

2012: Portfolio manager views

As we move into 2012, uncertainty abounds. Here, key portfolio managers from Fidelity offer their views on what the new year holds and reveal how investors can take advantage of the likely opportunities that will arise.

GLOBAL EQUITIES



Amit Lodha

Portfolio manager of Fidelity Funds
- Global Focus Fund, Fidelity Funds
- Global Real Assets Securities Fund

"I expect global economic growth to remain muted in 2012, with a continued and marked divergence between developed world and emerging market growth. The sovereign debt issues in the eurozone are far from resolved and the political intervention and consensus needed to stem the crisis will take time to materialise. Meanwhile, I expect the European economy to enter into recession on the back of constrained bank lending and austerity measures. The policy response from the ECB will dictate the length and depth of the recession, and its socio-economic implications.

My outlook for the US is more positive. Housing starts have begun to rise from an all-time low as ultra low interest rates are starting to incentivise buying rather than renting, and the backlog of foreclosed properties is starting to clear. Meanwhile, emerging markets continue to offer significant long-term growth potential. India, Indonesia and Thailand should benefit from inflation peaking in 2012. While a planned leadership change in China should be positive as the current government has undertaken sufficient policy tightening to create leeway for the new policymakers to settle-in.

On the corporate front, balance sheets the world over are in excellent shape. This could support capital expenditure and merger and acquisition activity. This will benefit sectors such as technology, late cycle industrials and investment banks.

During this low growth environment, my focus is on quality franchises with strong balance sheets, which do not rely on banks for funding. I look for companies that own assets where supply and demand is tight, sell products that all of us need on a daily basis, or are doing something truly innovative, which gives them pricing power."



Sudipto Banerji

Portfolio manager of Fidelity Funds
- Global Opportunities Fund

"Equities will be buffeted by macro developments relating to the combined fiscal and sovereign debt crises in Europe. This now appears to be building towards a crescendo so there is likely to be a refocus on the fiscal crisis that erupted in the US recently, especially in the run up to the US presidential elections. 2012 will also be a serious test of resilience for the emerging market growth story and its significance during the consequential economic slowdown in the developed world.

Markets 'got ahead of themselves' in the first half of 2011 with typical late cycle sectors such as energy and materials outperforming. An imminent peaking in the earnings cycle led me to position the portfolio towards stocks offering higher quality companies that offered a higher return and lower earnings volatility. This remains the core of the portfolio today. Incrementally, however, I am using market volatility to increase exposure to the high quality early-cycle names and secular growth stories. Consequently, my largest exposures are to consumer staples and technology sectors. While I am also slowly increasing emerging market investments.

The deleveraging process in the developed world is likely to lead to low levels of global growth for a number of years. I believe my portfolio is reasonably positioned for the next phase of what I sense will be a long multi-year grind back to full recovery. I'm identifying and investing in a select group of companies that have high but stable returns. I am also picking companies with capital re-investment opportunities in the areas that continue to offer growth and high quality early-cycle companies."

In Perspective

EUROPEAN EQUITIES



Anas Chakra

Portfolio manager of FAST Europe

“While investors are rightly concerned about levels of public debt in Europe, private sector and household debt levels are similarly alarming. Overall, debt levels need to be addressed. And there are three possible ways to achieve this: inflation, growth and debt restructuring. Inflation is unlikely given high level of spare capacity in the economy. Likewise, strong growth looks unachievable against a backdrop of austerity. Therefore, the only possible solution is debt restructuring, and in my view this will not just be limited to Greece or public debt.

Such an outcome will have a significant impact on financials and leveraged companies. Therefore, I remain cautious on the outlook and I am very conservatively positioned in the financials sector with a focus on names that are prudently funded and have limited exposure to the European periphery. Right now, I have a number of ‘steady compounders’ in the portfolio – quality names on attractive earnings and dividend yields with strong balance sheets and solid management. Short positions are typically in leveraged companies located in countries with a poor macro environment, or in areas where we have identified specific structural challenges – such as the medical technology segment.

The market is likely to remain volatile, driven by political news-flow. It is important to ignore short-term ‘noise’ and focus on the long-term. I invest in companies that are attractively valued on an absolute basis even when I apply very conservative assumptions. This provides some protection to the portfolio while also giving good upside potential on a longer-term view.”



Matt Siddle

Portfolio manager of Fidelity Funds - European Larger Companies

“The macro environment at the moment is extremely uncertain. While the situation in the US and China may look more like a normal mid-cycle slowdown today, the eurozone sovereign crisis raises significant uncertainty, not only within Europe, but also globally. The key problem is the level of debt and fears over the inability of Southern European countries to be able to deliver the GDP growth required to repay it.

There are five key actions that can be taken, none of which are without their problems. Firstly, governments can choose austerity and cuts; secondly, they can choose structural reforms; thirdly, the central bank can choose money printing or QE; fourthly, governments can choose to default; and finally governments can choose to leave the euro and default. European governments are hoping that the first two actions are sufficient, but we may be nearing the point where markets force further action.

The options politicians choose will be important to markets and the economy. QE would provide the most immediate stimulus to a market trading on low valuations. Structural reforms would help European companies to compete better and lead to stronger long-term returns, but this takes time to work. Default or exit for a major nation would lead to significant volatility and a very poor economic outlook globally.

In this environment, I believe investing in high quality companies that are likely to be resilient in volatile conditions is very important. For me, this does not necessarily mean investing only in ‘defensive’ or stable businesses, but also in high quality companies in more cyclical industries who can absorb the shock without permanently impairing their businesses and earnings capability. In particular, in an environment of funding stresses, it is important to own companies that have strong funding positions and are cash generative.”

In Perspective

US EQUITIES



Aris Vatis

Portfolio manager of Fidelity Funds -
American Growth Fund

“Overall, I expect the volatile environment to stay until the structural problems with the Euro and the geopolitical issues are resolved. In Europe, the political environment is much more complicated than in the US given the differences of opinion among several countries on the ways to address these issues. Given this uncertainty, Europe is now the number one risk.

In the US, the political pressure on both the Democrats and Republicans is such that we are likely to see some major fiscal reforms in the next few months; something that is not reflected in current valuations. In this uncertain environment, the US looks relatively defensive with housing starts, car sales and capital spending running well below normalised levels, all or some of which could become main drivers for the economy in 2012. Following the recent rotation towards defensive sectors, areas like industrials and technology are becoming increasingly attractive.”



Adrian Brass

Portfolio manager of Fidelity Funds -
America Fund

“My central case is that the debt situation in the Western world of consumers and governments will curtail economic growth for years to come as austerity in spending and deleveraging takes its toll. Therefore, I expect economic growth to be lower than experienced during the past decades. There are some big systemic risks in Europe. Since the outlook is anywhere in between low GDP growth down to systemic disruption, I am focussing on those businesses with the following profiles: true defensives and cyclical that are exposed to segments of the economy that never really recovered. These stocks can't have much more to fall and due to specific markets or internal drivers, should be growers even in a low growth environment. I still believe that sales and growth forecasts for US companies are too optimistic and have to come down further. With the upcoming election in 2012, I expect the volatile environment to continue as the political agenda and election uncertainty weigh on markets.”

In Perspective

EMERGING MARKET EQUITIES



Nick Price

Portfolio manager of Fidelity Funds - EMEA, Fidelity Funds - Emerging Markets Fund

“Within the region of Emerging Europe, Middle East and Africa (EMEA), we are blessed with companies that can grow regardless of the economic landscape. Without a doubt, the outlook for developed economies remains poor and the pains of the financial crisis in the eurozone are likely to be felt for some time. Consequently, we expect a degree of stock market volatility in our markets in the year ahead, but believe the long-term case for investing in the region remains as strong as ever. We are currently avoiding most Central European and Middle Eastern stocks as it will probably take some time before their overarching macro situations are resolved. Instead, we are buying into those businesses participating in the unappreciated African consumer and those miners involved in gold and silver production, as they should continue to do well.”

Global economic growth is expected to moderate in the new year as domestic activity in many countries eases and Western export markets weaken. However, emerging market valuations are attractive, especially in places like China and Russia. And while global markets may remain volatile in the near term, the growth potential for equities in the developing world significantly outweigh those offered by cash, debt and stocks in the more advanced economies. Despite the negative headwinds, we continue to find several interesting opportunities ranging from Asian smartphone component production to Russian oil and gas supply, to Nigerian beer consumption - all stories that have yet to be fully appreciated by the market. Therefore, we are positive over the long-term outlook, but remain fairly cautiously positioned until we see some sort of resolution to the current European crisis.”



Angel Ortiz

Portfolio manager of Fidelity Funds - Latin America Fund

“We are cautious about the outlook for Latin America in 2012 and are fairly defensively positioned. Investor sentiment is expected to continue to be affected as the solvency of many large global financial institutions, as well as some nations, remains in doubt. Given the slower economic backdrop, lower demand for natural resources from both Asia and the developed world is also likely to dent the returns of several commodity producers within the region. We are, however, relatively positive on the prospects for domestic consumers given next year’s wage increases and low unemployment in many countries. Furthermore, policymakers within Brazil and several other Latin America countries still have the tools to boost domestic growth through both monetary and fiscal stimulus.”

In Perspective

ASIAN EQUITIES



Anthony Bolton,
President - Investments

"The next twelve months should be a defining moment for Chinese investment when investors realise the economy is not about to collapse and the tightening period is over. We have been through an extraordinarily volatile year but I believe that when the dust settles and things calm down, investors will focus on the relative growth rates they can get in different parts of the world. This will result in money flowing out of developed markets with sovereign debt problems and weak prospects into the faster growing emerging markets, like China.

I am not saying that China is not immune to a developed market slowdown. The country's growth rate will slow down, but it will still rest at a robust 7.5% to 8% - this is very attractive compared to the rest of the world.

Inflation has been a key issue in 2011 but it has already started to come down. A slowdown in inflation has allowed the Chinese authorities to stop tightening monetary policy. This should be positive for markets. The speed and format of further loosening will depend partially on how the domestic situation develops from here, and whether the developed world returns to recession.

Some of the other issues that investors in China have been focusing on are banks' bad debts and falling residential property prices. There are some real challenges regarding potential future bad debts but the government has the financial resources to address these. The outlook for residential property in 2012 is poor. I am also more concerned about the uncertainty due to the important political changes that are due over the next 18 months and whether they will lead to a change in policy direction.

In terms of portfolio strategy going forward, I continue to be positive on the consumption and services sectors and remain underweight in exporters, commodities, infrastructure companies, banks and property companies. Consumption and services are not immune to any slowdown in China, but I believe these are the areas with the best long-term outlook where structural trends favour them. Even with a slowdown in GDP growth, I would expect these areas to outperform the general economy. If, however, I am wrong about the world outlook, and a new recession commences, then this would very likely lead to China embarking on another stimulus programme, which would be very beneficial for domestic Chinese consumption."



Martha Wang
Portfolio manager of Fidelity Funds -
China Focus Fund

"China's economic growth is expected to moderate as external demand from Europe and the US slows down and domestic economic activity falls. After tightening for the last two years, the policy environment will be more benign going forward. Recently, inflationary pressure has fallen, giving the government some room to ease monetary policy. Going forward, headline GDP growth will depend on the balance between looser monetary policies and weaker external demand.

I am positive on the outlook for the next 12 months. Indeed, there have only been a few periods in China's stock market history when valuation levels have been as attractive as they are currently. Most of the macro risks have been largely priced-in and the risk-reward outlook is very favourable. In terms of stock ideas, I favour the consumption space where I am finding many opportunities with attractive valuations."

In Perspective



Raymond Ma

Portfolio manager of Fidelity Funds -
China Consumer Fund

"The growth of the Chinese economy will be moderate in 2012, as the negative impacts from the European debt crisis and China's tightening measures filter through. However, I believe that the risk of a hard landing in China is minimal. Meanwhile, the growth of domestic consumption and infrastructure should remain resilient in light of a decent rise in income and continuing government support.

More importantly, the recent slowdown in inflation gives the Chinese government some room to spur growth by means of an easing in monetary policy. The reserve requirement ratio (RRR) for banks is expected to be further reduced in the first half of next year, improving the liquidity of the market. I believe the Chinese equity market should outperform their US and European counterparts in 2012.

Overall, Chinese corporates are expected to deliver top-line growth of around 15% in 2012. Sector-wise, consumer sectors are expected to outperform as they are driven by solid domestic demand and are less impacted by external and policy factors. While consumer staples were under huge margin pressures in 2011 on the back of soaring input costs, margins will once again expand in 2012, benefiting from falling commodities prices. Meanwhile, consumer discretionary should continue to benefit from robust income growth and the pro-consumption government policy."

FIXED INCOME



Ian Spreadbury

Portfolio manager of Fidelity Funds -
European High Yield Fund

"The fundamental issue of too much debt in developed economies will continue to hang over financial markets in 2012, keeping the level of economic uncertainty high. Growth will remain slow and we face several more years of painful de-leveraging. Damaged sovereign credit quality is feeding back into the real economy through the financial system and for bond investors it is hard to know where the safe havens are. I'm concerned that Gilts could lose their safe haven status at some point and with yields at such low levels I expect low returns at best from the asset class next year. Inflation is unlikely to be a problem in the near-term, but it makes sense to have some inflation protected bonds to hedge the medium-term tail risk. I see value in investment grade corporate bonds from companies that have pricing power, solid balance sheets and are able to survive a tough environment. The high yield market also offers some value, but dispersion will be high so good stock selection will be vital. However, the key to successfully navigating bond markets next year will be to remain flexible and well diversified."



Rick Patel

Portfolio manager of Fidelity Funds -
US Dollar Bond Fund

"Going into 2012, I believe that sovereign and political risk (both domestic and global) will remain at the forefront of investors' minds. Weak economic data, coupled with doubts over the prospects for US and global growth, will drive overall sentiment. US unemployment rates are unacceptably high and I expect downward pressure on growth from excess capacity in labour markets and industrial sectors. Whilst corporate fundamentals are still relatively strong, they are no longer improving, having come off their peak. However, with US Treasury yields at such low levels, coupled with the potential for further asset purchases by the US Federal Reserve, I expect market yields to stay low, driving investor demand for assets that offer higher levels of income; this should benefit corporate bonds.

Sovereign risk is much more important than industry or company risk. The eurozone's problems are not going to be resolved quickly and I expect further volatility from this area. I favour high quality short-dated corporate bonds and issues from companies in a deleveraging mode following a strategically sensible acquisition. I also expect the volatility to continue in 2012 and so will maintain a healthy position in liquid nominal US Treasury bonds and cash related instruments."

In Perspective



Andy Weir

Portfolio manager of Fidelity Funds -
Global Inflation-linked Bond Fund

“Economic growth in developed economies is still hampered by the debt overhang left in the wake of the financial crisis. Central banks are keeping interest rates low and maintaining a high degree of monetary support to boost economic growth and this is likely to persist in 2012. Against this backdrop, with unresolved issues in Europe, I expect the global bond market to remain extremely volatile. With highly solvent and/or liquid global sovereign bonds yielding at historically low levels, the outlook for global corporate bonds is favourable as corporate balance sheets remain relatively robust. Accommodative monetary policy also means that these bonds offer attractive valuations on selective names.

I believe the hunt for yield is likely to support investor inflows into the asset class, albeit, there is the potential for further spread widening due to sovereign volatility. Inflation poses a risk to both developed and emerging market growth due to continued elevated levels of local and global inflationary pressures. Although inflation is showing signs of cooling, there remains a tail-risk that developed market central banks continue to expand their quantitative easing programmes and reverse this ‘cooling’ period. Going forward, I would expect inflation-linked bonds to outperform in this environment.”



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