# Two flexible income strategies that invest outside the index

Q1 | 18

**Putnam Income Fund (PNCYX)**

A core bond strategy

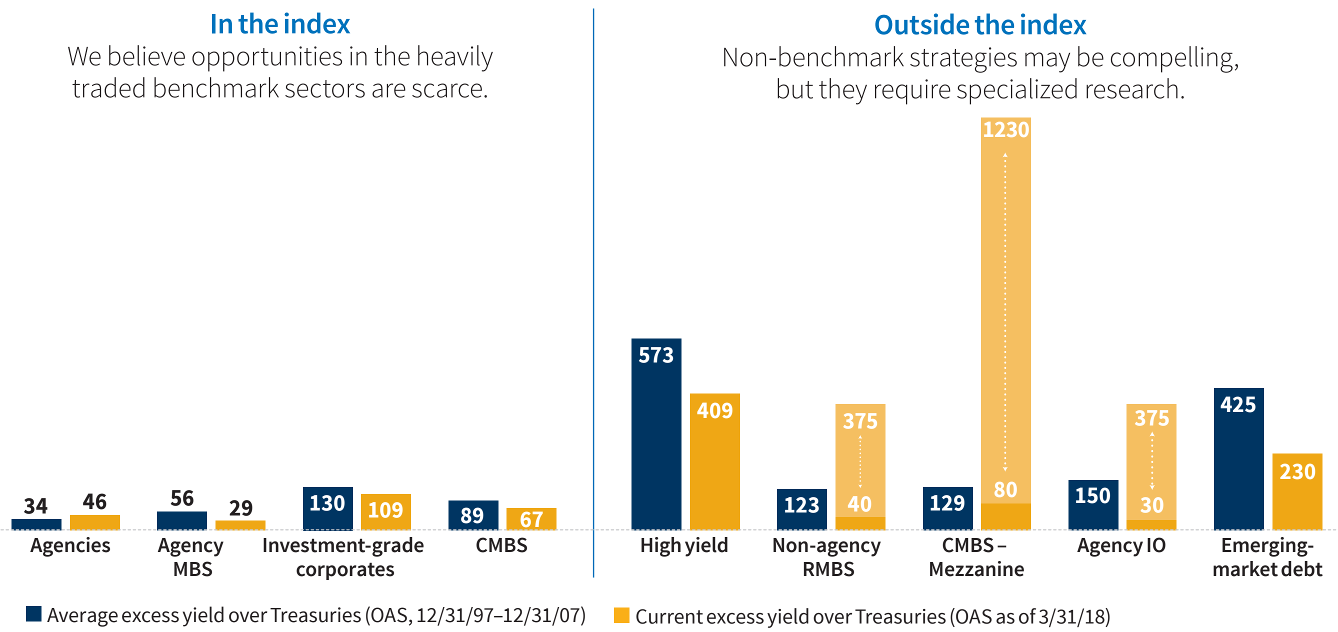
**Putnam Diversified Income Trust (PDVYX)**

A nontraditional income strategy

# Income Fund and Diversified Income Trust share a common approach of looking beyond the index

## We actively expand our focus to include sectors outside the index

As rates are rising, strategies aligned with the BBG Barclays U.S. Aggregate Bond Index offer fewer total return opportunities and are exposed to high levels of interest-rate risk. We devote our efforts to finding income opportunities in sectors outside the index that offer more attractive yield spreads and total return opportunities.




Sources: Bloomberg, Putnam, as of 3/31/18.

We show the 10-year pre-crisis average and contrast it to today's spreads to illustrate that there is a liquidity premium embedded in spreads today (and for much of the post-crisis era) that did not exist prior to the crisis. The reason we do not use more than 10 years of data is because not all the sectors (i.e., CMBS) have a history much longer than that.

Data is provided for informational use only. Past performance is no guarantee of future results. All spreads are in basis points and measure option-adjusted yield spread relative to comparable maturity U.S. Treasuries with the exception of non-agency RMBS and mezzanine CMBS, which are loss-adjusted spreads to swaps calculated using Putnam's projected assumptions on defaults and severities, and agency IO, which is calculated using assumptions derived from Putnam's proprietary prepayment model. Agencies are represented by Bloomberg Barclays U.S. Agency Index. Agency MBS are represented by Bloomberg Barclays U.S. Mortgage Backed Securities Index. Investment-grade corporates are represented by Bloomberg Barclays U.S. Corporate Index. High yield is represented by JPMorgan Developed High Yield Index. CMBS is represented by both agency and non-agency CMBS that are eligible for inclusion in the Bloomberg Barclays U.S. Aggregate Bond Index; mezzanine CMBS is represented by the same index using the AA, A, and BBB components. Average OAS for Mezzanine CMBS is for the 2000–2007 time period. Emerging-market debt is represented by the Bloomberg Barclays EM Hard Currency Aggregate Index. Non-agency RMBS is estimated using average market level of a sample of below-investment-grade securities backed by various types of non-agency mortgage collateral (excluding prime securities). Mezzanine CMBS is estimated from an average spread among baskets of Putnam-monitored new issue and seasoned mezzanine securities, as well as a synthetic (CMBX) index. Agency IO is estimated from a basket of Putnam-monitored interest-only (IO) and inverse IO securities. Option-adjusted spread (OAS) measures the yield over duration equivalent Treasuries for securities with different embedded options.

## Specialization, collaboration, and allocation to sources of risk drive our process

We view interest-rate risk as only one source of potential returns, and it isn't always the most attractive. That's why we use a risk-based approach focused on four key areas in pursuit of alpha generation: rates, credit, prepayment, and liquidity.

# Putnam Income Fund
## (PNCYX)

An all-weather strategy favoring investment-grade bonds

**The fund can invest in multiple sectors (X)**

| | | |
|---|---|---|
| INSIDE THE INDEX | Agencies | X |
| | Agency MBS | X |
| | Investment-grade corporates | X |
| | CMBS | X |
| OUTSIDE THE INDEX | High yield | |
| | Non-agency RMBS | X |
| | CMBS-Mezzanine | X |
| | Agency IO | X |
| | Emerging-market debt | |

**Average historic duration (3/31/15–3/31/18)**

**4.31**
INCOME FUND

**5.74**
BBG BARCLAYS U.S. AGGREGATE BOND INDEX

**Correlation to the index**

**0.51** The outcome of this outside-the-index approach is performance with low historical correlation to the index.

**Putnam Income Fund Team**

**Michael Salm**
Co-Head of Fixed Income
**29** years of investing
**21** years at Putnam

**Brett Kozlowski, CFA**
Portfolio Manager
**21** years of investing
**10** years at Putnam

**Emily Shanks**
Portfolio Manager
**19** years of investing
**6** years at Putnam

### Michael Salm describes Income Fund's approach to risk allocation

**Rates**
We actively manage rate risk. The portfolio's duration has often been lower than the Aggregate Index while still positive.

**Credit**
We pursue credit risk in both corporate and mortgage-backed securities, researched by experienced and specialized analysts.

**Prepayment**
We seek to add value by positioning in IOs and other securities as interest rates and mortgage refinancing trends change.

**Liquidity**
We invest in securities that we believe adequately compensate investors for liquidity risk.

Sources: Barclays, Bloomberg, Putnam, as of 3/31/18. Correlation figures shown are for the 3-year period ended 3/31/18 and use monthly data.

### Rates
Interest-rate risk (also called term structure risk) is a bond's sensitivity to changes in interest rates and the shape of yield curves.

### Credit
Credit risk is the possibility a borrower may fail to make payments to investors.

### Prepayment
Prepayment risk involves borrowers paying off debt early, typically in a falling-rate environment, which reduces the number of payments and interest received by investors.

### Liquidity
Liquidity risk refers to the relative difficulty of trading a security in a reasonable amount of time.

# Putnam Diversified Income Trust (PDVYX)

A nontraditional income strategy with increased flexibility

**The fund can invest in multiple sectors (X)**

| | Sector | |
|---|---|---|
| INSIDE THE INDEX | Agencies | X |
| | Agency MBS | X |
| | Investment-grade corporates | X |
| | CMBS | X |
| OUTSIDE THE INDEX | High yield | X |
| | Non-agency RMBS | X |
| | CMBS-Mezzanine | X |
| | Agency IO | X |
| | Emerging-market debt | X |

**Average historic duration (3/31/15–3/31/18)**

**-0.95**
DIVERSIFIED INCOME TRUST

**5.74**
BBG BARCLAYS
U.S. AGGREGATE BOND INDEX

**Correlation to the index**

**-0.30** The outcome of this outside-the-index approach is a fund with negative historical correlation to the index.

**Putnam Diversified Income Trust Team**

**D. William Kohli**
CIO, Fixed Income
**30** years of investing
**24** years at Putnam

**Michael Atkin**
Portfolio Manager
**30** years of investing
**21** years at Putnam

**Robert Davis, CFA**
Portfolio Manager
**19** years of investing
**19** years at Putnam

**Brett Kozlowski, CFA**
Portfolio Manager
**21** years of investing
**10** years at Putnam

**Michael Salm**
Co-Head of Fixed Income
**29** years of investing
**21** years at Putnam

**Paul Scanlon, CFA**
Co-Head of Fixed Income
**32** years of investing
**19** years at Putnam

**Bill Kohli describes Diversified Income Trust's approach to risk allocation**

### Rates
We actively manage rate risk with great flexibility. We make dynamic adjustments, and have often taken duration to negative levels.

### Credit
We can purse credit risk in corporates and mortgages as well as in below investment-grade debt and non-U.S. opportunities.

### Prepayment
We seek to add value by positioning in IOs and other securities as interest rates and mortgage refinancing trends change.

### Liquidity
We can pursue some opportunities with return potential that others may avoid due to constrained liquidity.

## Competitive returns over all major time periods

### Putnam Income Fund
(PNCYX)

Total returns as of 3/31/18

| | Class Y shares | BBG Barclays U.S. Aggregate Bond Index |
|---|---|---|
| 1 year | 4.12% | 1.20% |
| 3 years | 1.71 | 1.20 |
| 5 years | 2.50 | 1.82 |
| 10 years | 5.54 | 3.63 |

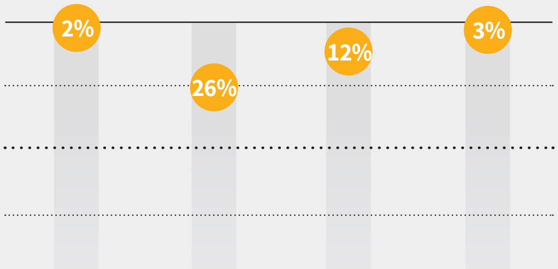
Total expense ratio: 0.63%

★★★★★

The fund received a 5-star Overall Morningstar Rating™ among 858 funds in the Intermediate-term bond category

Morningstar rankings as of 3/31/18

| YEARS | | | |
|---|---|---|---|
| 1 | 3 | 5 | 10 |
| INTERMEDIATE-TERM BOND FUNDS | | | |
| 13/999 | 209/858 | 100/784 | 14/561 |




### Putnam Diversified Income Trust
(PDVYX)

Total returns as of 3/31/18

| | Class Y shares | ICE BofAML U.S. Treasury Bill Index | BBG Barclays U.S. Aggregate Bond Index |
|---|---|---|---|
| 1 year | 6.22% | 1.04% | 1.20% |
| 3 years | 3.77 | 0.53 | 1.20 |
| 5 years | 3.31 | 0.35 | 1.82 |
| 10 years | 4.81 | 0.40 | 3.63 |

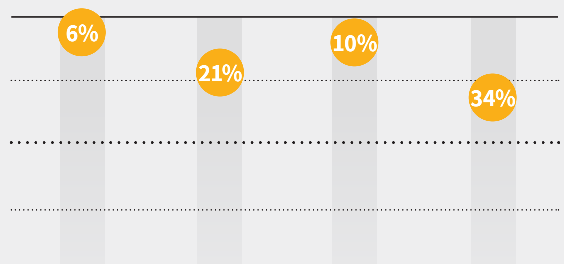
Total expense ratio: 0.75%

★★★★

The fund received a 4-star Overall Morningstar Rating™ among 264 funds in the Nontraditional bond category

Morningstar rankings as of 3/31/18

| YEARS | | | |
|---|---|---|---|
| 1 | 3 | 5 | 10 |
| NONTRADITIONAL BOND FUNDS | | | |
| 24/321 | 56/264 | 17/161 | 13/47 |




*Current performance may be lower or higher than the quoted past performance, which cannot guarantee future results. Share price, principal value, and return will vary, and you may have a gain or a loss when you sell your shares. Performance assumes reinvestment of distributions and does not account for taxes. For the most recent month-end performance, please visit putnam.com. Class Y shares before their inception are derived from the historical performance of the fund's class A shares, which have not been adjusted for the lower expenses; had they, returns would have been higher. For a portion of the periods, this fund may have had expense limitations, without which returns would have been lower. Class Y shares are generally only available for corporate and institutional clients and have no initial sales charge.*

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**BILL KOHLI**
CIO, Fixed Income

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**Consider these risks before investing:** International investing involves currency, economic, and political risks. Emerging-market securities carry illiquidity and volatility risks. Lower-rated bonds may offer higher yields in return for more risk. Funds that invest in government securities are not guaranteed. Mortgage-backed securities are subject to prepayment risk and the risk that they may increase in value less when interest rates decline and decline in value more when interest rates rise. Bond investments are subject to interest-rate risk (the risk of bond prices falling if interest rates rise) and credit risk (the risk of an issuer defaulting on interest or principal payments). Interest-rate risk is greater for longer-term bonds, and credit risk is greater for below investment grade bonds. Risks associated with derivatives include increased investment exposure (which may be considered leverage) and, in the case of over-the-counter instruments, the potential inability to terminate or sell derivatives positions and the potential failure of the other party to the instrument to meet its obligations. Unlike bonds, funds that invest in bonds have fees and expenses. Bond prices may fall or fail to rise over time for several reasons, including general financial market conditions, changing market perceptions (including perceptions about the risk of default and expectations about monetary policy or interest rates), changes in government intervention in the financial markets, and factors related to a specific issuer or industry. These and other factors may lead to increased volatility and reduced liquidity in the fund's portfolio. You can lose money by investing in the funds.

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