RISING RATES

What You Need to Know

FRANKLIN TEMPLETON
INVESTMENTS

“Although rising interest rates may primarily challenge those bond investments with the highest sensitivity to interest rates, we believe many parts of the global fixed income markets can provide reduced interest-rate risk and even be used to seek potentially strong performance in a rising interest-rate environment.”

—Christopher J. Molumphy, CFA®
Executive Vice President and Chief Investment Officer
Franklin Templeton Fixed Income Group®

RISING RATES—WHAT YOU NEED TO KNOW

It's important to remember the primary reasons to own fixed income funds don't change when market conditions, including interest rates, change. In addition to providing income, fixed income funds are an important component of a well-diversified portfolio.

The following pages will review the factors that can impact interest rates, why certain fixed income strategies are typically less interest-rate sensitive than others and Franklin Templeton funds to consider for a rising rate environment.

Learn more about:

WHAT DRIVES INTEREST RATES?

Short-term and long-term rates don't necessarily move in tandem. Learn what factors influence different parts of the yield curve.

NOT ALL FIXED INCOME IS CREATED EQUAL

Not all fixed income sectors react the same way to interest rate changes. Some sectors are less rate-sensitive than others.

A RANGE OF FUNDS TO CONSIDER

See specific Franklin Templeton funds to consider for a rising rate environment.

WHAT DRIVES INTEREST RATES?

In order to better understand the impact rising interest rates can have on your investments, it's important to understand the relationship between bond prices and yields, and the different factors that can influence short- and long-term rates.

When Yields Go Up, Prices Go Down (and Vice Versa)

Bond prices and yields have an inverse relationship. Typically, bond prices and interest rates move in opposite directions. That means when interest rates rise, bond prices tend to fall, and conversely, when interest rates decline, bond prices tend to rise. Likewise, the unit price of a fixed income mutual fund may move up or down, depending on movements in interest rates and their effect on the value of the bonds held in the fund's portfolio.

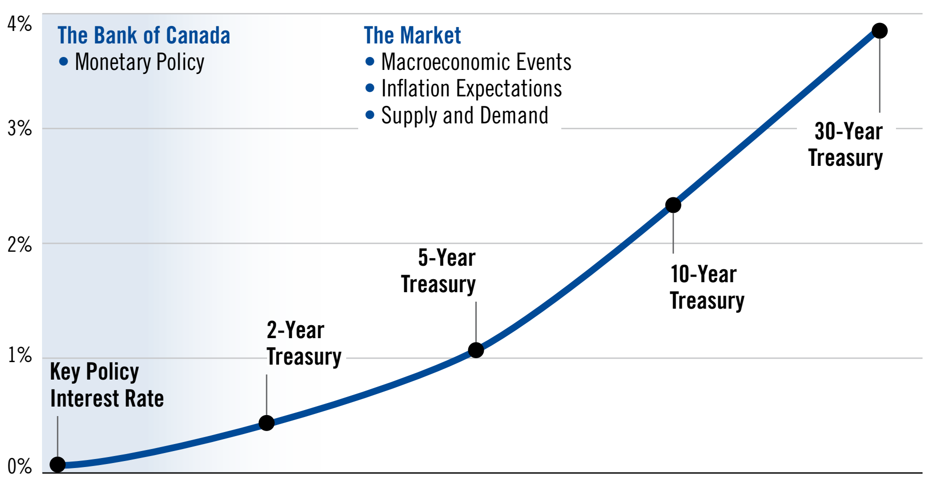
Different Factors Influence Short- and Long-Term Rates

In general, interest rates typically rise in a thriving economy, and in a sluggish economy, they tend to drop. But it's important to note that short-term and long-term rates don't necessarily move in tandem.

The Bank of Canada (BOC) controls the key policy interest rate, which in turn influences the market for shorter-term debt securities. The key policy interest rate is the rate that banks charge other banks for overnight loans. Canada's overnight target rate was cut to 0.25 per cent after the 2008-2009 financial crisis in order to combat the recession. That rate was pushed upward to 1.0 per cent in 2010 as Canada pulled out of the crisis earlier than the US. The overnight target rate remained at 1.0 per cent until early 2015, when the bank pulled its target down to 0.5 per cent to deal with the oil shock. The BOC has raised its overnight target rate twice in 2017, the latest in September, bringing the rate back up to 1.0 per cent.

WHAT DRIVES INTEREST RATES?

Hypothetical Normal Treasury Yield Curve



Understanding What Drives Rates

Bank of Canada policy decisions may make front page news, but that's only part of the interest-rate equation. BOC policy tends to have greater impact on the short end of the Treasury yield curve. The longer end of the curve is more heavily influenced by market factors such as macroeconomic events (a recession, for instance), inflation expectations, and supply and demand factors.

This chart is for illustrative purposes only and does not reflect the performance of any Franklin Templeton fund.
Past performance does not guarantee future results.

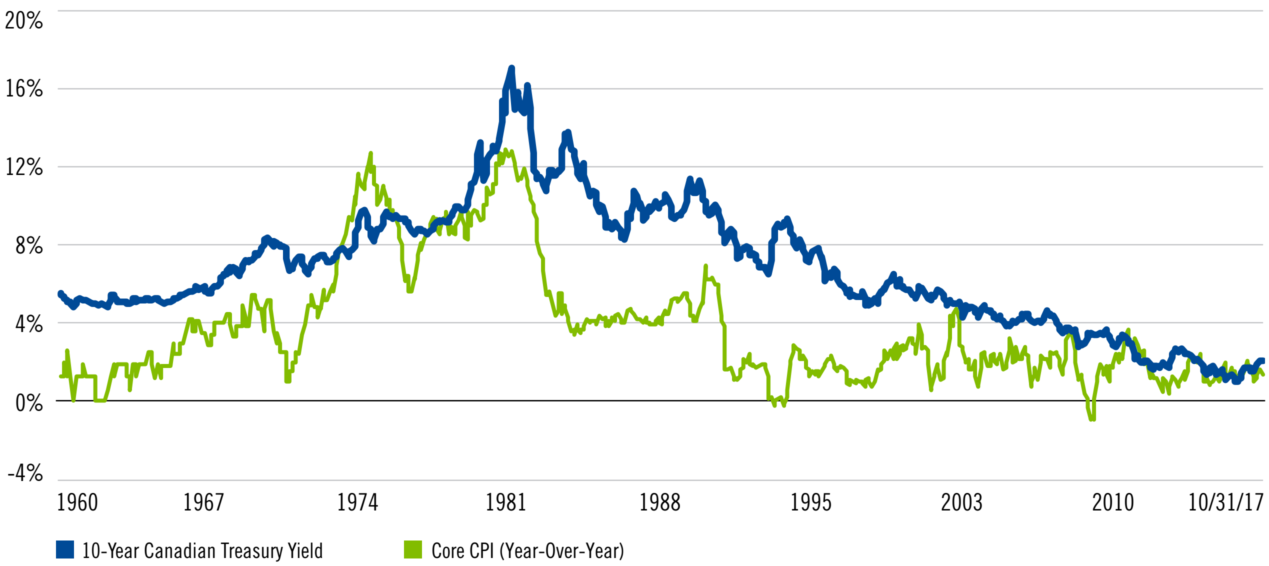
Longer-term interest rates, as represented by yields of 10-year and 30-year Government of Canada treasury bills, are typically market driven and may be influenced by macroeconomic events (such as economic expansion or contraction), inflation expectations, as well as supply and demand factors (including demand from foreign central banks). During September 2017, Canada sported the fastest growth among its developed peers yet had the flattest yield curve. A flat yield curve typically suggests that investors are concerned about the state of the economy. Yet, in Canada, the market indicated that investors were blasé about inflation and not necessarily pessimistic about the Canadian economy.

Inflation Has Historically Influenced Long-Term Rates

While different factors may affect interest rates at any given time, over the long-term inflation (or the rate at which the prices of goods and services are rising), has tended to be a key driver. Inflation is often a sign that the economy is expanding and expectations of growing inflation by the market may cause long-term rates to move higher.

10-Year Canadian Treasury Yield vs. Core CPI Year-Over-Year[2]

January 31, 1960–October 31, 2017



Rising Rates Have an Upside Too

There tends to be a sense of foreboding whenever the prospect of rising interest rates comes up, but it's important to remember that rising interest rates have an upside too. Rising rates may also be an indication of economic expansion, and the possibility that investors could see an increase in dividends and interest payments over time. For those investors whose investment horizon is longer than their bonds' time to maturity, they also have the opportunity to reinvest at the new higher rates.

1. Sources: Bloomberg, Federal Reserve H.15 Report, Bureau of Labor Statistics.

NOT ALL FIXED INCOME IS CREATED EQUAL

The size and scope of the fixed income market is much larger than the stock market. Within this large marketplace, different fixed income asset classes have their own set of unique characteristics, including interest rate sensitivity.

The Importance of Fixed Income Diversification

This table shows the annual returns of key fixed income sectors, on a year-by-year basis from 2007–2016, ordered from high to low. The outlined columns denote years when the Federal funds target rate and/or the 10-year Treasury bond yield increased.

AS A RESULT, "WINNING" SECTORS WILL TEND TO ROTATE

	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016
Best	Canadian Bonds 3.7%	US Government Bonds 40.6%	High Yield Bonds 31.0%	High Yield Bonds 8.4%	TIPS 16.4%	Emerging Market Bonds 15.3%	High Yield Bonds 14.7%	Municipal Bonds 18.9%	Municipal Bonds 23.9%	High Yield Bonds 14.2%
	TIPS -5.3%	Global Bonds 38.7%	Floating Loans 23.0%	Emerging Market Bonds 7.0%	Municipal Bonds 13.4%	High Yield Bonds 12.2%	Floating Loans 13.3%	US Investment Grade Corporate Bonds 17.2%	US Mortgage-backed Securities 21.7%	Emerging Market Bonds 6.1%
	Global Bonds -5.9%	US Mortgage-backed Securities 35.5%	Emerging Market Bonds 14.0%	Canadian Bonds 6.7%	US Government Bonds 11.7%	Floating Loans 7.0%	US T-Bill 6.8%	US Mortgage-backed Securities 15.6%	Emerging Market Bonds 21.5%	Floating Loans 6.1%
	US Government Bonds -7.8%	US T-Bill 28.1%	Canadian Bonds 5.4%	Floating Loans 4.2%	US Investment Grade Corporate Bonds 11.0%	US Investment Grade Corporate Bonds 6.9%	US Mortgage-backed Securities 5.2%	US Government Bonds 14.4%	US Government Bonds 21.0%	US Investment Grade Corporate Bonds 2.0%
	US Mortgage-backed Securities -9.3%	TIPS 22.1%	US Investment Grade Corporate Bonds -1.5%	US Investment Grade Corporate Bonds 2.8%	Canadian Bonds 9.7%	TIPS 4.6%	US Investment Grade Corporate Bonds 4.6%	Emerging Market Bonds 14.2%	US T-Bill 20.0%	Canadian Bonds 1.7%
	Emerging Market Bonds -10.8%	Municipal Bonds 22.0%	Municipal Bonds -4.1%	TIPS 0.8%	Emerging Market Bonds 9.6%	Municipal Bonds 4.4%	Municipal Bonds 4.0%	TIPS 13.0%	Floating Loans 19.5%	TIPS 1.1%
	US Investment Grade Corporate Bonds -10.9%	US Investment Grade Corporate Bonds 21.2%	TIPS -5.4%	US Government Bonds 0.0%	Global Bonds 9.0%	Canadian Bonds 3.6%	US Government Bonds 3.9%	Floating Loans 11.3%	US Investment Grade Corporate Bonds 19.0%	US Mortgage-backed Securities -1.8%
	US T-Bill -10.9%	Emerging Market Bonds 6.6%	US Mortgage-backed Securities -10.1%	US Mortgage-backed Securities -0.1%	US Mortgage-backed Securities 8.9%	US Mortgage-backed Securities 0.3%	Global Bonds 2.4%	High Yield Bonds 11.0%	TIPS 18.2%	Global Bonds -1.9%
	Municipal Bonds -12.3%	Canadian Bonds 6.4%	Global Bonds -12.9%	Global Bonds -0.3%	High Yield Bonds 8.1%	US Government Bonds -0.2%	Emerging Market Bonds 2.3%	US T-Bill 9.1%	Global Bonds 15.6%	US Government Bonds -2.4%
	High Yield Bonds -12.9%	High Yield Bonds -7.7%	US T-Bill -14.8%	Municipal Bonds -3.0%	Floating Loans 4.3%	Global Bonds -0.6%	Canadian Bonds -1.2%	Canadian Bonds 8.8%	High Yield Bonds 14.0%	US T-Bill -3.1%
Worst	Floating Loans -13.6%	Floating Loans -10.9%	US Government Bonds -16.9%	US T-Bill -5.0%	US T-Bill 2.6%	US T-Bill -2.1%	TIPS -2.5%	Global Bonds 8.5%	Canadian Bonds 3.5%	Municipal Bonds -3.2%

Source: Morningstar Research as of December 31, 2016. All returns shown in Canadian dollars. ■ Emerging market bonds, Barclays Capital Emerging Market TR; ■ Municipal bonds, Bloomberg Barclays Municipal TR; ■ US investment-grade corporate bonds, Bloomberg Capital US Credit TR; ■ US government bonds, Bloomberg Barclays US Government TR; ■ US mortgage-backed securities, Bloomberg Barclays US Mortgage-Backed TR; ■ Treasury Inflation Protected Securities (TIPS), Bloomberg Barclays US Treasury Inflation Protected Securities TR; ■ Global bonds, Citi World Government Bond Index; ■ High yield bonds, Credit Suisse High Yield; ■ Floating loans, Credit Suisse Leveraged Loan; ■ Canadian bonds, FTSE TMX Canada Universe Bond Index; ■ US T-Bill, Bloomberg Barclays US Treasury Bills TR.

This chart is for illustrative purposes only and does not reflect performance of any Franklin Templeton fund.
Past performance does not guarantee future results.

Diversification does not guarantee a profit or protect against a loss.

It's important to note that CDs are insured by the Federal Deposit Insurance Corporation (FDIC) for up to $250,000 and offer a fixed rate of return.

Treasuries, if held to maturity, offer a fixed rate of return and fixed principal value; their interest payments and principal are guaranteed.

FIXED INCOME SECTORS THAT TEND TO HAVE LOWER INTEREST RATE SENSITIVITY

Interest rate sensitivity can vary quite a bit across the fixed income universe. Generally speaking, higher quality sectors (such as Canadian government bonds) and longer duration bonds tend to be the most vulnerable to interest rate volatility. The following are strategies that have historically been less interest rate sensitive.

CONSIDER CREDIT-ORIENTED STRATEGIES

- **High-Yield Corporate Bonds**
- **Floating-Rate Bank Loans**

Credit-oriented sectors and, in particular, non-investment grade sectors such as high yield corporate bonds and floating-rate bank loans offer higher spreads over treasuries and have historically been less correlated to Canadian and US Treasuries as their performance is typically tied more to the overall economic outlook and corporate earnings landscape than interest rates.

KEEP IT SHORT

- **Adjustable-Rate Mortgages**
- **Short-Term Bonds**
- **Floating-Rate Bank Loans**

Shorter duration securities are generally not as sensitive to rate movements and can offer an attractive alternative to longer duration securities where rising rates typically have a greater effect on price and valuations.

GO GLOBAL

- **Global Bonds**
- **International Bonds**

International and global strategies can seek to capitalize on the differing business cycles and economic conditions present around the world, and thus are typically less impacted by rate changes in Canada and the US.

We are firm believers in diversion. Your financial advisor can show you the best way to achieve this goal.

What about Stocks?

Rising rates often signify an expanding economy. When rates are rising due to economic growth, they also tend to mean businesses and consumers are increasing their spending on goods and services—all of which tends to be good for the stock market.

And Alternatives?

Alternative funds that invest in hedge strategies can offer additional diversification to traditional stock and bond portfolios. Hedge strategies have historically shown a negative correlation to 10-year US Treasuries.[2]

2. Sources: © 2017 Morningstar, Citigroup. Based on 15-year period ended 12/31/16. Hedge strategies represented by the HFRI Fund Weighted Composite Index, 10-Year US Treasuries represented by the Citigroup 10-Yr US Treasury Index. Indexes are unmanaged and one cannot invest directly in an index. Treasuries, if held to maturity, offer a fixed rate of return and fixed principal value; their interest payments and principal are guaranteed. Past performance does not guarantee future results.

FRANKLIN TEMPLETON FUNDS TO CONSIDER FOR A RISING RATE ENVIRONMENT

CREDIT-ORIENTED	**Franklin Bissett Core Plus Bond Fund** **Franklin Bissett Corporate Bond Fund** **Franklin High Income Fund** **Franklin Strategic Income Fund**
SHORT DURATION	**Franklin Bissett Canadian Short Term Bond Fund**
GLOBAL	**Templeton Global Bond Fund**
HYBRID (STOCKS AND BONDS)	**Franklin Bissett Canadian Balanced Fund** **Franklin Bissett Monthly Income & Growth Fund** **Franklin Quotential Diversified Income Portfolio Fund** **Templeton Global Balanced Fund** **Franklin US Monthly Income Fund**
ALTERNATIVES	**Franklin Target Return Fund**

How to Prepare for Rising Rates

Although it's impossible to predict the exact timing and direction of interest rate changes, it's almost certain fluctuations will occur. To learn more about Franklin Templeton mutual funds, including those listed above that may be considered for a rising rate environment, talk to your financial advisor. An advisor offers market knowledge and planning expertise, and will take into account your individual investment needs to create an investment strategy tailored to your specific investment goals and risk tolerance.

FRANKLIN TEMPLETON FIXED INCOME EXPERTISE

Extensive Expertise

Franklin Templeton has been managing fixed income assets since 1948 and dedicated fixed income mutual funds since 1970. During that time, we have become one of the largest and most respected fixed income managers in the world.[3]

A Fixed Income Leader. Franklin Templeton manages about $450 billion CAD in fixed income assets.[4]

Research Expertise. Our fixed income team includes over 150 investment professionals with an average of 18 years of experience.[4] We are also able to tap the expertise of the Franklin equity research team, which gives us the ability to view our investments from yet another perspective.

Extensive Resources. Our dedicated risk management team partners with managers to analyze and monitor portfolio risk.

A Range of Fixed Income Offerings. We offer funds covering the entire fixed income spectrum, including government securities, municipal bonds, corporate bonds, floating-rate loans, global bonds and multi-sector strategies that capitalize on our expertise in each of these areas.[4]

"The Franklin Templeton Fixed Income Group has global specialist teams focusing on every major sector of the fixed income market. This worldwide breadth gives us an advantage in identifying investment opportunities for our fund portfolios."

CHRISTOPHER J. MOLUMPHY, CFA®, EVP and CIO, Franklin Templeton Fixed Income Group

3. Strategic Insight, ICI as of 12/31/16.
4. As of 6/30/17.

WHAT ARE THE RISKS?

All investments involve risks, including possible loss of principal. Bond prices generally move in the opposite direction of interest rates. Thus, as the prices of bonds in a fund adjust to a rise in interest rates, the fund's share price may decline. 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. Floating-rate loans and high-yield corporate bonds are generally rated below investment grade and are subject to greater risk of default, which could result in loss of principal, a risk that may be heightened in a slowing economy. The risks of foreign securities include currency fluctuations and political uncertainty. Investments in developing markets involve heightened risks related to the same factors, in addition to those associated with their relatively small size and lesser liquidity. Derivatives, including currency management strategies involve costs and can create economic leverage in a portfolio which may result in significant volatility and cause a fund to participate in losses (as well as enable gains) on an amount that exceeds the fund's initial investment. A fund may not achieve the anticipated benefits, and may realize losses when a counterparty fails to perform as promised. Some derivatives are particularly sensitive to changes in interest rates. Stock prices fluctuate, sometimes rapidly and dramatically, due to factors affecting individual companies, particular industries or sectors, or general market conditions.

Alternatives: Hedge strategies are actively managed and could experience losses if an investment manager's judgment about markets, future volatility, interest rates, industries, sectors, and regions, or the attractiveness or the potential appreciation of particular investments prove to be incorrect. Short sales of securities involve the risk that losses may exceed the original amount invested. Merger arbitrage investments risk loss if a proposed organization in which the fund invests is renegotiated or terminated.

Please review a fund or ETF prospectus for a complete discussion of fund risks.

Index Definitions

FTSE TMX Canada Universe Bond Index is designed to track the performance of the bonds denominated in Canadian Dollars.

Credit Suisse High Yield Index is designed to mirror the investible universe of the US dollar-denominated high yield debt market.

J.P. Morgan Emerging Markets Bond Index Global tracks total returns for US dollar-denominated debt instruments issued by emerging market sovereign and quasi-sovereign entities.

Credit Suisse Leveraged Loan Index is designed to mirror the investible universe of the US dollar-denominated leveraged loan market.

Citigroup World Government Bond Index Non-US is a market capitalization weighted index consisting of investment-grade world government bonds (apart from US).

Citigroup World Government Bond Index is a market capitalization weighted index consisting of investment-grade world government bonds.

Bloomberg Barclays US TIPS Index covers the universe of inflation-protected notes issued by the US Treasury that have at least one year to final maturity.

Bloomberg Barclays Municipal Bond Index is a market-value-weighted index engineered for the long-term tax-exempt bond market.

Bloomberg Barclays US MBS Index is the MBS component of the Bloomberg Barclays US Aggregate Index and covers agency mortgage-backed pass-through securities (both fixed rate and hybrid ARM) issued by Ginnie Mae (GNMA), Fannie Mae (FNMA), and Freddie Mac (FHLMC).

Bloomberg Barclays Asset-Backed Securities (ABS) Index is the ABS component of the Bloomberg Barclays US Aggregate Index and includes credit and charge card, auto, and utility loans.

Bloomberg Barclays US Corporate Investment Grade Index is the US Corporate component of the Bloomberg Barclays US Credit Index and covers USD-denominated, investment-grade, fixed-rate, taxable securities sold by industrial, utility, and financial institution issuers.

Bloomberg Barclays US Government Index: 1–2 Year Component is the 1–2 year component of the Bloomberg Barclays US Government Index.

Bloomberg Barclays US Government Index is the US Government component of the Barclays US Government/Credit index and includes public obligations of the US Treasury with at least one year to final maturity and publicly issued debt of US Government agencies, quasi-federal corporations, and corporate or foreign debt guaranteed by the US Government.

Bloomberg Barclays US Agency Index is the US Agency component of the Bloomberg Barclays US Government/Credit Index and includes publicly issued debt of US Government agencies, quasi-federal corporations, and corporate or foreign debt guaranteed by the US Government.

Citigroup 10-Year US Treasury Index is a total return index based on a constant maturity instrument.

BofAML Preferred Stock Fixed Rate Index tracks the performance of fixed rate US dollar-denominated preferred securities issued in the US domestic market.

This communication is general in nature and intended for educational purposes only; it should not be considered tax, legal or investment advice, or an investment recommendation. Consult your financial advisor for personalized advice that is tailored to your specific goals, individual situation, and risk tolerance.

Investors should carefully consider a fund's investment goals, risks, charges and expenses before investing. To obtain a prospectus, which contains this and other information, talk to your financial advisor, call (800) 387-3830 or visit franklintempleton.ca. Please carefully read a prospectus before you invest or send money.

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