Fidelity Viewpoints®: Market Sense

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TRANSCRIPT

SPEAKERS:

Jim Armstrong   Jurrien Timmer   Rita Assaf

Jim Armstrong: Hey there. Thanks for joining us for *Market Sense*. I'm Jim Armstrong with Fidelity.

The first few months of the year have been proof, really, of why it can be a really good idea to build your own financial plan and then try to stick with it. For a lot of us, the longest long-term goal we have is retirement, so it can be good to check in every once in a while and ask ourselves how prepared we are. So, today, we're actually going to be analyzing the results of a yearlong Fidelity research project that looked at the overall retirement readiness of American households.

Now, before we get there, we're going to get the market's big picture, as we often do. We'll be joined by Jurrien Timmer; he's Fidelity's Director of Global Macro. And then we're also excited to welcome for the first time to the show, Rita Assaf; she's the Vice President for Retirement and College Leadership. We're going to be talking to her about that Retirement Savings Assessment and looking forward to hearing what she has to say.

So, big hello to everybody and thanks for making time to be with us.

Rita Assaf: Thank you for having me.

Jurrien Timmer: Great to be here. Hi, Rita.

RITA: Hi, Jurrien.

JIM: Let's start with you if we could, Jurrien, as we often do. It's Tuesday, March 28th. At the risk of us starting off with a massive understatement, a rocky couple of weeks, especially after all the turmoil in the banking sector, so it would be great if you could talk a little bit about that. Plus, last week the Fed raised interest rates by what you had predicted, about a quarter of a percentage point. Would love to get your sense of what you think that means for all of us as investors going forward.

JURRIEN: Yes. So, it's been of course a pretty crazy month actually. March is almost done and the month started off, if you remember, with Fed Chair Jay Powell going in front of Congress, basically saying, you know, we're going to be higher for longer in terms of interest rates. Maybe going to 5.75 and then staying there for a while until inflation has been tamed, and of course, we still have an inflation problem, for sure.

And then of course, a few days later, you know, Silicon Valley Bank and then Signature Bank and then some tremors with First Republic and then of course the Credit Suisse unwinding in Switzerland. And fortunately, things have calmed down. We're in a mode where no news is good news, basically. But it certainly has upended the market landscape. Of course, the markets, you know, came under some pressure. They've since stabilized. But bond yields have come down. The two-year Treasury yield, which is a very good measuring stick for where the market thinks the Fed is going to go with interest rates, that was at 5.08% when Jay Powell spoke in front of Congress. It then fell to 3.5% in the matter of a few days. We have not seen moves that big, that dramatic in many, many years. And so, again, things have stabilized here, but the Fed did meet last week, of course, and the Fed did go another quarter point, which I think was kind of the obvious thing to do, the right thing to do, because if the Fed had stuck with its half point moves from before, I think that would have scared the market a bit, and if the Fed had not done anything, if it had cut rates, that really would have scared the markets because then the markets would think, oh, what does the Fed know that we don't know?

So, staying kind of on course with the quarter point hike, I think, was the sensible thing to do. And I think what the Fed is trying to do is thread the needle by acknowledging that inflation is still a problem, so rate hikes are still happening, the Fed is still reducing its asset holdings on its balance sheet, while at the same time, the Fed is recognizing that there are some stresses in the banking system. I wouldn't call it a banking crisis like many people do but there are certainly some stresses, and the Fed is acknowledging that by providing liquidity to those who need it, at a cost, of course. I mean, it's not free. And that's what the Fed is supposed to do as well. The Fed is supposed to be the lender of last resort.

So, right now the Fed is doing both. Its balance sheet is kind of expanding again, but mostly because of loans being provided to the banks.

So, the Fed's kind of trying to thread the needle here, and the market is as well, and the more days go by without more headlines on the banking side, I think the more calm will be restored to the markets.

JIM: That's a perfect setup for what I wanted to ask you in terms of a follow-up here. You were talking about the markets at large. How about the banking sector in specific though? Definitely a lot more volatility there, a lot of attention there, certainly, as you said a couple of weeks ago. But is it, as days go by, as you said, are we past the point where we're going to see any repercussions there?

JURRIEN: Well, it's interesting because when we think about stresses in the banking sector, we always think about banks getting over their skis and making bad loans, so, and of course that happened during the financial crisis back in 2008 and the banks got heavily regulated as a result of that. And the irony is that some banks are in trouble not because they have bad loans but because they bought Treasury bonds. It's like—I mean, it's not funny but it's ironic that they used their assets to buy the safest instruments you can think of and now they have kind of a similar issue where those investments are at a loss, an unrealized loss that the banks don't have to realize unless they sell those securities, of course. But deposits are starting to leave some banks, and we're seeing that in the headlines, because we know that there's a limit to the FDIC deposit guarantee of $250,000, and some people have more money than that sitting at a bank. And I think that money is starting to move around, not only to seek those guarantees or those insurance amounts, but also in search of higher yields. That's why we're seeing money come into money market funds, for instance. And so, there's money moving around, and I think that is something that certainly we're keeping an eye on.

So, it's not necessarily a crisis-like thing, but we are seeing that banks are starting—at least the smaller and regional banks are starting to lose some deposits in favor for maybe the larger banks, and also in favor of higher rates.

And the consequence of that might be that as banks see—as the banks need to compete for those deposits more, they may have to pay higher rates on those deposits, which then will affect their, what we call the NIM, the Net Interest Margin, and that in turn could lead to banks making fewer loans.

So, when we typically think about recessions, they are kind of—we're told by an inverted yield curve, meaning short rates are higher than long rates, and certainly we've seen that for a number of months now. And then typically what you see is a credit crunch because as banks—as it costs them more to borrow than they get on lending, they make fewer loans. And so, that's something that could happen during this economic cycle, maybe if we end up in a recession in the coming 6 to 12 months, that's the thing we will point to saying, okay, that was a credit crunch because banks are more concerned about their deposits.

So, we don't know but those are the kind of things that we're thinking about as we look ahead for the markets.

JIM: Perfect. Perfect opportunity to bring Rita into the conversation here because we know concerns about the economy at the macro level, Jurrien, where you spend your time focusing and thinking, really start to show up in our individual savings and investment patterns at the microlevel, at our own personal checkbooks and savings plans.

I know here at Fidelity, we always talk about customers reaching out with questions, trying to figure out if they should maybe consider more conservative investment strategies, maybe even thinking about withdrawals, questioning when they'll be able to retire, if they'll run out of money when they retire, and again, as we mentioned, Fidelity has this new great study, the Retirement Savings Assessment. And so, Rita, I'd love if you could just start by walking us through what you found this year.

RITA: Sure. So, just a little backdrop of the retirement score. This is a measure of the estimated retirement income needed as a proportion of the required retirement income necessary to maintain a preretirement lifestyle in retirement, which is a lot of words but it's basically what's the income to cover your expenses in retirement.

And what we found in this year's survey was that there was a drop in retirement preparedness. So, America's score has actually moved back to the yellow, to a score of 78, which is a five point decline from 2020. 1 This means American savers are now projected to have only 78% of the income needed to cover their expenses in retirement.

And our assessment actually found that over half of those surveys may need to make moderate or significant changes to their retirement lifestyle if they want to make up that shortage. And more than a third were actually in the red, meaning they will likely have to make significant adjustments to prepare for retirement.[1]

JIM: And so if I'm hearing you, it sounds like by and large, we were generally better prepared for retirement before the pandemic. How—explain how that happened.

RITA: Well, two things have happened since then. First, some people are actually saving less, so you might have seen that there are actually people who had more money during the pandemic, but the amount that they were putting towards retirement on a periodic basis was actually lower.

And then second, some are investing more conservatively. In fact, those taking a conservative approach, nearly 60% of those respondents expressed concern about losing their savings because they were investing too aggressively. And this is a natural reaction if you think about what's happened in the last couple years. We had the pandemic, it's market volatility, and then the latest banking industry turmoil that you heard just Jurrien speak about about a minute ago.

JIM: Yeah. When you stop and think about it, it makes perfect sense, right, especially the closer you get to retirement, the more fearful you are about perhaps keeping more of your money invested in stocks. And point of fact, right, you have less time to make up any losses the older you are, so that makes sense.

But Jurrien, a great time to bring you back into the conversation. What do you see going for folks maybe in that preretirement space right now? Where do you see the markets going in the next year or so?

JURRIEN: Well, as you know, my thesis has been for a while that the markets are going through an adjustment phase. Last year, that adjustment was to higher interest rates, right, and if you think about how to value investments, whether they're bonds or stocks or crypto, anything, basically, you're looking at the present value of future returns. And the present value is based on future cashflows and interest rates, right, because if you calculate the present value of future cashflows, the higher the interest rate goes, the lower the present value goes, and vice versa.

So, last year was all about the Fed raising rates, raising the costs of capital. That lowered the present value of future cashflows, whether it was for Treasury bonds or high yield bonds, or stocks, or you name it, and that was the great reset that we saw in 2022. And of course, as we all are painfully aware, there was no place to hide last year because when the Fed raises the cost of money, basically everything gets hit, and the only place really that there was to hide was in like T Bills and money markets and things like that. But the problem with that is that if you're going to take your money out of long-term investments that tend to compound over time, which is how we generate wealth for our retirement, when you leave that space and you buy a 6-month T Bill, as good as it feels to do that, you are engaging in market timing. And market timing, I can tell you from experience, being in the business for almost 40 years, it's really, really difficult to do.

So, a far better approach, in my view, is to have a well-designed, diversified portfolio of stocks, bonds, other asset classes as well, some short-term as well, and that hopefully lets you ride out any storm.

And so, for 2023, and we've talked about this in recent weeks, my expectation has been that the markets would be flat and that both bulls and bears would be equally frustrated because the market would be basically directionless. It's not a very satisfying answer because everyone thinks in terms of up or down, very binary, but sometimes the market just treads water, and so far this year, that's exactly what's happened.

Actually, since June of last year, the markets have basically gone nowhere. And as—as frustrating as that may be, it's actually not a terrible outcome. If we're investing for the long-term, which I think most people on the call are doing, one year of sideways is not going to make a huge difference in your returns over the next 10 or 20 years.

But what we've seen in recent weeks with bond yields falling as investors start fearing a recession and maybe start pricing in the end of the Fed tightening cycle, bonds have done very, very well. And so, that combination of stocks and bonds, it didn't work last year, but generally speaking, it works, and it is certainly doing its job in 2023 so far.

So, my sense is the market has more work to do to kind of digest all of the moving parts here, but I think patience will be rewarded for investors going forward.

JIM: So, through that lens, Rita, I'd love to follow-up on something you said just a couple of minutes ago, this idea that I think it was close to a third of Americans probably need to do a little bit to a lot of work when it comes to getting themselves in a better place for retirement. What are some concrete steps you would suggest people do? There's the macro environment Jurrien is talking about, but we love to give people actual strategies and things they can consider doing themselves.

RITA: Yeah. So, there are three actions we at Fidelity suggest to help improve your retirement preparedness and this is regardless of age or income.

So first, if you can, save as much as you can. Aim to save about 15% of your pre-tax income each year. That also includes your employer match if you have access to one through a workplace plan like a 401(k).

We know that 15% can be tough, but if you even just increase each year, even by just 1% until you get to that 15%, you know, for a family or household making $60,000, 1% equals an extra $50 a month.[2]

Second, and Jurrien, you sort of touched upon this, examine your asset mix, especially for these long-term savings goals like retirement. Make sure you have an appropriate mix of stocks, bonds, and cash based on how far you are from retirement but also how comfortable you are with risk in your portfolio.

And third, reevaluate your retirement plan. If you're able to, waiting longer to retire has its advantages because you can spend more time building those savings or even increasing your Social Security payments. But we know that's not easy to do. Retiring later may not be in the cards for everyone. In this case, it might make sense to reevaluate how much you plan to spend in retirement.

And actually, one interesting trend that we've seen so far is that retirement may look different for some people. There's no longer that traditional view of I'm just going to stop working and that's it. Some people are actually working part time or they might be making money off their hobbies, and this might actually help you from tapping into your savings earlier. So, it's just another option to think through as you think of reassessing what your retirement plan could be.

JIM: So, you mentioned Social Security. So then I have to ask you, I have to pass along to you one of the most popular questions we get is, when do I claim Social Security? And I know that that's super specific to everybody's unique case and their—where they are in life and what their goals and expectations are, but I'll tell you, I'm in my 40's and even I start to think, oh, when should I do

that? I've got 20 years-ish or longer; when is a good time for me to do it? What do you tell people who hit you with that question?

RITA: It's really tempting to claim Social Security as soon as you're eligible, which is typically at age 62. I mean, you've been paying into the system for all of your working life and you're like, great, guaranteed monthly income. Sounds pretty good.

But the people that Fidelity interviewed for this Retirement Savings Assessment reported they actually planned to retire, on average, around age 65. So, as you think about a solid retirement income plan, there are sort of three things you want to think about. Guarantee to ensure core expenses are covered, growth potential to meet your long-term needs and legacies, and then flexibility to refine your plan as needed over time.

JIM: That's interesting. I know that sort of spectrum you showed before, the green to red, was for the nation as a whole, but you can also figure out your own on Fidelity's website and see where you fall in that spectrum. And it's interesting, if you play with the numbers and adjust the little levers differently, you can see really the difference in claiming Social Security at 62 versus 70. It will move you around from the—personally from the yellow to the green to the red or whatever the direction is. But if we all collectively made those decisions like that, I think what you're saying too is the overall readiness score for the country potentially could change too.

RITA: That's right. Even just changing one of those measures can increase your score considerably even if you can't even get to all three.

And if you do want to check out your score, you can go to Fidelity.com/score, but it is—it would be—even just taking just one of those actions would significantly improve your preparedness.

JIM: Excellent. All right. I want to thank you both again for taking the time to be with us today. Really good tips and of course, as always, a timely conversation.

For folks watching or listening, if you'd like to read more about Fidelity's Retirement Savings Assessment or just learn about perhaps in general how you might be able to think about getting more prepared for retirement, we've got an article that you can check out. You can just scan the QR code that you see on the screen right there and it will take you right to the page. And again, you can do that just by opening the camera on your phone and hovering the camera lens over that QR code and click on the link that appears, and it will take you to our webcast hub. Or then you can just type in the web address listed as well.

As always, if you've got questions about making a financial plan or staying on track, Fidelity can help with that too. You can give us a call, again, go online, visit our website, download our app, and find tons of ways to continue to learn more by doing that.

Thanks again for making time to be with us today and we'll see you next week.

[1]About the Fidelity Investments Retirement Savings Assessment
The findings in this study are the culmination of a year-long research project that analyzed the overall retirement readiness of American households based on data such as workplace and individual savings accounts, Social Security benefits, pension benefits, inheritances, home equity and business ownership. The analysis for working Americans projects the retirement income for the typical household, compared to projected income need, and models the estimated effect of specific steps to help improve preparedness based on the anticipated length of retirement. Data for the Fidelity Investments Retirement Savings Assessment were collected through a national online survey of 3,569 working households earning at least $25,000 annually with respondents [and spouses, if married] age 25 to 75, from August 22 through September 26, 2022. All respondents expect to retire at some point and have already started saving for retirement. Data collection was completed by Versta Research using NORC's probability-based nationally representative online panel. The responses were benchmarked and weighted against data from the American Community Survey and Current Population Survey conducted by the U.S. Census Bureau and the U.S. Bureau of Labor Statistics. Versta Research and NORC are independent research firms not affiliated with Fidelity Investments. Fidelity Investments was not identified as the survey sponsor. Fidelity's Retirement Score is calculated through Fidelity's proprietary financial planning engine. Of note, Fidelity continually enhances and evolves the retirement readiness methodology, guidance tools and product offerings. This year's survey processing includes enhancements including, but not limited to, demographic weighting, retirement income projections and social security estimates. This analysis is for educational purposes and does not reflect actual investment results. An investor's actual account balance and ability to withdraw assets during retirement at any point in the future will be determined by the contributions that have been made, any plan or account activity, and any investment gains or losses that may occur. For more information on Fidelity Investments® Retirement Savings Assessment, an executive summary can be found on Fidelity.com.

[2]How to save more money | Fidelity eReview: 660375.23.0

[3]Retirement Income | Coming up with a plan | Fidelity eReview: 895018.6.3

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