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Q4 2017 | Putnam Dynamic Asset Allocation Funds Q&A

# Global equities maintain momentum


**Robert J. Schoen**
*CIO, GAA*
Industry since 1990

**James A. Fetch**
*Co-Head, GAA*
Industry since 1994

**Jason R. Vaillancourt,** CFA
*Co-Head, GAA*
Industry since 1993


***Equity markets end strongly for the year.***

***Short-term rates increased though longer bonds were little changed.***

***Inflation indicators remained subdued.***

**What characterized the global investment environment during the quarter ended December 31, 2017?**

Equity markets maintained positive momentum during the fourth quarter in the United States and globally as investors' risk appetites showed no signs of abating. Economic conditions remained solid during the quarter, with U.S. gross domestic product [GDP] readings surpassing 3% quarter over quarter and the unemployment rate stable at just over 4%. Inflation readings remained steady in spite of third-quarter weather-related disruptions in the United States and an uptick in oil prices that ended the quarter at $60 per barrel. The U.S. dollar was mixed before ending slightly lower for the quarter, but significantly lower on the year. After a contentious legislative period, the U.S. Congress passed a comprehensive and business-friendly tax reform bill.

For the three months ended December 31, 2017, the S&P 500 Index was up 6.64%. The MSCI EAFE Index [ND], a benchmark for developed-market stock performance outside the United States and Canada, ended the period up 4.23%. Emerging-market stocks led equity returns for the quarter as reflected in the MSCI Emerging Markets Index [GD] return of 7.50%.

### How did bond markets perform during the quarter?

The yield curve continued to flatten as short-term rates increased and long-term rates were unchanged or slightly lower for the quarter. The Federal Open Market Committee [FOMC] raised rates 25 basis points at its December meeting, the third increase during 2017, and indicated expectations for three increases in 2018, pending economic readings and events that might change the outlook.

The Bloomberg Barclays U.S. Aggregate Bond Index rose 0.39%, as the benchmark 10-year note stabilized. In credit-sensitive fixed income, as defined by the performance of high-yield bonds, prices ticked higher, with the JPMorgan Developed High Yield Index returning 0.75% for the quarter.

### How did Putnam Dynamic Asset Allocation Funds perform during the fourth quarter of 2017?

Each of the three Dynamic Asset Allocation Funds had positive returns for the quarter, generally performing in line with our expectations, as the funds are currently invested close to our strategic allocations. The Growth Fund had the strongest absolute return at 5.36%. The Conservative Fund's more fixed-income-centric construction produced a lower absolute return of 2.57%, while the Balanced Fund's return of 4.25% represented stronger performance within equities and lower relative performance in rate-sensitive fixed income.

### What were the principal factors affecting the funds' performance results?

We made minor shifts around benchmark allocations to favor U.S. large-cap stocks, but otherwise we maintained allocations close to the strategic benchmark allocations across domestic and international stock categories. Our asset allocation strategies during the quarter had a positive impact. In particular, our preference for equities over rate-sensitive fixed-income securities was beneficial given that stocks performed well. During the quarter we also took an out-of-benchmark position in commodities. This exposure to a broad basket of commodities had a meaningfully positive impact on the portfolio and serves as an example of using our tactical asset allocation flexibility to find opportunities in undervalued areas of the market.

Security selection and implementation was also positive for the quarter. Our stock selection in the United States was rewarded, adding value above and beyond the general rally in stocks. Fixed-income security selection, which focused on securitized debt — primarily mortgages, was another positive contributor. In the Growth portfolio, emerging-market equity selection was also positive. Security selection and implementation in international developed equity markets was a detractor, though not enough to offset selection strength in other parts of the portfolio.

### What is your investment outlook for the first quarter of 2018?

After an extended period of strong stock market gains and low volatility levels, it is certainly possible that volatility could increase, but economic factors are not signaling a recession. For the most part, consumer and business confidence remains high. The Federal Reserve has indicated that it expects to make three rate increases in 2018, while gradually reducing its fixed-income holdings. Europe is seeing more inflation than expected, and this is not priced in to rates currently. This could produce some volatility in euro-based sovereigns and corporate bonds. We expect rate normalization to continue, though monetary policy on the whole remains mostly accommodative.

As of the end of 2017, we have positioned the funds to be able to take advantage of opportunities that may arise after a period of outperformance in some stock categories. Within dynamic asset allocation, we will continue to take a tactical approach, adjusting the funds' exposure across various markets as conditions warrant.

Within the U.S. equity market, we believe it will be necessary to remain flexible. With the new tax laws in place, infrastructure spending may take center stage. At the same time, there has been little movement on trade policy, leaving that an unknown. High-yield bonds, which ended slightly positive for the reporting period, are becoming less attractive as spreads tighten and the credit cycle advances.

As always, the global growth outlook will be a factor. We believe it currently has a solid foundation.

## Putnam Dynamic Asset Allocation Balanced Fund (PABYX)

Annualized total return performance as of 12/31/17

| Class Y shares<br>Inception 7/5/94 | Net asset value | Russell 3000 Index | Putnam Balanced Blended Benchmark |
|---|---|---|---|
| Last quarter | 4.25% | 6.34% | 3.74% |
| 1 year | 15.44 | 21.13 | 14.41 |
| 3 years | 7.49 | 11.12 | 7.56 |
| 5 years | 10.19 | 15.58 | 9.61 |
| 10 years | 6.79 | 8.60 | 6.63 |
| Life of fund | 7.54 | 9.67 | — |

Total expense ratio: 0.75%

Class A share inception: 2/7/94

## Putnam Dynamic Asset Allocation Conservative Fund (PACYX)

Annualized total return performance as of 12/31/17

| Class Y shares<br>Inception 7/14/94 | Net asset value | Bloomberg Barclays U.S. Aggregate Bond Index | Putnam Conservative Blended Benchmark |
|---|---|---|---|
| Last quarter | 2.57% | 0.39% | 2.07% |
| 1 year | 10.04 | 3.54 | 8.97 |
| 3 years | 5.06 | 2.24 | 5.04 |
| 5 years | 6.68 | 2.10 | 5.95 |
| 10 years | 5.61 | 4.01 | 5.55 |
| Life of fund | 6.26 | 5.31 | — |

Total expense ratio: 0.79%

Class A share inception: 2/7/94

## Putnam Dynamic Asset Allocation Growth Fund (PAGYX)

Annualized total return performance as of 12/31/17

| Class Y shares<br>Inception 7/14/94 | Net asset value | Russell 3000 Index | Putnam Growth Blended Benchmark |
|---|---|---|---|
| Last quarter | 5.36% | 6.34% | 4.90% |
| 1 year | 20.08 | 21.13 | 19.02 |
| 3 years | 9.08 | 11.12 | 9.10 |
| 5 years | 12.15 | 15.58 | 11.41 |
| 10 years | 6.92 | 8.60 | 6.82 |
| Life of fund | 8.31 | 9.67 | — |

Total expense ratio: 0.86%

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. Class Y shares, available to investors through an asset-based fee program or for institutional clients, are sold without an initial sales charge and have no CDSC. For the most recent month-end performance, please visit putnam.com.*

The funds' benchmarks are administered by Putnam Investments and have the following compositions: 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; 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); 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. 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.

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**Putnam Investments | One Post Office Square | Boston, MA 02109 | putnam.com**

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