

# Six things you should know about market cycles

---

When markets are volatile and the economy shows signs of weakness, investors start to wonder about the security of their investments. What stage are we at in the business cycle? How does this relate to equity returns?

In this paper, we review the relationship between the economy, the US presidential election cycle and equity market returns; we explore the value vs. growth debate, and we revisit the case for equity investing. Based on two centuries of market data, we conclude with the following:

- 1. Business cycles are a fact of life.**
- 2. A bear market typically precedes an economic downturn by three to nine months.**
- 3. It is exceedingly difficult to predict when shifts in markets will take place.**
- 4. Diversify.**
- 5. Mutual funds provide easy diversification.**
- 6. In spite of all the cycles, equities are the best performing asset class over the long term.**

## Where are we headed from here?

Over the past six years, the Canadian stock market was one of the best performing in the world. From its low in October 2002 to its high in June 2008, the S&P/TSX Composite Index rose a total of 165%. Thanks to voracious demand from Asia, the prices for commodities (oil, steel, potash) soared and pulled the Canadian market along with them. The Canadian dollar achieved parity with the US dollar and at one point, traded as high as US\$1.10.

Then in September/October 2008, these trends quickly reversed. Along with the rest of the world, the Canadian market tumbled. From its high on June 18 of 15,073, the S&P/TSX fell to 8,537, a correction of 43%. The Canadian dollar fell from 98.2 cents US to 77.6 cents over the same period, a drop of 21%. The US subprime crisis, which had been brewing for sometime, became a global credit crisis, dragging down global markets as large US financial institutions started to fail.

Investors have lost confidence, with millions of people pulling their money out of equity markets. Talk of a prolonged and nasty recession abound. The blame game continues: mortgage brokers, bankers who put the deals together, the US government that encouraged subprime lending and the Federal Reserve who failed to provide appropriate supervisory oversight of the major money centres.

Investors want to know where the economy and financial markets are headed. How bad will it get? How

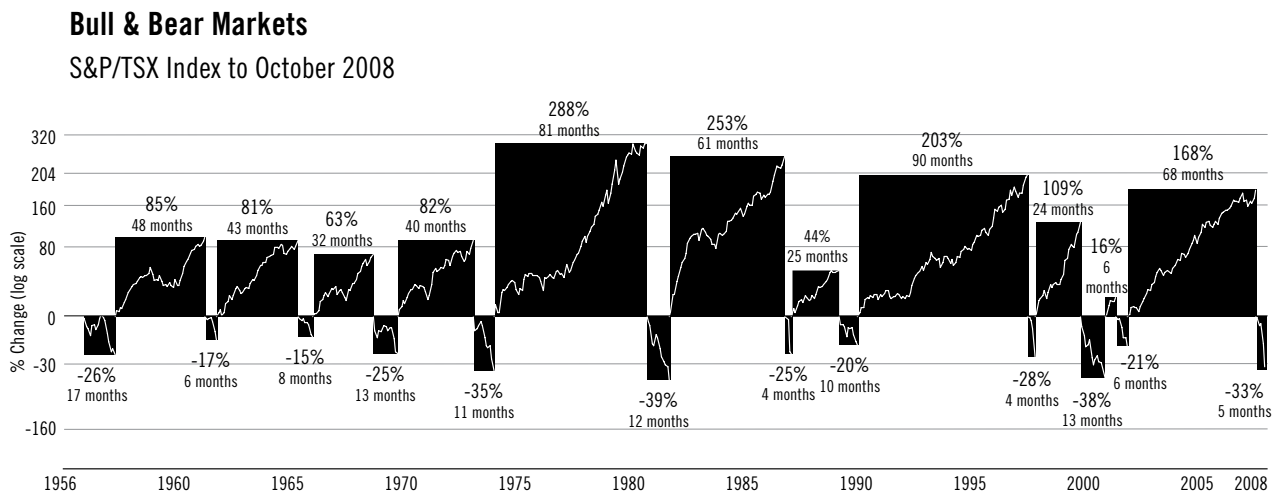
long will it last? What else can governments do? While recessions are unpredictable, those who know how markets and business cycles work understand that no trend lasts forever.

The stock market's cyclical nature demands a recovery at one point, though no one can accurately predict when things will turn around. For any market, the challenge is in forecasting how long each phase of the cycle lasts and which events will trigger a change in direction. However, if investors recognize that markets follow a recurrent pattern, they can better manage their expectations and emotions during difficult times.

## Now what?

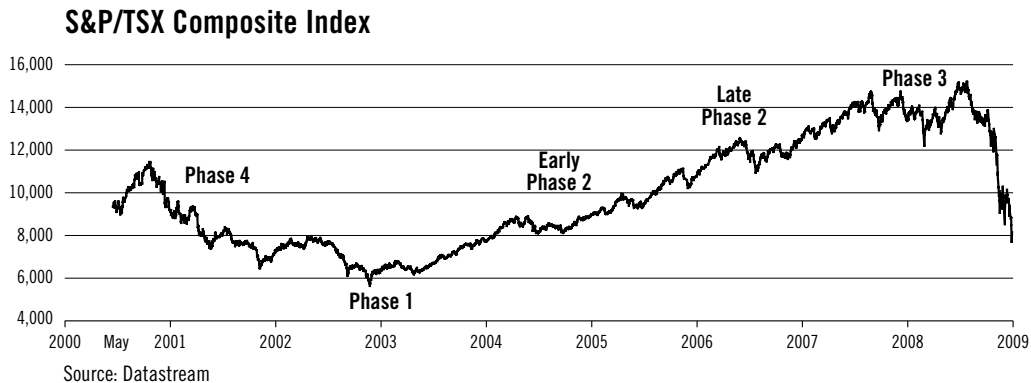
Cycles in the stock market are recurrent but not predictable. That means they follow a sequence of events over and over again, but these events are not repeated at regular intervals. In Canada, we had a bull market that lasted 90 months from 1990 to 1995, followed by a 4-month bear market in 1995. The market went up again for 24 months, down for 13, up for 6, down for 6, and from a bottom in October 2002, it went up for 68 months until June 2008.

As of November 2008, the Canadian market had been on a bearish trend for five months and counting. Our market is likely in Phase 4 – investors are feeling fearful with many capitulating. Markets are trying to find a bottom, making this a period of intense speculation about how much longer it will be until the market finally turns around.



Source: Mackenzie Financial (Datastream, October 31, 2008)

If one divides the stock market cycle into four phases, where are we in the current cycle?



**Phase 1**

- Market has bottomed
- Investors are bearish
- Smart money starts to buy

**Early Phase 2**

- Market is stable
- Prices are slowly rising
- Media speculates whether worst is over

**Late Phase 2**

- More investors start to jump in
- Valuations rise significantly
- Market is euphoric

**Phase 3**

- Investors have mixed feelings
- Market gets more volatile
- Sentiment changes – often quickly – to bearish tone

**Phase 4**

- Market starts clear downward trend
- Investors are fearful and capitulate
- Market reaches a bottom

**Bear markets are short**

In North America, bear markets have been relatively short. Since 1956, there have been 11 bull markets and 12 bear markets in Canada, with the average bear market lasting nine months. In the US, there have been 10 bull markets and 11 bear markets, with the average bear market lasting 14 months.

**What is a bear market?**

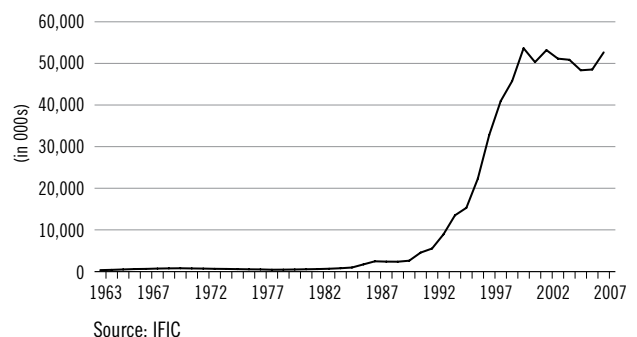
A bear market is characterized by declines of more than 20% across the board for a period of at least nine months.

Average bear market duration: 9 months Average loss: -27%  
 Average bull market duration: 47 months Average gain: 127%

For the vast majority of investors in Canada, this will only be their second bear market experience. (The first one was 2000-2002 following the technology crash.) That's because the general population did not start participating in the stock market (through mutual funds) until 1990. According to the Investment Funds Institute of Canada, there were about 2.6 million mutual fund accounts in 1990. That figure leapt to 4.5

**Mutual Fund Accounts**

Number of Mutual Fund Accounts in Canada 1963-2007



million in 1991 and by 2000, there were 53.6 million mutual fund accounts.

The broad market decline in September and October 2008 has indeed reduced the value of many portfolios. Markets will continue to gyrate as momentary optimism creates rallies while bad economic news takes markets back down. For both novice and experienced investors, learning to manage their emotions is key. Getting professional investment advice during volatile times can help avert classic mistakes that people make during bear markets.

## How is the stock market related to the business cycle?

Like the stock market cycle, the business cycle follows a sequence of events that is recurrent but not regular. The four phases of a business cycle are contraction, trough, expansion and peak.

A growing economy means happy times for a country. It's a period of low unemployment, stable inflation, rising corporate profits, and strong stock market activity. Naturally, a recession represents the bad times. Business conditions worsen and falling employment erodes consumer confidence. Recessions are painful and distressing, which is why their arrival, length and depth are widely debated.

A recession is popularly defined as a decline in a country's gross domestic product for two or more consecutive quarters. For Statistics Canada, a recession must be a decline of substantial depth and duration. The U.S. National Bureau of Economic Research (NBER) defines a recession as the period between the time when business activity has reached its peak and starts to fall until the time when business activity bottoms out.

It turns out that the stock market is one of the best leading indicators of the business cycle. The current price of a stock reflects the future earnings potential of the firm. Investors buy more shares if they feel optimistic and sell if they feel pessimistic. In the same way, if investors anticipate economic growth, they will expect profits to improve and stock prices will rise. If they think the economy is going to enter into a recession, then profits will fall and so will stock prices.

Typically, the stock market cycle leads the business cycle by three to nine months. For instance, in the previous recession, the S&P 500 Composite Index started its decline in September 2000 (bear market) but the recession in the US did not officially begin until March 2001.

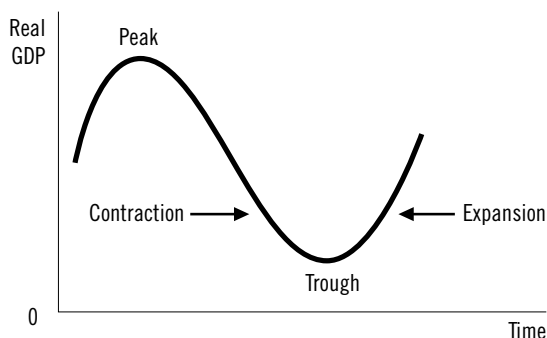
According to the NBER, the US has never had a recession without a major bear market preceding it. However, there have been major bear markets in the US, which weren't closely followed by a recession. One example was the stock market crash in October 1987. In both Canada and the US, the markets fell by almost 23% in one day. There were fears of an economic depression but instead, the economy continued to grow into the first months of 1990 before contracting.

Today, with global markets down about 40% over the past year, it's clear that a number of developed economies are headed for a recession. The questions – which won't be answered until it's all over – are: When did it start and end? How much did each economy contract?

## Can the presidential election cycle predict market direction?

The presidential election cycle theory says that stock prices in the US are weakest in the first two years following a presidential election and strongest in the last two years. More specifically, it says that stock prices decline in the first year after the presidential election, reach a trough in the second year, and peak either in the third or fourth year.

### Four Phases of a Business Cycle



#### Contraction (Recession)

- Businesses spend less
- Workers face lay-offs
- Overall economic activity slows down

#### Trough (the Low Point)

- Relatively high unemployment rates
- Annual incomes decline
- Overproduction
- This period can last from several weeks to many months

#### Recovery/Expansion

- Business begins to improve a little
- More workers are hired
- Consumer spending rises, furthering business activity

#### Peak (the High Point)

- Employment, consumer spending and production are at their highest level
- A period of prosperity especially if it's long term
- At one point, demand will start to fall

Because investors are unsure of the president's agenda, they are anxious during the first two years of a president's term. In these first two years, the administration usually introduces changes in policy as well as tough new measures, such as budget cuts, higher taxes and interest rate hikes.

Historically by the third year, the policies are in place and the president switches to a more favourable agenda – increased spending, tax cuts and lower interest rates. This stable environment starts the economy humming and usually in the third year, the US stock market

enjoys its best time as investors anticipate a brighter economy. By election day, both the economy and markets are in fairly good shape.

How well does the theory stand up? Given the severe financial crisis preceding the 2008 presidential elections, the theory failed to live up to expectations. Over the long term, however, the presidential election cycle is more compelling.

Here's data from *Stock Trader's Almanac* (2009) starting from 1902 for the Dow Jones Industrial Average:

4-Year Cycle Beginning	Elected President	Post-Election Year (1)	Mid-Term Year (2)	Pre-Election Year (3)	Election Year (4)
2005	G.W. Bush	0.6	16.3	6.4	-29.6 <sup>1</sup>
2001*	G.W. Bush	-7.1	-16.8	25.3	3.1
1997	Clinton	22.6	16.1	25.2	-6.2
1993*	Clinton	13.7	2.1	33.5	26.0
1989	G.H.W. Bush	27.0	-4.3	20.3	4.2
1985	Reagan	27.7	22.6	2.3	11.8
1981*	Reagan	-9.2	19.6	20.3	-3.7
1977*	Carter	-17.3	-3.1	4.2	14.9
1973	Nixon***	-16.6	-27.6	38.3	17.9
1969*	Nixon	-15.2	4.8	6.1	14.6
1965	Johnson	10.9	-18.9	15.2	4.3
1961*	Kennedy**	18.7	-10.8	17.0	14.6
1957	Eisenhower	-12.8	34.0	16.4	-9.3
1953*	Eisenhower	-3.8	44.0	20.8	2.3
1949	Truman	12.9	17.6	14.4	8.4
1945	F. Roosevelt	26.6	-8.1	2.2	-2.1
1941	F. Roosevelt	-15.4	7.6	13.8	12.1
1937	F. Roosevelt	-32.8	28.1	-2.9	-12.7
1933*	F. Roosevelt	66.7	4.1	38.5	24.8
1929	Hoover	-17.2	-33.8	-52.7	-23.1
1925	Coolidge	30.0	0.3	28.8	48.2
1921*	Harding	12.7	21.7	-3.3	26.2
1917	Wilson	-21.7	10.5	30.5	-32.9
1913*	Wilson	-10.3	-5.4	81.7	-4.2
1909	Taft	15.0	-17.9	0.4	7.6
1905	T.Roosevelt	38.2	-1.9	-37.7	46.6
1901	McKinley**	-8.7	-0.4	-23.6	41.7
<b>Total Gains (1902-2008)</b>		<b>First 2 years: 235.6%</b>		<b>Last 2 years: 546.9%</b>	

\* Party in power ousted

\*\* Death in office

\*\*\* Resigned

<sup>1</sup> Year-to-date to Oct. 31, 2008

Source: Stock Trader's Almanac 2009

Over the last hundred years (1902-2008<sup>1</sup>), the total returns from the first two years of a presidential term was less than half of the total return from the last two years (236% vs. 547%). If we only looked at the postwar period (1946-2008), the numbers are even more interesting: a total return of 166% for the first half and 339% for the second half.

Since 1939, the Dow Jones Industrial Average has yet to post a negative return in the third year of the presidential election cycle. In fact, the average return for the third year has been 17.6% since 1943.

While the pattern does not repeat itself exactly, it's something worthwhile for investors to keep in mind through each year of the four-year cycle. The theory would predict weaker performance for US stock markets in 2009 and 2010, with better markets in 2011 and 2012. But given the substantial market correction we've already seen, this time the future may unfold differently than the presidential election cycle theory would suggest. In other words, don't be too quick to write off 2009 and 2010.

## What's up next? Growth or Value?

Warren Buffett, perhaps the most successful investor in history, is a value investor. Since 1965, Buffett's holding company, Berkshire Hathaway has averaged an annual return of 21.1%. For Buffett, whose current net worth is over \$62 billion<sup>2</sup>, value investing will never go out of style even when the markets favour growth investing as they did in the late 1990s.

Value investors tend to be bargain hunters who look for companies that are selling for less than their estimated values. Value stocks are generally concentrated in the financial, consumer staples, utility, energy and materials sectors.

Growth investors tend to look for steadily growing companies and/or companies with the potential for strong earnings growth in the future. Growth stocks are typically represented in areas such as consumer discretionary, healthcare, media, telecom and technology.

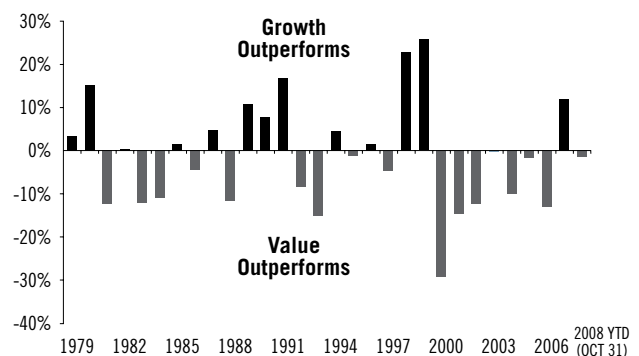
Given the long-term success of investors like Buffett, value investing is often viewed as a style that's superior

to growth. When you examine historical trends though, you can see that the growth and value styles of investing exchange leadership over time.

In his book, *Common Sense on Mutual Funds*, John C. Bogle looked at growth and value mutual funds from 1937 to 1997. From 1937 to 1968, growth mutual funds outperformed value funds. But value dominated from 1968 to 1976, after which growth took leadership again until 1980. From 1980 to 1997, value was again at the forefront. In terms of performance, Bogle found that for the full 60-year period, the compound total return for growth funds was 11.7% and for value, 11.5%.

Most investors remember the late 1990s when growth investing – powered by technology stocks – significantly outperformed value. Since 2003, however, value companies (often in sectors with traditionally lower price-to-book ratios such as energy and materials) have outperformed.

## Russell Growth 1000 vs. Russell Value 1000



Source: Datastream

In the 2008 credit crisis, both value and growth styles lost significant ground. Leading up to this correction, there was a good argument in favour of growth investing, as the performance of value had been two standard deviations above the norm for two years. In other words, growth investing was due to break out. It is impossible to say whether the dramatic market events mean that a "reset" button has been pressed and that all bets are off as far as investing style is concerned, or whether we will eventually see growth investing take the lead. Investors would be well served by following

<sup>1</sup> For 2008, the number are year-to-date to Oct. 31, 2008

<sup>2</sup> Kroll, Luisa, ed. "The World's Billionaires." *Forbes*, 5 March 2008  
[http://www.forbes.com/2008/03/05/richest-people-billionaires-billionaires08-cx\\_k\\_0305billie\\_land.html](http://www.forbes.com/2008/03/05/richest-people-billionaires-billionaires08-cx_k_0305billie_land.html)

managers known for sticking to their investment style, whether that style be growth or value, and perhaps diversifying over more than one investment style.

## Which sector and country will lead next year?

Hong Kong and Finland were not major financial newsmakers in 2007 and yet they were the top two performers among developed countries that year. According to the MSCI Country Indices, Hong Kong's one-year return was 37.8% while Finland's was 30.8% in 2007.

Meantime, emerging markets – which were among the worst performing group in the mid-to-late 1990s – had been on a blistering pace in the last few years. Their markets were the top performers in 2004, 2005,

2006 and 2007 with returns of 16.8%, 31.2%, 32.1% and 18.6% respectively but had dropped precipitously towards the end of 2008.<sup>3</sup>

Other commodities, sectors and countries also go through cycles of positive and negative returns, taking turns in leading the way. From the chart below, you can see that out of the 15 years between 1994 and 2008<sup>4</sup>, emerging markets has been at the top five times and at the bottom six times. US large caps took the number-one spot three times and the group was the bottom performer also three times.

In the last 15 years, Canadian large caps have been all over the chart. As various sectors and countries exchange leadership over time, it is impossible to guess which one will dominate in the coming year.

### “Predicting the winner is difficult” (current to October 2008<sup>4</sup>)

1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
Foreign Equities 14.5%	US Large Cap 33.9%	Cdn. Large Cap 28.7%	US Large Cap 39.2%	US Large Cap 37.7%	Emerging Markets 57.2%	Cdn. Bonds 10.3%	US Small Cap 8.8%	Cdn. Bonds 8.7%	Cdn. Small Cap 42.7%	Emerging Markets 16.8%	Emerging Markets 31.2%	Emerging Markets 32.1%	Emerging Markets 18.6%	Cdn. Bonds 1.0%
Global Equities 11.9%	US Small Cap 24.9%	Cdn. Small Cap 28.4%	US Small Cap 27.7%	Global Equities 33.7%	Cdn. Large Cap 31.7%	Cdn. Large Cap 7.4%	Cdn. Bonds 8.1%	Cdn. Small Cap -0.9%	Emerging Markets 27.8%	Cdn. Large Cap 14.5%	Cdn. Large Cap 24.1%	Foreign Equities 26.8%	Cdn. Large Cap 9.8%	US Small Cap -12.6%
US Large Cap 7.4%	Cdn. Bonds 20.7%	US Large Cap 23.4%	Global Equities 21.3%	Foreign Equities 28.9%	Cdn. Small Cap 20.3%	Cdn. Small Cap 7.3%	Emerging Markets 3.8%	Emerging Markets -7.0%	Cdn. Large Cap 26.7%	Cdn. Small Cap 14.1%	Cdn. Small Cap 19.7%	Global Equities 20.6%	Cdn. Bonds 3.7%	US Large Cap -17.3%
US Small Cap 4.0%	Global Equities 18.1%	US Small Cap 16.9%	Cdn. Large Cap 15.0%	Cdn. Bonds 9.2%	Foreign Equities 20.1%	US Small Cap 0.8%	Cdn. Small Cap 3.4%	Cdn. Large Cap -12.4%	US Small Cap 20.5%	Foreign Equities 12.4%	Foreign Equities 10.5%	US Small Cap 18.3%	Cdn. Small Cap 2.0%	Global Equities -24.0%
Cdn. Large Cap -0.2%	Cdn. Large Cap 14.5%	Global Equities 14.4%	Cdn. Bonds 9.6%	US Small Cap 4.4%	Global Equities 18.2%	US Large Cap -5.5%	US Large Cap -6.5%	Foreign Equities -16.4%	Foreign Equities 13.9%	US Small Cap 10.2%	Global Equities 6.6%	Cdn. Large Cap 17.3%	Foreign Equities -5.3%	Cdn. Large Cap -27.8%
Emerging Markets -1.8%	Cdn. Small Cap 13.9%	Cdn. Bonds 12.3%	Cdn. Small Cap 7.0%	Cdn. Large Cap -1.6%	US Small Cap 14.4%	Global Equities -9.5%	Global Equities -11.4%	Global Equities -20.2%	Global Equities 9.4%	Global Equities 7.3%	Cdn. Bonds 6.5%	Cdn. Small Cap 16.6%	Global Equities -7.1%	Int'l Equities -30.1%
Cdn. Bonds -4.3%	Foreign Equities 8.6%	Foreign Equities 6.7%	Foreign Equities 6.5%	Cdn. Small Cap -17.9%	US Large Cap 14.2%	Foreign Equities -10.6%	Cdn. Large Cap -12.6%	US Small Cap -21.1%	Cdn. Bonds 6.7%	Cdn. Bonds 7.2%	US Large Cap 1.6%	US Large Cap 15.7%	US Large Cap -10.6%	Emerging Markets -42.2%
Cdn. Small Cap -8.6%	Emerging Markets -7.8%	Emerging Markets 6.6%	Emerging Markets -7.7%	Emerging Markets -19.9%	Cdn. Bonds -1.1%	Emerging Markets -28.2%	Foreign Equities -16.4%	US Large Cap -22.7%	US Large Cap 5.3%	US Large Cap 3.3%	US Small Cap 1.3%	Cdn. Bonds 4.1%	US Small Cap -16.5%	Cdn. Small Cap -44.1%

Source: Globe HySales

**Canadian Bonds:** Dex Universe Bond Total Return Index

**Canadian Large Cap:** S&P/TSX Total Return Index

**Canadian Small Cap:** BMO Nesbitt Burns Cdn Small Cap Index

**Emerging Markets:** MSCI Emerging Markets Free Index (\$Cdn)

**Global Equities:** MSCI World Index (\$Cdn)

**Foreign Equities:** MSCI EAFE Index (\$Cdn)

**US Large Cap:** S&P 500 Total Return Index (\$Cdn)

**US Small Cap:** Russell 2000 Index (\$Cdn)

<sup>3</sup> Canadian Small Cap: BMO Nesbitt Burns Cdn Small Cap Index

<sup>4</sup> 2008 data is year to date to Oct. 31, 2008

## Why is it so hard to predict the market?

Take hundreds of millions of investors, add in market risks, throw in some herd mentality and a splash of overreaction, and what you get is unpredictability.

Besides the large number of participants in the market, there are also scores of uncertainties that they are trying to measure. At the present time, investors are grappling with the global economic crisis, the sudden tightening of credit markets after years of excess liquidity, and the widely anticipated worldwide recession.

It is impossible to know where the market is headed. Most individual investors are inexperienced when it comes to the market, and sooner or later, they fall prey to the herd mentality: when times are good, they buy what everyone else is buying. But when bubbles burst, they rush for the exits, causing markets to plummet.

Despite this, many investors still believe they have the ability to forecast the future. They chase performance when the markets are optimistic, believing good times are here to stay. And when times are bad, they tend to assume that bad times will also last forever, and misjudge how quickly trends can change.

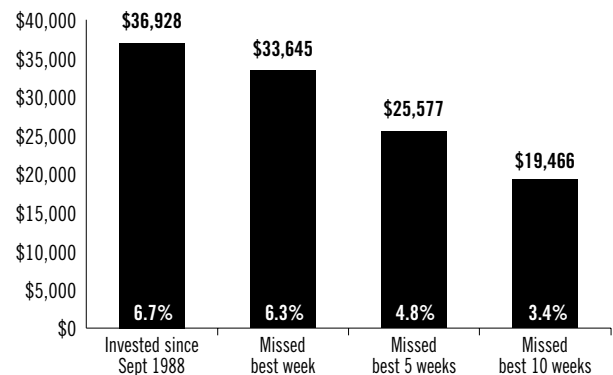
The last time this happened was following the technology crash. In 2001 and 2002, many Canadians saw their portfolios shrink significantly following the crash. Like the recent market downturn, that crash was dramatic in its speed and intensity. Discouraged, many investors abandoned the stock market throughout 2002 and 2003. And of course, 2003 was an excellent year for the Canadian stock market, with the S&P/TSX Composite posting 26.7% by the end of the year.

Staying invested in the market regardless of market conditions turns out to be one of the best long-term strategies for investors to abide by. There will always be uncertainty in the market and waiting on the sidelines could mean a missed opportunity. Past history has shown that trends can reverse quickly, and in reaction, investors have repeated the behaviour of the past.

From the chart below, you can see that if you had invested \$10,000 in the S&P/TSX Composite Index beginning September 1988, you would have made \$36,928 by September 30, 2008. If you took your money out and missed the best week, the return drops to \$33,645. If you missed the best 10 weeks – or 1% of the 1,040 weeks over the 20-year period – your return would only be \$19,466. Staying invested, even though it means experiencing the losses that stocks often endure, guarantees that you don't miss out on some of the best weeks in the market.

### 20 Years of the S&P/TSX You can't afford to miss the best weeks

Value of \$10,000 invested Sept 1988 to Sept 2008



Source: Datastream, S&P/TSX Price Index, Sept. 30, 2008

The other antidote to unpredictable market cycles is diversification. By owning a portfolio of different asset classes, participating in different styles of investing, and spreading their money around the world, investors can achieve, on average, higher returns and lower risk than any individual investment.

While a diversified approach will occasionally lead to lower returns than the leading category, the downside will also be less severe when the inevitable market and business cycles run their course.

## Why should you own equities?

Given the ups and downs of market cycles, along with the financial panics and economic crises, you might wonder whether you should even bother with the stock market. When you look beyond short-term swings, however, you will see that equities offer the best returns of all asset classes.

According to Jeremy Siegel, a professor of finance at the Wharton School and author of the investment classic *Stocks for the Long Run* (2002), the long-term real return on stocks after inflation has been between 6.5% and 7% a year. The average annual real return of bonds has been 3.5% – about half of real stock returns. Money market assets have averaged 2.9%.<sup>5</sup>

How does that translate into dollars over a 200-year period? If you had invested \$1 in stocks in 1802, that would have grown to \$597,485 by the end of 2003. The same dollar would have gotten you \$1,072 in bonds and \$301 in Treasury bills.

Explains Siegel, “The dominance of stocks over other assets is overwhelming. Swings in investor sentiment, as well as political and economic crises, can throw stocks off their long-term path, but the fundamental forces generating economic growth have always enabled equities to regain their footing. Despite our history of depressions, wars, financial panics, and most recently the terrorist attacks and scandals that we faced in 2001 and 2002, the resiliency of stock returns is indisputable.”<sup>6</sup>

As an equity investor then, you are theoretically entitled to a premium because you are a part owner of a business and you are risking your capital. Basically, the equity risk premium is the excess return that investors get over a risk-free rate, which is typically the interest rate on longer-term government bonds. For instance, if the risk-free rate is 5%, and the return on a stock is 13%, then the equity risk premium is 8%. The equity risk premium therefore comes in the form of a higher return. When investing in equities, most people focus on the potential for capital gains. But another reason why equities are worthwhile is income in the form

of dividends. Over time, dividends can be a major contributor to the total return. If you had invested \$10,000 in the S&P/TSX Composite Total Return Index in 1973, that money would have grown to \$241,942 by the end of Sept. 2008 – three times as much as the same amount invested in the S&P/TSX Composite Price Index (which doesn't include dividends). What's more, capital gains and dividends both provide more favourable tax treatment compared to fixed income in taxable accounts.

Finally, equities provide a hedge against inflation. Over the longer term, equities keep pace with inflation whereas fixed income and money market are hurt by inflation, sometimes resulting in negative returns.

There is no telling where the market will go tomorrow and when trends will change directions. History has shown, however, that over the long term, equities provide you with the best opportunity for investing success.

<sup>5</sup> Siegel, Jeremy J. *The Future for Investors: Why the Tried and the True Triumph Over the Bold and the New*. New York: Crown Business, 2005, 171.

<sup>6</sup> Ibid, 170.

## Summary of lessons

### **1. Business cycles are a fact of life.**

- The four phases of a business cycle are contraction, trough, expansion and peak
- This sequence of events is recurrent but not regular
- We have had a major expansion and are now entering a recession

### **2. A bear market typically precedes an economic downturn by three to nine months.**

- The stock market is one of the best leading indicators of the business cycle
- The US has never had a recession without a bear market preceding it
- Given the current bear market, we can expect a recession to follow

### **3. It is exceedingly difficult to predict when shifts in markets will take place.**

- Market trends can change swiftly and dramatically
- Investors tend to assume that current conditions will continue indefinitely
- Despite widespread gloominess, a recovery will occur

### **4. Diversify.**

- Own a portfolio of different asset classes
- Participate in both styles of investing – value and growth
- Spread your money around the world

### **5. Mutual funds provide easy diversification.**

- A single purchase in a fund lets you own a large number of securities
- There are numerous ways to diversify: by asset class, region, style, tax-efficiency, and currency
- Diversification reduces the risk in your portfolio

### **6. In spite of all the cycles equities are the best performing asset class over the long term.**

- Long-term real return on stocks after inflation has been 6.5% to 7% a year
- Compared to bonds and money markets, stocks offer the highest returns
- Stocks give you the best opportunity for investing success

## References

**Blackman, Matt.** “Understanding Cycles – The Key to Market Timing.” Investopedia. 5 May 2004  
<http://www.investopedia.com/articles/technical/04/050504.asp>

**Bogle, John C.** *Common Sense on Mutual Funds: New Imperatives for the Intelligent Investor.*  
New York: John Wiley & Sons, Inc., 1999.

**Bolten, Steven E. and Robert A. Weigand.** “The Generation of Stock Market Cycles.”  
*The Financial Review*, Vol. 33, No. 1, 1 Feb. 1998.

**Hirsch, Jeffrey A.,** *Stock Trader’s Almanac 2009.* New Jersey: John Wiley & Sons, Inc. 2008.

**Kroll, Luisa, ed.** “The World’s Billionaires.” *Forbes*, 5 March 2008  
[http://www.forbes.com/2008/03/05/richest-people-billionaires-billionaires08-cx\\_k\\_0305billie\\_land.html](http://www.forbes.com/2008/03/05/richest-people-billionaires-billionaires08-cx_k_0305billie_land.html)

**Schmitz, John J.** “Damn Yankees!...or The transmission of U.S. election cycles to international stock returns.”  
*Mackenzie Professional*, Nov 2000

**Siegel, Jeremy J.** *The Future for Investors: Why the Tried and the True Triumph.*  
New York: Crown Business, 2005.

**The Investment Funds Institute of Canada**

<http://www.ific.ca>

**Industry Statistics**

<https://statistics.ificmembers.ca/English/Reports/MonthlyStatistics.asp>

**National Bureau of Economic Research**

<http://www.nber.org>

**Statistics Canada**

<http://www.statcan.ca>

## MACKENZIE ALL-ACCESS SERVICE

To help save you time, we've made fund and account information available for you to access whenever you need through three convenient options:

**ONLINE** Get all of the information you require 24 hours a day, 7 days a week by logging into AdvisorAccess at [mackenziefinancial.com](http://mackenziefinancial.com). AdvisorAccess is a secure connection that only you can access.

For technical support, please call Client Services at  
1 800 387 0614

**TOUCH-TONE PHONE** You also have convenient and direct access to all your fund and account information by calling the Mackenzie AccessLine at  
416 922 9143 or  
1 800 440 0577

**FAX** Request a fax transmission through the Mackenzie AccessLine at  
416 922 9143 or  
1 800 440 0577

---

## GENERAL INQUIRIES

For all of your general inquiries, account details, fund information, or to order marketing literature and materials, please call:

**ENGLISH** 416 922 3217  
1 800 387 0614

**BILINGUAL** 416 920 5120  
1 800 387 0615

**ASIAN INVESTOR SERVICES** 1 888 465 1668

**FAX** 416 922 5660  
1 866 766 6623

**E-MAIL** [service@mackenziefinancial.com](mailto:service@mackenziefinancial.com)

Any statements contained herein that are not based on historical fact are forward-looking statements. Any forward-looking statements represent the best judgment as of the present date as to what may occur in the future. However, forward-looking statements are subject to many risks, uncertainties and assumptions, and are based on the present opinions and views. For this reason, the actual outcome of the events or results predicted may differ materially from what is expressed. Furthermore, the views, opinions or assumptions may subsequently change based on previously unknown information, or for other reasons. Mackenzie Financial Corporation and its affiliates assume no obligation to update any forward-looking information contained herein. The reader is cautioned to consider these and other factors carefully and not to place undue reliance on forward-looking statements.