

# How the maturing economic cycle could impact your portfolio

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# Overview

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# Summary Several cycles suggest slower pace of gains, more defensive leadership

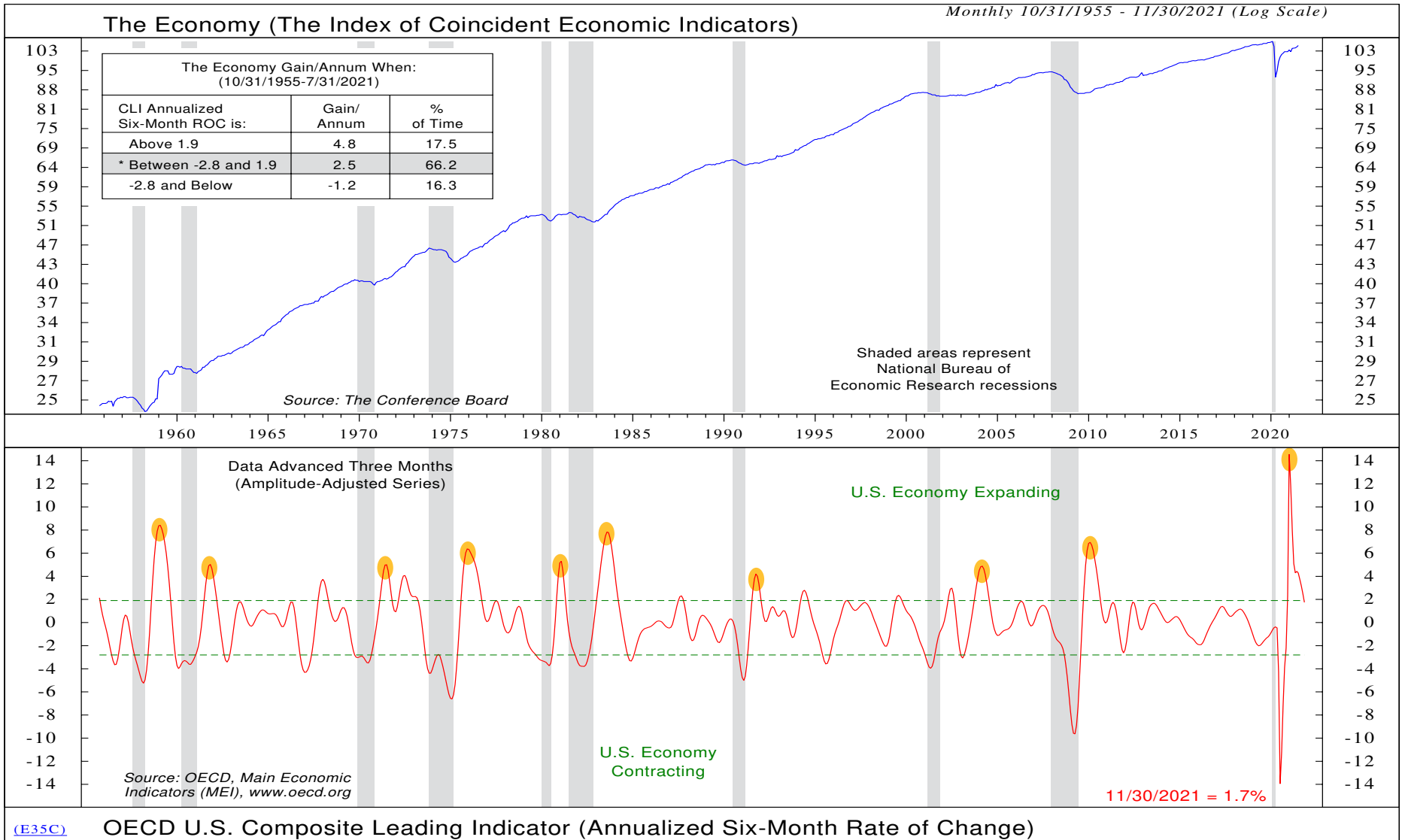
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## Key Cycle Summary (October 2021)

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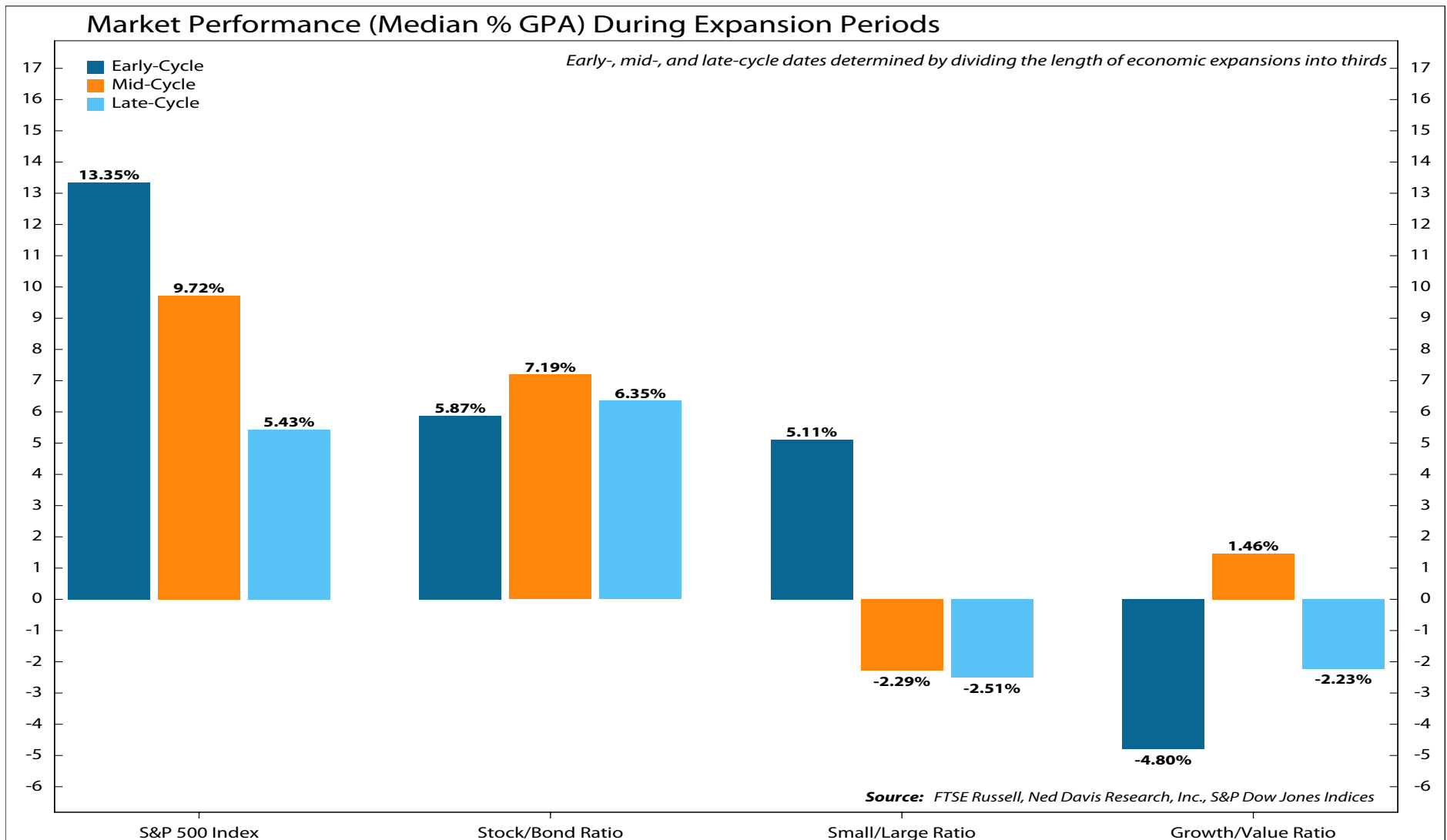
Cycle	Description	Market Implication
Economy	Growth slows from early cycle to mid-cycle	Stock market gains smaller Defensive, large-cap, and (somewhat) Growth
Echo bear	Common as economic & EPS growth slows	Shorter and shallower than recession bears Defensive sector & style leadership
Taper	Likely start in late-2020/early-2021	Broad market strength, stocks > bonds Brief cyclical strength, then stable Growth
COVID-19	Disjointed reopening	Another reopening trade?
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# Economy U.S. economy is 1/3 through the average post-war expansion.



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# Economy Stock gains slow and small to large as economy matures.

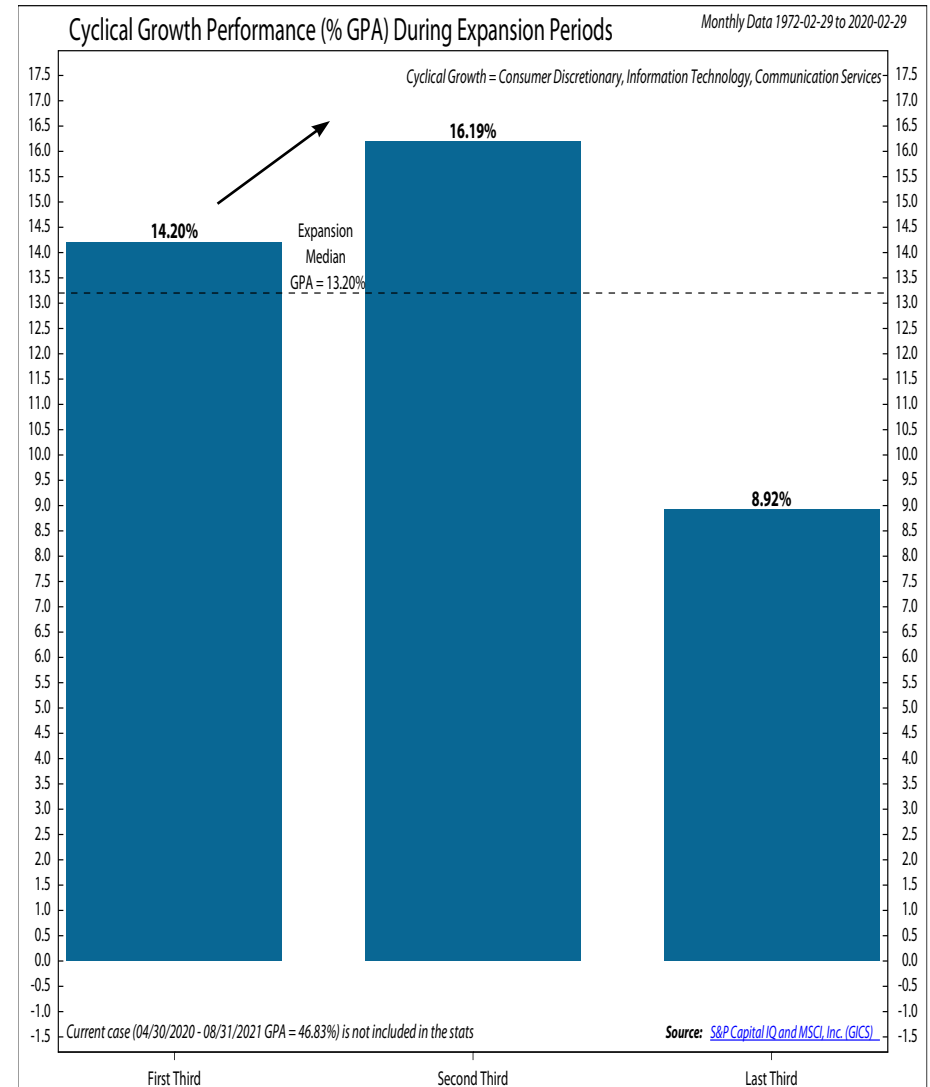
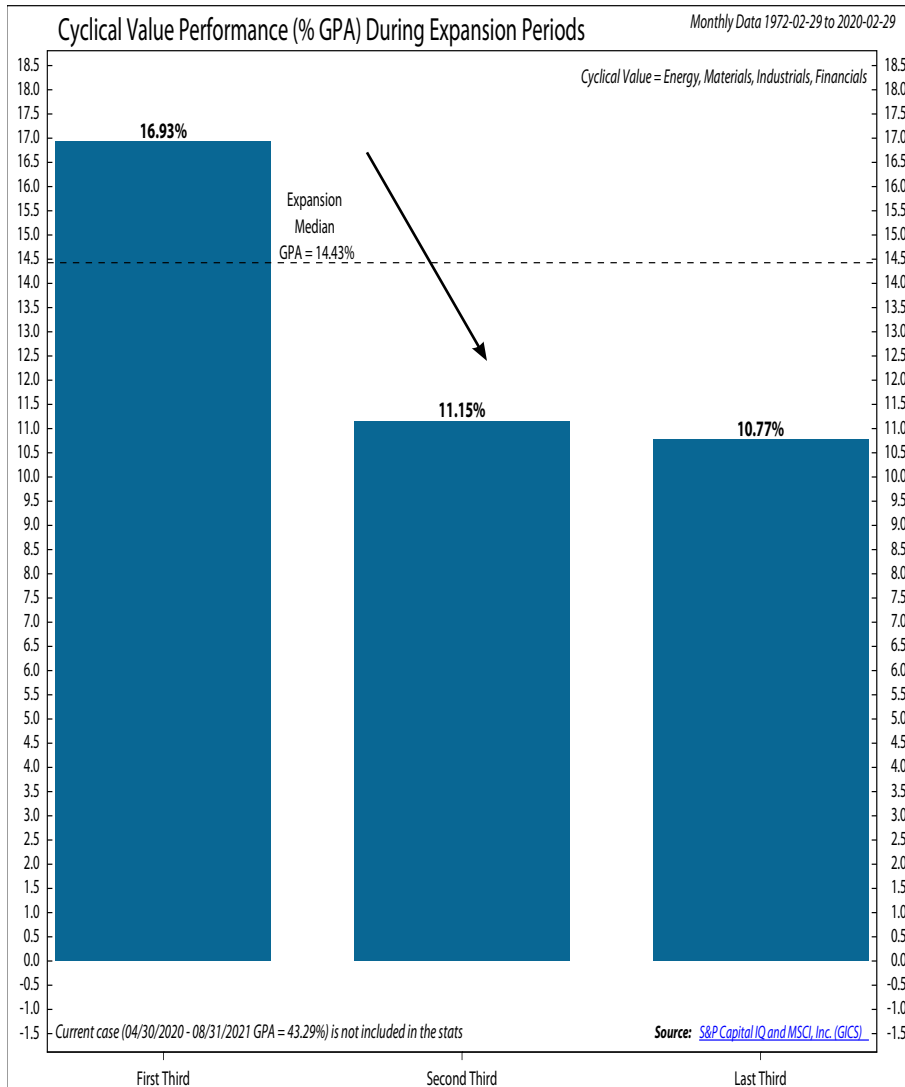


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# Economy Cyclical Value weakens, Growth strengthens mid-cycle.



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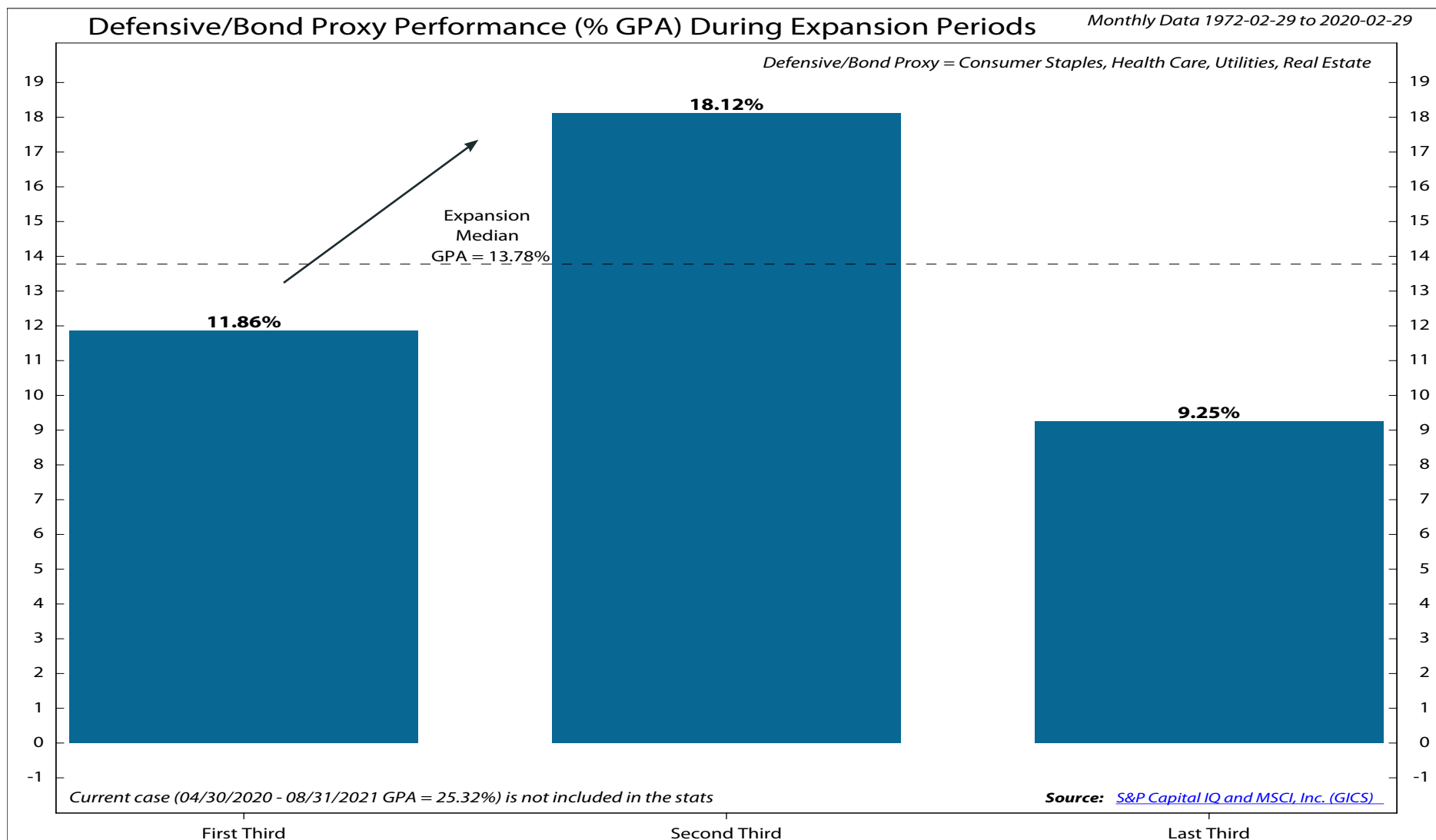
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# Economy Defensive sectors have highest GPA mid-cycle.



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# Economy Health Care and Staples strongest mid-cycle.

## Sector Performance during Expansion Periods

S&P 500 Sectors	Median Return (% GPA)		
	Early-Cycle	Mid-Cycle	Late-Cycle
Health Care	5.9	21.4	8.9
Consumer Staples	8.0	20.9	3.6
Communication Services	16.0	19.8	11.9
Consumer Discretionary	14.6	14.6	4.9
Real Estate	31.7	13.5	5.4
Utilities	13.1	13.4	17.1
Industrials	17.5	12.8	10.2
Materials	15.0	12.7	8.0
Financials	12.8	11.8	11.1
Energy	12.6	8.3	17.0
Information Technology	12.6	6.7	10.0
<b>S&amp;P 500 Index</b>	<b>13.4</b>	<b>9.7</b>	<b>8.5</b>
<b>Median Cyclical Value</b>	<b>13.9</b>	<b>12.2</b>	<b>10.7</b>
<b>Median Cyclical Growth</b>	<b>14.6</b>	<b>14.6</b>	<b>10.0</b>
<b>Median Defensive</b>	<b>10.6</b>	<b>17.2</b>	<b>7.2</b>

All expansions since 3/31/1975 included. Early, mid, and late determined by dividing each expansion into thirds. Source: S&P Dow Jones Indices.

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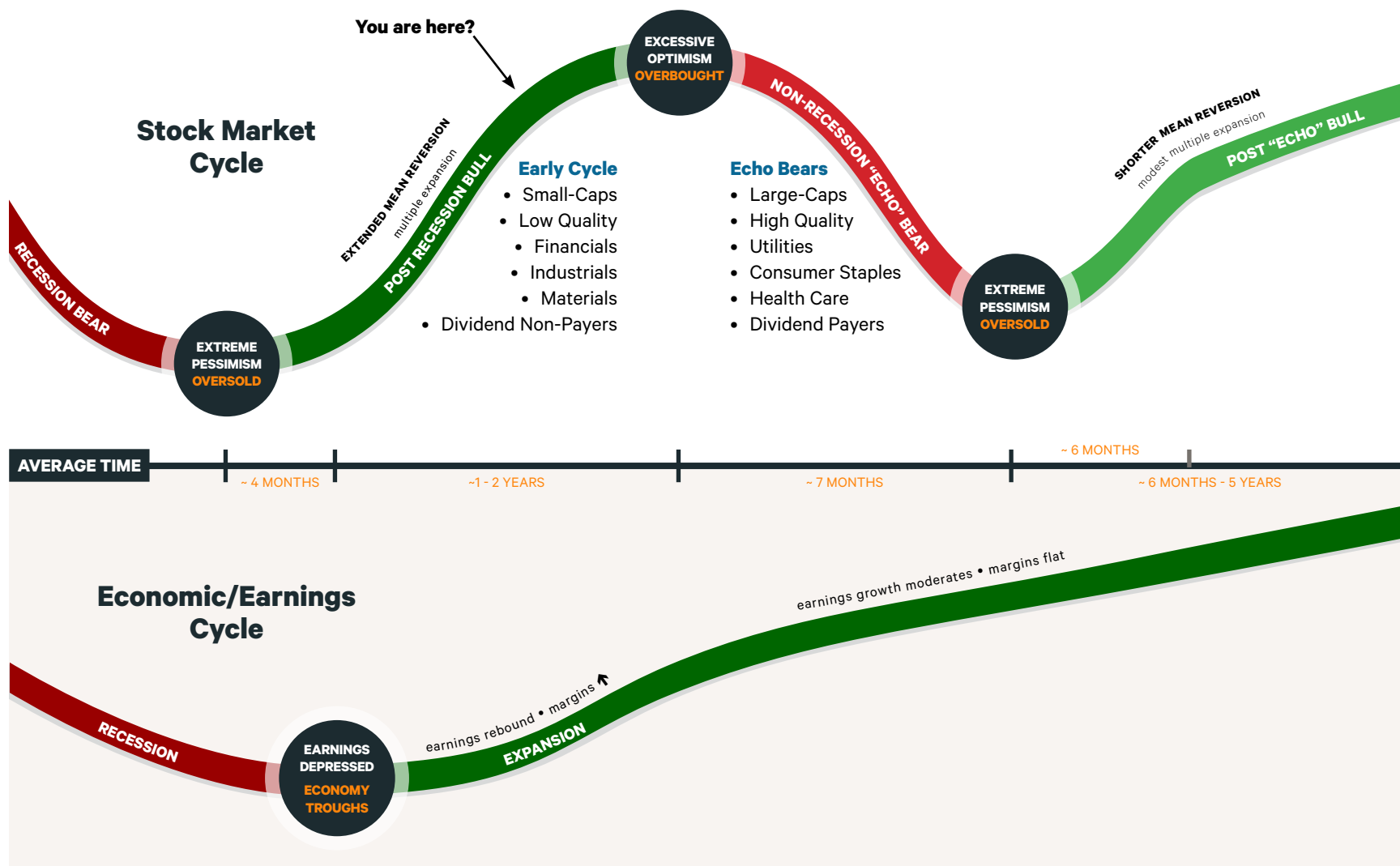
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# Echo bear

We are in the part of the cycle when big corrections/shallow bears are possible.

## Stock Market and Economic Cycles



# Echo bear Leadership defensive in echo bears.

## Market Performance during Post-Recession Bulls and Echo Bears since 1973

Market	Returns since 3/23/2020	Median Gain (%)	
		Post -Recession Bull	Echo Bear
S&P 500 Index	95.0	64.9	-19.3
Stock/Bond Ratio	90.9	81.9	-21.8
Small/Large Ratio	9.9	12.3	-7.3
Growth/Value Ratio	9.8	-0.4	1.3
Low Quality/High Quality Ratio	2.6	15.0	-11.1
Non-Payers/Payers Ratio	10.4	8.7	-6.7

Source: FTSE Russell, Ned Davis Research, Inc., S&P Dow Jones Indices. Dates of bull and bears listed in report T\_203. Current returns updated through 10/6/2021.

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# Echo bear Defensive sectors outperform during echo bears.

## Sector Performance during Post-Recession Bulls and Echo Bears since 1973

S&P 500 Sectors	Returns since 3/23/2020	Median Gain (%)	
		Post -Recession Bull	Echo Bear
Utilities	46.4	39.1	-2.5
Consumer Staples	44.6	52.4	-11.9
Communication Services	97.8	52.6	-14.2
Health Care	68.7	45.0	-16.4
Information Technology	114.2	85.7	-18.7
Consumer Discretionary	101.2	92.3	-20.3
Industrials	105.6	78.9	-21.3
Energy	128.5	59.0	-26.3
Financials	118.7	66.1	-28.6
Materials	109.2	77.4	-29.4
<b>S&amp;P 500 Index</b>	<b>95.0</b>	<b>64.9</b>	<b>-19.3</b>
<b>Median Cyclical Value</b>	<b>114.0</b>	<b>62.6</b>	<b>-23.8</b>
<b>Median Cyclical Growth</b>	<b>101.2</b>	<b>77.4</b>	<b>-20.3</b>
<b>Median Defensive</b>	<b>46.4</b>	<b>52.4</b>	<b>-11.9</b>

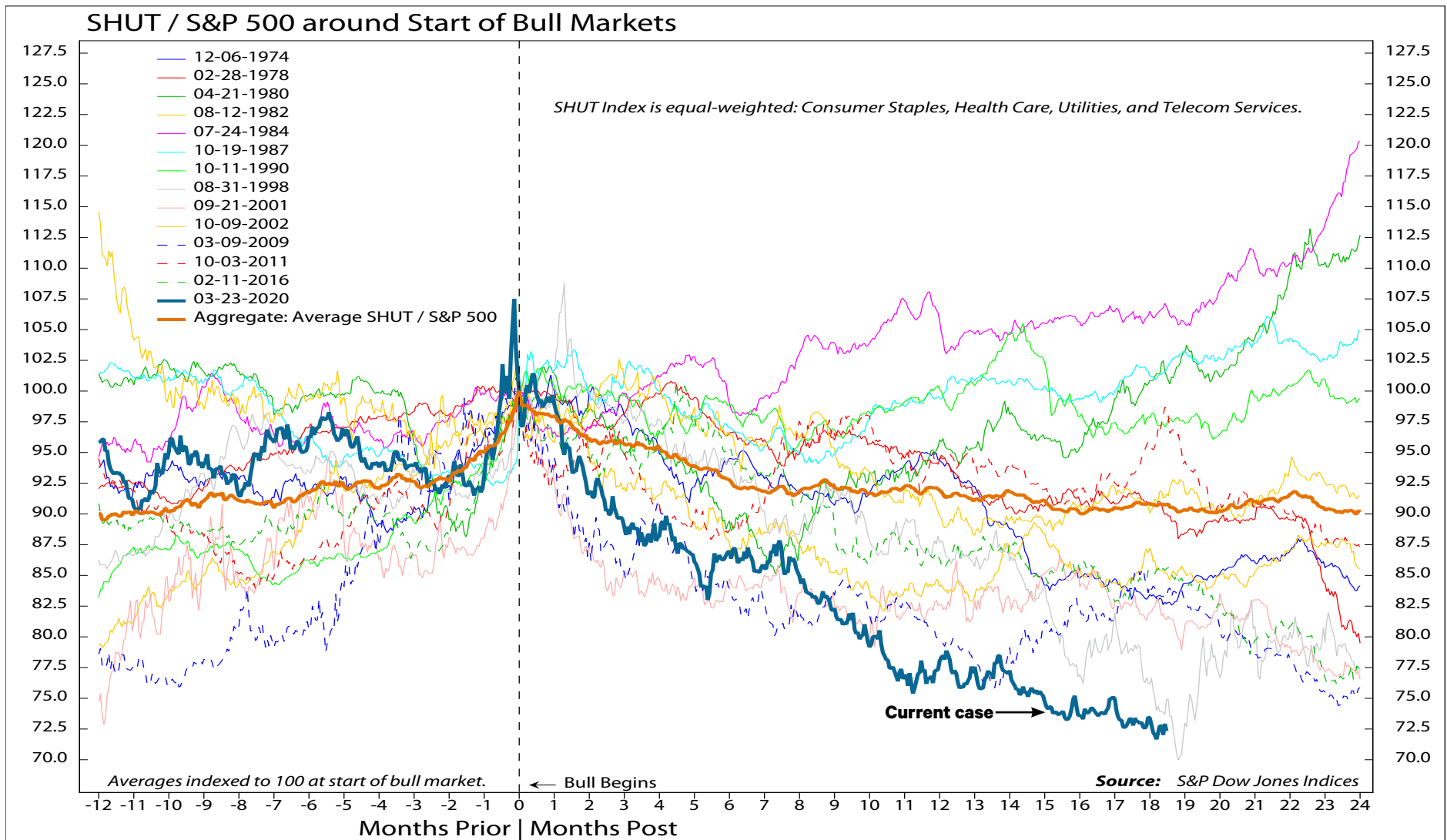
Real Estate excluded due to lack of history. Dates of bull and bears listed in report T\_203. Current returns updated through 10/6/2021.

Source: S&P Dow Jones Indices.

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# Echo bear Record defensive underperformance this cycle.

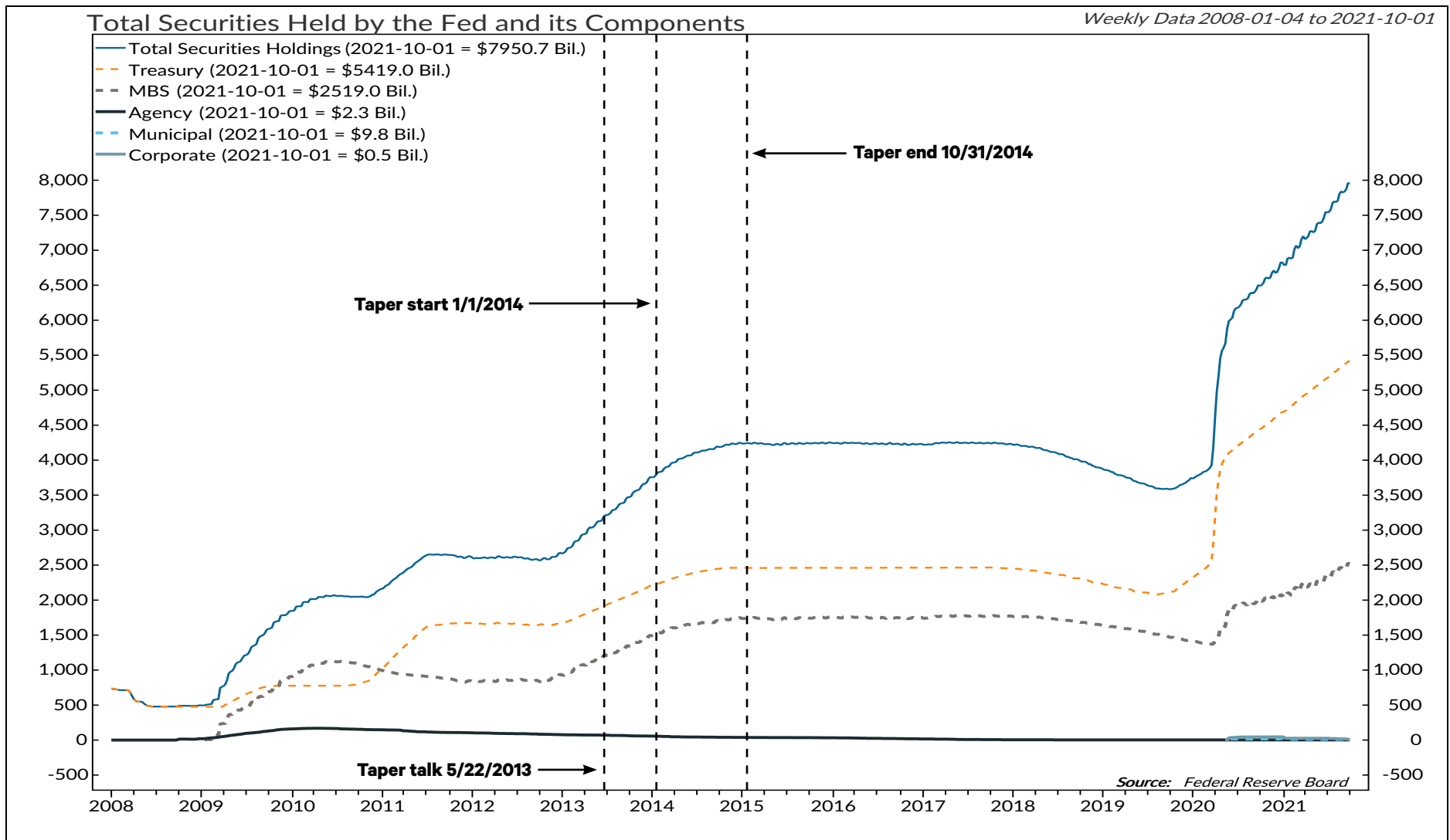


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# Taper The Fed is preparing the markets for tapering.



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# Taper Leadership more defensive as 2014 taper progressed.

## Market Performance Around 2013-2014 Taper Talk and Taper

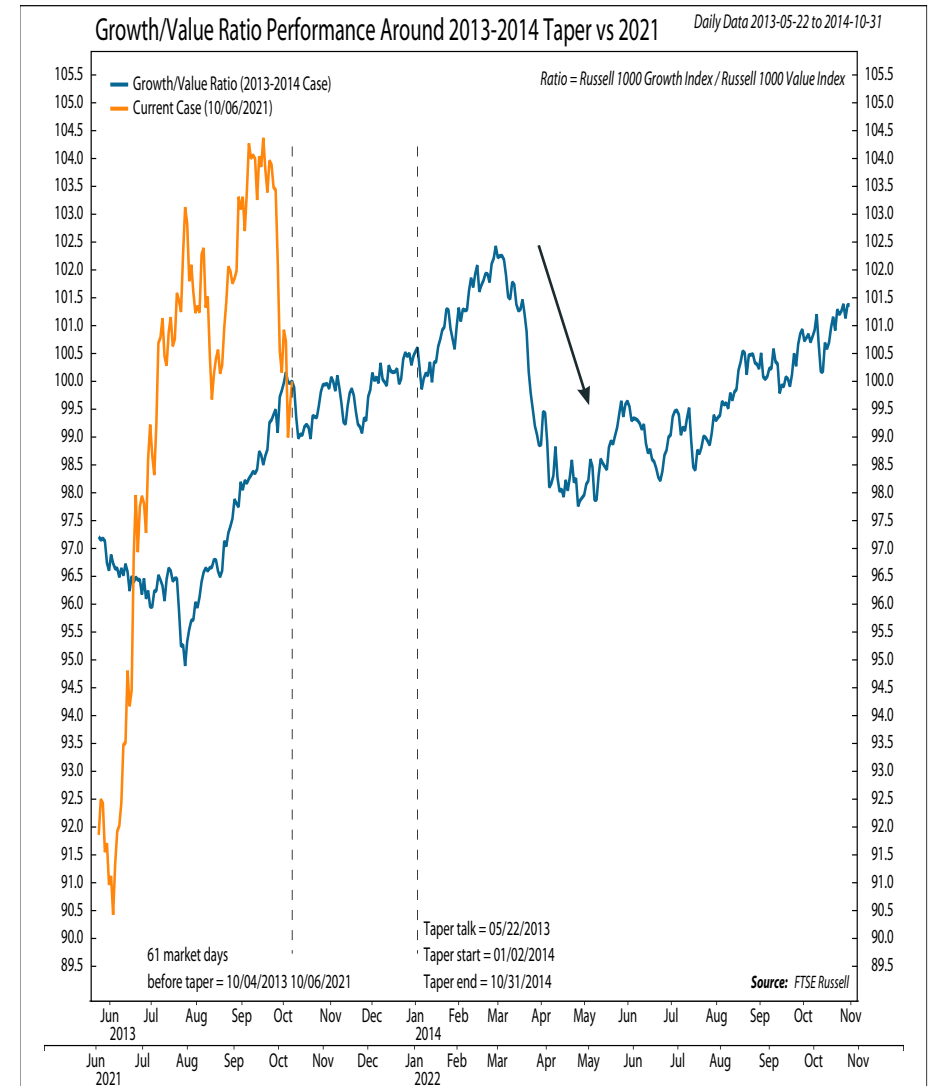
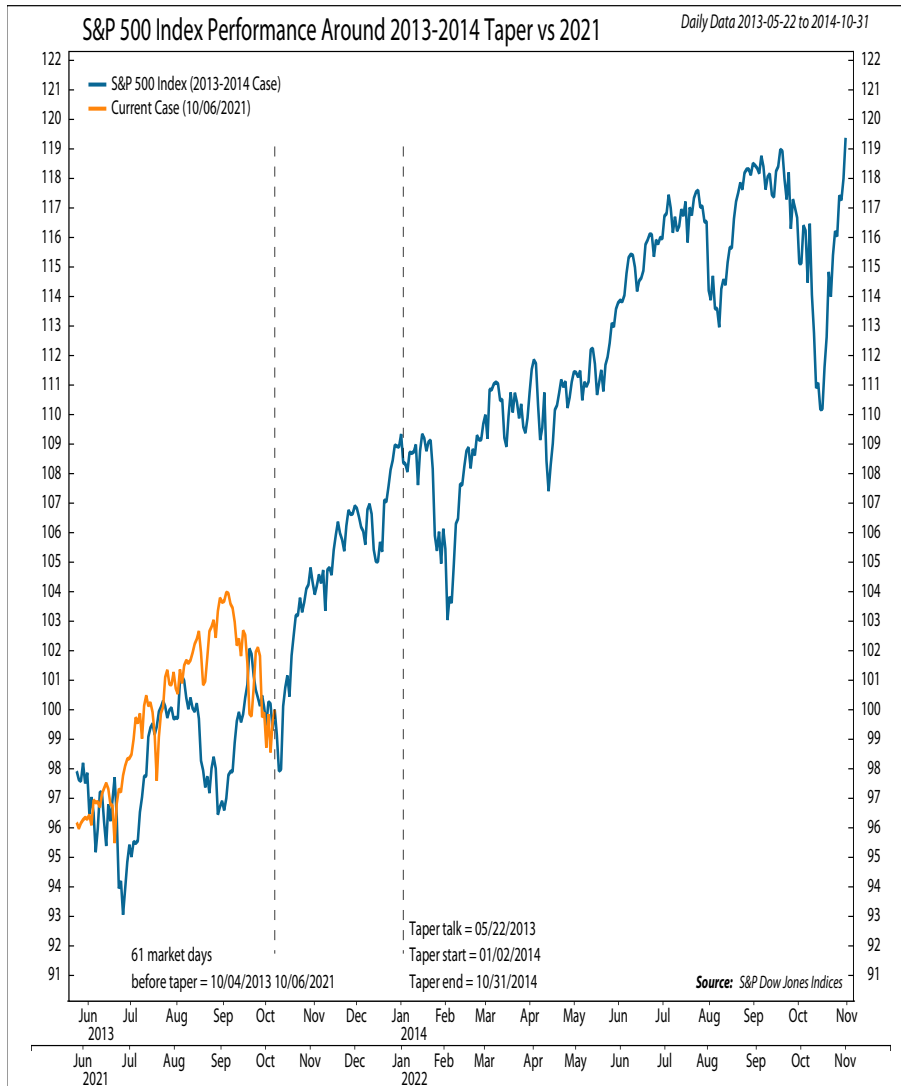
Index	Taper Talk to Taper Start 5/22/13 - 1/02/14		Taper Start to Taper End 1/02/14 - 10/31/14	
	% Change	% Max Correction	% Change	% Max Correction
S&P 500 Index	10.7	-5.2	10.2	-7.4
Stock/Bond Ratio	14.0	-4.4	6.6	-9.4
Small/Large Ratio	5.3	-3.5	-7.2	-13.5
Growth/Value Ratio	3.5	-2.4	0.8	-4.6
Low Quality/High Quality Ratio	0.8	-2.5	-1.3	-6.2
Non-Payers/Payers Ratio	2.6	-3.4	4.9	-7.2

Sources: S&P Dow Jones Indices, Bloomberg Barclays Indices, FTSE Russell, Refinitiv.

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# Taper S&P 500 rally continued, but Value staged counter trend rally.



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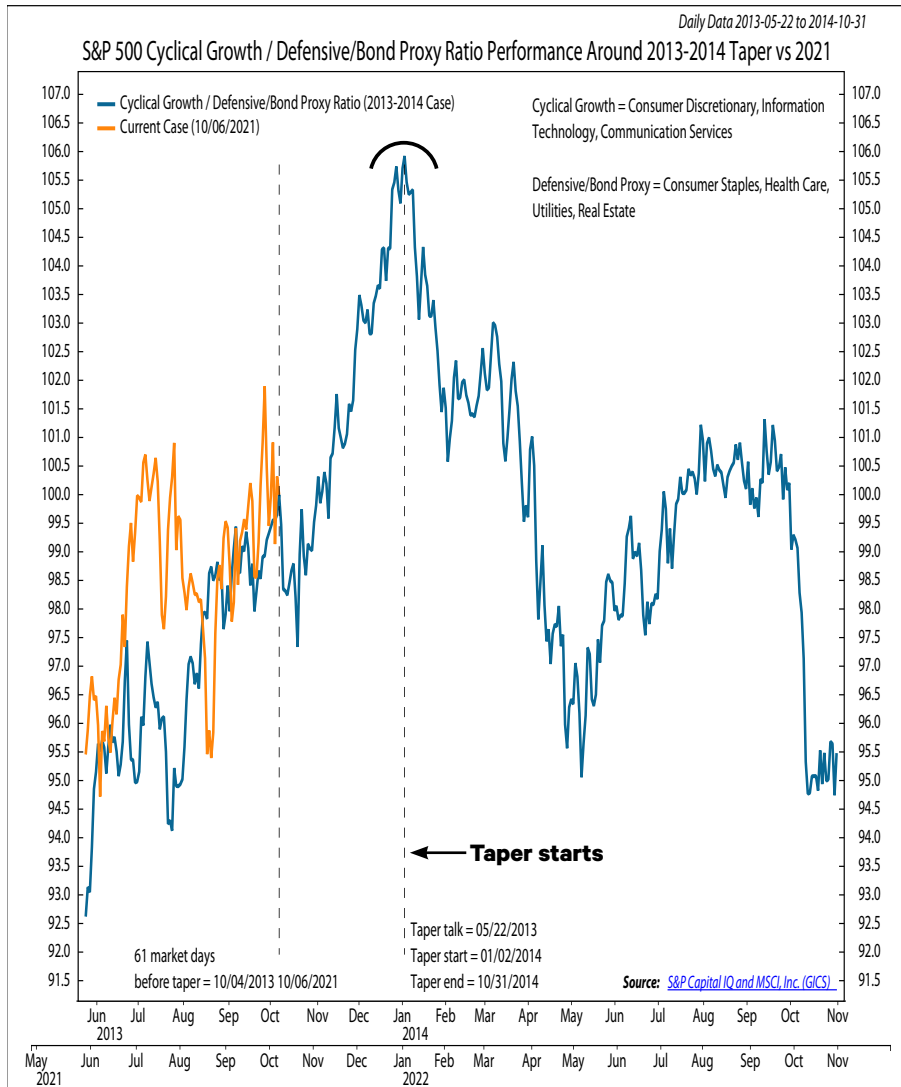
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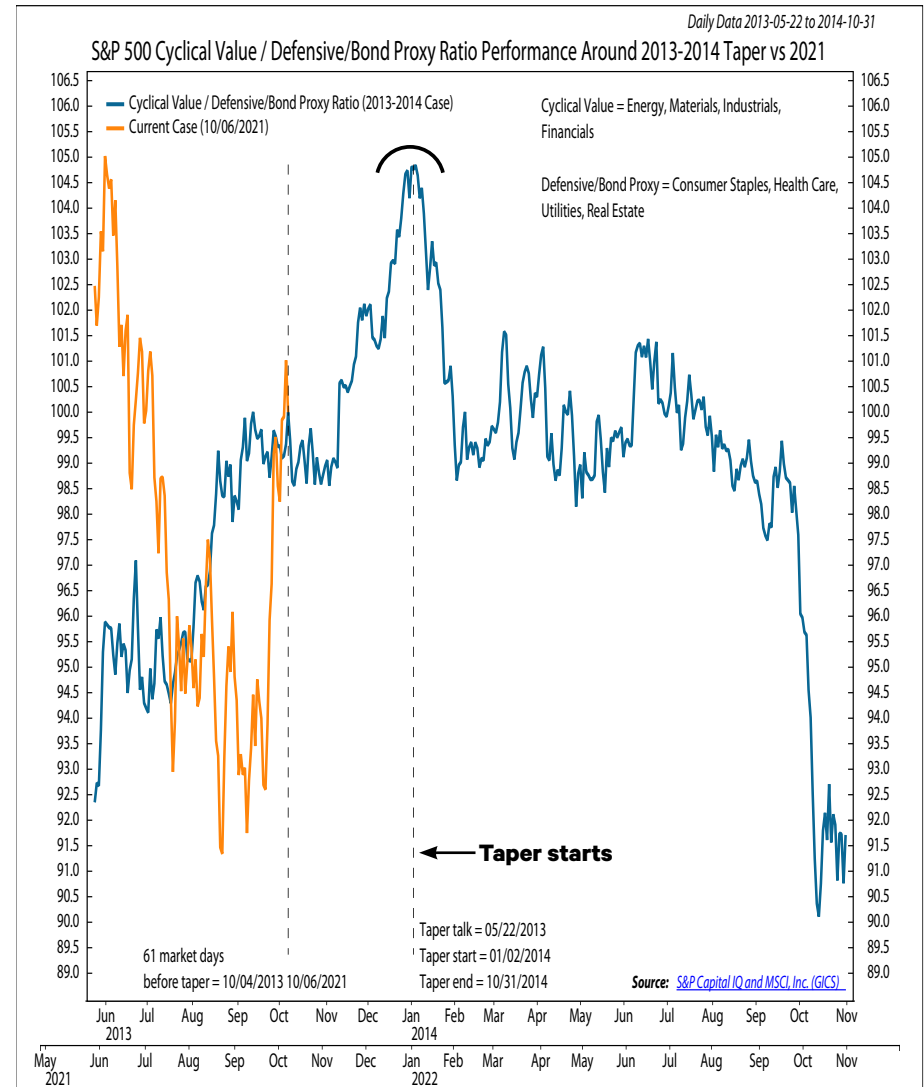
# Taper 2014 taper saw a quick transition to defensive sectors.



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# Taper Real Estate, Health Care, and Utilities best during 2014 taper.

## Sector Performance Around 2013-2014 Taper

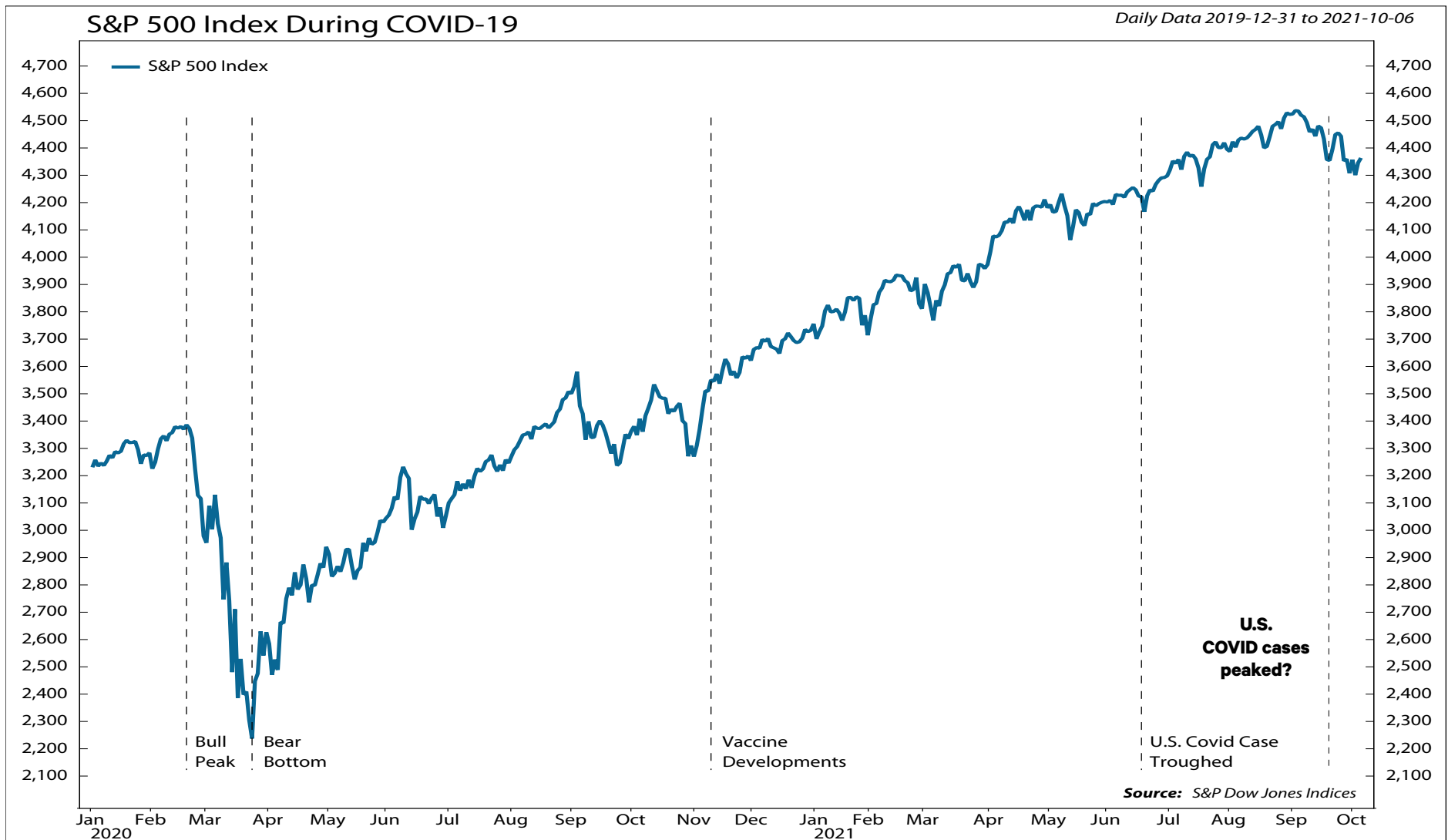
S&P 500 Sectors	Taper Talk to Taper Start 5/22/13 - 1/02/14		Taper Start to Taper End 1/02/14 - 10/31/14	
	% Change	% Max Correction	% Change	% Max Correction
Real Estate	-12.9	-16.4	22.2	-7.0
Health Care	12.1	-5.2	21.9	-7.8
Utilities	-4.8	-8.2	21.4	-9.4
Information Technology	13.3	-6.1	16.8	-8.5
Consumer Staples	2.5	-6.4	9.8	-6.4
Communication Services	13.9	-5.8	8.0	-9.0
Financials	14.0	-7.0	7.5	-8.8
Industrials	17.6	-5.3	6.3	-10.6
Materials	13.3	-6.2	5.1	-11.1
Consumer Discretionary	14.5	-5.4	-0.3	-8.9
Energy	6.7	-6.2	-0.3	-20.1
<b>S&amp;P 500 Index</b>	<b>10.7</b>	<b>-5.2</b>	<b>10.2</b>	<b>-7.4</b>
<b>Median Cyclical Value</b>	<b>13.6</b>	<b>-6.2</b>	<b>5.7</b>	<b>-10.9</b>
<b>Median Cyclical Growth</b>	<b>13.9</b>	<b>-5.8</b>	<b>8.0</b>	<b>-8.9</b>
<b>Median Defensive/Bond Proxy</b>	<b>-1.1</b>	<b>-7.3</b>	<b>21.7</b>	<b>-7.4</b>

Sources: S&P Dow Jones Indices, S&P Capital IQ and MSCI, Inc. (GICS).

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# COVID-19 After waterfall decline, S&P 500 has shrugged off COVID news.

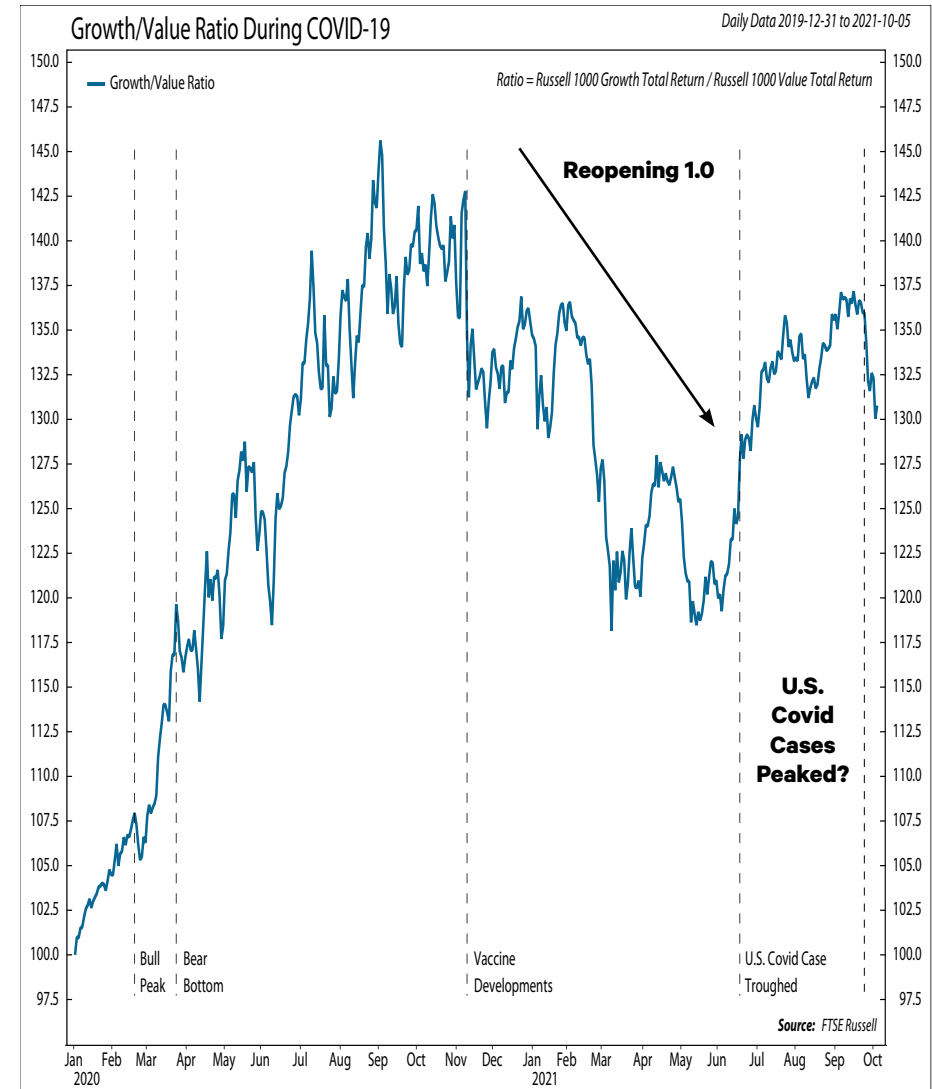
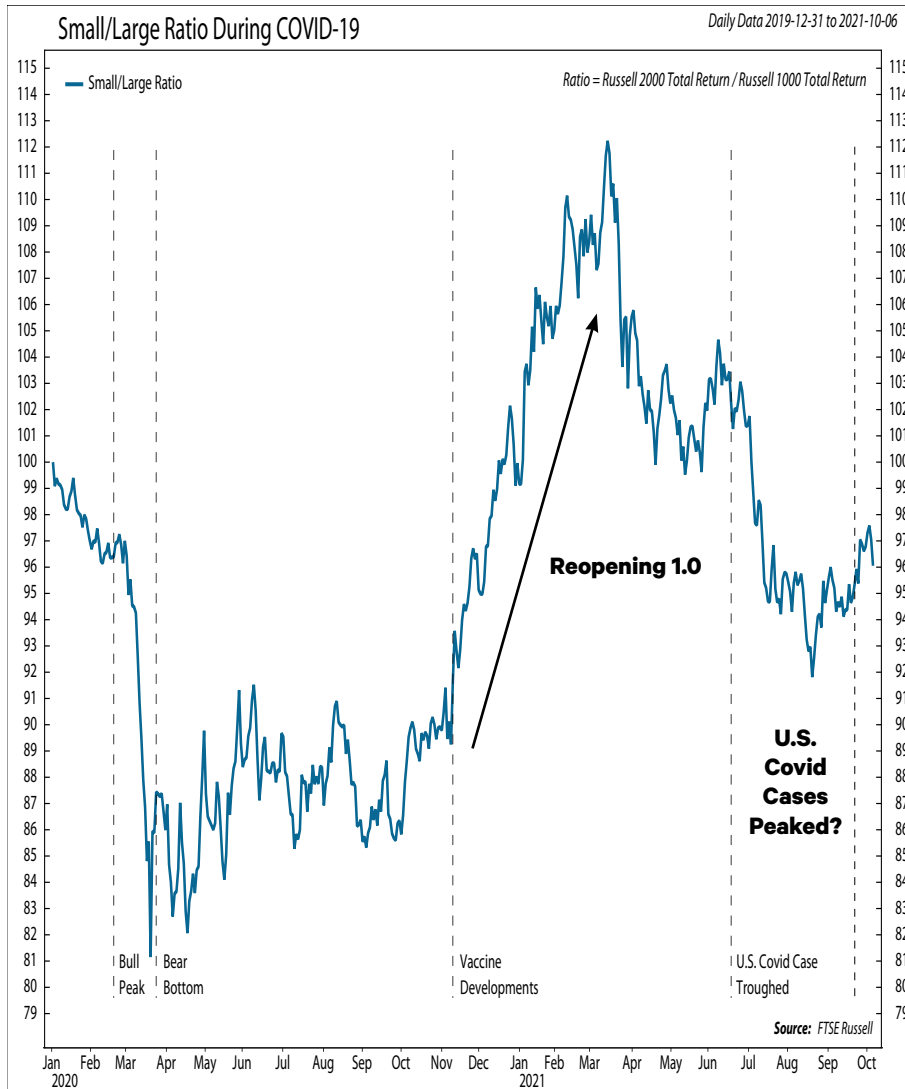


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# COVID-19 Equity leadership shifts around COVID events.



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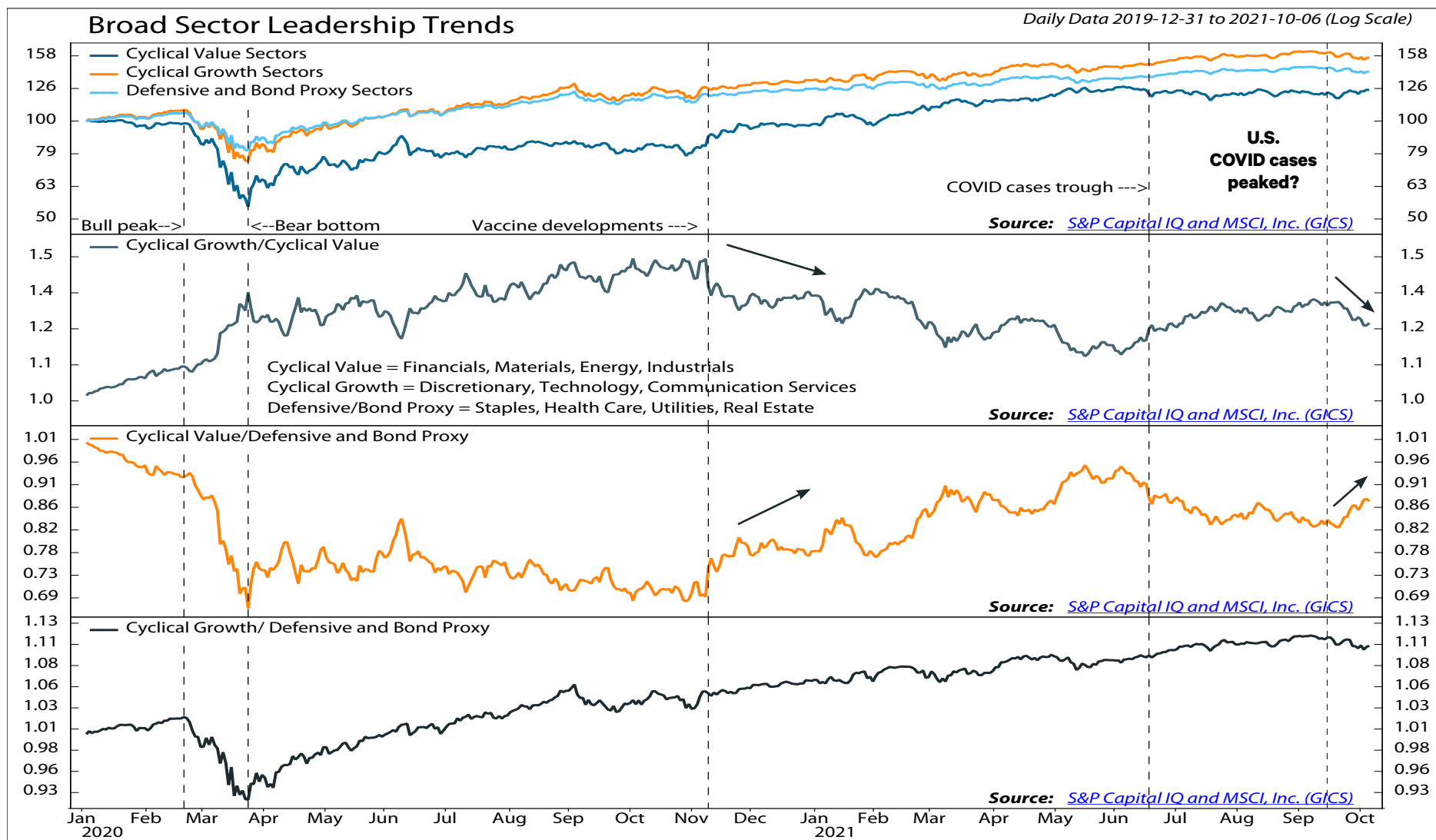
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# COVID-19 Sector leadership is similar to post-vaccine phase.



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## COVID-19 Cyclical Growth sectors leading since case trough.

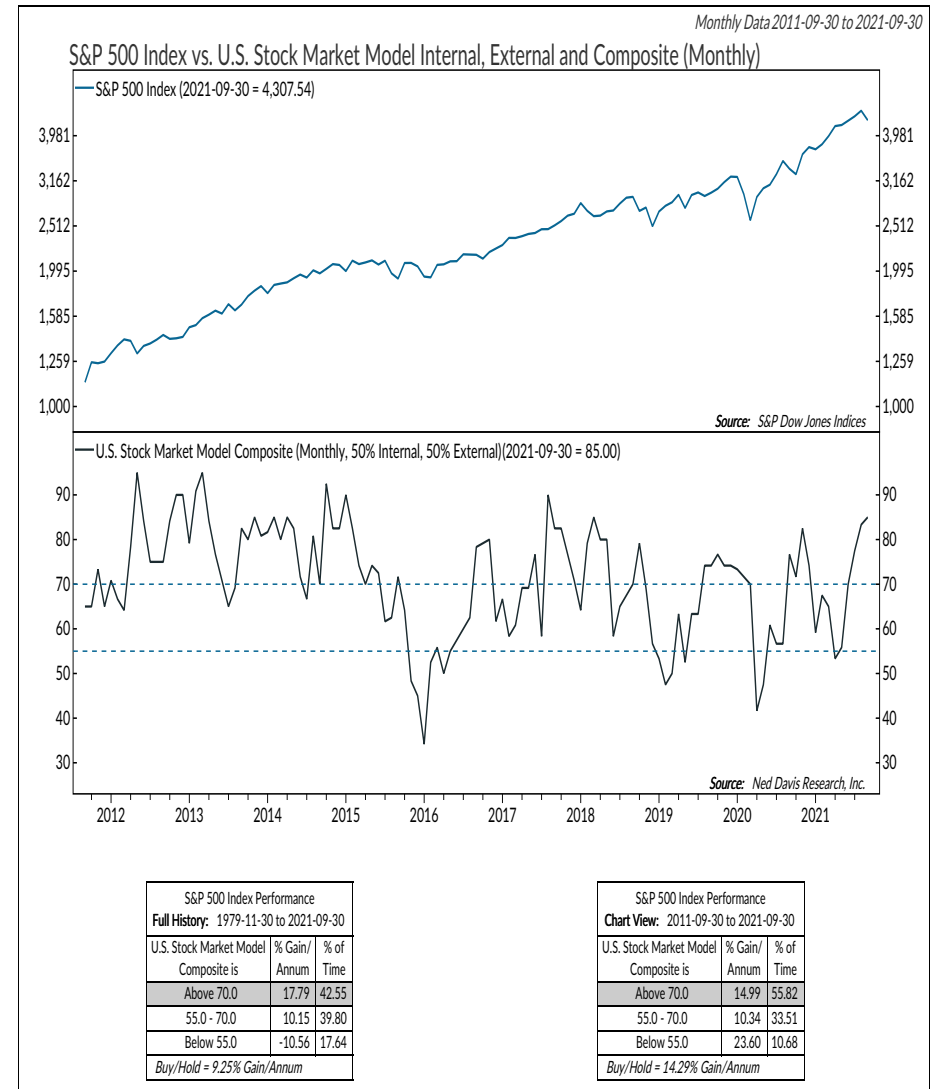
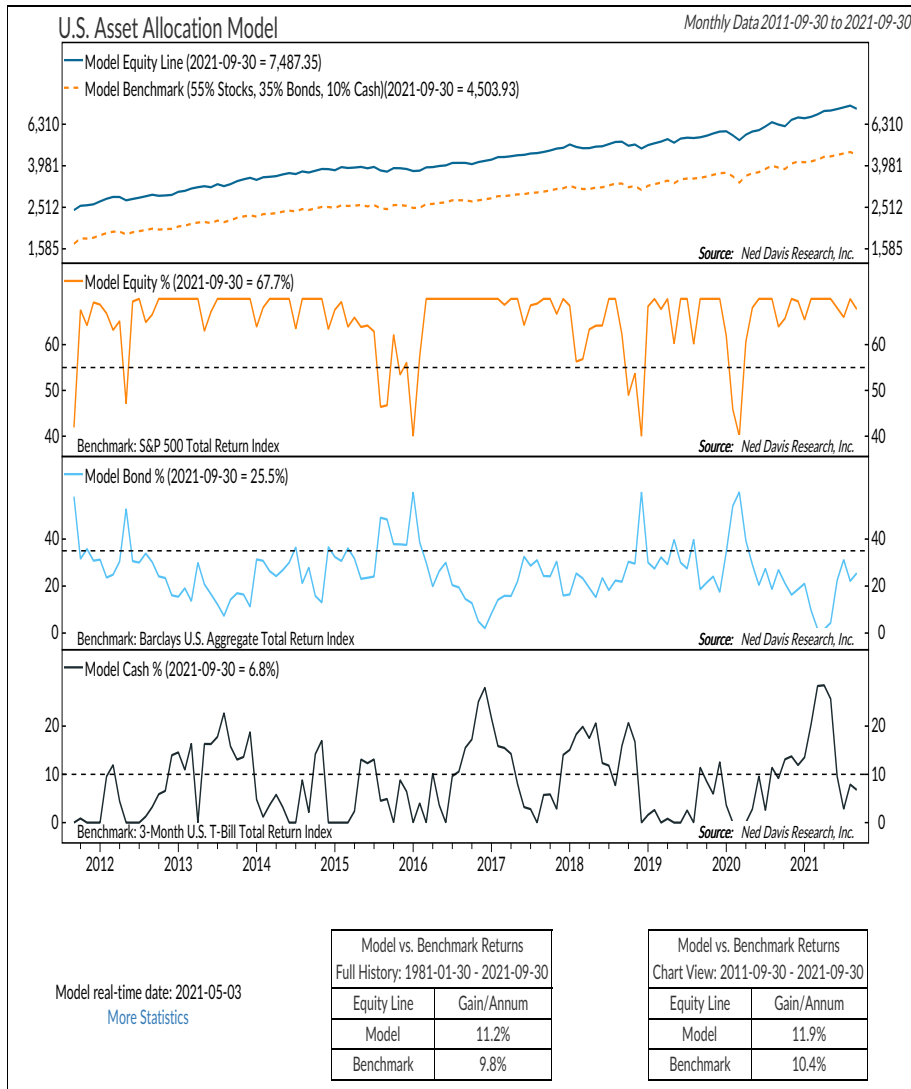
<b>Sector Returns (%) during COVID Phases</b>				
<b>Sector</b>	<b>Bull Peak to Bear Trough</b>	<b>Bear Trough to Vaccine Developments</b>	<b>Vaccine Developments to Case Count Trough</b>	<b>Case Count Trough to Current</b>
Real Estate	-38.0	42.8	23.8	0.5
Health Care	-28.1	48.3	12.7	1.0
Utilities	-35.9	45.6	0.1	0.4
Information Technology	-31.2	71.2	18.5	5.5
Consumer Staples	-24.3	32.9	7.8	0.9
Communication Services	-28.6	53.1	23.8	4.4
Financials	-43.0	52.6	33.6	7.3
Industrials	-41.8	72.3	19.8	-0.4
Materials	-36.4	80.7	17.6	-1.6
Consumer Discretionary	-31.9	73.5	12.6	3.0
Energy	-56.0	37.9	61.7	2.3
<b>S&amp;P 500 Index</b>	<b>-33.9</b>	<b>58.7</b>	<b>18.9</b>	<b>3.4</b>
<b>Median Cyclical Value</b>	<b>-42.4</b>	<b>62.5</b>	<b>26.7</b>	<b>1.0</b>
<b>Median Cyclical Growth</b>	<b>-31.2</b>	<b>71.2</b>	<b>18.5</b>	<b>4.4</b>
<b>Median Defensive/Bond Proxy</b>	<b>-32.0</b>	<b>44.2</b>	<b>10.3</b>	<b>0.7</b>

Dates in Study: bull peak - 2/19/2020, bear bottom - 3/23/2020, vaccine development - 11/9/2020, COVID cases trough - 6/17/2021. Current case updated through 10/6/2021. Sources: S&P Dow Jones Indices, S&P Capital IQ and MSCI, Inc. (GICS).

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# Models Models favor stocks on absolute and relative basis.



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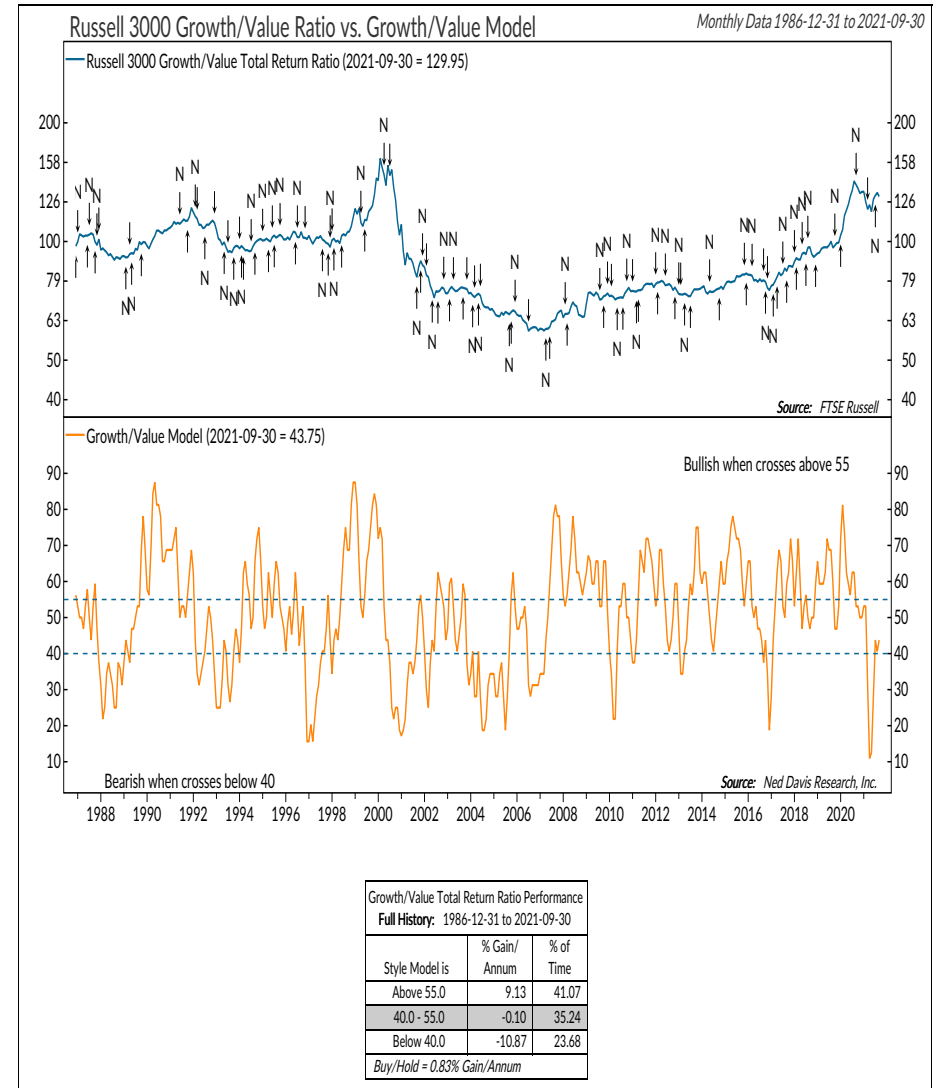
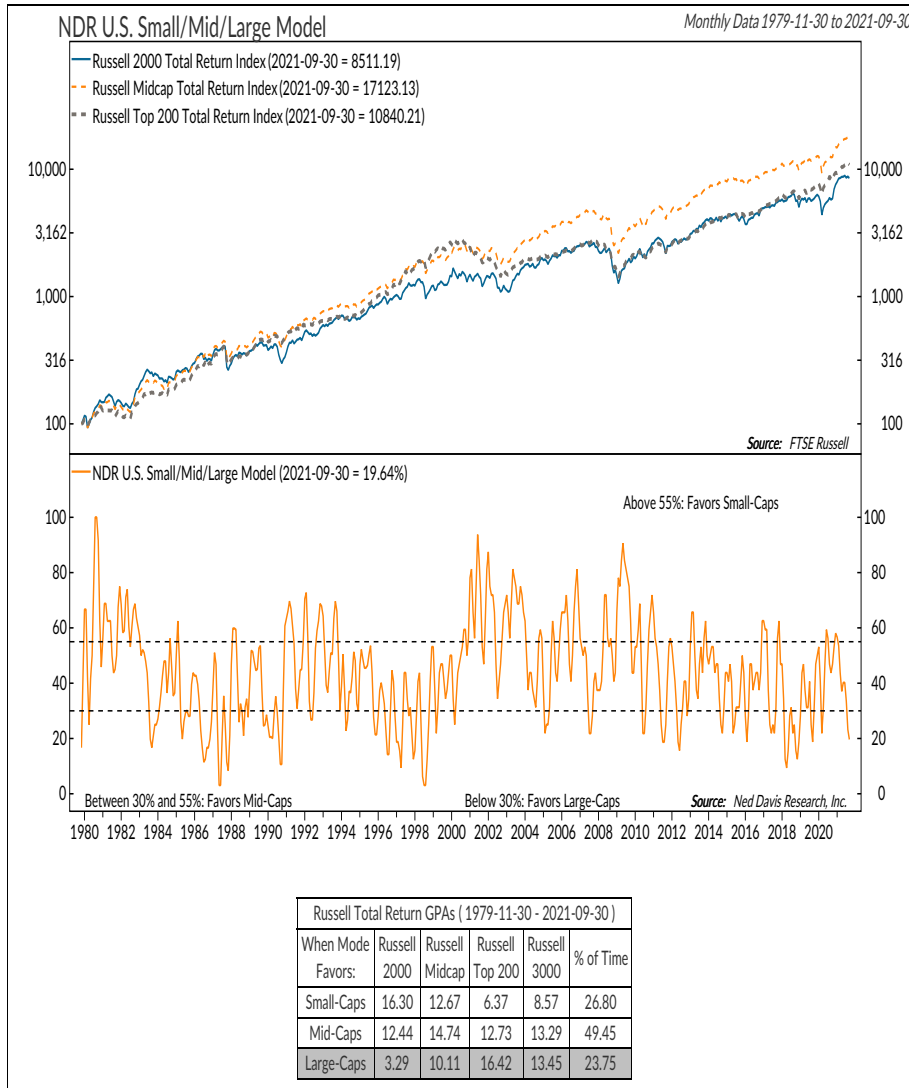
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# Models Style models moving away from early cycle leaders.



AA701








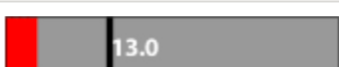





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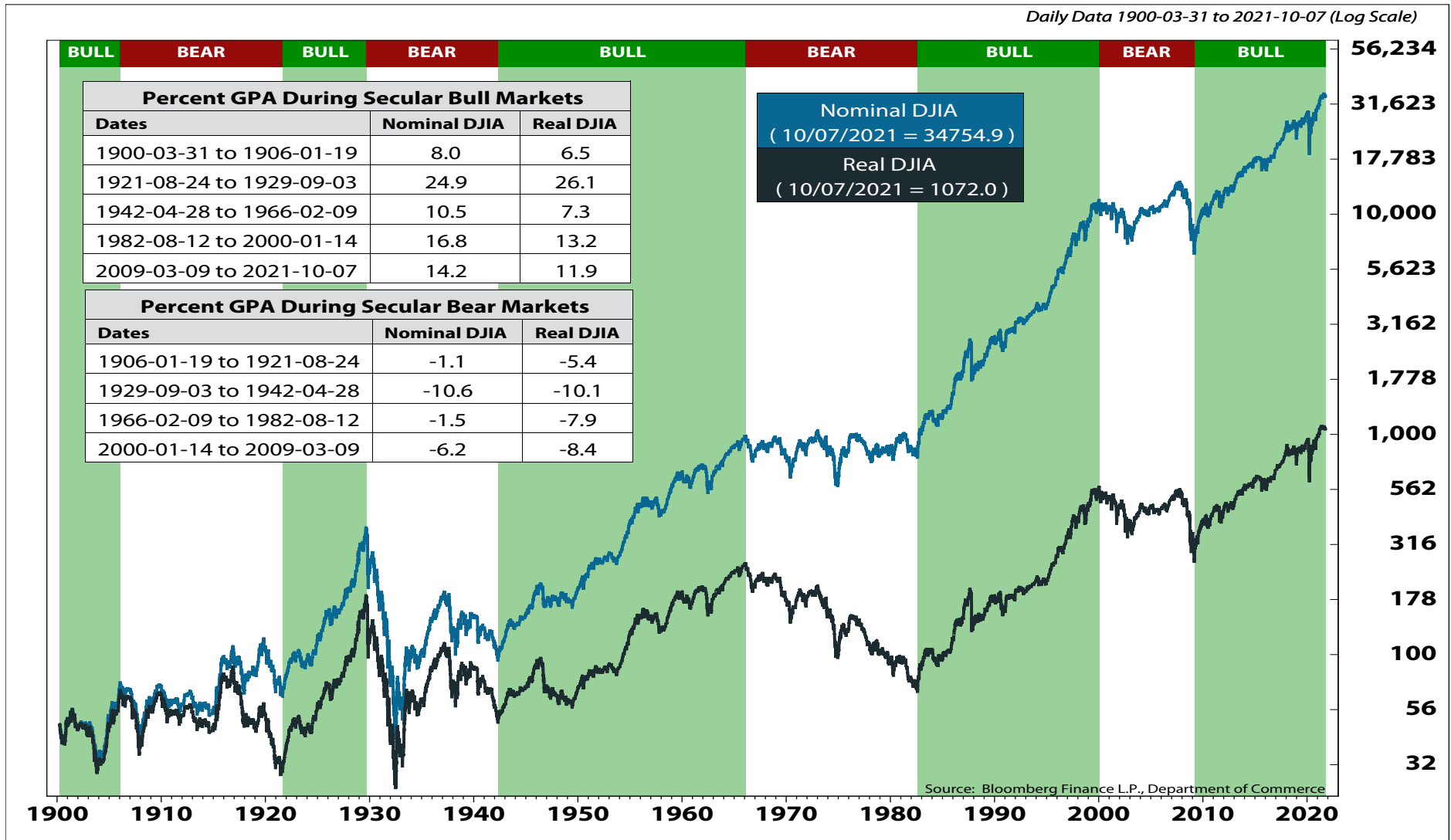
## Models No clear leadership message from sector model.

U.S. Sector Model Weights				
Sector	Model Weight vs. Benchmark Weight*	Month-End Readings		
		2021-09-30	2021-08-31	2021-07-30
<b><u>Energy %</u></b>	 2.5	5.9	4.3	3.5
<b><u>Materials %</u></b>	 2.6	1.7	2.1	1.6
<b><u>Industrials %</u></b>	 8.4	8.4	8.4	6.2
<b><u>Consumer Discretionary %</u></b>	 13.0	18.1	11.5	15.7
<b><u>Consumer Staples %</u></b>	 6.7	6.3	6.3	4.8
<b><u>Health Care %</u></b>	 13.0	3.3	8.6	12.7
<b><u>Financials %</u></b>	 10.6	10.1	10.1	9.8
<b><u>Information Technology %</u></b>	 27.0	27.4	30.1	30.2
<b><u>Communication Services %</u></b>	 11.2	12.5	9.8	8.1
<b><u>Utilities %</u></b>	 2.5	3.5	5.7	4.8
<b><u>Real Estate %</u></b>	 2.5	2.9	3.0	2.5



# Secular

Current secular bull comparable to previous ones.

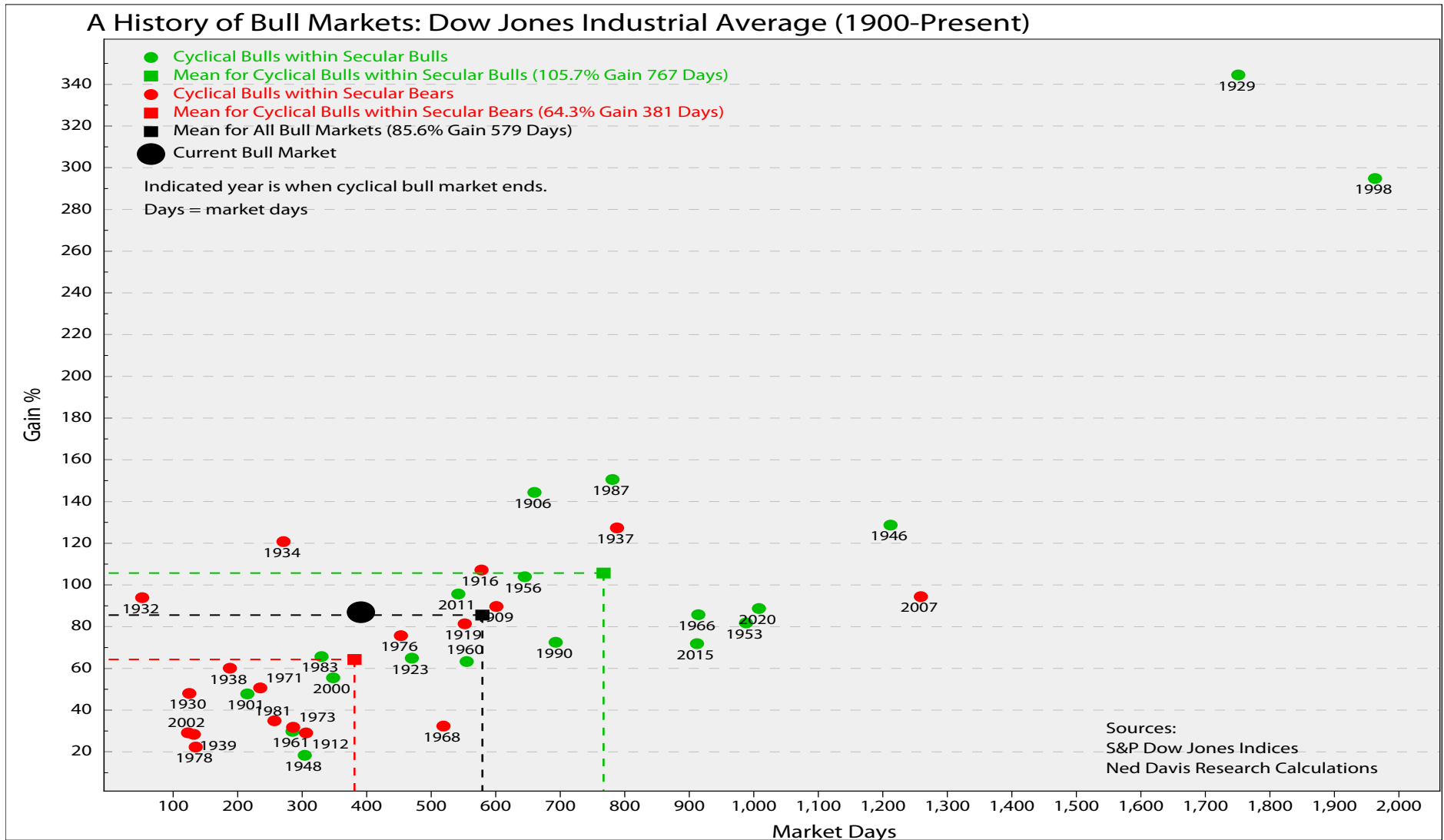


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# Secular Cyclical bulls stronger in secular bulls.

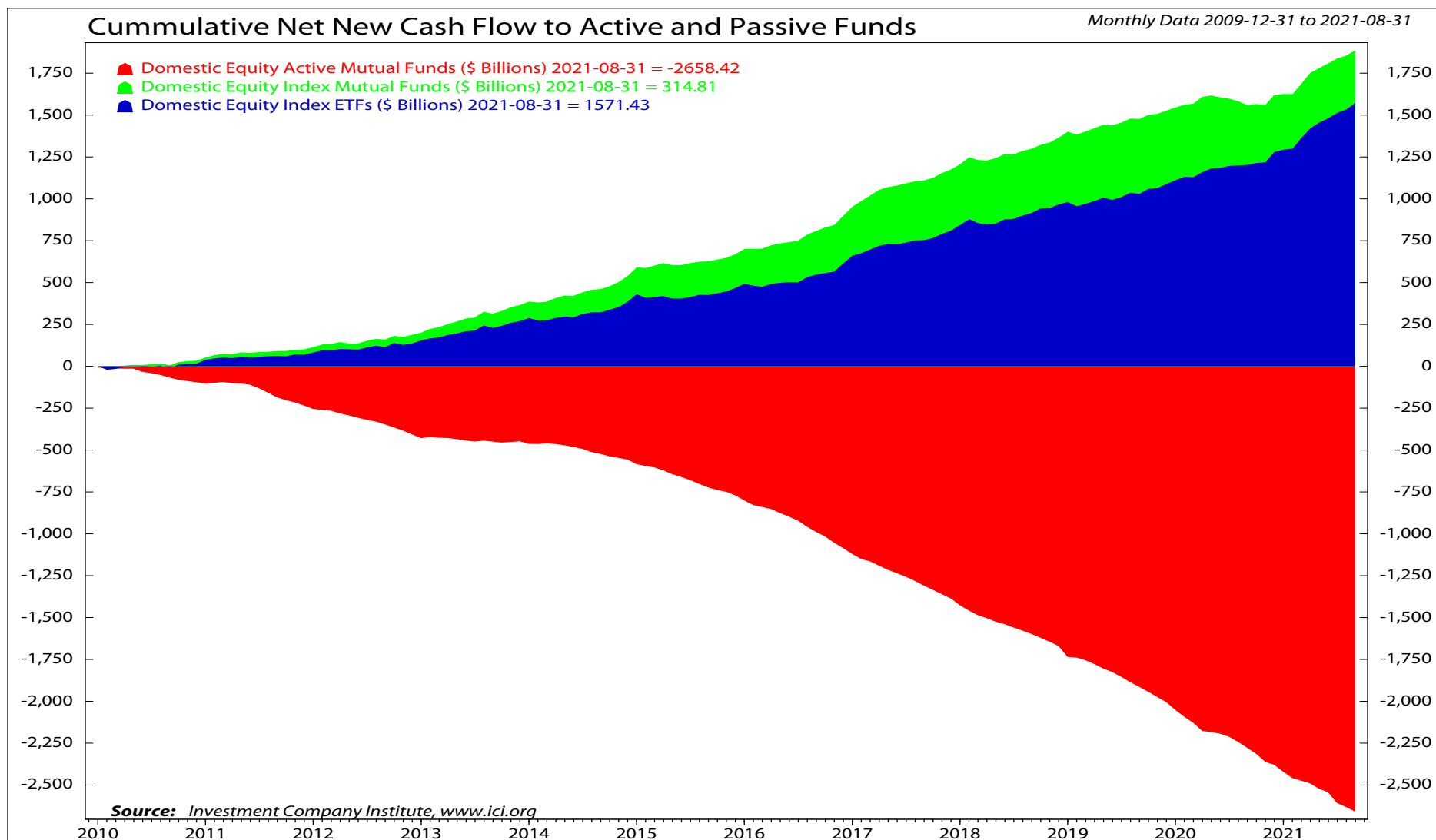


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# Secular Passive funds work just fine in secular bulls.

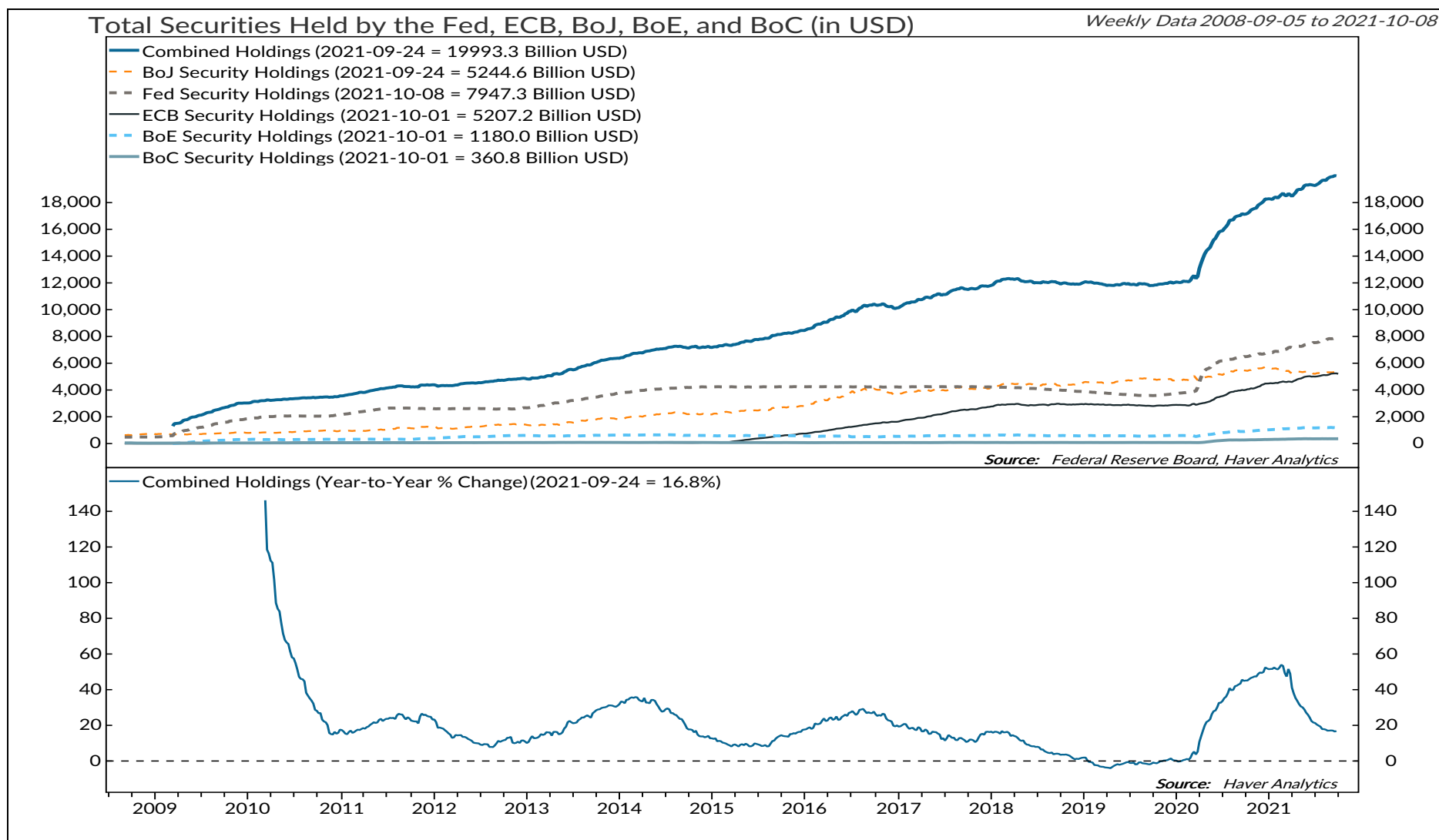


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# Secular Secular bull born of the Fed, likely die at hands of the Fed.

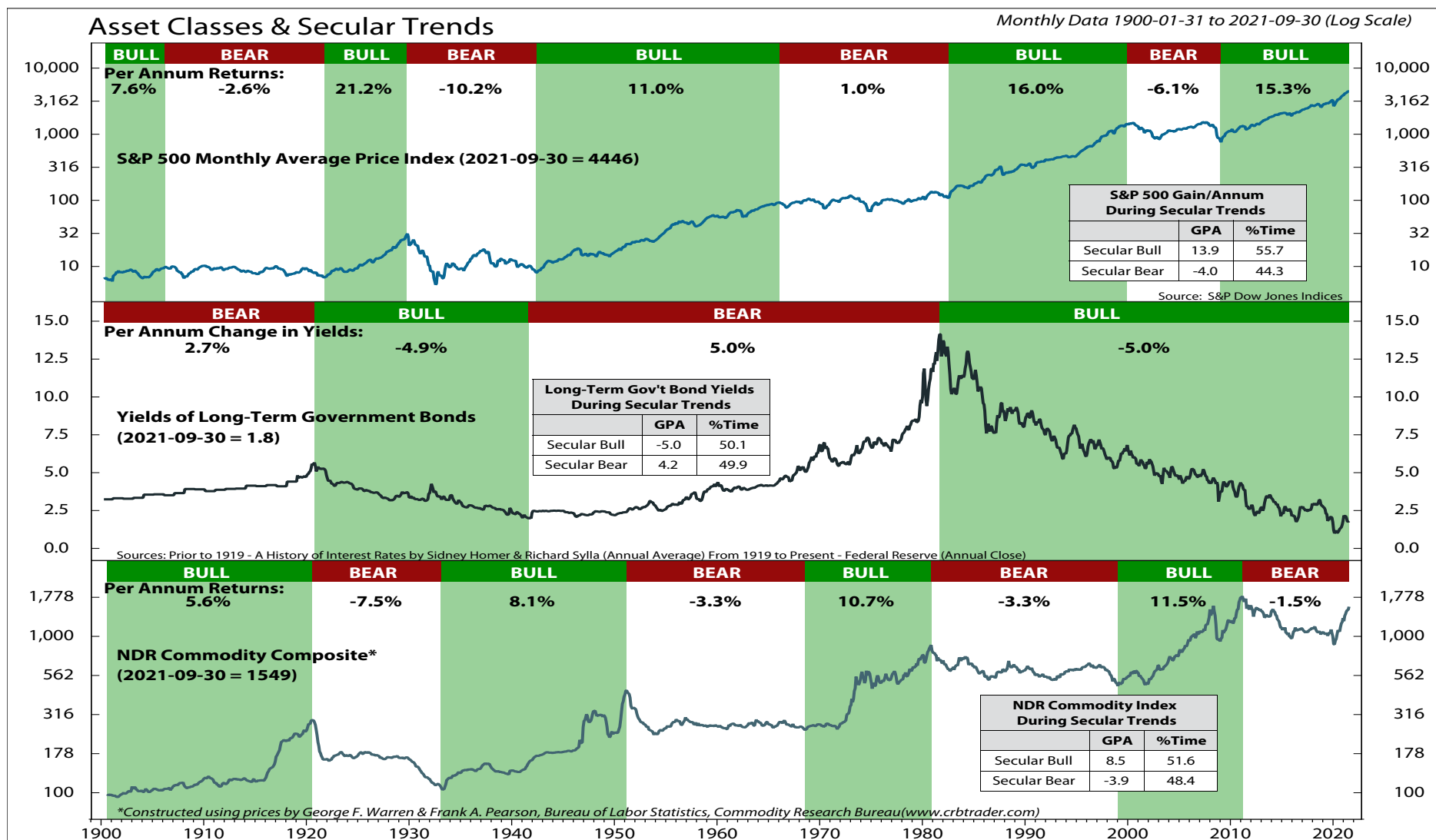


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# Secular Reports of bond secular bull's death have been greatly exaggerated.

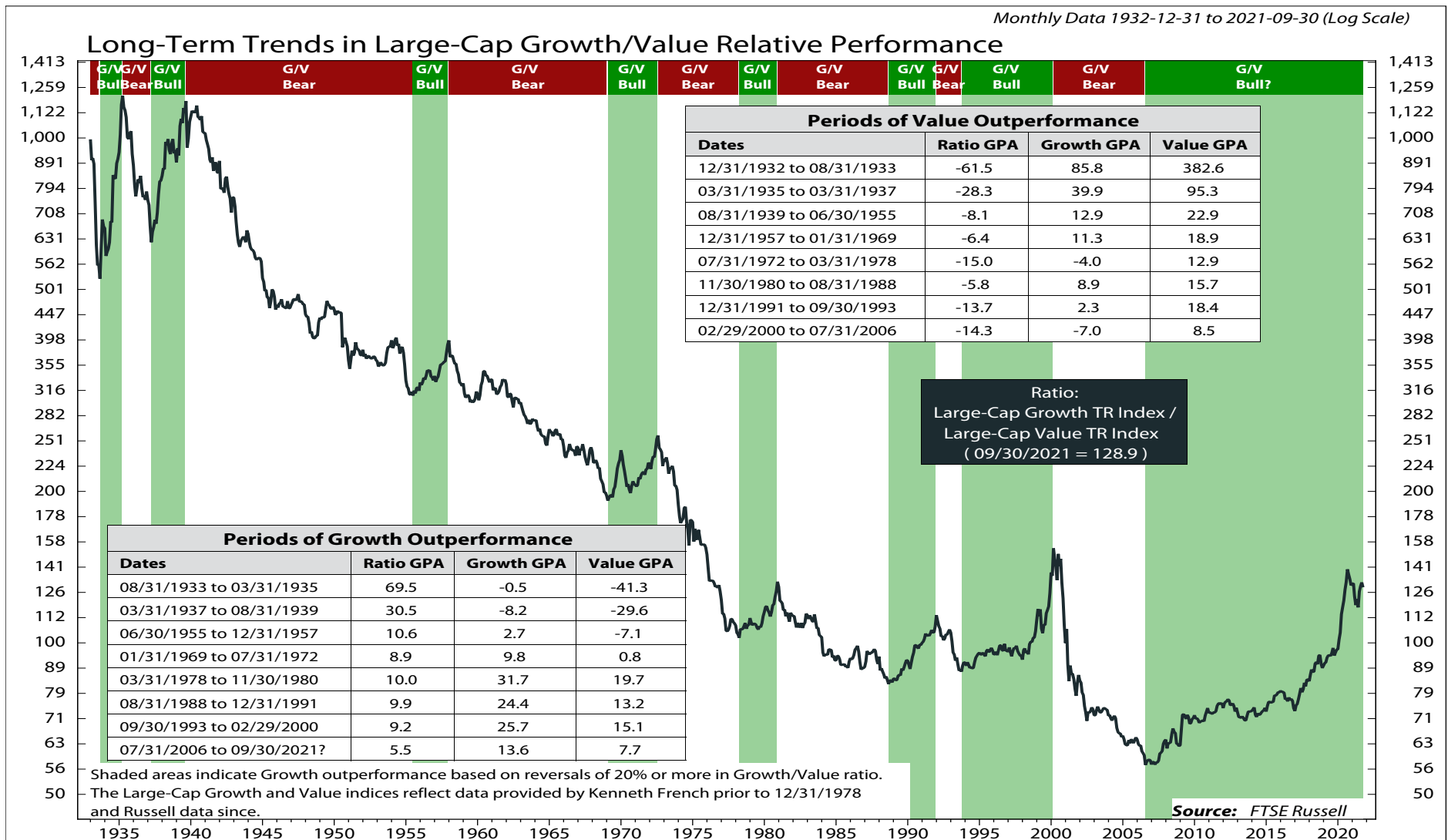


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# Secular Longest secular bull for Growth vs Value on record.

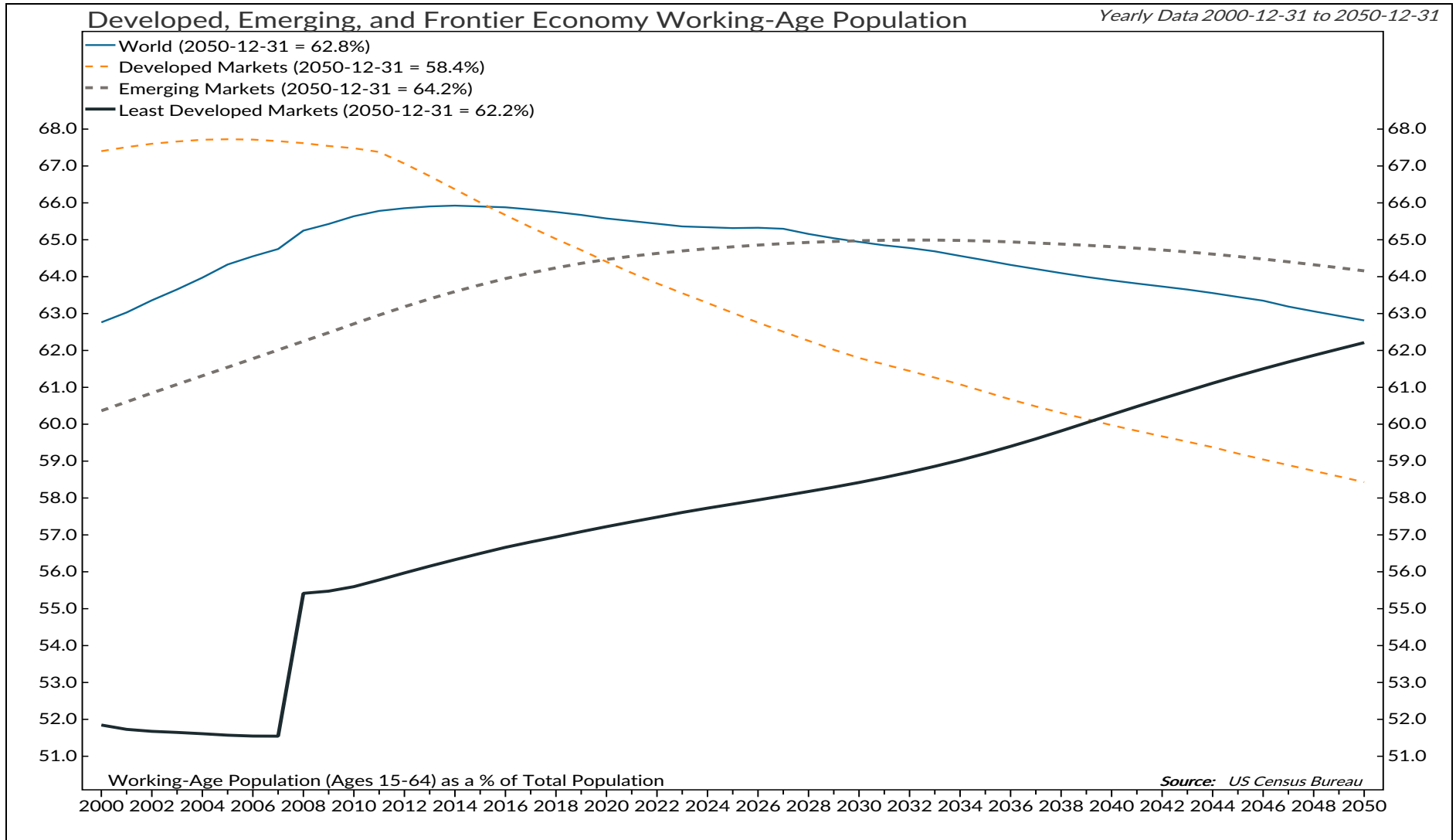


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# Secular Demographics cap growth rates.

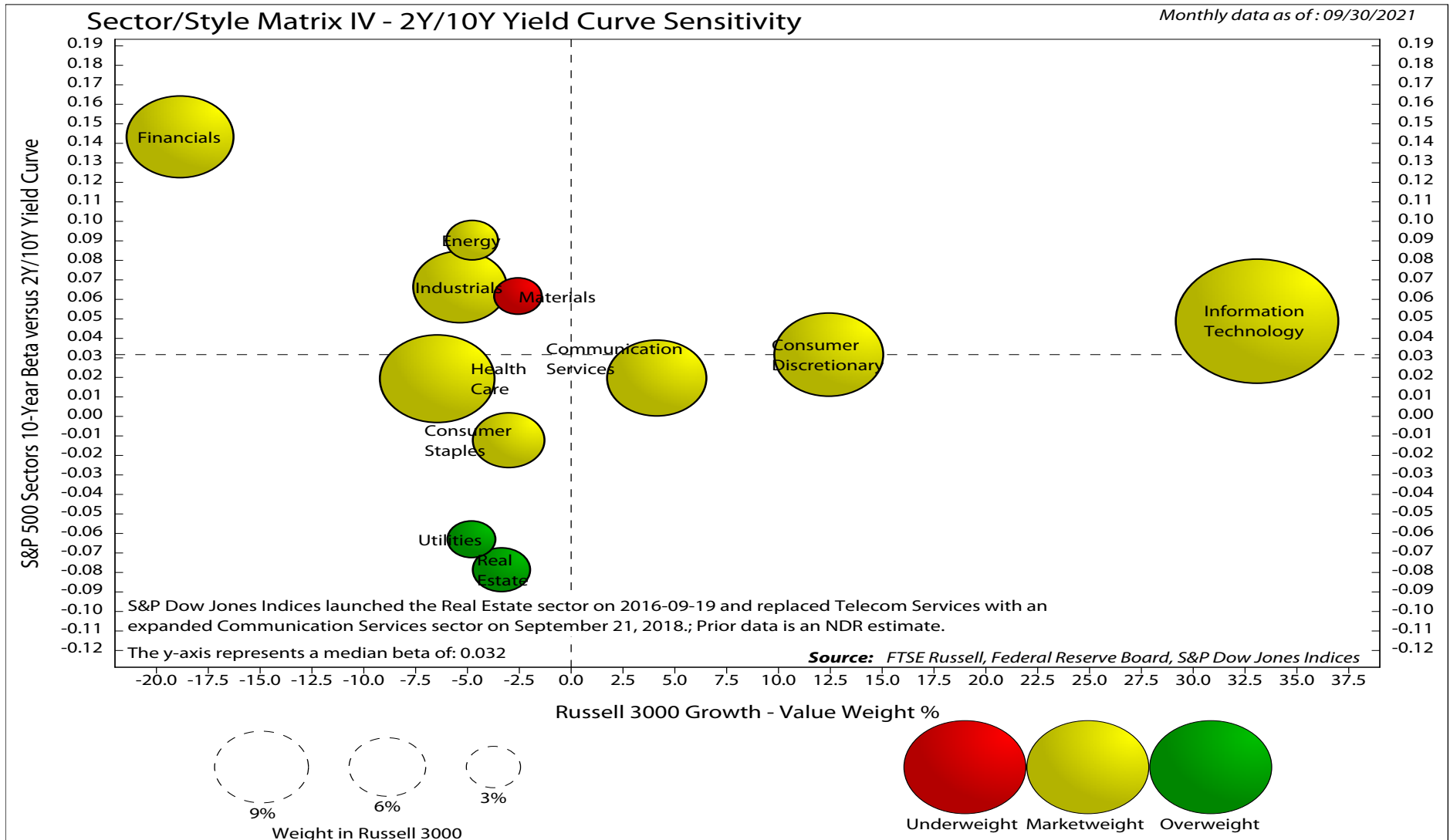


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# Secular New interest rate regime needed for Value secular bull.



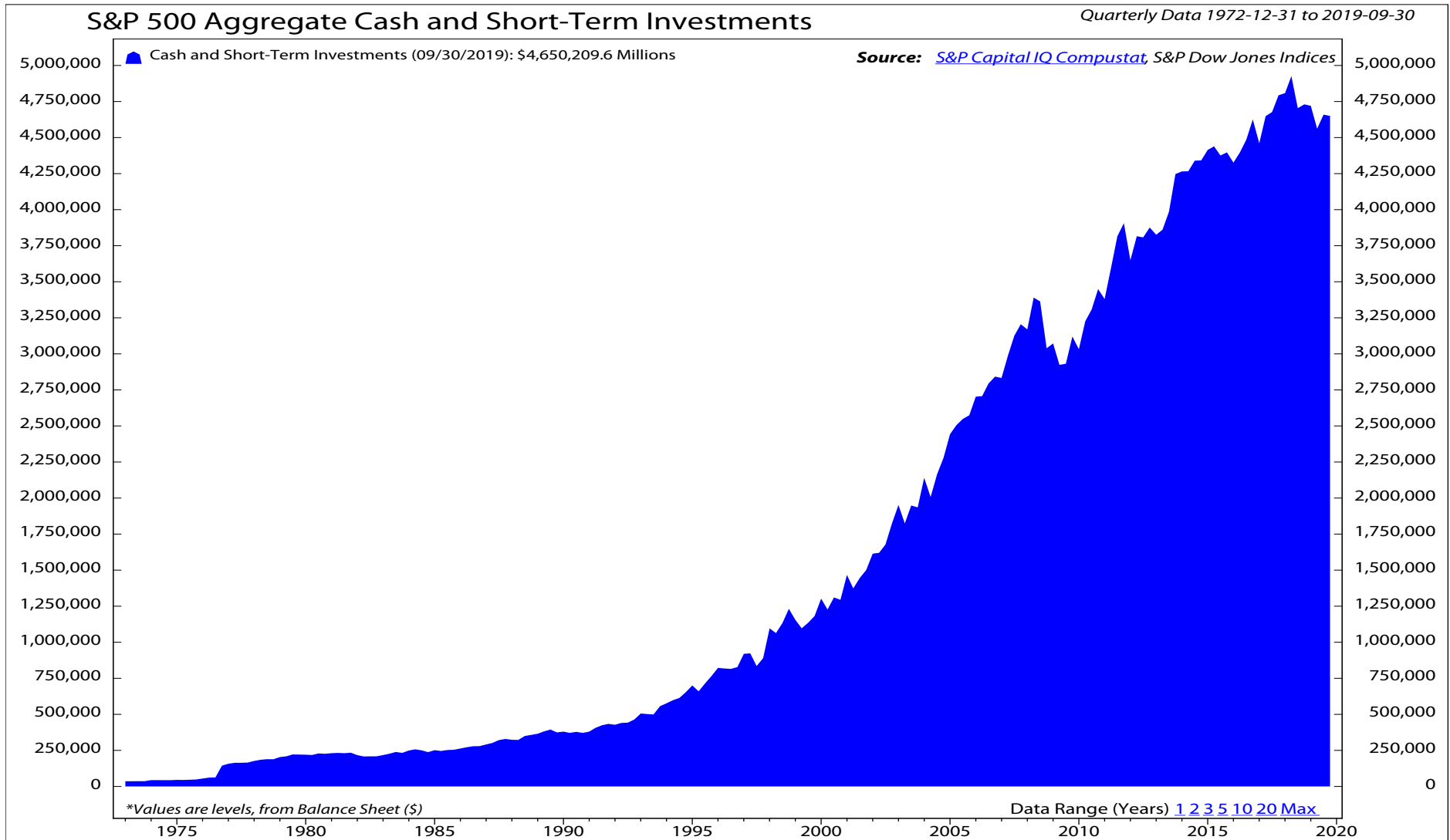
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# Secular In a slow-growth world, cash is king.

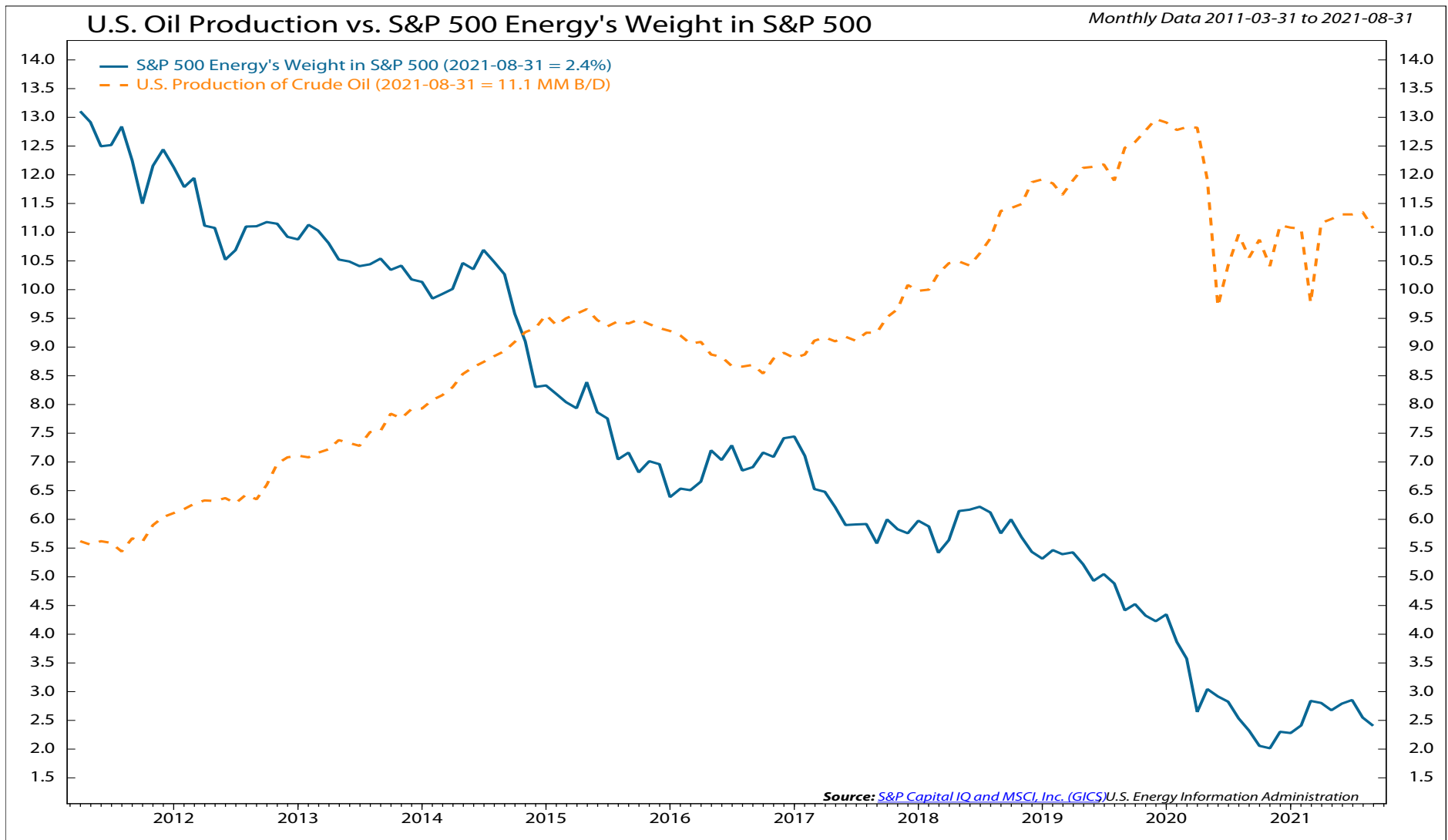


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# Secular Will green energy revolution spur secular bull in Energy sector?

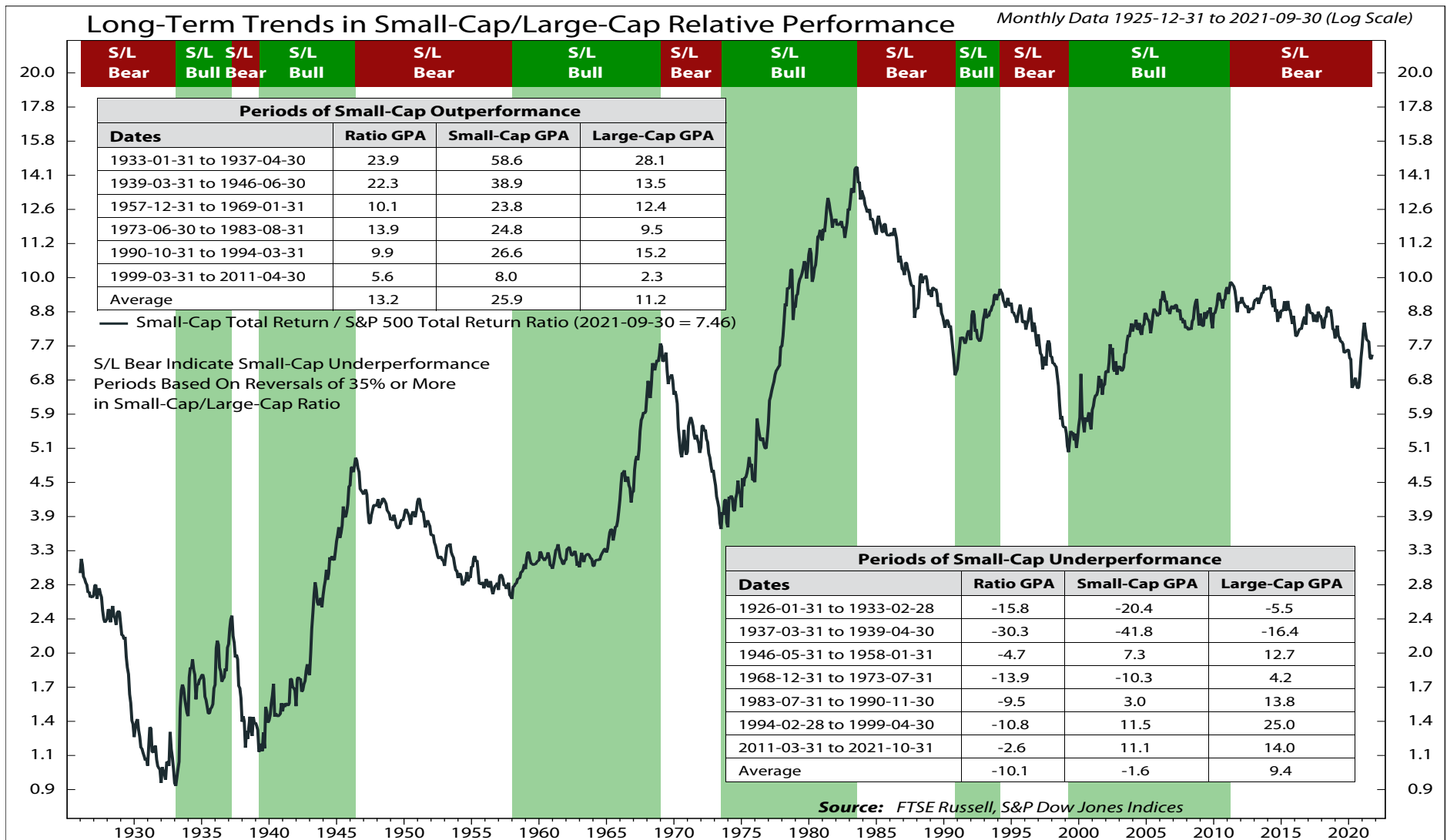


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# Secular Answer on small/large secular rotation could come in 2022.



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# Bottom Line

- Market gains moderate mid-cycle, with more frequent corrections
- Equity leadership transitions from small-caps, Value, and cyclical sectors to large-caps, Growth, and defensive sectors
- A COVID case drop could spur another reopening/cyclical Value trade
- Models favor stocks, large-caps, and mix of cyclical, and defensive sectors

NDR recommends maximum overweight allocation to equities and underweight allocations to bonds and cash. It is likely that we have seen a reset of the secular bull market that started in 2009.

## Equity Allocation

**U.S. |** We are overweight the U.S. relative to other regions and bullish on an absolute basis. Macro and fundamental conditions could turn less favorable as the cycle matures, but technical indicators remain constructive. As part of the maturing cycle, we neutralized our overweights to small-caps and Value. A neutral small/large recommendation is an implicit overweight to mid-caps.

**INTERNATIONAL |** We are overweight Japan, Europe ex. U.K., and the U.S., underweight Emerging Markets, U.K. and Pacific ex. Japan, and marketweight Canada.

## Macro

**ECONOMY |** The global economy fell into its deepest recession in the postwar era due to COVID-19, but pent-up demand and robust stimulus is setting the stage for a strong rebound in growth in 2021. Inflation will jump in the short-term, but long-term trends are anchored.

**FIXED INCOME |** We are 95% of benchmark duration. We are neutral on the yield curve. We are overweight MBS, ABS, HY corporates, EM, and TIPS. We are underweight Treasurys.

**GOLD |** Long-term uptrend intact. We are bullish.

**DOLLAR |** Our long-term technical composite is negative. We are bearish.

## Economic Summary

October 4, 2021

Near term activity: ● Accelerating ● Neutral ● Decelerating



Global Economy  
(6.1%)



U.S. Economy  
(5.0%-5.5%)



U.S. Inflation  
(3.5%-4.0%)

Economic gauges reflect changes in near-term economic activity. Numbers in parenthesis refer to NDR 2021 forecasts.

## Global Asset Allocation

● Overweight ● Marketweight ● Underweight

- Stocks (70%)
- Bonds (25%) | Cash (5%)

Benchmark: Stocks (55%), Bonds (35%), Cash (10%)

### Equities — Regional Relative Allocation

- U.S. (64%) | Europe ex. U.K. (16%) | Japan (9%)
- Canada (2%)
- Emerging Markets (6%) | U.K. (2%) | Pacific ex. Japan (1%)

Benchmark – U.S. (58.2%), Europe ex. U.K. (12.9%), Emerging Markets (12.9%), Japan (6.4%), U.K. (3.7%), Pacific ex. Japan (3.1%), Canada (2.8%)

### Global Bond Allocation

- U.S. (50%) | Europe (28%) | Japan (17%) | U.K. (5%)

Benchmark: U.S. (50%), Europe (28%), Japan (16%), U.K. (6%)

## U.S. Allocation

- Stocks (70%) | Mid-Cap
- Growth | Value
- Bonds (20%) | Cash (5%) | Large-Cap | Small-Cap

Benchmark: Stocks (55%), Bonds (35%), Cash (10%)

### Sectors

- Utilities (4%) | Real Estate (4%)
- Materials (1%)

Benchmark: Technology (27.0%), Health Care (13.1%), Financials (10.4%), Communication Services (11.2%), Consumer Discretionary (12.9%), Consumer Staples (6.9%), Industrials (8.4%), Energy (2.4%), Utilities (2.6%), Real Estate (2.5%), Materials (2.6%)

### U.S. Bonds — 95% of Benchmark Duration



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# Ed Clissold, CFA

## Chief U.S. Strategist

**Ed Clissold, CFA**, is the Chief U.S. Strategist for Ned Davis Research Group. He and his team are responsible for the firm's U.S. equity, style, sector and equity theme analysis. They do so via a combination of a top-down analysis of the macroeconomic and fundamental environments and a bottom-up analysis of factors specific to the asset class, market cap, style, sector, or theme. He and his team also provide in-depth macro research on fundamental topics such as earnings, dividends, and cash flow.

Ed writes several U.S. Strategy publications, which provide an intermediate-term outlook on U.S. markets via a combination of top-down and bottom-up analyses. He also writes a quarterly Benchmarks report, which analyzes the attribution of returns across asset classes, sectors, market cap, and styles.

Ed's market commentary is often quoted in **The Wall Street Journal**, **Barron's**, and other financial publications.

Ed has held a number of other positions since joining the firm in 2002, including Global Equity Strategist, Senior Global Analyst in the Global Asset Allocation group, and Analyst in the Custom Research Services department. Previously, Ed worked at Strong Capital Management and as a Market Strategist at J.C. Bradford & Co.

Ed is a CFA charterholder, a **magna cum laude** graduate in Economics from Transylvania University, and has earned his Masters in Business Administration in Finance, with distinction, from Indiana University (Kelley).



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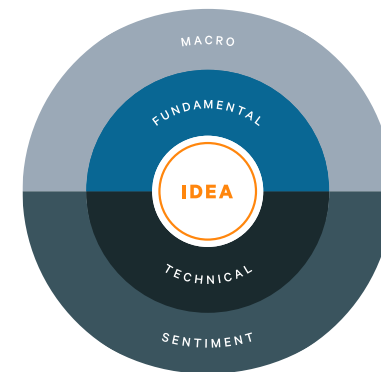
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