Q1 2021 | Putnam Dynamic Asset Allocation Funds Q&A

Bull market or pockets of bubble?

Robert J. Schoen
CIO, Global Asset Allocation
Industry since 1990

James A. Fetch
Co-Head of Global Asset Allocation
Industry since 1994

Jason R. Vaillancourt, CFA
Co-Head of Global Asset Allocation
Industry since 1993

Brett S. Goldstein, CFA
Portfolio Manager
Industry since 2010

We are bullish on equities in the second half of 2021 until the Fed signals a tapering of its bond-buying program.

The prospects of inflation and rising interest rates will test fixed-income markets.

President Biden's $1.9 trillion stimulus package and Covid-19 vaccinations will likely lift the economy.

How were market conditions in the first quarter?

Global financial markets ended the period mixed. Key equity market indices edged higher, driven by progress on Covid-19 vaccinations, stimulus packages, loose monetary policy and signs of economic recovery. In February and March, markets experienced bouts of volatility amid a sell-off in technology stocks, a trading frenzy in small and struggling companies, and inflation fears. The S&P 500 index, a broad measure of U.S. stocks, rose 6.17% for the quarter after hitting records in recent months. International stocks, as measured by the MSCI EAFE index (ND), climbed 3.48%.

The U.S. economic recovery is expected to support a stronger global comeback. President Biden's $1.9 trillion pandemic relief package has added tailwinds to the U.S. economy, boosted by vaccine rollouts. Stimulus-fueled growth and inflation expectations have driven yields on all but very short-term government debt higher during the quarter. Many investors are betting that inflationary pressures will eventually lead the Federal Reserve to raise short-term interest rates. As a result, rate-sensitive, fixed-income assets ended the period lower.

Yields on the 10-year U.S. Treasury note began the quarter at 0.93% and moved higher to end at 1.73%. Global bond yields, including high-yield and investment grade corporate debt, also trended slightly higher due to rising inflation concerns. Global bonds, as measured by the FTSE World Government Bond Index, fell 5.68%. The Bloomberg Barclays U.S. Aggregate Bond Index declined 3.37% for the period. U.S. high yield bonds experienced slight strength during the quarter.

How did the funds perform?

The three Dynamic Asset Allocation Funds had mixed results during the quarter. The Conservative Fund, with its more fixed-income-centric investments, fell 0.11%. The more equity-centric Balanced Fund and Growth Fund advanced 3.03% and 4.71 %, respectively. All three funds outperformed their custom benchmarks for the quarter.

What strategies affected performance?

Overall, our asset allocation decisions benefited the portfolios. Given the potential for a full reopening of the economy, we made a few changes to our allocation mix during the period. The portfolios began the period slightly overweight to equity risk relative to the custom blended benchmarks. Not long after, we increased our overweight position, which benefited the portfolios, as stocks soared to new highs with more stimulus and Covid-19 vaccine progress. We decreased our position to modestly overweight toward the end of the period, as it was an opportunistic time to take some profits.

In fixed income, we stayed neutral to rate risk throughout the duration of the period, which did not impact results. The portfolios were neutral to credit risk for the first half of the quarter, before we shifted to modestly overweight. This decision had a negligible effect on performance. An out-of-benchmark, long position to commodity risk, implemented in the beginning of the period, aided performance.

Our active implementation decisions slightly benefited results. Our quantitative U.S. large-cap equity strategy experienced strength, while our quantitative international equity strategy was slightly additive. Selection within opportunistic fixed income enhanced performance to a modest extent. These gains were partially offset by selection weakness from our fundamental U.S. large-cap growth strategy. The DAA Growth Fund experienced a slight loss from emerging-market equity selection.

What is your near-term outlook for the markets?

The global economy continues to recover, although at a slow pace. We remain encouraged by the current tailwinds for financial assets, which include the new U.S. stimulus package, easy monetary conditions, potential infrastructure spending, and ample liquidity. Still, we anticipate volatility in the months ahead as investors weigh the continued rollout of vaccines and the pace of reopening, with its implications for inflation and higher interest rates.

Given the current environment, we are bullish on equities in the second half of 2021 until the Fed is close to signaling a taper of their asset purchase program. The combination of pent-up demand and the Federal Reserve's easy monetary policy makes a compelling case for equities, we believe. In fixed income, our outlook on credit is modestly bullish. Banks have begun easing credit conditions for large corporate commercial and industrial loans, and average total leverage for new high-yield issues is back to the low levels seen in 2013. Our outlook on rate-sensitive fixed income is neutral, as we believe the distribution of potential outcomes is now roughly in line with long-term expectations. Fed officials have pledged to keep interest rates low until there is significant progress toward their inflation and employment goals for the U.S. economy.

Against this backdrop, we continue to have conviction in our investment strategies based on their strong long-term results. As for asset allocation, we will continue to take a tactical approach, adjusting exposure across various markets as conditions warrant. We will continue to monitor equity and fixed-income markets and add securities when we see attractive valuation levels.

Putnam Dynamic Asset Allocation Balanced Fund (PABYX)

Annualized total return performance as of 3/31/21

Class Y shares Inception 7/5/94	**Net asset value**	**Russell 3000 Index**	**Putnam Balanced Blended Benchmark**
Last quarter	3.03%	6.35%	2.36%
1 year	33.68	62.53	34.68
3 years	9.01	17.12	11.45
5 years	9.49	16.64	10.86
10 years	8.49	13.79	9.17
Life of fund	7.56	10.35	—

Total expense ratio: 0.71%

Class A share inception: 2/7/94

Putnam Dynamic Asset Allocation Conservative Fund (PACYX)

Annualized total return performance as of 3/31/21

Class Y shares Inception 7/14/94	**Net asset value**	**Bloomberg Barclays U.S. Aggregate Bond Index**	**Putnam Conservative Blended Benchmark**
Last quarter	-0.11%	-3.37%	-0.41%
1 year	16.19	0.71	17.30
3 years	6.40	4.65	8.23
5 years	6.16	3.10	7.17
10 years	5.98	3.44	6.46
Life of fund	6.13	5.13	—

Total expense ratio: 0.74%

Class A share inception: 2/7/94

Putnam Dynamic Asset Allocation Growth Fund (PAGYX)

Annualized total return performance as of 3/31/21

Class Y shares Inception 7/14/94	**Net asset value**	**Russell 3000 Index**	**Putnam Growth Blended Benchmark**
Last quarter	4.71%	6.35%	3.99%
1 year	46.53	62.53	46.99
3 years	10.16	17.12	12.76
5 years	11.52	16.64	12.94
10 years	9.60	13.79	10.29
Life of fund	8.37	10.35	—

Total expense ratio: 0.80%

Class A share inception: 2/8/94

Returns for periods of less than one year are not annualized.

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 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, these funds 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.

The funds' benchmarks are administered by Putnam Investments and have the following compositions: For Putnam Conservative Blended Benchmark, 65% Bloomberg Barclays U.S. Aggregate Bond Index, 25% Russell 3000 Index, 5% JPMorgan Developed High Yield Index, and 5% MSCI EAFE Index (ND); for Putnam Balanced Blended Benchmark, 50% Russell 3000 Index, 35% Bloomberg Barclays U.S. Aggregate Bond Index, 10% MSCI EAFE Index (ND), and 5% JPMorgan Developed High Yield Index; and for Putnam Growth Blended Benchmark, 60% Russell 3000 Index, 15% MSCI EAFE Index (ND), 15% Bloomberg Barclays U.S. Aggregate Bond Index, 5% JPMorgan Developed High Yield Index, and 5% MSCI Emerging Markets Index (GD). The Bloomberg Barclays U.S. Aggregate Bond Index is an unmanaged index of U.S. investment-grade fixed-income securities. The JPMorgan Developed High Yield Index is an unmanaged index of high-yield fixed-income securities issued in developed countries. The MSCI EAFE Index (ND) is an unmanaged index of equity securities from developed countries in Western Europe, the Far East, and Australasia. The MSCI Emerging Markets Index (GD) is a free float-adjusted market capitalization index that is designed to measure equity market performance in the global emerging markets. The Russell 3000 Index is an unmanaged index of the 3,000 largest U.S. companies. The MSCI World Index (ND) is an unmanaged index of equity securities from developed countries. The Dow Jones Industrial Average Index (DJIA) is an unmanaged price-weighted index composed of 30 blue-chip stocks. The S&P 500 Index is an unmanaged index of common stock performance. Securities in the funds do not match those in the indexes, and performance of the funds will differ. It is not possible to invest directly in an index.

For informational purposes only. Not an investment recommendation.

The views and opinions expressed are those of the portfolio managers as of March 31, 2021, are subject to change with market conditions, and are not meant as investment advice.

Consider these risks before investing: Allocation of assets among asset classes may hurt performance. The value of investments in the fund's portfolio may fall or fail to rise over extended periods of time for a variety of reasons, including general economic, political, or financial market conditions; investor sentiment and market perceptions; government actions; geopolitical events or changes; and factors related to a specific issuer, asset class, geography, industry, or sector. These and other factors may lead to increased volatility and reduced liquidity in the fund's portfolio holdings. International investing involves currency, economic, and political risks. Emerging-market securities carry illiquidity and volatility risks. Investments in small and/or midsize companies increase the risk of greater price fluctuations. Growth stocks may be more susceptible to earnings disappointments, and value stocks may fail to rebound. Funds that invest in government securities are not guaranteed. Mortgage-backed investments, unlike traditional debt investments, are also subject to prepayment risk, which means that they may increase in value less than other bonds when interest rates decline and decline in value more than other bonds 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). Default risk is generally higher for non-qualified mortgages. Interest-rate risk is generally greater for longer-term bonds, and credit risk is generally greater for below-investment-grade bonds. Unlike bonds, funds that invest in bonds have fees and expenses. The use of derivatives may increase these risks by increasing investment exposure (which may be considered leverage) or, in the case of over-the-counter instruments, because of the potential inability to terminate or sell derivatives positions and the potential failure of the other party to the instrument to meet its obligations. Our investment techniques, analyses, and judgments may not produce the outcome we intend. The investments we select for the fund may not perform as well as other securities that we do not select for the fund. We, or the fund's other service providers, may experience disruptions or operating errors that could have a negative effect on the fund. You can lose money by investing in the fund.

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Putnam Investments | 100 Federal Street | Boston, MA 02110 | putnam.com

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