

TRANSCRIPT

Bond investing in today's environment

Presenters: Fabian Weinstein-Jones, James P. McCloskey, Peter Stringfellow, Christine Thorpe

Pete Stringfellow: Welcome all. I want to take you back one year ago. One year ago, almost today, we were hosting a very similar webinar. Only what were we talking about? The lack of inflation, the lack of yield, to an extent the lack of volatility outside of upside volatility across markets. So today is a very different environment. And what we're going to be talking about today is really, how do we identify opportunities based upon the environment?

[00:00:36.68] Now, a lot of what we're going to discuss is tied to, let's call it, exogenous circumstances, circumstances that are outside of our life's control, our life's purview, what's happening in our day-to-day. But keep in mind, that is a very critical component to selection across a portfolio.

[00:00:58.34] And we'll hit on that. We'll hit on different ways to target opportunities across strategy that really targets not just the environment outside of our life or outside of our home but also what's pertinent to us, like, what makes the most sense in terms of supporting our efforts and our desires to get exposure across the fixed income market, in particular based on what makes the most sense.

[00:01:25.49] So what we're going to be doing today as we talk through selecting bonds in this current environment or really managing your portfolio in the current environment is first, context. So what is happening across the market? Second, we're going to talk a little bit about investing in individual bonds and really identifying opportunities across the bond landscape because it is so vast.

[00:01:53.41] Talk a little bit to how would you build and maintain your own individual bond portfolio? And then if you'd rather hand over the reins, talking about investing in separately managed accounts, which are a method of getting exposure to the bond market if you like the idea of having individual issues that are a part of your strategies. Then what we'll do is we'll bring Mo back in to talk through some questions.

[00:02:21.14] But first, let's set the stage. Let's set the foundation for the overall conversation today and bring in Fabian, who's going to talk a little bit to the 2022 bond market in context. And if you think about that, going back a year ago, the environment has changed significantly.

[00:02:44.83] Right now fed funds rates are 300 to 325 BIPs. We're likely looking at another increase here at the end of the day. So, Fabian, let me invite you here to the stage to speak a little bit to the context. And I'm happy to bring up your

first slide here. When you are ready, go ahead and just let me know when you'd like me to bring up that slide.

Fabian Weinstein-Jones: Awesome. We'll do. Thanks, Pete. Hi, everyone, Fabian Weinstein-Jones. Pleasure to be here. Thanks for joining us. It's interesting that Pete mentioned the context from last year because it's almost the exact opposite situation. So let me set the stage and provide a quick context for what's been going on in 2022 in the bond market.

[00:03:29.81] So first and foremost is we've been having waning fiscal and monetary support for the economy, as you touched on. And we'll continue to talk about a little bit that have been raising interest rates to combat inflation, and they're reversing their purchasing program in a process that's known as Quantitative Tightening or QT. In addition to that, no longer have the tailwind of federal stimulus dollars. So we sent a lot of money to individuals, businesses, local governments and municipalities, and that's starting to taper off.

[00:04:03.46] How does the economy look now that we no longer have that support at the back of at our backs? Touching on inflation a little bit, highest level in decades, global phenomenon, central banks around the world are tasked with

getting a handle on that. As they do that, they're going to try to dampen economic activity, build that, push us into recession or not.

[00:04:26.78] And then last but not least, we have geopolitical concerns and the potential impact on our markets. From Russia's invasion of Ukraine earlier in the year to more recently, we had a situation developing in the UK political situation where they have the shortest tenure of Prime Minister ever. And that had a knock on effects to our US rates market. That's just as another example. So with all that being said, let's turn to the first slide if you don't mind, Pete. Thank you.

[00:04:58.08] So slide one here tells us that it's been a challenging year for bonds to 2022. Bonds were caught in a maelstrom of central bank tightening activity. You can see from the chart that our total returns have ranged from minus 12% to minus 20%.

[00:05:16.22] How bad is that? Well, the US Agg index, which is the middle of this chart right here, the light blue, that's down roughly minus 15% year to date. The previous worst year for the Agg was 1994. It was down 3%. So this is five times worse than we've experienced ever.

[00:05:37.49] Now, in addition to higher rates, the market has also struggled with liquidity. At times, it's been difficult to buy and sell. As risk appetite waxed and waned throughout the year, the typical intermediaries were no longer willing to provide liquidity at the same clip that they used to. So one thing to keep in mind here is as interest rates increase, bond prices are going to fall or tend to fall, I should say.

[00:06:05.37] So if rates are going up rapidly, that means that bond prices are going to fall precipitously. And that's a large part of the reason why all of these sub asset class fixed income space had negative total returns. So let's delve into each one of these momentarily to talk about some of the issues that they were struggling with in addition to rising rates. So let's start with munis in the far right.

[00:06:30.05] Muni rates are slightly different from the typical treasury rates. And as a result, those rates didn't fall as much as the rest of the market or, I should say, those rates didn't increase as much. Those prices tend to fall as much as the rest of the market. The other thing that impacted the muni market was that there were large outflows. As prices started to decline, folks started taking their money out of munis. And munis had a challenging period of liquidity from time to time over 2022.

[00:07:00.95] Switching to TIPS and treasuries, these are pretty much beholden to a lot of the same forces. Rising rates, the Fed no longer doing their purchase program QT and the treasury space, increased need for the government to fund itself, and TIPS also had bouts of limited liquidity, especially versus treasuries.

[00:07:21.71] One thing to keep in mind, though, is that we still think that treasuries are an essential part of a diversified bond portfolio. And the reason for that is that they are the most liquid, typically the most liquid fixed income security out there. So when you're looking to manage your interest rate risk, treasuries are a very effective way of doing that.

[00:07:43.83] Another thing to talk about now is Mortgage Backed Securities or MBS. So they also had a negative total return as, once again, the fed QT had a direct impact, they weren't buying as much as they were before with respect to mortgages. Higher mortgage rates-- higher rates in general led to higher mortgage rates. We started the year around 3%. Now we're about 7%, 7 and 1/2% on a 30-year mortgage rate. So that's slowed housing activity a tremendous amount.

[00:08:13.62] Last but not least, though, MBS has additional interest rate sensitivities versus other bonds. And so as rates increase, interest rate risk and the MBS base also picked up. So that was another negative for MBS as a whole.

[00:08:30.70] Now, switching to investment grade corporates and corporates more generally, so corporates decline as folks start to worry about the overall economy. Is there going to be a recession? What does profitability look like for these companies?

[00:08:44.13] Now, one thing to note, though, is you see the IG corporate bar has a larger negative return than the high yield corporate environment. And a big part of that is because high yield corporates tend to have lower maturities. So if you're an investment grade company, folks aren't really necessarily as worried that they're going to get-- that you're going to pay them back versus the high yield space.

[00:09:07.44] One way to think about it is high yield companies have lower credit scores or FICO scores, whereas investment grade companies have higher FICO scores if you think about your own personal situation when you're looking to borrow money. And so as a result, high yield, their total return

wasn't as bad. But that was because the maturity for a typical high yield is significantly less than investment grade yield.

[00:09:34.98] Last but not least, we have emerging markets. And there they just could not catch a break this year. We had the global economic slowdown, increased geopolitical uncertainty that we've mentioned before, higher inflation, stronger dollar, and it's no surprise that we had a minus 20% return in the emerging market space. Next slide, please. Great.

[00:10:00.72] So now, what I'm showing here is bond returns in different rate environments. So we have the Agg index, which is the bars, and then the black line is the Fed funds rate, which is on the right hand side. So for those of you who don't know, the Fed funds rate is the rates that bank borrow from each other overnight. Is set by the Federal Reserve and Fed funds.

[00:10:24.18] And the reason why is important is because banks are required to hold a certain amount of reserves for the deposits that they have. So if they don't have enough reserves, they can go out and borrow from another bank to make sure that they meet the requirement. So why wouldn't they have enough reserves?

[00:10:41.79] Well, if they're making a lot of loans, it could be fairly profitable for them to borrow at a relatively low rate, and then go out and make loans at higher rates. So then as the Fed is raising the Fed funds rate now, they're going to be less likely to make loans, and any subsequent loan that they're going to make is going to require a higher level of interest. So that's how the Fed is trying to impact economic activity to slow it down by increasing the cost of money, so to speak.

[00:11:13.24] Now, as we've touched on and mentioned before, rates go up, bond prices go down. And you can see from the chart that there are times the Fed is raising rates, bonds had a negative total return although not always the case. 1994, the Fed moved 250 basis points, and we had a minus 3% return on the Agg.

[00:11:37.71] So far this year we've moved 300 basis points with two more meetings to go. And today we expect to have another 75 basis points move in the overall Fed funds rate. So that gives you some context once again of just how different 2022 has been versus the last period of intense Fed activity from 1994.

[00:12:02.73] So one thing to also note is that bond returns have typically recovered post rate increases. And why might that be the case? So the thing to remember is that when you're a bond investor, you're getting interest coupon along the way before you get your ultimate maturity of principal.

[00:12:21.06] And so now if rates are higher, you can take those coupon payments and reinvest them at higher rates. And higher rates are also higher yields are also going to provide more of a cushion to you for any other kind of price decline that you may experience in the near future.

[00:12:40.36] So, for example, the Agg index that we talked about at the beginning of the year had a yield of roughly 1 and 1/2% or so. Now, it's more than three times that at roughly 5%. So there's no guarantee that you're going to have a positive return in bonds post an increase in overall interest rates. But the key point is higher yields gives you more of a buffer to withstand the market declines. Next slide, please.

[00:13:17.13] We've talked about this a little bit. But inflation was a big story for 2022. The point that this slide is just to show how much of a global phenomenon as we're showing the US, UK, and Canada. And this is what central bankers-- or

some equivalent measure, central bankers are looking at because their job is to get this down.

[00:13:41.30] In September, we had the highest level of inflation that we've seen over the last 40 years here in the United States. So this is what the Fed is concerned about and other central bankers around the world. They want credible evidence that this is going to approach their long term averages or what level that they think is appropriate for the economy. And that's roughly 2 and 1/2%/3%. And since we're sitting at 7% to 9% here, they have a lot of work cut out for them.

[00:14:10.82] One of the risks for the Fed and others is that if inflation lasts longer than anticipated, then it becomes part of-- it becomes entrenched amongst the population. It becomes harder to combat because part of what sets inflation is our expectation for what inflation is going to be in the coming years.

[00:14:30.87] Now, initially, the Fed thought that its inflation situation was transitory. It was due to supply chain risk coming out of pandemic. We had less supply of the things that folks wanted. Demand was OK because we had, once again, those Federal stimulus dollars, and that led to higher prices.

[00:14:50.75] They've since realized is that tight labor market has fueled additional wage growth, and that's led to inflation being stickier than what they expected. So this is certainly going to be one of the key factors to consider for fixed income investments going forward. Next slide, please. Great.

[00:15:15.25] So you've touched on the interest rate environment. We've talked about how rates have gone higher. This is just a graphical representation for that. What this is showing here is the US Treasury yield curve.

[00:15:28.09] To make a concrete example out of it, one year ago, if the US government wanted to borrow money for roughly two years, they would have to pay almost nothing in order to do that. Today, if they wanted to borrow money for two years, it's going to cost them 4% or more. So this just gives you a sense for the dramatic increase that we've seen in interest rates over the last year.

[00:15:52.69] Now, the other thing to notice is that the yield curve has inverted. And what I mean by that is short term rates are higher than long term rates. And this is relatively atypical. Think about it this way. If you went to go get a mortgage, the rate of a 15-year mortgage is typically lower than a thirty-year. And that makes sense. As an investor, you're going to require more

compensation if you have to leave your money locked up in a longer term security.

[00:16:20.23] So what does this mean when the yield curve is inverted? Some say that it's a sign of a recession. And while it's true that in the past, an inverted yield curve has preceded a recession, that isn't always the case. What it does signify is that market expectations for future economic growth has fallen. And so as a result, investors expect this Fed part to eventually decline and reverse the rate hike cycle.

[00:16:48.58] Now, I want to stress, though, this is a market expectation. Doesn't necessarily mean it's going to happen and if it's going to happen any time soon. Moreover, market expectation is something that shifts as new information comes to light that economy involves. So, for instance, like I mentioned, today, the Fed is expected to raise rates 75 basis points, which is what the market is expecting.

[00:17:14.10] More importantly however, our crew are going to be looking forward to see what the Fed is potentially going to do down the line. Are they going to pause? Are they going to continue to hike rates at the level that they have recently because they still don't see inflation coming down anytime soon? And

so that additional information is going to set what folks expect. And that could shift the yield curve around to where it's either more inverted or less inverted and even what the market realizes.

[00:17:48.27] So in conclusion, 2022 was quite an unprecedented year. And as Pete mentioned, it's almost the opposite of where we were same time last year. Now, while that's the case, it also represents an opportunity. Higher yields to be touched on, an attractive proposition, especially if you're reinvesting coupon payments from lower yielding securities, as part of a diversified portfolio in the long run, we still believe that bonds are an essential part of a portfolio. So with that, I'll turn it back to you, Pete.

Pete: Fabian, thank you, sir. Phenomenal context I think, especially macro wise, gives us a really good foundation to consider, especially if we're bit more independent minded in regard to how we make decisions across the portfolio, where do we go? How do we find opportunities within the individual bond space? And then ultimately, how do we go about building and maintaining an individual bond portfolio? Because what's really important here in my mind, it actually makes me call on one of my favorite quotes.

[00:19:05.26] So if you're familiar with James Clear, he has this book Atomic Habits, really good book. But there's one quote that I really love in this book because it fits across so many different paradigms of life, and in particular in investing. Quote reads, "You do not rise to the level of your goals. You fall to the level of your systems."

[00:19:27.82] So, James, I'd love to invite you in here to talk a little bit to really first, what does that mean? Like what is building a system if we're trying to build a bond portfolio and manage a bond portfolio? But then, how do we actually do that through Fidelity's tools? So, James, maybe take a moment just to speak to that, and then we'll get into, specifically what are these individual bonds and how do we use them?

James P. McCloskey: Yeah, absolutely. Thank you, Pete. So I always advocate with my clients to come up with a defined strategy and a repeatable process. What is the purpose of the portfolio that you're building? I see a lot of times clients are just picking something that has the highest yields or maybe they put everything short term. You want to really set goals for your assets. And, Pete, if you could pull up the individual bond strategy.

[00:20:32.26] So to start here, if you take a step back and you think about all the volatility that Fabian spoke to and that we've seen in the markets this year, whether it's rising rates, inflation, declines in the equity market, there's an uncertainty about future. So this is a market where introducing certainty into your strategy goes a long way.

[00:20:54.66] So why do investors purchase fixed income? Simple, it's preservation of capital and income. So when you buy an individual bond, you have a fixed maturity rate and a fixed coupon. I know, for example, if I purchase, say, a five-year treasury bond at 4 and 1/4%, that five years from now I will get my principal back, and I know that year over year that has a 4 and 1/4% coupon that I will get that cash flow.

[00:21:24.94] So the price of the bond may fluctuate along the way due to market conditions, but I know my price of purchase. I know my coupon, my yield, and I know my future maturity value. That's a level of certainty that you can't find if you're purchasing a stock or, say, a mutual fund. There's no maturity date. There's no fixed yield.

[00:21:46.56] In terms of tax efficiency, there's a lot to choose from. For instance, in taxable accounts, you have the option of looking at municipal bonds. Those

are federally exempt. And if you buy a bond in your home state, they're also state and local exempt. Treasury bonds, for instance, those are state and local tax exempt so that they may make sense in a taxable account.

[00:22:11.43] So in terms of the individual bond positions, I'd focus, Pete, on, one, the fact that you have a maturity date. You have a fixed coupon, different bonds have different characteristics, and there's a lot to choose from. So, Pete, I think to your question though about, OK, I know that I want an individual bond strategy. But how do I come up with a design? How do I use the website to create a well-rounded portfolio? And that's what this next slide, Pete, focuses on.

[00:22:46.23] So you want to build, to Pete's point, a process and a system for designing your portfolio, so first defining your strategy. Is this a short term ladder treasury portfolio for cash management or are you looking for longer term income in retirement? Either way, the Fidelity platform gives you the tools and resources you need as an individual investor navigating the bond market.

[00:23:17.24] Look, if you look at the yield criteria, so when you go to News and Research and you pull up on the Fixed Income Bonds and CDs page, we show

you the entire yield curve with different types of bonds in different time frames. So maybe you're looking and noticing, well, shorter term treasury rates are high, but when to start going out longer term, maybe municipal bonds make sense.

[00:23:44.46] So if you get a sense when we aggregate all of the data there for you, it helps you analyze the yield curve and helps you with finding value in the market as you compare different types of bonds versus each other. And also helps with the risk reward conversation. If treasury rates are 4% and I can see that corporate rates are 5%, maybe, in that case, it would make sense to look outside of treasuries.

[00:24:14.93] So, Pete, I'll pause there to see if you have any thoughts or questions on building a system and a strategy.

Pete: Yeah, I mean, what's interesting to me, James, that you called out there is whether we're wanting to look for opportunities based on the market environment or based on our circumstances like what's happening in our lives, we have the ability to do either. Would that suffice to say?

James: Absolutely. Yeah, there's choice. And this choice and resources-- and this next slide-- and I really want to focus on this slide. So bonds are an over-the-counter market, meaning with equities, they trade on an exchange. The price of an Apple stock is the price of a share of Apple.

[00:25:02.12] When you're dealing with the bond market, you're dealing with an over-the-counter market, meaning there are market makers, dealers that have bonds and all becomes about access. The power of our platform lies in the choices that you have as an individual investor.

[00:25:19.64] If you look here on the left, we, on average, have 75,000 unique bond offers and 120,000 total offers, difference being that some bonds have multiple offers. When you use the Fidelity platform, you're not just seeing bonds that Fidelity owns. We connect you, through these three aggregators here, to a vast dealer network. And some bonds could be from some of the largest banks and broker dealers out there, could be smaller regional dealers, but this is a huge revolutionize and bond market.

[00:26:01.43] Years ago, if you were looking for-- run of the mill municipal bonds, you'd have to call a broker. And that broker would maybe have their desk or

maybe another platform with a few other offers. Here, you have access. And this helps you in a few ways.

[00:26:18.96] One, it gives you more choice. It also creates competition between dealers. If two dealers own the same bond, they can see where there-- are they best offer out there? Also creates narrower spreads, better pricing, and better liquidity.

[00:26:36.46] So this is a huge point. And we will get into, how do we narrow this down? But you want in a market-- in the fixed income market, having choice selection options to choose from, Pete, will help an investor build a strategy more accustomed to them.

Pete: Yeah, so I want to get a little crazy here. I know we're talking bonds, so it makes a lot of sense to get crazy. So, James, it sounds to me like this is somewhat revolutionary. And it almost sounds very parallel to, say, like a depth of book, level two type data, full montage type data on the equity side where you're able to see the transparency of bids and offers. Is that essentially what's happening in the way that we're aggregating bonds within the core within the platform?

[00:27:28.83] **James:** Yeah, it's becoming a more exchange-like experience in the bond market. We will show you-- and we'll get into this a little bit. We will show you-- there's a way on the Fidelity platform if you want to see every recent trade of a certain bond, say, like a municipal bond, you can see every trade that's been out there. And in the Treasury market, you may see the first price as the best price listed. But any one of these treasuries, Pete, if you pull up, say, just a one year Treasury system-- so now we're—

Pete: So, look, again, I'll just call out. What I just brought up here, James mentioned this a few minutes ago, being able to access the inventory. So in particular when you come into that Fixed Income Bonds and CDs landing page-- I'm scrolling down slightly-- this Yield tab, this is like the tabular version of the yield curve across essentially all sub asset classes of the bond market.

James: And, yes, and this is a great starting point because now I'm seeing the rates. I'm seeing the time frames. I'm seeing the different products pitted against each other.

Pete: So, James, maybe you can just speak to one thing here really briefly. I'm noticing we're looking at the highest yields out there. Is that the best approach

for us to assess the curve? Or would it make more sense to toggle over to media? And what do you think?

James: When you're looking at highest yield, say, in the Treasury market or, say, CDs where you're dealing with either a US government guarantee or an FDIC insured product, then it's a credit neutral. So I would look at the highest rate in that time frame. But when you look into, say, corporates or municipals, the highest yield could be something. Either it could be a credit that I've seen a recent downgrade or bad news. It could be something that trades overseas for the most part. So you would want to use the Median yield tab so that you get a more accurate gauge of the market.

Pete: Great, great. And then you had mentioned if we were to go into, for example, one year treasury, we're able to dive deeper into to see additional details related to not just a particular issue but really anything that's out there right now.

James: Right. So you're seeing a bid side and an asset side of the market. So you're seeing, OK, if I own this Treasury today, this is where I could sell it. If I want to buy this treasury, this is where I could buy it. And that speaks to that transparency of the platform. And let's pull up the depth of book here.

[00:30:00.80] So we're just looking at-- on this particular Treasury bond, you can see how many dealers we have and how many different offers are out there on this one bond on both the bid and the ask side. And there is the Recent Trade tab. So with municipals, corporates, that's something you'd want to use that you can see the recent trade history.

Pete: Got it. Now, this is really helpful, James. Thanks for walking us through. I'll toggle back over to our prepared content just for a moment here because I do think it's really worth calling out to James'es point, like, the unique bonds that are being offered and the total offerings available to any investor within fidelity.com can be found very easily and very quickly just from that News and Research tab going into Fixed Income Bonds and CDs.

[00:30:57.92] But to that end, James, I mean, what should we be looking for? I mean, I get that it depends on the sub asset class to an extent in terms of defining the parameters of our system or our strategy. But what are some really important and key aspects of diving a little bit deeper into searching for bonds?

James: The art and the science to it becomes narrowing down such a large universe of options to a manageable amount so that you can pin it to your risk

tolerance, your time horizon, and what asset class may make the most sense.

So, for instance, here, if we're doing a search for municipal bonds, we have 75,000 as average. But within the last two weeks, we actually hit over 100,000 unique offers.

[00:31:51.93] So if you pull up the munis-- the tab here-- so what we're doing is we're refining the vastness of what's out there into a manageable amount. So you can sort by maturity dates. So, say, we wanted, Pete, to look at January of 2024 to December of 2025, for instance, say, we wanted to do something a little bit shorter term, and let's say we only wanted to look, Pete, in the ratings column at AA minus or higher, so AA3 or higher because we want to stay higher quality.

[00:32:28.68] And let's go to the left. Let's say I'm in the state of New Jersey, for instance, and I want to see just my home state. And then, Pete, on the left in the Moody's rating category, make that AA3. Yeah, right there. And then on the right, just leave that as All. And same with the S&P, move the left to AA minus. And, yeah, as All, perfect.

[00:33:04.87] So now I've narrowed down that 80,000 something bonds into 100 different bonds that have my criteria, one to two years, AA or higher in my

home state of New Jersey. And you can see that Pete is going to pull up the results here.

[00:33:23.61] Now we're getting into all the data points that we provide. You can see the coupon, the maturity date. If it's callable, we'll put the call schedule in there. And on the right, you can also see the dealer, the amount that they have, the minimum quantity, and all the yield metrics you'd want to use when you're evaluating.

Pete: So, James, if we don't see anything in depth of book, what does that mean?

James: Municipal bond market is very fragmented. There's something 50,000 issuers. There's over a million different individual cusips, and so less than 1% trade on a daily basis.

[00:34:02.06] So when you don't see a depth of the book, what you're seeing what you're seeing is there's only one offer right now out there floating around on that exact bond. It's unlike the treasury market and the corporate market where it's generally speaking a two sided market. You can buy an individual piece at any time or sell an individual piece at any time.

Pete: So, James, if I were interested in, and just for the sake of random selection, the first result here, which looks like it's some sort of fire commissioner bond that's some geo bond, if I click into the description, what are some key areas that I would want to consider looking at if I'm targeting a muni strategy?

James: That's a great question. So first, if there is a research report out on that bond from Moody's, this one only has an S&P rating, but there would be right under Research Report, that any time you don't understand the issuer, that will go into great detail about outlook, rating history. Some of the other things you want to look at when you're analyzing the bond in the ratings category certainly worth looking at.

[00:35:10.67] If you go to Price and Performance, Pete, and the tab there next to Overview, this is where you can see, OK, I've got yield to maturity, yield to worse. On the right hand side, for some of our more advanced investors, some of the duration and OAS numbers that you'd use. But there's also a few recent trades, Pete.

[00:35:33.11] So if I know these bonds are listed at a certain price today, maybe I want to get a gauge on where this bond has been trading in the market. And to your question earlier about transparency, so there's not a lot of recent prints

but there are some, you can go in. And any trades that have been done on this exact bond, we'll post here on the Fidelity site.

Pete: Great. So, James, I think we probably best pivot a little bit here just for the sake of time into-- this is more of a reflection of the corporate space where we were looking at the muni space. Is there anything in particular you would call out like on a corporate compared to a muni [INAUDIBLE]?

James: Yeah, certainly I would leverage the resources. So when we pulled up that latest research report on that bond, it wasn't anything recently. But, again, look at the research report. We also link to any research reports that are out there on the equity side. So you can go into good detail.

[00:36:35.13] You can also view any recent events. So you can look at, was there a downgrade, an upgrade, mergers, acquisitions? All of that is in there when you're doing your more granular security selection searches.

Pete: Good. So I imagine a lot of our clients are interested in munis, and that's probably a perpetual interest. But what about on the new issues side, James? What can folks do on the new issue front?

James: New issue side, and I think you should definitely, definitely if you haven't done this under News and Research, you can sign up for alerts. And some of your options and alerts, one, you can get an alert any time that there's a new issue municipal in your state, or you could select a few states or all states.

[00:37:26.18] If you want to get an email alert any time that there's a new issue, the Fidelity platform is great. We'll send you an email. And you'll get the email, and you'll be able to look at the terms of the deal, the expected yield, the different maturity tranches. And that's a great way to get alerted because sometimes new issues can be time sensitive.

[00:37:47.12] And on that same alert screen, you can also sign up for notifications if you have a bond that's upgraded or downgraded or if there's been a recent maturity. So definitely use that as a way to stay on top of your existing portfolio and new issues that are coming to the market.

Pete: So you make a really good point when you call out your existing portfolio. I feel like a lot of what we've talked to up to this point is highly applicable if we have a portfolio in place, we have ladders or other strategies in place across the portfolio.

[00:38:20.57] Could you speak a little bit to someone who's maybe just looking at the opportunity as rates have been increasing and they're thinking, let's deploy some cash, let's put some money to work within the bond market, in particular maybe on the ladder side. What do we give folks that would help them in managing ladders or putting together ladders?

James: Yeah, if you go to the next slide, Pete, we actually have a laddering tool. So this is if you're sort of starting from scratch. And you can enter purpose of the funds to, again, going back to your first point, define your strategy first then come up with a process. You can define what the strategy goal is, set your time horizon, set some of your rating and risk tolerance parameters.

[00:39:04.79] And our site, our tool, can go out there and actually create a proposal based on your custom inputs and what's available in the market. And this is a good tool to use if you're starting from scratch. And a ladder is a great strategy.

[00:39:21.03] And, again, something in terms of process where, let's say, you're just investing with a five year time horizon, you invest 20% of your principal one, two, three, all the way up to five years, that way every year you have a bond maturing. The other bonds get shorter. You've locked in yield for a longer

period of time. And that's, again, one of the strategies that investors are using now.

Pete: And once we have these strategies in place in the platform, could you speak to how we might use Fidelity to monitor and manage the portfolio outside of just looking for opportunities?

James: Yeah, absolutely. So ongoing portfolio, maintenance monitoring is very important. And we have a Fixed Income Analysis tool. So when you're on your home page when you first log in, you can find this in the Analysis section. And you can see it. It breaks it out visually, and it gives you all the data points you would want.

[00:40:18.36] So we'll break out your principal and market value, your annual cash flow, your average maturity. As you can see with the blue and light blue chart, you can take a look and maybe on the longer end, maybe I want to even out these maturity buckets a little more evenly. So maybe I'd focus my purchasing there.

[00:40:39.40] So it helps inform where you're at and where you want to go. And then you can also break it out and look at average credit quality, taxability,

concentrated positions. This is a great way to see your cash flow, identify opportunity.

Pete: Great. So for the sake of time here, James, I'm going to give you a 10 second blurb on the cost factor if we're looking to do this on our own so we can give Christine a chance to dive into, what if this is too overwhelming? But what would you say on the cost side?

James: We are very transparent and pride ourselves in that. In the secondary market, we charge \$1 a bond*. So on \$100,000 investment with municipals and corporates, it's \$1 a bond. I do a lot of appointments where competitors are still charging 1%, 2%. So that's a big difference with treasuries in the secondary. If you do it yourself online, there's no cost.

***Minimum markup or markdown of \$19.95 applies if traded with a Fidelity representative. For U.S. Treasury purchases traded with a Fidelity representative, a flat charge of \$19.95 per trade applies. A \$250 maximum applies to all trades, reduced to a \$50 maximum for bonds maturing in one year or less. Rates are for U.S. dollar-denominated bonds; additional fees and minimums apply for non-dollar bond trades. Other conditions may apply; see [Fidelity.com/commissions](https://www.fidelity.com/trading/commissions-margin-rates?urltype=https://) for details. Please note that markups and markdowns may affect the total cost of the transaction and the total, or "effective," yield of your investment. The offering broker, which may be our affiliate, National Financial Services LLC, may separately mark up or mark down the price of the security and may realize a trading profit or loss on the transaction.**

Pete: Got it. Well, James, thank you very much, sir, for giving us the walk through the context, that insight into how to manage strategies through Fidelity's Tools and Resources. Very helpful, very insightful.

[00:41:53.18] So if any of you out there are feeling a little overwhelmed right now at putting together your own strategy, identifying opportunities, and then executing and maintaining, we've brought Christine in to speak a little bit to, how do you invest through separately managed accounts, which give you that exposure to individual issues but also give you a construct of management to support the efforts that are basically tying strategy to your circumstances and why you're executing a strategy within the portfolio without doing all the heavy lifting on your own?

[00:42:30.44] So, Christine, would love to have you come to the stage here in our virtual stage and speak a little bit to investing in separately managed accounts and some of the work that you and your team do.

Christine Thorpe : Sure will, Pete. I'll be happy to do this. And certainly it's-- I think this portion is a great complement to everything James walked us through. So maybe we could just start on slide 19.

[00:42:55.66] You're right. I think for the fixed income separately managed accounts that we manage, I'll use this time just to explain what the product is and give everyone an overview into our portfolio management process. But a lot of the benefits that James outlined, you also get through the get that through the SMA.

[00:43:18.91] So first of all, a separately managed account is just an account that is comprised of individual securities that are owned directly by you as the client. And really the key distinction here is that those bonds or securities in the account are professionally managed or overseen by a portfolio manager, like Fabian Weinstein-Jones, who we heard from at the top of the presentation. Now, there's just a couple of advantages to using the fixed income SMAs for your fixed income exposure.

[00:43:50.84] So first, again, you're getting that professional management and investment expertise of the portfolio manager to go out and pick the individual bonds for your account, and then taking that top level view to make sure

accounts are diversified across the various sectors, maturities, and credit qualities. But certainly the portfolio oversight process does not stop there.

[00:44:15.83] So for our SMAs, we are also monitoring them on a daily basis to determine, do they need to be rebalanced? Are there coupon payments or maturities that we need to reinvest? So really, this is where we're working with our fundamental and quantitative research analysts and our trading teams to help with that monitoring of the names just to help us, again, determine also other times where we should liquidate a position and find better opportunities in the market.

[00:44:50.20] Certainly in addition to the portfolio, construction, and oversight that we provide, the other advantages of an SMA include certainly that transparency you get into your holdings and your trades. And then we do offer some ability to customize SMAs across certain parameters for both our taxable and tax exempt strategies. So, Pete, if we could just go to slide 20.

[00:45:17.12] I think, first of all, our SMA products that are managed by Fidelity's fixed income investment team are our intermediate municipal and our core bond strategies. I'll certainly circle back to those in a minute. But what I think is important to understand about both of them is despite the fact they cover

different investment grade bond sectors, our investment philosophy across both are the same.

[00:45:44.42] And really, we're trying to strike that balance between the opportunity to generate income but also deliver capital appreciation, of course, while managing risk over the longer term. And really, there's a few components to how we do this.

[00:45:59.70] So first I want to just, again, emphasize that we're making a lot of our decisions based on fundamental research rather than trying to bet on which way interest rates are going to move and trying to get alpha that way. We've just found over, again, the longer term, that's not a consistent way to generate outperformance for clients.

[00:46:23.55] And so because fixed income is such a complex asset class just given its size, the US bond market is estimated to be around \$50 trillion, and that's spanning a wide variety of sectors and security types. So we have a really robust team in place to help us parse through all of that.

[00:46:45.24] In fact, our fixed income research team has over 100 professionals. And that team is providing our investment or providing our portfolio managers with

really critical and thorough credit analysis and different sector perspectives.

And then, certainly, we're also getting a lot of quantitative modeling into the various areas that we invest in.

[00:47:08.07] And so just by virtue of Fidelity size, our research analysts are able to get in front of issuers directly. Oftentimes they may meet with these issuers in-house. They may be going through some of those really lengthy offering statements or prospectuses. And really, the point of all of that is to make sure the portfolio managers have a full picture of an issuer beyond just what you may get from some summary statistics.

[00:47:40.07] Certainly, our analysts are also taking advantage of the broader Fidelity resources. So on the corporate side, this may mean they're working with their equity counterparts, again, trying to get that full picture about an issuer. They may be also getting updates from our asset allocation research team just to help better understand, where are we in the business cycle or the overall health of the global economy?

[00:48:05.46] And so because of all this work we've done up front, we're able to be nimble and react really quickly to market opportunities. In our taxable strategies, we're often participating in corporate primary issuance that can

really offer significant value for investors. And usually we're just finding out in the morning of about a deal that that's going to come to market later that day.

[00:48:33.42] So, again, having done all the work upfront, being able to leverage the expertise of our research analysts and our traders can help us make those decisions on the fly about whether or not we want to add a name to a portfolio.

[00:48:49.92] Second, in addition to all the fundamental research that we do, we are ultimately looking to maximize yield that's going to take into account different risks, such as changes in interest rates, rating downgrades, and liquidity, much of which Fabian already highlighted earlier. And certainly, this year, managing interest rate risk, just given all of the rate volatility that we've seen as a result of the Fed's actions, has been extremely important. And so we've certainly devoted quite a bit of time to that component. We can go to the next slide.

[00:49:29.33] I'll just touch on briefly, how do we do all of this? And really it's our investment process is how we put this philosophy into action. So when you think about just the broad based Bloomberg Aggregate Bond index, that has over 7,000 corporate bonds in it alone. And that's not even the full index

composition. Other major sectors are US treasuries and mortgage-backed securities. And it's the same story on the muni side.

[00:49:59.39] So the Bloomberg Muni bond index has over 50,000 bonds. And that's covering the various state and local entities that issue debt along with things like public transportation systems, or nonprofit hospitals, or education entities. And so as we're, again, trying to navigate through all of this, really our active management takes into account a couple of different factors.

[00:50:25.76] So first, our quantitative team is screening out on suitable bonds, and they're narrowing potential names to purchase based on some of our fundamental views and our risk parameters. From there, we're really looking to the input from our research analysts. Again, we may be hopping on a quick call with them. Or now that we're back in the office more, we may be huddling on the floor just to get their latest views on a name that we're thinking about taking action on.

[00:50:56.53] And then certainly on top of all this, we're layering on our trading team's insights and getting their perspective on relative valuations and the most efficient way to transact in the marketplace. And then, of course, when you have this entire picture, our portfolio managers are evaluating all these

inputs and really utilizing their investment expertise and their macro perspectives just to make those final decisions on what is traded within these accounts.

[00:51:27.76] So maybe I'll just close so we have time for a question or two just on slide 22. But we do have, as I mentioned, two fixed income SMA strategies that are managed by Fidelity. So the first is our intermediate municipal strategy, which really provides the opportunity to earn tax exempt income.

[00:51:49.65] Within this bucket, you can opt for our national offering, which is buying new bonds across the country. Or California, New York, or Massachusetts residents can also opt for our state specific strategies. And then finally, we do have the option to exclude bonds that are subject to the alternative minimum tax.

[00:52:09.24] Our second strategy are core bond portfolios. Here, again, we're primarily investing in US treasuries, government related bonds, corporates and mortgage-backed securities. And we do have some ability to customize here as well for certain excluding certain issuers or certain sectors.

[00:52:29.34] Now, since both strategies are intermediate, we do run both with an interest rate sensitivity that's pretty similar to our benchmark to help us manage risk. And certainly across both, we're looking to generate income by investing primarily in high quality bonds with low default risk to protect principal.

[00:52:49.62] And the last piece I'll just close with is for Fidelity and our fixed income division, we're managing close to half a trillion in investment grade bond assets. And so our separately managed accounts are fully integrated into this infrastructure and certainly benefit from the research and the trading access that comes from a trading floor of that side and certainly as well the experience we have managing fixed income through a number of different market cycles.

[00:53:21.64] So I think, again, it comes down to if you want to have a fixed income portfolio, you want to have transparency into your holdings and your trades. And perhaps some ability to customize that, a fixed income SMA may be the right choice. So with that, Pete, maybe I'll turn it back to you.

Pete: Christine, awesome. Thank you very much for the insight. I think that in terms of the flow here, Fabian setting the stage in terms of context and giving us

some insight on the macro landscape, and then James showing us how to take that foundation and build our own house, Christine, you've shown us not just like a track home that could be built for us but a customizable home that could be built for us based on our circumstances and what we're trying to accomplish within our bond portfolio. So thank you very much

[00:54:16.41] In terms of key takeaways, again, remember, a lot has changed here over the course of the last year. So fixed income continues to contribute. Think of it as a balance to the portfolio, reducing volatility and protecting principal. Transparency, Christine's point, and James's point earlier around transparency into the market, it helps you align with your needs.

[00:54:44.43] And if you like to manage your investments on your own, we give you the tools. We give you the resources, the insights to help you make those decisions. But if you'd rather identify the strategy and have Fidelity run the strategy for you, by all means, reach out to your financial consultant. And if you do not have one, call your local branch and talk with them about your options of either getting a planner, or an advisor, or a minimum meeting with us talk through what you might need individually. So thank you all very much.

Audio End

In general, the bond market is volatile, and fixed income securities carry interest rate risk. (As interest rates rise, bond prices usually fall, and vice versa. This effect is usually more pronounced for longer-term securities.) Fixed income securities also carry inflation risk, liquidity risk, call risk, and credit and default risks for both issuers and counterparties. Unlike individual bonds, most bond funds do not have a maturity date, so holding them until maturity to avoid losses caused by price volatility is not possible. Any fixed income security sold or redeemed prior to maturity may be subject to loss. The municipal market can be affected by adverse tax, legislative, or political changes, and by the financial condition of the issuers of municipal securities.

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