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Q3 2020 | Putnam Multi-Asset Absolute Return Fund Q&A

Equity gains in directional strategies help offset non-directional losses

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Global equity markets rallied in response to declining unemployment and hopes for a COVID-19 vaccine.

Directional strategies added to performance, while non-directional strategies detracted from performance.

The fund had near-neutral positioning at quarter-end as markets continued to absorb the economic impact of the pandemic.

What was the investment environment during the third quarter of 2020?

Global equity markets extended their rally in the third quarter, finishing with a second straight quarter of gains. Equity indices set record highs, driven by rising shares of big technology companies. For most of the quarter, markets continued to look past regional spikes in COVID-19 cases and a global health problem that has yet to be solved. Investor optimism rose with a recovering economy and hopes for a near-term coronavirus vaccine. However, this path to further gains was marked by increased volatility in September as uncertainties around additional stimulus, the presidential election, and the COVID-19 crisis lingered. Despite these concerns, the quarter closed on a positive note as economic data continued to surprise on the upside. The S&P 500 Index, a broad measure of U.S. stocks, and the MSCI World Index [ND] registered returns of 8.93% and 7.93%, respectively, for the quarter.

Rate-sensitive fixed income held up, as interest rates and inflation risk remained low. Federal Reserve Chairman Jerome Powell signaled a major policy shift to average inflation targeting to boost the economy and jobs market. The central bank has said they will allow inflation to run higher than the 2% target for some time before raising interest rates. High-yield bonds saw significant gains for the quarter, despite a volatile September. Commodity prices rose in the third quarter, but the pace of the recovery has slowed. Member nations of the Organization of the Petroleum Exporting Countries [OPEC] continued to reduce inventories, but virus concerns further stalled increases in demand. The Bloomberg Barclays U.S. Aggregate Bond Index posted a return of 0.62% for the three-month period. The yield on the benchmark 10-year Treasury note was range bound, starting the quarter at 0.66% and ending at 0.69%.

Before we discuss performance, would you summarize the fund's overall investment objective and strategy?

Putnam Multi-Asset Absolute Return Fund seeks a positive return exceeding the return of Treasury bills over a reasonable period of time, regardless of market conditions. The fund seeks to achieve risk-and-return characteristics by dynamically allocating assets using a combination of directional [or market sensitive] and non-directional [or market neutral] strategies.

The directional portion of the portfolio consists of two components: a risk-balanced portfolio of stocks and bonds, designed to efficiently capture long-term market returns, and a dynamic asset allocation overlay to reflect tactical views. The overlay consists of tactical longs and shorts to equities, rates, credit, and commodities based on the team's expectations for each of these asset classes. The team manages both the composition and total level of risk, depending on market conditions and the prevailing opportunity set.

The non-directional portion of the portfolio consists of long/short market neutral strategies that provide flexible uncorrelated sources of alpha.

How did the fund perform for the three months ended September 30, 2020?

The fund's class Y shares recorded a –0.19% decline, just falling shy of the cash benchmark, the ICE BofA U.S. Treasury Bill Index, which posted a return of 0.04%.

What factors had the biggest influence on performance?

Directional strategies added to performance in the third quarter. The equity portion of the risk-balanced portfolio finished positive, while our modest tactical short in equities at the beginning of the period detracted from performance. Our position was moved to neutral toward the latter half of the period. The portfolio was net long equity risk overall, resulting in a slightly positive contribution from directional equity performance. The fixed-income portion of the risk-balanced portfolio finished slightly positive, while our modest tactical short to interest-rate risk did not significantly impact performance. The portfolio was net long rates overall, resulting in a slightly positive contribution from directional rates. The portfolio benefited from our modest tactical long to credit risk.

Overall, non-directional strategies detracted from results in the third quarter. Equity-selection alpha strategies weighed down results. Specifically, our forensic accounting strategy, which seeks to identify and short companies that utilize overly aggressive accounting, experienced the greatest weakness. Our quantitative U.S. large-cap equity long/short and low-beta stock selection strategies detracted, but to a smaller extent. Strength in our emerging-market equity long/ short and global equity long/short strategies helped offset some of the loss. These strategies are designed to perform independently of global stock markets.

Within fixed income, our selection alpha strategy detracted from results. This was largely due to a selection strategy focused on structured mortgage credit.
Our regional fixed-income strategy slightly added to performance. The alternative beta strategy experienced strength, driven by volatility carry outperformance. Finally, our commodity alpha strategy was another notable positive contributor.

How was the fund positioned at the start of the fourth quarter?

The fund is positioned close to neutral as we enter the fourth quarter. Within our dynamic allocation overlay, we are tactically short interest-rate risk, neutral in terms of equity risk and commodity risk, and slightly long credit risk. Within the overall directional component, which includes the structural risk balanced portfolio and the dynamic allocation overlay, we are long all asset classes.

What is your outlook for the global economy?

Markets extended their rally in the third quarter, despite a rocky September. We enter the fourth quarter with the possibility of a resurgence in coronavirus cases and volatility leading up to the presidential election. However, we remain encouraged by COVID-19 medical advances, and the willingness of the Fed and Congress to provide support in the form of massive stimulus measures and policy changes. Credit markets finished higher for the quarter, as spreads continued to tighten, and yields declined. We remain optimistic due to increased levels of liquidity, a result of the Fed's bond buying program.

In equities, we remain close to neutral as the situation remains highly fluid. Markets are still working to assess the economic impact of this public health challenge. U.S. Treasuries continue to be in high demand relative to other developed government bonds. That said, economic weakness and a potential second wave of COVID-19, as well as ensuing economic shutdowns could cause the bellwether 10-year Treasury to test the lower bounds of the Fed's target range of 0%–0.25%.

Oil prices continue to increase in response to improved investor sentiment and ongoing supply cuts. However, we see downside risks until demand becomes more robust and the ongoing OPEC cuts lower inventories further.

Against this backdrop, we continue to look for signs of stabilization and any progress on the medical front to help stop the spread of COVID-19.

Putnam Multi-Asset Absolute Return Fund (PDMYX)

Annualized total return performance as of 9/30/20

Class Y shares *Inception 12/23/08*	**Net asset value**	**ICE BofA U.S. Treasury Bill Index**
Last quarter	–0.19%	0.04%
1 year	–10.11	1.19
3 years	–2.70	1.73
5 years	0.16	1.22
10 years	2.36	0.66
Life of fund	3.28	0.60

Total expense ratio: 0.71%
What you pay: 0.68%

"What you pay" reflects Putnam Management's decision to contractually limit expenses through 2/28/21.

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. For a portion of the periods, the 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.

The S&P 500 Index is an unmanaged index of common stock performance. The MSCI World Index (ND) is an unmanaged index of equity securities from developed countries. The Bloomberg (BBG) Barclays U.S. Aggregate Bond Index is an unmanaged index of U.S. investment-grade fixed-income securities. The ICE BofA U.S. Treasury Bill Index is an unmanaged index that tracks the performance of U.S. dollar-denominated U.S. Treasury bills publicly issued in the U.S. domestic market. Qualifying securities must have a remaining term of at least one month to final maturity and a minimum amount outstanding of $1 billion. You cannot invest directly in an index.

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Alpha is a measure of performance on a risk-adjusted basis. Alpha takes the volatility of a mutual fund and compares its risk-adjusted performance to a benchmark index. The excess return of the fund relative to the return of the benchmark index is a fund's alpha.

For informational purposes only. Not an investment recommendation.

The views and opinions expressed are those of the portfolio managers as of September 30, 2020, are subject to change with market conditions, and are not meant as investment advice. All performance and economic information is historical and is not indicative of future results.

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. Growth stocks may be more susceptible to earnings disappointments, and value stocks may fail to rebound. 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 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. 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, 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. The fund may have to invest the proceeds from prepaid investments, including mortgage- and asset-backed investments, in other investments with less attractive terms and yields. International investing involves currency, economic, and political risks. Emerging-market securities have illiquidity and volatility risks. Our alpha strategy may lose money or not earn a return sufficient to cover associated trading and other costs. Our use of leverage obtained through derivatives increases these risks by increasing investment exposure. 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. The fund's efforts to produce lower-volatility returns may not be successful. The fund may not achieve its goal, and it is not intended to be a complete investment program. 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. The fund's prospectus lists additional risks.

The fund is not intended to outperform stocks and bonds during strong market rallies.

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Request a prospectus or summary prospectus from your financial representative or by calling 1-800-225-1581. The prospectus includes investment objectives, risks, fees, expenses, and other information that you should read and consider carefully before investing.

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