Business Cycle Update

Global economy firmly in recession, no evidence of a sharp recovery

United States

- The U.S. is firmly in the recession phase with activity hitting deeper troughs in a much shorter span of time than during typical recessions.
- A historically rapid and expansive U.S. monetary and fiscal policy response helped mitigate the most acute near-term financial-market liquidity issues and is providing a partial offset to the economic damage.
- Unlike previous recessions, the durability and shape of the recovery will also be informed by the path of the virus, related easing of restrictions, and consumers' willingness to re-engage in economic activities. The future path of the employment market remains highly uncertain even with reopening activity.
- The combination of supply-chain issues and lower demand is likely to weigh heavily on corporate profits.

Global

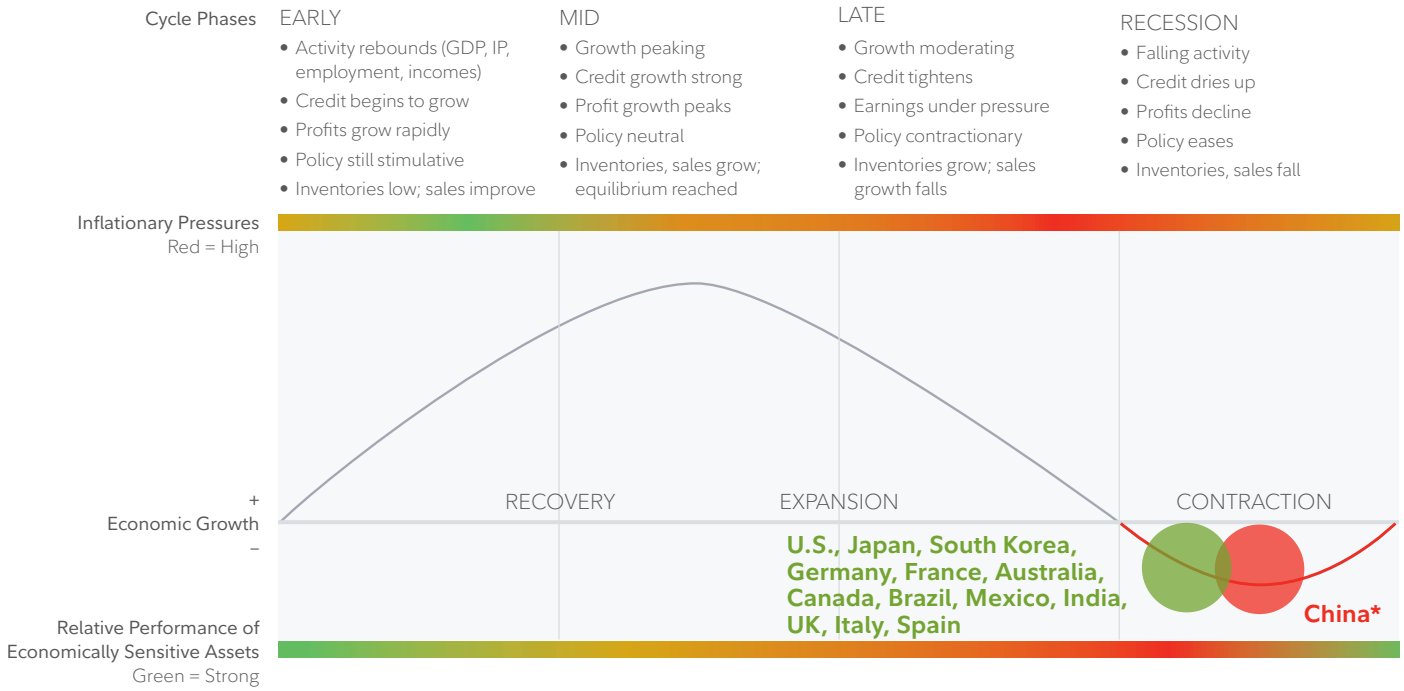
- The coronavirus shock continues to weigh heavily on global manufacturing, trade, and service activity.
- China is the furthest along in re-opening its economy, as increased mobility has coincided with improved economic activity. However, activity has recently remained range-bound and is significantly below pre-virus levels.
- China's path out of lockdown—as well as initial findings from other countries—strengthens our conviction that the path to normalcy for the U.S. and global economies will be hesitant and uneven.

Asset Allocation Outlook

- Uncertainty and volatility are likely to remain high—a more cautious near-term portfolio tilt may be warranted.
- More defensive assets such as high-quality bonds and non-cyclical equity sectors tend to do better during economic contractions.
- The end of the business cycle often provides more attractive long-term entry points.

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.



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. *A growth recession is a significant decline in activity relative to a country's long-term economic potential. We use the "growth cycle" definition for most developing economies, such as China, because they tend to exhibit strong trend performance driven by rapid factor accumulation and increases in productivity, and the deviation from the trend tends to matter most for asset returns. We use the classic definition of recession, involving an outright contraction in economic activity, for developed economies. Source: Fidelity Investments (Asset Allocation Research Team), as of Apr. 30, 2020.

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