

Global Market Outlook 2021

Navigating the new reality

Fidelity Sustainable Water and Waste Fund

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Back to basics

Water and waste services are essential businesses throughout economic cycles and shocks. We believe, they will come out of the crisis stronger as investors realign their portfolios by gradually switching from 'stay-at-home' stocks to 'real assets'. Moreover, strong tailwinds are at play including:

- 1) stringent regulation in water quality and waste efficiency;
- 2) client needs to achieve their sustainable objectives;
- 3) fiscal policies that will boost economies via infrastructure investment.

Key points

- Re-enforced mega trend for water and waste needs.
- Cost cutting and efficiencies may offer leverage to recovery.
- Current monetary and fiscal policies will be supportive.

What is your investment outlook for equities in 2021? To what extent is this tied to virus-related developments?

We have a positive outlook for equities in 2021. We believe the political action to deal with the virus pandemic may last until spring 2021. Monetary policies will remain accommodating to absorb the economic shock, which means low interest rate for longer, mixed with mild inflation. Meanwhile, fiscal policies will come into play to support investment and reallocation of resources globally. In this environment, equities should continue to be strong relative to other asset classes and sector rotation may occur in H1 2021, as companies begin to provide new earnings guidance and outlook.

What do you think could surprise the market in 2021 (either positively or negatively)?

In early 2020, many economists expected another strong year for the global equity market. A few months later we experienced the biggest economic disruption since the global financial crisis. This time, central banks and governments went all-in to prevent a repeat of the 2008 financial crisis and a liquidity crunch, which means that many businesses have been kept afloat. Companies have been relatively resilient and flexible to protect their balance sheet. They found this unique situation to optimise their businesses. As a result, it is possible that such companies may show improved operating leverage with a gradual economic recovery in late 2021. On a tactical point of view, we may see a reversal of the sector rotation we experienced in March, from 'stay-at-home' stocks to 'real economy' stocks. This means, big momentum companies are starting to look less attractive versus recovery counterparts.

On the downside, we could experience a slower growth post-crisis, as a significant part of the economy (mainly high street businesses) has been badly impacted, which could mean a high unemployment rate and a possible adverse tax impact to finance the deficits.

What themes, sectors or regions would offer opportunities or potential risks in a post COVID-19 world?

This year again, the US and Asia appear more flexible and well positioned compared to Europe, which has been significantly hit by the crisis. Looking at earnings growth, companies' YoY comparisons will be distorted until the second quarter of 2021, as we complete a full year since the first lock down. The need to normalise earnings growth will be important and may last until 2023 for full visibility out of the crisis.

Both water and waste companies offer opportunities. In particular, we believe there is great potential in equipment goods, services and utilities, as these companies currently trade at a relative discount to the market and I would expect them to re-rate during 2021.

Within your portfolio, what areas have highest convictions and what areas are you avoiding?

We believe that waste companies continue to offer fantastic growth opportunities as they provide great price setting, high cash conversion and they are more flexible on cost containment. Balance sheets have been very strong, and they stand to benefit from infrastructure stimulus.

It is also our belief that water stocks will offer growth, but we need to be selective if some industrial or municipal customers keep investment under control in the short-term, given budgeting constraints.

And we expect new M&A opportunities and IPOs in both the water and waste sectors in 2021 – a recurring theme from 2020.

How do you expect sustainability factors to influence returns and how is this reflected in your portfolios?

The strategy seeks to provide resilient growth, high cash-flow stability and a well-defined sustainable objective. During the COVID crisis, water and waste companies continued to perform well because they are essential services. There is no economy without water and no sustainable economy without waste management. We see 3 very strong tailwinds:

- 1) stricter regulation for water and waste issues that need to be addressed globally;
- 2) acceleration of all companies in the world to be more efficient to tackle UN sustainable targets: Water and Waste companies are in demand to help traditional businesses reach their goals;
- 3) monetary and fiscal policies will be accommodating for the foreseeable future. Any infrastructure and sustainable policies are a boost for both water and waste.

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