



INVESTING AT THE GLOBAL CROSSROADS

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What is risk?

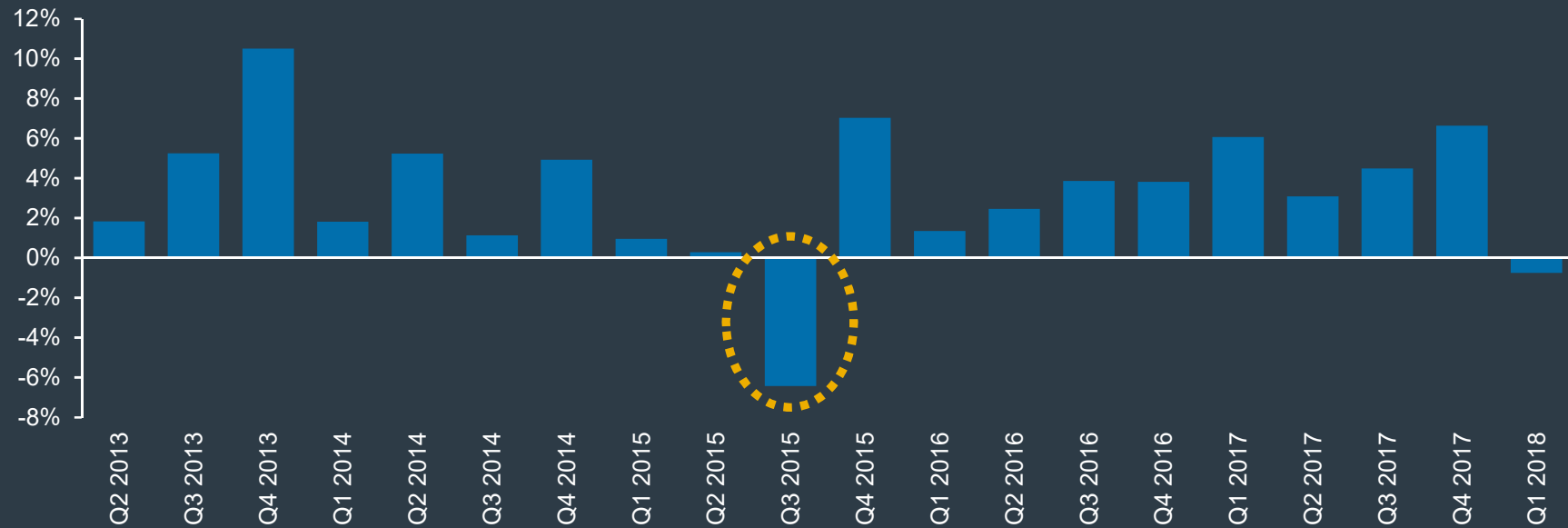


1. Risk of permanent capital loss
 2. Risk of inadequate return
 3. Risk of missing out
- ...but no return without risk

What is risk? An investor view...

Five years, one (significant) drawdown

S+P 500 quarterly USD total returns, 5 years to March 2018



Source: Bloomberg, Standard & Poor's, Fidelity International March 2018



Trying to avoid risk?

In a period of extraordinary monetary easing

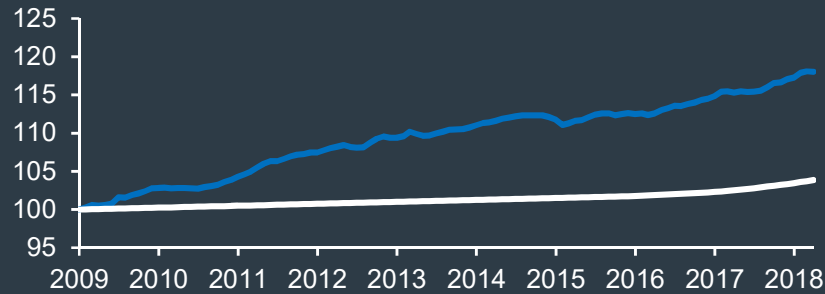


The (real) cost of low risk assets can be high

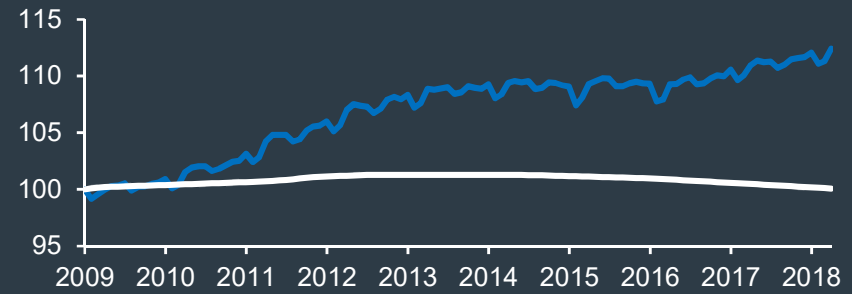


Holding cash has been an expensive option for some

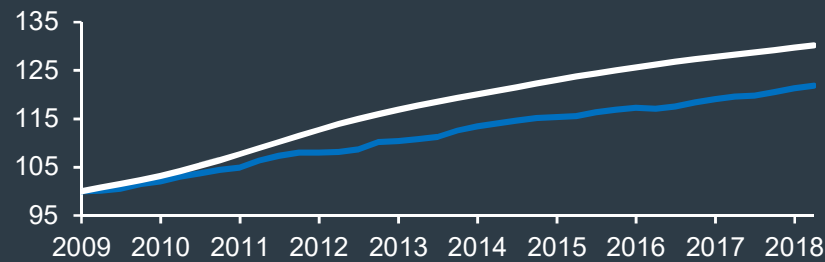
US



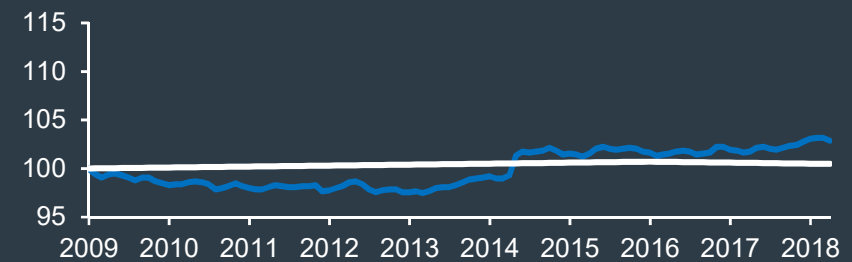
Euro area



Australia



Japan



— Price of goods

— Value of money

Source: Fidelity International, Bloomberg, April 2018



Will I be rewarded
for taking risk?

If worried
what can I do?



Late cycle, not the end of days

The very timeliest indicators point to a peak in growth...

...but given strong levels, and a lack of meaningful negative shocks in the global system, this is not (yet) the beginning of the end.

Inflation remains well-behaved so far...

...which means that central bank hikes and monetary policy expectations should not kill the economic cycle, though changes in the liquidity provision will be noted.

'Trade War' remains mostly rhetorical for the time being...

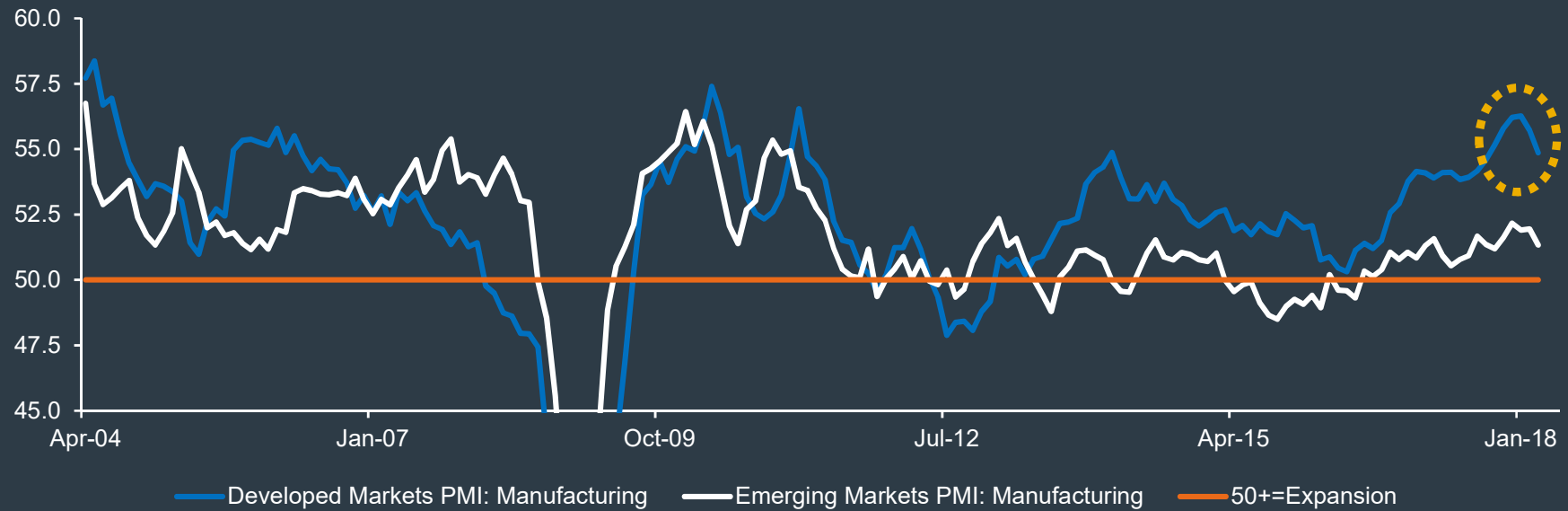
...instead, watch for China slowing, 'Quantitative Tightening' or an oil spike as catalysts for a more sustained downturn.



Has the global economic cycle peaked?

Late cycle environments are tougher, but still positive for risk

Manufacturing PMIs (March)



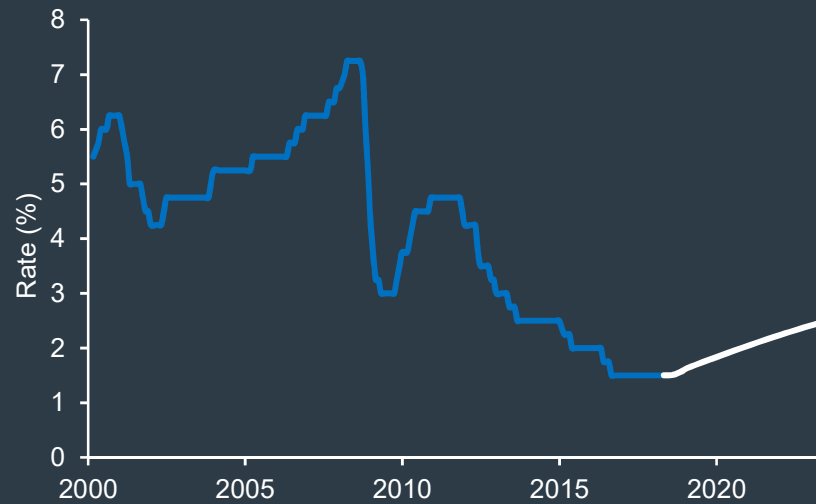
Source: IHS Markit, Haver Analytics, Fidelity International, April 2018.



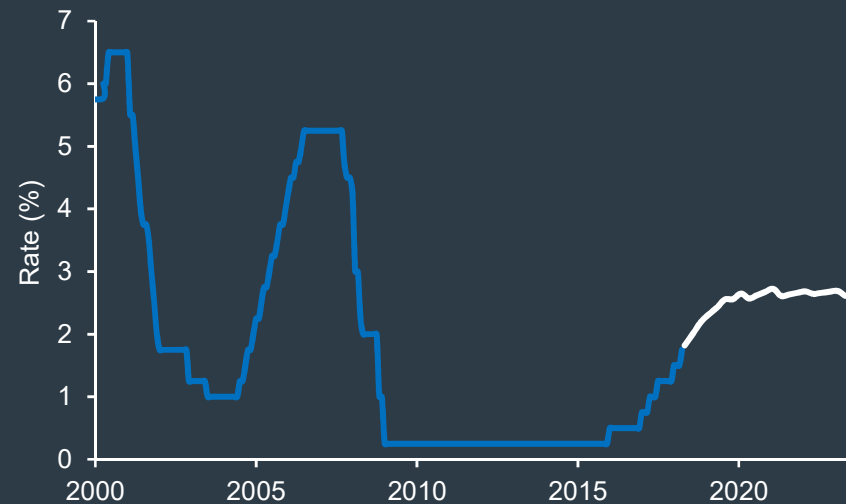
Interest rates aren't 'end of cycle'

Deposit rates and market projections

Australia



USA



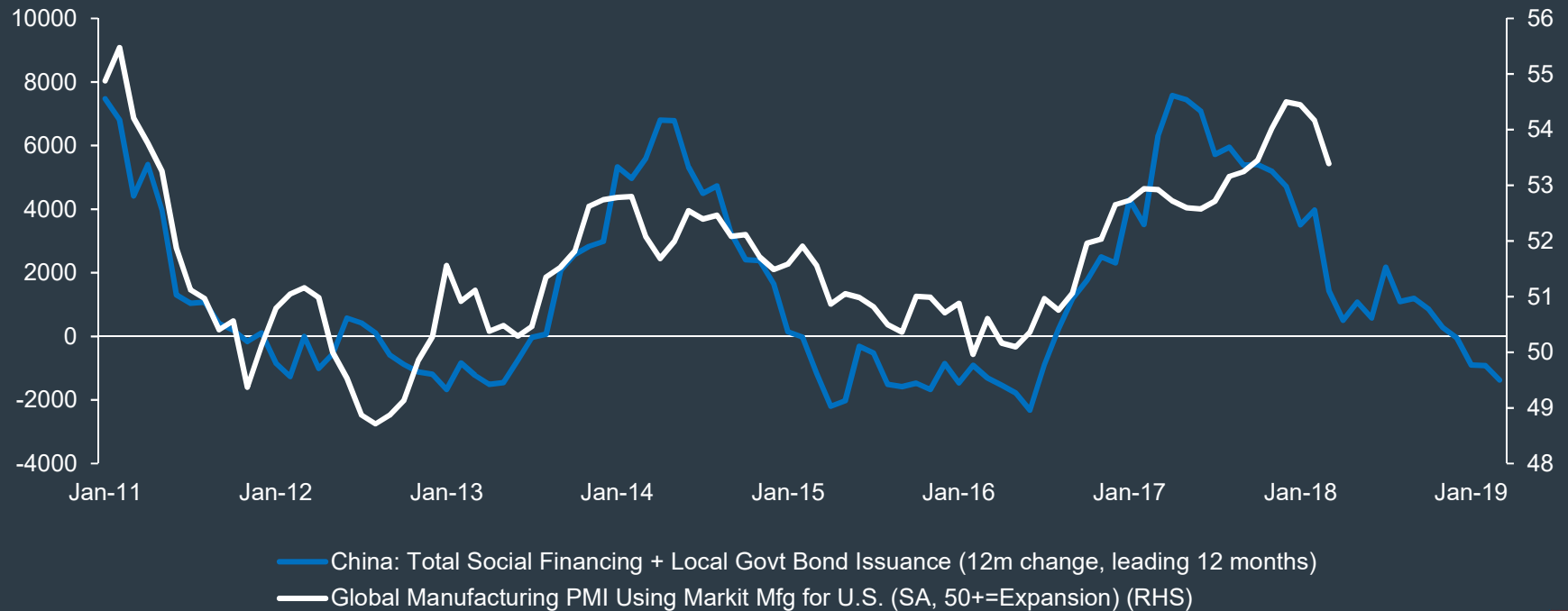
Source: Bloomberg, Fidelity International, April 2018



Tracking downside risks: China

Growth to slow on tighter financial conditions, but by how much?

China credit impulse vs global manufacturing PMI



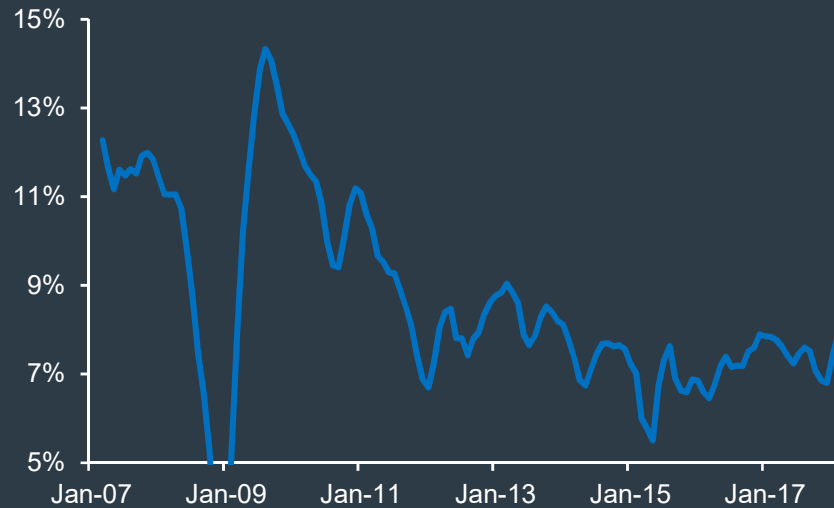
Source: PBoC, JPM/Markit; Haver Analytics. Fidelity International, April 2018.



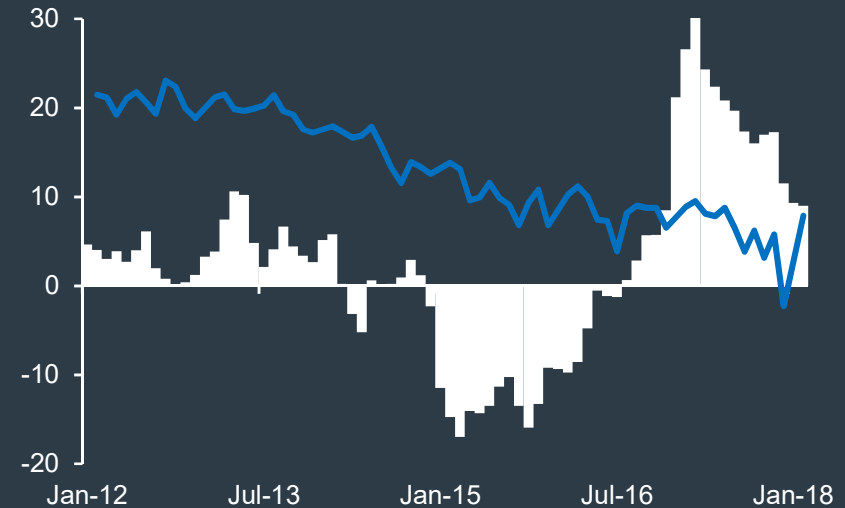
Tracking downside risks: China

Early 2018 data has confounded us with its strength

China GEAR (qoq% change annualised)



Investment and international trade



— China: Merchandise Imports (RMB, y/y%, 3mma)
— China: Investment in Fixed Assets (y/y%)

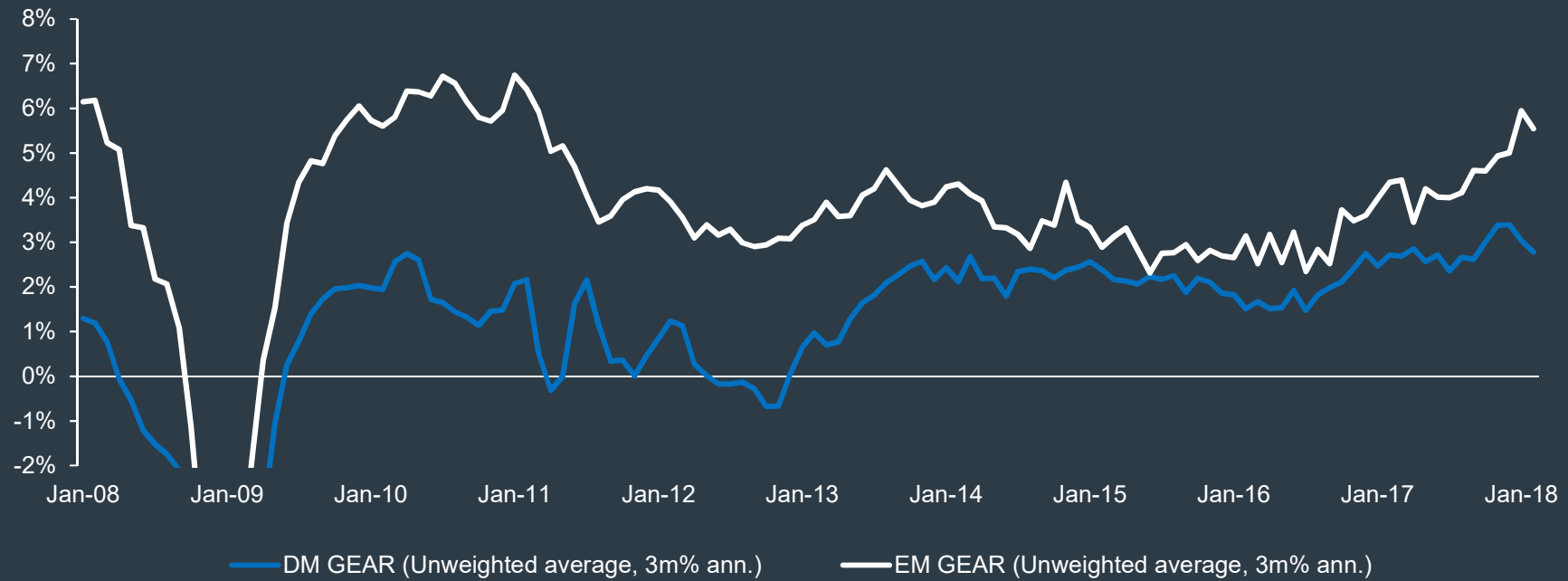
Source: Left chart: Fidelity International, April 2018. Global GEAR = 50% DM (unweighted average of 4 regions), 50% EM (unweighted average of 11 regions). Fidelity GEAR (Gauge of Economic Activity in Real Time) is a proprietary model of Fidelity Multi Asset. Right chart: IHS Markit, Haver Analytics, February 2018.



Emerging markets: young at heart

Strong growth, but dependency on China remains

Fidelity GEAR activity indices



Source: Fidelity International. April 2018. Fidelity GEAR (Gauge of Economic Activity in Real Time) is a proprietary model of Fidelity Multi Asset.



EM real yields might be a missing diversifier



Past performance is not a reliable indicator of future results.

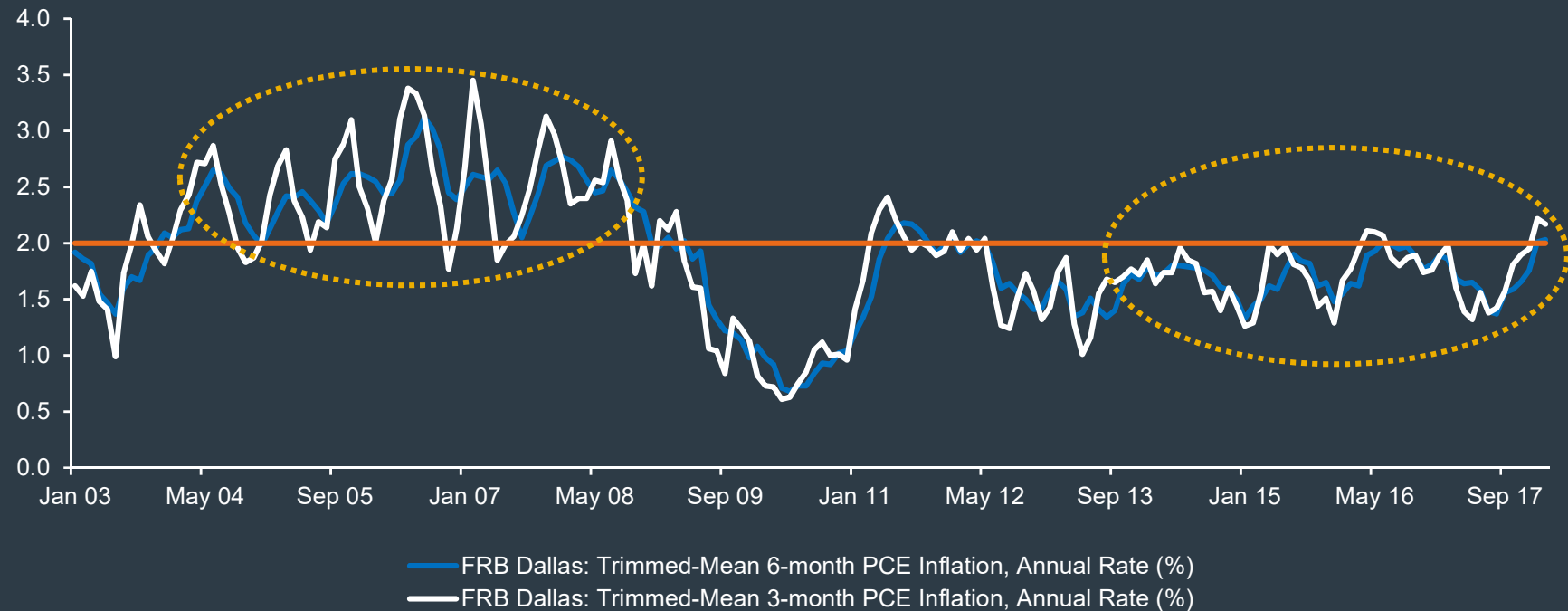
Source: Chart from a HSBC publication "EM Rates: Mind the gap" Figure 3, 1 August 2017.



DM inflation is benign and well-anchored

Central banks can stay cautious in absence of accelerating inflation

US core inflation: trending around the Fed's 'symmetric' 2% target



Source: Fidelity International, US Federal Reserve, March 2018.



US wages – scary or a welcome boost?

Wage growth is unlikely to ruin the party

Fidelity multi asset US wage model*



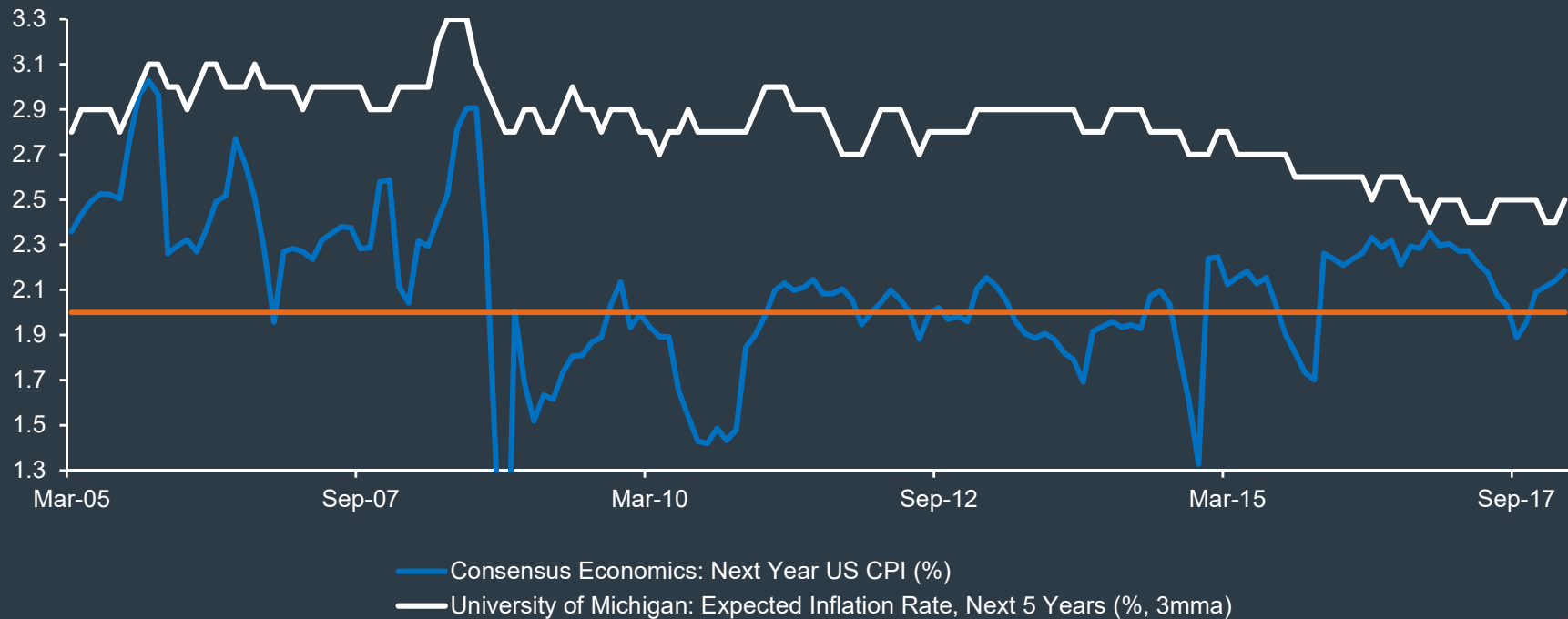
*This models US wage acceleration via changes in unemployment and effective tax rates, and the lagged impact of business confidence.
Source: Fidelity International, March 2018.



US inflation not concerning despite strong growth

Survey-based inflation expectations remain contained

Inflation expectations



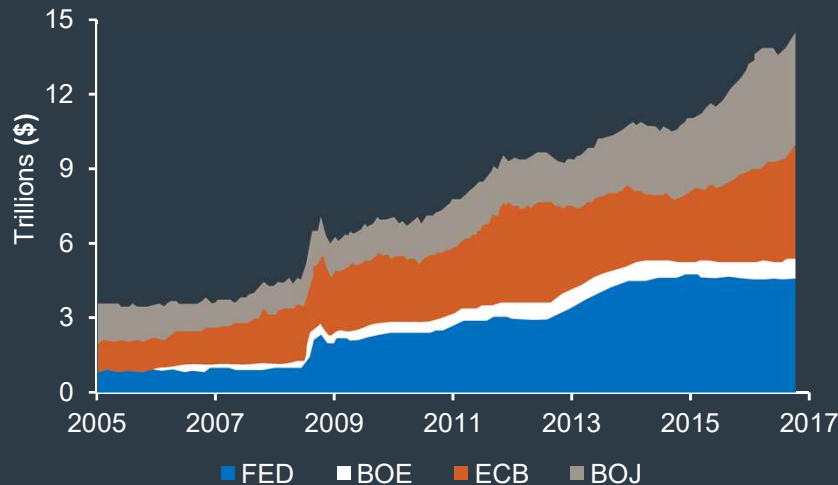
Source: Fidelity International, Consensus Economics, University of Michigan, March 2018.



Central Bank policy

Unprecedented synchronised liquidity support

Central Banks balance sheets

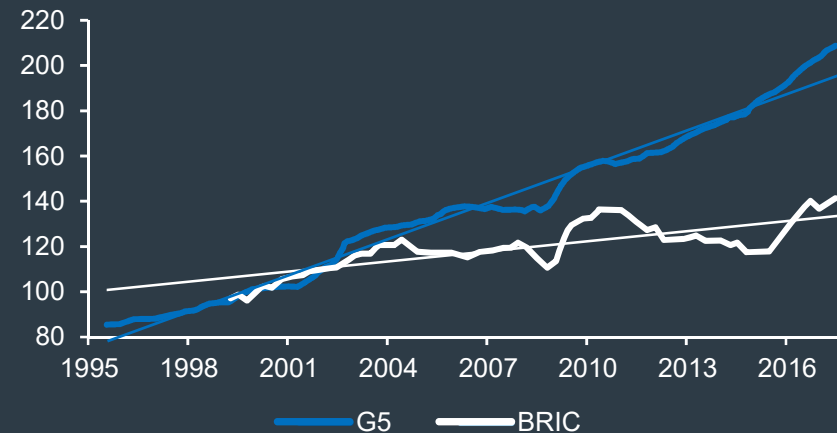


10-year sovereign yields as at 15 March 2018 (%)

US	UK	Germany	Japan
2.80	1.42	0.58	0.05

Source: Federal Reserve, Bank of England, European Central Bank, Bank of Japan, Harver Analytics, Fidelity Investments, (AART) 30 June 2017.

Excess liquidity expressed as M1/GDP – a main driver for asset prices globally



- M1/GDP for DM has improved since 2013 and is now well above trend
- EM liquidity was a laggard between 2012-15 but has improved over the last two years

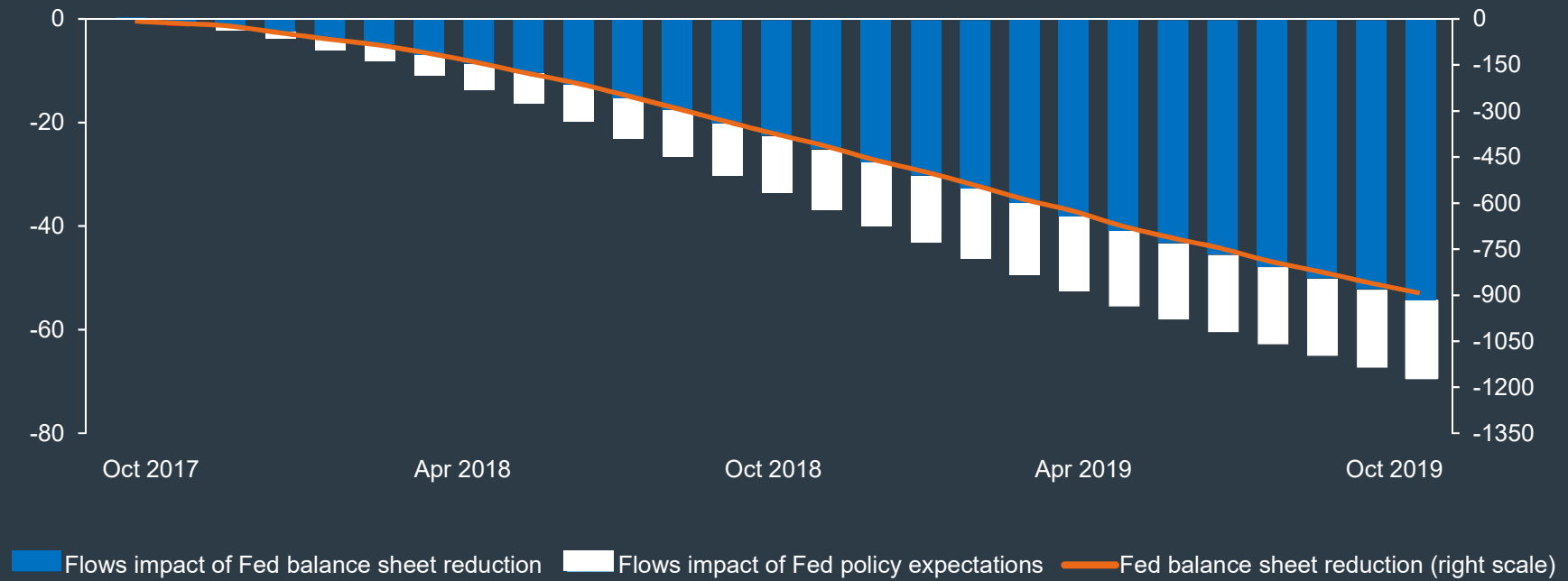
Source: National Sources, Morgan Stanley Research, November 2017.



QE to QT: How vulnerable are emerging markets?

\$35bn pa of portfolio flow reduction, vs \$200bn inflows in 2017

IMF estimate: cumulative contributions to EM portfolio flows (US\$ bn)

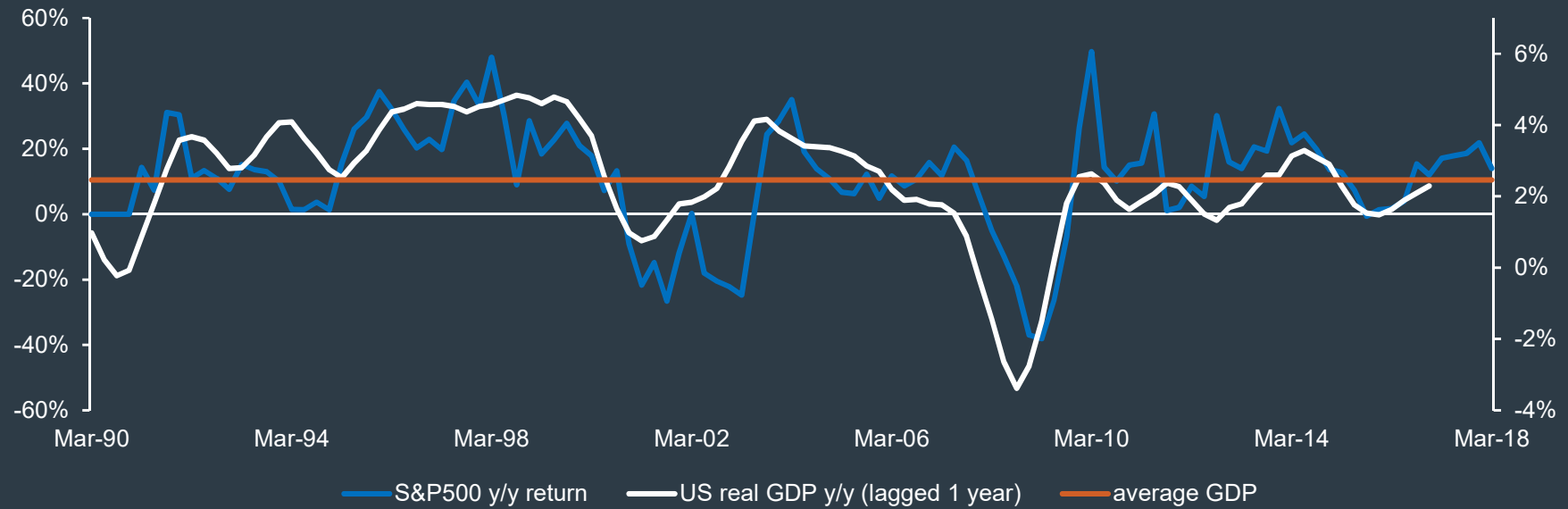


Source: IMF: Global Financial Stability Report, October 2017.



What has the US equity market priced in?

US equity returns and GDP



Source: Bloomberg, Fidelity International, April 2018



On a P/E basis, US equities look fair value

Forward price/earnings ratio of the S&P500

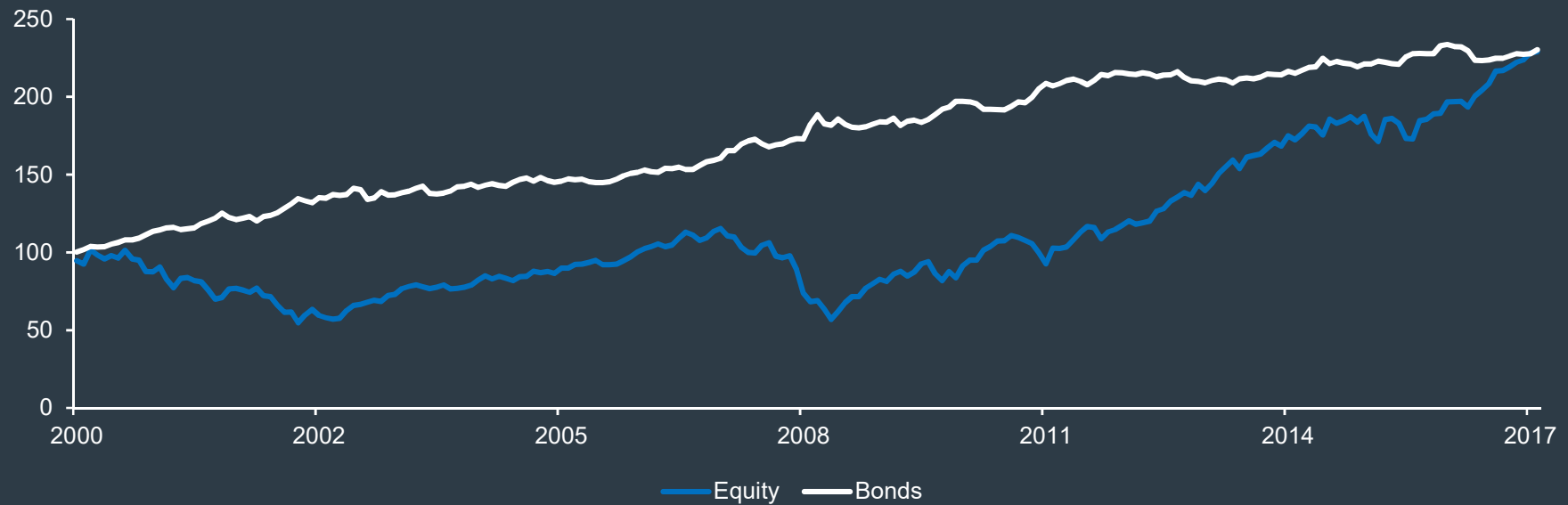


Source: Bloomberg, Fidelity International, April 2018.



Monetary policy affects asset prices

US total return indices



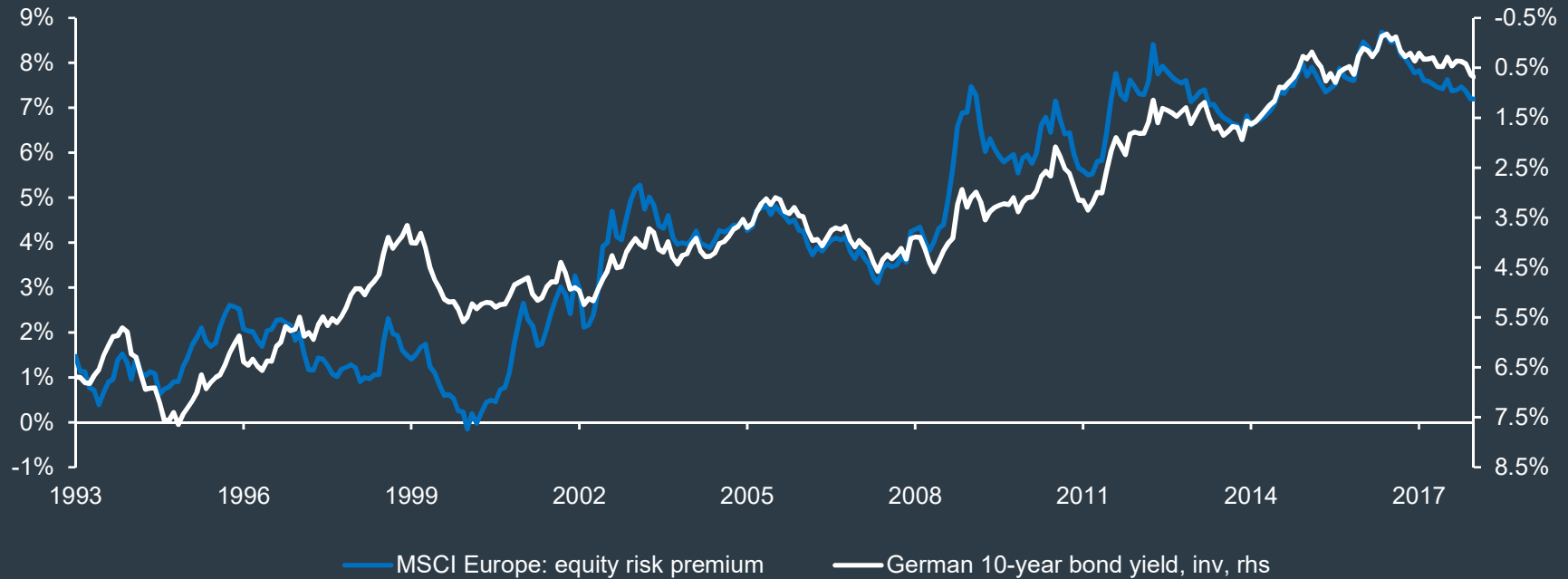
Source: Fidelity International, 31 August 2017. Equity: MSCI USA Total Return index, Bonds: Citi US Government Bond Index all Maturities – Total Return index



QE to QT: Equities might not like higher real yields

Equity risk premium

Estimates of combined impact of QT and budget deficits on monetary conditions



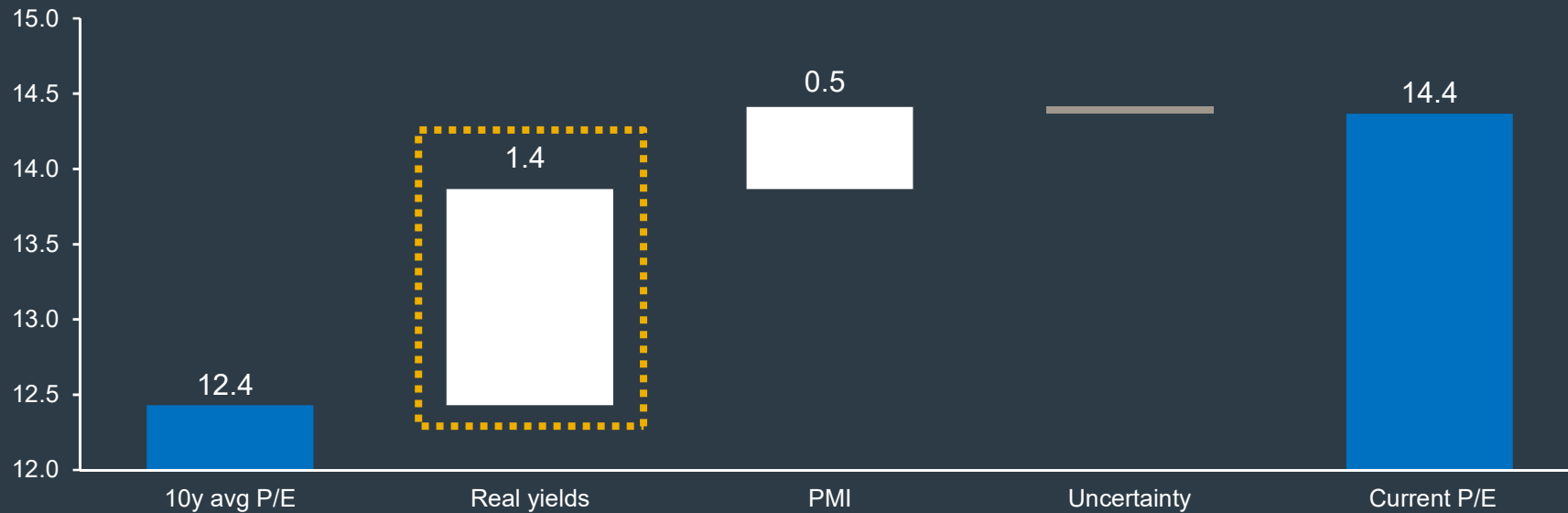
Source: Datastream, Haver, Bloomberg Finance LP, Deutsche Bank, as at 19 February 2018.



QE to QT: Valuation implications

Lower real yields main driver of multiple expansion

Drivers of deviation of European P/E from 10-year average



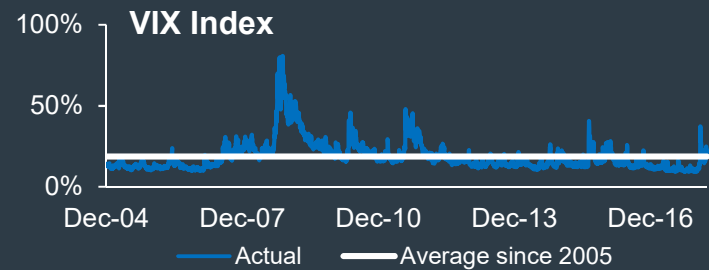
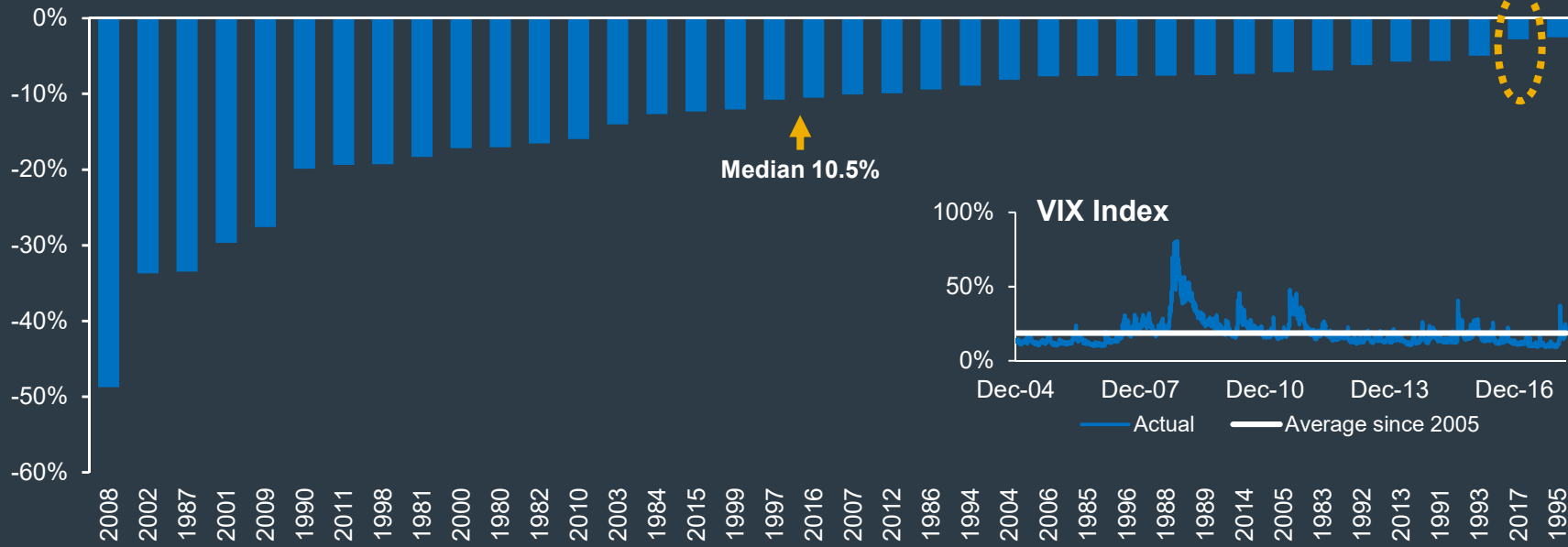
Source: Datastream, Haver, Bloomberg Finance LP, Deutsche Bank as at March 2018.



What to expect in 2018

2017 exceptional in historical context

S&P annual drawdown: 1980 – 2017



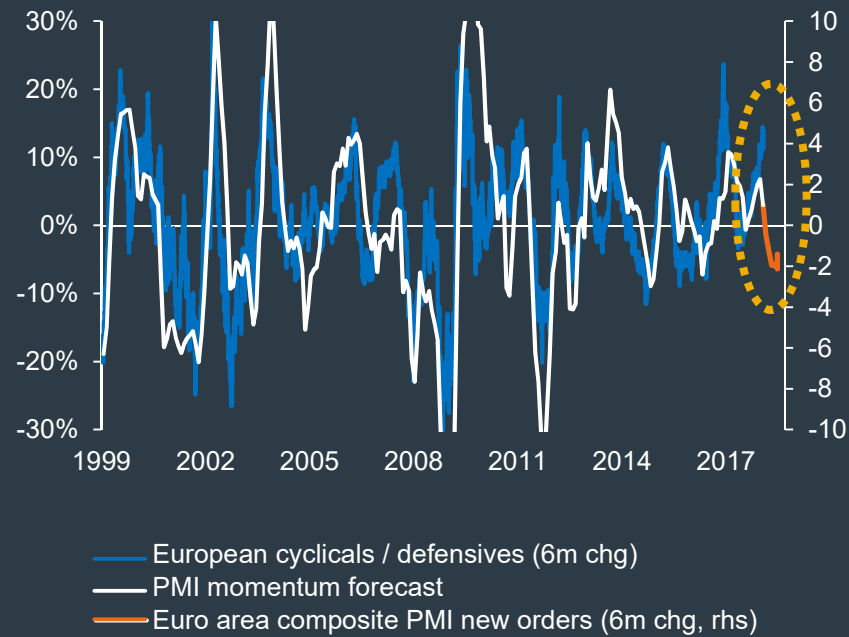
Source: Datastream, as at 31 March 2018.



What to expect in 2018?

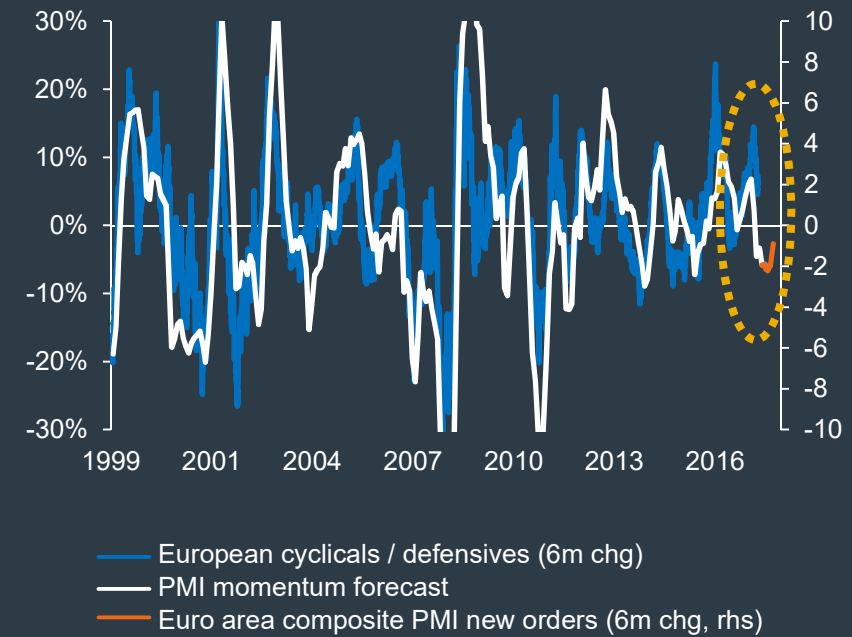
A change in global growth perception

As at 2 March 2018



Source: Datastream, Haver, Deutsche Bank, 2 March 2018.

As at 13 April 2018 – forecast was accurate



Source: Datastream, Haver, Deutsche Bank, 13 April 2018.



What to expect in 2018

Change in market leadership?

Period: 31/12/2013 to 21/03/2018

Ticker	Company	Total return contribution
SPX index	S&P 500 index	60.1%
Top 10 contributors		
1	Amazon.com Inc.	8.2%
2	NVIDIA Corp.	7.1%
3	Apple Inc.	5.6%
4	Microsoft Corp.	5.4%
5	Facebook Inc.	3.9%
6	Alphabet Inc.	3.2%
7	Netflix Inc.	2.3%
8	Berkshire Hathaway Inc.	2.1%
9	JP Morgan Chase & Co.	2.1%
10	United Health Group Inc.	1.8%

**Sums to 35.7%
more than half the 60.1%
S&P 500 increase**

Source: Goldman Sachs.



What to expect in 2018

Value generally outperforms when the economy is improving...except this time!

MSCI value vs growth



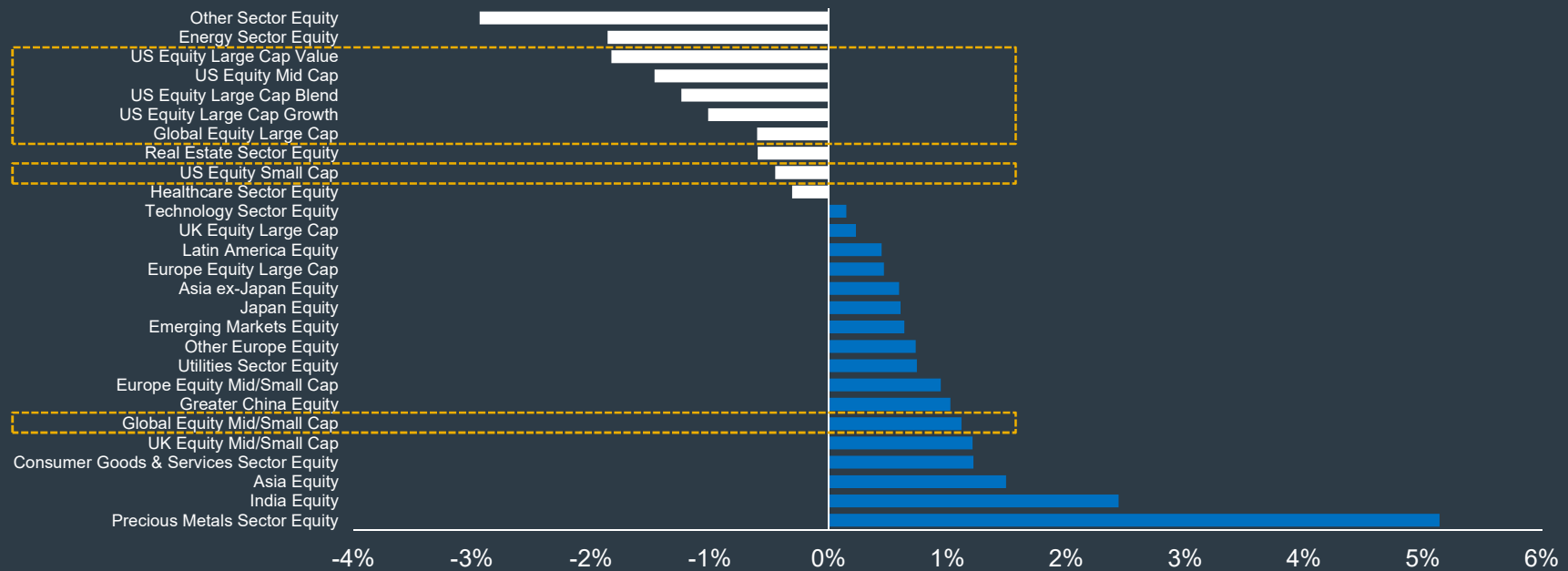
Source: Fidelity International, Bloomberg, 28 February 2018.



What to expect in 2018

Active vs passive performance: Chance of a revival for active managers?

2009-16 relative aggregate performance, by Morningstar Category

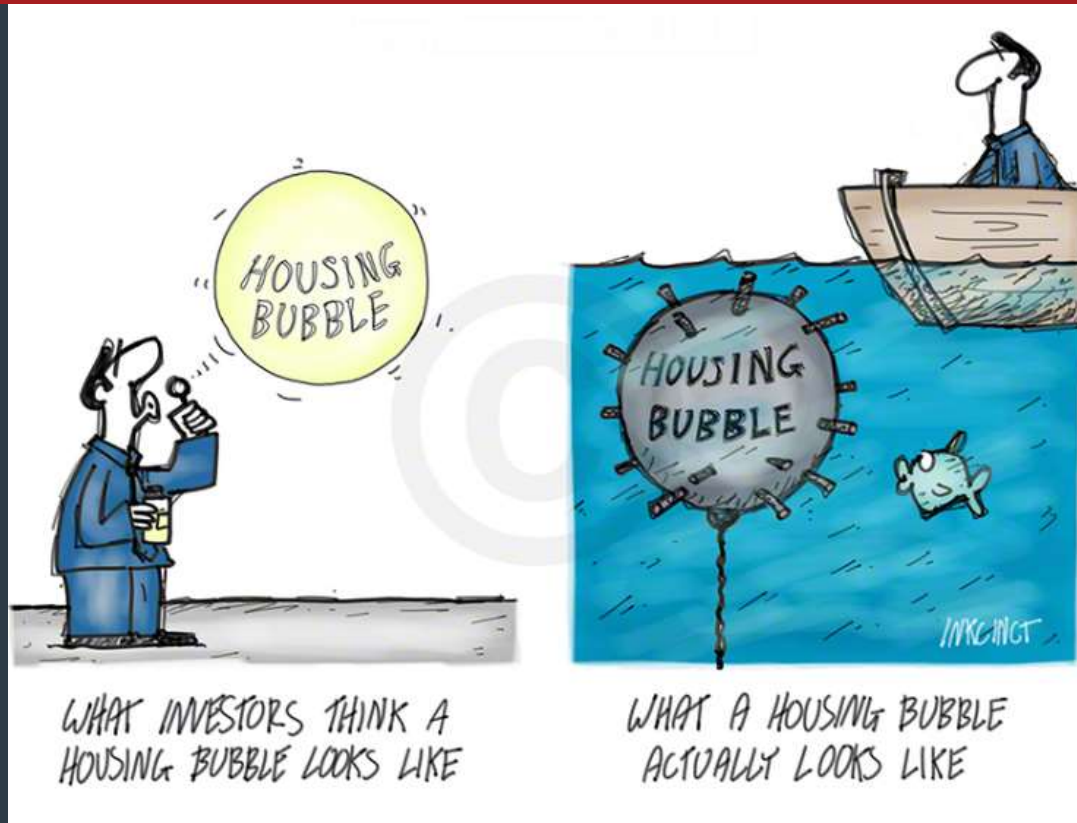


Past performance is not a reliable indicator of future results and the value of investments can be affected by changes in currency exchange rates.

Source: UBS Investment Bank, March 2018.



Key risks in the Australian market



Long-term interest rates

US government 10-year yield

Monthly since March 1942

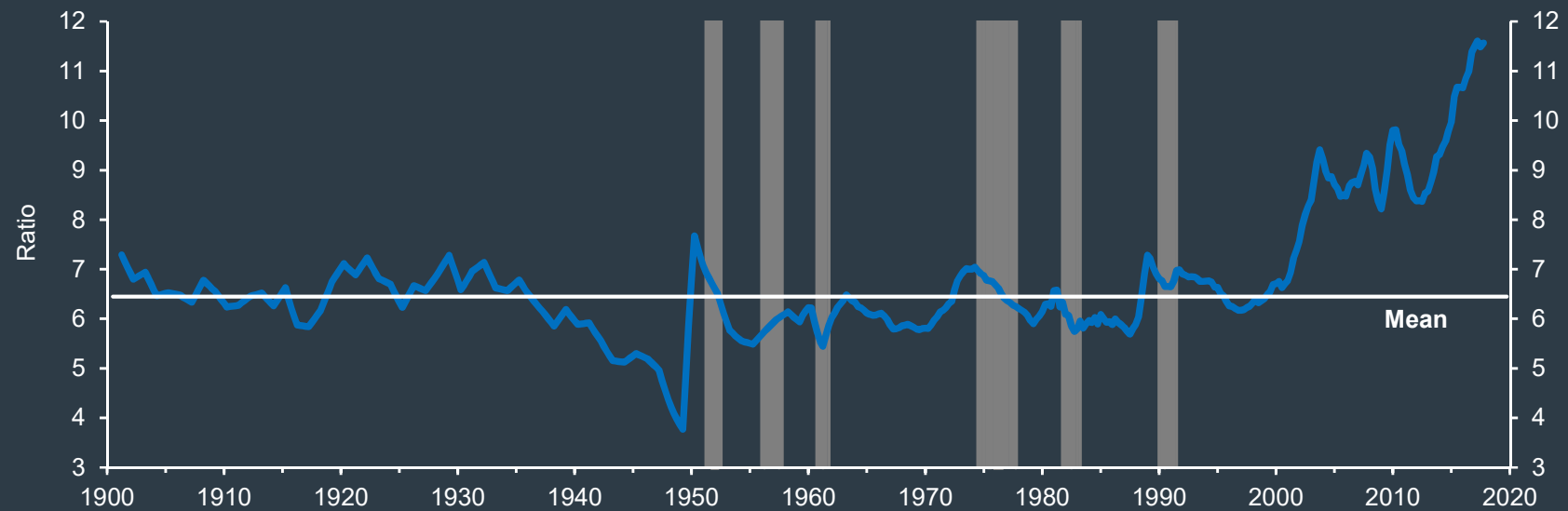


Source: Bloomberg and Multipl.com



The Australian housing market

Median house price / nominal GDP per capita

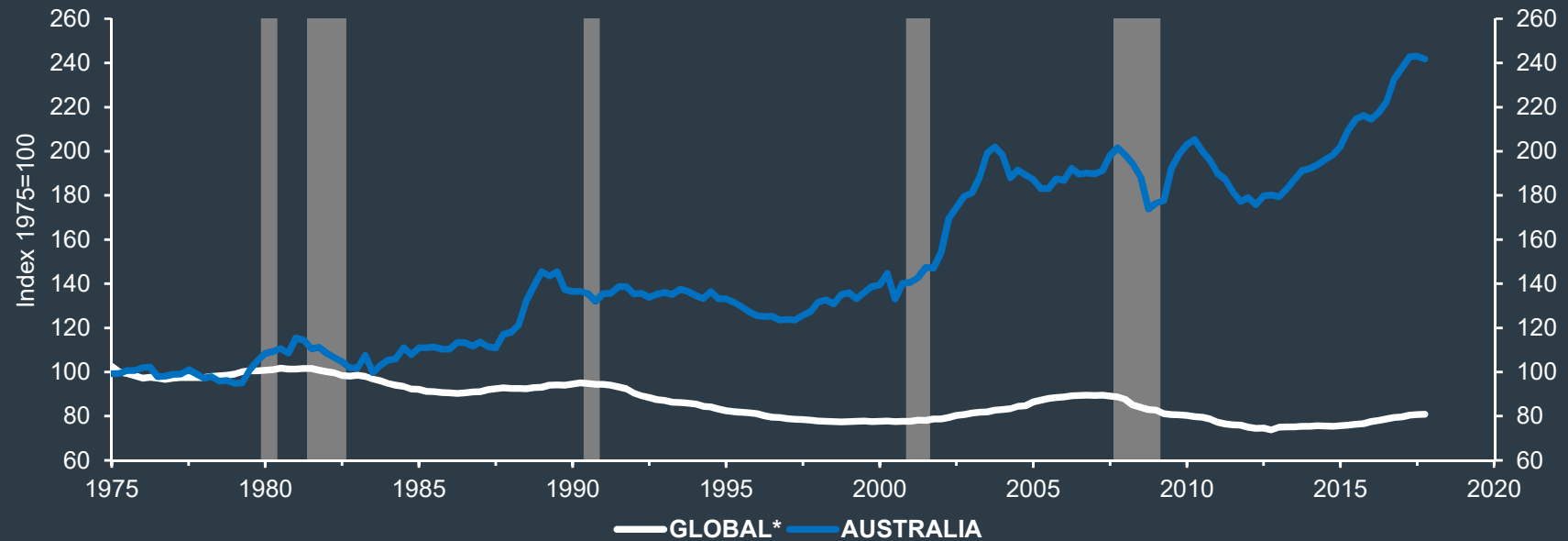


Recessions shaded after 1950.
Source: Minack Advisors



The Australian housing market

House price / per capita income



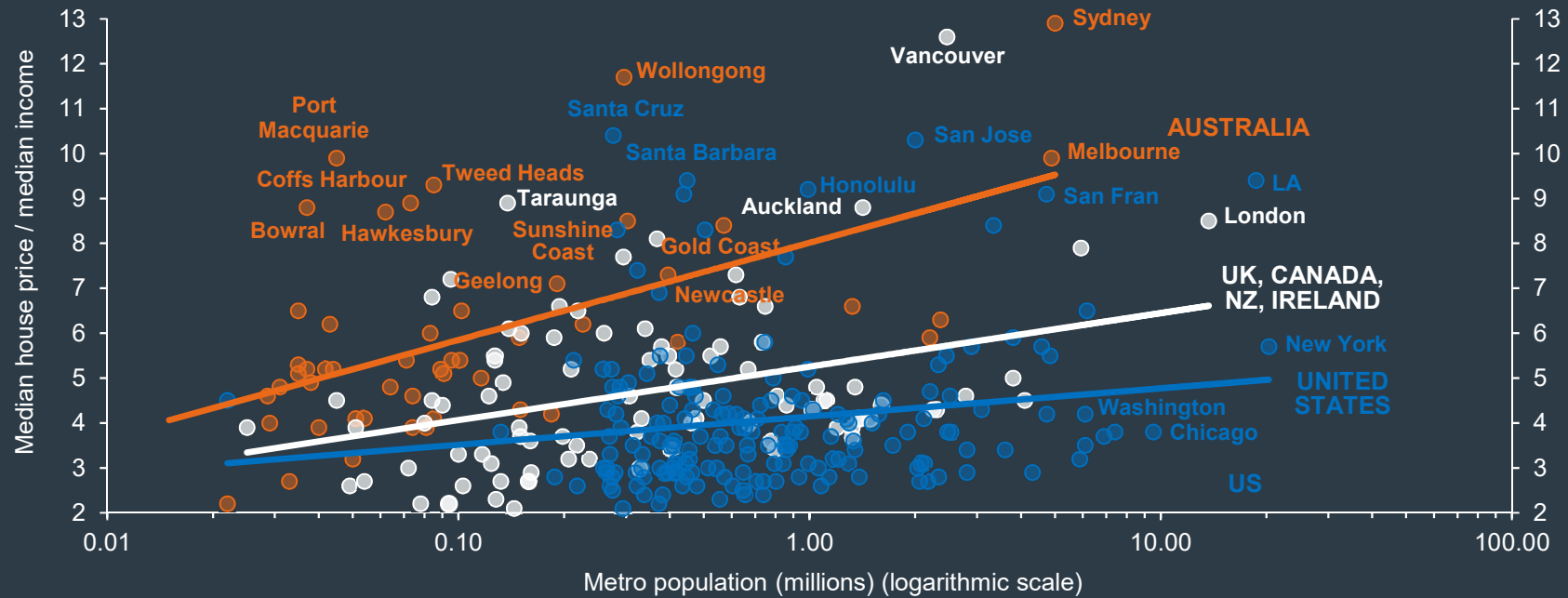
* GDP-PPP weighted average of Australia, Belgium, Canada, Switzerland, Germany, Denmark, Spain, Finland, France, UK, Ireland, Italy, Japan, Korea, Luxembourg, Holland, Norway, NZ, Sweden, US, South Africa, Croatia, Israel. US Recessions shaded. Source: Minack Advisors



The Australian housing market

House price / income and city size

Q3, 2017

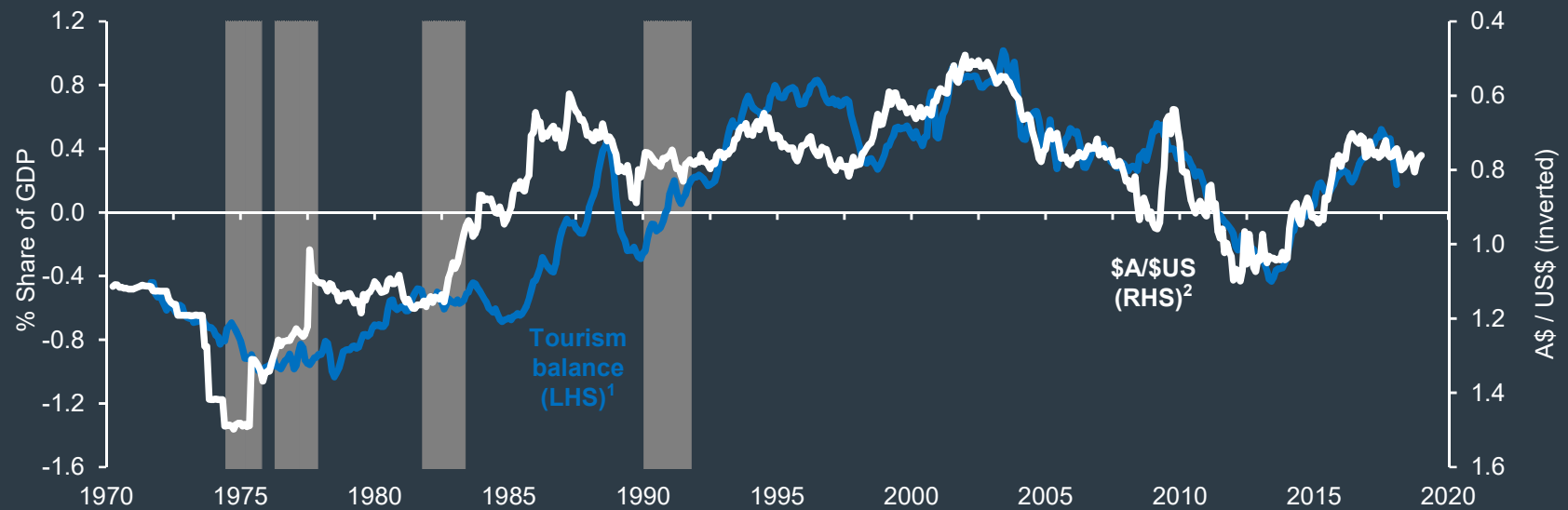


Source: Minack Advisors



Australian Dollar

A\$ and net tourism balance as share of GDP



1. Net balance of tourism services, rolling 3m sum as percent of GDP. 2. Inverted and leading by 9m.
Source: Minack Advisors

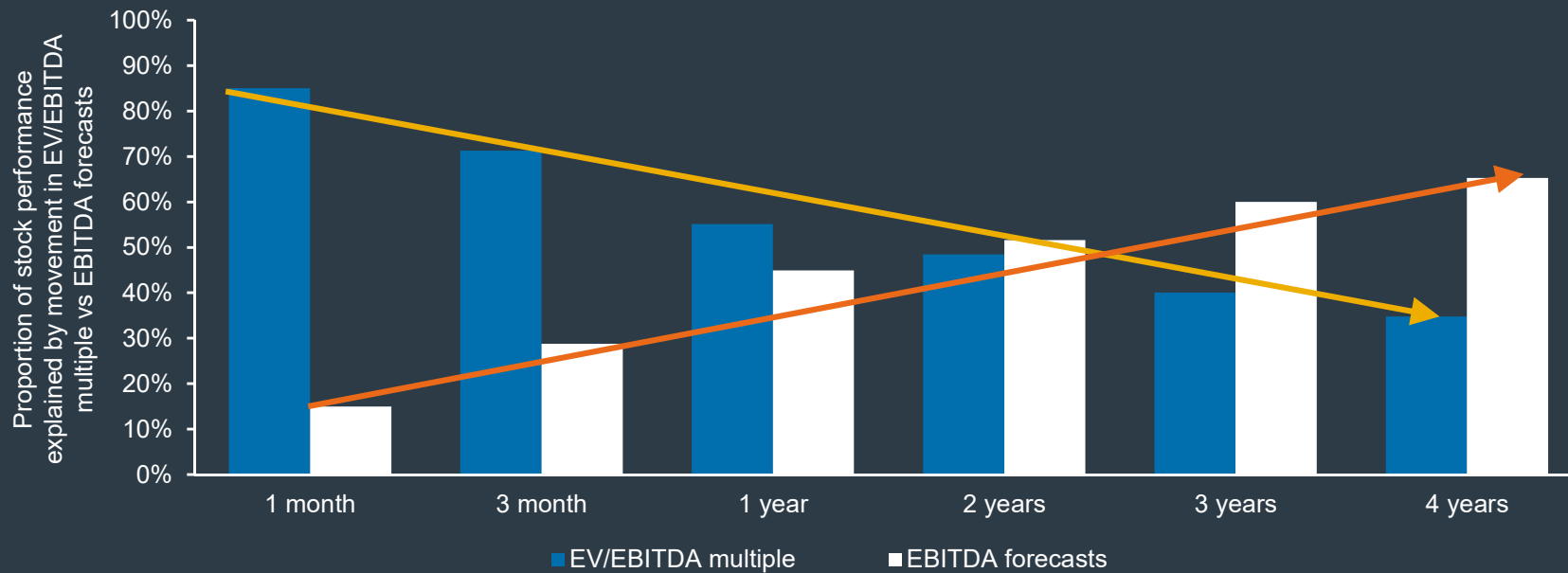


Other risks

- Government intervention/regulation
- Franking credits
- Slowing population growth
- Trade war
- China



Five-year investment horizon

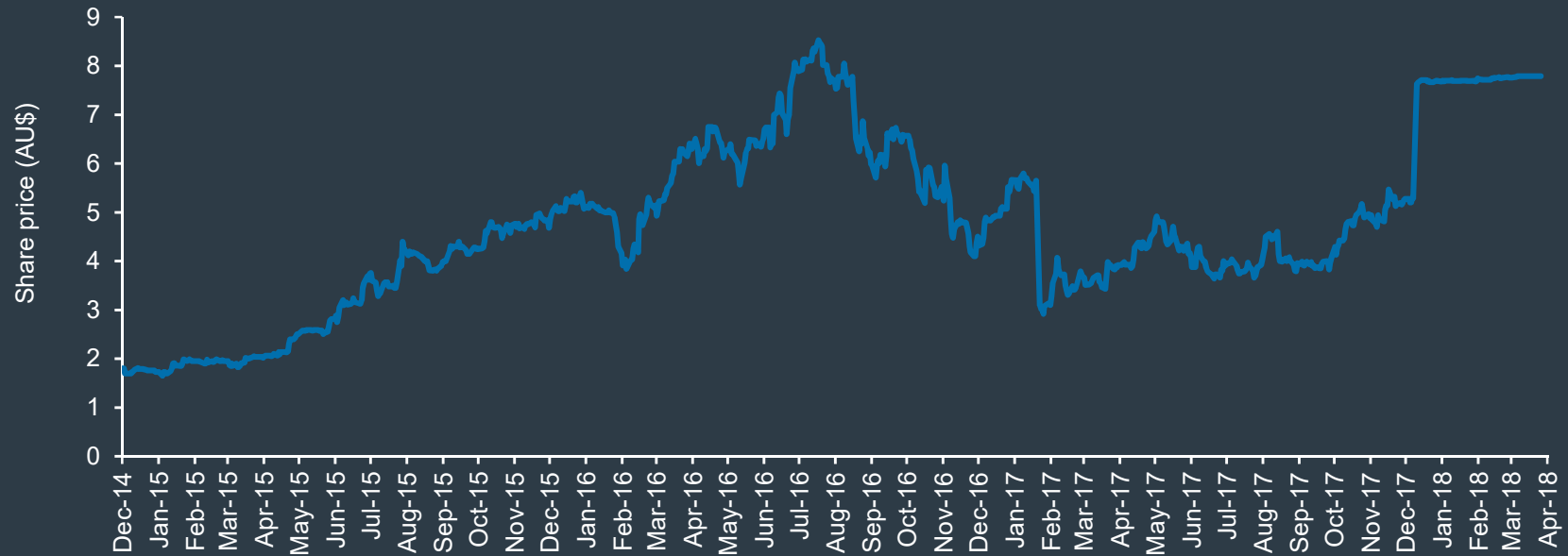


Source: Goldman Sachs. Proportion of shareholder return for explained by changes in valuation multiple (EV/EBITDA) vs. Change in earnings (EBITDA) forecasts. Based on the top 600 largest listed companies globally since 2010. Figures do not sum to 100. Holding period returns are the average of multiple holding periods between 2010 and 2015. As at January 2016.



Investing for the long-term

Case study: Aconex



Source: Fidelity International.



Summary Market Outlook

Considerations for asset allocation decision

Growth

- Global growth has tentatively rolled over, but from high levels. Significant downside drivers for growth are not visible in the data

Inflation

- Markets' 'original' downside risk, but concerns not borne out in data. Data points to normalisation
- Wage acceleration set to be modest and healthy, with pass-through to CPI weak at best
- Oil potentially the bigger risk. It could shock expectations and hurt consumers
- Structural drivers (demographics, debt overhang and productivity growth) will influence both medium term growth and inflation outlook

Central Bank

- 10 years of extraordinary monetary support has provided a unique environment for investors
- 'Beautiful normalization' might only exist in theory and might lead to increased volatility in asset markets





Summary



Cautiously...

- Cash looks expensive
- Recent back-up in yields positive for bonds
- Inflation looks contained but consider EM inflation linked if worried

...optimistic

- Assuming continued strong earnings, forward P/E Equities look at fair value relative to history
- Uncertain economic outlook and increased dispersion suggests more active management both at security selection and multi-asset level

Source: Fidelity International April 2018



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