

Fidelity Connects

The latest on global consumer spending

Aneta Wynimko, Portfolio Manager

Pamela Ritchie, Host

Announcer: Hello and welcome to Fidelity Connects – a Fidelity Investments Canada podcast – connecting you to the world of investing and helping you stay ahead.

Aneta Wynimko, Portfolio Manager of Fidelity Global Consumer Industries Fund, joins us today for a timely discussion on global consumer spending at a time when global economic activity may be slowing.

Aneta, who is based in London, shares that trends are showing an upcoming weakness in consumption, especially in Europe. This means investing in consumers could be complex, and it is very likely consumption in Asia will continue to grow.

Also today, with host Pamela Ritchie, Aneta shares that companies with strong brand and innovation will be successful, and she unpacks habits of Gen Z consumers, noting they place a large emphasis on sustainability and the value of their purchases.

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Pamela Ritchie: Great to see you again. How are you? Your garden looks lovely.

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Aneta Wynimko: Thank you, Pamela. Nice to see you as well and hello, everyone.

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Pamela Ritchie: We're very glad that you could join us here today. I wonder if we begin with sort of what is ... it does seem to be what everyone is talking about ... is sort of the energy story and it goes to the health of the consumer and the disposable income that is there. Can you sort of lay out for us? I think we know the general narrative but what it means when you look at it very carefully through the lens of consumer demand.

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Aneta Wynimko: Obviously, this is the big issue and the big problem that that we are facing going into winter and obviously, very much so in Europe, UK as well. There has been a lot of coverage by the news agencies and media of this impending crisis. I think consumers are very aware but maybe not necessarily yet taking measures in terms of saving and maybe cutting some of the spending that they need to be cutting.

On the other hand, we also have governments stepping in. I suppose people might have seen the latest from the new Prime Minister in the UK. The first thing she has done was introducing a cap that makes it much less painful than it could have been. We've seen similar measures taken in Germany. It is an unprecedented time and a bit like with COVID in unprecedented times the governments tend to step in and try and help. I think that's going to be the pattern of this winter but obviously quite, quite a difficult situation for the consumers.

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Pamela Ritchie: It is, and for the central banks but we're not going to talk about that so much right now. One theme that gets woven into ... it is part of the energy story, it's really the energy transition story, a year ago we were talking about sort of the stickiness of demand for companies who follow ESG fundamentals, for investors who want to make sure that they're investing with an ESG lens. How does that work, ultimately, with so much focus on just getting what we would call more traditional sources of energy through the pipelines, literally, at this moment?

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Aneta Wynimko: I know, it's very topical. Actually, only yesterday, I had the pleasure to speak to the CEO of Nestlé, Mark Schneider. Obviously, they, as a company, have a very robust agenda of moving towards sustainable manufacturing, sourcing, logistics, anything, but he's also aware that the situation for the consumers is going to be quite hard later this year and he's trying to balance all those important projects that he has ongoing with the need to invest in pricing as well because obviously what companies don't want end up doing is pricing themselves out of the affordability of consumers. It's a very delicate balancing act where you keep the initiatives going, maybe you slow them down a bit because, as he said, the planet is not going to wait. We have very big issues that need to be solved but at the same time, we are also facing a tough winter. I think companies which are thinking and kind of planning ahead, they all have these initiatives in place, how to balance this near-term with the long-term projects that definitely need to be implemented.

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Pamela Ritchie: It's really fascinating. I wonder if the issue ... these are all big chunks and we'll sort of spread out to the consumer in a second, but actually just the story of currencies and how we're watching different currencies. How does that also affect who is willing to buy, who's willing to spend, depending on what currency, in a global marketplace? Are you watching that as well?

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Aneta Wynimko: Yes, of course. Actually, the Canadians are in good shape.

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Pamela Ritchie: We're doing relatively well.

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Aneta Wynimko: In a good shape. I am probably in a country where the currency has completely collapsed. So obviously it has impact on how people decide in terms of their holidays. In Europe, we are seeing a boom of travel coming from North America. When you go around in Paris or Milan, there is so many tourists coming from the U.S., also from Canada. Actually, prices, especially of luxury goods, tends to be quite a bit lower, 10, 15%, and then you can get back your VAT. So those people who decided to come here also are spending. You have a group of companies that actually benefit from that.

But then, obviously, there's a whole lot of European consumers that cannot think of travelling to the U.S. or Canada because it has become very expensive. So yes, the currency movements have been massive when one looks year-on-year. It's also quite unprecedented. It puts the global consumption even more so on the shoulders of the American consumers who have been spending, who continue to spend and who are also benefiting the European companies by doing so.

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Pamela Ritchie: I'm very curious. I know pre-COVID you would make many trips to Asia, to China to check out opportunities for the fund, ultimately, there. How do you look at the consumer in China right now and also some of the companies that are there right now? Is it actually all priced in and therefore looking like there's a glimmer of hope or not?

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Aneta Wynimko: Again, case by case, China is going through a difficult, hopefully, last leg of COVID. It's taking very long for the government to get over all these medical issues that we managed to do. At the same time, there's also underlying economic weakness partially driven by the weakness in the property market. So, there's an overall weakness in the demand which is aggravated by lockdowns. But at the same time, the propensity of the Chinese consumers, especially the younger consumers, Generation Z, to spend is very high. Whenever they have the opportunity of the brands that they love, they do want to have the latest, the best product.

Generalizing with consumer is always very hard because of this huge population and many people in very different situations. There are segments of the space that are doing well and there are some other segments, especially exposed to the lower income consumers that are struggling. That is a pattern that we are seeing in Europe and in the U.S. as well.

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Pamela Ritchie: Let's talk about that segment of the market and then maybe we'll look at it sort of by age also. For those companies catering to a lower income customer or customers that are no longer willing to pay high prices, what do you see in there? What can you give as an example of what might be of interest to investors to take a look at?

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Aneta Wynimko: Those companies, we can take Walmart for example, huge U.S. retailer that has suffered and had a few profit warnings, partially self-imposed because they have gotten the inventory wrong. They ordered the wrong things and those wrong things arrived at the wrong time. So partially it's self-imposed. But there's also an element of them trying to stay price competitive. This is very important because, for example, what I am seeing in the UK, the [indecipherable], the [indecipherable] of this world are really struggling because they have the discounters, the likes of Lidl or Aldi, the German discounters that are taking market share in a very aggressive way.

So it's really an environment where the companies have to be very granular and think about the end consumer that they serve and make sure that they don't lose them because, obviously, winning back a business of consumers and loyalty is very hard. So, everyone is in that position and if you are really selling to the low-end consumer, it's a difficult situation because you need to stay price competitive and you cannot really fully take advantage of the inflation that we are seeing.

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Pamela Ritchie: On the other end of the spectrum, the luxury side of things which often people will say even in tough times will hold up, it tends to be recession-proof or by some accounts is. How is the luxury market looking right now? Has it shifted globally sort of where the luxury brands do best?

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Aneta Wynimko: It has shifted in the last few years. In a way, luckily, for the luxury goods companies the attention has shifted from China to the U.S. The U.S. has become a much bigger market and a much *[inaudible]* market. Today we talk about new store openings *[indecipherable]*, in all sorts of places that before they wouldn't even think about going, because the consumption is there because the local consumers that have made money, whether it's in gas or some other commodity place *[indecipherable]* but the fact that a lot of wealth creation in the U.S. has spread out through the country is benefiting the sector and the U.S. is really the strongest market or one of the strongest markets still. The momentum seems to be still there and it's kind of coming to Europe as well for travel.

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Another geography that is doing extremely well is Middle East. They're obviously benefiting from price of oil but also benefiting from the fact that people, whether Russians or Chinese or people from many countries that might be afraid of the environment in Europe in terms of regulation and the security of their money, they feel very comfortable in places like Dubai. So, yes, with luxury, there's always something happening in the world that is offsetting the pains in the other parts of the world and that's exactly what we're seeing.

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Pamela Ritchie: That's fascinating. I lived in the Middle East and they have a lot of malls in Dubai. Lot of places to buy luxury. It's great shopping. Very expensive shopping, actually.

But in the U. S., just for a moment, because I was curious about some of that coming back to the U.S., as you say, to offset China's lockdowns, essentially. Is it everyone heading back to New York City, for instance, or they're going to L.A.? Everyone's going back within the U.S. to sort of the big shopping centres?

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Aneta Wynimko: Well, New York is special. I actually went there in the summer and I had some meetings and the traffic on Fifth Avenue is back. They were quite pleased, and above what they expected. So, I think people go there just to go and spend time. I think also companies like Airbnb make it so much more exciting to go all over the place and experience and see and not just end up being in New York. So, I think this *[indecipherable]* is still to be happening. I think the travel within the U.S. is actually very strong and the hotels are benefiting from that as well. The travel outside of the U.S. has also picked up. I think this is something that has obviously flourished post lockdowns. The big question is, is that going to continue?

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Pamela Ritchie: That's so interesting. It's different parts of the U.S. as well as the big centres. I mean, it's sort of somewhat spread out, is it?

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Aneta Wynimko: Yeah, definitely.

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Pamela Ritchie: Going back to Generation Z or Z, just depends on how you look at it. You said there's sort of a propensity to spend but in particular ways and specific ways. I always think it's interesting to ask your opinion about this. I think we've asked before that actually there's often a propensity to spend in more sustainable ways. Is that still the case? Are there other areas of interest to you within sort of the mindset, ultimately, of how Gen Z and Z wants to spend?

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Aneta Wymimko: I think the way they want to spend is, luckily, different to the way maybe we've grown up spending. They really think about sustainability and they also think in terms of the value of what they buy, can they resell, so there is an element of that. Sometimes they buy because they are planning to sell the product thinking that it has high resale value. I think that element is quite important but also, today we, obviously, can get a lot of information digitally and very easily accessible and the whole social media, TikTok. It makes things that are popular very popular very quickly. We see lots of hot things that come out and maybe they stay hot for a while and then something else comes up. Obviously, Generation Z is a big part of that but I think the element of how the products are made and the tech behind the products and the way they are designed, I think is more and more important.

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Pamela Ritchie: What's an example of that type of product? You're talking about the tech, the way the technology is designed. What's an example?

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Aneta Wymimko: Company that has been very good at coming up, obviously, we can talk about Apple but that's an obvious one. Another one which might be obvious to you is Lululemon. Just to give you an idea, they have come up with a collection of shoes for women, running shoes, shoes to exercise. What's special about that? Well, they have spent three or four years designing those shoes and they have specifically designed it for the shape of women's feet. A lot of bigger brands, the athletic brands, they are much more focused on men and men's sports and they basically take the men's shoe and adjust it for women. It's a very different design and research process that ends up in a very different product. The launch of the shoes has been very successful. They haven't made enough of them, especially the ones in vibrant colours that they're putting out. It's just an example of one of the products. They have the whole line-up of products which are functional. So we all exercise and there is [crosstalk]...

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Pamela Ritchie: We all should exercise.

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Aneta Wymimko: We all should but we also all want to look good when we do so.

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Pamela Ritchie: Of even not when we're exercising. Yes.

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Aneta Wynimko: Even more so, actually. For the autumn they have a line-up of products which have little fluorescent patches. If you go running at night, I don't know, a car passing by will see you. But also the kind of coolness. So little things like that, it takes a lot of design and planning and thinking to come up with. And I think someone who gets that and comes up consistently, I think that Generation Z is all over it.

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Pamela Ritchie: Men and women are going back to work. I've noticed, I'm talking more about seeing a few men here and there wearing ties, wondering if they're going back with the suit look. Are there any traditional elements that are sort of on that side of things that are of interest or have things changed forever? I'm still curious about that.

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Aneta Wynimko: I think the traditional suit, tie look we will see but I think it really is going to look [*indecipherable*] someone who looks like that is either very traditional or eccentric. I think the mainstream look is already much more relaxed, maybe still a tailored jacket and still a nice tailored, maybe custom-made shirt but maybe not necessarily buttoned up with a tie. I think the opportunity for styling dressing is even bigger for men now than before because you can kind of combine colours and textiles and be much more creative a bit the way women have been dressing. I think that that actually is an opportunity, quite a big opportunity, in menswear.

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Pamela Ritchie: Shoes as well for men?

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Aneta Wynimko: Yes. There is the whole group of companies, some of the luxury, for example, Zegna, they are trying to revive the brand and make it much more younger and appealing to younger people. The beginning of the revival started with the shoes. They came out with a show called Triple Stitch that has been ... some of the people like Jamie Dimon from JP Morgan was seen in, but also lots of younger, cooler people... not that Jamie Dimon is not cool ... the shoe is also an opportunity to create iconic products and there are many men that buy them in all kinds of colours and the only shoe they wear. So yeah, I think it's an opportunity in this change of how people dress.

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Pamela Ritchie: I know that in the past we've talked about food and beverage and, ultimately, that side of things. We hear just an awful lot about, obviously, how expensive food is for everyone to buy, how do restaurants deal with that. Do you still look to food and beverage as places to invest or is it actually a pretty tricky spot right now?

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Aneta Wynimko: I have investments in food and in beverage. In food, it's such a fragmented market. The brands that operate are actually quite small in terms of their market share and it is a market where the opportunity for innovation, it's interesting. I had a meeting yesterday with the CEO of DSM and they've done a lot of research in terms of how to make mixtures for cows so that cows in different geographies, different types of cows benefit in terms of their metabolic system. I'm thinking there is more research done about that for cows than for humans. I think the opportunity...

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Pamela Ritchie: Someone should get on that, someone needs to get on that.

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Aneta Wymimko: Actually, Nestlé is on that already. They are doing a lot in terms of the metabolic cows and the things that they can do. I think food is a very interesting category. It's not very easy to invest because a lot of the traditional, especially the U.S.-based companies, they are really the packaged kind of mass-produced food that is really not what we should be eating at all and maybe that's okay in the near time when consumer is under pressure but long term I think we will completely move away from that and there will be much more space for the science-based personalized nutrition than people like Nestlé are thinking about.

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Pamela Ritchie: What about the beverage side of things? Well, I mean, Nestlé makes hot chocolate, of course, but I meant other kinds of beverages.

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Aneta Wymimko: What happens in the beverage space during COVID kind of continues. People have learned to be mixers, how to mix and how to make cocktails. I think they trained their palate in terms of drinking better, hopefully drinking a little bit less. The volumes point to actually, the volumes are quite strong. I think people are probably drinking more overall. The consumption continues because everyone still entertains and the expectations and abilities have improved and people are going out and drinking. The spirits market, especially in the U.S., has been quite strong. I've been on holiday in the U.S. trying to entertain some guests and I couldn't find Aperol. It was all sold out. I think that continues but, obviously, the question is as consumers get squeezed going into autumn, will they still afford this little pleasure of having a nice cocktail at home, or will they be cutting it obviously as a discretionary item?

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Pamela Ritchie: Yeah. Well, yes, yes. Coffee, is that's still an area of interest or, in fact, has that ... I don't know, how does that change as we come out of the pandemic? Do we drink more or less or we just go out for it, I guess, more?

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Aneta Wymimko: Yeah. We go back to Starbucks by the sound of it. I've been, for a long time, a fan of the category and trying to invest in it 'cause I think coffee is replacing ... it's the modern Coca-Cola. It really is a way ... and Generation Z is all over it as well.

Actually, this week Starbucks has an Investor Day, so I'm very fresh in terms of data about coffee consumption in the U.S. For them, 70% of coffee consumption in the U.S. is cold brew. It's not the hot drink but is the cold coffee. I remember when I went to the Investor Day probably in 2018 in New York, when they just introduced that and there was lots of skepticism, like who is going to drink cold coffee? What's the point? Today, the business has completely shifted. They really created a completely new category. So, coffee on the go, coffee is, I think, a category where ... and again, the Generation Z is a very big customer base.

What Starbucks also has been getting right with all the issues that they actually had that made Howard Schultz come back again, but what they got right was innovation and the way they went into the pink, orange, all kind of colours, drinks that look amazing in social media. I think coffee is a great category and the way I do have exposure is obviously Starbucks but also Nestlé has quite a strong business in coffee and I think it will continue to be.

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Pamela Ritchie: All the fruit from those drinks get stuck in the straw but they taste really good and they look beautiful. There's an issue on that. A little bit of a thumb up then when we look at, ultimately, how spending in the consumer is going to go and how you look at going to different areas of the consumer base based on how you feel. Just sort of remind investors what avenues need to be taken by you in terms of positioning.

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Aneta Wymiko: Obviously, investing in consumer is not easy these days but I think it has never been so maybe it's just part of the package. I think what we are going to see is, obviously, some weakness in consumption, especially in Europe. That's unavoidable. There's already a bit of a slowdown ongoing in the U.S. and it's, obviously, coming from a high base. We are going to probably experience that as well. At the same time, it is also quite possible that we are going to see some improvement, and maybe acceleration, in consumption in Asia. We have the Party Congress happening in October which is a very important point because, I think, once the political situation is clear, hopefully the government starts acting in a more rational way and thinking more about the economy but we don't know.

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My expectation is that the companies that have very strong brands, innovation and they are basically coming up with products that will excite the consumers, they should be okay. Consumption as a category is huge: it's 70, 80% of GDP. So obviously, there's lots of space and scope for sales. There's also danger of disappointment because it's not an easy environment. But I think there is group of companies with the execution, innovation are really very strong and obviously multiples on everything in the market, but also on some of those high-quality companies have come down substantially. We might be in a unique opportunity to really buy them and really own them for a very long time because they really are quite good with what they're doing.

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Pamela Ritchie: It's fascinating. It's fascinating to watch how you are manoeuvring this and your comments about China. I think so many people are wondering about that Congress and what it will mean. Aneta Wymiko, I want to thank you for joining us on Fidelity Connects. It's great to see you, as always. All the best.

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Aneta Wymiko: Pleasure as always. Thank you.

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