

# Anatomy of a Recession: Economic and Market Outlook

First Quarter 2026

As of February 1

## US outlook<sup>1</sup>

- Fiscal and monetary support may provide the foundation for solid economic growth to continue in 2026.
- The AI capital expenditure (capex) boom is likely to continue with current spending well within the range seen during prior technological innovation cycles.
- The overall signal from the ClearBridge Recession Risk Dashboard remains in green “expansion” territory.

## 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 <sup>2</sup>			
		January 31, 2026	December 31, 2025	September 30, 2025	June 30, 2025
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   — Not available<sup>2</sup>

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 January 31, 2026. 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.

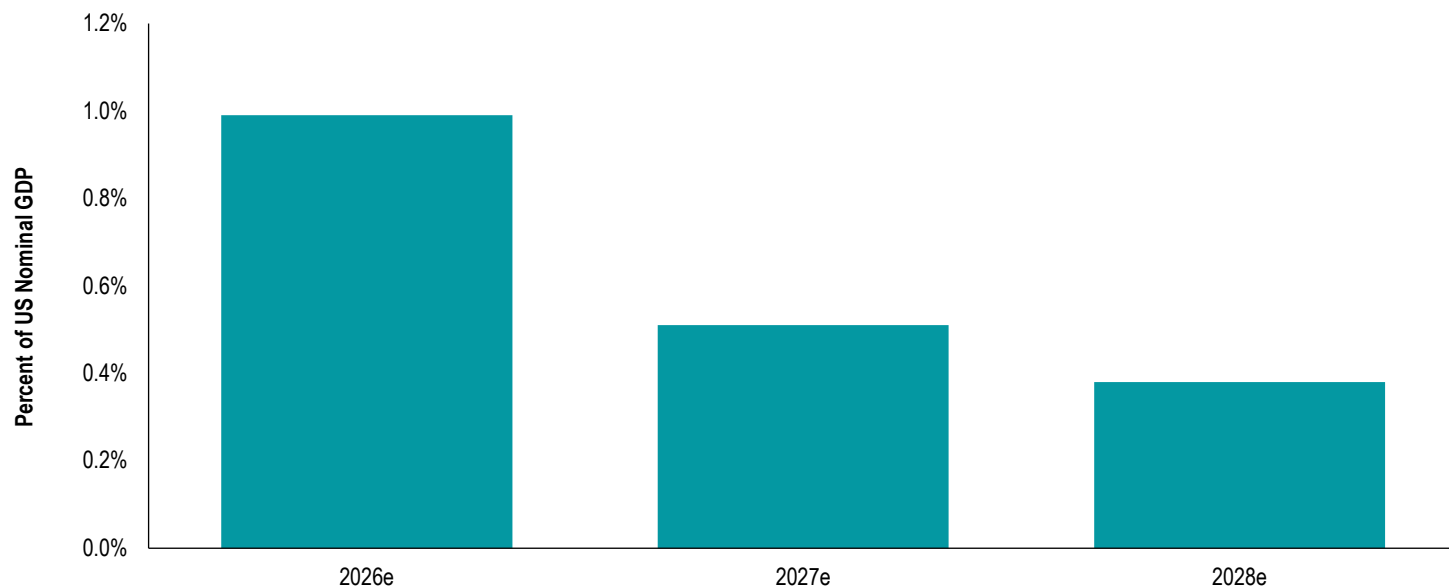
2. “Not Available” reflects data that has not been updated due to the government shutdown. Data as of January 31, 2026. Sources: BLS, Federal Reserve, Census Bureau, ISM, BEA, American Chemistry Council, American Trucking Association, Conference Board, Bloomberg, CME, FactSet and Macrobond. The ClearBridge 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

## Tax tailwind

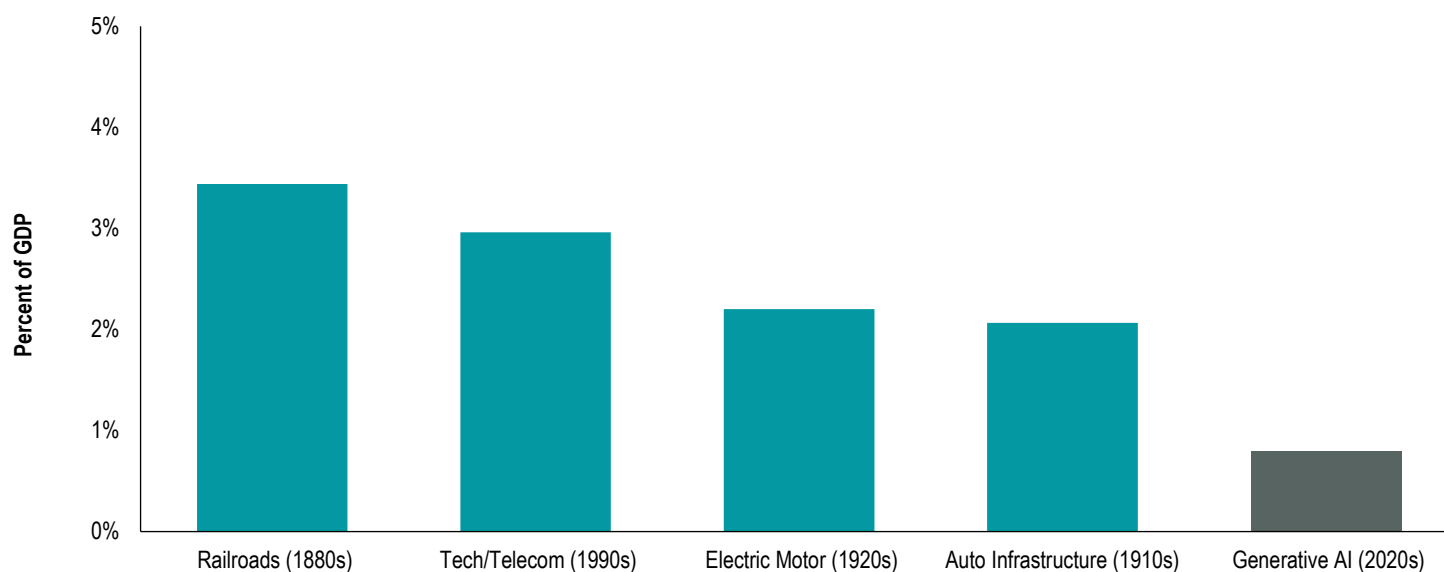
### Net Fiscal Impulse of the One Big Beautiful Bill (OBBB) as Percentage of Nominal GDP<sup>3</sup>



- The OBBB is expected to deliver fiscal stimulus equivalent to ~1% of GDP in 2026.
- The bill's impact should wane in 2027 and 2028 but will likely remain supportive at ~0.5% according to Congressional Budget Office (CBO) estimates.

## More AI capex ahead?

### Peak Historical Investment, Innovative US Technologies<sup>4</sup>



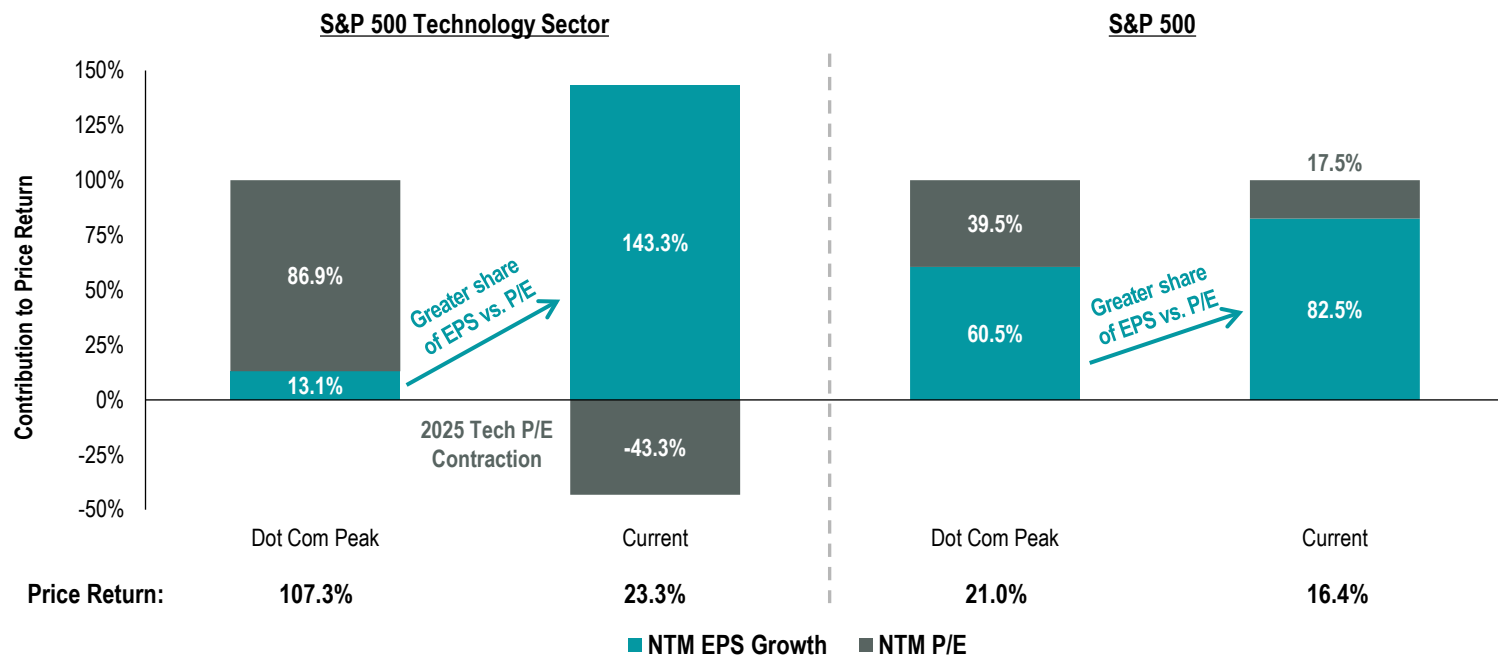
- Current levels of AI capex pale in comparison to peak spending seen during prior large US innovative technology cycles.
- Should history repeat, AI investment could surprise to the upside, which we believe would provide continued support for both the US economy and financial markets.

3. Sources: Wolfe Research, CBO, Macrobond. Based on CBO's Baseline Budget Projections from January 2025's report The Budget and Economic Outlook: 2025 to 2035. There is no assurance that any estimate, forecast or projection will be realized.

4. Data as of October 20, 2025; latest available as of December 31, 2025. Source: Bureau of Economic Analysis, Goldman Sachs GIR.

## It's (not) 1999

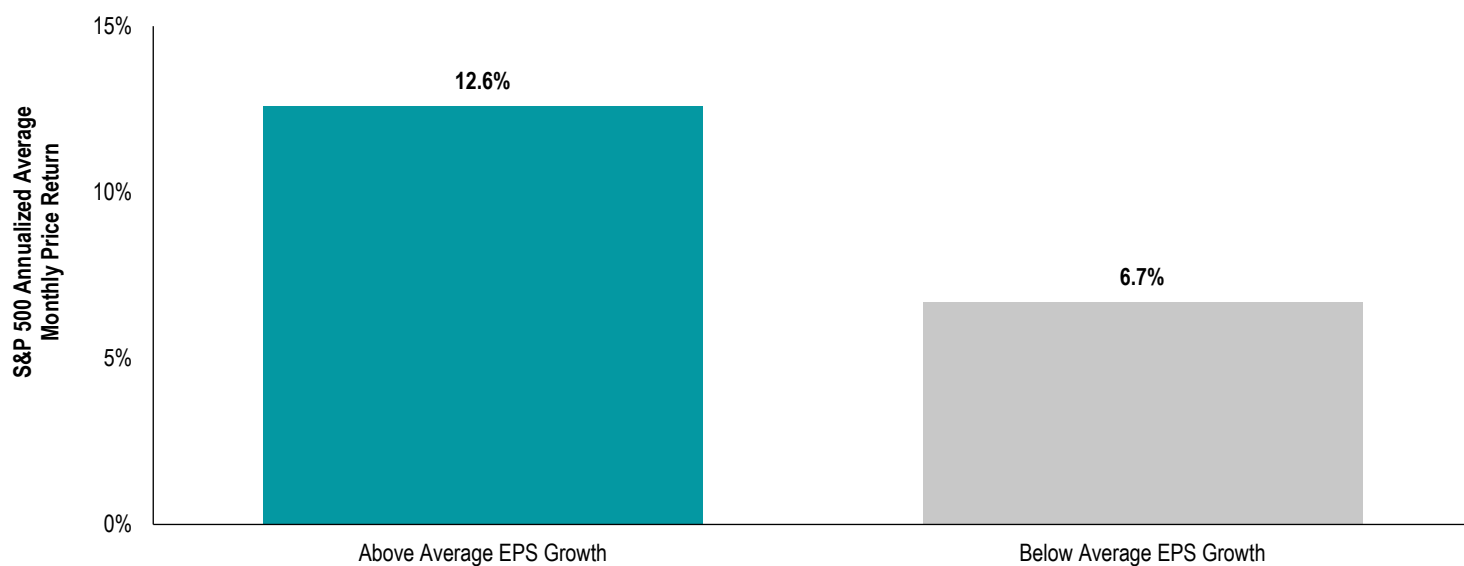
### Contribution to Return From earnings per share (EPS) and price/earnings (P/E): Prior 12 Months<sup>5</sup>



- Although recent market strength has similarities to the late 1990s, 2025's rally was primarily driven by improving EPS expectations as opposed to P/E expansion, a stark contrast to the final surge of the "dot com" bubble.
- With improving fundamentals driving recent market strength, we believe the rally can be sustained in 2026.

## Strong earnings, strong gains

### S&P 500 Price Return in Above- and Below-Average EPS Growth Regimes<sup>6</sup>

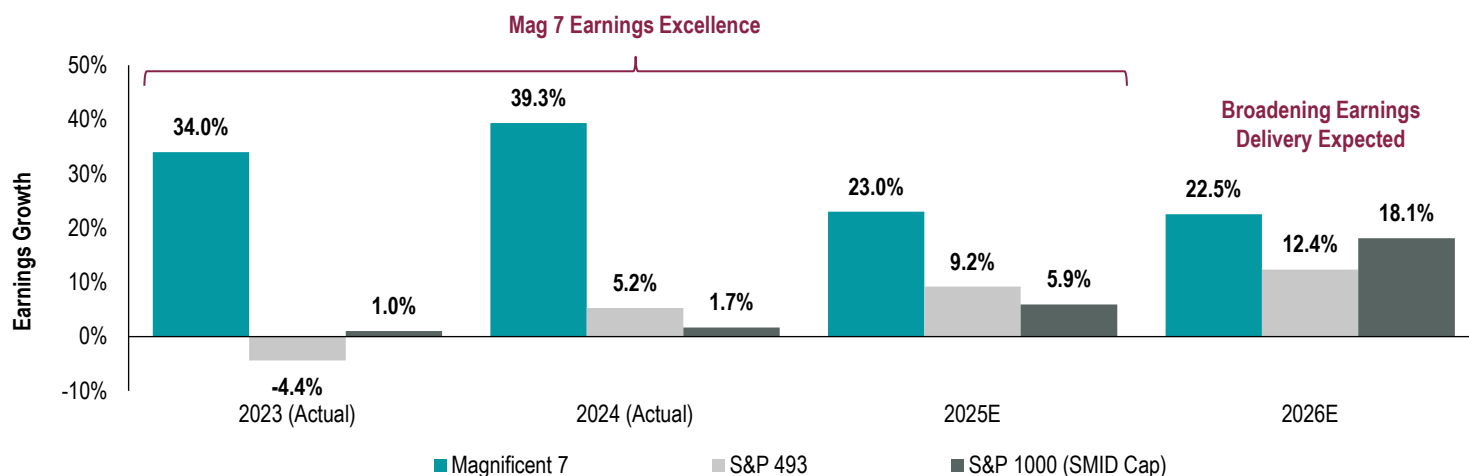


- Benchmark returns have historically been stronger when EPS growth is above average (9%).
- Sell-side consensus currently expects 15% EPS growth in 2026, suggesting a healthy market backdrop for the coming year.

5. Note: Dot com peak was March 23, 2000; Contribution to price return based on change in sell-side consensus next twelve months (NTM) EPS expectations and NTM P/E. Data as of December 31, 2025. Sources: S&P, FactSet.

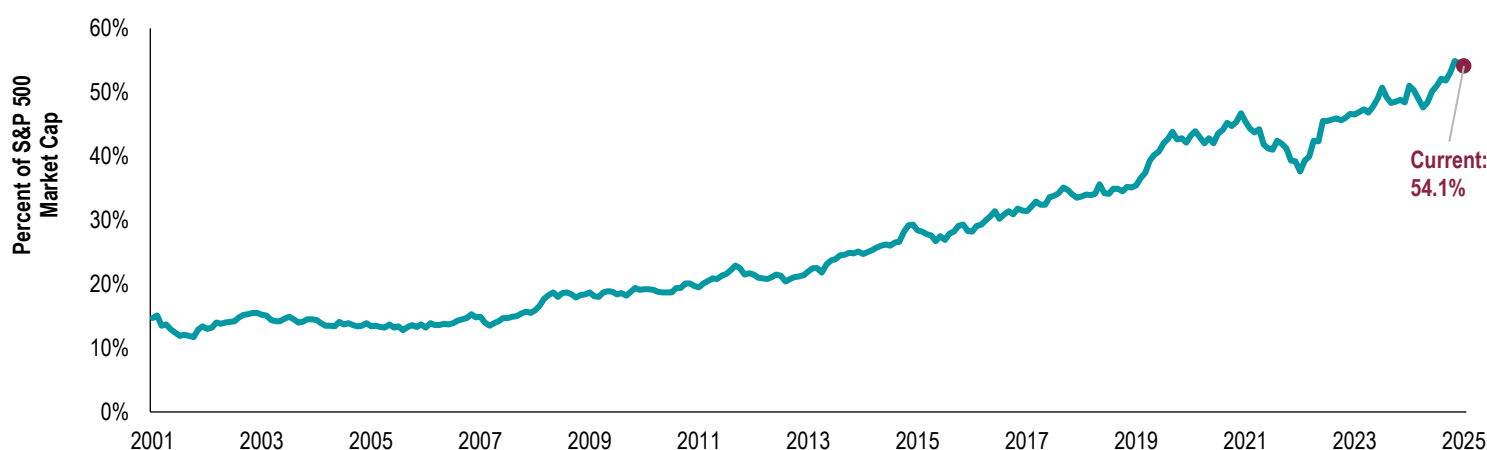
6. Annualized average monthly returns based on actual 12-month EPS growth. The term "consensus" within the capital markets industry refers to the average of earnings estimates made by professionals. Data as of December 31, 2025. Sources: FactSet, S&P.

## A key driver of the Magnificent 7 outperformance has been superior earnings growth<sup>7</sup>



- Bottom-up consensus expects this advantage to dissipate with broader earnings delivery across US equities in 2026.

## Percent of S&P 500 market cap that overlaps with the QQQ<sup>8</sup>



- The composition of the S&P 500 index has increasingly mirrored the more growth- and technology-oriented QQQ.
- Many investors may be overexposed to growth and technology due to this dynamic, with the current overlap breaching 50% in 2025.

7. The term "consensus" within the capital markets industry refers to the average of earnings estimates made by professionals. Magnificent 7 data refers to the following set of stocks: Microsoft (MSFT), Amazon (AMZN), Meta (META), Apple (AAPL), Google parent Alphabet (GOOGL), Nvidia (NVDA), and Tesla (TSLA). Data as of December 31, 2025. Sources: FactSet, S&P. There is no assurance that any estimate, forecast or projection will be realized. Company references are used for illustrative purposes and should not be construed as an endorsement of sponsorship of Franklin Templeton companies. This information is not intended as an investment recommendation, nor does it constitute investment advice.

8. QQQ is an ETF that tracks the Nasdaq 100 index. Data as of December 31, 2025. Sources: S&P, FactSet. Market cap is calculated using the sum of constituents.

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