## The Upside

**Lessons learned throughout two decades of investing**

**Dan Dupont,** Portfolio Manager

**Emily Anonuevo,** Host

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

Host Emily Anonuevo is joined today by portfolio manager Dan Dupont. Dan manages Fidelity Canadian Large-Cap Fund, co-manages Fidelity NorthStar Fund, as well as several other funds and private pools.

Dan reflects on how he first got into investing, which sparked from growing up on a farm and analyzing the farm's accounting. This led to analyzing businesses and their finances, and ultimately investing in companies, which he has been doing now at Fidelity for 20 years.

Dan shares his investment approach and his rigorous focus on protecting capital, being patient, and not trying to predict the unpredictable.

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**Emily Anonuevo:** It's been over 15 months since the world was rocked by what will go down as one of the worst pandemics in history. COVID-19 tested the resilience of people, brought communities together in spectacular ways and also shook our economies and markets to the core. For investors, we held on tightly to those who could help us weather the market cycle storm. And our guest today knows all about staying the course and investing with passion, even through the toughest of times. So, Dan, I'd like to begin the show and get to know more about you and your personal story. You started with Fidelity Investments twenty years ago. You started as a research analyst and then as a portfolio manager. So, tell us what actually sparked your interest in investing?

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**Dan Dupont:** I have a little bit of a different story. I was raised on a dairy farm in the rural part of Canada, and learned the hard way that sometimes things can be a little volatile. You know, we have seasons. You have seasons that are better. Some seasons are not as good. Cash flow's very important. And what's distinct about businesses like agriculture, and there's a lot of businesses like that and I'm sure a lot of people will relate, is that there's not a lot of really positive surprises. What you're looking for is just a smooth day, smooth functioning of your business, and to be able to go home and have a nice dinner at the end of the day. And so, you're going to be really satisfied on days where actually nothing special happens.

And frankly, that's stayed a little bit with me throughout the years. And now that I'm managing other people's money, I try to make sure that there's not a lot of too many bad surprises, just like we tried to do on the farm.

I'd say I love businesses. I loved analyzing the farm, the investments, the books, the accounting from a very young age, and then ultimately realized that you could actually do that for a living: analyzing businesses, looking at the numbers, meeting with people who are managing these businesses and investing on people's behalf. So that's why I got interested and frankly, got my dream job out of university at Fidelity, where I worked for 10 years in Boston and now since then in back to Canada.

But that's the background, you know, reading about Warren Buffett, reading about Peter Lynch, who was a legendary portfolio manager at Fidelity, wrote a few books that I read eagerly in my university days. And that's really when I decided, OK, this is exactly what I want to do. And then this dream job appeared and I got it.

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**Emily Anonuevo:** That's fantastic, and you're obviously doing something right, being with the firm for over 20 years. What sort of keeps you going and exciting day in and day out?

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**Dan Dupont:** Frankly, I'd say it's just knowing that I'm managing people's money for a lot of very important events and a lot of important things in the future, whether college or retirement. And on the flip side, also day-to-day, not knowing what my day is going to be like. Waking up in the morning, sometimes there's a news event, something big, a big merger and acquisition, a company that just disappoints investors significantly or meeting with these companies on a day-to-day basis, even if there's nothing new or exciting with their business, just understanding more and more of their businesses.

And again, I'm much more tilted to businesses that are more fundamental to the economy, that are a little easier to understand. My funds have slightly less technology. They'll have a bit more staples, a bit more telecom. And so, I really like digging into those numbers. I'm very much of a numbers guy and it's been very useful in this job.

Now, obviously everybody in investments has their own style. And I'd say my style is very different. So, on a day-to-day basis, I try to think about, and that really gets me going, thinking about what could go wrong with every investment we have, and preparing our portfolios for any adversity that could come our way. And, let's be honest, there hasn't been as much as I would have liked in the last 12 years in the stock market. The last year has been very volatile. But frankly, the rebound has been very quick. So, I love to always be ready for anything. I love when there's adversity. Last March was a lot of fun for me, did a lot of deployment of some liquidity that I had in the funds that I keep on the side, sometimes when I can't find anything else to buy. But day in, day out, it's always...for me, I've told a lot of people this, I'm really lucky to have a passion in life that is actually my job. So, I never feel like I'm working. So, I'm very lucky in that sense. But I also really like the idea that this is all for a purpose, for people to save money for something important in the future.

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**Emily Anonuevo:** Absolutely. So, you explained a bit there about your investment process. You talked about how you're a numbers guy. You like the adversity. Can you elaborate more just on the last year, Dan, obviously the COVID-19 pandemic rocking our world. So, what keeps you focused during those tough times? What investing principles do you stick to? Did that whole time faze you like you said? You know, we've rebounded quickly, but how did you stick through that that last year?

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**Dan Dupont:** No, it didn't faze me. These are the times when I get really, really happy to come to work. For me, this is kind of the periods where I tap dance to work, because there's so many opportunities, there's a lot of things moving. And the way I invest is a very defensive way. And, you know, over the years when there's not much happening, we invest in bread-and-butter companies and the companies that are stable that give us decent dividend, decent growth. But when there's turmoil, my style really tends to shine because a) it's more defensive, b) sometimes we'll have a little bit of liquidity on the side, so we'll keep a little bit of cash inside the fund. So, when markets recede like they did last March, it's very easy for me to deploy that, turn that cash into something that's really, really cheap out there. And frankly, things rebounded very quickly. I would have been ready for something a little bit more dramatic. But, things rebounded and we took advantage of it.

But I'd say generally my investment style is one that tries to look for all the risks. And it's kind of a dying breed out there because the stock market has been fairly benign. Again, rebounds have been quick. A quick rebound in '18 and a quick rebound in 2020 from the pandemic. It was very stressful, but in the end, governments and central banks threw a lot of money at the system. And we only had to stress for a few weeks and then things really started to mend themselves. So, we had an accelerated cycle, if you will. So that was kind of fun in a way for us, because we had seven, eight years of a typical economic cycle jammed into less than a year, because the government threw so much money after what was a little weaker—some of the areas that were a little weaker—which found a lot of room in the stock market. A lot of stock market companies benefited from a lot of the programs.

So, if we look forward for the next five, 10, I think that's where things are important to focus on. Yes, the last year was really volatile and was interesting and we took advantage of that. But I think the people listening, hopefully they interact with their advisors a lot and try to position themselves for the future and for any adversity that could come our way.

The stock market has been a place where there's been volatility, but the returns have been really good over the last 12 years, even 20 years, if you will, mostly in the U.S. So, what now? is the question. And again, this dying breed of investors, like myself, who are focusing on downside, first and foremost, sometimes are a little overlooked when the market seems to be either just really strong or going up and to the right very slowly but surely or when we have corrections, but they rebound very, very quickly. Sometimes adversity sticks around a little bit longer. We've had two 50% corrections in the last 20+ years: in 2001, 2002, and one was in 2008. And one of the best known investors, Warren Buffett, does say that if you are not ready for a 50% correction, 5-0, in the stock market, you should not be invested in the stock market. And I tend to agree with that, but I want to make sure that people can survive any correction that we would have.

So being a very defensive investor, one of my goals is to have my funds correct less than the market would if we had some real adversity. So, I typically tell our advisors and clients that I would like for our downside in Fidelity Canadian Large-Cap Fund, for example, to be about half what market corrections are doing. So, if the market goes down 20%, I'd like to be down 10% or less. And if the market goes down 50 in a significant event, I'd be I'd like to be down 25 or less. And there's a lot of benefits to being positioned that way, if you think long term enough.

First of all, the compounding is way easier once you're down from $100 to $75 versus $100 to 50, you already 50% ahead. That's, that's a big advantage. But there's also a huge psychological advantage because if you're only down 25, when everybody else around you is down 50%. And it's easy for us to discuss it here, but frankly, when it's your money, it's your retirement money, it's college money, it's money you've saved for just in case you get sicker over time if you have kind of a health issue. It's very, very important things. And you get stressed out when you lose a lot of it and maybe you'll panic at the wrong time.

So, I'm trying to help investors get the benefit of equity-type return. So, investing in the stock market, that tends to give you better returns over time than bonds, because as we know, interest rates are really, really low or certificates of deposit in banks. So, we want that high return and I've delivered that high return in Canadian Large-Cap Fund, but with a lot less volatility. And again, it's been it's been beneficial for the last 10 years while I've been managing the fund. But we also need to look forward. And what if, what if the market becomes volatile? What if we have a recession at some point next year or two, which is definitely not impossible, because, again, if we go back to the concept that this last year could have been a full economic cycle jammed into one year because of everything that happened and we've seen in the stock market. We've seen early-cycle type companies go up and then mid-cycle companies go up and then late-cycle companies have really gone up in the last three or six months. These are kind of technical issues, but it's really telling you that it's possible that in the next two to three years we could see a pretty decent recession.

We don't know because of the overhang of everything that's been thrown at the system, all this money that's been thrown everywhere, including real estate. I'm sure people are aware of how fast real estate prices have gone up, but these could revert, they could stop or they could revert and it could create some weakness in a lot of spots in the economy.

So, with my funds, people are ready for anything. I try not to compromise on returns over the last 10 years while I was managing it, but with a lot less volatility. And if we ever have adversity, I think it'll be extremely beneficial to be positioned the way we are.

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**Emily Anonuevo:** What are your thoughts on currency and does it play a role in your investment process? And then thoughts on banking and financial services.

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**Dan Dupont:** Well, they're fairly technical questions, but I'll try to make it simple.

Currencies are incredibly difficult to predict. I try to be really humble about what I do. And I'm really honest saying that some variables I don't try to predict because a) they're very, very difficult to predict and ii) the impact that these variables have on stocks themselves. Sometimes they don't even go the direction you think. If you tried to predict the Trump election a few years ago and then you were correct, the stock market, when the exact opposite of what everybody thought would have happened.

So, when it comes to currencies, it's the same. I tend to make sure that we are not hurt too much. And when it gets to an extreme level, then I may tilt the other way. So, if the Canadian dollar gets a little too weak, then it's probably a sign that I should be adding a few Canadian investments or adding some Canadian dollar exposure and vice versa.

If the Canadian dollar is getting a little strong, which, you know, currently it's a tad strong, so I would be starting to tilt a little bit against the Canadian dollar. Nothing to hurt us too much. But I think at the margin, it's one of the right steps to do.

And there's an additional technical reason why you would do that. You would tilt against the Canadian dollar, because the Canadian dollar in the global context is a risk-on currency. It's a currency that tends to go up when things are going well. It tends to go down when things are going badly. So, we saw it during the beginning of COVID, the Canadian dollar just started plummeting. It started plummeting in '08, started plummeting in '02. Whenever there's adversity in the world, the Canadian dollar is typically one of the first things to get wobbly. So, I keep that in mind as well when we look at that.

Financial services, as I said, Canadian real estate prices have been incredibly strong. The indebtedness of Canadian consumers is just frankly unbelievably high. And it could stay that way for a while. But I think at some point it has to at least level out, which will not be fantastic for profits, although right now profitability of banks is just amazing, simply because they took a lot of losses in the last year, anticipating that things would get really bad, but then the government and central bank really just threw so much money at the system that everything went well.

Consumers have on average, a lot of cash. Credit card balances are actually low for their tastes. They'd love for people to use their credit cards even more. So, to me, this as a person that always thinks about, OK, but what could go wrong here? This is an environment where profitability is fantastic for Canadian financial services, but I'm a little worried two or three years down the road, and mostly also because they benefited from the steepening of the yield curve. Again, very technical, but long rates went up and short rates are stuck at zero, so that we call that a steepening yield curve. And that typically is good for banks because they lend money at a much longer term than they have in their deposits from people. So, if you only have to give 0.1% per year on a deposit, but you can lend money to people at 4, 5, 6%, it's really good for you. So that's why a steepening is good and has been good for them. So financial services companies have been doing really well over the last six months, ever since the vaccine came out. But I'm a little bit more wary right now about them.

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**Emily Anonuevo:** What are your thoughts on inflation and does that affect your positioning?

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**Dan Dupont:** I'd say people are surprised because I've been saying that a little recently. I'm typically the person that worries the most about factors that could go wrong. And I am worried about inflation generally, but I say at this point, I seem to be less worried about inflation than the average person. It's everywhere in the news. Everybody's trying to think about how can we protect our portfolio against inflation because the numbers are really bad. They're coming out as being pretty high, depending on who you listen to, you know, 4, 5, 6 %, a lot of bottlenecks, a lot of supply issues everywhere. So, for the time being, the numbers look really, really bad. And central banks are saying it's probably in transition until we get to some more moderate levels. And people are kind of scoffing at that.

But I think in the end, there's just so much debt everywhere that unless we devalue the currency significantly against hard assets, I don't see inflation staying really, really high as a main point. But as I said earlier, inflation is one of those variables I'm not trying to predict too much. So, we'll try to position ourselves not to be hurt and be ready to move if inflation really sticks at a higher price, higher level.

But frankly, I'd say right now, one of the worries that nobody has on their mind is the opposite. What if inflation basically starts dropping fast? So, I always try to think about, I guess invert, always invert is the phrase. I always try to think about, OK, if everybody's thinking about one risk, what is the other risk we're not thinking about? So, yes, I am worried about inflation. The numbers look horrible and they're going to keep looking horrible for at least another quarter, two, maybe three. But I'm trying to think about what happens after that. What after the debt binge we've been on? What if the economy slows down a tiny bit? What is that? What is going to result from that?

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**Emily Anonuevo:** Fantastic questions to be asking and really interesting to get an explanation of how you really think in your investment process. Dan, you mentioned the conversations you have with financial advisors. And we know advisors add so much value in terms of helping investors stay focused and disciplined through the market ups and downs. What's the advantage there and how do you yourself navigate through all the market noise?

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**Dan Dupont:** I think the relationship between the advisors and clients as it relates to my funds is incredibly important because I manage money differently for the type of client that he's always asking their neighbours how well they're doing and their investments and are trying to replicate that and chasing returns. It's absolutely not for them. And I love that advisors are there. They're the front line for me to repeat that, no, if Dan has had a good year, it's not because he's taken risk. It's because we looked at some very cheap stocks that had very little downside and a bunch of them went up.

But the reason to own a fund like Fidelity Canadian Large-Cap Fun is for downside protection and compounding through losing less over time. And the math works beautifully. You just have to have a longer-term horizon in mind. And the advisor is perfectly positioned to just reinforce that and to show in graphs and articulate and think about slightly longer term, because it's easy once market's doing well to forget about the tougher periods. The advisors are there to help reinforce that we need to be prepared for the next five, 10 years. How about we invest with someone who is much more defensive that can protect your capital and help you control your emotions, also, when things are not going as well as we'd like.

We all like to think that we're very emotionally controlled and that we will never sell when the market goes down. But you need that help. And I'm there to help by being more defensive and the advisor's there to help to reiterate the plan and to explain why initially everything was set up the way it was.

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**Emily Anonuevo:** Now we're about five, six months into the year. It's flying by. More and more people in Canada are getting vaccinated. I'm just interested to know, Dan, what other themes are you excited about looking into for the rest of the year in your portfolio?

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**Dan Dupont:** I'd say in very typical fashion for me, I'm just thinking about all the risks. I'm trying to avoid them. And frankly, recently, I seem to be alone in thinking that what, maybe, just maybe some of these more cyclical companies that are just going straight up and to the right, maybe they're a little bit stretched on a valuation basis.

I understand that numbers are coming in and they're really good and they may continue to be really good. Commodity prices have been really, really strong. Financials, again, earnings have been really good. So, generally the news has been good.

The problem I see is that for a lot of these companies, the valuation has basically run ahead of some of these fundamentals. And let's hope that fundamentals keep surprising on the upside. So, because of all of that, I was very invested in more cyclical sectors in the last year. During the pandemic, I had more oil and gas. I had more financials before the yield curve went up, before the oil price went from -30 to $65. And now I look back and some of these moves were the right moves.

But some of these companies have gone way past where they should be, so more defensive position. I'm more excited about some more boring companies like Staples, food retailers, and drugstore chains and the like. And telecoms. I'm starting to look at utilities for the first time ever, literally for the first time ever.

And so, we're in an interesting environment, and that's what the stock market is. It's always new. And every day is a new day. And you have to look at what could be the best positioning for the next cycle. Because, let's be honest, the stock market is a little childish, if you want. Progress generally in science is secular. So, we just keep adding more and more knowledge on top of the knowledge we already had. But it seems like in investments, progress seems to be cyclical. So, we reiterate the same mistakes over and over again, different times in history and sometimes under a slightly different guise.

But we've seen problems in '01. We've seen problems in '08. And then some of these problems arose last year. But again, they were pasted over by a lot of money printing and then we'll see what the next cycle brings.

But for now, I see a lot of very expensive stocks. I don't have a lot of companies that really, really catch my eye. And the ones that do are slightly less cyclical, more cash-flow driven, just very, very strong fundamentally, typically have a really good market share, consolidated industries. And that happens from time to time.

You know, in Q1 2020, that's basically where I was very defensively positioned, had liquidity, and then all of a sudden out of the blue, something happens, and then you can move very quickly into companies that had been, frankly, just destroyed in valuation and gave us a really good opportunity.

So, until something like that happens again, we'll be a little bit more boring in Fidelity Canadian Large-Cap Fund. But honestly, history can now tell us that when I manage boringly, it doesn't mean that our returns are going to be worse off.

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**Emily Anonuevo:** Dan, if you could leave your investors with one message about what you do and your stewardship, what would it be?

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**Dan Dupont:** I guess that that one message would be, if you think about the show like The Deadliest Catch, what we're doing in the investment world, you're putting money at risk to try to get a better return than you would get elsewhere.

But what I try to do is to be the captain of that ship. And job number one is absolutely to get you back to port to have a quiet dinner with your family. So, I think about all the risks. I think about the downsides first. And I don't think there's a lot of people left around that think like me, but I think it's a really, really great way to invest. I think it's the best way to invest. And I do take their capital at heart. I take really good care of it. And I'm humble and I really thank them for the confidence they've put in me for now more than 10 years and hopefully for another 10 or 20.

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**Emily Anonuevo:** It's always so interesting to talk to you, Dan, whenever we have a conversation. I always love your stories, your personal stories, your analogies. It's so great. So, here's a last question. If you weren't doing what you're doing now as a portfolio manager, what else would you be doing or would you be doing this?

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**Dan Dupont:** Well, now that I have a lot of grey hair, I think, if I was younger, maybe I'd think of something, another answer, but I'd say and I've been saying to some people who have asked me that question before, I'd be doing this, but in my basement. I think I love this job too much, unfortunately, I hope it doesn't happen because I get such great access through Fidelity. We meet companies, we meet with the competitors, the suppliers, the customers, and all these resources. And Fidelity makes my life easy in the sense that all I have to do is to invest. They take care of everything else around it. I'm just focused on managing those assets and I don't, frankly, we do some of these webinars and webcast, but it's pretty rare. I'd say over 90, 95% of my time is spent analyzing companies, meeting with companies, and just making sure that the money is well invested. So, you know, I'm really grateful for all that.

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**Emily Anonuevo:** And we're grateful that you took a bit of time out of your schedule today to speak to us and speak to your investors. So, thank you, Dan.

**Dan Dupont:** You're welcome.

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