

The Upside

Your Investment Update and 2021 Sustainable Investing Trends

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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.

Portfolio manager Nicole Connolly believes that COVID-19 has brought more attention to how companies are treating their employees, and customers. Nicole, who is head of ESG investing at Fidelity, looks at key trends and provides an outlook for ESG investing in 2021.

Nicole manages Fidelity Women's Leadership Fund, and she'll unpack her fund with host Emily Anonuevo – providing an update on current positioning and outlooks, shares some success stories of gender-diverse companies and explains how she leverages Fidelity's deep fundamental and quantitative research expertise.

Today's podcast was recorded on February 11, 2021.

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Emily Anonuevo: Setting personal goals has proven to lead many people to great success and setting financial goals isn't anything different. Now more than ever it's important to stick to those goals and try to get ahead. Working with a financial advisor can help you do just that. An advisor helps you navigate through the ups and downs of the market, stay focused on your future and help capture potential upside while mitigating downside risk. Our guest today knows all about staying the course and investing with passion. Nicole Connolly is head of ESG and portfolio manager at Fidelity, and she's also a 20-year veteran at the firm. She joins me today to talk about her investment style, the Women's Leadership Fund and how she's using an ESG lens to look at opportunities this year. Welcome Nicole, so glad to have you here.

Nicole Connolly: Hi Emily. Thanks so much for having me and thanks everyone for joining.

Emily Anonuevo: Absolutely. Looking forward to our conversation today. I want to begin with a bit about you. You've been with Fidelity for over 20 years spending time in high-yield work, and director of research and heading up the Women's Leadership Fund. What has that journey been like for you, and how do you keep your passion for investing going?

Nicole Connolly: My journey actually starts with running. I ran track in college many, many years ago for Boston College. What I love about the sport is you have this number, or this time that tells you how you performed after every event, and I really liked the measurability of that. When I thought about a career, I wanted to keep competing in that way, and investing, like running, it doesn't matter what you look like, where you came from,

what your background is. If you put up good stock picks, just like if you put up good times on the track, you will succeed and move forward. For that reason I pursued a career in investing at Fidelity. Like you said, Emily, I've been at Fidelity for 20 years. It's an amazing place. I've worn a number of different hats. I was a research analyst for a number of years, both on the debt side and on the equity side, and then I was a director of research managing different sectors across the equity team. Then I had four kids in three years, and I came back from that last maternity leave after having twins, so that's how that happened, and really found that I wanted to have even more of an impact with my career and do work that was going to benefit my kids and future generations of children everywhere.

At the same time that I was feeling like that, Fidelity was doing a lot of work on the female investor and hearing from that woman that yes, she was often the breadwinner of the household and yes, she was making the major purchasing decisions for the family, but when it came to investing she was leaving her money in cash, or she was letting her spouse manage the finances, and we felt like maybe with a fund that she could feel like she was having impact and get excited about, that she would be more inclined to invest.

The other thing that was happening around that time was that ESG, environmental, social and governance investing, was gaining more momentum, and the idea of investing through a lens of making sure that a company is doing right by its employees, its customers, its communities, making sure it's limiting the impact it's having on the environment, that spoke to me and was a way of investing that made a lot of sense to me. So those combination of things that got me to where I am today with the fund and heading up our ESG investing efforts at Fidelity.

[05:13]

Emily Anonuevo: We will be touching upon ESG later in the show, but I wanted to go back to your point about the research. When Fidelity did that research, they found out that women want to invest in women-led companies, so let's talk a bit about the Women's Leadership Fund created almost three years ago. What does that fund actually focus on?

Nicole Connolly: One of the reasons we started the fund beyond trying to bring more women into investing was, Fidelity is a firm that believes deeply in the power of diversity and inclusion. Diversity and inclusion as a driver of culture, as a driver of innovation, as a driver of long-term financial performance. We thought let's have those principles be reflected in an investment product. This fund invests in companies that are deeply committed to diversity and inclusion. Sometimes they are led by women and sometimes they're not. We really want to see companies that have embraced diversity, inclusion, best practices, and we obviously are focused on gender, but increasingly we believe in the power of diversity beyond gender and so are weaving in more racial and ethnic diversity data into our framework.

After we've done the diversity deep dive on a company, we then do the fundamental work of saying is this a good business model, do they have a strong competitive position, what's the quality of the management team and the board, and we've developed a fund that has exposure to every sector in the market with that framework.

[06:58]

Emily Anonuevo: A lot there to unpack, but I wanted to bring in a great example of a female-led company that's making the news today, Bumble, of course. A great example of a female-owned company.

Nicole Connolly: Really excited for the Bumble team and for Whitney Wolfe Herd who's the CEO and founder of Bumble. She started that company when she was 24, and to see her original vision of, I think, developing a

kind, social network for women now be the second largest dating app globally is amazing, and her idea of having women swipe first and really helping women everywhere be empowered in their relationships is inspiring. So really excited to see where that company goes and I think it's got an exciting future ahead.

[07:55]

Emily Anonuevo: It really is a female-focused product because you can't start the conversation unless the woman starts the conversation, so that's what makes it really unique. When you were talking about the Women's Leadership Fund, you were talking about female-owned companies, about gender parity, racial equality, so looking ahead to 2021, how are you actively positioning the fund to capture as much upside and as little downside for the year ahead?

Nicole Connolly: There's what seems like two competing narratives in the market, or at least there's two competing narratives in my head. The first is that the consumer is flush with cash. They have benefitted from stimulus, they have foregone travel, eating out, going to concerts, and so they've saved a lot of money. There's this idea that once we all get vaccinated that we'll be off to the races. One of my colleagues calls it the light switch recovery. Think about the roaring '20s. That's kind of one narrative, and in that scenario you would want to own consumer discretionary, hotels, airlines, cyclicals, so early-cycle companies.

But the other narrative is are we in the later stages of a bull market? IPOs are pricing, and they're up 80 to 100% the next day. We're seeing more and more SPACS, which are special purpose acquisition companies where investors essentially give money to a company before they even own anything, and we're seeing five SPACS a day come to the market. In that scenario you probably want to be more defensively positioned, and on top of that we're seeing new strains of COVID emerge in the UK, and Brazil and South Africa. Basically I'm trying to own high-quality companies that can compound earnings and do well in most environments, but also make sure that I have exposure to more economically sensitive companies. I own a lot of retail. I own female-led GAP, Coles, Williams Sonoma. I also own hotels and airlines. I'm trying to stick with my high-quality focus, but make sure that I have some exposure to that light switch recovery thesis.

[09:57]

Emily Anonuevo: Definitely everybody's waiting for that light switch to go off. We just have to wait and see. I'm curious to know besides COVID and the vaccine rollout, how are you weaving in ESG? It has changed so much since the fund started in 2019, so how are you using ESG today to find opportunities within the fund?

Nicole Connolly: Maybe just to define ESG again for everybody, and really what we're talking about is looking for companies that are trying to limit their impact on the environment or maybe even provide solutions to help improve the state of the environment. We're looking for companies that are doing right by their employees, their customers, the suppliers, the communities they operate in. That's the essence of the S, social. And then companies with good governance. So good, diverse and independent boards, management teams that have compensation incentives that are aligned with the shareholder, good capital allocation. That's how we think about ESG, and Fidelity has just rolled out our own ESG ratings on every company that we own, and what's been helpful about that is I'm interested in this idea of finding companies whose ESG profile is improving. Our ratings framework at Fidelity, we have what's called our systematic rating which is the current snapshot in time of where a company is at with its ESG profile, but also a forward-looking ESG rating that's been developed by our fundamental research analysts. I can compare that current snapshot in time with the forward looking to really find companies that are improving.

GM is an interesting example of that. It's led by Mary Barra. It's a company I own in the fund. You wouldn't think of pick-up trucks as being environmentally friendly. But they are pivoting quickly to a zero-emission future. They just announced a goal of being carbon neutral by 2040, which is much more lofty than many of their peers. They have a goal of selling one million electric vehicles in 2025. I really think that that is a company that's going to look a lot different five years from now and is a good example of an improving ESG story.

I also recently bought a female-led utility who a few years ago was 95% coal generation. They're now 50% renewable with a goal of going to be 70% renewable, and they traded a substantial discount to their renewable energy peers. So I think as they get to that 70% over time, we should see the multiple rerate upward. So ESG improvement stories is what I'm looking for right now.

[14:05]

Emily Anonuevo: What a fantastic example there. I was going to follow up and ask, in the three years that this fund has been going on, has it been difficult or easy to find those companies that are female-empowered, female-led and also have a solid ESG profile? You must be learning so much as you go.

Nicole Connolly: It's a great point. Initially when we launched the fund we were focused on women's leadership, gender diversity, but as our work on ESG has evolved, as these ESG ratings have been launched, I am trying to weave in more of the holistic ESG assessment into the overall framework of the fund.

[14:54]

Emily Anonuevo: Switching gears a bit and focusing on the Biden administration that is now settling in. The U.S. is a big part of your country mix in the fund, so with the new administration there are expectations for a number of policy changes, how are you looking at that in terms of how it affects the way you approach particular sectors or industries?

Nicole Connolly: It's an exciting time, really excited about the Biden administration and the initiatives there. Since the fund launched, which was June of 2019 in Canada, I have been playing environmental themes. I was watching what was going on globally and seeing countries put out really aggressive carbon-reduction targets, and companies were putting out very aggressive, bold targets. I felt like there was a lot of momentum around the environment climate already, and now with Biden and his climate goals U.S. is kind of back in the mix, and Biden has committed to 2 trillion in investment in climate and has also recognized that disadvantaged communities have been more impacted by pollution, by toxic emissions, and so part of that 2 trillion is going to go to environmental justice efforts, which I think is great.

On the environmental theme I still own female-led Sunrun which is a leading residential solar company in the U.S.; NextEra which has a female CFO and is a large-scale utility solar; Ørsted and Vestas are wind plays both with female CFOs. I think the other aspect of the Biden administration that's really interesting is their focus on racial equality and this idea of bringing back fair housing practices, making access to health care and education available for disadvantaged communities, reforming criminal justice regulation. In terms of what that means from an investment perspective, Citigroup did a really interesting report last fall and said if we had been really focused on reducing the racial gaps, that we could've added 16 trillion to U.S. GDP. As we think about these racial-equality initiatives that the Biden administration is putting in, I think there could be some major investment takeaways left to GDP, and those are some of the things that we're continuing to research today.

[17:53]

Emily Anonuevo: If we can go back to the vaccine rollout for a bit, I know we talked about it a few minutes earlier, the rollout continues around the world, in some parts of the world faster and slower. How are you sort of timing this, looking at it in terms of certain opportunities for your portfolios? Is it hard to gauge when things will all be sort of rolled out and people are going to be vaccinated? I guess it's very tough to say when.

Nicole Connolly: I'm going to answer your question with a stock example, and I'll loop it back to your question. I own this company, Manpower, it's a 5 billion cap global-staffing company. Despite its name of Manpower, it actually has a strong women's story of 40% female representation both on the board and the management team. Typically staffing companies are good early-cycle plays. They benefit in the early part of a business cycle recovery. Manpower gets about half of its profit from France. The interesting thing about Manpower is that it trades at a substantial discount to the market, about 13 times next year's earnings versus the S&P over 20 times. One of the reasons why is because France has had a very slow vaccine rollout. To put some numbers around that, I think in France 3 out of every 100 people have received the first dose of the vaccine versus 14 out of every 100 people in the U.S. So they've been slow because of logistical issues and even getting the vaccine. I think some people in France are worried about getting the vaccine in general, like many people probably are, so I think that creates an opportunity with the stock which again is a good early-cycle play on the reopening, but is at a substantial discount because of concerns over the France vaccine rollout which I think are issues that will get resolved in the coming months. That's just a little bit of an example of how I'm thinking about how the vaccine rollout is different from country to country.

[20:18]

Emily Anonuevo: Does Fidelity's ESG rating try to look at the overall environmental impact? For example, how far down the supply chain does it go?

Nicole Connolly: When we developed this rating, we thought a lot about what are the material ESG factors for every sector. In energy the environmental factor should get a much higher weighting than maybe in health care where health care, we think a lot about product safety and drug pricing. We've kind of come at this rating from a place of materiality, and we do talk to companies about yes, you are complying from an environmental perspective, or from a labour-management perspective, but what about the rest of your supply chain? In our engagements with companies we do talk about the rest of the supply chain, how is it being audited, are you getting information from your supply chain about whether they're in compliance. It's a very good question, and it's something that both the ratings account for, and our engagement with companies which, as an active manager, is a major advantage we have. When you think about the passive players in ESG, they're not engaging with the companies the way we are to ask questions about supply chain oversight as an example.

[20:41]

Emily Anonuevo: Nicole, I want to talk a little bit about the value add that financials give investors about staying focused and disciplined through the market ups and downs. What keeps you focused? How do you navigate through all the market noise, especially in the last 13 months?

Nicole Connolly: One of the benefits of having been here for 20 years, which makes up for some of the greys that have happened of late, is that I've seen a lot of major pullbacks, lived through the great financial crisis, lived through COVID, and you just realize that these things are temporary. They are so painful, but they are temporary, and you just have to try to take the emotion out of it, which is very hard. There were days during the COVID sell-off where we were all working from home, the screen is red and it's just like, when is this going to end? But you do

have to stay the course. I think the other thing I think about is that this is a fund that's in this ESG product suite, and ESG, we're long-term focused as we think about these ESG issues. I don't run with a lot of turnover, so I'm not trading a lot, so that just helps me remember that I don't want to be in and out of names. I want to keep my turnover low, I want to be invested for the long term. So just coming back to the investment philosophy of the fund is helpful in times of volatility.

[23:14]

Emily Anonuevo: I'm just curious, if you weren't a portfolio manager, what career do you think you'd be in?

Nicole Connolly: I love to cook, so I think I would maybe be a chef. I don't know that I'm great at it, but I do love watching Joanna Gaines. If your audience doesn't know she's part-time entrepreneur, part-time home decorator, mom of five, and she's got a new show on Discovery called Magnolia Table, which is a cooking show, which I find on those stressful market days it's a nice way to unwind and watch a little bit of Joanna work her magic in the kitchen.

[23:59]

Emily Anonuevo: It's something so relaxing about her when she does her thing. I'm a big fan too.

Nicole Connolly: I know. And she makes it look so easy, and she's not trying to be perfect.

[24:12]

Emily Anonuevo: So chef it is. Second career. As we just wrap up here, Nicole, I wanted to know a message you'd like to leave your investors with about your stewardship, what would it be?

Nicole Connolly: I think long and hard when I'm investing in companies about whether there is truly a diversity women's leadership story there. I'm really wanting this fund to be authentic in that mandate. I think about whether the investors in this fund would expect to see this company, or whether they would maybe think that that was not an appropriate company for this fund, so at Fidelity we take our ESG initiative and commitment very, very seriously, and I want that to be reflected in this fund.

Emily Anonuevo: Nicole, thank you so much for joining me on the show. It really is a pleasure to speak to you. Your insights and your thoughts, it really is always a fantastic time to hear from you, so thank you so much for your time today.

Nicole Connolly: Thanks so much, Emily. Appreciate the support. Bye-bye.

Ending: [25:20]

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