Franklin Real Return Fund - Class A

PRODUCT PROFILE | FOURTH QUARTER 2013

FUND CHARACTERISTICS (AS OF 12/31/13)

NASDAQ Symbol	FRRAX
Fund Inception Date	11/17/04
Dividends	Monthly, if applicable on 2nd business day
Benchmark	Barclays U.S. TIPS Index
Lipper Classification	Inflation Protected Bond Funds
Morningstar Category™	US OE Inflation-Protected Bond
Total Net Assets—All Share Classes	420 million
Number of Holdings	194
Maximum Initial Sales Charge	4.25%

THIRD-PARTY FUND DATA

Overall Morningstar Rating™

Traditional

★

Load Waived

★★

As of December 31, 2013 the fund's Class A shares received a traditional 1 star overall Morningstar Rating™ and a load waived 2 star Morningstar Rating™, measuring risk-adjusted returns against 185 and 148 U.S.-domiciled US OE Inflation-Protected Bond funds over the 3- and 5-year periods, respectively. A fund's overall rating is derived from a weighted average of the performance figures associated with its 3-, 5- and 10-year (if applicable) rating metrics.

Load waived Class A share Morningstar Ratings do not include front-end sales charges and are intended for investors who have access to such purchase terms (e.g., fee-based programs and participants of a defined contribution plan). Investors should contact their financial advisor to determine their eligibility to purchase Class A shares without paying the sales charge.

FUND DESCRIPTION

The fund seeks to achieve total return that exceeds the rate of inflation over an economic cycle. The fund will generally invest a significant portion of its assets in inflation-protected securities. The manager also has the flexibility to invest in other sectors of the market as it seeks to achieve a high level of real return (total return less inflation), consistent with an acceptable level of risk.

PERFORMANCE DATA

Average Annual Total Returns for Periods Ended December 31, 2013 (%)

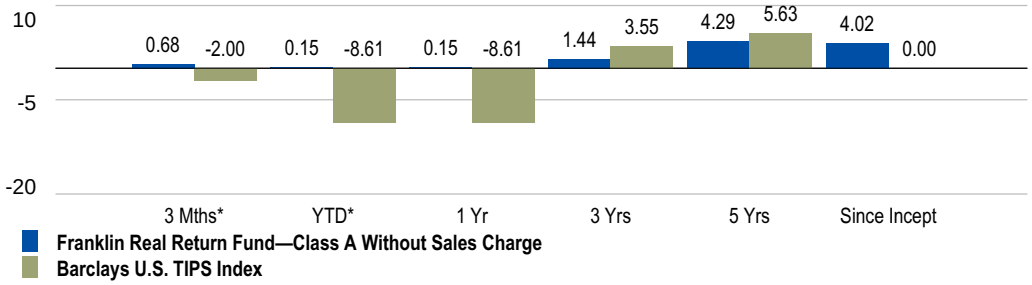
	3 Mths*	YTD*	1 Yr	3 Yrs	5 Yrs	Since Incept (11/17/04)
With Sales Charge	-3.64	-4.09	-4.09	-0.03	3.39	3.53
Without Sales Charge	0.68	0.15	0.15	1.44	4.29	4.02
Barclays U.S. TIPS Index	-2.00	-8.61	-8.61	3.55	5.63	N/A

Total Annual Operating Expenses—*With Waiver:* *0.91%* ***Without Waiver:*** *1.07%*

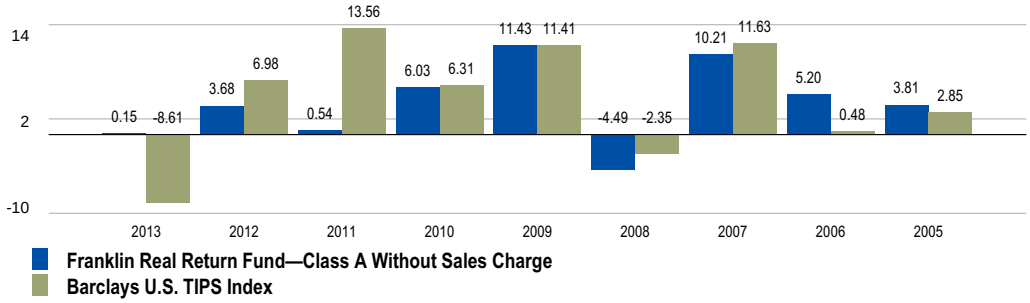
Performance data represents past performance, which does not guarantee future results. Current performance may differ from figures shown. The fund's investment returns and principal values will change with market conditions, and you may have a gain or a loss when you sell your shares. Please call Franklin Templeton Investments at (800) DIAL BEN/(800) 342-5236 or visit franklintempleton.com for the most recent month-end performance.

The fund has an expense reduction contractually guaranteed through at least February 28, 2014. The fund may also have a fee waiver associated with any investments it makes in a Franklin Templeton money fund, an arrangement that is contractually guaranteed through at least its current fiscal year end. Fund investment results reflect the expense reduction and fee waiver, as applicable; without these reductions, the results would have been lower.

Average Annual Total Returns for Periods Ended December 31, 2013 (%)



Calendar Year Returns As of December 31, 2013 (%)



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If the Fund's sales charge had been included, the returns would have been lower.

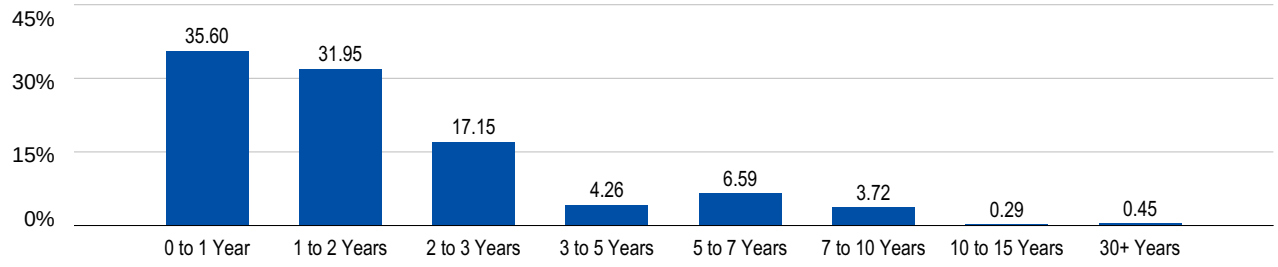
For information related to the "Fund Description," "Fund Characteristics," "Third-Party Fund Data," and "Performance Data" sections, please see Explanatory Notes.

*Cumulative Total Returns.

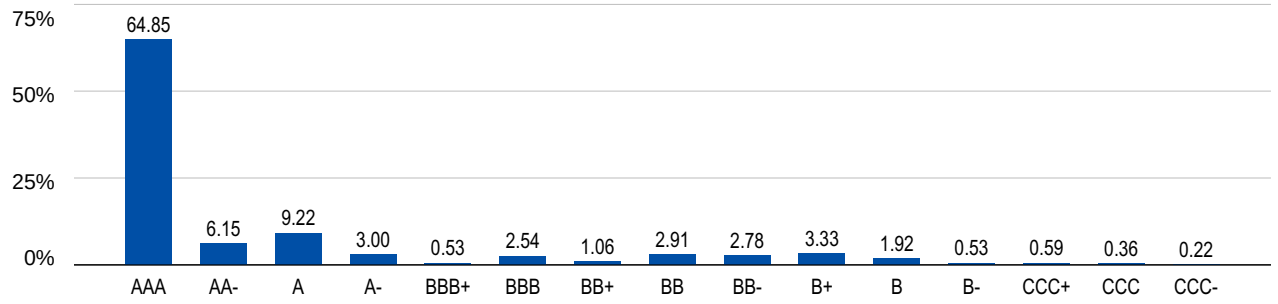
NOT FDIC INSURED | MAY LOSE VALUE | NO BANK GUARANTEE

PORTFOLIO DIVERSIFICATION (AS OF 12/31/13)—Fund

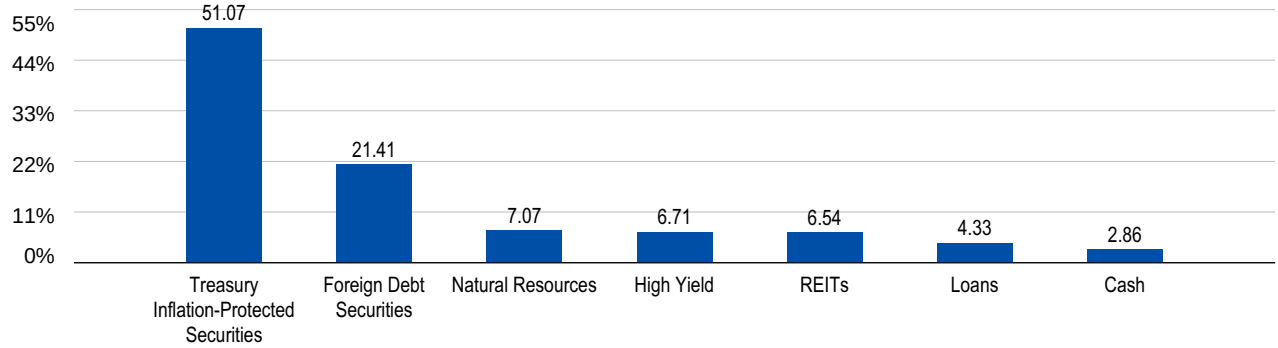
Maturity Weightings



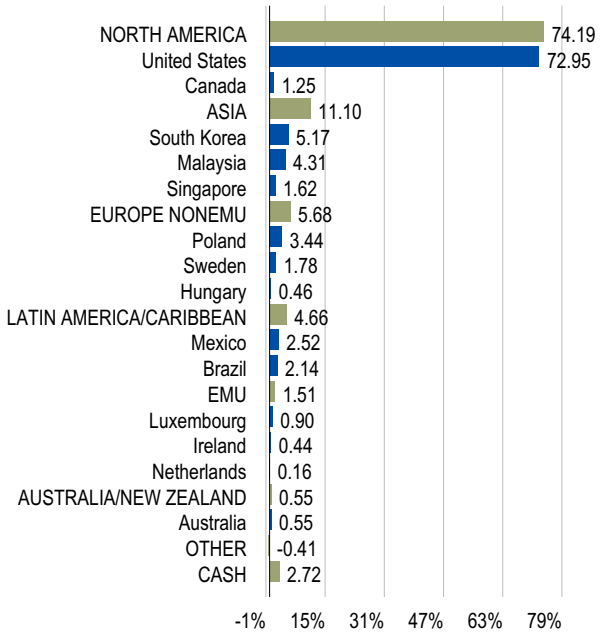
Quality Weightings



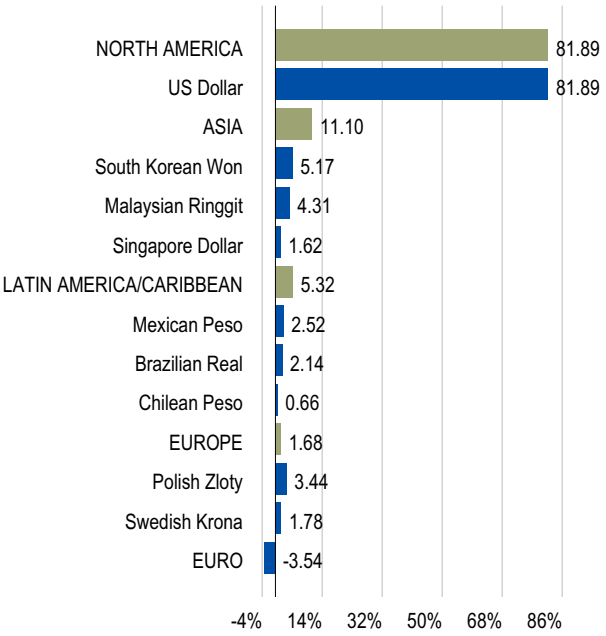
Sector Allocation



Geographic Allocation



Currency Allocation



Quality Weightings: Ratings shown are assigned by one or more Nationally Recognized Statistical Rating Organizations ("NRSRO"), such as Standard & Poor's, Moody's and Fitch. The ratings are an indication of an issuer's creditworthiness and typically range from AAA or Aaa (highest) to D (lowest). When ratings from all three agencies are available, the middle rating is used; when two are available, the lowest rating is used; and when only one is available, that rating is used. Foreign government bonds without a specific rating are assigned the country rating provided by an NRSRO, if available.Cash and equivalents (defined as bonds with stated maturities, or that can be redeemed at intervals, of seven days or less) as well as derivatives are excluded from this breakdown. As a result, the chart does not reflect the fund's total net assets.

For information related to the "Portfolio Diversification" section, please see Explanatory Notes.

PORTFOLIO CHARACTERISTICS (AS OF 12/31/13)

	Fund
Average Duration	1.38 Yrs
Average Weighted Maturity	1.93 Yrs
Annual Turnover Ratio (As of 10/31/13)	27.91%

GLOSSARY

Annual Turnover Ratio: Percentage of a fund's holdings replaced with other holdings during a fund's most recent full fiscal year. A fund's fiscal year end can be found in a fund's current summary prospectus and/or prospectus.
Average Duration: Also known as 'effective' or 'Macaulay' duration it is a measure of the sensitivity of the price (the value of principal) of a fixed-income investment to a change in interest rates. Duration is expressed as a number of years. It's an indication of an issue's coupon relative to its maturity. Rising interest rates mean falling bond prices; declining interest rates mean rising bond prices. The bigger the duration number, the greater the interest-rate risk; (or reward for bond prices). The weighted average duration of a fund reflects the effective duration of the underlying issues, based on the size of each holding. This value differs with 'Modified Duration' which is modified for the market (dirty) price of an issue.
Average Weighted Maturity: An estimate of the number of terms to maturity, taking the possibility of early payments into account, for the underlying holdings. The calculation uses the weighted average time to the receipt of all future cash flows for all holdings. Also known as 'average life' for fixed-term products. The weighted average maturity of a fund reflects the maturity of the underlying issues, based on the size of each holding.

MARKET REVIEW

Economic data for the fourth quarter of 2013 were initially overshadowed by political considerations, notably a 16-day partial government shutdown resulting from a political impasse in Congress. As the period progressed, in a sign of more confidence in the economic outlook, the US Federal Reserve (Fed) decided to cut its monthly asset purchases from US$85 billion to US$75 billion starting in January. The reduction in purchases will be split evenly between mortgage-backed securities (MBS) and US Treasuries. The Fed remains data-dependent and is not on a preset course, and it left open the possibility of increasing bond purchases again if the economy falters. In the broader economy, consumption spending, aided by an uptick in income growth and a lower savings rate, overcame some weak sentiment numbers at the beginning of the quarter and began to demonstrate marked improvement over the course of the period.

US industrial production also continued its expansionary trend over the quarter, aided by a weather-related surge in utilities production, as well as supportive new orders. In addition, although the housing market showed some signs of the impact from higher mortgage rates in the form of lower transaction volumes, home prices continued to rise in comparison with year-ago figures.

PERFORMANCE REVIEW AND CONTRIBUTORS TO PERFORMANCE

Performance Review

During the fourth quarter of 2013, the performance of our diversified allocation to inflation-sensitive assets was generally positive. Over the period, our natural resources securities, high-yield corporate bond exposure, foreign exchange allocation and Treasury Inflation Protected Securities (TIPS) allocation contributed to absolute fund performance. However, our allocation to real estate investment trusts (REITs) weighed on performance.

Portfolio Positioning

During the period, the fund invested in diversified securities across the allowable sectors. At period-end, exposure to the TIPS sector was less than half of the fund's total net assets. We slightly decreased our exposure to natural resources securities. For diversification, we also allocated some of the fund's assets to short-term non-US dollar-denominated securities, high-yield bonds and bank loans. We employed a non-dollar strategy to help hedge against US-dollar weakness versus certain currencies, and we concentrated our TIPS holdings in shorter maturities.

Outlook & Strategy

Important efforts have been made in the US Congress to arrive at a bipartisan agreement on federal government budget levels for the coming two years. The brokering of a modest deal on spending, while doing little to solve the country's long-term debt problems, reduces the chance of a further government shutdown in January and removes another source of uncertainty for would-be investors, in our view. In addition, the Fed decided in December to cut its monthly asset purchases from US$85 billion to US$75 billion starting in January, with the reduction in purchases split evenly between mortgage-backed securities and US Treasuries. We think the likelihood at this stage is that the Fed will continue to reduce the pace of its monthly asset purchases in measured steps, finally wrapping them up at the end of 2014 if the economy is on a sustainable recovery path. Overall, we believe that the Fed's forward guidance on low interest rates, combined with strengthening growth, low inflation and the congressional deal on US government spending, could continue to drive investors away from higher-quality strategies and toward "risk" assets.

The above commentary does not provide a complete analysis of every material fact regarding any market, region, industry, security, portfolio or pooled investment vehicle. Portfolio holdings information, opinions and other market or economic information and data provided are as of the date of the commentary, unless another date is expressly indicated, and may change without notice. Statements of fact cited by the manager have been obtained from sources considered reliable but no representation is made as to their completeness or accuracy. The manager's assessment of a particular industry, region, security, sector or investment is intended solely to provide insight into the manager's investment process and is not a recommendation to buy or sell any security, nor investment advice. References to particular securities or sectors are only for the limited purpose of illustrating general market or economic conditions and are not recommendations to buy or sell a security. Although historical data is no guarantee of future results, these insights may help you understand our investment management philosophy.

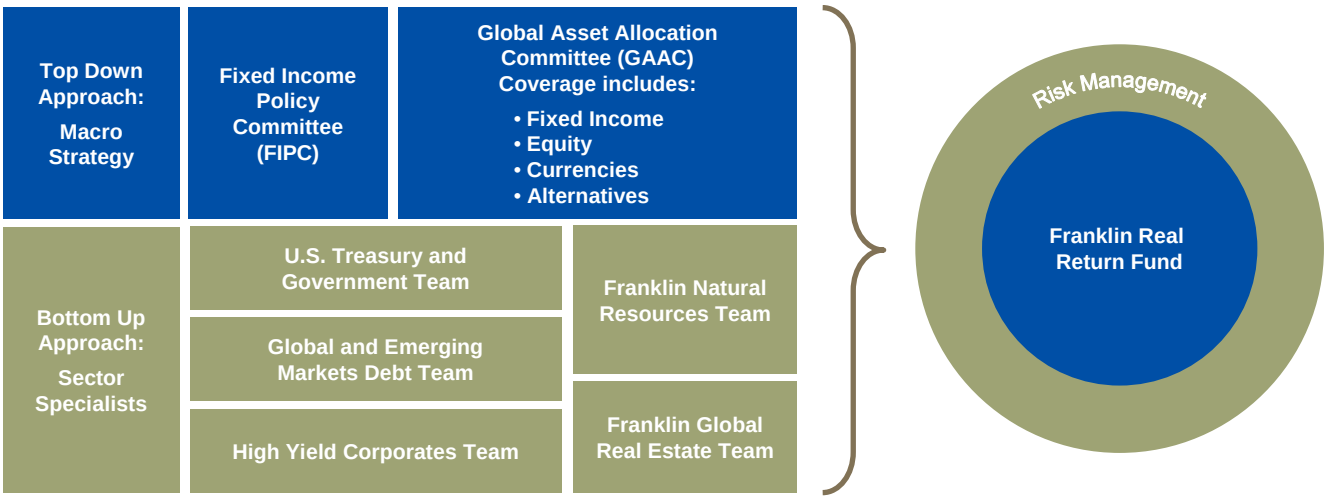
INVESTMENT PHILOSOPHY AND PROCESS

Investment Philosophy

- We believe we can maximize real return potential for shareholders by focusing on inflation-protected securities and other investments correlated to inflation.
- Since inflation-protected securities can move independently of either stocks or traditional bonds, the fund can also offer investors diversification that can potentially reduce overall portfolio volatility.

Investment Process

- We seek to add value through top-down economic analysis and bottom-up fundamental sector, security and issuer analysis. Additionally, we utilize robust quantitative and risk management tools.
- The manager evaluates inflation cycles, business cycles, yield curves, country risk and values between and within markets.
- Ultimately, the fund allocates its assets among securities in various market sectors based on the managers' assessment of changing economic, global market, industry and issuer conditions.



Inflation-protected securities are debt securities that are structured to provide protection against inflation. Depending on the type of inflation-protected security, the principal or the coupon rate is periodically adjusted according to the rate of inflation, as measured by a designated inflation index such as the Consumer Price Index (CPI). Investors in Franklin Real Return Fund who do not reinvest income that comes from inflation adjustments may not maintain the purchasing power of the investment over the long term. Income earned depends on the amount of principal invested, and that principal may not keep up with inflation if the investor does not reinvest the principal adjustment paid out as part of the fund's income.

INVESTMENT AND MANAGEMENT TEAM (AS OF 12/31/13)

Franklin Real Return Fund Management Team	Years with Firm	Years Experience
T. Anthony Coffey, CFA	24	24
Kent C. Burns, CFA	19	21
Franklin Templeton Fixed Income Group	**Number of Members**	**Average Years of Experience**
Portfolio Managers	52	20
Portfolio Managers/Analysts	24	16
Research Analysts	63	12
Traders	13	16
Franklin Templeton Multi-Asset Strategies	**Number of Members**	**Average Years of Experience**
Portfolio Managers	7	22
Portfolio Managers/Analysts	2	9
Research Analysts	19	10

WHAT ARE THE RISKS

All investments involve risks, including possible loss of principal. Interest rate movements will affect the fund's share price and yield. Bond prices generally move in the opposite direction of interest rates. As the prices of bonds in a fund adjust to a rise in interest rates, the fund's share price may decline. Foreign securities involve special risks, including currency fluctuations and economic and political uncertainties. Changes in the financial strength of a bond issuer or in a bond's credit rating may affect its value. Stock prices fluctuate, sometimes rapidly and dramatically, due to factors affecting individual companies, particular industries or sectors, or general market conditions. The fund is actively managed but there is no guarantee that the manager's investment decisions will produce the desired results. These and other risks are described in the fund's prospectus.

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For information related to the "Investment Philosophy" section, please see Fund Description and Expanatory Notes.

EXPLANATORY NOTES

FUND DESCRIPTION

Inflation-protected securities are fixed income securities that are structured to provide protection against inflation. Depending on the type of inflation-protected security, the principal or the coupon rate is periodically adjusted according to the rate of inflation, as measured by a designated inflation index such as the Consumer Price Index (CPI). Investors in Franklin Real Return Fund who do not reinvest income that comes from inflation adjustments may not maintain the purchasing power of the investment over the long term. Income earned depends on the amount of principal invested, and that principal may not keep up with inflation if the investor does not reinvest the principal adjustment paid out as part of the fund's income.

FUND CHARACTERISTICS

Dividends: The fund's yield and distributions should be expected to vary significantly from month to month. Because the fund has a significant investment in Treasury Inflation-Protected Securities (TIPS), it is highly influenced by the TIPS market and the monthly inflation adjustments on these securities. If inflation declines, it can result in negative inflation adjustments for TIPS, and thus a negative 30-day standardized yield. In this scenario, the fund may not earn enough net investment income from its investments in TIPS to pay out a dividend.

THIRD-PARTY FUND DATA

Morningstar Rating™: Source: Morningstar® 12/31/13. For each fund with at least a three-year history, Morningstar calculates a Morningstar Rating™ based on how a fund ranks on a Morningstar Risk-Adjusted Return measure against other funds in the same category. This measure takes into account variations in a fund's monthly performance after adjusting for sales loads (except for load-waived A shares), redemption fees, and the risk free rate, placing more emphasis on downward variations and rewarding consistent performance. The top 10% of funds in each category receive 5 stars, the next 22.5% receive 4 stars, the next 35% receive 3 stars, the next 22.5% receive 2 stars and the bottom 10% receive 1 star. Class A shares of Franklin Real Return Fund received a traditional Morningstar™ Rating of 1 and 1 star(s) for the 3- and 5-year periods, respectively. Load-waived Class A shares of Franklin Real Return Fund received Morningstar Ratings™ of 2 and 2 star(s) for the 3- and 5-year periods, respectively. The Morningstar Rating™ may differ among share classes of a mutual fund as a result of different sales loads and/or expense structure. **Past performance does not guarantee future results.** ©2014 Morningstar, Inc. All rights reserved. The information contained herein is proprietary to Morningstar and/or its content providers; may not be copied or distributed; and is not warranted to be accurate, complete or timely. Neither Morningstar nor its content providers are responsible for any damages or losses arising from any use of this information.

PERFORMANCE DATA

The fund offers other share classes subject to different fees and expenses, which will affect their performance.
Source for Index: FactSet. Indexes are unmanaged and one cannot invest directly in an index.

PORTFOLIO DIVERSIFICATION

Maturity/Quality Weightings/Sector/Geographic/Currency Allocation: Percentage may not equal 100% due to rounding. Information is historical and may not reflect current or future portfolio characteristics. All portfolio holdings are subject to change.

PORTFOLIO CHARACTERISTICS

The portfolio characteristics listed are based on the fund's underlying holdings, and do not necessarily reflect the fund's characteristics. Information is historical and may not reflect current or future portfolio characteristics. All portfolio holdings are subject to change.

FRANKLIN TEMPLETON INVESTMENTS

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Investors should carefully consider a fund's investment goals, risks, charges and expenses before investing. To obtain a summary prospectus and/or prospectus, which contains this and other information, talk to your financial advisor, call us at (800) DIAL BEN/(800) 342-5236 or visit franklintempleton.com. Please carefully read a prospectus before you invest or send money.

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