

Fidelity Viewpoints®: Market Sense

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TRANSCRIPT

SPEAKERS:

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HEATHER HEGEDUS: Hello there, everybody, and thank you so much for joining us for this special in-person edition of *Market Sense*. I'm Heather Hegedus, with Fidelity. And we are coming to you midway through the year, where the headline is an economy that seems to be firing on all cylinders. And the stock market continues to reach new all-time highs. And that is thanks to accelerating profit growth, renewed excitement over AI, and a pretty resilient job market.

We're going to be unpacking all of that today, and what it might mean for you, and also talk about potential risks and opportunities with a pretty superstar team of Fidelity professionals. I'm pretty thrilled that you all said yes when I gave you an invite to this conversation.

And I'm thrilled to be joined in person today by Jake Weinstein. He is a senior vice president on Fidelity's Asset Allocation Research Team, or AART, as we like to call them in-house. And their team helps to inform Fidelity portfolio managers and investment teams. And today, you're going to be talking about the economic backdrop and outlook for the rest of the year, Jake.

We are also delighted to be joined, as we often are on these outlook shows, by Denise Chisholm. Of course, she is Fidelity's director of quantitative market strategy, and she's going to be sharing her historical data approach to try to help identify potential stock opportunities.

And last but not least, rounding out the roundtable today, we have Scott McAdam. He's a CFA and an institutional portfolio manager on our Strategic Advisors team here at Fidelity, which manages millions of clients' accounts. And you are here to put together the information that we're going to get today from Jake and Denise and talk about what that might mean for your portfolio.

So we've got a great gang of three today, switching it up a little bit with a new face here, Scott McAdam. Thanks for making the time to come on your first outlook show.

SCOTT MCADAM: Oh, it's my pleasure. Thanks for having me.

DENISE CHISHOLM: Yeah, it's great to be back. Thanks for having me again. Always.

JAKE WEINSTEIN: No, I'm very happy to be here. Let's get going.

I will always extend the invitation to you three. I'm really excited about this. Let's get right in, because we have a lot to talk about. We got a jam-packed show for our audience today. And Jake, I want to start with you, as one of our senior leaders here on the Fidelity team that informs investment teams, just like Scott's. I think it would be helpful, like we often like to start these outlook shows, with a quick level set. Find out the lay of the land here.

So many Americans right now are really going through hard times, Jake. And I think that's really important point as we level-set here, that things cost more these days. We've got higher gas prices. We've got inflation that seems to be really sticky still. And yet this economy has been so resilient.

It's been remarkable. The economy keeps taking punches, and yet this economy has, a couple of times, seemed like it might be tipping towards a recession, and that never happened. So, in your team's mind, where are we right now, in terms of the business cycle, and how strong is the economy?

JAKE: Yeah no, absolutely. So it is obviously very difficult and challenging with these noise that comes out. We have headlines all the time that get us distracted. But you take it back a notch, focus on your question, which is very important on hand. And we feel, when we're looking at the US economy, even the global economy—we think we're in a solid expansion, and even, in the US, specifically, in a midcycle expansion.

Now, historically, when you're in a midcycle, that's a very good signal for equity markets. They tend to do very well during midcycle. Earnings tend to do well. The job market holds up. Inflation is a little bit of an issue, but not too bad of a problem. You got supportive policies. Credit is flowing.

And if you look at all the things—and the US economy is extremely diverse—that's really what helps it stay in this type of midcycle expansion, even if you were to get some of these unexpected shocks, like oil prices going higher, or other things that we've been seeing, even as early as this year. So, big picture, economy's doing pretty well.

HEATHER: And I think that, for some consumers, it's not how they feel, and they're surprised to hear that, right? But those sound like really solid signs that you just pointed out, Jake, so let's dig into what's working and what's not working right now.

And Scott, I'll turn to you for that. So we've seen some pretty wide performance gaps this year, when it comes to the stock market. Can you talk about the leaders in the stock market right now, when we think of the leaderboard? And that might include other asset classes as well. What do you think?

SCOTT: Sure, absolutely. So, coming into 2026, we were expecting that performance would probably broaden out away from the AI pure plays, like the hyperscalers. And by and large, that's what's happened, but not necessarily for the reasons that we were expecting. So, for example, one of the top-performing asset classes are energy stocks in the first half of this year. Why were they outperforming? Really, based on an exogenous event that happened in the Middle East, the conflict and spiking oil prices.

Another similar situation happened with emerging markets. Emerging markets outperformed the rest of the world. Why? Not because global economy is booming. It's because the reach of AI investment was bidding up a lot of the big tech companies in Taiwan and South Korea. We saw small- and midcap outperform large-cap. We see value outperforming growth.

Jake just mentioned we were in midcycle. Typically, that rotation occurs in early cycle, as an economy is emerging from a recession. So basically, we've seen AI reach very far and wide, and the value and the small-cap plays have been more speculative names, are related to AI—say, for example, speculative types of energy technologies that have come around.

So this is all really just to say and to promote the benefits of diversification. You want to own large and small, value, growth, international, US, because it's nearly impossible to predict what the next best thing is going to be. We like to say, at Strategic Advisors, we don't predict. We prepare. And so, by owning a lot of different types of investments, you position yourself to benefit from potential growth over time.

HEATHER: So, speaking of diversification, we have to talk about these IPOs because they're just generating a lot of excitement right now, and investors are asking. We know that that is a question that I'm sure you are getting from investors when you speak with Fidelity customers. Can you talk about what, first of all, the market impact might be from these IPOs? And also, for investors, how is your team thinking about the role these IPOs might play in a portfolio, if any?

SCOTT: Well, the market impact is anybody's guess, right? But I think it's beauty in the eye of the beholder. On the one hand, you've got a group of very enthusiastic investors that are looking forward to new capital coming into the market and acting as a rising tide, maybe lifting all boats. So that's the bull case.

There's another group that's more pessimistic that believes that the size of these offerings is just so much that it's going to torpedo the market. Now, what I think is interesting about it is this is a good example of how headlines are provocative, and they can be somewhat misleading. What I mean by that is that the focus today, headlines and otherwise, is really on three big, big IPOs that are huge, right?

There are three companies. The market capitalization of these three companies is \$3 trillion or more. And when you compare that to the S&P 500, there's probably a dozen or so companies that have a market capitalization of \$1 trillion or more. So three of these huge IPOs coming at the same time seems very daunting.

But here's what the headlines aren't telling you. The actual amount of stock that's being issued is not \$3 trillion. It's a fraction of that. It's estimated between \$300 and \$400 billion. \$300 to \$400 billion is not chump change, but it represents maybe one half of 1% of the S&P 500. So it's a much more manageable amount for the market to take.

So it seems like, at least from the signaling of recent market performance, that the market is likely to take these in stride. We'll see, obviously. But the other question, or other part of your question, was, how is that going to fit into portfolios? It really comes down to the eye of the beholder. Again, it's the manager.

So our managers will be evaluating each of these IPOs in terms of its appropriateness of whether it belongs in their portfolio or not. They evaluate the risk, the return, and the correlation of what these new IPOs could mean for their entire portfolio to see whether or not it makes sense.

HEATHER: And that can also vary per investors' individual needs as well. All right, Denise, thanks for your patience here. All right, so we're midway through the year. Let's talk about the strength of this bull market.

So think back to that market volatility that happened in the aftermath of the Iran conflict. We had that quick market recovery that followed. It was pretty remarkable. And it just indicates what a roller-coaster year for stocks this has been.

And a lot of investors may be surprised, in fact, by just how strong this stock market is right now, given all of the events in the world that we have seen this year. It might even feel excessively bullish to some at this point. How does it look to you?

DENISE: When you look at it quantitatively, I mean, you have to know, as an investor, that the market is always a discounting mechanism. So that means that it can discount good news in advance, but it can also discount bad news in advance. So you often see stocks going up on bad news. That's actually not a surprise when you look historically, and I think there's a couple reasons behind it, with the headlines that we've seen to date.

One is that this entire cycle—and I mean that from COVID—has been a very persistent fear in the equity market that you can measure mathematically. And I think most investors get it. Every time something hits, whether it's tariffs—I mean, we actually had a bank run. What was that, in 2023? And what we've seen with the geopolitical conflicts—anytime that there's a risk, you see sentiment reset very quickly to a very bearish position that you don't often see outside recessions.

So there has been this persistent fear in the equity markets. That is what has allowed, at least historically, when you look at the data, the ability of the equity market to climb that wall of worry that we say over and over. So it's not really a surprise, and that persistent fear allows that to happen. So, as much as investors want to say, well, stocks are up a lot, and they're expensive, neither of those two facts bend your odds toward lower odds of outperformance in the future. What usually does is when the equity markets are, I would call, statistically complacent.

I think the second part that equation is that oil is different this time, relative to the '70s and '80s, and you can measure that mathematically as well. So when you look at real oil prices, certainly, they've spiked. We saw a spike in the 1980s as a result of the war we saw it in the 1970s. We even saw it in 2009, when you adjust it. The difference this time is the oil efficiency of the economy has declined by, or increased by, about 75%.

So it's the same prices hitting very much more efficient economy. So if you think back to, well, let's not try and correlate price—let's try and think through the impact of what higher oil prices might mean, specifically for equity market investors—what might it mean to corporate profits? And you rebase corporate profits. What oil would have to be, to have the same shock as that we saw in the '70s and '80s, is between \$500 and \$1,000 a barrel.

So that is how high oil would have to be to generate the same amount of strain that we saw back then. Look, I don't know where oil is going to go, but I think you would have to have much more persistent, pervasive, high oil prices to see the kind of economic impact that many investors are worried about.

HEATHER: Just to drive home that point, you said oil would have to be \$500 to \$1,000 a barrel to have the same impact as consumers felt, and businesses felt, in the '70s.

Exactly.

Wow, all right. That puts things in perspective, for sure.

So, Jake, Denise was just saying the stock market has been able to shrug off, for the reasons that she just illustrated, the developments in the Middle East and rising oil prices. But the risk with higher oil prices, especially for longer—my understanding is that it can creep into other

areas of the economy, that inflation can creep into other areas of the economy. There's a ripple effect. So where else are you and your team seeing inflation right now, and what's your team's inflation outlook?

JAKE: I think that's the absolutely important question here because I've seen a lot of different opinions, or people are saying, oh, this oil increase is a one-time supply shock. "It's transitory" is words we heard a couple of years ago from the Federal Reserve, which didn't wind up being the case. And we've got an inflation print coming out this week, so we'll see the first evidence of it coming in the data.

When we do our research on the Asset Allocation Research Team, and we assess what the impact is of oil going higher, oil going higher has an immediate impact on headline inflation, but it could take, actually, about 6 to 12 months for it to have an impact and bleed into other areas of core inflation, which strip out the volatile food and energy sectors.

OK, and it's only been 100 days—

It's only been a few hundred days. And it's really hard to assess, because you've got other things like tariffs coming on, coming off, a lot of other factors. You've got this CapEx build. So isolating everything is really, really tricky, in terms of trying to assess what the impact has been so far, this time around.

But if you look at past episodes of oil supply shocks, or oil prices just going higher, it tends to bleed into other things, like fertilizers, which leads to higher food prices, packaging, shipping, other things. And the point here is, if the economy stays strong, and it stays OK, to Denise's point, if the economy can handle \$90- to \$100- to \$110-barrel oil, then the economy should be strong, and it would ultimately, probably lead to higher inflation down the road.

So not expecting the '70s type of inflation. You'd probably need the \$500 to \$1,000 to get that type of double-digit inflation. But probably heading higher, which will have an impact on the way the Federal Reserve and other central banks are thinking about inflation, going forward.

HEATHER: Perfect segue there because you just mentioned the Fed. And coming to the second half of the year, we now have a new chair of the Fed. We have Kevin Warsh, whose views on monetary policy would appear, by most accounts, to be different than his predecessor. I think that's a pretty safe statement to make. How do you think this might impact the outlook for rates, going forward now?

JAKE: Yeah, no, it's a great question, and we'll get our first taste soon and see, ultimately, what happens. I cannot predict with precision what is ultimately going to happen at the June meeting or beyond. One thing I think, if you take a step back—this is more of a positive view—there

was a lot of uncertainty coming into the Fed chair announcement, and would there be political influence on the Fed? And we knew that the administration wanted rates lower.

And basically, the assumption back then was he's going to put somebody in that's ultimately going to lead to lower interest rates. That, actually, story and narrative has shifted over the last six months, with inflation now higher and, really, with the market saying to the Fed, oh, you may not be able to cut rates, and you have to increase rates.

And there's been no real pushback from the administration or the Federal Reserve yet on that, and the market doing well through that. That's actually a positive sign. So it's helped alleviate concerns about the dollar falling. You've seen things like gold go down. You're seeing less concerns about the dollar. They call it the dollar debasement.

And so, ultimately, that, to us, basically means, right now, the market is OK with the fact that a new Fed chair is going to come in, even if we don't know exactly what's going to happen.

HEATHER: It is pretty remarkable or interesting when you think about the fact that President Trump made it pretty clear that he wanted lower rates. He nominated Warsh, and now the market's pricing in a higher chance that we will have a rate hike, not a rate cut. And we'll see that by the end of this year, by the end of 2027.

And Denise, probably a good time to turn to you because I know a lot of investors typically think of rate hikes as being bearish. But I know your research suggests that might not always be the case. What do you think?

DENISE: We certainly saw that in 2022, but that is not typically the case. I mean, the interesting part is, when there is growth, the equity market has had no problem, historically, with higher rates. And right now, you can measure growth in a bunch of different ways, especially in the manufacturing economy.

But durable goods orders that we just saw, which are companies buying big machinery, and it's ordering big machinery—that tends to lead an economic cycle. When that hits top quartile levels, you do see higher odds of durable earnings growth. You see higher odds of durable job growth. And you also see increased likelihood that the Federal Reserve will hike.

Now, I'm not saying that they will. We'll see. But when that has happened, when growth is in those top-quartile levels, you have above-average odds that the market actually advances. So the market goes up 75% of the time, historically, and it goes up around 80% to 85% of the time when you're at this top quartile, vertical, in terms of growth, even if the Federal Reserve raises rates.

So I think that there's a more important point to be said around this that a lot of math corroborates. If you said to equity market investors, what would you rather—would you rather the Federal Reserve be hiking, or would you rather that be cutting—for your odds of an equity market advance, you'd actually rather them be hiking, just by threadbare odds, but a little more, because, more often than not, which is not to say every time, those rate hikes are a reflection of growth, not necessarily a deterrent to it.

JAKE: Denise makes a good point because it's not just about—so rates are going higher. It's typically because the economy is doing well and Federal Reserve is able to raise rates. It's about the speed of hikes as well. And so if you look through those instances, 2022—there was a lot of inflation, and so the Fed had to actually raise rates pretty quickly. And that wound up being equity market wobbling as a result. Same thing in 1980, when inflation was super high and the Fed had to raise rates super fast.

So it's not just about the direction. We get one or two hikes—that's not the end of the world for equity markets. It's if inflation gets out of hand and they have to start going really, really quickly, which is not in our base case and not what we see right now in the data.

HEATHER: Not your base case, but still the “why” on rates are being cut or raised matters, and the cadence of it, how quickly the Fed—

DENISE: The sweet spot for the equity market advance is actually between 0 and 100 in any given year.

HEATHER: Wow.

DENISE: So those are the middle two quintiles. The Fed cutting has lower odds of a market advance. Sometimes they're cutting because there's a problem. And to Jake's point, the bigger the increase, the lower the odds of the equity market advance. But the sweet spot is actually them hiking a little for the right reasons.

HEATHER: Which might be a little counterintuitive to some investors. And let's bring Scott into this great conversation, too, because there are a lot of factors that could cause interest rates to go higher from here, Scott. So could that be a concern for fixed income? And what might that mean for bond allocation in a portfolio?

SCOTT: Yeah. I mean, for a broad-based, investment-grade bond portfolio, I don't think it's going to have much of an impact at all. And we're talking a lot about math and odds, and I don't want to barrage the audience with this. But basically, it really does come down to math.

HEATHER: You're speaking Denise's love language when you start talking numbers.

I'm eating it all up, believe me. I'm loving all this. But the point is that, really, the math doesn't work, in terms of hurting a bond investor too much, because really, what we have is current yields in the bond market are around 4 and 1/2%, 3/4%, roughly. If you have a modest increase in yields—you know, prices come down—that 4 and 1/2 could cushion that yield increase. So there's a natural effect there to cushion that yield.

Also, the second reason is, if you're a medium- or long-term bond investor, you just wait because, if prices go down, you just wait until that bond matures and pays you back at par. In the meantime, you're actually investing in a higher-yield environment, and it could actually enhance your total return.

So, from a bond investor or bond manager's perspective, it depends on the cadence. It depends on where in the maturity spectrum the rises occur. If it's happening in the short end, maybe floating-rate notes look more attractive than, say, treasuries. Maybe on the flip side, like we've seen recently, with long rates going higher, the 30-year up above 5%, all of a sudden, now US treasuries look very interesting because you're getting a high yield at a relatively low risk.

So we use bonds for a specific purpose in our multiasset-class, diversified client portfolios, and that's to provide income and stability. So the higher the rates, actually, the more enhanced those characteristics may become.

HEATHER: So all, potentially, positive reasons that higher rates may not be a negative thing. But one thing that we know from Econ 101, Denise, is that higher rates do increase borrowing costs, and that can be a lag on the economy. And I know you're constantly looking at all the different market signals, but there are a lot of market signals to navigate these days. So I'm wondering what market signals are standing out to you right now. What are you honing in on, and where is it leading you, in terms of potential opportunities that we see out there?

DENISE: I think I highlighted the first one, which is to say this persistent level of fear in the equity markets. Always remember that the bottom in the equity market between the two back-to-back recessions in the '80s was before either of them happened. The market bottomed in 1978. So, despite the fact that interest rates went to 15%, we had two recessions, the higher lows were in place during both of those markets. So that just shows you the power of the discounting mechanism.

HEATHER: Probably priced in because of investor fear.

DENISE: You can't always think about, the more visible the threat is, the more likely it is to be discounted, which is, again, not always the case. But that, you should always think—once it hits the headlines, the probability that it's discounted at least goes up. But I think the more interesting part to the cycle that has been, I would call it, anomalous has been the fact that the average company has not been profitable in quite a long time.

So we all talk about the cap-weighted indices and the overall earnings, which is obviously dollar-weighted. But it was really driven by a handful of companies, specifically in technology. For the median or average company, profitability actually peaked in 2018.

So this has been not the same magnitude as that we saw, obviously, in the financial crisis, or even in the dot-com bust. But, from a duration perspective, earnings growth for the average company has been fairly stagnant, or in a malaise, if you were, in this sort of stagnation. And the important thing about that is the duration of that contraction is really symmetrical to the duration of the recovery.

So when you see earnings numbers coming up by a lot, it's almost like it's a catch-up, meaning that it was so behind for so long, we're actually now starting to finally see the inflection. And if this is finally getting past prior peaks, when you look, once the average earnings for a company gets past prior peaks, it lasts about four years. So this could be the beginning of what might be a more durable and diffuse earnings cycle.

HEATHER: OK. Let's talk about other leaders as well. You really like tech. You talked a little bit about tech being a leader while the rest of the market is not—earnings for US companies have not been—it's been stagnant, to use your term—"malaise." So tech is a leader in your eyes.

Scott, how about you? Where are you and your team and equity managers seeing potential for growth? Where are we right now?

SCOTT: These days, we've got slight tilts toward momentum, small- and midcaps, and international. Generally speaking, we look through sectors, so it's really more important—or at least our managers look through sectors. And we're looking for growth in lots of different places, whether it's in the tech sector. It could be geographic, geographically diversified.

And we can derive, or at least our managers can derive, growth from places that people don't necessarily associate with growth. So I'll give you an example, the healthcare sector. A lot of people think of the healthcare sector as being relatively stable and defensive, but within healthcare are biotech companies, and those are very fast-growing businesses.

You also have, these days, I mentioned, the demand from AI projects. The power demand and supply equation is benefiting some utility companies and the utility sector. They're working on cutting-edge technologies to try and meet the demand of these AI projects. So again, it's not necessarily about the sectors or the geography. It's about the companies and having our managers go out and find those opportunities for us.

HEATHER: We talked about this strong stock market, but I think it's really important to revisit what I talked about at the top of the show, too, as we take stock in where we are right now. And that is that there is still this disconnect happening right now between what the stock market is doing and how people are truly feeling about the economy.

And just to drive home that point a little bit, if you would allow me to throw out a couple of stats, food prices—up 34% since 2019. I know that's certainly something I feel when I'm buying for my family every week. National average for a gallon of gas was \$5 a gallon this year. It's trending downward now, but still up \$1 a gallon, on average, more than it was this time last year.

So, Scott, I was thinking maybe you could help walk us through this disconnect a little bit more between Main Street and Wall Street. And we get this question a lot from our viewers, so I'll pose it to you. What can people who are in or nearing retirement do about the way that they're feeling about this?

SCOTT: Well, it is very much a valid issue. People refer to this as the K-shaped economy because there are parts of the populace that seem like they're going down, and there's other parts that are going higher. So the general mood can be captured by a number of different indicators. One of the most famous ones is the University of Michigan Consumer Sentiment Index. It just hit its low of all time in May.

So that just gives you one perspective. That was begun in the 1970s. But at the same time, as you mentioned—we've been talking about this—the stock market keeps hitting all-time highs. You've got property values that are moving higher, and so household net worth is moving higher as well. So there is a legitimate issue that's going on there.

My best takeaway, for anyone that's in or near retirement, is to have a financial plan and to try and grow your wealth as much as you can handle. Really, if you've got a spending budget, you're almost halfway there. You just need to develop an investment plan that could partially—or, hopefully, fully—offset your spending budget. But it really is about being invested in the market to the extent that you can.

HEATHER: Being invested in the market via equities—that's one way that investors can position their portfolios against inflation. What are some other options that investors have at their disposal to try to hedge against inflation?

SCOTT: As you mentioned, I mean, stocks are a great performer, as it relates to long-term inflation. They tend to outpace. But there are specific types of investments—we call them diversifiers—that do have mechanisms within them that adjust to higher inflation.

A great example are US Treasury Inflation Protected Securities, or TIPS. TIPS are US government securities, so they come with the full faith and credit of the United States government. But they've got a mechanism that adjusts to surprises in inflation. Their prices move higher.

You also have commodities, the very things that experience higher inflation, things like lumber and oil and gold and copper. They keep pace, generally speaking, in the higher inflationary environments. And then we're also using real estate investment trusts as an inflation hedge.

HEATHER: REITs.

REITs. That's right. There you go. And REITs are a stock, but they're backed by a real property. So real estate tends to keep pace with inflation over time as well. So again, there's ways of layering in different types of investments that will increase the durability and the resilience of a portfolio in the wake of, or in front of, higher inflation.

HEATHER: All right. That was a pretty comprehensive answer, Scott. Thank you for that. And certainly, inflation is a big part of the story of where we are right now, but I would argue an even bigger part of the story of where we are right now is the AI story if we take a step back and think about the times that we are living in right now.

I would love to get your thoughts on—and I'll pose this to you, Jake—just how momentous this moment is in time. There are people who say, well, is this just another period of advancement, like the advent of the personal computer, or the dot-com era that Denise had mentioned? Or are we living through, right now, fundamentally different times? How should we think about this?

JAKE: Yeah, no. It's obviously a question a lot of people ask, and you get a lot of different answers, depending on what people think, based on their views of what the technology is. Some people are very scared of it and think it's going to be bad for humanity. Other people think it's going to be absolutely amazing and be a long-term productivity driver and drive inflation down and ultimately lead to higher corporate profits. So lots of different opinions.

Two different ends of the spectrum.

Very different ends of the spectrum, and it is very hard to know in real time. So what we assess and what we do is, to your point, look back at the past. We have data that cover over 200 years of technological transformations—to your point, the personal computer, steam railways, electricity. And there's a pattern that's actually pretty consistent across all of those.

And it's three factors. And basically, the first thing that happens—stock prices go up because they get excited about the new technology. And we're there, right? So we're there. Mark is excited about it.

And then what happens is companies, especially those that see the technology being more accepted, realize this, and they start doing the capital investment. And we're seeing that from the hyperscalers, huge numbers coming across, investing in AI. But Scott was mentioning this before. We have yet to see that from smaller companies or the broader economy in aggregate, because there's a lot of uncertainty, whether it's concerns about the war, tariff, trade policy, supply chains.

A lot of different things that are just making it a little bit harder for the broader economy to really invest. So that doesn't mean they won't. It just means they haven't yet.

And the third thing that ultimately happens is a boost to long-term productivity trends, and we've seen some increases in productivity. I would argue it's something a little bit more along the lines of a near-term productivity boost that resulted from less hiring last year. That just made the numbers, basically output per hour, go up. But that doesn't mean it's ultimately sustained.

And so when you're starting to see—this is really good news, that job growth is coming back after such a weak year of job growth last year. That, to us, says that we're not quite at the point where we have that sustained long-term productivity trends, which suggests that the whole technological transformation cycle, which we don't know how long it is, isn't over yet. And we still think we're probably in the early to mid innings of it, which is ultimately good news for the longer-term cycle and what that means for growth, going forward.

So it's OK that we haven't had the productivity enhancement yet. There's still belief in this. So obviously, every technology is going to be a little bit different. Every cycle is going to be a different length. But the trends all seem to rhyme, which is market up, investment, and then sustained long-term productivity.

HEATHER: OK, I want to hit on something that you said about this divide between people who are really excited about AI, Jake, and then people who are concerned that we might be heading towards bubble territory. And Denise, I'd love to hear your thoughts on this, too, and how you're thinking about the AI trade these days.

DENISE: It looks a lot different from what we saw in the dot-com era. I mean, even when we're talking about capital expenditures and just how much the hyperscalers have spent, the difference via any other bubble time that you calculate is really the pervasiveness. It really was across the board when you looked at all technology companies in the 2000s.

So, to put some numbers to it—so if you think about capital expenditures, or CapEx, relative to the free cash flow that all companies produce, and you look at the entire Russell 3000, and you look back in history, at the peak of the bubble, the average or aggregate company was spending three and a half to four times, in CapEx, the amount of free cash flow they produced.

Right now, even after the hyperscalers, it's below one. They are still spending less capital expenditures than they have in free cash flow. So some of this is covered by free cash flow, so this is very, very different from what we saw. In some ways, you can think of it—they're spending what they have already made.

But there are a couple other differences that I think investors don't quite remember. For the median technology company back in the bubble, earnings peaked in 1996. When we talk about all the disconnects, that was the major one. So you saw earnings peak. Margins peaked in 1996. Stocks did not peak until four years later, in 2000.

So that we're not seeing. We've seen an inflection in not only cap-weighted earnings in technology companies, but also, median earnings are still actually increasing. Numbers are still too low. Numbers are still coming up.

And the third thing is probably the one that's most pervasive in the bubble, which is valuations. At the peak of the technology bubble, you were spending 70, 80 times earnings, in terms of valuation, price-per-earnings ratio. Now it's actually closer to 30. And in fact, at the sell-off, it was closer to 25. You were paying the same price-to-earnings ratio, or valuation, for a technology company as you were paying for some consumer staples companies at the low.

So when you look at it relative to the rest of the market, technology stocks are still in the bottom half of their distribution, relative to any other time. And that's mattered, historically. The cheaper technology stocks have been, the more likely they are to outperform, historically. So, back to the market as a discounting mechanism, some of whatever it is that you're concerned about might already be priced in.

HEATHER: OK, so all reassuring points for those who are concerned that we may be near a bubble. It's been such an eventful first half of the year, so thank you very much for walking us through some of the highs and the lows of the year so far. We talked about AI. We talked about the other big market event, the conflict with Iran, and the Strait of Hormuz closing, and the impact that has had on global oil.

But we can already see that investors who stayed in the game are doing better than those who didn't. So if the second half of the year brings more twists and turns—I'll pose this to you, Scott, but feel free to also chime in, Denise and Jake, if you would like to. What's your guidance to investors on how to navigate the second half of the year, if we see more market volatility?

SCOTT: I'm big on sayings, and I think one of my favorites is that patience is usually rewarded, but volatility is typically the price that we pay for outsized returns. And you can just look over the past six months and see plenty of examples of these volatility types of events. And then, if I were to tell you that all these things are going to happen, would you expect stocks to be up by single digits? You wouldn't, right?

And then you can zoom back out and look at the past 10 years, and it's the same story with 100—a pandemic that doesn't happen for 100 years, and interest rates going to 0, and global shutdown of economies, and wars in Europe. And we had four bear markets, effectively, in eight years. They typically happen once every five or six. The point is that the market resiliency of the US and the US stock market is just extraordinary because, over that 10-year period, the US stocks have more than quadrupled.

So the takeaway in my mind is—again, it's getting back to those sayings that I mentioned earlier. But if you haven't done so—if our clients haven't done this, if viewers haven't done this—meet with the financial representative, an advisor. Come up with a financial plan. And then set a goal. Set a monetary goal in the future to focus on for retirement, whatever your goal is. And then, whatever you do, don't let short-term events dictate the long-term investment decisions.

HEATHER: Great way—go, yeah.

JAKE: One point I did want to add to that—so, the point about bear markets and corrections. So I mean, we're here. Our team sees that we're in a good, solid midcycle environment. It's very normal to see corrections or even bear markets, even during a midcycle period like this.

And so when you're looking at that kind of—Denise—the quantitative aspect that she takes to her work—it helps you stay disciplined, where, as long as the macro environment's expected to be OK, and you could utilize these type of tools that Denise uses, and have more of a longer-term approach, as Scott talked about, that gives you confidence that you're more likely to see equity markets actually bounce back.

Volatility is extremely normal, and it should be there. I mean, markets are risky. They're risk assets. So that basically is how you put your long-term plan on it, but also having an idea of where you are in the cycle so that you can expect and understand, is this a sustained downtrend or not? Let's see, under the hood, what's happening at the macro level and at the company-by-company specific basis.

HEATHER: You make a good point to, Jake, that bear markets can happen, and that doesn't mean we're in a recession. The stock market is not the economy, and the economy is not stock market, right? OK, all right.

So a great way to sum things up. And thank you for adding that, Jake. And I wanted to leave a little bit of time for a quick lightning round for the second part of our conversation here, just to get some big takeaways for our audience. But we'll be mindful of our audience's time, too, here. We have about five minutes for this.

So, first question. We haven't talked yet about the fact that this is a midyear election year. So, in a few words, as an investor, how should we be thinking about these kinds of events? Jake, I'll start with you.

JAKE: Yeah, so we get asked questions about the election every two years. It always seems to be something that's on top of mind. I can say with high confidence that it is rarely the event, if not ever the event, that's going to be the thing that matters for markets, whether they go up or down. Oh, this person won. This group took over. Good for markets, bad for markets.

So I'd say it's probably just not the biggest thing that matters. But it is going to be a big focus that's going to get a lot of headlines and probably create, potentially, some volatility as we head in. But I wouldn't think it's any type of game-changer for the direction of the economy over the next, say, 6 to 12 months.

HEATHER: Not long-term volatility. Just near term. OK, Denise?

DENISE: The range of outcomes is wide. So, to Jake's point, I think that there are other critical drivers, like earnings, your starting point on valuations, stuff like that. That is the bigger driver to the market. But the interesting data, I would say, is that, 80% of the time, you do see a flip, in midterms, of the party in power, so that wouldn't be surprising at all. And that "divided government" aspect is marginally, on average, a little bit better for the markets.

HEATHER: OK. All right, Scott?

SCOTT: Again, slogans. Focus on policies, not politics. But midterms tend to introduce downside volatility in the marketplace. That's history. But the S&P 500 has not finished in a decline, 12 months, following the midterms, since 1938.

HEATHER: Well, the odds are in our favor, it sounds like. All right. Not quoting anything, because I don't want to get in trouble with the IP, legal folks there. But all right, let's talk about an economic signal that you think investors might be underestimating right now that maybe we should be paying attention to as we prepare ourselves for the second half of the year. Jake?

JAKE: One thing—and Scott alluded to this before—is interest rates are trending higher, market rates, especially the 30-year part of the curve, not just in the US, but globally. The good news has been markets have been able to digest this. But with high deficits, not only in the US, but globally, higher inflation potentially becoming a factor, I think the markets are probably underestimating the ultimate impact, if rates continue to go significantly higher from here. Again, not a base case, but they may be underestimating their impact.

HEATHER: Maybe. Denise?

DENISE: I would say the diffusion of the CapEx spending that's just starting to happen. I think that if you look over the last year—

HEATHER: What do you mean by diffusion of the CapEx spending.

More companies spending, in terms of CapEx, and not just being driven by technology companies. And going back to that durable goods orders for machinery and other goods, when you break it down, of the seven categories, all seven are accelerating. So it's not just the ones in technology. So you're starting to see that filter through, so I think that this looks like a more diffuse, robust, and durable CapEx recovery.

HEATHER: Scott?

SCOTT: So, Jake, you touched on this a little bit, with respect to productivity. I think that the speed to which AI will ramp up productivity is being underestimated, and that's going to have a positive impact on inflation.

HEATHER: All right, all fairly positive signals, it sounds like. All right, biggest surprise of 2026 so far?

JAKE: I'm amazed how fast markets came back after they took a little bit of a tumble after the Iran conflict. But they're still volatile. But that's my biggest surprise, I'd say, so far.

HEATHER: Fair enough.

DENISE: How little oil went up on the conflict. Would have expected more.

SCOTT: \$500 a barrel would have been tough, absolutely.

HEATHER: Don't need that kind of a price shock.

SCOTT: I'd say Taiwan and South Korea market capitalizations now exceed China's. That's a surprise to me.

HEATHER: Good one. And lastly, investing theme you are most excited about as we think about the second half of the year.

JAKE: You're asking the asset allocator, so it's boring. So I'm excited about it, but the need for more strategic diversification. Stock-bond correlation is going positive, people trying to figure out how if they're diversified appropriately. Scott alluded to it. So hey, that's mine, strategic diversification.

HEATHER: Positive correlation between stocks and bonds. Bonds and stocks aren't zigging and zagging, as you would say, right now. OK, Denise?

DENISE: I would say the durability of earnings growth. So that's the key to the cycle, is the earnings cycle. And I think that looks increasingly more durable, and more companies are earning more money over time.

SCOTT: To me, it's the onshoring of manufacturing. There's been a lot of jawboning about it. They've been talking about it for a year and a half now. I'd like to see some progress made in the second half of this year.

HEATHER: All right, we have to leave it at that, but just fantastic ideas and perspective and insights from the three of you. Thank you so much for your time.

And to our audience, if you would like to hear more from Jake, Denise, and Scott and our other thought leaders about what they are watching for the rest of 2026, we encourage you to visit Fidelity's 2026 midyear investing outlook page. We have an entire page dedicated to this thought leadership, if you just go to Fidelity.com/Outlook—that's Fidelity.com/Outlook—and you will find free insights, analysis, and guidance to help you through the back half of the year.

And just a reminder, too, before we go. *Market Sense* is a weekly show. We are on every Tuesday at 2:00 Eastern. Replays are available as well on YouTube and our website and wherever you get your podcasts.

All right. On behalf of Jake Weinstein, Denise Chisholm, and Scott McAdam, thank you so much for the pleasure of your time today. I'm Heather Hegedus. We hope you all have a great second half of the year.

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