FRANKLIN TEMPLETON

Franklin Municipal Green Bond SMA

Commentary | as of September 30, 2026

Key Takeaways

- **Markets:** In the third quarter of 2026, new issuance of municipal (muni) bonds continued at a record pace, with issuance 8% higher than the third quarter of 2025 and year-to-date volume running 6% ahead of last year (Source: Bloomberg). By quarter-end, the yield on the benchmark 10-year US Treasury (UST) note had risen by 82 basis points (bps) to 5.28% - its highest level since mid-2007 - while the yield on the 30-year UST bond was 68 bps higher at 5.63%. The September Federal Open Market Committee (FOMC), the policy-making body of the U.S. Federal Reserve (Fed), raised the federal funds target range by 25 bps to 3.75%-4.00%. Given that the hike was almost fully priced into the bond market, the genuinely new information was that the FOMC leans toward another increase, thus shifting the rates debate from a one-hike risk to how high a new tightening cycle might ultimately go.
- **Contributors:** Underweight allocation to munis with seven to 10 years to maturity.
- **Detractors:** Overweight positions in bonds with 15 to 20 years to maturity and three to seven years to maturity.
- **Outlook:** Municipal bond valuations are compelling relative to other fixed income sectors, in our view, giving investors an opportunity to harvest tax losses, rebalance duration and improve portfolio income without materially extending duration or relaxing credit standards. In a more challenging environment, strong bottom-up research and disciplined security selection will be essential to identifying relative value and preserving portfolio quality.

Performance Review

- The portfolio had a longer duration than its benchmark, which held back relative performance. Overweight allocations to bonds with 15 to 20 years to maturity and three to seven years to maturity detracted from relative performance, while an underweight to munis with seven to 10 years to maturity contributed.
- An overweight to AAA rated munis hindered relative results, while an overweight to AA rated issues contributed. From a sector perspective, the portfolios exposure to local general obligation munis detracted, while positions in prerefunded munis contributed to relative performance.

Outlook

- September's record supply and accelerating tax-loss selling tested market technicals, and the market struggled to absorb them. Munis trailed both Treasuries and corporates as yields rose across the curve and fund flows softened. Shorter-duration bonds held up better, as duration risk drove most of the losses. With supply likely to remain heavy, technicals will continue to be an important test of investor appetite, though the recent repricing may help attract buyers.
- Economic and credit fundamentals remain broadly supportive. Census estimates released in September showed second-quarter 2026 state and local tax collections at record levels, reflecting resilient labor markets and healthy tax bases, and stronger revenues should help issuers absorb rising costs. However, conditions vary materially across regions and credits, and credit outcomes are becoming more divergent. Tension between monetary and fiscal policy is also emerging as a key issue to watch, and we see scope for further yield curve steepening.
- In our view, the selloff has made absolute yields and relative valuations more compelling. Municipal yields now offer a substantial premium over comparable Treasuries at intermediate and longer maturities on a taxable-equivalent basis, with the long end offering the best relative value. Higher starting yields give investors an opportunity to harvest tax losses, rebalance duration and improve portfolio income without materially extending duration or relaxing credit standards. We favor capturing income and prioritizing quality over depending on a view of lower rates or tighter spreads. In this environment, active management and disciplined security selection remain essential to identifying relative value and preserving portfolio quality.

Not FDIC Insured | No Bank Guarantee | May Lose Value

Average annual total returns (%) - as of September 30, 2026

Composite	3-Mo*	6-Mo*	YTD*	1-Yr	3-Yr	5-Yr	10-Yr	15-Yr	20-Yr	25-Yr	Inception	Inception Date
Net of Fees	-5.11	-3.83	-4.12	-3.13	1.10	-1.95	—	—	—	—	0.21	10/31/2018
Pure Gross of Fees	-4.75	-3.11	-3.04	-1.67	2.62	-0.48	—	—	—	—	1.56	10/31/2018
Benchmark	-5.09	-3.51	-3.77	-2.41	2.79	0.29	—	—	—	—	1.90	—

*Cumulative total returns

Benchmark(s)

Benchmark =Bloomberg Municipal 1-15 Year Index

The strategy returns shown are preliminary composite returns, subject to future revision (downward or upward).

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Fees: Periods less than one year are not annualized. Performance results are for the composite which includes all actual, fully discretionary accounts with substantially similar investment policies and objectives managed to the composite's investment strategy. Composite returns are stated in U.S. dollars and assume reinvestment of any dividends, interest income, capital gains, or other earnings. The composite may include account(s) that are gross of fees and pure gross of fees. "Pure" gross-of-fee returns do not reflect the deduction of any expenses, including transaction costs. A traditional (or "true") gross-of-fee return reflects performance after the reduction of transaction costs but before the reduction of the investment advisory fee. The gross-of-fee return may include a blend of "true" gross-of-fee returns for non-wrap accounts and "pure" gross-of-fee returns for wrap accounts. Net-of-fee returns is reduced by a model "wrap fee" (1.5% is the maximum anticipated wrap fee for fixed income portfolios) which includes trading expenses as well as investment management, administrative and custodial fees. The model wrap fee used represents the highest anticipated wrap fee applicable to the strategy. Actual fees and account minimums may vary.
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Glossary

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

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.

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

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The **Bloomberg Municipal 1-15 Year Bond Index** is a market value weighted index of investment-grade fixed-rate municipal bonds with maturities of 1-15 years.

Source: Bloomberg Indices.

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