

Franklin Intermediate Investment Grade Credit SMA

Commentary | as of December 31, 2025

Key Takeaways

- **Markets:** Market sentiment improved across the fourth quarter of 2025 (Q4) due to the resolution of the US federal government shutdown through mid-November, partial resolution of some of the outstanding trade policy concerns and two 25-basis points (bps) rate cuts by the US Federal Reserve (Fed), which was well received by the market. The median Federal Open Market Committee (FOMC) projection currently suggests one more 25 bp rate cut in 2026, though there are outliers within the FOMC and delays in government data has created some uncertainty. Fixed income spread markets performed well as corporate bond spreads remained near multidecade lows by the end of the quarter. The benchmark 10-year US Treasury (UST) note rose by 15 basis points to end the quarter at 4.17%.
- **Detractors:** Security selection in BBB and BBB+ rated bonds. Security selection in technology-related issues.
- **Contributors:** Security selection in A rated bonds and overweight allocation to BBB+ rated bonds.
- **Outlook:** Spreads in corporate credit sectors remain stretched. We are still focusing on the short-end of the yield curve which can provide current high levels of yield and income while limiting exposure to widening spreads.

Performance Review

- Sector allocations contributed to performance for the quarter from positive return contributions from a lack of exposure to supranational and consumer non-cyclical bonds. This was offset by an overweight to communications securities which curbed results. Security selection hurt performance for the quarter led by selection in the technology, communications and energy sectors.
- Rating allocations supported results led by an overweight to BBB+ rated bonds and an underweight to AAA rated bonds. This was partially offset by avoidance to the lowest investment-grade rating of BBB-. Security selection in rating categories detracted from returns as selection in BBB, BBB+ and A+ rated bonds hurt results. In contrast, selection in A and A- rated bonds contributed to performance.
- Yield curve exposure contributed to performance for the quarter.

Outlook

- IG corporate bond spreads have moved tighter year-to-date, driven by investor demand for historically attractive yields, as well as diminished market concerns about the potential negative impact of US trade policies. After some volatility earlier in 2025, credit spreads are again well inside longer-term averages and are close to their tightest levels in the past 25 years. Credit fundamentals remain supportive, providing most IG issuers with substantial flexibility to manage through shifting economic and market conditions.
- In our view, IG corporate bonds continue to offer relatively safe yield, spread levels again offer little cushion for further economic, market or geopolitical surprises. Spreads can stay tight and trade in a tight range despite rising re-leveraging risk from mergers and acquisition activity, financial engineering, and outsized capital expenditure. Yields at or around current levels could continue to support demand, but there is some risk that lower yields, due to either aggressive Fed easing or weaker economic data, may begin to negatively impact market technicals.
- This leads us to maintain a neutral stance on IG credit while highlighting potential concerns on current valuation levels.

Average annual total returns (%) - as of December 31, 2025

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	0.81	2.23	5.89	5.89	4.11	0.00	1.54	1.88	—	—	2.72	1/31/2009
Pure Gross of Fees	1.18	2.99	7.47	7.47	5.67	1.50	2.82	3.02	—	—	3.83	1/31/2009
Benchmark	1.27	3.28	7.88	7.88	6.26	1.54	3.13	3.29	—	—	4.21	—

*Cumulative total returns

Benchmark(s)

Benchmark = Bloomberg US Intermediate Credit Index

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Glossary

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

Investment grade is a rating that indicates that a municipal or corporate bond has a relatively low risk of default. BBB is medium credit quality rating.

Supranational bonds are debt instruments issued by supranational organizations, which are institutions created by the governments of several countries to promote economic, political, and social cooperation.

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