Business cycle update: U.S. and global economies in advanced stages of the cycle

United States

- The U.S. is in the late-cycle phase, characterized by tight labor markets, less accommodative monetary policy, and a flattening yield curve.
- Recession risk remains low, and the U.S. consumer backdrop is strong amid a low unemployment rate, accelerating wage growth, and manageable financial obligations.
- Corporate earnings growth in 2019 is expected to decelerate as businesses face margin pressures from higher wages, global demand remains tepid, and the boost from 2018 tax changes fades.
- The policy backdrop is highly uncertain, with the direction of monetary and trade policies unclear.

Global

- Global growth remains positive but has become more uneven, and many major economies have progressed toward more advanced stages of the business cycle.
- Global manufacturing remains in expansion, but the outlook has deteriorated and activity levels have likely passed their peak.
- China is in a growth recession, and policy easing measures so far appear insufficient to sustain a reacceleration.
- China's slowdown, in addition to global monetary tightening and trade-policy uncertainty, has weighed on the industrial sectors in Europe and other export-oriented economies.

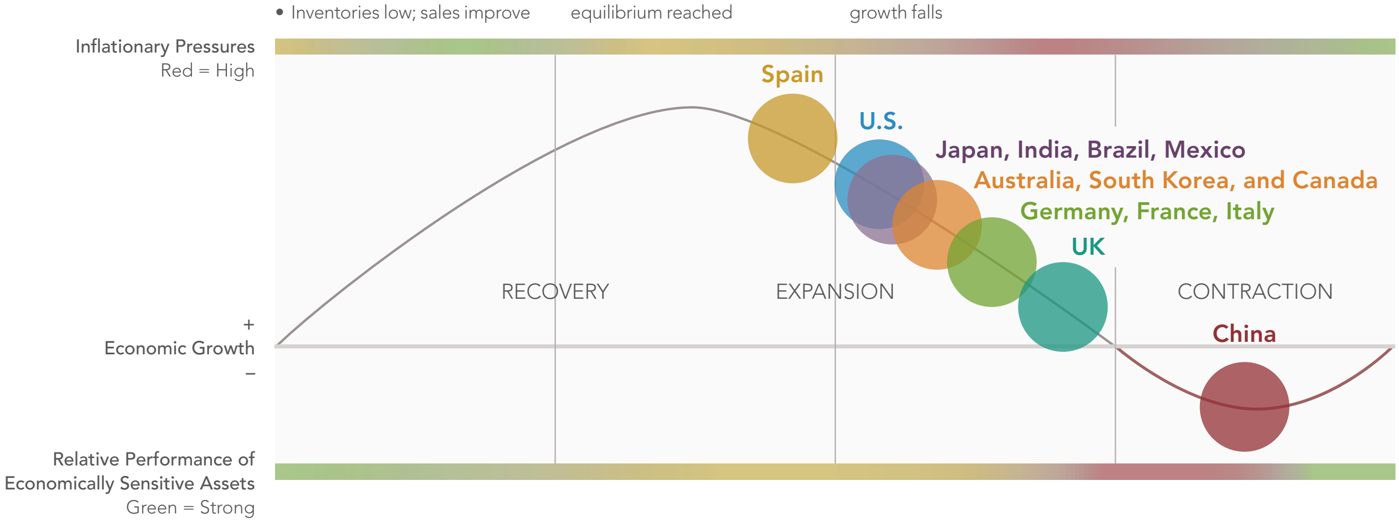
Asset allocation outlook

- Consistent with a maturing business cycle, asset class patterns may become less reliable, warranting smaller cyclical tilts and a prioritization on portfolio diversification.
- Meanwhile, low recession risk implies it's too early to have high conviction in extremely bearish scenarios.
- After an unprecedented period of global monetary easing, the shift toward global monetary tightening has turned into a liquidity headwind that may cause asset-market volatility to remain elevated.
- Overall, we expect the late-cycle environment to provide a less favorable risk-return profile for asset markets than during recent years.

Business Cycle Framework

The business cycle, which is the pattern of cyclical fluctuations in an economy over a few years, can influence asset returns over an intermediate-term horizon. Cyclical allocation tilts are only one investment tool, and any adjustments should be considered within the context of long-term portfolio construction principles and strategic asset allocation positioning.

Cycle Phases	EARLY	MID	LATE	RECESSION
	• Activity rebounds (GDP, IP, employment, incomes) • Credit begins to grow • Profits grow rapidly • Policy still stimulative • Inventories low; sales improve	• Growth peaking • Credit growth strong • Profit growth peaks • Policy neutral • Inventories, sales grow; equilibrium reached	• Growth moderating • Credit tightens • Earnings under pressure • Policy contractionary • Inventories grow; sales growth falls	• Falling activity • Credit dries up • Profits decline • Policy eases • Inventories, sales fall



Note: The diagram above is a hypothetical illustration of the business cycle. There is not always a chronological, linear progression among the phases of the business cycle, and there have been cycles when the economy has skipped a phase or retraced an earlier one. Source: Fidelity Investments (AART), as of Jan. 31, 2019.

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