Franklin Low Duration Total Return Fund

Advisor Class: FLDZX Class A: FLDAX | **Commentary | as of March 31, 2025**

Key Takeaways

- **Markets:** There was a significant swing in market sentiment across the first quarter of 2025 (Q1) as participants digested the first few months of US President Donald Trump's new administration's policies.
- **Detractors:** Overweight allocations to high-yield (HY) corporate bonds, senior secured floating-rate bank loans, and non-agency residential mortgage backed securities (RMBS). Security selection in senior secured floating-rate bank loans.
- **Contributors:** Overweight allocations to collateralized loan obligations (CLOs), collateralized mortgage obligations (CMOs), and Treasury inflation-protected securities. Security selection investment-grade (IG) corporate bonds.
- **Outlook:** Although we expect lower US growth this year with upside risks to inflation, we uphold our view that a significant growth slowdown should not be taken for granted just yet.

Performance Review

- The fund's overweight allocation to CLOs and security selection in IG corporate bonds contributed to relative performance. Conversely, overweight allocation to HY corporate bonds and exposure in senior secured floating-rate bank loans hindered results. We increased our allocation to IG corporates, HY corporates and senior secured floating-rate bank loans. We reduced our exposure to CLOs.
- Our overweight allocation to RMBS hindered performance, while our allocation to agency mortgage-backed securities (MBS) had a largely neutral effect on results. We increased our MBS, RMBS and commercial mortgage-backed security allocations.
- Our US duration exposure detracted from performance.

Outlook

- Financial markets are digesting the implications of President Trump's "Liberation Day" announcements after quarter-end that provided greater clarity on tariffs. As tariffs are essentially a tax on consumption of imports, there are concerns that they could lead to negative growth, although few would predict an outright recession. We maintain our view that tariff-induced inflation should be transitory in nature, which we estimate up to a 1.5 percentage point impact. (There is no assurance that any projection, estimate or forecast will be realized.) The growth impact on export-reliant foreign countries will be much more significant than for the United States, in our view.
- Although we expect lower US growth this year with upside risks to inflation, we uphold our view that a significant growth slowdown should not be taken for granted just yet. Hard data show the US economy is still in good shape, with a solid pace of economic activity and the labor market in a "low hiring, low firing" equilibrium with a still-low unemployment rate. We believe the macroeconomic outlook will be heavily influenced by the administration's entire economic policy package, including not just tariffs and immigration, but also deregulation and tax cuts (which are expected to follow). Assuming concrete progress on the latter two, they should help lift growth and contain inflation. Overall, we remain optimistic that pro-growth policy measures are still in the cards. We acknowledge, however, that the longer the uncertainty with a lack of progress on deregulation and tax reform, the higher the downside risk to the economy. Against this backdrop, we think the overall balance of risks should limit the US Federal Reserve to at most one rate cut this year. With the caveat on the aforementioned uncertainty on global growth, risks to US Treasury yields appear to the upside, in our view.
- We maintain our emphasis on diligent security selection and individual company fundamentals for the corporate credit sectors. While we believe IG corporate bonds continue to offer relatively attractive yield, current spread levels offer little cushion for downside economic, financial market or geopolitical surprises. This is particularly relevant as we face significant changes to trade, regulatory, fiscal and immigration policies, as well as international relations. Some of these changes may be positive for corporate credit quality and risk sentiment, while others may create market volatility or have a negative impact on some sectors and individual bond issuers. In the lower-credit-quality HY and floating-rate bank loan sectors, although we remain broadly constructive amid generally favorable technical conditions and still-supportive fundamentals, we continue to favor a focus on quality companies amid persistent market bifurcation, as some industries and issuers will be disproportionately impacted by tariff implementations.
- For securitized sectors, our generally neutral stance remains largely unchanged. For the MBS sector, prepayment speeds for the universe remain low, and we do not expect a material increase in 2025. Demand from US banks could increase as the yield curve steepens, deposits grow and the regulatory environment potentially becomes more favorable for banks. Potential cuts in the federal funds rate and a weaker US dollar could draw demand from overseas investors due to improved hedging costs. For RMBS, our neutral stance on the sector is driven by full valuations and modest home price growth expectations. Despite slowing home price growth, we do not expect a significant decline in home prices, and regional variances are likely to persist. A lack of inventory and steady household formation should keep the housing supply and demand mismatch supportive of home prices. In spite of our generally cautious stance, we are finding opportunities in higher-quality fixed income investments.

Fund Characteristics

Fund Characteristics	Fund
Distribution Frequency	Monthly
Effective Duration	1.74 Years
30-Day SEC Yield (Advisor Class)—With Waiver	4.43%
30-Day SEC Yield (Advisor Class)—Without Waiver	4.15%

Sector Exposure (% of Total)

Sector	Fund
Investment Grade Corporates	40.29
U.S. Treasuries	11.61
Asset-Backed Securities	9.97
Residential Mortgage-Backed Securities	7.06
Agency Mortgage-Backed Securities	7.05
Collateralized Loan Obligation	6.60
High Yield Corporates	4.75
Bank Loans	3.72
Other	42.36
Cash & Cash Equivalents	4.92

Credit Quality Exposure (% of Total)

Rating	Fund
AAA	24.07
AA	21.30
A	18.25
BBB	23.79
BB	3.83
B	3.89
CCC	0.37
CC	0.10
NR	3.97
Not Applicable	0.17
Cash & Cash Equivalents	4.92

Average annual total returns and fund expenses (%)

			Without Sales Charge							With Maximum Sales Charge							Expenses		Sales Charges		Inception
Class	CUSIP	Ticker	3-Mo	YTD	1-Yr	3-Yr	5-Yr	10-Yr	Inception	3-Mo	YTD	1-Yr	3-Yr	5-Yr	10-Yr	Inception	Gross	Net	Initial Charge	CDSC	Date
Advisor Class	353612617	FLDZX	1.52	1.52	5.81	3.47	3.77	2.10	2.79	1.52	1.52	5.81	3.47	3.77	2.10	2.79	0.72	0.45	—	—	11/17/2004
Class A	353612690	FLDAX	1.47	1.47	5.58	3.23	3.54	1.85	2.57	-0.86	-0.86	3.26	2.46	3.06	1.62	2.46	0.98	0.70	2.25	—	11/17/2004
Benchmark	—	—	1.63	1.63	5.61	3.10	1.56	1.73	—	1.63	1.63	5.61	3.10	1.56	1.73	—	—	—	—	—	—

Benchmark(s)

Benchmark =Bloomberg US Government & Credit (1-3 Year) Index

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

The fund began offering Advisor Class shares on 5/15/2008. Performance quotations have been calculated as follows: (a) for Advisor Class periods prior to 5/15/2008, a restated figure is used based on the fund's Class A performance. The performance was adjusted to take into account differences in class-specific operating expenses and maximum sales charges. (b) For periods after share class offering, performance for the specific share class is used, reflecting the expenses and maximum sales charges applicable to that class.

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 02/28/2026 without Board consent. Additional amounts may be voluntarily waived and/or reimbursed and may be modified or discontinued at any time without notice.

During periods of rising inflation, fund yields can vary significantly from month-to-month and may not be repeated.

What are the Risks?

All investments involve risks, including possible loss of principal. Fixed income securities involve interest rate, credit, inflation and reinvestment risks, and possible loss of principal. As interest rates rise, the value of fixed income securities falls. **Asset-backed, mortgage-backed or mortgage-related securities** are subject to prepayment and extension risks. **Changes in the credit rating** of a bond, or in the credit rating or financial strength of a bond's issuer, insurer or guarantor, may affect the bond's value. **Low-rated, high-yield bonds** are subject to greater price volatility, illiquidity and possibility of default. **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. The manager may consider **environmental, social and governance (ESG) criteria** in the research or investment process; however, ESG considerations may not be a determinative factor in security selection. In addition, the manager may not assess every investment for ESG criteria, and not every ESG factor may be identified or evaluated. These and other risks are discussed in the fund's prospectus.

Glossary

A **collateralized loan obligation (CLO)** is a single security backed by a pool of debt.

The **federal funds rate** is the interest rate at which a depository institution lends funds maintained at the Federal Reserve to another depository institution overnight. Also known as the "fed funds rate".

The **yield curve** shows the relationship between yields and maturity dates for a similar class of bonds.

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.

The **Bloomberg U.S. Government/Credit Index**: 1-3 Year Component includes investment-grade, U.S. dollar-denominated, fixed-rate Treasuries, government-related (sovereign, agency, local authority and supranational) and corporate securities with at least one year up to, but not including, three years to final maturity. Source: Bloomberg Indices.

Important data provider notices and terms available at www.franklintempletondatasources.com. All data is subject to change.

Effective Duration is a duration calculation for bonds with embedded options. Effective duration takes into account that expected cash flows will fluctuate as interest rates change. Duration measures the sensitivity of price (the value of principal) of a fixed-income investment to a change in interest rates. The higher the duration number, the more sensitive a fixed-income investment will be to interest rate changes. The **30-day SEC yield** is calculated using the net income (interest and dividends) per share earned over a trailing 30-day period (annualized), divided by the fund's share price at the end of that period. It may not equal the fund's actual income distribution rate, which reflects the fund's past dividends paid to shareholders.

Credit Quality is a measure of a bond issuer's ability to repay interest and principal in a timely manner. The credit ratings shown are based on each portfolio security's rating as provided by Standard and Poor's, Moody's Investors Service and/or Fitch Ratings, Ltd. and typically range from AAA (highest) to D (lowest), or an equivalent and/or similar rating. For this purpose, the manager assigns each security the middle rating from these three agencies. When only two agencies provide ratings, the lower of the two ratings will be assigned. When only one agency assigns a rating, that rating will be used. Foreign government bonds without a specific rating are assigned a country rating, if available. Securities that are unrated by all three agencies are reflected as such. The credit quality of the investments in the Fund's portfolio does not apply to the stability or safety of the Fund. These ratings are updated monthly and may change over time.
Please note, the Fund itself has not been rated by an independent rating agency.

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Before investing, carefully consider a fund's investment objectives, risks, charges and expenses. You can find this and other information in each prospectus, or summary prospectus, if available, at www.franklintempleton.com. Please read it carefully.

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