



Illustration by: Matt Chinworth

# Analyst Survey 2021

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This material is for investment professionals only



# Foreword

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This is the 11th annual Fidelity Analyst Survey but, like so much else over the past year, it is like no other that has gone before. I am writing this, not from a desk at the office, but from a converted bedroom at home. The commute might be easier, thanks to the Covid-19 lockdowns, but some aspects of work have been harder. Our team of 144 analysts who completed this survey would agree. They have maintained their punishing schedule of meetings with company managers via video, rather than shuttling around the world in person. It's much more efficient but they have had to work at building and sustaining the personal relationships that deliver the insights they share in this report.

Thankfully, an end is in sight. The analysts report that the coming year promises a sharp economic recovery across the globe. As long as there are no major surprises thrown at us by the virus, companies do seem to be "counting down the days" until business gets back to normal. And, as much as I like my home office, I confess I am too.

Of course, the pandemic and fast-moving political events are proof that surprises happen and we've had to adapt quickly to make sure this survey reflects the current situation. We had just finished collecting the data when the new variants of the virus emerged, followed swiftly by the run-off elections in Georgia which changed the political landscape in the US, leading to a fresh round of questions for our analysts.

Ultimately, behind the percentages are people. Our analysts have thousands of meetings a year with corporate executives and sectoral experts. They hear first-hand the hopes and concerns of decision makers, engaging and holding them to account on sustainability issues and spotting the trends that will evolve, in time, into opportunities. Their knowledge, presented in this annual snapshot, informs our asset allocation process. And we hope it will assist yours, no matter which room you are in.

Richard Edgar  
**Editor-in-chief**

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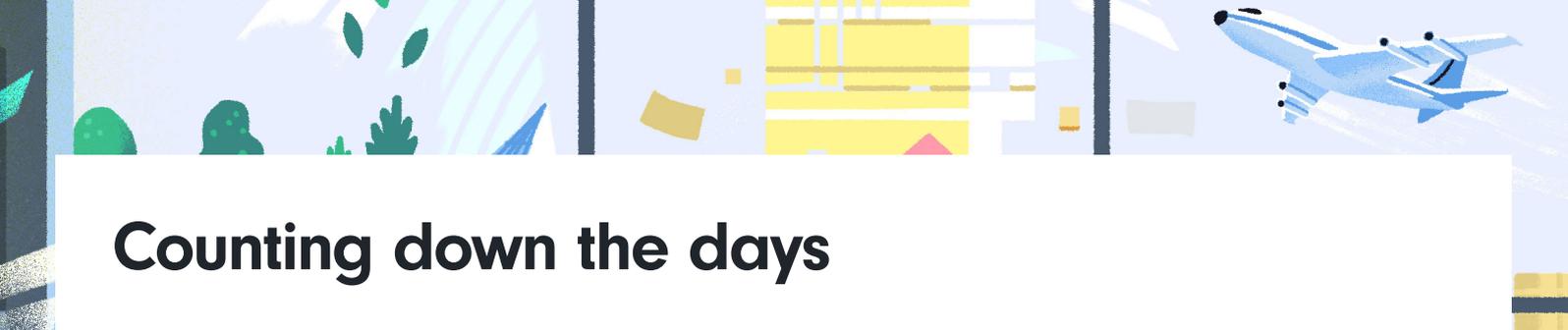
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# Counting down the days

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## Key takeaways

- Business optimism is rising, our analysts report. They expect a revival of global growth to be backed by both barrels of monetary and fiscal stimulus in 2021, assuming new Covid variants don't delay the easing of lockdowns. This will support corporate profits and bolster the case for equities.
- While the recovery will be uneven, varying by industry and region, those worst hit in 2020 should benefit most from any rebound in 2021. Capital is abundant though company leverage is set to decline.
- Finally, more companies than ever are discussing environmental, social and governance (ESG) initiatives, spurred on by regulatory and fiscal spending priorities. This should translate into a real-world reduction in CO2 emissions, with almost a quarter of companies expected to reach net zero by the end of the decade.

After months of lockdown in many parts of the world, it's not just home-bound workers counting down the days until Covid-19 restrictions are eased. Companies, countries and entire regions are poised to rebound strongly later in 2021 as pandemic measures are rolled back, according to 144 Fidelity International analysts we surveyed about coming trends.

Managers across the board are upbeat about the prospects for their companies. And they have good reason to be. Interest rates are low, real yields are negative and fiscal policy is supportive.

The survey took place in December, before the threat of new variants became clear. In light of this, we re-asked some of the key questions in early 2021. Our analysts report a short-term knock to management confidence as timelines are

moved back in some regions, but an even more optimistic corporate outlook for the year ahead. This survey offers investors some sense of the scale of that recovery.

For the first time, a majority of our analysts report that sustainability issues have become a priority for their companies globally, as industries are transformed in the race to net zero carbon emissions. The rise in concern for employee welfare observed during the pandemic will recede somewhat, although it is now permanently on the agenda.

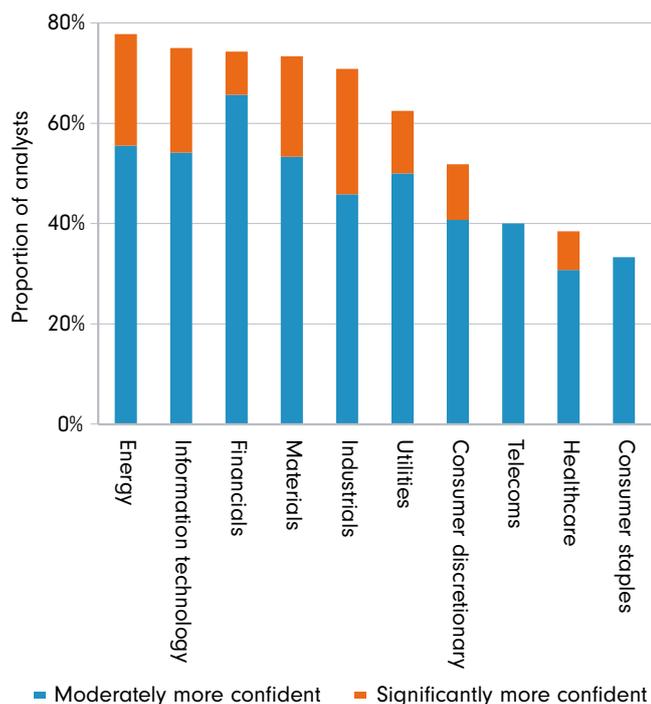
## Recovery differs across regions and sectors

Managers across the board are upbeat about the prospects for their companies. And they have good reason to be. Interest rates are low, real yields are negative and fiscal policy is supportive, signalling a favourable environment for a rebound in global growth in 2021 and beyond.

However, the pace of recovery will differ across countries and industries, depending on vaccine rollouts and the potential impact of new Covid-19 variants, creating investment opportunities and risks. China's 'first in, first out' advantage in 2020 should carry through into 2021. Europe and the US will gradually recover as vaccines are rolled out and economies reopen, with the potential for a surge in the second half.

The picture for sectors is positive, but more mixed. The CEOs of energy companies, which have been pandemic 'losers', are much more confident than they were for 2020, albeit after one of the worst ever years for the sector. Those running consumer discretionary companies (also net 'losers') are optimistic too, but to a lesser degree than those at pandemic 'winners' such as technology. Domestic sectors that suffered the most in lockdown should benefit the most from any reopening, though international sectors such as airlines may take longer to recover.

**Chart 1: Confidence for 2021 is high**



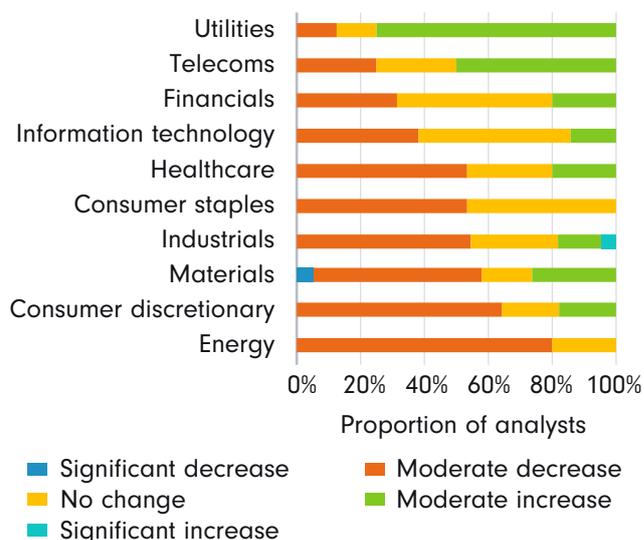
"How would you describe the confidence level of your companies' management teams to invest in their businesses over the next 12 months compared to the last 12 months?" Source: Fidelity Analyst Survey 2021.

Other findings support the overall improving trend. Our analysts report that mergers and acquisitions (M&A) are ticking up. Dividends should return after a year in which sectors such as banks and energy were compelled to cut them. Return on capital is set to rise across all regions and sectors (except telecoms and utilities), driven by higher end-demand growth and the restarting of investment that was put on hold due to the pandemic, according to the survey respondents.

Activity will be constrained, however, by a desire to reduce leverage in sectors that borrowed heavily in 2020 to survive. Overall debt is likely to decrease moderately or stay the same in 2021, according to 80 per cent of analysts. Simultaneously, default rates among listed firms are expected to drop from the elevated rates of 2020, assuming credit conditions remain favourable.

A consumer discretionary analyst puts it like this: "Management teams are more willing to invest from the subsistence level in 2021, but it's challenging given they burned so much cash in 2020."

**Chart 2: Corporate debt levels set to decrease or remain the same**



"How, if at all, do you expect overall debt levels to change at your companies over the next 12 months compared to now?" Source: Fidelity Analyst Survey 2021.

Fortunately, funding costs are expected to fall (everywhere except China), as many central banks seek to keep rates low. Raising capital shouldn't be a problem, even for sectors such as utilities and telecoms that need to fund big infrastructure projects. Equity and credit markets raised over US\$400bn in January 2021 alone, almost double the average for the month.<sup>1</sup>

## Not your usual cycle

More of our analysts report their sector is in the initial recovery phase of the economic cycle than in any other phase. However, some countries such as Japan (which is geared to cyclical upturns) are expected to have shifted towards mid-cycle expansion by the end of the year.

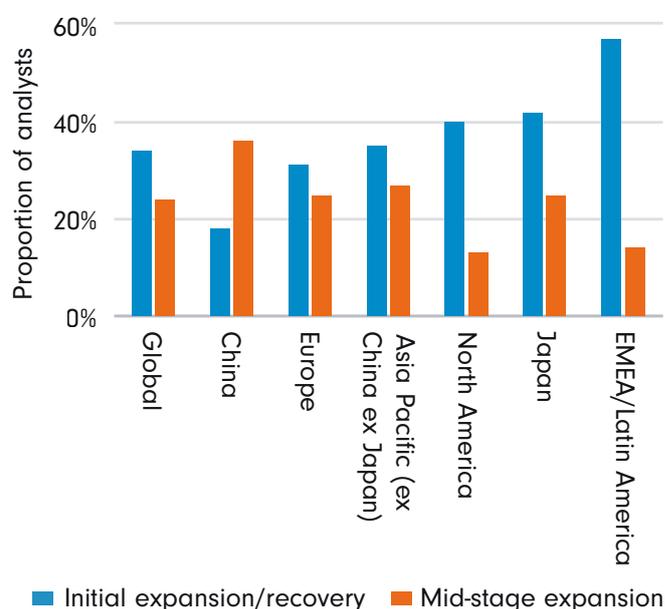
China appears to be further advanced in the economic cycle than other regions - 36 per cent of our analysts there report their companies are already in mid-cycle expansion compared to 24 per cent globally - with some analysts already expecting growth to slow towards the end of 2021 as the Chinese economy normalises fully. This may be accompanied by a retightening of credit conditions that could slow growth in China. But we expect the strong rebound in other economies would offset this at a global level.

One China consumer analyst based in Hong Kong points out that the sharp recovery last summer was driven by a lot of pent-up demand, with 30 to 40 per cent growth for some businesses, but consumer activity is still not back to 100 per cent. Sectors such as tourism and travel have been largely bypassed. The analyst says "That's not to say things aren't recovering in these areas; it will probably just take

some time. Consumption should be the main driver of growth this year, as export demand should moderate."

Such a rapid shift suggests this is not a typical cycle, in China and perhaps elsewhere. Instead, it looks more like a setback and recovery, rather than a full reset.

**Chart 3: Most areas are in the initial recovery stage of the cycle; China is an outlier**



"What stage of the cycle is your sector currently in?" Source: Fidelity Analyst Survey 2021.

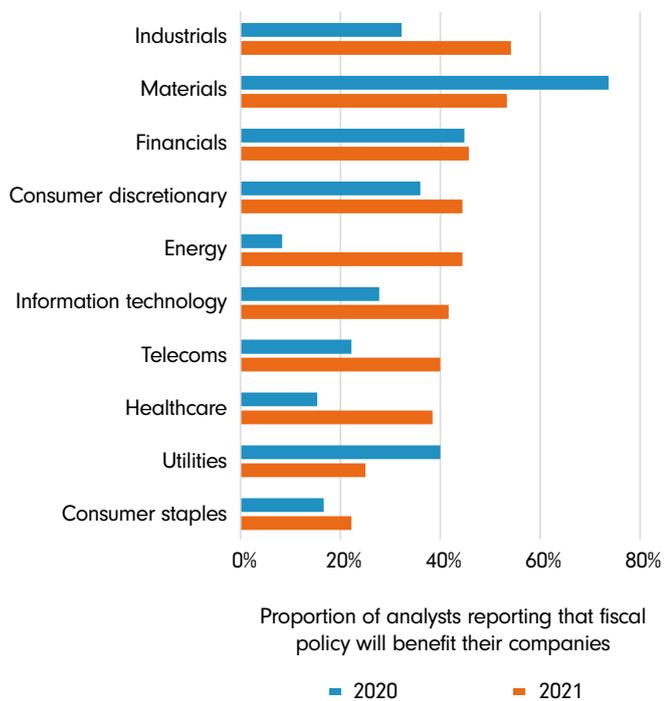
## Fiscal policy should be net positive

In some countries, the economic damage will take longer to repair. Governments have recognised the need for fiscal as well as monetary stimulus to help businesses recover. In aggregate, the majority of analysts believe that fiscal policy will have a more positive impact this year than last, most of all in Asia Pacific, according to our analysts who cover the region.<sup>2</sup>

<sup>1</sup>Source: FT.com: Companies raise US\$400bn over three weeks in blistering start to 2021 | Financial Times (ft.com)

<sup>2</sup>N.B. The survey was completed before the US\$1.9 trillion stimulus was announced in the US.

**Chart 4: Fiscal policy is likely to have a net positive impact in 2021**



"What impact do your companies expect from fiscal policy over the next 12 months compared to the last 12 months?" Source: Fidelity Analyst Survey 2021.

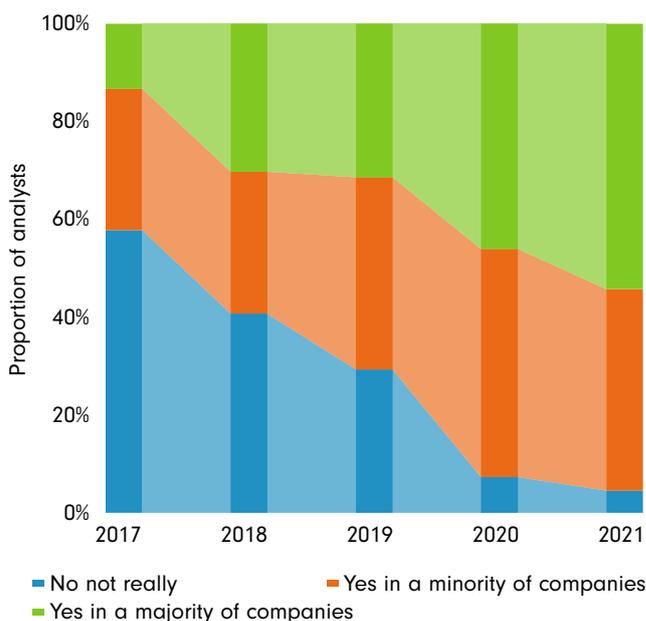
Global stimulus is expected to recede in 2021, especially in countries such as China where the pandemic is relatively controlled. But more support could be needed for specific sectors such as financials and hospitality in developed markets. One banking analyst says: "The vaccine has given some hope, but banks do expect bad loans to form as government schemes start to roll off." Governments' ability to borrow to keep schemes in place could be constrained by record debt levels, despite low interest rates.

Fiscal spending is likely to benefit sectors such as utilities and industrials most, especially in North America, while higher corporate taxes could weigh on areas such as healthcare. One industrials analyst says: "The extension of US renewable tax credits in a recent stimulus bill is an incrementally positive fiscal policy development."

## ESG emphasis rises again

This fiscal tilt towards sustainability ties in with a growing corporate emphasis on ESG, one that stretches across all sectors and regions and builds on a multi-year trend. For the first time, over half (54 per cent) of our analysts report that the majority of their companies now regularly discuss sustainability issues. This compares with 46 per cent in 2020 and just 13 per cent as recently as 2017. Moreover, a quarter of all the companies our analysts cover are likely to reach net zero emissions by the end of the decade. [For more on this topic, see 'Race is on to achieve net zero' on page 9.]

**Chart 5: ESG has come a long way in just a few years**



"Have you seen a growing emphasis among your companies to implement and communicate ESG policies in the last year?" Source: Fidelity Analyst Survey 2021.

## Rules relief for tech but not energy

New regulations on companies will increase at a slower rate in 2021 than in 2020, with the exception of those in China, according to our analysts. One

materials analyst covering China says: “Higher capex is likely to be used to meet more stringent environmental regulations around emissions.”

The energy sector appears to face the biggest regulatory risk in 2021.

Technology analysts - among the most optimistic for 2021 even after a strong 2020 - expect fewer new regulations in 2021. This is despite the social media storm around the US election and increased interest in regulating online platforms. Instead, the energy sector appears to face the biggest regulatory risk in 2021, especially in relation to curbing carbon emissions. One energy analyst says: “A legislative freight train is coming down

the track.” By contrast, after waves of regulation in recent years, financials analysts expect the pace of new rules to slow in the year ahead.

## Conclusion

A return to the daily commute still appears some way off for many, but the path to recovery is emerging. Vaccines are the way out of the pandemic, but they take time to roll out and must contend with new variants. Progress will differ between countries, with China still ahead. When economies do finally reopen, our analysts predict that activity could erupt, particularly in some of the worst hit sectors. Investors will have to pay special attention to sector and regional nuances in 2021.



Northern lights glow over Alaskan pipeline. (Credit: Getty Images / Stringer, Getty Images)

# Race is on to achieve net zero

## Key takeaways

- Europe is leading in the race to net zero, but other regions could catch up.
- Corporate focus is shifting back towards pre-pandemic priorities, with the surge of interest in employee welfare during the pandemic waning.
- Sustainability continues to climb the agenda in North America.

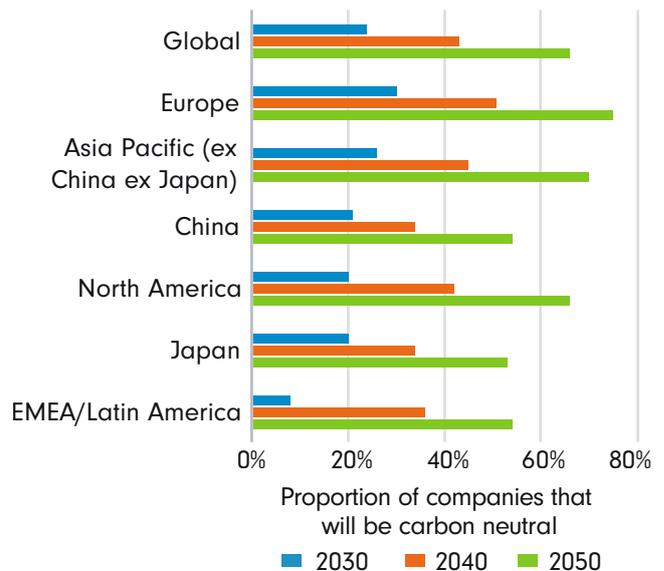
The race to net zero is on. Almost a quarter of all companies will be carbon neutral by the end of this decade, according to Fidelity International analysts.

To achieve this, companies must slash scope 1, 2 and 3 emissions. These include direct emissions from the company's own operations and energy use as well as indirect emissions up and down their value chains. Looking further out, analysts believe that 43 per cent of firms will get to net zero by 2040 and 66 per cent by 2050.

Europe once again has the highest proportion of analysts reporting growth in ESG activity at a majority of companies.

Our forecasts are based on companies' current plans, so we expect them to be revised higher in the coming years, as regulations tighten, new chief executives take the reins, and robust ESG practices become a baseline for attracting investor capital.

**Chart 6: Europe leads the race to net zero, but all areas may go faster**



"What percentage of your companies do you estimate will be carbon neutral (scope 1, 2 and 3) by: 2030, 2040 and 2050?" Source: Fidelity Analyst Survey 2021.

European companies are currently most advanced, with our analysts estimating that 30 per cent of firms will be carbon neutral by 2030. This highlights how embedded sustainability is in the region. As in last year's Analyst Survey, Europe once again has the highest proportion of analysts reporting growth in ESG activity at a majority of companies.

“I don’t have a company call anymore where ESG is not mentioned,” says one European materials analyst. “On the odd occasion I don’t ask a question about it, they will always bring it up themselves at the end of the meeting.”

## US could close sustainability gap with Europe

Other regions could eventually close the gap with Europe. New US President Joe Biden was elected on an ambitious climate platform that seeks to decarbonise US power generation by 2035.

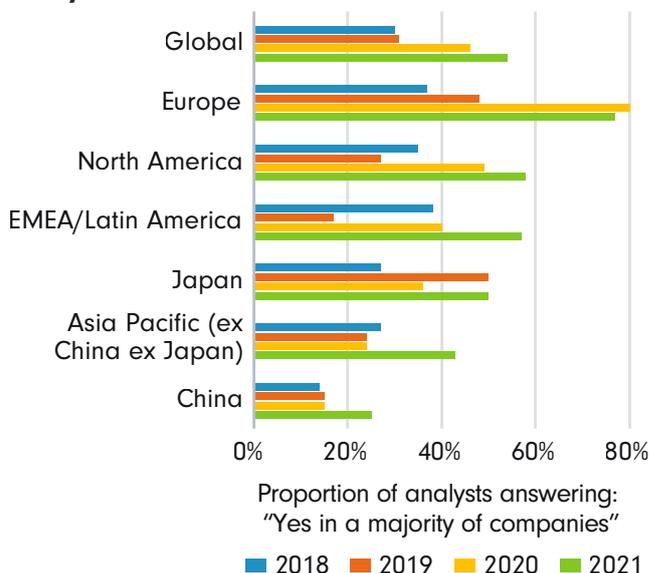
Indeed, sustainability issues continue to climb the agenda at North American companies. The proportion of analysts reporting an increased ESG focus at a majority of their companies has risen to 58 per cent, up from 49 per cent last year. President Biden’s changes will give these efforts a boost but there is still some way to go.

New US President Joe Biden was elected on an ambitious climate platform.

“ESG awareness in the US still considerably lags Europe” says one financials analyst covering North America, and “the gap has further widened in 2020.”

This may reflect a recent US rule change that discourages investment managers from considering non-financial factors, such as ESG, in decision-making. Expectations are high that this will now reverse, and sustainability considerations will form part of a manager’s fiduciary duty.

**Chart 7: Focus on ESG continues to rise everywhere**



“Have you seen a growing emphasis among your companies to implement and communicate ESG policies in the last year?” Source: Fidelity Analyst Survey 2021.

Of Fidelity analysts covering China, 25 per cent report a growing emphasis on ESG at a majority of their companies, having been stuck at around 15 per cent in the previous three years. This may be an early reflection of China’s 2060 net zero target.

There is work to do. For example, 68 per cent of our China analysts expect no increase in the level of corporate disclosure around the UN Sustainable Development Goals over the next 12 months, compared to an average of 34 per cent of analysts who cover other regions.

“ESG matters generally aren’t front of mind for my companies,” says one China industrials analyst. “Disclosure is limited and it’s only when you specifically ask that they engage on it.”

This ties in with Fidelity’s [China Stewardship report](#) from December 2020, which shows that Chinese companies do respond to ESG engagement efforts by investors, but that sustainability reporting is less mainstream than elsewhere.

## Corporate focus reverts to pre-Covid priorities

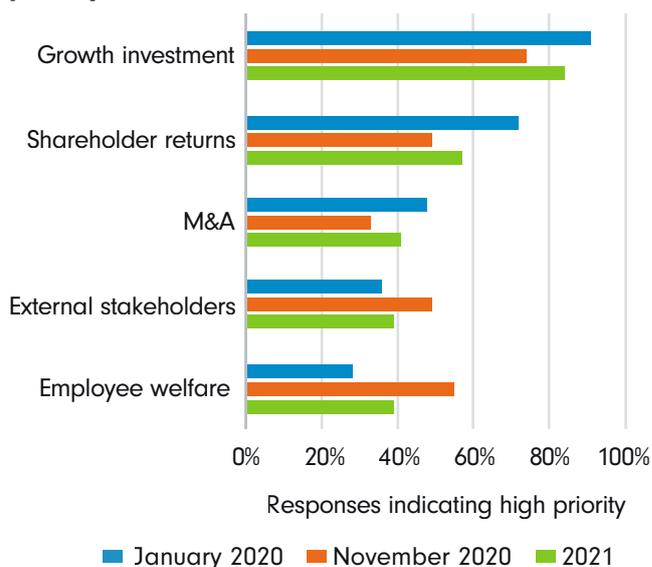
The past year has radically reshaped many things, companies included. Over that time, we have been tracking shifts in corporate priorities. In our November 2020 monthly survey, we asked our analysts to rank their companies' priorities and compare them to those of January 2020. Their responses revealed that social factors such as employee welfare and external stakeholders had become more important during the pandemic.

In the 2021 Annual Survey we asked our analysts to rank the same priorities for their companies over the coming year. The results show corporate focus in 2021 shifting back towards the pre-pandemic priorities of growth investment, shareholder returns, and M&A, while social factors are sliding down the corporate agenda.

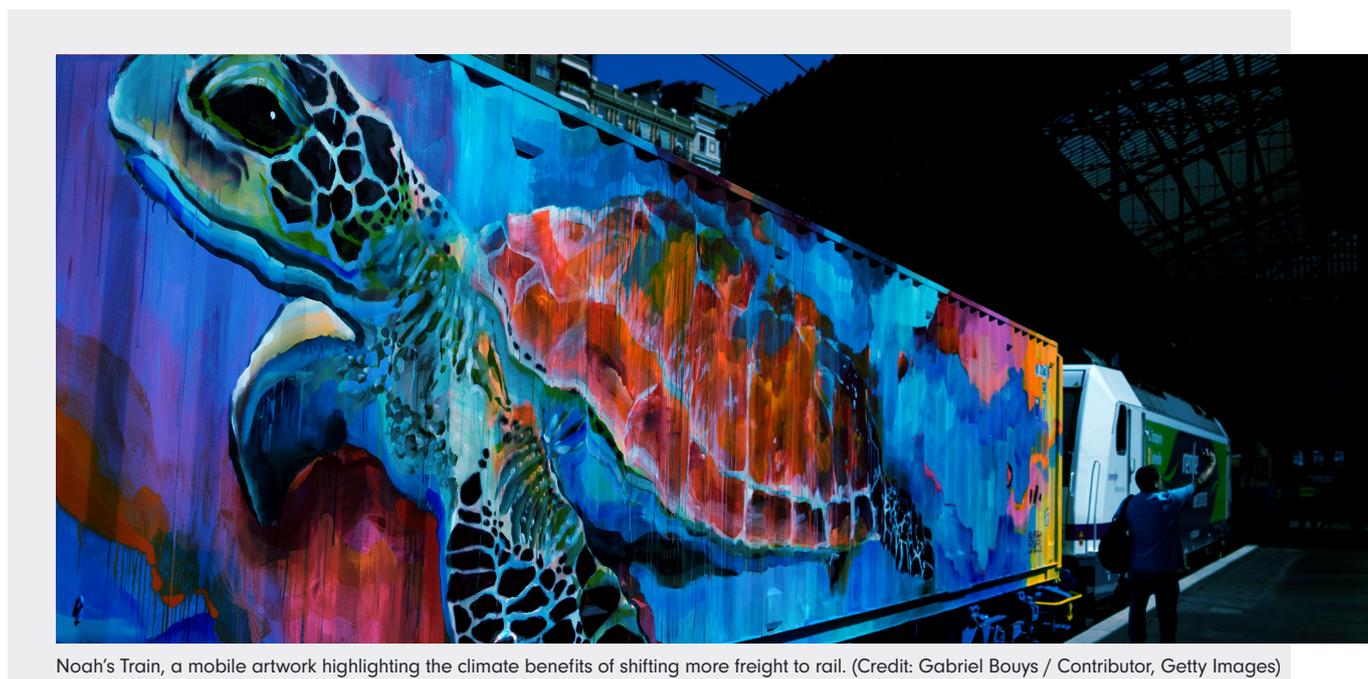
This suggests that companies' ESG strategies are strongly influenced by changes in government policy and investor behaviour, as well as the current discourse. Environmental factors are likely to take

centre stage again among ESG considerations as the Covid-19 crisis recedes, but the survey suggests social issues will continue to matter, not least as climate-driven risks start to have a bigger impact on populations and lay bare social divides.

**Chart 8: Employee welfare becomes less of a priority**



"What do you think will be the top priorities for your companies over the next 12 months?" Source: Fidelity Analyst Survey 2021.



Noah's Train, a mobile artwork highlighting the climate benefits of shifting more freight to rail. (Credit: Gabriel Bouys / Contributor, Getty Images)

# Engaging with companies matters even more after Covid-19

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## Jenn-Hui Tan

Global Head of Stewardship  
and Sustainable Investing



There is a lot to celebrate in the results of this year's Analyst Survey. And a lot to be concerned about.

Many companies are starting to take their carbon emission targets seriously, with two thirds aiming to become carbon neutral by 2050. Businesses in North America and China are becoming more focused on ESG issues, closing a long-standing sustainability gap with Europe. Our job as active investors will be to engage with our companies to ensure these commitments ripen into outcomes.

The survey shows the real-world impact of China's 2060 net zero carbon emissions target, and a change of leadership in the US under President Biden.

Regulatory change is a key driver. The survey shows the real-world impact of China's 2060 net zero carbon emissions target, and a change of leadership in the US under President Biden. Where the law goes, companies follow.

However, progress is uneven. Regulation differs across jurisdictions and doesn't always cover the full range of sustainability factors that we look at as investors. Employee welfare, a top priority at the end of last year, is now losing ground to the pre-pandemic concerns of growth investment and M&A.

And so, while some of the results are encouraging, they also show where we will have to hold companies' feet to the fire on issues of sustainability as the lockdowns ease.

# Sectors in the spotlight

2020 was an extraordinary year in which there was a big dispersion between sector winners and losers. But what will 2021 bring? Here we ask a few of our analysts about the key trends in their respective sectors in the wake of Covid-19.

## Tom Robinson

Equity Analyst, Energy (Europe)



### What really stood out for you in 2020?

Last year was pretty much the worst on record for the energy sector. European oil shares fell 30 per cent in absolute terms, while oil demand fell so low that prices dropped to their lowest level in 18 years. Earnings were down 75 per cent on average. This instilled a sense of urgency in management teams, who acted quickly to cut costs. They had learned from similar, but smaller, price moves when demand fell in 2014. This time, capital expenditure was cut by a quarter and dividends were slashed. Some took the opportunity to reset their dividend policy altogether to free up investment in cleaner energy sources. Companies also booked significant impairments in anticipation of future price risk.

### What will be the key themes in 2021?

2021 is clearly a recovery year. It will look dramatic because of the low baseline, but demand will take time to recover. Company valuations are pricing oil at US\$50-\$55 per barrel over the long term. Net debt should shrink by around 10 per cent and dividends and share buybacks will resume, but at a lower level than before. Small and mid-cap companies look better value against mid-cycle forecasts than the majors. Prices would need to reach US\$60-\$70 next year, demand to snap back and OPEC production to align with demand, for me to be bullish on the sector as a whole.

Sustainability issues in the oil industry will go global in 2021, having been Europe-centric until now. More environmental regulation and reduced investment in fossil fuels will put incremental pressure on the sector, increasing the cost of equity and, to a lesser degree, debt. Declining terminal values of companies will affect the margins of safety that investors require to invest. The EU's green taxonomy may not trigger mass selling, but investors will need to justify any lack of alignment with it.

### What is the future for energy companies?

There are several ways companies can navigate a mature industry in decline. The first is to transition towards new technologies. While there are niche restructuring stories, I'm sceptical as to how successfully oil giants can reallocate capital to activities like solar and onshore wind that have low barriers to entry and cheap financing, where they are latecomers. The second approach is to harvest the cash from current assets, by keeping costs low and distributing all your free cash flow.

European oil companies are adopting a hybrid strategy. But even if they hit their low-carbon production targets, clean energy will still only account for 5 to 10 per cent of their operating cash flow by 2025. I expect that some of the oil majors will spin off their low-carbon operations in the mid-2020s and rebrand, leaving the fossil fuel assets to run off and the clean energy ones to grow.

**Sahil Kapoor**  
Credit Analyst,  
Healthcare (North America)



### **Has the pandemic benefited healthcare?**

The healthcare sector is very broad. Of all its subsectors, pharmaceuticals have been among the most resilient over the last 12 months. For those like Pfizer, Johnson & Johnson and AstraZeneca that developed Covid-19 vaccines at speed, 2020 has been a landmark year. Their response to the pandemic improved their reputations, demonstrated the resilience of supply chains and created demand for vaccines that could persist for years to come.

There has been some negative impact. The initial lockdowns in March and April delayed clinical trials and inspections at manufacturing plants for non-Covid-19 related drugs. The number of doctor visits, regular screenings and travel-related appointments fell, which led to fewer new prescriptions and drug purchases.

Other parts of the sector suffered more. Medical technology firms that make artificial hips and knees were hurt in the second quarter of 2020 after dozens of elective procedures were postponed. Hip and knee sales fell 50 to 60 per cent. The market bounced back sharply in the second half of the year, however, after hospitals split into Covid and non-Covid zones. Elective procedures are an important source of profit for hospitals, so there was a financial incentive to bring them back quickly.

### **How will these companies fare in 2021?**

Second and third Covid-19 waves have weighed on the healthcare sector, but the impact has been much lower than in April and May 2020. Providers have developed better protocols to deal with Covid-19 risk and often monitor trials remotely.

Many companies are set to profit from longer-term trends such as aging populations, while the pandemic accelerated the move to online doctor consultations and super-charged diagnostic innovation. Firms not only developed Covid-19 tests but ramped up production very quickly, doubling revenues for some and benefitting other parts of the sector like laboratory testing companies. This trend could persist for a while, even once vaccines have been rolled out.

Demand for healthcare across developed markets will continue to rise, particularly in China. The country is approving drugs more quickly than it has in the past, which has prompted global companies to invest in its domestic healthcare businesses. Strong balance sheets should lead to more M&A in the sector, with a focus on bolt-on acquisitions of innovative drugs and therapies.

### **Has Covid-19 changed the way we view healthcare companies?**

Big pharma scored a lot of ESG brownie points in 2020. Companies were seen as serving the public good rather than just focusing on profitability. However, I don't think the virus will have a big impact on healthcare policy over the long term. Governments still need to limit the growing share of GDP spent on healthcare, so will want to drive down drug prices. This is especially true in the US, where any new regulation under the administration of President Biden could affect companies' ability to price drugs.

## Ben Li

Equity Analyst, Consumer staples and discretionary (China)



### How did companies cope with lockdowns last year?

Chinese consumer companies struggled at the beginning of last year after the government imposed rigorous neighbourhood controls and travel restrictions. All businesses (other than supermarkets) felt an impact, as shops closed and opening hours were shortened. Inventory accumulated in the first two quarters and retailers had to increase discounts and subsidise distributors to shift it.

Consumer discretionary companies were badly hit. Unsurprisingly, hotel and tourism operators were the worst affected. But many Chinese consumer staples companies are more discretionary in nature and rely on present buying, as well as beer and liquor consumption in restaurants and bars. This meant they were also hurt by lockdown measures.

The first phase of the pandemic coincided with Lunar New Year. Dairy companies usually benefit from high demand for premium liquid milk products during this period, which are a common festive gift. But last year sales were weak and inventory piled up as people stayed at home. Sales of baijiu, a Chinese spirit which people drink at banquets and large gatherings or buy as a gift, were also affected. Half of all beer consumption takes place in bars and restaurants, so brewers suffered when the hospitality industry closed.

The economy started to recover in the second quarter and the outbreak appeared to be largely under control. Consumption continued to recover throughout the year and the restaurant, travel and tourism industries rebounded, though to a lower level than before the pandemic. Some consumer discretionary companies benefited from pent-up demand during the Golden Week national holiday in October, with

some sportswear businesses seeing sales rise by 30 to 40 per cent.

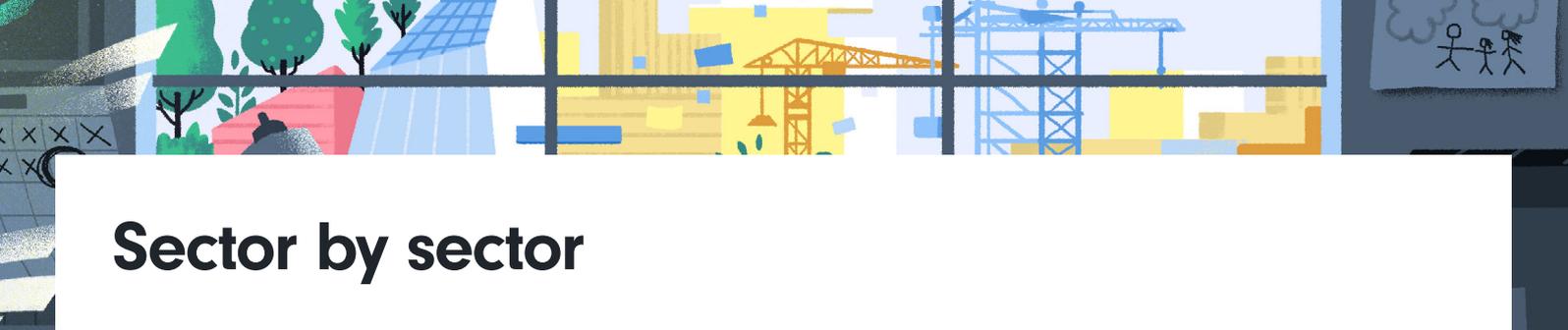
### What is your outlook for 2021?

There was a moderate resurgence in Covid-19 cases over the winter and some cities went into lockdown. This happened very close to the Lunar New Year and passenger traffic was 60 to 70 per cent lower than in 2019, as the government discouraged people from travelling to their hometowns. Some cities imposed restrictions on large banquets, which will have affected the dairy and baijiu industries.

But even though fewer people travelled, they still went out and spent money in the cities they work in. Travel restrictions could even benefit companies that operate mainly in larger cities. The resurgence was quickly brought under control and there are now almost no new cases in mainland China. Things should be better than last year when there were widespread lockdowns.

The pandemic also forced people to try things like remote education, health visits and food and grocery delivery for the first time, which has accelerated the growth of online business models. Companies now have the right technology in place and there shouldn't be as much push back from consumers.

Not all types of consumer activities are back to pre-pandemic levels, but I expect consumption to rise and drive growth in 2021. The collapse in economic activity last year means that GDP could expand by more than 15 per cent in the first quarter, although the growth rate should fall after that. The recovery is underway; it will probably just take some time for things to fully return to normal.



# Sector by sector

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## Key takeaways

- Healthy balance sheets after the pandemic pave the way for healthcare firms to focus on growth investment.
- Zero-carbon targets will push utilities companies to increase capex on renewable capacity even further.
- Regulatory pressure means sustainability issues will be front of mind for energy companies, changing the shape of the industry.

Fidelity International's 2021 Analyst Survey points to a rise in management confidence across all sectors this year. However, our analysts expect significant differences in the pace of individual sector recoveries, depending on how they fared in 2020 and their exposure to further Covid-19 restrictions.

## Healthcare

### What's changed

The healthcare sector is a broad one, covering everything from Covid-19 tests to hearing aids. Some companies have outperformed during the pandemic, while others have struggled with weak demand. Overall though, nearly 40 per cent of analysts report management teams are more optimistic about the year ahead, while not a single one reports shrinking confidence.

Almost all (93 per cent) say that growth investment is now a top priority for their companies, a return to the same level seen directly before the pandemic, while 60 per cent point to new markets and products as the main source of earnings growth, up from 46 per cent a year ago. One analyst covering Europe thinks there could be a rise in bolt-on acquisitions among diagnostics companies that have built up cash piles from selling Covid-19 tests.

Balance sheets look healthy across the sector. Many companies have already raised capital and are in a good position to fund deals. Others could use cash to pay down debt, with over half our healthcare analysts expecting debt levels at their companies to fall over the next 12 months.

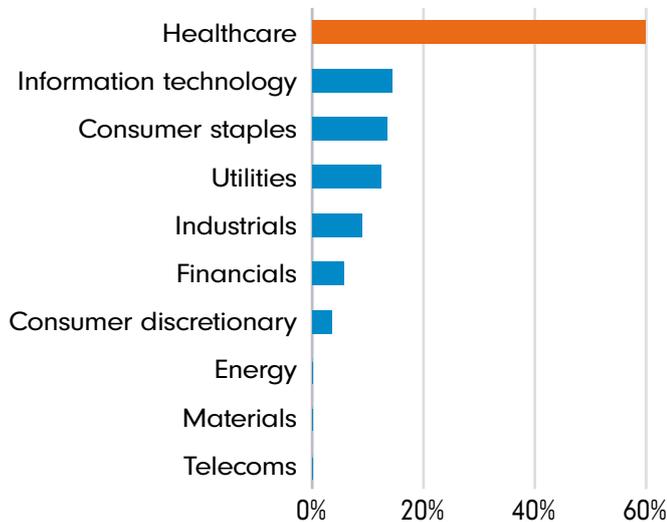
Nearly 40 per cent of analysts report management teams are more optimistic about the year ahead.

Analysts believe fiscal policy will have a mixed impact. While government stimulus has supported companies that offer Covid-19 treatment, testing and vaccines, an analyst who covers Europe argues: "The prospect of corporate tax increases in the US outweighs the positive of the likelihood of more Medicare coverage".

### Key takeaway

Healthcare companies that provide services or devices for elective procedures should start to recover as economies reopen, while diagnostics firms will continue to see strong demand.

**Chart 9: New markets and products will drive earnings growth for healthcare companies**



Proportion of analysts reporting that new markets/new products will be the main source of earnings growth

“What do the CEOs in your industry sector see as the main source of earnings growth for their companies?” Source: Fidelity Analyst Survey 2021.

## Utilities

### What’s changed

The utilities sector proved resilient in 2020. Although commercial electricity demand fell during the pandemic it stayed high for residential customers. The industry remains at the forefront of the transition to a low-carbon economy. All our analysts expect an increase in their companies’ commitment to developing sustainable products or services over the next 12 months.

The Democrats’ majorities in Congress and control of the Presidency could be “incrementally positive for clean energy policies in the US”, according to one analyst covering North America. Although President Joe Biden may struggle to achieve zero-carbon electricity by 2035, utilities companies will still need to invest in renewable energy sources and upgrading the grid. “Capex levels are likely to continue to rise at regulated electric utilities

and renewable independent power producers”, continues the analyst.

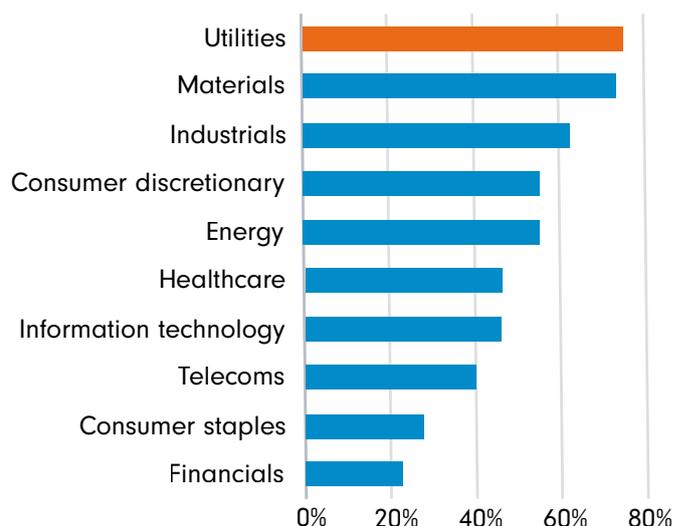
This phenomenon is not just limited to the US. One analyst says that the energy transition has created “major” opportunities for companies in EMEA and Latin America to increase capex.

While balance sheets look solid across the sector, 75 per cent of analysts expect that debt will increase as companies invest in renewable capacity. But, anecdotally, analysts believe that companies are in a good position to raise the requisite funds.

### Key takeaway

Utilities firms are expected to divert funding towards capex this year, as analysts argue that investing in renewable energy sources will help companies stay competitive.

**Chart 10: Utilities companies are increasing capex**



Proportion of analysts reporting that capex will increase

“What are your expectations for capex over the next 12 months compared to current levels?” Source: Fidelity Analyst Survey 2021.

## Energy

### What's changed

Last year was one of the worst on record for the energy sector as the oil price plunged (briefly below zero) and earnings took a severe hit. Our analysts expect a dramatic recovery in 2021 as demand picks up towards the second half of the year. More than three-quarters of our analysts report that management teams are more confident about investing in their businesses over the next 12 months, while all expect returns on capital to increase.

Companies need oil prices to bounce back, with 90 per cent of analysts saying that changes in commodity prices will drive earnings growth. But even though balance sheets are stretched, 80 per cent of analysts think debt will fall over the next year. "We are nine months into a sector crisis and companies have cut capex and operating costs significantly", reports one analyst covering Europe. While 40 per cent of analysts expect funding costs to fall, one analyst notes that fewer banks want to lend to fossil fuel companies.

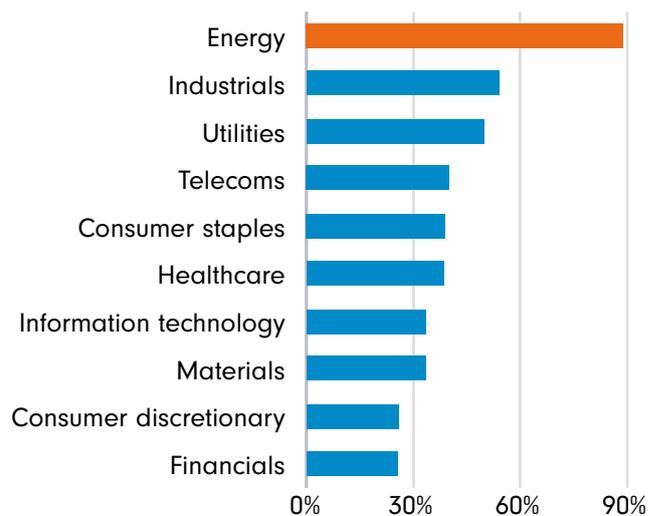
The sector faces numerous challenges and 89 per cent of analysts think regulations will increase, compared to 33 per cent last year. One analyst covering companies in Europe reports that he "expects incremental environmental regulations each year which will increase costs and reduce returns and cash flow".

Energy firms will need to change to survive. But the current pace of change is slow. While 90 per cent of analysts report a greater desire to communicate and implement ESG policies at their companies, they expect only 2 per cent of firms to be carbon neutral by 2030 (compared to a global average of 24 per cent). Don't hold your breath.

## Key takeaway

Prudent capital allocation and clear decarbonisation strategies will separate the winners from the losers in the energy sector.

### Chart 11: Energy companies are bracing for new regulations



Proportion of analysts reporting that regulations will increase

"Do you expect a change in the level of regulations that your companies must observe in the next 12 months compared to the last 12 months?" Source: Fidelity Analyst Survey 2021

## Financials

### What's changed

The outlook for the financials sector hinges on the vaccine rollout and the return of economic confidence. While 75 per cent of our financials analysts report rising confidence among management teams in 2021, there is considerable variation between the subsectors.

Insurance analysts are more positive about the year ahead, pointing to strong pricing for property and casualty insurance, greater certainty about pandemic losses and a muted impact from the European Insurance and Occupational Pensions Authority's review of Solvency II regulations (a set of uniform rules for European insurers).

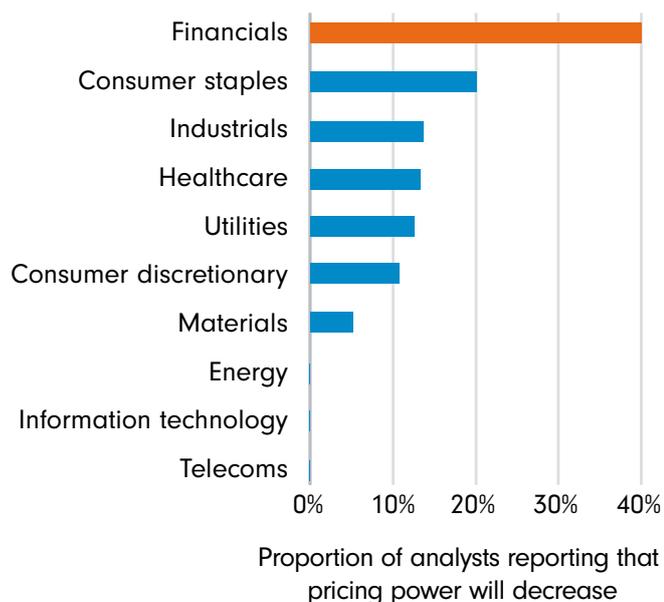
By contrast, banks remain under pressure from low interest rates. This means that 40 per cent of analysts covering financials expect pricing power to decline, compared to a global average of 15 per cent. And while loan losses have largely been prevented by government-guaranteed loan schemes, analysts worry that bad loans could start to accumulate as support is wound down.

A faster-than-expected recovery would lower the possibility of further interest rate cuts, allow firms to reinstate dividends, and reduce potential loan losses. M&A is expected to tick up, with one analyst arguing that domestic consolidation is seen “as the only remedy to low bank profitability”.

### Key takeaways

The trajectory of interest rates will determine how financial firms fare over the next 12 months, although insurance companies should perform well even in a low-rate environment.

**Chart 12: Financials struggle as pricing power remains poor**



“What are your expectations for pricing power at your companies over the next 12 months compared to the previous 12 months?” Source: Fidelity Analyst Survey 2021.

## Technology

### What’s changed

The outlook for the tech sector is relatively bright. While the Democrats’ control of Washington could mean more regulation for large US tech firms, the Covid-19 mutations mean that home working will continue for longer. “Most companies associated with home working are seeing a longer positive cycle than expected,” says one analyst covering China.

Almost half of our tech analysts think that political wrangling could have an impact on strategic investment plans.

Geopolitics are a cloud on the horizon. Almost half of our tech analysts think that political wrangling could have an impact on strategic investment plans. One analyst covering North America comments that US-China tensions could lead to “a permanent decoupling of the global tech supply chain”.

### Key takeaway

Geopolitical tensions are unlikely to go away, but fiscal stimulus and home working should continue to support tech firms.

## Telecoms

### What’s changed

Three-quarters of our telecoms analysts think that M&A will increase this year. While analysts covering other sectors expect bolt-on acquisitions to make up the majority of deals, those covering telecoms

expect to see more major strategic M&A in 2021 as a wave of consolidation continues. Balance sheets are sound, although analysts think that slightly more companies will need to raise capital than last year to fund new 5G networks.

Telecoms analysts are the most worried about geopolitics and 75 per cent think capex and M&A could be affected. Donald Trump may have left office, but Huawei's network supply still needs to be phased out, which will come at a cost to telecoms companies.

### **Key takeaway**

M&A should drive consolidation in the industry and help companies navigate higher price competition this year.

## **Consumer staples**

### **What's changed**

With many countries back in lockdown, the consumer staples sector should continue to enjoy a boost from eating at home. "The recent virus mutation and consecutive lockdowns have improved the food retail outlook", reports one analyst covering Europe.

But while analysts think that management teams are broadly more confident investing in their businesses over the next 12 months, fiscal policy is set to have a negative impact. Food retailers in Europe are expected to be exempt from further stimulus, while lower government transfers to consumers could affect spending.

### **Key takeaway**

Companies with strong brands, multi-channel operations and good customer loyalty should perform well as lockdowns are eased.

## **Consumer discretionary**

### **What's changed**

Although restrictions have tightened again in some parts of the world, more than half our consumer discretionary analysts say that management teams are more confident about investing in their businesses over the next 12 months. "Recovery expectations seem to be pushing a bit further into the future", reports one analyst covering North America. Analysts believe that pent-up demand could be unleashed later on in the year, with one pointing out that "high savings levels will continue to support consumption".

More than half our consumer discretionary analysts say that management teams are more confident about investing in their businesses over the next 12 months.

Recovering demand should increase return on capital, while funding costs are expected to fall from elevated levels. More than two-thirds of our analysts think companies will reduce leverage as EBITDA rises, cashflow improves and firms wait to resume shareholder pay outs.

### **Key takeaway**

While travel and entertainment are dependent on a quick vaccine rollout, pent-up demand should start to benefit luxury goods companies.

## **Industrials**

### **What's changed**

Industrials analysts are optimistic about the year ahead. While new lockdowns threaten demand,

the Democratic administration and control of Congress “set the stage for greater stimulus in the US and particularly anything geared to the energy revolution”, according to one capital goods analyst.

With rising metal prices and spreads, cash generation has improved significantly leading to stronger balance sheets.

But higher spending raises prices and 64 per cent of analysts think inflationary pressures on company cost bases will increase this year. This will decrease margins for some companies, as pricier fuel and raw materials hurt auto and airline earnings. Regulation will have a varied impact, with one analyst covering Europe pointing to “tighter regulations on internal combustion vehicles...and greater targets/incentives for electric vehicles”.

### Key takeaway

Most companies should benefit from higher infrastructure spending and government incentives, while a pickup in travel later in the year should improve the outlook for airlines.

## Materials

### What’s changed

Materials analysts expect that rising metal demand will push returns on capital higher this year, while leverage should fall as realised revenues increase. “With rising metal prices and spreads, cash generation has improved significantly leading to stronger balance sheets”, reports one analyst covering the Asia Pacific region. But, as with the industrials sector, rising prices will also affect costs and 89 per cent of analysts think inflationary pressures will increase for their companies.

Regulations will continue to weigh on the sector. “Tougher environmental and safety regulations will require significant investment over the next decade”, says one analyst covering EMEA and Latin America.

### Key takeaway

Demand for metals will boost the sector, while analysts argue that companies with strong decarbonisation strategies will outperform this year.



Cleaning a ladle used for transporting molten metal at a German steelworks. (Credit: Sean Gallup / Staff, Getty Images)

# Region by region

## Key takeaways

- North America analysts expect a boost from fiscal policy, tempered by higher regulations, under the Biden administration.
- European analysts are upbeat, particularly about the second half, and expect the most decreases in debt among the regions.
- China analysts see companies leading global peers in the recovery cycle, and forecast an increase in funding costs.

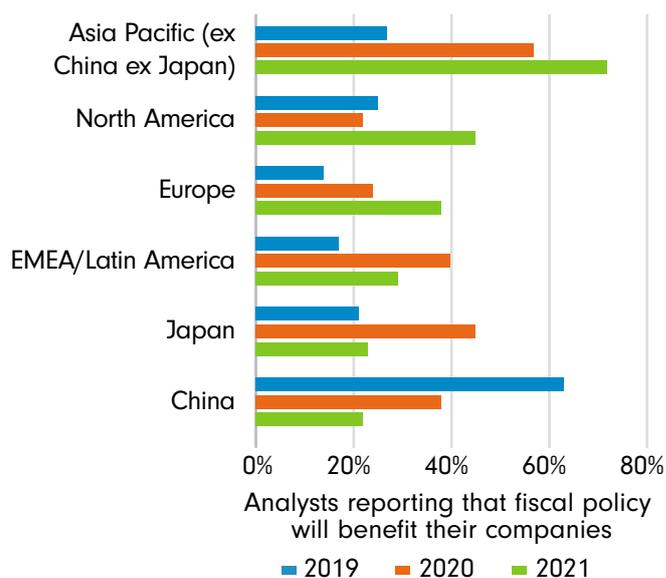
Regional differences will be crucial for investors in 2021 as vaccines are rolled out at varying paces across the globe. Here we look at what our analysts say will be the prevailing regional trends over the next 12 months.

## North America: Optimistic for a fiscal boost

Our 45 analysts covering North America highlight two key themes this year - the impact of the recent US election and business normalisation after the pandemic. The new administration under President Joe Biden and the Democrats' sweep of Congress could have wide ramifications across fiscal policy and regulations, especially those governing the environment.

Nearly half of our analysts expect fiscal policy to be a net positive for their companies this year, although the picture is nuanced because greater government spending may be followed by tax increases. Only 18 per cent of our analysts predict geopolitics will have a negative impact on investment plans this year, down from nearly 60 per cent last year. The damage from protectionist measures is also expected to subside.

**Chart 13: More North American companies set to benefit from fiscal policy in 2021**



"What impact do your companies expect from fiscal policy over the next 12 months compared to the last 12 months?" Source: Fidelity Analyst Survey 2021.

The possibility of a higher regulatory burden is another outcome of the recent US elections - just over half of analysts covering North America expect an increase in regulations, higher than the global average of 37 per cent.

Overall sentiment is positive though, with about four out of five analysts saying company managements are more confident to invest in their businesses this year than last. Nearly 60 per cent of analysts expect returns on capital to increase, with the majority of those citing higher demand as the main driver.

“Having taken a cautious approach during the pandemic, homebuilder management teams are beginning to acknowledge that they need to start spending again in order to satisfy surging demand,” one construction analyst commented.

The pandemic is also affecting the shape of the market. For example, consumers have been gravitating toward larger brands, and better-capitalised companies have continued investing, allowing them to increase market share.

“Supply contraction in the restaurant space caused by the pandemic” gives scope for upside surprises, one analyst notes. “Surviving restaurants are likely to benefit from increasing market share.”

## Europe: Low rates and stronger balance sheets

Our analysts covering Europe are upbeat about the year ahead. While the emergence of more transmissible Covid-19 variants may have delayed the return of economic activity in many sectors, causing month-on-month leading indicators and management confidence to moderate in January, the prevailing view is that the second half of the year will be much more positive. Analysts expect Covid-19 regulations to ease as governments roll out more vaccines. Confidence will return as populations become more mobile.

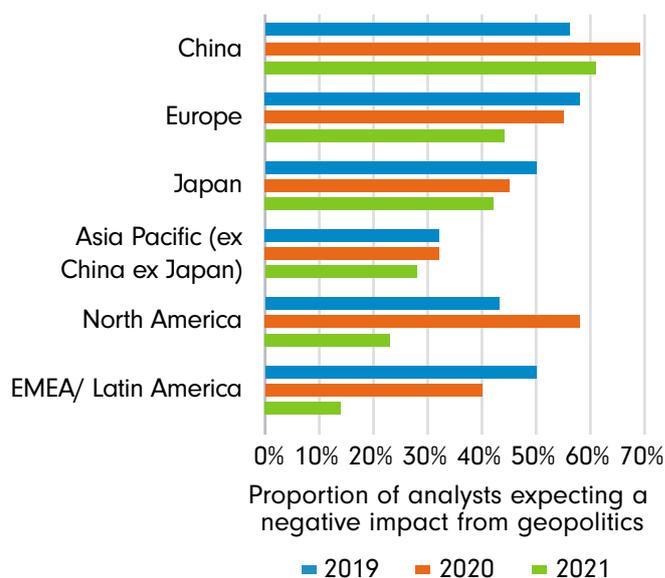
“There is scope for the recovery in demand in 2021 to exceed expectations as things get back to normal,” remarks an analyst covering

European apparel and luxury goods. “My companies have been positively surprised by the recovery in luxury demand so far and in the robustness of Chinese demand.”

Two-thirds of analysts expect a decrease in overall debt, more than any other region. Many companies took advantage of lower funding costs and policy support to over- or pre-fund in 2020. Stronger balance sheets, low rates and a brighter outlook pave the way for M&A that have been limited during the pandemic.

“There was already a divergence in the sector before the pandemic between winners and losers,” the apparel and luxury analyst continues. “The crisis has made this gap even wider, with the winners emerging stronger with solid balance sheets, which I expect they will use to increase M&A in 2021.”

**Chart 14: Geopolitics still weighing on investment in Europe**



“To what extent is the geopolitical backdrop having an impact on the strategic investment plans (capex and M&A) of the companies that you cover?” Source: Fidelity Analyst Survey 2021.

Geopolitical risk is still a hindrance to investment plans. Of our analysts covering European companies, 44 per cent expect geopolitics to have

a negative impact this year, the highest proportion of any region except China, and only slightly lower than last year despite the recent resolution of Brexit. Many European companies have a global network of buyers, and several analysts cite US-China tensions as a driver of this impact.

## China: Sentiment points to sustained lead in global recovery

Chinese executives enter 2021, the year of the Ox on China's lunar calendar, increasingly bullish about the economic outlook, including plans to boost capital expenditure and hire more workers, according to Fidelity's analyst survey.

More than half of our China analysts report management teams are more confident about the year ahead, with only 4 per cent noting confidence was lower. On a monthly basis, management optimism has further risen in January from December, bucking a global moderation of sentiment as Covid-19 variants emerged in many countries.

China analysts are more optimistic about job growth over the next 12 months than those in any other regions.

A "first in, first out" recovery from the Covid crisis is gathering steam in China, where spread of the coronavirus remains largely under control and exporters take advantage of supply-side disruptions in Western countries. While global firms appear to be in an initial phase of recovery, our analysts in China report their companies are further advanced

in the economic cycle - 36 per cent say their sectors are in the mid-stage of expansion, compared to a global average of 24 per cent. And only 18 per cent of China analysts report their sectors in an initial recovery, significantly below a 34 per cent global mean.

Meanwhile, China analysts are more optimistic about job growth over the next 12 months than those in any other regions. Our analysts expect workforces to grow by 6 per cent on average this year at Chinese companies, compared with an average of 2 per cent globally, and contractions in Europe and Japan.

**Chart 15: Hiring plans a sign of confidence in China**



"How, if at all, do you expect the typical workforce size at your companies to change from current levels over the next 12 months?" Source: Fidelity Analyst Survey 2021.

Despite the general optimism, China faces a unique challenge in the year ahead: it's the only region where analysts forecast a rise in funding costs. It's also the only region where default rates are expected to rise over the next 12 months.

As the recovery deepens, the normalisation of monetary policy, or at least the expectation of it, will loom large on the horizon. Tough measures against property speculation, including curbs on bank lending to developers and homebuyers, are adding to an increase in funding costs.

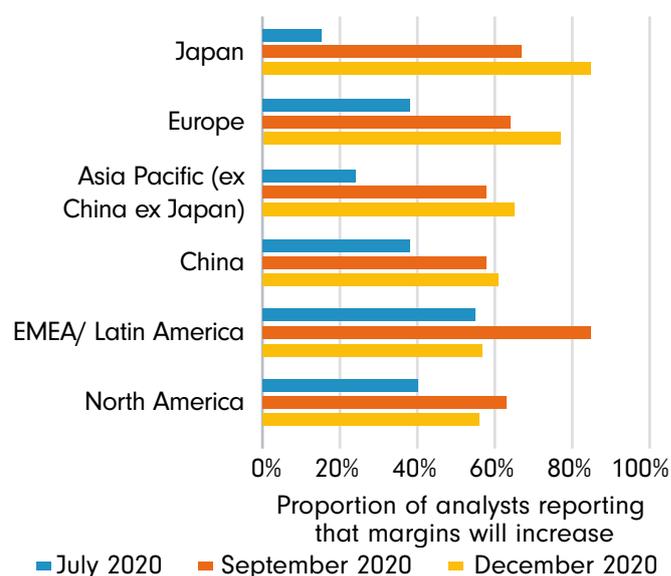
## Japan: Exporters bolstered by China recovery

Our analysts report that the management teams of Japanese companies are much more optimistic about the year ahead compared to last year's survey, citing sales growth and improving returns on capital. Like elsewhere in the world, the main factor analysts are watching is the economic recovery from the pandemic.

Just a quarter of analysts expect an increase in cost inflation at Japanese companies, compared to a global average of over 50 per cent.

Two-thirds of analysts report rising demand will be the main driver of earnings growth in Japan over the coming year, more than in any other region. The country also has the highest expectations for margin increases. This is mainly driven by companies with large exports to China, whereas those with a domestic focus will continue to struggle amidst Covid-19 lockdowns. In January 2021 the government expanded travel restrictions and restaurant curfews after a resurgence in Covid-19 cases.

**Chart 16: Export-focused companies will drive margin improvements in Japan**



"What are your expectations for EBITDA margins at your companies over the next 12 months compared to current levels?" Source: Fidelity Analyst Survey 2021.

"The scope for positive surprises depends on the speed of recovery after Covid," notes a consumer staples analyst in Tokyo. "The biggest risk factor is further lockdowns negatively impacting demand."

This uncertainty is forcing companies to be conservative about their spending plans. Many are cashflow positive and have ample cash on their balance sheets, but it's being used to pay down debt rather than expand capital expenditures. Not a single member of our team of Japan analysts expects debt to rise at their companies this year, compared to a global average of one in five.

Demographics remain a key challenge, affecting areas like hiring and inflation-targeting. Our analysts expect workforces to shrink due to lack of available labour, and many corporates have been forced to hire from outside Japan. Meanwhile just a quarter of analysts expect an increase in cost inflation at Japanese companies, compared to a global average of over 50 per cent. This reflects

the central bank's failure to reach its 2 per cent inflation target despite several years of negative interest rates.

The expected economic drag from protectionism will fall this year with US President Joe Biden's administration coming into office. An analyst who covers car manufacturers notes: "I would expect Biden's approach to be less aggressive on this front than the previous administration."

## **Asia Pacific: Coming out of the crisis stronger**

Companies in the Asia-Pacific region, excluding mainland China and Japan, are slowly but steadily moving out of the Covid-19 crisis with greater optimism, improving margins and stronger balance sheets. The region's pace of recovery, though slower than mainland China's, is faster than the rest of the emerging world.

Relatively good control of the virus in the region's economic powerhouses like Singapore, South Korea and Taiwan has helped to boost confidence. Supply disruptions in Western countries have brightened the region's short-term export outlook. A consumer discretionary analyst notes: "The economic recovery and consumer demand has been stronger than expected, especially in India, in spite of recent global lockdowns."

Nearly 70 per cent of analysts covering the Asia-Pacific region report management teams are feeling increasingly confident to invest this year, while nearly 60 per cent expect dividends to rise. Optimism has significantly improved from the first three quarters of 2020, and companies are forecast to boost capital expenditure and hire more workers over the next 12 months.

A materials analyst covering the regions adds: "With rising metal prices and spreads, cash generation has improved significantly, leading to stronger balance sheets and therefore a higher ability to invest for future growth."

As the recovery picks up, earnings margins are projected to expand in the region over the next 12 months. About 30 per cent of analysts expect that pricing power will strengthen.

Overall leverage is expected to decrease this year, with fewer companies needing to raise capital. The proportion of companies with fundraising needs has dropped to 19 per cent in 2021 - the lowest among regions except Japan - down from 34 per cent last year. "Many companies have already raised capital or have excess cashflows from Covid which can be used to reduce debt," reports a healthcare analyst.

But the region isn't immune to risks, and further Covid-19 lockdowns and ineffective vaccines leading to slowing growth are among those most commonly cited by analysts.

## **Eastern Europe, Middle East, Africa and Latin America: Recovery weak and slow**

Given the uneven impact of Covid-19 and the differing approaches to controlling it, there is understandably a good deal of variation in the prospects of the companies within a region that includes Eastern Europe, the Middle East, Africa and Latin America.

Overall, our analysts report sentiment is improving, but optimism is lower than in other regions. A financials analyst sums it up as follows: "The resurgence of Covid-19 cases has dented

management outlooks across the board.” Only 43 per cent of our analysts covering the region report management teams are feeling more confident about the year ahead than last year, compared to a global average of 62 per cent.

Weak public health infrastructure and a general lack of vaccine capabilities have hindered efforts to normalise economies in the region. When asked about the stage of recovery, 57 per cent of analysts report their sector is in the ‘initial expansion’ stage, compared with 34 per cent globally.

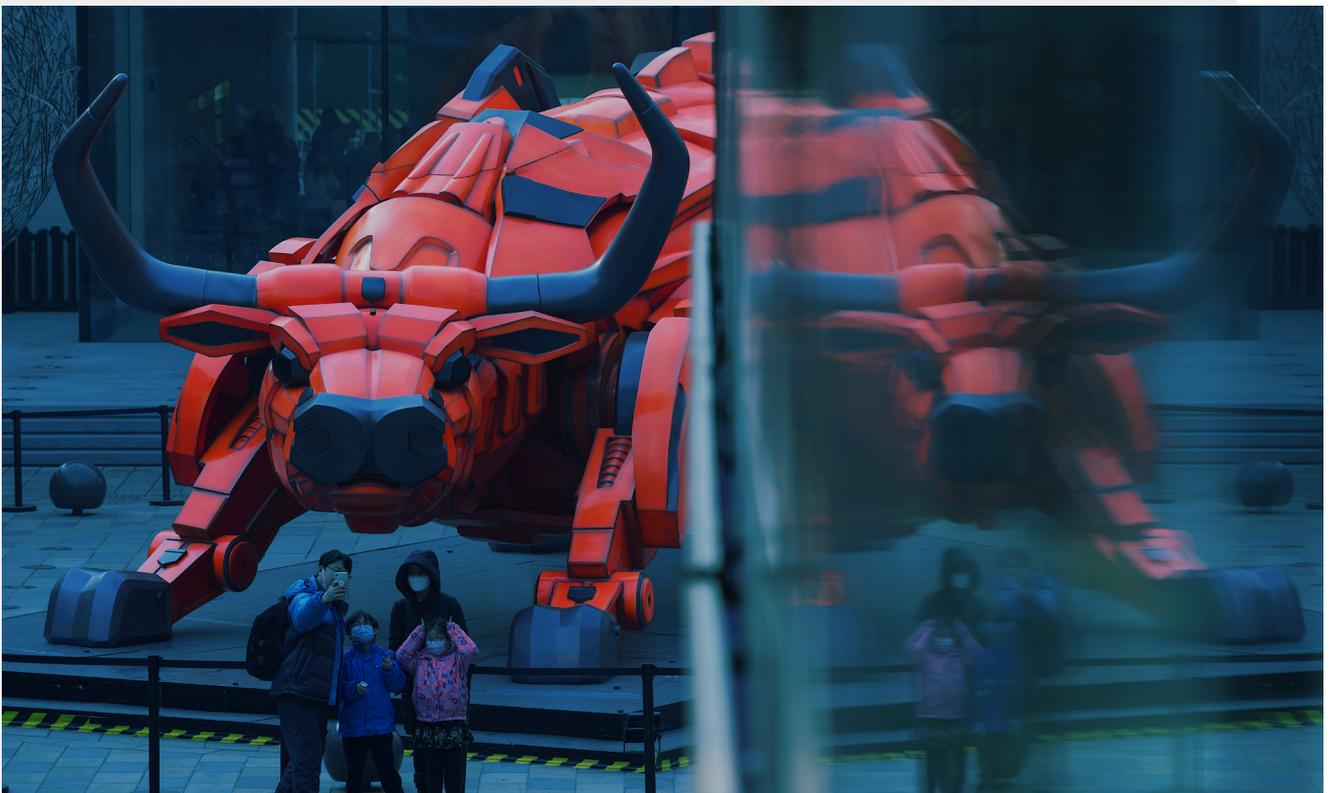
Funding costs will drop in line with the global trend, and default rates are projected to decline over the next 12 months. The utilities sector may benefit from cheaper money going after sustainable projects.

Borrowing costs “could potentially decrease further due to popularity of ESG-friendly projects”, notes one utilities analyst, while another adds:

“The energy transition has created major capital expenditure opportunities for the sector.”

Market consolidation may accelerate against the backdrop of economic weakness. About 85 per cent of analysts see mergers and acquisitions becoming more prevalent in EMEA/Latam over the next 12 months, the highest among all regions, comprising primarily of bolt-on deals rather than major strategic acquisitions.

Analysts cite public health and the general macro environment as the main risks to the outlook, while better cost management and successful post-pandemic M&A are among the reasons given for potential positive surprises.



China ushers in the Year of the Ox. (Credit: Noel Celis / Contributor, Getty Images)

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