FRANKLIN TEMPLETON

Franklin Total Return Fund

Advisor Class: FBDAX Class A: FKBAX | **Commentary | as of June 30, 2026**

Key Takeaways

- **Markets**: Some of the risk aversion that had characterized financial markets at the end of the previous quarter eased during the second quarter, although geopolitical developments remained a key focus. The Middle East conflict continued to drive sentiment through the quarter, with markets reacting to shifting news around negotiations, before the United States and Iran signed a 14-point Memorandum of Understanding (MOU) in late June. The MOU formalized a ceasefire, established a 60-day negotiation framework and included provisions to restore shipping through the Strait of Hormuz. The US dollar was modestly stronger over the quarter, appreciating against most other currencies. The Federal Reserve (Fed) kept policy rates unchanged, but its tone became more hawkish overall as internal disagreement over the easing bias increased; minutes suggested rates could remain unchanged for longer and the June meeting removed previous easing guidance despite a more dovish press conference from new Fed Chair Kevin Warsh. Fixed income volatility measures eased during the quarter as risk aversion retreated somewhat. For similar reasons, credit spreads narrowed over the quarter, with the declines more pronounced in the high-yield sectors. Total returns on corporate bonds were positive over the quarter. Securitized sectors generated a positive excess return versus duration-matched Treasuries. Over the period, the US Treasury (UST) yield curve experienced a bear flattening, as short-to-intermediate rates rose more sharply than long-term rates. By the end of the period, the benchmark 10-year UST yield rose by 15 basis points (bps) to 4.47%.
- **Contributors**: Overweight allocations to investment-grade (IG) corporate bonds, sovereign emerging market (EM) debt and commercial mortgage-backed securities (CMBS). Out-of-index allocations to high-yield (HY) corporate bonds, collateralized loan obligations (CLOs), collateralized mortgage obligations (CMOs) and senior-secured floating-rate bank loans. Security selection in HY corporate bonds and municipal bonds.
- **Detractors**: Underweight allocation to sovereign developed market debt. Security selection in IG corporate bonds and CLOs.
- **Outlook**: The June Federal Open Market Committee (FOMC) meeting reinforced our view that the Fed is likely to remain on hold in the near term, although persistent inflation has increased the risk of further tightening. Our base case remains one of continued economic expansion rather than recession, with inflation proving more persistent than previously expected.

Fund Characteristics	Fund
Distribution Frequency	Monthly
30-Day SEC Yield (Advisor Class)—With Waiver	4.50%
30-Day SEC Yield (Advisor Class)—Without Waiver	4.32%

Performance Review

- **Sector allocations contributed to performance**, led by overweight allocations to IG corporate bonds, sovereign EM debt, CMBS, agency mortgage-backed securities (MBS) and municipal bonds, along with out-of-index exposures to HY corporate bonds, CLOs, CMOs, residential mortgage-backed securities (RMBS) and senior-secured floating-rate bank loans. In contrast, an underweight allocation to sovereign developed market debt detracted from returns.
- **Security selection contributed to results** for the quarter, led by selection in HY corporate bonds, municipal bonds, sovereign EM debt, asset-backed securities (ABS) and senior-secured floating-rate bank loans. In contrast, selection within IG corporate bonds and CLOs curbed returns.
- **Yield curve exposure had a largely neutral effect on performance**.

Outlook

- After a soft end to 2025, the US economy regained some momentum in Q1 as tech-driven investment and a rebound in federal spending following last October's government shutdown helped boost growth. However, consumer spending growth softened, with weakness in certain discretionary categories, suggesting that consumers may be turning more selective about their purchases. The labor market remains firm, though hiring gains stay concentrated in a narrow set of sectors, while consumer confidence and housing indicators remain subdued. While geopolitical developments and supply-side risks continue to warrant close monitoring, the greater near-term focus is on whether inflation pressures prove persistent enough to shift the Fed away from its current hold. Latest purchasing managers indexes have turned more stagflationary, as economic expansion is occurring at an increasingly inflationary price while employment expectations remain stagnant. Our base case is that the Fed remains on an extended hold, but policy is finely balanced.
- On interest rates, the June FOMC reinforced our view that the Fed is likely to remain on hold in the near term, but the balance of risks has shifted modestly toward further tightening. While Chair Warsh's press conference struck a dovish tone, the Committee's updated projections, the removal of easing guidance and rising market rate expectations suggest increasing support for a restrictive stance should inflation remain persistent. With inflation continuing to firm and real policy rates already drifting lower, a year-end or early-2027 rate hike cannot be ruled out. Our base case remains one of continued economic expansion rather than recession, with inflation proving more persistent than previously expected. While geopolitical developments and supply-side risk continue to warrant close monitoring, the greater near-term focus is on whether inflation pressures remain sufficiently strong to prompt additional Fed tightening.
- US IG corporate bond spreads are now tighter since the start of the year. Spreads briefly touched +93 bps in mid-March, which represented the widest level for US IG Corporate spreads since May 2025. The conflict in Iran and related spike in oil and related petrochemicals prices drove the widening, which has since been retraced on hopes of a potential resolution. Despite the scale of disruption the closure of the Strait of Hormuz could have caused; spreads have been remarkably contained. We attribute this to strong technicals that are in large part driven by higher all-in yields. Despite the geopolitical turmoil, year-to-date supply is still trending at a record pace, with over US$1 trillion of new issuance. While deals have been well absorbed thus far, Hyperscaler- and AI-related supply have exceeded 20% of net issuance for the IG market, and these deals are increasingly demanding greater new-issue concessions. While valuations have adjusted modestly, the market is still pricing in a sanguine outlook with minimal room for policy errors, and therefore we continue to favor a balanced risk posture

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with a bias toward non-cyclical sectors. The US HY default rate (including distressed exchanges) increased in June but remains below long-term averages, ending the month at 2.67%. Technicals remain solid with strong demand and consistent new issues. Yields and sub-par dollar prices remain attractive while spreads remain at levels that are fair but not compelling.

- We maintain a moderately constructive outlook on agency MBS over the near and intermediate term, supported by attractive carry, favorable relative value versus investment-grade corporates and stable market technicals. Although the Federal Reserve's balance sheet runoff continues to reduce a source of structural demand, slower prepayments have limited incremental supply, while prepayment risk remains well below long-term averages, supporting stable cash flow profiles across much of the agency MBS market. We continue to find value in out-of-the-money agency interest-only (IO) securities and bonds backed by moderately seasoned, higher-coupon Ginnie Mae collateral, which offer attractive carry and spread premiums while remaining relatively insulated from prepayment risk. We also remain constructive on the RMBS sector. While housing affordability continues to weigh on home sales and mortgage origination activity, homeowner credit fundamentals remain supported by a resilient labor market, healthy household balance sheets and limited housing inventory, with home price appreciation expected to remain modest over the coming year. We continue to favor seasoned, high-quality collateral, particularly senior AAA-rated bonds across the non-QM, prime jumbo, and home equity line of credit (HELOC) sectors, which offer attractive carry and resilience to macroeconomic uncertainty. Within CMBS, healthy demand for new issuance, constructive market technicals and attractive relative value versus investment-grade corporates continue to support the sector. While refinancing challenges are expected to persist for weaker assets as more than US$100 billion of CMBS loans mature heading into 2026, we continue to favor extension bonds and select CMBS interest-only (IO) securities for their attractive carry, shorter spread duration and favorable positioning should refinancing activity remain constrained. We expect CMBS spreads to remain broadly range-bound with a modest tightening bias.

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Average annual total returns and fund expenses (%) - as of June 30, 2026

			Without Sales Charge							With Maximum Sales Charge							Expenses		Sales Charges		Inception
Class	CUSIP	Ticker	3-Mo	YTD	1-Yr	3-Yr	5-Yr	10-Yr	Inception	3-Mo	YTD	1-Yr	3-Yr	5-Yr	10-Yr	Inception	Gross	Net	Initial Charge	CDSC	Date
Advisor Class	353612849	FBDAX	1.15	0.94	4.11	4.46	0.00	1.65	4.10	1.15	0.94	4.11	4.46	0.00	1.65	4.10	0.67	0.48	—	—	8/3/1998
Class A	353612856	FKBAX	1.10	0.82	3.88	4.23	-0.22	1.41	3.84	-2.65	-2.98	-0.07	2.92	-0.98	1.02	3.70	0.93	0.73	3.75	—	8/3/1998
Benchmark	—	—	0.67	0.62	3.79	4.16	0.08	1.54	—	0.67	0.62	3.79	4.16	0.08	1.54	—	—	—	—	—	—

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%).

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.

The **Federal Open Market Committee (FOMC)** is the branch of the Federal Reserve that dictates U.S. monetary policy, specifically targeting the federal funds rate and managing open market operations.

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.

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