Insights Live: The markets, midterms, and your money

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TRANSCRIPT

SPEAKERS:

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Views expressed are as of 10/6/2022 and based on the information available at that time and may change based on market or other conditions. Please read the last page of this transcript for important additional information.

Mary Kay Leydon: If you have legal or tax questions about your specific situation, we encourage you to talk to your tax advisor. With that covered, why don't we go ahead and get started? I'd like to introduce our moderator, Roger Hobby. Roger is the head of private wealth management at Fidelity Investments. Thank you for joining us, Roger.

Roger Hobby: Oh, thank you, Mary Kay, and thank you to all of our viewers and our clients that have taken the time to log in today as well as submit some questions. The questions are very, very helpful for us because we understand what's on your mind, and we kind of shape a lot of the content.

And with the backdrop of inflation and market volatility and the midterm elections, we thought today would be a good time for us to spend a little bit of time talking with some of our colleagues who've got a lot of experience and insights into some of the challenges that are going on and help us provide a little bit of perspective around what it is that's going on to help you understand it as well as provide some suggestions for next steps to help you preserve some of your wealth and think about how to take advantage or manage through some of these difficult times.

We've got three of our—three of my colleagues that I work with. I'm very excited. I'll let them talk a little bit about what we're doing. But we have Denise Chisholm, who's one of our quantitative market strategists. We've got Matt Crane, who's one of our wealth advisors, one of our financial consultants that deals with clients and helps develop plans. And we've got Alice Joe from our government relations.

So we're going to be able to get a nice mix of perspectives around the market, perspectives from our clients, as well as a look from the hill around what's going on. But why don't I turn it over to our panelists and let them take a quick moment to introduce themselves and talk a little bit about their areas of expertise and some of the experience that they bring to the conversation? Why don't we start with you, Denise?

Denise Chisholm: Sure. Hi, everybody. I'm Denise Chisholm, as Roger said. So I am in equity research, which means basically that I pitch investment ideas to our diversified portfolio managers, but you can think of me as an equity market strategist essentially and one who uses historical probabilities really to inform our investment views.

ROGER: Great. We'll go to you next, Matt.

Matthew Crane: Hey, thanks, Roger, and hello, everyone. Wherever you find yourselves, good morning, good afternoon. Nice to be with you. My name's Matt Crane, I'm a financial consultant at Fidelity. What that means is I consult with Fidelity clients to understand their concerns and their goals, and then together, we construct financial and investment strategies that are tailored to their needs.

ROGER: Great. Thanks, Matt. And last, Alice, you're up.

Alice Joe: Thanks, Roger. So hi, I'm Alice Joe on Fidelity's federal government relations team, and I'm based here in Washington, DC. So I get a good feel of what's happening both in terms of Congress and the administration, so we keep a pulse on that for our Fidelity customers. But we also work to engage with lawmakers and policymakers to make sure that the policies align with a lot of the objectives of our clients and customers.

ROGER: Yeah, well, let's just jump right in, Alice. So say on everybody's mind is the upcoming elections, and what are your thoughts on what we can anticipate? What are some of the things that we should be aware of and looking out for and paying special attention to with this midterm election?

ALICE: Yeah, Roger. So we've got a midterm election coming up in less than four-and-a-half weeks here. And the House and Senate are up for grabs right now. Democrats clearly control the House and the Senate, but the margins are pretty thin—50/50 in the Senate. They just have a nine-seat margin in the House, so Republicans are looking to take over.

I will say that, looking at history, the political winds favor Republicans because if you look at the incumbent in the White House, that party, they tend going back to 1946, they have lost every single midterm election in the first term of a presidency in that party, with the exception of in 2002 when George W. Bush actually picked up a few seats in the Republican Party. But going back, President Trump, President Obama, President Clinton, they all lost seats then.

But aside from that, obviously, past is not indicative of the future. There's other key factors that you should consider in looking at the elections and how that might turn out. So one is the retirements in the house. You've got 32 Democrats who have decided to retire, so it's a lot harder to defend those seats when it's a new candidate coming in versus an incumbent defending their seats. And we've also seen a number of Democrats losing the primary, too, so that number is now up to 38 that they're going to have to defend.

The other piece here is, where is the president's approval rating? Because if you look in the past where President Clinton, President Trump, and President Obama were, they were hovering around the low 40s around the first midterm. That's where we see President Biden today, roughly around 42%, so that's an indication there. Another one is, where do people think the country is headed? Is it headed in the right direction? Recent polling suggests that 65%, 66% of voters out there aren't in favor of where the country is going.

And then, of course, candidates that are out there that are running for office. What is the quality? Are they resonating with the voters, do the values sort of align with them? So that's going to be an important factor in the elections as well. And then, finally, voter turnout, that's always critical here in terms of who's going to come out? Which party is going to motivate their base to come out more? And where are the independents? Are they coming out? And what are the top things that are going to be top of mind? Whether it's economic issues or social issues, that's really probably going to determine how we go here.

ROGER: Yeah, 65% is a troubling number of our people polled that are heading in the wrong direction. We're going to have to sort of tease that out a little bit more. But talk a little bit about the Senate. You mentioned 50/50. Where are we as it relates to the Senate?

ALICE: Yeah, so it's up for grabs. We've got Democrats defending 14 seats. Republicans have 21 seats, so it's a little bit more of an uphill climb for Republicans there. But there's probably 10 states that are really in play there, and four of them are with Republicans who are retiring. So again, that—not having an incumbent is going to make it harder for them. Three of them—three of those states, which are Ohio, Pennsylvania, and North Carolina, those are going to be really tough for Republicans to hold on to, or they're going to have to spend a lot more resources to defend those.

On the flip side, Democrats also have a number of states, too, that are, quote, what we call "in play," meaning the margins there are so close that we don't know. So I think places like Nevada, New Hampshire, and even possibly Arizona are big question marks at this point.

But the one state, I think, is the critical one here is going to be Georgia. Traditionally, Georgia's in the South. It generally tends to swing to the right, but right now, we've got two Democratic senators there. And the unique thing about Georgia is the election process there. They undergo what's called a jungle election, meaning if on election day, nobody gets over a 50% threshold, then they're going to have to go to a runoff. That's what we saw in 2020. And so it may not be till December 6 if things are 50–49. We may not know who actually takes control of the Senate—if Republicans take control or Democrats hold their majority.

ROGER: Yeah, we're going to have to hold our breath and keep our eyes tuned on that. Does it often happen that they get in these situations greater than 50% coming right out of the gate, or is it usually that there's an independent person that takes some of it that hurts the 50%?

ALICE: That's exactly what happens if there's three or four candidates there, some from different parties. It does pull the votes away. But if you have one candidate that's really, really strong, then certainly, they could easily avoid a runoff.

ROGER: Yeah, well, again, it'll be interesting to follow it. So Matt and Denise—Matt, I want to come to you in a second. Talk a little bit about what our clients are saying about some of these political things. I'm sure we've got people on all the whole spectrum associated with people's political views.

But Denise, I might ask you an unfair question, but I'm going to ask it anyway. If we look back historically, can we find times historically that have looked a little bit more like where we are right now, and can we learn from the past and start to think about what will the future potentially look like learning from times that were similar? Are there some times in the past that we can learn from, that we may be able to project a few scenarios that might play out in the future?

DENISE: Yeah. I mean, just weaving in the midterms. I think that of the four years in the presidential cycle, there's a lot of variability historically, with the exception of the one year following midterms. So it tends to have the narrowest range of outcomes. It tends to have the least amount of downside for the market, and conversely, it has 94% odds, going back to 1950, of an advancing market in that year. And I think that the corollary that we can use for our current situation is right before midterms tends to be a very significant period of uncertainty—

ROGER: Yep.

DENISE: Which is exactly where we are right now. And that tends to be a contrarian buy indicator for the market because typically highly uncertain environments get resolved, and that tends to decline in uncertainty, and that tends to be the impetus for a more bullish scenario for the market. So I think that there might be a silver lining to the uncertain environment that we are actually seeing right now.

ROGER: Yeah, that silver lining is where there's uncertainty. Eventually, we'll get some certainty from the selection process. And what you're saying is markets don't like uncertainty, and they like certainty. So once you get over that hump, that might actually be to our advantage, at least historically speaking, from that perspective. So, Matt, what are some of the things that clients could or should be doing around the different scenarios relative to the election? What are you hearing?

MATTHEW: Yeah, great question on that, Roger. Elections are tough, especially midterm elections because they're really short-term issues, and it's hard to plan a long-term plan around short-term issues. So one of three things is going to happen. You're going to have a short-term upward market, downward market, or sideways.

And so what I'm telling my—the clients that I work with—is control the things that you can control. That's what planning is all about because you're going to have these unpredictable outcomes that happen, including with the midterm elections. So you can't control what happens in DC. You can control having a strong financial plan.

There are three elements that you want to have in a strong financial plan, so maybe I'll talk to those for just a second. But the first is having money for your short-term expenses, money that's in an emergency fund that you can access in the event that you need money when the market's down. So if, for example, the market drops because of the midterm elections in the short term, you now have cash that you can access for those needs.

I would also say, in this vein, make sure that you're paying attention to the short-term investments that you're in right now. Money markets, for example, are yielding more than they were earlier this year, so make sure you call Fidelity, and whatever you choose, you're getting the most interest that you can.

The second place you want to have some of your money is in a protected position so this can be protected from the market, your assets, and protecting your principal, or it could be protecting your income. And then the third place is having a disciplined and responsible growth strategy. And I can't emphasize enough how important that is even in this market because at some point when this recovery happens, you're going to want to make sure, and you're going to thank yourself that you stayed in the market with some of your money in that growth strategy discipline.

ROGER: Yeah, I think it's a good advice, making sure that you take the time to cover your emergency situations as well as be still positioned for the appropriate time frames. Thank you, Matt. All right, Alice, I'm going to ask you to get your crystal ball out here if you don't mind just a little bit and talk a little bit about some of the election outcomes and what are some of the different scenarios that might play out as it relates to policy shifts or spending that could be coming down the pike here from some of the changes that we might anticipate happening from the elections.

ALICE: Yeah, absolutely, so let's talk about status quo. So let's just say Democrats maintain control of the House and the Senate. In fact, if they do take some extra seats in the Senate, we could potentially see some of the same things that they tried to push through earlier this year come back onto the table, things like the Build Back Better Act, where we saw some certain programs as well as some tax increases that might be back on the table if they maintain control.

However, if Republicans can take control of one chamber, certainly, that would eliminate the ability to use a reconciliation bill. And that's a vehicle that they use when it's a partisan issue where they only need a 50-vote threshold in the Senate rather than the 60-vote threshold that typically takes to pass a bill.

But if the Republicans are able to take the House, what I'd expect to see is increased oversight and investigations, oversight on some different policies that perhaps were passed five years ago or more recently in the past couple of years or this past Congress just to see what's working and what's not. And, of course, an investigation into actions among the executive branch was probably on the horizon as well.

If the Republicans are able to take control of the Senate, I think this is really the critical piece here, is because the Senate is the body that confirms nominees from the administration. So that would control some of the people who are appointed to the courts, including the Supreme Court, or have high-level policy positions within the executive branch. So they would sort of control the nominations process and perhaps cause some challenges to the sitting president in terms of nominating people that are of a less moderate ideology.

ROGER: Yeah, and it speaks to what Denise was saying. There's a lot of different scenarios that can play out, and there's a lot of uncertainty. And if we can get over the hump and figure out what the answers to those questions are, we'll start to have a little bit more certainty, and then the markets will behave themselves a little bit more.

Taxes, Alice, it's on everybody's mind, a lot of our clients' minds. Back when the Biden administration was proposing increasing taxes on income as well as estate planning, it was a lot of a buzz, but when the Inflation Reduction Act came out, it didn't include those. Is that something that—help our clients and viewers to understand. Could that be something that gets revisited? Could it be included in something else? And where does that stand? What's the likelihood of that being a part of the plan going forward, at least in the short to medium term?

ALICE: Sure. I think it absolutely could be back on the table if Democrats maintain control of the Senate and the House, but they also have to have that extra two seats going from 50% to 52% in order for those things to come back to fruition there. Having said that, I think the political winds are blowing towards a split Congress, so I think that's less likely to happen.

But I will say what people need to keep in mind is the Tax Cuts and Jobs Act that was passed in 2017, where we saw a shift in the different tax brackets as well as a reduction in the tax rates, those are set to expire in the end of 2025. So it's a few years away, but as you know, legislation takes a long time to pass.

And so they're going to have to start looking at whether or not they want to keep the structure the way it is to downplay the impact to individual investors. And I will say the one thing that's also included in that that impacts individuals as well is, if you remember, they doubled the standard deduction, so that's going to go back to half of where it is now. But then maybe they'd give us the personal exemption back and the dependent deduction that was taken out in 2017.

But it also—as you may recall, the estate tax, it was doubled in 2017, so that potentially could revert back to the five-point-something million indexed for inflation to where it was pre-2017. And then, of course, the big one I think a lot of people are thinking about is the state and local tax deduction, where it was unlimited before 2017 and is now limited to $10,000. So where does that go? To be determined.

ROGER: Yeah, no, it's a very insightful point. A lot of our clients and a lot of people don't realize that their wait time that those tax reductions or those increases were time boxed, and 2025 will be here before you know it. Matt, what should people be thinking about? What should our clients be thinking about now to take advantage of the certainty of what we know now, knowing that, potentially, things could potentially change in 2025 going forward? Are you having conversations with clients, and if so, what are we talking about on how to take advantage of those?

MATTHEW: Of course, Roger, I'm having conversations with clients every day, so that's my job. I—so there are a few things that do come to my mind, and in light of what Alice just said about tax cuts expiring, Roth conversions come to my mind as one of the most effective tools that you can take advantage of right now. While tax brackets are low, you can pay some tax on your pretax money. Move it to a Roth IRA, for example, and then that now grows tax-free.

So that's also a good tool for inheritance. So when your beneficiaries inherit your money, if it's pretax, they'll have to pay tax on that money, but if it's Roth and you've been doing these Roth conversions, then now they get to inherit that tax-free.

And then the last thing I would say on Roth conversions outside of taxes is just the timing of where the market is. The market being this low provides a pretty good opportunity to look at a tax as a—to look at a Roth conversion because when you convert money while the market's low into a Roth IRA, you now benefit from the bounce-back in the market—the recovery in the market in a tax-free vehicle.

Now, remember, we are not tax advisors. I have to give that disclaimer. I think that was already given, but just to make sure. So it's important to consult your tax advisor and make sure that a Roth conversion would make sense for you.

But two last things I would say on this point, Roger, and that is contribution limits also have gone up this year. They are typically indexed to inflation. So you can contribute more to a 401(k), for example, this year. With inflation as high as it is, many are assuming that 401(k) contribution limits will go up quite a bit next year as well, so look out for that.

And then the last thing is to get—speaking of wealth transfer, you can get around the gifting tax if you give up to $16,000 to someone as an individual, and as a married couple, you can give up to $32,000. Those are a few thoughts that come to my mind.

ROGER: Yeah, and they're very good thoughts. And I think that the idea of talking to an advisor like yourself and asking smart questions, I think that's really one of the most powerful things that our clients can do, is to take advantage of talking to our advisors and specifically asking these questions around how to take advantage of some of these opportunities now before the window closes potentially as well as—and, Matthew, you brought it up. We're going to see the other side of the inflation issue around. A lot more of the dollar amounts being indexed for inflation than going up probably in 2023, so it's something to talk to your advisor about as well.

All right, Denise, a lot of things are on people's minds. As Alice mentioned, the economy and inflation are key voter issues, but they're also key market issues. And we've seen lots of volatility—markets going up over a couple of days, markets going down over a couple of days. Inflation seems to still be running high.

So if we go look at from a historical perspective—again, looking back at the past to try to glean some sort of a perspective around what could happen going forward—can you talk a little bit about where have other times where this kind of an environment has existed and what can we learn from it and where did it go in the past and do you think it will go that way in the future?

DENISE: Yeah, I think midterms aren't the only thing that's uncertain right now. Obviously, inflation and the Federal Reserve and how much they're going to have to hike to bring down inflation is a deeply uncertain environment for the market, and that's really determining a lot of outcomes and volatility that you're actually seeing.

So a couple of points, too. One, it's important for investors to know that inflation has been decelerated. So the core PCE deflator, which is the Fed's preferred measure of inflation, has been decelerating for the last six months, just not necessarily as much or as quickly as the Fed would like.

But I think that the important thing, when I look at historical probabilities, that has been an impact for the market might be a silver lining, which is, while inflation is decelerating, wage growth is decelerating along with the economy overall, but it's the interplay between all of those factors that tends to be the most predictive, meaning that if inflation slows faster than wage growth, which is what we are seeing, real wages tend to rise. And that's a good thing for the US consumer because real income growth has been deeply negative over the last year, and I think that that is a silver lining, that when I look in the market, that might be the driver of the next one- to two-year returns.

But the second thing investors need to understand is, however dire the headlines look as it relates to inflation, just always remember that the market is a discounting mechanism. And that means, sometimes, you see very odd things historically with the market advancing, even though the news is bad or even stays bad, and I'll give you a very clear historical example.

I mean, certainly, what we saw in the recent sell-off in the market was when Jerome Powell essentially said, I'm coming great guns for inflation. We have seen this movie before in a little bit of a different setup with Paul Volcker in 1979. So you say, OK, Volcker did a similar speech that said, I'm coming great guns for inflation. We can look back in history and say, what happened?

Well, they raised interest rates very severely over the next six months. What we saw was a decline in industrial production by about 6%. The unemployment rate rose by about 300 basis points to about 7 and ½ percent, exactly what we're talking about now. And what did the market do? The market was actually up 25% from the day of that speech to one year later. So I think it's really important for investors not to be fearful of the headlines because, more often than not, it's a contrarian way to invest.

ROGER: Yeah, and it's because the market pundits like yourself and others are looking into the future and forecasting what they think is going to happen and pricing it in now. So I—it's a counterintuitive approach for a lot of our investors to think about—maybe you could kind of share with us a little bit about how could one of our investors—my two cents was when I fill my car up, and it's less than $100, I feel like things are actually kind of coming down. It's probably not the best measure.

But what can our investors—what can our clients look at to see whether or not inflation actually is starting to get under control? You mentioned that we're starting to make some progress there, but what are some of the tangible things?

DENISE: We're certainly starting to make progress. Again, it's just the speed of progress. But I think that you hit on a leading edge that is usually commodities. That is typically the leading edge of the predictor for inflation. And we have seen a significant decline in gasoline prices and crude oil. We'll see if that holds going forward. But that is an important thing to watch because it tends to lead a lagging indicator of inflation, and it tends to be a stimulus for the US consumer.

ROGER: Yeah, well, I'm going to ask an unfair question, but it's on everybody's mind. You got the geopolitical fallout with the war in the Ukraine, supply chain issues stemming from some of our large trading partners. How can we read the tea leaves there to start to see changes or progress or improvement from a layperson's perspective?

DENISE: Yeah, there are a lot of surveys. I mean, I don't know if anybody follows the economic data, but there are a lot of implicit surveys within the PMI, within the NFIB, which is the small business survey, that will give you some indication of supply or delivery times, which is essentially a proxy for all of that supply side snarl that we've seen over the last year.

They are all improving. I would say that they're not back to normalized levels, but all of those indicators are improving. So post, I'd call it, both a demand shock from a fiscal stimulus and a supply shock of the war in Ukraine, plus COVID, we're getting out of that. So we're normalizing but just slower than I think a lot of consumers would actually like.

ROGER: Gotcha. So, Matt, I'm going to come to you and talk a little bit about, in a second here, I would ask Alice a quick question, but just put it on your radar screen. How are our clients dealing with a lot of this unrest? How are our clients dealing and thinking about a lot of these changes? But before I ask you to address that, particularly, Alice, what is the government doing to address these particular issues? Would you talk a little bit about some of the policy associated with helping us try to sort of work through some of these challenges?

ALICE: Yeah, certainly, the supply chain is a huge concern here in Washington. And one of the few times that we've seen bipartisan action here was the summer when Republicans and Democrats got together and passed what we call the CHIPS Act. And that bill was intended really to help rebuild the supply chain for the semiconductor industry in the face of foreign competition there and some of our former trading partners pulling back a little bit, and this is a way really to keep the US competitive there. So there is significant money put out for tax incentives to boost manufacturing here in the US, as well as billions of dollars going into R&D for new investments there.

The one other thing I'd say about the supply chain is the current administration is definitely concerned about getting goods from point A to point B, which is really important. Even if you have the goods here, how do you get them out and distribute it? And so there's some potential strikes, including the more recent railway worker strike that we saw them intervene there and ensure that there is a continuous transportation of these goods back and forth. And there's some other issues potentially looming with the port workers as well, but so far, so good. They're definitely keeping an eye on these issues.

ROGER: Yeah, well, good. I know we're doing everything we can, but I think our clients and people, in general, are just tired of hearing things called supply chain and social distancing and pandemic. So it's getting a little bit hard to continue to deal with these things because they impact so much of our lives. So, Matt, what are our clients saying? What are the top concerns that we're hearing from them as it relates to these markets, as it relates to inflation, as it relates to the geopolitical issues? You talk to clients all day long. What are you hearing?

MATTHEW: So the common thing that I'm hearing from clients is they're worried obviously about the market and feeling like nothing is working in 2022. I hear them say, I feel like there's nowhere to hide in 2022. You've got stocks that are down because of market declines. You have bonds that are down, having one of their worst years on record because of interest rates rising. You have cash being eroded because of inflation. So all of these things coming to a head.

And clients are wondering, is this a repeat of the 1970s? Is it going to take a while to get through this in terms of bad equity markets and interest rate risk? And I think Denise could probably give us some more insight on that one.

DENISE: Yeah, I think that there are some pretty key differences when I look at the data between now and the 1970s. I'll give you three and one as sort of a similarity, but one is just the magnitude of the problem that we have is, to me, very, very different. So if you look at the annualized run rate of the core PCE deflator, again, the Fed's preferred measure of inflation, it's running around four to five. That was running around 10 to 19—let's call it '75 through '82. So this is half as bad just using that as a measure, which is not to say that it's not a shock to the US consumer. It certainly is.

ROGER: Yeah.

DENISE: But it is an order of magnitude different than what we saw in the 1970s.

And inflation isn't the only shock that the US consumer has needed to manage through. In fact, something more important historically has been the macro shock as a result of, specifically, crude oil, which is related to inflation but very, very different on its own. And that impact, to both the US consumer, corporate America, and the overall US economy, is meaningfully different than what it was in 1970.

Using the consumer as an example, as much as you're spending a lot more, Roger, on filling up your car, what you see is the energy goods and services as a percentage of overall disposable income to the US consumer is running around 5%. That was about 9% in the '70s. So again, this is a really key difference.

So even the shocks that we're managing through are less severe than we saw in the 1970s. And when I look at the valuation data that's predictive, it's not always just the multiple of the market or the P/E, price-to-earnings ratio, which is a measure of what—a measure of profitability in terms of the US corporates.

And what you look at and what is more often than not predictive is looking at that relative to Treasury yields. And because Treasury yields were so much higher in the 1970s, what you're finding now is the disconnect in terms of being priced for what could potentially be even worse news.

ROGER: Yeah, hey, Denise, share with our audience not but maybe 12 months, 18 months ago, closer to a peak price-to-earnings, valuations relative then to where we are now because I think it's been another overused word, "unprecedented dropping." Would you talk a little bit about that?

DENISE: Yes, so I think, a year ago, we were about 24 times, and now we're running around 15 times. So it has been a historic valuation compression, which the only other time you've seen it historically was in the stock market bubble of 2000. But at that point, you also saw an earnings decline, and our earnings are actually up 8%. So corporate America, relative to any other historical parallel, is much more profitable.

ROGER: Yeah. Energy's on a lot of people's mind. Matt, talk a little bit to me a little bit about what you're hearing from clients relative to energy, and then, Alice, maybe you could talk a little bit about what the administration is doing around energy. We read earlier this week around OPEC making some cuts in the impact that's going to have. So, Matt, first, bring the voice of a client in here. What are you hearing? Because it is the leading edge, it's so darn expensive. What are our clients saying about energy?

MATTHEW: Oh, they're saying the same thing that you just said, Roger. I mean, everybody's feeling that the price at the pump that's huge. The other thing that they're concerned about is the chainlike reaction that it's happening—that it's having, on food prices. And so it's—the economy—things are so interconnected to each other. And they're worried about energy inflation eating away at other parts of the economy. But I would love to hear what legislation, Alice, has to tell us about in terms of energy.

ROGER: Yeah. Alice, what are we doing about all of this?

ALICE: Well, I would say, coming into office, President Biden, one of his key priorities was focusing on climate change. And so I'll say that he's been fairly successful in getting a few pieces of legislation passed through Congress over the past 12 months, the first of that being the Infrastructure Investment and Jobs Act and the bipartisan infrastructure bill, which most people think infrastructure there. But it actually includes some significant investment into clean energy innovation, so that's going from R&D to demonstration to actual deployment. And that's going to be really key here for him in terms of achieving a net-zero emissions there.

The other piece of legislation—and I mentioned this earlier—is the CHIPS Act. Even that's focused on semiconductors, some of that $100 billion investment is actually going to go towards building a framework for this cutting-edge R&D technology and accelerating some of that innovation there, so another step forward in energy.

And then, finally, the Inflation Reduction Act, which did pass before the August recess but not on a bipartisan basis. It had a $360 million package there for clean energy. It was a combination of both tax credits and tax investments, but what that's really intended to do is build the infrastructure for all this new energy sources. It's building manufacturing plants, installing new energy assets, and producing the clean energy itself.

But I will say—so we've got all this investment here. A lot of those funds haven't quite been deployed yet, so we're going to probably start to see that go out in 2023. So it's still going to be a little bit of a timeline before we see the results of some of this new investment in technology.

But the one piece I'll say that is still missing is the permitting reforms because if you think about it, we're spending all this money to create this new technology. We come up with new forms of energy. But how do you get that from point A to point B? And right now, there's not the permits available to lay down some transmission lines to take this energy that's created here and distribute it to the rest of the country. So that's going to be something that's going to have to be done legislatively. They've started work on that, but it's more likely going to be next Congress before we see legislation on that front.

ROGER: There's a lot of infrastructure that needs to be retrofitted or created to do it. But it wasn't that long ago, Denise, that an electric car was a novelty and wind was an interesting concept. Solar has been around for a while but has become quite a bit more efficient. Where—and then, recently, we just saw OPEC. I'd love your thoughts on where are there opportunities for our clients in the energy sector now as well as into the future to think about making some investments in that space.

DENISE: Yeah, it's been a very protective space in the market, and certainly, as an equity market investor, it's been leadership over the last year, two-and-a-half years, I should say, it's been leadership. And what I'm seeing right now is actually less opportunities in the space, partly because we have had such a historic run and outperformance in the sector. We're now shifting from an environment where I'm looking at indicators where demand is likely to decline. And in fact, gasoline demand is declining in the US after not really recovering very much off the pandemic lows.

So you're in a situation now where demand is unstable, so that limits the probability that supply cuts, however the headline reads, as actually being very predictive for prices. So I think that that's a setup that has—at best, I think—your risk/reward is neutral to potentially even modestly negative. There's still certainly valuation support in the energy sector from a relative earnings perspective. But what you're seeing now is a massive disconnect between the relative performance of the stocks, which has beat the index by about 40% over the last nine months, with the commodity actually being down. And usually, even with strong valuation support, your risk/reward is not positive in the next year.

ROGER: Then why is that correlation at this particular moment so different between the commodity value and the stock price?

DENISE: Well, I think what we've seen in some ways is the reflection of that valuation. So I think what investors got wrong in, let's call it, the recovery out of the pandemic, was they underestimated the earnings from energy companies by about 10% a month, which is something that I look at in the data going back to 1962. I've never seen such an incorrect assessment of what companies could earn in any recovery, especially at the sector level.

So that valuation support provided really strong odds. And I actually talked about this in all my webinars that the stocks could outperform despite the outlook in the commodity, which ended up being negative. But now what you're seeing is that disconnect being large enough where you could see the flip where the commodity doesn't necessarily have to be weak for the stocks to potentially underperform, as you see, a rotation in the market to things that potentially already discounted a recession.

ROGER: Yeah, it's counterintuitive, but when you explain it, it makes sense. If not energy as an opportunity, where are you seeing some opportunities within the market? Are there any that are sort of glaring and obvious?

DENISE: Yeah, in some ways, for me, the glaring thing I see in the market is the relative valuation of, I'm going to call it, any kind of defensive option. So whether you look at it from a sector perspective, like consumer staples, health care, utilities, the old telecommunication services, whether you think about it from a factor perspective, like low volatility, all of those are very expensive, and by "expensive," I mean in the top decile of their history going back to 1990 or 1962. And that has created a very different risk margin for those defensive sectors, meaning that they might not be nearly as protective as you think they are, given that starting point and relative valuation.

And the opportunities, ironically, Roger, might actually be in the more economically sensitive sectors like consumer discretionary—is one I'm interested in—where you are seeing all of those negative indicators that you're seeing in the economy tend to be forward-looking predictors of outperformance in that sector because it traditionally discounts the recession sometimes, well, before it actually occurs from a trough perspective.

And the second area that I'm interested in is the financial sector, where valuation is very, very strong support, and investors might be interested to know that especially regional banks are orders of magnitude cheaper than they were in the great financial crisis on both relative price-to-book and relative earnings. So there's a strong valuation support, which might give you certainly the historical odds that you have discounted a mild-to-moderate recession.

ROGER: Yeah, in the consumer discretionary as well as in financial services, we'll benefit, I assume, from a postpandemic type of a world as well as the financials from an increasing interest rate. These are tailwinds for some of them. Is that a good read?

DENISE: Higher rates can certainly be a tailwind for the financial sector as long as there's not a credit issue. And right now, for the US consumer that is delevered over the last 10 years and is looking at record-low debt service as a percentage of disposable income, it looks less likely that there's a smoking gun for a credit issue in the United States.

ROGER: Gotcha. All right, Matt, markets don't always go up. We're learning that the hard way here. We certainly had a good run, but now we're seeing a bit of a pullback. We're getting a lot of questions from clients around asset protection and maybe starting to think more about their plan having more of an asset protection. Could you talk a little bit about how clients can help protect some of their assets? You mentioned it before, a balanced portfolio, but what are some of the specific strategies people can do to protect their assets from market risk?

MATTHEW: Yeah, well, protection is probably what drives most of the meetings that I have with clients these days, so it's top of mind for pretty much everyone. And it's markets like this for—that's the reason why we have protection plans in place in a portfolio. But the issue is, now that the markets have dropped so much, I'm hearing a lot about, well, is it too late to protect it? Should I sell some of my stocks that have gone down, for example?

And I would just say to, first, consider a few things. Number one is we don't—we're not going to ask you to protect everything or tell you to because, again, you need that growth. That responsible, disciplined growth strategy is a part of your financial plan, and that's when you get into market timing, which is impossible. So don't protect everything, but think about maybe—obviously, this has been a bad year in the market, but if you've had Fidelity managing your portfolio for the last three, four, or five years in a disciplined, well-balanced, rebalancing type of strategy, then chances are you're up on—and you have solid returns still that you can go in and protect if you would like.

The other thing I would say to consider is your risk tolerance and maybe how that's changed in light of the market volatility that we've had. So if the market is driving your every thought and you are just panicking and worried and stressed, first, call us, but then also maybe come to the realization that maybe you are taking on too much risk. We have the saying in the finance world that there's never a bad time for a good strategy, and protection is a part of a good strategy. So a few examples that I would say in terms of protecting your assets and getting interest would be secure investments like CDs or treasuries or fixed annuities.

ROGER: Matt, I think another thing that people might be a bit of a silver lining with, and I'd love to hear how you're talking about it with our clients is a lot of clients that are getting close to or are in retirement have, historically, for the last couple of years, been lamenting the income that they're able to get with interest rates being close to zero. Now, with a two-year Treasury over 4%, it provides an opportunity for people to rethink income, specifically people in retirement or close to retirement. You talk a little bit about some of the strategies now that are maybe a little bit more attractive in a increasing interest rate environment that people can take advantage of.

MATTHEW: Absolutely, so that's a huge concern for retirees, for people that are about to retire is, hey, I need to live on this income. I need this to provide me income, my assets, to provide me income now. And here, the market is down. So traditionally, there are three ways to take income from a portfolio. So I'll run through those with you, and then, at the end, I'll—we'll share some of the ways that you can protect it.

But the first way is through having a diversified portfolio and then taking income from it by actually selling down some of those assets. So each month, for example, you could go in, sell down some of your assets across the board, capture that income that you need.

The second way is through a dividends and interest strategy, and this is where you live on the interest from bonds or the dividends that you receive from stocks. And that, Roger, is what you're talking about where there is some new-ish opportunity there where you've got this two-year Treasury over 4%. Finally, it's been—we haven't seen it this high since 2007, really. So you can construct a bond portfolio now that's actually not only giving you income over 4% but is secure.

On the dividend stock side of it, dividends are good for two primary reasons when it comes to income. Number one is you get the income from the dividend. Number two is, historically, dividend stocks tend to have less volatility than the overall stock market, or non-dividend payers, at least.

And then the third way to take income is through guaranteed income sources. So that comes in three different ways—Social Security, pensions, and fixed-income annuities. So if you want to protect some income, if you need more income to supplement your Social Security or a pension, then you can look into a fixed-income annuity. And that is another beneficiary of these higher rates because the cash flow on these fixed-income annuities are now higher than they were this time last year, for example.

ROGER: Yeah, it's very well said, and you mentioned a plan to our clients out there to take advantage of Matt and his peers. Your financial plan should be a living document, should be a document that you revisit and that you talk about, that is something that you don't set it and forget it, put it in a drawer somewhere, and assume that it's going to be good. Having an ongoing dialogue and discussion to review your portfolio and your plan a couple of times a year is a very good idea. As you can see through all of the conversations that we're talking about, there's a lot of things in flux and staying connected, but having a good planning and having a good advisor or financial consultant is a super critical part of that.

ALICE: Yeah, Roger, so here in Washington, there's this adage that personnel is policy, so I think, with the midterm elections coming up in a little bit over a month, it's really important for everyone to go out and vote because some people say, well, my one vote's not really going to count, but we've seen countless elections where the candidate won by just a mere few votes, so absolutely, your vote will count.

ROGER: Yes, thank you. Get the vote out. Matt, last thought to you.

MATTHEW: I would just like to say thank you, everyone, for being a part of this and listening, and thanks to you, Roger, Alice, and Denise. It's been wonderful being here. But we've talked about so many challenges and concerns that our clients have, and the fact is, when inflation goes down eventually, when interest rates stop going up, there's going to be more challenges and more worries, and that's why the market doesn't just go up in a straight line.

So the word that comes to my mind is "myopic." The volatility can often lead us to have this kind of myopic vision or short-sightedness where the short-term impact of what's happening can get in the way of our long-term disciplined plan. And so if we shift our thinking and expand our perspective, focusing on that long-term disciplined plan, we'll be happy that we did many years down the road.

ROGER: Yeah, reminds me my father used to tell me a dollar bill doesn't come with instructions, Matt, so you—it's good to have a plan, my friend. So I do want to thank the panelists. Matt, Alice, and Denise, thank you very much for sharing your time and your wisdom. Maybe most importantly, I'd like to thank our clients and our viewers for taking the time. Hopefully, this was helpful.

We at Fidelity are very aware that these are very challenging times. We've got interest rates. We've got market volatility. We've got unprecedented catastrophic impacts of hurricanes down in Florida as well as in the Carolinas. And we're aware of all of that and sensitive and supportive of all of that. We want to make sure that everybody knows that we are doing everything we can to be as helpful as we possibly can, not only with the national disasters but also as providing this information and context.

So please use it as an opportunity to continue to sort of tap into Fidelity. We have a program called Fidelity Insights through the Fidelity Wealth Management program that you can sign up for to get more information, access to these types of webinars. Please take the time to do that. Hopefully, you found it helpful, and I certainly did. And again, I want to thank all of you for joining as well as our panelists for sharing their content and perspectives. I just wanted to wrap it up by saying I'm Roger Hobby. Thank you for being here, and we hope to see you again soon. Take care.

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