

ClearBridge

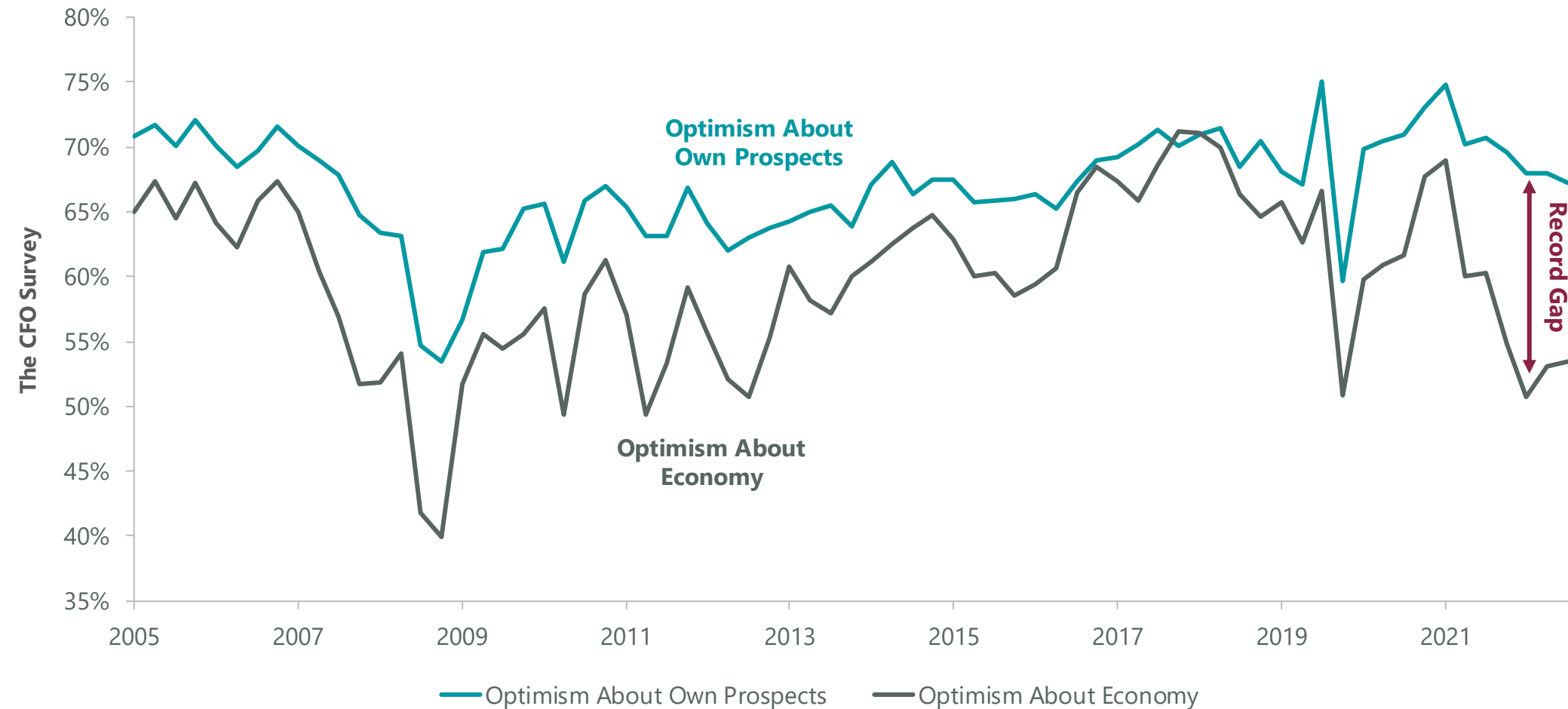
Investments

The Anatomy of a Recession: What to Look For and Where We're Headed

First Quarter 2023

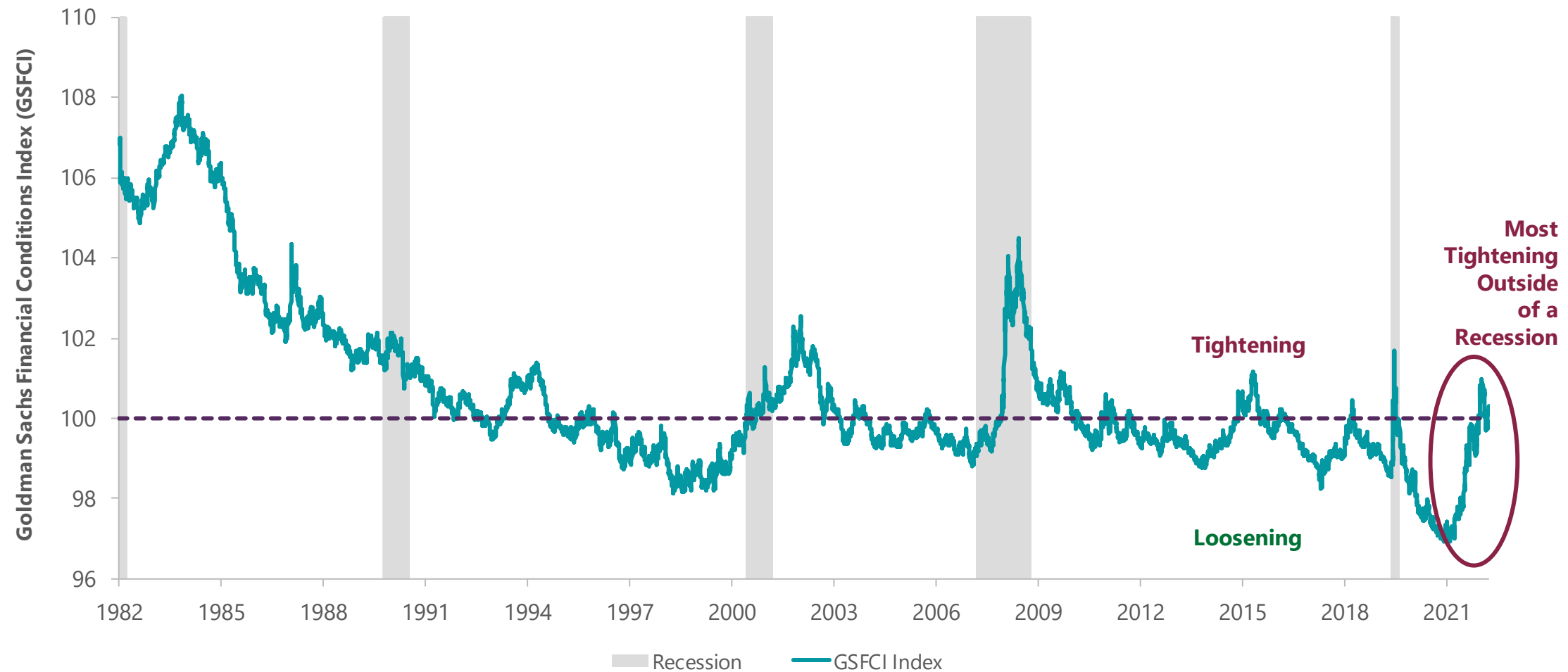
Past performance is no guarantee of future results. Financial term and index definitions are available in the appendix.

The Rorschach Economy: CFO Confidence



- ▶ **The Bad: CFO confidence about the economy is at near-recessionary levels.**
- ▶ **The Good: CFO confidence about their own businesses remains buoyant, potentially signaling less belt tightening to come.**

The Rorschach Economy: Financial Conditions



- ▶ **The Bad: 2022 has seen a sharp tightening of financial conditions, consistent with past recessions.**
- ▶ **The Good: Financial conditions have only recently moved into restrictive territory and are not yet at levels associated with past recessions.**

U.S. Recession Risk Indicators

- 12 variables have historically foreshadowed a looming recession
- The overall dashboard is currently signaling recession

		Current	Rapid Summer Deterioration		
		December 31	August 31	July 31	June 30
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

U.S. Recession Risk Indicators

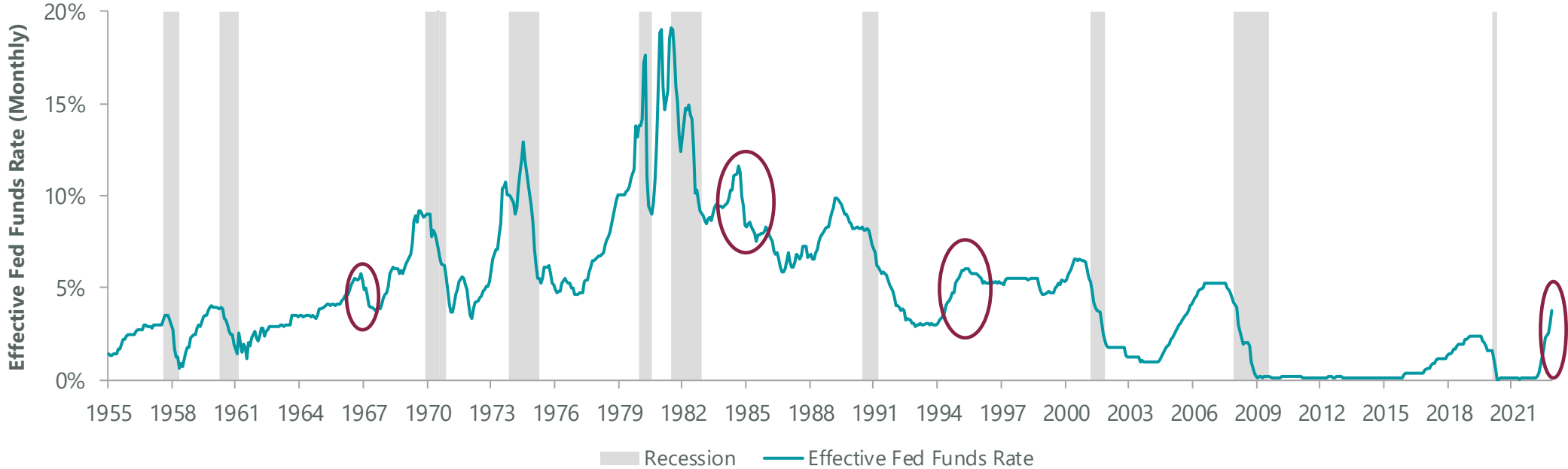
- 12 variables have historically foreshadowed a looming recession
- The overall dashboard is currently signaling recession

	Current	2020	2007-2009	2001	1990-1991	1981-1982	1980	1973-1975	1969-1970
Consumer	Housing Permits	●	↑	×	●	×	×	×	×
	Job Sentiment	●	●	×	×	×	×	●	●
	Jobless Claims	↑	↑	●	×	×	×	↑	×
	Retail Sales	×	↑	×	×	×	×	●	×
	Wage Growth	×	×	×	×	×	×	×	×
Business Activity	Commodities	×	↑	×	×	×	●	●	●
	ISM New Orders	×	●	×	×	×	×	×	×
	Profit Margins	×	×	×	×	×	×	●	×
	Truck Shipments	↑	↑	●	×	×	×	n/a	n/a
Financial	Credit Spreads	×	↑	×	×	×	×	↑	●
	Money Supply	×	↑	×	×	×	×	×	×
	Yield Curve	×	×	×	×	×	×	×	×
Overall Signal	×	●	×	×	×	×	×	●	×

↑ Expansion ● Caution × Recession

Data as of Dec. 31, 2022. Source: BLS, Federal Reserve, Census Bureau, ISM, BEA, American Chemistry Council, American Trucking Association, Conference Board, and Bloomberg. 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.

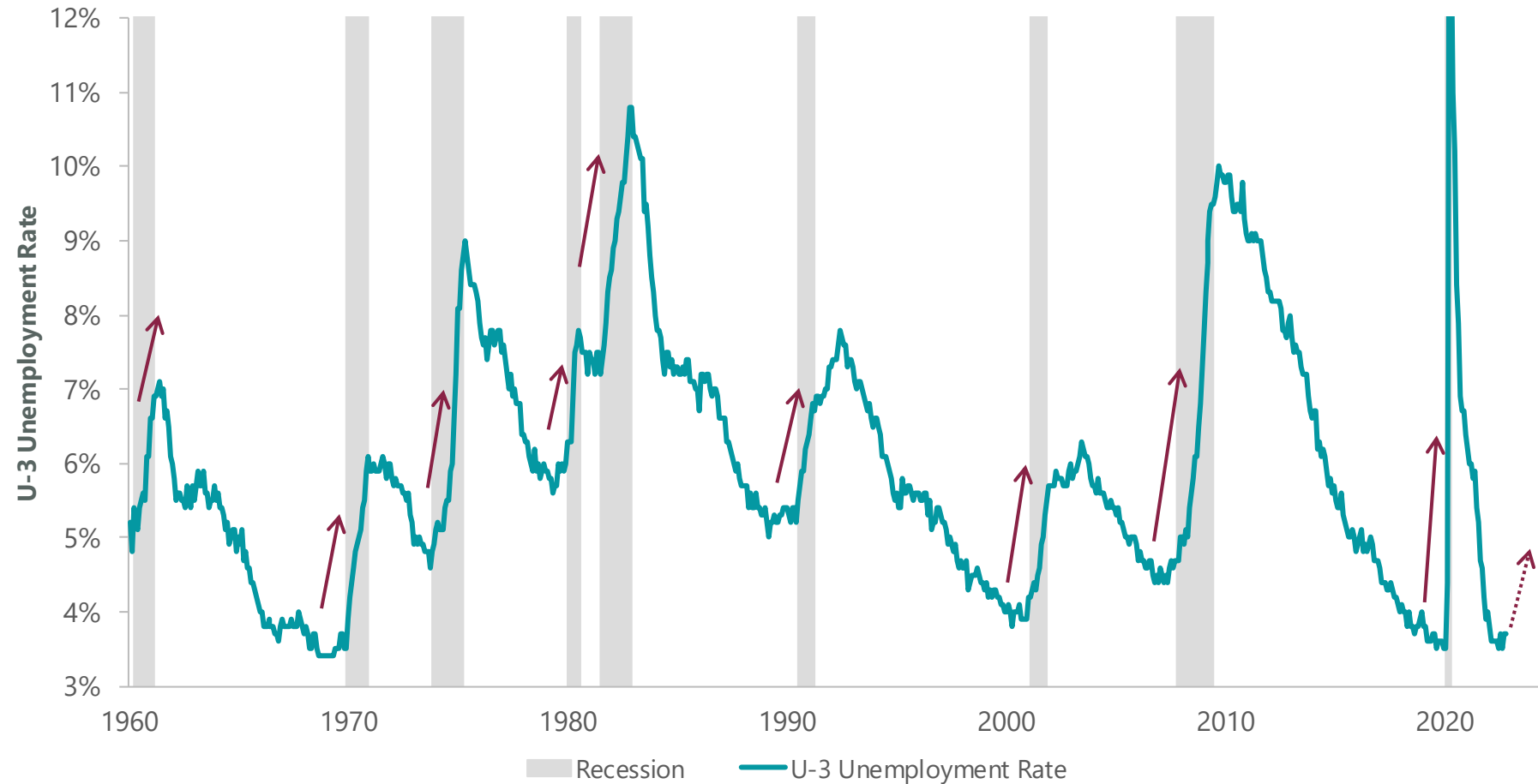
Don't Make the Same Mistake Twice



	Overall Recession Signal	Total Fed Rate Cut	Core Consumer Price Index YoY Percent Change			Unemployment Rate	
			Fed Pivot (or Current)	+12 Months	+36 Months	Fed Pivot (or Current)	Labor Market
December 1966	✘	-2.0%	3.3%	3.8%	6.2%	3.8%	Tight
September 1984	⬆️	-5.8%	5.1%	4.0%	4.3%	7.3%	Excess
July 1995	●	-0.8%	3.0%	2.7%	2.2%	5.7%	Slack
Current			6.0%			3.7%	

- ▶ **There have been 13 primary Fed tightening cycles historically, with 10 ending in a recession and three soft landings.**
- ▶ **With a tight labor market today similar to 1966, the Fed is likely wary of pivoting too early which could give way to a reacceleration of inflation.**

What's The Fed Telling Us?

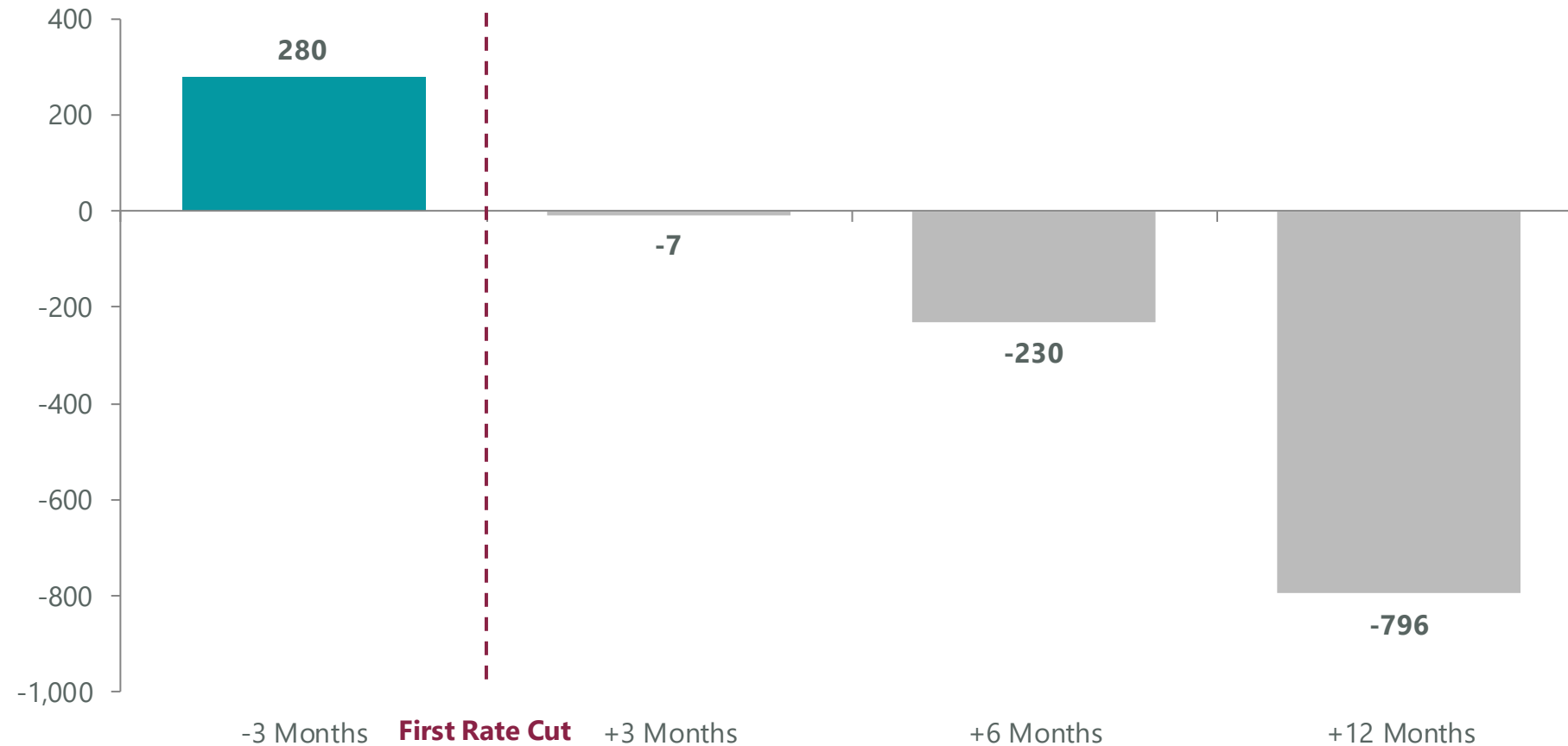


	Fed Projection
Current	3.7%
12/31/23	4.6%
12/31/24	4.6%
12/13/25	4.5%

- ▶ **Historically, an increase of 0.5% (or more) in the unemployment rate vs. the lows over the prior year has signaled a recession (the Sahm Rule).**
- ▶ **The Fed Dot Plot signals an expected 0.9% increase in the unemployment rate next year on top of the 0.2% rise that has already happened.**

The Fed Has Little Tolerance For Job Losses

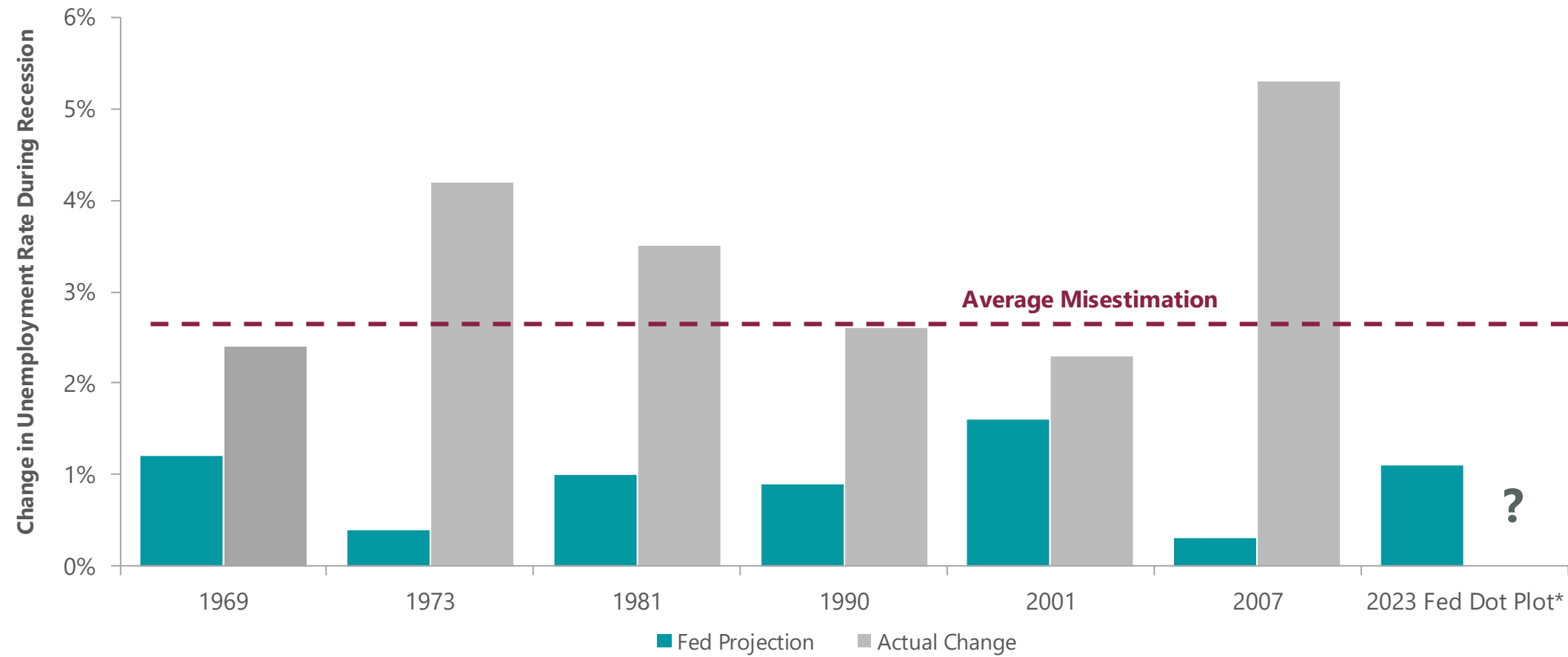
Median Cumulative NFP Gain/Loss (1,000's) Around First Fed Rate Cut



Fed Funds Rate	
Current	4.375%
12/31/23	5.125%
12/31/24	4.125%

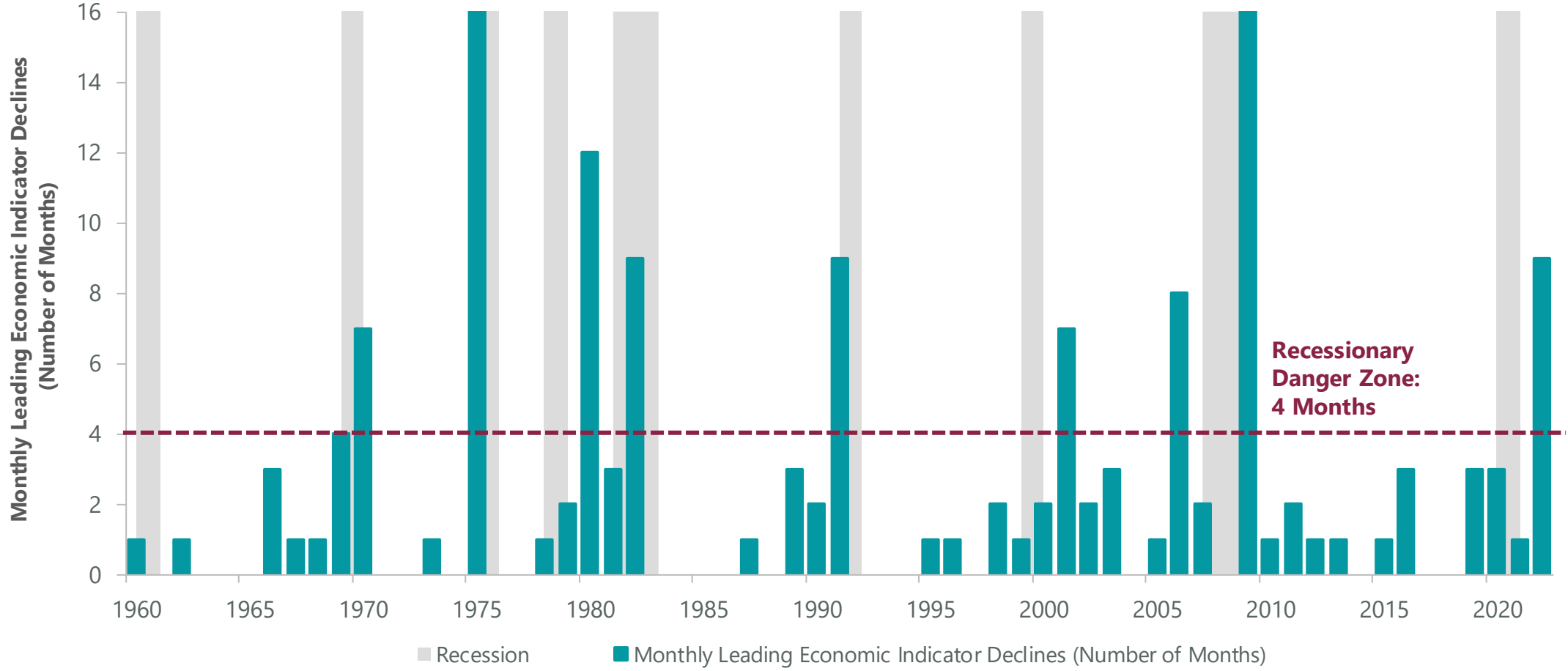
- ▶ Typically, the Fed anticipates layoff cycles (which tend to lag) and is quick to ease monetary policy as the labor market softens.
- ▶ The Fed Dot Plot implies 1.6 million job losses along with further rate hikes in the coming year. No cuts are expected until 2024 which is a departure from previous cycles.

The Fed's Rose-Colored Glasses



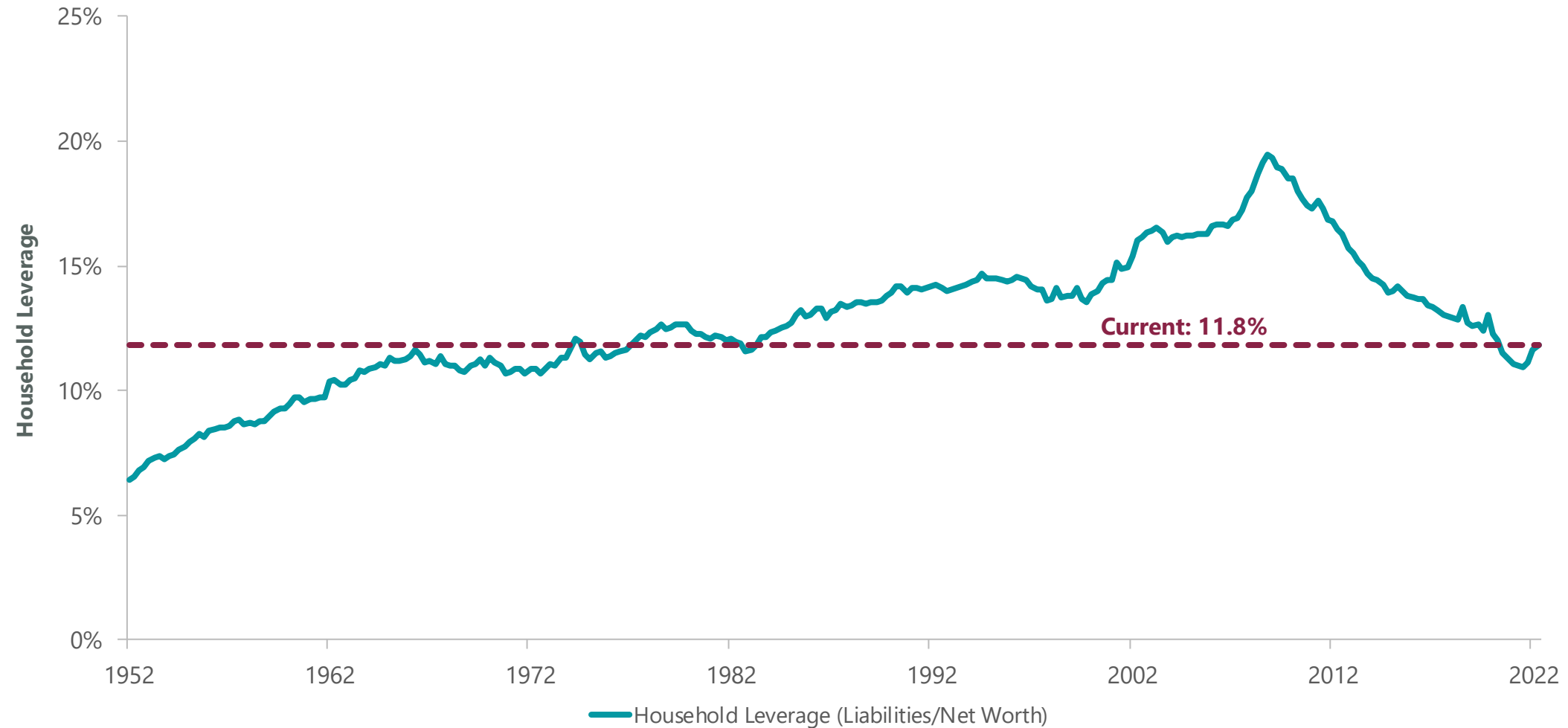
- ▶ **The Fed underestimates the pain in labor markets experienced during a recession by 2.5% on average.**
- ▶ **Although the Fed Dot Plot suggests unemployment rising to the mid-4% range, history suggests something even higher.**

Leading Indicators Point to Recession



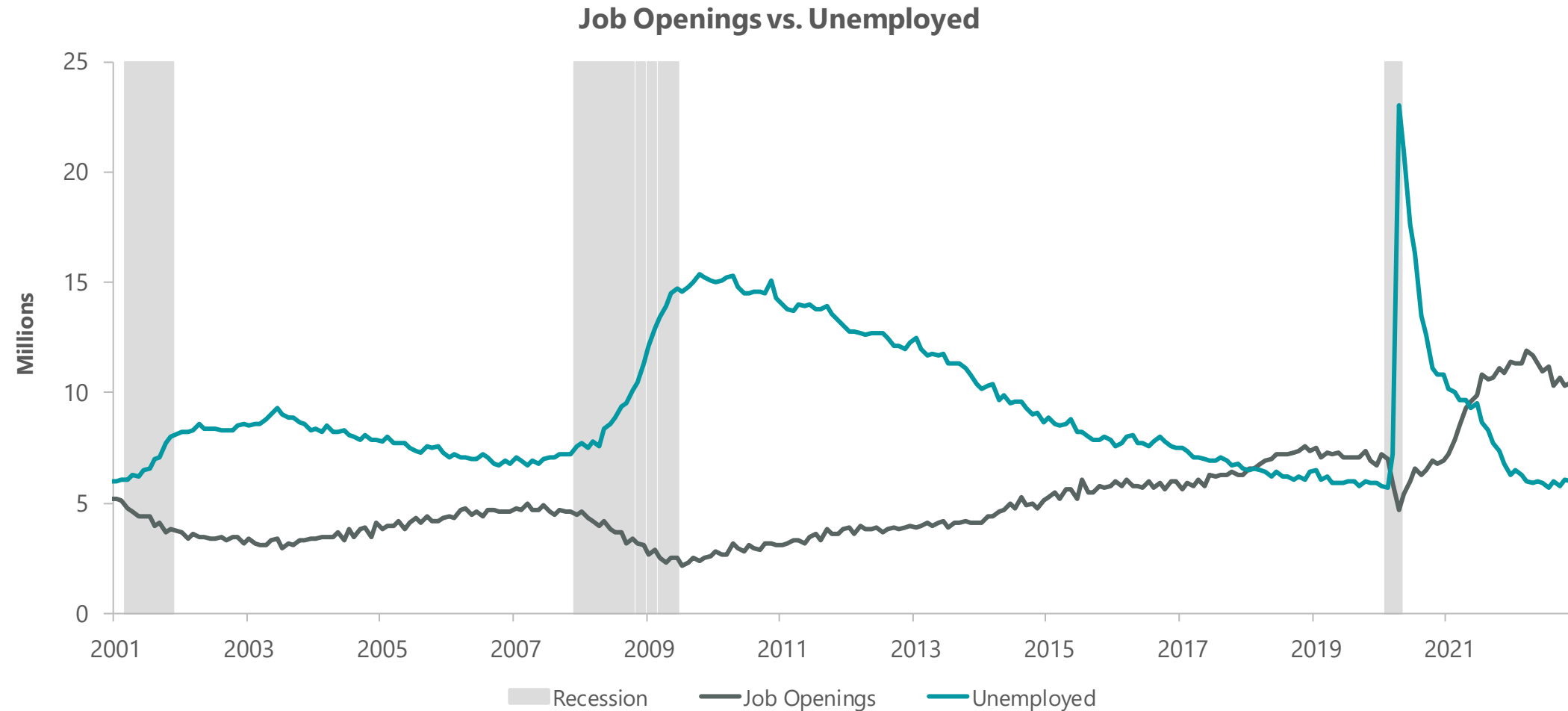
- ▶ **Historical declines in the Leading Economic Indicators lasting more than several months have foreshadowed economic downturns.**
- ▶ **The Leading Economic Indicators have been declining for the last nine months.**

Are Consumers Less Sensitive to Interest Rates?



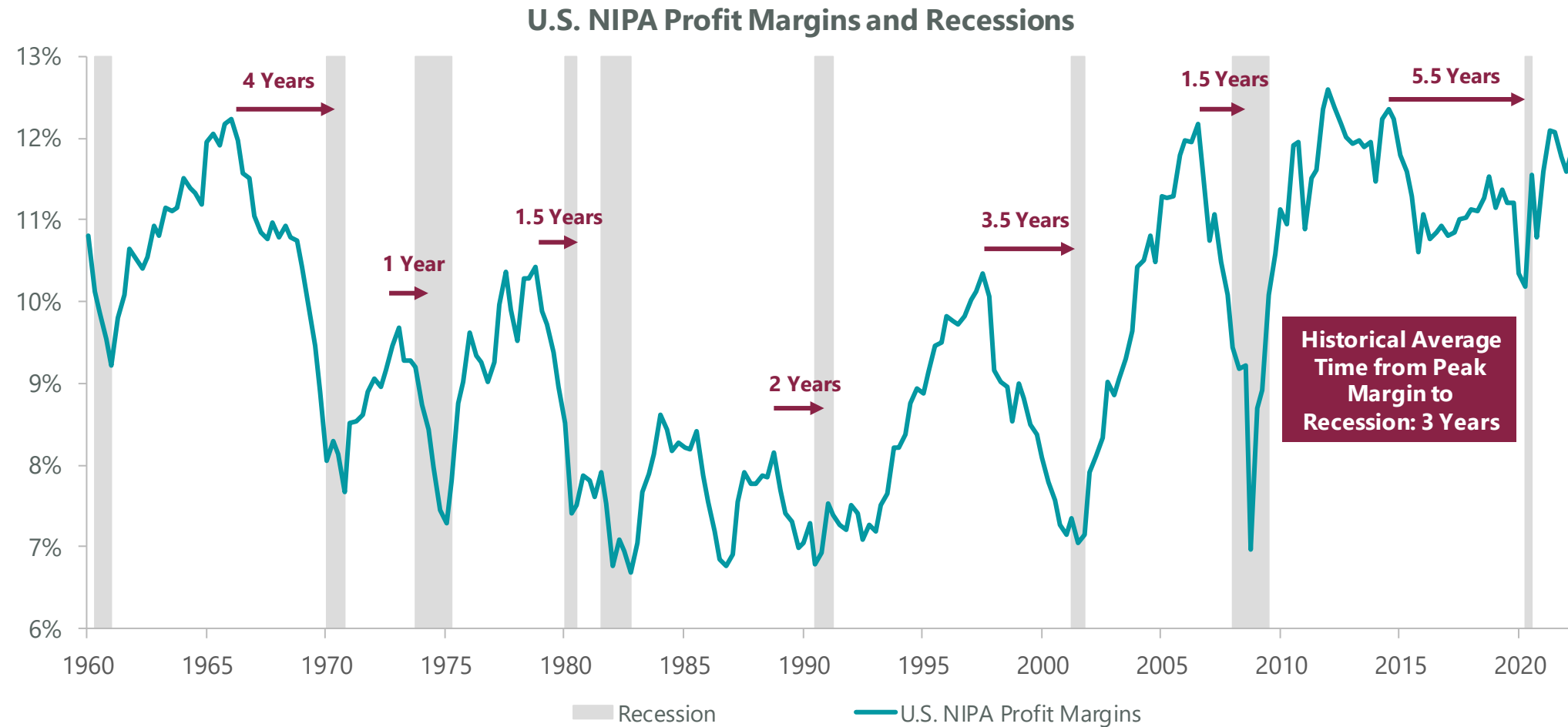
- ▶ **With household leverage near 50-year lows, the impact of higher rates may be blunted.**
- ▶ **The housing market is less sensitive to interest rates relative to history with adjustable-rate mortgages comprising 17% of total today vs. 51% at peak prior to the Global Financial Crisis.**

The Immaculate Slackening



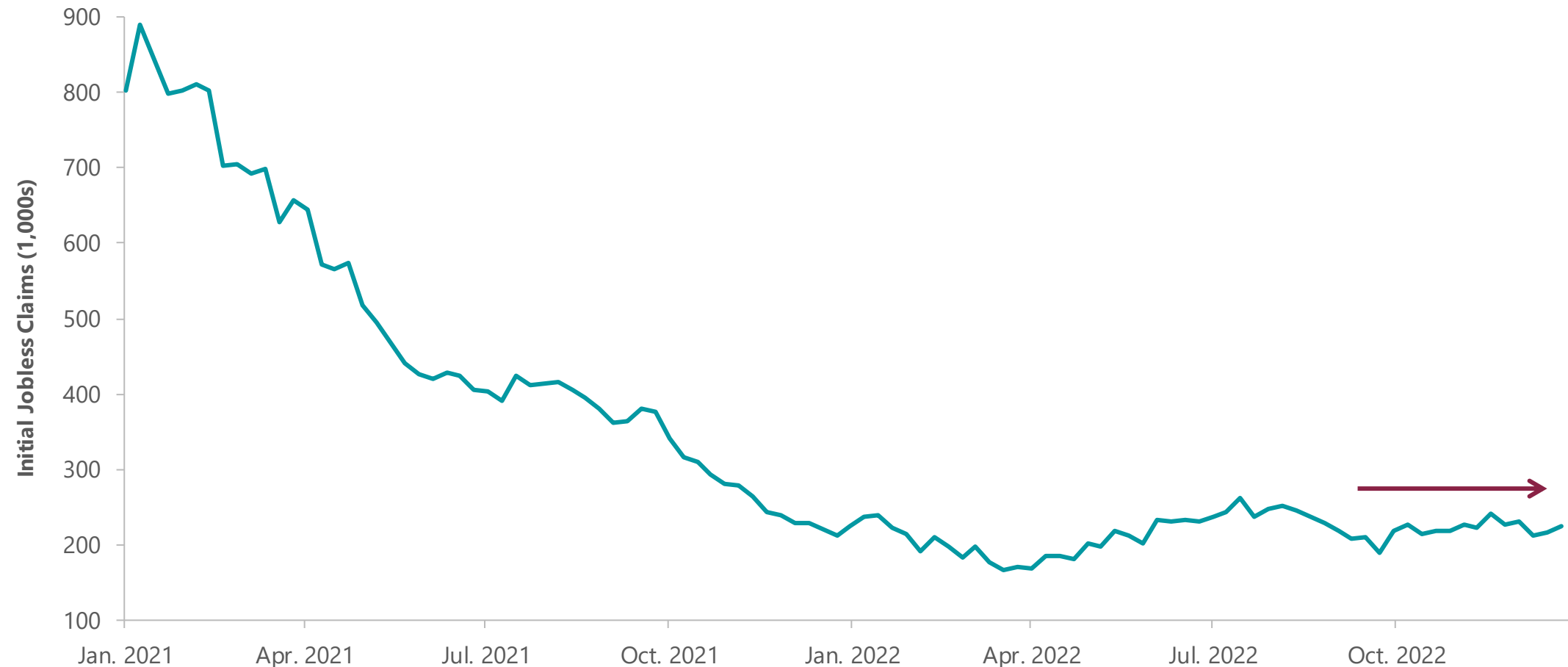
- ▶ **From peak, job openings have dropped by over 1.5 million, re-invigorating hope that the labor market can loosen without a substantial rise in unemployment.**
- ▶ **Historically, the two series have moved opposite to one another, but the current cycle bears little resemblance to history.**

The “Margin” for Error



- ▶ **Profit margins have typically peaked three years ahead of recessions.**
- ▶ **Labor has been the scarcest resource of the recovery, meaning businesses may opt to keep workers on the books with margins still near record levels.**

Canary in the Coal Mine



- ▶ **Following a rise in initial jobless claims from 53-year lows, claims have stabilized which suggests the labor market remains healthy.**
- ▶ **Initial jobless claims have been one of the best high-frequency indicators on the ClearBridge Recession Risk dashboard, making them particularly insightful into the health of this expansion.**

Long and Variable Lags

Start of Persistent* Hike Cycle	Start of Recession	Recession Within 3.5 Years?	Length from Start of Hiking Cycle (Months)
Nov. 1958	April 1960	Yes	17
July 1963	Dec. 1969	No	76
Nov. 1968	Dec. 1969	Yes	12
Jan. 1973	Nov. 1973	Yes	9
Aug. 1977	Jan. 1980	Yes	29
Aug. 1980	July 1981	Yes	11
March 1984	July 1990	No	75
March 1988	July 1990	Yes	27
Feb. 1994	March 2001	No	85
June 1999	March 2001	Yes	20
June 2004	Dec. 2007	Yes	41
Dec. 2016	Feb. 2020	Yes	38
Average for All Hiking Cycles			37
Average in Recessions			23

- ▶ **On average, a recession has historically begun a little over three years once a rate hike cycle gains momentum.**
- ▶ **In hard landing (recession) scenarios, this timeframe is condensed to just under two years.**

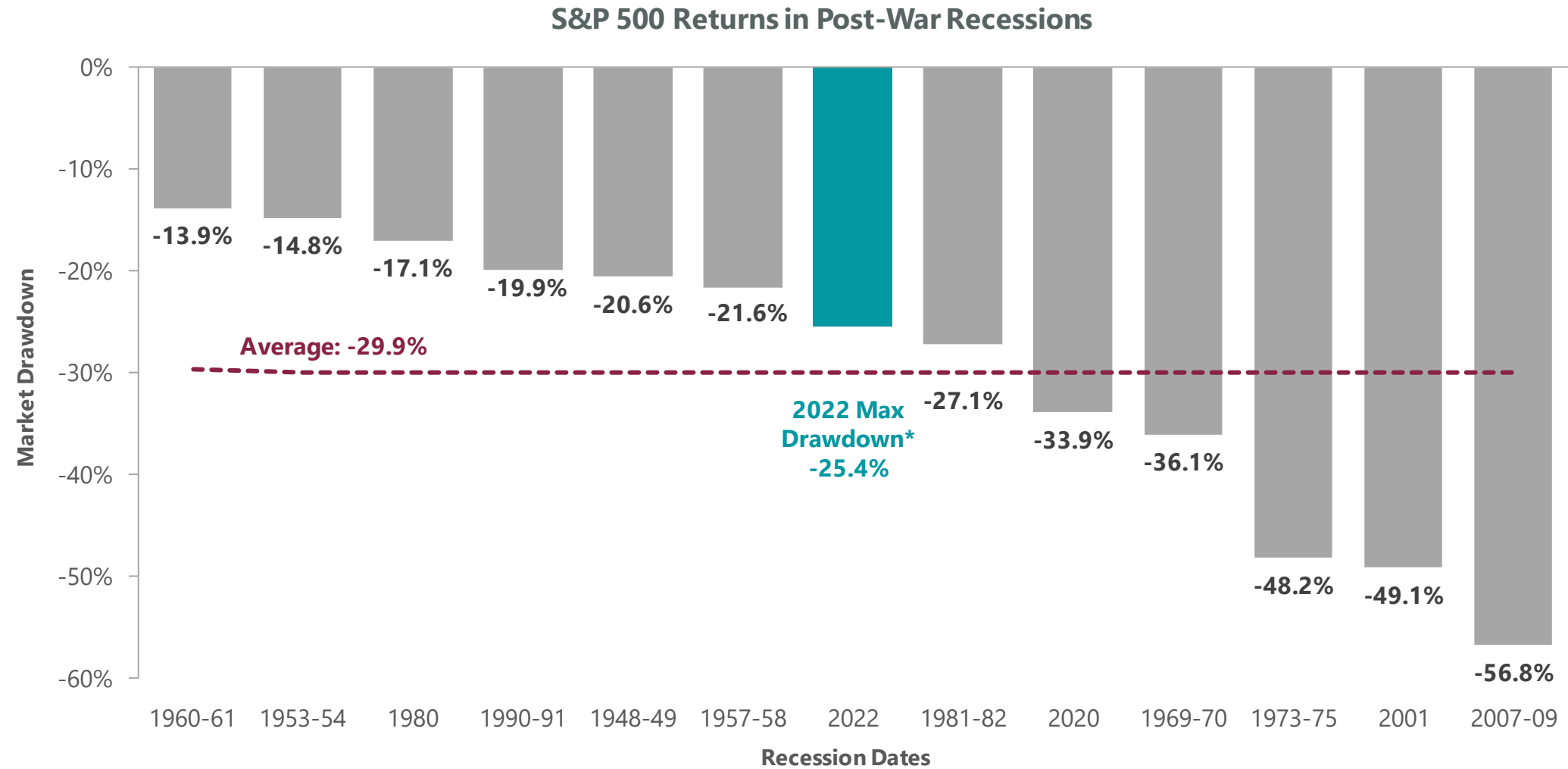
Further Pain Ahead?

Recession Start (Peak)	Recession End (Trough)	Unemployment Cycle Low	Change in Unemployment at Market Trough*	Change in Unemployment Full Cycle
Nov. 1948	Oct. 1949	3.4%	2.8%	4.5%
July 1953	May 1954	2.5%	0.6%	3.6%
Aug. 1957	April 1958	3.7%	1.5%	3.8%
April 1960	Feb. 1961	4.8%	1.3%	2.3%
Dec. 1969	Nov. 1970	3.4%	1.5%	2.7%
Nov. 1973	March 1975	4.6%	1.4%	4.4%
Jan. 1980	July 1980	5.6%	0.7%	2.2%
July 1980	Nov. 1982	7.2%	2.6%	3.6%
July 1990	March 1991	5.0%	0.9%	2.8%
March 2001	Nov. 2001	3.8%	1.9%	2.5%
Dec. 2007	June 2009	4.4%	4.3%	5.6%
Feb. 2020	April 2020	3.5%	0.9%	11.2%
Average			1.7%	4.1%
Current		3.5%	0.2%	???

- ▶ **The unemployment rate has historically risen by 4.1% from trough to peak in periods associated with recessionary cycles.**
- ▶ **Of this move, only 1.7% (~40%) had occurred when the market bottomed on average.**

Market Outlook

Are We There Yet?



▶ **Since World War II, the average recessionary selloff has been -29.9%, a level the current selloff is approaching but has not yet reached.**

Cart Before the Horse?

Recession Start	Recession End	Length (Months)	Market Low During Recession?	Distance from Recession Start (Months)	Distance from Recession End (Months)
Nov. 1948	Oct. 1949	11	Yes	6	-5
July 1953	May 1954	10	Yes	1	-9
Aug. 1957	April 1958	8	Yes	2	-6
April 1960	Feb. 1961	10	Yes	6	-4
Dec. 1969	Nov. 1970	11	Yes	5	-6
Nov. 1973	March 1975	16	Yes	10	-6
Jan. 1980	July 1980	6	Yes	2	-4
July 1981	Nov. 1982	16	Yes	12	-4
July 1990	March 1991	8	Yes	2	-6
March 2001	Nov. 2001	8	No	18	10
Dec. 2007	June 2009	18	Yes	14	-4
Feb. 2020	April 2020	2	Yes	1	-1
Average:		10.3		6.6	-3.8

- ▶ **Historically, market lows have come around the two-thirds mark during recessions.**
- ▶ **The strength of the labor market would suggest this point is not yet on the immediate horizon.**

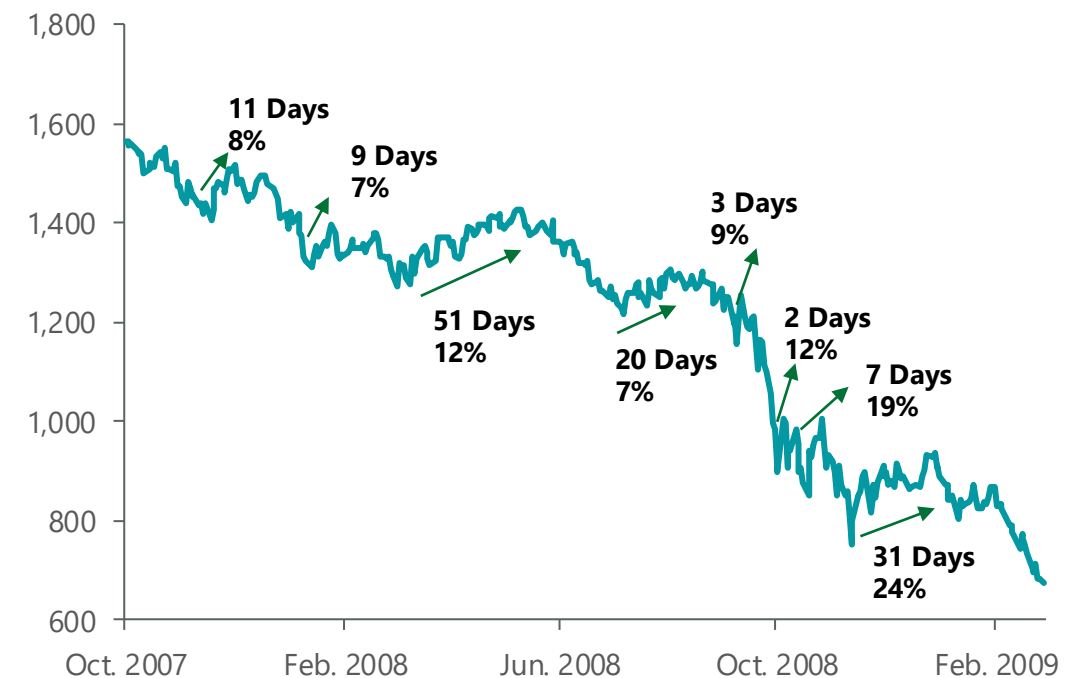
Countertrend Rallies Are Commonplace

Recessionary Bear Markets Often See Pockets of Strength

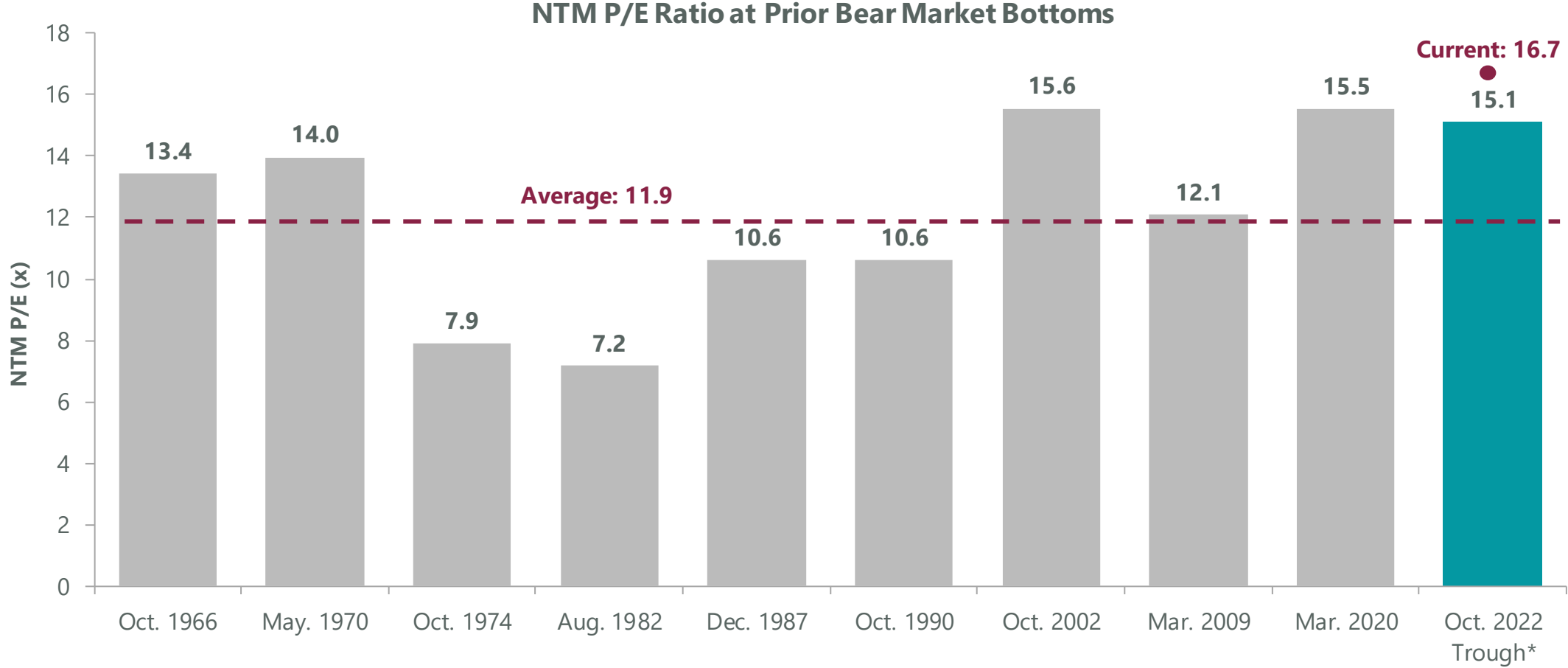
Largest Historical Recessionary Counter Trend Rallies

Recession Start	Recession End	Largest Counter Trend Rally
Dec. 1969	Nov. 1970	6%
Nov. 1973	Mar. 1975	10%
Aug. 1973	Oct. 1973	11%
Jan. 1980	July 1980	4%
Jul. 1981	Nov. 1982	12%
Jul. 1990	Mar. 1991	6%
Mar. 2001	Nov. 2001	19%
Dec. 2007	June 2009	24%
Feb. 2020	Apr. 2020	9%
Average:		11%
Current:		17%

S&P 500 Countertrend Rallies: 2007-2009



Finding Fair Value



- ▶ **Although U.S. equities have derated from greater than 21x, they are still well above the average multiple seen at prior bear market troughs.**
- ▶ **Over the last 20 years, major market lows have tended to occur at loftier valuations (14.4x) relative to history, perhaps a function of lower (discount) rates.**

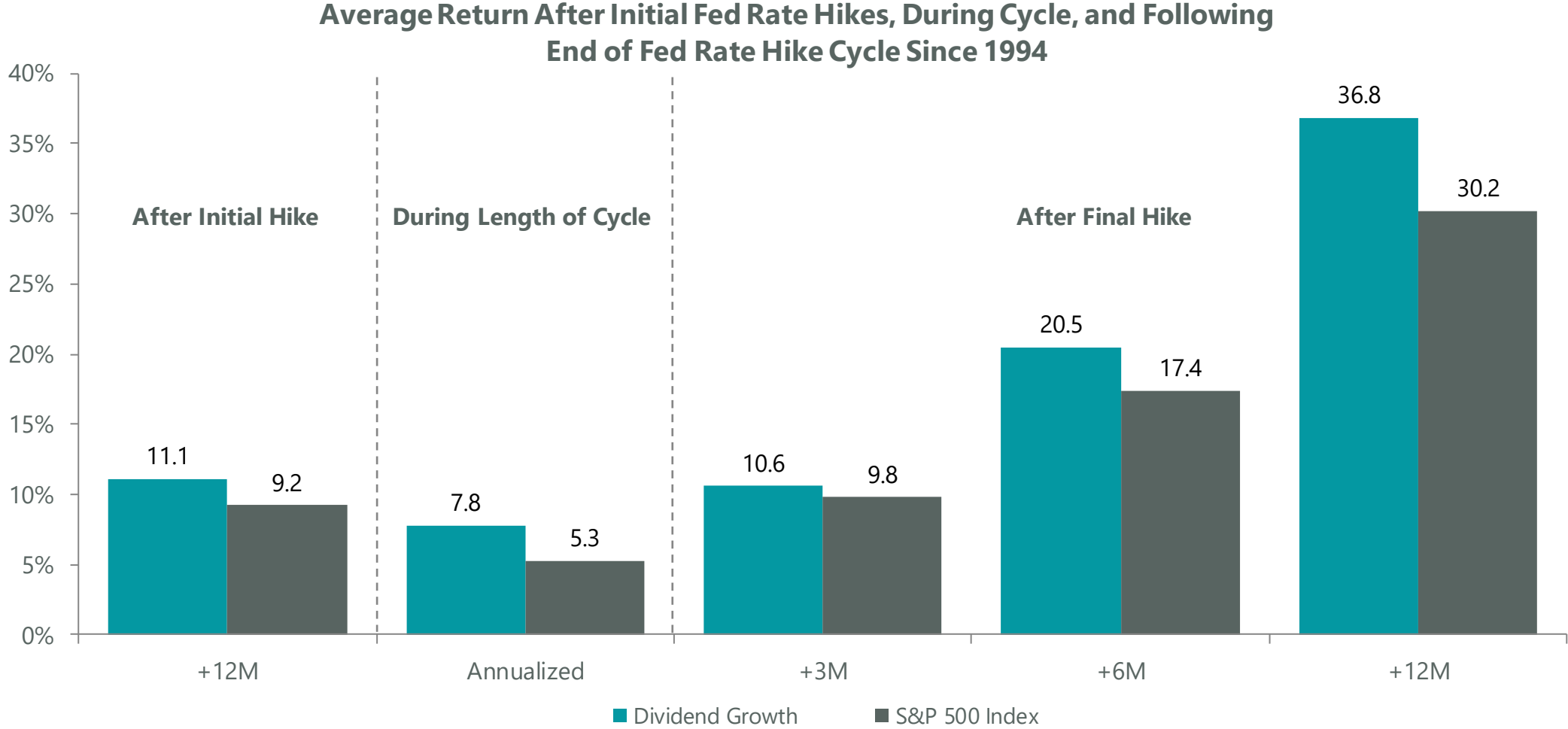
*Trough at Oct. 12, 2022. Note: Chart uses monthly NTM P/E ratios on the S&P 500 Index since 1964. Data as Dec. 31, 2022. Source: Federal Reserve, Standard & Poor's, FactSet, Credit Suisse. Past performance is not a guarantee of future results. Investors cannot invest directly in an index, and unmanaged index returns do not reflect any fees, expenses or sales charges.

What's the Path for Earnings?

NTM EPS Behavior							
Market Peak	EPS Peak	# of Days	Market Trough	EPS Trough	# of Days	EPS Peak – Trough	Market Peak – Trough
Recessions							
3/24/2000	8/7/2000	136	10/9/2002	12/17/2001	-296	-17.5%	-49.1%
10/9/2007	11/1/2007	23	3/9/2009	5/8/2009	60	-39.3%	-56.8%
2/19/2020	1/30/2020	-20	3/23/2020	5/15/2020	53	-20.6%	-33.9%
Average GDP Recession:		46			-61	-25.8%	-46.6%
Non-Recessionary EPS Declines							
7/17/1998	9/29/1998	74	8/31/1998	1/4/1999	126	-2.6%	-19.3%
5/21/2014	10/7/2014	139	8/25/2015	2/6/2015	-200	-5.5%	-7.2%
11/3/2015	9/8/2015	-56	2/1/2016	3/1/2016	29	-3.2%	-13.3%
9/20/2018	12/6/2018	77	12/24/2018	2/1/2019	39	-2.3%	-19.8%
Average GDP Recession:		59			-2	-3.4%	-14.9%
Current*							
1/3/2022	7/8/2022	186	10/12/2022	12/21/2022	70	-4.1%	-25.4%

- ▶ **Earnings revisions have declined by -26% on average across the last three recessions.**
- ▶ **It is not uncommon for earnings estimates to bottom after market lows have occurred. Earnings estimates have only recently started to come down.**

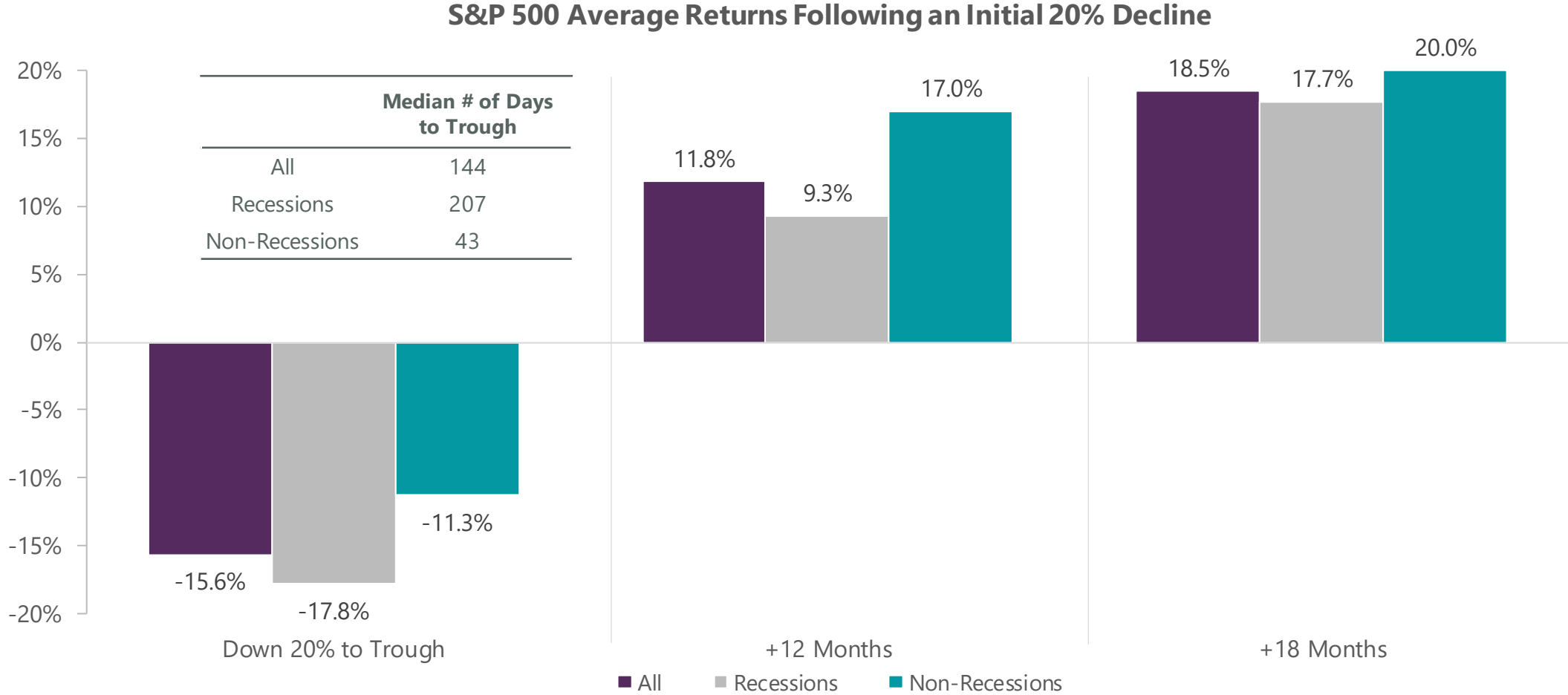
Dividend Growers Have Historically Dominated



▶ **Dividend growth has historically been a desirable trait for equities during and after Fed hiking cycles.**

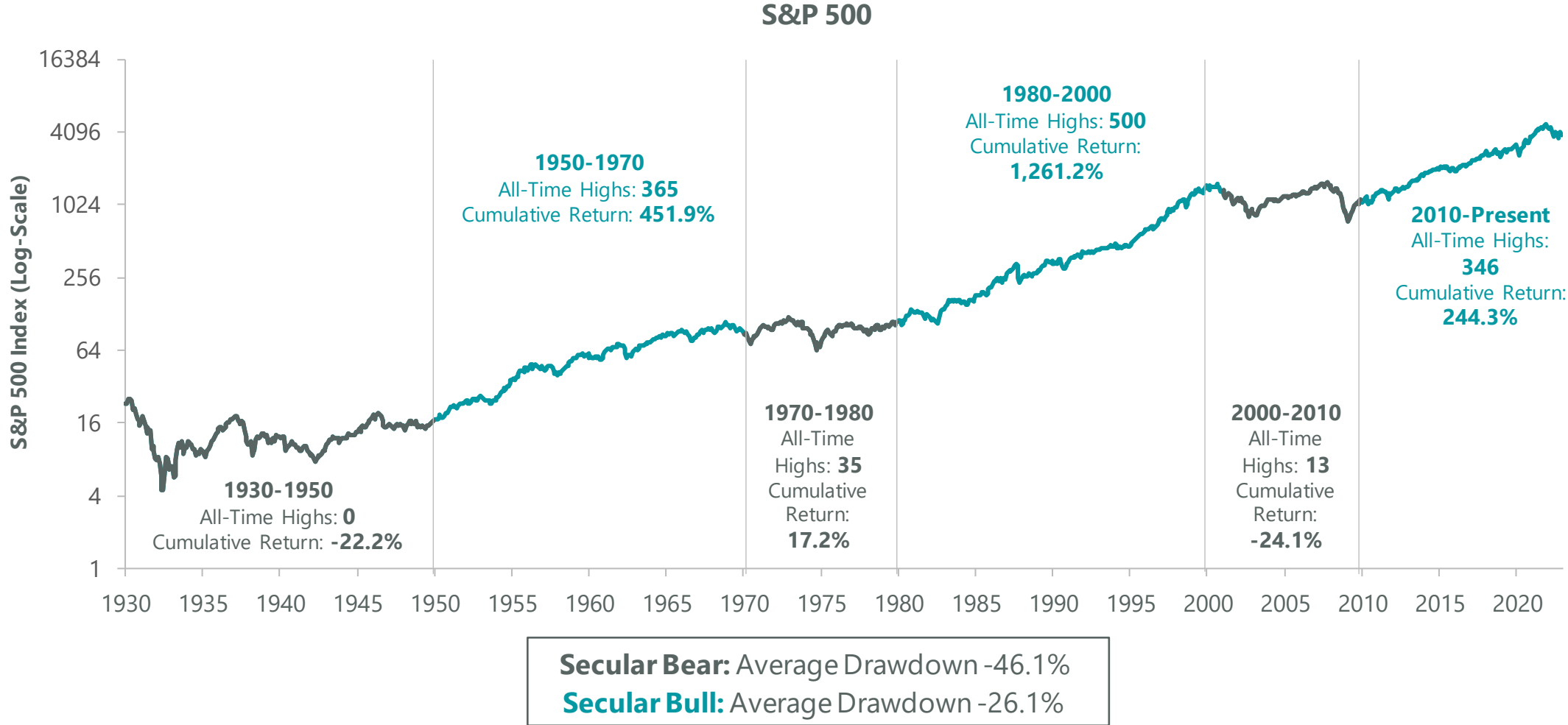
Source: BMO Capital Markets Investment Strategy Group, FactSet, Compustat, FRB. Dividend Growth Screening Methodology: S&P 500 stocks screened each month end, no dividend cuts in the past five years, latest one-year dividend per share growth greater than the S&P 500, current dividend yield greater than the S&P 500, free cash flow yield greater than the dividend yield, dividend payout ratio lower than the S&P 500. 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.

Bear Market Achieved, Good Entry Point?



- ▶ **Once a bear market (-20%) has occurred, markets typically continue to sell off with recessions experiencing larger drawdowns than non-recessions.**
- ▶ **However, patient investors have historically been rewarded for staying the course over the following year.**

New Secular Bull Market?



► **In the 12 months following an all-time high, stocks have historically been up 8.3% on average with positive returns 70% of the time.**

Economic and Market Summary

First Quarter 2023

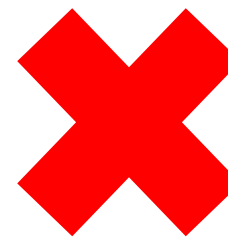
U.S. Economic Outlook

- U.S. recession risks remain elevated with the overall signal continuing to flash red.
- The lagged effects of Fed tightening could continue to weigh on an already slowing growth backdrop in 2023.
- The narrow path for a soft landing relies on a resilient consumer, and/or corporate reluctance to invoke a full scale layoff cycle.

U.S. Market Outlook

- While negative returns in 2022 were primarily driven by multiple contraction, downside to earnings expectations appears to be the primary risk in the coming year.
- We continue to believe that markets will experience heightened volatility until visibility is restored regarding the path forward for the economy and earnings.
- Historically, bear markets are rare and typically provide good opportunities for long term investors.

Recession Dashboard Overall Signal



Recession

Glossary of Terms

BEA: Bureau of Economic Analysis

Black Swan: An unlikely and unpredictable event with potentially extreme consequences for markets.

Bloomberg Barclays US Aggregate Bond Index: an unmanaged index of U.S. investment-grade fixed-income securities.

Bloomberg Barclays US Corporate Investment Grade Bond Index: an unmanaged index of U.S. investment-grade corporate bond securities.

Capex (Capital expenditures): corporate spending on productive assets (such as buildings, machinery and equipment, vehicles) intended to increase capacity or efficiency for more than one accounting period.

CPI (Consumer Price Index): measure of the average change in U.S. consumer prices over time in a fixed market basket of goods and services as determined by U.S. Bureau of Labor Statistics.

EPS (Earnings per Share): the portion of a company's profit allocated to each outstanding share of common stock.

FAANGM: Shorthand term for a group of leading technology stocks including Facebook, Apple, Amazon, Netflix, Google/Alphabet, and Microsoft.

GDP: Gross Domestic Product

GFC (Great Financial Crisis): the severe economic and market downturn experienced in 2007-2008.

Fed (Federal Reserve Board): the U.S. central bank, responsible for policies designed to promote full economic growth, full employment, and price stability.

LEI Index: Conference Board Leading Economic Indicators index.

Mortgage Bankers Association (MBA) Purchase Index: measure of relative change over time in mortgage applications for property purchases

MSCI All Country World Index: unmanaged index of large- and mid-cap stocks in developed and emerging markets.

MSCI EM Index: unmanaged index of large- and mid-cap stocks in 27 emerging market countries.

MSCI EAFE Index: unmanaged index of equity securities from developed countries in Western Europe, the Far East, and Australasia.

MSCI USA Index: unmanaged index of US large- and mid-cap equity securities.

NAREIT All-Equity REITS Total Return Index: free-float-adjusted market capitalization weighted index that includes all tax qualified REITS listed in the NYSE, AMEX and NASDAQ National Markets.

NFIB (National Federation of Independent Business): a U.S. small business advocacy association, representing over 350,000 small and independent business owners.

NFIB Small Business Optimism Index: measure of small business sentiment produced by the National Federation of Independent Business based on its monthly survey of small business owners.

Owners Equivalent Rent: the amount of rent that would have to be paid in order to substitute a currently owned house as a rental property.

PMI: Purchasing Manager's Index

Glossary of Terms

P/E Ratio: Price/Earnings ratio

Quantitative easing (QE): Monetary policy implemented by a central bank in which it increases the excess reserves of the banking system through the direct purchase of debt securities.

Russell 1000 Growth Index: unmanaged index of large-cap stocks chosen for their growth orientation.

Russell 1000 Value Index: unmanaged index of large-cap stocks chosen for their value orientation.

Russell 2000 Index: unmanaged index of small-cap stocks.

Shibor: Shanghai Interbank Offered Rate

S&P MidCap 400 Index: unmanaged index of 400 US mid-cap stocks

S&P 400 Growth Index: unmanaged index of mid-cap stocks having higher price-to-book ratios relative to the S&P 400 MidCap as a whole.

S&P 400 Value Index: unmanaged index of mid-cap stocks having lower price-to-book ratios relative to the S&P 400 MidCap as a whole.

S&P 500 Growth Index: unmanaged index of large-cap stocks selected based on sales growth, the ratio of earnings change to price and momentum.

S&P 500 Value Index: unmanaged index large-cap stocks selected based on the ratios of book value, earnings, and sales to price.

S&P 600 Index: unmanaged index of 600 US small-cap stocks

S&P 600 Growth Index: unmanaged index of US small-cap growth stocks, selected based on sales growth, the ratio of earnings change to price, and momentum.

S&P 600 Value Index: unmanaged index of US small-cap value stocks, selected based on ratios of book value, earnings, and sales to price.

S&P 500 Index: Unmanaged index of 500 stocks that is generally representative of the performance of larger companies in the U.S.



VIX: VIX is the ticker symbol and the popular name for the Chicago Board Options Exchange's CBOE Volatility Index, a popular measure of the stock market's expectation of volatility based on S&P 500 index options.

Yield Curve: Comparison of interest rates at a point in time of bonds with equal credit quality but different maturity dates.

YoY: Year Over Year

U.S. Treasurys: Direct debt obligations issued and backed by the "full faith and credit" of the U.S. government. The U.S. government guarantees the principal and interest payments on U.S. Treasuries when the securities are held to maturity. Unlike U.S. Treasury securities, debt securities issued by the federal agencies and instrumentalities and related investments may or may not be backed by the full faith and credit of the U.S. government. Even when the U.S. government guarantees principal and interest payments on securities, this guarantee does not apply to losses resulting from declines in the market value of these securities.

Biographies

Name and Position	Industry Experience	ClearBridge Tenure	Education, Experience and Professional Designations
 <p>Josh Jamner CFA Vice President, Investment Strategy Analyst</p>	13 years	<ul style="list-style-type: none">• Joined ClearBridge in 2017	<ul style="list-style-type: none">• Member of the CFA Institute• RBC Capital Markets - Assistant Vice President, Associate Strategist - U.S. Equity• Bessemer Trust - Assistant Vice President, Client Portfolio Analyst• BA in Government from Colby College
 <p>Jeffrey Schulze CFA Director, Investment Strategist</p>	17 years	<ul style="list-style-type: none">• Joined ClearBridge in 2014	<ul style="list-style-type: none">• Member of the CFA Institute• Lord Abbett & Co., LLC – Portfolio Specialist• BS in Finance from Rutgers University

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