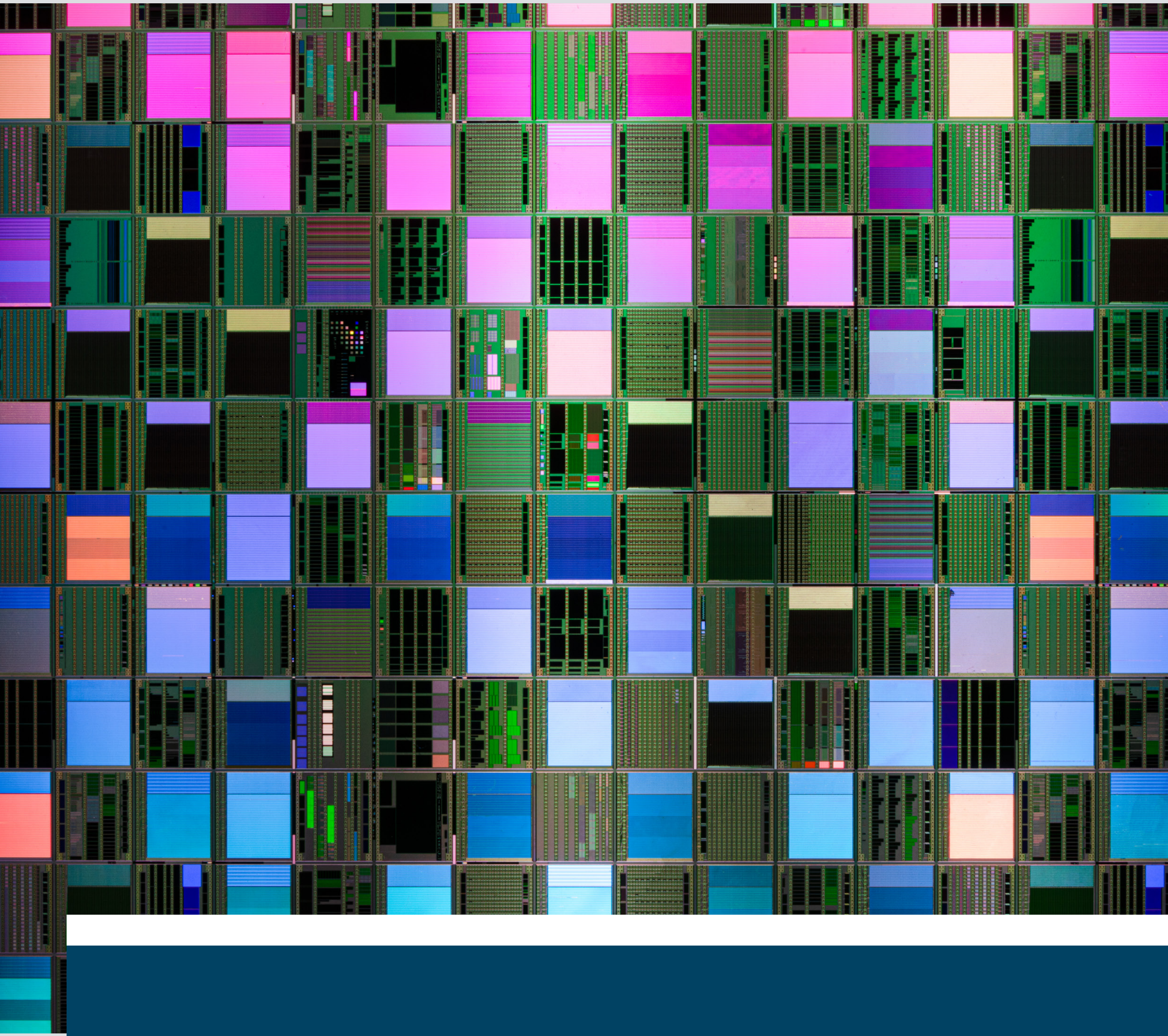


ANALYST SURVEY 2024

READY FOR A RESET

This material is for investment professionals only

Foreword

The Duck

Behold the duck.
It does not cluck.
A cluck it lacks.
It quacks.

It is specially fond
Of a puddle or pond.
When it dines or sups,
It bottoms ups.

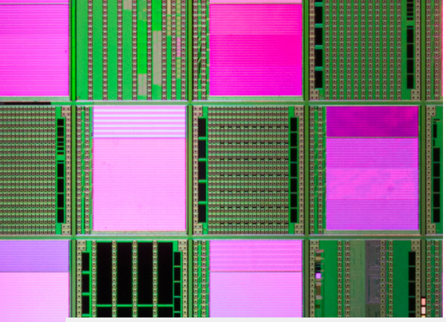
Ogden Nash

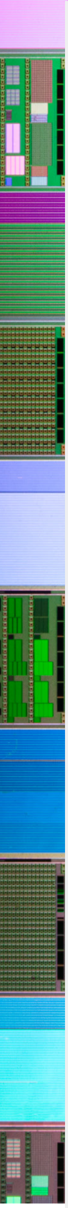
I'm not sure how Fidelity's analysts will take to being compared to ducks but I hope they forgive the connection to their bottom-up analysis that occurred to me when reading this poem by Ogden Nash: they find things that others - with their heads above water - can miss.

The report in your hands is a distillation of the observations formed not just from scrutinising company reports but from an extraordinary 20,000 meetings a year the analysts have with the companies they are assessing. Given this insight, you might notice how the survey complements and contrasts with top-down views of financial markets and macro-economics.

The depth and breadth of the analysts' knowledge is astounding and, as we set out in the pages that follow, their collective wisdom is a powerful predictive tool. Fidelity's investment team relies on it and I hope you find it useful too.

Richard Edgar
Editor in Chief





Contents

Overview: Ready for a reset

The past two years have been marked by a fear of how bad the first sustained economic slowdown since 2008 might become. Yet our annual survey of Fidelity International analysts suggests the conditions are settling into place for companies to look towards the expansion that should follow.


Gita Bal
Global Head of Fixed Income Research


Fiona O'Neill
Head of Global Cross-Asset Research Capabilities

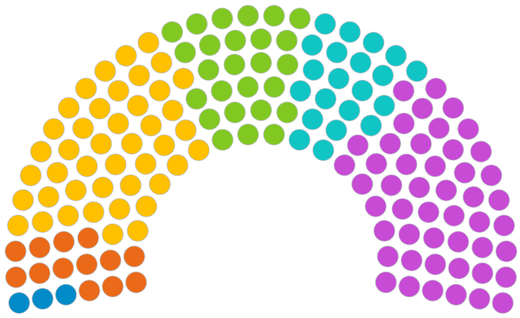

Patrick Graham
Senior Writer

Every sector has its own cycle. The results of our annual survey of Fidelity's company analysts shows nearly half (48 per cent) say the sectors they cover are now in economic slowdown or, in a handful of cases, outright recession. Yet conditions for turnaround are ripe. "No one talks about inflation anymore," says Brendan Cochrane, who covers North American consumer discretionary companies. "Labour wages were the last sticky aspect, but these seem to be normalising quickly as well."

Debt loads for most look manageable. Most CEOs expect earnings will grow. Asia appears as a bright spot, especially Japan. China's recovery from the Covid era, while still fragile, has received a boost from recent stimulus measures.

That is not to say the outlook is for clear blue skies. Many of the indicators in the survey, which gathers 155 responses from equity and credit analysts who cover businesses on the ground, are the most downbeat in years. A year of elections around the globe also comes with major geopolitical risks.

Chart 1: Stage of the cycle in 12 months' time



- Deep recession 3
- Shallow recession 13
- Slowdown 44
- Mature-stage expansion 26
- Mid-stage expansion 21
- Early-stage expansion / recovery 48

Chart shows responses to the question: "What stage of the cycle will your sector be in 12 months from now?" Chart shows percentage of analysts. Source: Fidelity International, January 2024. The survey was conducted in December 2023.

But look forward 12 months, as Chart 1 shows, and some 61 per cent of our analysts expect their sectors to be back in expansion mode. And as

Chart 2 shows, for the first time since the pandemic more of our analysts think companies' cost inflation will fall rather than rise in the year ahead.

Chart 2: Cost inflation pressures finally abating

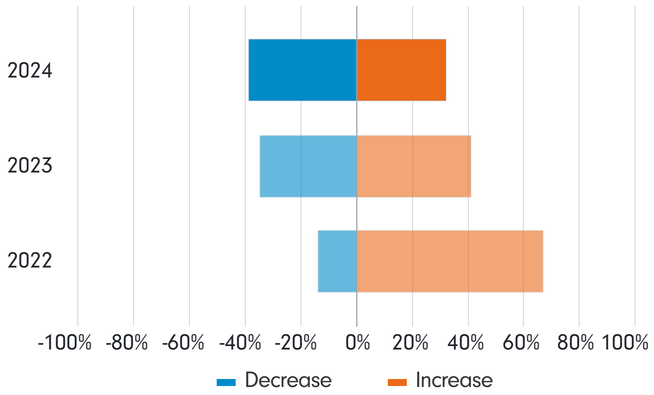


Chart shows responses to the question: 'How, if at all, do you expect inflationary pressures within your companies' cost bases to change over the next 12 months?' Analysts who responded 'No change' are not shown on the chart. Source: Fidelity International, January 2024.

Chart 3: 60 per cent of analysts say none or hardly any of their companies will have meaningful debt refinancing they need to do this year

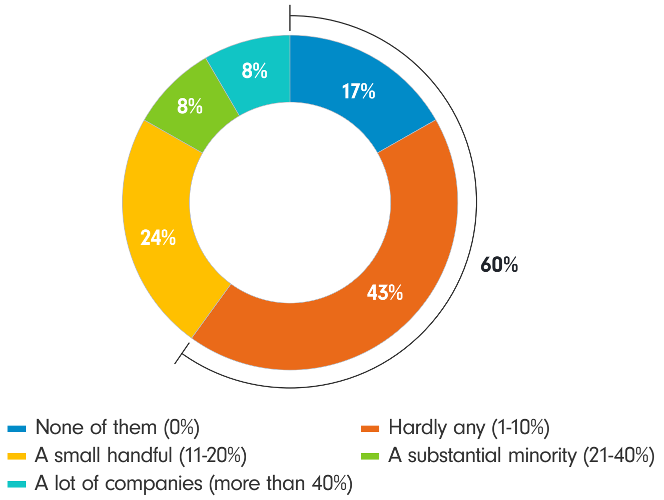


Chart shows responses to the question: "What percentage of your companies have meaningful debt refinancing to do in the next 12 months?" Chart shows percentage of analysts who answered 0%, 1-10%, 11-20%, 21-40%, and >40%. Source: Fidelity International, January 2024.

No maturity wall

The central macroeconomic argument last year for a slide into a painful and damaging recession was that sharply higher interest rates would hurt consumers and businesses, particularly in Europe and the United States. That didn't come to pass, and our analysts' assessment again this year is that most companies can further defer any meaningful debt refinancing: 60 per cent of the analysts believe that less than one company in every 10 they cover will need to roll over substantial sums of debt.

Only 8 per cent of analysts think there will be any trouble accessing finance for those who need to, and these financing challenges are concentrated in sectors and regions where financing pressures are well understood by the market.

In the meantime, bond markets have already pivoted towards lower rates and the spreads it costs companies to borrow are at historically low levels. One obvious beneficiary, as Chart 4 suggests, could be listed real estate companies. "The [market] rates decrease triggers optimism that we could be nearing the trough of valuation declines," says Othman El Iraki, a fixed income analyst covering Europe's battered real estate sector.

Chart 4: Turnaround sectors

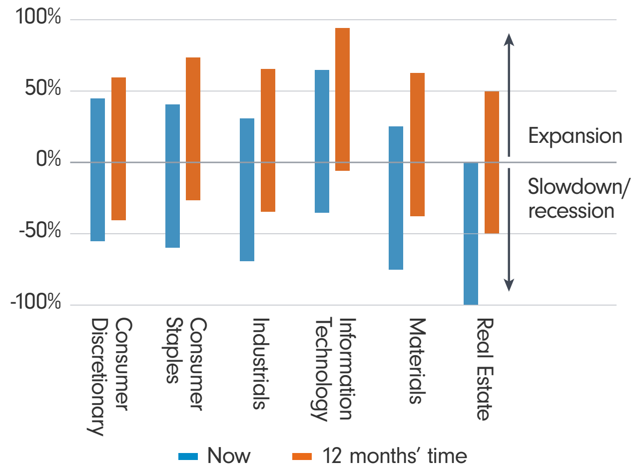


Chart shows responses to the questions: "What stage of the cycle is your sector currently in?" and "What stage of the cycle will your sector be in 12 months from now?" Chart shows percentage of analysts. Source: Fidelity International, January 2024.

Tough it out

For most sectors, the analysts who cover them expect that they will show improvement this year, with the proportion who say their sector is in expansion mode rising from 52 per cent right now to 61 per cent who expect that to be the case in 12 months' time. "Meetings with management teams have been surprisingly positive on the 2024 outlook," says James Filsell, who covers European industrials.

There are, however, a handful of sectors where our responses suggest conditions may prove tougher as the year goes on.

Chart 5: Sectors facing challenges

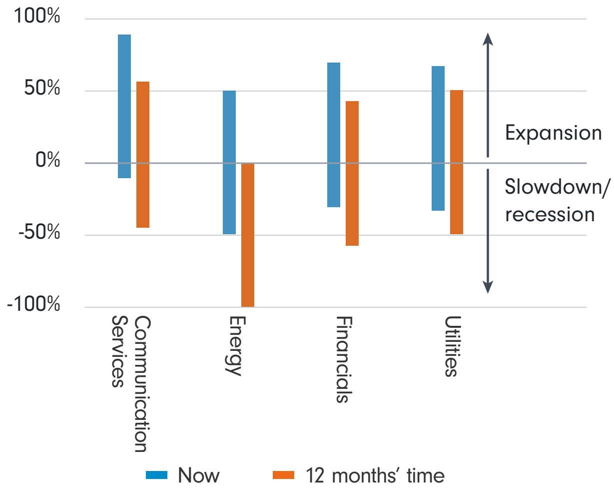


Chart shows responses to the questions: "What stage of the cycle is your sector currently in?" and "What stage of the cycle will your sector be in 12 months from now?" Chart shows percentage of analysts. Source: Fidelity International, January 2024.

Our analysts who cover North American and European oil and gas firms cite lower commodity prices as a headwind for the energy sector.

The financial sector will also see the flip side of the retreat in interest rates.

"Two factors are driving the somewhat negative sentiment," says Sukhy Kaur, a fixed income analyst who covers Nordic and Benelux banks. "Net interest income looks to have peaked across the majority of my coverage in the last quarter and, for some, inflationary pressure, particularly wages, will continue into 2024."

Asian exceptions

A similar split amongst regions is writ large across many of the survey's results. Fewer than a third of all analysts say returns on capital (ROC) will increase at their companies, but more than half of analysts covering Japan and Asia ex-China are expecting an improvement.

"Companies have a much better handle on costs and margins," says Rahul Gupta, who covers Apac internet companies, citing lower competition and an increase in consumer spending as additional tailwinds.

In China, however, only 11 per cent say returns will improve.

Chart 6: Are returns on capital set to rise or fall?

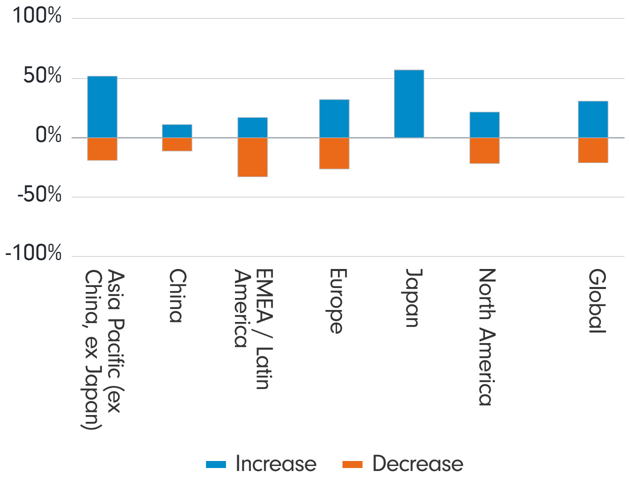


Chart shows responses to the question: "What is the outlook for overall returns on capital for your companies for the next 12 months?" Chart shows percentage of analysts responding they expect returns will increase or decrease. Analysts who responded "No change" are not shown on the chart. Source: Fidelity International, January 2024.

Grey cygnets?

Our analysts also identify events that could knock their soft-landing narrative off course. The most immediate is the glut of elections this year: more people will be asked to cast a vote in 2024 than in any other previous year in history, creating the risk of disruption.

There is division among companies when it comes to talking about election risks. Much boils down to particular scenarios in specific sectors. Only 28 per cent say the current geopolitical backdrop is encroaching on investment plans - the smallest proportion of analysts to say this since we started asking this question in 2017. But European industrials analyst Tristan Purcell cites the US presidential election as an important driver to the fundamentals of the companies he covers. “A Republican victory increases the likelihood of reversing stimulus measures like the IRA and CHIPS Act.”

Chart 7: How will geopolitics affect strategic investment at the companies you cover?

Chart shows responses to the question: “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?” Chart shows percentage of analysts who say impact will be positive or negative. Analysts who responded “No impact” are not shown on the chart. Source: Fidelity International 2024.

One of the survey’s most striking findings, however, is that most analysts (65 per cent) say their companies are not talking about elections at all.

“I do think that the companies I cover are not talking enough about these risks, it is a blind spot,” says Andras Karman, who covers European and North American auto manufacturers who are intimately tied to China and the fluidity of global trade. “I attribute this in part to the very sensitive nature of doing business in China.”

Chart 8: Not talking about a revolution

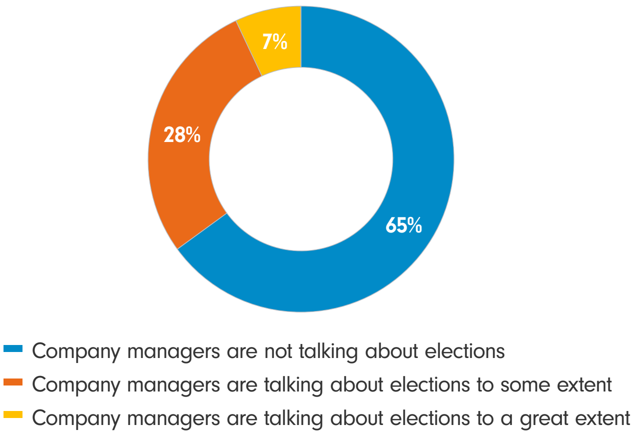


Chart shows responses to the question: “In 2024, countries making up an estimated >50% of global GDP will hold elections, including India and the United States (expected to be 76 countries in total). To what extent are your companies talking about this?” Chart shows percentage of analysts. Source: Fidelity International, January 2024.

Jonathan Tseng, who covers semiconductor producers in North America and Europe, says companies are lobbying heavily behind the scenes, but that few see any upside in wading into politics publicly.

“Even if you had a strong view, you’d be crazy to articulate it given history has showed the odds will be shifting right up to, and beyond, polling day,” he says.

Alan Zhou, who covers Asian conglomerates, explains the complexity companies face: “For autos, I think geopolitical risks will increase company costs mainly because they are unable to take care of multiple market interests with one supply chain anymore.”

But he adds that geopolitical tensions have actually been positive for conglomerates with resource assets because they have benefitted from price rises.

Next phase

The end of the era of zero rates was always going to bring tensions. Yet this year’s survey offers clear signs that, however the slowdown plays out, for most companies the system will reset and the next phase will lift them up rather than cast them down.

Optimism balloons from Japan's reflating economy

Japan leads the world on bullish sentiment in this year's Analyst Survey as its economy enters a reflating stage unique among developed nations.

Miyuki Kashima
Head of Investments, Japan

Yi Hu
Investment Writer

Japan is set to become the world's economic bright spot in 2024, according to Fidelity International analysts covering the country, who see much to be confident about across their sectors in the year ahead.

> Japan leads the world on bullish sentiment in this year's Analyst Survey

Expectations for revenue and earnings growth in 2024 are higher for Japan than for any other region. Analysts covering Japan are also the most optimistic about widening earnings margins.

Storming ahead

Japan leads the pack when it comes to expectations for capital expenditure, returns on capital, dividend increases, ability to pass on costs to consumers, and whether or not its companies will be in an expansionary phase of the business cycle by this time next year.

Chart 9: Fidelity's Japan-focused analysts see plenty of reasons for optimism

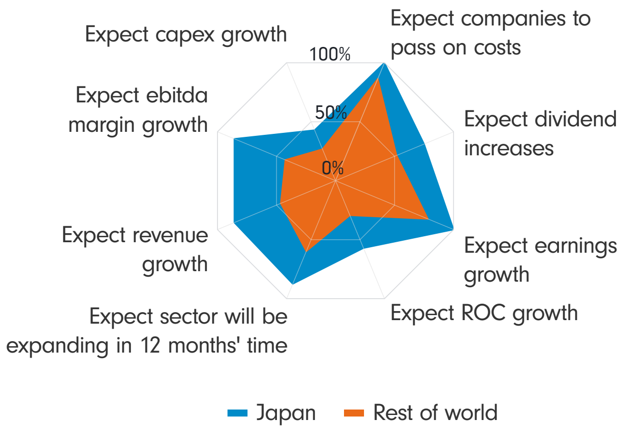


Chart shows percentage of Japan-focused analysts who answered positively for their companies in the following areas, versus analysts from all other regions. Source: Fidelity International, January 2024. The survey was conducted in December 2023.

There is a straightforward reason for much of this optimism. The Japanese economy has finally emerged from more than two decades of recessions and stagnation, with encouraging signs of broad-based price increases. While inflation has been a big headache for much of the world over the last few years, it's a good problem to have in Japan right now.

"Cost inflation weakened the earnings of device makers last year, but now the companies are able to pass higher costs to their customers," says healthcare analyst Aki Takaesu. She adds that a shortage of vital components has also eased, further boosting their earnings outlook.

While inflation has been a big headache for much of the world over the last few years, it's a good problem to have in Japan right now

The optimism contrasts with the higher level of caution in our previous annual survey conducted towards the end of 2022. For example, nearly a third of Japan analysts then said that the company CEOs they covered were expecting no earnings growth in 2023, the most pessimistic among all regions except EMEA/Latin America. The current survey has all Japan analysts saying that CEOs expect earnings to grow.

Similarly, expectations were significantly lower in the previous survey for revenue, earnings margins, and capital expenditure in Japan.

Chart 10: Japan will have more cost inflation than any other region (and that's a good thing)

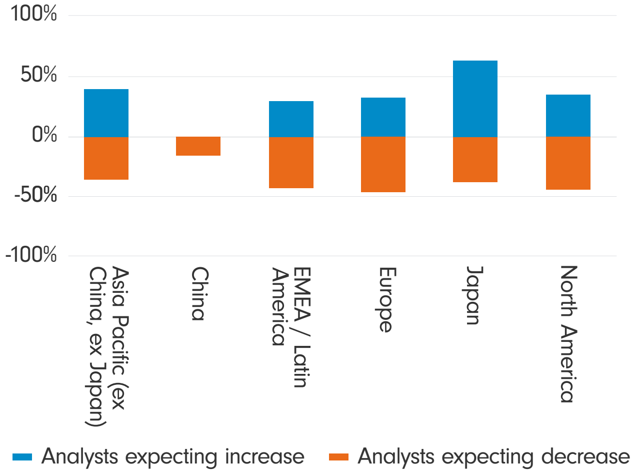


Chart shows percentage of analyst responses to the question: "How, if at all, do you expect inflationary pressures within your companies' cost bases to change over the next 12 months?" Analysts who responded "No change" are not shown on the chart. Source: Fidelity International, January 2024.

Our analysts expect higher cost inflation in Japan than analysts in any other region over the next 12 months. But they also think Japanese companies are the most able to pass on cost increases to customers. In fact, Japan is the only region where all of our on-the-ground analysts believe there can be at least some degree of cost transfer. By contrast, in both China and North America, 16 per cent of analysts think the companies they cover will not be able to pass on any higher costs.

Japanese companies largely avoided customer backlash when they raised prices in 2023, with many of them doing so for the first time in many years. So far, the country's consumers have shown tolerance for mild price hikes, making it easier for Japanese firms to handle cost inflation.

Business bump

When it comes to earnings, all of the Japan analysts report that their company CEOs are expecting them to grow over the next 12 months. This is a far rosier situation than other regions: 42 per cent of our China analysts and 24 per cent of our Europe analysts say their management teams are not expecting earnings growth at all.

Chart 11: All Japan analysts say CEOs expect earnings growth this year

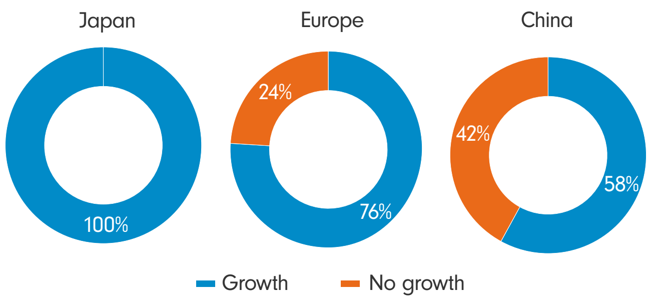


Chart shows responses to the question: "Do the CEOs in your industry sector expect earnings to grow over the next 12 months?" Source: Fidelity International, January 2024.

"Strong revenue growth in my sector will be driven by companies accelerating the IT system modernisation in response to an ongoing labour shortage and low cloud penetration in Japan," says Noriyuki Takizawa, an analyst covering software and IT services. Takizawa adds that CEO confidence in his sector is underpinned by strong books, which has led to backlogs - a clear expansionary signal.

Positive signals abound in Japan: 88 per cent of analysts are projecting an expansionary stage for their sectors in 12 months' time - the highest across all regions. At a global level, only 61 per cent of analysts envision an expansionary phase at the end of 2024.

Chart 12: Stage of the cycle in 12 months

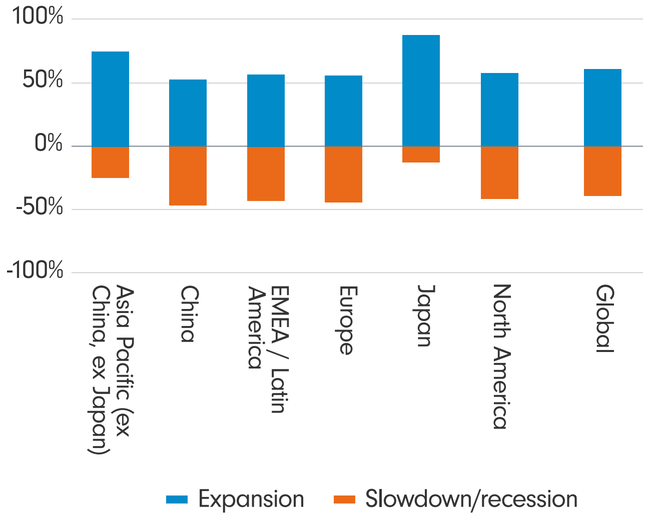


Chart shows percentage of analyst responses to the question: "What stage of the cycle will your sector be in 12 months' time?" Source: Fidelity International, January 2024.

"For commodity chemicals, the utilisation rate at ethylene plants has been improving over the last few months after hitting its lowest level since the Global Financial Crisis, suggesting that a bottom has been reached," says materials analyst Karens Muljadi.

88 per cent of analysts are projecting an expansionary stage for their sectors in 12 months' time

In addition, Japanese companies appear to have the lowest need for capital, due partly to adequate cash positions. On average, our analysts in Japan think that only 2 per cent of the companies they cover will need to raise funds in the next 12 months, versus 45 per cent in China and 27 per cent in Europe.

Chart 13: Japanese companies are cash rich and so have least need to raise capital

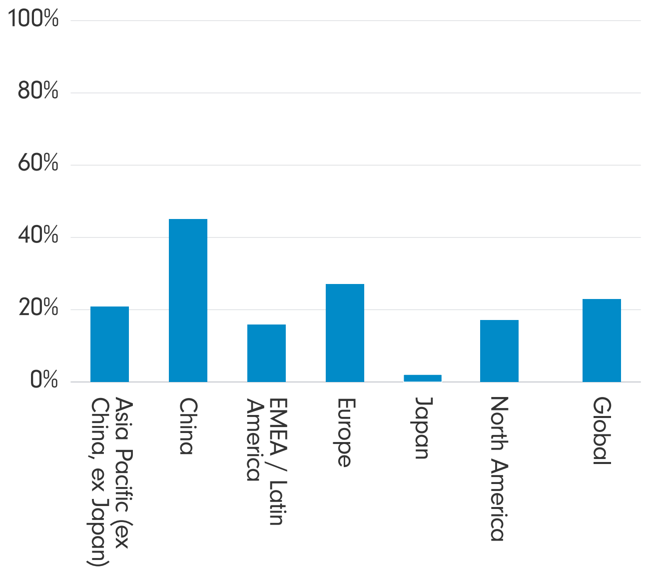


Chart shows responses to the question: "What percentage of your companies do you expect will need to raise capital in the next 12 months, via the equity or bond markets?" Chart shows average of responses. Source: Fidelity International, January 2024.

"Most of the companies I cover are net-cash and generate good cashflows," says Takaesu. "They are not planning a lot of large investments relative to their recent capex trends."

Mindful of the politics

Despite the abundant optimism, one distinct risk for corporate Japan that emerges from the survey results is geopolitics. Analysts covering Japan are more pessimistic than any other region about the impact of international tensions.

Chart 14: Geopolitics casts a shadow

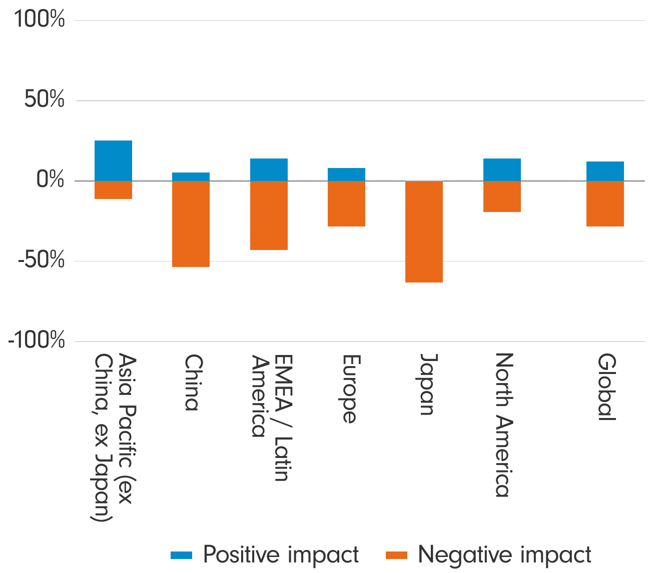


Chart shows responses to the question: "To what extent is the geopolitical backdrop having an impact on the strategic investment plans (capex and M&A) of the companies that you cover?" Source: Fidelity International, January 2024.

"Chip-related strife between China and the US may result in my companies, many of which produce semiconductor materials, having to diversify their production bases with excess capex," says Muljadi. "In a worst-case scenario, they'll have to take sides and risk losing the revenue stream from one side."

Japanese automakers could face higher costs too if the US pushes for greater localisation of car production, or if China curbs the export of some essential materials for making electric vehicles amid trade conflicts, according to auto analyst Daichi Ban.

All told, though, Japan still stands out as an economy being lifted by inflation rather than weighed down by it. Our survey's findings say that will continue in 2024.

China: The fragile recovery continues

Economic stimulus, low borrowing costs, and a loose labour market are proving supportive to most Chinese companies - for now. But sluggish demand is dampening management sentiment for 2024.

Monica Li
Director of Research

Judy Chen
Investment Writer

China's much-hailed reopening in early 2023 after three years of lockdown, did not generate the economic rebound many had hoped for (including us). But the disappointing performance was at least in part cushioned by policymakers' moves since July to ramp up stimulus intended to stabilise the property sector and defuse local government debt risks.

"The Chinese recovery is happening, but it is quite fragile," says Peter Carter, an equity analyst covering Chinese financial firms. "My base case is that the recovery will continue gradually for Chinese insurers and fintech lenders in 2024, whilst other financial subsectors will continue to face headwinds."

Consumption has become the country's engine of growth since restrictions were lifted, accounting for 83 per cent of real GDP growth in the first three quarters of last year[1]. Monetary easing and increased government spending on infrastructure have also boosted growth. About two thirds (63 per cent) of Fidelity's China analysts say the Chinese companies they cover are currently in an expansionary stage of the business cycle, up from 44 per cent a year ago[2].

Chart 15: More China analysts say their sector is now in expansion compared to a year ago

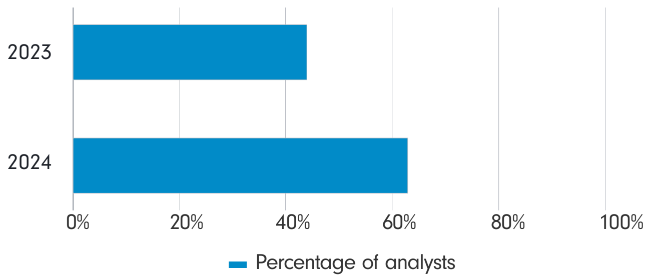


Chart shows responses to the question: 'What stage of the cycle is your sector currently in?' Chart shows percentage of analysts who answered either 'early-stage expansion', 'mid-stage expansion', or 'mature-stage expansion.' Source: Fidelity International, January 2024. The survey was conducted in December 2023.

[1]According to the National Bureau of Statistics of China.
[2]Fidelity International's Analyst Survey was conducted in December 2023.

But the prolonged property slowdown continues to weigh heavily on consumer confidence, since real estate accounts for a large proportion of household wealth in China.

"The priority from the top leadership is to stabilise the economic slowdown with a focus on high-quality growth instead of debt-fuelled growth," says real estate fixed income analyst Ming Gong. "I expect China to continue its structural slowdown."

Against this backdrop, analysts are cautious about the performance of their companies in the coming 12 months and their answers suggest a slight slowdown. Just over half of our China analysts say their companies will be in some form of expansion by the end of 2024.

Chart 16: China analysts are cautious on the future

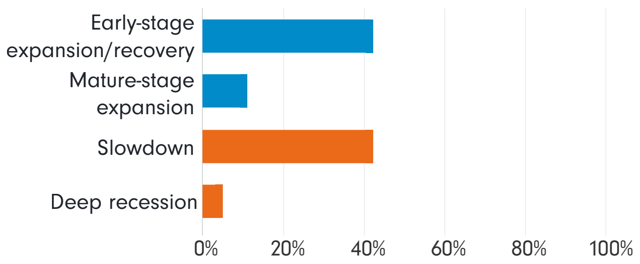


Chart shows responses to the question: "What stage of the cycle will your sector be in in 12 months' time?" Each bar represents the percentage of analysts who expect their sector will be in that stage of the cycle in 12 months. Source: Fidelity International, January 2024.

This figure is slightly lower than the percentage of analysts who say their companies are in an expansionary stage now, implying a slowdown.

Although analysts do forecast an increase in Chinese companies' revenues and profit margins in 2024, expectations are weak when compared to the rest of Asia.

Economic weakness pushes down costs

China stands out as the only region in this year's survey where more analysts expect labour costs to decrease than increase over the next six months. Labour demand remains sluggish, with more weakness in the market for younger and less experienced workers. This is a political hot potato but it eases pressure on company management teams.

Chart 17: China's loose labour market and falling wages

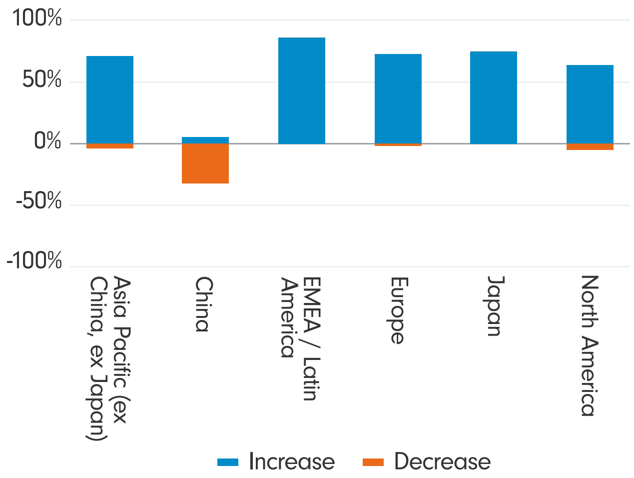


Chart shows percentage of analyst responses to the question: "For total labour costs, what are your expectations for your companies over the next six months compared with current levels?" Analysts who responded "No change" are not shown on the chart. Source: Fidelity International, January 2024.

China is also one of only two regions - the other being EMEA/Latin America - where more analysts anticipate non-labour costs to drop rather than go up.

The absence of inflation - a contrast to the experience of most countries after they reopened their economies - is helping Chinese companies to reduce costs. But it also reflects weak growth momentum, which could outweigh the benefit of falling costs.

"Automobile companies are having to cut new car prices as competition intensifies and consumer sentiment stays weak," says Eric Tse, an equity analyst covering Chinese auto companies.

Easing set to continue

The loose monetary environment was a boost for Chinese companies in 2023. First-time bond defaults in the onshore market fell sharply[3]. Low borrowing costs are likely to have helped companies service their debt and default risks are expected to stay low as the PBoC unveils more easing measures in 2024. "Growth is expected to slow down, and interest rates will trend lower in China," says Sherry Zhang, a fixed income analyst covering the financial sector.

But our analysts expect more differentiation in funding costs between state-owned and private-owned property developers. "Refinancing will not be a challenge for state-owned property developers, and interest costs may go down as China continues in its loosening monetary cycle," says Fiona Shou, an equity analyst covering property firms.

"However, for private-owned developers that have not defaulted, refinancing may become harder and interest costs may go up if contracted sales do not improve."

CEOs turn conservative

The country's muted economic outlook is making business leaders cautious. China is the region with the highest proportion of analysts who describe their companies' management teams as being less confident about investing in their business over the next 12 months compared to last year.

Most analysts still say chief executives expect earnings to grow, but the percentage has dropped from 81 per cent to 58 per cent in the past year.

[3]According to Fidelity International's analysis of data compiled by Wind Information.

Chart 18: Management confidence in China is fragile

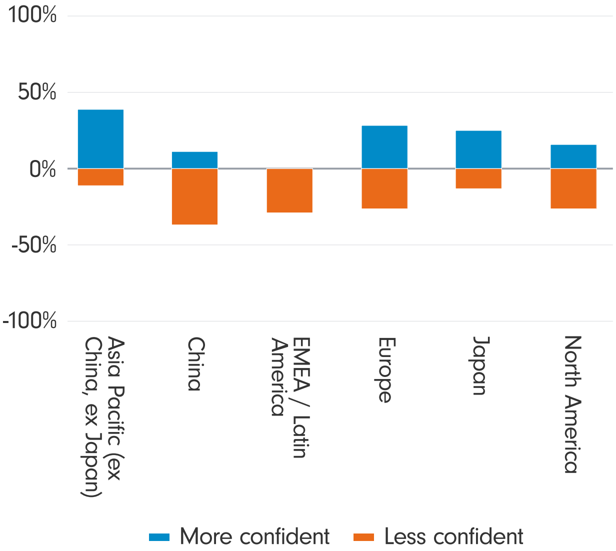


Chart shows percentage of analyst responses to the question: "How would you describe the confidence level of your companies' management teams to invest in their businesses over the next 12 months, compared to the previous 12 months?". Analysts who responded "No change" are not shown on the chart. Source: Fidelity International, January 2024.

Eric Zhu, a consumer discretionary analyst, says: "Management teams are still not confident about policy support and macro demand in 2024."

With slowing demand at home, many Chinese companies are looking beyond their own borders for growth. Leading firms in the automobile, machinery, and consumer sectors are venturing abroad, building factories or sales offices in the US, Europe, or Africa.

"Demand for electric vehicles and energy storage systems is slowing down," says auto analyst Eric Tse. "Companies aren't willing to invest in expansion for the domestic market, but they are active in investing in production facilities and sales channels abroad."

China's outlook may not be as bright as it was when the economy reopened a year ago. But further stimulus and a gradual adjustment by Chinese companies to a new economic backdrop should provide a year of stabilisation after a turbulent 2023.

Corporates face tougher ESG landscape

Companies continue to make progress towards their environmental, social, and governance goals. But it only gets harder from here.

Jenn-Hui Tan
Chief Sustainability Officer

Nina Flitman
Senior Investment Writer

Companies are entering a new phase in their approach to environmental, social, and governance (ESG) issues, responses to Fidelity's 2024 Analyst Survey show.

Analysts say that only about half of their companies are ready to meet their sustainability reporting requirements

"I think investors and lenders have been very lenient to date, understanding that establishing an ESG framework, setting up a committee, confirming goals and so on were the first steps, and that being 'early adopters' was seen as a positive," says Liz Brockway, a private credit analyst who covers the European chemicals sector. "Now the focus is moving to execution and delivery of these goals and promises."

From 2024, large companies in the European Union will need to track how their activities affect the environment and society in order to comply with the Corporate Sustainability Reporting Directive, and then start reporting this information annually in 2025. Meanwhile, global reporting standards developed by the International Sustainability Standards Board come into effect this year. Companies also face reporting requirements devised by the Task Force on Climate-related Financial Disclosures.

Many businesses still have a lot of work to do. Across all regions, analysts say that only about half of their companies are ready to meet their sustainability reporting requirements. This rises to around 60 per cent for analysts covering European firms, leaving many unprepared even in the most prepared region of the world.

Chart 19: Firms falling short on future reporting requirements

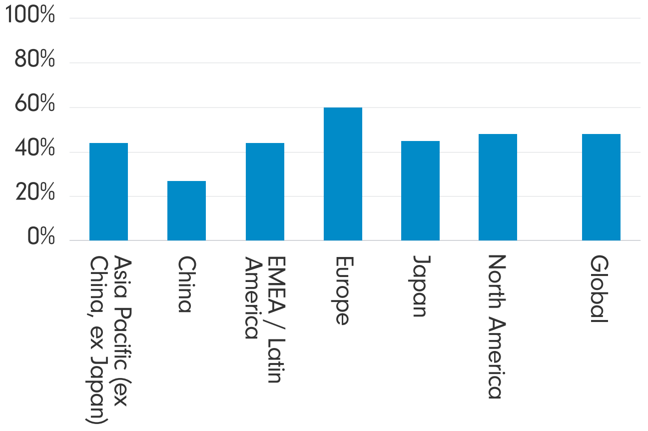


Chart shows average of responses to the question: "Starting in 2024, large companies around the world will have to fulfil new corporate sustainability reporting requirements (e.g. CSRD, ISSB, TCFD). What percentage of your companies would you estimate are ready to meet their respective reporting requirements?" Source: Fidelity International, January 2024. The survey was conducted in December 2023.

There is a risk that all these new rules are seen as moving the goalposts. Compliance will place a burden on companies. But there are advantages to developing a set of rules and reporting standards that will help prioritise companies' actions, a sentiment our analysts often encounter as part of their company engagements.

Currently, "investors have different ESG agendas and companies don't know which ESG areas to spend more time and money on," explains European retail analyst Serhat Birbilen. "It is hard for companies to focus on so many different ESG issues and they seem to be struggling in allocating the resources to the causes that generate the highest return for the environment and society."

Growing implementation

Despite these challenges, companies continue to make headway. Nearly a third of analysts say ESG implementation at their companies has improved from levels that were previously low. A further 28 per cent report improvement from already high levels, while 27 per cent say that ESG implementation was already high leaving little room for discernible improvement in 2024.

Chart 20: ESG implementation continues to improve

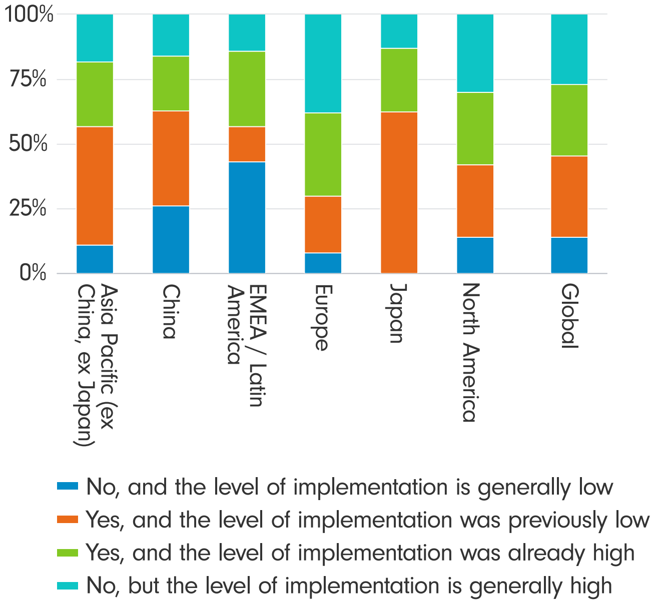


Chart shows percentage of analyst responses to the question: "Have you seen a growing emphasis among your companies to implement ESG policies in the last year?" Source: Fidelity International, January 2024.

Specific examples analysts cite include L'Oréal shifting away from its reliance on petrochemicals, with a target to ensure that 95 per cent of the chemicals used in its products come from plant-based ingredients (it is currently at around two thirds).

Elsewhere, Alexander Laing, a utilities analyst, notes: "Vestas has recently developed the first technology to break apart epoxy bonding resin for its wind turbine blades which means that these can be recycled for the first time. This has been a major issue for end-of-life in this industry until this point."

Changes in the energy sector

One of the biggest environmental challenges is also arguably the highest profile: reducing the emissions of the energy sector. Here too we see some evidence of progress, despite the often-depressing headlines.

"Five years ago, the oil and gas industry was quite dismissive in its approach to ESG, but companies have really changed their view," says Thomas Goldthorpe, an equity analyst covering energy in North America. "They're being proactive – proving willing to invest, willing to cut emissions, and willing to be a stakeholder at the table. They're serious about reducing their scope 1 and 2 emissions."

But while the industry may now be improving the efficiency of its exploration, production, and refining processes to reduce its scope 1 and 2 profile, that still leaves scope 3 emissions to be dealt with; those produced by the use of fossil fuels in society. These emissions are easily the most significant, and tackling them is not about dealing with the energy firms themselves but rather about focusing on where demand is coming from, ensuring that industry and society is decarbonising to reduce their reliance on energy produced by fossil fuels. There still needs to be much more progress in substituting fossil fuels for alternatives and Fidelity will continue to work with companies that are end-users (particularly those in hard-to-abate sectors such as heavy industry and transportation) to improve the efficiency of their processes.

Progress for firms in the energy industry itself remains a challenge. Last year, some high-profile companies rowed back on their commitments to tackle the intensity of their emissions or to increase their capex spend on sustainable processes. But there are some glimmers of hope that the looming energy transition is still driving some behaviour in this sector.

"It's no coincidence that ExxonMobil recently announced larger targets for its own clean energy capex," says Paul Gooden, another equity analyst covering North American energy firms. "For a Western oil major to say that around 25 per cent of its capex will be spent on low emissions projects by 2027 is remarkable. Around half of this will be spent on reducing the company's own emissions and half on reducing third-party emissions via biofuels, carbon capture and storage (CCS), and from hydrogen projects."

As part of this effort, ExxonMobil recently completed the takeover of Denbury, which owns and operates the biggest network of CO2 pipes in the US, increasing Exxon's CCS capabilities.

CCS appears to be a natural way for oil and gas firms to play a role in the energy transition - and not just because it provides a green argument for their continued operation.

"Being a utility is not what big oil does," says fixed income energy analyst Randy Cutler. "Big oil understands geology and that's what CCS is."

The Denbury deal was only part of a wave of M&A in the sector that looks set to continue. Every one of our energy analysts expects major strategic M&A in their sector this year.

Chart 21: Energy industry readies for strategic M&A

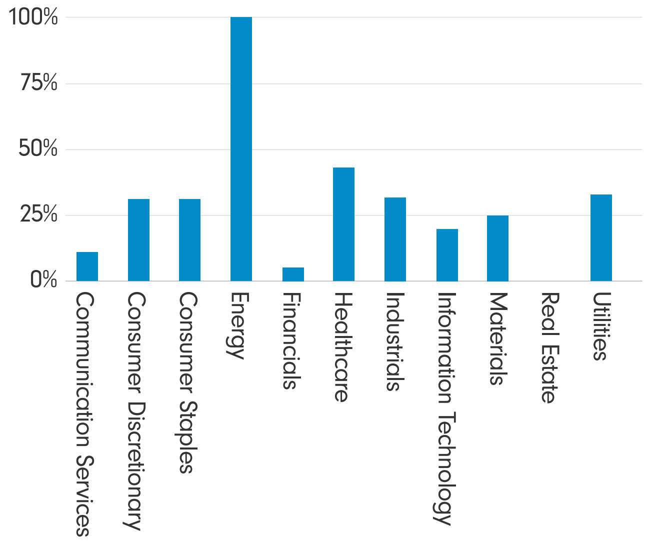


Chart shows responses to the question: "Where you are seeing M&A, what type is it? (Please select all that apply)" Chart shows percentage of analysts who expect to see major strategic M&A. Source: Fidelity International, January 2024.

To be clear, analysts do not believe that the main driver for this wave of M&A is sustainability, but rather valuations. Bigger companies on higher multiples are well placed to snap up cheaper rivals, looking to boost cashflow without adding to overall supply (which could push down energy prices).

> The energy transition puts a question mark over big projects that pay back over several decades

But the energy transition is also on everyone's mind. For large players it puts a question mark over big projects, which incur tens of billions of dollars in capex upfront, take several years to start generating cash, and then pay back over several decades. And for smaller companies, it's one more incentive to listen to suitors while their chequebooks are open.

"If you're a small company, what are the odds of surviving an energy transition?" asks Cutler. "It's better to sell now."

Companies staying the course

Perhaps the most compelling ESG finding in this year's survey is also the simplest. We asked analysts if the emphasis on sustainability among their companies has fallen in the last 12 months. Some analysts do say they have seen signs of ESG fatigue, while others suggest economic and geopolitical headwinds are drawing focus elsewhere.

Nonetheless, four out of five analysts say that no, the emphasis has not fallen among the companies they cover.

Chart 22: A firm focus - companies continue emphasis on ESG

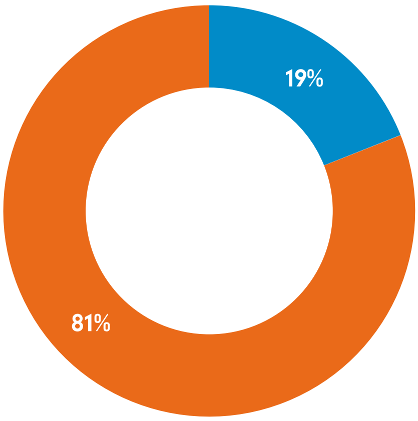


Chart shows percentage of analyst responses to the question: "Has the emphasis on ESG among your companies fallen over the last 12 months?" Source: Fidelity International, January 2024.

That's good news. Because it's not just reporting requirements that are likely to become more challenging in coming years. ESG is a key aspect of a company's societal license to operate and its ability to create long-term value for stakeholders. Businesses must be prepared to continue to tackle this increasingly demanding environment.

A company meeting every 10 minutes

The Fidelity Analyst Survey draws on the knowledge of our global research team in a way that helps you form a view on how businesses in different industries and regions will fare in the next few months. It's been doing that job for over a decade now and doing it well.

Ben Traynor
Senior Investment Writer

Fidelity analysts have more than 20,000 company meetings every year. Put another way, on any working day one of our analysts is speaking to a company's management every 10 minutes.

These aren't all Zoom calls, either. In the past year our analysts have gone to the deserts of Inner Mongolia, to the jungles of Borneo, to factories in Bangladesh, to countless boardrooms and conference halls and works sites, always seeking answers to the big question that never goes away: "What's happening?"

Because, as you may have found yourself, getting your boots (and if need be, your passport) dirty is often the only way to know what's really going on.

A decade of spotting trends early

The Analyst Survey is one way we draw on all that accumulated knowledge. Every December we ask our analysts around 80 questions that probe their knowledge of the companies and sectors they cover. Taken together, the responses paint a vivid picture of how different regions and sectors will fare in the year ahead - and beyond.

But that's only the start. We follow up on the most compelling responses, teasing out nuances and understanding context. We can do this to our heart's content because everyone who answers the survey works here. We don't have to take raw survey results at face value. We keep drilling.

> Over the past 10 years the survey has called booms in M&A, share buybacks, and dividend pay-outs

Our goal is to bring you a report you can easily digest, remember, and use as a guide. And Analyst Survey reports have often proved prescient. A decade ago, the 2014 survey correctly predicted that knowledge economy sectors like technology and pharmaceuticals would fare much better than sectors like energy and materials. The survey also warned about the wave of defaults among resource names in the high-yield bond market that arrived the following year. Over the past 10 years it has also called booms in M&A, share buybacks, and dividend pay-outs.

More recently, at the onset of the pandemic we began running shorter monthly and quarterly surveys to complement the annual. These include questions about companies' cost pressures. Fidelity analysts have shown a consistently strong understanding of how raw materials and other input costs are affecting their sectors; as well as when and how that is likely to change. Indeed, at a time when much of the inflation debate was focused on labour market dynamics, our analysts' responses about companies' non-labour costs proved to be a good early warning inflation signal.

Chart 23: An early warning of post-Covid inflation

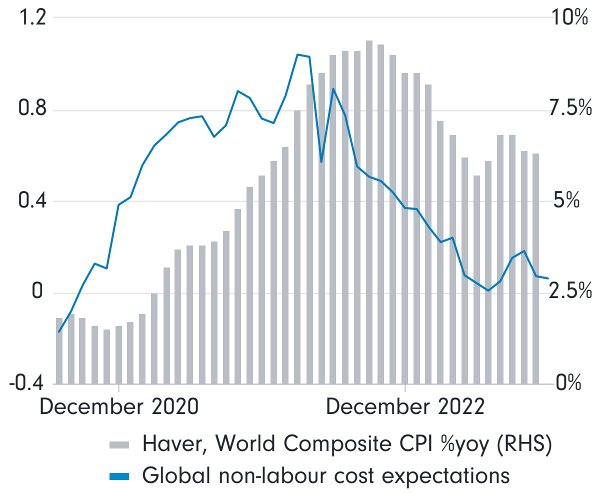


Chart shows World Composite CPI inflation against the weighted average of Analyst Survey responses to the question "What are your expectations for total non-labour costs at your companies over the next 6 months compared with current levels?" The responses "significant increase" and "significant decrease" receive a double weighting. Sources: Fidelity International Analyst Survey, Haver Analytics, January 2024.

Digging deeper, regression analysis shows a good relationship between the 6-month trend in analysts' responses to this question and the 6-month forward trend in changes to companies' non-labour costs. In other words, whenever our analysts grow more concerned about rising costs, the evidence shows it has tended to precede a period of rising cost inflation. And vice versa.

Chart 24: Seeing cost rises (and falls) before they come

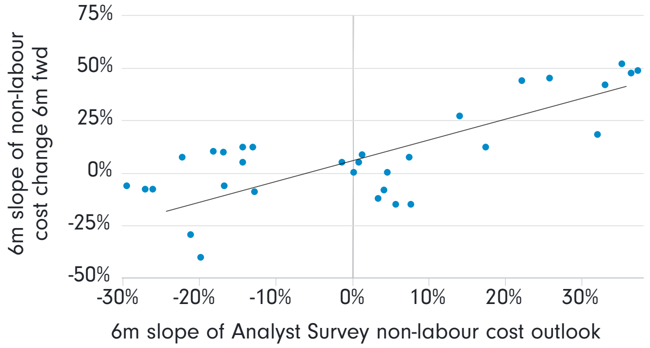


Chart shows the gradients of the line of best fit for 6 consecutive months of weighted averages of Analyst Survey responses to the question "What are your expectations for total non-labour costs at your companies over the next 6 months compared with current levels?" for the period July 2020 to July 2023, plotted against the gradients of the line of best fit for actual reported changes in companies' non-labour costs over the subsequent 6 months for the period December 2020 to December 2023. Sources: Fidelity International Analyst Survey, MSCI ACWI Aggregates, January 2024.

This makes sense, of course. Our analysts study their companies' supply chains, talk to their suppliers, obsess over industry minutiae, compare notes with other Fidelity analysts in the same and adjacent sectors, and, of course, have all those management meetings. It's their job to know what's happening with their companies' costs. And they do it well.

Cross-asset collaboration

Fidelity analysts are responsible for making individual security recommendations, which portfolio managers can then use to inform investment decisions for client funds. Our analysts talk to both listed and non-listed companies, and the global research team covers equities, fixed income, and private credit. That means that any analyst, covering any asset class, in any part of the world can talk to a colleague in one of our offices around the world and benefit from their expertise. They can then build up a detailed picture of a company's fundamentals.

And over the years, analysts' responses to survey questions have given valuable clues as to how those company fundamentals were about to change. Take the question about returns on capital in the next 12 months, which we have asked every year since 2014. We can compare analysts' responses to companies' actual reported ROC, proxied by MSCI ACWI aggregates, as of 31 December of every year up to 2022 (the 2023 numbers for comparison won't be available from company reports for another few weeks yet). That gives us nine years in total. Averaged together, our analysts' responses at the start of the year have correctly predicted the direction of ROC by the end of it in eight of those nine years.

Chart 25: Will ROC go up or down next year? And did it?

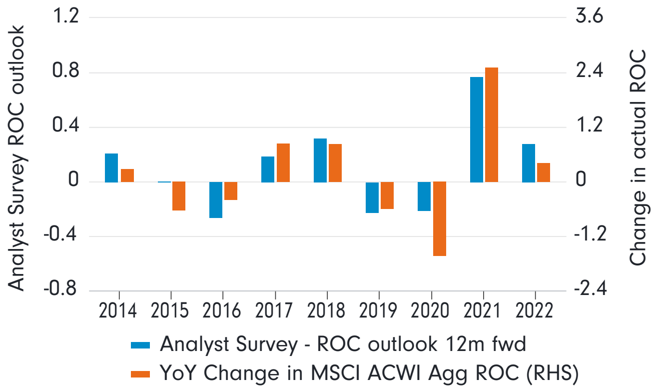


Chart shows weighted average of responses to the question "What is the outlook for overall returns on capital for your companies for the next 12 months?" plotted against the year-on-year change in actual reported returns on capital as of 31 December of that year. NB 2022 is the most recent year for which actual reported ROC data are currently available. Sources: Fidelity International Analyst Survey, MSCI ACWI Aggregates, January 2024.

It's a small sample size, but it shows the value of blocking out the noise and zeroing in on what matters most: the fundamentals.

Giving you the knowledge that top-down research misses

It is this focus on the nuts and bolts of individual companies that gives the Analyst Survey its power. This is not your usual 30,000 feet overview of economic conditions drawn from public data and official indicators. Our Analyst Survey is built from the ground up, drawing entirely on the knowledge of in-house experts.

We use the survey findings to inform our internal discussions, such as those at our Cross Asset Investment Forum, where we find the survey output often provides a healthy challenge to our other research, and at other times a confirmatory signal from a different perspective. We hope you too will find the survey a useful companion to your own research.

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Important Information

ED24-017

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