

Global Market Outlook 2021

Navigating the new reality

Fidelity Future Leaders Fund and Fidelity Global Future Leaders Fund

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2021: The outlook for small to mid-caps

Fidelity Future Leaders Fund

Macro conditions are improving domestically, with Australia battling its way out of our first recession in almost 30 years. A number of positive indicators such as building activity, retail sales, residential real estate prices and sales volumes, not to mention traffic, all demonstrate the recovery is under way. Accommodative monetary policy with interest rates at very low levels, coupled with high financial market liquidity, government rescue packages and strong sentiment are facilitating strong equity markets.

Market leadership in Australian equities is changing. The 2020 Covid “winners” such as gold, food delivery services, low doc consumer credit, online retailing, loss making momentum technology, home improvement and Covid related healthcare may all struggle in the 2021 equity market. As economic activity improves the upgrades and multiple expansion will likely move toward more “value” sectors such as building, construction, energy and other cyclicals.

Investors should be cautious of highly valued quality or momentum with extreme evaluations as the availability of growth options will likely lead to the “scarcity premiums” for quality and momentum stocks to fading downward while the “fear discount” in cyclicals or value stocks will be replaced with a cycle of multiple expansions if earnings growth and duration is delivered. This is a really important point and one that I would like to stress as the investment world always chases or is willing to pay a premium for what is scarce and what is certain, however, what and where that is constantly changes and evolves.

Bottom up stock picking will also become very important in the recovery phase as valuations have been quite generous in various pockets of quality and momentum and moving from all-time lows in value or transition names. Remember that everything is cyclical - earnings, valuations, sentiment, returns and investors time horizons.

Fidelity Global Future Leaders Fund

Global economic conditions remain difficult in many parts of the world, with Australia’s recovery an outlier that is ahead of the recovery wave that will likely emerge in 2021. However, the reality of rapidly produced and administered vaccines coupled with returning consumer and corporate confidence is lifting sentiment strongly for 2021 and the V shaped recovery is emerging as a commonly accepted consensus. Global financial market liquidity is very high, interest rates are very low, inflation is low and government balance sheets are growing to ensure economic recovery.

During 2020 global sector leadership has come from Technology, Healthcare and Industrials. Future Leaders themes and performance were dominated by software and healthcare as the world rapidly seeks out productivity solutions in our personal and professional lives while looking to improve the quality and longevity of our lives through healthcare and biotech. This may not change that dramatically in 2021 as a structural trend.

Shifting trends in valuations and cyclical adjusted earnings expectations is likely to be a significant style focus for the global equity market. As economic activity improves the upgrades and multiple expansion will likely move toward more “value” sectors in financials, consumer, industrials and energy which have generally been negatively affected by Covid19 in 2020. November 2020 was a significant month for low price/earnings and “value” sectors which may have been a window into the rotation that will likely broaden and deepen in 2021 as the Covid recovery trades begin the upward climb in earnings and multiples.

After a number of ‘head fakes’, it will be interesting to see whether the underlying ingredients for a sustained value-led rally will fall into place. Value tends to benefit from a tailwind when inflation expectations are rising. With record amounts of fiscal and monetary stimulus being fed into the system, coupled with central banks suggesting that they will keep rates lower for longer, policy stance is supportive. This is of interest not only from a style perspective (i.e. value vs growth), but it also influences sector (cyclical vs defensives) and size behaviour (small/mid cap vs large cap).

Looking ahead

2020 delivered significant changes to market structures, product demand, market leaders, valuations, risk premia which have moved to extremes and now back toward more normalised levels as we approach the end of the calendar year. There is certainly concerns over valuation bubbles in technology and biotech, growing SPAC funds (special purpose acquisition vehicles), opportunistic small cap IPO market issuance. We continue to be vigilant towards frothy areas of the market that pose elevated risks for investors.

While our lives have been personally affected and our lifestyle shocked into dramatic change in 2020, what this will mean for 2021 is still unclear. Many social activities such as holidays and dining out are rapidly returning while other areas such as international travel and office interaction are likely to remain altered for some time.

The Future Leaders of 2021 will likely be highly adaptive, sustainable, highly intelligent, long duration businesses, striving to solve problems in a unique way for the world, despite all the challenges.

We wish you all a Merry Christmas and festive season with your loved ones after a tumultuous year of unprecedented change.

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