

Fidelity Viewpoints®: Market Sense

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TRANSCRIPT

SPEAKERS:

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HEATHER HEGEDUS: Hey, there everybody, and happy holidays. And thank you so much for making the time—I know it's a busy time of year—for *Market Sense*. I'm Heather Hegedus with Fidelity.

So this is the last full trading week of 2025 already, and it is a busy one. We are finally getting some jobs and inflation data that had been delayed because of the government shutdown. Also stocks are reaching new highs, and this time it's happening without the help of big tech, stocks which usually dominate the market. So that's pretty unusual, some pretty interesting developments as we get ready now to close out the year.

So to talk about all of this and what it might mean for investors, we are thrilled to be joined today by Naveen Malwal, who's in for Jurrien today. And he's a CFA charterholder here at Fidelity and an institutional portfolio manager. He and his team manage millions of client accounts here at Fidelity.

We're also thrilled, equally as thrilled, to be joined by Fidelity's director of quantitative market strategy, Denise Chisholm. So we asked Denise, who is constantly researching historical trends and opportunities, to do a little research for us here at *Market Sense*, as if she didn't have enough to do with holiday shopping and "end of the year" loose ends to tie up. So we asked Denise to put together a stock market report card for 2025 to help us be informed on performance from 2025 and put that into perspective as we try to prepare ourselves for success in 2026.

So this is the first time we've done this sort of exercise. Denise, thanks so much for taking the time to do that. I'm excited to unpack your data and get the takeaway from both of you. And, Naveen, great to see you.



NAVEEN MALWAL: Hey, it's good to see both of you.

DENISE CHISHOLM: Yeah, it's great to be back.

HEATHER: Well, today is Tuesday, December 16. Guys, this is our last *Market Sense* episode of the year, and we're going to finish out the year strong with this one. I'm really excited to hear your learnings, Denise, and the takeaways from this.

So first of all, let's just talk about—we always like to start with some headlines, and we got that big economic data that we had been waiting for this morning, the first new job market report since the government shutdown. And that data showed what investors might view as conflicting information.

It shows that job growth beat expectations for November. But the unemployment rate also ticked up, and it ticked up to 4.6% which is the highest level we have seen in four years. First, before we get into our discussion of the stock market report, let's unpack this, Naveen. Can you talk about what we learned from this report?

NAVEEN: Yeah, so this report actually captured two months of data, both October and November. And October saw a decline in jobs of over 100,000. That actually goes back to the Federal Government job cuts back in the spring. Many of those workers are given six months to find new roles, and the ones who did not finally filed for unemployment or are now considered unemployed as of October.

So you saw a decline take place in October. And then, as you point out, there was some job growth in November. You net that out, you did have some negative job numbers between the two of them.

Plus, unemployment is an interesting formula. What they ask is, are you looking for work? And if you're looking for work, are you finding work? So if more people are just looking for work versus a couple of months ago, that can also drive up the unemployment rate.

So the latest release, Heather, built on a theme we've seen most of the year, which is the job market is getting softer, so not a lot of hiring happening, not a lot of firing happening. But unemployment has been gradually ticking up higher. I think most people can feel it. It takes a while to get a job if you're looking for one, for example. There's occasionally headlines on layoffs.

But overall, the job market is still in a relatively healthy place, despite these trends. So what I look at is the level of unemployment versus this long-term history. It's still well below its long-term average. It's still well below the typical levels in recessions.

So despite the latest update, I think the job market is worth paying attention to. But it's not quite at the level yet where I'm getting overly concerned about it.

HEATHER: And, Denise, let's bring you in and talk to you, given your historical lens here. What does your data say about what this could mean for 2026? We're seeing softening continue. What could that mean for unemployment for next year? Could it continue to climb?

DENISE: Well, when you look at payrolls as an indicator and you think about whether or not I should buy and sell equities, we always say payrolls are a lagging indicator. So sometimes if payrolls or job growth is actually weak, that actually portends better news for the stock market ahead because oftentimes the stock market has already discounted it, which is another way to say maybe you shouldn't look at lagging indicators. You should be looking at something that's a leading indicator.

And we had one of those in the earlier part of I think it was this week or last week in the small business survey. And they have a survey that's gone back to 1977, and it surveys small businesses. And one of the areas that they survey is intention to hire.

And you saw a really steep inflection. That hasn't really happened in a long time. It's a top-decile inflection. And you can see that there has been a really strong relationship.

The more small businesses intend to hire, even though they're just one small segment of the market, the more likely the unemployment rate is to go down rather than up, which is a way to say, again, to Naveen's point, we're in a full employment position. So I wouldn't expect the unemployment rate to go down a lot.

But it is to say a lot of the leading indicators, if you had to bet on the job perspective getting better or worse into 2026, a lot of the leading indicators we're looking at suggest it's better. And this makes a ton of sense given that we've seen a friendlier Fed. And for the first time in a long time, the average company, not just the big cap stocks, but the average company is more profitable.

You put those two things together, and you end up with 70-75% odds that small businesses will intend to hire more over the next year. So we're starting to see surveys confirm some of the fundamental changes, which give 2026 a better outlook for jobs than what we've seen in the past.

HEATHER: Fantastic news. All right. We'll be watching alongside you with that, Denise. But let's start a discussion now as we look back on 2025 to help inform us for next year on the stock market.

We're calling this our stock market report card. And let's start with a big picture market question to kick things off, Denise. So we've seen some volatility in recent weeks, but at last check, the S&P had just such a tremendous performance this year.

It returned almost 18% year to date. That's phenomenal. Overall, that's the big story, a great year for the stock market, a great year for stock market investors. And those gains follow a remarkable recovery, from, thinking back to last spring, the tariff announcement, it led to an almost 20% sell off. So if we can start with just a 30,000 foot view from here, Denise, in other words, a really high-level view, can you talk about the major highs and lows for the stock market this year and the major indexes and what the highlights were in your eyes?

DENISE: Yeah, it did not end how we thought it would have ended, given how it started in terms of liberation day and the what we'll call the tariff tantrum. So I think a lot of times in markets, you tend to focus on the very visible headwinds because they are the most visible and flashing at you all the time. So tariffs were a big change and something that we haven't seen in a very, very long time.

At the end of the day, the headwinds associated with tariffs were enough to make the stock market discount something more onerous than ended up happening, meaning at the time of that almost bear market, stocks had discounted another earnings recession, which we hadn't seen since 2022. And given the fact that as we ended the year, earnings not only did not come down but stayed strong and earnings numbers had to come up a lot, you ended up in a situation with, yet again, the S&P put in a double-digit year with leadership from the NASDAQ and growth stocks.

So that's where the leadership had been coming into this year. And that's actually where the leadership stayed, which, again, you wouldn't have guessed with the headlines that we saw in April.

HEATHER: Anything to add Naveen?

NAVEEN: Yeah, just to build on that, thinking about how the markets performed, there was clearly volatility along the way. And with the millions of accounts that we manage, we get a lot of questions from our clients.

And the things I heard about all year long was, can the rally continue? The stocks are getting expensive. This tariff situation is unsettling. The administration that's coming to DC this year, they're making a lot of changes. How can the market possibly rise?

And what my team focuses on time and again are the same things Denise is pointing to. What is the economy showing you? Where's the earnings growing?

Historically, what we've seen is a lot of the headlines can feel like that's what matters, but at the end of the day, the fundamentals of the market tend to lean much more on the economic story and the earnings story. And as those were positive and probably better than how most people were expecting them to play out, not only did we see good growth in the US stock market, but as we'll talk about in more detail later in the show, saw a very strong performance overseas in international markets and even the bond market up almost 7% so far this year, which is an exceptional number for bonds.

Overall, a very solid environment for investors, despite all the concerns that are out there.

HEATHER: Yeah, and it's worth talking about that stuff that you brought up, international, bond market, and a little bit, Naveen. But let's stick first of all to our discussion about the stock market. And let's talk about what made the stock market so strong this year. Can you talk about some of the tailwinds, as you like to say, Denise, or, for folks at home, the primary key factors that really propelled the bull market this year?

DENISE: Yeah, the tax legislation was certainly one. We should not forget about that. There was a little there for the consumer, but broader based, it was a big cut in the effective corporate tax rate by R&D expensing and bonus depreciation and pulling that forward. So it was definitely an increase in profitability for corporate America, and that's certainly one driver of earnings.

But that is not the only driver that we saw in terms of tailwinds going forward. We did see a friendlier Fed because, despite the fact that tariffs increase some prices, there was not a broader-based rise in the overall inflation numbers to the extent that the Fed thought it would be, which allowed them to continue to normalize monetary policy.

And third, we should never forget that energy prices are, as much as tariffs are a tax increase to the consumer—we just don't exactly how much falls on the consumer—energy prices and decreases there are almost like a tax cut to the consumer. So energy prices, after two years of double-digit declines, declined yet again this year. And in some ways, if you try and add up the billions of dollars, that was the tax increase to the consumer under tariffs, it almost equated the billions of dollars in a tax cut to the US consumer from the decline in energy prices.

So again, it's always you got to be careful with the headlines because, what do they say? I think the quote is something like, anything negative hurts twice as is twice as bad as something positive feels. So I always think that we focus more on the negative numbers and don't exactly gravitate towards figuring out what those tailwinds were. But these are some pretty visible tailwinds as we enter 2026, which should support the overall economy and should support another year of strong earnings growth.

HEATHER: It's important to keep in mind. You're right. Anything negative hurts twice as bad as something positive feels.

So we don't always talk about specific stocks here on *Market Sense*. We're not going to do that today. But we do talk sectors, right, Denise? And I'd love to talk about who the big winners were this year as we talk about a report card for the stock market.

Obviously everybody's talking about tech still. But what else? Were there any surprises with the leaderboard?

DENISE: Yeah, the leaderboard was definitely technology this year. Communication services and information technology were the top two sectors, and for anybody who's followed the [? GIC ?] changes over the last couple of years, communication services has Google and Meta, so it's like information technology lite.

HEATHER: Thank you for explaining that because I think people might see communication and think telecom or think streaming.

DENISE: It also has telecommunication services and also has media. It was a conglomerated sector level. But it's dominated by those technology names that used to be in the information technology sector, like Google and Meta.

So it really has been, at least over the last year, a very strong tech-led market. And for some part of the year, there was a lot of staggered leadership between what was in, we call it the muddy middle of outperformers. And at the end of the day, industrials eked out the only other third spot of outperformance.

So you really only saw three sectors outperform the broader benchmark, which is a little bit atypical. Most years it's broader than that. It's more likely five.

But in some ways, when you go back to the fundamental data, you understand the reasons behind it because, certainly for this year—and it's not true of every single year—but stocks follow earnings. And information technology and communication services had the best earnings growth in 2025.

HEATHER: Just a follow-up question for you on tech because, in November, a lot of people were talking about the tech bubble question. It was the question of the month. And we did see some market volatility around AI valuations, concerns around AI valuations. So what is your latest take on tech stock valuations, Denise? Do you think they're overvalued?

DENISE: Yes. There's no debate that they're expensive, and let me define my terms. When you look back in the data, you can see that they are on a relative valuation basis or on an absolute valuation basis in the top quartile of their history. This is nothing like we saw during 2000, but let's just focus on the current levels that you see.

So if you look over the last 20 years and you say, OK, when they are in this top quartile position and they have strong earnings growth, is that a good setup or a bad setup as we enter the next year? And actually that has higher odds of outperformance if they're expensive and growing fast versus if they are cheaper and growing fast.

So it's an interesting twist on what you think you know about valuation. It's almost like, instead of really having a framework for a risk reward, valuation just tells you how strongly visible earnings growth really is because, if earnings growth is visible, stocks and sectors alike will price it in before that comes to fruition. But the driver of those sectors and stocks going forward is not always the starting point in valuation. It's usually the durability of that earnings growth.

So from a statistical perspective, yes, they're expensive. But no, that doesn't really dissuade me from having a strong risk reward into 2026 because it hasn't been predictive in the past. Said more succinctly that many times in the past when technology stocks were expensive, they still grew pretty fast and managed to outperform.

HEATHER: Very interesting twist on valuations, but big takeaway is, yes, it's expensive. No, it doesn't dissuade you.

All right. we talked about the winners. Let's talk on the flip side of things, about the laggards, the less-strong performers this year in terms of sectors. What were they, Denise?

DENISE: Yeah, it's a little bit the flip side of stocks follow earnings on the positive. It was true on the negative side as well. It was staples, materials, and real estate, and staples and materials had some of the lowest earnings growth that we've seen, really, for both sectors over the course of the last five years but certainly in the bottom of the segment this year.

So again, I think when you look at the leaders and laggards, it's not really a surprise, given the fundamentals were so strong for information technology and communication services and so weak for consumer staples and materials. Now, again, if you look at the patterns through history, this isn't particularly atypical.

What you see from a sector perspective is usually there are two or three sectors that lead by about 2,000 to 2,500 basis points and that lag by about the same amount, two or three sectors. And the rest are in that muddy middle. The interesting part or the twist that people might not expect was communication services and information technology only actually outperformed by about half that.

So when you look relative to history, yes would say it was a little more narrow, three sectors outperformed versus the average of five, so there were more sectors underperforming. But you would also say our leadership was only half as good as typical leadership usually is at the sector level, which is an interesting twist when you think that technology stocks might be extended.

HEATHER: Lots of twists that you're talking about today. But the bottom line, real estate, consumer staples, materials were the big laggards.

DENISE: You got it.

HEATHER: Or were the laggards, not big laggards, I guess I should say. Great insights, Denise.

By the way, I wanted to mention, we're always trying to share resources for further education on what we're talking about and our partners at Viewpoints just put out a weekly newsletter, an Active Investor newsletter, which is part of Viewpoints, with an article highlighting our sector manager's top ideas for the year ahead. So you can get articles like that sent right to your inbox by signing up at Fidelity.com/ActiveInvestor, which is there on your screen, if you'd like to hear more about some of the sectors that Denise was just talking about.

All right, Denise, thank you very much for that. Naveen, I know your team manages millions of client accounts, and you had a tilt toward international when you were coming into 2025 this year with your clients' portfolios. How did international stocks end up doing this year?

NAVEEN: So our tilt was there based on our expectations of earnings improving pretty dramatically for that group, despite some of the tariff headlines that were out there. And it managed to pay off. So just as an example, S&P 500 including dividends, up roughly 17% year to date through yesterday. International markets are up over 30%, and that's true for both developed markets, like Europe and Canada, and emerging markets, which include Asia, Latin America, and other regions outside of those developed areas.

And it's a pretty broad-based story. So looking at the countries that benefited from this, they included in developed markets, countries like Canada or Germany. And then in emerging markets, countries like Brazil, South Korea, really stood out as well. And the earnings came in exceptionally strong for those regions, and in some cases, the expectations are very low. The valuations on those stocks are extremely low, which can sometimes lead to a dramatic improvement in prices, which is what we saw this year from these firms across the board.

The other point I'll make, going back to the headlines, think about Europe, Canada, South Korea, Brazil. They were all at some point in the headlines for tariff news. So if you just do a shortcut and think, gee, there's tariff news happening, maybe I should avoid those markets, sometimes that kind of shortcut doesn't really pan out. It often pays off to dig deeper than that and look at the actual earnings story and economic development taking place beyond just the headline to get ideas for portfolios that extend beyond perhaps the most popular names that are always in the media.

HEATHER: Denise, let's talk quickly. We're tight on time here, but I wanted to talk about large and small caps quickly because you know small caps historically have returned more than large caps. So you'd expect small caps to lead. That hasn't been the case over the past few years.

We talked earlier about tech dominance and the concern tech valuations are moving too high. What has that meant for the large cap versus small cap debate? And what could that mean going into 2026?

DENISE: Yeah, valuations are still stretched going into 2026, meaning small cap stocks are still much cheaper than large cap stocks. But when you add up all the fundamentals in terms of tailwinds, what you do find is that fundamentals are probably still on the side of large cap stocks, meaning that tax cut was disproportionately beneficial to them and tariffs are much more onerous on small businesses.

So I do think that the risk reward, as much as we thought in the beginning of the year, given the valuation disconnect would be better for small caps, I think as we approach 2026, I wouldn't expect a deep period of small cap underperformance. I think the risk reward is still positive for large caps around the fundamentals. And I don't think that that's much of a surprise, given that secular bull markets, and that is what I expect that we are still in, are actually dominated by large caps.

HEATHER: And final thoughts from you, Denise, do you remain bullish going into 2026?

DENISE: Yes. Earnings growth is durable, and I think that that's almost the definition of a secular bull market.

HEATHER: And, Naveen, putting it all together, your takeaways for 2026 for investors?

NAVEEN: Key one really is to diversify. As I just mentioned, international stocks did exceptionally well last year. It's not all just about the US tech. There's other opportunities out there.

So by looking at the fundamentals, looking at different trends that are developing, don't presume last year's winners will keep progressing. They may keep progressing, but there's other opportunities out there. And for the folks who are concerned about volatility or market pullbacks, there's ways of investing in bonds or commodities or real estate stocks that may be able to provide some diversification benefits, just in case there are some hiccups in the stock market next year.

HEATHER: Fantastic, thorough discussion. Thank you to both of you for all the research and thoughtfulness that I know you put into preparing for this discussion today. Our next live show—with a replay available, of course, but it will be live first—will be Tuesday, January 6 at 2 o'clock Eastern. And I'm thrilled that both Denise and Naveen, along with Jurrien, will be joining me to be together in one room live for our 2026 Outlook Special.

And you can register by going right now to Fidelity.com/2026. When you're there, scroll down on that page. On the page on the left, you're going to see our *Market Sense* logo. That's what you need to click on to register for that 2026 outlook show.

The reason we're taking you to that page is because that's actually where all of our outlook thought leadership articles from our Fidelity Viewpoints team live. So there you can also learn more about six top investing ideas for 2026, and those ideas are organized by theme, if you're interested in doing more research on some of the areas that both Naveen and Denise hit on today.

I can't believe that was our last show of 2025, guys. That's it. It's a wrap.

Thank you so much to both of you for making time all year to come on here and lend your expertise every single week. And thank you to the viewers at home, who, almost 45 episodes this year, tuned in. So on behalf of Denise, Naveen, and Jurrien, who is with his family right now, hope you have a wonderful holiday with your family, and we'll see everybody next year. Take care.

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