Q1 2019 | Putnam Retirement Advantage Funds Q&A

Markets rebound as the Fed turns dovish

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

Brett S. Goldstein, CFA
Portfolio Manager, GAA
Industry since 2010

Global equity markets recover from 2018 lows as risk aversion declines.

Parts of the U.S. Treasury yield curve have inverted, raising concerns about a recession.

Federal Reserve turns dovish on interest rates as U.S. economy cools.

What was the equity market environment during the first quarter?

Global equity markets recovered during the quarter, rebounding from last quarter's slide that was spurred by worries over global economic growth and rising interest rates. The Federal Reserve left its benchmark rate unchanged in March and signaled little appetite for raising it again in the near future. The Fed's dovish pivot boosted U.S. and international equities and sent long-term Treasury yields on a declining streak. Large-cap stocks and their mid- and small-cap counterparts gained as market volatility fell. The broad S&P 500 Index rose 13.65% during the quarter, and the MSCI World Index [ND] gained 12.48%.

U.S. growth is cooling from last year under the weight of the Trump administration's trade war, economic slowdowns in Europe and China, and fading stimulus from the tax cuts of 2017. The economy grew at a 2.2% annual rate in the fourth quarter of 2018, after expanding 3.4% in the third quarter. Still, the unemployment rate touched multi-decade lows, inflation remains anchored, and the likelihood of a recession remains low. Slowing economic activity contributed to the Fed's decision to pause its three-year campaign to tighten monetary policy. The Fed will also begin to taper the runoff from its estimated $4.5 trillion bond portfolio in May and end it in September.

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The global economy is also slowing. China's economy, the world's second-biggest, is also grappling with a slowdown as policy makers roll out more fiscal and monetary measures to cushion growth. China and the United States appear to be close to a trade deal, and any truce would be a positive step. Across the Atlantic, the European Central Bank [ECB] also left benchmark interest rates unchanged in March. The bank said it expects its key interest rates "to remain at their present levels" at least through the end of 2019.

How did bond markets perform?

U.S. Treasury yields generally fell across the yield curve, which continued to flatten. The yield on the benchmark 10-year note traded around 2.41%, while the two-year yield fell to around 2.27% at the end of March 2019. Parts of the Treasury yield curve have inverted. In March, the yield on the 10-year note dipped below the yield on 3-month bills for the first time since mid-2007. An inverted yield curve — which plots bond yields with differing maturity dates — is considered a potential recession indicator.

High-yield bonds had positive returns for the period and generally outperformed investment-grade fixed-income securities. The return of investor appetite for holding riskier assets and a lack of new issuance helped pull high-yield bond spreads tighter. The more rate-sensitive Bloomberg Barclays U.S. Aggregate Bond Index rose 2.94%.

How did Putnam Retirement Advantage Funds perform?

The Retirement Advantage funds had positive returns during the quarter. Performance was generally in line with our internal custom benchmarks, with near-retirement strategies outperforming benchmarks while strategies further from retirement lagged slightly.

The glide path of Retirement Advantage strategies is an important tool that distinguishes Putnam from its peers. Our glide path starts off more aggressive than the average for our peer group, with a higher equity weight in the early part of the glide path for funds serving people retiring in the 2050s or 2060s. Our glide path becomes more conservative relative to peers for the funds serving investors nearing retirement in the 2020s or 2030s. Given strong equity returns during the first quarter, our near-retirement portfolios underperformed longer-dated strategies given the orientation of the glide path and our emphasis on protecting near-retirement participants.

What strategies affected performance?

The funds' positive performance resulted from our investments in equities, bonds, and commodities. Each of the portfolios held out-of-benchmark positions in commodities at the start of the year. This allocation boosted the funds' returns as energy prices rebounded from the sell-off in the fourth quarter. We also held an overweight position in U.S. equities at the start of 2019. These positions helped performance because of the sharp bounce in stock prices in January and February.

Our active implementation decisions and security selections detracted at the beginning of the year. Our quantitative strategy in U.S. large-cap stocks was the primary area of weakness during the quarter. As we discussed before, our team analyzes stock market history to identify characteristics of stocks [factors] that have excess risk-adjusted returns. Despite a strong long-term relationship between these factors and positive stock performance, the strategies underperformed during the quarter. We did see positive contributions from our fixed-income selection strategies. But that was not enough to offset losses from our equity selection.

Overall, the positive contributions from our dynamic allocation decisions were largely offset by implementation weakness. That left our strategies near the benchmark performance for the quarter.

What is the outlook for the second quarter of 2019?

Higher interest rates, weaker demand from China, political troubles in the eurozone, and protectionist tariffs have put pressure on growth. But we expect global growth to stabilize as 2019 progresses. The U.S. economy is also facing rising headwinds and is expected to expand at a more moderate pace in 2019 compared with last year. The Fed expects 2.1% growth this year, down from the 2.3% it forecast in December. We believe inflationary pressures will also remain modest.

The Fed's Jerome Powell said at the March rate-setting meeting that short-term interest rates could be on hold for "some time" as global risks weigh on the economic outlook and inflation remains muted. In December 2018, Fed officials said they expected two rate increases this year and another in 2020. They now project one rate hike in 2020 and none in 2021.

We expect stock and bond market volatility to persist in 2019. During the quarter, we decreased our exposure to equity, inflation [commodities], and interest rates [government bonds] and increased our exposure to credit [corporate bond spreads]. We downgraded our position in equities from overweight to slightly overweight relative to the benchmarks. We had increased our equity allocation in the fourth quarter to take advantage of short-term market weakness. But we have reverted to only a slight overweight because of the rebound in stocks in January, improvements in market sentiment and positionings, and the continued potential for negative trade-related headlines.

In credit-sensitive fixed income, we upgraded our position to a slight overweight. This is due to positive signals from our quantitative model, attractive bond spreads, and lower new issuance. In rate-sensitive fixed income, we downgraded our position to underweight. We expect interest rates to trend higher given the below-average real yields on the 10-year Treasury and the historically low premium attached to the 10-year note.

Finally, we downgraded our commodities exposure to neutral and removed commodities from our portfolios. The strong rally in energy prices made the qualitative view more balanced after being skewed positive following the fourth-quarter sell-off. We moved to neutral in the absence of strong qualitative or quantitative signals.

Putnam Retirement Advantage Funds

Annualized total return performance as of 3/31/19

Class I	Inception	Last quarter	1 year	3 years	5 years	10 years	Life of fund
Putnam Retirement Advantage Maturity:I	1/3/08	6.68%	4.41%	6.27%	4.66%	9.22%	4.99%
Retirement Advantage Maturity Benchmark	—	5.99	5.30	4.85	4.70	6.88	5.06
Putnam Retirement Advantage 2020:I	1/3/08	6.68	4.23	5.31	4.54	9.69	4.88
Retirement Advantage 2020 Benchmark	—	6.05	5.27	5.57	4.73	9.04	4.68
Putnam Retirement Advantage 2025:I	1/3/08	7.44	3.66	7.00	5.60	11.20	5.37
Retirement Advantage 2025 Benchmark	—	7.09	5.13	7.46	5.84	10.70	5.39
Putnam Retirement Advantage 2030:I	1/3/08	9.03	3.53	8.37	6.33	12.14	5.68
Retirement Advantage 2030 Benchmark	—	8.99	5.45	8.95	6.60	11.74	5.83
Putnam Retirement Advantage 2035:I	1/3/08	10.20	3.03	9.30	6.85	12.76	5.97
Retirement Advantage 2035 Benchmark	—	10.10	5.28	9.94	7.11	12.41	6.10
Putnam Retirement Advantage 2040:I	1/3/08	11.04	2.81	9.79	7.14	13.14	6.07
Retirement Advantage 2040 Benchmark	—	10.89	5.29	10.50	7.46	12.90	6.21
Putnam Retirement Advantage 2045:I	1/3/08	11.34	2.83	10.12	7.33	13.51	6.18
Retirement Advantage 2045 Benchmark	—	11.40	5.32	10.94	7.72	13.34	6.33
Putnam Retirement Advantage 2050:I	1/3/08	11.59	2.84	10.44	7.52	13.82	6.38
Retirement Advantage 2050 Benchmark	—	11.88	5.33	11.38	7.98	13.70	6.52
Putnam Retirement Advantage 2055:I	12/22/10	11.75	2.83	10.73	7.67	—	9.86
Retirement Advantage 2055 Benchmark	—	12.32	5.36	11.74	8.19	—	9.96
Putnam Retirement Advantage 2060:I	2/10/16	11.81	2.80	10.75	—	—	13.89
Retirement Advantage 2060 Benchmark	—	12.55	5.43	11.81	—	—	15.20
S&P 500 Index	—	13.65	9.50	13.51	10.91	15.92	8.46*
Bloomberg Barclays U.S. Aggregate Bond Index	—	2.94	4.48	2.03	2.74	3.77	3.76*

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

* Returns reflect the period 1/2/08–3/31/19.

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. Performance data reflect the impact of a 0.50% management fee. In certain cases, your plan's management fee may be higher and your return lower. For the most recent month-end performance, call your plan's toll-free number.

The Retirement Advantage Custom Benchmarks are unmanaged indexes administered by Putnam Management, consisting of various indexes that follow the underlying strategies of the portfolios. The S&P 500 Index is an unmanaged index of common stock performance. The Bloomberg Barclays U.S. Aggregate Bond Index is an unmanaged index of U.S. investment-grade fixed-income securities. You cannot invest directly in an index.

Each Putnam Retirement Advantage Fund has a different target date indicating when the fund's investors expect to retire and begin withdrawing assets from their account, typically at retirement. The funds are generally weighted more heavily toward more aggressive, higher-risk investments when the target date of the fund is far off, and more conservative, lower-risk investments when the target date of the fund is near. The principal value of the funds is not guaranteed at any time, including the target date.

For informational purposes only. Not an investment recommendation.

The views and opinions expressed are those of the portfolio managers as of March 31, 2019, are subject to change with market conditions, and are not meant as investment advice.

The funds are a collective trust managed and distributed by Putnam Fiduciary Trust Company, a non-depository New Hampshire trust company. However, they are not FDIC insured; they are not a deposit or other obligation of, and are not guaranteed by, Putnam Fiduciary Trust Company or any of its affiliates. The funds are not a mutual fund registered under the Investment Company Act of 1940, and their units are not registered under the Securities Act of 1933. The funds are only available for investment by eligible, qualified retirement plan trusts, as defined in the declaration of trust and participation agreement.

Diversification does not guarantee a profit or ensure against loss. It is possible to lose money in a diversified portfolio.

Consider these risks before investing: 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. 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.

Money market options are not insured or guaranteed by the Federal Deposit Insurance Corporation (FDIC) or any other governmental agency. Although the funds seek to preserve the value of your investment at $1.00 per share, it is possible to lose money by investing in these funds.

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. You can lose money by investing in the funds. See the fund’s offering statement for more information.

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You should carefully consider the investment objective, risks, charges, and expenses of a fund before investing. To request the offering document of the fund, call your financial representative or call Putnam at 1-800-225-1581. You should read the offering document carefully before investing.

Putnam Retail Management

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

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