Managing Risk Around the Business Cycle

Martin J. Pring

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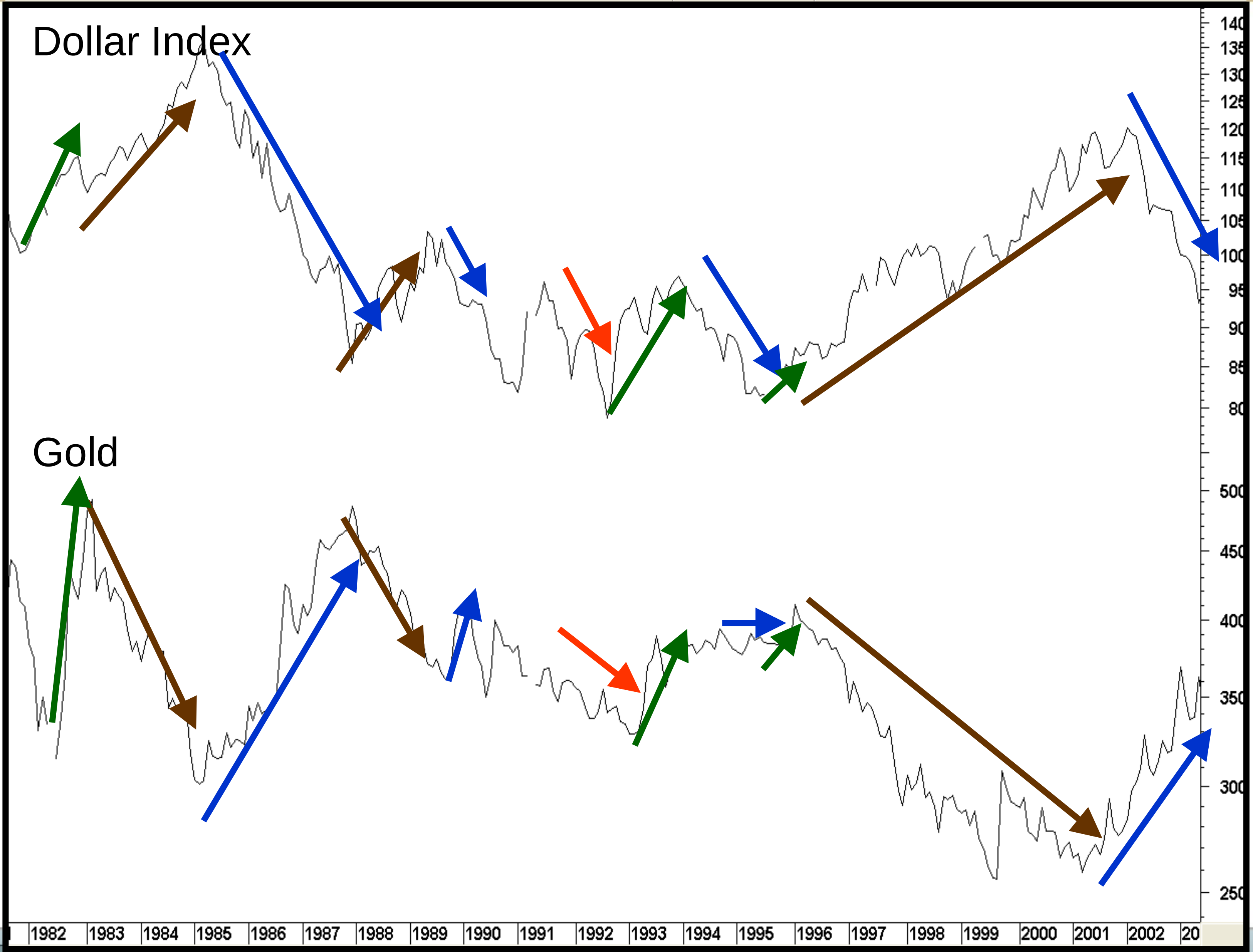
Pring Turner Capital Group

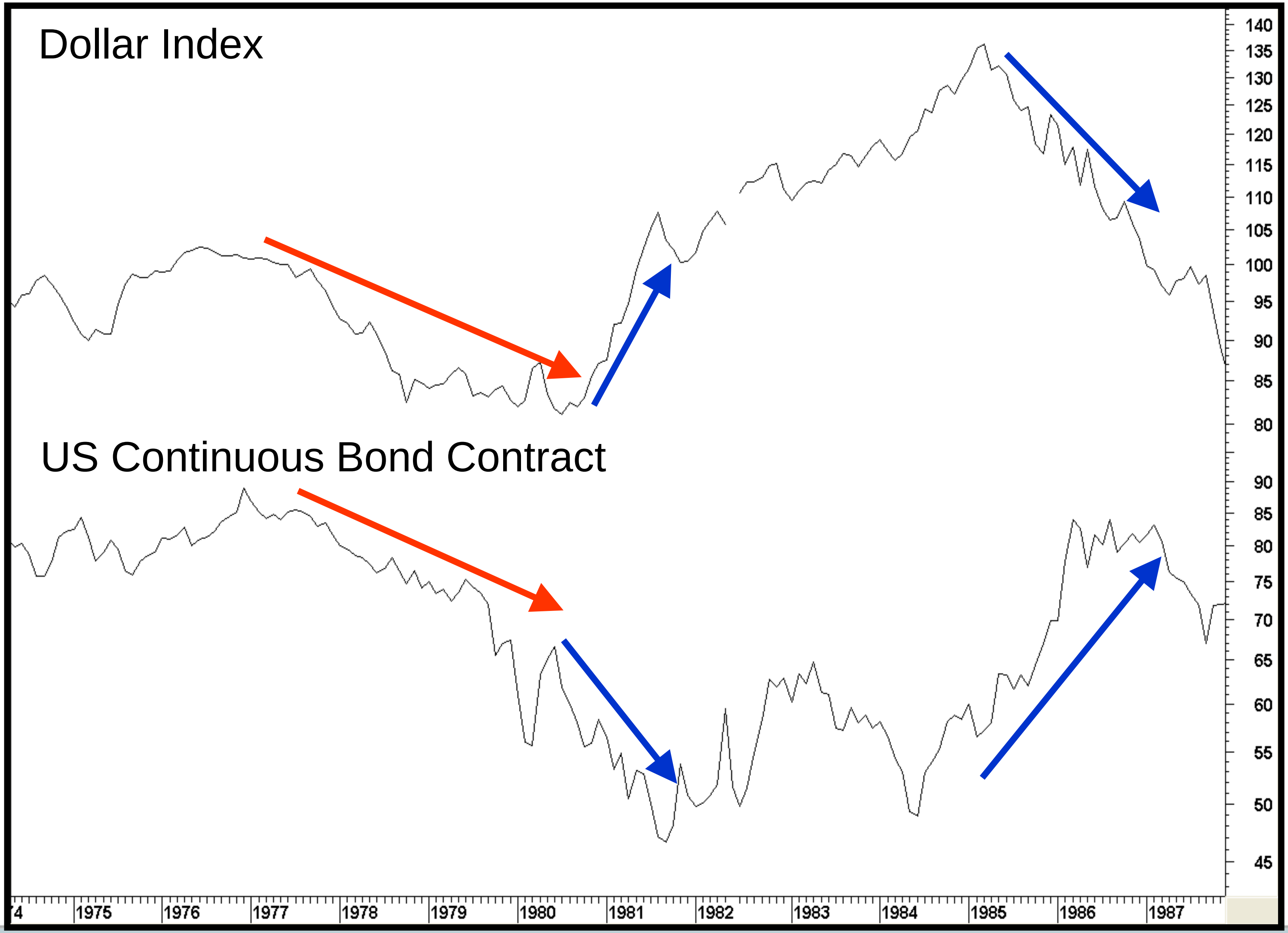
What drives markets?

Dollar Index vs Gold 1982-2003



The dollar drives gold… until it doesn't.

Dollar Index vs Bond Prices 1974-1987



The dollar drives bonds… until it doesn't.

The Dollar vs. Bonds and Gold

1. For a specific, but indefinable period of time, this intermarket relationship can be used to forecast bond and gold prices.

For certain periods, there is a definite linkage between the dollar and bonds and gold.

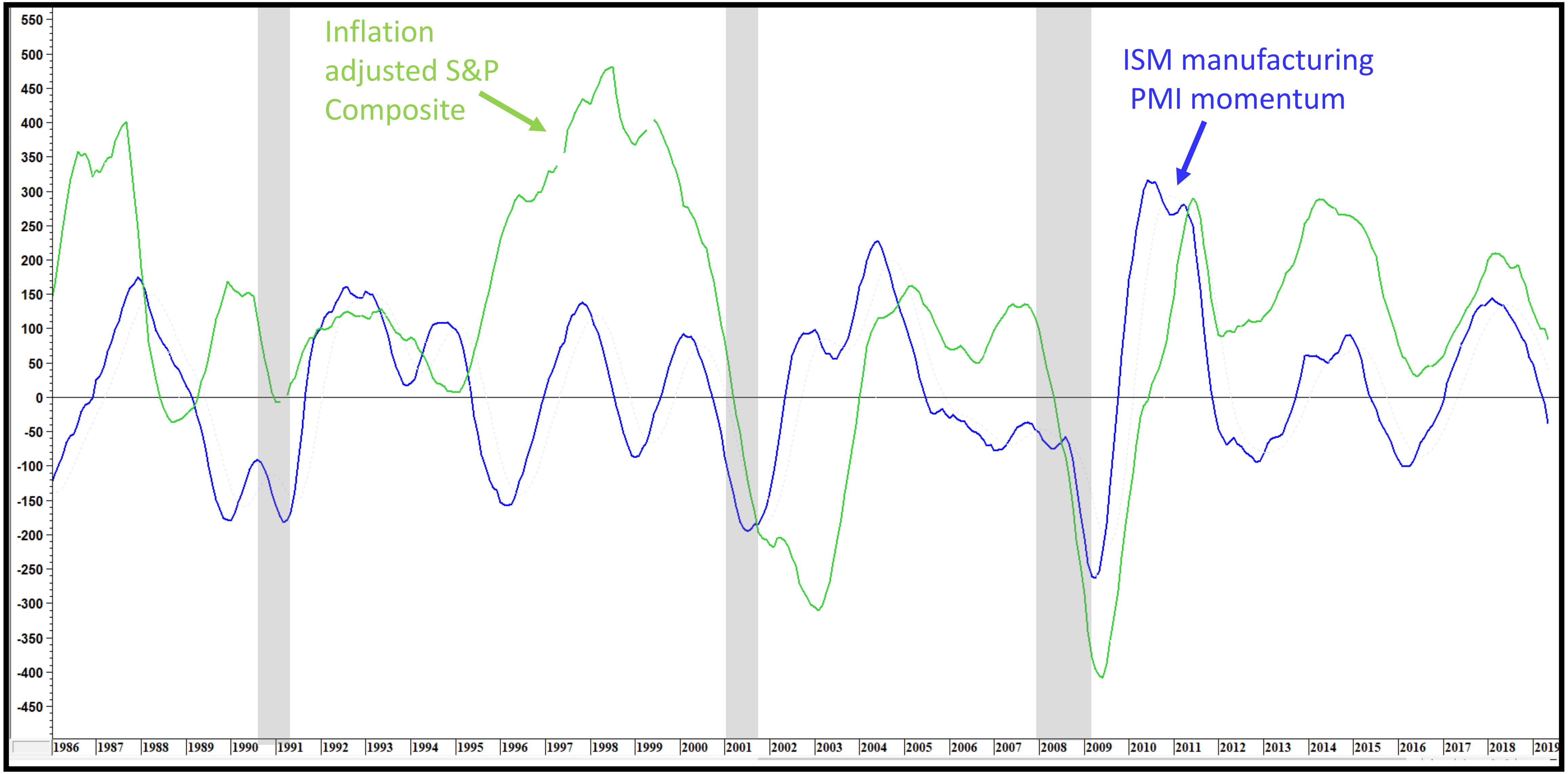
2. There is no consistent relationship between them.

3. If the dollar does not consistently drive bond and gold prices, what does?

Financial Markets and the Business Cycle

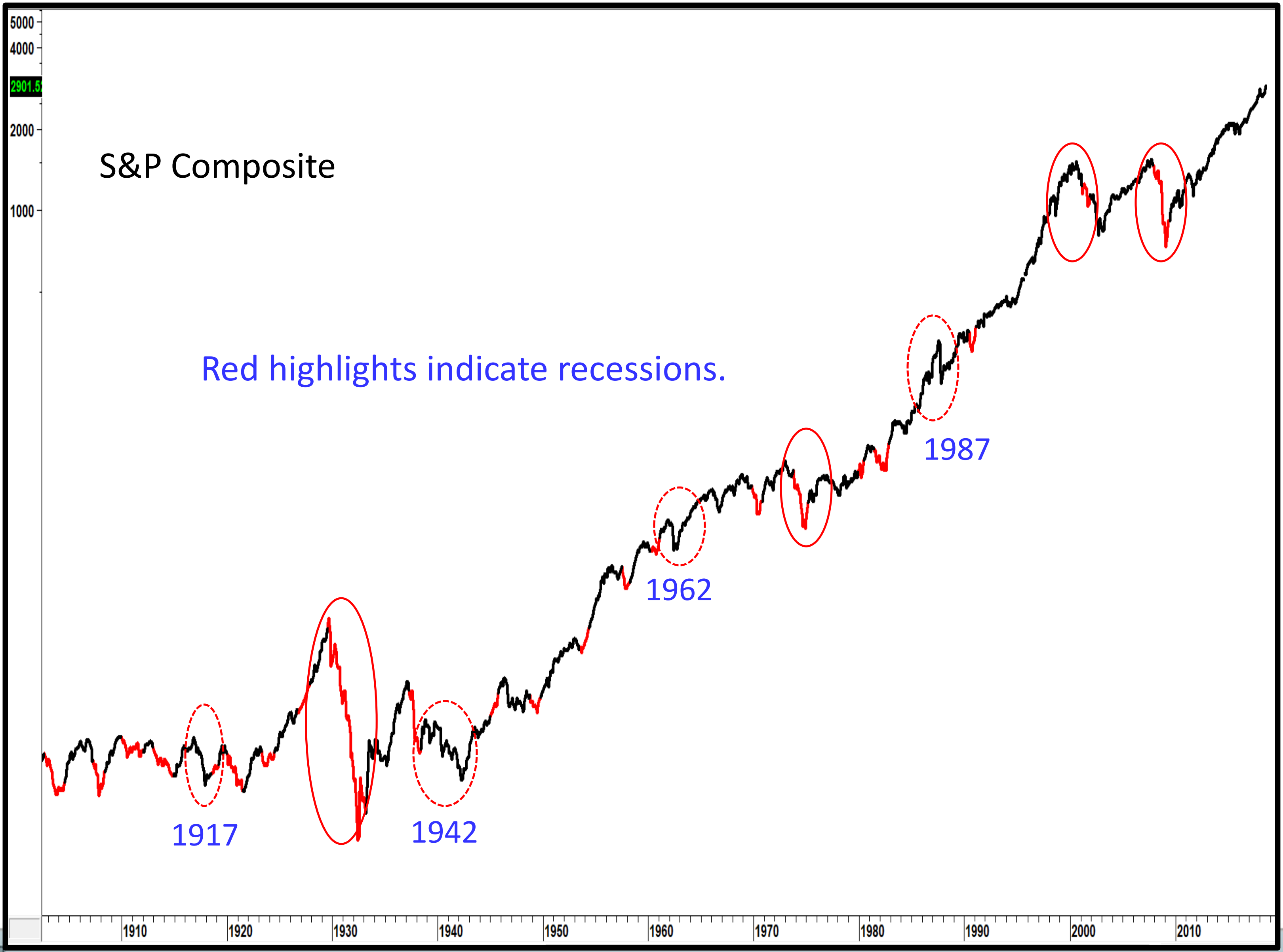
The vast majority of primary trend equity price swings can be explained by changes in the economy and investors attitudes to those changes.

S&P versus ISM Momentum 1996-2019



Normally stocks and the economy move in tandem.

S&P Composite 1900-2018



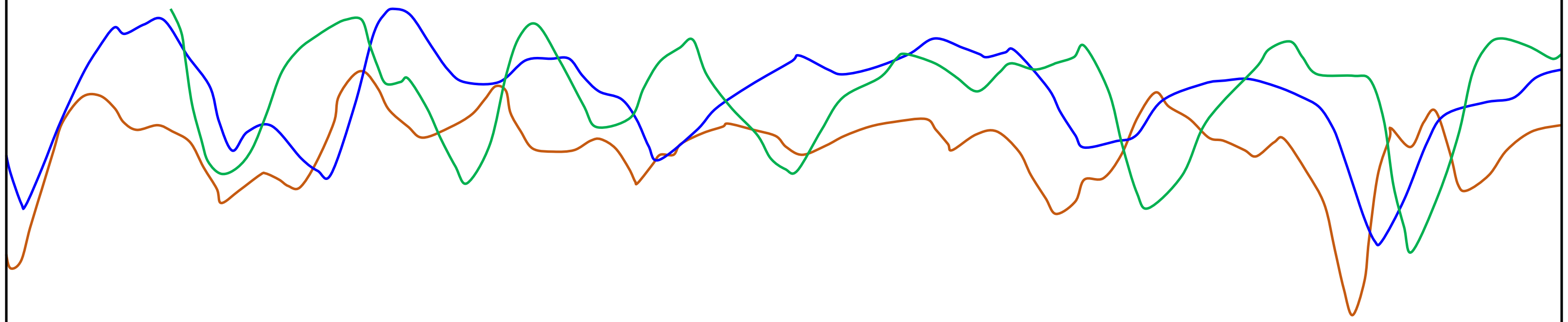
The largest declines are typically associated with recessions.

Part II
The Business Cycle—a Set Series of Chronological Events that Keep Repeating

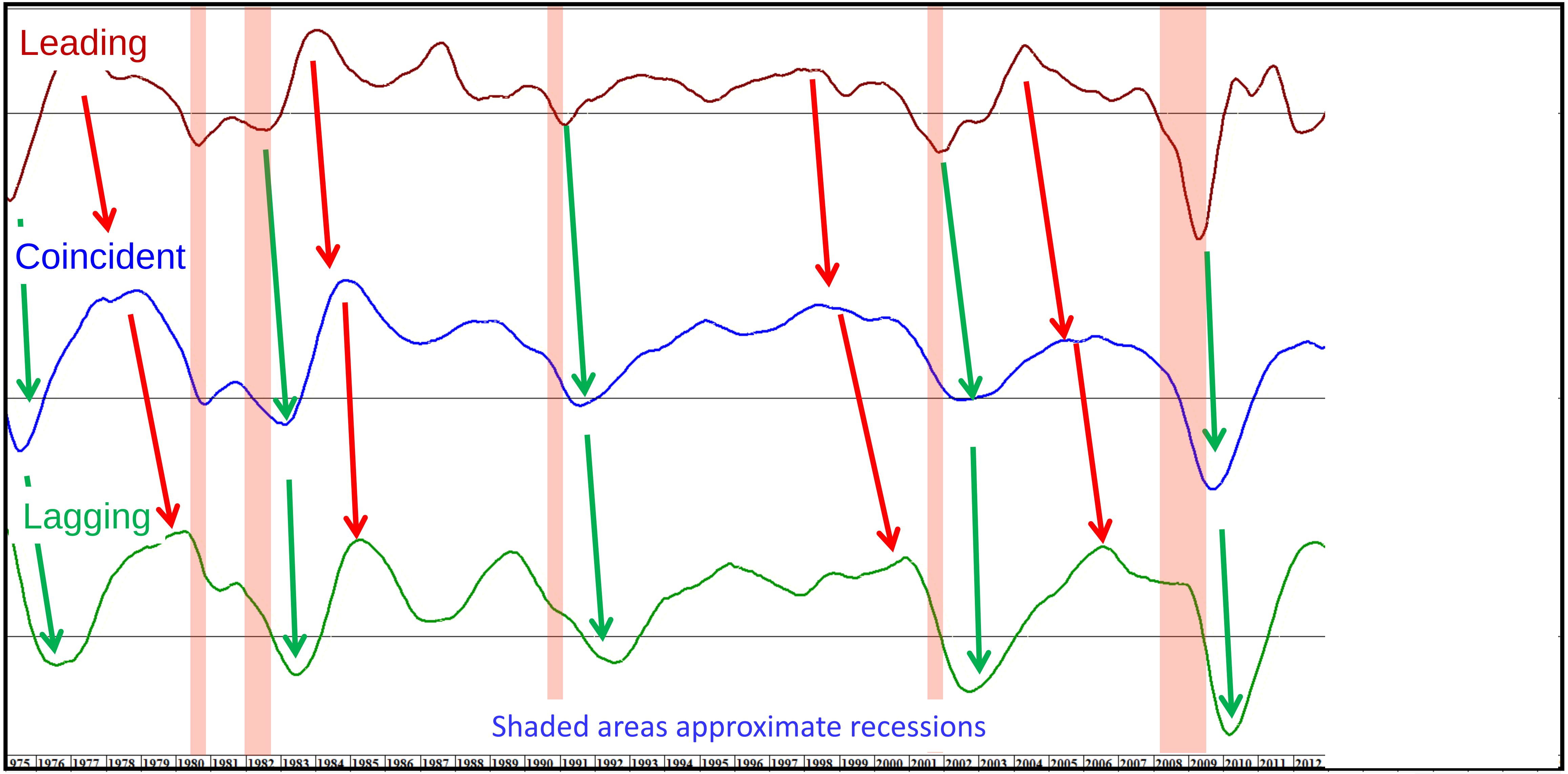
The Random Noise of Economic News!

Does the world seem like a jungle of random data points and knee jerk reactions to economic news?

There’s got to be a better way



Momentum of ECRI Economic Indicators 1975-2019

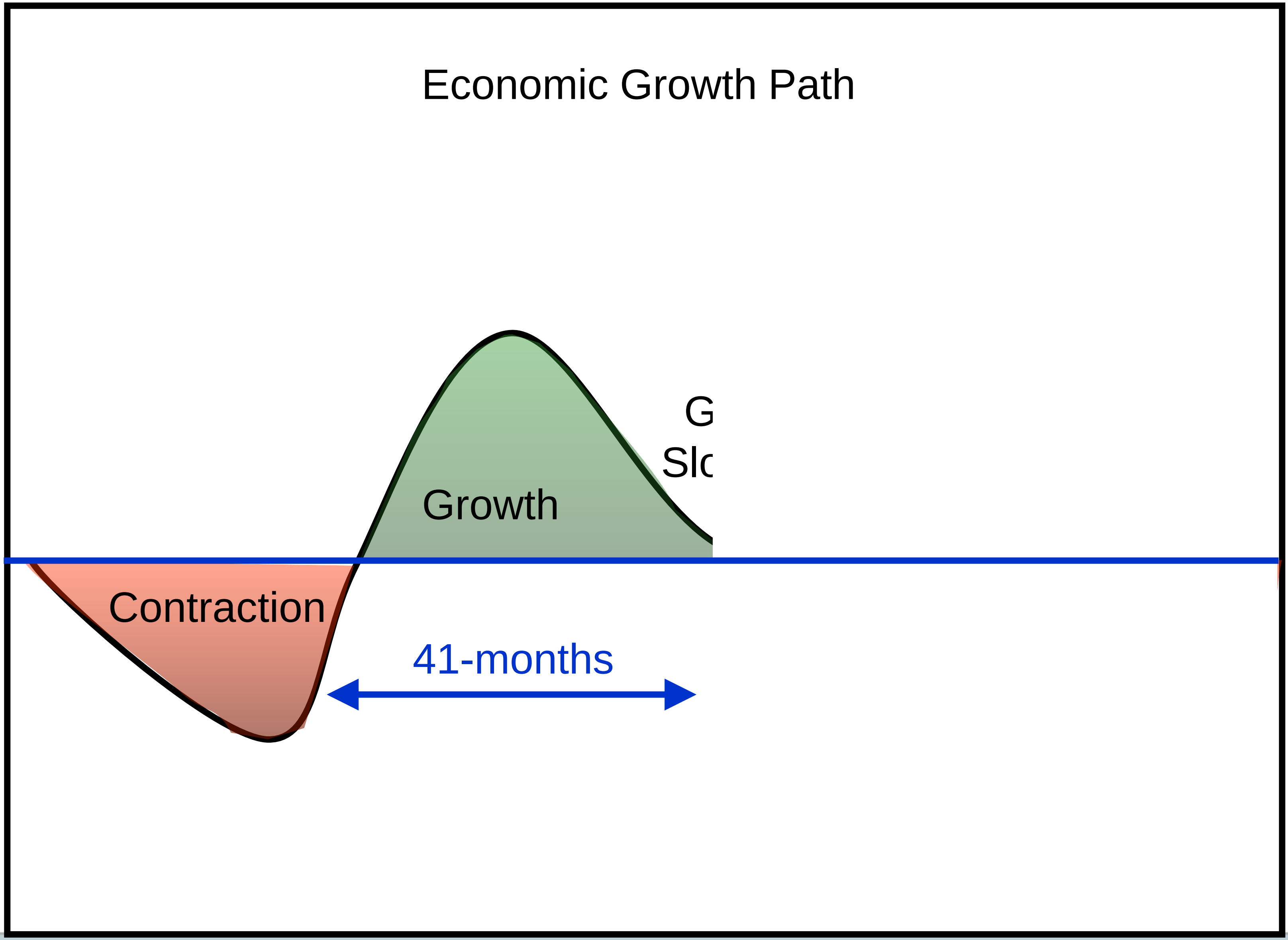


Demonstrating the business cycle chronological sequence.

41-month Business Cycle

- 1. In 1923 Joseph Kitchin identified a 41-month cycle in bank clearings and wholesale prices.
- 2. A 41-month cycle in stock prices has been observed between 1871 and 1946. In all, there were 22 cycles.
- 3. Since 1958 a 41-month cycle has operated in the US economy, embracing 17 recessions and slowdowns.

Theoretical Business Cycle Growth Path



The 41-month cycle still exists, but includes growth slowdowns as well as recessions.

Momentum of ECRI Economic Indicators 1975-2019

We are currently in the third slowdown of this recovery.

Growth Slowdowns

1. Cathartic experience as the economy pauses to refresh.

2. Associated with 10-15% decline in the stock market.

3. Explain secular bull markets for equities.

Bonds

Stocks

Are all part of the business cycle sequence.

Commodities

Calendar Year

Spring

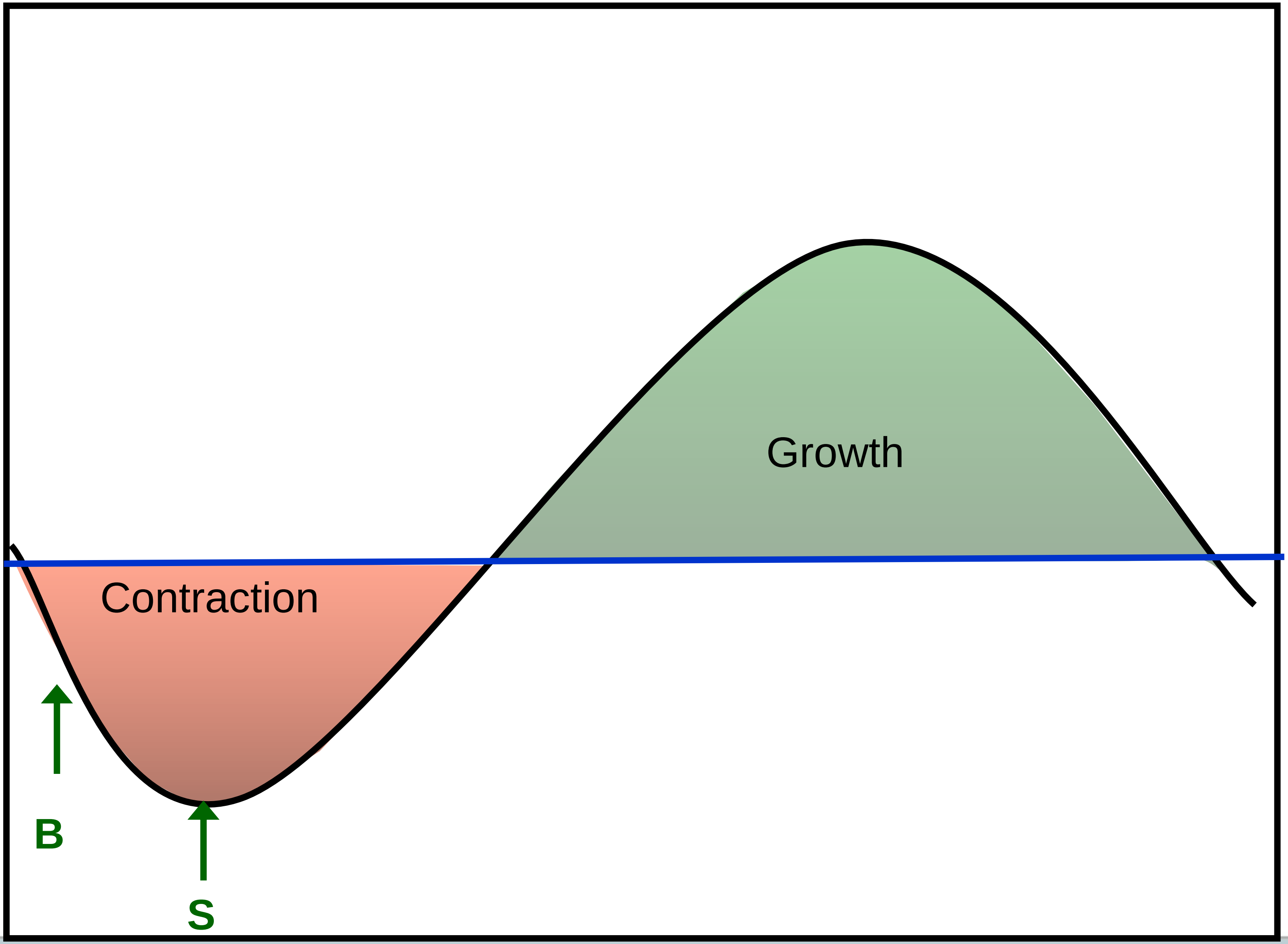
Summer

Autumn

Winter

Financial Market Business Cycle Sequence

Idealized Business Cycle



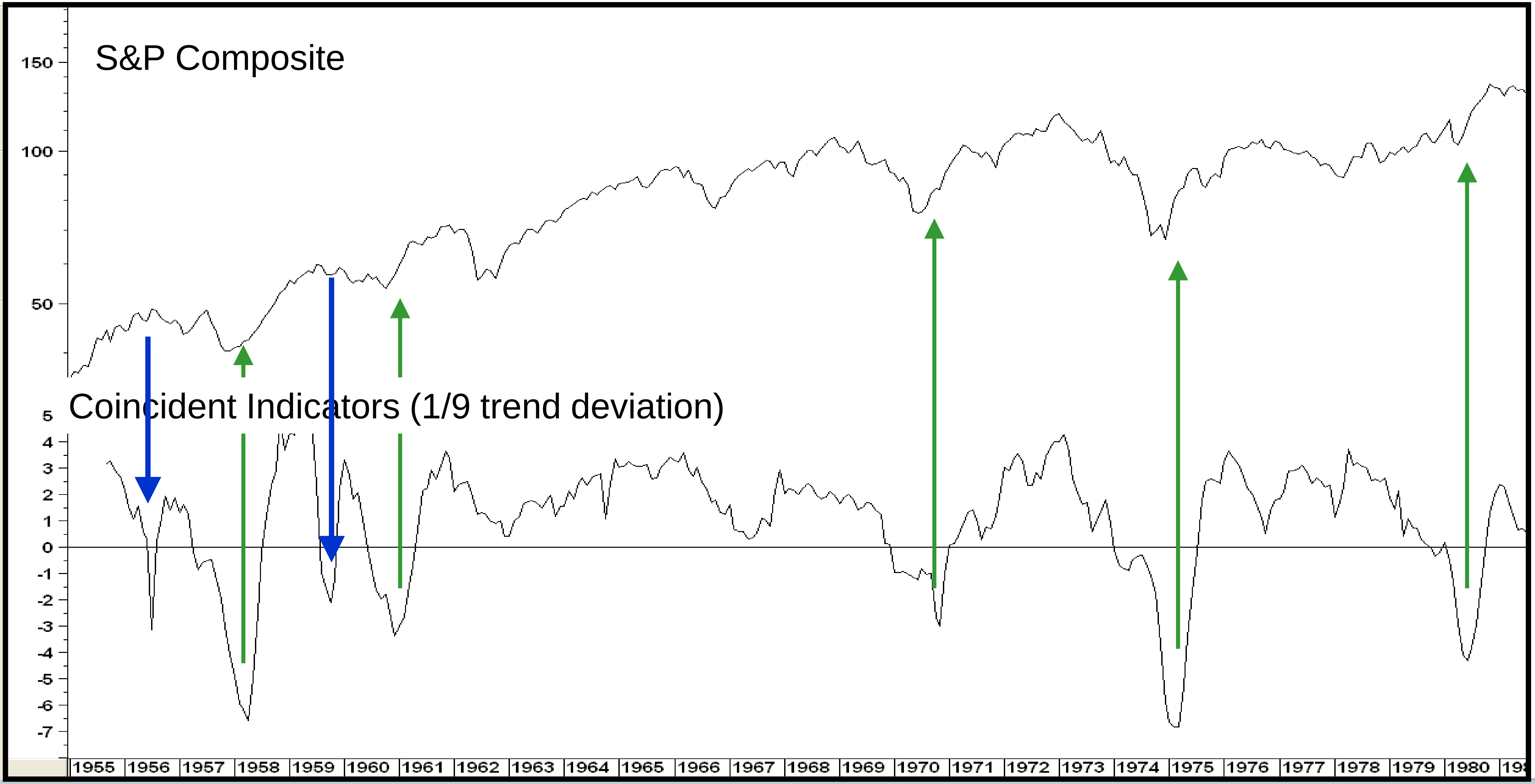
Initial equity rally is usually strong because…

1. Large short position has to be covered.

2. Weak holders have liquidated because of bad news.

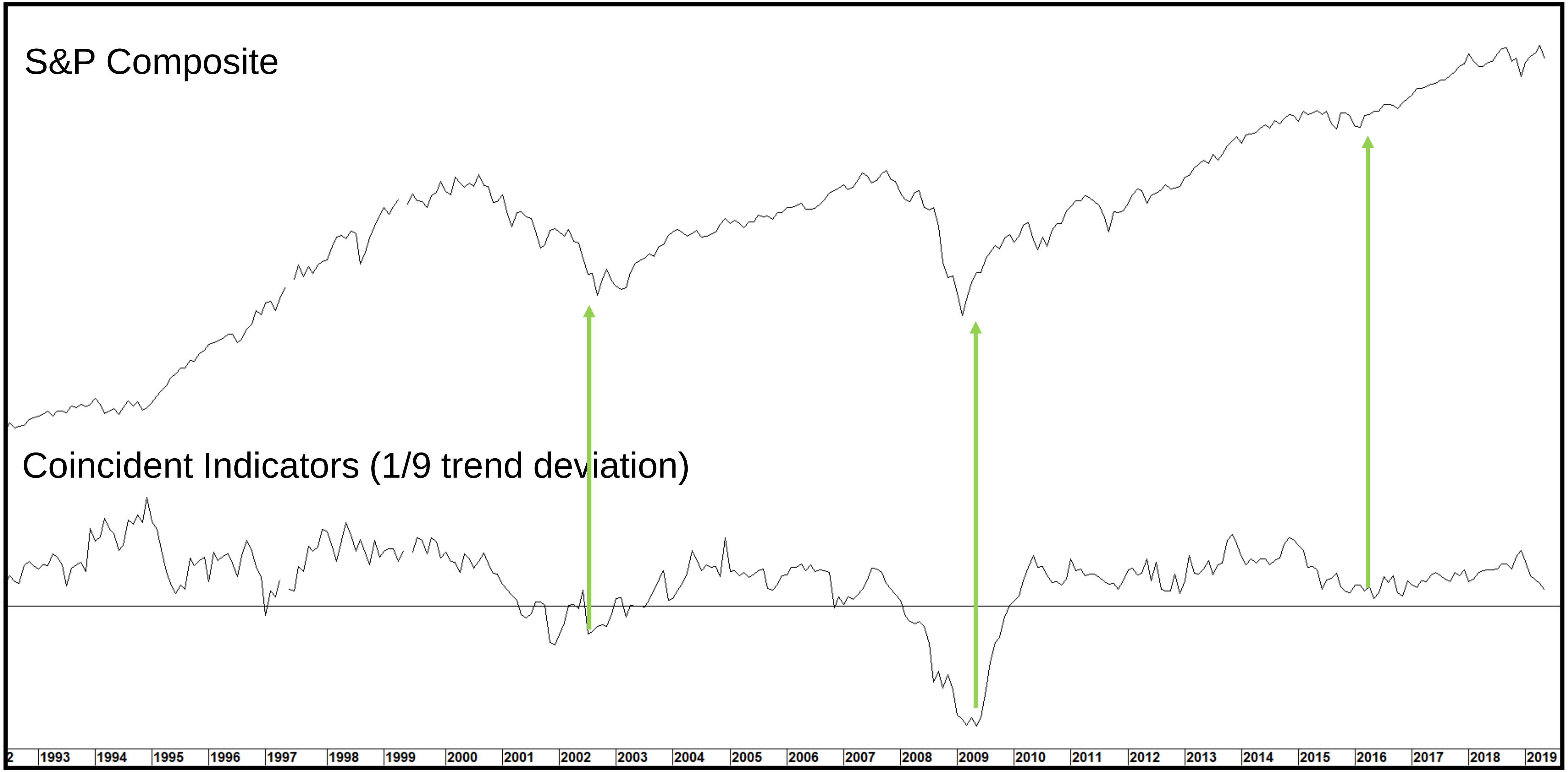
3. Higher prices needed to flush out new stock.

S&P vs Economic Momentum at Troughs 1955-81



Stocks usually bottom at the worst economic inflexion point.

S&P vs Economic Momentum at Troughs 1997-2018



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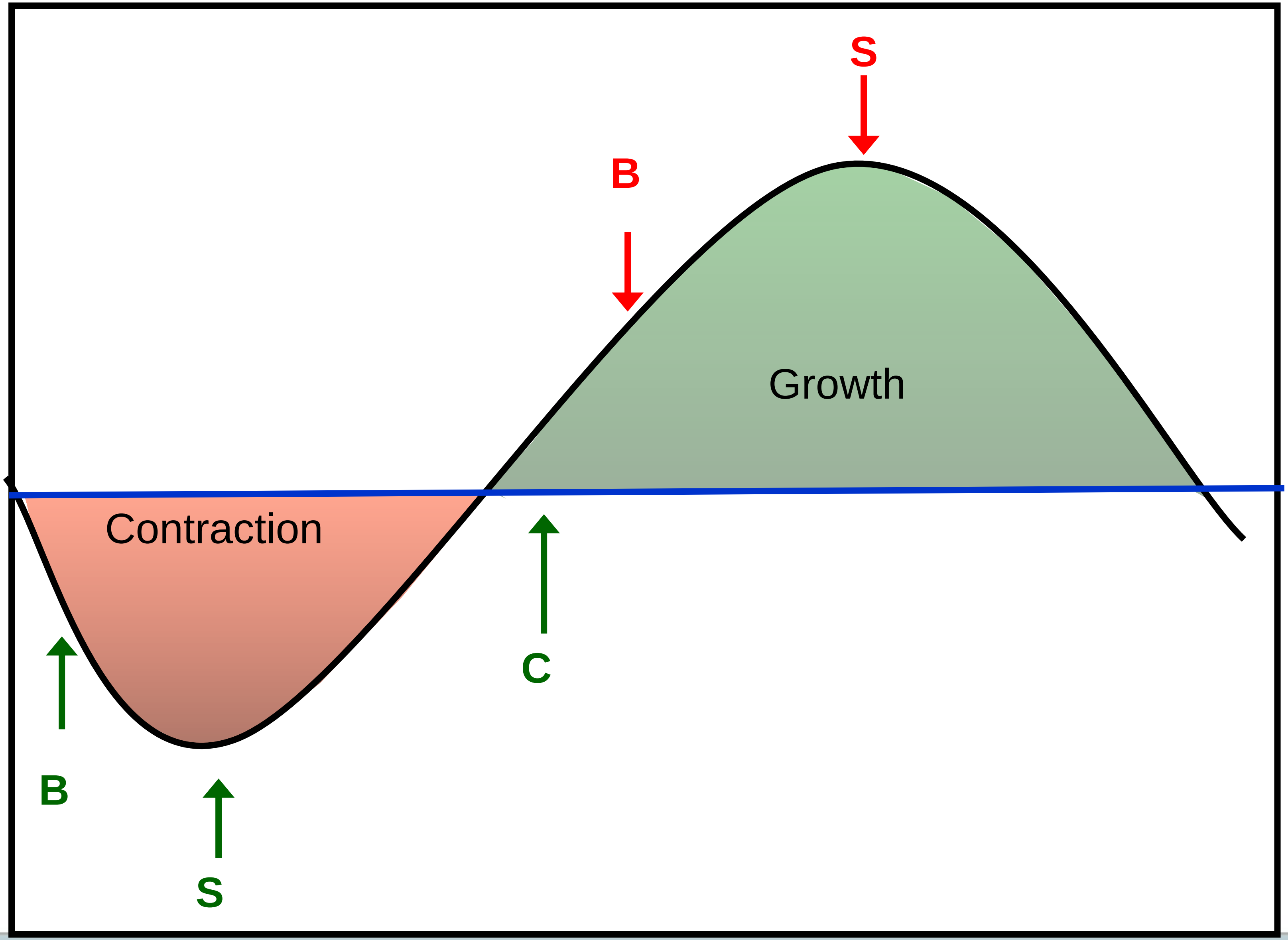
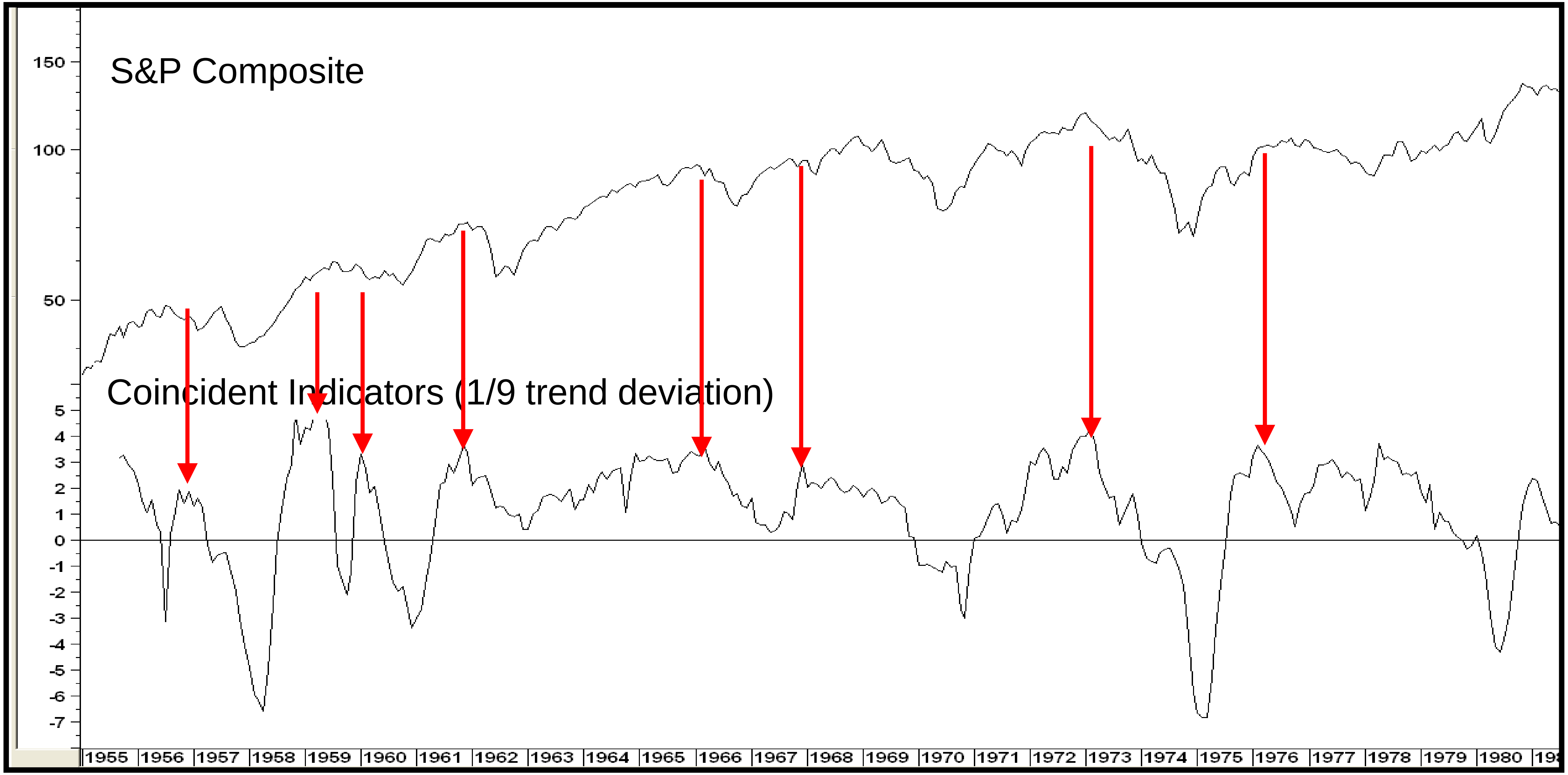
Financial Market Business Cycle Sequence

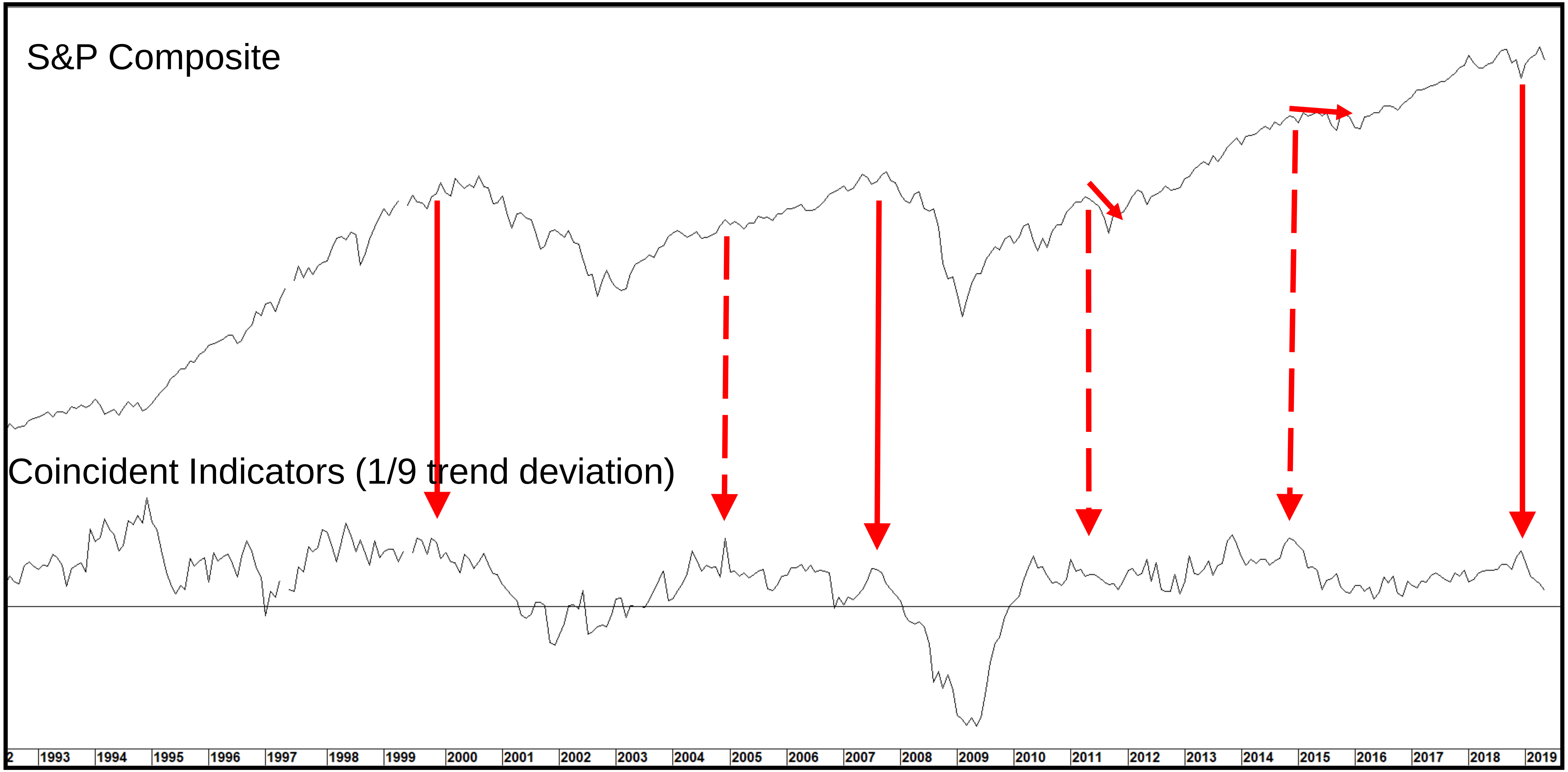


S&P vs Economic Momentum at Peaks1955-1982



Stocks usually peak around the time when the economy is strongest.

S&P vs Economic Momentum at Peaks 1997-2019



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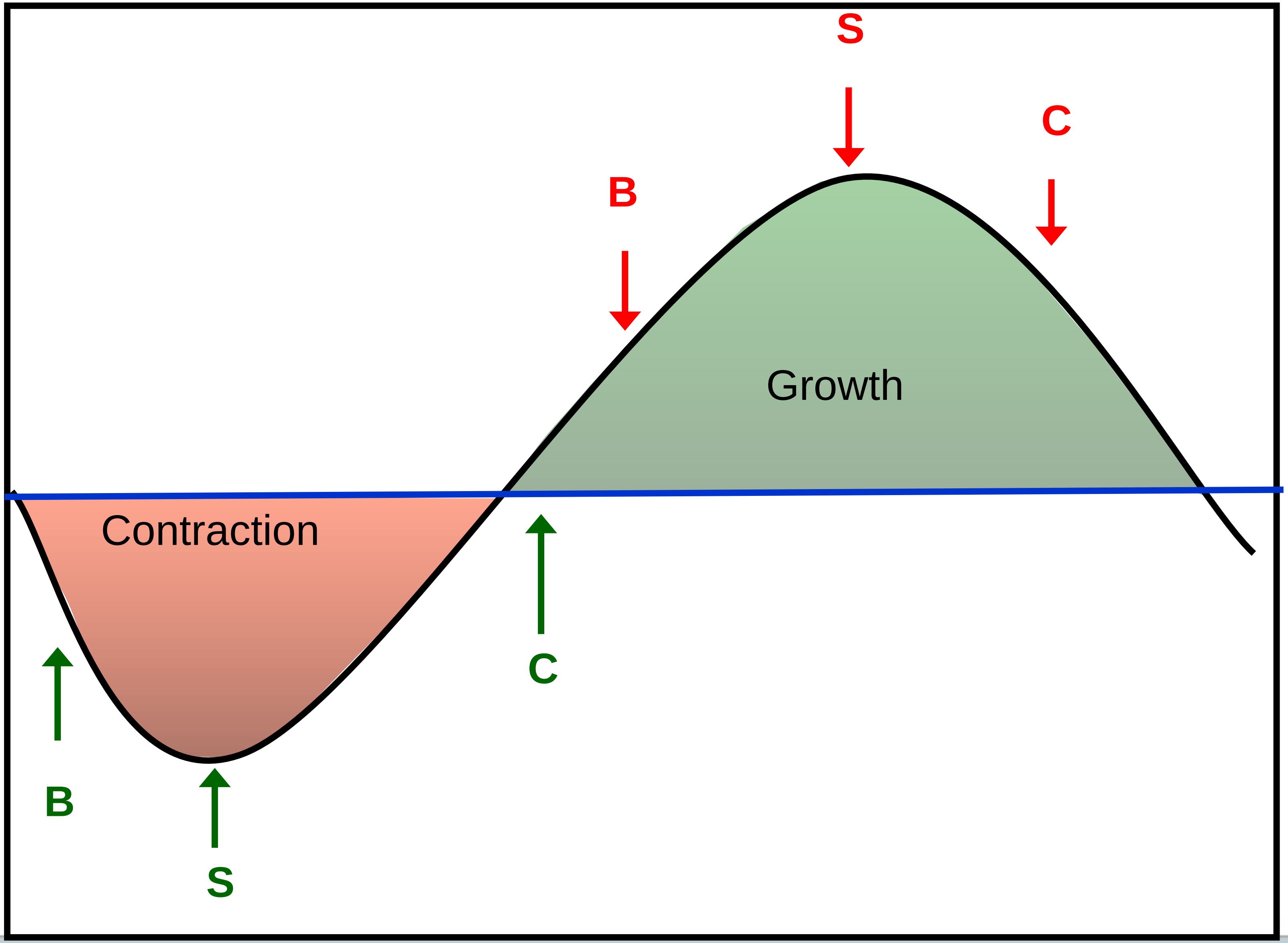
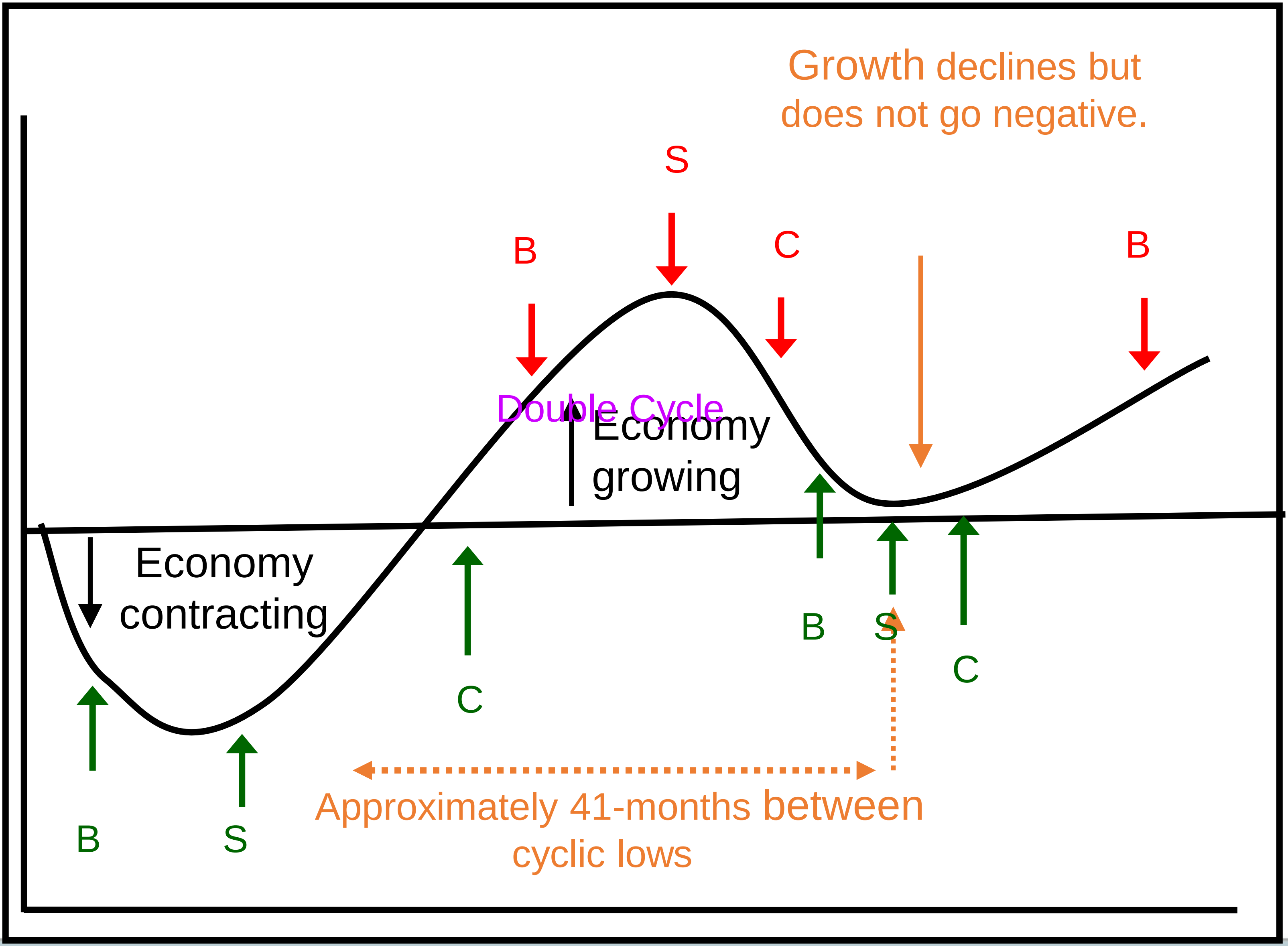
Financial Market Business Cycle Sequence



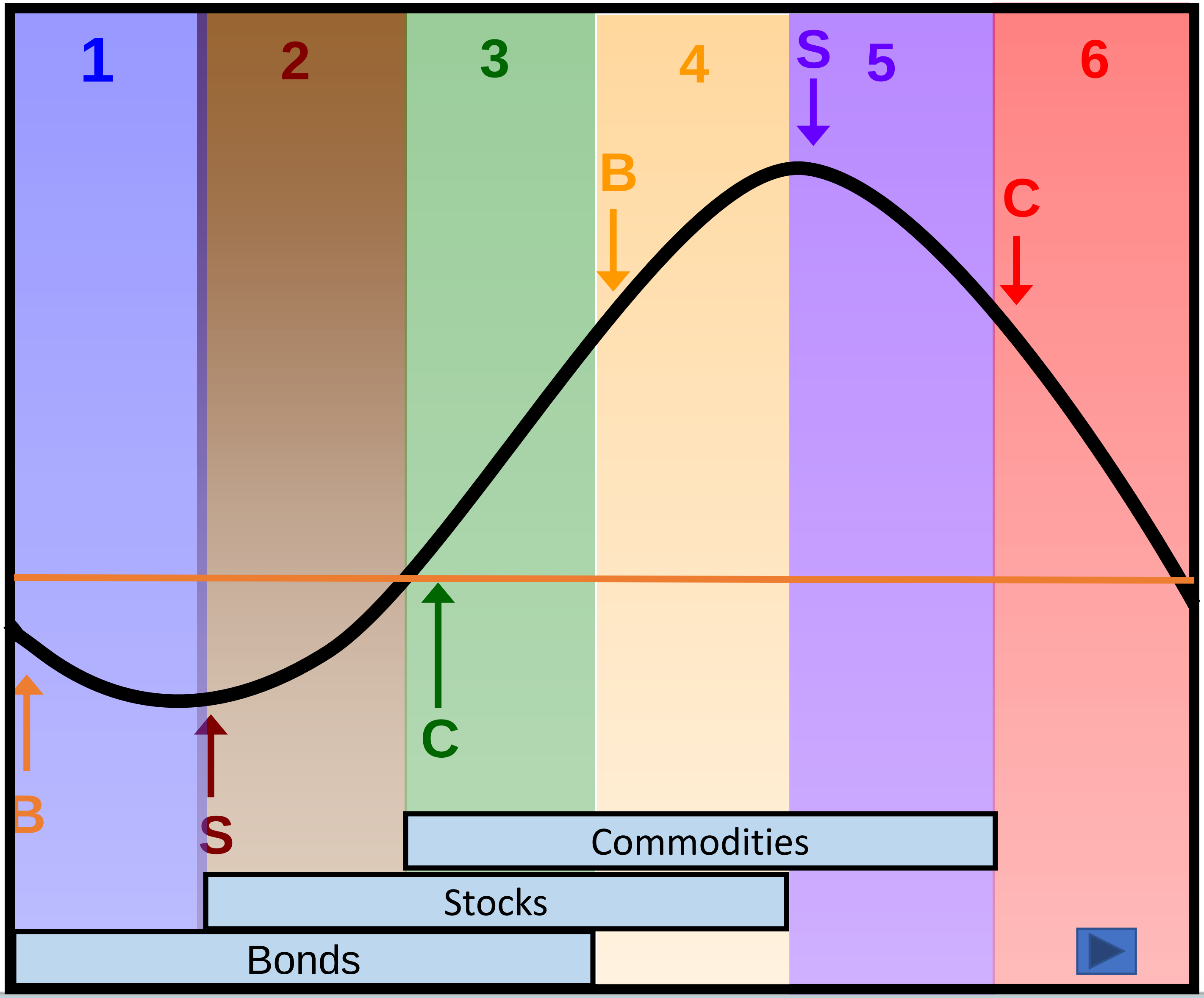
Theoretical Financial Market Sequence in a Double Cycle



The sequence repeats during double cycles.

Part II
Introducing the Six Stages

The Pring Turner Six Stages



How to allocate assets around the business cycle.

Part III Sector Rotation

The economy has leading and lagging sectors, so too does the stock market!!

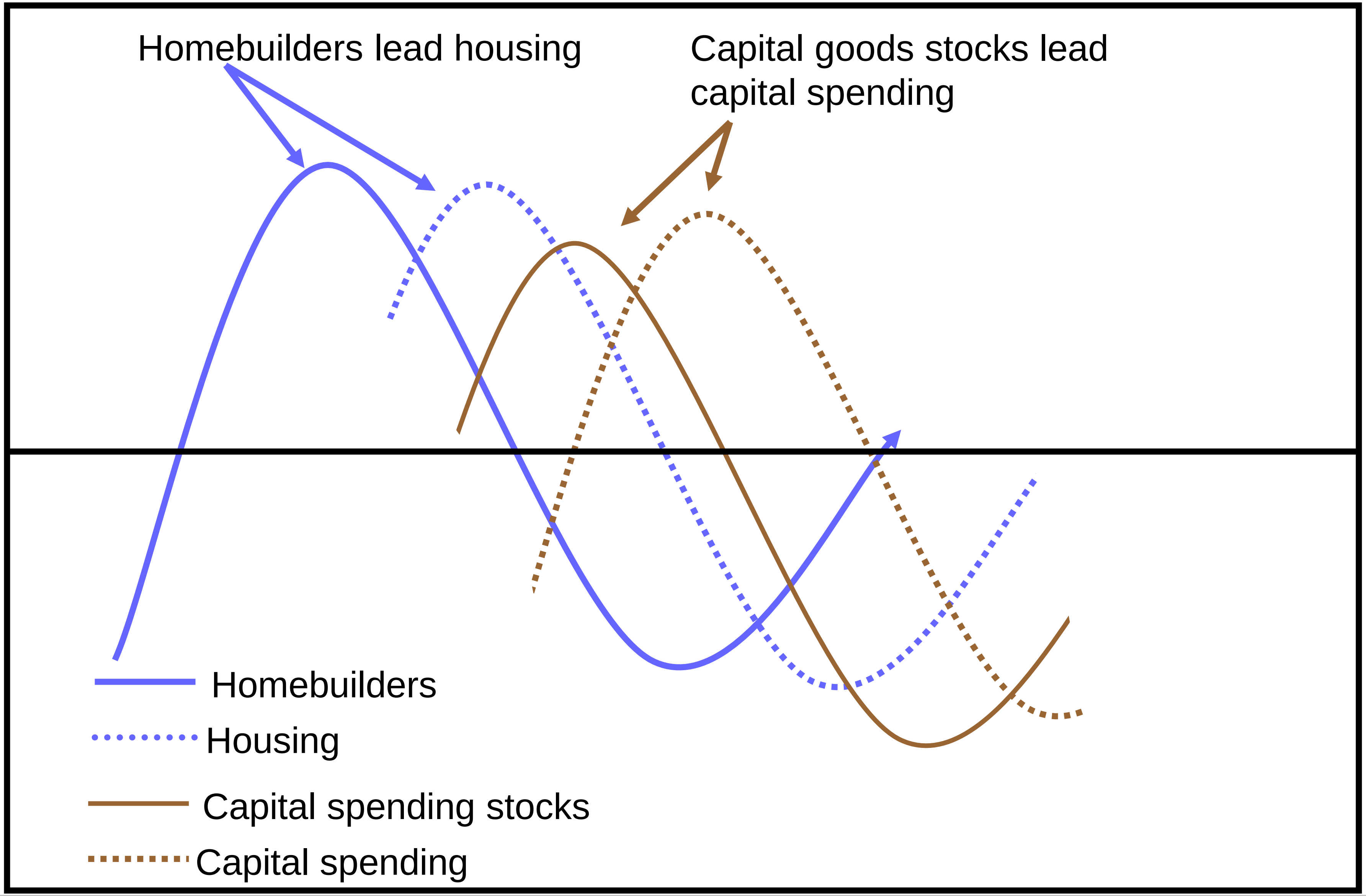
A measure of the overall market, like the S&P Composite, is really a coincident indicator for equities in general.

The Market's Discounting Mechanism

If the stock market discounts the economy then ……

….individual stock market sectors should discount the economic sector they represent!

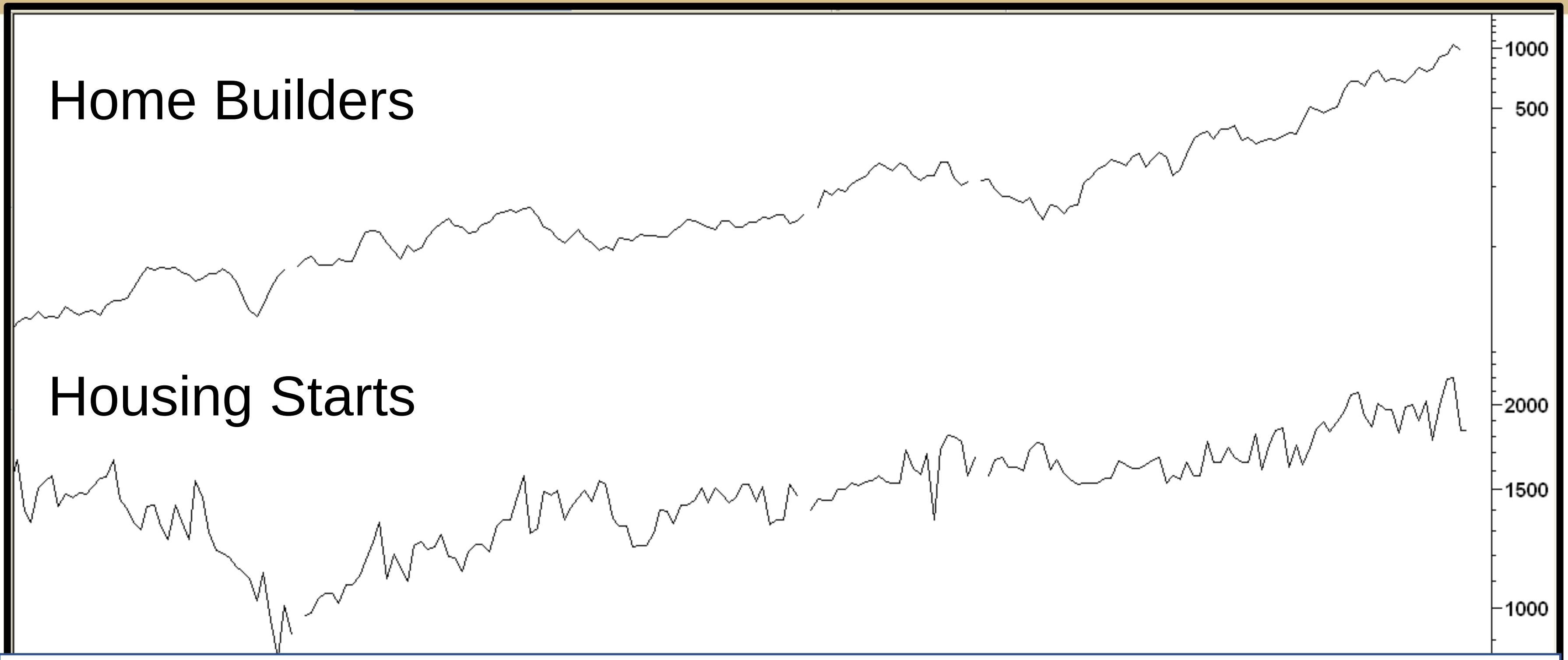
How Market Sectors Lead Economic Sectors
Demonstrating How Sectors Lead their Part of the Economy



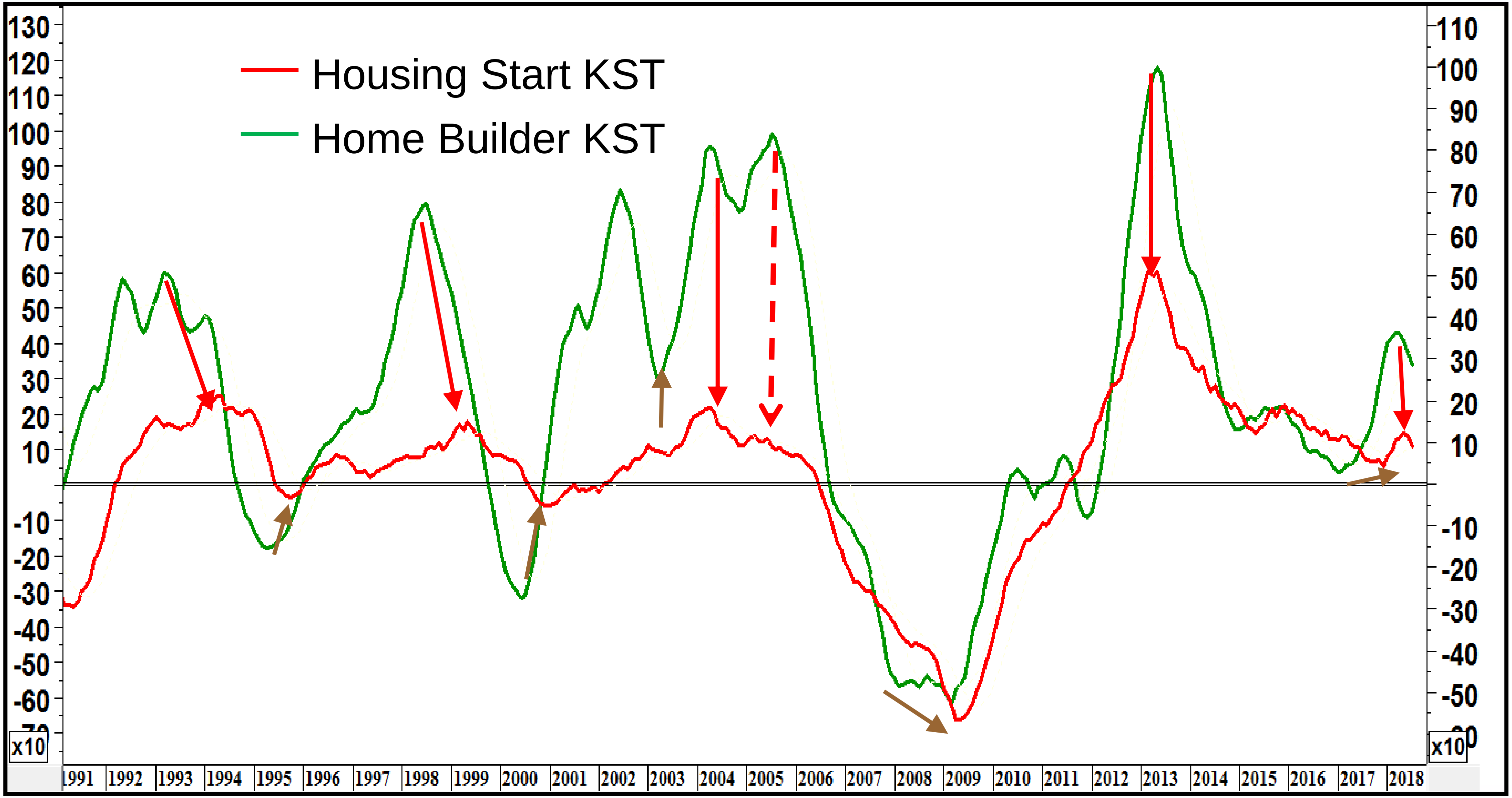
The prices of homebuilder shares discount housing starts

Homebuilders vs. Housing Starts

Homebuilders vs Housing Stocks



Homebuilders vs. Housing Starts 1999-2018



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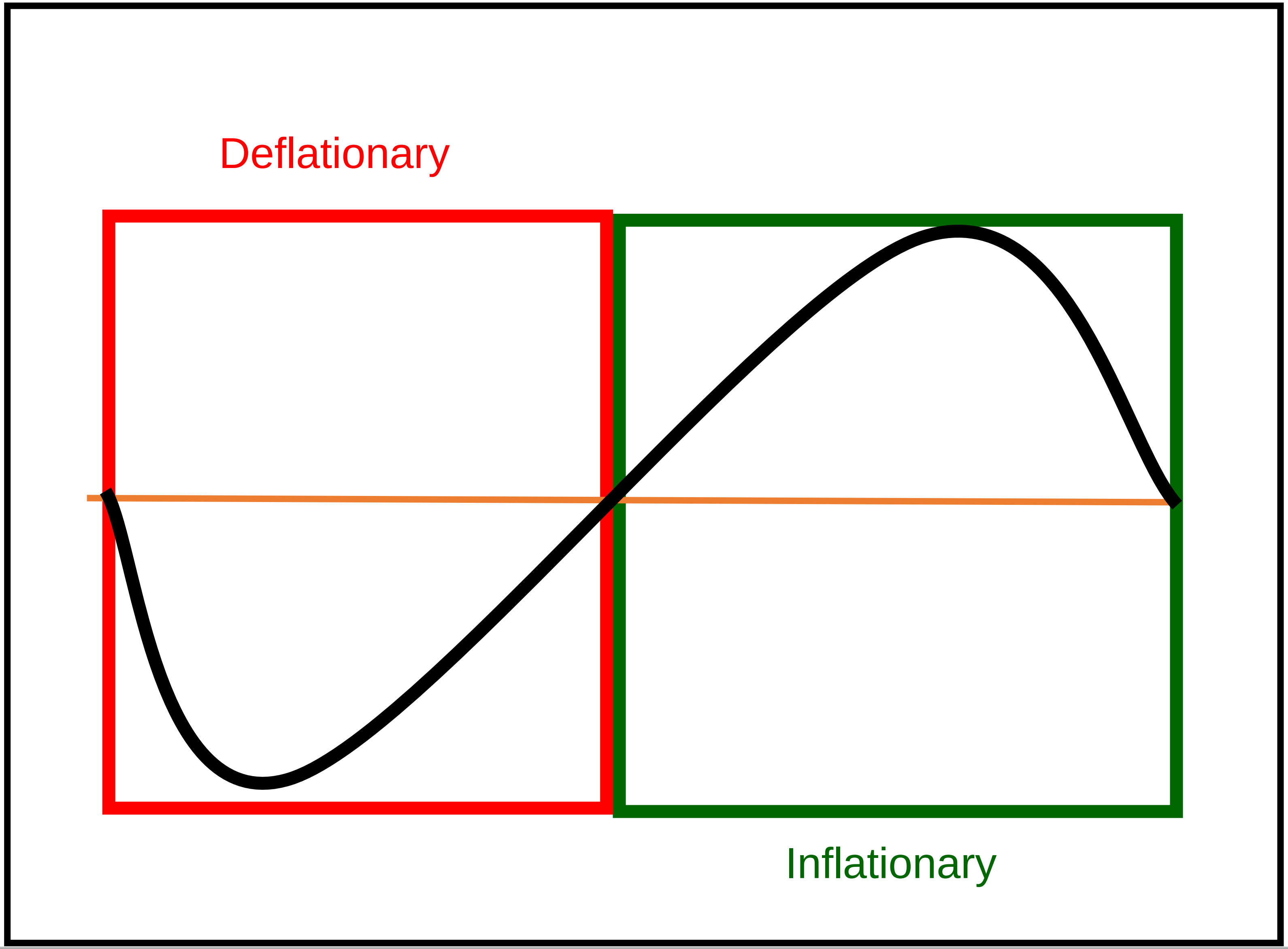
Arrows show the stocks lead the industry.

www.pringturner.com

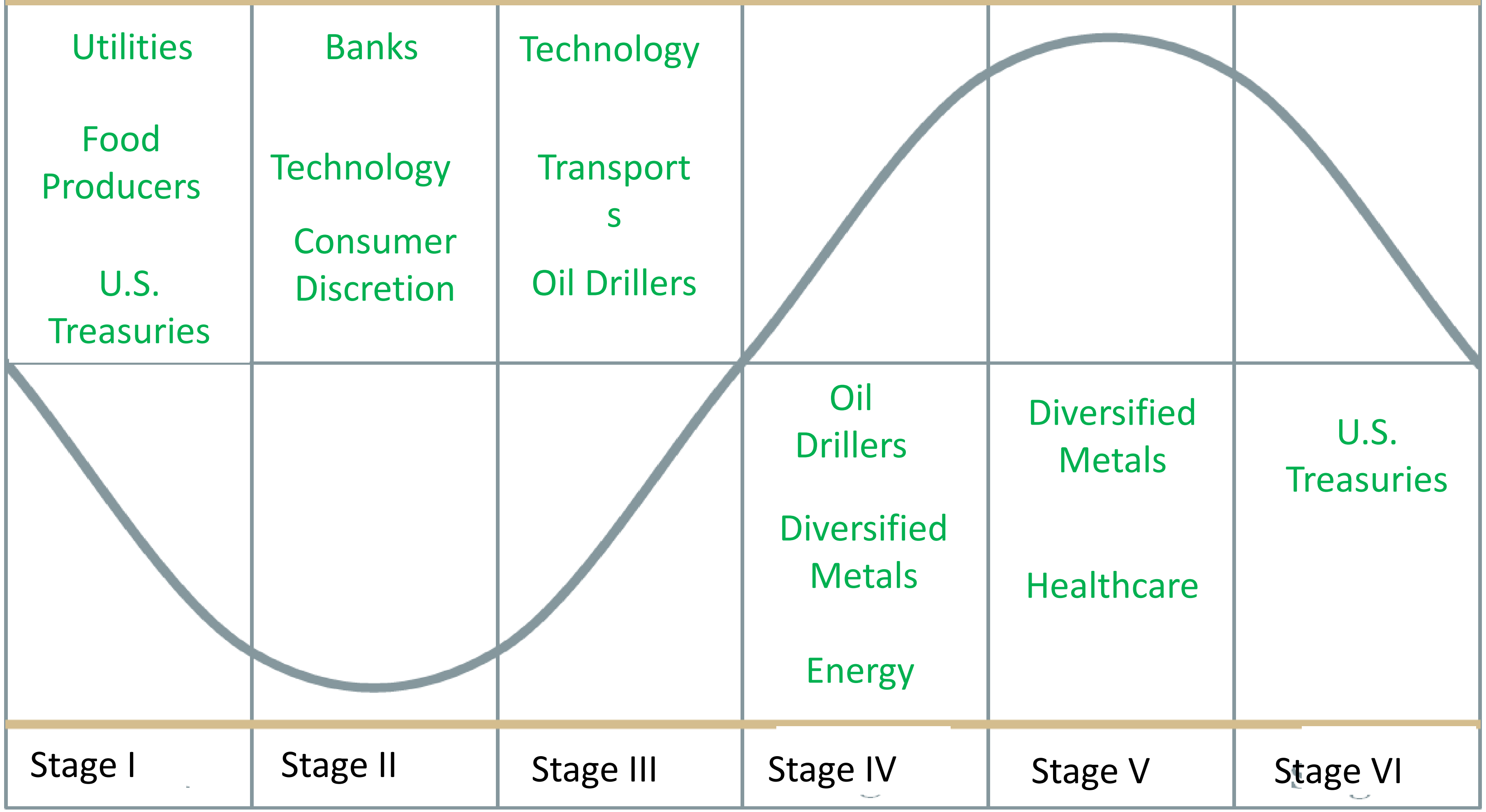
Sector performance through the Six Stages

Idealized Business Cycle



Pring Turner's Six Business Cycle Stages

Sector Emphasis

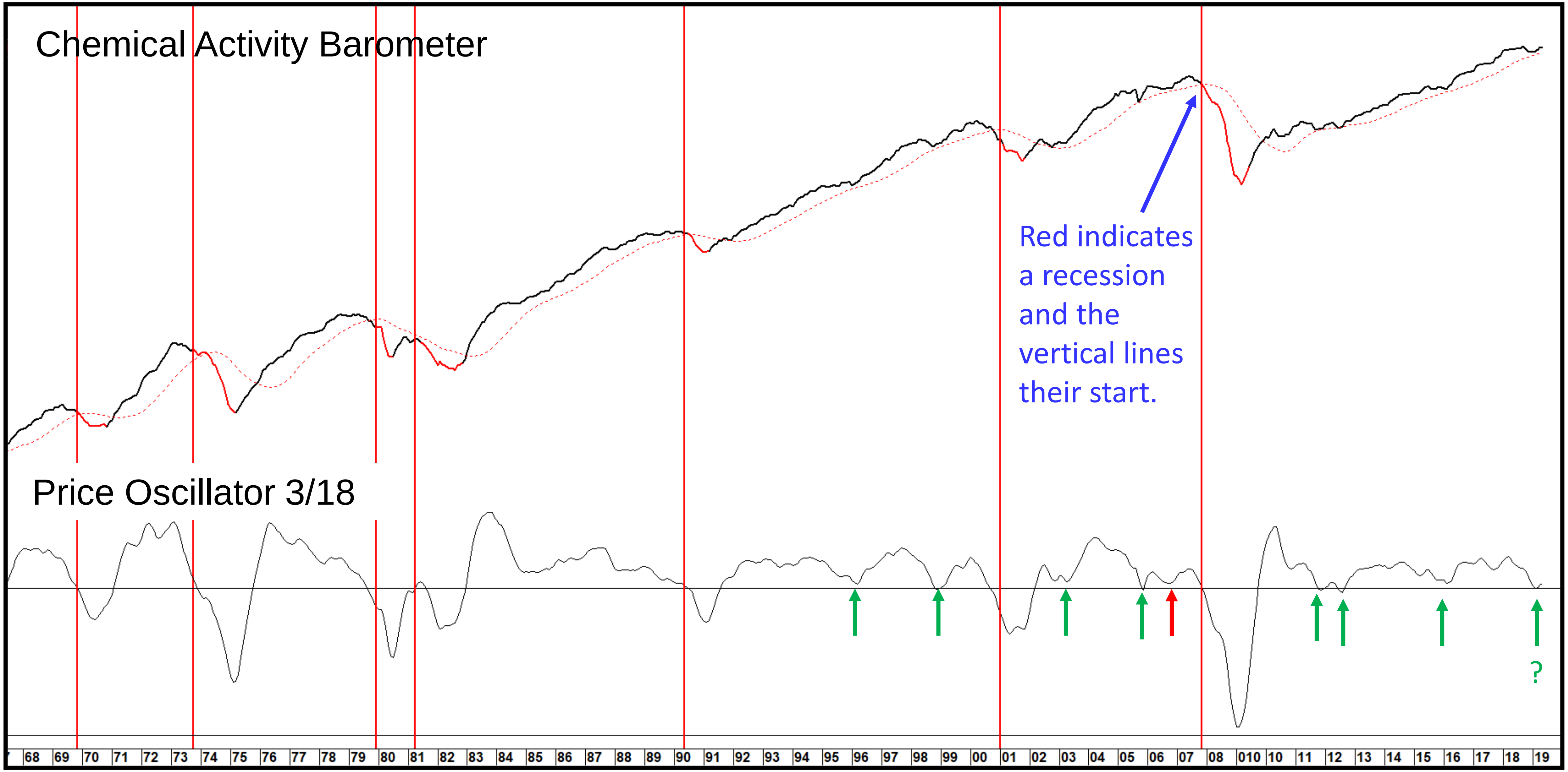


Pring Turner Six Stages

Stage	1	2	3	4	5	6
Best Performers	XHB Home Builders	IAI Brokers	Communication Equipment	IEO Oil Drillers	XLV Health Care	Household Products
	Restaurants	CARZ Automobiles	XME Diversified Metals	IYW Computer Hardware	Diversified Chemicals	Life Insurance
	XRT Department Stores	Semiconductors SMH	Energy	GDX Gold Shares	XLP Consumer Staples	Food Products
Worst Performers	Diversified Metals	Copper/Gold	Leisure	Hotels	General Merchandising	Chemicals
	Industrials	Oil Drillers	Airlines	Brokers	Automobiles	Railroads
	Communication Equipment	Energy	Home Furnishing	Home Building	Semiconductors	Steel Companies

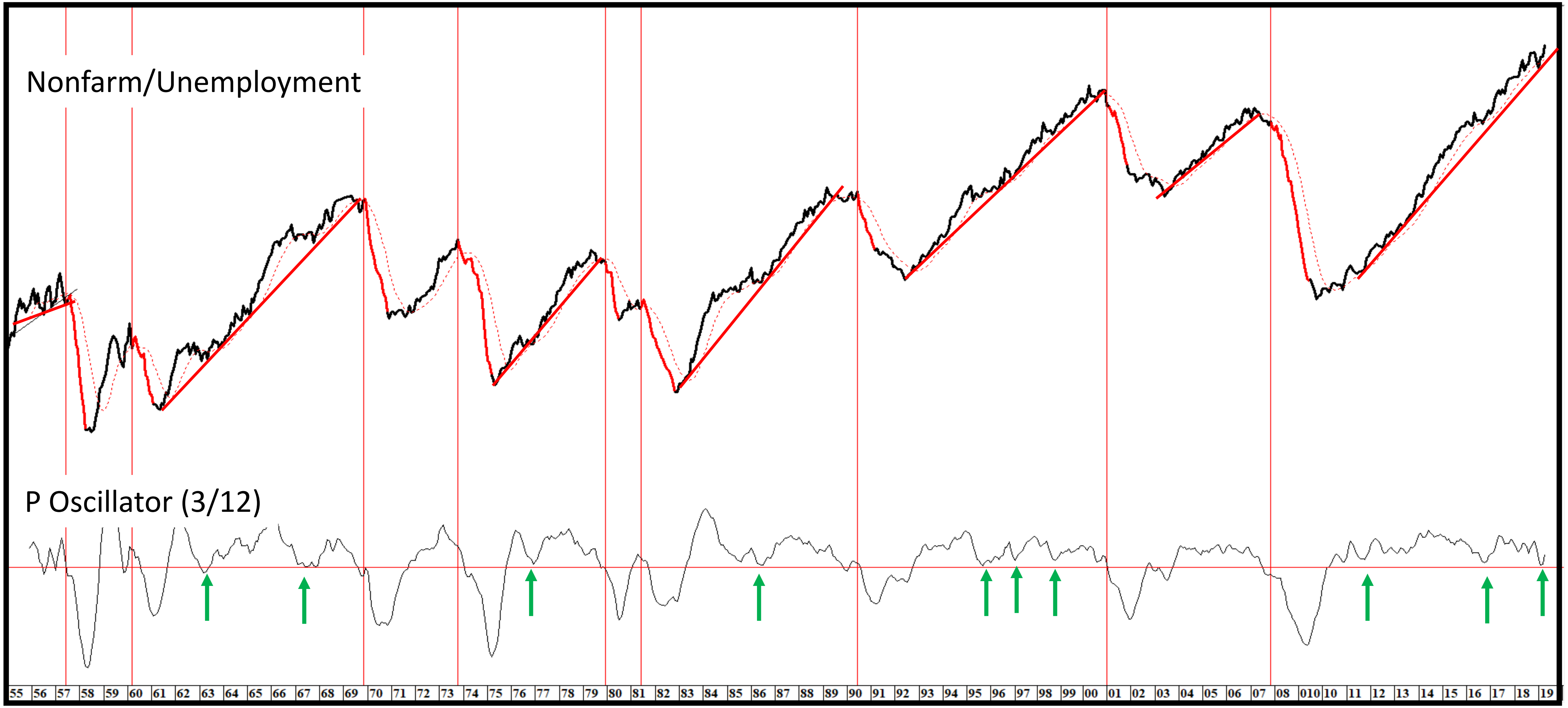
Where are we now?

Chemical Activity Barometer 1967-2019



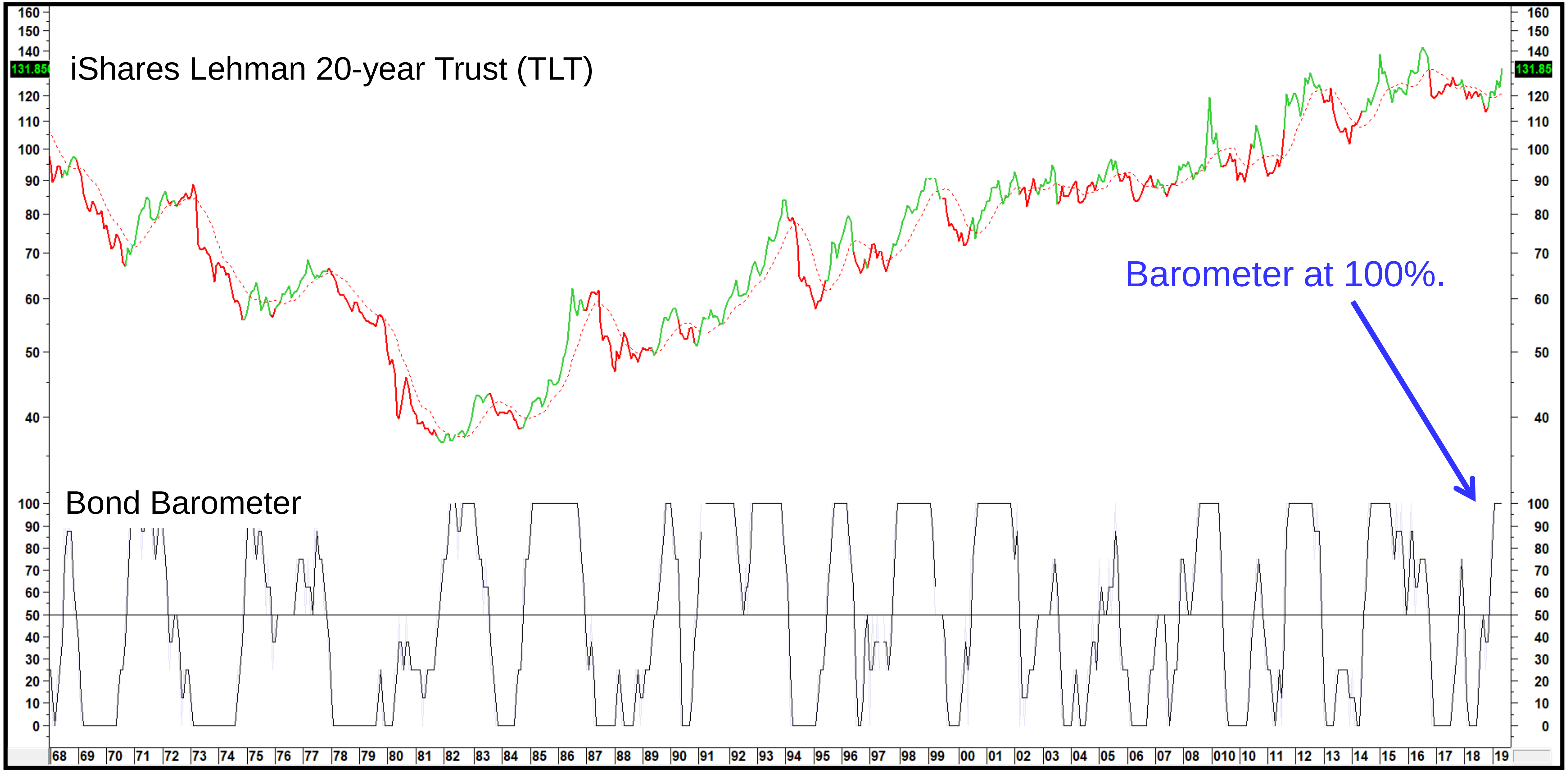
Negative oscillator crossovers offer recession warning.

Nonfarm/Unemployment Ratio and a Price Oscillator 1955-2019



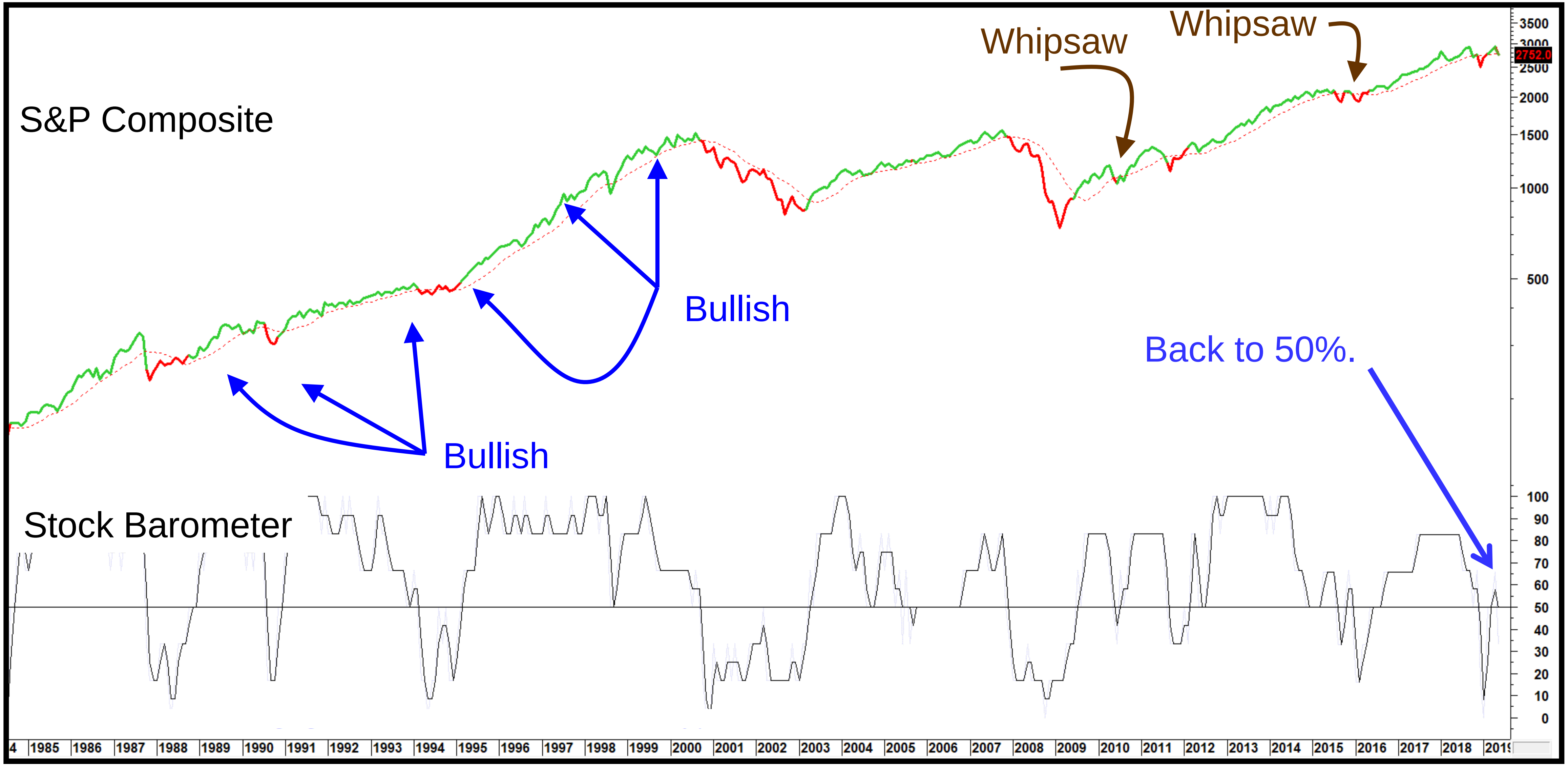
Price oscillator negative zero crossovers warn of a likely recession.

iShares Lehman 20-year Trust and the Pring Turner Bond Barometer



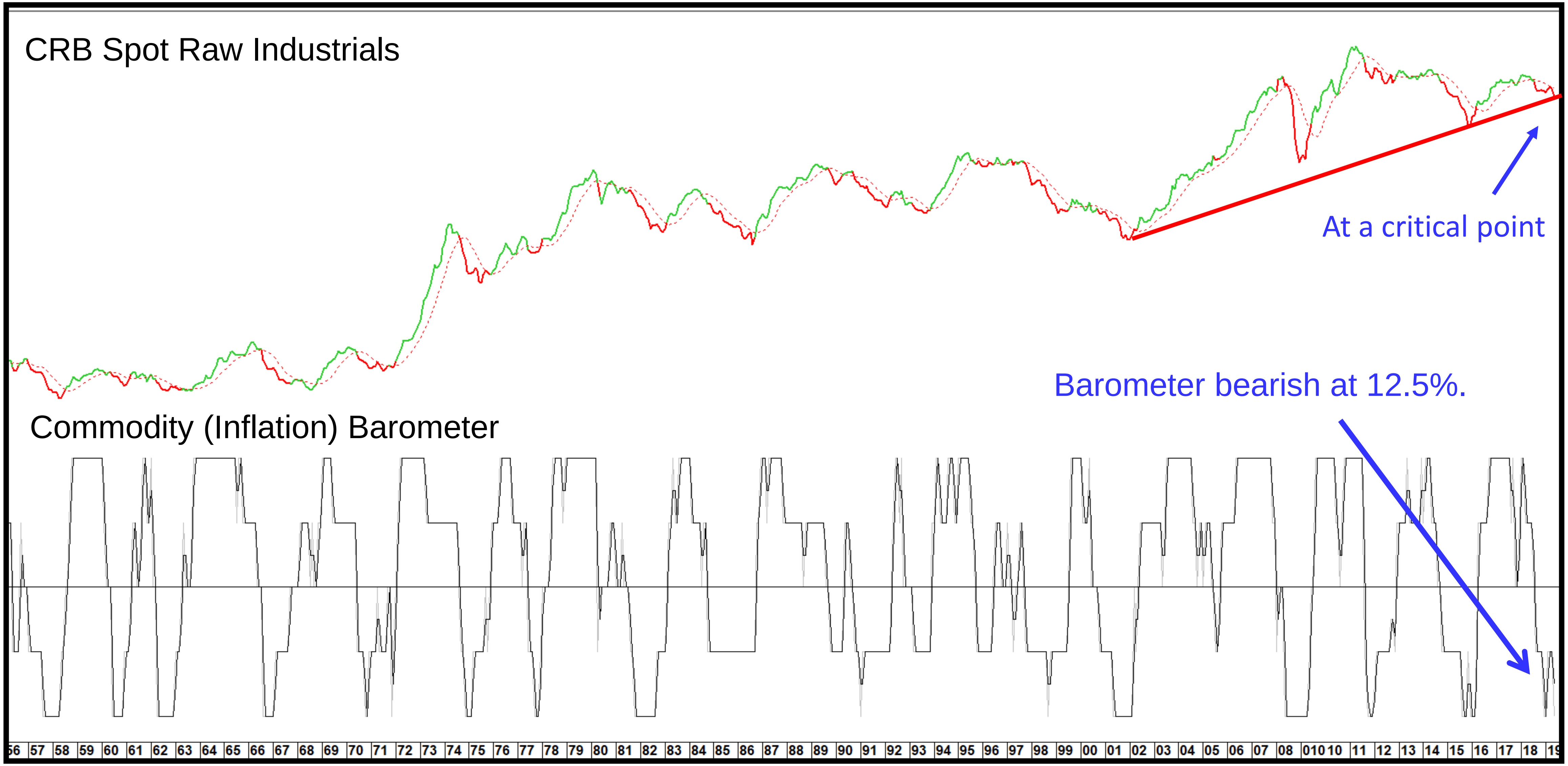
Green and red highlights reflect bullish and bearish Barometer readings

S&P Composite and the Stock Barometer 1984-2019



Green and red highlights indicate when the Stock Barometer is bullish or bearish.

CRB Spot Raw Industrials and the Inflation Barometer 1959-2019



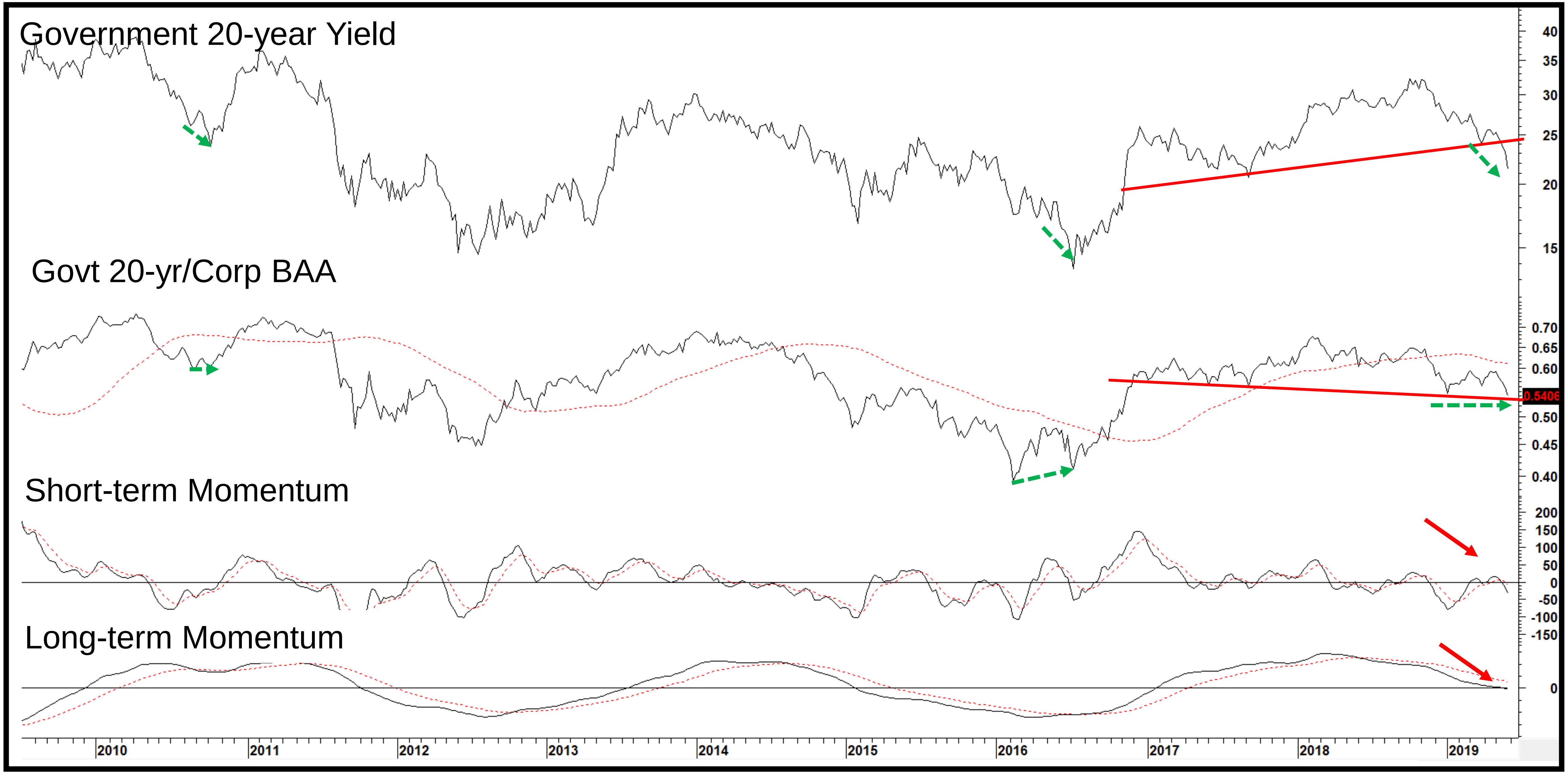
Green and red highlights indicate when the Commodity Barometer is bullish or bearish.

Bonds

US Govt Bond Yield 1870-2019

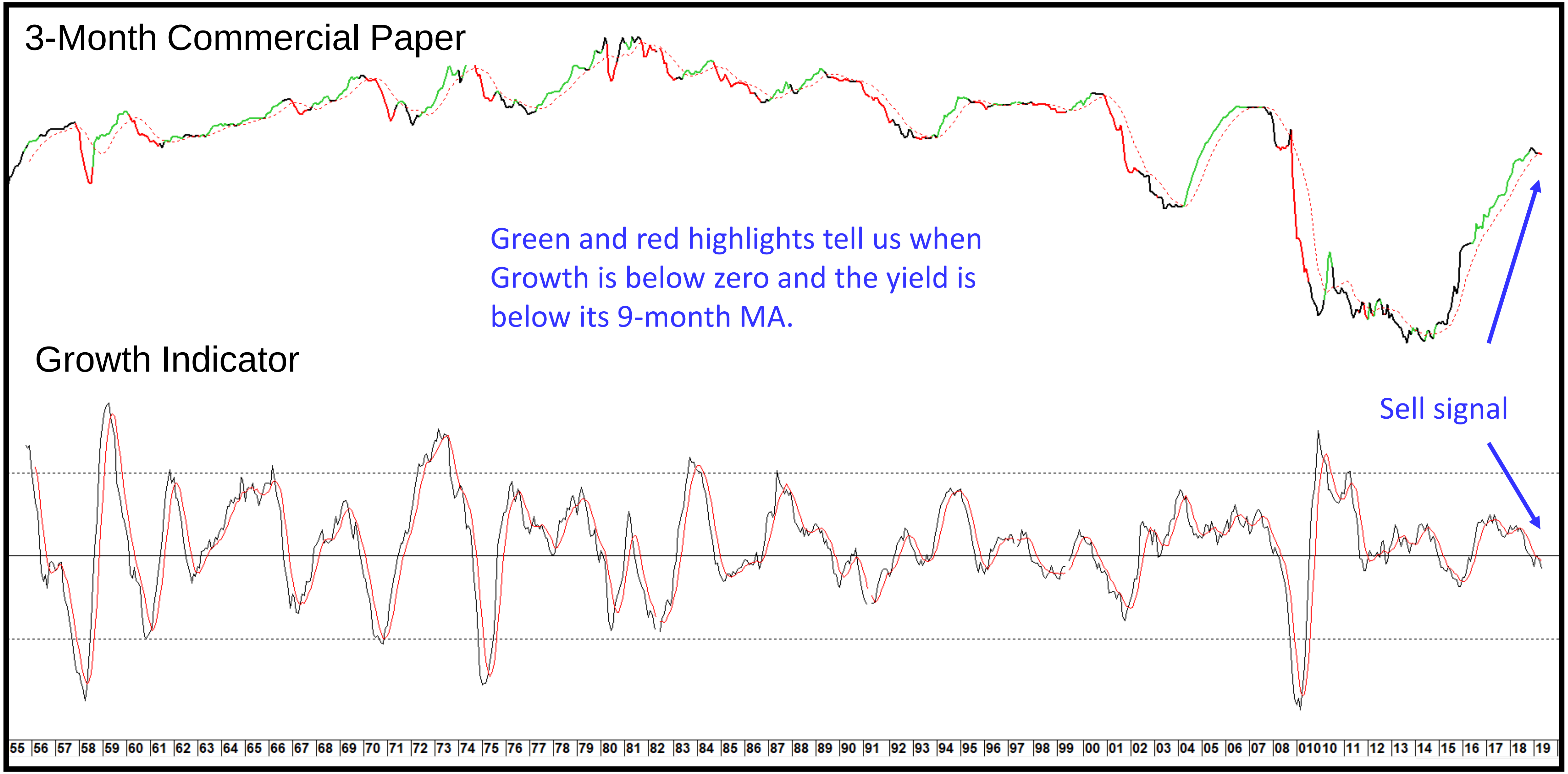
Secular trend reversals are associated with multi-year trading ranges.

US Govt Bond Yield and Three Indicators



Bond yields rise and fall with swings in investor confidence.

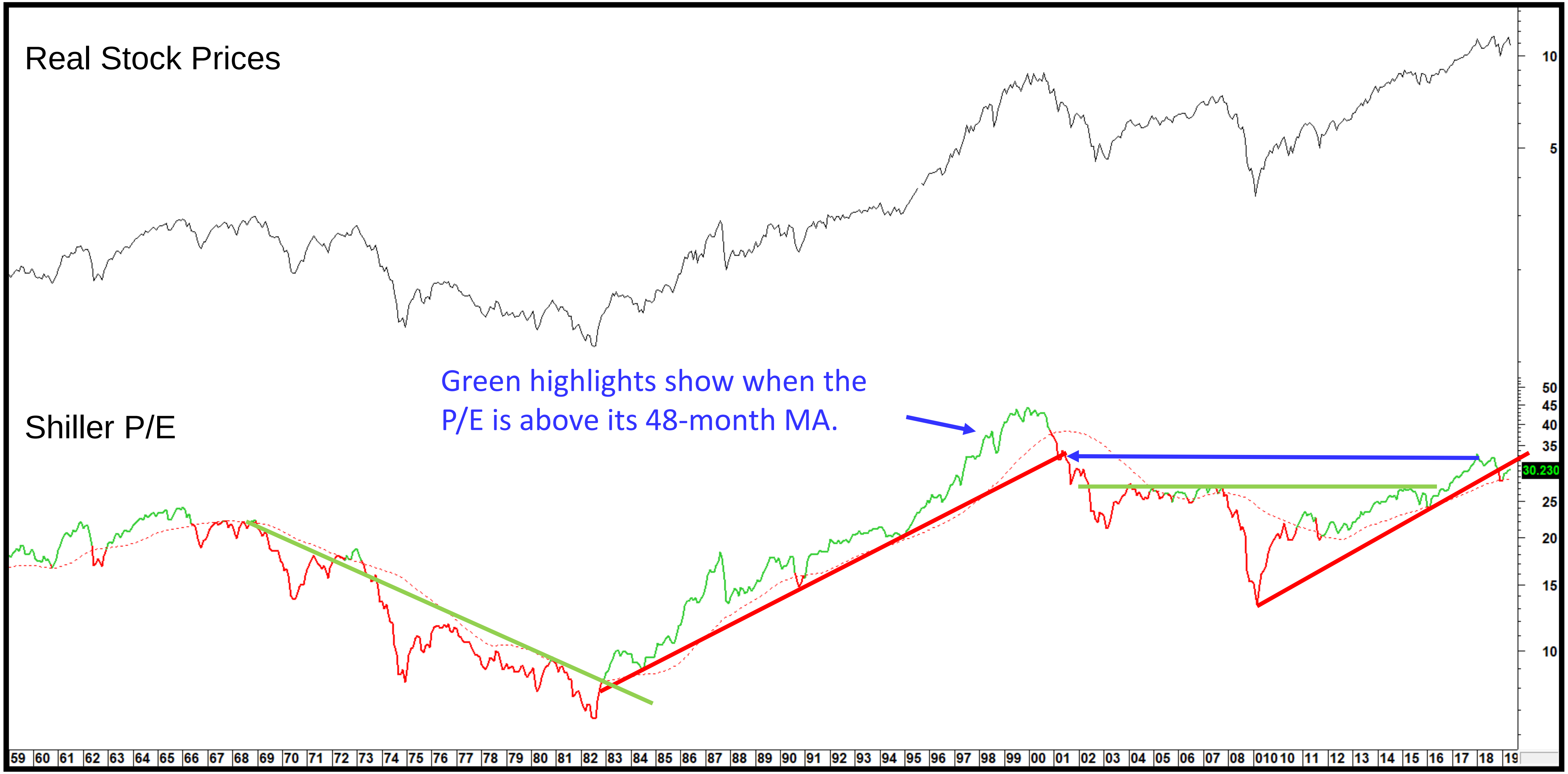
3-Month Commercial Paper Yield and an Economic Indicator 1955-2019



A sub zero Growth Indicator is consistent with a trend of declining rates.

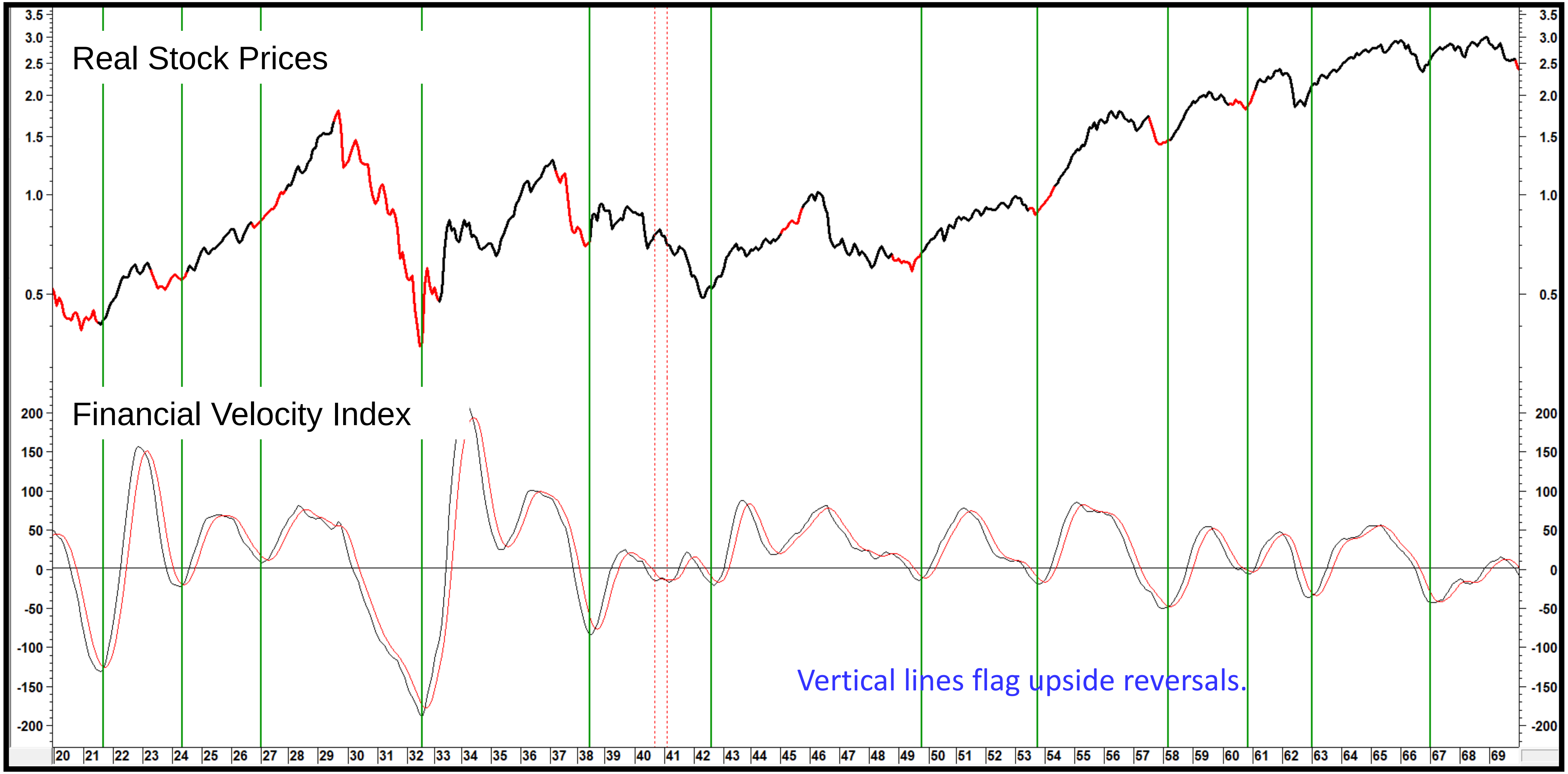
Stocks

Inflation Adjusted Stocks and the Shiller P/E 1959-2019



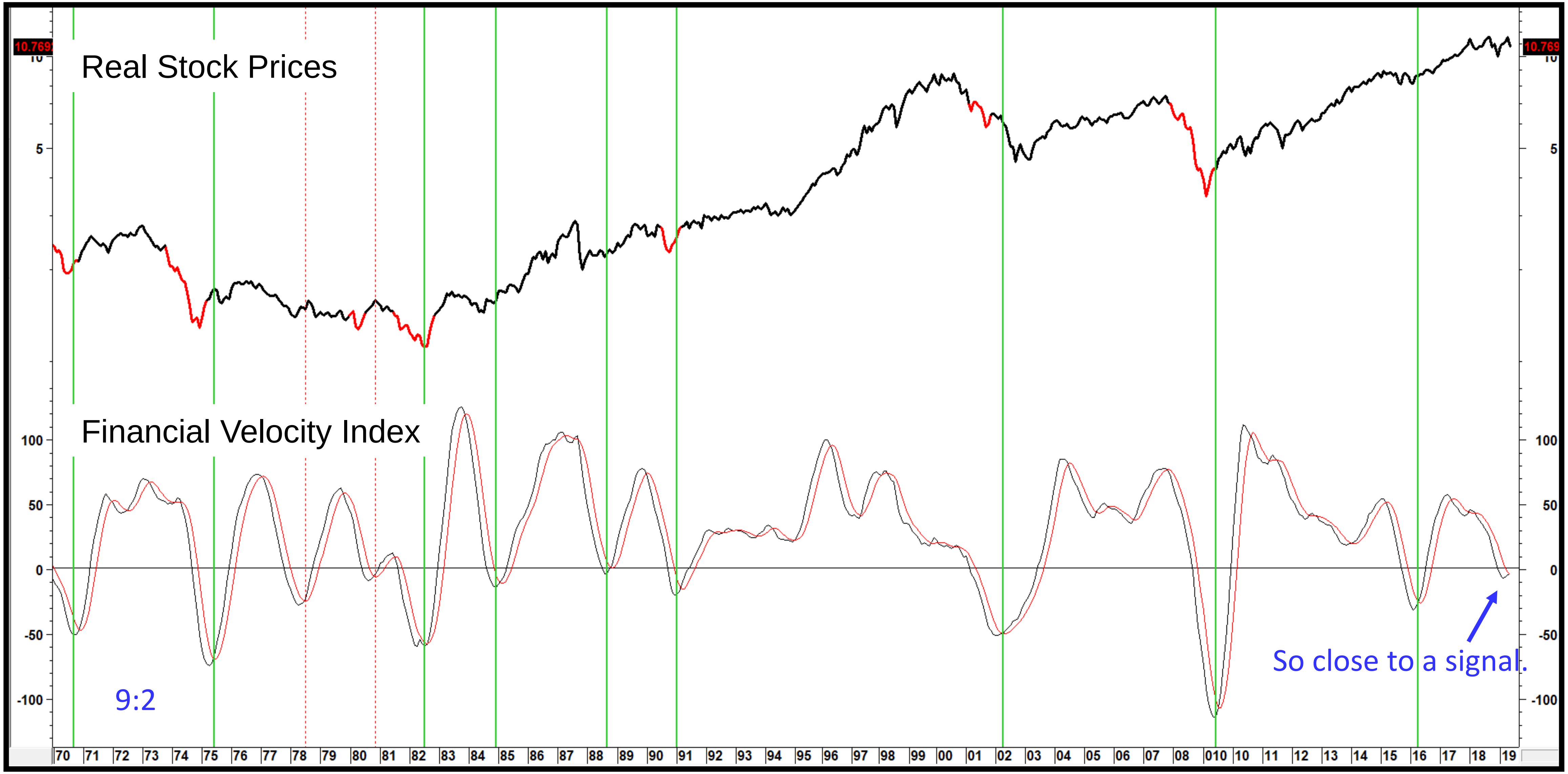
Except for 1999-2000 the Shiller P/E has never been higher. Records go back to 1870.

Inflation Adjusted Stocks and the Financial Velocity Indicator 1920-1969

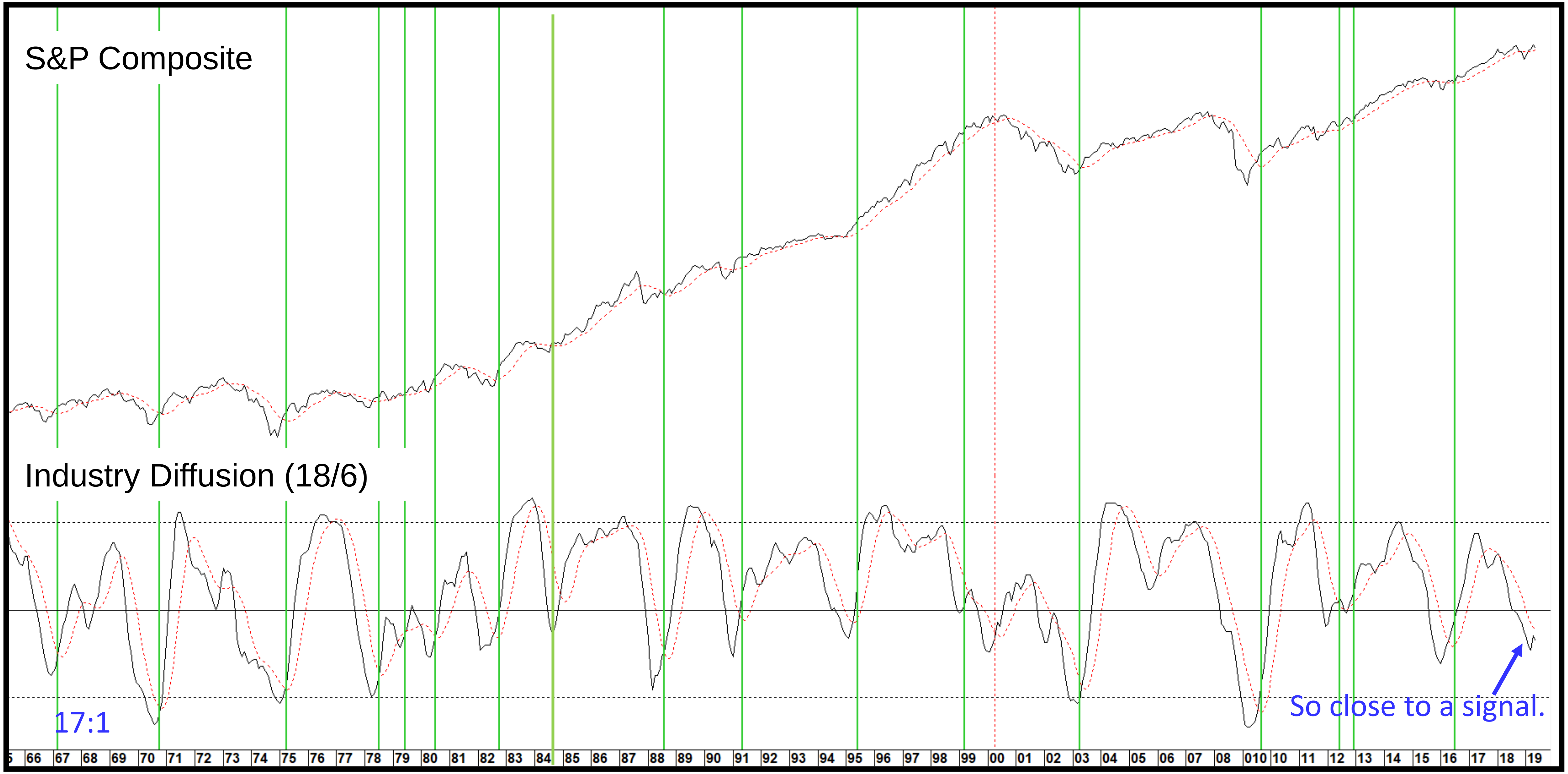


Upside reversals in Financial Velocity signal bull markets in inflation adjusted equities.

Inflation Adjusted Stocks and the Financial Velocity Indicator 1970-2019



S&P Composite and an Industry Diffusion Indicator 1965-2019

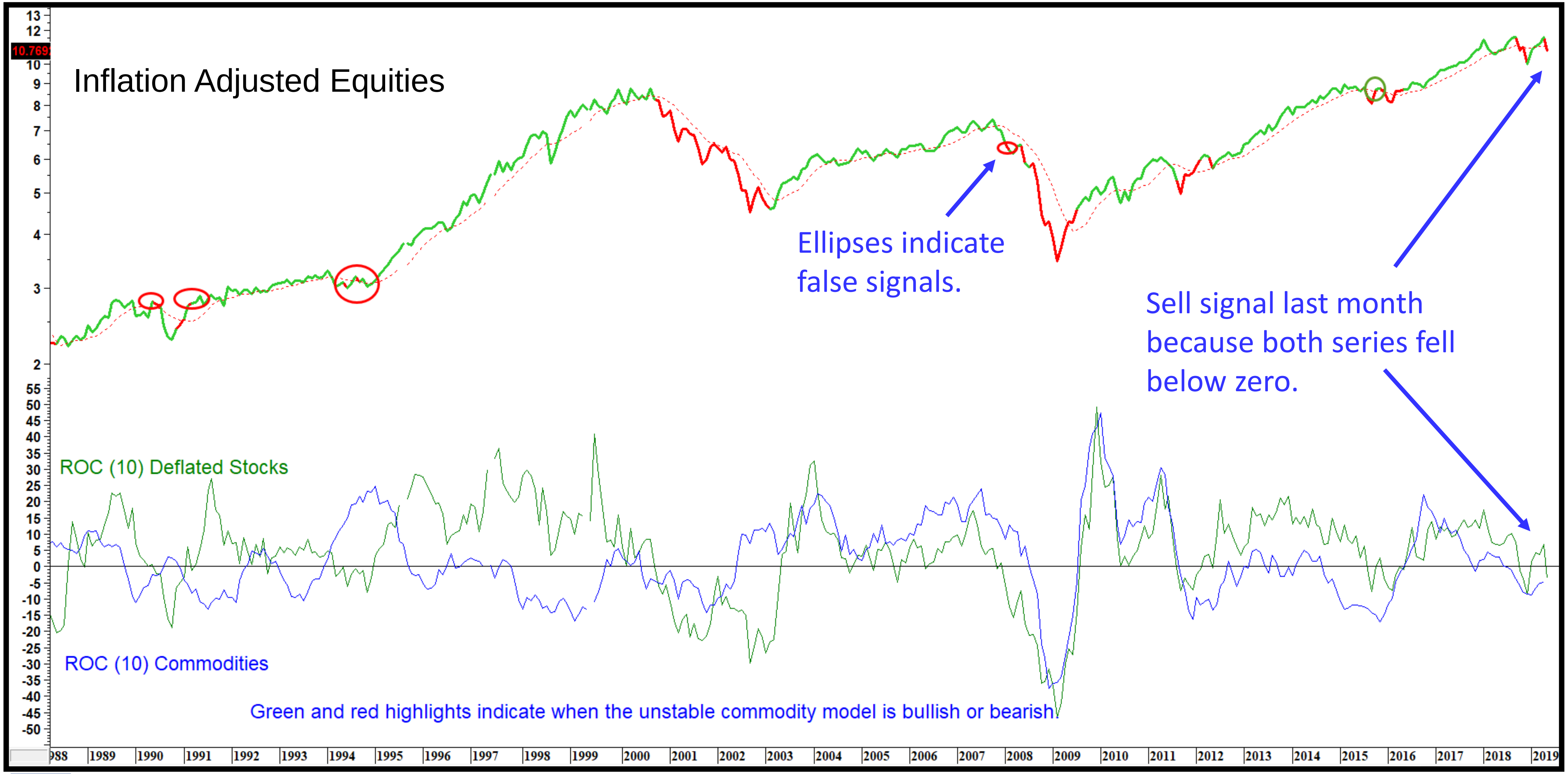


Oversold upside reversals signal bull moves in equities.

Inflation Adjusted Stocks and Equity and Commodity Momentum 1900-1982

Green and red highlights signal bullish and bearish periods as signaled by our Unstable Commodity model..

Inflation Adjusted Stocks and Equity and Commodity Momentum 1988-2019



Model went bearish in May.

Using intermarket and interasset relationships to identify the current environment.

Importance of Commodity/Bond Trend Reversals

1. Provides a clue as to where we are in the cycle.

2. Whether we should emphasize bonds or commodities in portfolios.

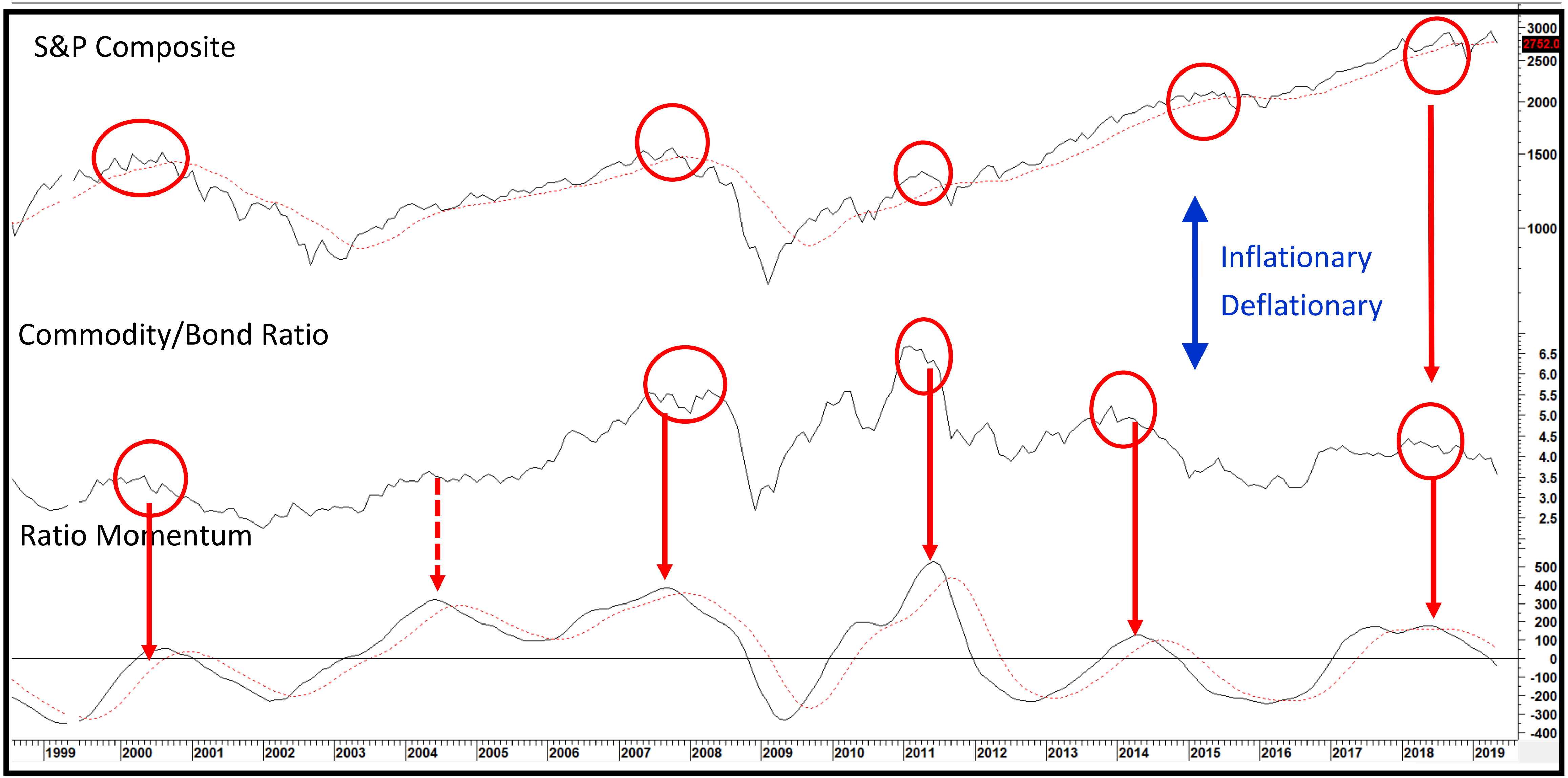
3. Should equity exposure be slanted to early or late cycle leaders?

Implication of a Commodity/Bond Reversal for Asset Allocations

Commodity/Bond momentum buy signals indicate that it's time to be emphasizing bonds and early cycle equities.

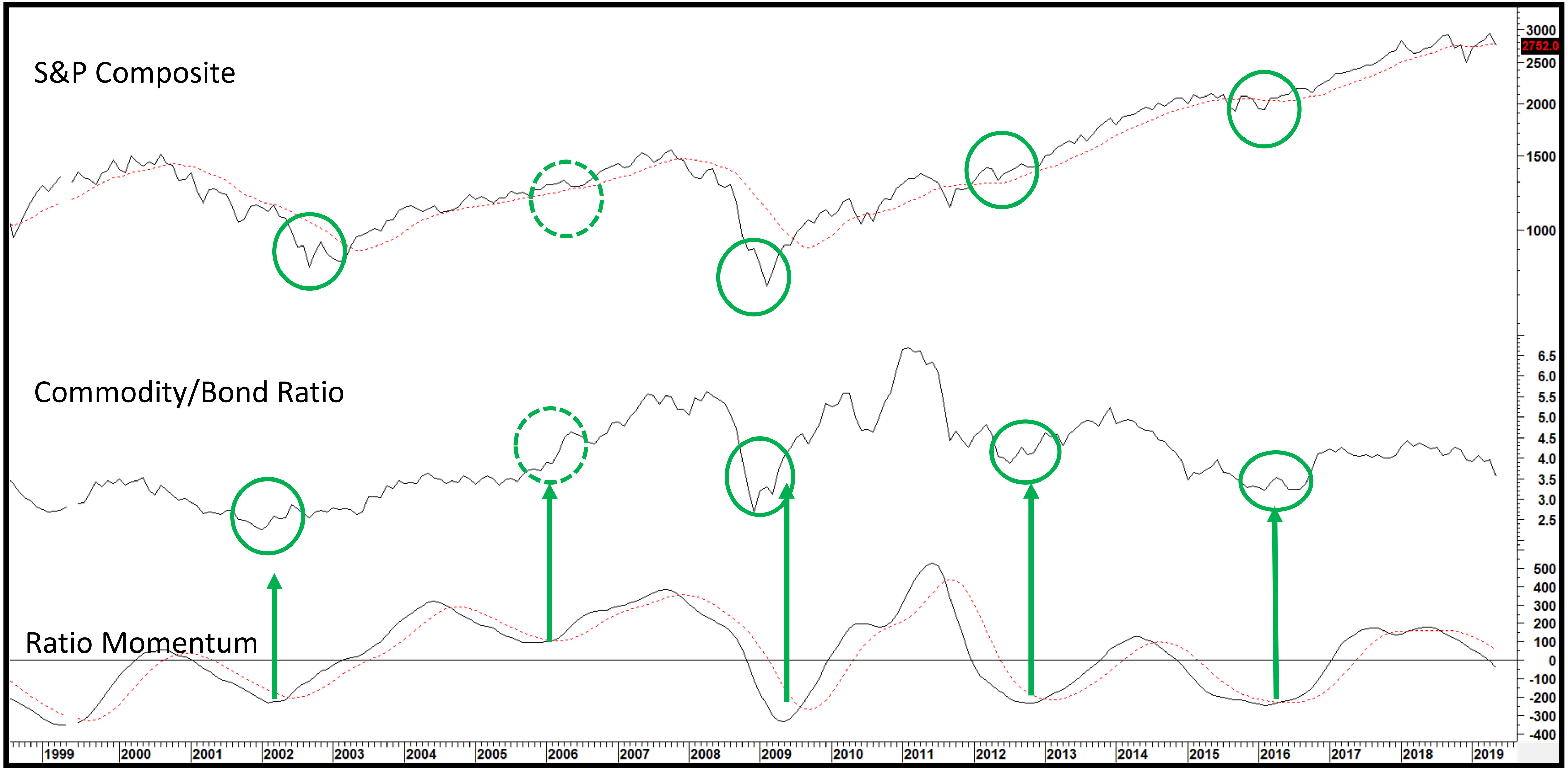
Commodity/Bond momentum sell signals indicate that it's time to be selling commodities and earnings driven equities.

S&P Composite vs Commodity/Bond Ratio 1998-2018



Commodity/Bond momentum sell signals when it’s time to lower equity exposure.

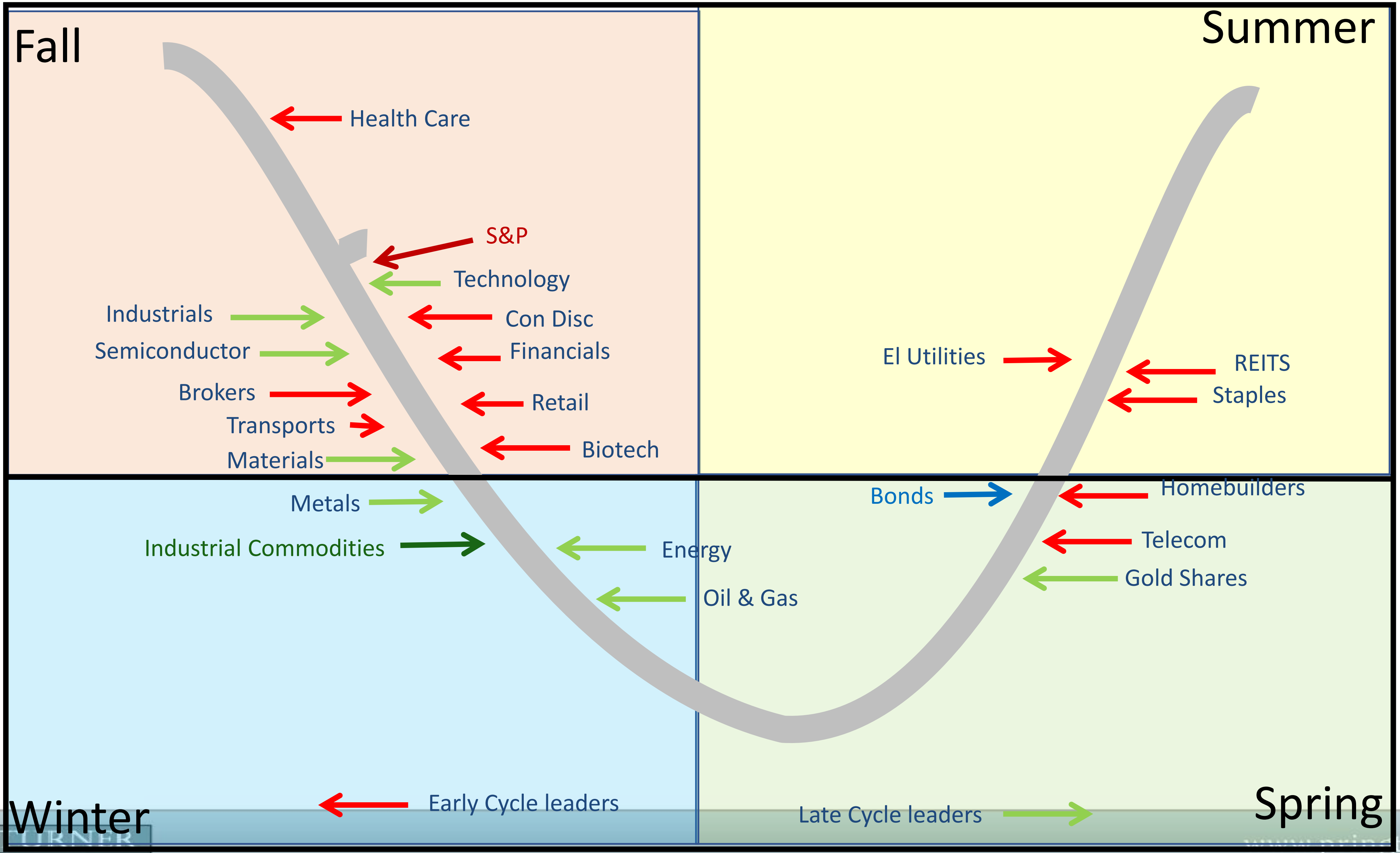
S&P Composite vs Commodity/Bond Ratio 1998-2018



Commodity/Bond momentum buy signals say when it's time to buy stocks.

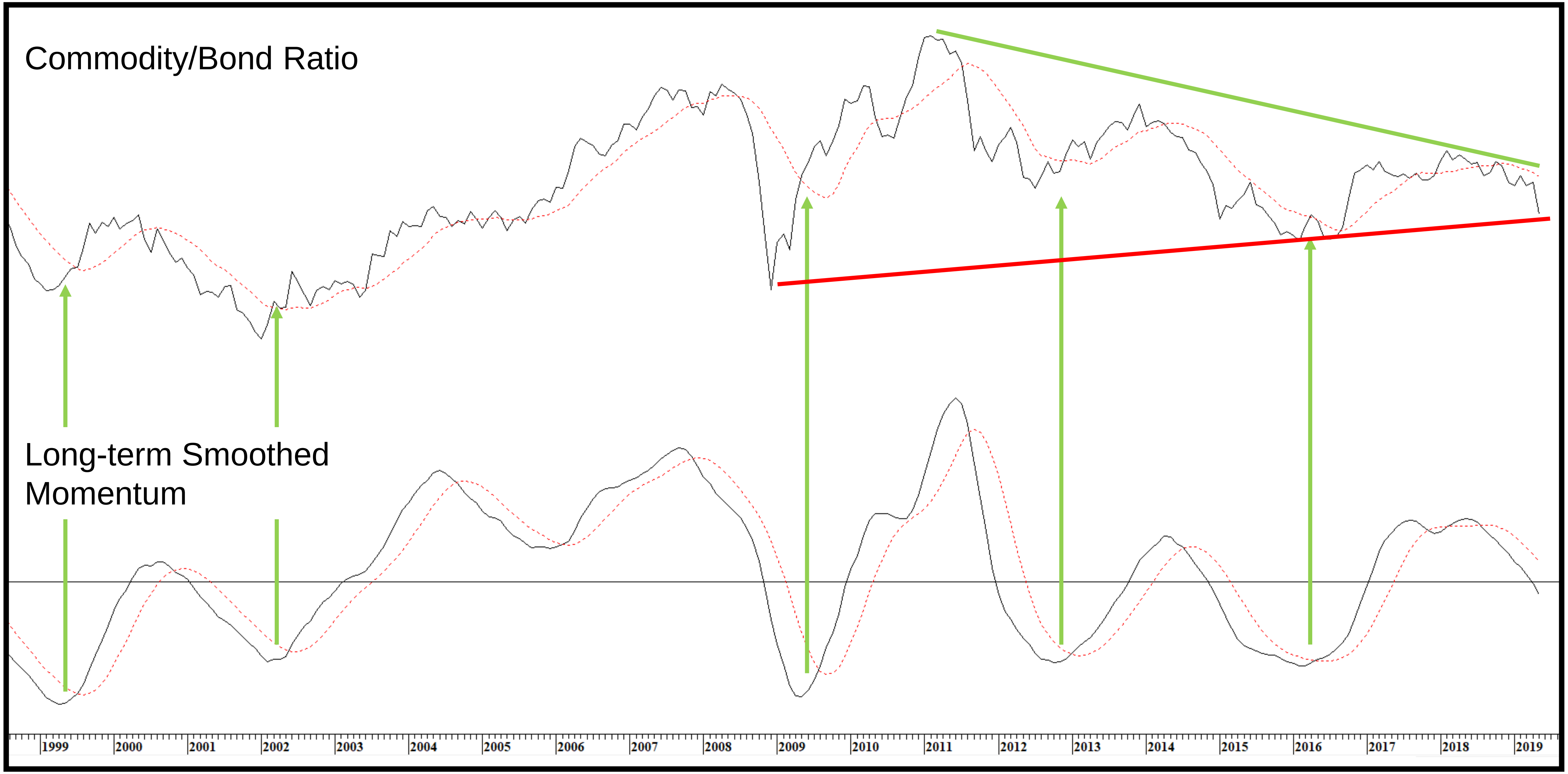
Long Term Momentum Position February 2014

Long Term Momentum Position June 2019



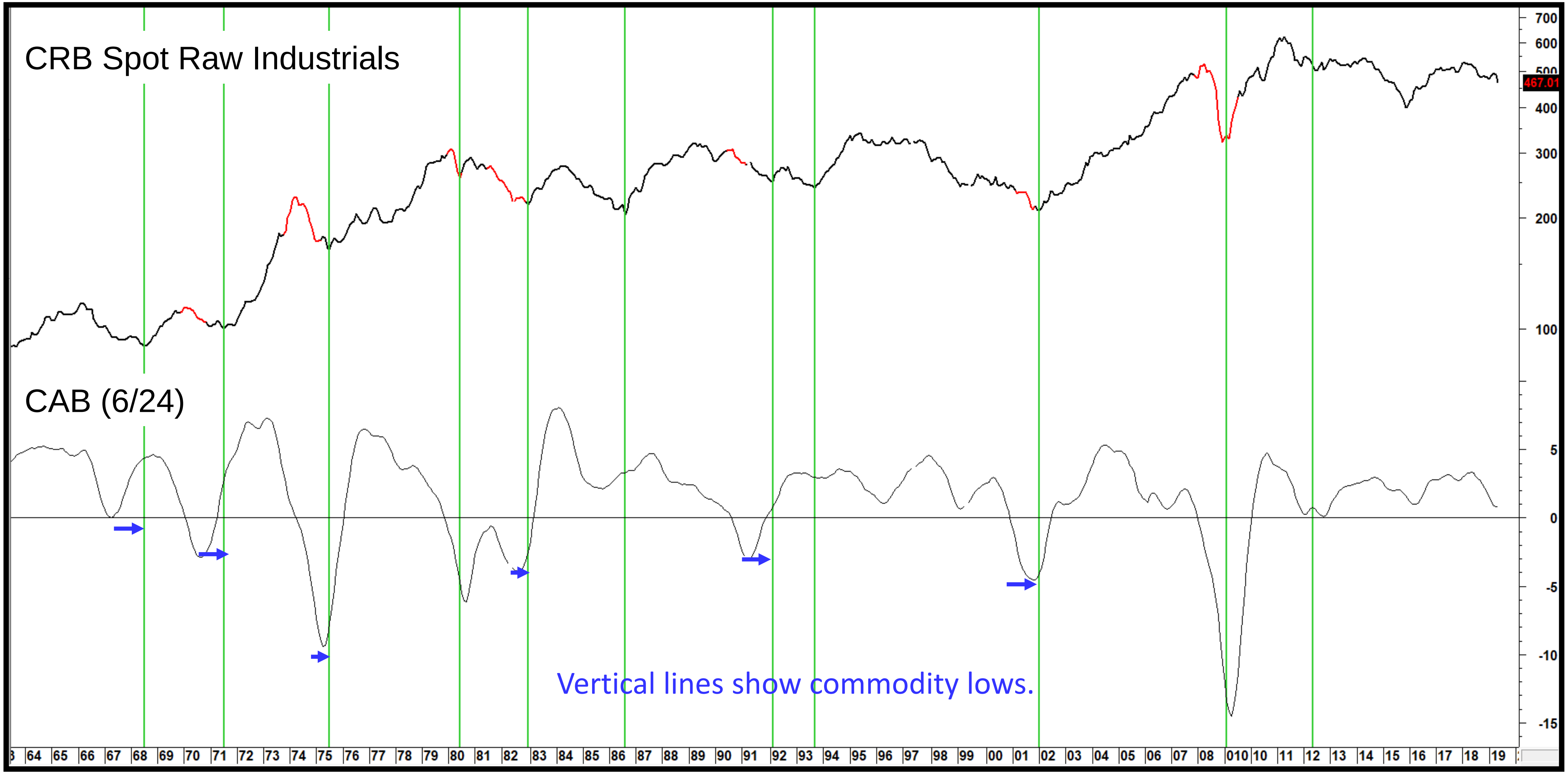
Commodities

Commodity/Bond Ratio and Long-term Momentum 1999-2019



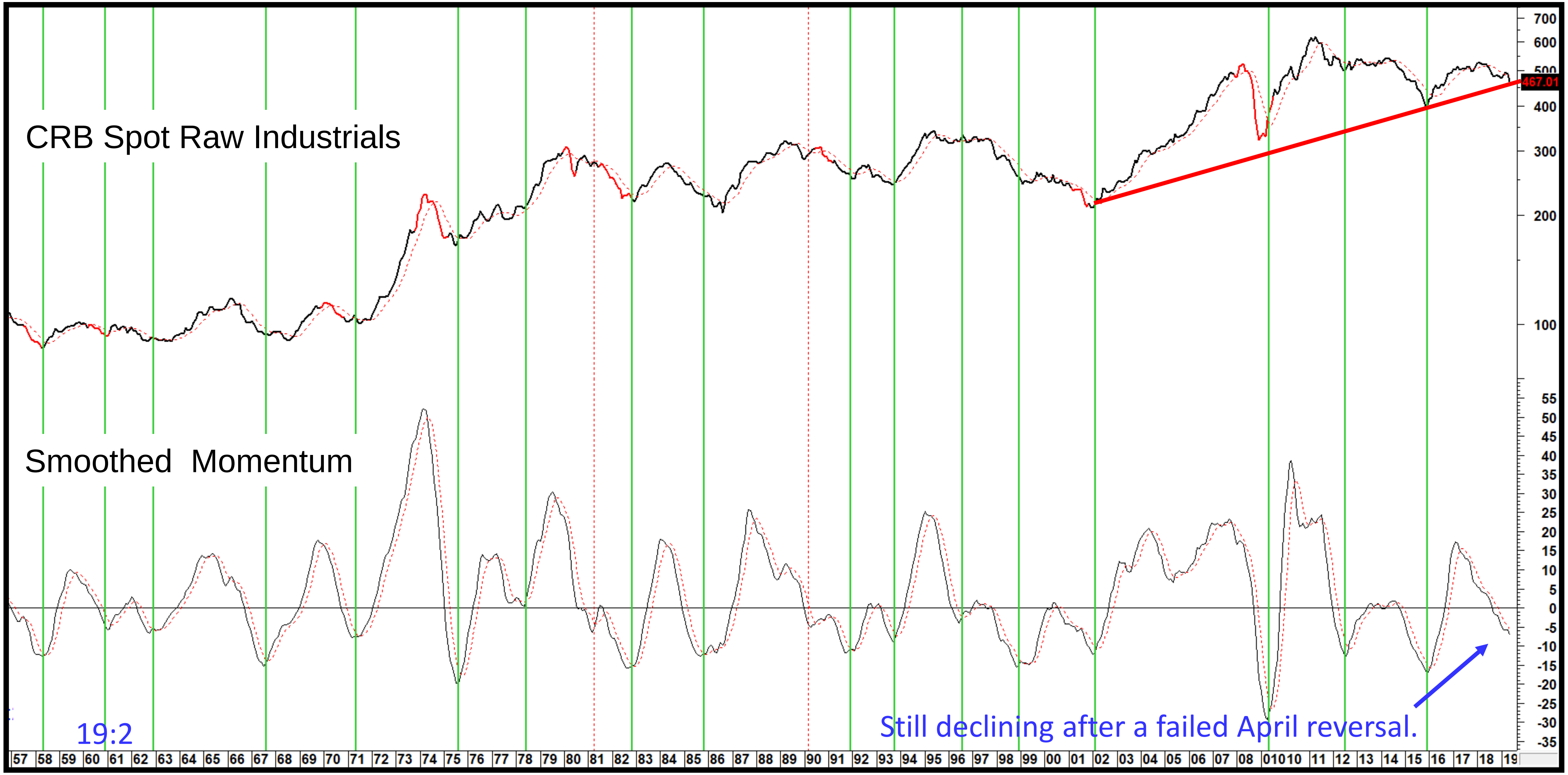
Commodity/Bond ratio is on the brink.

CRB Spot Raw Industrials and Chemical Activity Barometer Momentum 1963-2019



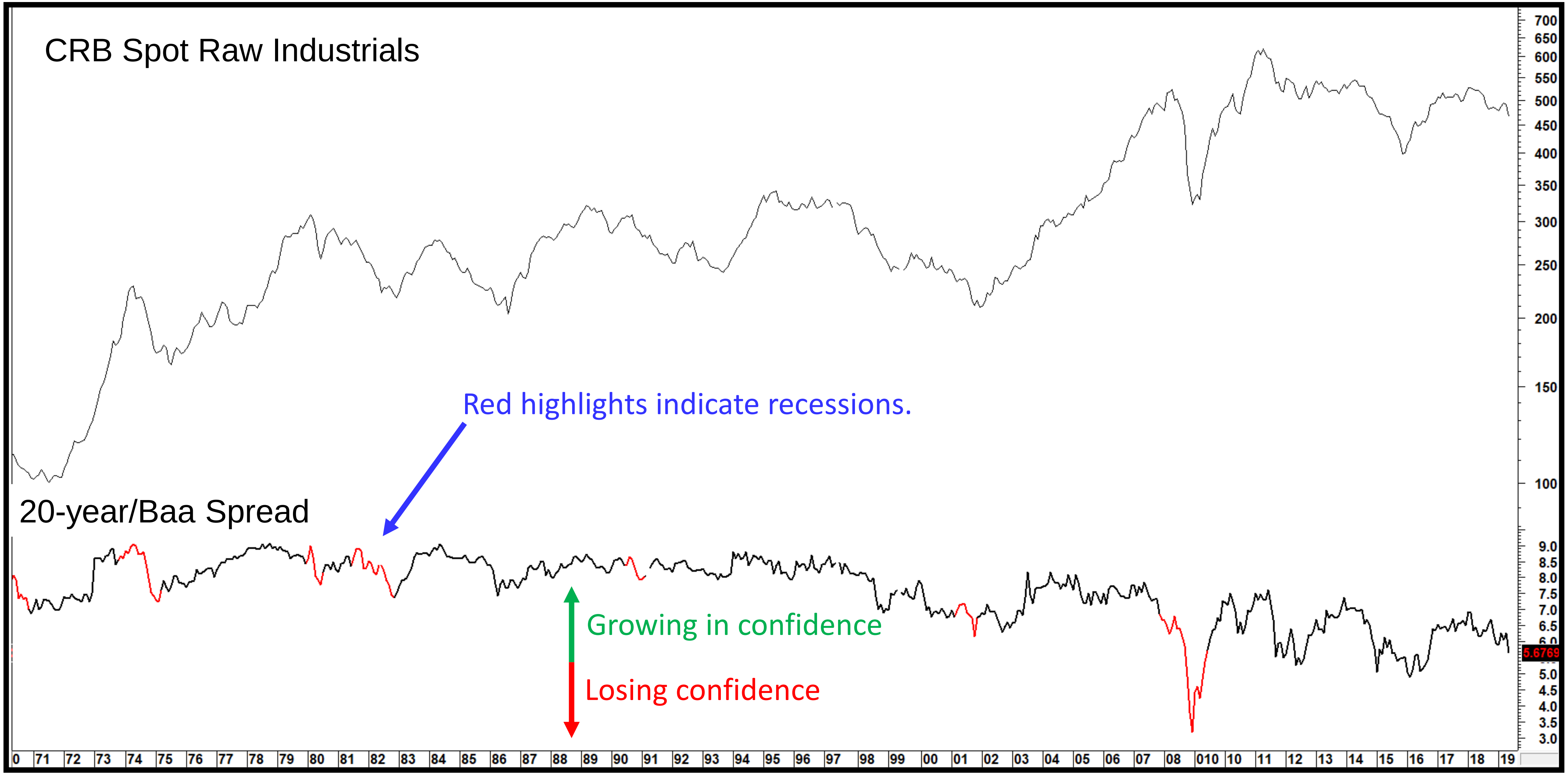
Chemical Activity Barometer momentum usually leads commodity prices.

CRB Spot Raw Industrials and Its Smoothed Momentum 1957-2019



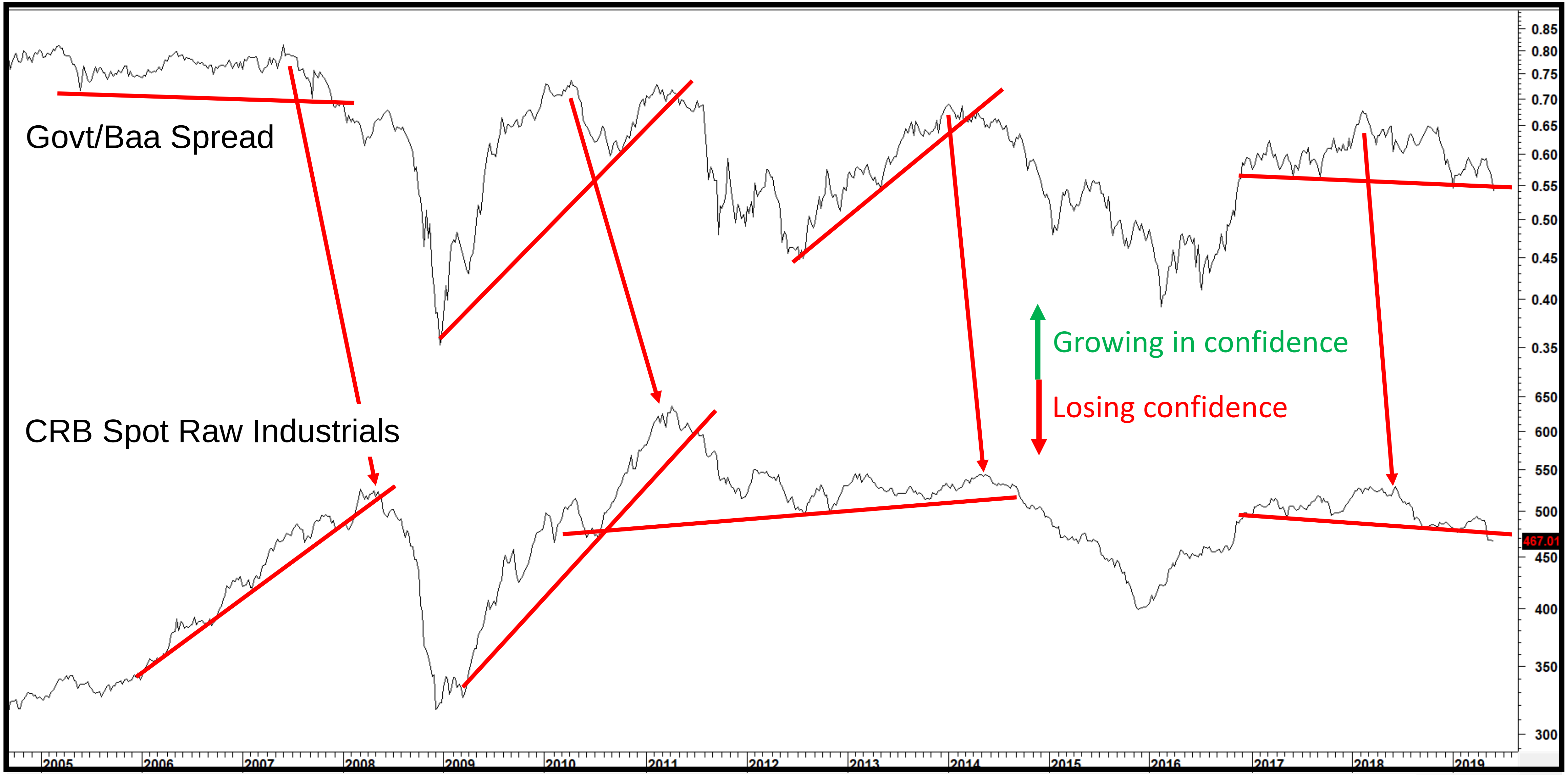
Commodities usually rise its momentum reverses.

CRB Spot Raw Industrials vs 20-year/BAA Credit Spread 1969-2019



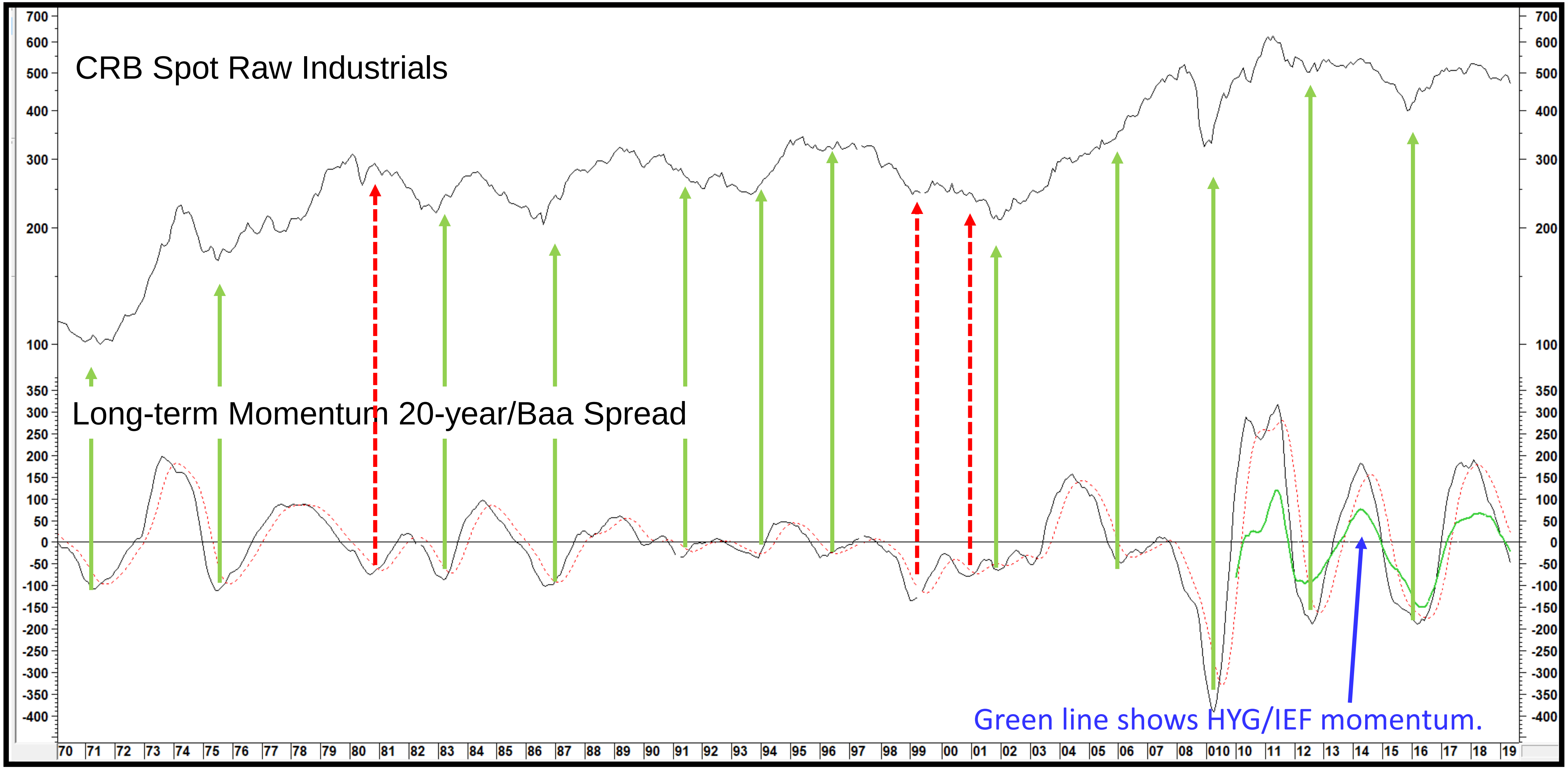
Commodities usually rise and fall on swings in confidence.

CRB Spot Raw Industrials vs 20-year/BAA Credit Spread 2005-2019



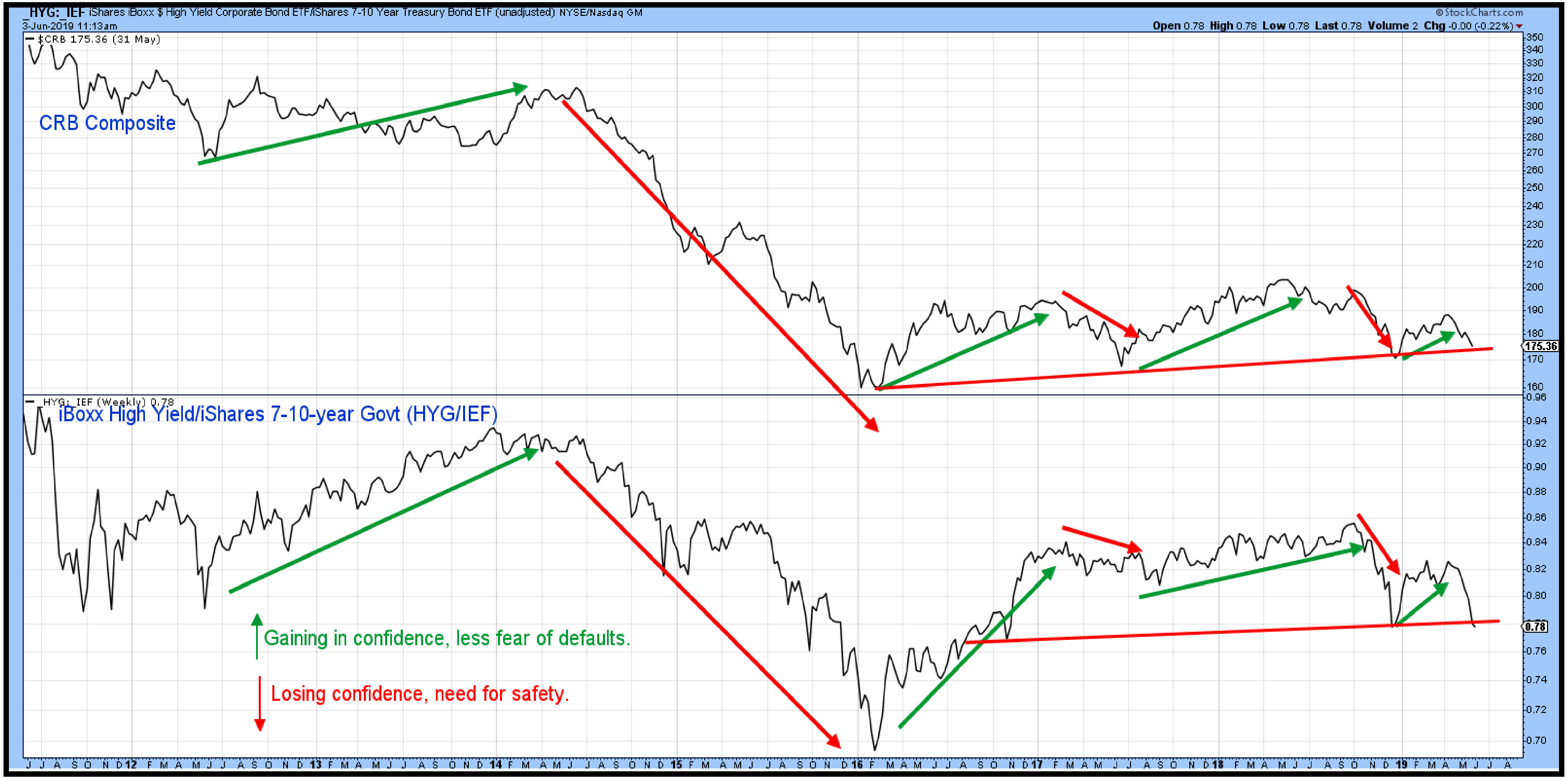
Commodities usually rise and fall on swings in confidence.

CRB Spot Raw Industrials vs 20-year/BAA Credit Spread 1970-2019



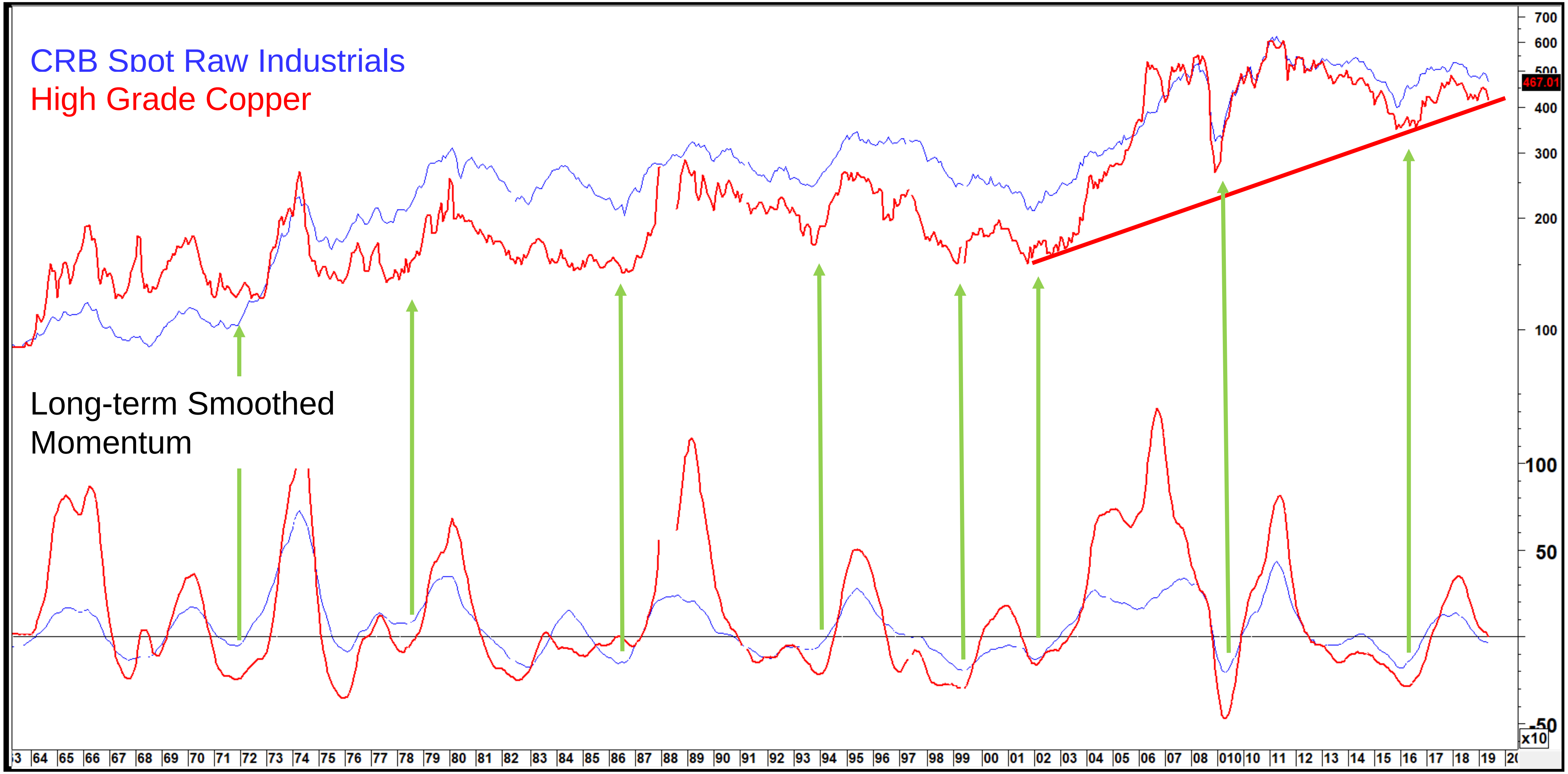
Commodities usually rise and fall on confidence..

CRB Spot Composite vs the HYG/IEF Ratio 2011-2019



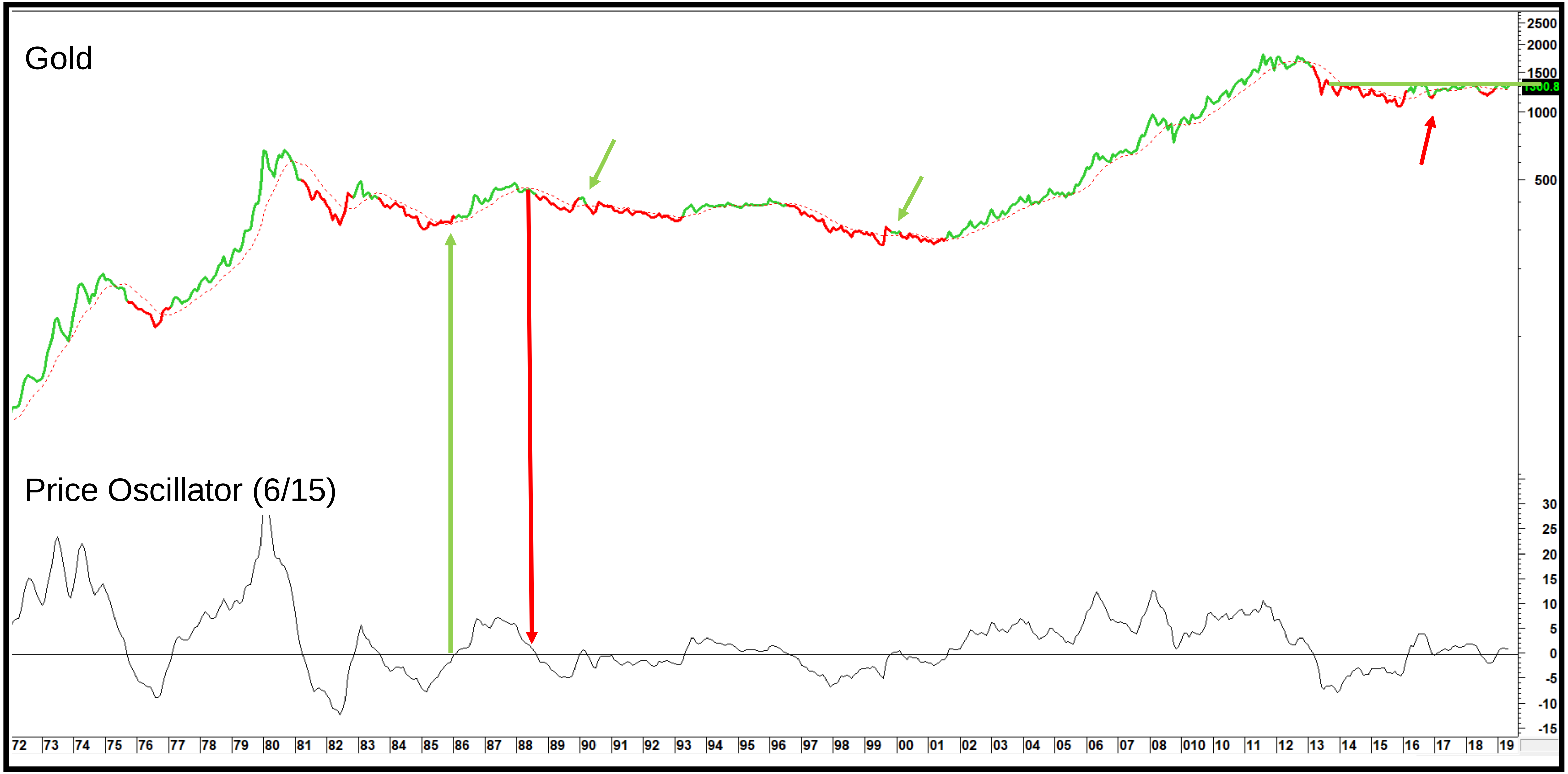
Ratio can be plotted at StockCharts.com for free using the symbols _HYG:_IEF

CRB Spot Composite vs Copper 1963-2019



Movements in copper are similar to the Index.

The Gold Price and a Price oscillator 1972-2019



Green and red highlights indicate when the oscillator is above or below zero..

The End

For more information please go to Pring.com or Pringturner.com