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TRANSCRIPT

SPEAKERS:

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HEATHER HEGEDUS: Hello, there. And thank you so much for taking time out of your busy life to join us today for *Market Sense*. I'm Heather Hegedus with Fidelity. So the bull market is—has been continuing to charge with the S&P 500 reaching another all-time high last week. And now, investors are turning their attention to third-quarter earnings season, which could be key in determining how much higher the indexes can go in the short term.

And then the other big market story that has continued to play out since the summer, of course, has been the market broadening, with the market now showing strength across many sectors, and not just tech. And the equal weighted S&P is now also making new all-time highs. So to talk about that, we've got Naveen Malwal. He's a CFA charter holder and institutional portfolio manager here at Fidelity. And he's going to also discuss what this broad bullish March might mean for investors.

We've also got Leanna Devinney with us here today. She's a Boston-based vice president and branch leader. We asked her to come talk with us about the five biggest and most-common mistakes that investors seem to be falling into the trap of these days with election and tax season looming right now, right around the corner for us. Leanna is going to be sharing with us some tips and strategies for avoiding some of the most common traps, and staying level headed during challenging times. So a big welcome to both of you. Thanks for making the time.

LEANNA DEVINNEY: Thank you. Excited to be here.

NAVEEN MALWAL: Yeah, good to see you both.

HEATHER: And today is Tuesday, October 22. And Naveen, as I mentioned, quarter three earnings season off to a great start. Something like 21% of S&P 500 companies are set to report this week. So it's still pretty early in the reporting season. But so far, from what you've seen, who have been the big winners?

NAVEEN: Yeah, it's been a good start overall. We've had nearly a fifth of the S&P 500, so a little less than a hundred companies, already report. And we're seeing positive earnings growth, building on a trend we've really seen all year long, which has been a nice change from last year where earnings slipped slightly. So with these companies that have reported, on average, earnings are up about 5% or 6%. As you mentioned, it is early, but we'll see what the total number is for the quarter as these following weeks come in. So far, a very nice start.

One area I focused on in particular was the financial services area. They've had the most companies reports, a lot of banks, other financial services companies coming in. And they have very nice earnings growth north of 6% so far. That to me is a nice measure because banks are so tied in to so many parts of the economy that it might reflect well upon how other parts of the economy are doing overall, which includes consumers, businesses, and other aspects of the financial system. So a nice start to the earnings season. Hopefully, it continues over the coming weeks.

HEATHER: OK, and that's why it matters to investors, these companies reporting their earnings, because it can be a reflection of how the economy is doing. All right. We are just two weeks away from the presidential election as well. And just for a moment, take a step back and think back to what we've all experienced collectively in the past four years. We've had a global pandemic, then we had that supply chain crisis. Remember that? Historic inflation, and so many other events that impacted the markets.

So certainly, not the easiest of times to navigate in four years' time. So we thought today might be a good time to reset, so to speak, and ensure that we are making the right investment decisions as we get ready to enter the second half of this decade already. So we want to start with mistake number one, which is worrying that every market stumble could be the start of a crash. We were just talking about some of the events that do impact markets. But that doesn't mean that every event will. Naveen, what would you say to investors who seem to be particularly nervous when those kinds of dips come along?

NAVEEN: Right. And to your point, we've been through a lot in the last four or five years. You could add to that the stuff that's happened overseas, whether we're talking about Ukraine, Russia, which started in 2022, or with more recent developments in the Middle East, or tensions in China. In other words, no shortage of reasons for investors to get nervous, or worried about the markets. Yet, despite all of that, you go back to five years ago, before the pandemic even began, and look at where stocks are now. They have nearly doubled in value despite all of those challenges.

So that's the big takeaway today is, yes, there will always be something in the news that may cause concern, may cause worry, may even lead you to hesitate to invest. But over the long run, what we've seen is globally, economies tend to rise over time, and earnings tend to rise over time. The stock market at the end of the day is trying to reflect earnings growth.

So historically, the trend has been very positive despite really negative headlines. I would say what I focus on much more than the news headlines of the day are the fundamentals of the market, focusing on things like earnings, how the economy is doing, what's happening with interest rates. Those seem to matter much more to the long-term growth trajectory for most investors as opposed to the day-to-day headlines that can trip us up on occasion.

LEANNA: Yeah, and I'd also say that a lot of times, when we get those pauses or temporary declines, that's a signal that really the market is often processing new information. And investors, we sometimes have to take a pause. And it's not necessarily a bad thing, but we just saw last summer, there was a pretty significant steep dip in late July and early August. The market had to take a moment, and we were taking a look at new information from unemployment. And it was falling, and many investors were getting a little worried thinking it was the start of a bear market.

But after that, the market kind of reprocessed those new data points. And we've had significant highs since then. So sometimes, it just does take a moment to pause. And also, really make sure I've said this on the show a lot before, but stay true to the goals—to the goals that you have, and make sure that your investment strategy is aligned to those goals, and not the day to day of the market.

HEATHER: Fantastic point, Leanna, that sometimes those setbacks can feel so permanent, and they end up really being temporary. And then we're looking at them in the rear-view mirror thinking, why did I worry about that? And that's true with so many things in life. All right. Mistake number two is something that we try to discourage by sharing evidence-based data here on *Market Sense,* and that is trying to time the market.

So Naveen, what do you say to investors who are really watching these all-time highs right now, wondering if there isn't much room left for this bull market to run, and they're wondering if it's time to get out?

NAVEEN: Yeah, so market timing, often, people think about trying to buy the dip. But this is the opposite challenge. A lot of investors now are wondering, gee, the market's gone up so much. It's hitting all-time highs. It must be due for a correction. So why should I get in now? I think that might be a misrepresentation of how the markets have done historically. If you go back in time, looking back to the 1950s, for example, to today, so over 70 years of market data, we have seen many expansions with some occasional recessions here and there.

The expansions tend to last for years at a time. And as those expansions are happening, we typically have seen rising stock markets make new all-time highs for quarters, if not years, at a time. So it's not always true that an all-time high has meant that the market needs to correct or there's going to be a downturn. More often than not, the US economy is expanding, like it is today, earnings are growing like they are right now, and typically, historically, has meant rising stock markets.

So what we have typically seen is what's been playing out so far this year is we're making new all-time highs month after month. There are pullbacks. As Leanna said, there was a pullback this summer. And there was maybe a moment of market digesting information. But over the long run, the trend seems to be positive earnings, positive economy, new all-time highs. That is not a reason by itself to take a break from the market or to hesitate from putting new money into the investment space.

HEATHER: All right. Great news. And I know our director of global macro, one of the regulars on our show here, Yuri and Tim, are thinks that this bull market still has room to run. He thinks we're in about the seventh inning. All right. Moving on to mistake number three, focusing on narrow groups of stocks. So we've been talking about this this year, big tech has created a conundrum for a lot of investors because for the past two years, big tech was driving the bull market. But as the market broadens now, investors may be wondering if it's time to sell those stocks.

So Naveen, is there a risk in having too many eggs in one basket, even if the eggs in that basket have been doing really well, and up until now have been leading this market?

NAVEEN: Yeah, so all very good points. And the too many eggs in one basket is a conundrum either way. So either you might feel like you don't have enough, maybe you should have had more this whole time, or you have been the investor who is mostly focused on an area like technology the last few years. And now, you're wondering, gee, some of these stocks have gotten kind of expensive. Over the last few months, they lag other parts of the market.

International stocks did better than the US stocks over the last quarter. Most other sectors in the US did better than tech stocks last quarter. So if the market is broadening out, what does one do? And this is where it may be helpful to think about the risks one wants to take. This is a very personal decision at the end of the day. Some investors may feel very comfortable owning a smaller part of the market and dealing with the volatility that comes with that.

But most investors I speak with and work with day to day, they tend to want a smoother investment experience over the long run. And many of them typically may find diversification beneficial. So that is the idea of investing across different parts of the US stock market, not just technology. And it could include also investing in other parts outside of US stocks. It could be international stocks, or bonds, or other diversifiers that can help provide a smoother investment experience.

Over the long run, what are the trade offs? Hey, maybe the small set of stocks will continue to do really well. And maybe you will see extraordinary gains. But sometimes, these stocks, the story shifts. And the stocks can just do OK, or below average, or maybe even go through a correction at some point. The broader market tends to be less sensitive to specific things that might impact one industry or one part of the market. So they tend to have less volatility overall by looking at a combination of stocks and bonds, than, say, an individual part of the market or a handful of stocks typically done at a time.

So diversification, not a guarantee of profits, not a guarantee that you're not going to lose money. But it does generally, historically, provide a smoother investment experience than focusing narrowly on one slice of the market.

HEATHER: OK, and like you said, it can be a very personal decision. All right, Naveen. Thank you. Leanna, I want to bring you back in here for the next mistake, because another common mistake that I know you've talked about this year on *Market Sense* is seeing investors with too much money in CDs and other short-term investments. And we know that short-term investments have been a tempting spot in the past two years to park money because of higher interest rates.

But now, the Fed has started a cut. They cut in September. It's been priced in that the fed will continue to cut. So what is your message to people who still have a lot of money in these kinds of investments?

LEANNA: So this is a common conversation. Me and my team are having this almost daily, because you're right. Short-term CDs, treasuries, money markets, they've really come into favor among investors the past two years because rates have been so high. And many investors just feel comfortable in these investments because they're low risk. We always used to hear, cash is king. And there are some wonderful features to short-term investments because you get flexibility, they're liquid, they feel safe.

But investors with a long-term outlook have historically been better off with different parts of the market. So thinking growth vehicles like equities, or the diversified strategies Naveen was just talking about. So I just say the key challenge with the short-term investments really is lack of stronger growth potential because it's inability to keep pace with inflation over time.

So I'd say although rates on these investments may appear attractive, even just looking at the runup in the markets and how strong it has been, you have the potential of missing out on those types of returns if you're not in a strategy aligned to what your goals are. So if you have a growth type of goal, or you don't need to use the money for a longer period of time, it'd be really advantageous to look at some other options.

HEATHER: What are some other options for anybody with money in short-term investments? And what if you need that money for something like a house that you kind of need access to that money in the short term?

LEANNA: And that's very valid. So I would say it depends on the goals. So for those that need access and liquidity, like a home, the most suitable option is going to stay in short-term investment vehicles like cash, money markets, or short-term CDs. That's when you know, OK, I need this money back in three months, six months.

For those who have a longer-term horizon, but they also want to stay conservative, it would be worthwhile exploring longer-term CDs, or more moderately invested portfolios. But investors who have overallocated to cash just with due to the high rates, this could be an opportunity to just revisit your goals, revisit your investment strategy, and start exploring things like that diversified portfolio.

We have conversations with investors recently about a strategy called dollar-cost averaging. And this is a helpful way for many to really ease back into the market. And it's a strategy where you invest your money in equal portions, regular intervals. So you can do small amounts over a period of time. And basically, you're purchasing on this intervals. So regardless of the stock market being high or low, you're getting into the market kind of slow and steady wins the race in that example. But that's been a great way to get back into the market and align to a strategy that makes sense for you.

HEATHER: OK, so that's a way you can get invested over time, small increments. Baby steps. All right. All right, Leanna. Thank you. So finally, we know a lot of our *Market Sense* viewers and listeners are DIY investors, meaning doing it themselves. And often, one thing that DIY investors tend to overlook or not take into consideration as much as they should are taxes. Failing to factor taxes into investing decisions. Is the final common investing mistake that we have pinpointed.

Nobody wants to get a giant bill at the end of the year. So Naveen, what do investors need to think about when it comes to this time of year when you're trying to make sure that you've got all of your accounts in the most tax efficient funds?

NAVEEN: Yeah, there's so many things that an investor has to think about. And taxes is right there near the end of the list. But it is something that can affect your returns maybe a few months after you've actually taken your transactions on your account. So for a lot of brokerage accounts, some investors may feel, this is the place where I want to have more short term views over time, make some adjustments based on the new cycle, or other variables that I consider important.

The trade off there, though, is the tax code tends to tax investments that are held for less than a year at a much higher rate than something considered a long-term investment, which is something you have held for more than a year. So if an investor isn't careful about that, they may wind up giving up a big chunk of their gains back in taxes at the end of a tax year. There are strategies available to help minimize this, though, to help manage the tax impact of the different transactions that may take place in their accounts.

So one idea is to focus on short term versus long term. The goal here is, see if you can find ideas that you do believe in enough to hold on to them for at least a year, because that can significantly reduce the tax impact once the tax year is over. Another area to consider is investing in more tax-efficient investments. One classic example in the bond space is looking at municipal bonds because their interest is not as taxable as, say, a corporate bond, or even a federal government bond, in most cases.

So that can be an attractive opportunity. Other options include looking at exchange-traded funds, or ETFs. They tend to be more tax efficient by design, or even looking at mutual funds that specifically are looking to manage their investments in a more tax efficient manner. There's more that an investor can do. Those are three things to think about at the outset.

HEATHER: All right. You mentioned mutual funds, ETFs. How about you, Leanna? What strategies do you talk about with clients to help make use of investment losses and taxes?

LEANNA: So there are a few strategies out there. And I'd say it's all about we want to keep more of what you're earning and we have to be tax smart with our investing. So investors who do have mutual funds, ETFs, or individual stocks in your taxable portfolio, one common strategy we talk about is a mechanism called tax-loss harvesting. And that's really the mechanism and strategy out there where you can sell investments that incurred at a loss, and no one wants that loss, but then you can replace them with a similar ETF or mutual fund in this example, in that same asset class.

And by doing this over and over, your tax loss harvesting, you can net those gains and losses against each other and essentially minimize your tax liability. So tax-loss harvesting, it can achieve several goals. So first, again, minimizing your tax exposure to capital gains that you have. And we're talking long-term capital gains. It's just a way, again, to manage risk in your portfolio. Many investors won't sell because they're buying and holding. But this is just a great way to, again, to minimize taxes.

Just things to be cognizant of, though, is wash sale rules. So the rule generally states that your tax loss will be disallowed if you buy that same security back. You have to wait 30 days. So with strategies like tax-smart investing and tax-loss harvesting, we would say to work with a tax professional. And we can help—or a financial professional, and we can help navigate and talk about some of these strategies.

HEATHER: All right. Excellent examples of strategies and of things to be cognizant about. Great discussion, guys. Before we go, we always like to talk about what investors might want to be paying attention to this week. So Naveen, what's on your radar this week?

NAVEEN: So along with the continuing earnings season, I'll also be looking at factory orders to see if consumers are back into buying bigger-ticket items. And then also looking at both the jobless claim numbers, and consumer sentiment to gauge how they're feeling overall.

HEATHER: Factory orders. OK, we don't hear that one too often on what-to-watch segment. All right, Naveen, Thanks so much. On behalf of Naveen and Leanna, I'm Heather Hegedus. We will see you back here next week. And remember, we are live Tuesdays at 2:00 Eastern. Take care, everybody.

[1]CNBC, October 18, 2024: https://www.cnbc.com/2024/10/16/stock-market-today-live-updates.html

[2]Fidelity Viewpoints, October 2024: https://www.fidelity.com/learning-center/wealth-management-insights/5-investing-mistakes

[3]Fidelity Viewpoints, August 2024: https://www.fidelity.com/learning-center/trading-investing/smart-investor

[4]Fidelity Viewpoints, November 2023: https://www.fidelity.com/viewpoints/active-investor/managing-your-tax-loss-with-sectors

[5]Fidelity Viewpoints, September 2022: https://www.fidelity.com/learning-center/personal-finance/bear-market-investing

[6]Investor.gov: https://www.investor.gov/introduction-investing/investing-basics/glossary/wash-sales

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