Fidelity Funds (FF) – Global Industrials Fund

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Cyclical sectors to remain in spotlight; continue to favour quality franchises and long-term winners

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The Strategy:

The Fidelity Funds (FF) - Global Industrials Fund is a hybrid sector fund which invests in quality franchises across three pools: industrials & chemicals, metals & mining, and energy. By the nature of its mandate, about 65% of the fund (industrials and materials ex metals and mining) is generally driven by the business cycles of different industrials and chemicals sub-sectors, 10% of the fund (metals and mining) is driven by various kinds of commodity prices (iron ore, copper, gold, etc) and 25% of the fund (energy) is driven by oil and gas prices.

Overlaying all these drivers is the alpha driven by the **bottom-up stock picking skill** of the portfolio manager (PM).

Also, all the three pools, industrials & chemicals, metals & mining and energy are related to fixed asset investment. Thus, the overall FF Global Industrials Fund is a holistic way to gain exposure to the global fixed asset investment theme which we believe will accelerate over the next decade due to decarbonization, energy security needs, electrification, automation, reshoring, and supply chain resiliency. ***While investing in this multi-sector fund, investors have to keep three aspects in mind - near & short-term dynamics, medium to long-term dynamics affecting these sectors and most important of all, investment philosophy and process of the fund manager.***

Short-term dynamics of these sectors:

Global Industrials and Materials excluding metals and mining

In short-term, global industrials and materials excluding metals and mining stocks are broadly undergoing a cyclical downturn as evidenced by falling global manufacturing PMI trends (PMI of <50 indicates contraction in manufacturing activities).

Many different factors have contributed to this weakness, such as lower US residential and commercial building activities, weakness in European industrial activities due to energy shock, softness in the domestic Chinese demand led by the property sector and broad destocking trends since post-covid stocking boom. However, there are a few pockets of strength in the sector including electricals (led by utilities and data centre demand), aerospace and European defence activities. These pockets of strength have resulted in the relative performance of the MSCI ACWI Industrials sector broadly being flattish over the last couple of years.

But the MSCI ACWI Chemicals (a rough proxy for the MSCI ACWI Materials excluding metals and mining stocks) has not been resilient, because of its higher exposure to the cyclical drivers and less exposure to the strong subsectors like electricals and aerospace.

Going forward, we believe that the destocking driven pressure points are expected to moderate and the sectors which have suffered the most like US housing and EU chemicals should stabilise. This could result in a recovery in global manufacturing PMIs helping the stocks and subsectors which have suffered the most over the last couple of years while the strong subsectors like electricals and aerospace are likely to continue to be strong driven by structural drivers as discussed in the next section. On the other side, auto and commercial buildings and offices could be weak due to a lagged impact from higher interest rates. However, the sector dynamics overall are more likely to improve.

Global Energy

Oil prices have been broadly rangebound for the last couple of years with Brent staying in a range of $70-$90 per barrel despite many geopolitical shocks and a very volatile macro environment. One of the reasons why the oil price has stayed in this range is that this price range works for everyone from consumers to producers. Barring a major shock in either direction (wars, recession, etc), oil price could be expected to stay in this range. This has resulted in the sector being generally flattish in absolute term for the last couple of years with its relative performance being more a function of what happens to the rest of the market than to the energy sector. As mentioned earlier, barring a major shock, this trend is expected to continue.

Global Metals and Mining

The key drivers for the subsector are commodity prices like iron ore, steel, copper, gold, aluminium, etc. This subsector has performed poorly due to the weakness in demand largely driven by the slump in the Chinese property sector.

Going forward, its performance should be similar to the cyclical parts of the global industrials and materials sectors as some of the drivers are similar though not exactly the same (metals and mining more levered to the Chinese property sector, key drivers for gold being macro than industrial activities).

Medium / long-term considerations:

We believe that the key medium-term drivers for the underlying sectors of this fund are US fiscal stimulus, supply chain reconfiguration, reshoring, electrification, energy and infrastructure resiliency and automation.

Over the last five years, global supply chain has suffered many shocks including tariffs, covid, Ukraine war and more recently Red Sea disruption. This has resulted in corporates rethinking their supply chain. Over the last three decades, supply chain was all about low-cost sourcing and just in time inventory. However, the shocks over the last few years have exposed the risks of a supply chain strategy rooted in low-cost and just in time thinking. Now, corporates are increasingly thinking about resiliency of their supply chain. **This has resulted in a new supply chain strategy which will be based on local for local and redundancy in the sourcing and procurement strategy. We are seeing increased investment in near-shoring and onshoring activities. Many countries like Vietnam, India, Mexico and US are major beneficiaries of these initiatives.**

In addition to these corporate led bottom-up activities, there are top-down government led initiatives also to accelerate this supply chain reconfiguration. The US government has announced many initiatives over the last few years towards this goal. These initiatives will achieve two goals - to accelerate the supply chain reconfiguration and to fix the infrastructure deficiencies in the US economy. Through these various fiscal stimulus schemes, the US government will stimulate about $1.5tn of investment in fixed assets over the next few years. This could potentially result in about 200bps (2%) of additional fixed asset investment growth over the next few years in the US. The main components of these stimulus schemes are infrastructure investment (about $550bn of new money in US infrastructure like roads, ports, airports, grid, water, etc), Inflation Reduction Act / IRA (about $400bn, 70% of which will flow via tax credits in different kinds of electrification and clean energy projects) and CHIPS act (about $280 bn to be invested in semiconductor manufacturing, research and development). The design of these stimulus schemes and bipartisan nature of benefits will ensure that a big part of these stimulus schemes will survive all kinds of political environment.

Electrification and energy resiliency are major needs of the global economy not only to make progress towards decarbonization but also to achieve energy security during a period of energy transition from fossil fuel to clean energy sources. If this transition is not handled without proper investment, the global economy runs a serious risk of energy insecurity, a glimpse of which we saw during the Russia Ukraine war. This requires an upgrade of the existing electricity grid infrastructure and investment in different energy storage technologies. The IEA estimates that the world would need about $4.5tn in clean energy investments by early 2030s, from $1.8tn in 2023, to meet net zero aspirations.

The world also needs to accelerate investment in infrastructure resiliency given the challenges from climate change. We are already seeing the impact to infrastructure from increasing frequencies of unpredictable wildfires, floods and storms. This would necessitate increasing investment in infrastructure to make the existing assets more resilient. One of the goals of the recent rounds of US fiscal stimulus schemes is to increase the resiliency of the US infrastructure to make them more resilient to unpredictable weather events. The global economy will have to increasingly think about these issues and accelerate investment in infrastructure.

All of the above would not be possible without an increased investment in automation given the labour constraints the global economy is going to face in future, which will be a structural issue given the demographic trends. The industrial technology, software and automation investment has a lot of potential to capitalize on the technological progress which has been made over the last few decades in the fields like sensors, edge computing, AI, computer vision, robotics, etc.

Without these investments, supply chain reconfiguration and infrastructure and energy resiliency would be close to impossible.

All of the above issues are already impacting the level of industrial investments. These issues will be the most important drivers for the industrial investment in the next decade.

Our investment philosophy and process:

The investment philosophy of the fund rests on three key beliefs:

- **Only good companies run by good management teams create value over long term.**
- **Stock prices over long term reflect the intrinsic values of the underlying businesses.**
- **Market underappreciates change events, either over-penalizing good companies for short-term problems or underappreciating long term positive changes**

Based on these beliefs, the fund invests in good or improving businesses which are not priced for their quality and long-term potential. The fund leverages the deep industry and company research done by Fidelity analysts to uncover these investment ideas. This tried & tested investment approach proven over the eight years plus track record, supported by the core investment belief of value and quality along with fund's diversified exposure to three different sectors has delivered consistent returns for our clients, and we expect it to continue going forward, leveraging the strength of our research ecosystem.

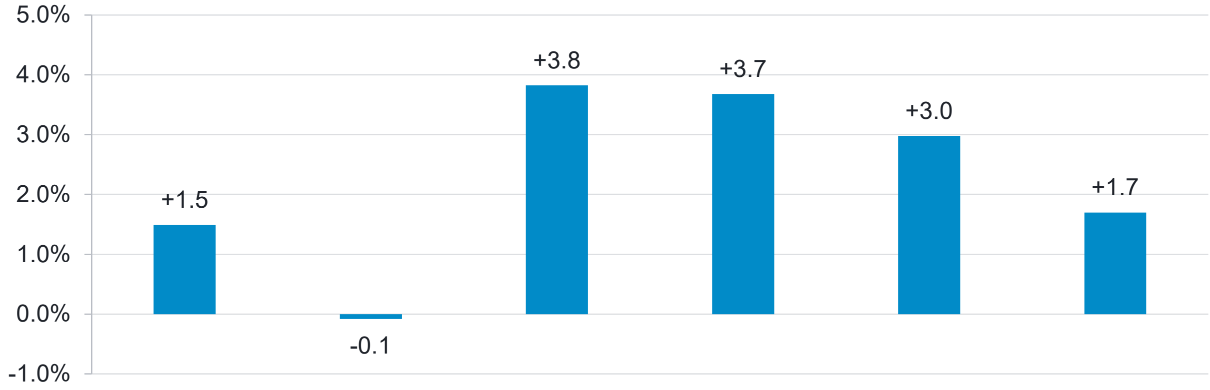
Why invest in Global Industrials Fund?

- ✓ **Unique PM skill & experience set** in a complex sector: Ashish Bhardwaj's industrials experience stretches back to 2009; has been managing the fund since October 2015.
- ✓ Unique focus on **quality with strong risk-adjusted return profile**: Investing in good quality businesses at reasonable valuation allows for consistent alpha across time periods.
- ✓ Offers exposure to **both cyclical and long-term structural themes**: Automation, reshoring, decarbonization, clean energy, electrification and digitalisation & mobility gives good exposure to key focus areas for fiscal stimulus in all geographies.
- ✓ Exposure to **diversified underlying sectors** across **different business models.**
- ✓ **Bottom-up stock selection approach** and **active management** allow best of both worlds without picking up unknown factor exposures.
- ✓ **Delivery of meaningful relative returns** across the cycle.

FF Global Industrials Fund Performance

Past performance does not predict future results. This fund invests in overseas markets and the value of investments can be affected by changes in currency exchange rates.

Standard Period Excess Returns (%, in Euro, Net of Fees), As of 31 March 2024



Net of fees (%)	3 months	6 months	1 year	3 years (p.a.)	5 years (p.a.)	Since tenure (p.a.)
Fund	11.4	14.5	23.8	16.0	13.2	12.1
Index	10.0	14.6	19.9	12.3	10.3	10.4
Excess returns (%)	**+1.5**	**-0.1**	**+3.8**	**+3.7**	**+3.0**	**+1.7**

Rolling 12-Month Excess Returns (%, in Euro, Net of Fees)

12 month period ending	Mar' 15	Mar' 16	Mar' 17	Mar' 18	Mar' 19	Mar' 20	Mar' 21	Mar' 22	Mar' 23	Mar' 24
Fund	15.4	-12.0	27.0	-8.1	13.3	-25.1	59.3	20.3	4.8	23.8
Index	19.5	-13.6	25.7	-1.9	9.0	-24.5	52.4	17.3	0.7	19.9
Excess returns (%)	**-4.2**	**+1.6**	**+1.3**	**-6.2**	**+4.2**	**-0.6**	**+6.9**	**+3.0**	**+4.1**	**+3.8**

Source: Fidelity International, 31 March 2024. Performance is for Fidelity Funds – Global Industrials Fund A-Euro share class. Basis nav-nav, net of fees in euro terms, with gross income reinvested. Comparative index: MSCI AC World Industrials + Materials + Energy (N). Holdings will vary from the index quoted. For this reason, the comparative index is used for reference only. Ashish Bhardwaj Tenure Start Date: 1st October 2015. Data shown does not take into account any initial charge that may apply. Numbers may not sum due to rounding.

Important Information:

- The value of investments and the income from them can go down as well as up and investors may not get back the amount invested.
- Funds are subject to charges and expenses. Charges and expenses reduce the potential growth of your investment. This means you could get back less than you paid in. The costs may decrease or increase as a result of currency and exchange fluctuations.
- This fund invests in overseas markets and the value of investments can be affected by changes in currency exchange rates.
- This fund invests in emerging markets which can be more volatile than other more developed markets.
- This fund does not offer any guarantee or protection with respect to return, capital preservation, stable net asset value or volatility.
- Investors should note that the views expressed may no longer be current and may have already been acted upon.
- Past performance does not predict future returns. The fund’s returns may increase or decrease as a result of currency fluctuations.