



# TRANSITIONS

## INVESTING IN THE LATE-CYCLE

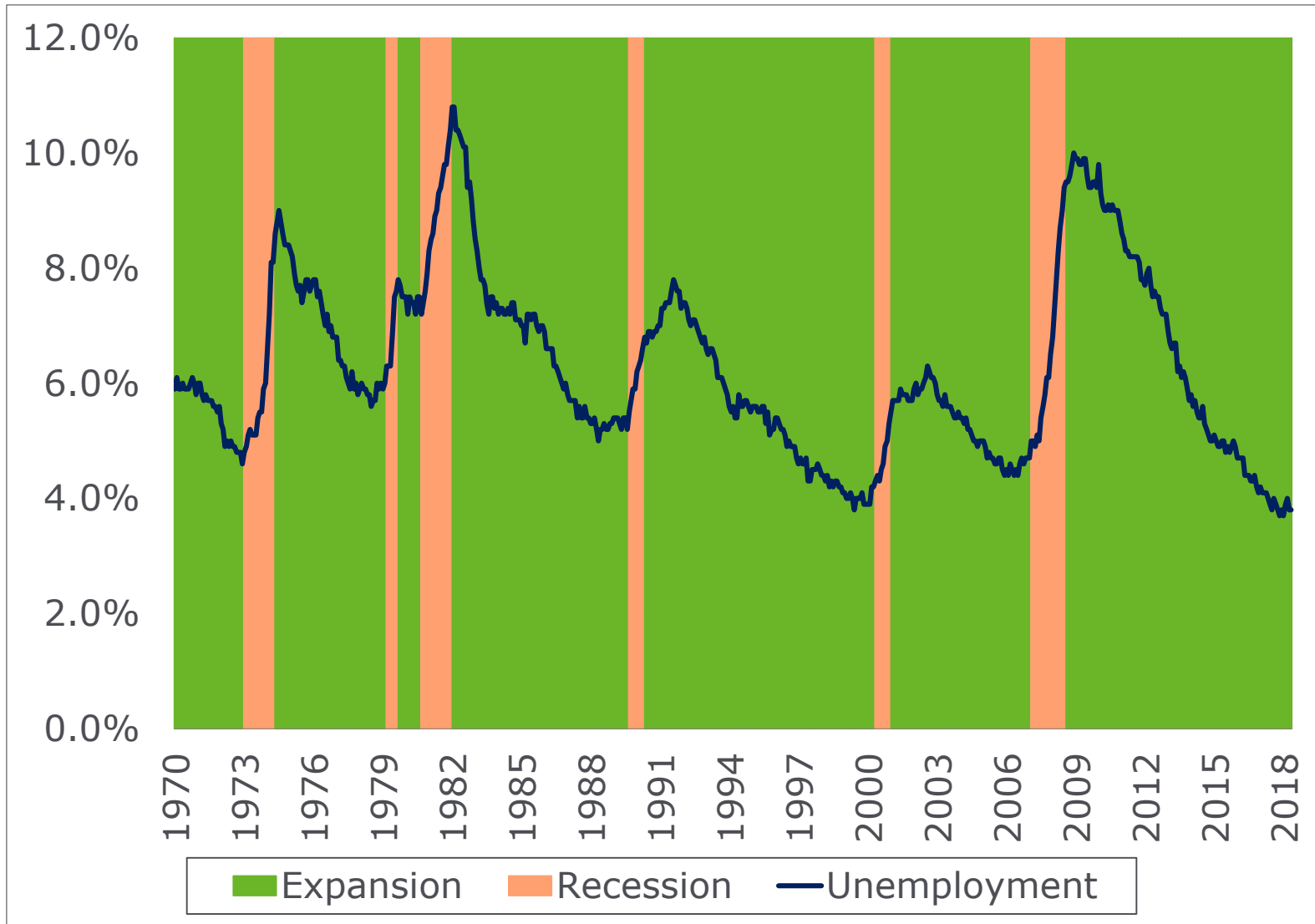
**Tim McCusker, Chief Investment  
Officer**



**NEPC'S 24<sup>th</sup> ANNUAL INVESTMENT CONFERENCE**

MAY 7-8, 2019 | BOSTON, MA

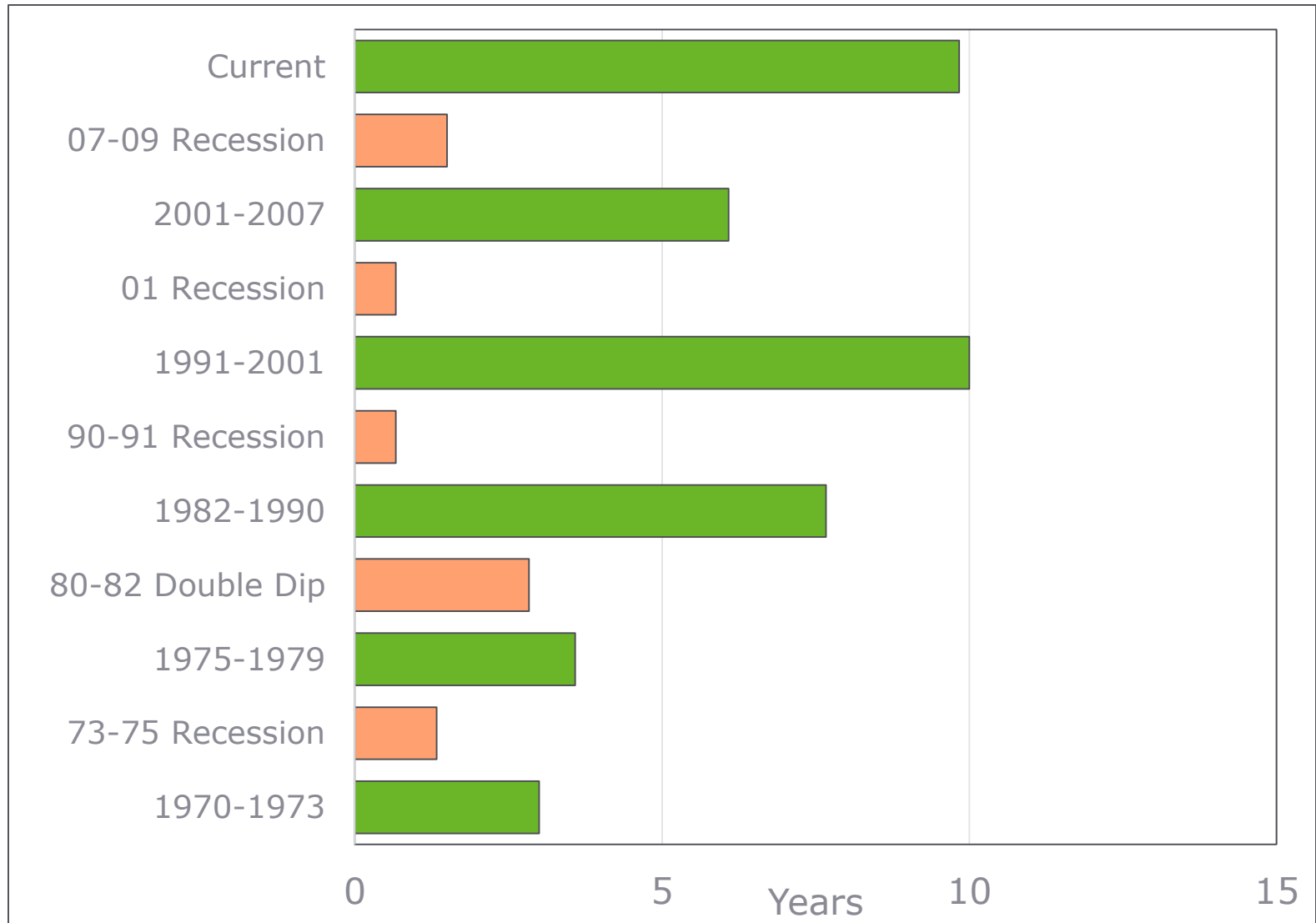
# ECONOMIC CYCLES



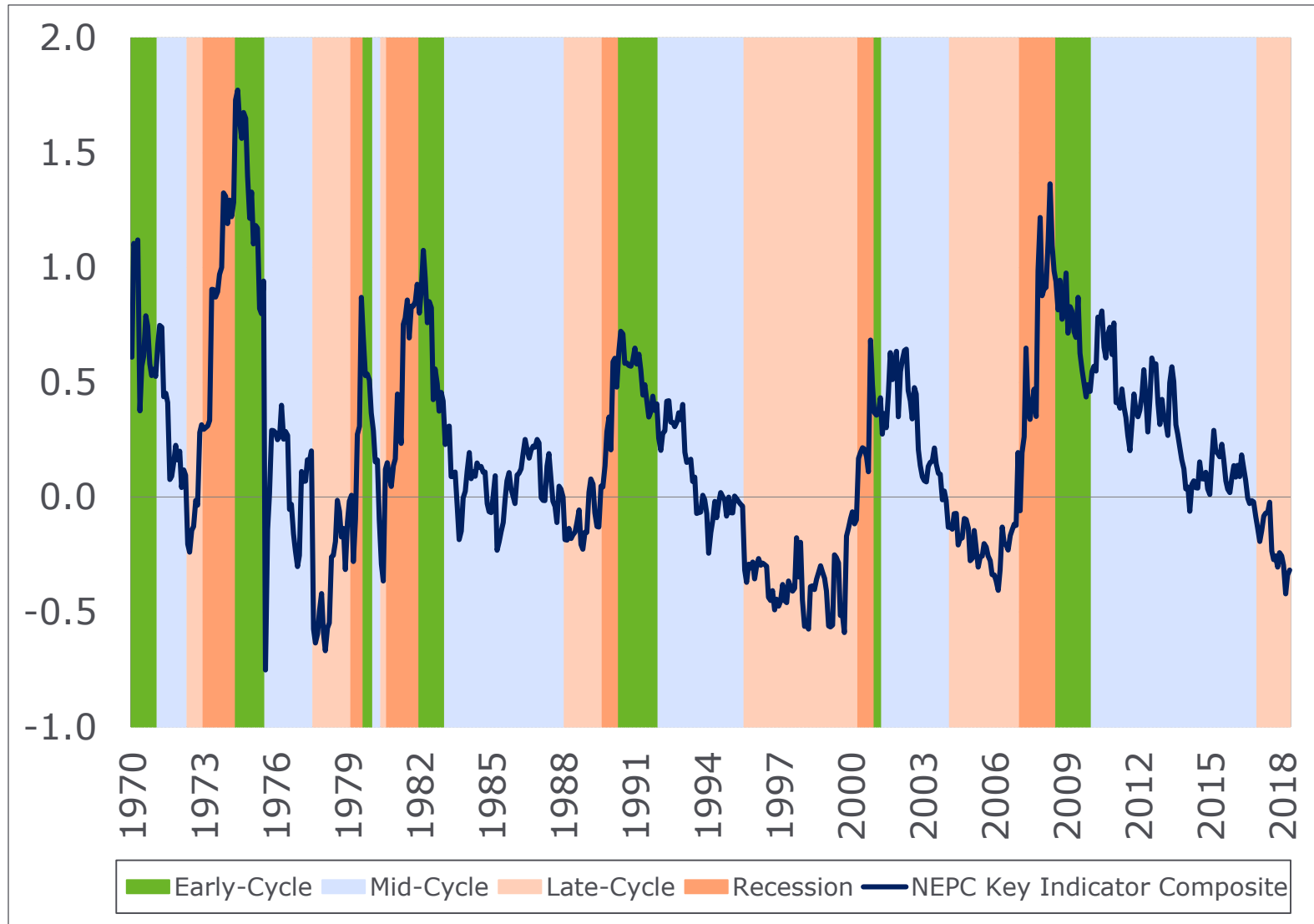
Source: St. Louis Federal Reserve, NBER



# EXPANSIONS AND RECESSIONS



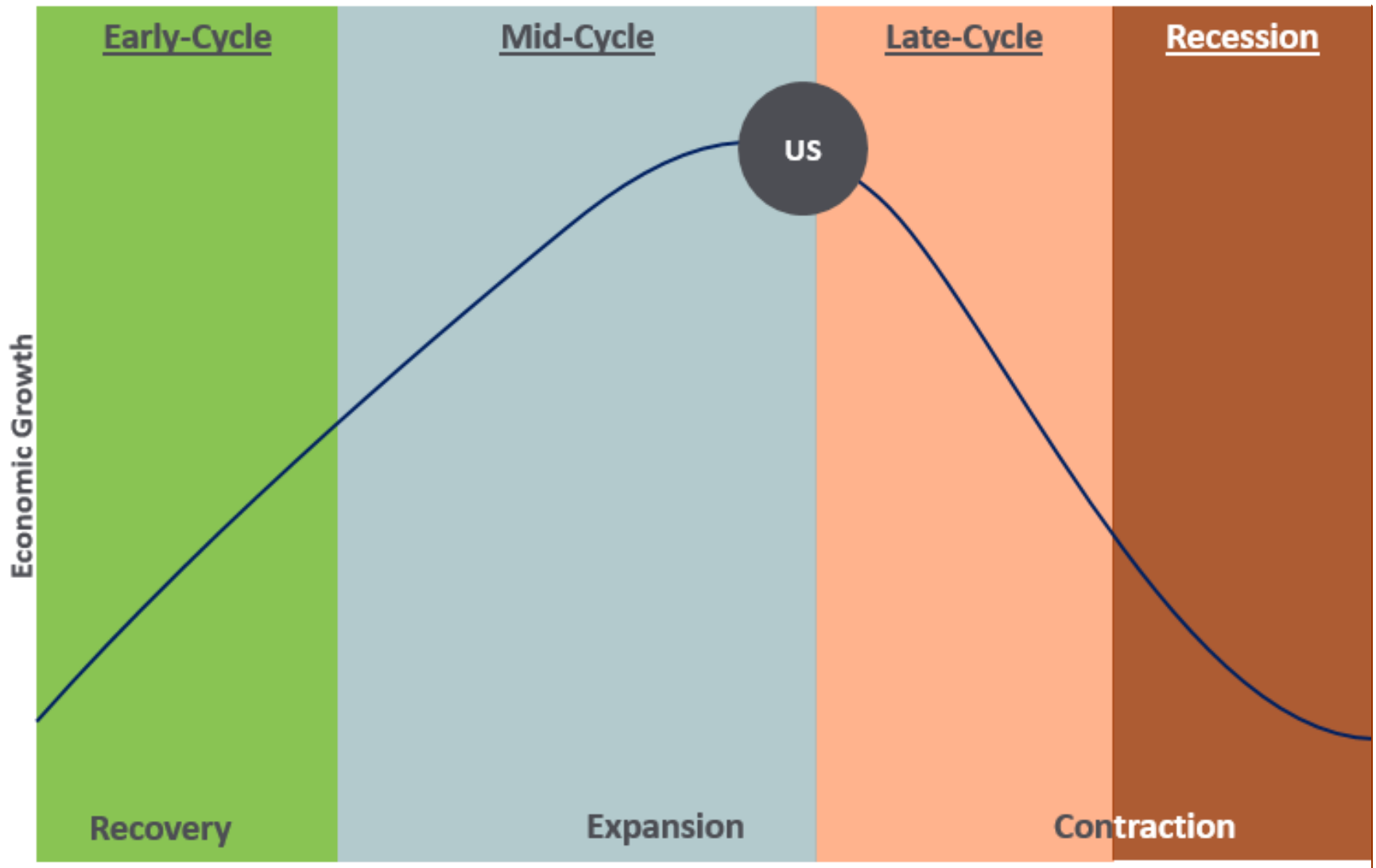
# VARIOUS STAGES OF MARKET CYCLES



Source: St. Louis Federal Reserve, NBER, NEPC



# ECONOMIC CYCLES



# KEY LATE-CYCLE INDICATORS

Certain key economic indicators have often preceded the end of economic expansions and equity bull markets. Barring any unforeseen events or shocks, changes to these key indicators have historically provided a useful guide to recognize changes in the economic cycle.

Interest  
Rates/Policy

The Yield  
Curve

Economic  
Growth

Output Gap

Inflation

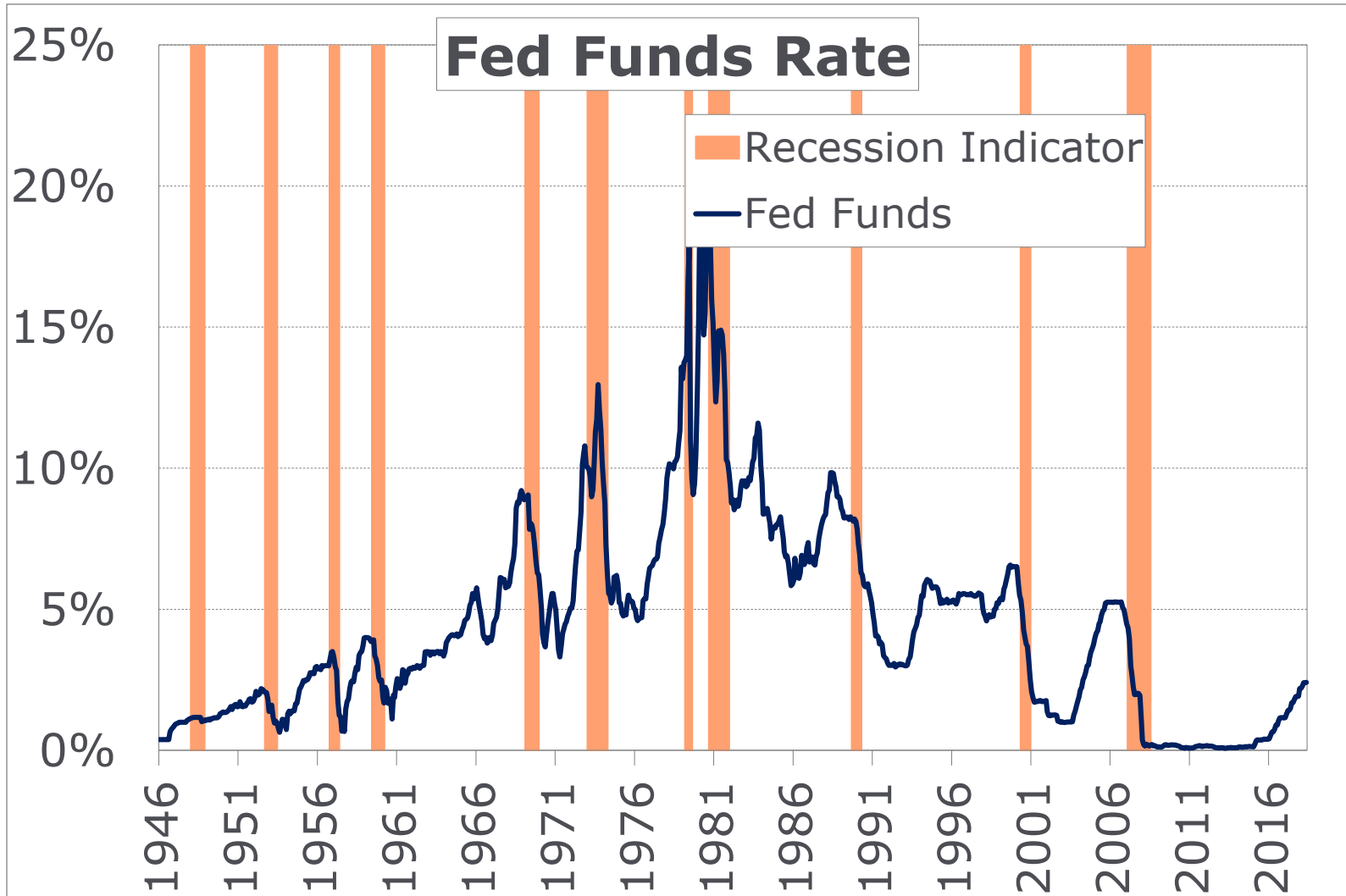
Unemployment

Equities

Credit Spreads

# INTEREST RATES/POLICY

**Expected Late-Cycle Behavior:** Rising and then stabilizing

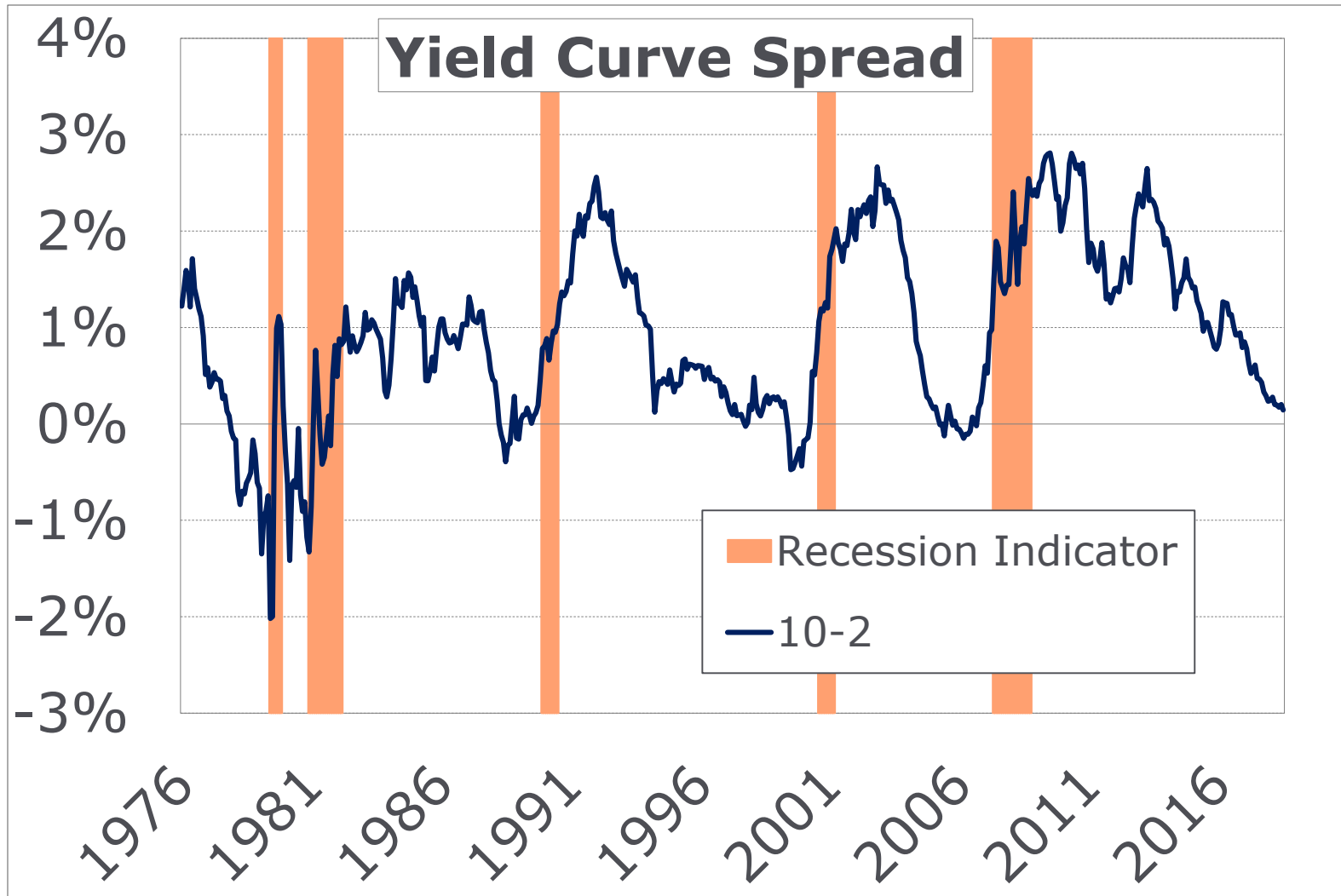


Source: St. Louis Federal Reserve, NBER, NEPC



# THE YIELD CURVE

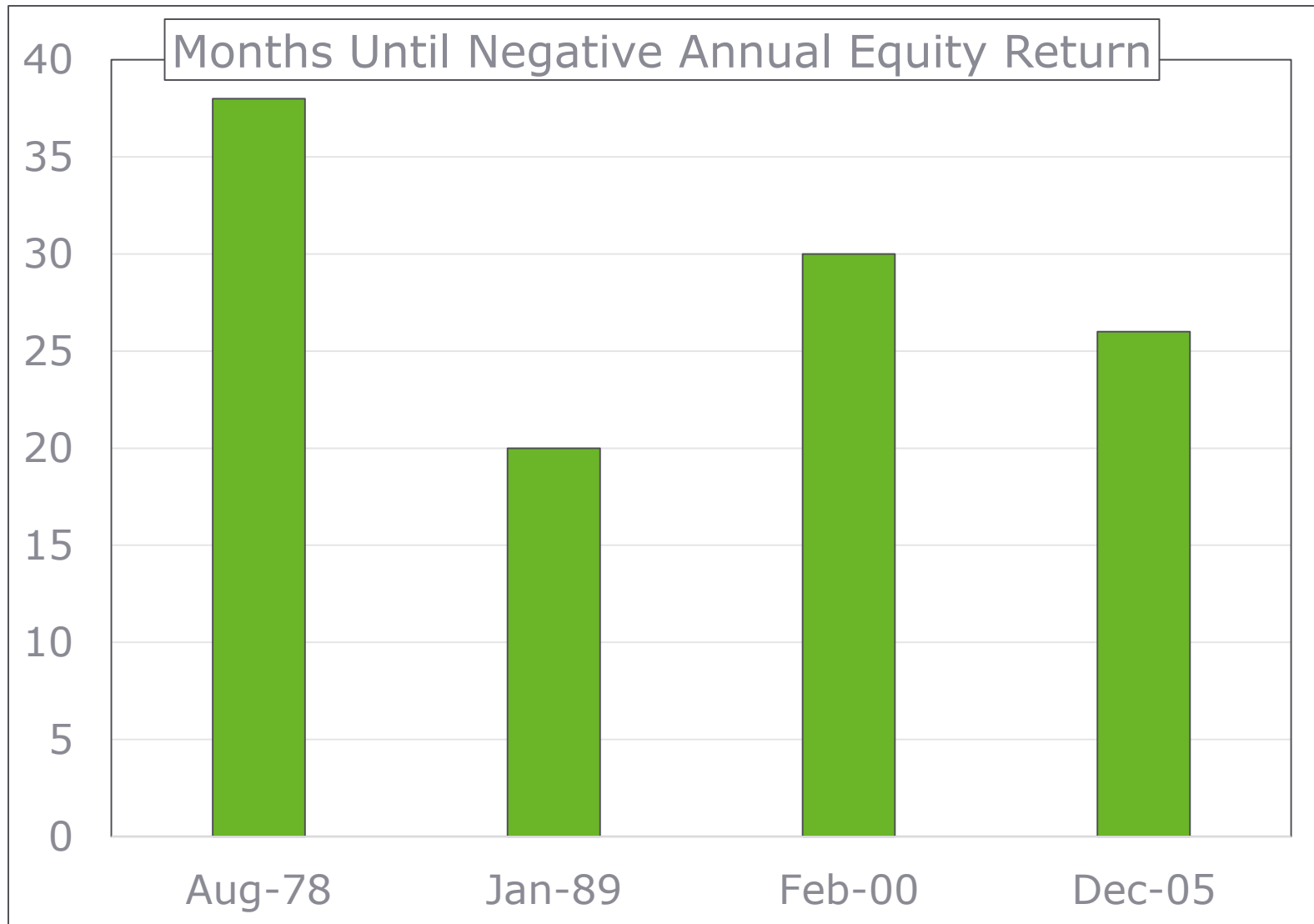
**Expected Late-Cycle Behavior:** Flattening



Source: Bloomberg, NBER, NEPC

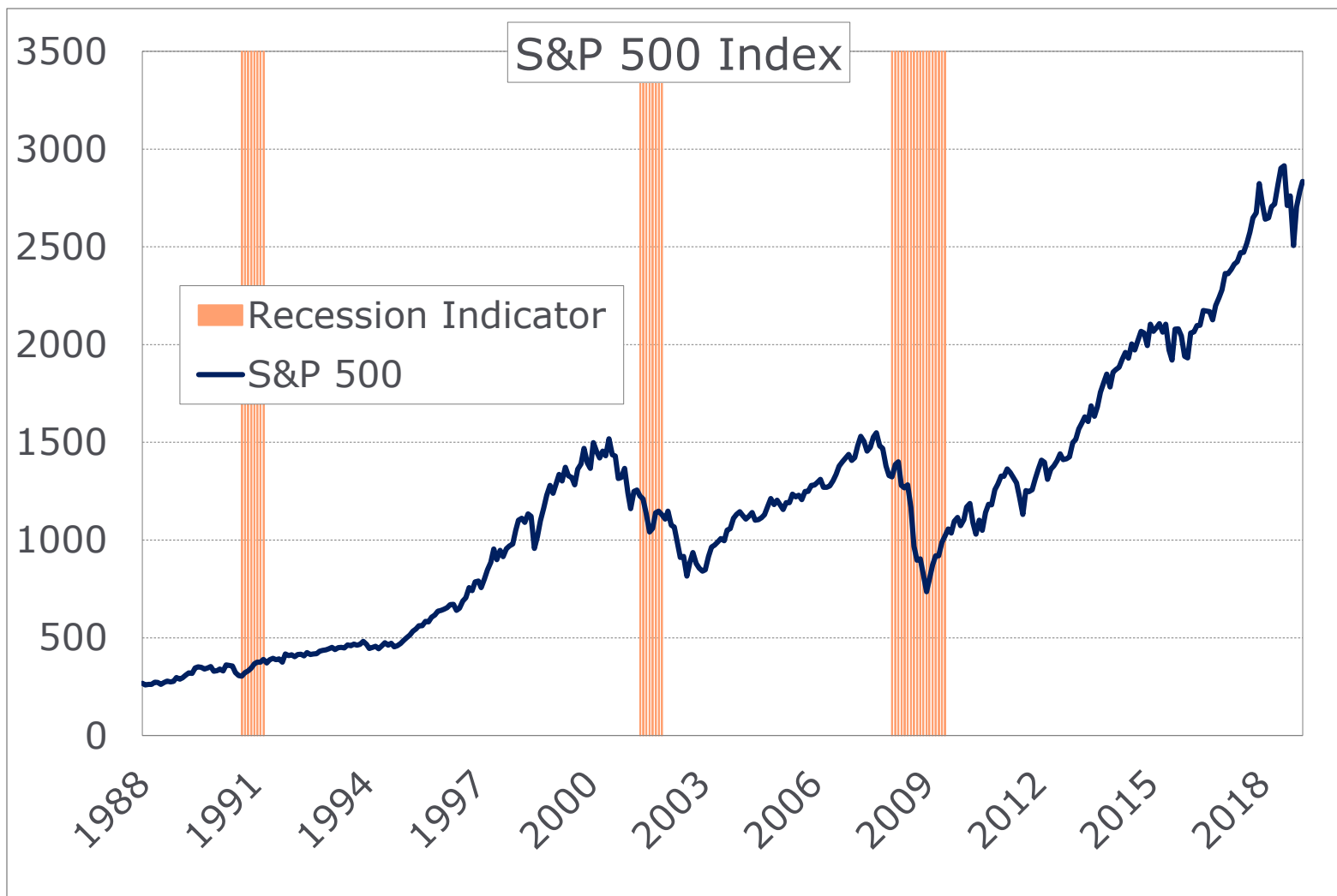


# YIELD CURVE INVERSION AND EQUITIES



# EQUITIES

## Expected Late-Cycle Behavior: Peaking

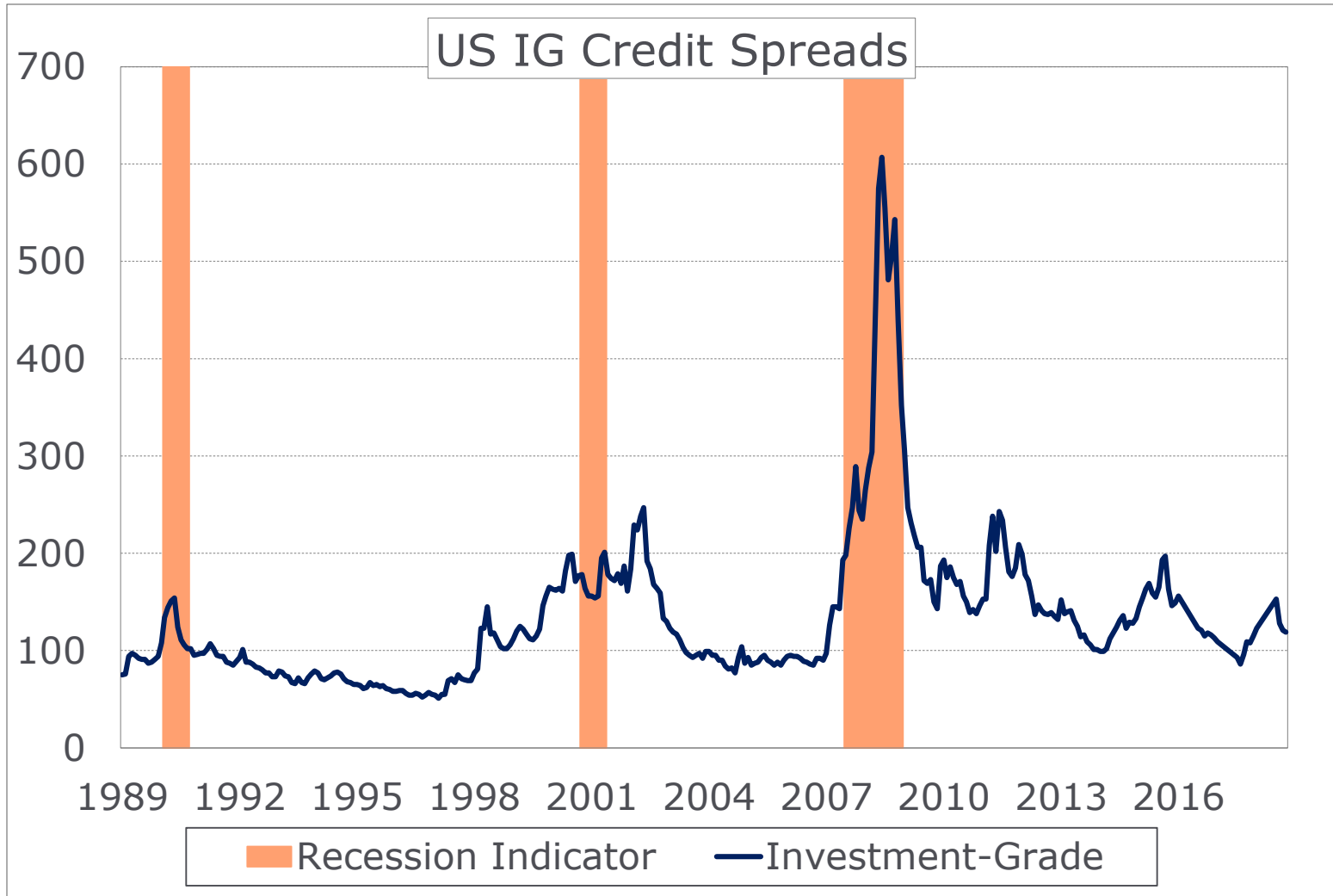


Source: S&P, Bloomberg, NBER, NEPC



# CREDIT SPREADS

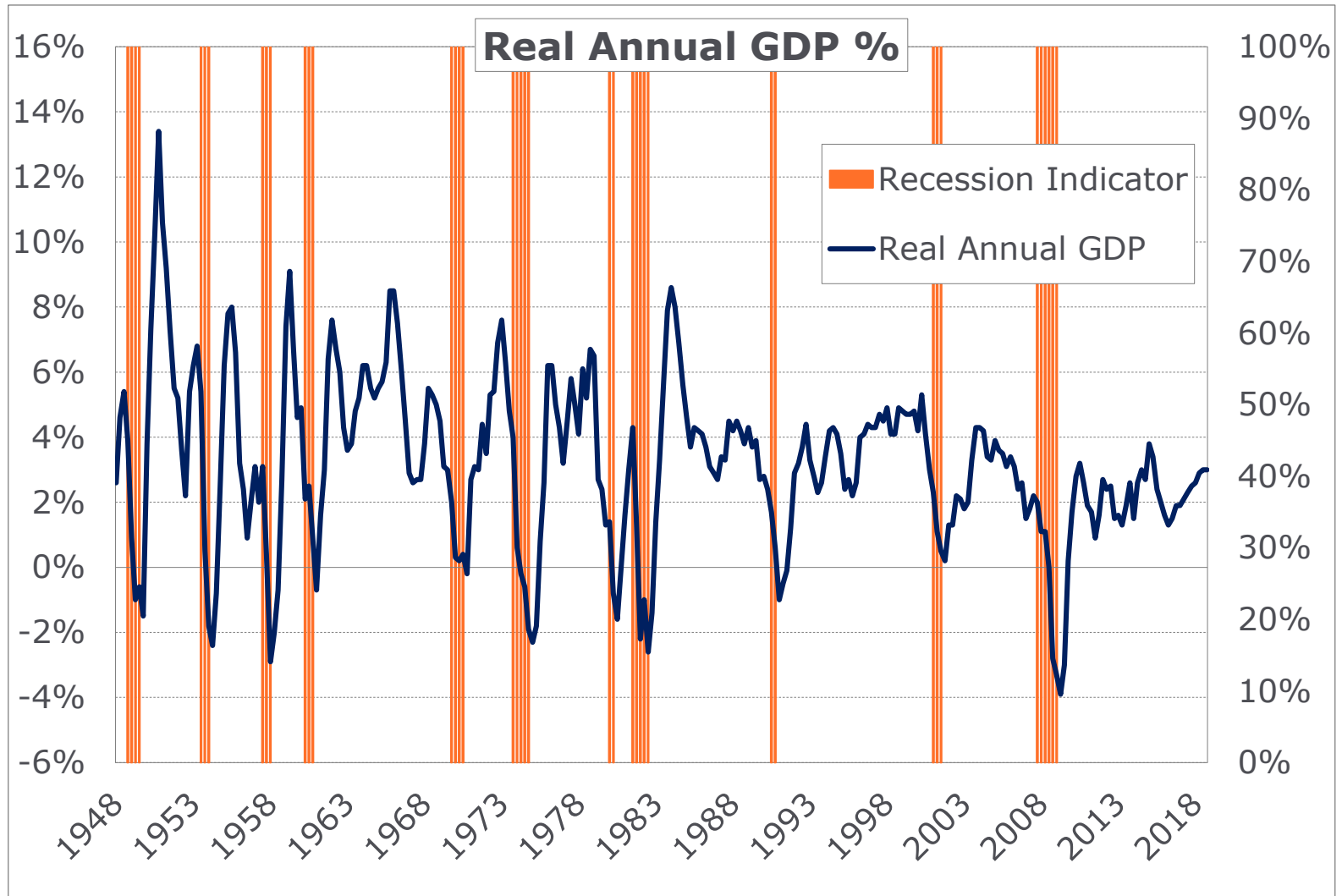
**Expected Late-Cycle Behavior:** Stable/Rising



Source: Barclays, Bloomberg, NBER, NEPC

# ECONOMIC GROWTH

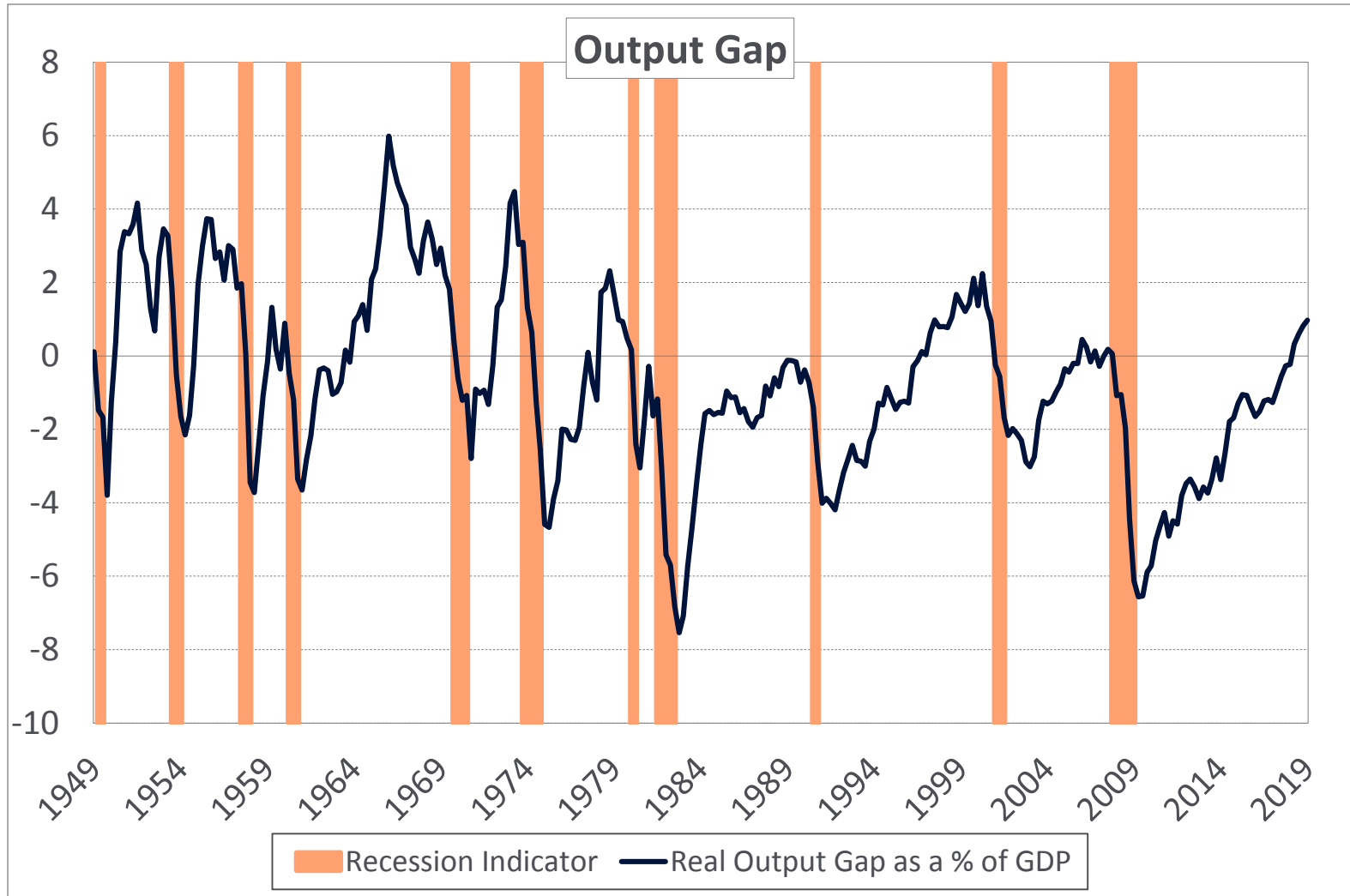
## Expected Late-Cycle Behavior: Moderating



Source: Bloomberg, NBER, NEPC

# OUTPUT GAP

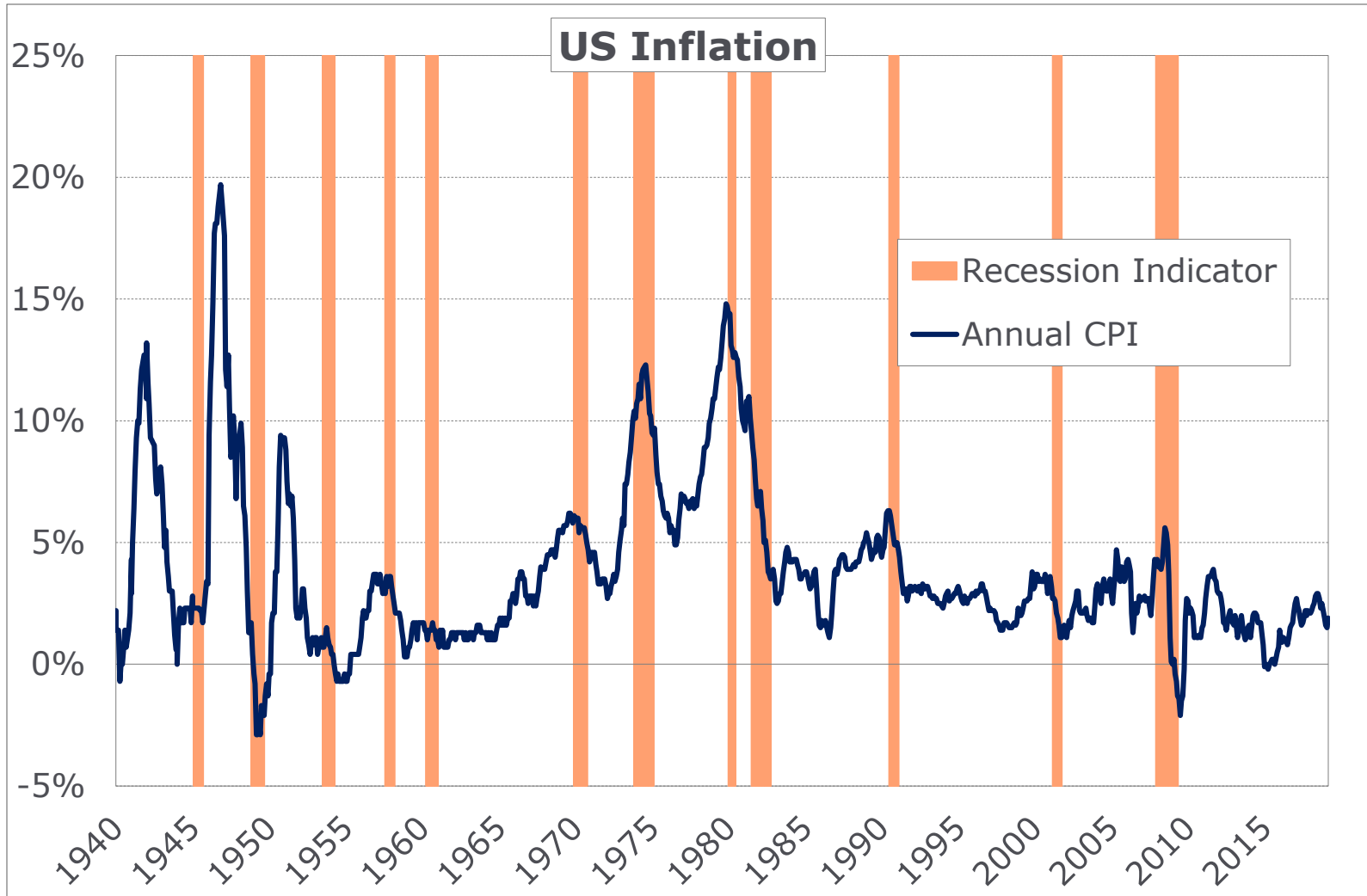
**Expected Late-Cycle Behavior:** Near/Above Potential Output Gap



Source: Bloomberg, NBER, NEPC

# INFLATION

**Expected Late-Cycle Behavior:** Rising

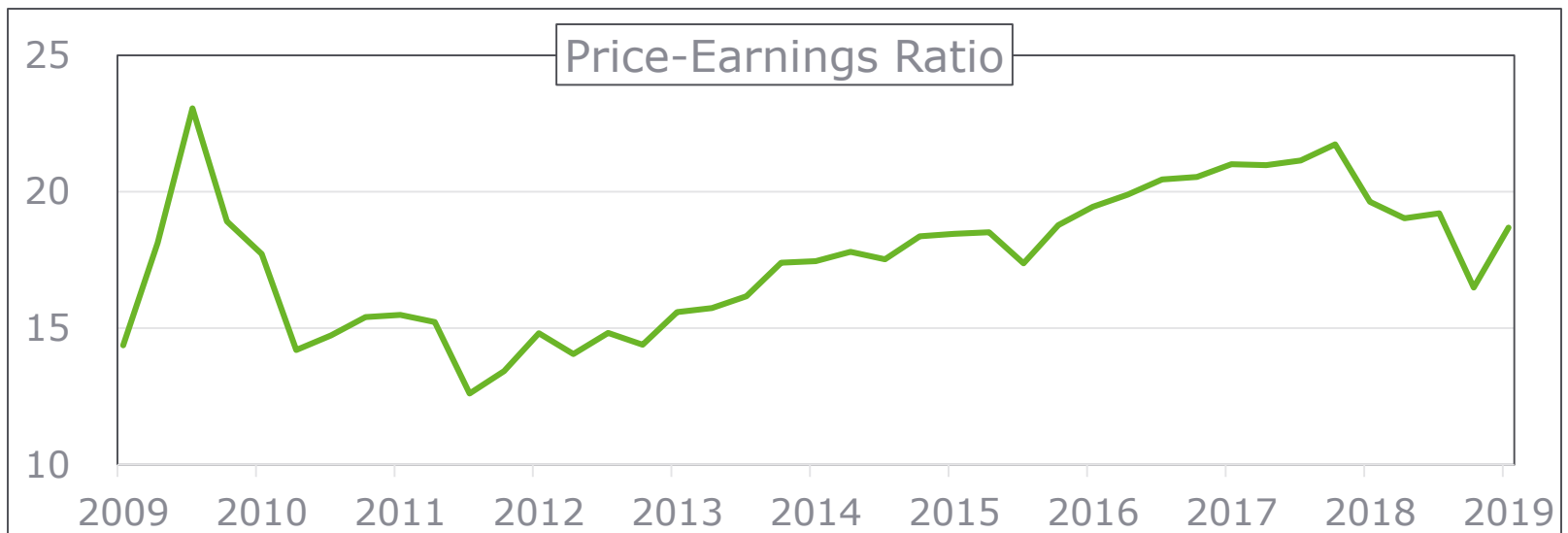
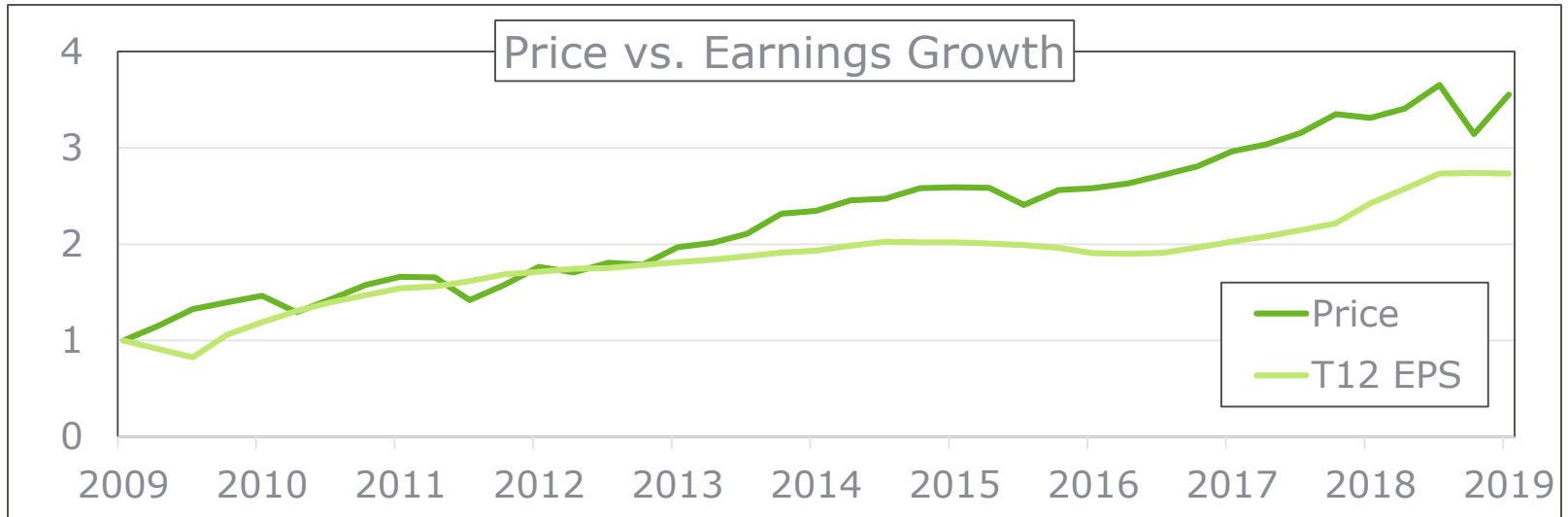


Source: Bloomberg, NBER, NEPC

# CURRENT INDICATORS SUMMARY

Key Indicator	Expected Late Cycle Behavior	Late Cycle Conditions?
Interest Rates	Rising, then stabilizing	Yes
The Yield Curve	Flattening	Yes
Equities	Peaking	<i>Uncertain</i>
Credit Spreads	Stable/Rising	Yes
Economic Growth	Moderating	<i>Uncertain</i>
Output Gap	Near/Above Potential	Yes
Inflation	Rising	Yes, but low
Unemployment	Falling/Bottoming	<i>Uncertain</i>

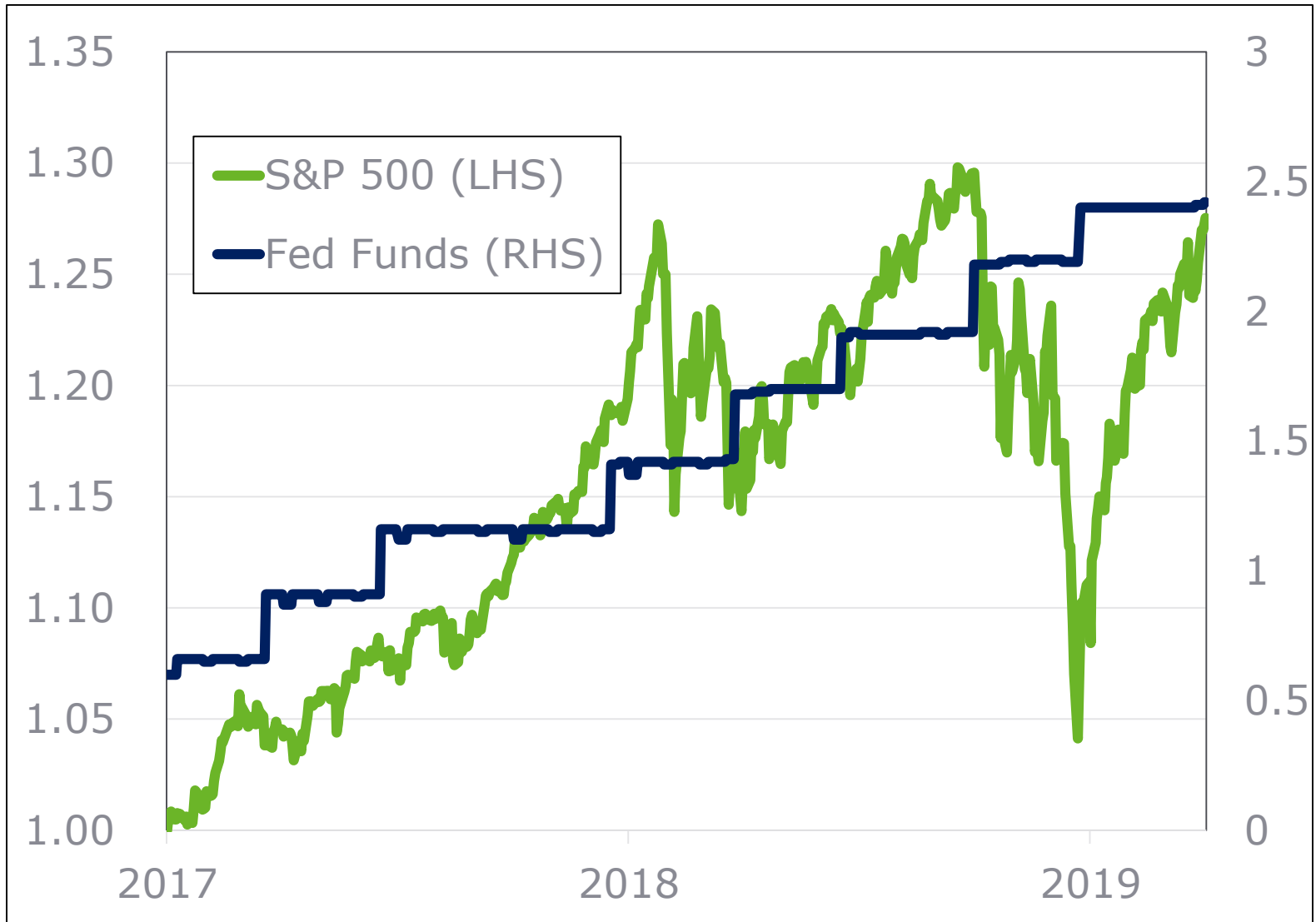
# VALUATIONS AND EARNINGS INFLUENCE



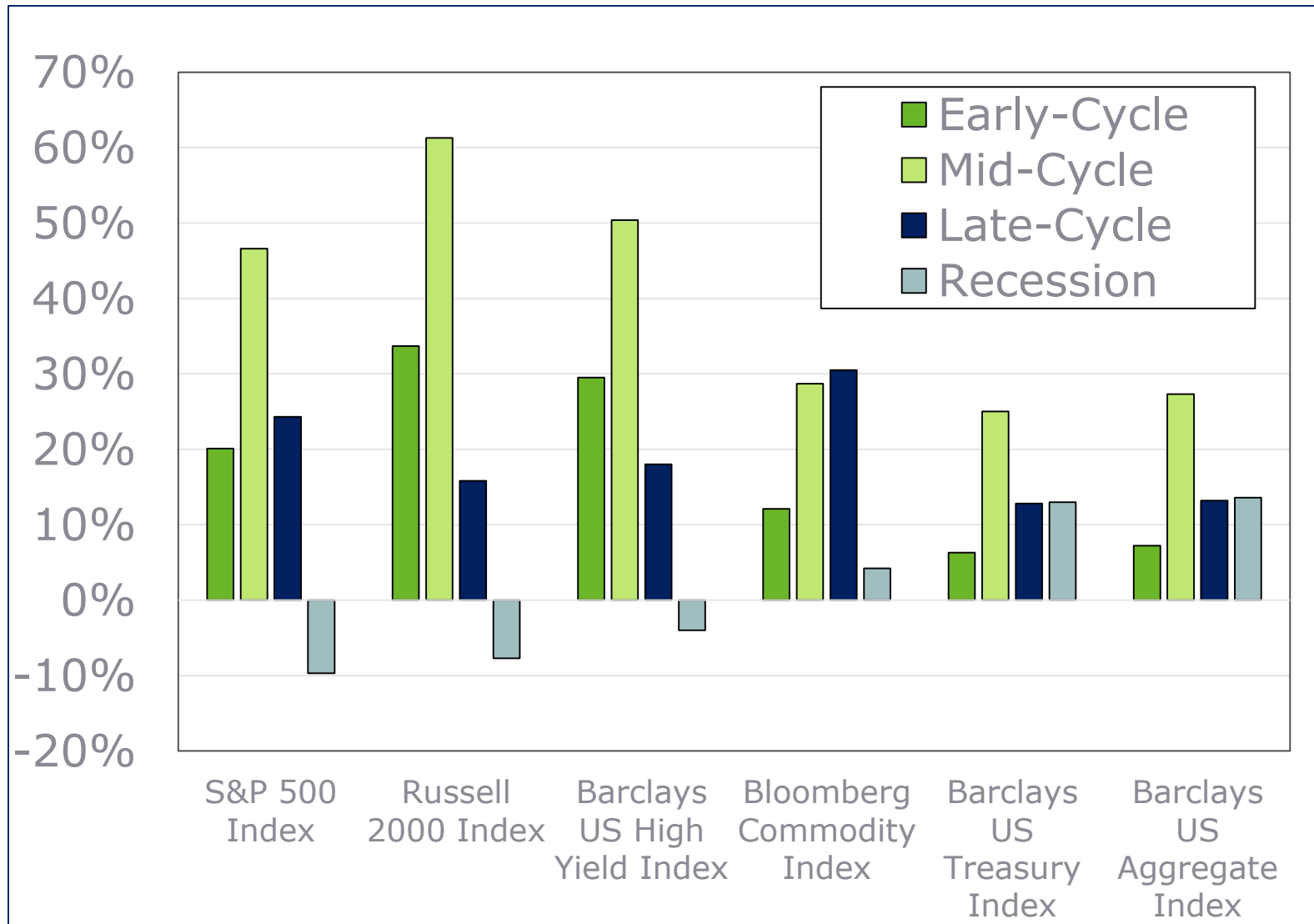
Source: Bloomberg, NEPC



# CHOPPINESS IS TYPICAL IN LATE CYCLE



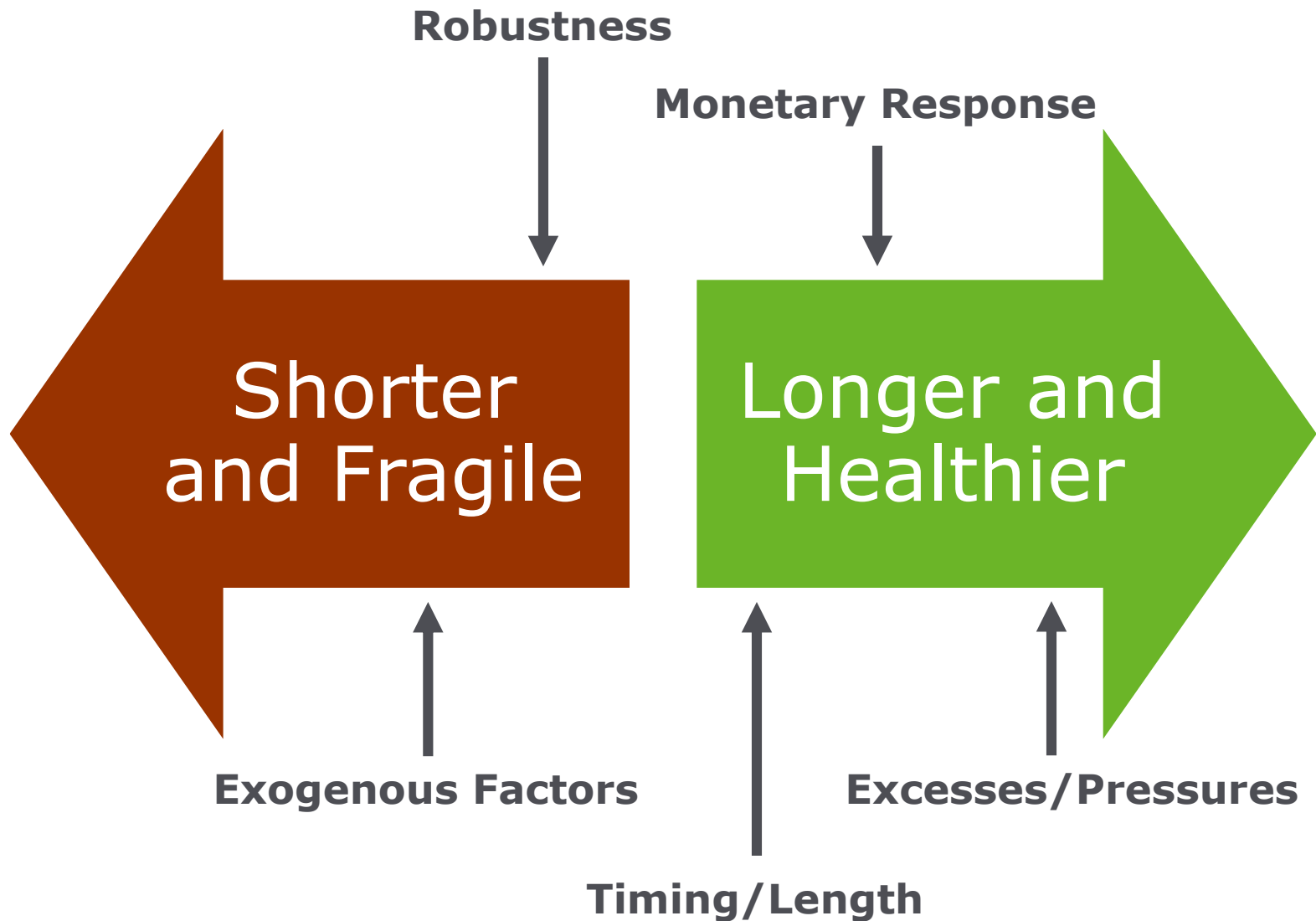
# MONEY TO BE MADE IN THE LATE CYCLE...



# EVERY LATE CYCLE IS UNIQUE

- **Robustness**
- **Excesses/Pressures**
- **Monetary Response**
- **Exogenous Factors**
- **Timing/Length**

# WHERE ARE WE TODAY?



# ASSET ALLOCATION ACTION LIST

- **Diversify for range of scenarios**
- **Evaluate total risk exposure**
- **Rebalance regularly**
- **Scrutinize portfolio liquidity**
- **Consider countries not in late cycle**

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