

Anatomy of a Recession: Economic and Market Outlook

Second Quarter 2023

As of June 1st

Anatomy of a Recession (AOR): US Recession Risk Indicators

ClearBridge Investments, one of Franklin Templeton's specialist investment managers, utilizes 12 different economic indicators to assess the risk of recession. Each individual indicator can signal expansion, caution or recession in the economy. The signals from each of the 12 indicators are combined into an overall dashboard signal. The indicators, signals and changes are based on ClearBridge's interpretation of the data. The dashboard is not a crystal ball but can serve as a tool to evaluate the risk of recession in the US economy.

There is no change to the Recession Risk Dashboard with the May 31st update after April's deterioration in Job Sentiment, Jobless Claims and Truck Shipments.

	Current ¹	Deepening Red Signal				
	May 2023	March 2023	December 2022	September 2022		
Consumer	Housing Permits	✗	✗	●	●	↑ Expansion ● Caution ✗ Recession
	Job Sentiment	✗	●	●	↑	
	Jobless Claims	●	↑	↑	↑	
	Retail Sales	✗	✗	✗	✗	
	Wage Growth	✗	✗	✗	✗	
Business Activity	Commodities	✗	✗	✗	✗	
	ISM New Orders	✗	✗	✗	✗	
	Profit Margins	✗	✗	✗	●	
	Truck Shipments	●	↑	↑	↑	
Financial	Credit Spreads	✗	✗	✗	✗	
	Money Supply	✗	✗	✗	✗	
	Yield Curve	✗	✗	✗	●	
Overall Signal	✗	✗	✗	✗		

1. Data as of May 31, 2023. Source: BLS, Federal Reserve, Census Bureau, ISM, BEA, American Chemistry Council, American Trucking Association, Conference Board, and Bloomberg. The ClearBridge Recession Risk Dashboard was created in January 2016. References to the signals it would have sent in the years prior to January 2016 are based on how the underlying data was reflected in the component indicators at the time.

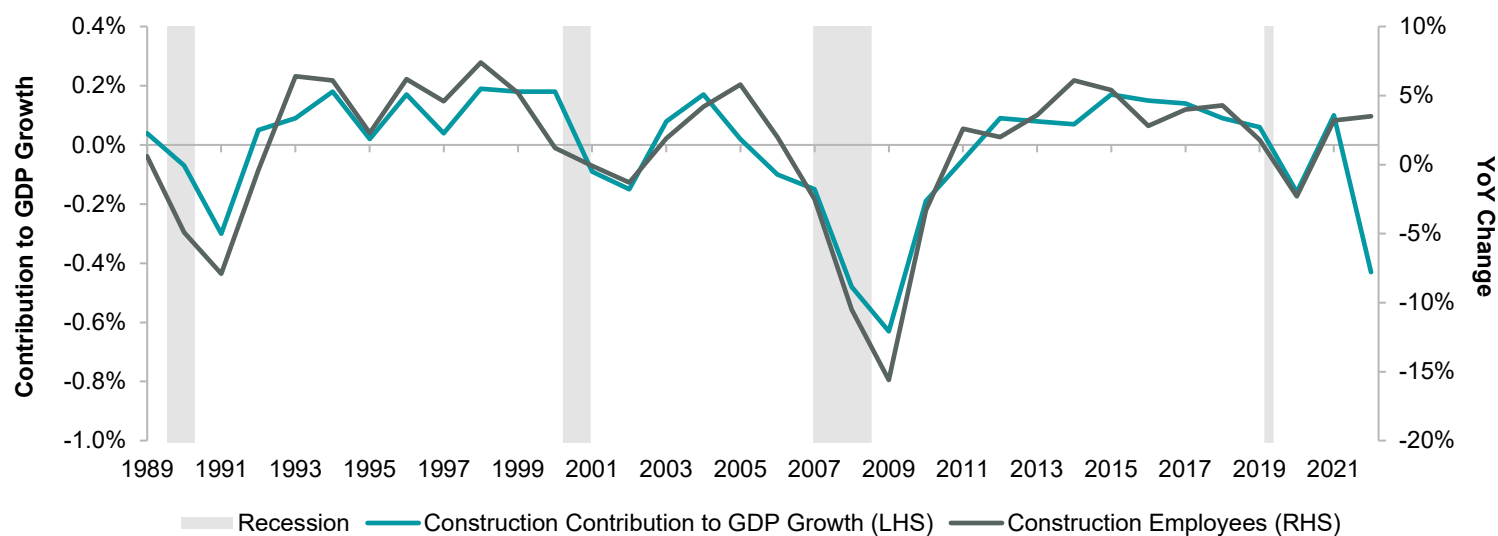
Where are we in the economic and market cycle?

Monetary policy takes time to impact the economy: long and variable lags²

Start of Persistent* Hike Cycle	Start of Recession	Recession Within 3.5 Years?	Length from Start of Hiking Cycle (Months)
Nov. 1958	April 1960	Yes	17
July 1963	Dec. 1969	No	76
Nov. 1968	Dec. 1969	Yes	12
Jan. 1973	Nov. 1973	Yes	9
Aug. 1977	Jan. 1980	Yes	29
Aug. 1980	July 1981	Yes	11
March 1984	July 1990	No	75
March 1988	July 1990	Yes	27
Feb. 1994	March 2001	No	85
June 1999	March 2001	Yes	20
June 2004	Dec. 2007	Yes	41
Dec. 2016	Feb. 2020	Yes	38
Average for All Hiking Cycles			37
Average in Recessions			23

- On average, a recession has historically begun a little over three years after a rate hike cycle gains momentum.
- In hard landing (recession) scenarios, this timeframe is condensed to just under two years.

Construction layoffs are on the horizon³



- Typically, employment in the construction industry closely tracks construction's contribution to GDP.
- This relationship has broken down recently given a backlog of completions. As the pipeline clears, history suggests construction labor should fall.

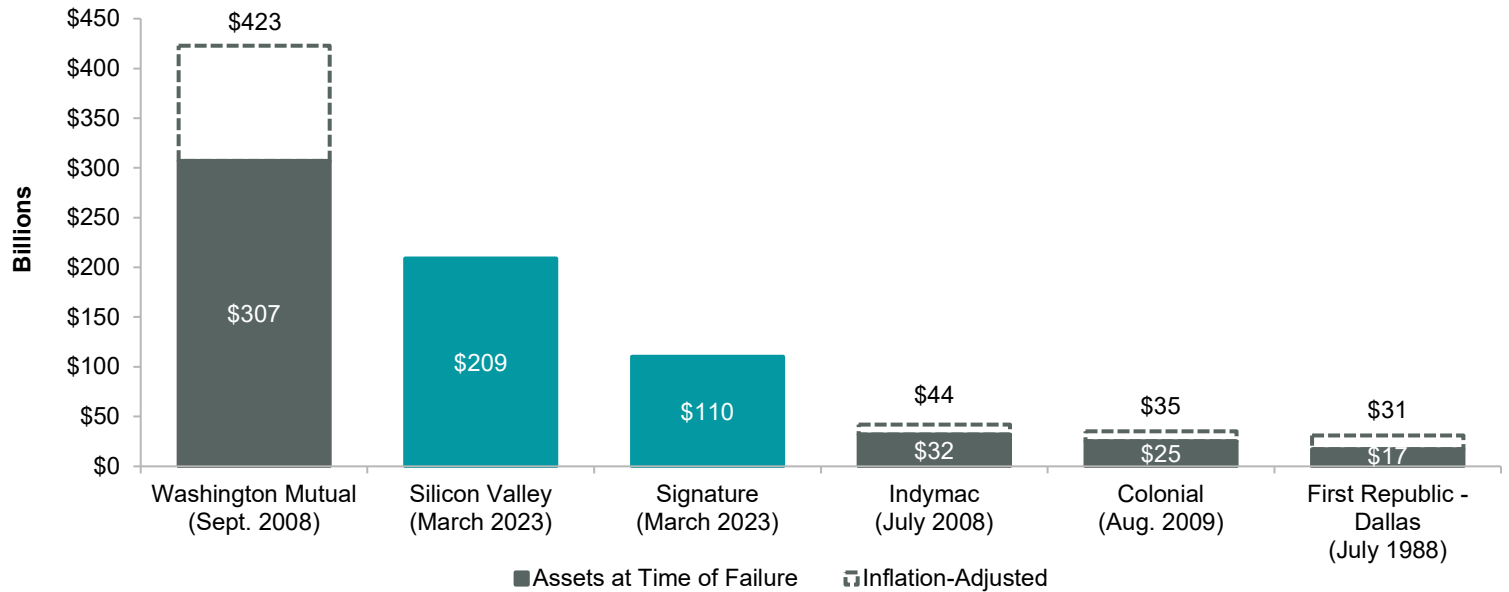
2. *Persistent Hike Cycle is when the vast majority of Fed rate hikes in a tightening cycle occur and may not align with initial hike when there have been long delays between initial and subsequent hikes. Source: FactSet. Past performance is not a guarantee of future results.

3. Data as of Dec. 31, 2022, latest available as of March 31, 2023. Source: BEA, BLS, NBER. Past performance is not a guarantee of future results.

Where are we in the economic and market cycle?

The first victims of the Fed's aggressive monetary policy

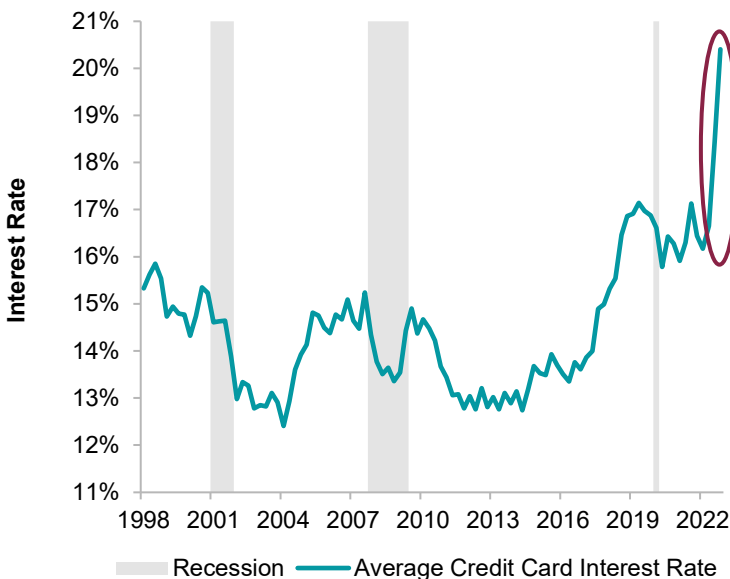
Largest bank failures in US history by assets⁴



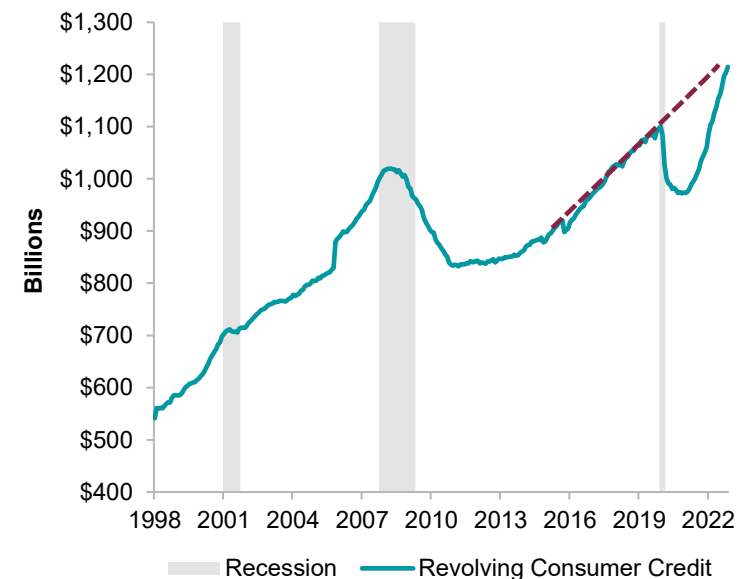
- Following a year of aggressive rate hikes, the first tangible sign of the lagged effects of tighter monetary policy has arrived.

A path to slower consumption

Average credit card rate⁵



Revolving consumer credit⁶



- The normalization in credit use has helped fuel consumption even as accumulated savings wane and wage gains moderate.
- Spiking credit card rates and the return to pre-pandemic trends in borrowing suggests that debt fueled consumption will be less of a boost going forward.
- Recent banking issues will likely tighten lending standards to consumers further into levels seen in prior recessions.

4. As of March 31, 2023. Source: BankRate, BLS and Bloomberg. Assets are rounded to nearest billion. Past performance is not a guarantee of future results.

5. Data as of Dec. 31, 2022, latest available as of March 31, 2023. Source: FactSet and Federal Reserve. Past performance is not a guarantee of future results.

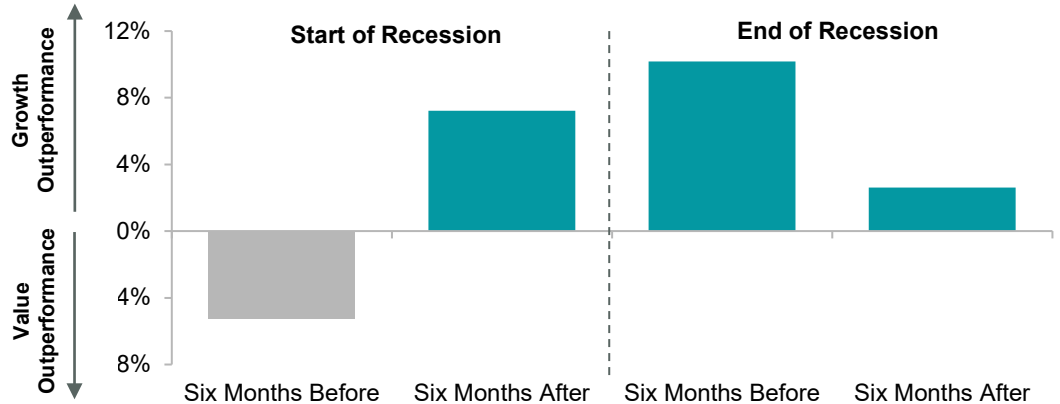
6. Data as of Feb. 28, 2023, latest available as of March 31, 2023. Source: FactSet and Federal Reserve. Past performance is not a guarantee of future results.

Possible market implications

Leadership to and through recessions

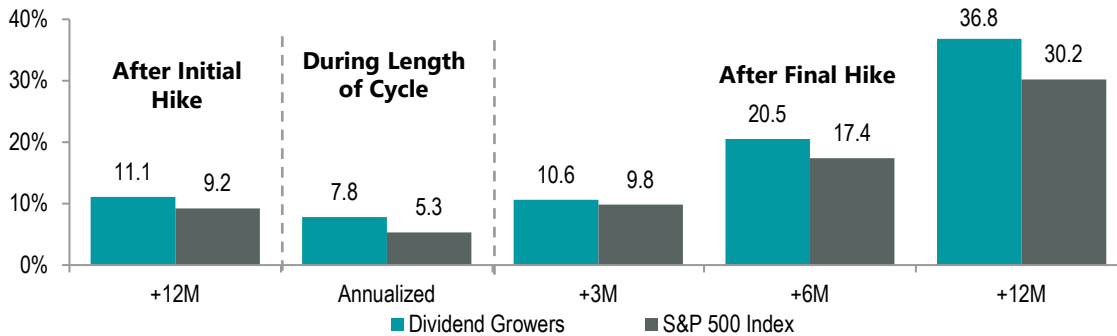
Growth vs. value relative performance around recessions⁷

- Typically, value has outpaced growth leading into a recession.
- However, leadership often flips with growth picking up the baton once the recession is underway.
- Quality is still key whether growth or value outperforms.



Dividend growers have historically dominated

Average return after initial Fed rate hikes, during cycle, and following end of Fed rate hike cycle since 1994⁸



- Dividend growth has historically been a desirable trait for equities during and after Fed hiking cycles.

7. Averages in the chart include the last three NBER recessions that occurred from March 15, 2001 through Nov. 16, 2001, Dec. 15, 2007 through June 15, 2009, and Feb. 15, 2020 through April 15, 2020. Indices used for each asset class include the following: Growth - Russell 1000 Growth; Value - Russell 1000 Value. Source: NBER, FactSet. Data as of March 31, 2023. Past performance is not a guarantee of future results. Investors cannot invest directly in an index, and unmanaged index returns do not reflect any fees, expenses or sales charges.

8. Source: BMO Capital Markets Investment Strategy Group, FactSet, Compustat, FRB. Dividend Growth Screening Methodology: S&P 500 stocks screened each month end, no dividend cuts in the past five years, latest one-year dividend per share growth greater than the S&P 500, current dividend yield greater than the S&P 500, free cash flow yield greater than the dividend yield, dividend payout ratio lower than the S&P 500. Past performance is not a guarantee of future results. Investors cannot invest directly in an index, and unmanaged index returns do not reflect any fees, expenses or sales charges.

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