

Franklin Total Return Fund

Advisor Class: FBDAX Class A: FKBA

Commentary | as of March 31, 2026

Key Takeaways

- **Markets:** The war in the Middle East, which began in late February when the United States and Israel struck Iran, dominated much of the news flow and financial market sentiment over the remainder of the quarter. The reaction in markets has evolved, initially seeing a traditional risk-off move in both the US dollar and US bonds, which then turned into a stagflationary-focused selloff in core developed bond markets as oil prices surged (although the dollar remained well-supported). The US Federal Reserve (Fed) remained on hold throughout the quarter. The March Federal Open Market Committee (FOMC) meeting statement and press conference emphasized uncertainty related to the Iran war, indicating that the Fed would look through any initial oil supply shock effect on inflation to focus on core developments, while also noting a likely dragging effect on the economy; ultimately the Committee retained an easing bias. Fixed income volatility measures rose during the quarter, with much of the increase coming in the wake of the onset of the war in the Middle East. Credit spreads rose over the quarter, with the increase significantly more pronounced in the high-yield sector; total returns in corporate bonds were negative over the quarter. Securitized sectors generated a positive excess return versus duration-matched Treasuries. US Treasury (UST) yields moved higher across the curve over the three-month period, resulting in a broader upward shift in the interest rate environment. By the end of the period, the yield on the benchmark 10-year UST note had risen by 15 basis points to 4.32%.
- **Contributors:** Out-of-index allocations to residential mortgage-backed securities (RMBS), collateralized loan obligations (CLOs) and collateralized mortgage obligations (CMOs). Security selection in investment-grade (IG) corporate bonds. Yield curve exposure.
- **Detractors:** Overweight exposure to IG corporate bonds and sovereign emerging market (EM) debt. Out-of-index holdings of high-yield (HY) corporate bonds and senior-secured floating-rate bank loans. Security selection in HY corporate bonds.
- **Outlook:** Looking ahead into 2026, we have a favorable view toward the US economy, which remains resilient despite rising external pressures. Impending fiscal stimulus and an intact artificial intelligence (AI)-driven capital expenditure cycle could offset consumption drags. While our GDP growth forecast faces downside risks, structural expansion continues, making slower growth far more likely than a recession. Meanwhile, we expect the Federal Reserve to hold rates steady to combat any persistent inflation risks.
- Fixed income spreads remain tight on a historical basis, but they still provide opportunities when looked at from an income and yield prospective.

Fund Characteristics

| Fund Characteristics | Fund |
|---|---------|
| Distribution Frequency | Monthly |
| 30-Day SEC Yield (Advisor Class)—With Waiver | 4.45% |
| 30-Day SEC Yield (Advisor Class)—Without Waiver | 4.26% |

Performance Review

- **Sector allocations detracted from performance,** led by overweight allocations to IG corporate bonds and sovereign EM debt, along an out-of-index exposure to HY corporate bonds and senior-secured floating-rate bank loans. In contrast, an out-of-index allocation to RMBS, CLOs and CMOs lifted returns.
- **Security selection contributed to returns** for the quarter, led by selection in IG corporate bonds. Selection in HY corporate bonds curbed results.
- **Yield curve exposure supported performance.**

Outlook

- US growth has remained surprisingly resilient despite a steady stream of bearish narratives. While rising energy costs tied to escalating Middle East tensions, if sustained, will likely squeeze consumption, the impending fiscal stimulus should offset part of the drag. Meanwhile, the AI-driven capital expenditure (capex) cycle remains intact. Our above-consensus forecast of 3.0% for 2026 US gross domestic product (GDP) growth now faces some downside risk. While recession risk is no longer negligible, it remains a tail risk. The more likely outcome is slower growth, not contraction, with the structural expansion still intact. We expect the Fed to remain on hold through the end of Chair Jerome Powell's term and potentially throughout the year given rising upside risks to inflation. Should inflation broaden beyond energy and become persistent, the Fed could be forced to keep rates higher for longer or even consider renewed tightening.
- While the 2026 FOMC dot plot distribution has narrowed and some participants have shifted their projections higher, the maintenance of unchanged medians suggests a relatively low bar for renewed easing. We feel that as long as growth remains resilient and the expansion continues in line with our expectations, the Fed will remain on pause at least through the end of Powell's term in May 2026, despite their signals of a potential cut. That said, any signs of labor market weakness or evidence that the supply-driven oil price shock is spilling over into core inflation or inflation expectations could force a policy reaction under Powell or his successor. If our views on growth and inflation prove correct and the Fed cuts fewer times than currently priced, we believe US Treasury yields should drift higher, though somewhat favorable demand-supply technicals may limit the extent of this move.
- While IG corporate bond spreads widened recently due to geopolitical tensions and rising energy prices, reaching their widest levels since May 2025, spreads remain broadly contained as investor demand for attractive all-in yields and consistent inflows continue to provide strong technical support. Corporate fundamentals generally remain supportive, with most IG-rated issuers maintaining the balance sheet flexibility to manage through shifting economic conditions. Nevertheless, macroeconomic crosscurrents and technological disruptions are creating notable dispersion across the market. Looking ahead, new-issue supply is projected to reach record-breaking levels in 2026, acting as a multiyear technical headwind driven heavily by AI-related infrastructure and capital expenditures. We remain focused on industry and company fundamentals, the health of balance sheets, generation and use of free cash flow and the resiliency of credits to slower economic growth, while we are cautious on deeply distressed names. The US HY default rate (including distressed

exchanges) increased marginally in March but remains below long-term averages, ending the month at 2.07%. While valuations have adjusted modestly, the market continues to price in a sanguine outlook with minimal room for error, favoring a balanced risk posture with a bias toward non-cyclical sectors.

- With mortgage rates remaining above 6%, prepayment risk remains near historically low levels, as limited refinancing incentives keep prepayments subdued. Our outlook on agency mortgage-backed securities (MBS) is neutral to cautiously constructive in the near term, supported by strong mortgage credit quality and the backstop provided by GSE purchase programs. Value remains present in bonds backed by moderately seasoned, higher-coupon Ginnie Mae collateral, which offer attractive spread premiums. Overall, we maintain a neutral view of the residential MBS (RMBS) sector is maintained, given rich valuations and our expectations for muted home price growth. Despite stretched housing affordability, US homeowner fundamentals remain well-positioned. Low unemployment, modest wage growth, steady household formation and ongoing inventory shortages should continue to support home prices, while significant accumulated equity helps contain delinquencies. Preference continues to be for short or seasoned collateral, such as senior AAA-rated bonds across the non-QM, prime jumbo and HELOC subsectors, which are more insulated against macroeconomic shocks and offer limited extension risk. In the commercial real estate sector, generic spreads do not currently reflect underlying risks, namely higher rates and the potential for further labor market deterioration. Furthermore, underwriting standards are deteriorating, particularly in conduit deals, as a growing percentage of weaker-tier assets are included. Despite these headwinds, specific opportunities remain attractive in extension bonds given their shorter spread duration, natural liquidity from payoffs and lower beta to macroeconomic and corporate credit spreads. Additionally, commercial mortgage-backed securities (CMBS) interest-only bonds can mitigate against refinancing difficulties, supporting a constructive approach to current positioning.

Average annual total returns and fund expenses (%) - as of March 31, 2026

| Class | CUSIP | Ticker | Without Sales Charge | | | | | | | With Maximum Sales Charge | | | | | | | Expenses | | Sales Charges | | Inception Date |
|---------------|-----------|--------|----------------------|-------|------|------|------|-------|-----------|---------------------------|-------|------|------|-------|-------|-----------|----------|------|----------------|------|----------------|
| | | | 3-Mo | YTD | 1-Yr | 3-Yr | 5-Yr | 10-Yr | Inception | 3-Mo | YTD | 1-Yr | 3-Yr | 5-Yr | 10-Yr | Inception | Gross | Net | Initial Charge | CDSC | |
| Advisor Class | 353612849 | FBDAX | -0.21 | -0.21 | 4.43 | 3.81 | 0.28 | 1.79 | 4.09 | -0.21 | -0.21 | 4.43 | 3.81 | 0.28 | 1.79 | 4.09 | 0.67 | 0.48 | — | — | 8/3/1998 |
| Class A | 353612856 | FKBAX | -0.28 | -0.28 | 4.20 | 3.58 | 0.06 | 1.55 | 3.84 | -4.04 | -4.04 | 0.34 | 2.26 | -0.70 | 1.16 | 3.69 | 0.93 | 0.73 | 3.75 | — | 8/3/1998 |
| Benchmark | — | — | -0.05 | -0.05 | 4.35 | 3.63 | 0.31 | 1.70 | — | -0.05 | -0.05 | 4.35 | 3.63 | 0.31 | 1.70 | — | — | — | — | — | |

Benchmark(s)

Benchmark = Bloomberg U.S. Aggregate Index

Performance data quoted represents past performance, which does not guarantee future results. Current performance may be lower or higher than the figures shown. Principal value and investment returns will fluctuate, and investors' shares, when redeemed, may be worth more or less than the original cost. Performance would have been lower if fees had not been waived in various periods. Total returns assume the reinvestment of all distributions and the deduction of all fund expenses. Returns with sales charge reflect a deduction of the stated maximum sales charge. An investor cannot invest directly in an index, and unmanaged index returns do not reflect any fees, expenses or sales charges. Returns for periods of less than one year are not annualized. All classes of shares may not be available to all investors or through all distribution channels. For current month-end performance, please visit franklintempleton.com.

The fund began offering Advisor Class shares on 8/3/1998. Performance quotations have been calculated as follows: (a) for Advisor Class periods prior to 8/3/1998, a restated figure is used based on the fund's Class A performance. The performance was adjusted to take into account differences in class-specific operating expenses and maximum sales charges. (b) For periods after share class offering, performance for the specific share class is used, reflecting the expenses and maximum sales charges applicable to that class.

Gross expenses are the fund's total annual operating expenses as of the fund's prospectus available at the time of publication. Actual expenses may be higher and may impact portfolio returns. Net expenses reflect contractual fee waivers, expense caps and/or reimbursements, which cannot be terminated prior to 02/28/2027 without Board consent. Additional amounts may be voluntarily waived and/or reimbursed and may be modified or discontinued at any time without notice.

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

What are the Risks?

All investments involve risks, including possible loss of principal. Fixed income securities involve interest rate, credit, inflation and reinvestment risks, and possible loss of principal. As interest rates rise, the value of fixed income securities falls. **Asset-backed, mortgage-backed or mortgage-related securities** are subject to prepayment and extension risks. **Changes in the credit rating** of a bond, or in the credit rating or financial strength of a bond's issuer, insurer or guarantor, may affect the bond's value. **Low-rated, high-yield bonds** are subject to greater price volatility, illiquidity and possibility of default. **International investments** are subject to special risks, including currency fluctuations and social, economic and political uncertainties, which could increase volatility. These risks are magnified in **emerging markets**. **Derivative instruments** can be illiquid, may disproportionately increase losses, and have a potentially large impact on performance. The manager may consider **environmental, social and governance (ESG) criteria** in the research or investment process; however, ESG considerations may not be a determinative factor in security selection. In addition, the manager may not assess every investment for ESG criteria, and not every ESG factor may be identified or evaluated. These and other risks are discussed in the fund's prospectus.

Glossary

A **basis point (bp, or bps)** is one one-hundredth of one percent (1/100% or 0.01%).

Capital Expenditure (capex) are funds used by a company to acquire or upgrade physical assets such as property, industrial buildings or equipment.

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

Commercial mortgage-backed securities (CMBS) are a type of mortgage-backed security backed by commercial mortgages rather than residential real estate. CMBS tend to be more complex and volatile than residential mortgage-backed securities due to the unique nature of the underlying property assets.

Duration is a measure of the sensitivity of a bond's price to changes in interest rates.

Free cash flow (FCF) is a measure of financial performance calculated as operating cash flow minus capital expenditures.

Gross domestic product (GDP) is the market value of all final goods and services produced within a country in a given period of time.

Residential mortgage-backed securities (RMBS) are a type of mortgage-backed debt obligation created from residential debt, such as mortgages, home-equity loans and subprime mortgages.

Stagflation is a seemingly contradictory condition described by slow economic growth and relatively high unemployment, or economic stagnation, which is at the same time accompanied by rising prices (i.e. inflation).

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

Important Information

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

The **Bloomberg US Aggregate Index** is comprised of investment-grade, U.S. dollar-denominated government, corporate, and mortgage- and asset-backed issues having at least one year to maturity.

Source: Bloomberg Indices.

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

The **30-day SEC yield** is calculated using the net income (interest and dividends) per share earned over a trailing 30-day period (annualized), divided by the fund's share price at the end of that period. It may not equal the fund's actual income distribution rate, which reflects the fund's past dividends paid to shareholders.

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