Franklin Templeton Investment Funds

Templeton Global Total Return Fund

Fund Manager Report

Fixed Income
LU0170475585
31 January 2016

Fund Characteristics

Base Currency	USD
Total Net Assets (USD)	24,314,034,329
Fund Inception Date	29.08.2003
Number of Holdings	407
Primary Benchmark:	Barclays Multiverse Index
Average Credit Quality	BBB+
Average Duration:	
Fund	-0.08 Yrs
Benchmark	6.44 Yrs
Yield to Maturity (%)/Current Yield (%)	6.83/5.90
Bloomberg Code - A(Mdis)	TGTRFAD LX

Fund Management

Michael Hasenstab, PhD: United States
Sonal Desai, PhD: United States

Ratings - A(Mdis) USD

Overall Morningstar Rating™: ★★★★★

Overview

- In January, a global flight to quality drove yields lower across much of Europe, Asia and the Americas and drove credit spreads wider, most notably in the lowest-rated credit tiers. The yield on the 10-year U.S. Treasury note decreased 35 basis points to 1.92%.
- For the month, the fund's negative absolute performance was primarily due to currency positions, followed by overall credit exposures and interest-rate strategies.
- The fund's underperformance of its benchmark index was primarily due to interest-rate strategies, followed by currency positions. Overall credit exposures had a largely neutral effect on relative results.

Performance (%) (As of 31 January 2016)

Cumulative Performance

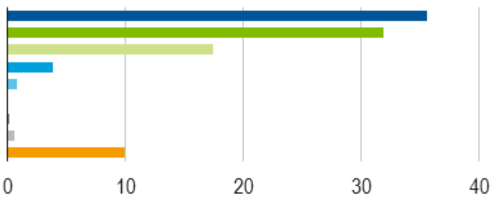
	1 Yr	3 Yrs	5 Yrs	10 Yrs	Since Incept (29.08.03)
Templeton Global Total Return Fund - A(Mdis) USD—NAV	**-6.87**	**-5.37**	**13.42**	**109.47**	**171.52**
Barclays Multiverse Index USD	-2.38	-3.46	5.69	44.94	67.55

Annualized Performance (%) – Net Of Sales Charge^ (As of 31 January 2016)

Historical Performance

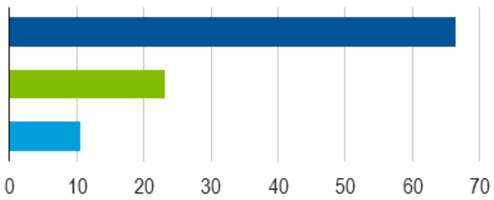
	1 Yr	3 Yrs	5 Yrs	10 Yrs	Since Incept (29.08.03)
Templeton Global Total Return Fund - A(Mdis) USD	-11.53	-3.49	1.50	7.12	7.93

Geographic Breakdown (%)



Asia, Non-Japan	35.55
Non-USA America	31.85
Non-EMU Europe/Africa	17.38
EMU	3.82
USA	0.82
Japan	0.00
Supranational	0.13
Other	0.58
ST Cash and Cash Equivalents	9.86

Credit Quality Breakdown (%)



Investment Grade	66.35
Non-Investment Grade	23.19
Cash	10.44

Data in this report is preliminary.
For information related to the heading "Fund Characteristics", please see note regarding Fund Ratings on back page. See Credit Quality Breakdown note on back page. Source for "Fund Characteristics", "Credit Quality Breakdown", "Geographic Breakdown", "Cumulative Performance": Franklin Templeton Investments, as of 31 January 2016. **Past performance is not an indicator or a guarantee of future performance.** Where a Fund invests in emerging markets, this investment can be more risky than an investment in developed markets.
Performance calculated as at 31 January 2016 in USD; NAV-NAV; dividend reinvested. Past performance is not indicative of future performance. ^Initial sales charge of 5%.

Market Review

Global market volatility escalated during January as oil prices declined below US$30 per barrel and investors renewed their concerns over global growth and economic conditions in China. A global flight to quality drove yields lower across much of Europe, Asia and the Americas and drove credit spreads wider, most notably in the lowest-rated credit tiers. The yield on the 10-year U.S. Treasury note decreased 35 basis points (bps) to 1.92%, and the 10-year German Bund yield dropped 37 bps to a yield of 0.26%. The Bank of Japan (BOJ) introduced a negative interest-rate policy during the month, and 10-year Japanese government bond yields dropped to 0.00%.

A majority of currencies continued to depreciate against the U.S. dollar during January, while some currencies appreciated, such as the Malaysian ringgit and Indonesian rupiah. In our assessment, several emerging-market currency depreciations continued to be excessive, leading to fundamentally cheap valuations. We selectively add to our strongest convictions in periods of volatility and believe that global market fundamentals will eventually re-emerge.

The BOJ and the European Central Bank (ECB) continued with their quantitative easing (QE) programs in January, and both central banks indicated that they intend to expand their QE programs into 2017. The euro and Japanese yen modestly depreciated against the U.S. dollar during the month.

Performance Review and Contributors to Performance

In January, the fund's negative absolute performance was primarily due to currency positions, followed by overall credit exposures and interest-rate strategies. Among currencies, positions in Latin America detracted from absolute results, as did positions in peripheral European currencies against the euro. Currency positioning in Africa also detracted from absolute performance. However, the fund's net-negative positions in the Japanese yen, the euro and the Australian dollar contributed to absolute results, as did its currency positions in Asia ex Japan. Among credit exposures, high-yield corporate bonds and subinvestment-grade sovereign credits detracted from absolute performance. The fund maintained a defensive approach regarding interest rates in developed and emerging markets. Negative duration exposure to U.S. Treasuries detracted from absolute results, while select duration exposures in Latin America and Asia ex Japan contributed.

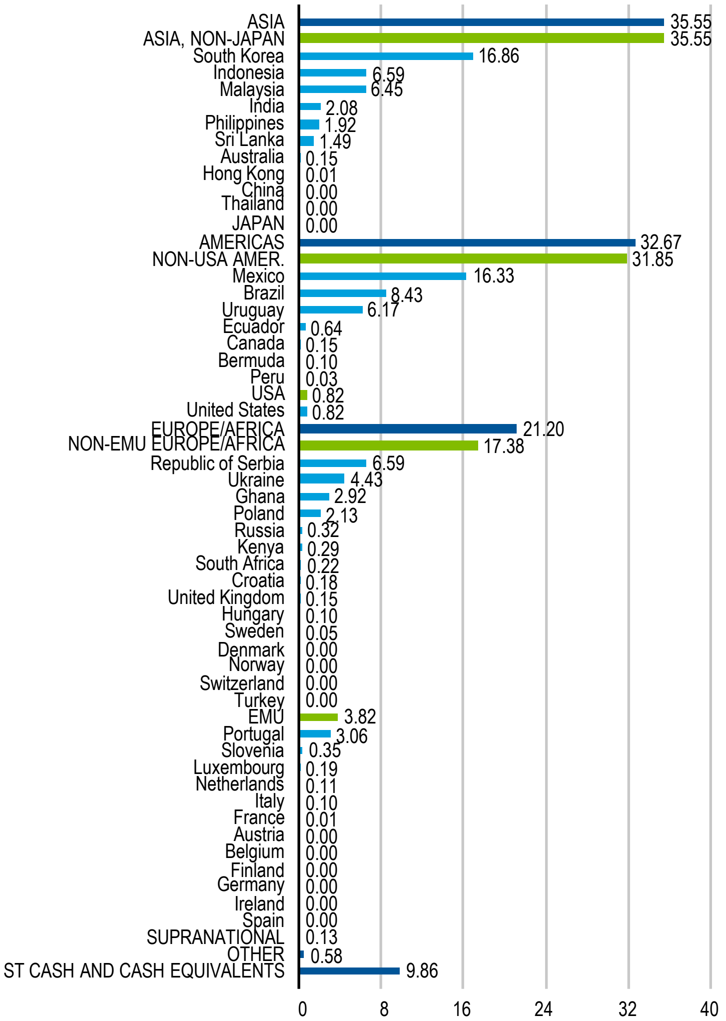
The fund's underperformance of its benchmark index was primarily due to interest-rate strategies, followed by currency positions. Overall credit exposures had a largely neutral effect on relative results. Underweighted duration exposures in the United States and Japan detracted from relative performance, as did select underweighted duration exposures in Europe. However, select overweighted duration exposures in Latin America and Asia ex Japan contributed to relative results. Among currencies, overweighted positions in Latin America detracted from relative performance, as did overweighted positions in peripheral European currencies against the euro. Select overweighted currency positioning in Africa also detracted from relative results. However, the fund's underweighted positions in the Japanese yen, the euro and the Australian dollar contributed to relative performance, as did its overweighted currency positions in Asia ex Japan. Among credit exposures, overweighted exposures to subinvestment-grade sovereign credits and high-yield corporate bonds detracted from relative results, while underweighted exposure to investment-grade corporate bonds contributed.

Portfolio Positioning

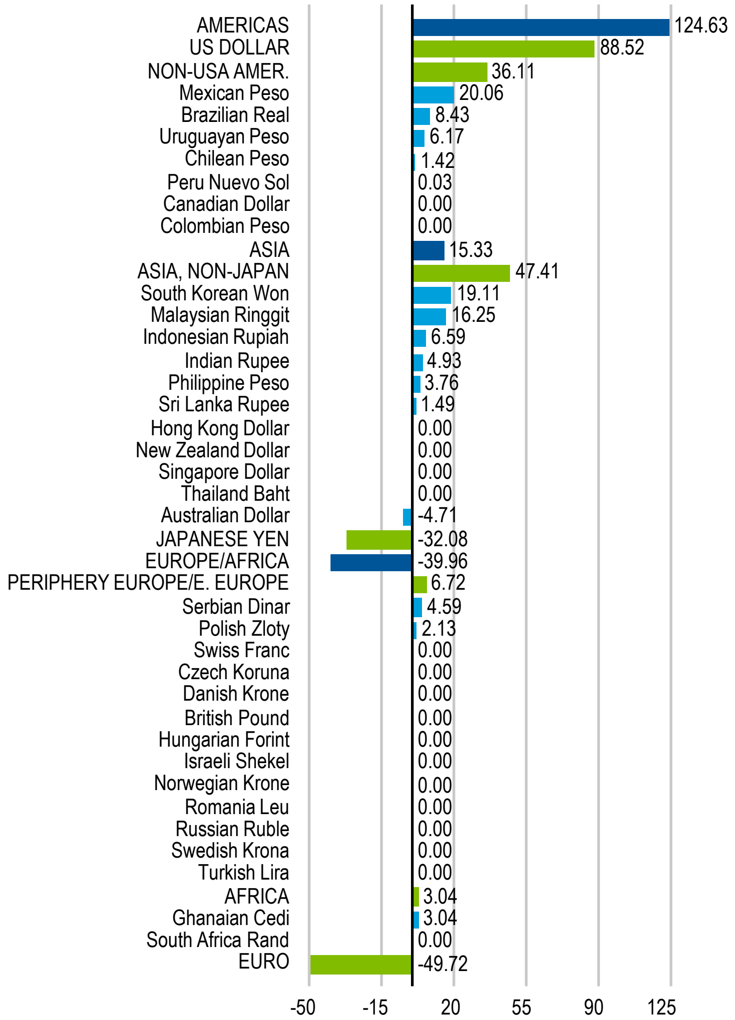
On the whole, we have continued to position our strategies for rising rates by maintaining low portfolio duration and aiming at a negative correlation with U.S. Treasury returns. We have also continued to actively seek select duration exposures that can offer positive real yields without taking undue interest-rate risk, favoring countries that have solid underlying fundamentals and prudent fiscal, monetary and financial policies. When investing globally, investment opportunities may take time to materialize, which may require weathering short-term volatility as the longer-term investing theses develop. Despite the escalation of volatility in the beginning of 2016, we remain encouraged by the vast set of fundamentally attractive valuations across the global bond and currency markets. Currently we favor currencies in countries where inflation is picking up and growth remains healthy, yet the local currency remains fundamentally undervalued.

Portfolio Diversification (As of 31 January 2016)

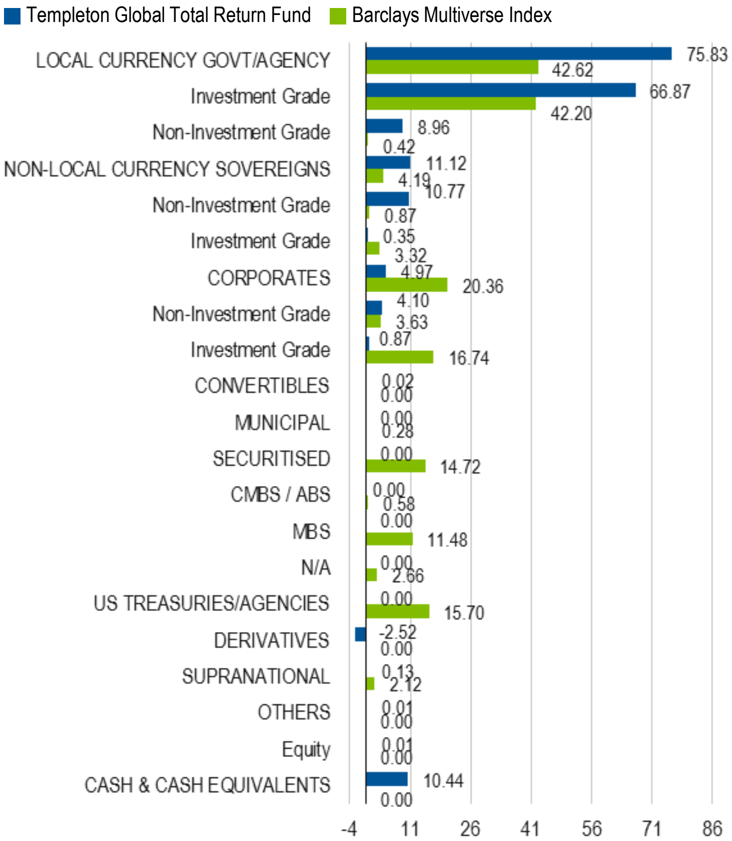
Geographic Weightings (%)



Currency Weightings (%)



Sector Weightings vs. Benchmark (%)



Source for the above figures: Franklin Templeton Investments as of 31 January 2016.

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Portfolio Diversification (continued)

Top Ten Holdings

Security	Industry	% of Total
Government of Portugal, Reg S, 5.125%, 10/15/24	Government Securities	3.06
Government of Mexico, senior note, M, 5.00%, 6/15/17	Government Securities	2.43
Government of Uruguay, senior bond, Index Linked, 4.375%, 12/15/28	Government Securities	2.34
Korea Monetary Stabilization Bond, senior note, 2.07%, 12/02/16	Government Securities	2.20
Korea Treasury Bond, senior note, 3.00%, 12/10/16	Government Securities	1.90
Letra Tesouro Nacional, Strip, 7/01/19	Government Securities	1.63
Korea Monetary Stabilization Bond, senior note, 1.61%, 11/09/16	Government Securities	1.52
Korea Treasury Bond, senior note, 2.00%, 12/10/17	Government Securities	1.39
Government of Malaysia, senior note, 3.394%, 3/15/17	Government Securities	1.36
Government of Indonesia, senior bond, FR70, 8.375%, 3/15/24	Government Securities	1.35
Total		**19.19**

Investment Outlook

We remain confident in the economic outlook for the U.S. and continue to expect rising interest rates from the U.S. Federal Reserve (Fed). U.S. labor markets remain close to full employment, economic growth is right around potential at about 2% and core inflation has remained stable. These conditions would justify a normalization of interest rates, in our assessment.

We believe there is a significant disconnect between the current market pessimism and the underlying fundamentals. Markets have reacted as if conditions are worse than the 2008 global financial crisis, or the Asian financial crisis of 1997 and 1998, yet several emerging-market countries are in far better shape, with larger foreign reserves and more diversified, growing economies. We believe concerns of a systemic crisis have been exaggerated, as there are significant differences across the asset class. Most commodity exporters, and emerging markets with poor macroeconomic fundamentals, remain vulnerable. Other emerging countries, however, have solid policies and better underlying fundamentals that have not been recognized by market valuations.

A strengthening U.S. economy, along with the likelihood of higher U.S. interest rates, may increasingly magnify the fundamental differences between healthy and vulnerable economies. We anticipate that countries with relatively stronger fundamentals, such as Mexico, will likely be in a better position to potentially raise interest rates in conjunction with U.S. interest-rate hikes. However, countries with relatively weaker fundamentals, such as Turkey and South Africa, are likely to be negatively impacted by U.S. interest-rate hikes.

We anticipate significant divergences in monetary policies around the world in 2016; we expect the Fed to continue tightening policy while the BOJ and the ECB continue to expand monetary accommodation through QE. The BOJ has indicated that its QE program will likely continue into 2017, and the ECB has indicated it will likely continue QE through March 2017. In our assessment, both the BOJ and ECB need to continue these current expansionary policies, which should continue to depreciate the yen and euro against the U.S. dollar. In the eurozone, QE has been driving the euro weaker to stimulate export-driven economic growth and lift inflation toward the ECB's target; in Japan, QE has become explicit debt financing for the government and a cornerstone of "Abenomics."

Markets have overreacted to conditions in China, in our assessment, and these fear-motivated responses are driving the broad market selloffs. We view the recent moderation of growth in China as an inevitable normalization for an economy of its size. Its nominal level of gross domestic product (GDP) is now five times the size of what it was 10 years ago. Thus a lower rate of growth still represents a massive level of global aggregate demand. A 6.0%–7.0% growth rate creates a much larger quantum of demand when compared with China's 10%–12% growth rate from a decade ago. Additionally, the quality of growth in China has improved in recent years. Increasing labor costs and interest rates have put downward pressure on profits; however, higher wages boost consumption, which has increasingly become the anchor of Chinese growth. We estimate that consumption is close to 60% of GDP and rising. Additionally, new interest-rate liberalization policies can redirect capital to the whole economy, particularly the private sector, which we expect to be the future driver of growth.

We continue to believe that an unconstrained global strategy is the most effective way to position for a rising-rate environment because it provides access to the full global opportunity set. Unconstrained strategies can adjust duration to any suitable level for prevailing interest-rate risks; this includes driving overall portfolio duration down to near zero while taking negative duration exposure to U.S. Treasuries. We are also able to selectively add suitable duration exposures from specific emerging markets with relatively higher yields. Additionally, the unconstrained nature of our strategies provides flexibility to directionally position (long positions and short positions) across currency markets, which present a wide range of valuation opportunities. We have used shorts of the euro and yen to guard against broad-based strengthening of the U.S. dollar, while taking long positions in select emerging-market currencies with attractive longer-term valuations.

The portfolio manager for the Fund reserves the right to withhold release of information with respect to holdings that would otherwise be included in the top 10 holdings list.

Investment Objective

Templeton Global Total Return Fund's principal objective is to maximize, consistent with prudent investment management, total investment return consisting of a combination of interest income, capital appreciation and currency gains. Under normal market conditions, the Fund will invest in a portfolio of fixed- and floating-rate debt securities and debt obligations of governments, government-related or corporate issuers worldwide.

Investment Philosophy

Templeton Global Macro fosters an active management approach, based on top-down, in-depth research of macroeconomic factors, combined with bottom-up fundamental valuations and portfolio construction.

The managers of Templeton Global Total Return Fund believe that applying a fundamental, research-driven approach focused on identifying potential sources of high current income worldwide and seeking to capitalize on global interest rates and currency trends provides the best potential for superior risk-adjusted returns. Our strategies are run independently of their benchmarks, allowing the managers to hold positions they feel will benefit performance. This is a high alpha global strategy that may include allocations to both developed and emerging markets. We seek out securities that we believe offer superior relative value and actively manage duration, currency, and credit exposure. Our funds employ a mix of credits; however, we tend to favor credits with solid fundamentals.

Explanatory Notes

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Fund performance data include reinvested dividends, and is net of management fees. Sales charges, other commissions, taxes and other relevant costs to be paid by the investor are not included.

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Source: Franklin Templeton Investments. The average credit quality (ACQ) rating may change over time. The portfolio itself has not been rated by an independent rating agency. The letter rating, which may be based on bond ratings from different agencies, is provided to indicate the average credit rating of the portfolio's underlying bonds and generally ranges from AAA (highest) to D (lowest). The ACQ is determined by assigning a sequential integer to all credit ratings AAA to D, taking a simple, asset-weighted average of debt holdings by market value and rounding to the nearest rating. An ACQ is not a statistical measurement of the portfolio's default risk and is provided for informational purposes only. Derivative positions and unrated securities are not reflected in the ACQ.

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