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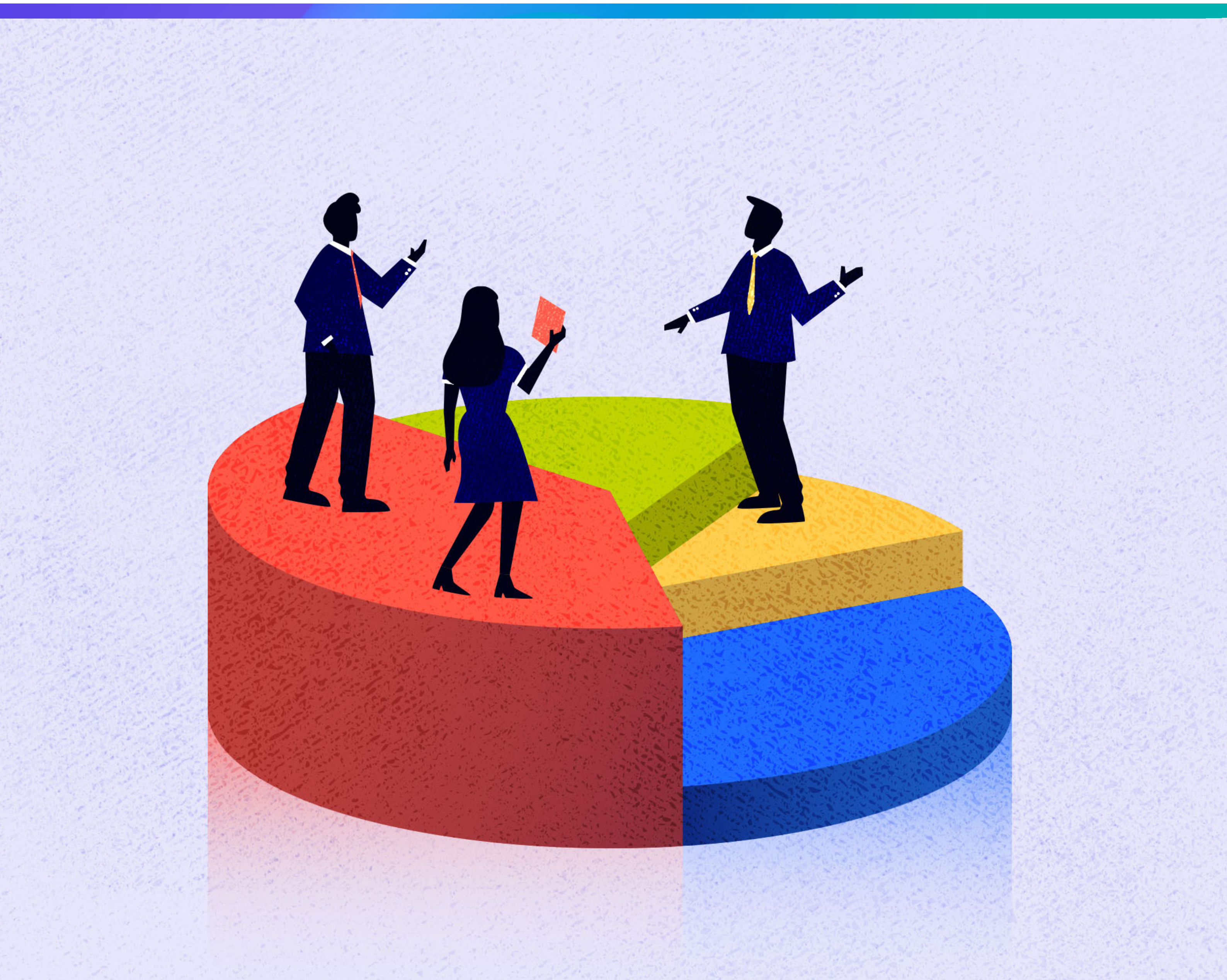
Institute | Global Investment Outlook

Franklin Templeton Thinks™

July 2022

Midyear outlook: Income arrives in many shapes and sizes



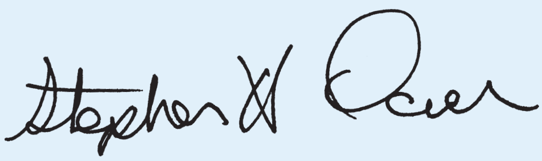
Introduction

Stephen Dover, CFA
Chief Market Strategist
Franklin Templeton Institute

The first half of 2022 has been challenging for investors across asset classes, and the uncertainties plaguing markets remain—particularly with regard to inflation, interest rates and the possibility of recession. As we look toward the second half of the year, our investment management teams gathered to discuss where income-seeking investors may find opportunities. Below are highlights of our discussions.

- "This volatile environment has also uncovered opportunities. One of these opportunities is in higher-quality fixed income securities, particularly those with longer duration or more exposure to interest-rate increases. We've seen historic selloffs in bond prices, and the yields that investors can buy into now are significantly higher than they were just six to nine months ago."
  Ed Perks, Franklin Templeton Investment Solutions
- "Opportunities exist in the corporate credit space with companies that have pricing power given the inflationary backdrop. We think staying higher in credit quality is sensible given where we are in the cycle and economic headwinds."
  Brian Giuliano, Brandywine Global
- "Bank loans—also known as leveraged, floating-rate or senior secured loans—tend to act as a good hedge against interest-rate risk."
  Reema Agarwal, Franklin Templeton Fixed Income
- "Dividend growth is great in regular periods, but critical during inflationary periods. As inflation erodes the value of a dollar, growing dividends help to maintain purchasing power despite the increasing cost of living."
  Michael Clarfeld, ClearBridge Dividend Strategy
- "In some ways, managing to income is part of managing volatility. Companies that have more predictable cash flows and more resilient dividends are likely to be less volatile. The key is to invest in high-quality, blue-chip companies, which allow for better dividend growth and stronger dividend resilience during difficult times."
  Matt Quinlan, Franklin Equity Group
- "Infrastructure assets act as an inflation hedge due to the largely pre-programmed way—through regulation and contracts—infrastructure adjusts to inflationary environments."
  Shane Hurst, ClearBridge Investments
- "Historical precedence suggests that private real estate can effectively hedge inflation as a steady income-producing asset. The industrial and multifamily segments merit particular attention now."
  Clarion Partners

Read on for our midyear Global Investment Outlook. We hope it inspires you to think strategically as we navigate the rest of the year.



Casting a wide net for income

The financial landscape is changing dramatically. Inflation is at levels not seen in four decades, pandemic-driven supply and demand imbalances continue to batter global economies, and the Ukrainian war threatens geopolitical stability. Furthermore, central bank policymakers around the world—including the US Federal Reserve (Fed)—have taken a decidedly hawkish turn in their rhetoric and actions as they aim to dampen worrisome inflation. The Fed delivered a surprise 75 basis-point hike in June, and expectations of future rate increases have shifted up sharply, sparking worries about a potential recession.

"The first half of 2022 has created another challenge as equities and fixed income have both shown similar downside volatility in lockstep with each other. Income-focused investors must be active and nimble against this shifting backdrop, casting a wider net as rising interest rates have led to a reduction in principal value of fixed income and equities."

The first half of 2022 has created another challenge as equities and fixed income have both shown similar downside volatility in lockstep with each other. Income-focused investors must be active and nimble against this shifting backdrop, casting a wider net as rising interest rates have led to a reduction in the principal value of fixed income and equities. We believe the addition of alternative assets such as real estate and infrastructure to a portfolio can offer both a less correlated source of yield, while diversifying to better protect principal. If investors held any excess cash, this provided protection from the volatility of other assets and now provides liquidity to invest in income-producing assets at more attractive values and higher yields. It is a balance of accepting reasonable levels of risk to enhance the yield of their portfolios, while diversifying income sources to protect principal. Our independent investment managers have differing views on the best way to approach income investing in this environment.

Volatility provides opportunities for income investors

Ed Perks, manager of multi-asset income strategies, focuses on two challenges: the rise in interest rates and the broad-based selloff across all assets. Ed thinks investors should be cognizant about diversifying their sources of income to manage for these risks. This volatile environment has also uncovered opportunities. One of these opportunities is in higher-quality fixed income securities, particularly those with longer duration or more exposure to interest-rate increases. The yields that investors can buy into now are significantly higher than they were just a few months ago.

Don't reach for yield

Brian Giuliano from Brandywine Global offers a different view that although investors may be inclined to reach for yield to earn income, he thinks that's a mistake. With little margin of safety relative to valuation and macro conditions, reaching for yield requires taking on too much risk.

Brian thinks opportunities exist in the corporate credit space with companies that have pricing power given the inflationary backdrop. If market conditions continue to deteriorate, increasing exposure to high-quality government bonds would be wise and could offer return potential through appreciation if yields fall in reaction to a slowing economy, as well as a source of uncorrelated return relative to credit assets and equities.

Floating-rate loans can provide shelter from rising interest rates

Reema Agarwal from the Franklin Templeton Fixed Income team highlights that bank loans—also known as leveraged, floating-rate or senior secured loans—tend to act as a good hedge against rising interest rates given their higher nominal yields, lower duration and relatively lower volatility. Floating-rate loans do have credit risk. In the current environment, loan selection remains critical and investors should focus on stable, income-generating, higher credit quality investments, rather than on more deeply discounted, lower credit quality loan issuers that may offer attractive yields, but also carry outsized credit risk amid uncertain macroeconomic conditions.

Dividend stocks and hybrids can be key sources of yield

Accepting some equity risk in the form of dividend-paying stocks may be attractive to enhance portfolio yield and protect against rising inflation. Michael Clarfeld from ClearBridge Investments and Matt Quinlan of Franklin Equity Group share their views on using effective dividend strategies to mitigate market volatility and hedge against inflation.

Of note, income gains from dividends that are reinvested are a significant contributor to total return over the long-term. Over the last 31 years, spanning January 1990 through June 2022, the compounding effect of reinvesting dividends accounted for close to 50% of the cumulative total return of the S&P 500 index (Exhibit 1).

There is also an opportunity to utilize the liquidity created by this income to re-allocate assets in volatile markets. This is an often-overlooked source of total return, as the income can be reinvested to optimize longer-term outcomes. In other words, when the market environment provides valuation opportunities due to temporary dislocations, dividends provide investors with additional capital to rebalance toward strategic asset allocations.

Real estate as an inflation hedge

Some income investors may consider turning to traditionally private markets in search of yield. For example, commercial real estate (multi-family, industrial, office, retail, life sciences and warehousing) has become more accessible to retail investors as an instrument for portfolio diversification and income generation.

Moreover, commercial real estate has historically acted as a hedge against inflation. As the team at Clarion Partners discusses, multi-family housing illustrates this as landlords generally can adjust rents more quickly (typically on an annual basis) during an economic expansion. For perspective, according to the CBRE, as of the fourth quarter last year, multi-family rents grew by 13.4% in 2021, much faster than US headline consumer price inflation of about 7.0% in the same year.

Infrastructure provides another option

Shane Hurst at ClearBridge reminds us that current income is important, but yield quality is also critical. As the economy re-thinks globalization, it will need to invest in infrastructure, further supporting high visibility and predictability of earnings for assets such as toll roads, utilities and mid-stream energy infrastructure. These "user-pays" assets could benefit from continuing economic reopening and could dampen the effects of an otherwise slowing economy. There are idiosyncrasies that make this cycle unique and encourage differentiating between companies. We also expect the difference between real and nominal interest rates will require dynamic positioning, for example allocating between the United States and Europe.

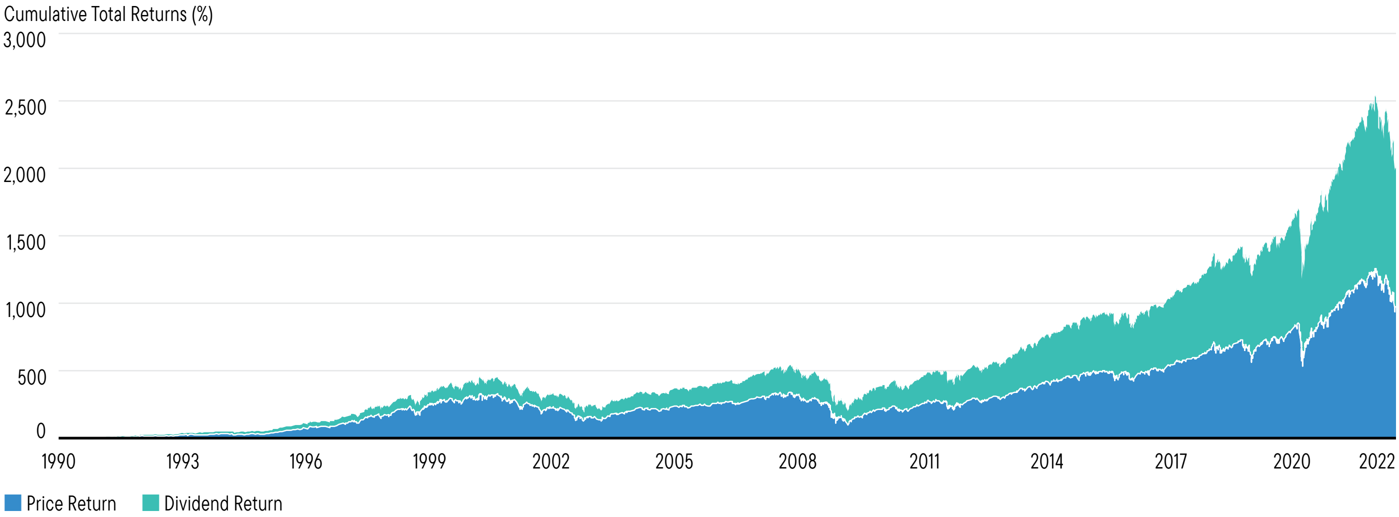
Recognizing income in all its forms

Ideally, being able to look at income opportunities across all asset classes widens the toolkit and should enhance diversification of income sources and improve portfolio yield. This is not a passive activity. We believe active management is key to continually uncover opportunities and build a resilient income portfolio.

Dividends Can Drive Returns: Receipt and Reinvestment of Dividends Account for about 50% of Total Return Over the Long-term

Exhibit 1: Total Return Composition of the S&P 500 Index

As of June 30, 2022



Source: Bloomberg, Past performance is not indicative of future performance.

Multi-asset focus: The volatile markets have created many opportunities to find income across asset classes

Being able to pull many levers—from duration to equities to alternatives (that behave differently than stocks or bonds)—presents opportunities. These opportunities may lead to a steady flow of income when skillfully navigated.

Risks present opportunities

Ed Perks, CFA
Chief Investment Officer
Franklin Templeton Investment Solutions

We need to consider both the challenges and the opportunities of income investing. In today's difficult market environments investors tend to just focus on the risks, but there is an upside to the volatility as well.

First, let's consider two main challenges. The first is interest-rate risk. When the year began, many investors were simply thinking about equity risk, and to some extent credit risk. Interest-rate risk as a topic of concern was largely nonexistent. This is because central banks across the globe have kept interest rates near zero for the better part of a decade. Naturally, markets had become accustomed to extremely loose monetary policy and quantitative easing. Interest-rate risk seemed irrelevant. Of course, the landscape has changed over the last six months. Central banks are not just needing to normalize interest rates, they have been forced to act aggressively to tamp down runaway inflation at levels not seen since the 1970s. So, today interest-rate risk is of major concern to investors.

> **"...this volatile environment has also uncovered opportunities. One of these opportunities is in higher-quality fixed income securities, particularly those with longer duration or more exposure to interest-rate increases. We've seen historic selloffs in bond prices, and the yields that investors can buy into now are significantly higher than they were just six to nine months ago."**

Second, we have witnessed a broad-based selloff across all assets. We have seen major declines in risk assets like equities and corporate debt, as well as in traditional safe-haven assets like US Treasuries. As such, investors have had to be cognizant about diversifying their sources of income to manage for these risks.

Now on the positive side, this volatile environment has also uncovered opportunities. One of these opportunities is in higher-quality fixed income securities, particularly those with longer duration or more exposure to interest-rate increases. We've seen historic selloffs in bond prices, and the yields that investors can buy into now are significantly higher than they were just six to nine months ago.

For example, two-year US Treasury yields have risen from 0.6% on December 31, 2021, to 3.4% today, and high-yield debt indexes have seen yields rise from around 4% to almost 9% over the same period. This movement allows investors who are looking for short duration, low-risk assets as well as more enterprising investors looking for higher income (high yield) to achieve income goals regardless of their risk tolerance. Similarly, with the decline in equities, investors can find bargains, allowing them to selectively position and broaden their opportunity set. We think the current environment offers income-seeking investors a lot of potential opportunities. In addition, the market seems to be pricing in a very high probability of both elevated inflation and slower growth, creating opportunities if the macroeconomic outcome is not as extreme as anticipated.

Fixed income focus: Higher interest rates provide opportunity

As central banks embark on aggressive policy tightening measures, opportunities in shorter duration are emerging in floating-rate debt. However, investors need to use caution when thinking about reaching for yield. Despite rising rates, in some instances valuations are only marginally compelling, and perhaps not worth the risk.

Capturing income with safety in mind

Brian Giuliano, CFA
Client Portfolio Manager
Brandywine Global

Investors seeking income should actively adapt income and risk exposures to changing market conditions. It is important not to just reach for yield. A myopic focus on income can lead investors to take on too much risk—heightened volatility, increased drawdowns, higher correlations to equities, and less liquidity.

It's important to cast the net broadly to a range of market segments or sectors, in my view.

Income will always be an important source of return in a fixed income portfolio, but it's not the only return driver. Capital appreciation through sector rotation, duration management, quality rotation and security selection can be important sources of return, complementing income generation.

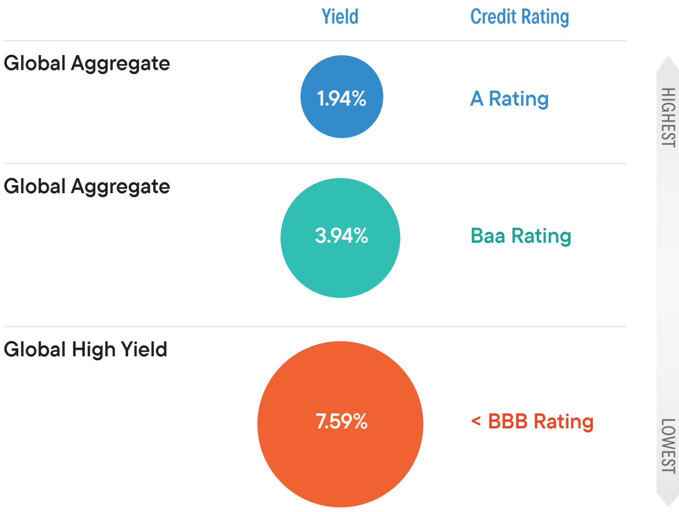
Don't reach for yield blindly

We anticipate market volatility will remain elevated as yields are rising globally. This landscape may present opportunities to take advantage of valuations at good entry points as the macro backdrop stabilizes. Challenges exist from both a valuation and macro standpoint. Thanks to a rising rate environment, fixed income has income again, but overall valuations (i.e., yield level and spreads) are only marginally compelling. Given the environment (still relatively low levels of yield), investors may be inclined to reach for yield to earn income. We think that's a mistake. With little margin of safety relative to valuation and macro conditions, we think reaching for yield would require taking on too much risk (Exhibit 2).

Adding Credit Risk Increases Default and Loss Possibilities

Exhibit 2: Yield by Credit Quality for Select Fixed Income Indexes

As of May 31, 2022



Sources: Morningstar, Bloomberg Barclays Indices, Credit Suisse, Macrobond. Global high yield represented by Bloomberg Barclays Global High Yield Index and global aggregate represented by Bloomberg Barclays Global Aggregate Index. 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 or a guarantee of future results.**

Opportunities exist in the corporate credit space with companies that have pricing power given the inflationary backdrop. We think staying higher in credit quality is sensible, too, given where we are in the cycle and economic headwinds. Tactically, if market conditions continue to deteriorate, increasing exposure to high-quality government bonds would be wise, in our view. Although those securities don't offer as compelling a yield as other segments of fixed income, they do offer two things: return potential through appreciation if yields fall in reaction to a slowing economy, as well as a source of uncorrelated return relative to the credit assets noted previously.

Bank loans: Turning the Fed's lemons into lemonade

Reema Agarwal, CFA
Portfolio Manager
Franklin Templeton Fixed Income

It's clear interest rates are marching higher in the foreseeable future. However, the pace and scale of such policy moves remain uncertain. Higher-than-expected inflation data continue to stoke concerns about potentially more aggressive central bank action as policymakers grow increasingly uneasy about the persistence of high inflation.

The prospect of higher interest rates is not necessarily bad news for financial markets. Strong growth and robust macro fundamentals underscore the need to withdraw policy stimulus. In addition, policy rates are only starting to climb from crisis era lows and have not reached levels that could meaningfully constrain economic activity.

Bank loans—also known as leveraged, floating-rate or senior secured loans—tend to act as a good hedge against interest-rate risk. These instruments have already attracted significant retail and institutional investor interest amid the rapid rise in the 10-year US Treasury yield.

Riding the wave of higher interest rates

Looking ahead, the outlook for bank loans remains constructive, with rising interest-rate expectations and supportive demand conditions providing modest tailwinds. Aided by their floating-rate structure and short-duration trait, bank loans look attractive to us relative to traditional fixed income assets in a rising interest-rate environment.

Nevertheless, proactive portfolio management, heightened selectivity and enhanced scrutiny on provisions are increasingly important when investing in bank loans. There are risks in credit. Broader market conditions such as the after-effects of COVID-19, supply and demand constraints due to the ongoing lockdowns in China, issues related to the Russia-Ukraine war, as well as the Fed tightening cycle, are impacting certain issuer fundamentals. Issuers at the lower end of the credit quality spectrum are faced with high inflation in raw materials or labor, which they are unable to pass through to customers or offset. As a result, we believe loan selection remains critical and requires focus on stable, income-generating investments, rather than more deeply discounted, lower-rated loan issuers.

Equity focus: Mitigating market volatility and hedging against inflation with dividends

While bonds generally offer fixed coupons, dividends have the potential to provide a steady and rising cash flow stream over time. Dividends are a fundamental tool in managing for income during both normal economic periods and especially during inflationary periods. Growing dividends help to maintain purchasing power despite increased living expenses. Dividends reinvested also help to smooth returns over time.

High-quality dividend payers can rebut inflation pressures

Michael Clarfeld, CFA

Portfolio Manager

ClearBridge Dividend Strategy

The year began with an expensive market and high inflation: tumbling stock prices have not been much of a surprise. Against this backdrop, high-quality dividend payers have shined as their three key attributes—downside protection, current income and dividend growth—have proved critical.

When selling pressure becomes self-fulfilling and buyers go on strike, dividends can break the feedback loop. A healthy dividend yield provides a cash flow-based guidepost for valuing securities, which can help investors look past current volatility to step in and buy. In short: robust dividends provide support to stock prices in weaker periods.

Bear markets remind us that dividends—albeit prosaic—are responsible for 40% of total return over the long term. In flat-to-down markets, meanwhile, dividends provide a cash flow return to investors that can offset share price stagnation or depreciation. As markets improve, dividends and dividend increases are an excellent reflection of underlying earnings growth, and these follow each other over time.

Total return may best be viewed as the combination of price appreciation and income or dividends received over a period of ownership. We look for attractive upfront yield, but, importantly from a total return perspective, dividend growth. Unlike bonds, which typically offer fixed coupons, dividends have the potential to offer rising cash flow streams over time.

Dividend growth is great in regular periods, but critical during inflationary periods. As inflation erodes the value of a dollar, growing dividends help to maintain purchasing power despite the increasing cost of living.

The real power of dividends is their ability to compound over time, and our approach to finding this growth potential begins with looking for companies that are typically leaders in their respective sectors and that have strong balance sheets with higher levels of cash or modest amounts of debt. We also look for companies that generate significant free cash flow and have a strong dividend profile. To us, great companies have recurrent predictable revenues and big moats—this is where we spend the bulk of our time in our analytical process.

Energy prices have risen substantially in 2022, with commodity inflation presenting both a risk and an opportunity for investors. After years of limited interest, natural gas, oil and copper stocks in the energy and materials sectors are squarely on the radar of active dividend investors, with copper demand being driven by the electrification of the global economy (See Exhibit 3). Given the cyclical and volatile nature of commodity prices, it is imperative that companies have strong balance sheets to weather the vagaries of these markets. After years of fiscal conservatism and significant debt repayment, we believe many commodity companies now have terrific balance sheets. We favor commodity stocks with small, base dividend payouts, which can be maintained throughout the cycle. Targeted commodity selection may make the inflation resilience of a conservative dividend portfolio even stronger.

As we enter the second half of the year, investors continue to face myriad risks: inflation at its highest level in decades, interest rates rising sharply, and still-elevated asset values in some areas of the market. We believe a dividend portfolio selectively comprising a diversified set of businesses with strong balance sheets; recurring, predictable revenues; robust competitive advantages; low risk of secular disintermediation; reasonable valuations; and attractive dividend growth profiles is well-suited to thrive amid elevated global challenges.

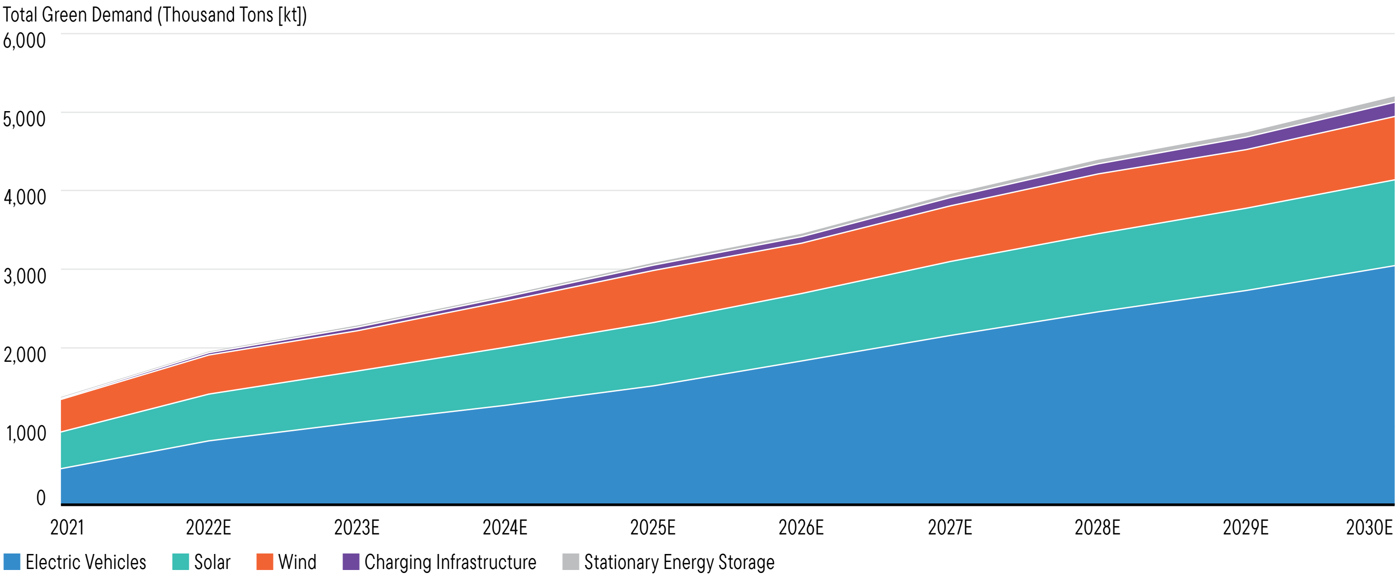
A strong outlook for dividends

Matt Quinlan
Portfolio Manager
Franklin Equity Group

We have seen very strong dividend trends over the past 12 months and good opportunities across sectors (Exhibit 4 on the next page), and the outlook remains positive. Many companies that cut dividends during the pandemic have reinstated them, and in some instances, at higher levels than before the recovery. Consider the energy sector as an example. During the early months of COVID-19, many energy companies were cutting dividends.

Decarbonized Economy Will Be a Copper-intensive Environment

Exhibit 3: Energy Transition or "Green" Demand for Copper
As of April 7, 2022



Source: Goldman Sachs Investment Research. There is no assurance that any estimate, forecast or projection will be realized.

“As global economies slow, we anticipate smaller dividend increases going forward, and we expect cuts from struggling companies. These scenarios sharpen our focus on companies with stronger moats that may be more resilient during recessionary periods.”

This trend has reversed over recent quarters, and for many companies their dividend growth has been high. In some cases, special dividends have been distributed because cash flows have been so strong. The banking sector is another area where the pandemic initially hampered dividend growth, but we have seen solid expansion since last summer. We have a positive dividend outlook in the health care sector, an industry that has more predictable demand and good pricing innovation. Finally, we still see opportunities in the technology sector as well.

An income focus helps mitigate volatility

In our view, an effectively optimized income strategy generates income through attractive dividend-paying companies, equity-linked notes and convertibles, while also offering the potential for market gains. Focusing on income leads to companies with attractive cashflow profiles. In some ways, managing to income is part of managing volatility. Companies that have more predictable cash flows and more resilient dividends are likely to be less volatile.

In our view, the key is to invest in high-quality, blue-chip companies, which allow for better dividend growth and stronger dividend resilience during difficult times. We look to identify market-leading businesses that have proven track records, attractive free cash flow profiles, investment-grade balance sheets, improving cash-flow trends, large addressable markets, and are gaining market share. These companies likely offer strong dividend resilience during tougher times.

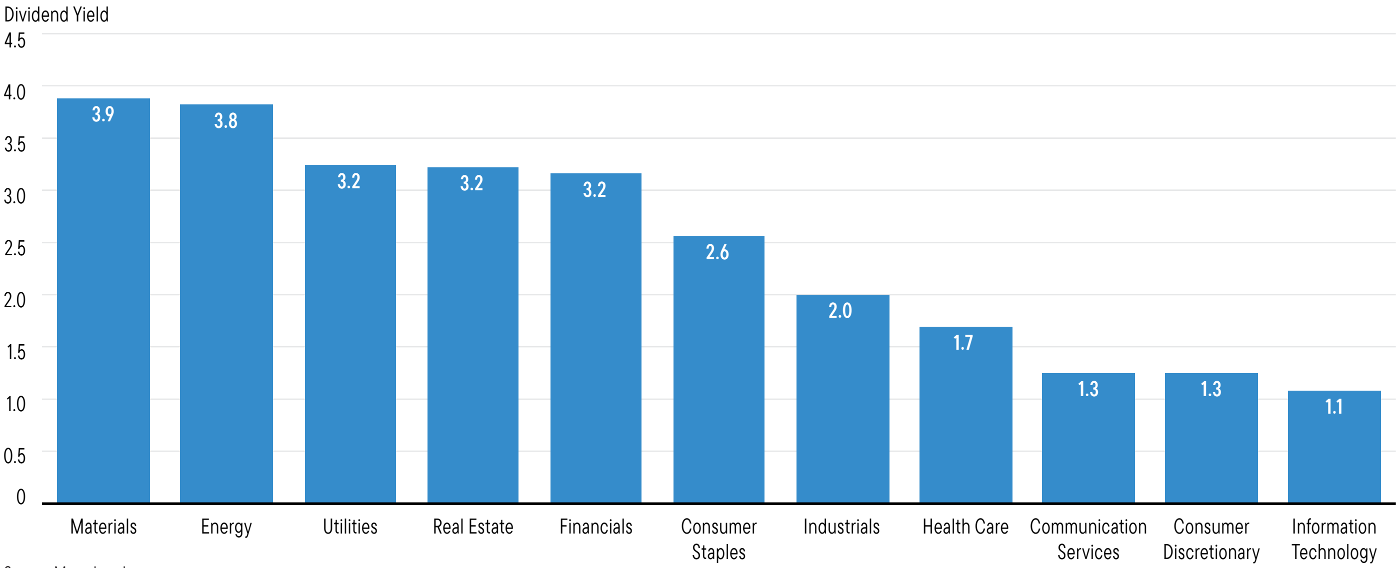
As global economies slow, we anticipate smaller dividend increases going forward, and we expect cuts from struggling companies. These scenarios sharpen our focus on companies with stronger moats that may be more resilient during recessionary periods.

For example, companies with pricing power benefit during inflationary periods. Low-cost producers, such as semiconductor manufacturers, are important suppliers to their end market, whether it be industrial or auto. All industries see pressure when growth stalls, but some are better insulated to withstand headwinds. Companies with good brand equity are valued partners to their customer base and tend to perform better.

Equity Yield Sources Are Diversified Across Multiple Sectors

Exhibit 4: MSCI All Country World Index Sector Dividend Yields

As of May 31, 2022



Source: Macrobond.

Alternative focus: Real estate and infrastructure to counter inflationary headwinds

Both real estate investments and infrastructure assets may pass-through rising inflation costs to end users. In this way, an investor can mitigate the risk of inflation—or even potentially benefit from it.

Equity headwinds are often infrastructure tailwinds

Shane Hurst
Portfolio Manager
ClearBridge Investments

Persistent inflation and rising interest rates have weighed on equity markets in 2022, but macro-economic headwinds are often infrastructure tailwinds due to the way infrastructure treats inflation and the rising rates it engenders largely as a pass-through. Infrastructure assets act as an inflation hedge due to the largely pre-programmed way—through regulation and contracts—infrastructure adjusts to inflationary environments. This applies to both utilities and user-pays assets such as toll roads or rail, as both generate inflation-linked revenues.

Such pricing power comes from the essential nature of infrastructure assets: even at times of economic weakness, consumers continue to use water, electricity and gas, drive cars on toll roads and other essential infrastructure services. Just as importantly, the income we look for from infrastructure is underpinned by long-term contracts, which ensure a steady flow of revenue over a long period.

> **"If there has been one constant in 2022, it is that risk conditions have been changing quickly. From December to March, we saw a significant move lower for US gross domestic product (GDP), from growing 6.9%+ in the fourth quarter of 2021 to contracting 1.6% in the first quarter of 2022."[1]**

Current income is important, but yield quality—which for us means a company's dividend today, dividend growth over the next few years, and the cash flow coverage of those dividends—is also crucial in our assessment of total return. We look for a real required return over five years and consider risks stemming from the costs of equity—again adjusted for inflation—and liquidity. Typically, this has meant dividend growth above inflation and closely tracking our underlying companies' asset growth.

If there has been one constant in 2022, it is that risk conditions have been changing quickly. From December to March, we saw a significant move lower for US gross domestic product (GDP), from growing 6.9% in the fourth quarter of 2021 to contracting 1.6% in the first quarter of 2022.[1]

As a result, the road ahead looks to be rough. Midstream energy infrastructure could see some profit taking, though this may be tempered compared to past risk-off environments given the commodity backdrop and the benefit they will garner as they assist in facilitating the clean energy transition. Utilities are looking more attractive to us in this environment, though we continue to evaluate it through the lens of customer affordability given elevated electricity and gas prices. Traditionally, utilities have lagged the market until the first interest-rate hike is announced and the path of rate hikes becomes more certain. Much of the effect of higher nominal bond yields was priced into utilities in 2021, when the risk-on rally broke down the typical correlation between expected real yields and expected price-earnings for utilities. With the path of rate hikes clearer now, we think this correlation will move closer again and will be a tailwind for the sector, which has strong asset and earnings growth.

Meanwhile, user-pays infrastructure is still seeing its recovery play out. User-pays assets with reopening still to come could dampen the effects of an otherwise slowing economy. There are idiosyncrasies that make this cycle unique and encourage differentiating between companies. We also expect the difference between real and nominal interest rates will require dynamic positioning, for example allocating between the United States and Europe.

Following the Fed's aggressive hike in June, consensus has come around to our view that a recession is more likely than not, and at the least we will see slower growth and higher energy prices. Global central banks continue to remove liquidity from economies, targeting higher inflation at the expense of growth. For infrastructure, the path is simpler. As the economy deglobalizes, it will need to invest in infrastructure, further supporting high visibility and predictability of earnings for infrastructure, which should be well bid in the months ahead.

Diversity of opportunity in private real estate

Clarion Partners

Historical precedence suggests that private real estate can effectively hedge inflation as a steady income-producing asset. An analysis of the 44-year history of the NCREIF Property Index performance under different economic scenarios suggests that private real estate total returns were strong during the years of high/medium real GDP growth and high/medium inflation. The latest case in point was the 12-month period through the first quarter 2022, when the annual real GDP growth rate and core inflation rate were –1.5% and 6.4%, respectively, and the NCREIF Property Index returned a robust annual rate of 21.9%, also outpacing the S&P 500 Index at 15.7% and the Bloomberg Barclays US Aggregate Bond Index at –4.2%.[2]

Our analysis of the structural shifts and path of innovation within the US economy currently lend to heightened opportunity within several segments of the market. The industrial and multifamily segments merit particular attention now; both have some of the strongest fundamentals on record and return performance, as well as strong pricing power (Exhibit 5). We favor both sectors, as well as a few alternative property types, such as life sciences, single-family rentals (SFRs) and self-storage.

Industrial and Multifamily Segments Showing Strong Performance

Exhibit 5: Fundamentals and Pricing Power by Property Sector

As of June 2022

Robust	Strong	Improving	Flat
Industrial	Data Center	Infill Necessity Retail	Regional Mall
Multifamily	Student Housing	Hotel	High-Street Retail
Life Sciences	Medical Office	Senior Housing	Net Lease
SFR/BTR		Office	
Manufactured Housing			
Self-storage			

Sources: NCREIF, Clarion Partners Investment Research, as of June 2022. Notes: 1) The numbers shown above represent estimates based on a combination of Clarion internal projections/underwriting assumptions (i.e., rent growth forecasts), market sales comp observations and broker input (i.e., cap rates) and external projections; the estimates are not indicative of performance for any Clarion product(s) or fund(s). 2) Targets are based on current fundamentals and return forecasts.

In addition, the Industrial sector has benefited tremendously from the rapid expansion of e-commerce activity, a two-decade trend that accelerated greatly during the COVID-19 pandemic. The ongoing transition to omni-channel consumption has rapidly increased demand for large-scale fulfillment centers located near major metros and traditional retail operations in proximity to critical mass. In 2021, the market absorbed 432 million square feet of industrial warehouse space, the highest annual level on record. Vacancy has hit a historic low of 3.0%.[3]

The multifamily segment has benefited from the ongoing US housing shortage and strong demographics. Robust household formation and soaring home prices bode well for ongoing demand. For-sale housing appreciation has spiked almost 30% since the start of the pandemic. Overall, affordability challenges across all residential formats have strengthened the apartment market. Demand in 2021 (674,000 units) eclipsed the previous record by more than 60%, and vacancy is now at 2.3%.[4]

Endnotes

1. Source: US Bureau of Economic Analysis, as of June 29, 2022.
2. Sources: NCREIF, Bloomberg, as of April 2022.
3. Source: CBRE-EA as of Q1 2022.
4. Ibid.

About Global Investment Outlook

Global Investment Outlook allows the Franklin Templeton Institute strategists to highlight manager's views on markets across the firm. The mission of the Institute is to deliver research-driven insights, expert views and industry-leading events for clients and investors globally through the diverse expertise of our autonomous investment groups, select academic partners and our unique global footprint.

Two related Franklin Templeton Thinks publications of note are Allocation Views, produced by Franklin Templeton Investment Solutions, which offers you our best thinking on multi-asset portfolio construction; and, Macro Perspectives, produced by the Institute, featuring economists from across the firm dissecting key macroeconomic themes driving markets.

Contributors

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ClearBridge Dividend Strategy

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ClearBridge Investments

CLARION PARTNERS

Notes

Notes

WHAT ARE THE RISKS?

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