

From the US Market Desk

Volatility action plan—Discipline over emotion



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Macro

- Our forecast for real growth in gross domestic product (GDP) for 2026 is 2.5% (based on our [Global Investment Management Survey](#)), which is above the Federal Reserve (Fed) forecast of 2.3% and the Wall Street consensus of around 2%. The main drivers of our GDP forecast are the continued capital expenditure (capex) spending by big technology firms, a resilient consumer and expected higher tax refunds in 2026 relative to past years, as well as the possibility of future interest-rate cuts. The duration of the current Middle East conflict is the primary risk to our forecast. Higher oil prices resulting from the conflict work like a tax on the consumer.
- We expect the Fed to cut rates twice in 2026 and core personal consumption expenditures (PCE) to remain stable in the 2.5% to 3.0% range. The last tick for core PCE data came in at 3.1% for January. The U-3 unemployment rate was 4.4% for February, just off the recent high print in November of 4.5%, which was the highest level going back to October of 2021. Should the Middle East fighting persist and drive oil prices higher for longer, it could put the Fed in a box. Fed fund futures have reacted to exactly that possibility. At the start of 2026, fed fund futures priced in two to three interest-rate cuts. Last week, that fell to pricing in less than one cut. Similarly, we know that the two-year note yield historically leads the Fed.
- Inflation expectations have moved up in the near term. One-year inflation breakeven rates are now 4.72%, an alarming move to say the least, although it is important to remember there is a seasonal component that historically has affected the first-quarter data. No doubt, some or even all of this move is resulting from higher oil and natural gas prices. Two-year breakeven rates are 3.20%. Five-year breakeven rates are 2.67%. These numbers represent the bond market pricing annualized inflation expected over the coming one, two and five years.
- On the currency front, we think the US dollar will be essentially flat for the year despite the recent volatility. The US Dollar Index (DXY) is trading at US\$99.74 and is at the high side of its 11-month range, defined as US\$96 to US\$100. Many investors are concerned about the US dollar losing value, and some believe the dollar has recently weakened materially. The fact is that the US dollar is at the same level today as it was in April of 2025 and higher than it was in early July of 2025, late September of 2025 and mid-January of 2026.

Equities

- We are constructive on US equities and have established a target range of 7,000 to 7,400 for the S&P 500, based on expected earnings-per-share growth of 8% to 13% year-over-year (based on our [Global Investment Management Survey](#)). We don't expect this current geopolitical conflict to impact our outlook unless oil trades north of \$100 and stays there for months. We expect high levels of volatility to persist in the near term.
- Let's talk about volatility and the emotion it creates. Volatility creates uncertainty. Negative newsflow causes market drawdowns. In today's world, the negative drumbeat can be 24/7/365—24 hours per day, seven days per week, 365 days per year. It is constant and often becomes amplified. Investing is an emotional game, and getting wrapped up in the headlines can lead to second guessing yourself and your plan, and it can cause you to make mistakes. Trust me, I made

Equities (continued)

- (continued) mistakes as an analyst and as a portfolio manager; everyone in those positions has. This is where discipline comes in. The ability to separate the signal from the noise is critical. Remember this: The world doesn't end that often.
- Let's look at what we know from history. According to Carson Investment Research, since 1940 there have been 43 major geopolitical events including wars, terrorist attacks, financial bubbles, and presidential assassinations and attempted assassinations. Of these 43 events, measuring returns forward from the day of the event, the median one-month S&P 500 return was -0.2%, and the hit rate for positive returns was 47%. The worst one-month drawdowns occurred at the start of World War Two (-20%) and the collapse of Lehman Brothers (-16%). Again, for the 43 events, the median three-month forward return was 2.7%, while the hit rate for positive returns over three months was 67%. The worst three-month drawdown was -26%, which happened with the collapse of Lehman Brothers and Bear Stearns during the great financial crisis (GFC). Returning again to the broad sample, the median six-month return was 5.3% with a 62% hit rate for positive results. The worst six-month drawdown was, again, the Lehman/Bear Stearns/GFC period at -35%. The median 12-month return was 7.4% with a 65% positive-return hit rate. The worst 12-month drawdown was found in the OPEC oil embargo of 1973 at -43% followed by the Lehman/Bear Stearns/GFC event at -42%.
- Of the 43 major events, the oil embargo and the GFC did the most damage. The end of the tech/dot-com bubble in the late 1990s was no picnic, either. However, away from those points in time, it was very manageable. My takeaway from reviewing this research is this: Don't panic and don't change course. Stay with your plan.
- Let's talk about where we are right now and how to deal with this conflict and the volatility it is creating. It's time for discipline over emotion. It's time to have a plan. Here is my plan: If the VIX index closes over 30, using weekly data, I would favor dollar-cost averaging into equities. On Friday, March 6, the VIX closed at 29.49—close, but no cigar.
- A VIX reading of 30 or higher is my first line in the sand for action. Since 1990, when the VIX closed at 30 or higher on a weekly basis, forward returns for the S&P 500 were positive. Ranking three-month forward returns for those periods, the median was 6.85%, and the hit rate was 80.28% for positive returns. The six-month median forward return was 15.15%, and the positive-return hit rate was 80.28%. The one-year median forward return was 23.46%, and the hit rate was 88.57%. I like those odds. Favor discipline over emotion.
- Similarly, if market movements get out of hand, and the VIX index closes over 50 on a weekly basis, in my playbook it becomes time for a little more aggressive approach. Rather than dollar-cost averaging, buying quality stocks may be another approach. In the periods of the weekly VIX closing above 50 since 1990, the median forward return one-year out was 24.06%, with a 100% hit rate. Discipline over emotion.
- Remember the Rule of 16. This rule gives you an idea of the magnitude of price movements you can expect. The calculation is $(\text{VIX Index level}/16) = \text{expected price movement in percentage terms}$. A VIX Index reading of 32 $(32/16) = 2\%$ expected movement.
- We are bullish on the market broadening theme, which includes a preference for US small- and mid-cap stocks and emerging market (EM) equities. You can read more about the global equity opportunity in our Institute paper, "[Broadening momentum: From US technology leadership to US small caps and emerging markets.](#)"
- Consider this: As of the March 12 market close, 267 stocks, or 53% of the components of the S&P 500, are beating the index itself year-to-date (YTD). Similarly, 186 stocks, or 37%, of the components, are up more than 5% YTD, and 198 stocks, or 39%, of the components, are down more than 5% YTD. We view this dispersion as a bullish signal for active management. It indicates that stock-picking is driving alpha.
- This is our bottom line: We think it's best to have a diversified equity playbook that includes large-, mid-, and small-cap exposure in the United States with a balance of growth and value. The same can be said for ex-US equity exposure: We favor positions in EMs and developed international markets. To act on the broadening theme, consider reducing concentration and diversifying portfolio exposure. The VIX index parameters described above can be helpful for deciding further action.
- Have a listen to this recent [Animal Spirits podcast](#), where I had the chance to speak with Michael Batnick and Ben Carlson of Ritholz Wealth Management.

Fixed income

- We expect US 10-year Treasury bond yields to trade in a range of 4.0% to 4.25% during 2026. Last week, the yield rose to 4.26%, on the high side of that range. The two-year Treasury yield also rose, punching out of its range with a trade at 3.74%. The US yield curve has flattened recently, with the two-year-to-10-year spread falling to 51 basis points (bps). We expect bull-steepening of the yield curve in 2026.

Fixed income (continued)

- We expect short-duration fixed income mandates and corporate credit to outperform cash again next year. Considering our views on US 10-year Treasury yields, we do not expect duration to be a significant driver of total return this year. Rather, all-in yield capture seems to be the play.
- Credit spreads have made big moves in the last week. Investment-grade spreads (one-year/three-year option-adjusted spreads, or OAS) are 62 bps over Treasuries, up from 44 bps in early February. High-yield spreads, as proxied by the Bloomberg US Corporate HY OAS, reached 298 bps over Treasuries in the past week, up from 250 bps in January. Corporate fundamentals remain healthy, we think, although we also are seeing stress in the system now.
- We are bullish for municipal bonds again this year and find taxable-equivalent yields to be attractive, along with robust fundamentals. Importantly, the increased supply that hit the marketplace in 2025 has run its course for now, and muni bonds have been performing well since last August. We think this positive trend can continue. To get a current update on the municipal sector, have a listen to Ben Barber, Director of Municipal Bonds at Franklin Templeton Fixed Income, and Rick Polsinello, my colleague at Franklin Templeton Institute, discussing “[The opportunity in municipal bonds](#),” in our recent “Talking Markets” podcast.

Sentiment

- The percentage of bullish investors in the latest AAIL Investor Sentiment survey dropped to 32% last week, down one tick from the prior week’s reading. The percentage of bearish investors in the AAIL survey was 46%, up 10 ticks from the prior week.
- Neither of these readings has reached extremes, but sentiment is growing more cautious. Remember, market analysts view this as a contrary indicator.

We will continue to analyze the markets and will offer insights again next week.

*Source of data (except where noted) is Bloomberg as of March 13, 2026. There is no assurance that any forecast, projection or estimate will be realized. An investor cannot invest directly in an index, and unmanaged index returns do not reflect any fees, expenses or sales charges. **Past performance is not an indicator or a guarantee of future performance.** Important data provider notices and terms available at www.franklintempletondatasources.com.*

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Glossary of terms

The AAIL (American Association of Individual Investors) Sentiment Survey: This survey offers insight into the opinions of individual investors by asking them their thoughts on where the market is heading in the next six months.

Breakeven rates: The difference between yields of Treasury bonds and TIPS for issues of the same tenor/maturity, calculated by subtracting TIPS yields from Treasuries; a measure of inflation.

Capital expenditure (capex): Funds that companies spend to acquire, upgrade or maintain physical assets, such as buildings, technology or equipment, with the purpose of maintaining or growing future operations.

Duration: A measure of how much a bond’s price changes relative to changes in interest rates.

Option-adjusted spread (OAS): Measures the spread between a bond’s interest rate and the risk-free rate, while adjusting for any embedded options like callables or mortgage-backed securities.

Personal Consumption Expenditures (PCE) and core PCE: Measures the price changes in goods and services purchased by US households; core PCE excludes food and energy prices. Both are measures of inflation.

Taxable-equivalent yield: The yield of a municipal bond investment calculated to reflect the benefits of income tax exemption and to be comparable to the yield of a taxable bond.

U-3 unemployment rate: The official measure used by the US Bureau of Labor Statistics (BLS) to report the percentage of the labor force that is unemployed and actively seeking work.

Yield spreads/tights: Spreads are the difference between yields on differing debt instruments of varying maturities, credit ratings, issuers or risk levels. "Tight" in reference to spreads indicates small differences in yields.

Indexes

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 of future results.

Bloomberg US Corporate High Yield Index: Tracks the performance of the USD-denominated, high yield, fixed-rate corporate bond market.

S&P 500® Index (SPX): A market capitalization-weighted index of 500 stocks, a measure of broad US equity market performance.

US Dollar Index: A basket of six foreign currencies (euro, Japanese yen, UK pound sterling, Canadian dollar, Swedish krona, and Swiss franc) used to track the relative strength of the US dollar, with a higher index value representing US dollar strength.

The Chicago Board Options Exchange (CBOE) Volatility Index (VIX): A measure of market expectations of near-term volatility as conveyed by S&P 500 stock index option prices.

WHAT ARE THE RISKS?

All investments involve risks, including possible loss of principal.

The **allocation of assets** among different strategies, asset classes and investments may not prove beneficial or produce desired results.

Diversification does not guarantee a profit or protect against a loss.

Equity securities are subject to price fluctuation and 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. **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**.

The **investment style** may become out of favor, which may have a negative impact on performance.

Large-capitalization companies may fall out of favor with investors based on market and economic conditions.

Small- and mid-cap stocks involve greater risks and volatility than large-cap stocks.

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