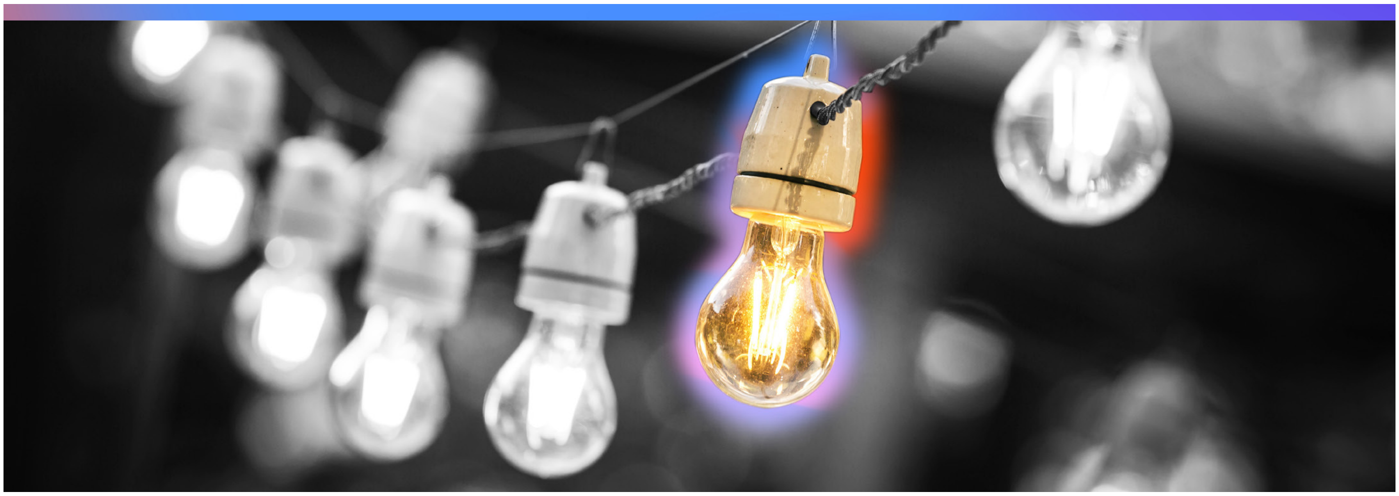


Investment Ideas
Opportunities abound

Stephen Dover, CFA
Chief Market Strategist
Head of the Franklin Templeton Institute

In a reversal from the first half of the year, stocks and bonds endured losses in the third quarter (Q3) of 2023. Concerns about "higher for longer" interest rates from the Federal Reserve (Fed), alongside substantial US government debt issuance, pushed up bond yields and undermined equity valuations. Meanwhile, resilient growth and declining inflation characterized the US economy. After strong advances in the first half of the year, investors pared positions and increased cash allocations.

Overall view: The case for fixed income remains strong. US and global interest rates ought to be nearing their highs as inflation continues to decline and weaker growth emerges. The US dollar also appears to be softening as US interest rates peak, providing opportunities in emerging market debt.

Macroeconomic backdrop

The US economy's resilience is beginning to fade. Lags between monetary policy and economic activity have lengthened given a rising proportion of long-term borrowing in recent years, but interest costs have risen sharply for new borrowers and refinancing. Consumers have drawn down savings. US student loan repay-ments are resuming in the fourth quarter of 2023 and will likely be a drag on consumer spending. The tailwinds from fiscal spending are set to fade into 2024.

Fixed income investment ideas

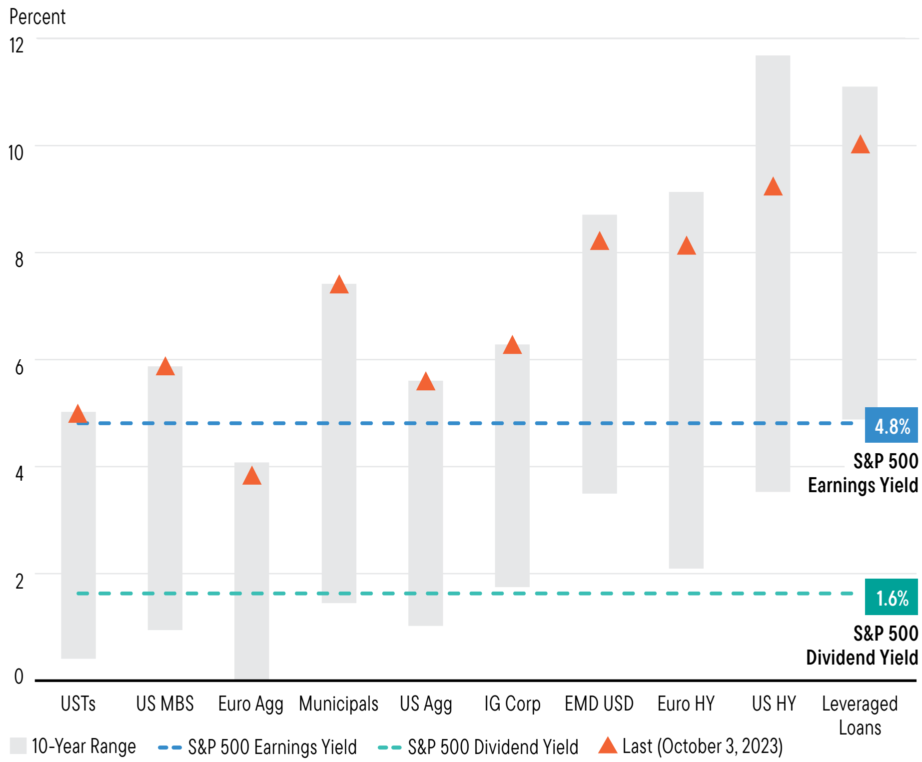
Focus on quality

Fixed income valuations are attractive and yields are high relative to history and equities. If, as we expect, the economy slows and inflation continues trending lower, duration fixed income assets are apt to produce solid returns. As interest rates peak and then decline, medium- and longer-duration notes and bonds will likely outperform cash investments.

Fixed Income Now Offers Opportunities Across-the-Board

Exhibit 1: Current Yield-to-Worst versus 10-Year Range across Fixed-Income Sectors

October 3, 2013–October 3, 2023



Sources: Analysis by Franklin Templeton Institute, Bloomberg, Macrobond. USTs = Bloomberg US Treasury Index, US MBS = Bloomberg US MBS Index, Euro Agg = Bloomberg EuroAgg Index, Municipals = Bloomberg Municipal Bond Index, US Agg = Bloomberg US Aggregate Index, IG Corp = Bloomberg US Corporate Index, EMD USD = Bloomberg EM USD Aggregate Index, Euro HY = Bloomberg Pan-European High Yield Index, US HY = Bloomberg US Corporate High Yield Index, Leveraged Loans = Credit Suisse Leveraged Loan Index. All sectors shown are yield-to-worst except for Municipals, which is based on the tax-equivalent yield-to-worst assuming a top-income tax bracket rate of 37% plus a Medicare tax rate of 3.8%. Yield-to-worst is the lowest possible yield that can be received on a bond apart from the company defaulting. The earnings yield refers to the earnings per share for the most recent 12-month period divided by the current market price per share. Indexes are unmanaged and one cannot directly invest in them. They do not include fees, expenses or sales charges. **Past performance is not an indicator or a guarantee of future results.**

Current supply and demand dynamics of the municipal bond market point to a more immediate opportunity. Municipal (muni) bond credit quality is particularly strong today, and there is currently a shortage of muni bond supply because issuance of new bonds has been lower as state and local budgets are in better shape following the COVID-19 pandemic. In contrast, issuance of US Treasuries and corporate debt has increased dramatically. Along with a smaller supply of munis, demand is rising, and historically this combination has preceded strong performance. This strong performance is illustrated by the table above, which uses flows into muni bond funds as a proxy for supply/demand of the bonds themselves.

What Will Happen When the Current Outflow Cycle Comes to an End?

Exhibit 2: Municipal Bond Performance Relative to Mutual Fund Flows

January 2008–September 2023

	Outflow Period Statistics			Following Inflow Period Statistics		
Quarterly Outflow Cycle	Number of Quarters	Total Outflows (Billions)	Performance During Outflow Cycle	Number of Quarters	Following Cycle Inflows (Billions)	Performance During Inflow Cycle
4Q 2008	1	–$13.81	0.74%	7	$104.82	20.62%
4Q 2010–2Q 2011	3	–$41.12	0.07%	7	$70.34	13.53%
2Q 2013–4Q 2013	3	–$66.44	–2.83%	5	$38.42	10.16%
2Q 2015–3Q 2015	2	–$3.88	0.75%	4	$61.94	5.58%
4Q 2016	1	–$24.34	–3.62%	7	$38.26	5.03%
4Q 2018	1	–$10.82	1.69%	4	$93.69	7.54%
1Q 2020	1	–$21.21	–0.63%	7	$144.81	7.49%
1Q 2022–4Q 2022	4	–$145.15	–8.53%	1	$4.72	2.78%
2Q 2023–3Q 2023	2	–$9.16	–4.05%	—	—	—
Average	**2**	**-$37.33**	**-1.82%**	**5.25**	**$69.62**	**9.09%**

Sources: Franklin Templeton, Bloomberg, ICI. Quarterly inflow/outflow period defined as $1 billion or more. Performance should be cumulative, even if periods are over one year. This chart is for illustrative purposes only and does not reflect the performance of any Franklin Templeton affiliated fund. **Past performance is not an indicator or a guarantee of future results.**

Investment-grade debt is attractively valued. Many companies have strong balance sheets that should withstand a mild recession. Balance-sheet strength has been a global trend gaining momentum over the past 20 years, but as yields fell, the attractiveness of corporate bond credit quality was not appreciated as a reason to invest. With the rise in rates since this tightening cycle started, if rates are close to peak levels and the economic outlook softens, this combination would make longer-duration, high-quality corporate bonds attractive from a total return perspective.

Corporate Balance Sheets Are Stronger

As of December 31, 2022

Sources: Analysis by Franklin Templeton Institute, FactSet, MSCI Indices, Bloomberg. Cash balances are based on the MSCI All Country World Index constituents. Net Debt-to-EBITDA is the ratio of gross debt in excess of cash to Earnings Before Interest, Tax, Depreciation and Amortization (EBITDA). Interest Coverage is the ratio of Earnings Before Interest and Tax to Interest Expense. Indexes are unmanaged, and one cannot directly invest in them. They do not include fees, expenses or sales charges. Important data provider notices and terms available at www.franklintempletondatasources.com. **Past performance is not an indicator or a guarantee of future results**.

Exhibit 3a: Cash and Short-Term Investments on Companies' Balance Sheets

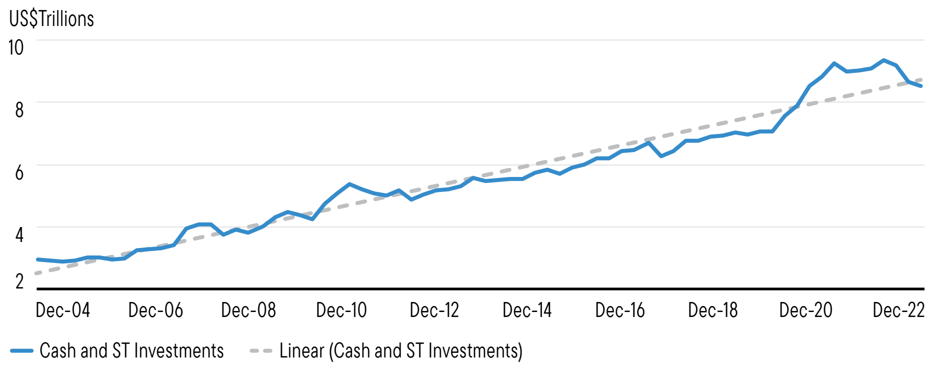


Exhibit 3b: Net Debt-to-EBITDA Ratio

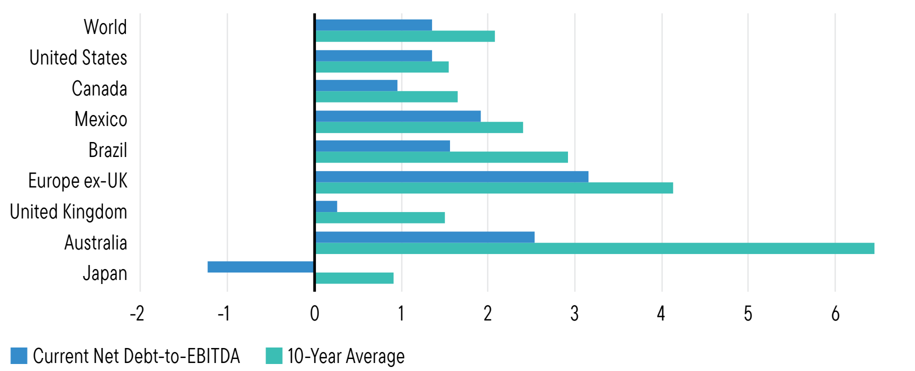
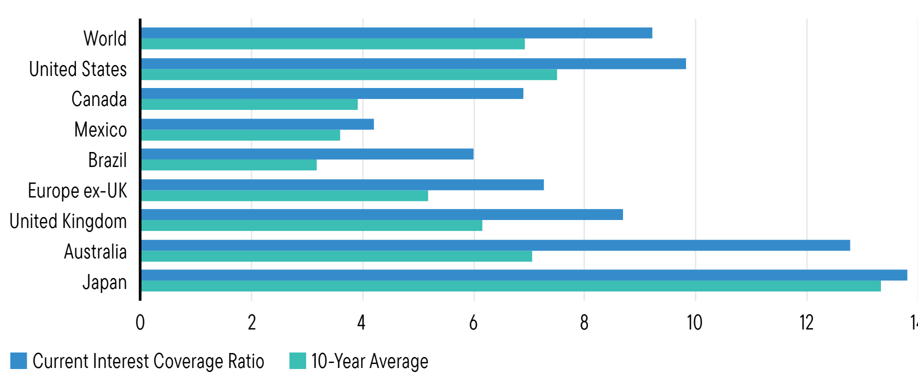


Exhibit 3c: Interest Coverage Ratio

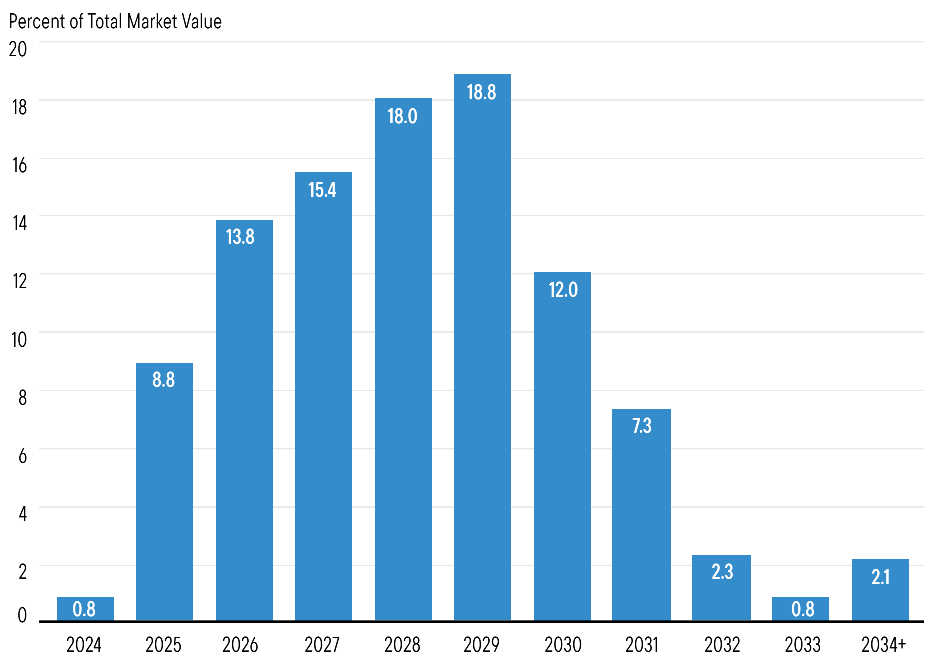


High-yield bonds face minimal refinancing risk until 2025. The proportion of high-yield debt maturing through 2024 is relatively low, so issuers will be unlikely to face the impact of higher rates until at least 2025. With high-yield debt yielding almost 9%, and trading at discounts to par in many cases, the value proposition appears attractive. That said, it is important to choose the high-yield credits least likely to incur financial problems if there is a recession.

High-Yield Bonds Face Minimal Refinancing Risk until 2025

Exhibit 4: US High Yield Debt Maturity Schedule

As of October 31, 2023



Sources: Analysis by Franklin Templeton Institute, ICE BofA Indexes. The chart shows the percent of US high yield bonds outstanding by maturity year that are part of the ICE BofA US High Yield Index as of October 31, 2023. Indexes are unmanaged, and one cannot directly invest in them. They do not include fees, expenses or sales charges. Important data provider notices and terms available at www.franklintempletondatasources.com. **There is no assurance any forecast, projection or estimate will be realized.**

Equity investment ideas

Look for persistent income and emerging growth

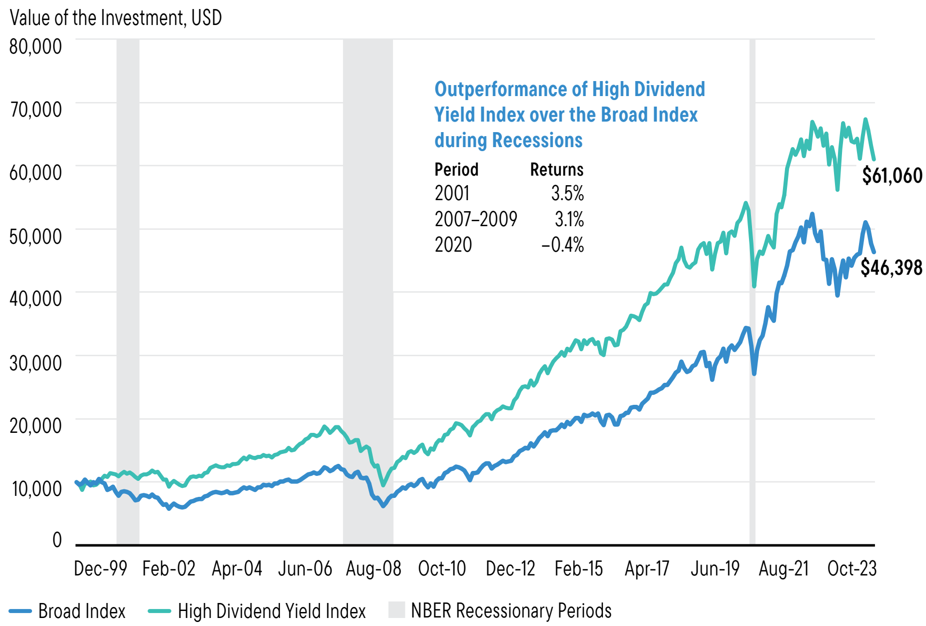
Dividends can provide stability and growth. Stocks with strong cash flows that support dividends become attractive when economic and growth uncertainty increases, which is likely to be the case if the economy slows in 2024. Quality companies—ones that consistently grow dividends based on sustainable and less volatile sources of profitability—can provide better stability and downside protection in challenging markets. In order to provide stability through the ups and downs in the economy, quality companies often have less cyclical exposure and are exposed to attractive secular themes, which can in turn provide growth participation throughout the expansion phase of a market cycle.

High Dividend Paying Stocks Accumulate More Value over the Long-Term

Exhibit 5: Growth of $10,000 in MSCI US Index—Dividend Index versus Broad Index

December 1999–October 2023

Sources: Analysis by Franklin Templeton Institute, MSCI Indices, Macrobond. Indexes are unmanaged, and one cannot directly invest in them. They do not include fees, expenses or sales charges. Important data provider notices and terms available at www.franklintempletondatasources.com.
Past performance is not an indicator or a guarantee of future results.



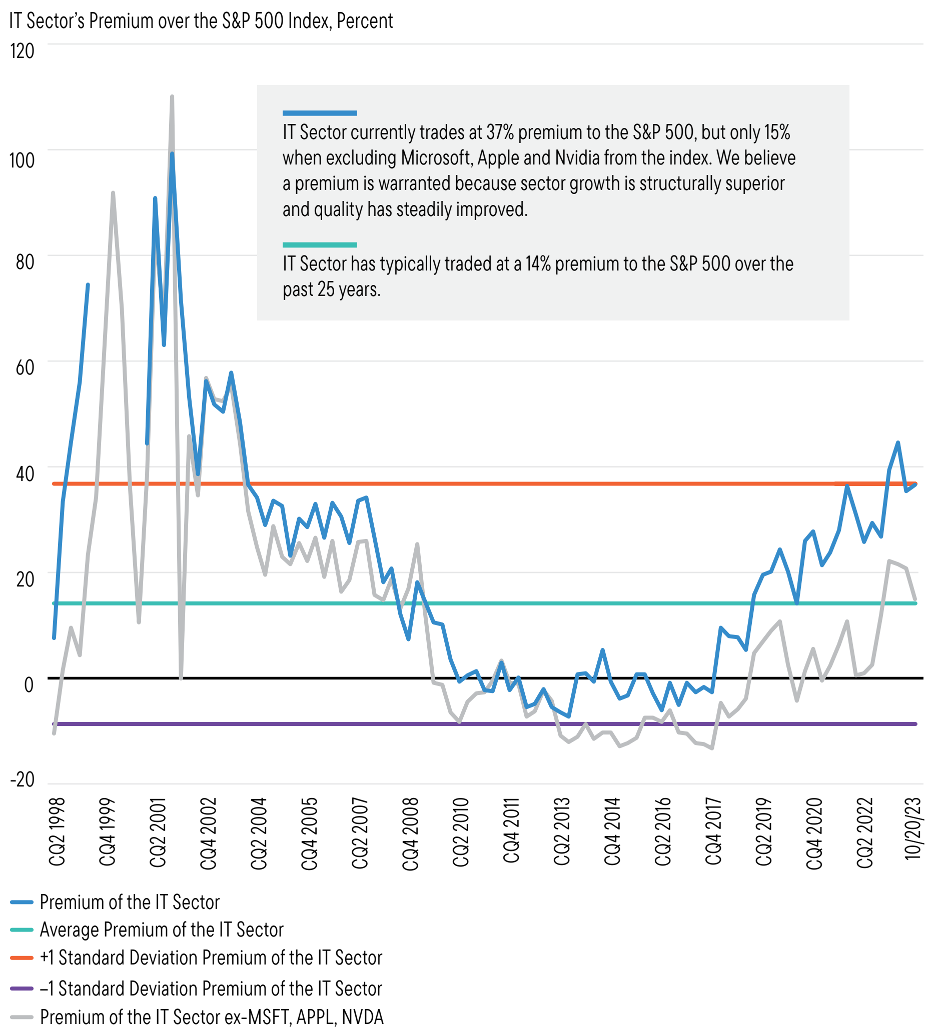
Opportunities exist in innovation outside of the largest companies. A small number of high-performing companies continue to lead broad US indexes. The promise of artificial intelligence, among other digital transformations in the economy, continue to propel these high-performing stocks However, the best future investment opportunities may lie in other technology companies, many of which appear more attractively valued relative to the largest names. We believe research and security selection will be important to identify the best performers in 2024.

Finding Opportunities in Technology beyond the Current Leadership

Exhibit 6: The Information Technology Sector's Premium over the S&P 500 Index

As of October 20, 2023

Sources: Franklin Templeton, SPDJI, Bloomberg. As of October 31, 2023. Sectors shown are part of the S&P 500 Index. Indexes are unmanaged, and one cannot directly invest in them. They do not include fees, expenses, or sales charges. Important data provider notices and terms available at www.franklintempletondatasources.com. **Past performance is not an indicator or a guarantee of future results.**

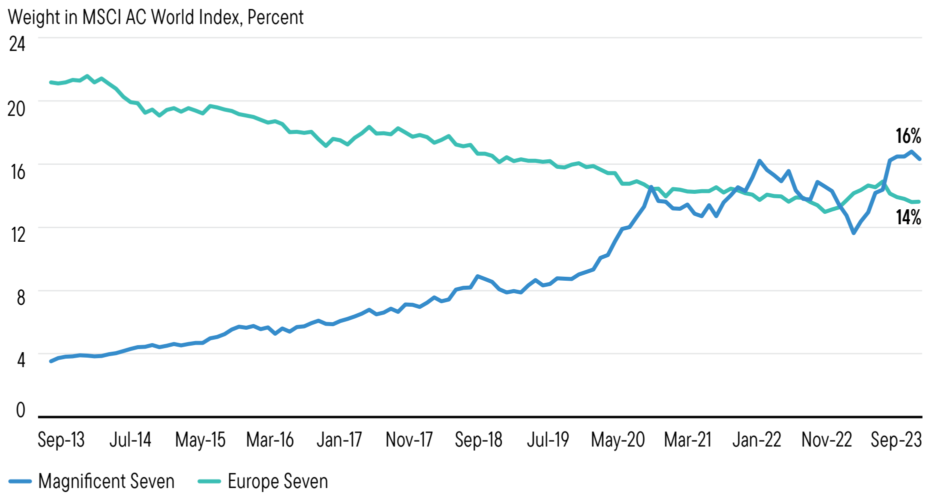


International opportunities are increasing as geopolitics drives reshoring. The tendency toward more regionalized trade patterns and reshoring provides opportunities for countries like India and Mexico, which are direct beneficiaries of these trends. Also, if the US dollar has peaked, its fall is likely to help global companies. The fact that the "Magnificent Seven" stocks in the Unites States (Microsoft, Amazon, Meta, Apple, Alphabet, Nvidia, Tesla) have grown to be larger in aggregate than entire regions is in direct contrast to these trends and present an opportunity to diversify portfolios to better reflect economic reality.

The Weighting in Global Indexes of the Magnificent Seven is Greater than That of Europe's Seven Largest Stock Markets Combined

Exhibit 7: Share of MSCI AC World Index of Magnificent Seven and Europe Seven

As of September 30, 2023

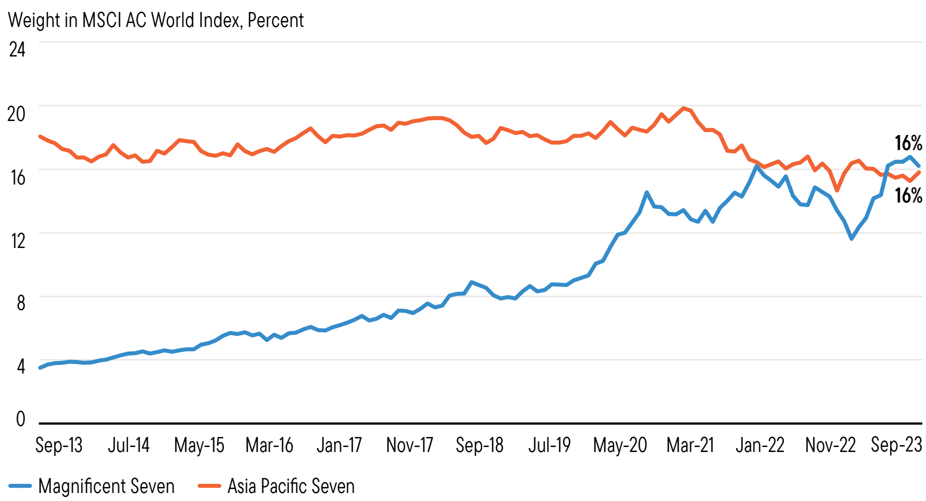


Source: Templeton Global Equity calculations based on FactSet data. Largest Seven European Markets as % of MSCI All Country World, August 2023, United Kingdom, France, Switzerland, Germany, Netherlands, Denmark, and Sweden. Indexes are unmanaged and one cannot directly invest in them. They do not include fees, expense, or sales charges. **Past performance is not an indicator or a guarantee of future results.**

The Weighting in Global Indexes of the Magnificent Seven is Greater than That of Asia Pacific's Seven Largest Stock Markets Combined

Exhibit 8: Share of MSCI AC World Index of Magnificent Seven and Asia Pacific Seven

As of September 30, 2023



Source: Templeton Global Equity calculations based on FactSet data. Largest Seven Asia Pacific Markets as % of MSCI AC World Index, August 2023, Japan, China, Australia, India, Taiwan, Korea, and Hong Kong. Indexes are unmanaged and one cannot directly invest in them. They do not include fees, expenses, or sales charges. **Past performance is not an indicator or a guarantee of future results.**

Alternative investment ideas

Historic opportunity in private credit

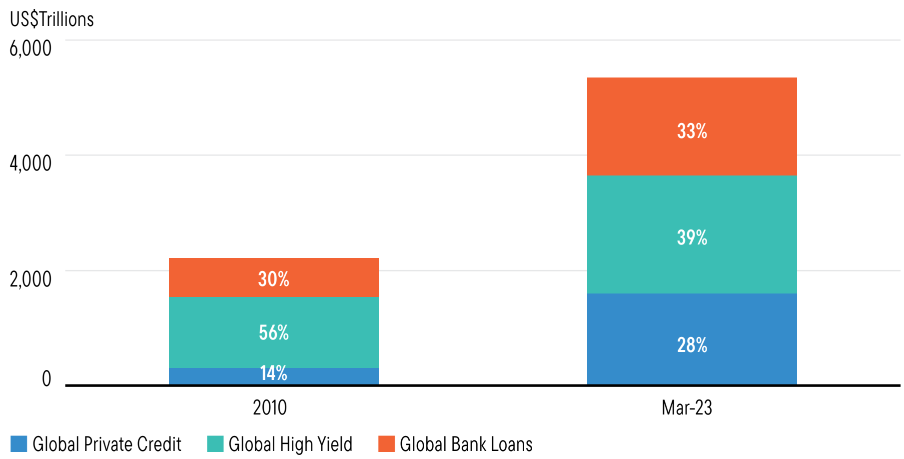
Private credit is becoming a more critical player in providing financing to companies. As traditional financing markets have become less reliable, private credit has grown significantly and has proven to be a resilient source of financing, offering borrowers several advantages. Potential borrower benefits of private financing include partnership with the lender, execution speed and efficiency, certainty of terms, flexibility of structuring, and confidentiality. Borrowers are willing to finance at a premium in private markets to compensate lenders for their value-added solutions.

Private Credit Continues to Gain Market Share from Traditional Financing Sources

Exhibit 9: Global Leveraged Finance Market

As of March 31, 2023

Sources: Franklin Templeton Capital Market Insights Group, ICE BofA, Preqin, Pitchbook LCD, FactSet, Macrobond. Indexes are unmanaged and one cannot directly invest in them. They do not include fees, expenses or sales charges. Important data provider notices and terms available at www.franklintempletondatasources.com. **Past performance is not an indicator or a guarantee of future results.**



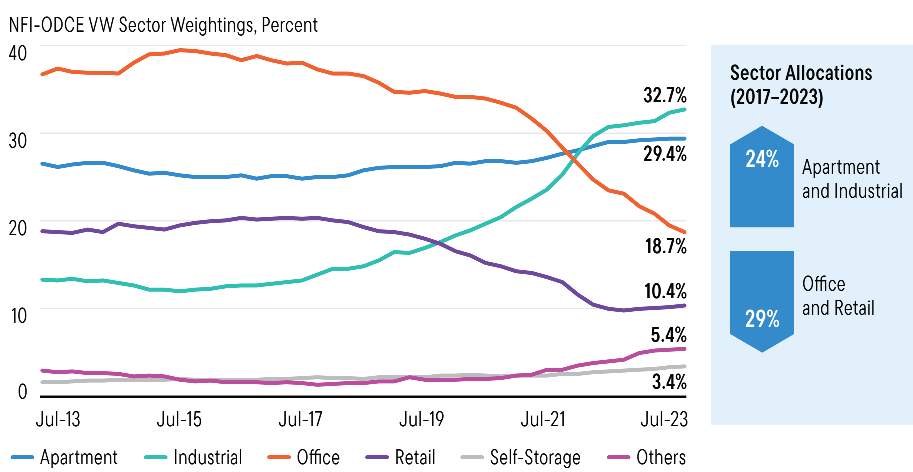
Megatrends are driving opportunities in private real estate. Demographics, technology, deglobalization, housing affordability/shortages and climate change are all contributing to shifting dynamics in terms of finding the best opportunities in commercial real estate. While factors such as "work from home," are challenging commercial office spaces, low vacancies and higher demand are appealing in sectors such as industrial warehouses, life sciences, self-storage, and multi-family real estate.

Changing Investment Themes Are Influencing Portfolio Allocation Decisions

Exhibit 10: Private Real Estate Sector Allocation in Recent History

As of third quarter 2023

Sources: Clarion Partners Investment Research, NCREIF, 2023 Q3. NFI-ODCE VW Sector Weightings (%) stands for NCREIF Fund Index—Open End Diversified Core Equity (NFI-ODCE) Value Weighted (VW) sector weightings (%).Indexes are unmanaged and one cannot directly invest in them. They do not include fees, expenses or sales charges. Important data provider notices and terms available at www.franklintempletondatasources.com. **Past performance is not an indicator or a guarantee of future results.**



Glossary

Bloomberg US Treasury Index measures the performance of U.S. dollar-denominated, fixed-rate, nominal debt issued by the U.S. Treasury with at least one year until final maturity. Treasuries, if held to maturity, offer a fixed rate of return and a fixed principal value; their interest payments and principal are guaranteed.

Bloomberg US MBS Index tracks the performance of fixed-rate agency mortgage-backed pass-through securities guaranteed by Ginnie Mae (GNMA), Fannie Mae (FNMA) and Freddie Mac (FHLMC). Effective June 1, 2017, hybrid adjustable-rate mortgages were removed from the index.

Bloomberg EuroAgg Index is a benchmark that measures the investment grade, euro-denominated, fixed-rate bond market, including treasuries, government-related, corporate and securitized issues. Inclusion is based on currency denomination of a bond and not country of risk of the issuer.

Bloomberg Municipal Bond Index is a market value-weighted index of tax-exempt, investment-grade municipal bonds with maturities of one year or more.

Bloomberg US Aggregate Index measures the performance of the investment-grade, U.S. dollar-denominated, fixed-rate taxable bond market. The index includes Treasuries, government-related and corporate securities, mortgage-backed securities (agency fixed-rate and hybrid adjustable-rate mortgage pass-throughs), asset-backed securities and commercial mortgage-backed securities (agency and nonagency).

Bloomberg US Corporate Index measures the investment grade, fixed-rate, taxable corporate bond market. It includes USD denominated securities publicly issued by US and non-US industrial, utility and financial issuers.

Bloomberg Emerging Markets Hard Currency (EM USD) Aggregate Index is a flagship hard currency Emerging Markets debt benchmark that includes USD-denominated debt from sovereign, quasi-sovereign, and corporate EM issuers.

Bloomberg Pan-European High Yield Index measures the market of non-investment grade, fixed-rate corporate bonds denominated in the following currencies: euro, pounds sterling, Danish krone, Norwegian krone, Swedish krona, and Swiss franc. Inclusion is based on the currency of issue, and not the domicile of the issuer.

Bloomberg US Corporate High Yield Index measures the USD-denominated, high yield, fixed-rate corporate bond market. Securities are classified as high yield if the middle rating of Moody's, Fitch and S&P is Ba1/BB+/BB+ or below.

Credit Suisse Leveraged Loan Index (CS LLI) is designed to mirror the investable universe of the U.S. dollar-denominated leveraged loan market. Loans must be below investment grade and rated no higher than Baa/BB+ or Ba1/BBB+ by Moody's or S&P.

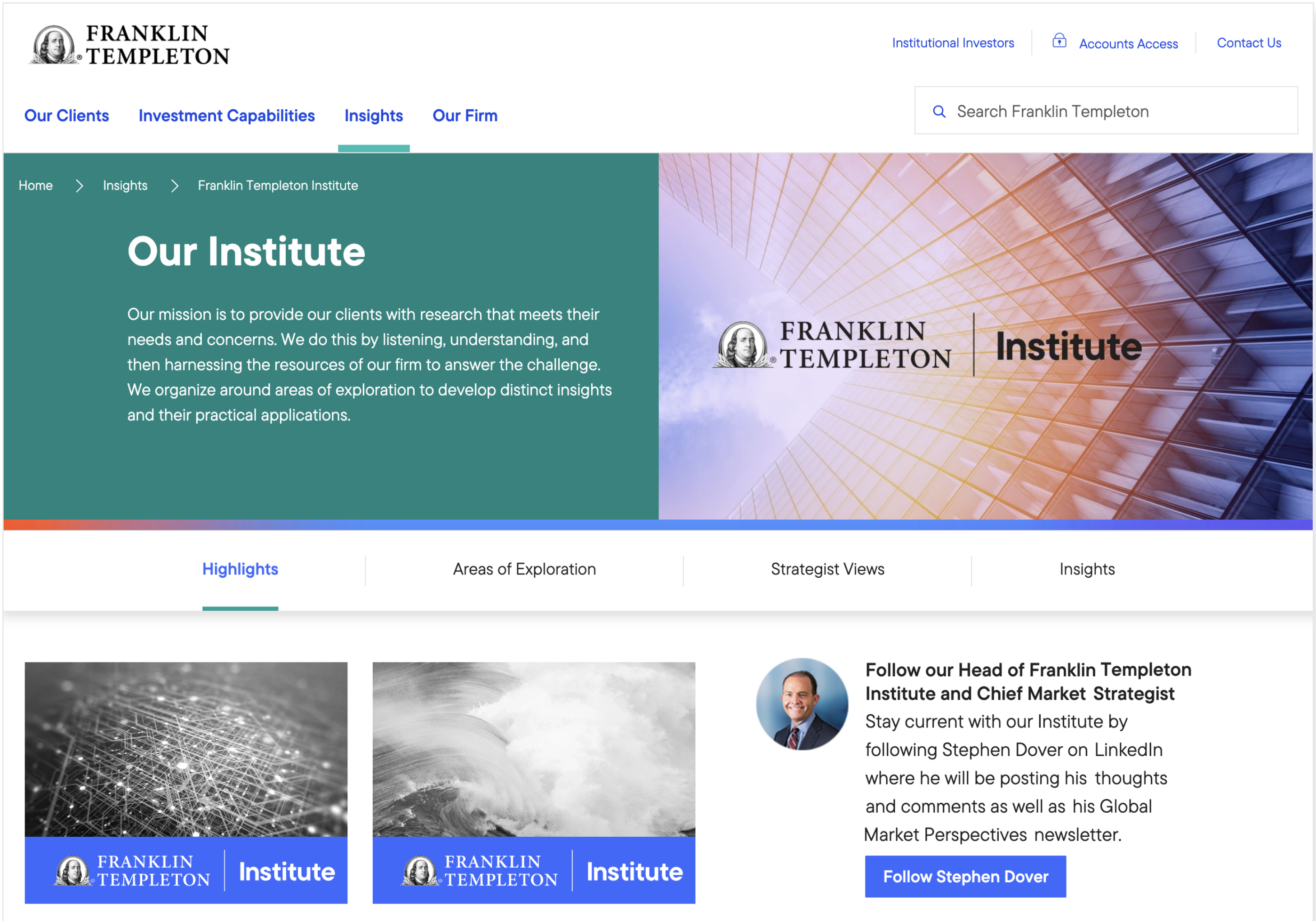
MSCI All Country World Index is a market capitalization-weighted index that is designed to measure equity market performance of developed and emerging markets. MSCI makes no warranties and shall have no liability with respect to any MSCI data reproduced herein. No further redistribution or use is permitted. This report is not prepared or endorsed by MSCI.

ICE BofA US High Yield Index tracks the performance of US dollar denominated below investment grade rated corporate debt publicly issued in the US domestic market. To qualify for inclusion in the index, securities must have a below investment grade rating (based on an average of Moody's, S&P, and Fitch) and an investment grade rated country of risk (based on an average of Moody's, S&P, and Fitch foreign currency long term sovereign debt ratings).

MSCI US Index is designed to measure the performance of the large- and mid-capitalization segments of the US market. With 627 constituents, the index covers approximately 85% of the free float-adjusted market capitalization in the U.S.

NCREIF Fund Index—Open End Diversified Core Equity (NFI-ODCE) Index is a capitalization-weighted index based on each fund's net invested capital, which is defined as beginning market value net assets (BMV), adjusted for weighted cash flows (WCF) during the period. Open-end funds are generally defined as infinite-life vehicles consisting of multiple investors who have the ability to enter or exit the fund on a periodic basis, subject to contribution and/or redemption requests, thereby providing a degree of potential investment liquidity. The term Diversified Core Equity style typically reflects lower risk investment strategies utilizing low leverage and generally represented by equity ownership positions in stable U.S. operating properties diversified across regions and property types.

For more detail on the current environment and opportunities, read the Franklin Templeton Institute's latest publications



WHAT ARE THE RISKS?

All investments involve risks, including possible loss of principal.

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.

Equity securities are subject to price fluctuation and possible loss of principal.

Investments in lower-rated bonds include higher risk of default and loss of principal. Changes in the credit rating of a bond, or in the credit rating or financial strength of a bond's issuer, insurer or guarantor, may affect the bond's value.

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**.

Alternative strategies may be exposed to potentially significant fluctuations in value.

Privately held companies present certain challenges and involve incremental risks as opposed to investments in public companies, such as dealing with the lack of available information about these companies as well as their general lack of liquidity.

Real estate securities involve special risks, such as declines in the value of real estate and increased susceptibility to adverse economic or regulatory developments affecting the sector.

Because **municipal bonds** are sensitive to interest-rate movements, a municipal bond portfolio's yield and value will fluctuate with market conditions. Bond prices generally move in the opposite direction of interest rates. Thus, as prices of bonds in an investment portfolio adjust to a rise in interest rates, the portfolio's value may decline. Changes in the credit rating of a bond, or in the credit rating or financial strength of a bond's issuer, insurer, or guarantor, may affect the bond's value.

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