionately from the low interest rate environment which has been prevalent since the Global Financial Crisis, and the sudden unwinding of this is causing major moves within various sectors and industries. Expensive defensives, healthcare, gold and loss-making early stage ventures, which not too long ago were all market darlings, now seem to have been pushed aside.

Even the fabled FAANG (Facebook, Amazon, Apple, Netflix and Alphabet/Google) stocks have seen their relentless march upwards come to a grinding halt.

In their place, the market has fallen in love with new stocks – stocks which, for the better part of the past decade, have been out of favour. Financials, miners, steel, energy and industrials are all back in vogue. Even within the technology sector, semiconductors are finally having a moment in the sun. The rotation towards value, small cap, cyclicals and non-US stocks seems to be gathering some momentum. These are reversals that have long been needed by the market for the sake of its long-term health but which have always felt so far away.

Fortunately, the journey of positioning the portfolio accordingly was something we commenced many months ago. For over six months now, we have been incrementally adding to positions in select financials, energy, semis and even steel, while maintaining a good exposure to high-quality industrials. We have funded this from some of our healthcare holdings, gold and cash. This has allowed us to navigate the turbulent last few months relatively well.

It remains to be seen whether the moves of the last few weeks peter out or continue for a while longer. A lot depends on how aggressively central banks respond to these market moves. Either way, we're very happy with the structure of the current portfolio, which gives our investors a balanced exposure to high-quality, long-term compounders as well as more cyclically exposed value stocks.

fidelity.com.au