FRANKLIN TEMPLETON

ClearBridge Investments

Anatomy of a Recession: Economic and Market Outlook

Third Quarter 2023

As of August 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 July 31 update after Q2 deterioration in Job Sentiment, Jobless Claims and Truck Shipments. We continue to believe there is a strong probability of a recession over the next 12 months.

		Current[1]	Deepening Red Signal		
		July 2023	**March 2023**	**December 2022**	**September 2022**
Consumer	Housing Permits	✗	✗	●	●
	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	✗	✗	✗	✗

↑ **Expansion**
● **Caution**
✗ **Recession**

1. Data as of July 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?

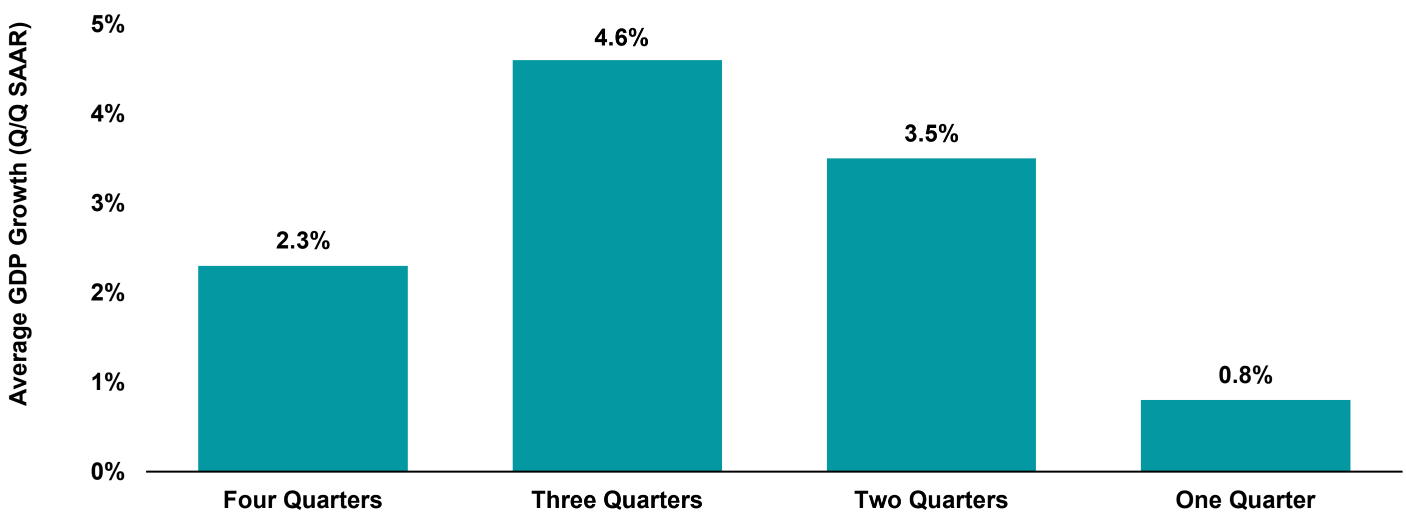
Monetary policy takes time to impact the economy: long and variable lags[2]

Start of a Hiking Cycle	Start of Recession	Recession Within 3.5 Years?	Duration 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 when recession started within 3.5 years	**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.

Economy can turn quickly[3]

GDP growth prior to onset of recessions



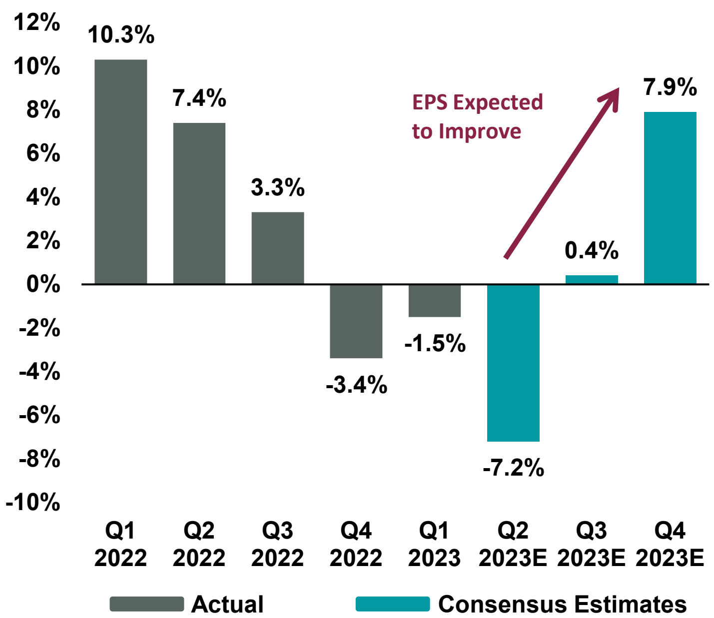
- Economic growth often holds up quite well leading into a recession, with a rapid decline only coming just before the onset.

2. A Persistent Hike Cycle is the period when the majority of Fed rate hikes occur in a tightening cycle. The date of the initial rate hike in the tightening cycle may not align with the start of the Persistent Hike Cycle. For example, a Persistent Hike Rate Cycle began in December of 2016, however the first hike in the tightening cycle was in December of 2015. The Fed than paused for 12 months before hiking again in December of 2016. Source: FactSet. Past performance is not a guarantee of future results.
3. The chart includes data from recessions according to NBER, starting with the recession that began in Dec. 1969. Data as of March 31, 2023, latest available as of June 30, 2023. Source: FactSet, U.S. Bureau of Economic Analysis , NBER. Past performance is not a guarantee of future results.

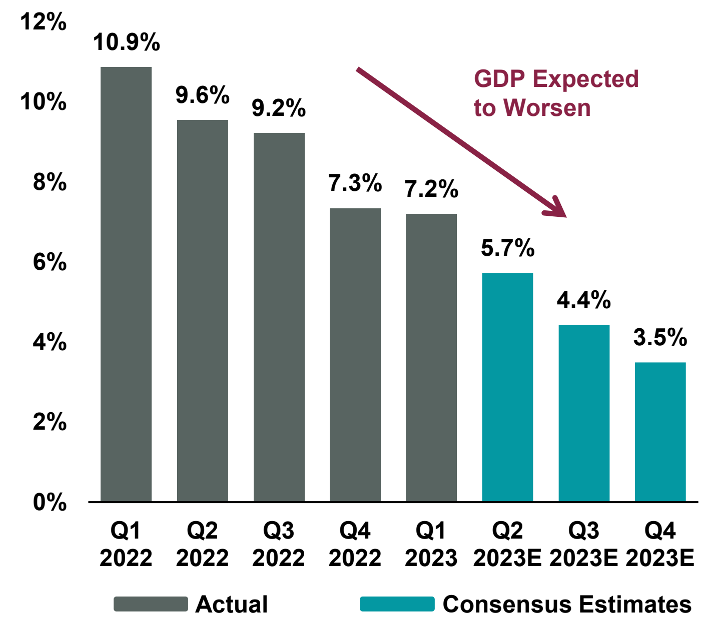
Where are we in the economic and market cycle?

Who's right?

S&P 500 EPS growth YoY[4]



Nominal GDP YoY[4]



- Consensus estimates for equity markets and the economy have diverged for 2023, providing fuel for both bulls and bears.

Cart before the horse?[5]

Recession Start	Recession End	Length (Months)	Market Low During Recession	Distance from Recession Start (Months)	Distance From Recession End (Months)
Nov. 1948	Oct. 1949	11	Yes	6	-5
July 1953	May 1954	10	Yes	1	-9
Aug. 1957	April 1958	8	Yes	2	-6
April 1960	Feb. 1961	10	Yes	6	-4
Dec. 1969	Nov. 1970	11	Yes	5	-6
Nov. 1973	March 1975	16	Yes	10	-6
Jan. 1980	July 1980	6	Yes	2	-4
July 1981	Nov. 1982	16	Yes	12	-4
July 1990	March 1991	8	Yes	2	-6
March 2001	Nov. 2001	8	No	18	10
Dec. 2007	June 2009	18	Yes	14	-4
Feb. 2020	April 2020	2	Yes	1	-1
Average		**10.3**		**6.6**	**-3.8**

- Historically, market lows have come around the two-thirds mark during recessions.
- The strength of the labor market would suggest this point is not yet on the immediate horizon.

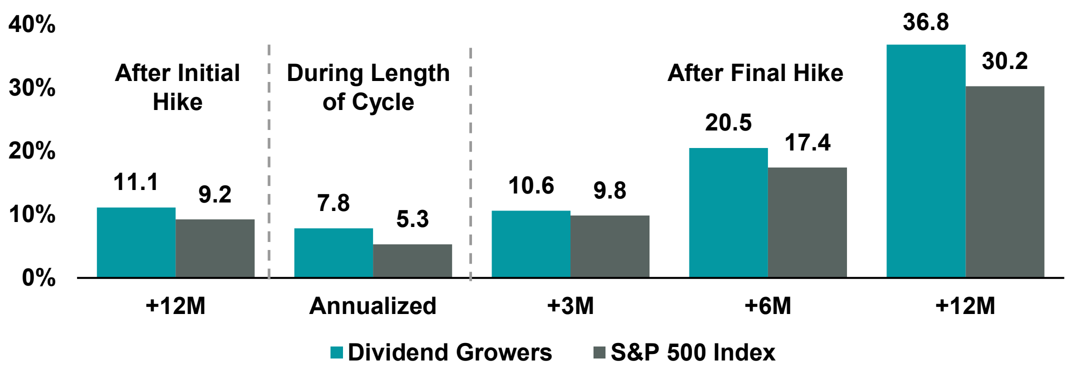
4. EPS Growth YoY is YoY growth of current constituents. Data as of June 30, 2023. Source: Bloomberg, BEA, FactSet, S&P. Past performance is not a guarantee of future results. Investors cannot invest directly in an index, and unmanaged index returns do not reflect any fees, expenses or sales charges.
5. Distance from recession start and distance from recession end do not add to length due to rounding. Source: NBER, S&P, FactSet, and Bloomberg. 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.

Possible market implications

Dividend growers have historically dominated

Average return after initial Fed rate hikes, during cycle, and following end of Fed rate hike cycle since 1994[6]

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



Normalizing volatility, higher returns?

Historical 12-month annualized returns by starting MOVE Index level[7]

	Leveraged Loans	Corporate Bonds	Emerging Market Bonds	Global Bonds	High Yield Bonds	Multi-Sector	MBS	TIPS	Short-Term Bonds	U.S. Treasury Bonds
MOVE <76	4.10%	3.05%	3.34%	1.27%	5.25%	1.41%	2.09%	2.74%	1.85%	2.15%
MOVE 76-100	4.36%	4.93%	8.41%	3.21%	4.85%	3.34%	4.20%	6.08%	2.86%	4.29%
MOVE >100	6.05%	7.85%	13.41%	6.45%	10.56%	6.63%	5.95%	7.66%	4.05%	5.53%
Average	4.78%	5.03%	7.78%	3.38%	6.81%	3.53%	3.83%	5.13%	2.79%	3.75%

- Historically, when bond market volatility has been elevated at these levels (MOVE >100), subsequent 12-month returns were strong.

Current MOVE Index (as of June 30, 2023): 110.64

6. 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.
7. The MOVE Index measures U.S. interest rate volatility through U.S. Treasury options pricing and is designed to measure fixed income market sentiment. Data represents period from January 29, 1999 through June 30, 2023, as of June 30, 2023. Source: ICE, Bank of America Merrill Lynch, Bloomberg, Credit Suisse. 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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