FRANKLIN TEMPLETON INVESTMENTS

2017 GLOBAL INVESTMENT OUTLOOK

Actively Navigating a Dynamic World

2017 GLOBAL INVESTMENT OUTLOOK

WHAT'S INSIDE

WHAT ARE THE RISKS?

All investments involve risks, including possible loss of principal. Special risks are associated with foreign investing, including currency fluctuations, economic instability and political developments. Investments in emerging markets, of which frontier markets are a subset, involve heightened risks related to the same factors, in addition to those associated with these markets' smaller size, lesser liquidity and lack of established legal, political, business and social frameworks to support securities markets. Because these frameworks are typically even less developed in frontier markets, as well as various factors including the increased potential for extreme price volatility, illiquidity, trade barriers and exchange controls, the risks associated with emerging markets are magnified in frontier markets. Bond prices generally move in the opposite direction of interest rates. Thus, as prices of bonds in an investment portfolio adjust to a rise in interest rates, the value of the portfolio may decline. Changes in the financial strength of a bond issuer or in a bond's credit rating may affect its value. Floating-rate loans and high-yield corporate bonds are rated below investment grade and are subject to greater risk of default, which could result in loss of principal—a risk that may be heightened in a slowing economy. Stock prices fluctuate, sometimes rapidly and dramatically, due to factors affecting individual companies, particular industries or sectors, or general market conditions.

December 2016

The coming year will mark the 70th anniversary of Franklin Templeton Investments. We have grown from a handful of dedicated employees in a small office on Wall Street to a premier global investment management organization with over 9,000 employees in 35 countries.

The theme of our 2017 global investment outlook is "Actively Navigating a Dynamic World," a concept that has perhaps never been more relevant than it is today. Global markets have undoubtedly been volatile over the short term, as a host of global macroeconomic and political factors increase investors' anxiety.

It's times like these when professional, active management matters most. Volatile markets present active managers like Franklin Templeton with an environment where research and long-term focus helps uncover investment opportunities that you simply can't find through passive approaches. With our talented workforce and extensive global footprint, I'm excited about capturing the many opportunities that I see in front of us.

The pages that follow spotlight our investment expertise in key areas central to many of our clients' portfolio decisions.

Michael Hasenstab, Ph.D. – As CIO of Templeton Global Macro, Michael leads a team of economists who integrate global macroeconomic analysis with in-depth country research to identify long-term imbalances that translate to investment opportunities. Michael and his team manage Templeton global bond strategies, including unconstrained fixed income, currency and global macro.

Chris Molumphy, CFA – Chris is CIO of Franklin Templeton Fixed Income Group. The group has depth and breadth of expertise in all major sectors of the fixed income market, including investment-grade and high-yield corporate bonds, mortgage- and asset-backed securities, global sovereign and emerging-market debt, municipal securities and bank loans. Each sector is covered by a dedicated team, enabling them to thoroughly examine the market and seek distinctive opportunities.

Ed Perks, CFA – Ed oversees our diverse equity teams that include Franklin Equity Group, Templeton Global Equity Group, Franklin Mutual Series and Franklin U.S. Value. Our equity teams continue to manage their own bottom-up research. By sharing perspectives across teams embedded in several key equity markets, they can strengthen their overall convictions.

Mark Mobius, Ph.D. & Stephen Dover, CFA – Stephen is CIO for Templeton Emerging Markets Group, Franklin Local Asset Management and Templeton Private Equity Partners. Last year, to further align the company's emerging markets equity teams under one organizational structure, while increasing formal collaboration across investment groups, Templeton Emerging Markets Group and the emerging markets equity teams of Franklin Local Asset Management were combined under Stephen. Mark is now a thought leader for the group, sharing his macro perspective on investment opportunities across emerging markets.

We hope the insights we've prepared will be valuable to you as you prepare to make important decisions about your portfolio in this dynamic global marketplace. Thank you for the trust you place in us and best wishes for a prosperous 2017.

Greg Johnson

Global Macro Outlook

2017 OUTLOOK: ***"Despite an increase in developed-market political risks, we see a number of compelling opportunities across specific emerging markets that give us optimism for the upcoming year. We also continue to anticipate rising inflation in the US as wage pressures grow, while the euro-area and Japan diverge markedly from the US with ongoing monetary accommodation."***

Throughout much of 2016, bond markets held onto stretched valuations in US Treasuries, largely ignoring the undercurrents of rising inflation and resilient strength in the US labor market. During the first half of the year, there were even a number of market participants arguing that inflation had become structurally lower and that deflationary risks were of great concern. Our research indicated just the opposite, and we warned investors of what we believed were exceptional vulnerabilities in US Treasury valuations and asymmetric risks in longer duration exposures. Markets began to incrementally trend toward that viewpoint in October as the 10-year US Treasury note's yield modestly rose. By November, a sharp correction in US Treasury valuations was fully underway, manifesting very quickly after the results of the US election as markets appeared to

rapidly move toward our long-held view that inflation pressures were rising. Once those corrections to yields began, they were quite severe in a very short period of time, demonstrating just how extreme those valuations had become. Rising yields in the US were accompanied by depreciations of the Japanese yen and the euro.

Michael Hasenstab, Ph.D.
Chief Investment Officer
Templeton Global Macro

As we look toward 2017, we expect many of those underlying conditions in developed economies that were rapidly driven back into market pricing in late 2016 to only deepen and extend. We anticipate increasing inflation in the US as wage pressures rise and the economy continues to expand, while the euro-area and Japan diverge markedly from the US path. These global trends are likely to continue to pressure bond markets in the developed world but also to generate significant opportunities in specific local-currency emerging markets (EMs) where yields have been high and currencies already appeared extremely undervalued, even as their economic fundamentals have remained resilient. We are optimistic on the valuations in specific EMs in Latin America and Asia ex Japan, but remain wary of duration risks across the developed world.

We Expect Rising US Inflation Pressures in 2017

Our case for rising inflation in the US is primarily centered on rising wage pressures across a US labor force that has been at full employment for much of 2016 and continues to strengthen, accompanied by overly loose monetary policy and fiscal policy set to expand. Core CPI (Consumer Price Index) inflation has persisted above 2.0% throughout 2016 and shows signs of continuing to trend higher. Ultimately, we expect headline inflation to rise above 3.0% in early 2017 as the base effects from last year's decline in oil prices fall out of the figures. Additionally, we expect an escalation in government spending from the incoming US administration, notably in the form of increased infrastructure development, which would add to existing inflation pressures, along with giving a boost to growth and likely increasing the level of US Treasury issuance. In the event that the incoming administration imposes trade restrictions and tariffs, this would also drive up the costs of goods in the US. Taken together, we expect inflation to exceed the US Federal Reserve's (Fed's) target by early 2017 and believe the Fed needs to continue to hike rates. We also see scenarios in which the market should continue to drive yields higher regardless of the Fed's timeline.

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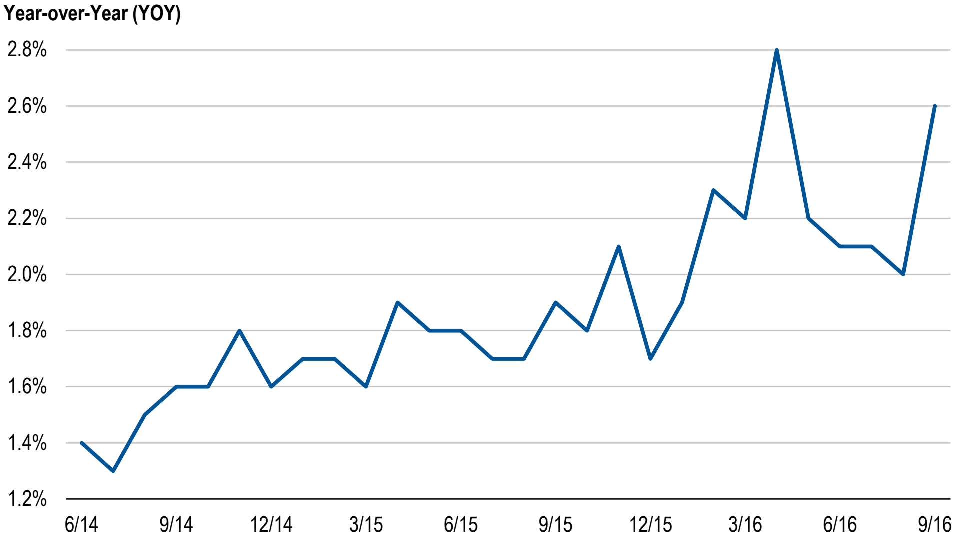
Wage Pressures Continued To Rise in 2016

Wages and Salaries: Private Industry, Employment Cost Index
June 2014–September 2016



Source: US Bureau of Labor Statistics. Data as of 9/30/16.

Weakness in the Euro and Japanese Yen Is Likely To Continue, in Our View

As rates trend higher in the US, we expect continued strengthening of the US dollar against a number of vulnerable currencies, most notably the euro and Japanese yen. Markets began to see a refortifying of the euro's and yen's depreciating trends in October as US Treasury yields rose while the European Central Bank (ECB) and Bank of Japan (BOJ) continued to run exceptionally accommodative monetary policies. Those depreciations only deepened after the US election results in November as the 10-year US Treasury note's yield surged above 2.20%. We continue to see strong cases for ongoing monetary accommodation in the eurozone and Japan as both regions need currency weakness to support their export sectors and drive growth, and each relies far more on the weakness in their currencies than the US does. Both regions also need inflation, particularly Japan.

The growing rate divergences between the low to negative yields in the eurozone and Japan, and rising Treasury yields in the US, should benefit the objectives of the ECB and BOJ, in our view, motivating the central banks to take more assertive measures now that they can be more effectively deployed against firmer rate increases in the US. The euro also faces increased pressures from rising political risks with the recent rise of populist movements in the European Union (EU). Upcoming elections in France and Germany in 2017 will be important indications of just how strong or vulnerable the political will is to uphold the EU and eurozone project. On the whole, Europe's need for continued policy accommodation and currency weakness is more immediate to the upcoming year, while Japan's need is more ongoing and long term. Nonetheless, we expect weakness in both currencies in the upcoming year.

Select EMs Remain Resilient and Undervalued, in Our Assessment

Across EMs, we continue to see significant variations between vulnerable economies and a number of much stronger ones. Markets reacted negatively toward a broad group of EMs in the wake of the US election in November, on fears that protectionist US policies could damage global trade.

However, we have seen a shift in the incoming administration's earlier warnings of enormous tariffs to more of a balance of free and fair trade. There are several scenarios in which the actual impacts to specific EM economies from trade policy adjustments could be minimal to negligible, in our assessment.

Additionally, a number of EMs have already weathered severe shocks over the last year and appear far more resilient to potential increases in trade costs at the margin than markets have indicated. In fact, several EMs have significantly improved their resiliencies over the last decade by increasing their external reserve cushions, bringing their current accounts into surplus or close to balance, improving their fiscal accounts, and reducing US-dollar liabilities. During periods of short-term uncertainty, markets tend to overplay the potential US policy factors and under-recognize the more important domestic factors within the countries. We expect those valuations to ultimately revert back toward their underlying fundamentals over the longer term as markets more accurately assess their actual value.

We have positive outlooks for several local-currency exposures in specific EMs that we view as undervalued, notably Mexico, Brazil, Argentina, Colombia, Indonesia and Malaysia, among others. Specifically regarding Mexico, any free trade restrictions would not end trade between the US and Mexico, they would just raise the costs. Many of the largest US corporations have extensive investments in Mexico and have integrated Mexican production into their supply chains. This considerably complicates the ability of any administration to significantly reduce trade between the two countries, even with an imposition of tariffs. Negative effects on the Mexican peso from potential trade restrictions have been excessively priced in by markets, in our view, and do not reflect fair value even when factoring in a reversion to WTO (World Trade

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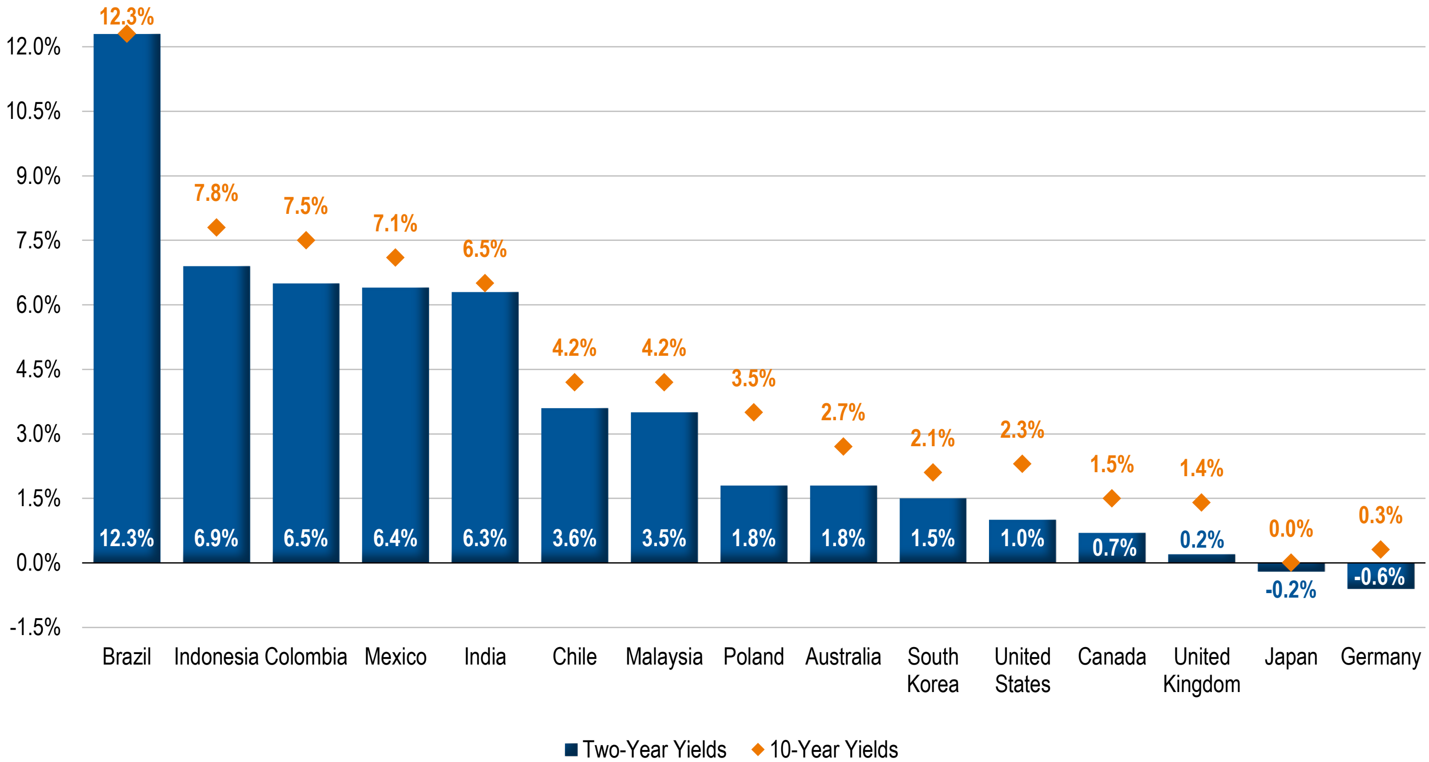
Bond Yields Have Been Significantly Higher Across Specific EMs

Two- and 10-Year Government Bond Yields
As of November 15, 2016



Source: Bloomberg. This chart is for illustrative purposes only and does not reflect the performance or portfolio composition of any Franklin Templeton fund. **Past performance does not guarantee future results.** Higher risks are associated with investing in emerging-market debt, including heightened risks associated with currency fluctuations and economic and political uncertainties. Higher-yielding, lower-rated bonds are generally subject to higher risk of default and loss of principal.

Organization) trade standards. We expect a recovery in the peso as the country's central bank continues to use policy to strengthen the currency and markets adjust to the underlying fair value.

Indonesia is also a strong example of the resiliency in specific EMs. We saw commodity prices collapse, trade volumes decline and China's growth moderate, yet Indonesia has still been growing at 5%, with a balanced current account when including foreign direct investment. Additionally, we have seen massive depreciations in EM currencies in 2016, yet there have been no solvency issues in countries like Indonesia or Malaysia. Twenty years ago, it may have been more difficult for many of these countries to weather a protectionist trade shock, a commodity price shock and an exchange rate shock all at the same time. Yet today these countries are in much stronger positions to handle these types of macro shifts and changes to global trade policies. Should the Trans-Pacific Partnership (TPP) not be concluded, it would not be catastrophic to countries like Indonesia—certainly the region would be stronger with that type of trade agreement, in our assessment, but Indonesia was strong without the TPP and is not dependent on an enhanced trade agreement to continue doing well. Markets have tended to follow the headline impact of trade policy rhetoric, in our opinion, yet the underlying fundamentals tell a much stronger story.

Overall, as we turn the calendar to 2017, the risks of rising populism in Europe and the US and the potential impacts to global trade from protectionist policies bear watching. Despite an increase in developed-market (DM) political risks, there are a number of compelling opportunities across specific EMs that give us optimism for the upcoming year. Ironically, several Latin American countries, such as Brazil, Argentina and Colombia, have recently turned away from previous failed experiments with populism and have moved toward more orthodox policies, taking pro-market and fiscally conservative approaches while maintaining credible monetary policy, proactive business environments and outward-looking trade. We continue to prefer a number of undervalued opportunities across local-currency EMs over many of the overvaluations and low yields across the DMs. It is our hope for 2017 that developed countries experimenting with populism can skip the negative consequences by instead returning to the successes from more orthodox policy-making.

Multi-Sector Fixed Income Outlook

2017 OUTLOOK: ***"In a world still hungry for yield, our view is that a number of fixed income sectors still represent potentially attractive opportunities in terms of income-generating potential, particularly on a risk-adjusted basis."***

US Economy Poised To Continue on a Slow-but-Steady Path

In terms of the economic backdrop, our base expectation for the coming year is for a continuation of the kind of slow-but-steady growth that we have seen in the United States since the end of the financial crisis. Although we recognize the potential for a slight acceleration on the back of additional infrastructure spending, it may be a number of months before a final plan from the incoming presidential administration is hammered out and several more months before the effects are reflected in the economy. In the meantime, we think consumption looks well supported by decent labor market conditions. We may, in fact, see a modest acceleration in inflation stemming from growth in wages, but such an impulse should remain largely contained, in our view. Moreover, we think it likely that an ideologically divided Republican majority means campaign rhetoric may be tempered somewhat in practice, resulting in less change in the status quo than many initially expected. Overall, we think it likely that the US economy continues to maintain its broad trajectory into the coming year, though that would be still somewhat below the pace of traditional expansionary periods.

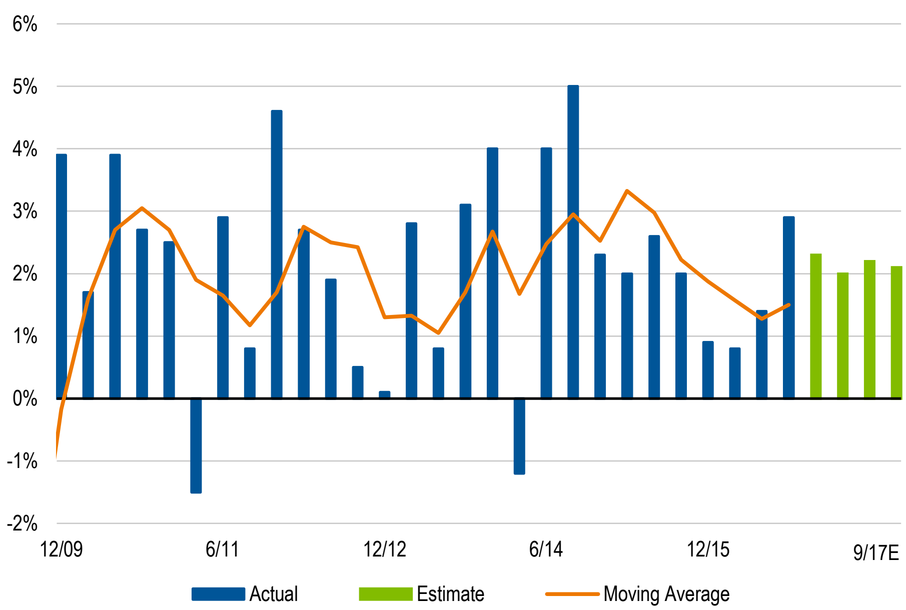
Divergent Monetary Policy Continues To Favor the US Dollar

From a monetary policy standpoint, divergence has been one of the primary themes of the past year. In retrospect, the Fed has proven to be fairly cautious in its approach to policy normalization and Fed meeting minutes have shown the committee's readiness to take not just

Christopher J. Molumphy, CFA
Chief Investment Officer
Franklin Templeton Fixed Income Group

A Likely Continuation of Slow-but-Steady US Growth

US Real Gross Domestic Product, Quarter-over-Quarter
December 2009–September 2017 (Estimate)



Source: US Bureau of Economic Analysis, Bloomberg Monthly Survey: US Economic Forecasts. Estimates from Bloomberg survey of 64 economists' forecasts, surveyed from 10/13/16–10/28/16; reported on 10/28/16. **There is no assurance that any forecast will be realized.**

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> **“While idiosyncratic conditions are likely to continue affecting individual issues, our view is that we have seen the peak of this effect and we should see default rates remain fairly well contained into 2017, particularly as energy-related defaults roll off the calculations.”**

domestic, but also global, financial conditions into account when considering policy adjustments. This suggests to us that the Fed, while still unlikely to deviate from its current shallow path of rate hikes, may be more sensitive to signs of inflation that would be communicated through various channels. At the same time, the BOJ’s fall 2016 decision to hold off on further monetary easing suggests that it may be somewhat concerned with the unforeseen impact of negative interest rates and that Japanese policymakers may be forced to rely on other levers to accomplish their goals. Moreover, headline inflation within the EU has recently shown some signs of stirring, albeit from very low levels. Faced with the current, uncertain environment, including the ultimate form and timing of Brexit (the United Kingdom’s referendum

vote to leave the EU), it is difficult to forecast what changes the ECB might make to its current policy stance. Should conditions continue to improve over the coming year, however, it is conceivable that the ECB could begin the discussion of when and how to exit the current period of extraordinary policy accommodation. Against the general direction of global central bank policy, we continue to favor the US dollar over the Japanese yen and the euro.

Overall Market Outlook and Perspective

Led by more stability in energy markets, investor sentiment has improved steadily during 2016, with some US market sectors also feeling the influence of foreign flows in search of relatively stronger returns. While recognizing that many US dollar-denominated fixed income sectors have seen strong performance over the past year, with global liquidity likely to remain at high levels and growth on a generally stable footing, it appears entirely possible to us that the current constructive backdrop for the bond market could persist for some time despite some shorter-term volatility. In terms of credit conditions, while we see no reason to expect an imminent end to the current credit cycle, we do recognize that it has been one of the longest on record and that we are likely to be closer to its end than its beginning. Nonetheless, we have yet to see any of the early warning signs that normally indicate an increase in credit stress.

Against this backdrop, our view is that a gradual move to a more defensive credit positioning would be a prudent one for the coming year. Therefore, we would seek to move up in credit quality while trimming our exposure to sectors that have appreciated the most over the past year. Having a cache of dry powder available to be able to take opportunistic advantage of potential periods of elevated volatility could also prove beneficial during the coming months. In addition, we would favor a more neutral positioning relative to the direction of interest rates. While we acknowledge that there is little, from a fundamental perspective, to suggest that we could see a deviation from the current shallow trajectory of interest rates, we also note that it is at such times that complacency on the part of market participants can set in.

Fundamentals Still Constructive for Corporate Credit

Given a fundamental backdrop that remains largely benign, we do not think corporate credit requires acceleration in the pace of growth to continue to reflect positive performance potential.

In this environment, investment-grade corporate bond issuer fundamentals have remained solid, if unspectacular. While leverage has ticked up, we have yet to see any sign that credit conditions have materially deteriorated. Moreover, with interest rates still close to historical lows, investor interest in high-quality issuers has generally remained strong given a risk premium that still holds appeal. As a result, we continue to remain constructive on the investment-grade corporate bond sector.

Within the high-yield corporate sectors, we see much the same story. Helped by light supply over the past year, interest coverage levels for high-yield issuers such as high-yield bonds and bank loans have remained little changed overall. At the same time, these sectors have been beneficiaries of the stability in economic conditions, similar to their investment-grade counterparts. In terms of defaults for below-investment-grade issuers, rates rose over the past year as the impact of lower commodity prices took a toll on weaker producers. While idiosyncratic conditions are likely to continue affecting individual issues, our view is that we have seen the peak of this effect and we should see default rates remain fairly well contained into 2017, particularly as

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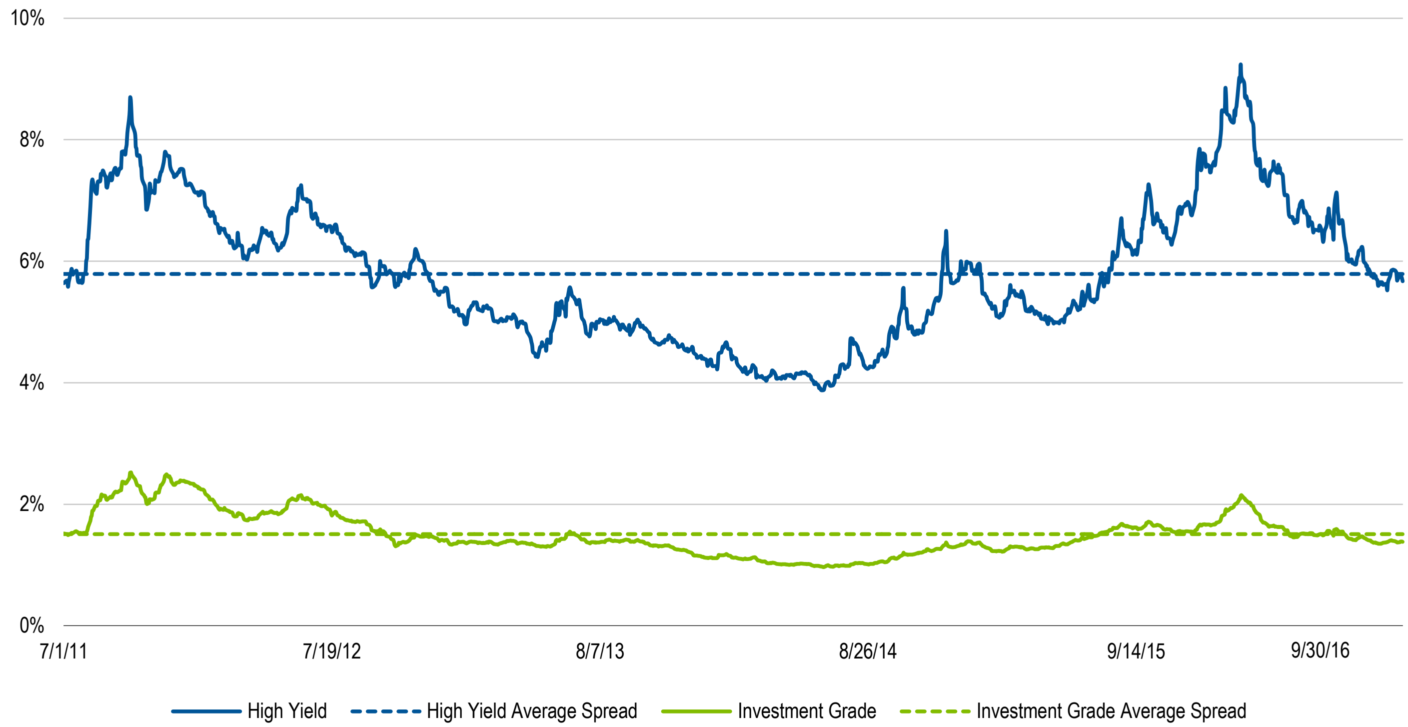
Spreads for Corporate Bonds Still Look Attractive to Us

Yield Spreads for Investment-Grade and High-Yield Bonds
As of September 30, 2016



Source: Bloomberg. Credit Suisse (High Yield Index Spread-to-Worst), Bloomberg Barclays (U.S. Corporate Investment Grade Index Option-Adjusted Spread). Spread-to-worst represents the difference in overall returns between two different classes of securities, or returns from the same class, but different representative securities. The spread-to-worst measures the difference from the worst-performing security to the best, and can be seen as a measure of dispersion of returns within a given market or between markets. The spread-to-worst can vary significantly depending on different market and economic variables. Option-adjusted spread (OAS) measures the yield spread that is not directly attributable to the security's characteristics. OAS is a measurement tool for evaluating price differences between similar products with different embedded options. A larger OAS implies a greater return for greater risks.

energy-related defaults roll off the calculations. In broad terms, the commodity-sensitive sectors that retreated during 2015 came back strongly in 2016 amid increased stability in commodity prices, which contributed in large part to the relatively stronger performance seen for the below-investment-grade corporate sectors. As a result, while we do not necessarily expect a repeat performance in 2017, positive fundamentals and a constructive macroeconomic backdrop could still result in moderate performance potential for the asset class, in our view. With risk premiums modestly below their long-term averages and a largely benign short-term view on credit conditions, we think the US bank loan and high-yield bond sectors still offer relative values we regard as attractive on a risk-adjusted basis.

Leveraging Broad Research Resources To Look Ahead

In a world still hungry for yield, our view is that a number of fixed income sectors still represent potentially attractive income-generating opportunities, particularly on a risk-adjusted basis, despite recent volatility following the US elections. In coming months, any gradual replacement of monetary stimulus with fiscal stimulus could also lead to periodic volatility. However, we believe that fundamental demand for income-producing securities has not diminished and that such demand should provide support for bonds. Overall, therefore, we welcome the gradual normalization of markets and regard periodic volatility as a signal of healthy markets functioning normally.

Our goal over the coming year continues to be to take advantage of what we believe are the most attractive risk-adjusted opportunities for our clients. While this task may be more complex than in the past, it is one to which I believe we are particularly well suited, given our combination of broad research resources and single-minded focus on this goal.

Global Equity Outlook

2017 OUTLOOK: ***"As we move forward, we think a stronger US economy offers a positive dynamic for many other economies and markets, allowing for a potential shift in equity market leadership from the United States to other parts of the world."***

Edward D. Perks, CFA
Chief Investment Officer
Franklin Templeton Equity

Subdued Pace of Unsynchronized Global Growth Appears Set To Improve in 2017

Out-of-sync global growth appears apt to continue in 2017, much as we have seen in the past few years. In our view, incremental improvement in global economic output should be supported by a combination of slow-but-steady consumer spending, employment and household formation in the United States, together with improvements in EMs and continued accommodative monetary policies by non-US central banks. Although the US economy technically enters its eighth year of economic expansion in 2017, we believe it is likely to continue to expand modestly in the near term. In our analysis, conditions such as excesses in capital investment or the housing market are not yet in place to foster a conventional investment cycle-driven recession.

While the pace of economic growth may remain relatively subdued, we see reasons for optimism in US and global equity markets in 2017, even as investor uncertainties over commodity prices and upward-trending US interest rates will likely persist. Low global growth may prompt further fiscal stimulus efforts in DMs outside the United States. We also anticipate longer-term economic rebalancing in EMs and structural reforms. Many DMs are contending with disinflationary pressures. Subsiding inflation in EMs leaves room for monetary policy flexibility, in contrast to their developed counterparts, where central banks appear to have exhausted operational tools. In the United States, hints of wage growth, encouraging employment data and an overall build in key inflation gauges have led to growing market sentiment that the Fed is on track to raise interest rates in 2017, though the path is uncertain and will remain data dependent.

Outside the United States, the path to higher rates is less clear. Global debt levels are at historically high levels as global economic growth has remained tepid. The consensus view appears to be that to bolster growth while also reducing debt, fiscal stimulus should be used to spark inflation along with financial repression to keep real interest rates negative. After years of austerity, ECB President Mario Draghi recently appealed for more expansive budgetary policy. Meanwhile, Japanese policymakers announced a fiscal stimulus package, and the BOJ commenced efforts to engineer a steeper yield curve (i.e., increase the differential between longer-term and shorter-term government bond yields). Even with these policy shifts, the long-term risks to growth due to Brexit and other geopolitical challenges remain to be seen.

EMs also present risks and opportunities, in our view. China's ongoing rebalancing from investment-led to consumption-led growth will likely lead to a continued slowdown in its still-powerful economic engine over the near term as the country manages the transition. Meanwhile, the recession in Latin America might find fresh relief from a mild recovery in commodity prices and generally easier financial conditions. Sanctions have played a role in the collapse of Russia's petro economy

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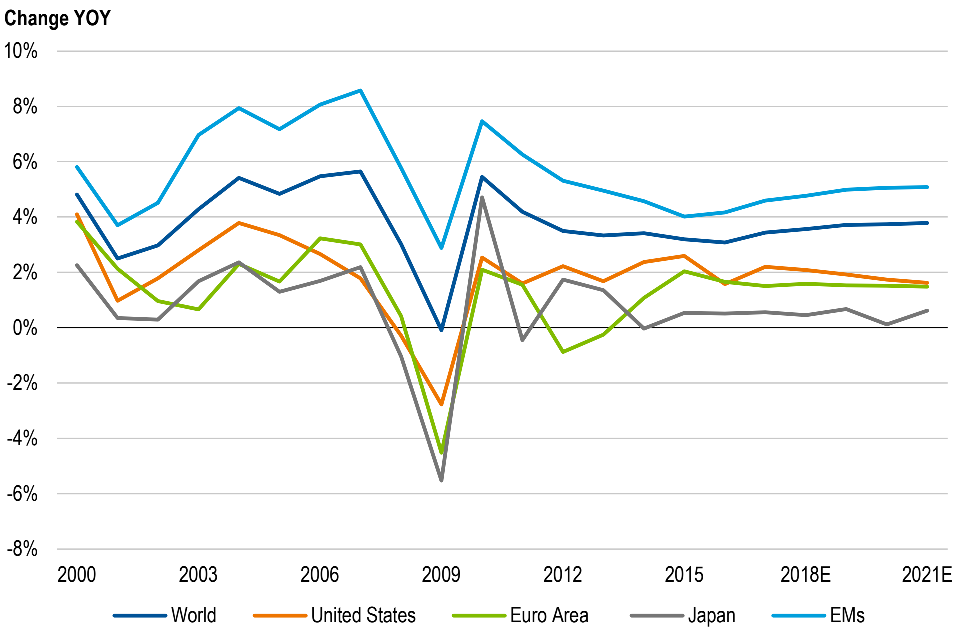
Global Economic Growth Has Remained Tepid but May Improve in 2017

International Monetary Fund Growth Projections
As of October 2016 (% change over previous year)



Source: FactSet, International Monetary Fund. **There is no assurance that any forecast will be realized.**

and negative gross domestic product (GDP), and Brazil's protracted period of tremendous political upheaval has impacted its economy quite significantly. However, the broader components of EM economies—such as the important developing countries outside China, a list that includes Malaysia, the Philippines and Indonesia—intrigue us. In South America, we think Mexico, Chile and Peru offer a much different and more constructive outlook. And while Russia and Brazil may have been key detractors to global GDP growth in 2016, we are optimistic that these countries could potentially outpace investors' low expectations for growth in 2017.

Global Equity Markets: Caution and Optimism

Amid the persistence of systemic headwinds like low economic growth, high public debt and areas of political uncertainty, as well as an aging US bull market in stocks and elevated equity valuations relative to history in key sectors, it appears the general consensus of equity market investors is that caution seems warranted. Though rising commodity prices and corporate access to credit markets have mitigated some short-term risks, we see the potential for other challenges over the longer term. Contributing to these risks are an unsettled political climate, which makes entrenched problems harder to tackle, some weak financial institutions in DMs, and generally heavy corporate debts in EMs.

In broad terms, global equity valuations in late 2016 appear to be pricing in strong economic and earnings rebounds, while dovish central bank policy seems to be reflected in the prices of many global equities. DM indicators, confidence surveys, financial conditions and profit margins have been mixed in some areas. On the upside, global manufacturing gauges have expanded and earnings breadth has improved. With the uncertainty of the US election behind us and a favorable view toward growth ahead of us, we believe firmly that Franklin Templeton's active management strategy can prove beneficial, and we see the prospects for continued fundamental strength as positive. To this end, we think one of the greatest advantages we can offer is the ability to employ thoughtful, fundamentally rigorous analysis to seek to distinguish between those stocks that appear rightly and wrongly priced for the future, in our analysis.

Although we aim to uncover investment ideas through bottom-up fundamental security analysis, we also bear in mind the top-down considerations likely to drive financial markets over our investment horizon. In an inflationary environment, equities historically have generally fared better than many segments within fixed income markets. Though the prospect of rising rates may pressure prices of bond proxies within equity markets, such as real estate investment trusts, downward volatility may also create buying opportunities for investors with long time horizons. This environment could also be favorable for areas such as financials, resource-oriented and consumer cyclical sectors. Following the results of the US presidential election, support for financials stems from a perception that we might see net interest margins expand and an easing of burdensome regulatory requirements. Within health care, there has been a lot of attention on the potential repeal or replacement of the Affordable Care Act and less pressure from the drug-pricing controversy that dominated investor sentiment in 2016. We see industrials as likely to be the key beneficiaries of potentially higher growth and expanding infrastructure spending. As we move forward, we think a potentially stronger US economy offers a positive dynamic for many other economies and markets, allowing for a potential shift in equity market leadership from the United States to other parts of the world.

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Secular Growth Drivers and Capital Allocation

Some may be concerned that profits are typically cyclical and may have already peaked, leading to unsustainable valuations. We think significant secular improvements from globalization, technology and increased productivity have served to drive multi-decade profitability expansion. Though this profitability improvement has on occasion been subject to disruption, we expect it to remain consistent through 2017. As we look at the level of corporate profits and operating margins of companies around the world, we do not see excesses that might portend a pending decline in earnings going forward.

Another area of focus for us relates to corporate capital allocation. We think there is a healthy dynamic between what companies are doing with capital versus the business challenges they are facing. For example, US corporations have increasingly focused on dividends, stock buybacks and capital expenditures in recent years. Merger-and-acquisition activity has remained a focus globally and has shown an accelerating trend in recent years as companies seek strategic drivers of new growth. Many companies have also taken advantage of the low interest-rate environment, extending their debt maturity runways and substantially reducing debt financing costs. Investing in growth while supporting or growing dividends may ultimately contribute to generating attractive performance potential going forward. For investors searching for yield, we believe these dynamics are likely to continue to favor equities in many parts of the world.

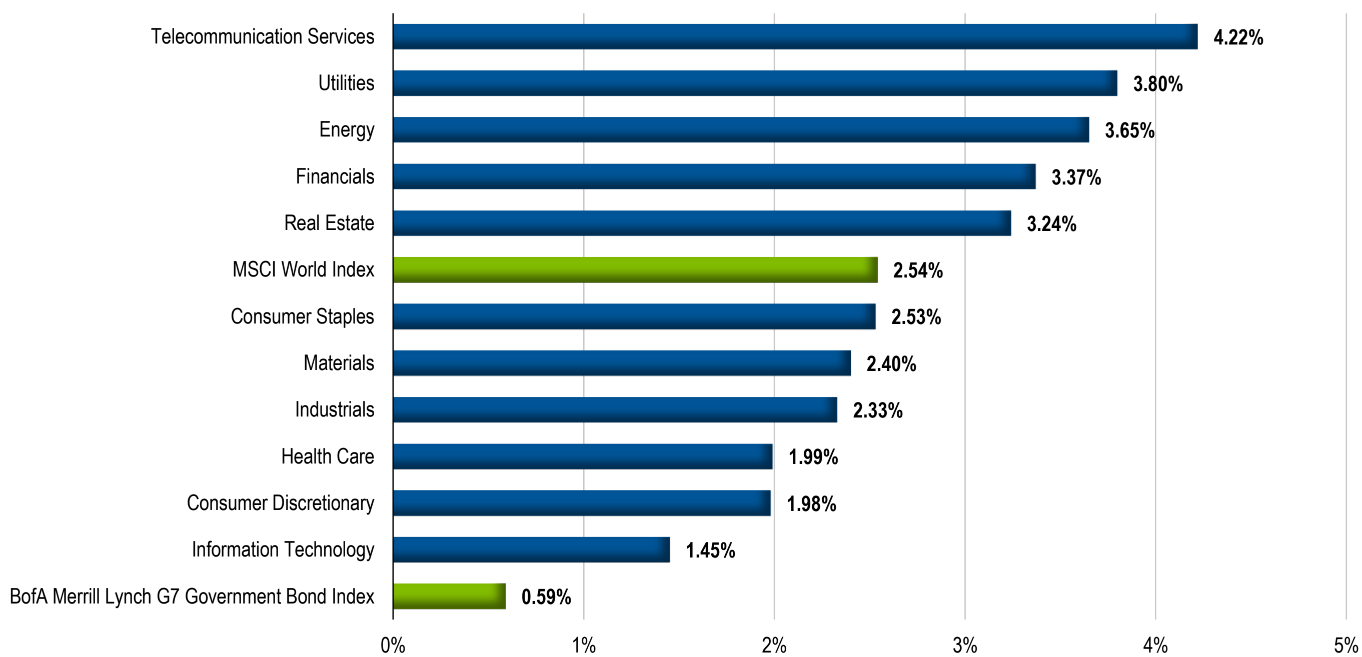
An Object Lesson in Unpredictability

As we reflect on 2016, one of the key themes that emerged was unpredictability. January and February brought negative volatility followed by a swift, albeit narrow, market recovery. Brexit and the heightened political uncertainty tied to the US election cycle also contributed to uncertainty. Events such as these, while analyzable at some level, are very difficult to predict. However, bouts of volatility often create opportunities for longer-term investors with a staunch fundamental focus to take advantage of dislocations in equity markets.

Through it all, fundamental analysis and bottom-up stockpicking have remained the primary focus for many of our investment teams, while sector-specific insights from our seasoned team of analysts across the globe sharpen our views on the year ahead. Despite the uncertainty surrounding the pace of global economic growth and the duration of the current economic expansion, we regard numerous factors as supportive of equities across geographies and sectors, offering investors the potential for multiple opportunities in the year ahead.

Seeking Income in a Low Yield Environment: Breadth of Yield Opportunities Across Sectors

Yields by MSCI World Index Sector
As of September 30, 2016



Source: FactSet. MSCI makes no warranties and shall have no liability with respect to any MSCI data reproduced herein. No further redistribution or use is permitted. This report is not prepared or endorsed by MSCI.

Emerging-Market Equity Outlook

2017 OUTLOOK: "*On balance, although we are mindful of the potential for volatility and watchful for the risks, we believe sentiment toward emerging markets could continue to become more positive.*"

EMs started 2016 on a weak note as equities were buffeted by concerns surrounding China's economy and falling oil prices. However, as the year progressed, positive factors took hold of investor sentiment, leading to EM strength and building, we believe, a robust foundation for EM equities as we look toward 2017.

Mark Mobius, Ph.D.
Executive Chairman,
Templeton Emerging Markets Group

Stephen H. Dover, CFA
Managing Director,
Chief Investment Officer, Templeton Emerging Markets Group and Franklin Local Asset Management

Solid Growth, with Momentum and Valuation Support

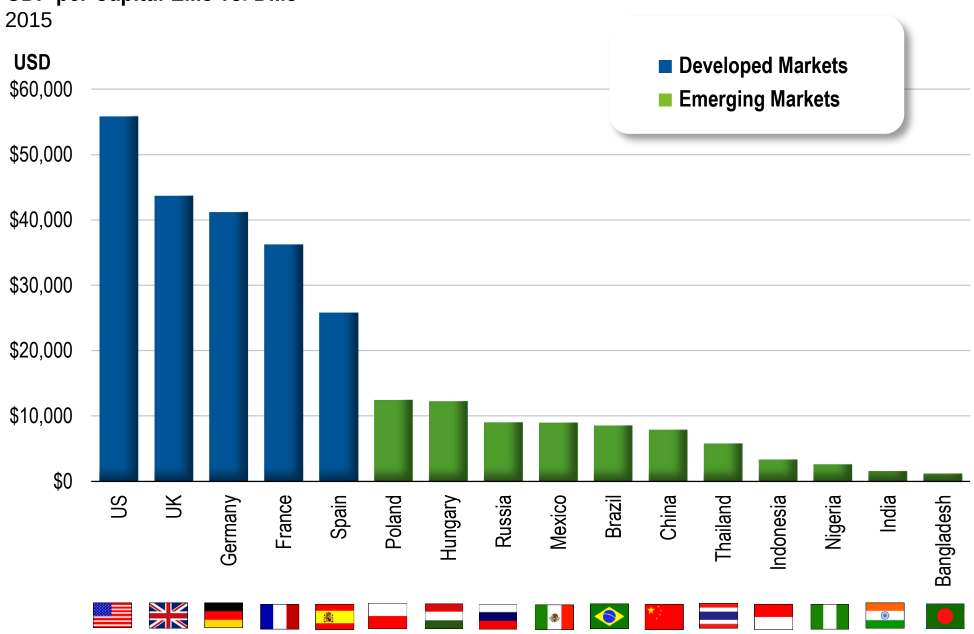
Following recent improvements, we expect macroeconomic advances to continue in 2017. This could bode well for top-line growth opportunities and the earnings outlook for EM equities.

We believe that, while GDP growth in a number of EM countries has been gaining ground, it is likely that over the next few years we could see further relative advances in sizable economies like Russia and Brazil. The economies of these two countries are still contracting, but they are on an improving trajectory and could significantly influence the growth rate of the whole group if they continue to progress. Meanwhile, China's growth, which has been a key concern for many observers, has shown signs of stability and remains at a strong level compared to most other large economies. In the third quarter of 2016, the country's year-on-year growth in GDP came in at a rate of 6.7%, which was in line with the pace reported in the previous two quarters.

Overall, we expect to see GDP growth for EMs in 2017 at a solid and accelerating level, markedly above the rate expected from DMs. EM countries are still far behind their DM counterparts when it comes to overall GDP-per-capita, and so we continue to expect strong growth prospects over the long term.

Additional economic factors are, we believe, important to our expectations for likely further strength in EMs. First, as a group, manufacturing economies are generally back into a position of current account surplus, while there has also been headway in bringing down the deficits of commodity-exporting countries. Second, the debt-to-GDP ratios of EM countries are generally below those of DMs, providing a more stable and, we believe,

GDP per Capita: EMs vs. DMs
2015



Source: Bloomberg, the World Bank. Data as of 10/4/16.

— Continued

sustainable economic foundation. Finally, interest-rate differentials between the two groups are wide, giving EM central banks greater flexibility to maneuver, if required, in the future.

The “hunt for yield” has been a frequently used term in recent years, yet the issue still remains front and center for many market participants. With low and negative yields on many government bonds globally, we continue to expect investors to look toward EM equities, given the income prospects available. For example, the dividend yield was an eye-catching 2.5% as of October 31, 2016, for the MSCI Emerging Markets Index.[1] Year-to-date flows toward EMs have been positive, partly due to the attractive income expected. However, this follows three years of outflows, and so further moves into EMs could be another of 2017’s trends to look out for.

In terms of valuations, the MSCI Emerging Markets Index has traded at a significant discount to the MSCI World Index, for example, on a price-to-earnings-multiple basis. Earnings growth trends have improved markedly during

2016, and we expect this turnaround to continue, with economies and corporate fundamentals across the asset class stabilizing.

Sectoral Opportunities and Challenges

We believe that companies in the consumer-related and information technology (IT) sectors are particularly attractive in the current environment. Select stocks in the consumer sectors can provide an effective means to gain exposure to EM economic expansion and, in particular, access to growth in spending as rising regional wealth fuels a burgeoning consumer class. IT in particular is becoming increasingly integral and competitive in EMs, and, although we are cautious of the recent rapid share-price advances in many of the China-based Internet stocks, we see value in the sector across EMs as a whole. Elsewhere, select commodity shares remain attractively valued, in our view, even though oil prices, for example, are currently significantly above their 2016 lows.

We remain cautious of China’s banks as non-performing loan recognition dampens our outlook for the country’s financial firms. Like banks, China’s real estate sector has staged a striking turnaround from a lengthy downturn, but we have remained on the sidelines, in part due to risks of overleverage and regulation.

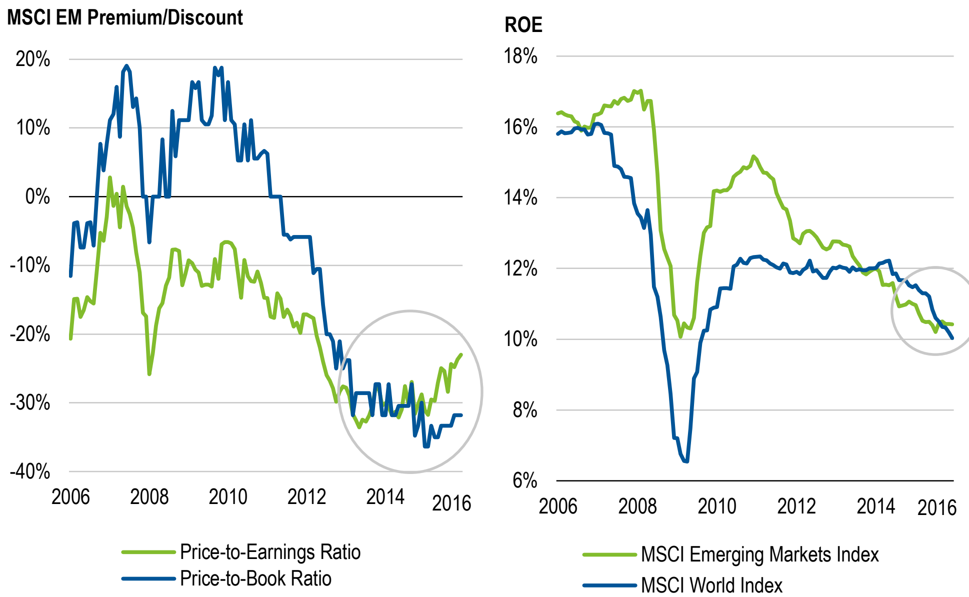
A Small but Attractive Prospect

We continue to like Asian small-capitalization stocks as they are particularly exposed to the solid growth potential we expect from this region over the long term. This is helped by small-cap companies’ generally greater domestic focus than their larger peers, binding them less to challenging macroeconomic factors at a global level. Their valuations typically reflect the stronger growth expected from the smaller equities, but, given there are thousands of small-cap stocks in Asia, the opportunities to discover mispriced securities are often plentiful. These valuation anomalies usually occur due to market inefficiencies as research coverage for many of these companies can be thin on the ground.

> “Information technology in particular is becoming increasingly integral and competitive in emerging markets…”

EM Valuations: Is the Turnaround Just Beginning?

Valuations: MSCI Emerging Markets Index vs. MSCI World Index (Left-Hand Chart)
Return on Equity (ROE): MSCI Emerging Markets Index vs. MSCI World Index (Right-Hand Chart)
October 2006–September 2016



Source: Bloomberg, Nomura Research. MSCI makes no warranties and shall have no liability with respect to any MSCI data reproduced herein. No further redistribution or use is permitted. This report is not prepared or endorsed by MSCI. Data as of 9/30/16.

1. Source: FactSet, MSCI, as of 10/31/16. **Past performance does not guarantee future results.**

— *Continued*

Fed Policy: A Key Impediment to EMs?

Fed monetary policy is still a source of apprehension for many participants in EMs. We expect the trajectory of any rate increases to be gradual, although larger- or faster-than-expected US interest-rate moves could dampen sentiment and lead to volatility.

Other meaningful tests for the global economy may include geopolitical troubles, currency fluctuations, the UK's progress toward leaving the EU and commodity-price moves. Meanwhile, recent political events in the United States may also test markets; the US presidential election victory for Donald Trump is likely to have many implications for markets around the world, including EMs, and may well add to volatility in equities. It is something we will continue to monitor closely. However, we believe it will be important for investors to take a long view and not be swayed by short-term gyrations that we could continue to see in financial markets.

Active Management; Prepared for Change

On balance, although we are mindful of the potential for volatility and watchful for the risks, we believe sentiment toward EMs could continue to become more positive. In our opinion, the search for higher yields and improving risk perception toward EMs, helped by robust economic tailwinds, could provide a basis for further strength in EM equities.

But markets are fast-moving and dynamic. So, whatever the environment in 2017, we believe active equity management, driven by our experienced team located across the globe, will allow us to move deftly as we look to uncover the best investment opportunities as they arise.

TEAM UPDATE >

In accordance with succession planning, Dr. Mark Mobius, Executive Chairman of Templeton Emerging Markets Group (TEMG), has transferred day-to-day management of the group to Mr. Stephen Dover, Chief Investment Officer.

GO ONLINE TO FIND >

MORE INVESTMENT INSIGHTS

Visit our website to learn more about how our multiple world-class investment teams view the complex, interconnected global financial markets they invest in. The portfolio managers listed below describe what they foresee as investment opportunities in 2017. Read more at franklintempleton.com/outlook2017.

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Franklin Templeton Fixed Income Group

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