Fidelity Viewpoints®: Market Sense

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TRANSCRIPT

SPEAKERS:

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JIM ARMSTRONG: Hello, and thank you for joining us for this week's edition of *Market Sense*. I'm Jim Armstrong with Fidelity, filling in for Heather Hegedus this week, who is enjoying some well-deserved vacation time with her family.

The S&P 500 continues to hit record highs as investors seem to double down these days on anticipation that the Fed will, in fact, cut interest rates next month. So you have this very exciting time, what feels like an exciting time on Wall Street right now, which seems to be standing in contrast to the way the average investor or consumer is reporting they feel about the economy. Lots of concerns about the falling power of the US dollar, increasing concerns about tariffs and inflation, lots going on in this space.

We are thrilled today to have Naveen Malwal join us to help us dive a little bit deeper underneath those headlines today and talk about what they mean for investors. Naveen is a CFA Charterholder and an Institutional Portfolio Manager. He and his team here at Fidelity manage millions of client accounts.

We're also thrilled to welcome back Maura Clow to the show. Maura is a Vice President and Financial Consultant with Fidelity. Before coming to Fidelity, Maura actually worked for many years as a tax preparer. So she's going to help us understand—better understand potentially tax loss harvesting and explain why that can be an important strategy for investors all year round. Maura, Naveen, thanks for making time to be with us today.

MAURA CLOW: Thanks for having me.

NAVEEN MALWAL: Yeah, it's good to be here, Jim.

JIM: Naveen, we'll start with you if that's OK. It is Tuesday, the 19th of August, and maybe you can help me get my head around this idea that I've been struggling with a little bit lately. With all the uncertainty, some of which I just described off the top of the show, concerns about tariffs and inflation and rate cuts, whether or not they will come, how is it the case that the US stock market is up double digits this year with that as the backdrop? How is that happening?

NAVEEN: Yes. So it's a strong return so far through August, considering that in a typical year, the market might go up 10%, 11%, 12%. And we're sitting at about a 10% gain already if you include dividends on the S&P 500. Yet it wasn't that long ago in April we were staring at close to a minus 20% on the S&P 500. And that's when we perhaps at the height of uncertainty around tariffs, around certain geopolitical situations, questions around earnings growth, questions on the economy, inflation. So a lot of stuff happening all at once.

But over that time from April through August, investors have had a lot of time to digest what's been happening. And things have changed significantly as well. One of the biggest changes, in my view, is the tariff situation went from a very big unknown with very high tariff levels in a lot of countries to something that has a lot more certainty to it.

And then supporting the market through all of that, one of the things I try to do whenever I see a news headline is ask myself, how big of an impact is this really going to have on corporate profits? Because historically over the long run, earnings growth and stock prices have tended to move in the same direction. There's always exceptions, of course. But generally speaking, the trend has been very strong.

So as we start to get more certainty on what these tariffs may or may not mean—there are some delays, some adjustments, some trade deals being stuck with Europe and Japan more recently—now an investor could ask—could look at that and say, well, this is probably going to be the impact on earnings growth. Earnings growth may not grow as fast as perhaps analysts expected coming into this year, but they're still expecting positive earnings growth.

And the second quarter was a good confirmation of that. We had positive earnings growth in the second quarter in the United States S&P 500. We saw that globally as well, positive earnings coming through.

And earnings for the most part are starting to come in better than they were expected to. So after the tariff announcement, a lot of analysts cut their earnings estimates. And most companies are beating those lower estimates to the point where analysts are starting to increase their estimates for later in the year.

If I were to summarize why the positive market, really it comes down to the economy is still growing, earnings are still growing. Yes, we have faced and continue to face a lot of headlines.

But historically, the trend of earnings growth and stock market prices has been very strong and seems to be working out so far this year as well.

JIM: Great. Really great perspective there, Naveen. Also, just while I have you, what other thoughts or what else are you tracking right now, sort of that level below the headlines? What else do you have your eyes on?

NAVEEN: Yeah, so there are still question marks out there. Some of the key ones for me, the trade situation continues to evolve. We still have major trading partners like Canada, Mexico, China without a final deal yet. They're still negotiating. There's still some work to be done behind the scenes and what that's going to look like going forward. So that could have more information for us to digest.

At the same time, we are seeing other data points where maybe there's question marks being raised. So just last week, we got an indication that perhaps inflation is starting to creep in at the wholesaler level. So factories, manufacturers, they're starting to pay a bit more for things. Will that eventually spill over to inflation for consumers? That's the question mark. And then if that does start to happen, how does the consumer manage through that?

So there's still a lot for us to follow closely over the balance of the year in terms of managing risk. But to me, it's always important to look at those risks, but then balance that with the positive news that's developing sometimes more quietly in the background as well.

JIM: You mentioned the rest of the year. I want to ask you right now about the rest of this week, because just in a couple of days on the 21st, actually, is the big, big annual meeting that the Fed will host in Jackson Hole, Wyoming. It's a big marquee event every year where you get economists and policymakers, central bankers all gathering together.

The theme this year is labor markets in transition. And certainly, we know that part of the Fed's dual mandate is, in fact, achieving maximum employment, as well as keeping rein on inflation via interest rates. So Naveen, ahead of this big meeting happening in just a couple of days, do you have any sense of what we should be looking for to come out of this meeting as investors? Any big decisions get made there, or what will we hear?

NAVEEN: Yeah. So historically, this is an event that's been taking place for years. You have central bankers coming in from around the world to partake in this. And you get some fun shots of people who are normally in suits walking around in cowboy hats and enjoying hikes and whatnot.

But between those hikes, they're also talking about big picture items around the economy globally, US, internationally. And they'll do the same this year. As part of the proceedings, there is usually some commentary from the Fed chairman. He'll come out and just talk about things in general, not necessarily related to the conference.

Now, this isn't a time for the Fed historically to be used for a rate announcement, right? So they're not going to announce their intention for rates going forward. But it is more of a way for them to survey the landscape and share with viewers and listeners, here's what we're seeing with the economy. As you're going to say, here's the cross-terms. Here's the things that are maybe going more positively. Here's some of the challenges right now.

And I think for the Fed, typically they've used that meeting just to give some general comments and give themselves plenty of room for their upcoming rate decisions. In other words, I wouldn't expect to necessarily get a strong indication of which way they might go with interest rates in September. The market is expecting perhaps a hike is going to happen in September, but the Fed doesn't want to box itself in by confirming that too much, either directly or subtly.

So hey, surprises can always happen. But going into the meeting, based on precedent I would expect some commentary, some update, a view of the landscape, but not necessarily fireworks coming out of that commentary from the Fed chairman.

JIM: Understood. Got it. Naveen, thanks for that look at the news headline landscape there. Maura, thank you for your patience. Would love to bring you into the conversation now as we start to talk a little bit more about tax-smart investing and how to potentially turn a loss into a possible gain come tax season.

As a reminder, Fidelity does not provide tax advice. But today, we are going to be talking about ways to possibly make your investing accounts more efficient. So Maura, I hope I'm in the majority when I say I really don't start thinking seriously about my taxes until probably December at the earliest, but I feel like that's later than you would advise.

MAURA: That's right, Jim. Most people don't want to think about their taxes at all. But when the market has volatility, there are three things you can do. You can sell out and go to cash, and that's probably the worst action you need to do unless you need the cash to pay for expenses. The second thing you can do is sit and wait for the stock to come back as the market improves. That's what most people do.

Or the third, you could harvest the lost, sell the stocks that have experienced a devaluation, and then buy something similar to keep your portfolio diversified. You're now buying the new investment at a low hopefully, and saving the losses to offset any future gains when the market comes back.

While many investors focus on tax loss harvesting towards year end, it's actually a powerful strategy that can help investors year round. Like we said, so many investors only think about to do this at the year end. But December has rarely been the ideal month for tax loss harvesting, as market volatility has historically occurred throughout the year.

So as an investor, it's inevitable that you'll lose some money on investments and make profits on another. But with tax loss harvesting, there's a bright side to those losing investments. At its core, tax loss harvesting is selling stocks, bonds, mutual funds, or ETFs, or other investments you own in taxable accounts that have lost value since you bought them to offset any realized gains elsewhere in your portfolio. So you want to be able to identify those losses before tax season, because they can potentially save you money on your tax bill.

JIM: Excellent. All right. So you've sold me there, Maura. I'm hooked. But I've got to imagine there's probably at least a few rules that I need to follow to be able to do what you just said.

MAURA: Yeah, there's always rules when you deal with finance and taxes. And you just need to know them to use them to your advantage. These are my top three rules.

First, you can only apply tax loss harvesting strategies to taxable brokerage accounts because 401(k)s IRAs are both tax-deferred accounts. The second rule comes from the IRS. If your capital losses exceed your capital gains, you can deduct up to $3,000 per year against your ordinary income, such as wages or salaries.

Here's the best part. Any losses exceeding the $3,000 annual limit can be carried forward to future tax years to offset future gains or income. And the third, you can't sell a security at a loss or buy the same or substantially identical security within 30 days before or after the sale date. This is called a wash sale, and the IRS will not count this against your gains.

So just make sure when your tax loss harvesting you're reinvesting in different securities than the ones you're using for losses. So as an example, you could sell a health stock at a loss, but you still want exposure to health care in your portfolio. So instead of buying that stock again, you could buy a mutual fund or an ETF instead that targets that same sector, and that would prevent a potential wash sale.

So we'll show you an example. We have a slide on the screen. But if you're listening to this as a podcast, don't worry. I'm going to walk you through it. The slide shows if you had a stock that had a long-term $5,000 gain and then a loss of $4,000. Your net gain is now only $1,000, and your federal tax liability has been reduced from $750 to just $150. If you're not sure, you should always consult a tax advisor before making any purchases.

JIM: We get lots of questions about wash sales, Maura, so thank you for taking the time to walk us through that. Another popular question that we get asked a lot, not just on Market Sense, but frankly, on webinars throughout the universe of shows that Fidelity offers, is this idea between long-term and short-term investments and the differences in taxation there. So can you spend a minute or two walking us through that?

MAURA: Absolutely. So any time you're tax loss harvesting, you also want to look at how long you've owned the investment. There are two types of gains and losses, short term and long term. The key difference is they're taxed at different rates.

Short-term capital gains and losses are those realized from the sale of an investment that you've owned for one year or less. These are taxed at your marginal tax rate. The top marginal federal tax rate is 37%.

Long-term capital gains and losses are realized after selling an investment held longer than one year. For long-term capital gains, the lower capital gains tax rate applies. Depending on your income and filing status, you'll likely fall into the three tax brackets you see on the screen. 0%, 15%, or 20%.

It's really also important to note that long-term losses are first applied to long-term gains, while short-term losses are first applied to short-term gains. If you have excess losses in any one category, you can apply them to gains of either type. So as an example, if you were to sell a long-term investment at a $15,000 loss, but only had $5,000 in long-term gains for that year, you could apply the remaining $10,000 excess to offset any short-term gains.

If you've harvested short-term losses but you only have unrealized long-term gains, you may want to consider realizing those gains in the future. The least effective use of harvested short-term losses would be to apply them to long-term capital gains. But depending on the circumstances, that still may be preferable to paying the long-term capital gains tax.

JIM: Yeah, absolutely. And like you said, depends on the circumstances entirely. Maura, what are some strategies that you think people might consider for using tax loss harvesting throughout the full year?

MAURA: Sure. When you're looking for tax loss selling candidates, consider the investments that no longer fit your strategy, have poor prospects for future growth, or can easily be replaced by other investments that fill a similar role in your portfolio. Harvesting losses regularly and proactively when you re-balance your portfolio, for instance, can save you money over the long run, effectively helping to boost your after-tax return. As I said before, do not wait until December.

Remember this saying. Don't let the tax tail wag the investment dog. If you choose to implement tax loss harvesting, be sure to keep in mind that the tax savings should not undermine your investment goals. Ultimately, a balanced strategy and frequent re-evaluation to ensure that your investments are in line with your objectives is the smartest approach.

JIM: Absolutely. Hey, Naveen, if I can, I'd love to bring you into the conversation as well, because I know that your team manages both retirement accounts as well as taxable accounts for your clients. So I'm curious how the team looks at tax loss harvesting for managed accounts.

NAVEEN: Yeah. So Maura's done a great job describing the process and how to execute on it, including some of the rules to watch out for. Our group, we manage a lot of retirement accounts and taxable accounts to your point, Jim. For the taxable accounts, we have a dedicated team of experienced investment professionals who look after these accounts. And with the help of cutting-edge technology, they're continuously monitoring these accounts for tax loss harvesting opportunities, along with other ways of managing this money more efficiently tax-wise over the long run.

Just to add to Maura's story, so for one of these accounts, for someone who has a lot of positions and maybe doesn't really want to do this kind of trading on your own—you don't always think about doing this day in and day out, week after week—this team can take this on for you, which can be very helpful. Take that work on your behalf and help you experience some of those tax loss harvesting benefits without undertaking the work behind it.

But beyond that, this team uses some strategies that are perhaps harder for individuals to execute. One example of this is instead of investing, say, in a index mutual fund or index ETF that owns, say, the 500 largest companies in the US, what one could do instead is invest in what's called a separately managed account. And in a separately managed account, the way we would use it in this strategy, rather than own one ticker or one holding with all those stocks wrapped up under that one lever, we would actually have those individual positions, many of them throughout the portfolio.

What this could allow an investor to do is even in a rising market, there's usually a range of outcomes for individual stocks. While the S&P might be up 10% this year, I'm sure there are some companies that have done better or worse than others. So you could look for perhaps hundreds of opportunities beyond just what the index is doing to harvest losses and take advantage of some of the math that Maura was showing you earlier.

So we offer these separately managed accounts on their own. So a client might just say, I just want one, Naveen, for US stocks or international or for bonds. Many of our clients do opt to get a multi-asset class portfolio where we look to have opportunities to bring in US and international separately managed accounts as part of an overall strategy, a mix of stocks and bonds and other investments. But those are just a few ways of several ways that this team and my team seeks to manage taxable accounts for clients to deliver better after-tax returns over the long run.

JIM: Maura, a quick follow-up for you as well if I could. So some folks might well work with a financial consultant like Naveen or someone on his team. Maybe they work with a tax professional. So tax loss harvesting could be something that's already happening inside those accounts. But I'm curious for your perspective on whether and to what extent this is something that a DIY or a do-it-yourself investor can feel confident taking on themselves.

MAURA: Yeah, absolutely. People can do this on their own. You should be a dedicated investor to do it, though. And if you're a Fidelity customer, there's a free tax loss harvesting tool that helps simplify the process and lets anyone take advantage of this strategy, although you still always may want to check with your tax professional.

Once you're logged into the tool, it can show you your taxable accounts where you've had some gains, but still have losses that you haven't sold or closed out yet. You can also estimate how much you might owe in taxes based on your short-term and long-term gains. This is an important distinction for tax purposes, and something you can read about more in Fidelity's Learn Center when you search for articles about tax loss harvesting.

The tool then helps you sell the losing stocks you've chosen with just a few simple clicks. And just like that, you've offset the taxes from some of your gains and offloaded some of those losing stocks. Plus, now you have the funds from those losing stocks to pick investments that might do better in the future.

The deadline for a sale of stock to count towards your taxes for the current tax year is December 31, so now it's a great time to go and try out the tool and see how selling unrealized losses could affect your taxes before it's too late. Trying out the tool now and becoming familiar with the language and consideration around tax loss harvesting can give you that confidence you need to use this strategy to your benefit when you're ready. And the best part? After your taxes are done, you can keep using the tool year round to estimate your future tax impact.

JIM: Love it. Maura, thank you for walking us through that. Really appreciate it. In the minute or so we have left, Naveen, love to end on a question to you just about what you're looking forward to in the next week or so in terms of economic headlines. What have you got your eyes trained on?

NAVEEN: Yeah, so we touched on the Jackson Hole meeting. We'll be following that to see what comes out of it, just to read the notes behind it, the Chairman's commentary as well. Along with that, most of earnings season for the S&P 500 is done. More than 450 companies have already reported, but we'll get the last few reports just to finish off the season.

And then there's always updates for the economy. So this time around, I'll be focused on jobs and manufacturing numbers coming out over the coming days. That can give me further clues on what's happening in the background for the market and earnings potential later on in the year.

JIM: Excellent. All right. Thank you for that. And that's where we will leave it this week. Thank you to everybody out there watching and listening, and certainly sending us your questions. I promise that the Market Sense team literally reads each and every question. They are tremendously helpful in helping the team shape the content of future shows just like this one.

If you're a Fidelity customer and you want to check out the tax loss harvesting tool that Maura was just walking you through, just a reminder that that address is Fidelity.com/Tax LossHarvestingTool. Fidelity.com/Tax LossHarvestingTool. On behalf of Naveen and Maura, I'm Jim Armstrong with Fidelity. Thank you so much for joining us. Remember, we are live every Tuesday at 2 o'clock Eastern with a replay available as well. We hope to see you again soon.

[1]Fidelity Viewpoints: February 28, 2024: www.fidelity.com/learning-center/personal-finance/managing-taxes/tax-smart-strategies

[2]Fidelity Viewpoints: May 26, 2025: **https://www.fidelity.com/viewpoints/personal-finance/tax-loss-harvesting**

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