FRANKLIN TEMPLETON

ClearBridge

Anatomy of a Recession: Economic and Market Outlook

Fourth Quarter 2024

As of November 1

US Economic Outlook[1]

Fourth Quarter 2024

- The US economy appears headed toward a soft landing. The overall signal from the ClearBridge Recession Risk Dashboard is in green with continuous improvement throughout 2024.
- The consumer has been a bright spot despite a normalizing labor market. Strong consumer balance sheets and resilient wage gains should continue to drive consumption in the coming year.
- The Fed has embarked upon its long-awaited cutting cycle. History shows this should lead to a pickup in economic activity in 1H 2025.

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.

		Current[2]		
		October 2024	June 2024	March 2024
Consumer	Housing Permits	Caution	Caution	Caution
	Job Sentiment	Recession	Recession	Recession
	Jobless Claims	Expansion	Caution	Caution
	Retail Sales	Caution	Caution	Caution
	Wage Growth	Expansion	Expansion	Recession
Business Activity	Commodities	Expansion	Caution	Caution
	ISM New Orders	Recession	Caution	Caution
	Profit Margins	Expansion	Expansion	Recession
	Truck Shipments	Caution	Caution	Caution
Financial	Credit Spreads	Expansion	Expansion	Caution
	Money Supply	Caution	Caution	Recession
	Yield Curve	Recession	Recession	Recession
	Overall Signal	Expansion	Expansion	Caution

Expansion

Caution

Recession

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.

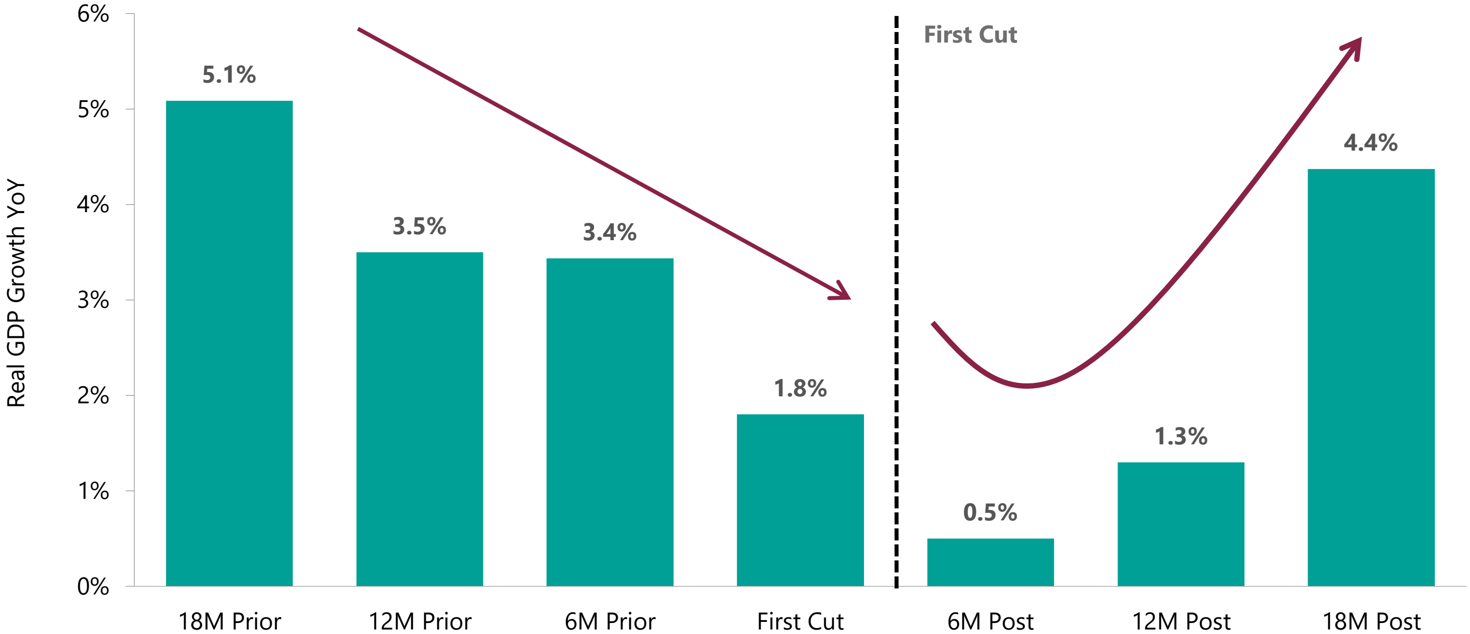
1. As of October 31, 2024. All opinions and data included in this commentary are as of the publication date and are subject to change. The opinions and views expressed herein are of the author and may differ from other portfolio managers or the firm as a whole and are not intended to be a forecast of future events, a guarantee of future results or investment advice. This information should not be used as the sole basis to make any investment decision.

2. Sources: BLS, Federal Reserve, Census Bureau, ISM, BEA, American Chemistry Council, American Trucking Association, Conference Board, Bloomberg, CME, FactSet and Macrobond. Data as of October 31, 2024. 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.

Not a Deposit | Not FDIC Insured | May Lose Value | Not Bank Guaranteed

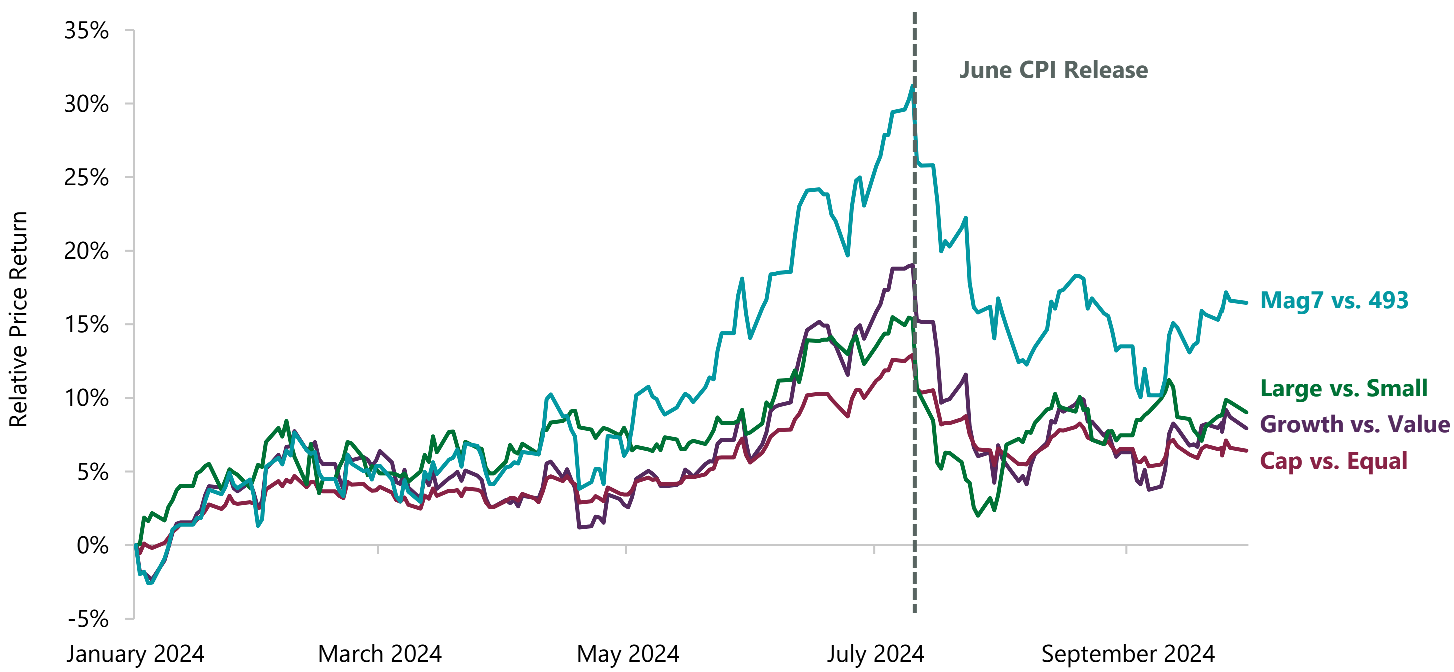
Not insured by any Federal Government Agency

Economy Needs Fed Resuscitation[3]



- Sustained Fed cut cycles have historically led to inflections in economic growth two quarters later.
- With the long-awaited cutting cycle now underway, the economy should re-accelerate in 2025.

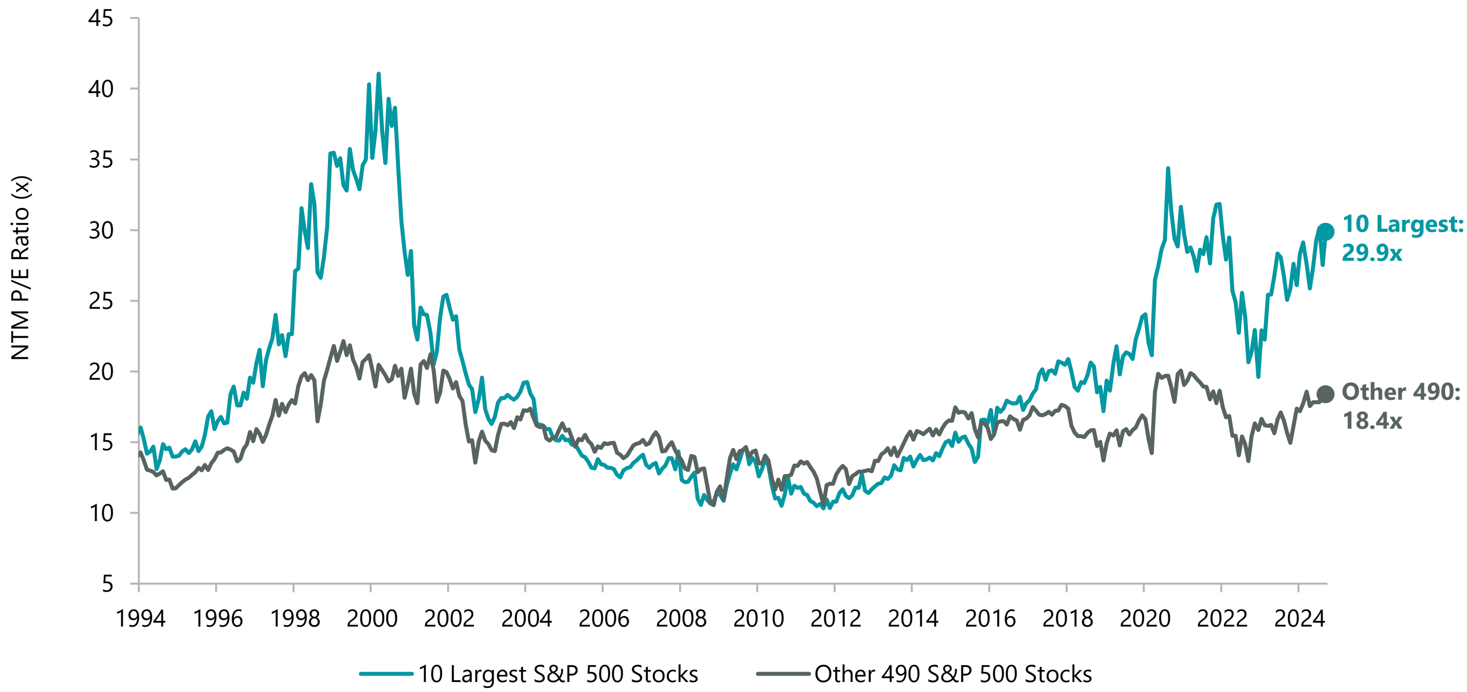
The Rotation Has Begun[4]



- Market leadership experienced a reversal following the soft June CPI data that paved the way for the Fed cutting cycle to commence.
- Recent leadership trends could persist in 2025 should a soft landing occur.

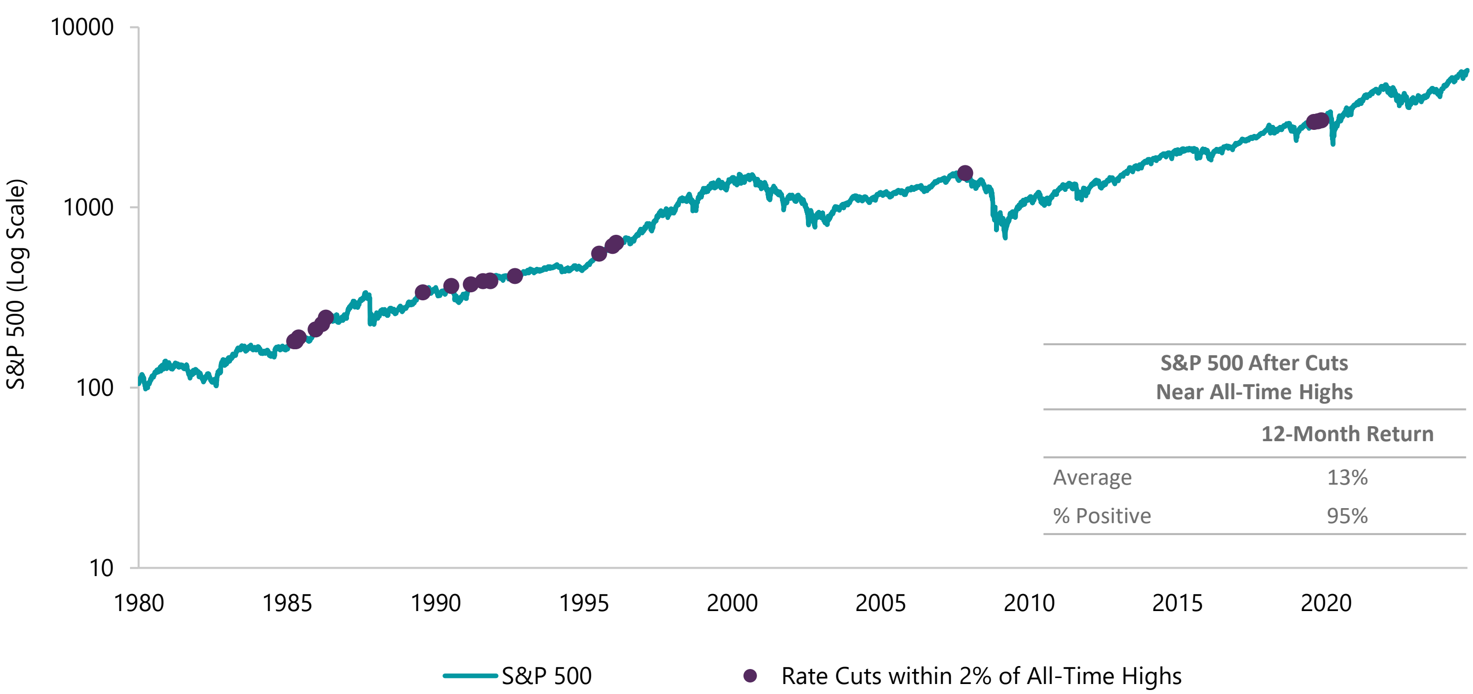
3. Sources: BEA, Federal Reserve, FactSet. Data as of September 30, 2024. Rate-cut cycles of at least 75 bps that did not occur within broader hiking cycles.
4. Sources: S&P, Russell, UBS, and Bloomberg. Data as of September 9, 2024. Note: Mag7 vs. 493 is the UBS Magnificent 7 relative price return vs. UBS S&P ex Magnificent 7; Cap vs. Equal is the S&P 500 relative price return vs. S&P 500 Equal Weight; Large vs. Small is the Russell 1000 relative price return vs. Russell 2000; Growth vs. Value is the Russell 1000 Growth relative price return vs. Russell 1000 Value.

Largest Stocks Distorting Valuations[5]



- The largest stocks in the S&P 500 Index trade at a significant premium which is distorting the broader benchmark's valuation.
- The typical stock (other 490) trades at a more reasonable valuation, closer to historical averages.

Cuts Near All-Time Highs a Good Omen[6]



- Equities have historically continued to move higher in the year following historical Fed cuts that came with the S&P 500 near all-time highs.

5. Source: UBS. Data as of September 30, 2024. NTM = Next 12 Months.
6. Source: FactSet. Data as of Sept. 26, 2024.

Equity Leadership Following the Cut[7]

Initial Rate Cut	Economic Outcome	Subsequent 12-Month Price Return: Cash (3M T-Bills)	Russell 1000 Growth	Russell 1000 Value	Russell Mid Cap	Russell 2000
Apr. 1980	Recession	13.5%	39.0%	30.1%	51.41%	66.3%
June 1981	Recession	15.9%	-18.4%	-15.2%	-18.35%	-20.5%
Oct. 1984	Soft Landing	8.9%	9.5%	10.8%	11.96%	8.5%
June 1989	Recession	8.7%	17.5%	4.2%	4.50%	-1.5%
July 1995	Soft Landing	5.5%	22.5%	18.2%	17.26%	19.1%
Jan. 2001	Recession	4.4%	-15.6%	-5.7%	-3.08%	5.3%
Sept. 2007	Recession	3.2%	-17.6%	-25.4%	-19.29%	-12.8%
July 2019	Recession	1.5%	24.9%	-9.2%	-0.71%	-5.7%
Average		**7.7%**	**7.7%**	**1.0%**	5.5%	7.3%
Recessionary Average		**7.8%**	5.0%	**-3.5%**	2.4%	5.2%
Soft Landing Average		**7.2%**	**16.0%**	14.5%	14.6%	13.8%

- Cash and large-cap growth stocks have historically performed best following the commencement of a rate-cutting cycle.
- Rate cuts that preceded soft landings have historically given way to substantial equity outperformance compared with cash.

Bond Leadership Following the Cut[8]

Initial Rate Cut	Economic Outcome	Subsequent 12-Month Return: Cash (3M T-Bills)	Short-Term Bonds	US Treasury Bonds	Core/Core Plus Bonds	Investment-Grade Corporate Bonds	High-Yield Bonds
Apr. 1980	Recession	13.5%	15.1%	13.1%	13.0%	13.2%	
June 1981	Recession	15.9%	16.9%	15.2%	14.9%	14.6%	
Oct. 1984	Soft Landing	8.9%	16.4%	20.6%	22.0%	23.8%	22.7%
June 1989	Recession	8.7%	9.3%	8.7%	9.4%	9.2%	-2.6%
July 1995	Soft Landing	5.5%	5.5%	2.8%	3.3%	3.0%	9.7%
Jan. 2001	Recession	4.4%	8.0%	4.9%	7.0%	8.8%	5.1%
Sept. 2007	Recession	3.2%	5.9%	10.6%	6.0%	-1.7%	-4.7%
July 2019	Recession	1.5%	4.4%	12.0%	10.2%	12.6%	4.0%
Average		7.7%	10.2%	**11.0%**	10.8%	10.4%	**5.7%**
Recessionary Average		7.8%	9.9%	**10.8%**	10.1%	9.5%	**0.5%**
Soft Landing Average		**7.2%**	11.0%	11.7%	12.7%	**13.4%**	**16.2%**

- Cash has historically been the worst performer following the commencement of a rate-cutting cycle irrespective of economic outcome.
- In soft landings, investors have historically been rewarded by taking on credit risk whereas the safety of Treasuries has typically shined through during recessions.

7. Sources: FactSet, Bloomberg, S&P, Russell, ICE BofA, NBER. Data as of Sept. 30, 2024. For illustrative purposes only and not reflective of the performance or portfolio composition of any Franklin Templeton fund.
8. Sources: FactSet, Bloomberg, ICE, NBER. Data as of Sept. 30, 2024. Rate-cut cycles of at least 75 bps. Investment-Grade Corporate Bonds represented by the Bloomberg US Corporate Total Return Value Unhedged Index, Core/Core Plus Bonds represented by the Bloomberg US Agg Total Return Value Unhedged Index, Short-Term Bonds represented by the Bloomberg 1-3 Yr US Gov/Credit Total Return Index. High-Yield Bonds represented by the Bloomberg US Corporate High Yield Total Return Index Value Unhedged USD Index. For illustrative purposes only and not reflective of the performance or portfolio composition of any Franklin Templeton fund.

All investments involve risks, including possible loss of principal. Stocks historically have outperformed other asset classes over the long term but tend to fluctuate more dramatically over the short term. **Small- and mid-cap** stocks involve greater risks and volatility than large cap stocks. **Fixed income securities** involve interest rate, credit, inflation and reinvestment risks, and possible loss of principal. As interest rates rise, the value of fixed income securities falls. **Low-rated, high-yield bonds** are subject to greater price volatility, illiquidity and possibility of default. **International investments** are subject to special risks, including currency fluctuations and social, economic and political uncertainties, which could increase volatility. These risks are magnified in **emerging markets**.
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