Fidelity Viewpoints®: Market Sense

Week 163 June 24, 2025

TRANSCRIPT

SPEAKERS:

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HEATHER HEGEDUS: Hi there. Thank you so much, everybody, for making the time to join us today for *Market Sense*. I'm Heather Hegedus with Fidelity. The conflict in the Middle East continues to dominate headlines, despite retaliatory attacks and attempts at a truce. And that has concerns remaining that this could all impact oil prices, the markets, and the global economy. So we wanted to take the time today to address those geopolitical concerns for you and to unpack many of the top questions that may be arising out of this conflict.

And today, we are so fortunate to be joined by Naveen Malwal, an Institutional Portfolio Manager here at Fidelity and a CFA charterholder, I should mention, whose team manages millions of client accounts here at Fidelity. We're going one-on-one with Naveen today, and there is no other voice of reassurance that I would rather share this time with Naveen, you and I have collaborated on a number of special reports together. We've guided our *Market Sense* audience through all kinds of uncertainty, including tariffs and a debt ceiling debate. So I truly appreciate you allowing us to turn to you during this time. Thanks for being with me.

NAVEEN MALWAL: Yeah, I'm glad to be here with you.

HEATHER: And today is Tuesday, June 24. And as I mentioned off the top, right now, the markets seem to be in a holding pattern, some up and down movement yesterday as investors watched to see what happens in the Middle East, Naveen. So first of all, I was hoping you could just start off by catching up on what you see to be the major developments that you have been keeping your eyes on throughout all of this.

NAVEEN: Yeah, whenever we have these headlines around conflicts, it can be unnerving and especially when the US is directly involved or somewhat involved, so for folks who have either people they know who live around there or are stationed around there, very stressful times. Our heart goes out to them. Focusing on what's happened, we did have some bombardments from the US take place over the weekend in the Middle East. And since then, tensions did ratchet up on Sunday and Monday. But they seem to have eased considerably.

There have been talks about a ceasefire. We'll see if it holds or not, so a lot of conversations happening across a number of different countries and regions on trying to find a long-term resolution to the situation. But we've seen with things like Russia, Ukraine, or what's happening in Israel, these headlines can move pretty quickly on these geopolitical events. So for now, I think it's reassuring we've reached a moment of perhaps more calm, but a situation that my team and I are monitoring very closely because it can change pretty quickly.

HEATHER: So far, we haven't seen much market volatility following these attacks, Naveen. To be sure, oil prices have actually been down over the past 24 hours. At some point, as things were escalating, it was about $75 a barrel. But tensions have eased now. It's dropped back into the $60 a barrel range. So I'm wondering, were you surprised by that? Is this a surprising reaction from the markets, and especially when uncertainty has been a driving factor in recent market volatility? Were you surprised by that?

NAVEEN: It is surprising. I think most folks would expect that some of the headlines you saw over the weekend would lead to stock market volatility, perhaps a jump up in some bond prices as investors reach for those, and perhaps a jump in oil prices as well. Yet, we haven't seen that play out. So a couple of takeaways here—one, it is almost impossible to predict these things. So it's a big reminder to not try to time the markets around news headlines because, one, they can change quickly. But two, even though we might have a thesis or a view that, hey, maybe Middle East tensions will lead to higher oil prices, it doesn't always play out that way.

And the other thing I'll just remind all of us is what I touched on in the opening is, hey, it's nice to get some relief right now. But we're talking about a ceasefire. We've seen, again, over the last few years, ceasefires don't always hold. There's still a lot of issues to be resolved here between some of the countries that are taking part in some of the tensions here. This has not been taken care of just yet, so this may still have further legs to run in terms of volatility and news headlines for a while, still.

HEATHER: We touched on why oil prices didn't move up. And maybe this is a sign that things are going to be OK, Naveen. But can you talk a little bit more about why oil prices weren't impacted more by this? Are there other factors at play here that investors should keep in mind?

NAVEEN: So it's interesting with oil prices, it seems things like what's happening with the Middle East will have a big impact. But the oil industry has changed quite a bit over the past few decades. And one of the biggest changes we've seen has been a shift in how the US has become a major oil producer. So for those folks who maybe remember some of the oil shocks from the 1970s or 1980s, the world is a different place now. We're not nearly as beholden to just Middle East production of oil prices. And that has led to perhaps a deeper oil market and an oil market that can be more resistant to headlines and volatility that are taking place just in the Middle East.

And again, these things, as you touched on, are really hard to call day to day or even headline by headline. So over the long run, I think with any investment, I tend to focus much more on the long-term fundamentals of supply and demand, in the case of oil, or with stocks, I focus a lot on earnings and economic growth, rather than what's happening in the news moment to moment.

HEATHER: There's a lot of domestic production of oil in Texas and New Mexico. Where do you think things might go from here in terms of the market impact? Do you think the markets will be able to continue to shake this off?

NAVEEN: So if we don't have crystal balls, unfortunately, no predictions on this show, but we can look to history as a guide as to what may take place when we have moments like this, where there are headlines around conflicts. And we're going to share visual here for those of you watching the video. And I'll describe it for those who are listening. It's a visual showing you the history of several conflicts where the US was involved.

And what you tend to see is, perhaps, a period of uncertainty or even volatility for stocks. But there is eventually a resolution. And eventually, stock markets have historically started to rise during different conflicts and even as the conflict has carried on. So while for the moment in the beginning, a lot of investors start to worry what this might mean, they then start to focus on the fundamentals of the economy and earnings and look to that as a source of reassurance.

So that, to me, is a key driver of why perhaps stocks can rise surprisingly, even when we have headlines around different conflicts. In some of these, the US is very directly involved, like the Gulf War, for example. So this isn't something that just happens somewhere across the world, didn't even relate to the US. In some cases, we were right in it. And still, the US stock market, other stock markets, bond investments, they all have managed to grow over time, despite these conflicts.

And the other thing to think about is sometimes conflicts can last a while. It's hard to tell exactly when they start and when they stop. So it's not as easy as saying, well, we just got a headline saying the conflict is now done. We can all move on with their lives. I think typically investors just gauge, is this going to cause a major economic issue? And if it's not, then they can start to focus on the fundamentals more and maybe put the headlines aside as they think about their investment plans.

HEATHER: Yeah, and to your point, I was listening to Fed Chair Jay Powell today speaking before a congressional committee today. And many of the congressmen and women were saying, it's so hard to predict what might happen next with the Middle East and that it's sort of hour by hour even, and not even day by day at this point. So it is hard to determine when a conflict is truly over.

Just to give our audience a little bit of background on you, Naveen, for context purposes, your team manages millions of client accounts. And we're talking about stock or bond portfolios. Or they could be a diversified mix of many kinds of investments. So I'm wondering how your team manages clients' portfolios throughout events like this.

NAVEEN: Yes, so these types of events unfortunately do come up. It seems like every few months, there's another challenge for investors. So a few takeaways—number one is we try not to time the market based on the headline. So as we discussed several times already, very difficult to tie headlines to what's going to happen with the prices. Sometimes it makes sense. Other times, it can be a surprising outcome. So that doesn't tend to lead to long-term success.

What we have found is more helpful is to focus on a few key things, like having a long- term focus, having a general plan of how we want these investments to grow over time, and then managing risk. How that takes place in times like this is we do follow news developments very closely. But what we seek to assess is, what's the impact of all of this to economic growth, especially in the US, as many of our client assets are tied to US investments?

And quite often, the answer winds up being, this is a little bit of an impact, but not a major impact that's going to lead to a significant slowing of the US economy. And when that's the case, typically earnings expectations also don't shift dramatically. So oftentimes, in these situations, although the temptation might be to react and do something, it often pays off just to wait and let the market settle down and then eventually recover at some point.

Our team will tend to make adjustments to client accounts if we feel we need to on a few different fronts. So one is thinking about the mix of stocks, and bonds, and alternative investments, and commodities, and real estate. Perhaps we need to adjust those, given how the market responded. Maybe there have been some cheaper valuations that have showed up, for example, or some parts that have felt more expensive.

Another thing to think about is within those asset classes, within US stocks, for example, do you want to make the shift towards value away from growth, or from large companies to small companies, or towards quality stocks? Those are all considerations that our team takes care day to day. And especially when these headlines come up, we just double check our thesis, make sure we don't make any changes there.

And the last thing I'll point to, we typically invest with fund managers within our asset classes. So for example, if we have investments in an international fund manager, they might consider, hey, where do we want to have adjustments to different regions internationally right now? Do I want to lean away from some parts of the world, closer to others? Are there certain companies I want to lean more towards, like defense stocks, and maybe move away from other things, like consumer stocks? So those are the kinds of decisions that tend to take place. But all of those are driven by research on fundamentals and the economy and less so by spur-of-the-moment thoughts based on just news headlines.

HEATHER: I wanted to talk about oil prices just for a little bit more. So Iran's parliament approved a measure over the weekend, endorsing the closure of the Strait of Hormuz, of course, the major oil transportation route, in reaction to the US airstrikes. So far, that closure hasn't happened. It's just, again, hard to predict where the price of oil might be headed, given this uncertainty. But again, the price of a barrel of Brent crude oil is, a global benchmark, is down right now. I'm wondering, not just near term, but long term, what the range of possibilities could be here going forward.

NAVEEN: Yeah, the range is quite wide. So to your point, we have oil supplies here in the US. We have oil supplies in the Middle East and in other parts of the world as well. So it's a very global market. And the market tends to, over the long run, follow supply and demand. So if there's a lot of oil, prices fall off. If the demand picks up, the prices tend to rise and vice versa. But at the same time, sometimes you get these surprises of the economy. You get these risks that perhaps some part of the supply chain may get affected, perhaps by an embargo or perhaps by some sort of damage to some parts of the oil market.

Now, in the case of this idea of Iran perhaps impacting this part of the world where so much energy is applied, north of 20% of the energy supply in the world tends to ship to and from the Middle East. On the one hand, Iran, that is a potential opportunity for them to really get someone's attention. But on the other hand, it's a significant risk for them as well.

If they take actions that cause a global oil price shock, they're not going to have a lot of allies supporting them on that front. Every country kind of depends on a steady supply and price of oil, so that will likely upset their trading partners, along with folks who they're trying to get attention of. And then even for Iran itself, if they disrupt that strait, how will their oil get out? And that economy is so reliant on oil exports that, in a way, going down that road may be very painful for almost everybody involved. So to me, hey, it's hard to know what's possible. Anything, I guess, is possible. But this feels like a very unlikely scenario to me.

And just to zoom out a bit on oil prices, we've seen a lot of movement in oil prices of late. So we want to share with you another visual on the history of oil prices going back a few years. And just to describe what you're seeing here is the history of oil prices going back five, six years, if not more. And what you have is a range of oil prices.

And right now, as Heather mentioned, looking at the West Texas Intermediate Index, which is a very common US index of oil prices, that index level has fallen back into the 60-something barrel range. And that's a relatively low range. It's a very comfortable range for consumers, for producers to put oil out. It's a nice kind of equilibrium range to have. And while tensions are rising, oil prices did get back into the 70s for a little while. But even those levels are far below the prices we saw just a few years ago.

So back when Russia invaded Ukraine, there was a lot of disruption to energy markets and commodity markets. And back then, the oil prices shot over $100 a barrel. So even the most recent volatility we've seen has been well below those kinds of levels. And now that prices are cooling off again, we're on the lower range of where prices have been going back for many years now, over 10 years now. So that to me is reassuring in terms of how the economy is able to digest what's happened. I think there's been much of an impact because the punch up in oil prices is relatively short. You normally need a sustained level of higher prices to affect the economy. And we didn't see that play out so far.

HEATHER: Well, that really puts things into perspective. The example of 2022, the war with Ukraine, $120 something a barrel, and now we're in the $60 range. Let's talk a little bit more about the consumer impact and the US economic impact with all of this, Naveen. We've had thought leaders, like Denise Chisholm, come here on the show and explain to our *Market Sense* audience that lower prices can help offset tariffs. Lower oil prices can potentially act like a tax cut for consumers and potentially boost the economy, what economists refer to as a tailwind. So again, we've talked about how oil prices are down. But if oil prices were to tick back up again, what could that potentially mean for the headway we're making into inflation and the US economy at large?

NAVEEN: Yeah, I agree with Denise's take. Typically, lower oil prices are a nice boost to consumers. Anything we spend less at the gas pump, we can spend in other parts of the economy. So generally, a tailwind, the prices are falling. So the opposite is also true. When the prices are rising, consumers can feel it. And they may have to cut back on spending in other areas to make sure their gas tank is full in the car.

So one thing about this is, those day-to-day swings in the price, or even week to week, yeah, they make headlines. But that's not typically the kind of thing that will affect the economy. What you need is the level of oil prices to reach a certain level, then stay there for a while for it to have a sustained impact. So what we just saw the last couple of weeks, I don't think is going to have a meaningful impact on the oil price. If the oil price went back up to, say, in the 70 range, if tensions ratcheted up again, that will have some impact to inflation, but not enough, I don't think, to cause a lot of stress on the consumer to the point where it'll severely impact their spending and then severely spill into overall economic growth.

Over here at Fidelity, the Asset Allocation Research Team is the team I work with very closely. And their view is inflation is likely to head a little bit higher as the year progresses, especially if we get more tariffs coming on in the back half of the year. Those tariffs have kind of been put on pause for a while. But again, we're not talking about very high levels, like we saw a few years ago, where we got to 8%, 9% inflation. Maybe we go from 3% to 3.5% or 4%, so not comfortable, but something we think the economy can manage without getting derailed.

HEATHER: How about the potential for impact to the global economy? Could it cause a global economic slowdown? Or could this geopolitical situation put us into a bear market again?

NAVEEN: It potentially could. But that's, again, a possibility. I don't think it's a likelihood. I think one thing that's been reassuring with this episode, one, it was relatively quick. So I think part of the reason was that so many countries, I think for the whole world, this situation of tensions rising and oil prices being at risk is very fraught. It's very risky for every economy in the world. So you had a lot of countries, either directly or behind the scenes, getting involved and trying to reach some quick resolution on this before it became a broader, more sustained issue.

So hopefully, everybody who is part of this got the message that there might be limits on how much the world might be able to tolerate with things spilling over with the broader economy. So you asked the question, could it happen? Yeah, anything's possible. But given what's taken place the last few days, and especially the easing of tensions, I don't think what's taken place so far will be enough to cause the world economy to slow down, either.

HEATHER: And what has been the reaction internationally in terms of the impact on international financial markets?

NAVEEN: Yeah, international stocks did react a bit differently on Monday. US stocks kind of held steady. And international stocks did slip a little bit. I think other parts of the world are more exposed to Middle East oil, where, of course, the US has its own oil sources, and the rest of the world maybe does not have that as much. But those stocks have recovered nicely as well. I think it ties back to the conversation you and I just had that, hey, that was a scary moment. But it felt like it was so short that it likely won't have a lasting impact on those international stocks. And so far this year, international stocks have done much better than the US stocks. That could continue if those stocks are able to maintain earnings and economic growth towards the back half of the year.

HEATHER: I had mentioned that Fed Chair Powell was testifying today before the House Financial Services Committee. And, of course, last week the Fed made the decision to hold interest rates steady. Could this geopolitical situation, could oil concerns, impact interest rates at all?

NAVEEN: If the price of oil became higher and we saw some bleeding into the inflation level that was meaningful, the Fed may at that point decide to ratchet up interest rates. But it's interesting. So far, the Fed's commentary has left the market believing the Fed is looking for opportunities to actually cut rates. So the Fed typically focuses on two things. One is inflation. And the other is the US job market. And the US job market is still very strong, very low unemployment rate, for example. But we are seeing signs that it is taking longer for people to find new jobs, for example. Or it's not as comfortable to quit a job if you're not happy at work right now. So those are signs the market might be slowing down. So it seems like the Fed is more focused on that—excuse me—and less focused on inflation right now.

HEATHER: I'll give you a second to catch your breath there and clear your throat. You've been doing so much talking today, and we're almost at time. But I just wanted to quickly ask you, what else are you watching this week that we might want to be paying attention to as well?

NAVEEN: So I think the economy, overall, consumer sentiment, consumer confidence, anything along those fronts, will be helpful to look at. And then inflation numbers, how are those playing out, will also be helpful to consider as the week comes up.

HEATHER: All right, Naveen, fantastic job there. I really wore you out today. Thank you so much, my friend. I can't think of a better partner to address these questions with, so terrific job. Just a quick note to everybody out there watching and listening, be sure to bookmark Fidelity.com/MarketVolatility.

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