# *Fidelity Viewpoints®*: Market Sense

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**TRANSCRIPT**

**SPEAKERS:**

Jim Armstrong Jurrien Timmer Leanna Devinney

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**Jim Armstrong:** Hello and thank you for joining us for Market Sense. I'm Jim Armstrong with Fidelity. Well, those ups and downs of the market certainly continue today, sharp day to day swings that we've all become, unfortunately used to and today is a perfect example unfortunately again. Now the labor department's latest numbers that were released this morning are showing us that, perhaps to no one's surprise, inflation is still a persistent problem. Prices up 8.3% from where they were last year at this time.

And Jay Powell, the chair of the Federal Reserve is warning us as customers to brace for more pain, indicating, you know the potential for future rates hikes in the coming in the Fed's attempt to both slow inflation but not push the economy into a recession. So, there has been never a more apt time to talk about staying calm and planning for the future in the face of volatility. So, today that's what we will be focusing on. The long term, saving for retirement, other long-term goals, and how to plan for the eventual loss of that steady paycheck when you do stop working full time. Jurrien Timmer and Leanna Devinney are, as always excellent guides for today's conversation. Jurrien is the Director of Global Macro here at Fidelity. He's got insights into both the latest world and national news, market conditions and of course he can explain what they all mean to us as investors. And Leanna has got her finger on the pulse of the client's top questions. She will be sharing how to she and her team are really helping people evolve their financial plans to stay on track with their goals. Guys, thank for making time. We have been off for a couple of weeks because of the holiday but it's great to see you back

**Leanna Devinney:** I know, it's great to be back.

**Jurrien Timmer:** Yeah, nice to see you as well. Greetings from New York City, I'm in a hotel room today.

**JIM:** No shortage of travels, Jurrien. It is Tuesday, September 13. I wanted to start with you, in part because, some folks might not know this about you, but you make that annual pilgrimage, that annual trip out to the Burning Man Festival, the Arts Festival in the middle—smack dap in the middle of the Nevada desert there. As always, sounds like an amazing trip. But as you were describing to us, it sounds like even Burning Man with it's utopian like image, is not insulated from the effects of inflation and volatility. What did you see there?

**JURRIEN:** Yeah, so first of all I may be the most boring person at Burning Man. But at the same time people really dress up because of radical self expression is one of the principles. And I just basically wear what I wear to the office which is sometimes pretty wild stuff. But so yes, I was at Burning Man, my fourth year. It was very hot and dusty this year and I co-managed a food camp. So, we make meals for the artists there and being what's a TCO, or a theme camp organizer I got to experience firsthand this year all the stuff that we have been talking about for months and months, you know inflation, supply chain bottle necks, resource constraints. And so, the way we run this camp is in December we decide okay, we need so many people, so many chefs in the kitchen, so many people helping out to make the meals that we try to make for the artists there.

And so, then we back in to that okay, how much is that going to cost. And this is always an imperfect—inexact science because we are doing this in December-January and we don't get the bills for all the things that we need to buy until probably March or April. And normally that's okay, you can kind of just take last year's increase and you apply that. We make a very robust budget but this year, of course with all the inflation that we've had, it was really just a shot in the dark. And so, as a TCO I need to rent a generator, a 70-kilowatt generator to fuel the camp because we have a full commercial kitchen. So, we need power for that. If you have a generator, you need diesel. And this is stuff that all needs to be lined up ahead of time. You can't show up at Burning Man and say, "Oh, I need some diesel." Like, you need to prepay for this.

For our kitchen equipment we need propane and we need, obviously running water, potable water. That means we need water tanks. And all of this stuff are things that we rent and then, you know, the gray water gets put in holding tanks. And then you need the pump out truck to pump out your holding tanks. It is kind of like camping in an RV, only this is a, you know full on kitchen. And again, all of this has to be prearranged, prescheduled, prepaid. And, you know, diesel was costing us $7 a gallon this year. And so, you know, just trying to line all this up. And we had to buy some new kitchen equipment and dealing with, you know uncertainties about, is stuff still even available, right? You order a sink and all of a sudden you realize it is on back order. Then you need to buy another triple sink, a stainless-steel triple sink. So, firsthand I got to kind of see not only the inflation but just how resource constrained the economy is and, you know Reno, Nevada is, sort of the staging area for Burning Man, that's the nearest big city—or the biggest little city as they Reno is called. And just finding, you know labor just like in the summer months, it's like, I need two strong guys to help lift the kitchen equipment out of the storage container. Even that was proving to be very, very difficult. So Burning Man this year was a good microcosm of all of the things that have been plaguing the economy and us as consumers over the past year or so.

And my guess is we probably reached sort of the peak of that during this year's Burning Man. My sense is that next year things will be a little easier, you know oil prices are already down, et cetera. But yeah, it was a real—a good sort of hands-on view of just, you know, how resource constrained the economy is right now.

**JIM:** And for those of you who didn't have to cook for several hundred people at one time can certainly still appreciate what you are describing there.

**JURRIEN:** Yeah, so we cooked 500 meals a day. I made dinner on Saturday and I alone, along with the help of our kitchen crew we served 250 people. I made Indonesian rijsttafel, which I always make, it's become a tradition. So, a camp of 78 people the budget is about $120,000. Cooking 500 meals a day is a pretty good outcome.

**JIM:** Leanna, let's hear what you have to say when it comes to maybe other inflation related questions that people coming into Fidelity's branches these day are having. Maybe folks come to your branch that have been to Burning Men but I'm expecting maybe not a ton. What are the question you're hearing from people as the summer is drawing to a close?

**LEANNA:** It is not as exciting of a Burning Man trip. But we are still hearing a lot of concerns around high inflation. And for clients who are closer to retirement, in semi-retirement or in retirement I'm hearing a lot of worry about spending in this environment and taking from their portfolio. So, withdrawing from their investable monies that they have just due to the market volatility. But that being said, a long-time viewer who has watched most of our Market Sense shows actually had shared with us that this is a really challenging market that we're in and feeling that and some of the emotions and nerves that can come with investing and just nine months of this significant volatility. But had shared having that diversified portfolio, having that investment plan, having that income plan—and we'll talk though that—has helped not be as emotional. So be excited to talk through some of the strategies and ways that we help alleviate some of the concerns in this challenging environment.

**JIM:** Jurrien, in your Burning Man answer you sort of alluded to more of a hope that maybe next year things might be calmer, prices more easy to track and predict. Why do you say that? Is that what you are seeing in the markets?

**JURRIEN:** Yeah, so when you look at what the market is expecting and the market is not always right by any means. But when you look at the bond market and what's priced in to the TIPS market—the TIPS market is the Treasury Inflation Protected Securities market—the market in its collective wisdom, if you will, is expecting inflation to come back down and actually come back down all to 2.5%, in the coming years. But you know for the Fed, that's cold comfort because the Fed right now is facing, you know, persistent pricing pressures. And we had the CPI report this morning and the overall CPI was not that far from expectations. But the core CPI, which excludes food and energy, was pretty sticky. And we're looking at I think it is 6.3% year over year change.

The overall headline CPI is more like 8.5% or so. And the Fed really needs to see the whites of the eyes of inflation to be able to kind of call the all clear, if you will.

And until we actually see that, the Fed is going to have to keep a pretty hawkish line. And, you know, the irony for the Fed and we will talk about this a little bit later, is that as soon as the Fed starts to signal to the market that okay, we are going to go to 4% and then we are probably done. As soon as that market gets that all-clear signal from the Fed—even if the Fed's not actually there yet—the market starts to rally and that means that financial conditions actually start to ease and that actually undermines the very effect that the Fed is trying to create.

So, it's kind of a chicken and the egg thing. But, you know, when I was on last on this show was about three weeks ago, I think. Where we left things was that the market had rallied and had retraced half of its decline and if you look at this chart, that shows the retracement of the decline that we saw from January to June until the recent high in August compared to other bear market rallies. And I don't necessarily think this is a bear market rally but it gives you some context that when you have recoveries in bear markets, they tend to not retrace more than half of the decline. And so, at that point we had retraced half of it and my sense was that the market was being a little complacent about how far the Fed needed to push things. And it turns out it was the correct thesis and the market has given back some of those gains. It's still above the old low, but it has given back some these gains. And so, the market is in an ongoing repricing mode. Not so much driven by earnings because the earnings picture has held up pretty well. But entirely driven by valuation, you know when rates are rising and the Fed is raising rates, what that means is that the present value of future earnings goes down.

And that's the pricing adjustment that the market is going through. And we can see today, market's down 3% because this inflation number was stubborn. You know, this repricing is not over and who knows when it will be over but until the Fed is done, I think we're going to be in this kind of ongoing period of adjustment.

**JIM:** So, during this period of adjustment, Leanna, I'm curious what you and the folks on your team say to customers who come to visit you in a branch, maybe on the phone, Zoom call, whatever it may be, they, you know in a lot of cases have these long term goals. Perhaps retirement chief among them so you have this feeling that time is on your side, whether you have got five years or 25 years until you retire, you feel like time is on your side. And it doesn't stop you from getting rattled from what Jurrien just laid out. So what do you say to folks?

**LEANNA:** Exactly. So when we talk our investors who have longer term goals farther away, you know 25 plus years lets say it's retirement, we are spending time looking at how you are invested. We take a look at your allocation. We also discuss the power of compounding and really why the impact of inflation on portfolios.

So, starting with the asset allocation, so we really want to make sure we get that right because again those farther away, we have time on our sides. So, here on the slide is showing, kind of the spectrum and showing risk and return, but the different asset mixes that you can invest or what your portfolio can look like. So, asset allocation that's really the foundation of your portfolio, having that mix of equities, fixed income and short-term investments like cash. And on the left-hand side those are more conservative portfolios, on the right side is aggressive growth—more aggressive where you are going to see a lot more in stocks. So, when you are farther away, we really want to make sure we get that investment plan aligned to your goals so if you are farther away you have that ability to navigate through more of the ups and downs. So you are likely going to see more of a portfolio on the right hand side so you have the growth and you have that power of compounding. Because with those things that's going to give you the most opportunity to potentially combat inflation. And we are in a very high period of inflation right now but over the long term we don't expect it to continue that high. But inflation will still exist and so investing will help navigate that one of the key risks being inflation.

Recently though, I spoke with a group of young investors who said that even though this is my longer-term retirement goals, I really don't like watching that portfolio go up and down. And just reflecting on that, this was the investor's first time experiencing this longer bout of volatility, it's certainly unnerving, it can be stressful but we did talk about the importance of remembering why we invest in the first place. And making sure that we don't let the market dictate and have us make decisions. And we make sure that we are keeping that investment strategy aligned to the goals. So, if it is farther away, it is really important to stay invested and stay growth oriented because that's really going to give us that power compounding, have that growth to help combat inflation as well as reach your goals in the long term.

**JURRIEN:** If I could just can add to that, you know it is important to remember that even though it seems kind of easy, well inflation is a problem, the Fed is tightening, maybe I should just sell? If you do that, you at some point need to go back in and buy otherwise that compounding math does not work for you. And, you know, buying back is a very, very—selling may be easy but buying back is very, very difficult because the market can literally bottom at any point, do this massive V shape recovery and then you are out when the market is going up. So it is just important to remember that there is more to it than just saying if I'm not sure I'm just going to sell.

**JIM:** Yeah, for sure. Those are great things to think about during that accumulation phase, right, when we are working and adding to that account. But Leanna, what do we need to watch out about maybe as you get closer to retirement? I know a lot has to do with how do I get the money out and how do I spend it.

**LEANNA:** Exactly. So, when you are approaching retirement, of course we are still going to keep your allocation front of mind. The, you know risk of inflation but we really want to take a look at your spending and what your withdrawal rate will be. So, this chart is showing this hypothetical, it is showing $500,000 in a balanced portfolio. And it is showing the blue line here is taking 4% out of that portfolio. And you can see by taking 4%, this hypothetical investor does not run out of money, their assets continue to grow. But just this green line taking a step up going from 4% to 5% you can see that this example runs out of money by age 89. And if you take out more you run out far sooner. So, we help plan for this withdrawal rate risk and make sure you don't take out too much too soon and have that spending plan and match your investments as well.

**JIM:** Yeah, definitely want to be deliberate there. I think that's probably the question—it is a question I get most and I don't do your job. My friends say how much do I need to retire, I don't want to run out of money. Help me make sure that my money, you know doesn't outlive me or I don't outlive my money I should say. What are other strategies for people have who have that concern?

**LEANNA:** So, one of the strategies we talk through is your income plan and how do you make sure that again we are not letting the market dictate our spending. When we reach retirement, we have worked long and hard. We don't want to sit home and say okay I'm not going to go out to dinner tonight because the market is doing poorly. Some of your investors have an income annuity. And this is one of the ways to create a little bit peace of mind and have that guaranteed income plan and it's not in the market so you don't have to worry about market volatility. So, an income annuity is a way you can purchase an income annuity to help cover your essential expenses in retirement that may not be met by Social Securities or Pensions. So, just the think if Income Annuity, it is like a personal pension. You are receiving a guaranteed income stream for the rest of your life or the rest of your loved one's life as well. So, you pay a lump sum of money to an insurance company in exchange for a monthly income stream, again for the rest of your life so similar to a pension.

That income never runs out. It is very similar to just having a predictable paycheck that's guaranteed. And, again it will never run out no matter what the markets are doing. So, keep in mind it is transferring a portion of your wealth in exchange for that guaranteed income. So, that portion of wealth that you are exchanging is irrevocable, and in many cases, you're not going to get that money back but it to get that guaranteed income forever. There are trade-offs though, so that lump sum going to the annuity is not invested in the market. So, when the market is doing well and accommodating you are not getting growth on that because again it's an exchange for guaranteed income.

But we talk about this often because in times of volatility, many are stressed to withdraw from their portfolio. We saw that on the chart before. So, this is a way to have a diversified income plan, give you peace of mind, alleviate some stress and have a guaranteed income plan.

**JIM:** And by no means no one size fits all, right? That's what I've heard you say so many time, it all depends on your risk tolerance and your goals and makes sense to have those options laid out in front of you so thank you for that.

Jurrien, I want to wrap up ending today by looking forward. I think the Fed meets a week from today, next week right around this time. And from what I was reading today it is sounding like not just another hike, but another three quarters of a percent hike. Does that sound about right to you?

**JURRIEN:** Yes. This in chart and this chart is from a couple of days ago, so it is slightly different now. But the Fed is meeting I think next week. A 75-basis point or a three-quarter point hike is completely priced in. So, the Fed will take that free option and do that, you know we have gone from 0 to 2.5-ish. And the market is expecting around 4 and a quarter as being the end point of the cycle. And then the market is expecting per that orange line for the Fed to start easing next year, cutting rates again which may seem counterintuitive but I think what the market is saying is that the Fed will either achieve, you know, its mission to contain inflation and then return to a more neutral policy from a restrictive policy. Or the more glass half empty view is that the Fed will be forced to ease because we will be in a recession then.

And, of course nobody knows whether that's going to happen but either way the market is expecting the Fed to keep pushing in large increments until it gets to, you know 4.25% or so on the Fed funds rate and then maybe return to neutral. And the risk is that either the Fed needs to go more than that or that the Fed goes to 4.25% but then is not able to ease again. But again, when you look at what the bond market is pricing in, the bond market is pricing in a return to two and a half percent inflation over the next several years. And if that's the case then I think that would be great news, right? That would be Goldilocks returning, but we need to get from here to there. And from between here and there is the Fed pushing rates high and then, you know hopefully without breaking something in the economy. And that's what is keeping the market sort of on this cliff-hanger for now.

**JIM:** All right. Plenty to keep our eyes on in the weeks and months so thank you Leanna and Jurrien for helping us do just that.

As always, if you have got questions about making a financial plan or staying on track with the one you have, Fidelity can help. Give us a call or go online. Visit our website, download our app. There is lots of ways to continue to learn more and get your questions answered. Again, thanks for making time to be here with us and we hope to see you right here again next week.

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