WHAT FRANKLIN TEMPLETON THINKS...

Q3 2020

...About THE ECONOMY AMID COVID-19

The Low Point May Be Past

- We believe the economic low point has passed for many economies.
- Overall, momentum in the global economy is improving, but it is too early to call an end to the deep recession that has ensued from the coronavirus crisis.
- We expect multiple stages of relief rallies and corrections in financial markets before a sustainable recovery eventually takes hold.
- The challenges of recovering from this virus-induced recession are global in nature. Europe is now taking steps to accelerate its recovery.
- The $860 billion EU recovery fund is one giant leap as it signals greater fiscal cooperation among EU members by selling common bonds whose proceeds will be used to aid member countries suffering due to the pandemic.
- The current recession created a gap in income statements and balance sheets not yet repaired in many sectors. This gap has been temporarily filled by large-scale fiscal stimulus and monetized by central banks.
- Barring a COVID-19 second wave, it remains to be seen whether policymakers can continue to plug this gap in a fragile, recovering economy, especially in an election year with heightened political risks.
- With significant levels of fiscal and monetary stimulus in place, markets are taking an optimistic view of the balance of risks and opportunities.
- We expect the transformational changes from the accelerated adoption of technological solutions to allow remote working and new ways of conducting business to persist even as the immediate driver of this change eases.
- We believe that for the balance of the year, politics will have a growing impact on investment decisions. However, health and related economic variables are likely to be more important than narrow, traditional political considerations.
- Core inflation has dipped back toward the lows seen over the last 10 years. We continue to believe changes in demand will be the main driver of inflation.
- Recent supply shocks may have lowered productive capacity, but the deceleration in global activity that we have seen since 2019 will be much more powerful, in our view.

...About FIXED INCOME

Too Far, Too Fast...in Some Credit Sectors

- Weak global growth, and a bias toward easier monetary policy, contrast with long-term valuations that have become more expensive.
- Renewed widening of corporate bond spreads may occur if the recovery slows or financial conditions tighten. We maintain a more cautious view of bonds at the asset allocation level, reflecting valuation concerns.
- Looking across credit sectors, we believe high yield has probably gone too far, too fast.
- We continue to prefer the investment-grade space, but some sectors will be impacted for a longer period of time; for example, those related to business travel, hospitality and leisure.
- We think mounting credit pressures could mean ratings reductions for some states if more federal funding doesn't materialize from the US Congress this summer. Some states were ill-prepared to weather a normal cyclical downturn, let alone the dramatic economic shock of COVID-19.

...About US EQUITIES

Liquid Courage

- The amount of stimulus in response to this crisis is unprecedented; the fiscal, monetary, and political responses globally have led to a world awash with liquidity, much of which has gone into the stock markets.
- Equities require sustained economic recovery to support valuations, as corporate earnings are expected to have weakened through the second quarter.
- We anticipate supportive liquidity conditions to offset concerns about downside risk to capital investment plans.
- Despite COVID-19 headwinds, trend US growth remains stronger than in other developed markets, and technology exposure sustains the market opportunity.
- Investors are playing growth stories that are likely to prevail over the long run no matter the valuation, because value needs an economic recovery.

...About GLOBAL EQUITIES

A World Out of Whack

- Ten years ago, the US constituted about 40% of the market capitalization of the world. Now it's approaching 60%, which on a relative basis makes an argument to invest outside of the United States.
- The UK market appears historically cheap, so long as corporate profits are not too severely impacted, though uncertainties remain over Brexit.
- We maintain a more cautious view on Europe ex-UK, which reflects a lower outlook for earnings, and valuations that are no better than neutral relative to history.
- In Japan, price-to-book valuations have been attractive, but earnings per share and return on equity are weakening relative to peers.
- Our focus continues to be on stock picking across the full market—without taking on too much balance sheet or valuation risk.

...About EMERGING MARKETS

Secular Trends Accelerating

- The crisis has highlighted strengths of emerging markets, including fiscal and corporate reforms undertaken over the last two decades.
- Robust balance sheets across emerging markets have proven to be a source of resilience, and we believe that will continue.
- Secular trends driving opportunities in EM have accelerated because of the crisis. In effect, the future has been brought forward.
- That boosts our optimism in economies and companies that benefit from this evolution of the asset class. These include areas of innovation, where EM infrastructure and business models are leapfrogging developed markets, such as mobile telecom, broadband, e-commerce and, amid the lockdown, education and health care.
- The rhetoric around US-China relations is likely to heat up ahead of the US election, but both countries benefit from the relationship, so an improved tone should follow, especially if a recovery takes hold.

Franklin Templeton Investments comprises multiple independent investment teams located around the world. As individual portfolio managers and teams pursue different fund mandates, there will always be different views held on the markets, and we consider that a strength. The insights above represent the current views of senior investment leaders and are subject to change. This content does not incorporate the views of the Specialist Investment Organizations from the Legg Mason acquisition.

Key Themes

THEME	RATIONALE
STAY DIVERSIFIED TO HELP MITIGATE RISK	In a world of low sovereign yields, investors may need to expand beyond their traditional stock/bond mix to diversify equity and credit risk exposures, while still obtaining a potential return. Alternative risk strategies and less traditional bond portfolios may start to make more sense for some investors, within the context of a diversified portfolio.
GAIN A BROADER PERSPECTIVE	In broad terms, developed markets outside the US may be less desirable, but on an individual basis, opportunities persist. Selectivity is essential. In emerging markets, the same is true as idiosyncratic risk and cyclicality concerns must be weighed against attractive valuations and long-term structural trends.
TAKE THE HIGHER GROUND IN BONDS	Traditional high quality and investment grade bond funds offer income and some of the historical counterbalance to equities, even in a zero bound interest rate world where the 10-year Treasury has offered yields of less than 70 basis points for most of the quarter ending June 30. Municipal bonds can be (if chosen with care) a high quality alternative to government bonds. The current yield pick-up provided by munis becomes more compelling for those investors with high income tax rates.* Lower volatility strategies in fixed income may help investors in managing overall portfolio fluctuations without going to cash.
THERE ARE OTHER SOURCES OF INCOME THAN BOND FUNDS	Diversified multi-sourced income funds can flexibly search out the best opportunities—even within a single company's capital structure—for the best yield/risk scenarios as conditions warrant. Funds investing in quality, dividend-paying stocks are another way to derive income while you wait for economic recovery.
INNOVATION LOOKS BEYOND THE RECESSION	The coronavirus pandemic has accelerated changes that may have taken a decade or more to occur. The economy is currently bifurcated between the digital and the hands-on. Innovation is driving both, but is more immediately relevant in the digital economy. It looks past the current economic environment offering a vision for growth in an uncertain world. And, we have often observed that it's a poor investment to invest against human ingenuity.

*Treasuries are backed by the full faith and credit of the US government. Interest and principal are guaranteed.

All investments involve risks, including the possible loss of principal. Special risks are associated with foreign investing, including currency fluctuations, economic instability and political developments. Investments in emerging markets involve heightened risks related to the same factors, in addition to those associated with these markets' smaller size, lesser liquidity and lack of established legal, political, business and social frameworks to support securities markets. Non-diversified funds that concentrate in the biotechnology sector involve risks such as patent considerations, product liability, government regulations, and regulatory approval. Smaller, mid-sized and relatively new or unseasoned companies can be particularly sensitive to changing economic conditions, and their prospects for growth are less certain than those of larger, more established companies. Investments in fast-growing industries like the technology sector could result in increased price fluctuation especially over the short term, due to the rapid pace of product change and development and changes in government regulation. Non-diversified funds concentrate in a single sector, which may entail higher risk. Alternative strategies may include risks in effectively allocating to subadvisors and currency, merger arbitrage and liquidity risks. Bond prices generally move in the opposite direction of interest rates. As the prices of bonds in a fund adjust to a rise in interest rates, the fund's share price may decline. These and other risk considerations are discussed in each fund's prospectus.

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Investors should carefully consider a fund's investment goals, risks, charges and expenses before investing. To obtain a summary prospectus and/or prospectus, which contains this and other information, talk to your financial professional, call us at (800) DIAL BEN®/342-5236 or visit **franklintempleton.com.** *Please carefully read the prospectus before you invest or send money.*

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