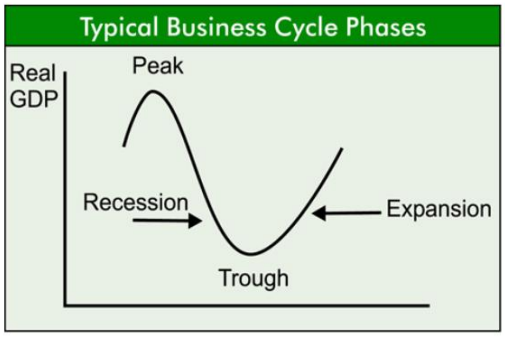


Name_____

**Industry Investment Strategy**

Based on our discussion in class and the information in the handout, formulate a "Industry Investment Strategy" with your partner. Discuss these questions, write down your answers on your own sheet, and hand it in at the end of class. It will be marked as an activity.

**1. Which industries do you think will perform well in the short term (next 10 weeks)? Why?**

**2. Which industries do you think will perform poorly in the short term (next 10 weeks)?**

**3. Which industries would you like to include in your SMG portfolio? List 3 companies in each of the industries you would like to include.**

# Cyclical vs Non-cyclical Industries

Investors cannot control the cycles of the economy, but they can adjust their investing practices with its ebbs and flows. Adjusting to economic transitions requires an understanding of how industries are characterized by their relationship to the economy. It's important for you to know the fundamental difference between cyclical and non-cyclical companies so that you can distinguish between sectors that are affected by economic changes and those that are more immune. Here we look at the industries that reside within these categories, and identify where it's best to put your money when the economy starts to decline.

**What Does Cyclical and Non-Cyclical Mean?**
These terms, cyclical and non-cyclical, refer to how highly correlated a company's share price is to economic fluctuations. Non-cyclical stocks repeatedly outperform the market when economic growth slows, while cyclical companies are highly correlated to the economy. The non-cyclical securities, also called defensive stocks, experience profit regardless of economic gyrations because they produce or distribute goods and services we always need: food, power, water and gas. The sales of companies with cyclical stocks, on the other hand, depend on whether or not the economy is strong; sales will thrive when people have extra income to spend on luxuries, and they'll decline when the economy slumps.

**The Concept**
The difference between cyclical and non-cyclical industries is simply the difference between necessity and luxury. There are certain items we can't live without and won't likely cut back on even when times are tough. The stocks of companies producing these things are non-cyclical and are "defended" against the effects of economic downturn, providing great places to invest when the economic outlook is sour. For example, household non-durable goods - a fancy term for the things you use up quickly around the house - such as toothpaste, soap, shampoo and dish detergent may not seem like essentials, but you can't really sacrifice them. Most people don't feel they can wait until next year to lather up with soap in the shower.

Contrast this to the new car you've had your eye on. Although it's more exciting to buy a new car than soap, you are more likely to postpone the car for a year or two if your finances feel the effects of an economic slump. Another good example of a cyclical industry is fine dining. When things are good people are more inclined to take the family out for an expensive meal; macaroni and cheese, on the other hand, has to suffice when finances are depressed. Other examples of cyclical industries are manufacturing, the steel industry, travel and construction - the sectors that produce things we can live without when money is tight. These are exactly the types of industries you want to avoid when the economy turns sour.

***Utilities***
An excellent example of a non-cyclical industry is utilities, which can help investors avoid losses when highly cyclical companies are suffering. For instance, selling your Caterpillar stock and buying a share in, say, Minnesota Power Inc. is a type of maneuver that investors have used for years during economic downturns. If times become tough, there's not much money for building projects, so construction companies are less likely to purchase heavy machinery. But, no matter what, people's top priority will always be to have power and heat

for themselves and their families. By providing a service that is consistently used, utility companies grow conservatively and do not fluctuate dramatically - these companies provide safety, but this also means they are not going to skyrocket when the economy experiences growth.

***Household Non-Durables***
As we mentioned before, people will always need certain essentials around the house. From deodorant to bleach, we can't really sacrifice the things that keep us and our living spaces clean. For this reason, companies such as Procter & Gamble, Colgate-Palmolive and the Gillette Co. are all attractive investment choices when the economy is in the dumps.

***Tobacco***
It is easy to see why tobacco companies are considered non-cyclical: it's hard for smokers to stop smoking, even during a recession. So a company such as British American Tobacco will exhibit more stability during these times. Even though tobacco is considered a "sin" industry and may be unethical for some investors, it does have the characteristics of a non-cyclical sector.

Read more: http://www.investopedia.com/articles/00/082800.asp#ixzz234R3qwQy