Fidelity Viewpoints®: Market Sense

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TRANSCRIPT

SPEAKERS:

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JIM ARMSTRONG: Hello, and thank you for joining *Market Sense.* I'm Jim Armstrong with Fidelity, filling in for Heather today. Oh, we had to sum up what's going on in the markets over the past couple of days and weeks. I think uncertainty would probably be the word to use. The stock market certainly is feeling that.

Economic uncertainty overall is rising. Consumer confidence is down, as are estimates of first quarter growth. We've also seen upticks in unemployment, upticks in layoff numbers, and kind of constant drumbeat of policy changes at the federal level that have been casting a little bit more uncertainty on the overall outlook. So we really wanted to use today's conversation to help dig deeper into a lot of those different signals and then discuss possible ways to help you protect your money, regardless of what's happening in Washington or on Wall Street.

We have a couple of amazing guests absolutely familiar to people who watch *Market Sense*. Jurrien Timmer is here. He's Fidelity's Director of Global Macro. He's going to be looking at some of those big picture issues for us. And we also have Leanna Devinney with us as well.

She's a Vice President here at Fidelity and heads up a team of financial consultants in one of our Massachusetts branches just south of Boston. Leanna, Jurrien, great to see you guys.

LEANNA DEVINNEY: Great to see you, Jim. Welcome back.

JURRIEN TIMMER: Five years almost to the day is when we started this show, and it was the three of us. So great to see you both again.

JIM: That's exactly right. A little bit of an Easter egg for what's to come later on in the show, when we reflect on the fact that it has been five years of *Market Sense,* but we're going to start with what's happening today. It is Tuesday, the 11th of March. We have seen, to understate it, some serious volatility in the markets, in particular over the past couple of days, but really going back over the past couple of weeks.

Some of it has to do, of course, with tariffs and the threat of looming tariffs. Others have to do with some of the economic data that I was just talking about a moment ago. And really, when you put it all in context, Jurrien, a lot of what's happening very recently is coming off a two or three year really, really strong market. So a lot of people are looking at what's happening right now and asking, has the end finally arrived? Is what's happening now the beginning of a bear market?

JURRIEN: It's certainly an understandable question. And there's been so much to unpack. And actually, you know, we working, all of us at Fidelity, we know all about how much we use acronyms around here. And the new acronym I'm learning about is the TSNR, The Signal to Noise Ratio. And that's been a real challenge over the last, you know, four to six weeks or so is just to try to figure out what is real and what is noise. What are the things that we need to pay attention to in the markets, you know, as the political landscape continues to unfold.

And of course, it's happening at a time, as you mentioned, that the bull market, the cyclical bull market, started in October of 2022, is now about 29-months-old. So a little bit over two years. And the median bull market, going back 100 years, lasts about 30 months. That doesn't mean that we have one month left and then it's over. The median, of course, is a highly dispersed median of many different outcomes.

But because it's happening, you know, more than two years into a bull market when prices have gained a lot, right, about 70% and valuations are high, you know, people, obviously, understandably, start to worry about, is the show over? Should I get out? And of course, it's never that easy. We don't really know.

There are a lot of headlines. And I think what's been happening, of course, is that we had an election last November. That election was perceived to be too close to call at the time. And so the markets hadn't really done much going into that election. Then the election happened, it was a decisive outcome.

You know, the playbook for that outcome was played in the market. The markets repriced themselves very quickly. And the consensus was, OK, animal spirits are going to return. We're going to have deregulation, tax cuts are going to be extended. And yes, there's this tariff thing, but we're not going to worry about the tariffs because maybe it's just a negotiating ploy. And we're just going to kind of, you know, keep our fingers crossed.

And so this playbook was executed. Stronger dollar, higher yields, strong US markets, small caps as well. And now, of course, we're in 2025 and the tariff thing is a real thing. And we still don't know, like, how long they will last. You know, I mean, it's tariffs today. They get reversed tomorrow.

But I think the market is starting to have some headline fatigue, if you will. And so the markets are starting to price in the risk, maybe not the likelihood, but at least the risk that the economy will not be able to manage this uncertainty as well as maybe investors thought a few months ago. And it's not just the tariffs, of course. It's also, you know, the whole DOGE phenomenon and what's happening in Washington with federal spending.

And of course, you know, I'm not here to say that it's good or bad. I mean, chances are that the efficiencies that are being worked in Washington, in terms of federal spending, will have obviously a silver lining, because we're on an unsustainable fiscal path. But still, you know, if you reduce spending at the federal level, it means fewer people getting paychecks, and that, you know, that plays a role.

And so you have some actual contraction going on there, although they're not really showing up yet on the unemployment numbers. But you've got the uncertainty. And of course, tariffs, if they do lead to a trade war, which we don't yet know that they will, that tends to be stagflationary, right? So inflation could go up and growth could come down.

And so I think the markets, after being somewhat euphoric and confident that this was going to be a really easy landscape, are now having to reprice themselves. And I think that's why, you know, the S&P as we speak is down 10% from its high. And just a reminder, 10% corrections happen about 40% of the time, right?

So we had one last summer. And I think most people have long forgotten about that one. So hopefully, we will have forgotten about this one in a few months as well. But while it happens, it's obviously difficult to navigate.

The market goes up 60, 70% of the time, which means it goes down 30 to 40% of the time. And that's a fairly large amount of time. And navigating those periods is, of course, where Leanna and her colleagues come in, because we don't want to make emotional decisions when the market doesn't do what we want it to do.

JIM: I do, before we go to Leanna though, Jurrien, I did want to ask you a follow-up question exactly to that point. I mean, the stock market is, of course, but one data point in a sea of data points. But we know it's a forward-looking mechanism. And so when it starts to fall and fall precipitously, a lot of people worry if the rest of the larger economy will fall. We know that people are worried about it because they sent us questions over the past couple of days and weeks using the word recession.

So let me quote a couple of them for you here. "Will there be a recession this year?" "Is it close?" "Are we already in one?" Those are just three different ones. Jurrien, is it too soon to be asking that question?

JURRIEN: No, it's not. And, you know, maybe we'll have one, maybe we don't. I hate to give such a stupid answer, but let me just unpack. You know, the markets always are discounting the future. Now, they're not always correctly discounting the future, but markets are always ahead, right?

And so that's why five years ago when we started this show, the markets bottomed in March and were making new highs by June, even though the pandemic was still raging and earnings were still falling. And at the time, it didn't make any sense. But it always does, you know, after the fact.

And so the markets are a brutally efficient discounting mechanism. And every new bit of information is always being discounted. And that's why market timing is so difficult, because the price action doesn't line up with the things we see happening in the economy, right? Like, the layoffs, if there's a recession, there will be layoffs. That's usually one of the key things.

And we are seeing some in Washington, but not enough to bring the whole economy down. But by the time you really see that data unfold, the market has already moved on. So that's just a caution against market timing.

But the market can go up and down for many reasons, of course. And it can go down because of a recession, right? Because if you think about it, the markets come down to earnings, interest rates, and valuation. So if there's a recession, that would drop earnings, then prices come down.

If interest rates rise, that lowers the present value of future earnings and the market can go down for that reason, even though there's no recession. That's what happened in 2022 when the Fed was raising rates and the market fell 28%, there was no recession and we still had a bear market. So you can have bear markets that do not happen because there's a recession but because rates go up.

And then there's the valuation side, if stocks have just run up too much. For instance, right now, the Magnificent Seven, those big monster tech companies, even though the S&P is down 10%, those stocks are down over 20%. And they're so big that as they go down, they kind of drag the rest of the market with it. And that has nothing to do with neither interest rates or earnings. And that could just be a technical phenomenon within the market.

So short answer is, there are many reasons why the market can go down. And if it's a 10% correction on the way back to new highs, you know, further innings in the bull market, it would likely be really just a pricing, a repricing, based on uncertainty, but not based on a recession. If we do get a recession and it's a bad one, chances are the market would go down further because then you have an earnings drop. But so far, there really are very few signs of that happening.

JIM: All right. And let's not go too much further down that path just yet. But based on where we are at the moment, Leanna, we know certainly a lot of people may be checking their portfolio balances today. Don't like what they see. It's scary. It's uncomfortable.

Fully appreciate that. What do you and your team say when someone calls up or comes in to the branch and says, I want to go to cash, I want out of the market, I want my money someplace I perceive it to be safe and someplace I can get it freely?

LEANNA: Yeah, thank you. I've been speaking with my team a lot this week. You know, fortunately, we haven't gotten a lot of that just yet. But we are getting a lot of questions just around the uncertainty. And what we say often, no one likes market volatility. We don't want to be feeling these ups and downs.

But as Jurrien said, it is a normal part of investing. And so time and time again, we hear these words, I heard them often in 2020, 2022, and now a little bit of, well, this time feels different than other times of volatility. So what we share with our clients and investors is, is we do give perspective. And we use this chart just coming up on the screen.

And it really does explain, you know, how common market volatility is. You know, while unsettling, it's very normal. And what this is showing, you know, you probably see a lot of green and red on the screen here. But it shows the intra-year pullbacks. You know, on average, we see intra-year pullbacks of 14%.

But despite all of that intra-year volatility, and certainly a lot of times of corrections and even recessions during this period, you know, on average, the return has been 13%. And this chart's going back to 1980. And we've seen those that have stayed invested have had positive annual returns 36 of the last 44 times. 44 years, excuse me.

And you can see on the bottom here, it just brings that to life. If you invested $10,000 and you were able to stay invested, based on the assumptions of this chart, that 10,000 would be almost $1.4 million. So this is just a nice view to give that long-term perspective, because many are investing for the long-term. You know, even if you're close to retirement, we're hoping for, you know, 20, 30-year time horizon.

And investors who have been able to stick with their long-term strategy, not saying all in the stock market by any means, but a well diversified portfolio invested based on you, that has certainly paid off for investors.

JIM: Thank you for that. And not to be outdone, Leanna, I have a chart of my own that just sort of finishes your point. It was created by our Viewpoints team. Really just further explains what you were trying to talk about, the positive annual returns coming out a large majority of the time.

Since 1980, the S&P has experienced a drop of 5% or more 93% of calendar years. To Jurrien's earlier point, it's almost all the time that a drop of 5% occurs in the S&P 500. A drop of 10% or more almost half of the time, 47% of calendar years. But as you pointed out, overall, the average calendar year return since 1980 has still been more than 13% positive.

JURRIEN: And, you know, if I just kind of put some frosting on that. You know, there is no free lunch in life or for investing, right? So we know that stocks compound over 100, 150 years at about 10, 11% per year. But there's a price to be paid for that excess, that high return, and that price is occasional volatility.

So that is your admission. You know, that's what you have to endure to get that return. And the difference between the people who stay in and who don't is the difference between compounding those returns and just getting whipsawed by the market. And remember, even if you get the perfect spot to get out of the market, you still need to get back in at some later point. And like I was saying, price is always ahead of the fundamentals. So if you wait for things to get better, it's going to be too late.

JIM: Echoes, strong echoes of conversations the three of us had back in 2020 and 2021. One new element, though, Jurrien, I want to ask you about that we weren't talking about then is this idea of tariffs, right? That's the word that a lot of people are using for the first time, perhaps, over the past year or so. A lot of debate over whether or not tariffs could have a negative overall impact on the economy.

I want to ask you if the fear of tariffs, the unknown and the uncertainty, have that same power to drag the economy down, because right now that's where we are. We're not sure what's going to happen day to day.

JURRIEN: Yes, it's a great question. And so if you ask any economist, and I'm not an economist, but no one will tell you that tariffs are good for anyone. Everyone loses. It's just a question of who loses more, right? And so the stats that I'm reading is that if tariffs go up by 10 or 20% kind of across the board, it will shave maybe half a percent of growth from the US GDP.

So that may not be enough to cause a recession. It just may, but it does mean less growth. And if it comes with higher prices, you get into that dreaded stagflationary kind of fear of higher prices but lower growth. But for the countries that export, that really rely on exports to the US, it could have a much bigger impact if tariffs are, you know, relatively permanent.

And no matter what, they're going to do a number on the economic data, which may, again, increase—it may lower that signal to noise ratio. So right now there is one sort of nowcasting GDP thing by one of the Fed branches that shows that GDP is going to be negative in the current quarter, which would argue for a recession. But then you go into the numbers, and the reason the GDP is negative is because the trade deficit is getting sharply worse.

And why is it getting worse? Because companies are front-running tariffs by importing everything they can now while prices are cheap. And then the import versus export math gets all wobbled and you get to a negative GDP, even though the economy is fine. So you're going to get into all that kind of noise about what is even happening. But basically, tariffs are generally not considered to be good, although how bad or how good they are is very nuanced.

And it depends on many factors about whether companies can pass through their prices, and then the consumers pay higher prices, or whether it comes out of a company's bottom line. And also how much of it is offset by the dollar getting either stronger or weaker. So there is not a simple answer to any of this other than, tariffs generally are considered a bad thing.

JIM: And with all of those moving pieces, Leanna, I know you've cautioned in the past viewers not to be reactionary when it comes to making changes in their portfolio. One way to not be that way, especially if you have a long-term perspective, is to have a defensive strategy or a defensive outlook. Just talk a little bit about that if you could, please.

LEANNA: Exactly. So defensive strategies will come up often during times like this. And that's a preference to your strategy. So if you do have a long-term plan that's well diversified, it's likely best to stay the course. But if you are feeling that you want to make changes or you're even feeling I want to sell out, this is an option where you can add a defensive overlay.

A defensive strategy, it really has a track record when we look at the total return, they perform significantly better in down markets, you see a smaller drawdown. But there's a price of that protection, as Jurrien said, no free lunch. What it means is over time, it's typically you're experiencing a lower total return over time.

JIM: OK, so if somebody is willing to accept that trade-off, how do you start building that defensive portfolio?

LEANNA: So I'm going to show you an example of a defensive strategy we have that's a managed portfolio. It's a 60-40 makeup. 60% equities, 40% is the makeup of the allocation.

I'm going to start with the 40. So this would be the bond side. Typically how it's made up is going to be high-quality bonds and Treasuries. So high-quality bonds are typically less volatile than stocks. You know, Treasuries, as we know, backed by, you know, the faith in government. So more fixed investments.

In a traditional 60-40 mix, you might have bonds that are high-yield bonds or different corporate bonds, not as high-quality. So it's just that overlay of safer kind of bond exposure in that example.

JIM: And that's the 40, that's the bond side of it. How about the 60? The bigger side, the equities?

LEANNA: So the 60 is made up of the equities. And typically what we see in defensive strategies, this is going to make up of things like dividend paying stocks, low volatility stocks, some more what we call recession-resistant stocks, if you will. These are the defensive segments of the stock market.

So just giving some examples. It could be sectors we've typically seen, like healthcare, utilities, consumer, staples. Historically, these have been more recession-resistant than other sectors and have outperformed during downturns. So that's the defensive, during times of volatility.

And I would share this with investors over time. You know, no matter if you're in an expansion period or a recession, but in a recession, people are still buying toilet paper, paper towels, cereal, right, your medicine cabinet type items. Another is just high-quality dividend stocks. So companies that pay sustainable dividends, those are often less volatile, historically speaking.

These tend to be more mature companies, but they may experience slower earnings growth, but more stable than some of the faster growers. So you know, keep in mind, this is showing you a 60-40. You can have this defensive preference on whatever allocation, 50-50, 80-20. But that's the defensive strategy overlay.

JIM: Excellent. Thanks for walking through that. We are just about out of time. But as you mentioned at the top of the show, this month, March, is the fifth anniversary of *Market Sense.* We have a couple of old photos from back in the day, when the three of us launched this show in the throes of what, in retrospect, were the darkest days of COVID, with actually plenty of dark days to follow as well.

Lots of scary moments for investors and just for us as humans during that time. But I wonder if each of you could just reflect back in the past half-decade, as crazy as that sounds, what were some of the learnings, maybe, that we picked up during COVID that still apply today?

LEANNA: Jurrien, you want to start?

JURRIEN: Well, one thing I learned, as you see in that picture, is I had no idea how tall you were, Jim, because—

JIM: [LAUGHS] That's one.

JURRIEN: We'd always be sitting in a Zoom Room doing this. But, you know, this was obviously a few months after the restrictions were lifted. But, you know, COVID was five years ago. I've been at Fidelity 30 years. It's hard to believe that COVID is already 5 years out of that 30.

But you know, like I said earlier, price always moves faster than the fundamentals. And the market will reprice usually faster than we can rework our portfolio. And so having just a portfolio that makes sense to you where you are maximizing your risk-adjusted returns, letting you sleep, maybe not every night, but most nights, and then using periods of volatility to rebalance, right? To sit down with Leanne and say, OK, walk me through this. What do I need to know? Maybe I hadn't looked at the portfolio for way too long and now is a chance to do that.

Those are lessons that always apply, but when there's a really big shock, it really drives it home. And hopefully it was an opportunity for all of us and everyone watching to just kind of always be—you don't want to look at it so much that you're going to always freak out, but you want to look at your portfolio on a regular basis just to make sure it's still what you think it should be.

JIM: Yeah. Leanna.

LEANNA: Yeah, I remember that time. And we spoke to 100 of clients and investors during 2020. And just, it was a really challenging time, but really emphasized on the importance of having that investment plan, having a disciplined process in place.

But I would just say, you know, so much happens in five years. I look at myself. Back then, I didn't have two kids under four, and a home and, you know, all this stuff. So if now feels even harder because you're closer to retirement or different life events, it may be a great time to sit down with someone and just make sure you're in the right investment plan that you're comfortable with.

JIM: Excellent. We ran out of time to do Timmer's Take this week, but I want to thank you both for five years worth of fantastic insights and thoughtful context for our viewers. We really appreciate it.

As always, we do want to leave our audience with a resource to help you keep learning. So you can scan the QR code that you see on your screen to be taken to our Market Insights page, where we have Fidelity Viewpoints articles with deeper dives on a lot of what we talked about today, including more background on tariffs, on potential government shutdowns, as well as ideas for navigating choppy markets.

If you're listening to us as a podcast and can't see that QR code, just use this URL to be taken to the same page. It's an easy one, Fidelity.com/Marketvolatility.

On behalf of Jurrien and Leanna, I'm Jim Armstrong, filling in for Heather today. Hope to see you back here next week at our regular time, Tuesday at 2:00 o'clock, Eastern. We'll be talking about another timely topic, bonds. We hope to see you then.

[1]Bloomberg, March 7, 2025: https://www.bloomberg.com/news/articles/2025-03-07/us-hiring-rises-at-solid-pace-unemployment-unexpectedly-higher?srnd=homepage-americas

[2]Standard & Poor's, Bloomberg Finance L.P.

[3]Bloomberg, March 6, 2025: https://www.bloomberg.com/news/articles/2025-03-06/trump-likely-to-defer-tariffs-on-goods-services-under-usmca?srnd=homepage-americas

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