K2 Alternative Strategies Fund

United States - Retail

Advisor Class
Class A
December 31, 2024

Product Commentary

Performance Review

- Global equities collectively rose in local-currency terms in the fourth quarter of 2024, but the US dollar's strength against most currencies contributed to a slight decline in US dollar terms. Global stocks were pressured by investor concerns about economic growth, persistent inflation in some regions and the likelihood of further interest-rate cuts in 2025. While Donald Trump's presidential victory and the potential for additional tax cuts and expansionary fiscal policy supported US equities, investors outside the United States were concerned about the president-elect's tariff plans and their implications on global trade. As measured by MSCI indexes in US-dollar terms, developed market equities fared better than a global index, while emerging market (EM) equities underperformed it. Global growth stocks significantly outperformed global value stocks. Fixed income spread sectors saw mixed absolute returns. US Treasury (UST) yields moved higher across much of the curve, and aside from the UST market, lower-rated credits generally fared better than their higher-rated counterparts. In the US, investment grade corporate bonds posted a negative return, while those in Europe managed positive returns, as did and US dollar-denominated EM bonds. The global commodities complex had mixed results as the declines that persisted from October through mid-November were largely recouped through year-end despite ample supplies and stiff headwinds from the strong US dollar.

QUARTERLY KEY PERFORMANCE DRIVERS

	Strategy	Manager	Sectors/Currencies/Index Hedges (Fund Level)
HELPED	Global Macro	CFM (Global Macro)	Currency Hedges
	Long/Short Equity	ActusRay (Long/Short Equity)	Industrials (Long)
	Relative Value	Electron (Long/Short Equity)	Financials (Long)
HURT	Event Driven	Jennison (Long/Short Equity)	Health Care (Long)
	—	Athena (Relative Value)	Utilities (Long)
	—	Graham (Global Macro)	Interest Rate Derivatives (Long)

- On a gross basis, three of the four strategies contributed to the portfolio's performance in the fourth quarter, while six of the 10 underlying managers produced positive results. Gains were driven by the global macro and long/short strategies, as well as cash positioning. The relative value strategy made a modest contribution. Conversely, the event driven strategy and the Strategic Overlay weighed modestly on returns. At the asset-class level, currency positioning, which remained short overall, was the key contributor. Long fixed income positioning also aided performance. Long equity positioning was a modest contributor. In contrast, short interest rate positioning and long credit positioning were modest detractors.
- The global macro strategy was the largest driver of positive performance, due to currency positioning, fueled in large part by long positioning in the Japanese yen—which recovered against the US dollar during the period—and the US dollar, especially against the Swiss franc and the Canadian dollar. Commodity positioning also contributed meaningfully. Currency positioning was the key driver for subadvisor CFM, the largest overall contributor during the quarter. CFM's positive performance was driven by gains in all asset classes, led by currency hedges, especially US dollar longs. Cash positioning also contributed. Subadvisor BlueBay was a more modest contributor, owing largely to long fixed income positioning, led by gains in high yield hard currency sovereign credit and in portfolio hedges. Subadvisor Graham was a slight detractor amid weakness in positioning across long fixed income (US and European longs), commodities (energy shorts) and equities (driven primarily by European equity indexes).
- The long/short equity was also a substantial contributor, due almost exclusively to long equity positioning, especially in industrials, financials and equity index futures. Subadvisors ActusRay and Electron were among the quarter's largest contributors across all strategies. Actus Ray's strength was powered by both the quant base and the discretionary overlay, and assisted by the subadvisor's recent neutralization work on thematic, such as US tariffs and China stimulus. Momentum and quality factors supported gains early in the quarter. In December, the subadvisor benefitted from a favorable environment for quant strategies globally. Trump's election victory in November created increased inflation expectations and therefore higher rates, which were positive for the value factor. Subadvisor Electron benefitted from rising volatility amid a focus on macroeconomic data and the upcoming US election. Later, the portfolio featured many significant contributors as volatility cleared after the election. Key holdings included long positions in a Germany-based power conglomerate and a US-based energy equipment company. In contrast, subadvisor Jennison was a meaningful detractor, owing to long equity positioning, especially in the pharmaceuticals, biotechnology and life sciences industry. Weakness in the health care sector early in the quarter combined with the overall equity market pullback to close the year weighed on returns, with losses in the long book only partially offset by gains in the short book.
- The relative value strategy was a modest contributor, due primarily to long equity and cash positioning, which offset detraction from long fixed income positioning. Subadvisors Lazard and Apollo were contributors. Lazard's positive performance was driven by gains across all factors, especially volatility yield, carry and special situations. Apollo had a strong month in November, with performance largely keeping pace with the broader, risk-on market despite the subadvisor's defensive portfolio. A notable contributor was a US-based satellite communications company that advanced on continued momentum from a favorable court ruling. Additionally, a founder of one of the company's largest equity holders was tapped by to be the next deputy secretary of defense. Conversely, Athena detracted, despite solid contribution from cash positioning. The subadvisor posted negative returns in equity and currency positioning amid weakness across much of its equity portfolio, especially in the consumer staples, information technology (IT) and communication services sectors.

- The event-driven strategy weighed slightly on returns, as losses in long equity positioning were only partially offset by gains in long fixed income positioning. Subadvisor Bardin Hill posted a modest loss, dragged in part by a declined in merger-and-acquisition (M&A) volumes ahead of the US election. A long equity position in a China-based traditional medicine and pharmaceuticals provider was a key detractor as the firm's privatization deal fell apart amid a failure to obtain regulatory approval. In contrast, top contributors included a Mexico-based REIT (real estate investment trust) that was the subject of a bidding war.
- The Strategic Overlay posted a slightly positive return, owing to its exposure to the US dollar and long positioning in NASDAQ 100 Index futures. Long positioning in the Standard & Poor's® 500 Index (S&P 500) futures weighed modestly on returns.
- During the quarter, the team increased exposure to the global macro strategy across multiple subadvisors, and increased exposure to the event driven strategy. The portfolio's weighting in cash was significantly lower than at the start of the quarter. Within the Strategic Overlay, the team added a long futures position in the NASDAQ 100 Index.

ONE-MONTH KEY PERFORMANCE DRIVERS

	Strategy	Manager	Sectors/Currencies/Index Hedges (Fund Level)
HELPED	Global Macro	CFM (Global Macro)	Currency Hedges
	Long/Short Equity	ActusRay (Long/Short Equity)	Energy futures (Long)
	Relative Value	Graham (Global Macro)	Equity Index Futures (especially S&P 500)
HURT	—	Electron (Long/Short Equity)	Health Care (Long)
	—	Jennison (Long/Short Equity)	Utilities (Long)
	—	BlueBay (Global Macro)	Industrials (Long)

- Six of the 10 underlying subadvisors delivered absolute gains in December, while all four primary strategies contributed to performance. The Strategic Overlay posted a modest gain but essentially had no impact. At the asset-class level, currency hedges were the largest contributor, followed by cash. Long fixed income positioning was the only meaningful detractor.
- The global macro strategy was the strongest performer, owing primarily to currency hedges. Commodity positioning, which was short overall, also bolstered returns. Subadvisor CFM was the top overall contributor regardless of strategy, fueled in large part by long positioning in the US dollar, especially against the Canadian dollar and the Swiss franc. Subadvisor Graham was also a top contributor, bolstered by its currency positioning, especially gains in US dollar longs, which outweighed detraction from commodities (metals longs). Subadvisor BlueBay weighed on performance, due primarily to losses in local currency debt (especially in Brazil) and currency positioning.
- The long/short equity strategy was a slight contributor as gains from currency hedges and cash positioning outweighed detraction from long equity positioning, particularly in the health care and utilities sector. Subadvisor ActusRay was a top overall contributor in a favorable environment for quant strategies globally, bolstered by the value factor, recent thematic neutralization work and risk controls. Conversely, subadvisors Electron and Jennison were among the largest detractors during the month. Both subadvisors long-book losses were only partially offset by gains in their short books. While Electron outperformed its global utilities benchmark and Jennison did the same in the health care sector, returns were negative as the market pulled back.
- The relative value strategy was a modest contributor as gains from subadvisor Lazard and Athena outweighed modest detraction from Apollo. Long fixed income positioning was the key asset class at the strategy level, outweighing gains from long equity positioning. For Athena, long equity positioning weighed on returns, driven in part by weakness in the S&P 500 Index. Lazard's positive performance was driven by gains in all factors of the portfolio, particularly carry, volatility yield and special situations. Apollo's long positions in a US-based satellite communications company and a US-based luxury resale platform led the way.
- The event driven strategy and subadvisor Bardin Hill posted a modest positive return as the new year approached amid a relatively optimistic outlook. The subadvisor believes the new administration is bullish for the strategy, though geopolitics continue to be a risk. Top individual contributors included winners included a marine liquefied natural gas (LNG) infrastructure firm whose shares continued to rise, driven by further development and partnership with a state-run energy company in Argentina. Conversely, a home health care company was a leading detractor due to a merger extension amid regulatory concerns.
- The Strategic Overlay's modest detraction was driven by losses from S&P 500 futures.
- In December, the team increased exposure to the global macro strategy and reduced cash positioning.

Outlook & Strategy

- Given that the current market environment is characterized by high economic uncertainty, increased geopolitical risks, elevated valuations, and tight credit spreads, the outlook for hedge fund strategies in 2025 is very favorable. These factors are expected to lead to higher volatility across asset classes and increased dispersion within various sectors, as political and economic influences impact sectors differently. This environment is particularly favorable for active strategies that can benefit from being dynamic, non-directional, and agile.
- We have a positive outlook for discretionary global macro strategies, which are well-positioned to benefit from geopolitical uncertainty, changing interest rate regimes, and secular shifts in foreign exchange (FX) rates. Relative value strategies also show promise, as they can capitalize on corporate events and dispersion across asset classes and sectors. Additionally, volatility and risk mitigation strategies present a very attractive entry point due to the low VIX levels (and high valuations), despite the potentially elevated uncertainty and the risk of policy missteps as we head into 2025.

- Overall, the combination of these market conditions and the inherent flexibility of hedge fund strategies suggests that 2025 could be a year of significant opportunities for investors who are able to navigate the complexities of the market effectively.
- We maintain a neutral rating for long/short equity, with modestly increased conviction quarter-over-quarter. Global deal volumes rebounded in 2024, especially towards the end of the year. Market participants expect that momentum to continue into 2025 with activity likely accelerating under the incoming Trump administration. Long/short equity managers should benefit from higher levels of activity because M&A transactions serve as a catalyst for managers to unlock value in specific positions. More generally, corporate events of all types create complexities and inefficiencies that serve as opportunities for investors who are less constrained and better equipped to analyze these situations.
- Despite some modest improvement in some factors for relative value strategies, we retain a neutral outlook. We believe the environment going forward will be characterized by elevated volatility and significantly increased dispersion, prompted by changes in the regulatory regime, potentially less predictable fiscal and monetary policy, and higher geopolitical uncertainty. This should lead to higher volatility of volatility, possibly offering better trading opportunities for both directional and relative value managers in that asset class.
- We've seen a notable improvement in the intermediate outlook for event-driven investing. There is a general belief that regulatory risks that plagued event-driven investing in recent years will abate as new political leadership takes over across major global economies. We are particularly positive in our outlook for activist strategies, which benefit from generally favorable investor sentiment, excess dry powder on corporate balance sheets, and attractive seasonality. Merger volumes have remained generally subdued this year, and there is now hope that merger activity will experience a pickup in the new year, now that antitrust risks are expected to be less of an overhang.
- The outlook remains positive for global macro strategies, albeit with risk around policy implementation and shifting economic data that could disrupt current central bank trends. Many managers are focused on expected changes under a new US administration, which have the potential to create significant opportunities both within the United States and abroad. Tariffs, taxation, regulation, and immigration are all areas of focus during the early part of the new administration. Regional dispersion in economic trends has also increased, with the potential for policy shifts at different speeds or even in different directions being increasingly likely.

Thematic Update

Current View	Momentum	Macro Elements	
Yellow	Stable	1	Global GDP growth
Green	Easing	2	Global central banks' interest rate policies
Red	Increasing	3	Global inflation
Yellow	Stable	4	Global fiscal policy
Red	Increasing	5	Global geopolitical tensions
Yellow	Stable	6	US earnings growth outlook
Yellow	Stable	7	US real estate prices
Yellow	Stable	8	US unemployment rates
Green	Increasing	9	US dollar
Green	Improving	10	Environment for corporate events
Yellow	Stable	11	Investor risk appetite
Yellow	Stable	12	Emerging markets outlook

KEY:	
Green	Constructive
Yellow	Neutral
Red	Cautious

Fund Details

Inception Date	10/11/2013
Benchmark	HFRX Global Hedge Fund Index, ICE BofA US 3-Month Treasury Bill Index

Fund Description

The fund's principal investment goal is capital appreciation with lower volatility relative to the broad equity markets. The fund seeks to achieve its investment goal by allocating its assets across multiple alternative strategies, primarily including Long Short Equity, Relative Value, Event Driven and Global Macro.

Performance Data

Average Annual Total Returns[1] (%)

	1 Mth	3 Mths	1 Year	3 Year	5 Year	10 Year	Since Inception	Inception Date
Advisor Class - With Sales Charges[a]	0.79	2.22	11.61	1.89	3.15	2.96	3.48	10/11/2013
Advisor Class - Without Sales Charges[a]	0.79	2.22	11.61	1.89	3.15	2.96	3.48	10/11/2013
Class A - With Sales Charges[a]	-4.74	-3.38	5.23	-0.27	1.73	2.13	2.70	10/11/2013
Class A - Without Sales Charges[a]	0.79	2.23	11.40	1.64	2.89	2.71	3.22	10/11/2013
HFRX Global Hedge Fund Index[b]	0.01	0.18	5.27	1.23	2.81	1.99	1.89	-
ICE BofA US 3-Month Treasury Bill Index	0.40	1.17	5.25	3.89	2.46	1.77	1.58	-

Performance data quoted represents past performance, which does not guarantee future results. *Current performance may be lower or higher than the figures shown. Principal value and investment returns will fluctuate, and investors' shares, when redeemed, may be worth more or less than the original cost. Performance would have been lower if fees had not been waived in various periods. Total returns assume the reinvestment of all distributions and the deduction of all fund expenses. Returns with sales charge reflect a deduction of the stated maximum sales charge. Returns for periods of less than one year are not annualized. All classes of shares may not be available to all investors or through all distribution channels. For current month-end performance, please call Franklin Templeton at (800) DIAL BEN/(800) 342-5236 or visit www.franklintempleton.com.*

An investor cannot invest directly in an index, and unmanaged index returns do not reflect any fees, expenses or sales charges.

Share Class Details

			Sales Charges		Expenses	
	CUSIP	Ticker	Max	CDSC	Gross	Net
Advisor Class	35241W500	FABZX	–	–	2.53%	2.19%
Class A	35241W104	FAAAX	5.50%	–	2.76%	2.44%

Monthly reporting HFRX Index constituents are comprised of private hedge funds. The **HFRX Global Hedge Fund Index** is designed to be representative of the overall composition of the hedge fund universe. It is comprised of all eligible hedge fund strategies, including but not limited to convertible arbitrage, distressed securities, equity hedge, equity market neutral, event driven, macro, merger arbitrage, and relative value arbitrage. The strategies are asset weighted based on the distribution of assets in the hedge fund industry. Source: Hedge Fund Research, Inc. The HFR indices are being used under license from Hedge Fund Research, Inc., which does not endorse or approve of any of the contents of this report. Unlike most asset class indexes, the HFR Index reflect fees and expenses.

The **ICE BofA 3-Month U.S. Treasury Bill Index** is an unmanaged index that comprises a single U.S. Treasury issue with approximately three months to final maturity, purchased at the beginning of each month and held for one full month. Source: The index data referenced herein is the property of Intercontinental Exchange ("ICE") and/or its licensors and has been licensed for use by Franklin Templeton. ICE and its licensors accept no liability in connection with this use.

Investment Team

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Years with Firm 20
Years Experience 34

Art Vinokur
Years with Firm 20
Years Experience 20

Robert Christian
Years with Firm 14
Years Experience 35

1. Periods shorter than one year are shown as cumulative total returns.

What Are The Risks?

All investments involve risks, including possible loss of principal. The fund is actively managed and could experience losses if the investment **manager's and subadvisors'** judgment about particular investments made for the fund's portfolio prove to be incorrect. The **allocation** of assets among different strategies, asset classes and investments may not prove beneficial or produce the desired results. Some subadvisors may have little or no experience managing the assets of a registered investment company. **International investments** are subject to special risks, including currency fluctuations and social, economic and political uncertainties, which could increase volatility. These risks are magnified in **emerging markets. Derivative instruments** can be illiquid, may disproportionately increase losses, and have a potentially large impact on performance. **Low-rated, high-yield bonds** are subject to greater price volatility, illiquidity and possibility of default. **Currency management** strategies could result in losses to the fund if currencies do not perform as expected. **Short selling** is a speculative strategy. Unlike the possible loss on a security that is purchased, there is no limit on the amount of loss on an appreciating security that is sold short. Investments in companies engaged in **mergers, reorganizations or liquidations** also involve special risks as pending deals may not be completed on time or on favorable terms. **Liquidity risk** exists when securities or other investments become more difficult to sell, or are unable to be sold, at the price at which they have been valued. These and other risks are discussed in the fund's prospectus.

Important Information

The information provided is not a complete analysis of every material fact regarding any country, market, industry, security or fund. Because market and economic conditions are subject to change, comments, opinions and analyses are rendered as of the date of this material and may change without notice. A portfolio manager's assessment of a particular security, investment or strategy is not intended as individual investment advice or a recommendation or solicitation to buy, sell or hold any security or to adopt any investment strategy; it is intended only to provide insight into the fund's portfolio selection process. Holdings are subject to change.

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a. Gross expenses are the fund's total annual operating expenses as of the fund's prospectus available at the time of publication. Actual expenses may be higher and may impact portfolio returns. Net expenses reflect contractual fee waivers, expense caps and/or reimbursements, which cannot be terminated prior to 09/30/2025 without Board consent. Additional amounts may be voluntarily waived and/or reimbursed and may be modified or discontinued at any time without notice.
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