Business Cycle Update: Global Expansion Solid but Continues to Mature

United States

- Broad-based U.S. growth implies a low probability of recession, and the U.S. remains in a prolonged shift between the mid- and late-cycle phases of economic expansion.
- Profit growth and credit trends have yet to show the signs of significant deterioration that typically occur during the late stage of the business cycle.
- However, U.S. labor market tightness is supporting wage pressures, which act as a restraint on profit margins and should give the Federal Reserve (Fed) further confidence to continue to tighten monetary policy.

Global

- The global expansion remains steady and relatively synchronized across major economies.
- Broadly speaking, most developed economies have low recession risk and are in more mature (mid-to-late) stages of the business cycle, with the eurozone enjoying above-trend growth in both core and periphery countries.
- China's economy remains in an expansionary phase, but policy-makers' continued tightening stance has begun to affect growth. Activity in the property and industrial sectors has softened over the last several months, and we believe China is poised to decelerate.
- Overall, the global expansion is on firm ground, but maturing cycles imply that inflationary pressures are building and peak activity levels have probably already been reached.

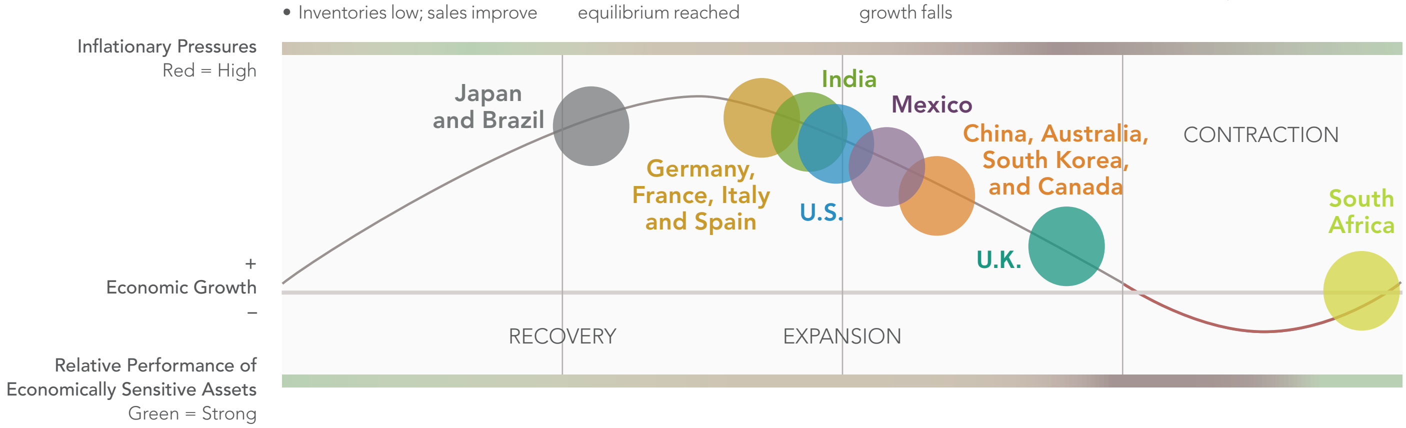
Asset allocation outlook

- We continue to favor global equities in an environment of steady growth, low inflation, and significant monetary accommodation.
- However, we believe the world is in the midst of a slow transition toward a less accommodative monetary policy stance, global activity is likely peaking, the U.S. business cycle continues to mature, asset valuations are generally elevated, and geopolitical risks are rising.
- We anticipate that firming global inflation will foster the shift toward monetary policy tightening, leading to slower liquidity growth and higher volatility in the financial markets. Therefore, smaller cyclical tilts are warranted, in addition to thorough portfolio diversification that includes international equities and inflation-resistant assets.

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 March 5, 2018.

[See related reports from Fidelity's Asset Allocation Research Team (AART), including "The Business Cycle Approach to Asset Allocation" (Jan. 2017) and "Still a Good Time for International Equities" (Feb. 2017).]

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Stock markets, especially non-U.S. markets, are volatile and can decline significantly in response to adverse issuer, political, regulatory, market, or economic developments. Foreign securities are subject to interest rate, currency exchange rate, economic, and political risks, all of which are magnified in emerging markets.

Investing involves risk, including risk of loss.

Past performance is no guarantee of future results.

Diversification and asset allocation do not ensure a profit or guarantee against loss.

All indices are unmanaged. You cannot invest directly in an index.

The Business Cycle Framework depicts the general pattern of economic cycles throughout history, though each cycle is different; specific commentary on the current stage is provided in the main body of the text. In general, the typical business cycle demonstrates the following:

During the typical **early-cycle phase**, the economy bottoms out and picks up steam until it exits recession, then begins the recovery as activity accelerates. Inflationary pressures are typically low, monetary policy is accommodative, and the yield curve is steep. Economically sensitive asset classes such as stocks tend to experience their best performance of the cycle. • During the typical **mid-cycle phase**, the economy exits recovery and enters into expansion, characterized by broader and more self-sustaining economic momentum but a more moderate pace of growth. Inflationary pressures typically begin to rise, monetary policy becomes tighter, and the yield curve experiences some flattening. Economically sensitive asset classes tend to continue benefiting from a growing economy, but their relative advantage narrows. • During the typical **late-cycle phase**, the economic expansion matures, inflationary pressures continue to rise, and the yield curve may eventually become flat or inverted. Eventually, the economy contracts and enters recession, with monetary policy shifting from tightening to easing. Less economically sensitive asset categories tend to hold up better, particularly right before and upon entering recession.

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