Market Insights: New Developments, What to Consider, and Top Questions Answered

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TRANSCRIPT

SPEAKERS:

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Jim Armstrong: Hello and welcome to Market Insights. Thanks for joining us today. I'm Jim Armstrong with Fidelity. You've probably heard our panel talk in the past about tax deferred accounts. Maybe you've even started contributing to one yourself. But here's the thing—there's a second step to that process that a lot of people miss—myself included. A little embarrassing. We'll talk about it later. Can be disappointing and frustrating, certainly, to fall into that category. So that's a big part of what we're going to be talking about today—the common oversight that people make with IRAs, HSAs and some other accounts. This is a good time to bring it up because of this year's delayed federal tax filing deadline. So we'll explain why that matters in a moment as well. For today's discussion, we are proud to be joined once again by Jurrien Timmer, who's going to be talking about what he sees going on in Wall Street and in the economy as a whole. And then Jenn Sirois is here as well to talk about what she's seeing in her daily work building financial plans with Fidelity's customers. Jenn, Jurrien, great to have you here again. Happy Tuesday.

Jenn Sirois: Happy Tuesday, Jim. Great to be back.

Jurrien Timmer: Great to see you guys.

JIM: Jurrien, let's start with you. It is Tuesday, April 27. You are our big picture go to. And for more than a year, I think it's fair to say our big picture has really been dominated by both COVID and the recovery from COVID. So I was hoping you could start us off today just by kind of catching us up on where the markets and overall economy are now through that lens, in particular.

JURRIEN: Yeah, so we'll start with where we are, you know, in terms of the battle against this pandemic. And, you know, it's still a major healthcare crisis around the world. We see the stories out of India. You know, parts of Europe are still in lockdown. Even our neighbors to the north in Canada are in a fairly strict lockdown again. But the news in the U.S. has been very, very promising. You know, this chart—I've shown this in the past, but if you look at the gray bars, that shows the number of hospital beds in the U.S. occupied by COVID patients. And a few weeks or even a few months ago, as vaccinations started to get rolled out, there was talk about—okay, maybe there'll be yet another surge coming because people are just kind of tired of all the social distancing and they're going to feel more complacent. And we got a little bit of a wave—you can see that, but it's been very, very small and it's already rolling over. So very encouraging news there. So the number of hospital beds occupied by COVID patients bottomed at 5.6% about a month or two ago after having reached 19% earlier in the year. It went up to 6.4%, but it is rolling over and the number of new cases is starting to fall off. And clearly, vaccinations have a big thing to do with that. The blue line here shows the combination of Americans who have gotten COVID, so that's about 32 million people have gotten the disease—so are immune presumably from it that way. And another 93 million and counting have been fully vaccinated. So when you add those two up, you're getting to about 37% of the population that is basically immune from COVID one way or the other. Now, that's not herd immunity—that's closer to 60, 70 plus percent. But it's certainly a huge improvement, and you can see how rapidly that line is rising. And so my guess is—and I'm not a health expert, but my guess is that the lack of another surge and one that only had a small amount of impact and is already rolling over—that has to do—presumably, that must have something to do with the fact that more and more people are immune from this. I wish this good news could be repeated around the world. But certainly, in the U.S., you know, this is a major factor. And obviously, this spills into the markets, because this allows the economy to reopen, and that is reflected by the stock market, and we'll talk about that in a moment.

JIM: Yeah. That's exactly where I wanted to head next, so thank you for teeing that up. Based on what you were just saying, I was wondering if you could tell us where the markets might be headed based on that. Asking specifically right now because in a couple minutes, we're going to start talking to Jenn about some investing strategies, particularly for people who might be thinking in the medium to long term. So they're looking at what's happening now and trying to wrap their brains around what might be about to happen.

JURRIEN: Yeah. Well, so—you know, among my many rules for investing, one of them is that being able to predict the future is only half the battle. And of course, none of us can predict the future. But even if you knew with perfect certainty how the economic cycle was going to unfold, that's still not enough because you also have to look at what actually is already reflected in the market. Right? The market always discounts the future or what the market thinks is the future. It's not always correct in doing so, but this was our conversation over the last year, of course—you know, when the market bottomed in March and things were still getting worse, even though, like, through April, May, June, the reason that could happen was that the market was already anticipating better days ahead. So knowing what is going to happen only gets you halfway there. But knowing what's priced in is the other half. So the bottom line right now is that, as I just showed, you know—the COVID curve really in good shape, economies reopening, we saw more news from the CDC this morning about mask wearing for people that have been vaccinated outside. So you can really sense that, you know, life is starting to come back to normal. But the market's already kind of there, right? The market has been pricing this in for months now. We saw that in the rotation from growth stocks to value, the rise in interest rates, et cetera. And so one way of looking at this is in the chart here, in the top panel, I showed the weekly jobless claims, and you can see kind of that heart attack last year, March, and then the recovery from that. The bottom panel, the orange line shows the New York Federal Reserve's series called the weekly economic index. So that's a very fast-moving weekly series that measures kind of where the economy is, and a year ago, it was at -11. This index today is at plus 12. Full round trip. But again, the market always looks ahead. So what we really need to look at—if you're someone like me and always looking at where markets are relative to what's happening—you have to look at the rate of change. Or—we call that the second derivative, to use a fancy term. And the rate of change peaked a few weeks ago. Similarly, a year ago, in March of last year, the rate of change bottomed the week of March 27th, which coincidentally is the exactly the week the market bottomed. So markets often inflect when the rate of change of whatever economic series you are looking at also inflects. And so that rate of change peaked a few weeks ago. That's exactly the time when the bond yield, the 10-year treasury yield peaked at 175. It's down to 155. The growth to value rotation kind of, you know, took a pause. And so, to me, that doesn't mean the market's going down or anything like that, but after a very large run up in anticipation of the reopening—which is exactly what is now happening—so the market was exactly correct in anticipating this. Now that we're actually there and it's starting to happen, my guess is that the market probably is going to take a breather here because there isn't really a lot of new incremental news to discount at this point. So the markets always go through phases where they go through price discovery, and then they rest, and then they go through price discovery. And I think we're kind of at that consolidation phase right now.

JIM: 100%. Again, something we're going to be asking you about in the coming weeks and months. So thank you for bringing it up again. Jenn, I want to turn to you—to bring you into the conversation here to talk about the topic at hand for the day. This idea that if you're a long-term investor, maybe you've got goals 10, 20, 30 years away. I've heard you and others say opening and contributing to a tax advantaged account could be step one. What are some folks forgetting?

JENN: Great question, Jim. So making contributions—that is a great first step. Key to long term savings is simply getting started. So as an investor, you have options we've talked about before: traditional IRAs, Roth IRAs, health savings accounts or what we call HSAs. They all have the potential to offer tax advantages for us, but many people that I work with or have had conversations with—they think that once they put money into the account, they're done. And they're missing a second step. So what happens is—or what I am finding is they feel like the account behaves just like what they experience with their workplace 401(k) or 403(b). I set up the account, my investment is—I either choose something or something—a default is chosen for me. Either way, money is coming out of the paycheck, going into the investments, and you've got that moving forward. However, to reiterate, that's not how things happen in an IRA or a health savings account. When you make your contribution to that account, the money stays there in cash. It's not invested and it's bringing very low interest or investment potential. So the second step is you need to choose how you want the money to be invested, and that is the misstep that I'm here to help people avoid. So I think you have a story to share with us, Jim.

JIM: Yeah, I need Jim Armstrong in a time machine is what I need right now. Because I will fess up—I did this in my mid-20s. I was super proud of myself—I opened up a Roth IRA, I was contributing every month, and was just doing everything right. And maybe about a year in, I went to look at the balance and it hadn't grown very much. I thought, "What's going on here?" Everything I contributed for that year was sitting in cash the whole time.

JENN: Yeah, so as a financial consultant, I hear stories like this all the time. And this time of year—tax time—is often when we typically spot it. Because I have—you know, we work with families that will fund accounts in lump sum deposits. So either they're doing it because they're eligible for a tax deduction for the prior year or maybe they got their tax refund and they're saying hey, this is a great opportunity to boost my long-term savings. So we'll talk more about that in a minute. But just remember that keeping the money in cash means there's not a benefit from the power of compound interest potential. So I'll ask you to consider this example here. So if today, you were 25 and you were able to invest $6,000, which is the maximum annual contribution for an IRA in 2021. After 40 years, that one contribution, Jim, could grow to almost $90,000. So, just a reminder: if you're 50 or older right now, you can actually contribute $7,000 a year. So we took that into account in this hypothetical example as well. So when we ran the numbers in this hypothetical example, we assumed a 7% return on a $6,000 contribution made annually for 25 years. So that's starting at age 25, ending at age 49. And then $7,000 a year contribution from age 50 through the age of 70. And if all of that came to fruition, that individual investor could actually have close to $2 million by the time they're 70, if, if her money was invested. So if that investor stayed in cash in a very low interest cash account, like what we're seeing today—in the end, there might be $300,000 when she reaches age 70. So really not a lot more than what the initial investments totaled up to be. Just to follow up on my earlier thought: you have, when it comes to making contributions and the tax deadline, you actually have until the current tax filing deadline to make a contribution for the prior year. So for 2020. So if you haven't filed your taxes yet in 2021, you may still be able to contribute up to the account maximum for 2020 to accounts like your IRAs and your traditional, your Roth or your health savings accounts. This year, you have the opportunity to do that until May 17th. You would want to work with your tax professional to see if this is going to be a benefit from a tax perspective. So that would be someone else to connect with on that, Jim.

JIM: And on that same front—just a quick follow up for you. You mentioned earlier folks might be able to use a tax refund maybe to enhance their saving strategies. Can you just help folks understand how to get their heads around that if they're curious about it?

JENN: Yeah, absolutely. So I see people take their refund all the time and earmark it for their—in this case, their retirement savings. But just a reminder: you don't have to put money in in one big lump sum. Maybe you consider equal monthly payments or maybe something once a week. That's what we consider dollar cost averaging. One reason many people miss the step of investing their contributions could be because they believe that their IRA is an investment itself. So it's not unusual that we hear: "So, Jenn, how much does your IRA pay? Or how much does it earn, rather?" But the IRA is simply the holding account where you put your contributions into. So beyond keeping them in cash, there are many options for a self-directed or do it yourself investor. You've got exchange traded funds, mutual funds, bonds, CDs. And the process to choose the—or to choose how to invest the money can be as easy as some pull down options or menus, clicking a couple of buttons once you know what you'd like to do with it. But Jim, I'll tell you, one of the hurdles for many is that there are thousands of choices that can become overwhelming, and people get afraid of making the wrong decision. I often think of—hey, I'm at the grocery store, and I'm from front of the—you know, the yogurt case. And there's all these different kinds—you know, you've got things with candy or different exotic fruits. And I'm standing there saying "Where's the strawberry? Where's the blueberry? Where can I find it?" Sometimes it can be almost immobilizing. So to help avoid the decision overload, there are resources available to sort through. So Fidelity's website is a great choice. Working with a Fidelity representative is also another great choice to help with that decision-making process.

JIM: Totally resonates with me. I'm sure there is a better term for it, but it's choice overload, right? There's too many things out there to help—to make your mind. But I can say, like—once that Roth IRA- when I moved it out of cash and into something that was actually being invested, it just felt a lot better to have that done. It felt smarter, a little bit, frankly. Jurrien, as we wrap up, I wanted to actually ask you a question to start a conversation that we're actually hoping to continue next week—and that's about taxes. A lot of folks are interested in hearing about the Biden administration's potential plans for taxes, and I'm just curious, from your perspective, sort of what do you know? What should we know? And what might we expect?

JURRIEN: Yeah. So, certainly, there was news last week—although it really wasn't new news. It was actually part of the Biden campaign platform. But that was that capital gains, taxes could go up a lot. They could actually go up—they could actually double from their current 20%, along with an increase in corporate taxes as well as top marginal rates for income taxes. And, you know, it's really not surprising. I mean, if you look at this chart, this goes back to 1900. When debt levels go up, as they are rapidly right now, taxes generally follow because the debt has to be paid for in one way or another. And so over the last 13 months, we've been on the—kind of the receiving end with stimulus checks and, you know, fiscal policy that has a positive multiplier effect on the economy. And now, I think we are going into the other side where we go on to the liability side in terms of higher taxes. Now, having said that, this is by no means a done deal. My guess is that taxes will go up, but maybe not as much as are being telegraphed. Because, you know, like the 1.9 trillion stimulus program that was passed, you know, a month or two ago—whatever comes next, whether it's part of an infrastructure program or a clean energy program, the taxes will have to be folded into that. And it'll have to go through the reconciliation route in all likelihood, which means the democrats will need all 50 senators to be on board. They've only got so many shots on goal because there's only so many times you can go through reconciliation. And so it is by—far from a foregone conclusion that capital gains taxes will go up to 40%. Maybe up, but a lot less. And so—but this is, you know, a moving part in this conversation. You know, I've looked at this, many people—other people have looked at this in terms of what it means for the market. You know, it's kind of a chicken and egg theory. You know, the market goes up, valuations go up, when people sell, they have more capital gains because the market goes up, so they pay more taxes on it. Whether—how much of that is affected by the rate that you pay on the capital gains—I mean, are you not going to invest in stocks because the capital gains tax is 28% instead of 20%? I don't think so. I mean, it's—you're still going to invest in whatever is the most productive asset out there. So I don't think it's a foregone conclusion, from my side, at least, that higher capital gains taxes are a negative for the market in general or even for the economy. But this is part of the conversation, and we're going to be hearing a lot more of it. And I know we're going to talk about this again next week as well.

JIM: Yeah. That's exactly right. So thank you for beginning that conversation with us. Already a lot to think about. So thank you both for being with us today. And for our viewers, thank you, of course, for watching. Just a reminder that if you would like help with your financial planning or you've just got questions about what we have to offer, you can certainly visit Fidelity's website or download the Fidelity app on a mobile device. Those are a couple of really good ways to explore our planning solutions and get answers to your questions and start to learn more about the topics we covered today and a whole lot more than those as well. Again, tremendous, huge thanks to Fidelity's Jenn Sirois and Jurrien Timmer. Next week—again, we're going to take a bit of a deeper dive into those proposed potential tax increases, what they might mean to us as investors, as well as some strategies that you might consider in a potentially higher tax environment. So we hope to see you then.

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