



Brainy's Articles on Share Trading**

Investing in cyclic stocks

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page 1 of 6
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Introduction

When we make investment decisions about which stocks to include in our portfolio, there is a bewildering variety of very well-accepted approaches and strategies from which to choose.

One of these approaches considers the current state of the *business or economic cycle*, to help choose either a so-called *cyclical stock*, or a *defensive stock*, as appropriate. It all sounds good in theory. However, many investors choose to ignore the cycles, and select stocks using a type of bottom-up approach. So, which approach should we use?

This Article in Brainy's series on Share Trading and Investing (number ST-6310) discusses this very topic. The content of this Article (text and charts) is due for authorised publication by the ASX in the October 2012 edition of the monthly ASX *Investor Update* newsletter.

Cyclic investing — is easy?

The experts suggest that we could invest in shares while being mindful of the *economic cycle*. To help us visualise the cycle we could consult the infamous *investment clock*, remembering there are four key stages to the economic cycle:-

- Expansion — boom time with the economy growing in the lead up to 12 o'clock.
- The top of the boom and the economic cycle — growth starts to slow.
- Contraction — the slowdown after 12 o'clock.
- Trough and cycle bottom — and a possible recession at 6 o'clock.

The accepted economic cycle can run for as many as ten to twelve years. We might be able to work out the current time on the investment clock, and where we are along the economic cycle, but it is not easy to accurately predict how the economy will unfold in the months ahead.

There are several indicators of economic activity to help us determine the current time on the investment clock, including: Purchasing Managers Indices, US job reports, Australian labour market measures, industrial production (in China and elsewhere), global and Australian commodity prices, consumer price inflation, business confidence, consumer confidence, real estate values, interest rates and credit availability. Other signposts that we could read are the bond prices around the world, and company earnings and growth forecasts. But accessing and processing all this information is not that easy or simple.

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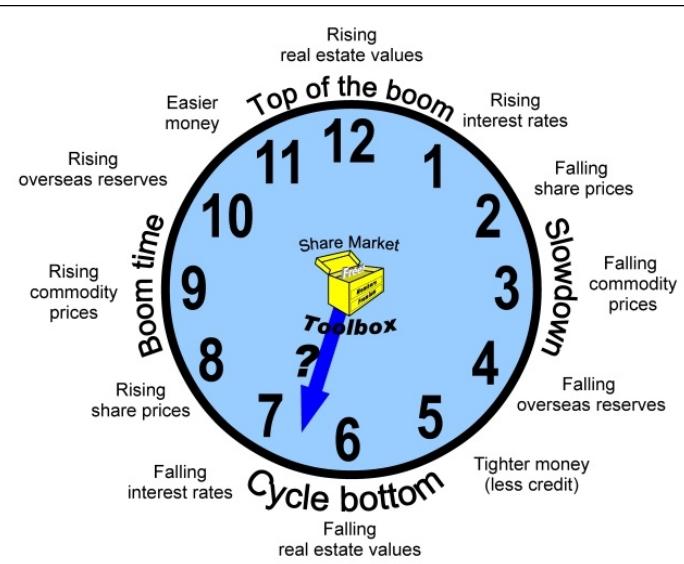


Figure 1: Investment Clock — what is the current time?

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** - The two words *trading* and *investing* are often used somewhat interchangeably.

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