DECEMBER 31, 2013

ANNUAL REPORT

AND SHAREHOLDER LETTER



Sign up for electronic delivery at franklintempleton.com/edelivery

MUTUAL FINANCIAL SERVICES FUND



Franklin • Templeton • Mutual Series

Franklin Templeton Investments

Gain From Our Perspective®

Franklin Templeton's distinct multi-manager structure combines the specialized expertise of three world-class investment management groups—Franklin, Templeton and Mutual Series.

SPECIALIZED EXPERTISE

Each of our portfolio management groups operates autonomously, relying on its own research and staying true to the unique investment disciplines that underlie its success.

Franklin. Founded in 1947, Franklin is a recognized leader in fixed income investing and also brings expertise in growth- and value-style U.S. equity investing.

Templeton. Founded in 1940, Templeton pioneered international investing and, in 1954, launched what has become the industry's oldest global fund. Today, with offices in over 25 countries, Templeton offers investors a truly global perspective.

Mutual Series. Founded in 1949, Mutual Series is dedicated to a unique style of value investing, searching aggressively for opportunity among what it believes are undervalued stocks, as well as arbitrage situations and distressed securities.

TRUE DIVERSIFICATION

Because our management groups work independently and adhere to different investment approaches, Franklin, Templeton and Mutual Series funds typically have distinct portfolios. That's why our funds can be used to build truly diversified allocation plans covering every major asset class.

RELIABILITY YOU CAN TRUST

At Franklin Templeton Investments, we continuously seek to provide investors with strong risk-adjusted returns over the long term, as well as the reliable, accurate and personal service that has helped us become one of the most trusted names in financial services.

FRANKUN TEMPLE ON TRANSPORTED TO THE PARTY OF THE PARTY O

MUTUAL FUNDS | RETIREMENT PLANS | 529 COLLEGE SAVINGS PLANS | SEPARATELY MANAGED ACCOUNTS

Contents

Shareholder Letter

Innual Report		Financial Highlights and		Report o
Nutual Financial		Statement of Investments	19	Register
Services Fund	6	Financial Statements	28	Account
Performance Summary	12	Notes to Financial		Tax Info
our Fund's Expenses		Statements	32	Board M
our runu s Expenses	17			Shareho

Report of Independent Registered Public	
Accounting Firm	50
Tax Information	51
Board Members and Officers	53
Shareholder Information	58

Shareholder Letter

Average Annual Total Return

Class Z	12/31/13
1-Year	+25.67%
5-Year	+12.13%
10-Year	+4.36%

Performance data represent past performance, which does not guarantee future results.

Investment return and principal value will fluctuate, and you may have a gain or loss when you sell your shares. Current performance may differ from figures shown.

Please visit franklintempleton.com or call (800) 342-5236 for most recent month-end performance.

Dear Mutual Financial Services Fund Shareholder:

In 2013, most major equity markets ended significantly higher, led by Japan and the U.S. Optimism about global growth appeared to overcome concerns about Federal Reserve Board (Fed) tapering, European peripheral fiscal problems, China's new emphasis on consumption and most other major potentially negative developments. Highlighting the breadth of the advance, nearly every industry in the Standard & Poor's® 500 Index (S&P 500®) rose by double digits for the first time in nearly 20 years, and the index posted a one-year total return of +32.39%.¹ Emerging markets were the exception to the strong upward moves. For Mutual Financial Services Fund, 2013 was strong in absolute terms, and Class Z shares returned +25.67% with belowmarket volatility. Given our value investing strategy in a significant bull market, combined with a dearth of opportunities in traditional distressed and merger arbitrage activity, modest underperformance relative to the broad market index was a typical result.

The U.S. economy and market made strong progress, with the market perhaps the stronger of the two. Economic growth has been slowly accelerating and unemployment dropping. The recovery's strength is somewhat more impressive considering that growth came despite far-reaching federal spending cuts in 2013. On the other hand, some point out that the suppression of interest rates resulting from the Fed's ongoing quantitative easing (QE) program artificially stimulated the economy and equity markets. Toward year-end, fixed income markets started to price in the long-awaited taper of QE but without any negative impact on stocks.

1. Source: © 2014 Morningstar. All Rights Reserved. The information contained herein: (1) is proprietary to Morningstar and/or its content providers; (2) may not be copied or distributed; and (3) 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. STANDARD & POOR'S®, S&P® and S&P 500® are registered trademarks of Standard & Poor's Financial Services LLC. The index is unmanaged and includes reinvested dividends. One cannot invest directly in an index, and an index is not representative of the Fund's portfolio.

NOT FDIC INSURED | MAY LOSE VALUE | NO BANK GUARANTEE

Now that the S&P 500 finished its best year in well over a decade and doubled over the past five years since the heart of the global financial crisis, where are we?

So five years on, U.S. equity markets reached new highs and the U.S. recovery appeared to be real as extraordinary fiscal and monetary measures fade. Investments in U.S. equities remained attractive, but new opportunities became harder for us to find. In part this was because markets anticipated future growth, or perhaps became less fearful about another recession. In 2013, earnings for the S&P 500 rose by just 4%, but the prices investors were willing to pay for those earnings, expressed as a price-to-earnings multiple, rose by 23% the average price-to-earnings multiple on current year earnings rose from 14.2 times to 17.4 times over the course of the year. We do not think this price rise signaled a new U.S. stock market bubble, and we continued to hold many attractively valued U.S. companies, but we found more new opportunities outside the U.S. in markets that have lagged the U.S. stock market rise.

Europe's past five years were much rockier than those of the U.S. Initially Europe began to recover much like the U.S., but an intra-Europe crisis over the euro and the still-incomplete European integration stalled the recovery. These concerns peaked in 2011 and only faded once the European Central Bank committed to unlimited support of the euro. This commitment triggered a resumption of the natural process of economic recovery. This past year was good for Europe, but European markets remained below 2007 highs and have lagged those of the U.S. As was the case with U.S. markets, stock market advances in 2013 were more a reflection of price-earnings multiple expansion than actual earnings growth — stocks appreciated almost 20% while underlying earnings were up less than 1%, as measured by the MSCI Pan-Euro Index.² Most of our funds invest globally, and their exposure to Europe and the euro crisis has hindered returns over the past five years. We continue to believe the euro crisis is fading, Europe's recovery is gaining momentum and our investments in Europe can yield benefits for our shareholders.

The diverse Asian economies and markets told different stories in 2013. China entered 2013 with a new leader amid a peaceful and orderly transition of power. The new administration continued to focus on rebalancing the Chinese economy away from excessive investment toward consumption. China's massive stimulus program helped its economy power through the global downturn.

^{2.} Source: Bloomberg LP. The MSCI Pan-Euro Index captures large cap representation across 15 developed markets (DM) countries in Europe. With 199 constituents, the index covers a major portion of the free float-adjusted market capitalization across the European DM equity universe. DM countries in Europe include: Austria, Belgium, Denmark, Finland, France, Germany, Ireland, Italy, the Netherlands, Norway, Portugal, Spain, Sweden, Switzerland and the U.K.

Now the country needs to reallocate resources in a way that discourages speculative investment (and corruption) and allows China to grow without as much dependency on the health of trade partners. As a result, China's role as the engine of global growth may be fading, and firms that prospered by supplying China with the materials used for the past 10 years' massive investments could face significant headwinds.

The Japanese stock market was the 2013 global leader in local currency returns as Japan continued to struggle with the deflationary pressures that began when the Nikkei Index collapsed 24 years ago. Prime Minister Shinzō Abe pursued aggressive financial policies, including market reform and ambitious new monetary experiments. The result was an almost 60% rise in the Nikkei Index and a 20% drop in the value of the ven relative to the U.S. dollar. Whether the policies and the monetary stimulus can generate real economic growth remains to be seen.

The diverse opportunities available in Asia have been a modest portion of most of the Mutual Series portfolios, including the Fund's, but we continued to spend considerable time and effort on this region. The underperformance of many Asian markets could help us find attractive opportunities that offer a sufficient margin of safety and material upside potential for us.

The Fund's notable new investments in 2013 included European insurers Delta Lloyd and UNIQA Insurance Group.3

Aviva, a large U.K.-based insurer, was negatively affected by the euro crisis and subsequent drop in interest rates and needed to raise capital in early 2013. It did this through the secondary offering of its 20% ownership in Delta Lloyd, a Dutch insurer. This forced sale gave us the opportunity to invest in Delta Lloyd at a price we considered attractive. Delta Lloyd was not a well-understood company, with a history of volatile earnings driven by changes in interest rates and equity values. Management recognized this problem and instituted a hedging program to dampen the volatility of earnings and capital. We anticipated that this hedging program would be viewed positively as the financial results became less volatile. Additionally, the company's book value was understated by conservative discounting of insurance reserves in the Netherlands, which made comparisons with other European life insurers less meaningful. The increasing stability of earnings and understated book value combined with the company's significant market position in the Netherlands made Delta Lloyd an attractive investment opportunity for us.

^{3.} Mutual Financial Services Fund's holdings are based on total net assets as of 12/31/13: Delta Lloyd 1.8% and UNIQA Insurance Group 1.7%.

UNIQA is a diversified insurance business based in Austria, with subsidiary operations in emerging European economies. The firm was formed in 1999 through consolidation in the Austrian insurance industry and had limited public float until 2013. UNIQA's poor performance through the credit crisis led to several capital calls on its majority shareholders. Over the past two years, the company strengthened its management team, reduced balance sheet risk and refocused its business. In 2013, the firm held a public rights offering, which presented an opportunity to invest in a company that had lost nearly half its market value since 2009 and traded at a discount to book value and just six times expected earnings. The revamped management team had a plan to increase cash flow through a combination of cost cutting, improved crossselling of its products and process efficiency gains. Additionally, UNIQA's strong market position in Austria would allow it to invest in its business in emerging Europe where insurance penetration is low and growth prospects are better than in the industrialized countries of Europe.

The Fund's distressed debt investing has been more limited lately, as globally low interest rates and easy credit have meant few bankruptcies and distressed opportunities. Although the Fund made a material investment in the Lehman bankruptcy in the first half of the year, the second half yielded few new opportunities. Economic growth, Fed tapering and ample liquidity suggested to us a continuation of this environment in 2014.

Merger arbitrage was a very small part of the Fund's activities in 2013. Few major mergers were announced, and globally depressed short-dated interest rates led to anemic returns available from the few potential arbitrage positions. The fundamentals for acquisitions remained strong, with potential buyers having ample cash and credit, and market reaction (from the acquirer's perspective) to many of the announced deals was quite positive, unlike the negative market reaction we typically see. Nevertheless, the expected wave of activity, particularly from private equity firms, has yet to materialize. When attractive arbitrage opportunities appear, we will be ready.

The past year was strong for equities in almost all markets. Despite market gains, significant questions remain about the future of the global economic recovery. We believe the Fed will proceed with a gradual withdrawal of monetary stimulus. Although the Bank of Japan has added liquidity to the global economy, this transition may have unexpected effects. Meanwhile, the normal forces of economic recovery appear to be making progress in the U.S. and Europe. In 2013, financial markets began to anticipate these improvements, but unexpected delays or setbacks could produce a significant market reaction. These different forces should continue to provide us with attractive opportunities to allocate capital and generate attractive long-term returns for our investors.

We thank you for your trust and your support.

Sincerely,

Peter A. Langerman

Chairman, President and Chief Executive Officer

Franklin Mutual Advisers, LLC

Peter A Langerman

The letter reflects our analysis, opinions and portfolio holdings as of December 31, 2013, the end of the reporting period. The way we implement our main investment strategies and the resulting portfolio holdings may change depending on factors such as market and economic conditions. These opinions may not be relied upon as investment advice or an offer for a particular security. The information is not a complete analysis of every aspect of any market, country, industry, security or the Fund. Statements of fact are from sources considered reliable, but the investment manager makes no representation or warranty as to their completeness or accuracy. Although historical performance is no guarantee of future results, these insights may help you understand our investment management philosophy.

Annual Report

Mutual Financial Services Fund

Your Fund's Goals and Main Investments: Mutual Financial Services Fund seeks capital appreciation, with income as a secondary goal, by investing at least 80% of its net assets in securities of financial services companies that the manager believes are available at market prices less than their intrinsic value. The Fund concentrates its investments in securities of issuers such as banks, savings and loan organizations, credit card companies, brokerage firms, finance companies, subprime lending institutions, investment advisors, investment companies and insurance companies.

Performance data represent past performance, which does not guarantee future results. Investment return and principal value will fluctuate, and you may have a gain or loss when you sell your shares. Current performance may differ from figures shown. Please visit franklintempleton.com or call (800) 342-5236 for most recent month-end performance.

This annual report for Mutual Financial Services Fund covers the fiscal year ended December 31, 2013.

Performance Overview

Mutual Financial Services Fund – Class Z posted a +25.67% cumulative total return for the 12 months under review. For comparison, the Fund's narrow benchmark, the Standard & Poor's 500 (S&P 500) Financials Index, which tracks financials stocks in the S&P 500 Index, generated a +35.63% total return.¹ For the same period, the Fund's broad benchmark, the S&P 500 Index, which is a broad measure of U.S. stock performance, posted a +32.39% total return.¹ You can find more of the Fund's performance data in the Performance Summary beginning on page 12.

Economic and Market Overview

The 12 months under review were characterized by reinvigorated policy support and an economic recovery in developed markets. However, differences in global economic trends corresponded with increasingly divergent monetary policies, and growth in emerging market economies tended to slow. The central banks of key developed markets generally reaffirmed their accommodative monetary stances while some emerging market counterparts tightened policy rates as they sought to control inflation and currency depreciation.

The dollar value, number of shares or principal amount, and names of all portfolio holdings are listed in the Fund's Statement of Investments (SOI). The SOI begins on page 23.

^{1.} Source: © 2014 Morningstar. All Rights Reserved. The information contained herein: (1) is proprietary to Morningstar and/or its content providers; (2) may not be copied or distributed; and (3) 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. The indexes are unmanaged and include reinvested dividends. One cannot invest directly in an index, and an index is not representative of the Fund's portfolio.

In the U.S., economic growth and employment trends generally exceeded expectations, underpinned by consumer and business spending and rising inventories. Historically low mortgage rates and improving sentiment aided the housing market recovery, evidenced by increased new and existing home sales, rising home prices, low inventories and multi-year lows in new foreclosures. The U.S. Federal Reserve Board (Fed) expanded its asset purchase program to \$85 billion per month from \$40 billion early in the year. After encouraging economic and employment reports, the Fed announced in December it would reduce its monthly bond purchases by \$10 billion beginning in January 2014; however, the Fed committed to keeping interest rates low. In October, the federal government temporarily shut down after Congress failed to authorize routine federal funding amid a disagreement over a new health care law. However, Congress subsequently agreed to fund the government through early 2014 and later passed a two-year budget deal that could ease automatic spending cuts and lower the risk of another shutdown.

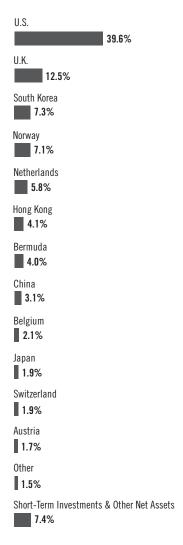
Outside the U.S., the eurozone emerged from its longest recession on record during 2013's second half and Japan's growth moderated. The European Central Bank reduced its key interest rate to a record low and pledged to maintain systemic support following political turmoil in Greece, Spain, Portugal and Italy. Germany's re-election of Chancellor Angela Merkel was largely perceived as a vote of support for ongoing eurozone reform measures. In Asia, the Bank of Japan set an explicit inflation target and pledged to double bond purchases in an unprecedented wave of policy reform. The U.S. dollar fell versus the euro but rose versus the Japanese ven in 2013.

Growth in many emerging markets moderated based on lower domestic demand, falling exports and weakening commodity prices. Political turmoil in certain emerging markets, the Fed's potential tapering of its asset purchase program and the Chinese central bank's effort to tighten liquidity to curb real estate and credit speculation led to a sell-off in emerging market equities and a sharp depreciation in regional currencies against the U.S. dollar. Central banks in Brazil, India and Indonesia raised interest rates in the second half of 2013 as they sought to curb inflation.

The stock market rally in developed markets accelerated during 2013 amid ongoing central bank commitments, continued corporate earnings strength and increasing signs of economic progress. Emerging market stocks rebounded toward period-end, although Latin American stocks trailed their emerging market peers. Oil prices rallied in the third quarter and rose for the year mainly owing to supply concerns related to geopolitical turmoil, but gold posted its largest annual price decline in more than three decades. Increasingly divergent economic and political circumstances during the period resulted in declining market correlations across regions and between asset classes, which many bottom-up investors perceived as more favorable.

Geographic Breakdown

Based on Total Net Assets as of 12/31/13



What is return on equity?

Return on equity is an amount, expressed as a percentage, earned on a company's common stock investment for a given period. Return on equity tells common shareholders how effectually their money is being employed. Comparing percentages for current and prior periods also reveals trends, and comparison with industry composites reveals how well a company is holding its own against its competitors.

What is meant by "hedge"?

To hedge a position is to seek to reduce the risk of adverse price movements in an asset. Normally, a hedge is implemented as an offsetting position in a related security, such as a currency forward contract.

What is a currency forward contract?

A currency forward contract, also called a "currency forward," is an agreement between the Fund and a counterparty to buy or sell a foreign currency at a specific exchange rate on a future date.

Investment Strategy

We strive to provide investors with superior risk-adjusted returns over time through our distinctive, value investment style, which includes investments in undervalued common stocks, distressed debt and risk arbitrage. Rigorous fundamental analysis drives our investment process. We attempt to determine each investment's intrinsic value as well as the price at which we would be willing to commit shareholder funds. While valuation remains our key consideration, we utilize numerous fundamental factors such as return on equity, financial leverage and long-term earnings power. We also consider factors such as management quality and competitive position. As always, our approach to investing is as much about assessing risk and containing losses as it is about achieving profits. In addition, it is our practice to hedge the Fund's currency exposure when we deem it advantageous for our shareholders.

Manager's Discussion

In an environment of generally rising equity prices, many Fund investments increased in value during the 12-month period. Three of the top contributors were insurers CNO Financial Group, Protector Forsikring and MetLife.

CNO Financial is a diversified life insurance company with a focus on serving the less affluent senior and middle-income U.S. markets. CNO stock performed well during the period as restructuring efforts led to an increase in profitability. CNO Financial completed a debt recapitalization plan, lowering its interest costs and improving its capital structure. Amid these efforts, CNO Financial generated significant cash flow, which was used to create shareholder value throughout the year through dividends, buybacks and a debt restructuring.

Norwegian insurer Protector Forsikring reported impressive growth in premiums and improved underwriting margins, which drove earnings forecasts higher and supported the stock's positive performance during the year. The company's strong Nordic franchise has allowed it to increase prices, resulting in improved underwriting margins and a higher return on equity. Strong operational performance, in our view, also contributed further stability to the firm's attractive dividend payment moving into 2014.

MetLife shares appreciated during the period under review owing to solid quarterly results and a dividend increase. In the first half of the year, the U.S.based life insurer reported better-than-expected earnings and an improvement in margins. In April, the company raised its quarterly dividend 49%, representing the company's first increase since 2007. Efforts to rationalize capital allocation policies by shifting from capital-intensive to more capital-efficient businesses drove operational results while diversifying the company's risk

profile. At period-end, the company's balance sheet remained strong and significant excess capital presented the potential for increased returns to shareholders, in our view.

During the period under review, some of the Fund's investments negatively affected performance. These included U.K.-headquartered RSA Insurance Group, U.S. bank holding company Bond Street Holdings and U.K.-based F&C Asset Management.

After cutting its dividend early in 2013, RSA Insurance Group suffered substantial weather-related losses, which precluded the company from achieving its annual return on equity target. RSA's share price came under additional pressure in November when the company announced it would suspend the chief executive officer, chief financial officer and claims director of its Irish unit amid an investigation into aggressive reserve accounting practices.

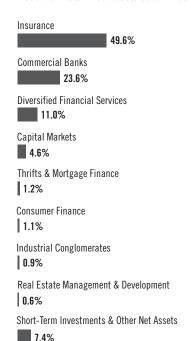
Although our investment in Bond Street Holdings declined in value for the period, the group reported positive operating results during the year, led by solid loan growth in its portfolio of Floridian community and commercial banks. However, its net interest margin (NIM) came under pressure as the persistently low interest rate environment meant new loans came in at lower yields while older, higher yielding loans have gradually run off the balance sheet. NIM is a profitability measure relating the difference between interest income earned on a bank's assets and interest paid on its liabilities. The Miami-based holding company has been able to reduce costs, primarily in integration, professional and credit-related expenses and at period-end, we believed the company continued to make progress toward reaching a healthy level of profitability.

F&C Asset Management was under pressure in 2013 as investor focus shifted away from its ongoing corporate restructuring toward management's ability to retain key institutional asset management mandates that are up for renewal over the next few years. Investors wanted to see further evidence that the company's organic asset gathering efforts can be successful. Although redemptions will hurt future revenues and create some uncertainty regarding F&C's prospects, the amount of outflows by key institutional customers has so far been modest, in our view. In addition, at period-end, we believed F&C's organic asset gathering prospects were gaining positive momentum.

During the year, the Fund held currency forwards and futures to hedge a portion of the currency risk of the portfolio's non-U.S. dollar investments. The hedges had a positive impact on the Fund's performance during the period.

Portfolio Breakdown

Based on Total Net Assets as of 12/31/13



What is a futures contract?

A futures contract, also called a "future," is an agreement between the Fund and a counterparty made through a U.S. or foreign futures exchange to buy or sell an asset at a specific price on a future date.

Top 10 Equity Holdings 12/31/13

Company Sector/Industry, Country	% of Total Net Assets
ACE Ltd. Insurance, U.S.	3.3%
Protector Forsikring ASA <i>Insurance, Norway</i>	3.3%
PartnerRe Ltd. <i>Insurance, Bermuda</i>	2.7%
CNO Financial Group Inc. Insurance, U.S.	2.7%
ING Groep NV, IDR Diversified Financial Services, Netherla	2.6% ands
Resolution Ltd. <i>Insurance, U.K.</i>	2.6%
Catlin Group Ltd. Insurance, U.K.	2.5%
Hana Financial Group Inc. Commercial Banks, South Korea	2.3%
MetLife Inc. <i>Insurance, U.S.</i>	2.2%
Oslo Bors VPS Holding ASA Diversified Financial Services, North	2.1% way

Thank you for your continued participation in Mutual Financial Services Fund. We look forward to continuing to serve your investment needs.





Andrew Sleeman, CFA Portfolio Manager



Richard Cetlin Assistant Portfolio Manager



Anohen B Dunhaupt

Andrew B. Dinnhaupt, CFA Assistant Portfolio Manager

Mutual Financial Services Fund

CFA® is a trademark owned by CFA Institute.

The foregoing information reflects our analysis, opinions and portfolio holdings as of December 31, 2013, the end of the reporting period. The way we implement our main investment strategies and the resulting portfolio holdings may change depending on factors such as market and economic conditions. These opinions may not be relied upon as investment advice or an offer for a particular security. The information is not a complete analysis of every aspect of any market, country, industry, security or the Fund. Statements of fact are from sources considered reliable, but the investment manager makes no representation or warranty as to their completeness or accuracy. Although historical performance is no guarantee of future results, these insights may help you understand our investment management philosophy.

Andrew Sleeman has been portfolio manager for Mutual Financial Services Fund since 2009. He has also been a co-portfolio manager for Mutual International Fund since 2009. Mr. Sleeman joined Franklin Templeton Investments in 2007. Previously, he was with Fox-Pitt, Kelton, a financials specialist firm, where he focused on international financial equities. Prior to that, he worked in international equities at BNP Paribas. Mr. Sleeman also worked in Australia in the fixed income division of JP Morgan Investment Management.

Richard Cetlin has been assistant portfolio manager for Mutual Financial Services Fund since 2010 with primary coverage of European banks. Prior to joining Franklin Templeton Investments in 2010, Mr. Cetlin was a consultant for Asian Century Quest, a hedge fund focused on the Asia-Pacific region. In this role, he focused on the analysis of banking, insurance and real estate stocks in China and banking stocks in Hong Kong and South Korea. Prior to that, Mr. Cetlin worked for 14 years at AllianceBernstein where he was a senior vice president and senior analyst for U.S. banking and specialty finance.

Andrew Dinnhaupt assumed assistant portfolio manager responsibilities for Mutual Financial Services Fund in December 2013 and has been an analyst for Franklin Mutual Advisers since 2011, specializing in the global insurance industry. Previously, Mr. Dinnhaupt was a portfolio manager and senior analyst covering the global financial services sector for RBC Capital Markets. Prior to RBC, Mr. Dinnhaupt worked at several hedge funds where he was responsible for analyzing and managing portfolios in the financial services sector. Before that, he worked at Mitchell Hutchins Asset Management where he covered the financial services industry and managed the PaineWebber Financial Services Fund.

Performance Summary as of 12/31/13

Your dividend income will vary depending on dividends or interest paid by securities in the Fund's portfolio, adjusted for operating expenses of each class. Capital gain distributions are net profits realized from the sale of portfolio securities. The performance table and graphs do not reflect any taxes that a shareholder would pay on Fund dividends, capital gain distributions, if any, or any realized gains on the sale of Fund shares. Total return reflects reinvestment of the Fund's dividends and capital gain distributions, if any, and any unrealized gains or losses.

Price and Distribution Information

Class Z (Symbol: TEFAX)		Change	12/31/13	12/31/12
Net Asset Value (NAV)		+\$3.31	\$16.90	\$13.59
Distributions (1/1/13-12/31/13)				
Dividend Income	\$0.1748			
Class A (Symbol: TFSIX)		Change	12/31/13	12/31/12
Net Asset Value (NAV)		+\$3.32	\$16.96	\$13.64
Distributions (1/1/13–12/31/13)				
Dividend Income	\$0.1300			
Class C (Symbol: TMFSX)		Change	12/31/13	12/31/12
Net Asset Value (NAV)		+\$3.31	\$16.92	\$13.61
Distributions (1/1/13–12/31/13)				
Dividend Income	\$0.0225			
Class R6 (Symbol: n/a)		Change	12/31/13	5/1/13
Net Asset Value (NAV)		+\$1.99	\$16.88	\$14.89
Distributions (5/1/13-12/31/13)				
Dividend Income	\$0.2072			

Performance

Cumulative total return excludes sales charges. Aggregate and average annual total returns and value of \$10,000 investment include maximum sales charges. Class Z/R6: no sales charges; Class A: 5.75% maximum initial sales charge; Class C: 1% contingent deferred sales charge in first year only.

Class Z		1-Year	5-Year	10-Year
Cumulative Total Return ¹		+25.67%	+77.26%	+53.21%
Average Annual Total Return ²		+25.67%	+12.13%	+4.36%
Value of \$10,000 Investment ³		\$12,567	\$17,726	\$15,321
Total Annual Operating Expenses ⁴	1.24%			
Class A		1-Year	5-Year	10-Year
Cumulative Total Return ¹		+25.32%	+74.64%	+48.64%
Average Annual Total Return ²		+18.13%	+10.48%	+3.43%
Value of \$10,000 Investment ³		\$11,813	\$16,461	\$14,006
Total Annual Operating Expenses ⁴	1.54%			
Class C		1-Year	5-Year	10-Year
Cumulative Total Return ¹		+24.50%	+68.53%	+38.70%
Average Annual Total Return ²		+23.50%	+11.00%	+3.33%
Value of \$10,000 Investment ³		\$12,350	\$16,853	\$13,870
Total Annual Operating Expenses ⁴	2.24%			
Class R6				Inception (5/1/13)
Cumulative Total Return ¹				+14.86%
Aggregate Total Return ⁵				+14.86%
Value of \$10,000 Investment ³				\$11,486
Total Annual Operating Expenses ⁴	0.99%			

Performance data represent past performance, which does not guarantee future results. Investment return and principal value will fluctuate, and you may have a gain or loss when you sell your shares. Current performance may differ from figures shown. For most recent month-end performance, go to franklintempleton.com or call (800) 342-5236.

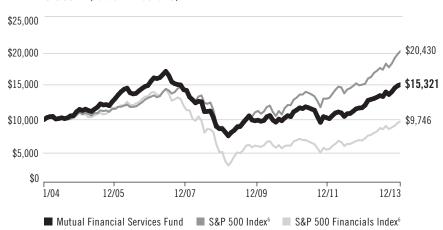
Total Return Index Comparison for a Hypothetical \$10,000 Investment

Total return represents the change in value of an investment over the periods shown. It includes any applicable maximum sales charge, Fund expenses, account fees and reinvested distributions. The unmanaged indexes include reinvestment of any income or distributions. They differ from the Fund in composition and do not pay management fees or expenses. One cannot invest directly in an index.

Average Annual Total Return

Class Z	12/31/13
1-Year	+25.67%
5-Year	+12.13%
10-Year	+4.36%

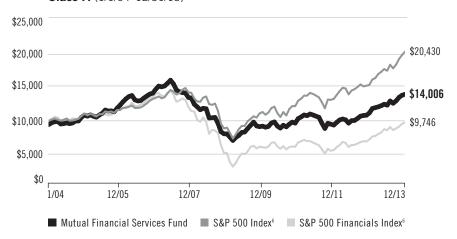
Class Z (1/1/04–12/31/13)



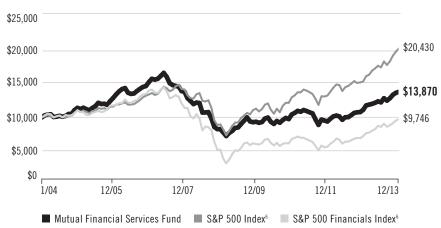
Average Annual Total Return

Class A	12/31/13
1-Year	+18.13%
5-Year	+10.48%
10-Year	+3.43%

Class A (1/1/04-12/31/13)



Class C (1/1/04–12/31/13)



Average Annual Total Return

Class C	12/31/13
1-Year	+23.50%
5-Year	+11.00%
10-Year	+3.33%

Class R6 (5/1/13-12/31/13)



Aggregate Total Return⁵

Class R6	12/31/13
Since Inception (5/1/13)	+14.86%

\$5,000			
	5/13		12/13
	■ Mutual Financial Services Fund	S&P 500 Index ⁶	S&P 500 Financials Index

Endnotes

All investments involve risks, including possible loss of principal. Value securities may not increase in price as anticipated or may decline further in value. Investing in a single-sector fund involves special risks, including greater sensitivity to economic, political or regulatory developments impacting the sector. In addition, the Fund invests in foreign securities whose risks include currency fluctuations, and economic and political uncertainties. The Fund's investments in smaller company stocks carry an increased risk of price fluctuation, particularly over the short term. The Fund may also invest in companies engaged in mergers, reorganizations or liquidations, which involve special risks as pending deals may not be completed on time or on favorable terms, as well as lower rated bonds, which entail higher credit risk. The Fund is actively managed but there is no guarantee that the manager's investment decisions will produce the desired results. The Fund's prospectus also includes a description of the main investment risks.

- Shares are available to certain eligible investors as described in the prospectus.
- Class C: These shares have higher annual fees and expenses than Class A shares.
- Class R6: Shares are available to certain eligible investors as described in the prospectus.
- 1. Cumulative total return represents the change in value of an investment over the periods indicated.
- 2. Average annual total return represents the average annual change in value of an investment over the periods indicated.
- 3. These figures represent the value of a hypothetical \$10,000 investment in the Fund over the periods indicated.
- 4. Figures are as stated in the Fund's current prospectus. In periods of market volatility, assets may decline significantly, causing total annual Fund operating expenses to become higher than the figures shown.
- 5. Aggregate total return represents the change in value of an investment for the period indicated. Since Class R6 shares have existed for less than one year, average annual total return is not available.
- 6. Source: © 2014 Morningstar. The S&P 500 Index is a market capitalization-weighted index of 500 stocks designed to measure total U.S. equity market performance. The S&P 500 Financials Index is market capitalization weighted and consists of all financial stocks in the S&P 500 Index.

Your Fund's Expenses

As a Fund shareholder, you can incur two types of costs:

- Transaction costs, including sales charges (loads) on Fund purchases; and
- Ongoing Fund costs, including management fees, distribution and service (12b-1) fees, and other Fund expenses. All mutual funds have ongoing costs, sometimes referred to as operating expenses.

The following table shows ongoing costs of investing in the Fund and can help you understand these costs and compare them with those of other mutual funds. The table assumes a \$1,000 investment held for the six months indicated.

Actual Fund Expenses

The first line (Actual) for each share class listed in the table provides actual account values and expenses. The "Ending Account Value" is derived from the Fund's actual return, which includes the effect of Fund expenses.

You can estimate the expenses you paid during the period by following these steps. Of course, your account value and expenses will differ from those in this illustration:

- 1. Divide your account value by \$1,000. If an account had an \$8,600 value, then $$8,600 \div $1,000 = 8.6$.
- 2. Multiply the result by the number under the heading "Expenses Paid During Period." If Expenses Paid During Period were \$7.50, then $8.6 \times 7.50 = 64.50$.

In this illustration, the estimated expenses paid this period are \$64.50.

Hypothetical Example for Comparison with Other Funds

Information in the second line (Hypothetical) for each class in the table can help you compare ongoing costs of investing in the Fund with those of other mutual funds. This information may not be used to estimate the actual ending account balance or expenses you paid during the period. The hypothetical "Ending Account Value" is based on the actual expense ratio for each class and an assumed 5% annual rate of return before expenses, which does not represent the Fund's actual return. The figure under the heading "Expenses Paid During Period" shows the hypothetical expenses your account would have incurred under this scenario. You can compare this figure with the 5% hypothetical examples that appear in shareholder reports of other funds.

Your Fund's Expenses (continued)

Please note that expenses shown in the table are meant to highlight ongoing costs and do not reflect any transaction costs, such as sales charges. Therefore, the second line for each class is useful in comparing ongoing costs only, and will not help you compare total costs of owning different funds. In addition, if transaction costs were included, your total costs would have been higher. Please refer to the Fund prospectus for additional information on operating expenses.

Class Z	Beginning Account Value 7/1/13	Ending Account Value 12/31/13	Expenses Paid During Period* 7/1/13–12/31/13
Actual	\$1,000	\$1,134.80	\$ 6.13
Hypothetical (5% return before expenses)	\$1,000	\$1,019.46	\$ 5.80
Class A			
Actual	\$1,000	\$1,133.50	\$ 7.74
Hypothetical (5% return before expenses)	\$1,000	\$1,017.95	\$ 7.32
Class C			
Actual	\$1,000	\$1,129.60	\$11.49
Hypothetical (5% return before expenses)	\$1,000	\$1,014.42	\$10.87
Class R6			
Actual	\$1,000	\$1,135.60	\$ 5.17
Hypothetical (5% return before expenses)	\$1,000	\$1,020.37	\$ 4.89

^{*}Expenses are calculated using the most recent six-month expense ratio, annualized for each class (Z: 1.14%; A: 1.44%; C: 2.14%; and R6: 0.96%), multiplied by the average account value over the period, multiplied by 184/365 to reflect the one-half year period.

Financial Highlights

Class Z	2013	Year E	nded Decemb 2011	er 31, 2010	2009
Per share operating performance (for a share outstanding throughout the year)	2013	2012	2011	2010	2009
Net asset value, beginning of year	\$13.59	\$11.53	\$13.01	\$12.05	\$10.80
Income from investment operations ^a :					
Net investment income ^b	0.24	0.20	0.28	0.26	0.15c
Net realized and unrealized gains (losses)	3.24	2.09	(1.48)	1.27	1.44
Total from investment operations	3.48	2.29	(1.20)	1.53	1.59
Less distributions from net investment income	(0.17)	(0.23)	(0.28)	(0.57)	(0.34)
Net asset value, end of year	\$16.90	\$13.59	\$11.53	\$13.01	\$12.05
Total return	25.67%	19.98%	(9.26)%	12.84%	14.82%
Ratios to average net assets					
Expenses before expense reduction ^d	1.16%	1.24%	1.24%	1.28%	1.26%
Expenses net of expense reduction ^d	1.16%e	1.24%	1.24%	1.28%	1.25%
Expenses incurred in connection with securities sold short	—%	—%	—%	—%	—%f
Net investment income	1.51%	1.56%	2.22%	2.07%	1.24%℃
Supplemental data					
Net assets, end of year (000's)	\$105,279	\$86,519	\$80,105	\$97,487	\$99,610
Portfolio turnover rate	25.73%	12.65%	23.58%	35.37%	81.29%

^aThe amount shown for a share outstanding throughout the period may not correlate with the Statement of Operations for the period due to the timing of sales and repurchases of the Fund shares in relation to income earned and/or fluctuating market value of the investments of the Fund.

bBased on average daily shares outstanding.

Net investment income per share includes approximately \$(0.09) per share related to an adjustment for uncollectible interest. Excluding the effect of this adjustment, the ratio of net investment income to average net assets would have been 2.09%.

Includes dividend expense on securities sold short and borrowing fees, if any. See below for the ratios of such expenses to average net assets for the periods presented.

eBenefit of expense reduction rounds to less than 0.01%.

fRounds to less than 0.01%.

Financial Highlights (continued)

Class A	2013	Year 2012	Ended Decem 2011	ber 31, 2010	2009
Per share operating performance (for a share outstanding throughout the year)	2010	2012	2011	2010	2003
Net asset value, beginning of year	\$13.64	\$11.57	\$13.05	\$12.09	\$10.83
Income from investment operations ^a :					
Net investment income ^b	0.19	0.16	0.25	0.22	0.11c
Net realized and unrealized gains (losses)	3.26	2.10	(1.49)	1.27	1.46
Total from investment operations	3.45	2.26	(1.24)	1.49	1.57
Less distributions from net investment income	(0.13)	(0.19)	(0.24)	(0.53)	(0.31)
Net asset value, end of year	\$16.96	\$13.64	\$11.57	\$13.05	\$12.09
Total return ^d	25.32%	19.55%	(9.49)%	12.45%	14.53%
Ratios to average net assets					
Expenses before expense reductione	1.46%	1.54%	1.54%	1.58%	1.55%
Expenses net of expense reductione	1.46% ^f	1.54%	1.54%	1.58%	1.54%
Expenses incurred in connection with securities sold short	-%	—%	—%	—%	—%g
Net investment income	1.21%	1.26%	1.92%	1.77%	0.95%⁰
Supplemental data					
Net assets, end of year (000's)	\$240,529	\$184,681	\$173,167	\$226,172	\$245,251
Portfolio turnover rate	25.73%	12.65%	23.58%	35.37%	81.29%

^aThe amount shown for a share outstanding throughout the period may not correlate with the Statement of Operations for the period due to the timing of sales and repurchases of the Fund shares in relation to income earned and/or fluctuating market value of the investments of the Fund.

bBased on average daily shares outstanding.

Net investment income per share includes approximately \$(0.09) per share related to an adjustment for uncollectible interest. Excluding the effect of this adjustment, the ratio of net investment income to average net assets would have been 1.80%.

dTotal return does not reflect sales commissions or contingent deferred sales charges, if applicable.

elncludes dividend expense on securities sold short and borrowing fees, if any. See below for the ratios of such expenses to average net assets for the periods presented.

^fBenefit of expense reduction rounds to less than 0.01%.

gRounds to less than 0.01%.

Financial Highlights (continued)

Class C	2013	Year E 2012	Ended Decemb 2011	er 31, 2010	2009
Per share operating performance (for a share outstanding throughout the year)					
Net asset value, beginning of year	\$13.61	\$11.55	\$13.01	\$12.05	\$10.80
Income from investment operations ^a :					
Net investment income ^b	0.08	0.07	0.16	0.13	0.03c
Net realized and unrealized gains (losses)	3.25	2.08	(1.48)	1.26	1.44
Total from investment operations	3.33	2.15	(1.32)	1.39	1.47
Less distributions from net investment income	(0.02)	(0.09)	(0.14)	(0.43)	(0.22)
Net asset value, end of year	\$16.92	\$13.61	\$11.55	\$13.01	\$12.05
Total return ^d	24.50%	18.67%	(10.13)%	11.69%	13.64%
Ratios to average net assets					
Expenses before expense reductione	2.16%	2.24%	2.24%	2.28%	2.26%
Expenses net of expense reduction ^e	2.16% ^f	2.24%	2.24%	2.28%	2.25%
Expenses incurred in connection with securities sold short	—%	%	-%	%	—% ^g
Net investment income	0.51%	0.56%	1.22%	1.07%	0.24%⁰
Supplemental data					
Net assets, end of year (000's)	\$86,370	\$69,046	\$68,324	\$89,989	\$97,404
Portfolio turnover rate	25.73%	12.65%	23.58%	35.37%	81.29%

aThe amount shown for a share outstanding throughout the period may not correlate with the Statement of Operations for the period due to the timing of sales and repurchases of the Fund shares in relation to income earned and/or fluctuating market value of the investments of the Fund.

bBased on average daily shares outstanding.

Net investment income per share includes approximately \$(0.09) per share related to an adjustment for uncollectible interest. Excluding the effect of this adjustment, the ratio of net investment income to average net assets would have been 1.09%.

dTotal return does not reflect sales commissions or contingent deferred sales charges, if applicable.

elncludes dividend expense on securities sold short and borrowing fees, if any. See below for the ratios of such expenses to average net assets for the periods presented.

^fBenefit of expense reduction rounds to less than 0.01%.

gRounds to less than 0.01%.

Financial Highlights (continued)

Class R6	Period Ended December 31, 2013 ^a
Per share operating performance	2010
(for a share outstanding throughout the period)	
Net asset value, beginning of period	\$14.89
Income from investment operations ^b :	
Net investment income ^c	0.13
Net realized and unrealized gains (losses)	2.07
Total from investment operations	2.20
Less distributions from net investment income	(0.21)
Net asset value, end of period	\$16.88
Total return ^d	14.86%
Ratios to average net assets ^e	
Expenses before waiver, payment by affiliates and expense reduction	2.18%
Expenses net of waiver, payment by affiliates and expense reduction	0.97% ^f
Net investment income	1.70%
Supplemental data	
Net assets, end of period (000's)	\$6
Portfolio turnover rate	25.73%

^aFor the May 1, 2013 (effective date) to December 31, 2013.

bThe amount shown for a share outstanding throughout the period may not correlate with the Statement of Operations for the period due to the timing of sales and repurchases of the Fund shares in relation to income earned and/or fluctuating market value of the investments of the Fund.

cBased on average daily shares outstanding.

dTotal return is not annualized for periods less than one year.

 $^{{}^{\}mathrm{e}}\mathrm{Ratios}$ are annualized for periods less than one year.

¹Benefit of expense reduction rounds to less than 0.01%.

Statement of Investments, December 31, 2013

	Country	Shares/Units/Warrants	Value
Common Stocks and Other Equity Interests 90.3%			
Capital Markets 3.8%			
a,b Acquisition 1234 PLC	United Kingdom	18,057	\$ 19,734
^a China Cinda Asset Management Co. Ltd., H	China	195,507	121,525
China Everbright Ltd	Hong Kong	3,014,000	4,773,053
F&C Asset Management PLC	United Kingdom	1,163,275	1,769,276
Morgan Stanley	United States	184,390	5,782,470
Sun Hung Kai & Co. Ltd	Hong Kong	7,457,704	4,154,737
			16,620,795
Commercial Banks 23.5%			
AB&T Financial Corp.	United States	226,100	122,094
Aozora Bank Ltd	Japan	2,950,341	8,349,493
^{1,d} The Bankshares Inc.	United States	456,903	2,178,966
Barclays PLC	United Kingdom	888,492	4,000,339
BB&T Corp.	United States	85,130	3,177,052
e Bond Street Holdings LLC, A, 144A	United States	286,469	4,297,035
^a Capital Bank Financial Corp., A	United States	42,649	970,265
Re Capital Bank Financial Corp., B, 144A, non-voting	United States	153,021	3,481,228
CIT Group Inc.	United States	138,480	7,218,962
Columbia Banking System Inc.	United States	178,332	4,905,913
dColumbia Banking System Inc., wts., C, 10/23/16	United States	8,117	1,535,525
d First Southern Bancorp Inc.	United States	110,792	534,040
Guaranty Bancorp	United States	266,761	3,747,992
Hana Financial Group Inc.	South Korea	243,313	10,117,636
HSBC Holdings PLC	United Kingdom	561,180	6,154,940
KB Financial Group Inc.	South Korea	178,863	7,158,078
PNC Financial Services Group Inc	United States	78,520	6,091,582
Southern National Bancorp of Virginia Inc.	United States	547,560	5,481,076
State Bank Financial Corp.	United States	137,860	2,507,673
SunTrust Banks Inc.	United States	209,110	7,697,339
Wells Fargo & Co.	United States	186,280	8,457,112
Woori Finance Holdings Co. Ltd	South Korea	262,880	3,311,756
	000000000	202,000	101,496,096
Consumer Finance 1.1%			
^a Comdisco Holding Co. Inc.	United States	103	556
Samsung Card Co. Ltd.	South Korea	130,850	4,635,477
		,	4,636,033
Diversified Financial Services 9.6%			
Citigroup Inc.	United States	65,609	3,418,885
Deutsche Boerse AG	Germany	33,107	2,741,428
First Pacific Co. Ltd.	Hong Kong	7,714,902	8,775,131
a ING Groep NV, IDR	Netherlands	802,283	11,145,756
JPMorgan Chase & Co.	United States	108,420	6,340,402
Oslo Bors VPS Holding ASA	Norway	911,000	9,162,421
55.5 5.5 TO TOTALING NO.	Horway	311,000	41,584,023
Industrial Conglomerates 0.9%			
Shanghai Industrial Holdings Ltd.	China	1,039,000	3,805,296
		, -,	

Statement of Investments, December 31, 2013 (continued)

	Country	Shares/Units/Warrants	Value
Common Stocks and Other Equity Interests (continued) Insurance 49.6%			
ACE Ltd.	United States	139,770	\$ 14,470,388
Aegon NV	Netherlands	637,658	6,018,650
Ageas	Belgium	208,183	8,862,709
^a Alleghany Corp	United States	12,747	5,098,290
American International Group Inc	United States	154,888	7,907,032
Argo Group International Holdings Ltd	United States	105,712	4,914,551
Catlin Group Ltd	United Kingdom	1,109,668	10,671,277
China Pacific Insurance (Group) Co. Ltd., H	China	1,561,940	6,123,399
CNO Financial Group Inc	United States	654,910	11,585,358
Delta Lloyd NV	Netherlands	318,343	7,899,369
Direct Line Insurance Group PLC	United Kingdom	2,119,159	8,756,998
^a Enstar Group Ltd	United States	65,199	9,056,793
^{a,d} Imagine Group Holdings Ltd	Bermuda	68,631	501,418
Korean Reinsurance Co	South Korea	600,118	6,508,656
Lancashire Holdings Ltd	United Kingdom	431,280	5,786,454
Maiden Holdings Ltd.	United States	496,740	5,429,368
MetLife Inc.	United States	177,140	9,551,389
^{a,d} Olympus Re Holdings Ltd	United States	7,480	
PartnerRe Ltd.	Bermuda	112,420	11,852,441
PICC Property and Casualty Co. Ltd., H	China	2,116,029	3,138,153
° Protector Forsikring ASA	Norway	4,479,410	14,180,256
RenaissanceRe Holdings Ltd	United States	42,200	4,107,748
Resolution Ltd	United Kingdom	1,898,597	11,124,643
RSA Insurance Group PLC	United Kingdom	3,892,653	5,896,336
^a Storebrand ASA	Norway	1,200,174	7,499,727
UNIQA Insurance Group AG	Austria	564,365	7,203,139
Validus Holdings Ltd.	Bermuda	119,914	4,831,335
White Mountains Insurance Group Ltd	United States	12,068	7,277,969
Zurich Insurance Group AG	Switzerland	28,050	8,128,384
·			214,382,230
Pool Estate Management 9 Development 0 69/			
Real Estate Management & Development 0.6%	Virgin Islands (British)	2.070.650	2,586,537
Dolphin Capital Investors Ltd	VIIGIII ISIAIIUS (DIILISII)	3,979,650	2,366,337
Thrifts & Mortgage Finance 1.2%			
Cape Bancorp Inc	United States	264,663	2,688,976
Westfield Financial Inc	United States	319,620	2,384,365
			5,073,341
Total Common Stocks and Other Equity Interests			
(Cost \$306,650,783)			390,184,351
Convertible Preferred Stocks 0.1%			
Commercial Banks 0.1%			
Columbia Banking System Inc., cvt. pfd., B	United States	1,224	392,483
^{a,d} First Southern Bancorp Inc., cvt. pfd., C	United States	190	354,700
Total Convertible Preferred Stocks			
(Cost \$312,400)			747,183
(==== +=== , -==,			. 17,100

Statement of Investments, December 31, 2013 (continued)

	Country	Shares/Units/Warrants	Value
Preferred Stocks 1.1%			
Diversified Financial Services 1.1%			
a,d Hightower Holding LLC, pfd., A	United States	3,000,000	\$ 2,859,000
^{a,d} Hightower Holding LLC, pfd., A, Series 2	United States	968,000	1,841,233
Total Preferred Stocks (Cost \$4,782,324)			4,700,233
		Principal Amount*	
Corporate Bonds (Cost \$1,158,755) 0.3%			
e,f Baggot Securities Ltd., secured bond, 144A, 10.24%, Perpetual	Ireland	816,000 EUR	1,185,824
		Shares	
Companies in Liquidation 0.8%			
^{a,d} FIM Coinvestor Holdings I, LLC	United States	4,357,178	_
^{a,g} Lehman Brothers Holdings Inc., Bankruptcy Claim	United States	7,766,103	3,494,746
Total Companies in Liquidation (Cost \$3,483,802)			3,494,746
Total Investments before Short Term Investments			
(Cost \$316,388,064)			400,312,337
		Principal Amount*	
Short Term Investments 7.2%			
U.S. Government and Agency Securities 7.2%			
^h U.S. Treasury Bills,			
1/02/14	United States	12,100,000	12,100,000
1/09/14 - 4/24/14	United States	13,000,000	12,998,821
6/26/14	United States	6,000,000	5,997,666
Total U.S. Government and Agency Securities			
(Cost \$31,096,035)			31,096,487
Total Investments (Cost \$347,484,099) 99.8%			431,408,824
Other Assets, less Liabilities 0.2%			774,895
Net Assets 100.0%			\$432,183,719

^{*}The principal amount is stated in U.S. dollars unless otherwise indicated.

^aNon-income producing.

bSecurity has been deemed illiquid because it may not be able to be sold within seven days. At December 31, 2013, the value of this security was \$19,734, representing less than 0.01% of net assets.

[°]See Note 10 regarding holdings of 5% voting securities.

^dSee Note 8 regarding restricted securities.

eSecurity was purchased pursuant to Rule 144A under the Securities Act of 1933 and may be sold in transactions exempt from registration only to qualified institutional buyers or in a public offering registered under the Securities Act of 1933. These securities have been deemed liquid under guidelines approved by the Trust's Board of Trustees. At December 31, 2013, the aggregate value of these securities was \$8,964,087, representing 2.07% of net assets.

fPerpetual security with no stated maturity date.

Bankruptcy claims represent the right to receive distributions, if any, during the liquidation of the underlying pool of assets. Shares represent amount of allowed unsecured claims. ^hThe security is traded on a discount basis with no stated coupon rate.

Security or a portion of the security has been pledged as collateral for open futures and forward contracts. At December 31, 2013, the aggregate value of these securities and/or cash pledged as collateral was \$3,557,045, representing 0.82% of net assets.

Statement of Investments, December 31, 2013 (continued)

At December 31, 2013, the Fund had the following futures contracts outstanding. See Note 1(c).

Futures Contracts

Description	Туре	Number of Contracts	Notional Value	Expiration Date	ealized eciation	Unrealized Depreciation
Currency Contracts						
EUR/USD	Short	47	\$8,100,450	3/17/14	\$ _	\$ (34,571)
GBP/USD	Short	93	9,624,338	3/17/14	_	(89,156)
Unrealized appreciation (depreciation)					_	(123,727)
Net unrealized appreciation (depreciation)						\$(123,727)

At December 31, 2013, the Fund had the following forward exchange contracts outstanding. See Note 1(c).

Forward Exchange Contracts

Currency	Counterparty ^a	Туре	Quantity	Contract Amount	Settlement Date	Unrealized Appreciation	Unrealized Depreciation
Euro	BANT	Sell	2,082,256	\$ 2,720,363	1/17/14	\$ —	\$ (143,756)
Euro	BBU	Sell	2,082,272	2,719,156	1/17/14	_	(144,986)
Euro	FBCO	Sell	239,515	320,125	1/17/14	_	(9,325)
Euro	DBFX	Sell	131,394	173,450	1/17/14	_	(7,282)
Euro	SCBT	Sell	63,611	84,360	1/17/14	_	(3,135)
British Pound	BANT	Sell	2,981,970	4,540,279	1/21/14	_	(396,869)
British Pound	FBCO	Sell	1,004,216	1,606,055	1/21/14	_	(56,591)
British Pound	DBFX	Sell	1,575,519	2,391,795	1/21/14	_	(216,739)
British Pound	HSBC	Sell	142,796	229,079	1/21/14	_	(7,343)
British Pound	SCBT	Sell	37,518	59,882	1/21/14	_	(2,236)
British Pound	SSBT	Sell	940,000	1,517,329	1/21/14	_	(38,997)
Japanese Yen	BONY	Buy	29,200,000	299,038	1/22/14	_	(21,704)
Japanese Yen	FBCO	Buy	58,946,490	601,409	1/22/14	_	(41,551)
Japanese Yen	DBFX	Buy	12,000,000	124,660	1/22/14	_	(10,687)
Japanese Yen	HSBC	Buy	29,599,765	300,667	1/22/14	_	(19,536)
Japanese Yen	BONY	Sell	38,300,000	385,859	1/22/14	22,096	_
Japanese Yen	FBCO	Sell	932,293,434	9,277,659	1/22/14	422,978	_
South Korean Won	BANT	Buy	766,773,929	716,933	2/12/14	7,289	_
South Korean Won	FBCO	Buy	703,434,120	655,699	2/12/14	8,698	_
South Korean Won	HSBC	Buy	2,492,813,398	2,295,135	2/12/14	60,251	(909)
Swiss Franc	BBU	Buy	67,560	73,381	2/12/14	2,382	_
Swiss Franc	FBCO	Buy	2,888,873	3,195,987	2/12/14	43,629	_
South Korean Won	BANT	Sell	6,024,622,910	5,365,014	2/12/14	_	(325,276)
Swiss Franc	BANT	Sell	2,765,865	3,013,707	2/12/14		(87,966)
South Korean Won	FBCO	Sell	14,155,766,283	12,658,937	2/12/14		(711,264)
Swiss Franc	FBCO	Sell	139,843	150,171	2/12/14		(6,650)
South Korean Won	DBFX	Sell	11,237,045,759	10,006,130	2/12/14		(607,322)
South Korean Won	HSBC	Sell	6,009,070,166	5,515,738	2/12/14	3,764	(163,626)
Swiss Franc	HSBC	Sell	16,827	17,962	2/12/14		(908)
Swiss Franc	SCBT	Sell	33,898	36,522	2/12/14		(1,492)
British Pound	BANT	Sell	4,174,249	6,487,873	2/19/14		(421,924)
British Pound	BBU	Sell	2,127,777	3,311,827	2/19/14		(210,365)
Euro	SCBT	Buy	823,379	1,128,038	2/28/14	4,519	_

Statement of Investments, December 31, 2013 (continued)

Forward Exchange Contracts (continued)

					Settlement	Unrealized	Unrealized
Currency	Counterpartya	Туре	Quantity	Contract Amount	Date	Appreciation	Depreciation
Euro	BANT	Sell	175,548	\$ 231,680	2/28/14	\$ —	\$ (9,786)
Euro	BONY	Sell	78,222	102,875	2/28/14	_	(4,719)
Euro	BBU	Sell	1,190,458	1,586,136	2/28/14	_	(51,338)
Euro	FBCO	Sell	4,692,559	6,350,868	2/28/14	_	(103,744)
Euro	HSBC	Sell	1,287,960	1,718,679	2/28/14	_	(52,909)
Euro	SCBT	Sell	48,757	64,764	2/28/14	_	(2,301)
Euro	BANT	Buy	121,607	167,242	4/16/14	99	(70)
Euro	BONY	Buy	65,978	90,793	4/16/14	_	(40)
Euro	BBU	Buy	30,753	42,274	4/16/14	27	_
Euro	HSBC	Buy	160,215	220,477	4/16/14	41	(143)
Euro	SCBT	Buy	121,572	167,048	4/16/14	231	(57)
Euro	SSBT	Buy	72,763	100,114	4/16/14	4	(32)
Euro	BANT	Sell	1,648,947	2,241,125	4/16/14	_	(26,999)
Euro	BBU	Sell	1,814,660	2,467,403	4/16/14	_	(28,660)
British Pound	BANT	Sell	2,148,823	3,478,289	4/22/14	_	(76,987)
British Pound	FBCO	Sell	1,707,959	2,753,230	4/22/14	_	(72,627)
British Pound	HSBC	Sell	105,914	174,657	4/22/14	_	(580)
British Pound	SCBT	Sell	2,988,927	4,818,150	4/22/14	_	(127,097)
Euro	BANT	Sell	7,291,010	9,811,241	5/15/14	_	(217,909)
Euro	BONY	Sell	400,000	541,696	5/19/14	_	(8,527)
Euro	SCBT	Sell	232,558	313,932	5/19/14	_	(5,964)
British Pound	BANT	Buy	2,106,559	3,458,392	5/21/14	26,113	_
British Pound	BBU	Buy	282,961	461,605	5/21/14	6,447	_
British Pound	HSBC	Buy	198,592	323,725	5/21/14	4,770	_
Norwegian Krone	BANT	Buy	1,374,782	222,439	5/21/14	3,050	_
Norwegian Krone	BONY	Buy	325,000	52,670	5/21/14	636	_
Norwegian Krone	BBU	Buy	5,318,900	854,740	5/21/14	17,653	_
Norwegian Krone	BANT	Sell	188,650,175	30,768,474	5/21/14	_	(173,517)
British Pound	BBU	Sell	4,056,465	6,520,970	5/21/14	_	(188,917)
British Pound	HSBC	Sell	2,863,841	4,605,056	5/21/14		(132,084)
Unrealized appreciation (dep	reciation)					634,677	(4,943,446)
Net unrealized appreciation	n (depreciation)						\$(4,308,769)

^aMay be comprised of multiple contracts using the same currency and settlement date.

See Abbreviations on page 49.

Financial Statements

Statement of Assets and Liabilities

December 31, 2013

Assets: Investments in securities:	
Cost - Unaffiliated issuers	\$ 335,208,177 12,275,922
Total cost of investments	\$ 347,484,099
Value - Unaffiliated issuers	\$ 417,106,474 14,302,350
Total value of investments	431,408,824
Cash	38,610 6,009,642
Capital shares sold	449,278
Dividends and interest	378,567
Unrealized appreciation on forward exchange contracts	634,677
Other assets	150,862
Total assets	439,070,460
Liabilities: Payables:	
Capital shares redeemed	1,058,407
Management fees	288,964
Administrative fees	27,524
Distribution fees	260,437
Transfer agent fees	133,464
Trustees' fees and expenses	22,791
Variation margin	18,513
Unrealized depreciation on forward exchange contracts	4,943,446
Accrued expenses and other liabilities	133,195
Total liabilities	6,886,741
Net assets, at value	\$ 432,183,719
Net assets consist of:	
Paid-in capital	\$ 562,611,056
Undistributed net investment income	1,155,140
Net unrealized appreciation (depreciation)	79,488,676
Accumulated net realized gain (loss)	(211,071,153)
Net assets, at value	\$ 432,183,719

Financial Statements (continued)

Statement of Assets and Liabilities (continued)

December 31, 2013

Class Z:	
Net assets, at value	\$ 105,279,196
Shares outstanding	6,230,577
Net asset value and maximum offering price per share	\$16.90
Class A:	
Net assets, at value	\$ 240,528,945
Shares outstanding	14,186,173
Net asset value per share ^a	\$16.96
Maximum offering price per share (net asset value per share ÷ 94.25%)	\$17.99
Class C:	
Net assets, at value	\$ 86,369,907
Shares outstanding	5,105,334
Net asset value and maximum offering price per share ^a	\$16.92
Class R6:	
Net assets, at value	\$ 5,671
Shares outstanding	336
Net asset value and maximum offering price per share	\$16.88

^aRedemption price is equal to net asset value less contingent deferred sales charges, if applicable.

Financial Statements (continued)

Statement of Operations

for the year ended December 31, 2013

Investment income:	
Dividends: (net of foreign taxes of \$741,191)	\$ 9,329,195
Unaffiliated issuers Non-controlled affiliated issuers (Note 10)	\$ 9,329,195 686,027
Interest	404,754
Income from securities loaned	85,529
	· · · · · · · · · · · · · · · · · · ·
Total investment income	10,505,505
Expenses:	2 1 4 2 5 2 4
Management fees (Note 3a)	3,142,524
Administrative fees (Note 3b)	299,545
Class A	645,477
Class B	470
Class C	786,074
Transfer agent fees: (Note 3e)	,
Class Z	198,349
Class A	437,246
Class B	102
Class C	158,782
Class R6	44
Custodian fees (Note 4)	34,390
Reports to shareholders	80,573
Registration and filing fees	74,195
Professional fees	106,872 10,626
Other	16,068
Total expenses Expense reductions (Note 4)	5,991,337 (219)
Expenses waived/paid by affiliates (Note 3f)	(43)
Net expenses	
·	5,991,075
Net investment income	4,514,430
Realized and unrealized gains (losses):	
Net realized gain (loss) from:	
Investments	10,024,642
Foreign currency transactions	1,025,499
Futures contracts	(470,825)
Net realized gain (loss)	10,579,316
Net change in unrealized appreciation (depreciation) on:	
Investments	73,855,058
Translation of other assets and liabilities denominated in foreign currencies	(1,982,190)
Net change in unrealized appreciation (depreciation)	71,872,868
Net realized and unrealized gain (loss)	82,452,184
Net increase (decrease) in net assets resulting from operations	\$86,966,614
- ·	

Financial Statements (continued)

Statements of Changes in Net Assets

	Year Ended December 31,				
	2013			2012	
Increase (decrease) in net assets:					
Operations:	.	-14400		4 005 406	
Net investment income		514,430	\$	4,005,426	
Net realized gain (loss) from investments, foreign currency transactions and futures contracts Net change in unrealized appreciation (depreciation) on investments and translation	,	579,316		14,653,384	
of other assets and liabilities denominated in foreign currencies	71,8	372,868		40,432,930	
Net increase (decrease) in net assets resulting from operations	86,9	966,614		59,091,740	
Distributions to shareholders from:					
Net investment income:					
Class Z	. ,	085,169)		(1,463,197)	
Class A	(1,8	340,120)		(2,589,323)	
Class B		_		(2,287)	
Class C	(]	118,179)		(490,530)	
Class R6		(70)			
Total distributions to shareholders	(3,0)43,538)		(4,545,337)	
Capital share transactions: (Note 2)					
Class Z	,	248,625)		(7,268,399)	
Class A	,	777,938	(17,774,465)	
Class B		374,083)		(1,633,368)	
Class C	5	503,579	(10,673,792)	
Class R6		5,000			
Total capital share transactions	7,6	63,809	(37,350,024)	
Net increase (decrease) in net assets	91,5	586,885		17,196,379	
Net assets:					
Beginning of year	340,5	596,834	3	23,400,455	
End of year	\$ 432,1	183,719	\$3	40,596,834	
Undistributed net investment income included in net assets:					
End of year	\$ 1,1	155,140	\$	1,566,225	

Notes to Financial Statements

1. ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES

Franklin Mutual Series Funds (Trust) is registered under the Investment Company Act of 1940, as amended, (1940 Act) as an open-end investment company, consisting of seven separate funds. The Mutual Financial Services Fund (Fund) is included in this report. The financial statements of the remaining funds in the Trust are presented separately. The Fund offers four classes of shares: Class Z, Class A, Class C and Class R6. Effective May 1, 2013, the Fund began offering a new class of shares, Class R6. Effective March 22, 2013, all Class B shares were converted to Class A. Each class of shares differs by its initial sales load, contingent deferred sales charges, voting rights on matters affecting a single class, its exchange privilege and fees primarily due to differing arrangements for distribution and transfer agent fees.

The following summarizes the Fund's significant accounting policies.

a. Financial Instrument Valuation

The Fund's investments in financial instruments are carried at fair value daily. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants on the measurement date. The Fund calculates the net asset value (NAV) per share at the close of the New York Stock Exchange (NYSE), generally at 4p.m. Eastern time (NYSE close) on each day the NYSE is open for trading. Under procedures approved by the Trust's Board of Trustees (the Board), the Fund's administrator, investment manager and other affiliates have formed the Valuation and Liquidity Oversight Committee (VLOC). The VLOC provides administration and oversight of the Fund's valuation policies and procedures, which are approved annually by the Board. Among other things, these procedures allow the Fund to utilize independent pricing services, quotations from securities and financial instrument dealers, and other market sources to determine fair value.

Equity securities and derivative financial instruments (derivatives) listed on an exchange or on the NASDAQ National Market System are valued at the last quoted sale price or the official closing price of the day, respectively. Foreign equity securities are valued as of the close of trading on the foreign stock exchange on which the security is primarily traded or as of the NYSE close, whichever is earlier. The value is then converted into its U.S. dollar equivalent at the foreign exchange rate in effect at the NYSE close on the day that the value of the security is determined. Over-the-counter (OTC) securities are valued within the range of the most recent quoted bid and ask prices. Securities that trade in multiple markets or on multiple exchanges are valued according to the broadest and most representative market. Certain equity securities are valued based upon fundamental characteristics or relationships to similar securities.

Debt securities generally trade in the OTC market rather than on a securities exchange. The Fund's pricing services use multiple valuation techniques to determine fair value. In instances where sufficient market activity exists, the pricing services may utilize a market-based approach through which quotes from market makers are used to determine fair value. In instances where sufficient market activity may not exist or is limited, the pricing services also utilize proprietary valuation models which may consider market characteristics such as benchmark yield curves,

Notes to Financial Statements (continued)

1. Organization and Significant Accounting Policies (continued)

a. Financial Instrument Valuation (continued)

credit spreads, estimated default rates, anticipated market interest rate volatility, coupon rates, anticipated timing of principal repayments, underlying collateral, and other unique security features in order to estimate the relevant cash flows, which are then discounted to calculate the fair value. Securities denominated in a foreign currency are converted into their U.S. dollar equivalent at the foreign exchange rate in effect at the NYSE close on the date that the values of the foreign debt securities are determined.

Certain derivatives trade in the OTC market. The Fund's pricing services use various techniques including industry standard option pricing models and proprietary discounted cash flow models to determine the fair value of those instruments. The Fund's net benefit or obligation under the derivative contract, as measured by the fair value of the contract, is included in net assets.

The Fund has procedures to determine the fair value of financial instruments for which market prices are not reliable or readily available. Under these procedures, the VLOC convenes on a regular basis to review such financial instruments and considers a number of factors, including significant unobservable valuation inputs, when arriving at fair value. The VLOC primarily employs a market-based approach which may use related or comparable assets or liabilities, recent transactions, market multiples, book values, and other relevant information for the investment to determine the fair value of the investment. An income-based valuation approach may also be used in which the anticipated future cash flows of the investment are discounted to calculate fair value. Discounts may also be applied due to the nature or duration of any restrictions on the disposition of the investments. Due to the inherent uncertainty of valuations of such investments, the fair values may differ significantly from the values that would have been used had an active market existed. The VLOC employs various methods for calibrating these valuation approaches including a regular review of key inputs and assumptions, transactional back-testing or disposition analysis, and reviews of any related market activity.

Trading in securities on foreign securities stock exchanges and OTC markets may be completed before the daily NYSE close. In addition, trading in certain foreign markets may not take place on every NYSE business day. Occasionally, events occur between the time at which trading in a foreign security is completed and the close of the NYSE that might call into question the reliability of the value of a portfolio security held by the Fund. As a result, differences may arise between the value of the Fund's portfolio securities as determined at the foreign market close and the latest indications of value at the close of the NYSE. In order to minimize the potential for these differences, the VLOC monitors price movements following the close of trading in foreign stock markets through a series of country specific market proxies (such as baskets of American Depositary Receipts, futures contracts and exchange traded funds). These price movements are measured against established trigger thresholds for each specific market proxy to assist in determining if an event has occurred that may call into question the reliability of the values of the foreign securities held by the Fund. If such an event occurs, the securities may be valued using fair value procedures, which may include the use of independent pricing services.

Notes to Financial Statements (continued)

1. Organization and Significant Accounting Policies (continued)

a. Financial Instrument Valuation (continued)

Also, when the last day of the reporting period is a non-business day, certain foreign markets may be open on those days that the NYSE is closed, which could result in differences between the value of the Fund's portfolio securities on the last business day and the last calendar day of the reporting period. Any significant security valuation changes due to an open foreign market are adjusted and reflected by the Fund for financial reporting purposes.

b. Foreign Currency Translation

Portfolio securities and other assets and liabilities denominated in foreign currencies are translated into U.S. dollars based on the exchange rate of such currencies against U.S. dollars on the date of valuation. The Fund may enter into foreign currency exchange contracts to facilitate transactions denominated in a foreign currency. Purchases and sales of securities, income and expense items denominated in foreign currencies are translated into U.S. dollars at the exchange rate in effect on the transaction date. Portfolio securities and assets and liabilities denominated in foreign currencies contain risks that those currencies will decline in value relative to the U.S. dollar. Occasionally, events may impact the availability or reliability of foreign exchange rates used to convert the U.S. dollar equivalent value. If such an event occurs, the foreign exchange rate will be valued at fair value using procedures established and approved by the Board.

The Funds does not separately report the effect of changes in foreign exchange rates from changes in market prices on securities held. Such changes are included in net realized and unrealized gain or loss from investments on the Statement of Operations.

Realized foreign exchange gains or losses arise from sales of foreign currencies, currency gains or losses realized between the trade and settlement dates on securities transactions and the difference between the recorded amounts of dividends, interest, and foreign withholding taxes and the U.S. dollar equivalent of the amounts actually received or paid. Net unrealized foreign exchange gains and losses arise from changes in foreign exchange rates on foreign denominated assets and liabilities other than investments in securities held at the end of the reporting period.

c. Derivative Financial Instruments

The Fund invested in derivatives in order to manage risk or gain exposure to various other investments or markets. Derivatives are financial contracts based on an underlying or notional amount, require no initial investment or an initial net investment that is smaller than would normally be required to have a similar response to changes in market factors, and require or permit net settlement. Derivatives contain various risks including the potential inability of the counterparty to fulfill their obligations under the terms of the contract, the potential for an illiquid secondary market, and/or the potential for market movements which expose the Fund to gains or losses in excess of the amounts shown on the Statement of Assets and Liabilities. Realized gain and loss and unrealized appreciation and depreciation on these contracts for the period are included in the Statement of Operations.

Notes to Financial Statements (continued)

1. Organization and Significant Accounting Policies (continued)

c. Derivative Financial Instruments (continued)

Derivative counterparty credit risk is managed through a formal evaluation of the creditworthiness of all potential counterparties. The Fund attempts to reduce its exposure to counterparty credit risk on OTC derivatives, whenever possible, by entering into International Swaps and Derivatives Association (ISDA) master agreements with certain counterparties. These agreements contain various provisions, including but not limited to collateral requirements, events of default, or early termination. Termination events applicable to the counterparty include certain deteriorations in the credit quality of the counterparty. Termination events applicable to the Fund include failure of the Fund to maintain certain net asset levels and/or limit the decline in net assets over various periods of time. In the event of default or early termination, the ISDA master agreement gives the non-defaulting party the right to net and close-out all transactions traded, whether or not arising under the ISDA agreement, to one net amount payable by one counterparty to the other. However, absent an event of default or early termination, OTC derivative assets and liabilities are presented gross and not offset in the Statement of Assets and Liabilities. Early termination by the counterparty may result in an immediate payment by the Fund of any net liability owed to that counterparty under the ISDA agreement.

Collateral requirements differ by type of derivative. Collateral or initial margin requirements are set by the broker or exchange clearing house for exchange traded and centrally cleared derivatives. Initial margin deposited is held at the exchange and can be in the form of cash and/or securities. For OTC derivatives traded under an ISDA master agreement, posting of collateral is required by either the Fund or the applicable counterparty if the total net exposure of all OTC derivatives with the applicable counterparty exceeds the minimum transfer amount, which typically ranges from \$100,000 to \$250,000, and can vary depending on the counterparty and the type of the agreement. Generally, collateral is determined at the close of fund business each day and any additional collateral required due to changes in derivative values may be delivered by the Fund or the counterparty within a few business days. Collateral pledged and/or received by the Fund for OTC derivatives, if any, is held in segregated accounts with the Fund's custodian/counterparty broker and can be in the form of cash and/or securities. Unrestricted cash may be invested according to the Fund's investment objectives.

The Fund entered into exchange traded futures contracts primarily to manage exposure to certain foreign currencies. A futures contract is an agreement between the Fund and a counterparty to buy or sell an asset for a specified price on a future date. Required initial margins are pledged by the Fund, and the daily change in fair value is accounted for as a variation margin payable or receivable on the Statement of Assets and Liabilities.

The Fund entered into OTC forward exchange contracts primarily to manage exposure to certain foreign currencies. A forward exchange contract is an agreement between the Fund and a counterparty to buy or sell a foreign currency at a specific exchange rate on a future date.

See Note 9 regarding other derivative information.

Notes to Financial Statements (continued)

1. Organization and Significant Accounting Policies (continued)

d. Securities Lending

The Fund participates in an agency based securities lending program. The Fund receives cash collateral against the loaned securities in an amount equal to at least 102% of the market value of the loaned securities. Collateral is maintained over the life of the loan in an amount not less than 100% of the market value of loaned securities, as determined at the close of fund business each day; any additional collateral required due to changes in security values is delivered to the Fund on the next business day. The collateral is invested in a non-registered money fund. The Fund receives income from the investment of cash collateral, in addition to lending fees and rebates paid by the borrower. The Fund bears the market risk with respect to the collateral investment, securities loaned, and the risk that the agent may default on its obligations to the Fund. The securities lending agent has agreed to indemnify the Fund in the event of default by a third party borrower. At December 31, 2013, the Fund had no securities on loan.

e. Income and Deferred Taxes

It is the Fund's policy to qualify as a regulated investment company under the Internal Revenue Code. The Fund intends to distribute to shareholders substantially all of its taxable income and net realized gains to relieve it from federal income and excise taxes. As a result, no provision for U.S. federal income taxes is required.

The Fund may be subject to foreign taxation related to income received, capital gains on the sale of securities and certain foreign currency transactions in the foreign jurisdictions in which it invests. Foreign taxes, if any, are recorded based on the tax regulations and rates that exist in the foreign markets in which the Fund invests. When a capital gain tax is determined to apply the Fund records an estimated deferred tax liability in an amount that would be payable if the securities were disposed of on the valuation date.

The Fund recognizes the tax benefits of uncertain tax positions only when the position is "more likely than not" to be sustained upon examination by the tax authorities based on the technical merits of the tax position. As of December 31, 2013, and for all open tax years, the Fund has determined that no liability for unrecognized tax benefits is required in the Fund's financial statements related to uncertain tax positions taken on a tax return (or expected to be taken on future tax returns). Open tax years are those that remain subject to examination and are based on each tax jurisdiction statute of limitation.

f. Security Transactions, Investment Income, Expenses and Distributions

Security transactions are accounted for on trade date. Realized gains and losses on security transactions are determined on a specific identification basis. Interest income and estimated expenses are accrued daily. Amortization of premium and accretion of discount on debt securities are included

Notes to Financial Statements (continued)

1. Organization and Significant Accounting Policies (continued)

f. Security Transactions, Investment Income, Expenses and Distributions (continued)

in interest income. Dividend income is recorded on the ex-dividend date except that certain dividends from foreign securities are recognized as soon as the Fund is notified of the ex-dividend date. Distributions to shareholders are recorded on the ex-dividend date and are determined according to income tax regulations (tax basis). Distributable earnings determined on a tax basis may differ from earnings recorded in accordance with accounting principles generally accepted in the United States of America. These differences may be permanent or temporary. Permanent differences are reclassified among capital accounts to reflect their tax character. These reclassifications have no impact on net assets or the results of operations. Temporary differences are not reclassified, as they may reverse in subsequent periods.

Common expenses incurred by the Trust are allocated among the funds based on the ratio of net assets of each fund to the combined net assets of the Trust. Fund specific expenses are charged directly to the fund that incurred the expense.

Realized and unrealized gains and losses and net investment income, not including class specific expenses, are allocated daily to each class of shares based upon the relative proportion of net assets of each class. Differences in per share distributions, by class, are generally due to differences in class specific expenses.

Distributions received by the Fund from certain securities may be a return of capital (ROC). Such distributions reduce the cost basis of the securities, and any distributions in excess of the cost basis are recognized as capital gains.

g. Accounting Estimates

The preparation of financial statements in accordance with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the amounts of income and expenses during the reporting period. Actual results could differ from those estimates.

h. Guarantees and Indemnifications

Under the Trust's organizational documents, its officers and trustees are indemnified by the Trust against certain liabilities arising out of the performance of their duties to the Trust. Additionally, in the normal course of business, the Trust, on behalf of the Fund, enters into contracts with service providers that contain general indemnification clauses. The Trust's maximum exposure under these arrangements is unknown as this would involve future claims that may be made against the Trust that have not yet occurred. Currently, the Trust expects the risk of loss to be remote.

Notes to Financial Statements (continued)

2. SHARES OF BENEFICIAL INTEREST

At December 31, 2013, there were an unlimited number of shares authorized (without par value). Transactions in the Fund's shares were as follows:

	_ 20	Year Ended [December 31,	012
	Shares	Amount	Shares	Amount
Class Z Shares:				
Shares sold	688,935	\$ 10,392,063	1,024,689	\$ 13,275,422
Shares issued in reinvestment				
of distributions	57,352	946,286	96,383	1,304,659
Shares redeemed	(883,206)	(13,586,974)	(1,703,585)	(21,848,480)
Net increase (decrease)	(136,919)	\$ (2,248,625)	(582,513)	\$ (7,268,399)
Class A Shares:				
Shares sold	3,661,594	\$ 56,607,499	2,053,865	\$ 26,219,145
Shares issued in reinvestment				
of distributions	107,325	1,772,519	183,716	2,490,728
Shares redeemed	(3,124,833)	(48,602,080)	(3,664,473)	(46,484,338)
Net increase (decrease)	644,086	\$ 9,777,938	(1,426,892)	\$(17,774,465)
Class B Sharesa:				
Shares sold	54	\$ 759	2,961	\$ 36,601
Shares issued in reinvestment				
of distributions	_	_	166	2,141
Shares redeemed	(25,977)	(374,842)	(134,684)	(1,672,110)
Net increase (decrease)	(25,923)	\$ (374,083)	(131,557)	\$ (1,633,368)
Class C Shares:				
Shares sold	1,115,744	\$ 17,176,940	393,032	\$ 4,966,381
Shares issued in reinvestment				
of distributions	7,101	111,402	34,214	457,649
Shares redeemed	(1,088,960)	(16,784,763)	(1,271,876)	(16,097,822)
Net increase (decrease)	33,885	\$ 503,579	(844,630)	\$(10,673,792)
Class R6 Sharesb:				
Shares sold	336	\$ 5,000		

^aEffective March 22, 2013, all Class B shares were converted to Class A.

3. Transactions with Affiliates

Franklin Resources, Inc. is the holding company for various subsidiaries that together are referred to as Franklin Templeton Investments. Certain officers and trustees of the Fund are also officers and/or directors of the following subsidiaries:

Subsidiary	Affiliation
Franklin Mutual Advisers, LLC (Franklin Mutual)	Investment manager
Franklin Templeton Services, LLC (FT Services)	Administrative manager
Franklin Templeton Distributors, Inc. (Distributors)	Principal underwriter
Franklin Templeton Investor Services, LLC (Investor Services)	Transfer agent

^bFor the period May 1, 2013 (effective date) to December 31, 2013.

Notes to Financial Statements (continued)

3. Transactions with Affiliates (continued)

a. Management Fees

The Fund pays an investment management fee to Franklin Mutual based on the average daily net assets of the Fund as follows:

Annualized Fee Rate	Net Assets
0.800%	Up to and including \$1 billion
0.770%	Over \$1 billion, up to and including \$2 billion
0.750%	Over \$2 billion, up to and including \$5 billion
0.730%	In excess of \$5 billion

b. Administrative Fees

The Fund pays its allocated share of an administrative fee to FT Services based on the Trust's aggregate average daily net assets as follows:

Annualized Fee Rate	Net Assets
0.150%	Up to and including \$200 million
0.135%	Over \$200 million, up to and including \$700 million
0.100%	Over \$700 million, up to and including \$1.2 billion
0.075%	In excess of \$1.2 billion

c. Distribution Fees

The Board has adopted distribution plans for each share class, with the exception of Class Z and Class R6 shares, pursuant to Rule 12b-1 under the 1940 Act. Distribution fees are not charged on shares held by affiliates. Under the Fund's Class A reimbursement distribution plan, the Fund reimburses Distributors for costs incurred in connection with the servicing, sale and distribution of the Fund's shares up to the maximum annual plan rate. Under the Class A reimbursement distribution plan, costs exceeding the maximum for the current plan year cannot be reimbursed in subsequent periods. In addition, under the Fund's Class B and C compensation distribution plans, the Fund pays Distributors for costs incurred in connection with the servicing, sale and distribution of the Fund's shares up to the maximum annual plan rate for each class. The plan year, for purposes of monitoring compliance with the maximum annual plan rates, is February 1 through January 31.

The maximum annual plan rates, based on the average daily net assets, for each class, are as follows:

Class A	
Class B	1.00%
Class C	1.00%

The Board has set the current rate at 0.30% per year for Class A shares until further notice and approval by the Board.

Notes to Financial Statements (continued)

3. Transactions with Affiliates (continued)

d. Sales Charges/Underwriting Agreements

Front-end sales charges and contingent deferred sales charges (CDSC) do not represent expenses of the Fund. These charges are deducted from the proceeds of sales of Fund shares prior to investment or from redemption proceeds prior to remittance, as applicable. Distributors has advised the Fund of the following commission transactions related to the sales and redemptions of the Fund's shares for the year:

Sales charges retained net of commissions paid to	
unaffiliated broker/dealers	\$84,242
CDSC retained	\$ 5.405

e. Transfer Agent Fees

Each class of shares, except for Class R6, pays transfer agent fees to Investor Services for its performance of shareholder servicing obligations and reimburses Investor Services for out of pocket expenses incurred, including shareholding servicing fees paid to third parties. These fees are allocated daily based upon their relative proportion of such classes' aggregate net assets. Class R6 pays Investor Services transfer agent fees specific to that class.

For the year ended December 31, 2013, the Fund paid transfer agent fees of \$794,523, of which \$438,183 was retained by Investor Services.

f. Waiver and Expense Reimbursements

Investor Services has contractually agreed in advance to waive or limit its fees so that the Class R6 transfer agent fees of the Fund do not exceed 0.01% until April 30, 2014.

4. EXPENSE OFFSET ARRANGEMENT

The Fund has entered into an arrangement with its custodian whereby credits realized as a result of uninvested cash balances are used to reduce a portion of the Fund's custodian expenses. During the year ended December 31, 2013, the custodian fees were reduced as noted in the Statement of Operations.

5. INDEPENDENT TRUSTEES' RETIREMENT PLAN

On January 1, 1993, the Trust adopted an Independent Trustees' Retirement Plan (Plan). The Plan is an unfunded defined benefit plan that provides benefit payments to Trustees whose length of service and retirement age meets the eligibility requirements of the Plan. Benefits under the Plan are based on years of service and fees paid to each trustee at the time of retirement. Effective in December 1996, the Plan was closed to new participants.

Notes to Financial Statements (continued)

5. INDEPENDENT TRUSTEES' RETIREMENT PLAN (continued)

During the year ended December 31, 2013, the Fund's projected benefit obligation and benefit payments under the Plan were as follows:

^a Projected benefit obligation at December 31, 2013	\$22	2,791
^b Decrease in projected benefit obligation	\$	656
Benefit payments made to retired trustees	\$	468

^aThe projected benefit obligation is included in accrued expenses and other liabilities in the Statement of Assets and Liabilities.

6. INCOME TAXES

For tax purposes, capital losses may be carried over to offset future capital gains. Capital loss carryforwards with no expiration, if any, must be fully utilized before those losses with expiration dates.

At December 31, 2013, capital loss carryforwards were as follows:

O : t - I	1		.f l -	I- : I-	1 -	expiration:
ı anıtaı	IUGG	carr	/TONWards	CHIDIACT	TO	evniration.

2016	\$105,848,544
2017	73,527,713
2018	31,091,133
Capital loss carryforwards not subject to expiration:	
Short term	3,334,336
Long term	1,454,330
Total capital loss carryforwards	\$215,256,056

During the year ended December 31, 2013, the Fund utilized \$9,458,122 of capital loss carryforwards.

The tax character of distributions paid during the years ended December 31, 2013 and 2012, was as follows:

	2013	2012
Distributions paid from ordinary		
income	\$3,043,538	\$4,545,337

At December 31, 2013, the cost of investments, net unrealized appreciation (depreciation) and undistributed ordinary income for income tax purposes were as follows:

Cost of investments	\$347,991,428
Unrealized appreciation	\$119,588,802 (36,171,406)
Net unrealized appreciation (depreciation)	\$ 83,417,396
Distributable earnings – undistributed ordinary income	\$ 1,286,493

^bThe decrease in projected benefit obligation is included in trustees' fees and expenses in the Statement of Operations.

Notes to Financial Statements (continued)

6. INCOME TAXES (continued)

Differences between income and/or capital gains as determined on a book basis and a tax basis are primarily due to differing treatments of foreign currency transactions and passive foreign investment company shares.

7. INVESTMENT TRANSACTIONS

Purchases and sales of investments (excluding short term securities) for the year ended December 31, 2013, aggregated \$97,248,809 and \$91,708,923, respectively.

8. RESTRICTED SECURITIES

The Fund invests in securities that are restricted under the Securities Act of 1933 (1933 Act) or which are subject to legal, contractual, or other agreed upon restrictions on resale. Restricted securities are often purchased in private placement transactions, and cannot be sold without prior registration unless the sale is pursuant to an exemption under the 1933 Act. Disposal of these securities may require greater effort and expense, and prompt sale at an acceptable price may be difficult. The Fund may have registration rights for restricted securities. The issuer generally incurs all registration costs.

At December 31, 2013, the Fund held investments in restricted securities, excluding certain securities exempt from registration under the 1933 Act deemed to be liquid, as follows:

		Acquisition		
Shares/Warrants	Issuer	Dates	Cost	Value
456,903	The Bankshares Inc	3/22/07	\$ 4,569,030	\$2,178,966
8,117	^a Columbia Banking System Inc., wts., C, 10/23/16	10/23/09	_	1,535,525
4,357,178	FIM Coinvestor Holdings I, LLC	11/20/06 - 6/02/09	_	_
110,792	First Southern Bancorp Inc	1/27/10 - 7/07/10	2,337,711	534,040
190	First Southern Bancorp Inc., cvt. pfd., C	1/27/10 - 7/07/10	190,000	354,700
3,000,000	Hightower Holding LLC, pfd., A	3/31/08 - 1/05/10	2,362,324	2,859,000
968,000	Hightower Holding LLC, pfd., A, Series 2	6/10/10 - 5/10/12	2,420,000	1,841,233
68,631	Imagine Group Holdings Ltd	8/31/04	702,884	501,418
7,480	Olympus Re Holdings Ltd	12/19/01	700,734	_
	Total Restricted Securities (Value is 2.	27% of Net Assets)	\$13,282,683	\$9,804,882

^aThe Fund also invests in unrestricted securities or other investments in the issuer, valued at \$5,298,396 as of December 31, 2013.

Notes to Financial Statements (continued)

9. OTHER DERIVATIVE INFORMATION

At December 31, 2013, the Fund's investments in derivative contracts are reflected on the Statement of Assets and Liabilities as follows:

Asset Derivatives

Liability Derivatives

Derivative Contracts Not Accounted for as Hedging Instruments	Statement of Assets and Liabilities Location	Fair Value Amount	Statement of Assets and Liabilities Location	Fair Value Amount
Foreign exchange contracts	Unrealized appreciation on forward exchange contracts	\$634,677	Unrealized depreciation on forward exchange contracts / Net assets consist of - net unrealized appreciation (depreciation)	\$5,067,173ª

alnoludes cumulative appreciation (depreciation) of futures contracts as reported in the Statement of Investments. Only current day's variation margin is separately reported within the Statement of Assets and Liabilities.

For the year ended December 31, 2013, the effect of derivative contracts on the Fund's Statement of Operations was as follows:

Derivative Contracts Not Accounted for as Hedging Instruments	Statement of Operations Locations	Realized Gain (Loss) for the Year	Change in Unrealized Appreciation (Depreciation) for the Year
Foreign exchange contracts	Net realized gain (loss) from foreign currency transactions and futures contracts / Net change in unrealized appreciation (depreciation) on translation of other assets and liabilities denominated in foreign currencies	\$1,635,632	\$(1,989,732)

For the year ended December 31, 2013, the average month end fair value of derivatives represented 0.97% of average month end net assets. The average month end number of open derivative contracts for the year was 121.

At December 31, 2013, the Fund's OTC derivative assets and liabilities are as follows:

	Gross and Net Amounts of Assets and Liabilities Presented in the Statement of Assets and Liabilities			
	Assetsa	Liabilitiesa		
Derivatives Forward Exchange Contracts	\$634,677	\$4,943,446		

absent an event of default or early termination, OTC derivative assets and liabilities are presented gross and not offset in the Statement of Assets and Liabilities.

Notes to Financial Statements (continued)

9. OTHER DERIVATIVE INFORMATION (continued)

At December 31, 2013, the Fund's OTC derivative assets which may be offset against the Fund's OTC derivative liabilities and collateral received from the counterparty, is as follows:

		the iabilities			
	Gross and Net Amounts of Assets Presented in the Statement of Assets and Liabilities	Financial Instruments Available for Offset	Financial Instruments Collateral Received	Cash Collateral Received	Net Amount (Not less than zero)
Counterparty					
BANT	\$ 36,551	\$ (36,551)	\$—	\$—	\$—
BBU	26,509	(26,509)	_	_	_
BONY	22,732	(22,732)	_		_
DBFX	_	_	_		_
FBCO	475,305	(475,305)	_	_	_
HSBC	68,826	(68,826)	_		_
SCBT	4,750	(4,750)	_	_	
SSBT	4	(4)	_	_	
Total	\$634,677	\$(634,677)	\$—	\$—	\$—

At December 31, 2013, the Fund's OTC derivative liabilities which may be offset against the Fund's OTC derivative assets and collateral pledged to the counterparty, is as follows:

	Amounts Not Offset in the Statement of Assets and Liabilities						
	Gross and Net Amounts of Liabilities Presented in the Statement of Assets and Liabilities	Financial Instruments Available for Offset	Financial Instruments Collateral Pledged ^{a,b}	Cash Collateral Pledged	Net Amount (Not less than zero)		
Counterparty							
BANT	\$1,881,059	\$ (36,551)	\$(1,267,709)	\$—	\$ 576,799		
BBU	624,266	(26,509)	(300,000)	_	297,757		
BONY	34,990	(22,732)	_	_	12,258		
DBFX	842,030	_	(837,475)	_	4,555		
FBCO	1,001,752	(475,305)	(526,447)	_	_		
HSBC	378,038	(68,826)	(259,948)	_	49,264		
SCBT	142,282	(4,750)	_	_	137,532		
SSBT	39,029	(4)	_	_	39,025		
Total	\$4,943,446	\$(634,677)	\$(3,191,579)	\$—	\$1,117,190		

In some instances, the collateral amounts disclosed in the table above were adjusted due to the requirement to limit collateral amounts to avoid the effect of overcollateralization. Actual collateral received and/or pledged may be more than the amounts disclosed herein.

See Note 1(c) regarding derivative financial instruments.

bSee the accompanying Statement of Investments for securities pledged as collateral for derivatives.

Notes to Financial Statements (continued)

10. Holdings of 5% Voting Securities of Portfolio Companies

The 1940 Act defines "affiliated companies" to include investments in portfolio companies in which a fund owns 5% or more of the outstanding voting securities. Investments in "affiliated companies" for the Fund for the year ended December 31, 2013, were as shown below.

Name of Issuer	Number of Shares Held at Beginning of Year	Gross Additions	Gross Reductions	Number of Shares Held at End of Year	Value at End of Year	Investment Income	Realized Capital Gain (Loss)
Non-Controlled Affiliates AB&T Financial Corp	226.100			226.100	\$ 122.094	¢	\$
Protector Forsikring ASA	.,	_	_	4,479,410	14,180,256	686,027	φ <u> </u>
Total Affiliated Securities (Value	ue is 3.31% of Net A	Assets)			\$14,302,350	\$686,027	\$

11. CREDIT FACILITY

The Fund, together with other U.S. registered and foreign investment funds (collectively, Borrowers), managed by Franklin Templeton Investments, are borrowers in a joint syndicated senior unsecured credit facility totaling \$1.5 billion (Global Credit Facility) which, after an extension of the original terms, matured on February 14, 2014. This Global Credit Facility provides a source of funds to the Borrowers for temporary and emergency purposes, including the ability to meet future unanticipated or unusually large redemption requests. Effective February 14, 2014, the Borrowers renewed the Global Credit Facility which matures on February 13, 2015.

Under the terms of the Global Credit Facility, the Fund shall, in addition to interest charged on any borrowings made by the Fund and other costs incurred by the Fund, pay its share of fees and expenses incurred in connection with the implementation and maintenance of the Global Credit Facility, based upon its relative share of the aggregate net assets of all of the Borrowers, including an annual commitment fee of 0.07% based upon the unused portion of the Global Credit Facility. These fees are reflected in other expenses on the Statement of Operations. During the year ended December 31, 2013, the Fund did not use the Global Credit Facility.

12. FAIR VALUE MEASUREMENTS

The Fund follows a fair value hierarchy that distinguishes between market data obtained from independent sources (observable inputs) and the Fund's own market assumptions (unobservable inputs). These inputs are used in determining the value of the Fund's financial instruments and are summarized in the following fair value hierarchy:

- Level 1 quoted prices in active markets for identical financial instruments
- Level 2 other significant observable inputs (including quoted prices for similar financial instruments, interest rates, prepayment speed, credit risk, etc.)
- Level 3 significant unobservable inputs (including the Fund's own assumptions in determining the fair value of financial instruments)

Notes to Financial Statements (continued)

12. FAIR VALUE MEASUREMENTS (continued)

The input levels are not necessarily an indication of the risk or liquidity associated with financial instruments at that level.

For movements between the levels within the fair value hierarchy, the Fund has adopted a policy of recognizing the transfers as of the date of the underlying event which caused the movement.

A summary of inputs used as of December 31, 2013, in valuing the Fund's assets and liabilities carried at fair value, is as follows:

	Level 1	Level 2	Level 3	Total
Assets:				
Investments in Securities:				
Equity Investments: ^a				
Capital Markets	\$ 16,601,061	\$ —	\$ 19,734	\$ 16,620,795
Commercial Banks	89,469,302	3,873,711	8,900,266	102,243,279
Diversified Financial Services	41,584,023	_	4,700,233	46,284,256
Insurance	213,880,812	_	501,418 ^b	214,382,230
All Other Equity Investments ^c	16,101,207	_	_	16,101,207
Corporate Bonds	_	1,185,824	_	1,185,824
Companies in Liquidation	_	3,494,746	b	3,494,746
Short Term Investments	31,096,487			31,096,487
Total Investments in Securities	\$408,732,892	\$8,554,281	\$14,121,651	\$431,408,824
Forward Exchange Contracts	\$ —	\$ 634,677	\$ —	\$ 634,677
Liabilities:				
Futures Contracts	123,727	_	_	123,727
Forward Exchange Contracts	_	4,943,446		4,943,446

^aIncludes common, convertible preferred and preferred stocks as well as other equity investments.

blncludes securities determined to have no value at December 31, 2013.

[°]For detailed categories, see the accompanying Statement of Investments.

Notes to Financial Statements (continued)

12. FAIR VALUE MEASUREMENTS (continued)

A reconciliation of assets in which Level 3 inputs are used in determining fair value is presented when there are significant Level 3 investments at the end of the year. At December 31, 2013, the reconciliation of assets is as follows:

Assets:	Balance at Beginning of Year	Purchases	Sales	Transfers Into Level 3	Transfers Out of Level 3 ^a	Cost Basis Adjustments ^b	Net Realized Gain (Loss)	Net Unrealized Gain (Loss)	Balance at End of Year	Net Change in Unrealized Appreciation (Depreciation) on Assets Held at Year End
Investments in Securities:										
Equity Investments:										
Capital Markets	\$ —	\$28,059	\$ —	\$	\$ —	\$ —	\$ —	\$ (8.325)	\$ 19.734	\$ (8,325)
Commercial Banks	10,856,078	_	_	_	(3,344,000)	_	_	1,388,188	8,900,266	2,063,047
Diversified Financial	,,				(=,=::,===;			-,,	-,,	_,,
Services	5,154,639	_	_	_	_	_	_	(454,406)	4,700,233	(454,406)
Insurance	792,077 ^d	_	_	_	_	(1,818)	_	(288,841)	501,418 ^d	(288,841)
Real Estate Management &										
Development	159,657		(130,745)	_	_	_	(9,706,180)	9,677,268	_	
Total	\$16,962,451	\$28,059	\$(130,745)	\$—	\$(3,344,000)	\$ (1,818)	\$(9,706,180)	\$10,313,884	\$14,121,651	\$1,311,475

^aThe investments were transferred out of Level 3 as a result of the availability of a broker quote.

^bMay include accretion, amortization, partnership adjustments, and/or other cost basis adjustments.

clncludes common, convertible preferred and preferred stocks as well as other equity investments.

dincludes securities determined to have no value.

Notes to Financial Statements (continued)

12. FAIR VALUE MEASUREMENTS (continued)

Significant unobservable valuation inputs developed by the VLOC for material Level 3 investments and impact to fair value as a result of changes in unobservable valuation inputs as of December 31, 2013, are as follows:

Description	Fair Value at End of Year	Valuation Technique	Unobservable Inputs	Amount/ Range	Impact to Fair Value if Input Increases ^a
Assets: Investments in Securities: Equity Investments: ^b					
Commercial Banks	\$ 4,603,231	Market comparables	Discount for lack of marketability	10%	Decreasec
			Price / tangible book multiple	1.0x -1.4x	Increasec
		Option pricing model	Stock price volatility	26.7%	Increase
Diversified Financial Services	4,700,233	Discounted cash flow model	Cost of equity	17%	Decrease
			Long-term revenue growth rate	6.2% - 34.9%	Increased
			Adjusted EBITDA margin	10.6% - 23.3%	Increase
Insurance	501,418	Market comparables	Discount for lack of marketability	14%	Decrease ^c
			Price / book multiple	1.0x	Increase
All Other Investments ^e	4,316,769				
Total	\$14,121,651				

Represents the directional change in the fair value of the Level 3 investments that would result from a significant and reasonable increase in the corresponding input. A significant and reasonable decrease in input would have the opposite effect. Significant impacts, if any, to fair value and/or net assets have been indicated.

Abbreviations List

EBITDA - Earnings before interest, taxes, depreciation and amortization

13. New Accounting Pronouncements

In June 2013, the Financial Accounting Standards Board issued Accounting Standards Update (ASU) No. 2013-08, Investment Companies (Topic 946): Amendments to the Scope, Measurement, and Disclosure Requirements. The ASU modifies the criteria used in defining an investment company under U.S. Generally Accepted Accounting Principles and also sets forth certain measurement

blncludes common, convertible preferred and preferred stocks.

^cRepresents a significant impact to fair value but not net assets.

dRepresents a significant impact to fair value and net assets.

elncludes fair value of immaterial investments developed using various valuation techniques and unobservable inputs. May also include investments with values derived using prior transaction prices or third party pricing information without adjustment for which such inputs are also unobservable.

Notes to Financial Statements (continued)

13. New Accounting Pronouncements (continued)

and disclosure requirements. Under the ASU, an entity that is registered under the 1940 Act automatically qualifies as an investment company. The ASU is effective for interim and annual reporting periods beginning after December 15, 2013. Management has reviewed the requirements and believes the adoption of this ASU will not have a material impact on the financial statements.

14. SUBSEQUENT EVENTS

The Fund has evaluated subsequent events through the issuance of the financial statements and determined that no events have occurred that require disclosure other than those already disclosed in the financial statements.

ABBREVIATIONS

Counter	party	Curre	enc	y	Selected	Portfolio
BBU -	Bank of America N.A. Barclays Bank PLC Bank of New York Mellon	EUR GBP USD	-	Euro British Pound United States Dollar	IDR -	International Depositary Receipt
DBFX -	Deutsche Bank AG					
FBCO -	Credit Suisse Group AG					
HSBC -	HSBC Bank USA, N.A.					
SCBT -	Standard Chartered Bank					
SSBT -	State Street Bank and Trust Co., N.A.					

Report of Independent Registered Public Accounting Firm

To the Board of Trustees of Franklin Mutual Series Funds and Shareholders of the Mutual Financial Services Fund:

We have audited the accompanying statement of assets and and liabilities, including the statement of investments, of Mutual Financial Services Fund (the "Fund") (one of the funds constituting Franklin Mutual Series Funds), as of December 31, 2013, and the related statement of operations for the year then ended, the statements of changes in net assets for each of the two years in the period then ended, and the financial highlights for each of the periods indicated therein. These financial statements and financial highlights are the responsibility of the Fund's management. Our responsibility is to express an opinion on these financial statements and financial highlights based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements and financial highlights are free of material misstatement. We were not engaged to perform an audit of the Fund's internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Fund's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements and financial highlights, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our procedures included confirmation of securities owned as of December 31, 2013, by correspondence with the custodian and brokers, or by other appropriate auditing procedures where replies from the brokers were not received. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements and financial highlights referred to above present fairly, in all material respects, the financial position of Mutual Financial Services Fund (one of the funds constituting Franklin Mutual Series Funds) at December 31, 2013, the results of its operations for the year then ended, the changes in its net assets for each of the two years in the period then ended, and the financial highlights for each of the periods indicated therein, in conformity with U.S. generally accepted accounting principles.

Ernet + Young LLP

Boston, Massachusetts February 19, 2014

Tax Information (unaudited)

Under Section 854(b)(1)(A) of the Internal Revenue Code (Code), the Fund hereby reports 42.59% of the ordinary income dividends as income qualifying for the dividends received deduction for the fiscal year ended December 31, 2013.

Under Section 854(b)(1)(B) of the Code, the Fund hereby reports the maximum amount allowable but no less than \$7,308,579 as qualified dividends for purposes of the maximum rate under Section 1(h)(11) of the Code for the fiscal year ended December 31, 2013. Distributions, including qualified dividend income, paid during calendar year 2013 will be reported to shareholders on Form 1099-DIV by mid-February 2014. Shareholders are advised to check with their tax advisors for information on the treatment of these amounts on their individual income tax returns.

At December 31, 2013, more than 50% of the Fund's total assets were invested in securities of foreign issuers. In most instances, foreign taxes were withheld from income paid to the Fund on these investments. As shown in the table below, the Fund hereby reports to shareholders the foreign source income and foreign taxes paid, pursuant to Section 853 of the Code. This written statement will allow shareholders of record on December 19, 2013, to treat their proportionate share of foreign taxes paid by the Fund as having been paid directly by them. The shareholder shall consider these amounts as foreign taxes paid in the tax year in which they receive the Fund distribution.

The following table provides a detailed analysis of foreign tax paid, foreign source income and foreign qualified dividends as reported by the Fund, to Class Z, Class A, Class C and Class R6 shareholders of record.

Class	Foreign Tax Paid Per Share	Foreign Source Income Per Share	Foreign Source Qualified Dividends Per Share
Class Z	\$0.0263	\$0.2295	\$0.1378
Class A	\$0.0263	\$0.1923	\$0.1154
Class C	\$0.0263	\$0.1032	\$0.0618
Class R6	\$0.0263	\$0.1460	\$0.0861

Foreign Tax Paid Per Share (Column 1) is the amount per share available to you, as a tax credit (assuming you held your shares in the Fund for a minimum of 16 days during the 31-day period beginning 15 days before the ex-dividend date of the Fund's distribution to which the foreign taxes relate), or, as a tax deduction.

Tax Information (unaudited) (continued)

Foreign Source Income Per Share (Column 2) is the amount per share of income dividends attributable to foreign securities held by the Fund, plus any foreign taxes withheld on these dividends. The amounts reported include foreign source qualified dividends that have not been adjusted for the rate differential applicable to such dividend income.¹

Foreign Qualified Dividends Per Share (Column 3) is the amount per share of foreign source qualified dividends plus any foreign taxes withheld on these dividends. These amounts represent the portion of the Foreign Source Income reported to you in column 2 that were derived from qualified foreign securities held by the Fund.¹

By mid-February 2014, shareholders will receive Form 1099-DIV which will include their share of taxes paid and foreign source income distributed during the calendar year 2013. The Foreign Source Income reported on Form 1099-DIV has not been adjusted for the rate differential on foreign source qualified dividend income. Shareholders are advised to check with their tax advisors for information on the treatment of these amounts on their 2013 individual income tax returns.

Qualified dividends are taxed at reduced long term capital gains tax rates. In determining the amount of foreign tax credit that may be applied against the U.S. tax liability of individuals receiving foreign source qualified dividends, adjustments may be required to the foreign tax credit limitation calculation to reflect the rate differential applicable to such dividend income. The rules however permit certain individuals to elect not to apply the rate differential adjustments for capital gains and/or dividends for any taxable year. Please consult your tax advisor and the instructions to Form 1116 for more information.

Board Members and Officers

The name, year of birth and address of the officers and board members, as well as their affiliations, positions held with the Fund, principal occupations during at least the past five years and number of portfolios overseen in the Franklin Templeton Investments fund complex are shown below. Generally, each board member serves until that person's successor is elected and qualified.

Independent Board Members

Name, Year of Birth and Address	Position	Length of Time Served	Number of Portfolios in Fund Complex Overseen by Board Member*	Other Directorships Held During at Least the Past 5 Years
Edward I. Altman, Ph.D. (1941)	Trustee	Since 1987	11	None
c/o Franklin Mutual Advisers, LLC				
101 John F. Kennedy Parkway				
Short Hills N I 07078-2789				

Principal Occupation During at Least the Past 5 Years:

Max L. Heine Professor of Finance and Director of The Credit and Debt Markets Research Program, Salomon Center, Stern School of Business, New York University; editor and author of numerous financial publications; financial consultant; an adviser to numerous financial publishing organizations; and formerly, Vice Director, Salomon Center, Stern School of Business, New York University.

Ann Torre Bates (1958) c/o Franklin Mutual Advisers, LLC 101 John F. Kennedy Parkway Short Hills, NJ 07078-2789	Trustee	Since 1995	38	SLM Corporation (Sallie Mae), Ares Capital Corporation (specialty finance company), Allied Capital Corporation (financial services) (2003-2010) and United Natural Foods, Inc.,
				(October 2013).

Principal Occupation During at Least the Past 5 Years:

Director of various companies; and formerly, Executive Vice President and Chief Financial Officer, NHP Incorporated (manager of multifamily housing) (1995-1997); and Vice President and Treasurer, US Airways, Inc. (until 1995).

Burton J. Greenwald (1929)	Trustee	Since 2002	18	Franklin Templeton Emerging Markets
c/o Franklin Mutual Advisers, LLC				Debt Opportunities Fund PLC and
101 John F. Kennedy Parkway				Fiduciary International Ireland
Short Hills, NJ 07078-2789				Limited.

Principal Occupation During at Least the Past 5 Years:

Managing Director, B.J. Greenwald Associates (management consultants to the financial services industry); and formerly, Chairman, Fiduciary Trust International Funds; Executive Vice President, L.F Rothschild Fund Management, Inc.; President and Director, Merit Mutual Funds; President, Underwriting Division and Director, National Securities & Research Corporation; Governor, Investment Company Institute; and Chairman, ICI Public Information Committee.

Name, Year of Birth and Address	Position	Length of Time Served	Number of Portfolios in Fund Complex Overseen by Board Member*	Other Directorships Held During at Least the Past 5 Years
Keith E. Mitchell (1954) c/o Franklin Mutual Advisers, LLC	Trustee	Since 2009	11	None

101 John F. Kennedy Parkway Short Hills, NJ 07078-2789

Principal Occupation During at Least the Past 5 Years:

Managing Member, Mitchell, Hartley & Bechtel Advisers, LLC (formerly, Mitchell Advisers, LLC) (advisory firm); director of various boards of asset management firms; and formerly, Managing Director, Putnam Lovell NBF.

Trustee Since 1998 Charles Rubens II (1930) None c/o Franklin Mutual Advisers, LLC 101 John F. Kennedy Parkway Short Hills, NJ 07078-2789

Principal Occupation During at Least the Past 5 Years:

Private investor and president of non-profit organizations; and formerly, an executive of Time, Inc.; and Trustee of Colorado College.

Since 2009 11 None Jan Hopkins Trachtman (1947) Trustee c/o Franklin Mutual Advisers, LLC 101 John F. Kennedy Parkway Short Hills, NJ 07078-2789

Principal Occupation During at Least the Past 5 Years:

President and Founder, The Jan Hopkins Group (communications consulting firm); President, Economic Club of New York; serves on Advisory Board of Knight Bagehot Fellowship; and formerly, Anchor/Correspondent, CNN Financial News (until 2003); Managing Director and Head of Client Communications, Citigroup Private Bank (until 2005); Off-Air Reporter, ABC News' World News Tonight; and Editor, CBS Network News.

Robert E. Wade (1946) Trustee since El Oro Ltd (investments). Trustee and c/o Franklin Mutual Advisers, LLC Chairman of 1993 and 101 John F. Kennedy Parkway Chairman of the the Board Short Hills, NJ 07078-2789 Board since 2005

Principal Occupation During at Least the Past 5 Years:

Attorney at law engaged in private practice (1972-2008) and member of various boards.

Interested Board Members and Officers

Name, Year of Birth and Address	Position	Length of Time Served	Number of Portfolios in Fund Complex Overseen by Board Member*	Other Directorships Held During at Least the Past 5 Years
**Gregory E. Johnson (1961)	Trustee	Since 2007	152	None
One Franklin Parkway				
San Mateo, CA 94403-1906				

Principal Occupation During at Least the Past 5 Years:

Chairman of the Board, Member - Office of the Chairman, Director, President and Chief Executive Officer, Franklin Resources, Inc.; officer and/or director or trustee, as the case may be, of some of the other subsidiaries of Franklin Resources, Inc. and of 44 of the investment companies in Franklin Templeton Investments; and Chairman, Investment Company Institute.

Name, Year of Birth and Address	Position	Length of Time Served	Number of Portfolios in Fund Complex Overseen by Board Member*	Other Directorships Held During at Least the Past 5 Years
**Peter A. Langerman (1955) c/o Franklin Mutual Advisers, LLC 101 John F. Kennedy Parkway Short Hills, NJ 07078-2702	Trustee, President and Chief Executive Officer – Investment Management	Trustee since 2007, President and Chief Executive Officer – Investment Management since 2005	11	American International Group, Inc. (AIG) Credit Facility Trust (2010–2011).

Principal Occupation During at Least the Past 5 Years:

Chairman of the Board, Chief Executive Officer and President, Franklin Mutual Advisers, LLC; officer and/or director, as the case may be, of four of the investment companies in Franklin Templeton Investments.

Alison E. Baur (1964)	Vice President	Since 2012	Not Applicable	Not Applicable
One Franklin Parkway				
San Mateo, CA 94403-1906				

Principal Occupation During at Least the Past 5 Years:

Deputy General Counsel, Franklin Templeton Investments; and officer of some of the other subsidiaries of Franklin Resources, Inc. and of 46 of the investment companies in Franklin Templeton Investments.

Philippe Brugere-Trelat (1949)	Vice President	Since 2005	Not Applicable	Not Applicable
101 John F. Kennedy Parkway				
Short Hills, NJ 07078-2789				

Principal Occupation During at Least the Past 5 Years:

Executive Vice President, Franklin Mutual Advisers, LLC; officer of three of the investment companies in Franklin Templeton Investments; and formerly, Portfolio Manager of Eurovest SA (French registered Investment Company, Sicav).

Laura F. Fergerson (1962)	Chief Executive Since 2009	Not Applicable	Not Applicable	
One Franklin Parkway	Officer –			
San Mateo, CA 94403-1906	Finance and			
	Administration			

Principal Occupation During at Least the Past 5 Years:

Senior Vice President, Franklin Templeton Services, LLC; and officer of 46 of the investment companies in Franklin Templeton Investments.

Aliya S. Gordon (1973)	Vice President	Since 2009	Not Applicable	Not Applicable
One Franklin Parkway				
San Mateo CA 94403-1906				

Principal Occupation During at Least the Past 5 Years:

Senior Associate General Counsel, Franklin Templeton Investments; officer of 46 of the investment companies in Franklin Templeton Investments; and formerly, Litigation Associate, Steefel, Levitt & Weiss, LLP (2000-2004).

Steven J. Gray (1955) One Franklin Parkway San Mateo, CA 94403-1906	,	Secretary since 2005 and Vice President since	Not Applicable	Not Applicable
		2009		

Principal Occupation During at Least the Past 5 Years:

Senior Associate General Counsel, Franklin Templeton Investments; Vice President, Franklin Templeton Distributors, Inc.; and officer of 46 of the investment companies in Franklin Templeton Investments.

Name, Year of Birth and Address	Position	Length of		Other Directorships Held During at Least the Past 5 Years
Selena L. Holmes (1965)	Vice President	Since 2012	Not Applicable	Not Applicable

100 Fountain Parkway AML St. Petersburg, FL 33716-1205 Compliance

Principal Occupation During at Least the Past 5 Years:

Director, Global Compliance Monitoring; and officer of 46 of the investment companies in Franklin Templeton Investments.

Robert Kubilis (1973) Since 2012 Not Applicable Not Applicable Treasurer, 300 S.E. 2nd Street Chief Financial Fort Lauderdale, FL 33301-1923 Officer and Chief Accounting Officer

Principal Occupation During at Least the Past 5 Years:

Assistant Treasurer, Fund Accounting, Franklin Templeton Investments; and officer of five of the investment companies in Franklin Templeton Investments.

Kimberly H. Novotny (1972) Vice President Since March 2013 Not Applicable Not Applicable

300 S.E. 2nd Street

Fort Lauderdale, FL 33301-1923

Principal Occupation During at Least the Past 5 Years:

Associate General Counsel, Franklin Templeton Investments; Vice President and Secretary, Fiduciary Trust International of the South; Vice President, Templeton Investment Counsel, LLC; Assistant Secretary, Franklin Resources, Inc.; and officer of 46 of the investment companies in Franklin Templeton Investments.

Robert C. Rosselot (1960)	Chief	Since March 2013	Not Applicable	Not Applicable
300 S.E. 2nd Street	Compliance			
Fort Lauderdale, FL 33301-1923	Officer			

Principal Occupation During at Least the Past 5 Years:

Director, Global Compliance, Franklin Templeton Investments; officer of 46 of the investment companies in Franklin Templeton Investments; and formerly, Senior Associate General Counsel, Franklin Templeton Investments (2007-2013); and Secretary and Vice President, Templeton Group of Funds (2004-2013).

Karen L. Skidmore (1952)	Vice President	Since 2009	Not Applicable	Not Applicable	
One Franklin Parkway					
San Mateo, CA 94403-1906					

Principal Occupation During at Least the Past 5 Years:

Senior Associate General Counsel, Franklin Templeton Investments; and officer of 46 of the investment companies in Franklin Templeton Investments.

Craig S. Tyle (1960)	Vice President	Since 2005	Not Applicable	Not Applicable
One Franklin Parkway				
San Mateo, CA 94403-1906				

Principal Occupation During at Least the Past 5 Years:

General Counsel and Executive Vice President, Franklin Resources, Inc.; and officer of some of the other subsidiaries of Franklin Resources, Inc. and of 46 of the investment companies in Franklin Templeton Investments.

Name, Year of Birth and Address	Position	Length of	Number of Portfolios in Fund Complex Overseen by Board Member*	Other Directorships Held During at Least the Past 5 Years
------------------------------------	----------	-----------	--	--

Lori A. Weber (1964)

300 S.E. 2nd Street

Fort Lauderdale, FL 33301-1923

Not Applicable

Not Applicable

Principal Occupation During at Least the Past 5 Years:

Senior Associate General Counsel, Franklin Templeton Investments; Assistant Secretary, Franklin Resources, Inc.; Vice President and Secretary, Templeton Investment Counsel, LLC; Vice President, Fiduciary Trust International of the South; and officer of 46 of the investment companies in Franklin Templeton Investments.

*We base the number of portfolios on each separate series of the U.S. registered investment companies within the Franklin Templeton Investments fund complex. These portfolios have a common investment manager or affiliated investment managers.

**Gregory E. Johnson is considered to be an interested person of the Fund under the federal securities laws due to his position as an officer and director of Franklin Resources, Inc., which is the parent company of the Fund's investment manager and distributor. Peter A. Langerman is considered to be an interested person of the Fund under the federal securities laws due to his position as an officer of Franklin Mutual Advisers, LLC, which is an affiliate of the Fund's investment manager.

Note 1: Officer information is current as of the date of this report. It is possible that after this date, information about officers may change.

Vice President Since 2011

The Fund's Board has determined that certain of the members of the Audit Committee, including Ann Torre Bates, are audit committee financial experts, and "independent," under those provisions of the Sarbanes-Oxley Act of 2002, and the rules and form amendments adopted by the Securities and Exchange Commission, relating to audit committee financial experts.

The Statement of Additional Information (SAI) includes additional information about the board members and is available, without charge, upon request. Shareholders may call (800) DIAL BEN/342-5236 to request the SAI.

Shareholder Information

Proxy Voting Policies and Procedures

The Fund's investment manager has established Proxy Voting Policies and Procedures (Policies) that the Fund uses to determine how to vote proxies relating to portfolio securities. Shareholders may view the Fund's complete Policies online at franklintempleton.com. Alternatively, shareholders may request copies of the Policies free of charge by calling the Proxy Group collect at (954) 527-7678 or by sending a written request to: Franklin Templeton Companies, LLC, 300 S.E. 2nd Street, Fort Lauderdale, FL 33301, Attention: Proxy Group. Copies of the Fund's proxy voting records are also made available online at franklintempleton.com and posted on the U.S. Securities and Exchange Commission's website at sec.gov and reflect the most recent 12-month period ended June 30.

Quarterly Statement of Investments

The Fund files a complete statement of investments with the U.S. Securities and Exchange Commission for the first and third quarters for each fiscal year on Form N-Q. Shareholders may view the filed Form N-Q by visiting the Commission's website at sec.gov. The filed form may also be viewed and copied at the Commission's Public Reference Room in Washington, DC. Information regarding the operations of the Public Reference Room may be obtained by calling (800) SEC-0330.

Householding of Reports and Prospectuses

You will receive the Fund's financial reports every six months as well as an annual updated summary prospectus (prospectus available upon request). To reduce Fund expenses, we try to identify related shareholders in a household and send only one copy of the financial reports and summary prospectus. This process, called "householding," will continue indefinitely unless you instruct us otherwise. If you prefer not to have these documents householded, please call us at (800) 632-2301. At any time you may view current prospectuses/summary prospectuses and financial reports on our website. If you choose, you may receive these documents through electronic delivery.

This page intentionally left blank.

This page intentionally left blank.

Franklin Templeton Funds

Literature Request. To receive a summary prospectus and/or prospectus, please call us at (800) DIAL BEN/342-5236 or visit franklintempleton.com or etf.franklintempleton.com for Franklin Short Duration U.S. Government ETF. Investors should carefully consider a fund's investment goals, risks, charges and expenses before investing. The prospectus contains this and other information. Please carefully read a prospectus before investing.

VALUE

Franklin All Cap Value Fund
Franklin Balance Sheet Investment Fund
Franklin Large Cap Value Fund
Franklin MicroCap Value Fund
Franklin MidCap Value Fund
Franklin Small Cap Value Fund
Mutual Beacon Fund
Mutual Quest Fund
Mutual Recovery Fund²
Mutual Shares Fund

BLEND

Franklin Focused Core Equity Fund Franklin Large Cap Equity Fund Franklin Rising Dividends Fund

GROWTH

Franklin DynaTech Fund Franklin Flex Cap Growth Fund Franklin Growth Fund Franklin Growth Opportunities Fund Franklin Small Cap Growth Fund Franklin Small-Mid Cap Growth Fund

SECTOR

Franklin Biotechnology Discovery Fund Franklin Global Listed Infrastructure Fund Franklin Global Real Estate Fund Franklin Gold & Precious Metals Fund Franklin Natural Resources Fund Franklin Real Estate Securities Fund Franklin Utilities Fund Mutual Financial Services Fund

GLOBAL

Franklin World Perspectives Fund Mutual Global Discovery Fund Templeton Global Opportunities Trust Templeton Global Smaller Companies Fund Templeton Growth Fund Templeton World Fund

INTERNATIONAL

Franklin India Growth Fund
Franklin International Growth Fund
Franklin International Small Cap Growth Fund
Mutual European Fund
Mutual International Fund
Templeton Asian Growth Fund
Templeton BRIC Fund
Templeton China World Fund
Templeton Developing Markets Trust
Templeton Emerging Markets Small Cap Fund
Templeton Foreign Fund
Templeton Foreign Smaller Companies Fund
Templeton Frontier Markets Fund

HYBRID

Franklin Balanced Fund
Franklin Convertible Securities Fund
Franklin Equity Income Fund
Franklin Income Fund
Templeton Emerging Markets Balanced Fund
Templeton Global Balanced Fund

ALTERNATIVE

Franklin K2 Alternative Strategies Fund Franklin Pelagos Commodities Strategy Fund

ASSET ALLOCATION

Franklin LifeSmart™ Retirement Target Funds (2015-2050)⁶

Franklin Templeton Corefolio® Allocation Fund
Franklin Templeton Founding Funds Allocation Fund
Franklin Templeton Conservative Allocation Fund
Franklin Templeton Growth Allocation Fund
Franklin Templeton Moderate Allocation Fund
Franklin Templeton Global Allocation Fund
Franklin Templeton Multi-Asset Real Return Fund

FIXED INCOME

Franklin Adjustable U.S. Government Securities Fund⁷ Franklin Floating Rate Daily Access Fund Franklin Global Government Bond Fund Franklin High Income Fund Franklin Limited Maturity U.S. Government Securities Fund⁷

Franklin Low Duration Total Return Fund

Franklin Real Return Fund

Franklin Short Duration U.S. Government ETF

Franklin Strategic Income Fund Franklin Strategic Mortgage Portfolio Franklin Templeton Hard Currency Fund

Franklin Total Return Fund

Franklin U.S. Government Securities Fund⁷
Templeton Constrained Bond Fund
Templeton Emerging Markets Bond Fund
Templeton Global Bond Fund
Templeton Global Total Return Fund
Templeton International Bond Fund

TAX-FREE INCOME®

National

Double Tax-Free Income Fund⁹ Federal Tax-Free Income Fund High Yield Tax-Free Income Fund Insured Tax-Free Income Fund^{10,11}

Limited-/Intermediate-Term

California Intermediate-Term Tax-Free Income Fund Federal Intermediate-Term Tax-Free Income Fund Federal Limited-Term Tax-Free Income Fund New York Intermediate-Term Tax-Free Income Fund

State-Specific

Alabama	Kentucky	New York
Arizona	Louisiana	(2 funds)
California	Maryland	North Carolina
(4 funds)11	Massachusetts	Ohio
Colorado	Michigan	Oregon
Connecticut	Minnesota	Pennsylvania
Florida	Missouri	Tennessee
Georgia	New Jersey	Virginia

INSURANCE FUNDS

Franklin Templeton Variable Insurance Products Trust¹²

- 1. The fund is closed to new investors. Existing shareholders and select retirement plans may add to their accounts.
- 2. The fund is a continuously offered, closed-end fund. Shares may be purchased daily; there is no daily redemption. However, each quarter, pending board approval, the fund will authorize the repurchase of 5%–25% of the outstanding number of shares. Investors may tender all or a portion of their shares during the tender period.
- 3. Effective 6/3/13, the fund closed to new investors, with limited exceptions.
- 4. Effective 12/10/13, the fund closed to new investors, with limited exceptions.
- 5. Effective 6/28/13, the fund closed to new investors. Existing shareholders and select retirement plans may add to their accounts.
- 6. Effective 5/1/13, the Franklin Templeton Retirement Target Funds changed their names to Franklin LifeSmart Retirement Target Funds. The funds' investment goals and principal investment strategies remained unchanged. These funds' target dates are in five-year increments.

- 7. An investment in the fund is neither insured nor guaranteed by the U.S. government or by any other entity or institution.
- 8. For investors subject to the alternative minimum tax, a small portion of fund dividends may be taxable. Distributions of capital gains are generally taxable.
- 9. The fund is closed to all new investments (other than reinvestment of dividends and capital gains distributions).
- 10. The fund invests primarily in insured municipal securities.
- 11. Effective at the close of market on 3/1/13, Franklin Insured Tax-Free Income Fund and Franklin California Insured Tax-Free Income Fund closed to all new investments (other than reinvestment of dividends and capital gains distributions).
- 12. The funds of the Franklin Templeton Variable Insurance Products Trust are generally available only through insurance company variable contracts.

VALUE | BLEND | GROWTH | SECTOR | GLOBAL | INTERNATIONAL | HYBRID | ALTERNATIVE | ASSET ALLOCATION | FIXED INCOME | TAX-FREE INCOME



< GAIN FROM OUR PERSPECTIVE® >

Annual Report and Shareholder Letter MUTUAL FINANCIAL SERVICES FUND

Investment Manager

Franklin Mutual Advisers. LLC

Distributor

Franklin Templeton Distributors, Inc. (800) DIAL BEN®/342-5236 franklintempleton.com

Shareholder Services

(800) 632-2301 - (Class A, C & R6 (800) 448-FUND - (Class Z)

Authorized for distribution only when accompanied or preceded by a summary prospectus and/or prospectus. Investors should carefully consider a fund's investment goals, risks, charges and expenses before investing. A prospectus contains this and other information; please read it carefully before investing.

To ensure the highest quality of service, telephone calls to or from our service departments may be monitored, recorded and accessed. These calls can be identified by the presence of a regular begoing tone.