FRANKLIN TEMPLETON

Franklin U.S. Government Ladder 1-5 Year SMA

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. Over the period, the UST yield curve experienced a bear flattening, as short-to-intermediate rates rose more sharply than long-term rates. The one-month UST bill yield decreased by three basis points (bps) to 3.66%, while the three-month UST bill yield increased by 14 bps to 3.81%. Yields climbed by 38 bps to 4.17% on the two-year UST note, and by 29 bps to 4.23% on the five-year UST note.
- **Contributors**: Underweight overall duration.
- **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.

Performance Review

- Yield curve positioning helped results, as relative underweight duration exposure to the two- and five-year portions of the curve contributed to returns amid rising UST yields.

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.

Not FDIC Insured | No Bank Guarantee | May Lose Value

Average annual total returns (%) - as of June 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	-0.06	-0.17	-0.17	1.33	2.76	0.28	—	—	—	—	-0.03	6/30/2020
Pure Gross of Fees	0.31	0.58	0.58	2.85	4.30	1.78	—	—	—	—	1.47	6/30/2020
Benchmark	0.22	0.37	0.37	2.69	4.30	1.46	—	—	—	—	1.15	—

*Cumulative total returns

Benchmark(s)

Benchmark =Bloomberg 1-5 Year Treasury Index

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

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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.

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.

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The **Bloomberg 1-5 Year Treasury Index** measures the performance of public obligations of the U.S. Treasury with maturities of 1-5 years. Source: Bloomberg Indices.

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