Fidelity's Perspectives on Sector Investing

Hello, I'm Denise Chisholm, a sector strategist here at Fidelity Investments. Welcome to our new video series, Fidelity's Perspectives on Sector Investing. Our goal is to share our thoughts and some of our equity sector insights to help our customers achieve their investment objectives.

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Today, I'd like to share three important topics when considering equity sector investing:
1. Why equity sector investing is an important part of a portfolio.
2. How history may provide unique insights about sector performance.
3. Key investment themes to watch as the year progresses.

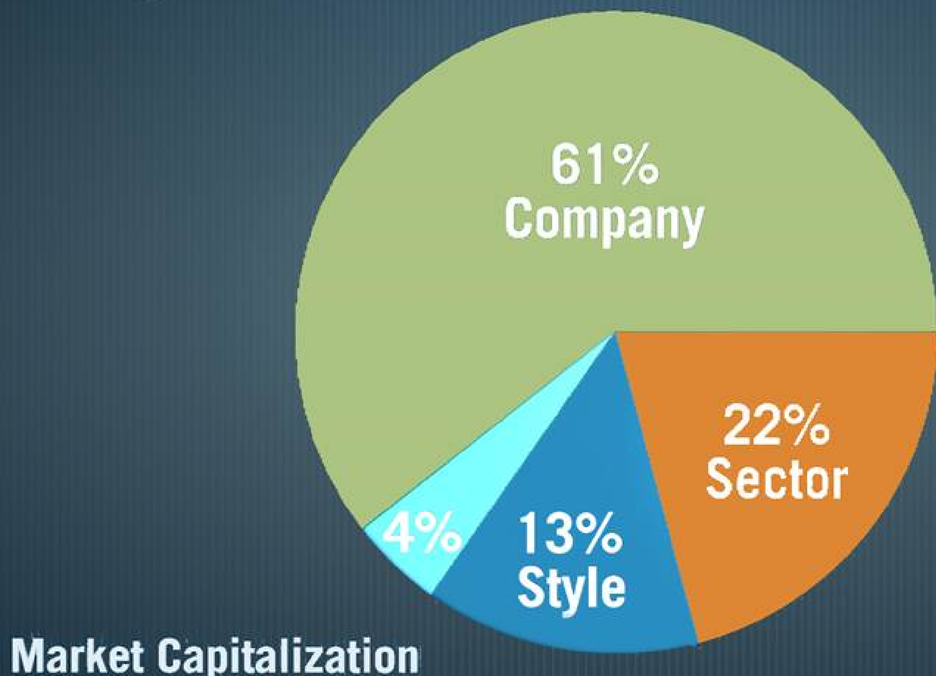
Why is equity sector investing an important consideration for a portfolio?

Sectors have been an important driver of returns. Unfortunately, they are often overlooked as investors typically diversify along the lines of style (meaning value or growth), or market capitalization—large cap, small cap, and mid cap.

Historically, 22% of a portfolio's performance is driven by sector factors compared to only 4% for market capitalization and 13% for style. Although most investors build portfolios around the style box, sectors have been a bigger driver of returns, and therefore may be a more effective building block. Of course, past performance is no guarantee of future results.

Sector Exposure Has Been a Significant Driver of Returns

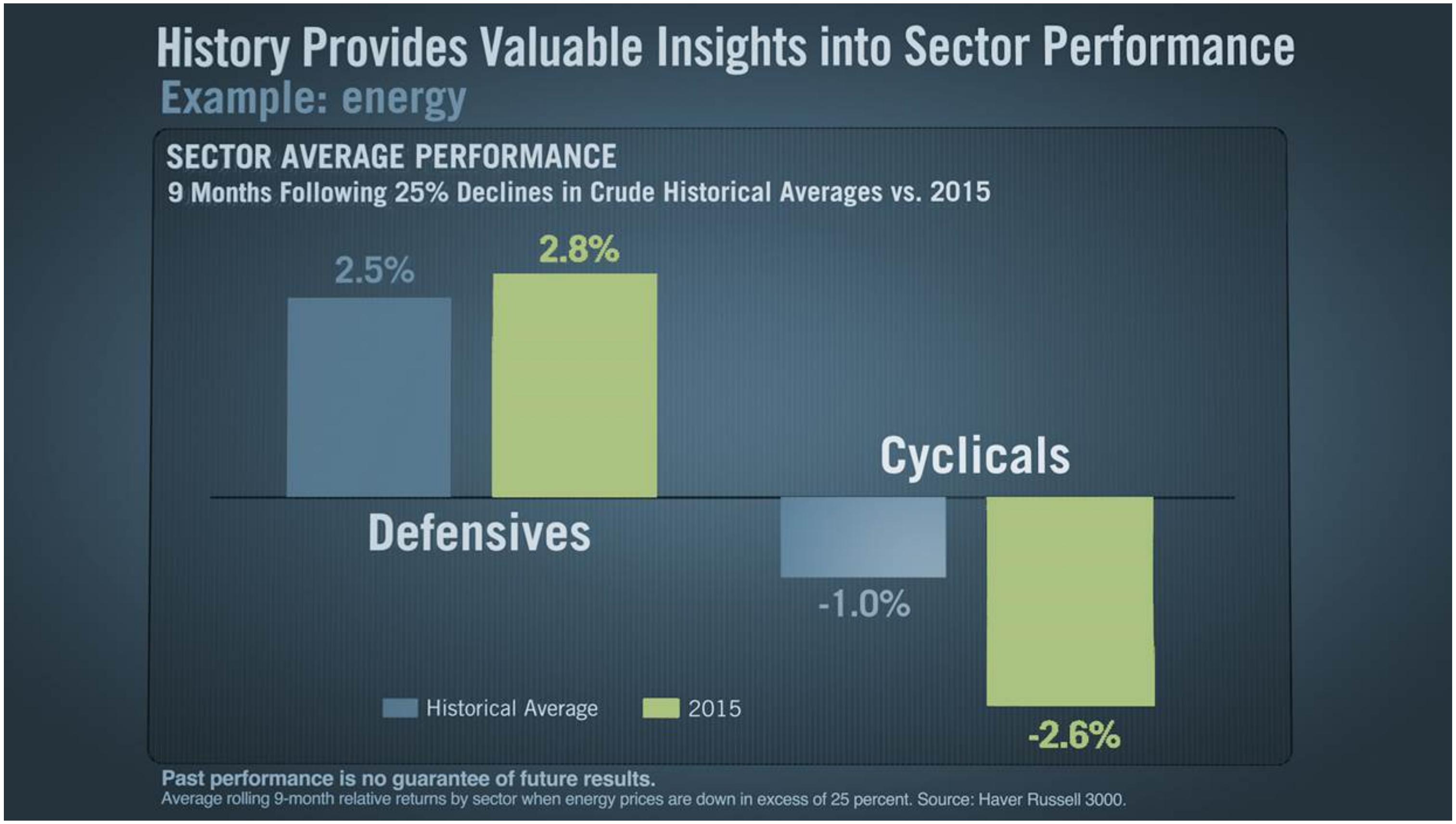
Average Source of Returns for U.S. Stocks 1/1/90–12/31/15



Source: Fidelity Investments as of 12/31/2015, based on rolling 12-month analysis of variance (ANOVA), which uses statistical models to attribute the variance of a variable (stock returns in the Russell 3000®) to certain factors (sector, style, and market cap). The residual is attributed to other company-specific factors. Past performance is no guarantee of future results. It is not possible to invest directly in an index. All market indices are unmanaged. Index performance is not meant to represent that of any Fidelity mutual fund.

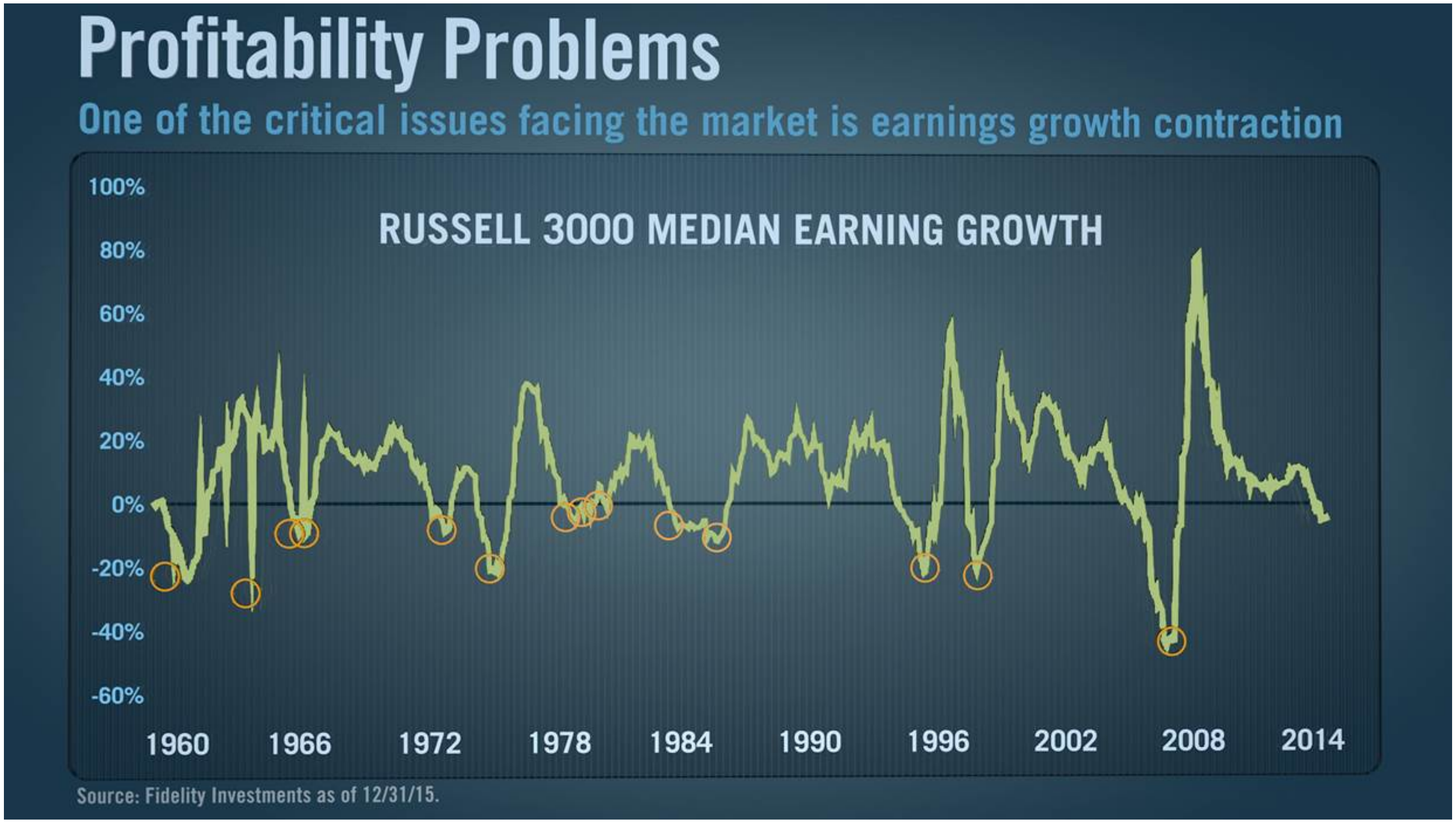
How can history give us insight into sector performance?

At Fidelity, we believe history offers valuable insights into sectors. When you examine the probabilities of performance associated with key macroeconomic and fundamental variables, sector performance patterns often become evident. Here’s an example: When the price of oil fell by more than 30 percent last year, many thought that would provide a stimulus to the U.S. consumer and subsequently give a boost to the economy. Many market participants thought it would result in a procyclical bias—where cyclical sectors would outperform more defensive sectors. However, when you look back through history, in the nine months that follow significant oil price declines, cyclical sectors on average underperform. And in fact, what happened in 2015 is almost right in line with what happened on average since 1970. This is an example of how history can be a great guide to sector investing.



What key themes are we watching this year?

First, the issue at the forefront—“profitability problems.” Earnings growth on a median basis is contracting. And this is not just an energy phenomenon; seven out of the ten sectors have a median stock with declining earnings. If profitability problems like this continue, the defensive sectors of consumer staples, health care, and utilities most often outperform. Market participants remember that people tend to buy toothpaste, go to the doctor, and turn the lights on regardless of economic conditions. On the other hand, the technology, industrials, and financials sectors are more cyclical. They tend to struggle in this type of market environment because their earnings tend to rely on discretionary purchases that can change with economic conditions.



A related theme is currency. What we've seen over the past two years is an appreciation in the dollar. This is important, because this is one of the reasons for the profit deterioration we just discussed. Using history as a guide, we may be able to take advantage of either bull or bearish outlooks on the dollar. If the dollar continues to strengthen, based on past historical performance, domestically oriented sectors such as consumer discretionary, financials, telecom, consumer staples, and health care may be sectors to consider. Alternatively, if it looks like the dollar will depreciate in the coming months, history suggests investors may want to consider tilting a portfolio toward the more globally exposed sectors of materials, technology, and energy.

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Earnings

- Defensive sectors of consumer staples, health care, and utilities have most often outperformed.
- Technology, industrials, and financials sectors are more cyclical and tend to struggle in this type of market environment.

Currency

- If the dollar continues to strengthen, domestically oriented sectors, such as consumer discretionary, financials, telecom, consumer staples, and health care, may be sectors to consider.
- If the dollar depreciates, investors may want to consider tilting a portfolio toward the more globally exposed sectors of materials, technology, and energy.

I hope this discussion about why sectors are important, how we use history as a guide, and the key themes we're watching has been helpful. And I look forward to bringing you more equity sector insights in the coming months. Please stay tuned for future episodes that will dig deeper into each of the themes we discussed today. Thank you for watching and for more information, please visit www.fidelity.com/sectors.

Important Information

Investing involves risk, including risk of loss. Diversification does not ensure a profit or guarantee against loss.

Stock markets are volatile and can decline significantly in response to adverse issuer, political, regulatory, market, economic, or other developments. These risks may be magnified in foreign markets.

Investment decisions should be based on an individual's own goals, time horizon, and tolerance for risk. Nothing in this content should be considered to be legal or tax advice, and you are encouraged to consult your own lawyer, accountant, or other advisor before making any financial decision.

Past performance is no guarantee of future results.

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Index Definition
Russell 3000® Index is a market capitalization-weighted index designed to measure the performance of the 3,000 largest companies in the U.S. equity market.

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