April 2026

Franklin Templeton Investment Solutions

Allocation Views

From Goldilocks to geopolitics—repositioning for an energy shock

Summary and themes

Our approach to risk remains highly tactical moving into April, as conflict in the Middle East continues to drive markets.

Disruption of energy supplies is the main reason for tension in financial markets, and Iran retains the ability to impede energy production and transit regardless of US military dominance.

A complete resolution of hostilities is unlikely, in our view, despite the fragile ceasefire. As a result, we believe energy prices will remain elevated, feeding into inflation expectations, eroding private sector confidence and slowing economic growth.

Rising inflation makes it harder for central banks to stimulate sluggish economies, feeding the stagflation[1] narrative and supporting a defensive approach to asset allocation.

Against this background, we have neutralized our cross-asset positioning but still hold some risk within our intra-asset allocations.

Macro themes

Growth steady, but weakening

- Leading economic indicators have weakened somewhat, as business activity is crimped by higher input costs and waning confidence.
- Corporate sentiment appears strong, as evidenced by positive earnings revisions and guidance for calendar year 2026.
- The US economy has proven relatively robust, while labor market data is disparate but remains stable.

Persistent inflation pressures

- Inflation pressures were already increasing prior to the energy price shock, with most prints above central bank targets.
- Elevated energy prices may diminish real incomes and suppress demand, contributing to stagflationary conditions within major economies.
- Tariffs have been absorbed by both US consumer prices and business margins. As a result, core goods inflation remains above trend, albeit pressures may have peaked.

Policy bifurcation

- There is an increasing bifurcation between supportive fiscal policy and restrictive monetary policy as markets assess the energy price shock.
- The Middle East conflict has catalyzed a recalibration of policy expectations, with multiple hikes now priced in for most regions.
- Fiscal policy in major economies is generally supportive of growth. US tax refunds will likely offset tariff headwinds, while energy support packages could also prove influential.

Portfolio positioning themes

Tactically neutral

- Forecasting geopolitics is difficult and always requires a degree of humility. As a result, we strive to curtail the tracking error in our portfolios and reduce equity risk, as we await greater clarity.
- The macro backdrop has become more challenging, as inflation limits expectations for stimulative monetary policy.
- Sentiment and positioning have retreated to more attractive levels, supporting risk assets, while corporate fundamentals are relatively supportive.

Rotating toward core

- We have reassessed our US equity positioning, adding to core equities as the conditions for market breadth have weakened, amid a less attractive macro backdrop.
- We have trimmed our overweight allocation to Japanese and emerging market (EM) equities, given greater sensitivity to energy supply constraints caused by the Middle East conflict.
- We coordinate those changes with a reduction in underweight exposure to European and UK equities, as we strive to reduce tracking error.

Neutralizing government bonds

- We expect demand destruction to play a greater role in monetary policy decisions than inflation.
- Resilient US growth and sticky inflation make Federal Reserve (Fed) easing less likely, in our view. As a result, we stay underweight US duration.
- We have decreased exposure to EM local-currency bonds, taking a more cautious view of debt in this region amid ongoing uncertainty and US dollar strength.

1. Stagflation: A combination of high inflation, elevated unemployment and stagnant growth.

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Disruption of energy supplies is the main reason for tension in financial markets, and Iran retains the ability to impede energy production and transit regardless of US military dominance.

A complete resolution of hostilities is unlikely, in our view, despite the fragile ceasefire. Negotiations to facilitate a full deescalation may be protracted and supply constraints are likely to persist. As a result, we believe energy prices will remain elevated, feeding into inflation expectations, eroding private sector confidence and slowing economic growth.

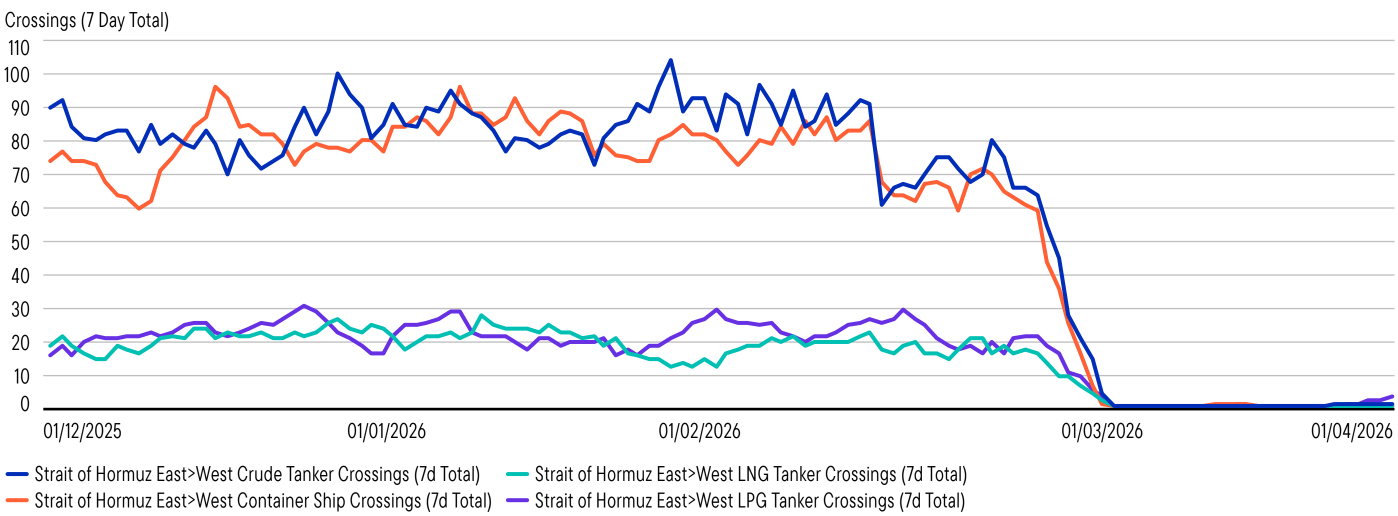
Rising inflation makes it harder for central banks to stimulate sluggish economies, feeding the stagflation narrative and supporting a defensive approach to asset allocation.

Against this background, we have neutralized our cross-asset positioning but still hold some risk within our intra-asset allocations. Most of these positions are predicated on a transitory energy supply shock and should benefit from concrete evidence of deescalation. Conversely, any signs of a more drawn-out conflict may require a reassessment of those exposures.

The Strait of Hormuz Is Effectively Closed

Shipping Has Fallen Sharply and Remain Very Limited

Exhibit 1: Weekly Ship Transits Through the Strait of Hormuz



Source: Macrobond. As of April 1, 2026.

Signs of macro fragility

Geopolitical tensions aside, macro indicators remain resilient, but we have seen some weakening recently that supports our neutral view of risk. Softer leading economic indicators and Purchasing Managers' Index (PMI) data point to slowing growth, while sticky core inflation is arguably more of a concern than an energy price shock.

Nowcast data from the Federal Reserve Bank of Atlanta has weakened, with the most recent estimate forecasting US economic growth of 1.3% (as of April 7, 2026).[2] US and European business activity slowed substantially in March, according to PMI data, impacted by rising input costs and lower business confidence.[3]

Elsewhere, the Federal Open Market Committee (FOMC) has revised projections for core personal consumption expenditures (PCE) inflation upward to 2.7% by the end of 2026, from 2.5% in its fourth quarter release.[4] Core PCE inflation rose by 0.40% (month-on-month) in both December and January, to move above 3.0% (year-on-year).

2. Source: GDPNow Estimate. Federal Reserve Bank of Atlanta. April 7, 2026.
3. Source: US Flash PMI. S&P Global. March 2026.
4. Source: Summary of Economic Projections (FOMC median). US Federal Reserve. March 2026.

Higher energy prices have not yet begun to materially influence consumer behavior or spending. Anecdotal evidence points to pricing adjustments for purchases most closely tied to energy, such as parcel deliveries, but demand remains strong.

Market expectations for monetary policy have pivoted decisively around the energy price shock, as rate hikes are now expected in most major economies. This may have a negative impact on growth by adding to borrowing costs and influencing business and consumer sentiment. It is likely to weigh more heavily on lower income consumers, widening gaps in the K-shaped economy.

Resilient earnings, improving valuations

Conflict in the Middle East has not affected the positive outlook for corporate earnings, given elevated energy prices have yet to influence margins or spending.

Global earnings are expected to grow by almost 18% during the next 12 months, based on IBES[5] consensus estimates, while revisions to those expectations have also accelerated, rising by 20% compared to 12 months ago. In addition, earnings revisions breadth has improved, indicating a broadening of economic resilience. Our proprietary US earnings model is slightly more conservative but still expects US earnings to grow by 13.1% over the next year, against market consensus of 17.6%.

As we mentioned earlier, these figures are predicated on a transitory energy price shock, which remains our base case. An analysis of fast-moving economic indicators such as credit card spending, jobless claims, retail sales and consumption shows no material impact from the crisis, although weakness in some areas—such as mortgage applications and consumer sentiment—bears watching.

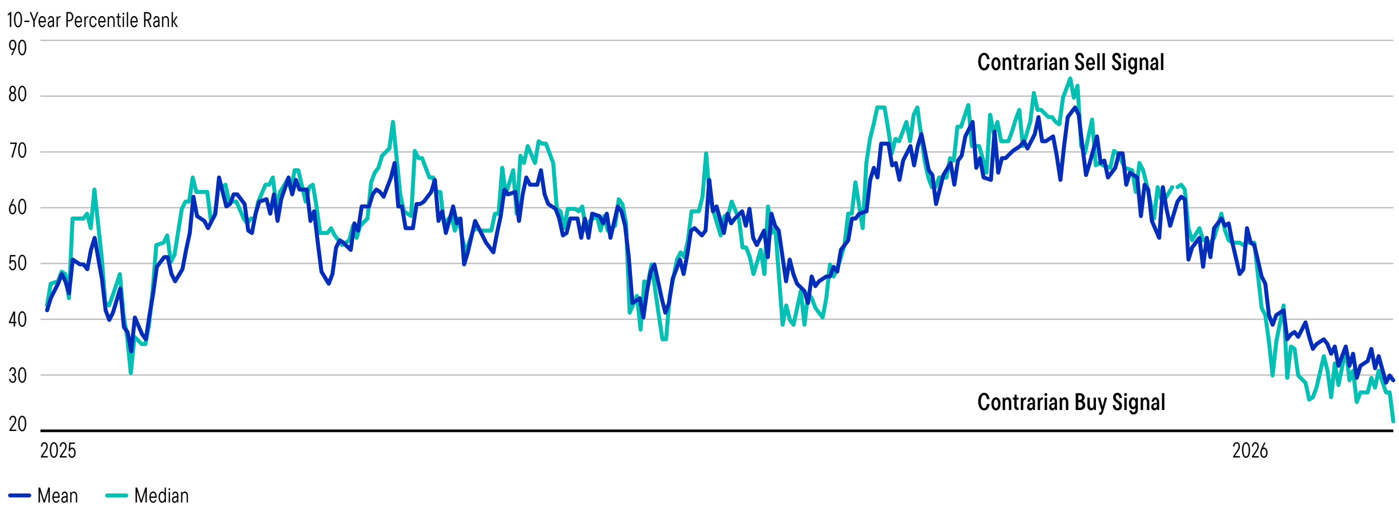
Changes to sentiment and positioning offer further support to equities, given a material retrenchment in previously stretched indicators. A cross-section of these technical indicators suggests levels are declining sharply toward a contrarian buy signal, where signals had been flashing sell at the end of February.

In addition, the recent drawdown has curtailed market momentum and improved equity valuations. However, equities still look overvalued when set in the context of macro volatility, slowing growth and persistent inflation. Our model also suggests that US stocks are overvalued relative to other regions.

Favorable Technical Setup

A Range of Sentiment and Positioning Indicators Are Now Flashing a Contrarian Bullish Signal

Exhibit 2: A Cross-section of Technical Indicators Compared Against a 10-year Trailing Average



Sources: CBOE, CFTC, NAAIM, AAII, San Francisco Fed, University of Michigan, ZEW, Macrobond. As of March 31, 2026.

5. Institutional Brokers' Estimate System (IBES).

US core defensiveness

Prior to the conflict, markets were set up around the continuation of a "goldilocks" scenario of resilient growth, ongoing disinflation and stimulative fiscal and monetary policy.

This environment informed the tilt toward US value stocks in our portfolios, as we weighed up expensive valuations for mega-cap growth stocks alongside capital expenditure concerns and artificial intelligence (AI) replacement fears.

Corporate fundamentals remain strong and continue to support the tilt toward value, but economic developments have changed the calculus elsewhere and pushed us to neutralize our style-factor preferences.

Labor data has softened somewhat, while core inflation has begun to rise, complicating any response from the Fed. A backdrop of slowing growth has also weakened earnings momentum.

Inflation risks from the oil price shock have made it less likely that the Fed will be able to make multiple interest-rate cuts, even if consumer spending or labor market data deteriorate further. Higher energy prices could also increase manufacturing costs and neutralize fiscal stimulus, given that a modest increase in crude oil prices could offset tax rebates for lower income consumers.

As a result, we see greater perceived safety in large-cap core equities, which are more defensive and less impacted by a broad economic downturn.

Tactical positioning

We have trimmed our overweight allocations to EMs and Japan moving into April. These markets are more vulnerable to recent developments in the Middle East given greater reliance on natural gas, oil and other raw materials from the region to power their economies. However, several factors inform our ongoing optimism toward these regions, despite reduced exposure.

In Japan, Prime Minister Sanae Takaichi has embarked on an ambitious program of fiscal stimulus in the order of 21 trillion yen, designed to boost the economy. Government funds are likely to target semiconductors, rare-earth elements production, robotics and defense with the aim of raising manufacturing activity.

Earnings have also risen along with higher inflation, which has allowed Japanese companies to raise consumer prices. As inflation has stabilized and moderated in the last few months, those companies have established and maintained healthier profit margins. Trailing earnings growth has risen to 11.4%,[6] while the breadth of earnings revisions has also outstripped other regions recently, reflecting a healthier economy.

In EMs, earnings expectations continue to accelerate, helped by improved corporate governance, greater policy support and the critical role Asia plays in the production of AI hardware.

Set against these positives is vulnerability to an energy price shock due to a heavy reliance on imports from the Middle East. Japan imports 93% of its crude oil through the Strait of Hormuz, while Taiwan, India and South Korea import 67%, 42% and 36%, respectively, via the same route. Japan and South Korea hold more than 200 days of oil inventories to offset supply constraints, meaning their economies would be relatively unaffected by dwindling supplies for at least six months. However, the impact could be more serious for India, which holds just 30 days of oil inventory.[7]

Taiwan is particularly important to the global semiconductor industry and relies heavily on natural gas to power its factories. It imports 28% of its natural gas from the Middle East, but holds just 10 days of inventory, creating an urgent problem should supplies continue to be restricted.

6. Sources: IBES estimates. March 24, 2026. There is no assurance that any estimate, forecast or projection will be realized.
7. Sources: Statistical Review of World Energy, Energy Institute; India Ministry of Power; International Energy Agency (IEA). There is no assurance that any estimate, forecast or projection will be realized.

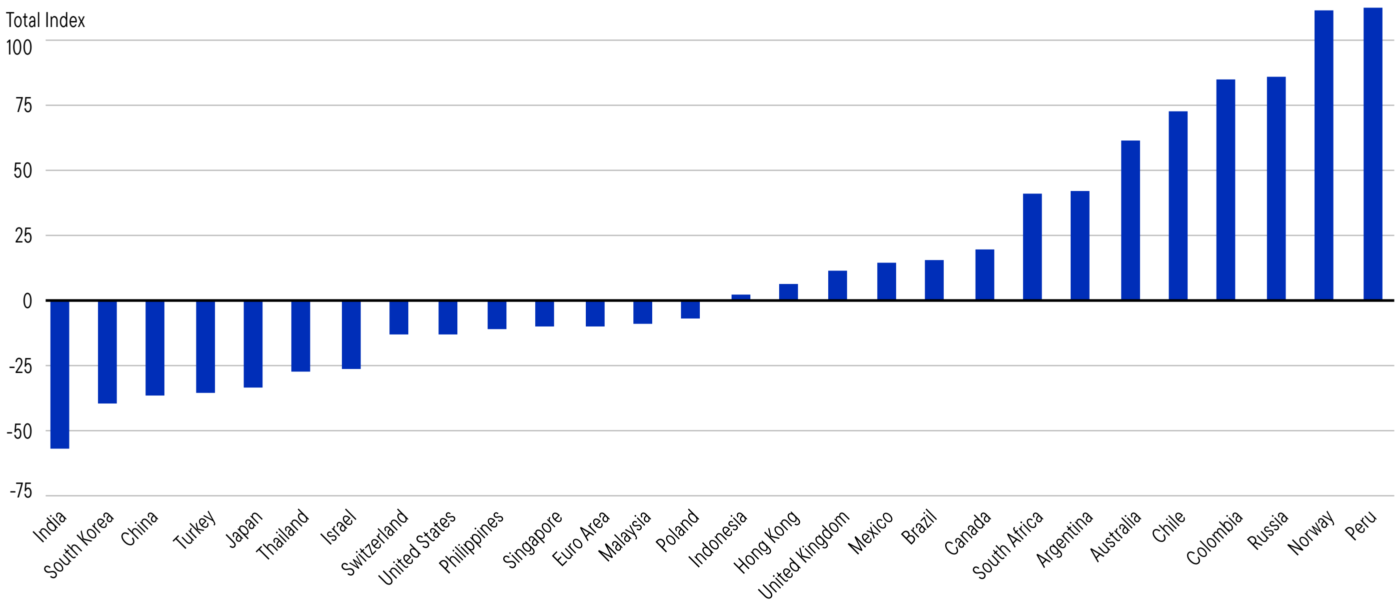
Our optimism toward Japan and EMs rests on an assessment that the energy supply shock should be temporary, but the reduction in exposure offers a measure of protection for portfolios should energy shortages become more critical.

We also reduced exposure to EM debt moving into April amid a strengthening US dollar and a more uncertain macro background.

Energy Vulnerability

Expensive Energy Imports Are Weighing on Asian Countries

Exhibit 3: Commodity Terms of Trade Indexes for a Range of Global Economies



Sources: Sources: Citi, Macrobond. As of April 1, 2026.

Monitoring inflation dynamics

Conflict in the Middle East has caused a significant change in expectations for monetary policy. Financial markets now expect most central banks to raise interest rates two or three times this year to combat higher inflation, a major pivot from just a few weeks ago, when markets expected rate cuts for most economies.

There is a chance that the energy price shock could have a material impact on inflation, but only if it becomes embedded in the real economy and starts to impact core inflation readings. This would require it to spill over into wages, expectations and broad-based core pricing, which is something we don't currently see.

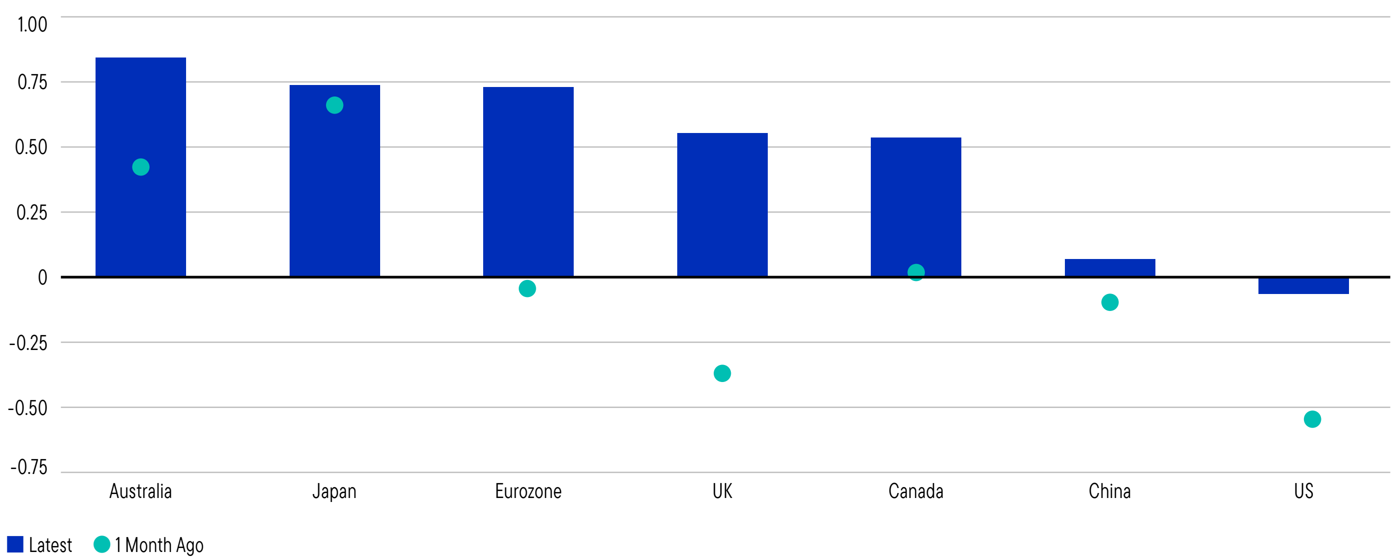
It is more likely, in our view, that higher energy prices will destroy demand, weaken real incomes and margins and thus ease inflation pressures. Hiking interest rates amid an energy supply shock could deepen the growth slowdown in the global economy, triggering a swift loosening of policy, particularly if the conflict deescalates and energy supplies begin to return to normal.

As a result, we remain overweight duration[8] in weaker economies that may require policy support, such as Canada and the United Kingdom. Conversely, we are underweight US Treasuries, where growth appears more robust, and core inflation appears elevated, complicating policy intervention from the Fed.

Hawkish Global Policy Pivot

Most Central Banks Are Now Expected to Raise Interest Rates

Exhibit 4: Expected Change in Central Bank Policy Rates Over the Next 12 Months (Latest vs One Month Ago)



Sources: Bloomberg, Macrobond. As of April 2026.

8. Duration: A measure of how much a bond's price changes relative to changes in interest rates. A duration strategy has sensitivity to interest rates.

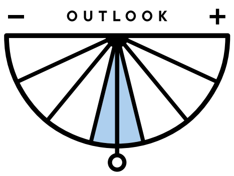
Allocation settings views—April 2026

Pendulum settings reflect cross-asset-class views

High level allocation tier

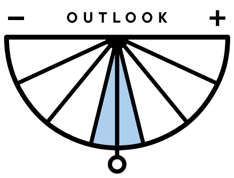
Asset class | **Conviction** | **Our viewpoint**

Equities



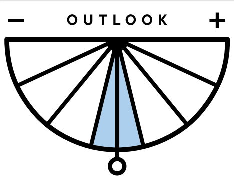
- Our approach to risk remains highly tactical moving into April as conflict in the Middle East continues to drive markets.
- A complete resolution of hostilities is unlikely, in our view, meaning risks will remain, albeit reduced from current levels. The macro backdrop has become more challenging, as growth indicators weaken and inflation limits expectations for stimulative monetary policy.
- However, sentiment and positioning have retreated to more attractive levels, supporting risk assets.

Bonds



- We expect demand destruction to play a greater role in monetary policy decisions than inflation.
- The recent inflationary-fueled uptick in yields may present an opportunity to add selectively to duration amid a weakening macro backdrop.
- However, rising inflation makes it harder for central banks to stimulate sluggish economies, feeding the stagflation narrative and supporting a defensive approach to asset allocation.

Alternatives

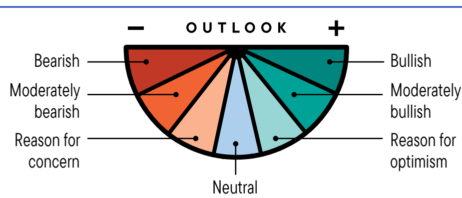


- The recent rise in energy prices means the risks attached to “Operation Epic Fury” now appear adequately priced into markets.
- Beyond conflict in the Middle East, increased demand from AI should offer long-term support to energy and industrial metals.
- Elsewhere, we see structural attractions in naturally diversifying alternatives such as private assets.

Cash

- We believe elevated short-term yields currently offer attractive risk-free returns.
- However, the requirement to lower our portfolios’ interest-rate sensitivity has moderated as yields have risen month-on-month.
- We have added slightly to cash during the period, influenced by elevated uncertainty.

Understanding the pendulum graphic



Arrows represent any change since the last month end.

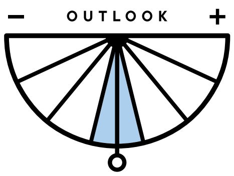
Allocation tier

Asset class | **Conviction** | **Our viewpoint**

Equity regions: Pendulum settings relative to equity asset class broadly

Growth

United States



- High-quality stocks tend to outperform in an environment of macro risks, and markets have historically rewarded growth names when the economic outlook has faltered.
- Rotation momentum has been reduced by stagflation risks, which typically impact the real economy, hurting consumption and manufacturing.
- We remain concerned about the sustainability of AI capital investment, but more immediate macro concerns mean we favor core US equities as a defensive measure.

Value

United States

- Corporate fundamentals remain strong, but economic developments have changed the calculus elsewhere and pushed us to neutralize our style factor preferences.
- Growth has been slowing and labor data has softened somewhat, while core inflation has begun to rise, complicating any response from the Fed.
- Slowing growth typically weakens cyclical earnings momentum, working against the broadening-out trade.

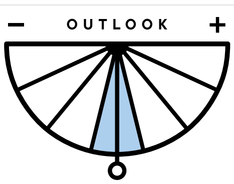
Small-Cap Stocks

United States

- The weakening US macro backdrop is negative for small-cap stocks, as are market expectations for more hawkish monetary policy to combat inflation.
- An energy-cost shock is generally bad for small caps given their relatively low pricing power and higher operating leverage.
- The Russell 2000 Index has relatively more financials, industrials and consumer discretionary stocks which are likely to face greater disruption from energy volatility.

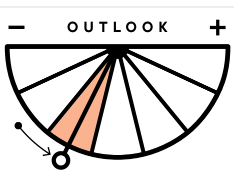
International

Canada



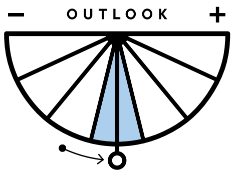
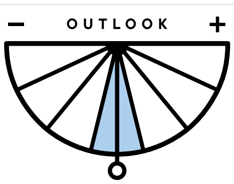
- Canadian macro indicators were mixed in February, as the manufacturing PMI strengthened, but the services PMI remained weak and trailing earnings growth declined.
- However, the Bank of Canada (BoC) has chosen to prioritize inflation, which remains somewhat elevated in certain areas. The BoC may need to raise rates to combat energy inflation rather than stimulate the economy.
- Canada's over-reliance on commodities is also a weakness, in our view, given some overextension in materials markets.

Europe ex United Kingdom



- Manufacturing activity continues to soften, due to structural weaknesses in Germany—including high energy costs, labor shortages and regulatory burdens.
- A subdued macro backdrop, higher energy prices and weak domestic demand could begin to weigh on eurozone equities. We are seeing this reflected in thinner profit margins and narrower market leadership.
- Despite this, we have trimmed our underweight to eurozone stocks as these markets have less direct exposure to Middle East energy than their Asian counterparts.

Allocation tier

Asset class	Conviction	Our viewpoint
United Kingdom		• UK consumers have been saving more, while disposable income growth has fallen sharply into negative territory amid a weakening labor market. • The United Kingdom is facing significant macro headwinds, including slowing economic growth and negative employment growth. Higher energy prices are beginning to exacerbate these factors. • However, the United Kingdom is a defensive market, influenced by global energy majors, and should perform better in the current volatile conditions. As such, we have improved our view and have neutralized positioning.
Japan		• Japan is particularly vulnerable to an energy price shock, given its heavy reliance on oil from the Middle East. • However, the country holds healthy energy reserves and should have no supply concerns for the next few months. • The new Japanese government coalition is pushing ahead with fiscal policy stimulus, while earnings growth and revisions remain strong.
Australia		• Hotter-than-expected inflation prompted the Reserve Bank of Australia (RBA) to raise interest rates in March, in addition to the rate increase in February. Against this background, growth has begun to slow. • Weak demand in China likely puts a ceiling on Australia's industrial production momentum in the months ahead. • Corporate earnings revisions are relatively weak compared to other regions, while trailing earnings also remain negative. Equity market breadth has fallen amid persistently weak productivity.
Emerging ex China		• Influential Asian EMs, including Taiwan and South Korea, are vulnerable to energy price shocks linked to the closure of the Strait of Hormuz. • Taiwan's semiconductor industry is highly reliant on natural gas and has dwindling inventories at its disposal. • Having said that, we remain positive, given earnings expectations are rising rapidly across EMs ex-China. Significant AI capital spending by hyperscalers has been boosting hardware component makers in Asia.
China		• Macro and corporate fundamentals in China remain weak and fiscal and monetary stimulus measures have had little impact. Domestic demand continues to stagnate due to a deteriorating property sector and a weak labor market. • Chinese consumer sentiment remains at all-time lows, with weak domestic demand spilling over into earnings for technology firms amid intense price competition. • However, domestic flows from maturing term deposits have risen, as have foreign flows as investors seek stable markets amid the current conflict.

Allocation tier

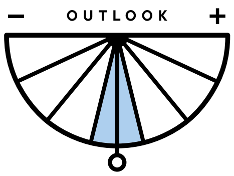
Asset class | **Conviction** | **Our viewpoint**

Fixed income sectors: Pendulum settings relative to fixed income asset class broadly

US Treasuries

- Markets are no longer pricing in interest-rate cuts from the Fed, despite a slight deterioration in labor markets and signs of slowing growth.
- Sticky core inflation and energy price concerns will likely make it difficult for the Fed to ease policy.
- Rising fiscal deficits and tax cuts add to upward pressure on yields, keeping us underweight US duration.

Eurozone Government Bonds



- In Europe, we expect demand destruction to play a greater role in monetary policy decisions than inflation.
- Europe is less reliant on the Middle East for energy than Asian economies and should therefore be less vulnerable to an inflation spike delivered by an energy price shock. Higher prices have the potential to add further pressure to an economy already weakened by regulatory burdens, labor shortages and competition from China.
- However, German fiscal expansion could result in increased sovereign issuance, adding upward pressure to eurozone yields.

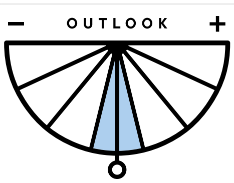
UK Government Bonds

- We expect demand destruction to play a greater role in monetary policy decisions than inflation.
- In our view, slowing wage growth, weak labor market momentum and fiscal tightening are likely to increase the attractiveness of UK Gilts.
- The UK government has raised taxes to narrow its fiscal deficit. As back-loaded taxes feed through, it is likely to slow economic growth, lower inflation and compound labor-market weakness. With policy still above neutral, the Bank of England should have room to ease further as growth slows.

Canada Government Bonds

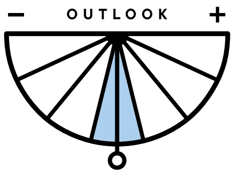
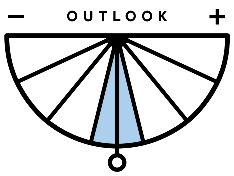
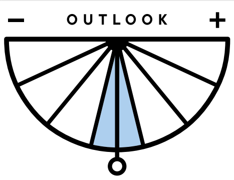
- The BoC held rates steady in March, but markets have priced in rate increases amid a focus on sticky inflation readings. We think this is optimistic and would expect yields to fall, if growth forecasts disappoint.
- There are some risks to the Canadian economy, amid a dependence on cyclical sectors. US trade restrictions and uncertainty continue to disrupt growth and exports.
- Labor-market data looks robust but is skewed by part-time workers, in our analysis.

Japan Government Bonds



- We believe recent interest-rate increases have moved Japanese government bond yields closer to equilibrium.
- However, the real policy rate is still below zero, in line with a deflationary environment, meaning the Bank of Japan (BoJ) remains stimulative.
- This gives the BoJ room to raise rates to combat energy-related inflation and support the Japanese yen, particularly against a background of additional stimulative fiscal policy.

Allocation tier

Asset class	Conviction	Our viewpoint
Australian Government Bonds		• The RBA raised interest rates at its March meeting, amid firmer inflation and tight labor market conditions. • The RBA remains data-dependent and has deemed a tight labor market, sticky inflation and a stable macro environment as reasons to become more restrictive. • However, relatively weak economic growth and negative trailing earnings growth may change that calculus.
Investment Grade		• The investment-grade sector has benefited from resilient corporate fundamentals and improved guidance, but a modest deterioration in macro forecasts is a concern. • Credit spreads have widened but remain relatively narrow, making the risk/return profile less attractive to us in a “risk-off” environment. • Against this background, we hold a neutral position on higher-quality credit, preferring the potential defensive features of government bonds.
High Yield and Loans		• Spreads have widened but remain relatively tight. In our view, they do not fully reflect the risks and tightening in financial conditions stemming from the conflict in Iran. • Moreover, spreads have not widened in line with the equity selloff. Investors are not benefiting from the usual cushion of falling rates in this scenario. • We believe the balance of risk and rewards favors neutrality.
Emerging Market (EM) Debt		• We have trimmed our exposure to EM local-currency debt amid a strengthening US dollar and growing risks to macro stability in Asia. • EM local-currency debt still offers a compelling long-term opportunity, as fiscal and monetary policy stability, in tandem with corporate governance improvements, should help to boost inflows of foreign capital. • However, risks related to conflict in the Middle East see us neutralize our position as we seek to manage tracking error within our portfolios.

Allocation Views

At **Franklin Templeton Investment Solutions (FTIS)**, we translate a wide variety of investor goals into portfolios powered by Franklin Templeton's best thinking around the globe. We serve a variety of institutional clients, ranging from sovereign wealth funds to public and private pension plans in addition to retail multi-asset clients around the world.

The hallmark of our approach is a central forum—the Investment Strategy and Research Committee (ISRC)—which generates a top-down view across asset classes and regions. Furthermore, it connects and synthesizes the bottom-up sector and regional insights of the global investment teams at Franklin Templeton. The ISRC also calibrates firmwide views with original analysis from our dedicated teams, which include both fundamental and quantitative research professionals.

FTIS actively engages with clients in an ongoing, collaborative partnership, to understand each client's particular needs and then to draw from our extensive global resources and capabilities to meet those goals. These portfolios are built, managed and monitored in the framework established by the ISRC, and undergo rigorous tests under multiple scenarios and market regimes.

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WHAT ARE THE RISKS?

All investments involve risks, including possible loss of principal.

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

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.

The allocation of assets among different strategies, asset classes and investments may not prove beneficial or produce the desired results. To the extent a strategy invests in companies in **a specific country or region**, it may experience greater volatility than a strategy that is more broadly diversified geographically.

Commodity-related investments are subject to additional risks such as commodity index volatility, investor speculation, interest rates, weather, tax and regulatory developments.

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 government's participation in the economy is still high and, therefore, **investments in China** will be subject to larger regulatory risk levels compared to many other countries.

Investing in privately held companies presents certain challenges and involves 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.

Active management does not ensure gains or protect against market declines. **Diversification** does not guarantee a profit or protect against a loss.

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