Fixed Income

UNDERSTANDING CAPITAL STRUCTURE

What is capital structure and why does it matter?

Capital structure is key to understanding how a company finances its business.

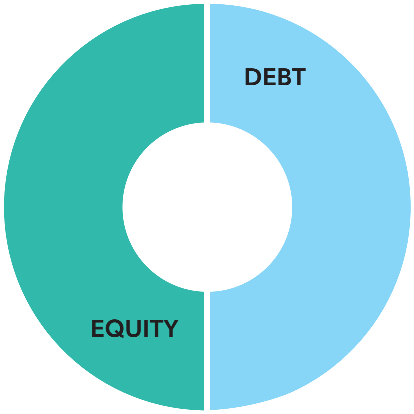
A company's capital structure is the combination of the debt and equity it uses to finance its long-term operations and growth. Debt generally comes in the form of bonds and loans, while equity broadly consists of common stock and preferred stock. Investors can look at the capital structure as the master financial blueprint of the firm. It can tell you which securities (bonds or stocks) might rank first when it comes time to distribute company profits, and which securities come later in line. It can also indicate which investors may benefit most in a reorganization.

The two pillars of the capital structure are equity and debt. Companies balance these two, making tradeoffs in deciding whether to raise debt or issue equity to finance their operations. The amount of debt that a company uses in comparison to equity (referred to as the debt-to-equity ratio or use of leverage) can provide insights into how risky a company is. Usually, a company that is heavily financed by debt is said to have a more aggressive capital structure (i.e., it has high leverage), and therefore poses greater risk for investors.

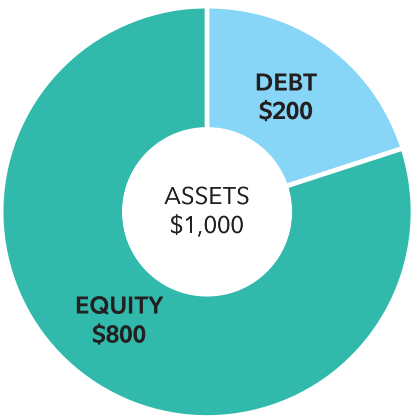
Equity is represented by the different kinds of stock offered to investors, and debt by the bonds and notes issued as a way to borrow money. Stocks can be either common or preferred shares. Common shares give shareholders an ownership stake of the company. Preferred shares often give shareholders the first right to receive any dividends a company pays.

Bonds, on the other hand, may be of many kinds: secured or unsecured, and senior or junior, or a combination of these. Secured debt gives an investor the primary claim to the cash flows or assets that are offered as security. Unsecured debt, in contrast, can generally be paid only from resources that were not otherwise committed. Senior debt generally takes precedence over junior debt when interest is being paid.

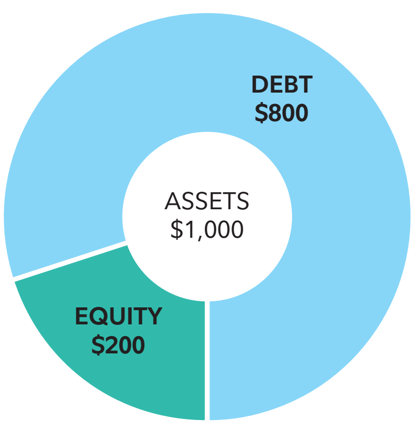
Capital Structure



Low Leverage

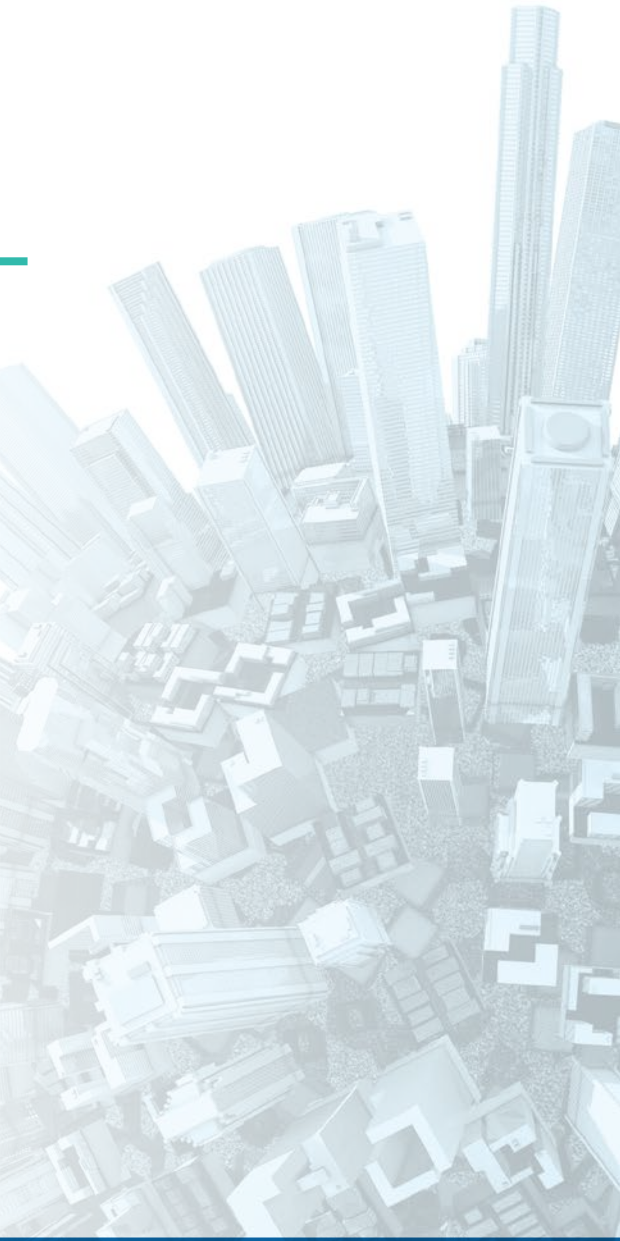


High Leverage



For illustrative purposes only.

360° Perspective



A company's stocks and bonds can have other features, but the basic capital structure that they make up is an essential consideration in making informed investment decisions. In evaluating a company's capital structure, Fidelity has equity analysts who look at a company's stock and fixed income analysts who review its bonds. Both perspectives are essential. Equity holders and bondholders can have different motivations to invest in a company, and a company might manage its messaging differently depending on whether it is talking to one or the other.

For example, when a company speaks to an equity investor, it might focus on growth plans that involve issuing bonds to expand production, or on projected stock buybacks or dividend payouts. This might be attractive to stockholders, but it could be detrimental for bondholders, as it could increase the risk that the company's bonds will not be repaid. Alternatively, a company might tell a very credit-friendly story to bondholders that focuses on balance sheet discipline or paying down debt – features that could be less attractive for stockholders.

Fidelity gets both perspectives: it has extensive equity and fixed income divisions monitoring and analyzing companies around the world – and exchanging their insights.

At Fidelity, there's no equity side and credit side: our analysts get a 360-degree view by hearing a company's pitch to bondholders and shareholders, not just one or the other. All this gives us an advantage over competitors who are focused primarily on equity investing or fixed income. Our 360-degree view of a company's capital structure enables Fidelity to make informed investment decisions for investors, based on a holistic view of a company's goals.

WHY FIDELITY FOR FIXED INCOME?

A global network

A wide investment reach through Fidelity's extensive global network of fixed income specialists, equity analysts and asset allocation professionals.

Integrated perspective

Connecting fixed income investment professionals with equity investment professionals to gain a 360-degree view of a company's capital structure.

Systematic approach

A team-based approach to fixed income investing that is clearly defined, repeatable and fosters deep levels of collaboration.

WHY DOES IT MATTER?

Through Fidelity's extensive global network, we gain access to a wide array of products, tools and insights. With investment professionals worldwide, Fidelity takes unique local market knowledge, identifies real investment opportunities and makes them available to you here at home.

We are research focused, with comprehensive global coverage of credit and equity markets. Our investment professionals gain insight into companies by combining views from both equity and credit research when making investment decisions for our clients.

Having a disciplined, repeatable investment process is a key element in navigating broad and diverse market conditions. At Fidelity, hundreds of investment professionals, including analysts, traders, lawyers, policy experts and asset allocators, collaborate to identify attractive investment opportunities that others may have overlooked.

Talk to your Fidelity representative today or visit fidelity.ca/**fixedincome**

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