

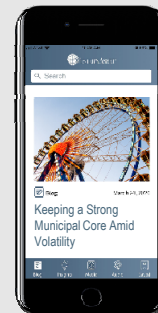


Thank you for joining Western Asset's
2Q20 Market & Strategy Update webcast
featuring CIO Ken Leech.

The presentation will begin shortly.



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2Q20 Market & Strategy Update

April 7, 2020

Ken Leech
Chief Investment Officer

Coronavirus Shock

Sharpest monthly decline in risk assets on record

Both a demand and supply shock

Government-mandated economic shutdown experiment

Extent and length of growth shortfall unknown

Oil price adds deflationary impulse

Not GFC; while timing is unknown, the growth shortfall should prove transitory

US Growth Dramatically Downgraded for 2020

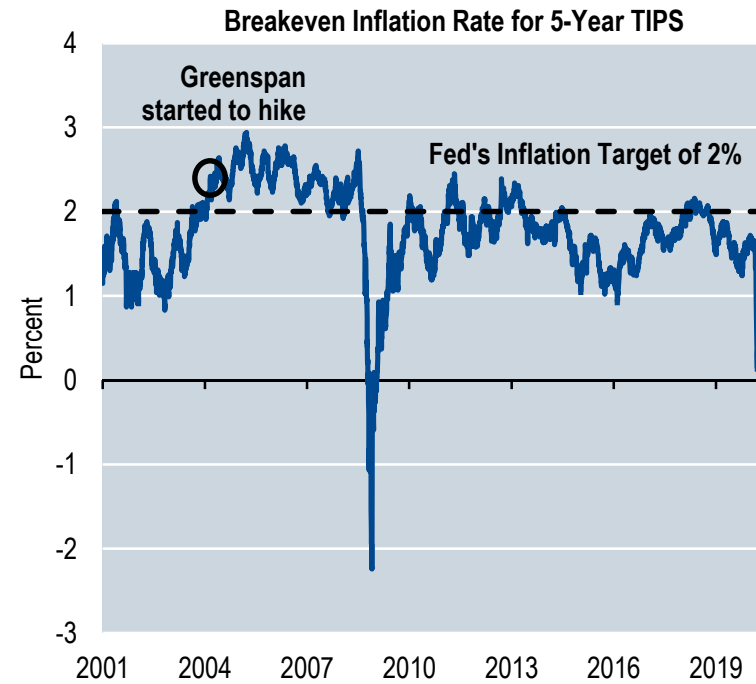


Source: Wall Street Bank, Western Asset. As of 06 Apr 20

Inflation – Expectations and Trends

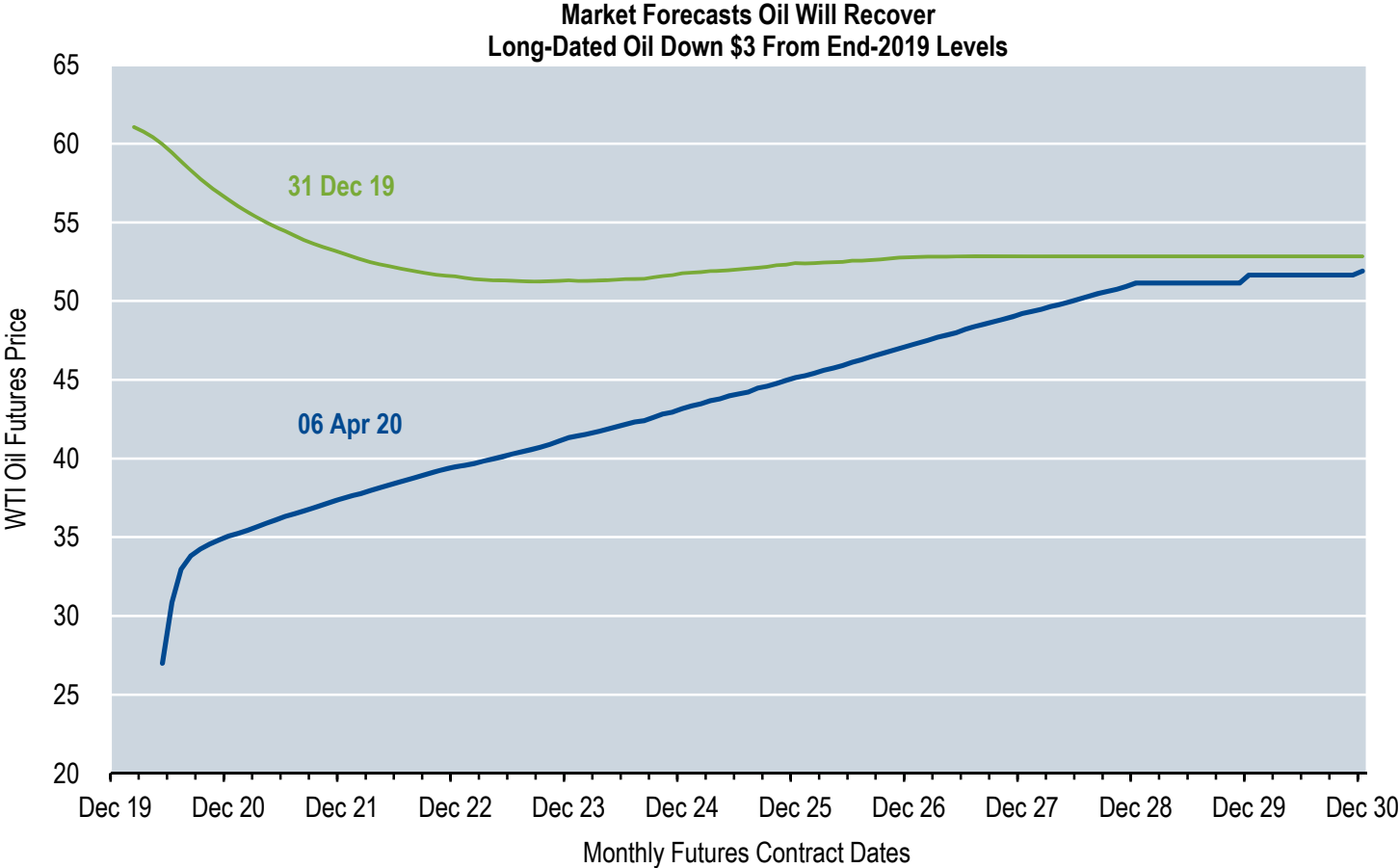
10-Year Breakeven Inflation (%)	
Australia	0.63
Canada	0.49
Germany	0.50
Japan	-0.16
US	1.16

Source: Bloomberg. As of 06 Apr 20



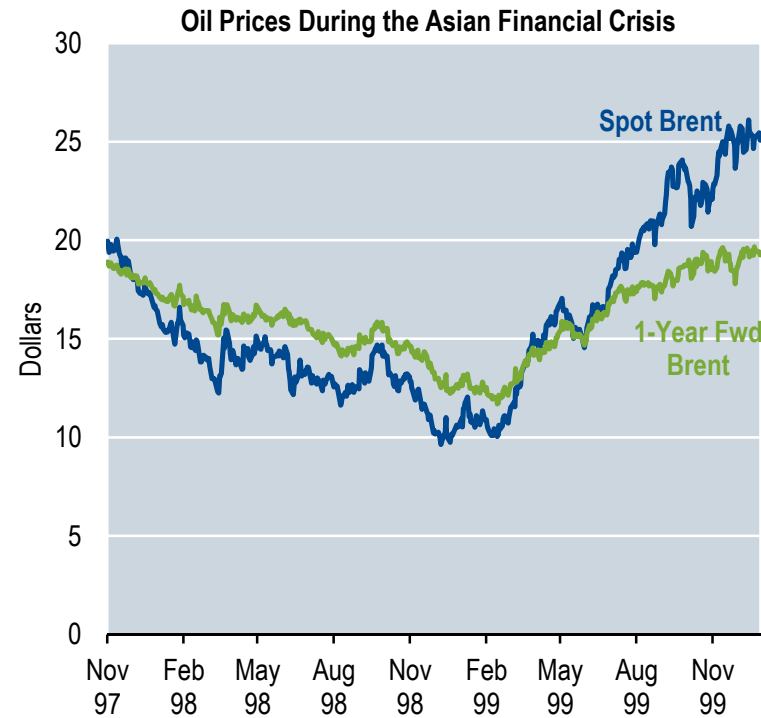
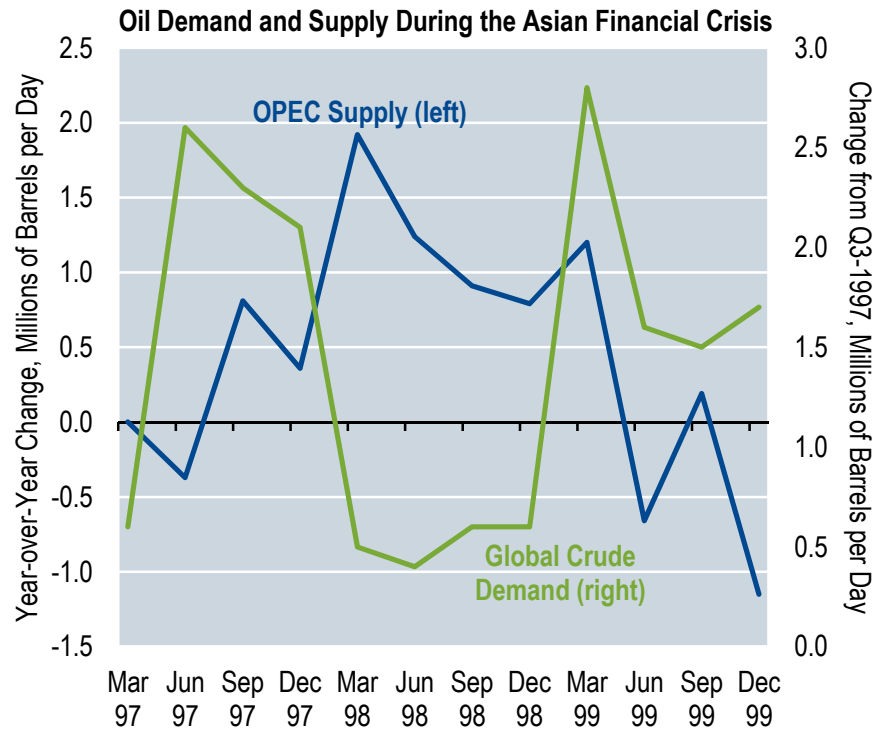
Source: Gavekal. As of 03 Apr 20

Oil Price War Has Added a Deflationary Shock



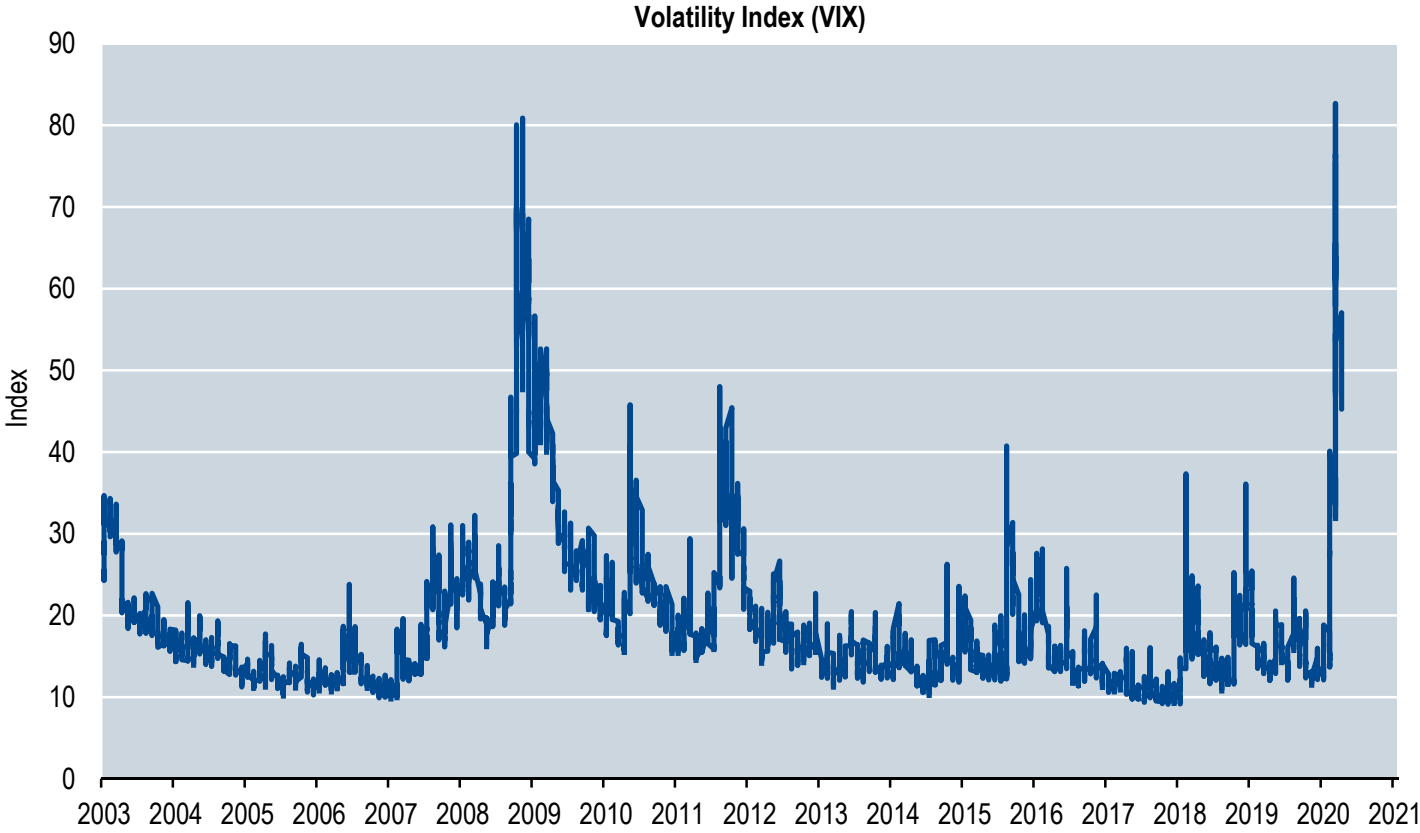
Source: Bloomberg. As of 06 Apr 20

Oil Prices Recovered With Demand Following the Asian Financial Crisis



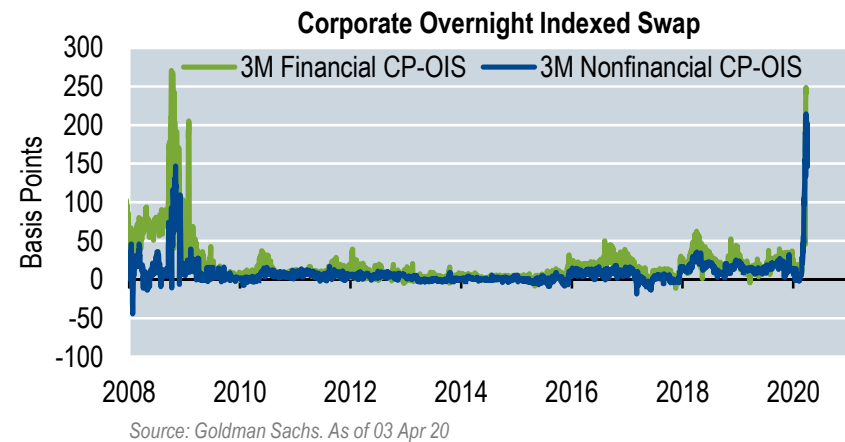
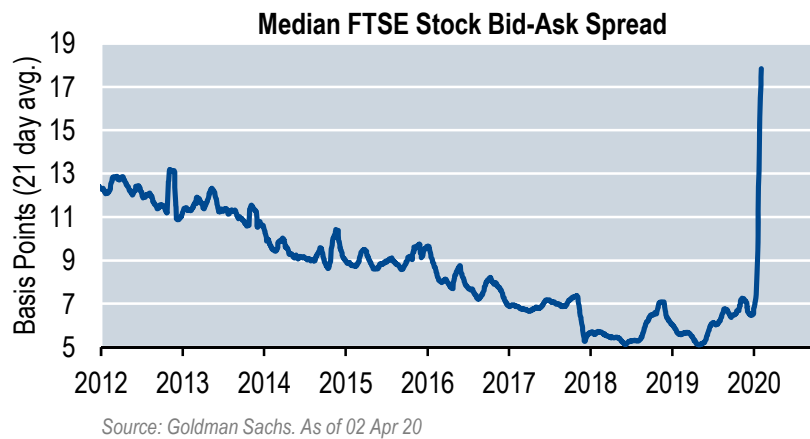
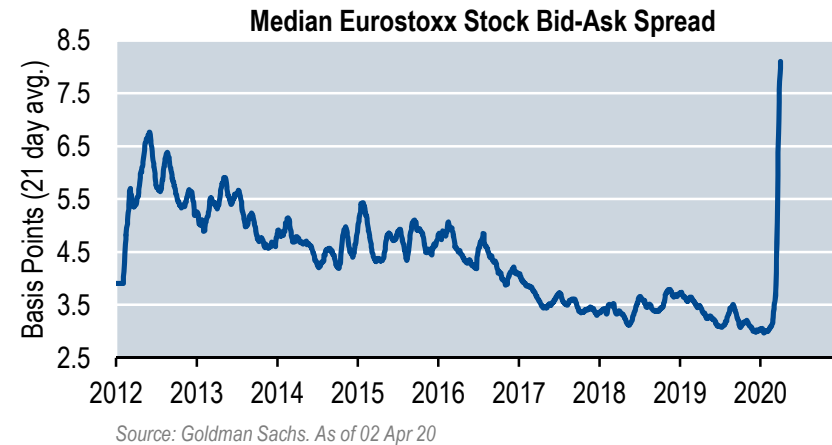
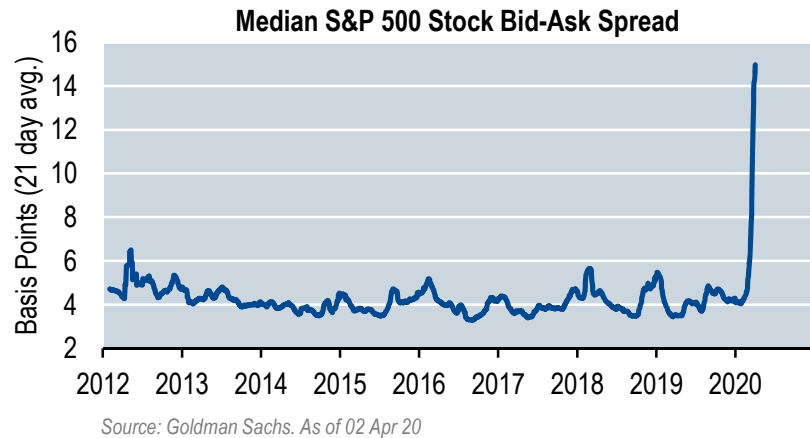
Source: IEA, DOE, Bloomberg. As of 31 Dec 99

Equity Stress Reaches GFC Levels

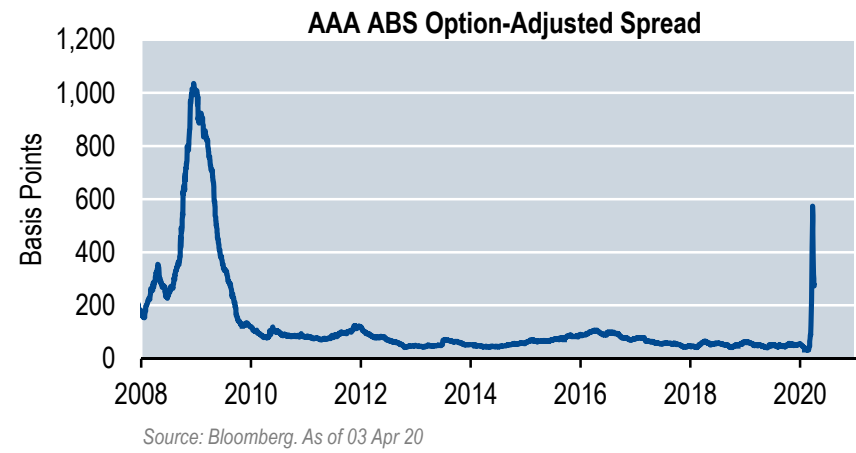
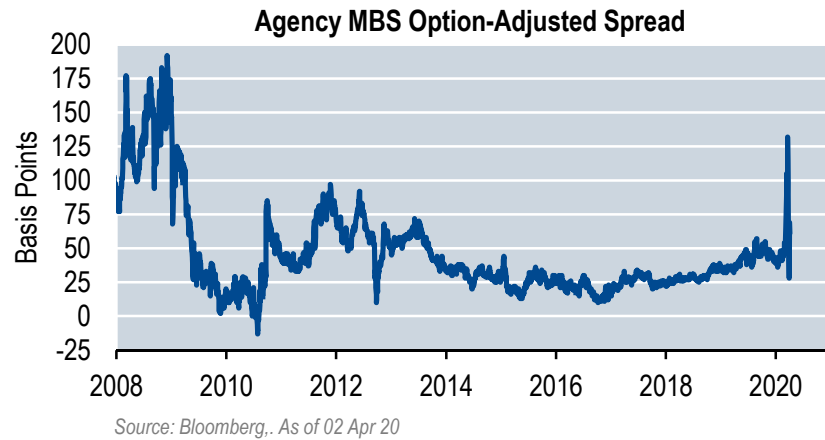


Source: Bloomberg. As of 06 Apr 20

Global Equity Liquidity Evaporated

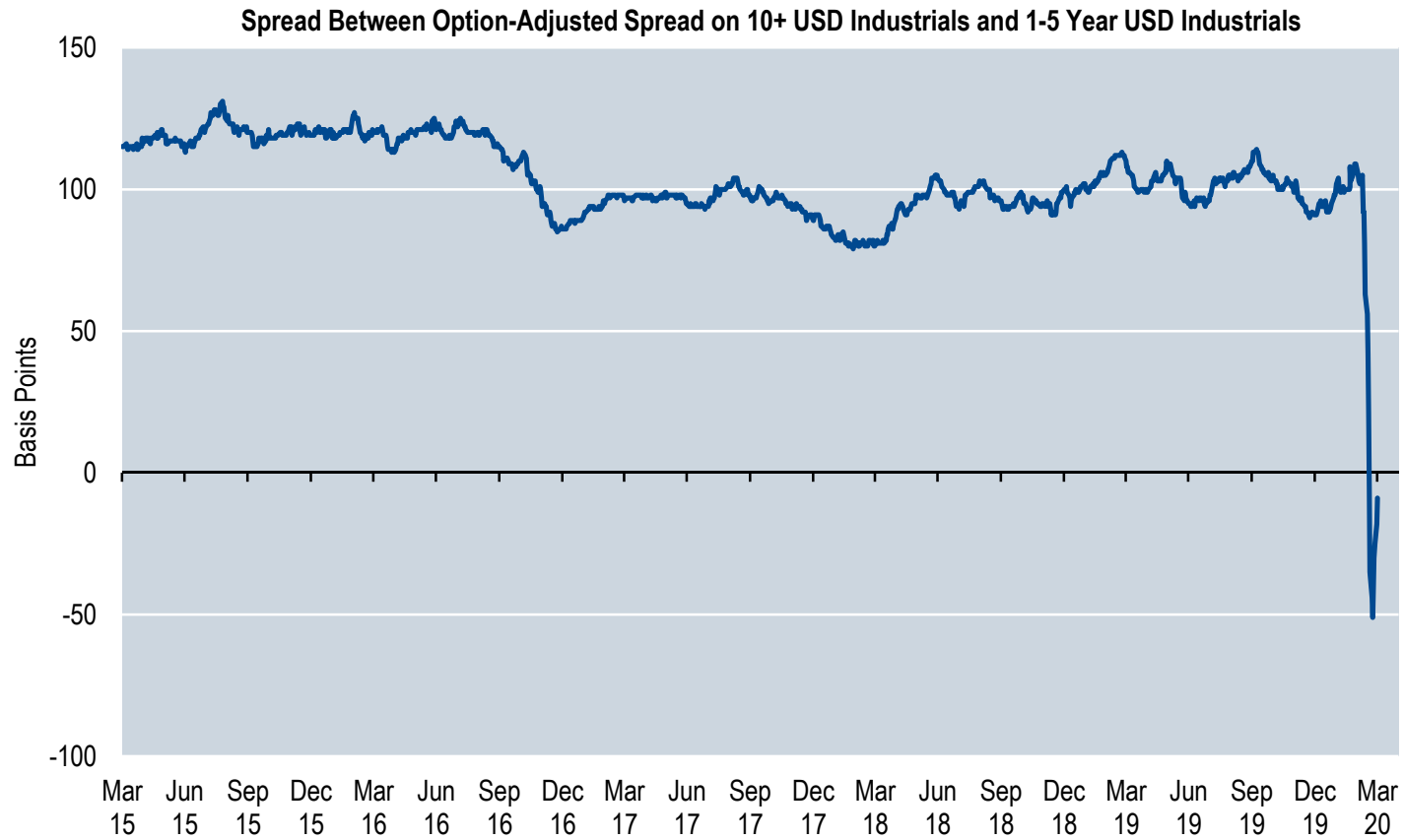


Agency and AAA Sectors Collapsed



Credit Curve Inversion

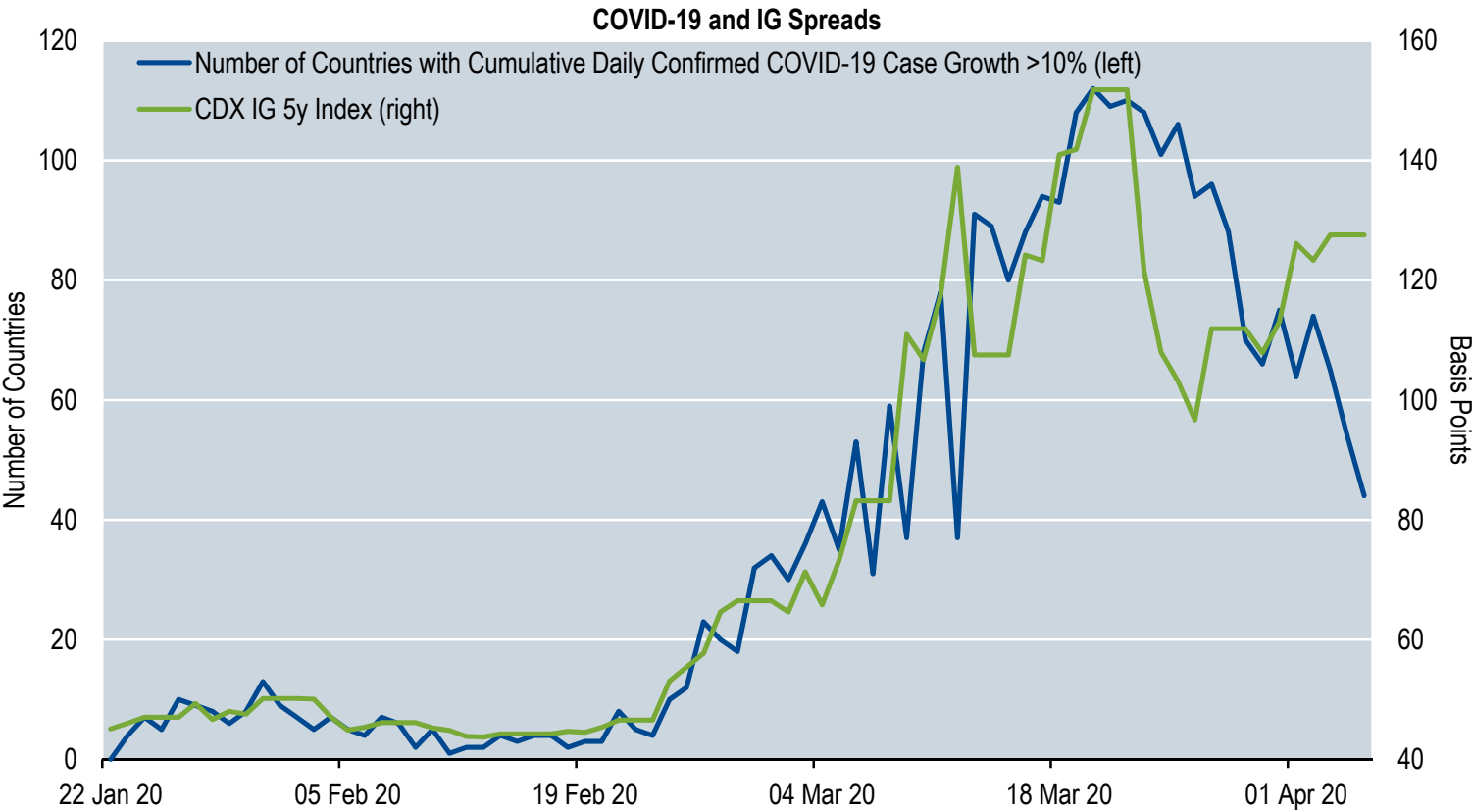
Front-end spreads have meaningfully underperformed.



Source: Bloomberg. As of 31 Mar 20

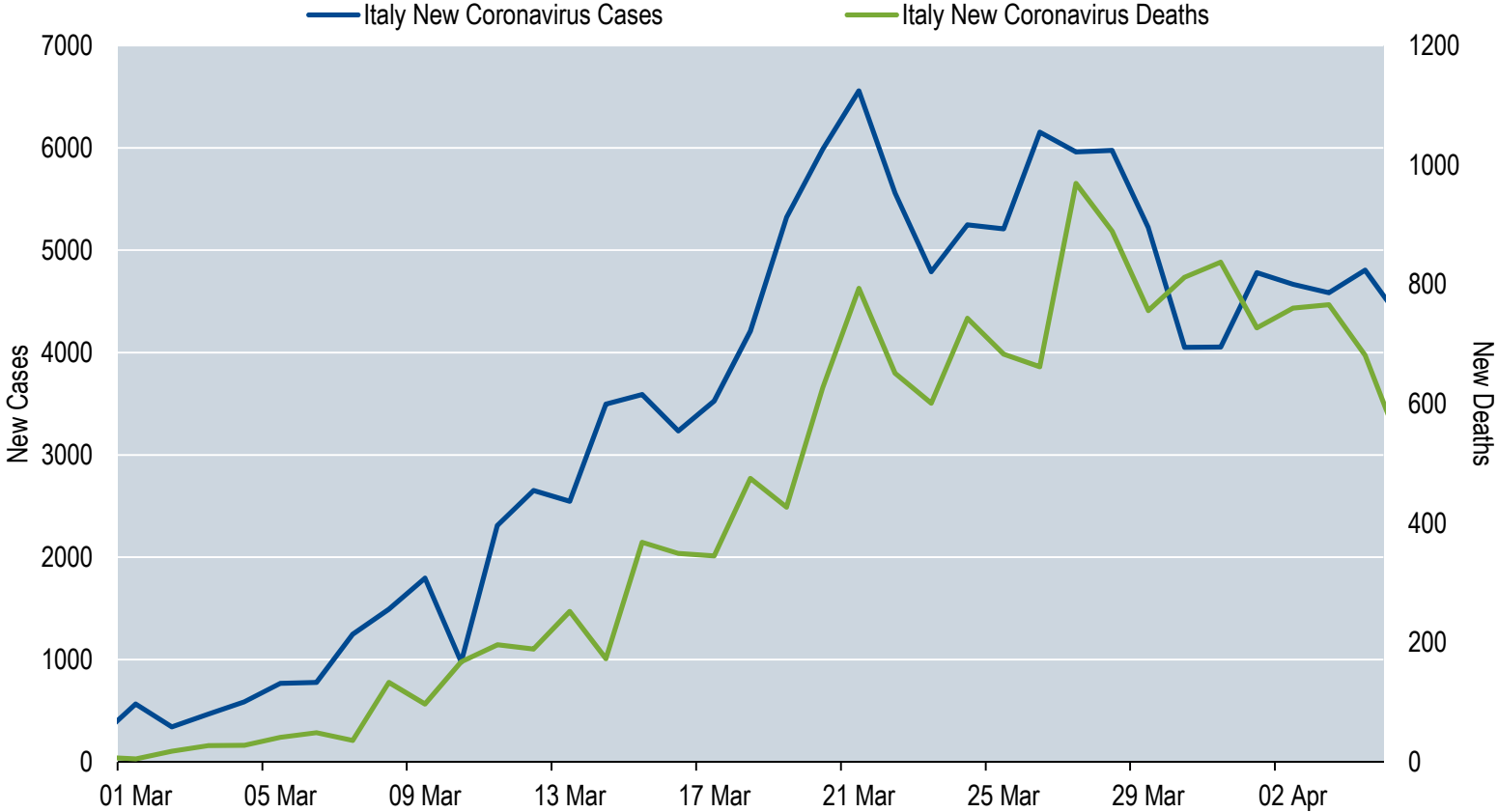
- **The virus is extremely contagious and hard to predict**
- **Modelling error has been high, as the denominator is still unknown**
- **Policy tradeoffs between saving lives and saving the economy**
- **Testing is the key to the puzzle**
- **A vaccine would be a game changer, but is likely many months away**

Market Is Following the Path of the Virus



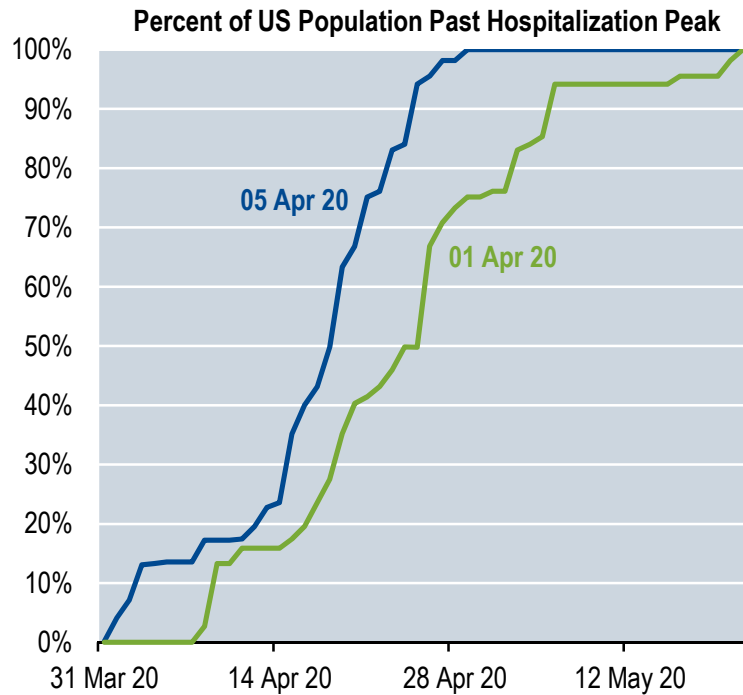
Source: JP Morgan, Bloomberg. As of 06 Apr 20

Recent Virus Data in Italy Is Encouraging

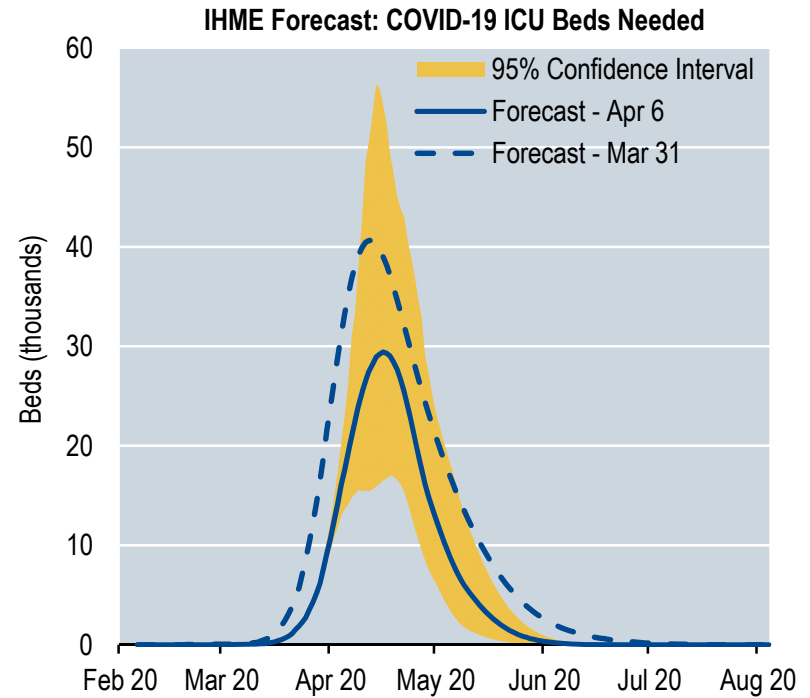


Source: Bloomberg. As of 04 Apr 20

IHME Forecast Constantly Subject to Substantial Revisions

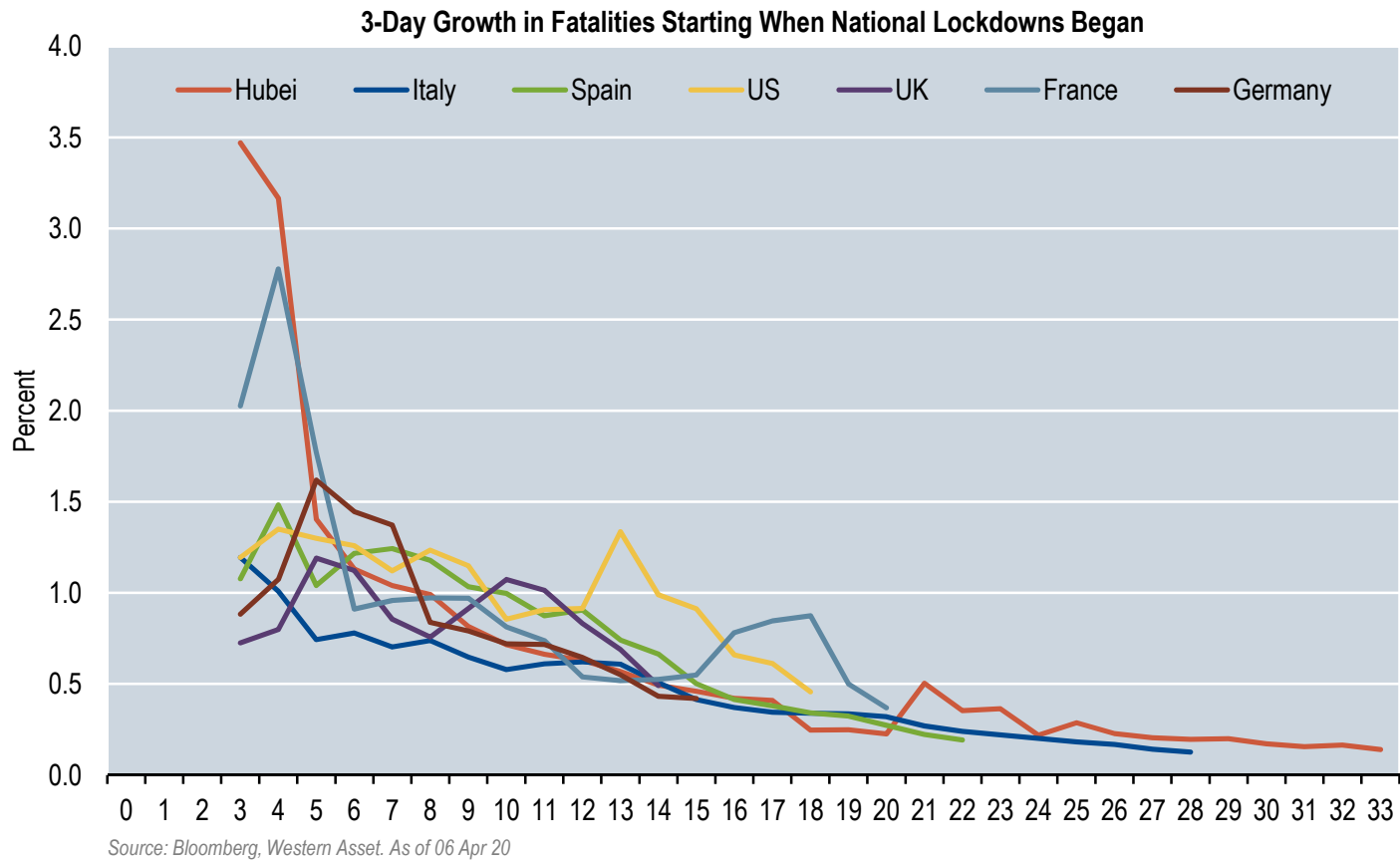


Source: Institute for Health Metrics and Evaluation. As of 05 Apr 20



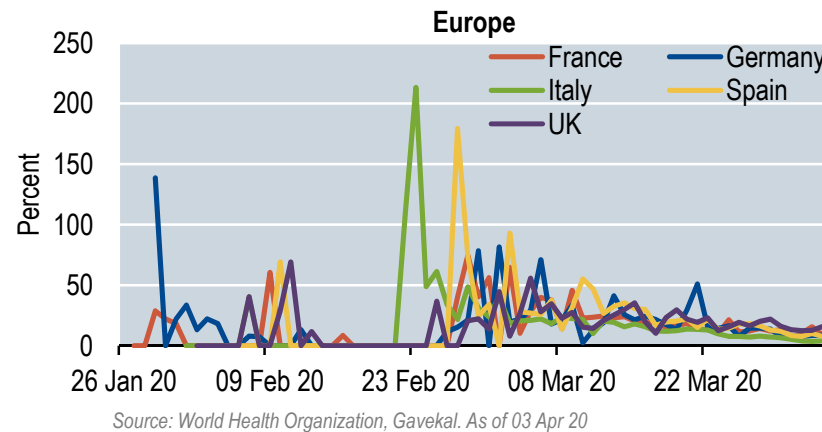
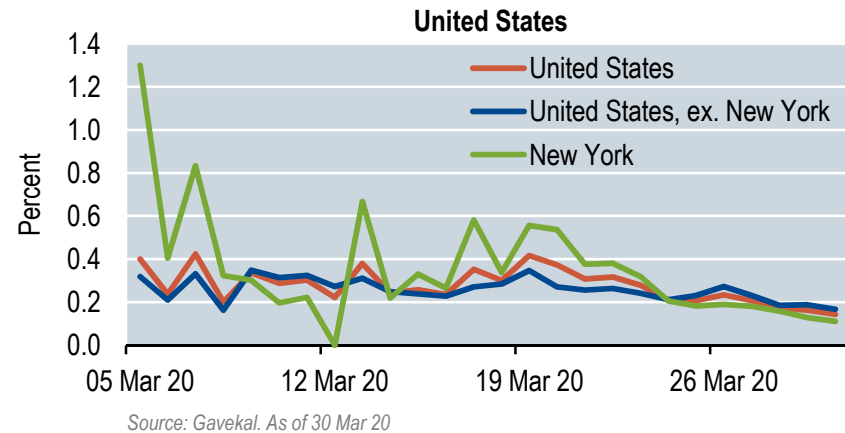
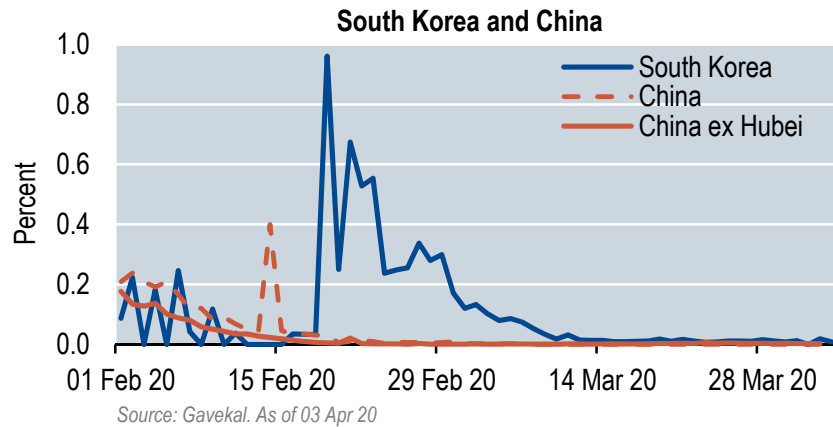
Source: Institute for Health Metrics and Evaluation. As of 06 Apr 20

Fatality Growth Rates Converging to Hubei Levels



The Virus Map Is Looking Similar Globally

Jolt of Confirmed COVID-19 Cases (Change in Growth Rates)



Coronavirus Task Force Base Case

The impact of COVID-19 is looking more like the Spanish flu than SARS

Peak US health care utilization suggests containment measures will be in place through at least early May

After peak hospitalizations, an opportunity to relax containment, starting in late Q2

- Concerns over reinfection will slow relaxation and keep borders closed

Economic recovery starts in Q3 and gains steam in Q4

- China as a case study – economic activity is back to 70-80% of pre-virus levels two months after lockdown
- Consumer spending recovery may lag – travel/leisure/sports impacted

Health care/technology – more of a 2021 event

- Increased virus and antibody testing should help the return to work
- Vaccines and therapeutics – not expected until 2021

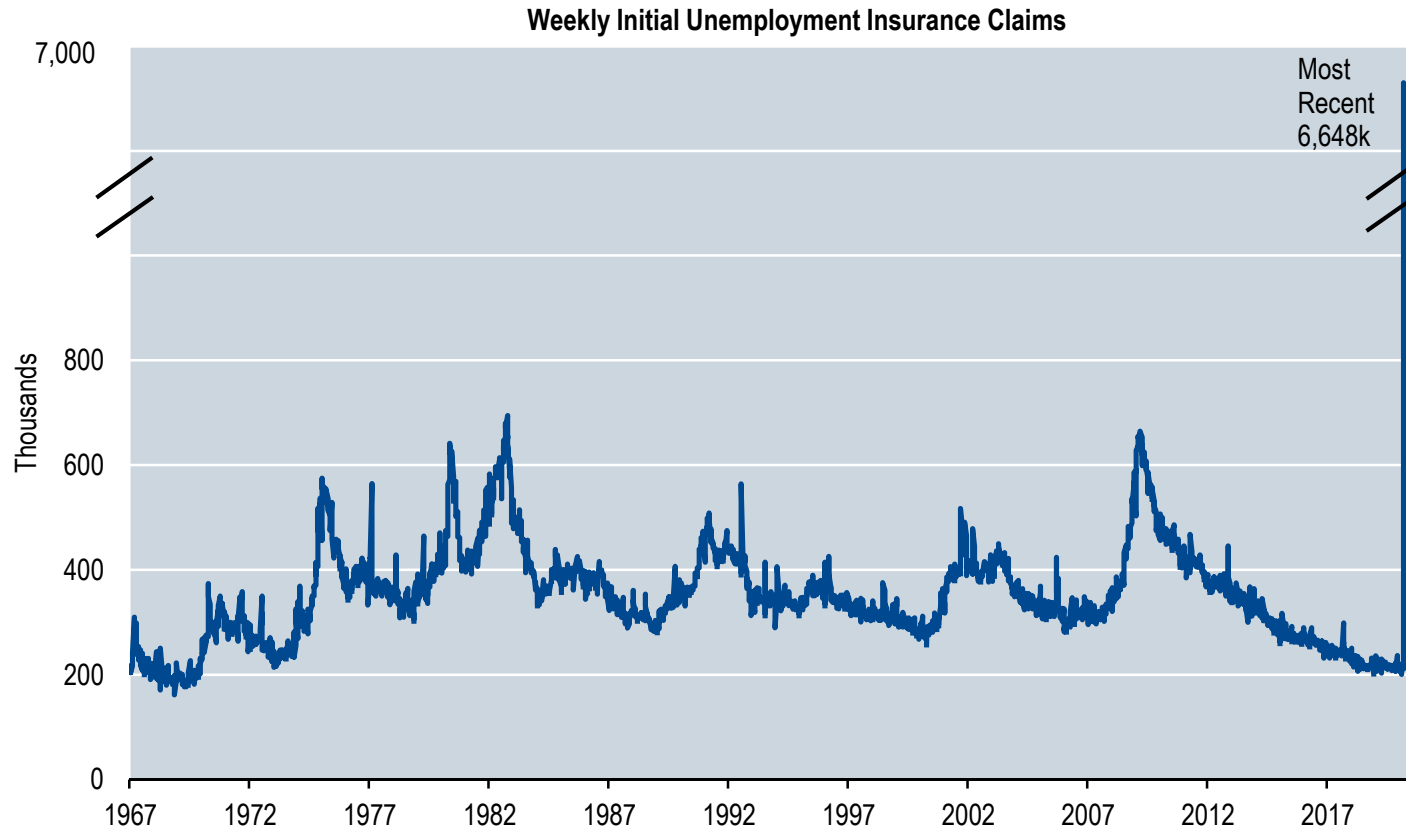
Risks we are monitoring

- Threat of second waves of infection – would prolong containment measures and economic recovery
- Changes in virus behavior – mutation could increase severity, but more asymptomatic cases could improve herd immunity

A Different Sort of Crisis?

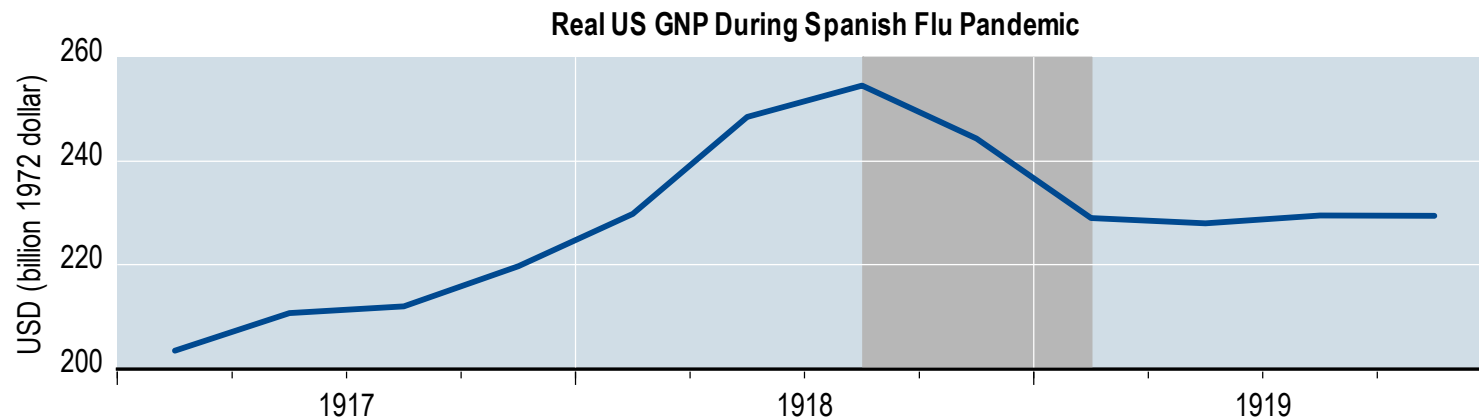
- **Length and depth of downdraft unknown**
- **Strong likelihood for eventual recovery**
- **What form might future policy take and how long might it be needed?**
- **Global monetary and fiscal stimulus have accelerated and will continue to accelerate**

US Growth Falling Fast and Furious



Source: US Department of Labor. As of 02 Apr 20

Effects of Spanish Flu Were Quite Short-Lived



- The decline in GNP shown in the chart coincides BOTH with the deadliest months of the Spanish flu and also the end of WWI. The demobilization following the end of fighting would typically, by itself, be associated with recession, so it is hard to disentangle the effects of war's end and pandemic on economic output.
- Spanish flu is thought to have infected 500 million people, 25% of world population then, with associated fatalities of 17 to 50 million, possibly as high as 100 million. US incidence estimated at 450,000 deaths.
- Pandemic lasted from Jan 1918 through Dec 1920 worldwide. The "second wave," starting in August 1918 proved to be more deadly.
- "After the lethal second wave struck in late 1918, new cases dropped abruptly – almost to nothing after the peak in the second wave. In Philadelphia, for example, 4,597 people died in the week ending 16 October, but by 11 November, influenza had almost disappeared from the city."

Source: Wikipedia, National Bureau of Economic Research

Very Different Recession

- **No physical destruction**
- **Self-imposed shutdowns**
- **Monetary and fiscal policy completely supportive**

China Outlook: Nascent Signs of Economic Normalization

Despite abating coronavirus outbreak, China maintains systematic control

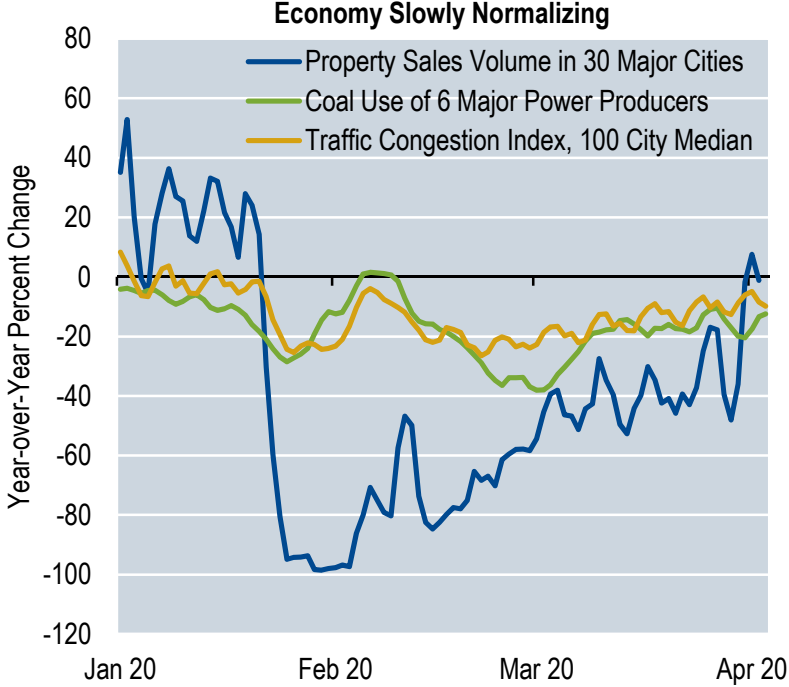
March leading indicators are encouraging

Financial market conditions continue to be growth-supportive

Fiscal policy is also becoming supportive

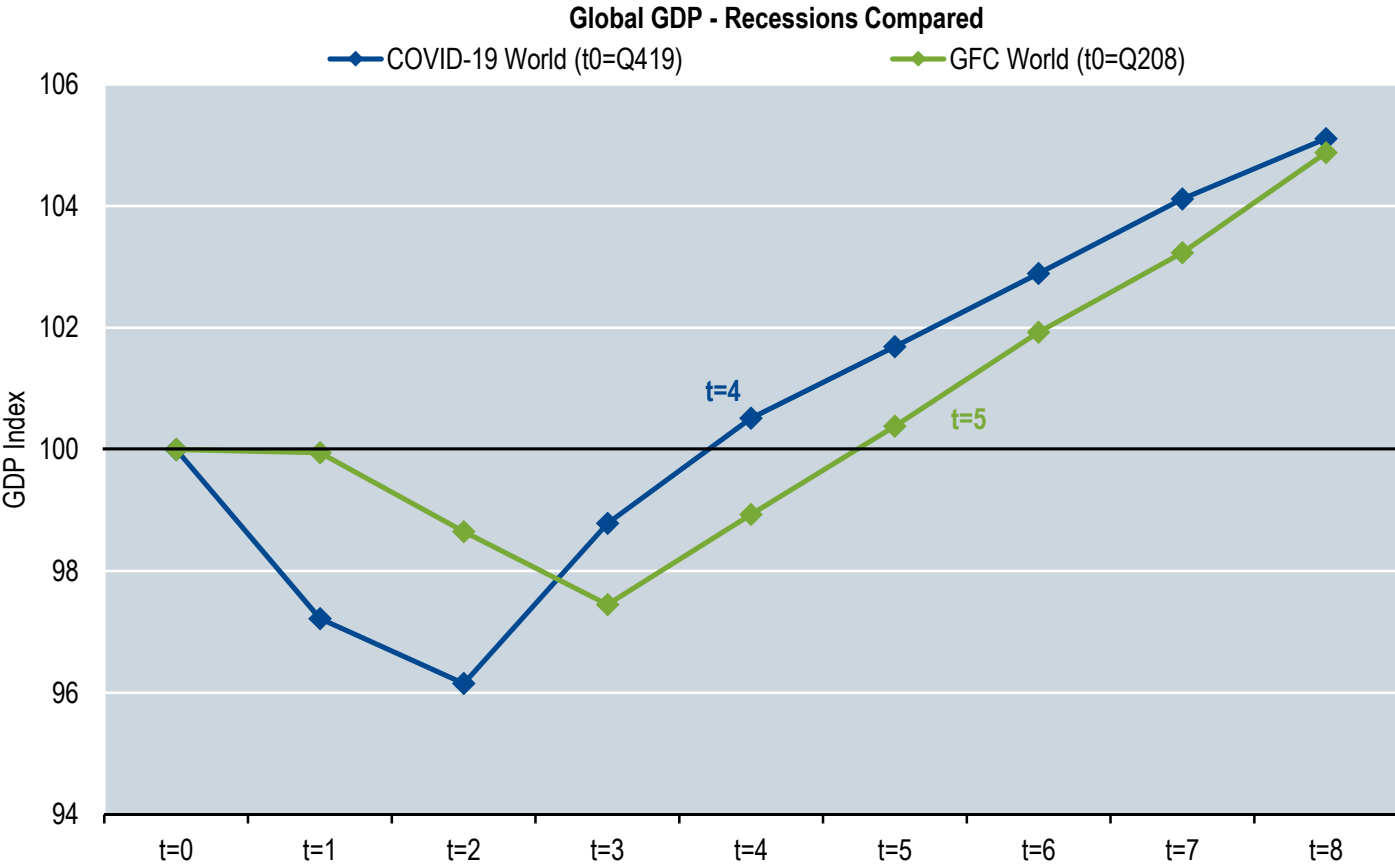


Source: Bloomberg. As of 31 Mar 20



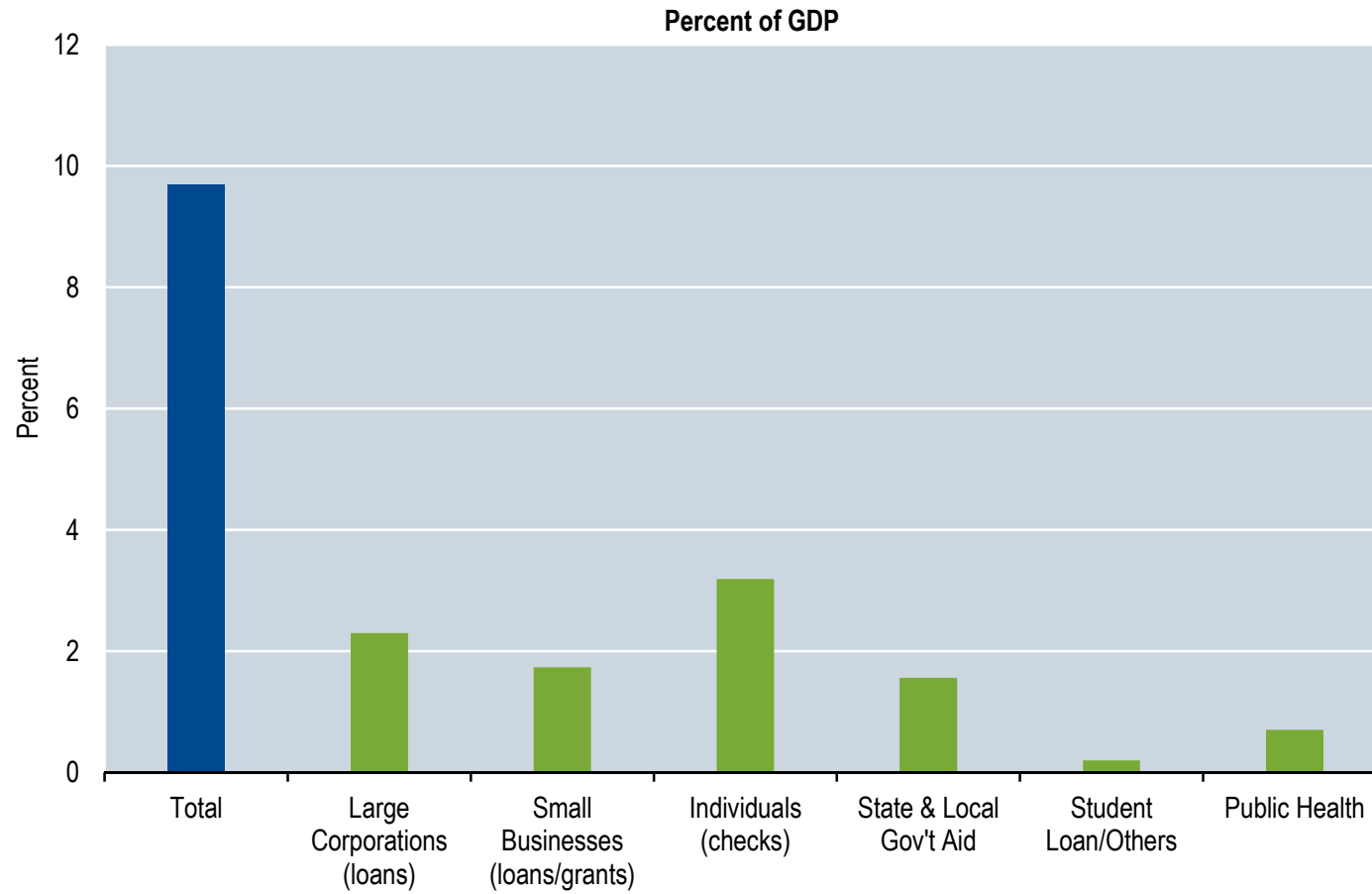
Source: Gavekal. As of 03 Apr 20

How Well Will the Global Economy Hold Up?



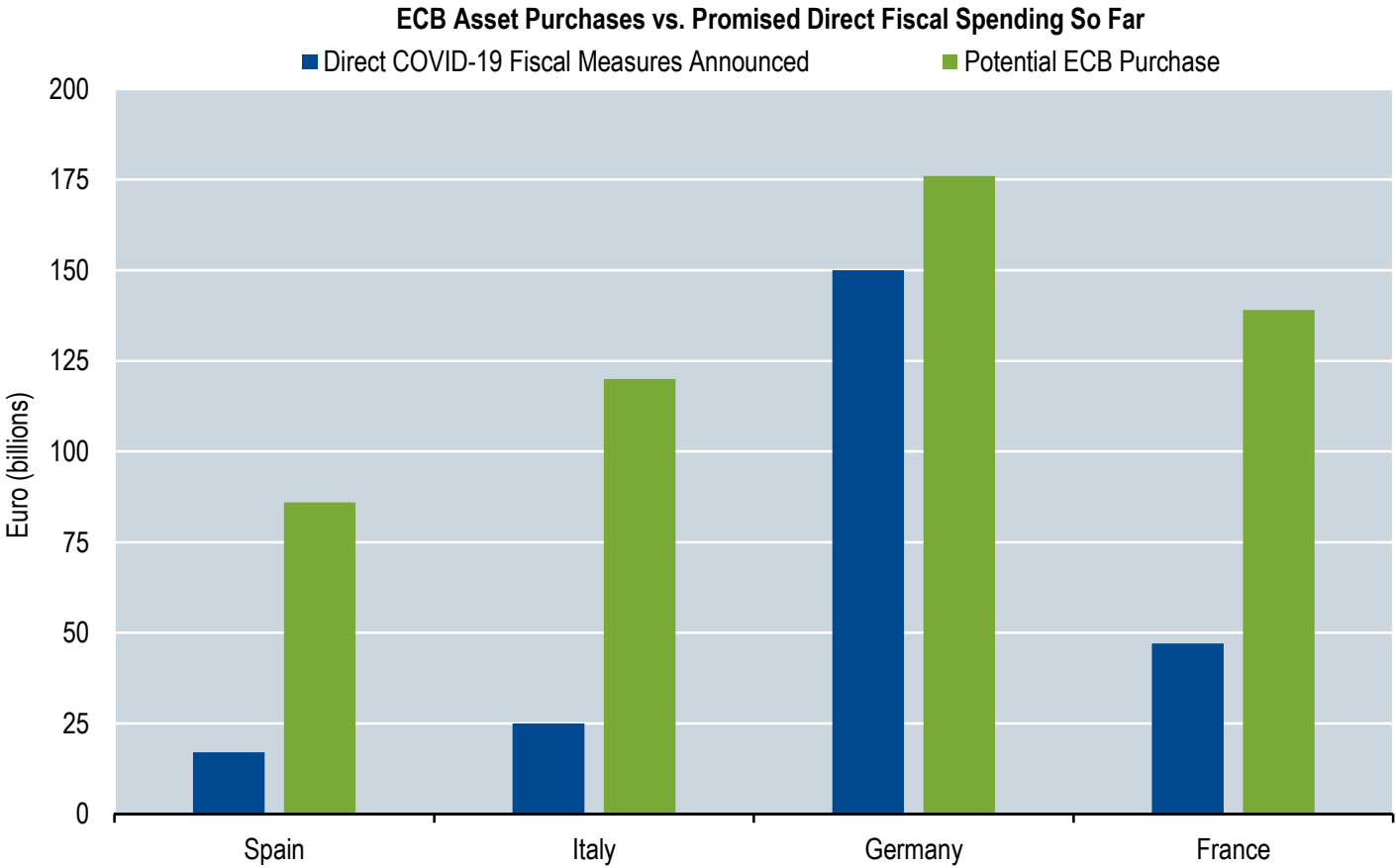
Source: UBS, Haver, JP Morgan. As of 31 Mar 20

The CARES Act



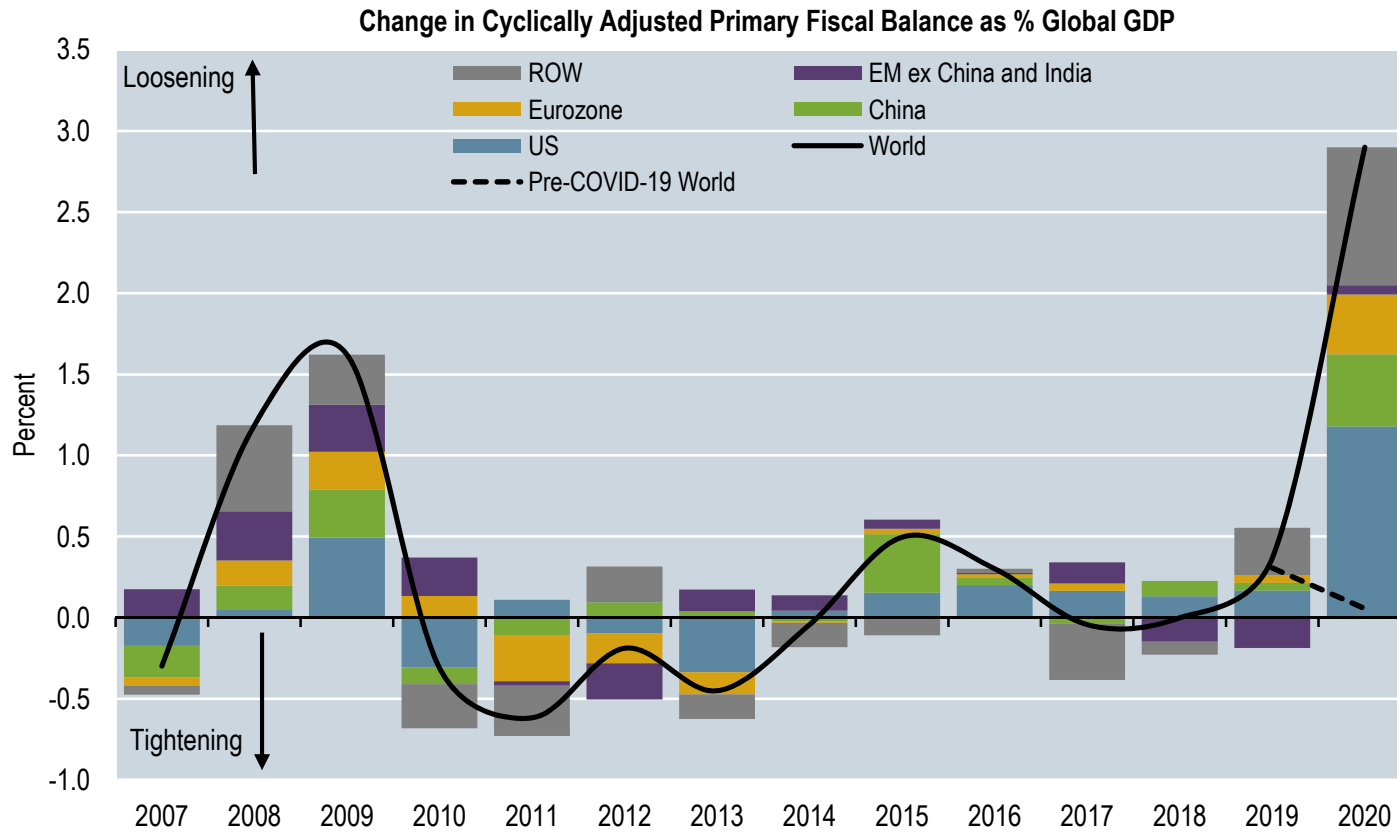
Source: Gavikal

Europe Responds Forcefully



Source: Gavekal

Will the Enormity of Global Stimulus Prove Sufficient?

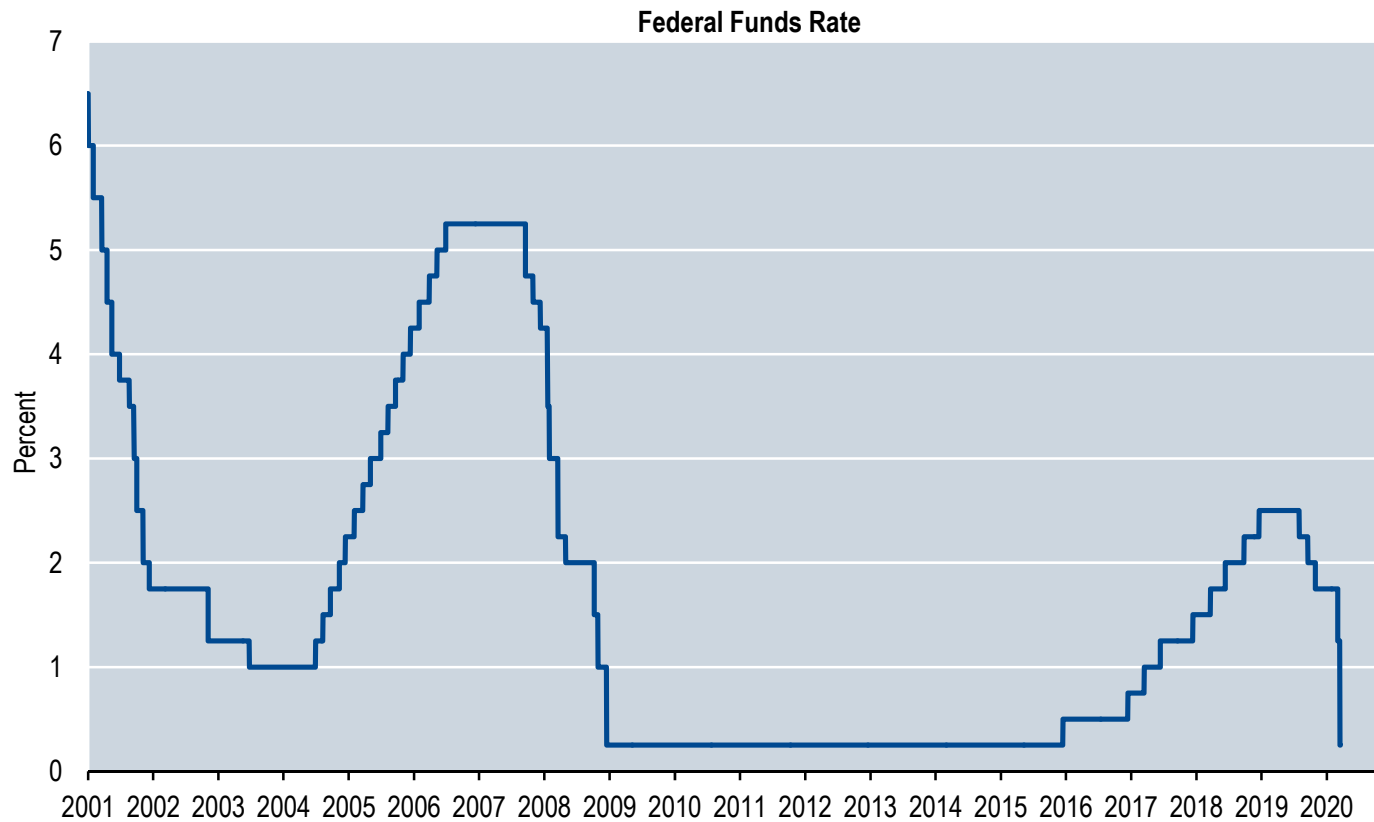


Source: UBS, Haver, European Commission, CBO. As of 31 Mar 20

Fed Cut Rates Extremely Fast, Will Raise Rates Extremely Slowly

“That’s actually one of the main things we’re trying to do by assuring the flow of credit in the economy and keeping rates low, **is to assure that that rebound, when it does come, is as vigorous as possible.**”

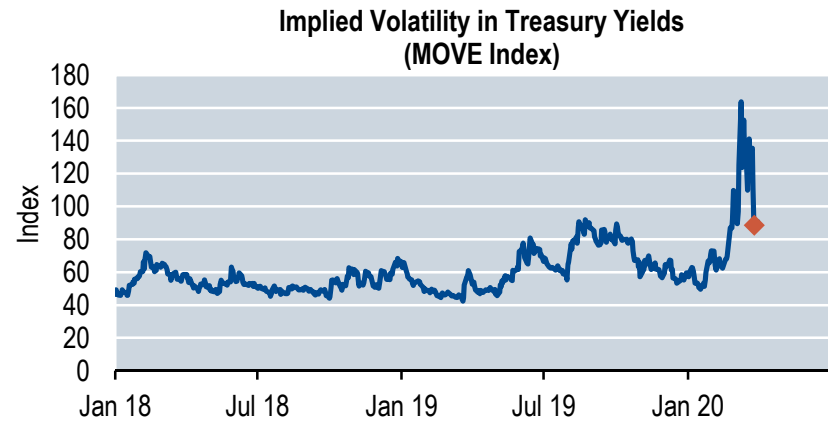
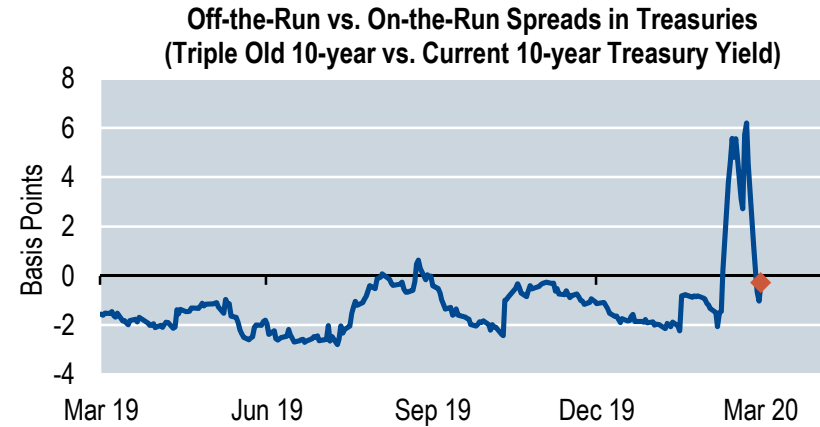
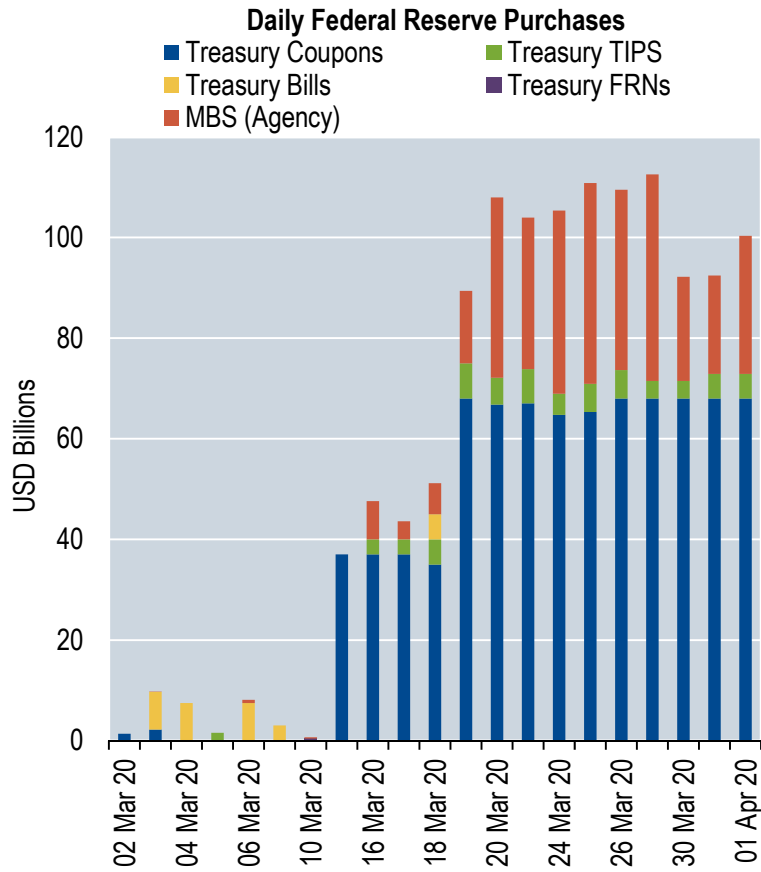
– Chair Powell, March 26, 2020 Appearance on *The Today Show*



Source: Federal Reserve, As of 31 Mar 20

Fed Is Providing Liquidity “As Needed”

Treasury Market Showing Signs of Stabilization



Source: Bloomberg, Federal Reserve. As of 31 Mar 20

Fed's Credit Facilities Will Be a Meaningful Intervention

“When it comes to this lending, **we're not going to run out of ammunition**. That doesn't happen.”

“The **main thing we're doing now is really with our lending programs**. That's the principle thing we're doing now to support the economy, is through that channel.”

- Chair Powell, March 26, 2020 Appearance on *The Today Show*

Federal Reserve Credit Lending Programs	
Programs	Primary Market Corporate Credit Facility (PMCCF), Secondary Market Corporate Credit Facility (SMCCF), Term Asset-Backed Securities Loan Facility (TALF), Money Market Mutual Fund Liquidity Facility (MMLF), Commercial Paper Funding Facility (CPFF), and a “Main Street Lending Program”
Structure	Special Purpose Vehicles: US Treasury in first loss position, Federal Reserve providing financing. Leverage is 10:1
Available Resources	Initial Capital from Exchanges Stabilization Fund: \$50 billion Additional Capital provided by CARES Act: \$450 billion Eventual Size: \$4+ trillion (assuming 10:1 leverage)

Source: Federal Reserve, As of 31 Mar 20

Fed Is Buying IG Corporate Credit for the First Time

Secondary Market Corporate Credit Facility (SMCCF)

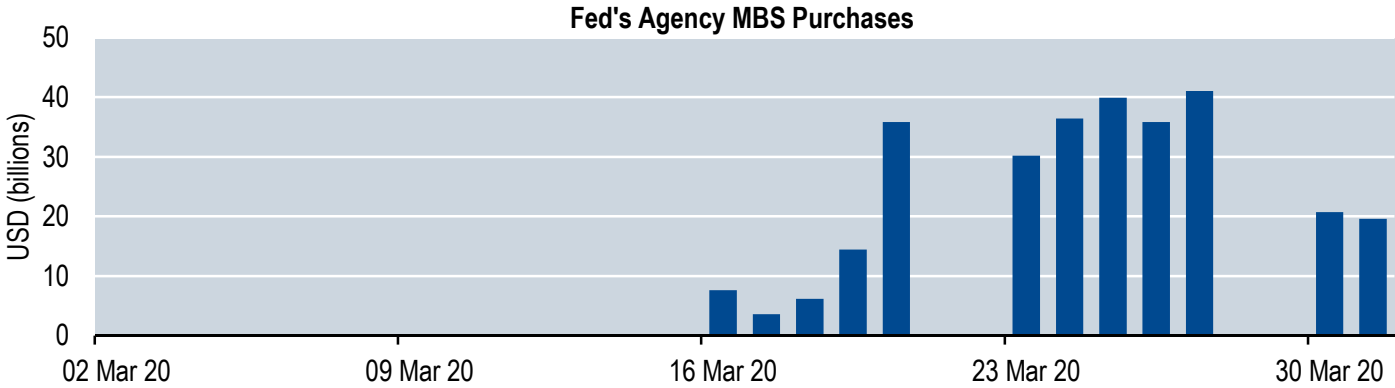
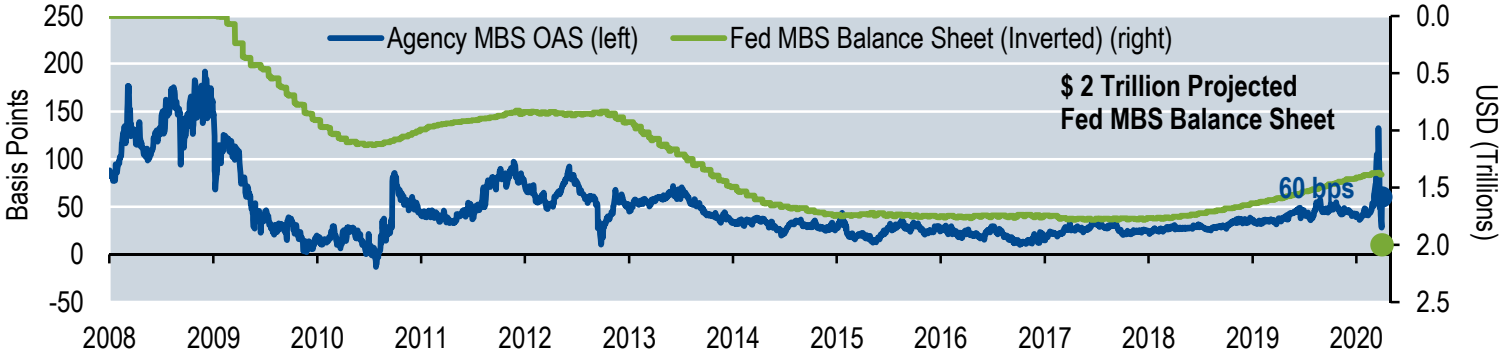
- Eligibility: BBB- and above, <5 years to maturity, max 10% per issuer
 - Eligibility likely to be expanded with additional resources from the CARES Act
- First time Fed has supported IG credit; first time Fed is supporting secondary market for credit
- Fed is an outright buyer (even as prices recover, Fed to keep buying)
- Likely to include bank debt
- Direct support for credit and financial conditions

Residential Mortgage Spreads

March 15 – Fed announced \$200 billion in buying in coming months

March 23 – Fed announced QE and has purchased more than \$343 billion

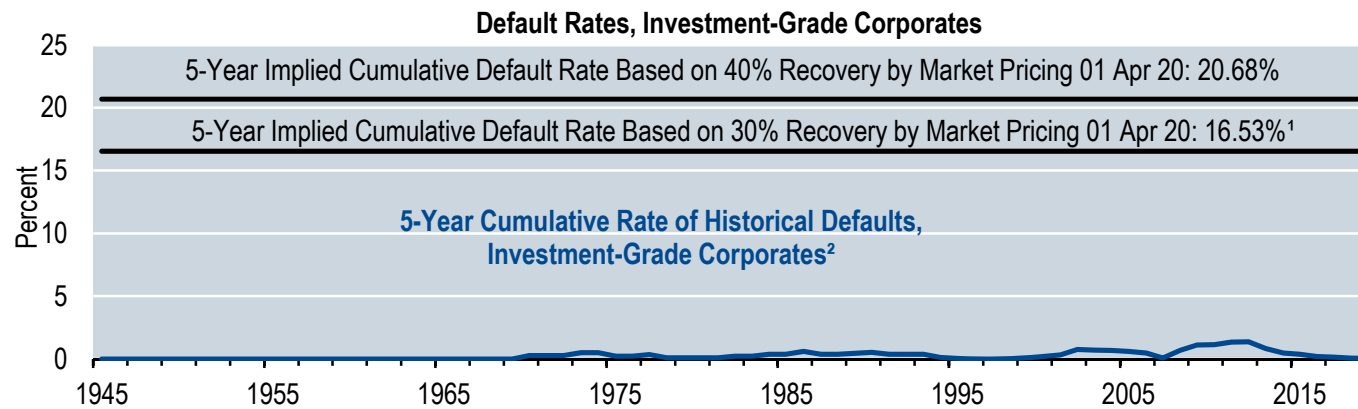
March 27 – CARES Act passed



Source: Bloomberg, J.P. Morgan. As of 31 Mar 20

Investment Themes – Corporate Bonds

Implied Default Rates



Source: Moody's, Bloomberg Barclays, Bloomberg. As of 01 Apr 20

¹Calculation assumes 25 bps liquidity premium

²As of 31 Dec 19

High Quality Companies Chose to Pay Decade High Spreads to Borrow in March 2020



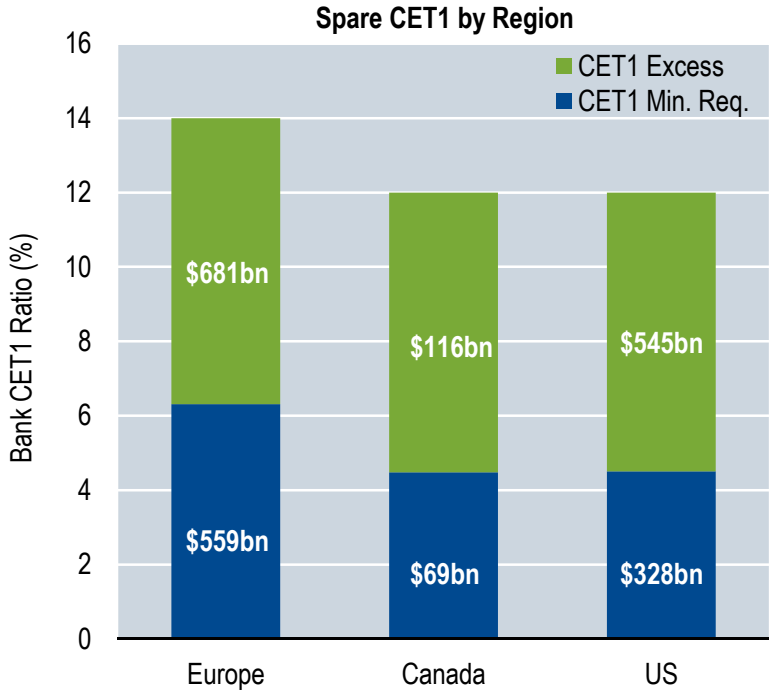
Banks in Sound Financial Shape

Banks are generally well capitalized

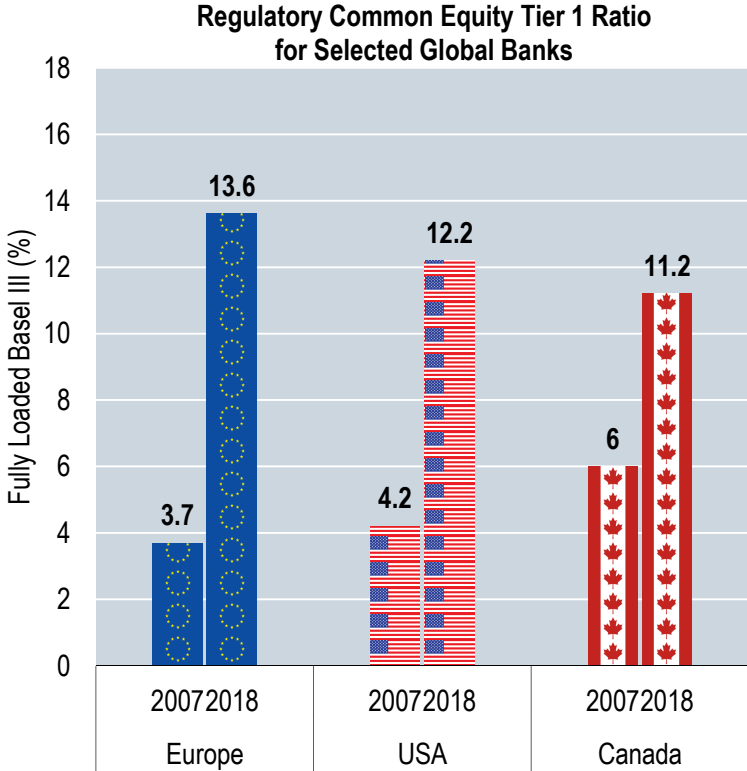
CET1 levels are more than double that of the minimum requirements

The introduction of more capital buffers has led to this build up of “excess” capital

The authorities have signalled that the buffers can be used



Source: BNP Paribas; Bank Annual Reports and Quarterly Updates 2019.
As of 19 Mar 20
Number of banks in sample: Europe 39, Canada 7, US 12



Source: BNP Paribas. As of 28 Feb 19

Investment-Grade Energy – Unprecedented Supply and Demand Shock

Since 2016, IG Managements Have

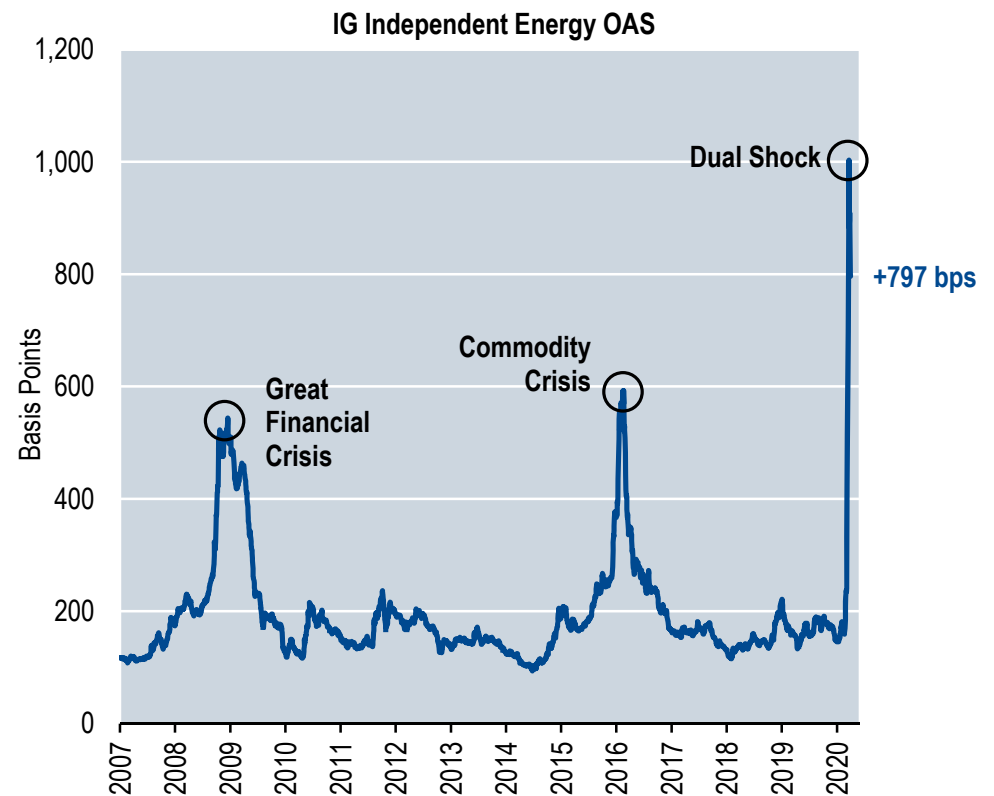
- Acted conservatively
- Lowered cost structures
- Improved cash flow
- Delevered balance sheets
- Extended maturity runways
- Improved liquidity
- Implemented hedges

Have Additional Levers

- Cut capital budgets
- Cut dividends

Conclusion:

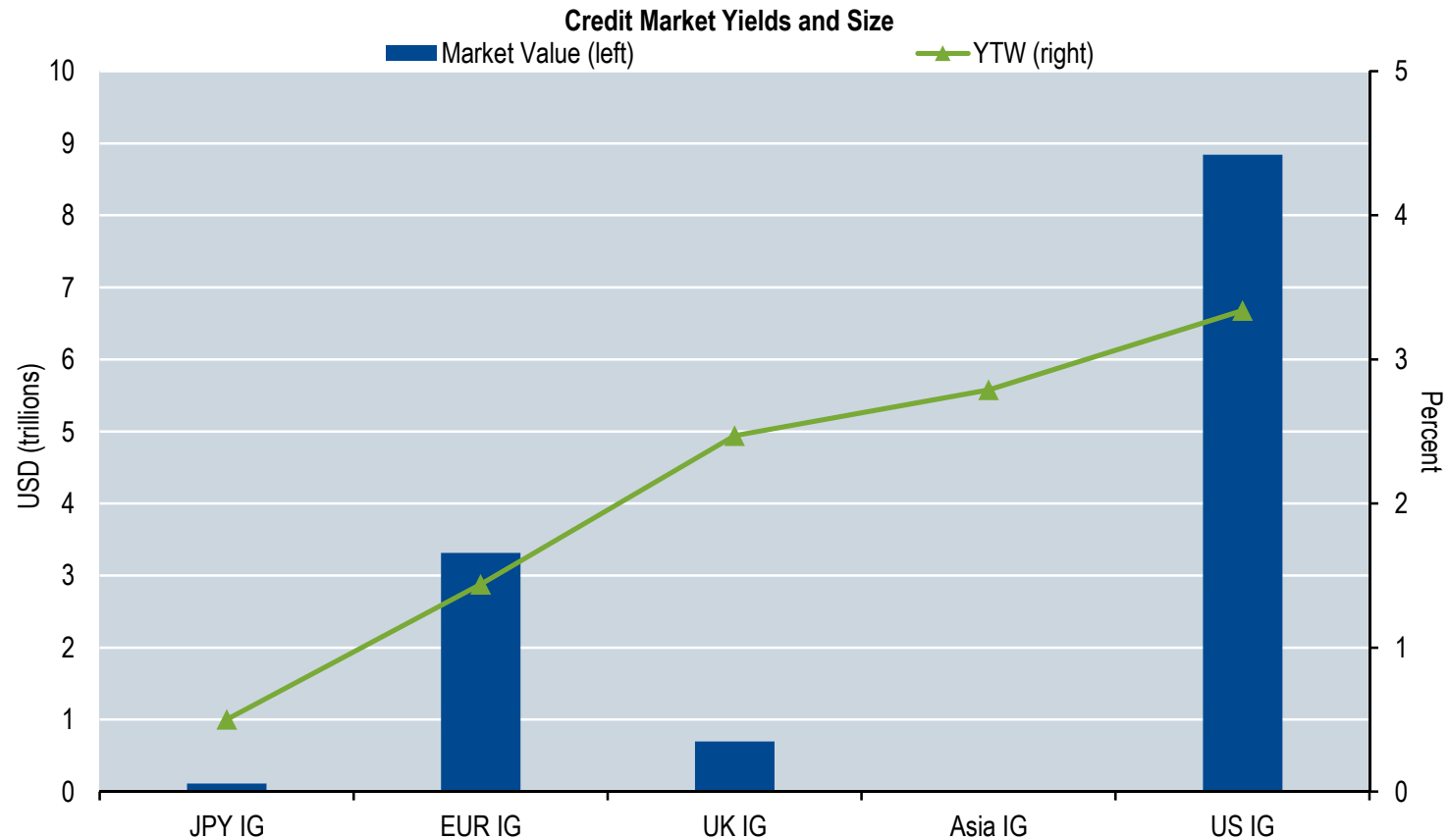
- Severe downward price action
- Valuations extreme
- Downgrades happening
- Capital preservation in focus



Source: Bloomberg Barclays. As of 31 Mar 20

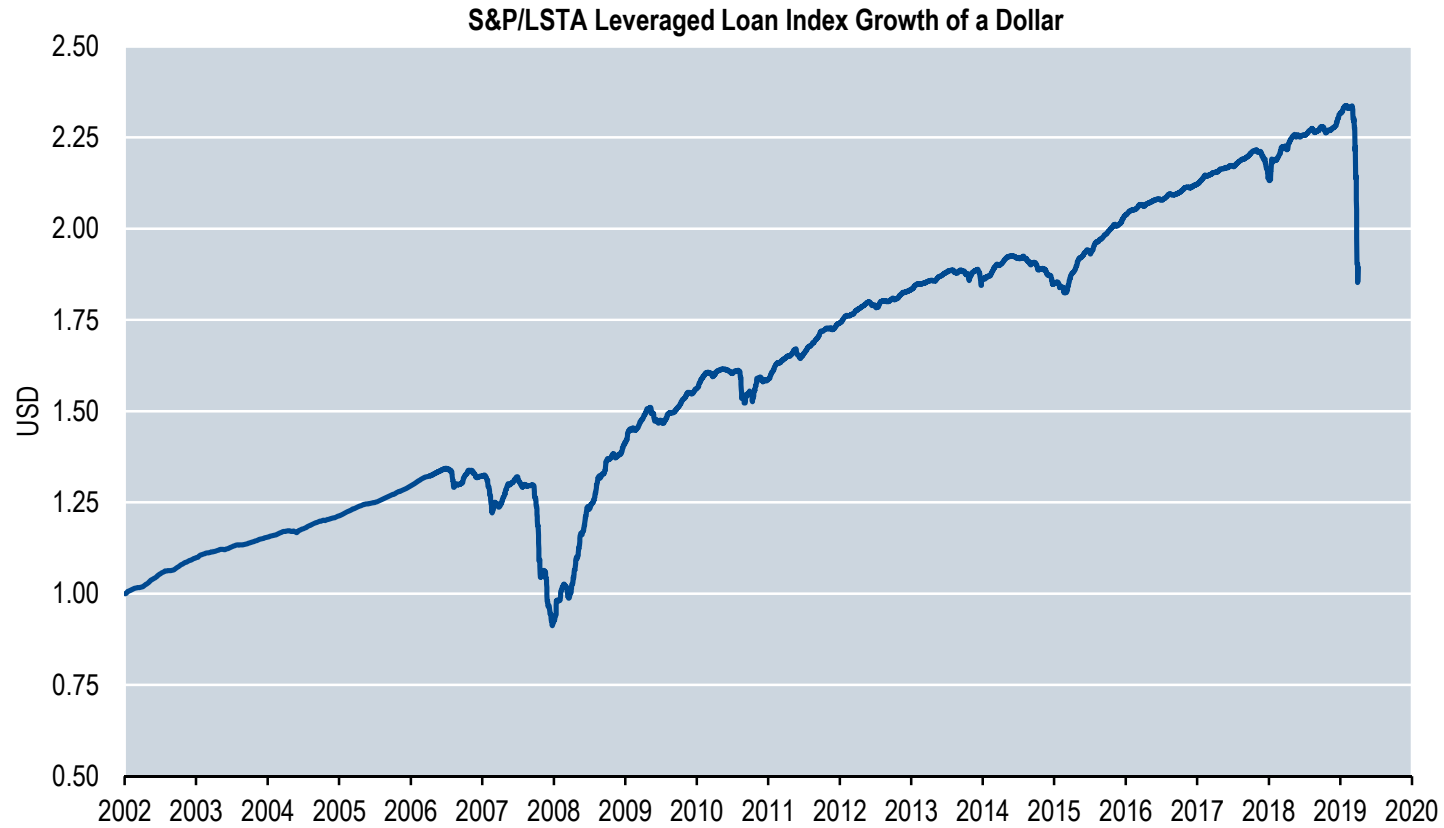
US Credit Markets Offer Both Attractive Yield and Size

Relative to other mature markets, US credit markets are attractive to a global investor.



Source: Bloomberg Barclays. As of 01 Apr 20
Bloomberg Barclays Global Credit Index by Currency

Long-Term Performance of Bank Loans



Sources: LCD, an offering of S&P Global Market Intelligence; S&P/LSTA Leveraged Loan Index as of 25 Mar 20

High Yield ... Another “Historic” Opportunity

Valuations look attractive on a historical basis.



Bloomberg Barclays U.S. High Yield Index OAS: +942 bps

Recovery Rate: 30%	Year 1	Year 2	Year 3	Year 4	Year 5
Annual Default Rate	12.6%	12.6%	12.6%	12.6%	12.6%
Cumulative Default Rate	12.6%	23.6%	33.2%	41.6%	49.0%

Recovery Rate: 40%	Year 1	Year 2	Year 3	Year 4	Year 5
Annual Default Rate	14.5%	14.5%	14.5%	14.5%	14.5%
Cumulative Default Rate	14.5%	27.0%	37.6%	46.6%	54.4%

Source: Bloomberg Barclays, Western Asset. As of 03 Apr 20

14 times when HY spread exceeded +900 at month end.
Annualized returns for HY when spreads exceeded +900 at month end.

	OAS (bps)	1 Year Later Annualized Return (%)	2 Years Later Annualized Return (%)
Jun 2009	945	26.77	21.07
May 2009	1,067	28.79	23.39
Apr 2009	1,219	42.58	27.17
Mar 2009	1,514	56.18	33.61
Feb 2009	1,544	56.24	35.51
Jan 2009	1,476	51.15	32.52
Dec 2008	1,662	58.21	34.96
Nov 2008	1,833	64.95	38.79
Oct 2008	1,479	48.10	32.95
Sep 2008	1,020	13.37	16.17
Oct 2002	1,014	32.95	22.58
Sep 2002	996	29.98	20.95
Aug 2002	918	24.86	19.22
Jul 2002	915	26.96	19.81
Average		40.08	27.05

Source: Bloomberg Barclays. As of 30 Jun 11

High-Yield Should Benefit from Stimulus Package

While the Fed's corporate market facilities target investment-grade companies, the mid-sized business loan program in the CARES Act should offer more assistance to the high-yield market¹

- 48% of high-yield issuers are eligible for the potential 2% loan under the CARES Act, versus 19% of investment-grade issuers²

Airlines

- \$25 billion in wage grants and \$25 billion in loans

Automotive TALF 2.0

- Enable efficient funding in the ABS market

Areas of focus in high-yield:

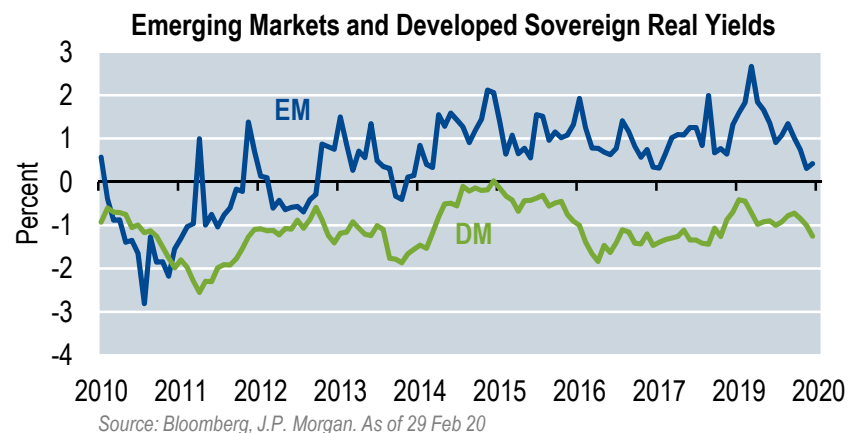
- **Industries that can endure** throughout a protracted downturn
 - Cable, wireless, healthcare, food & beverage, and other consumer non-cyclicals
- **Deeper value/higher return potential opportunities** in certain, more stressed sectors
 - Energy, airlines, metals & mining (with a focus on copper). **Individual issuer selection is crucial!**

¹Specific Industry support

²Source: Barclays, March 26th, Barclays Tuesday Credit Call)

Emerging Markets: Market Impact and Valuations

- EM is particularly growth-sensitive given existing balance sheet quality and external vulnerability
- Capacity for monetary policy and fiscal stimulus is more limited in EM
- Valuations displaced across all EM sectors
- Thinking of local rates as carry rather than total return, while EMFX will remain vulnerable to virus-related growth downside
- We find value in high quality EM hard currency bonds and displaced front-end paper



Great Value Medium-Term

	Rating	Yield to Worst (%)	Duration (yrs)
J.P. Morgan GBI EM Global Diversified	BBB	5.5	5.2
Bloomberg Barclays US Treasury	AAA	0.6	7.1
Bloomberg Barclays Euro Area Treasury	AA-	0.2	8.4
Bloomberg Barclays UK Treasury	AA	0.4	13.8
Bloomberg Barclays Japan Treasury	A+	0.0	9.8
Bloomberg Barclays US IG Credit	A	3.3	7.7

Source: Bloomberg Barclays, J.P. Morgan. As of 30 Mar 20

Outlook

2020

Coronavirus-related growth setbacks have meaningfully reduced global and US growth

The medical battle will take time and prolonged efforts; recent developments are encouraging

US and global inflation rates will be very subdued

Central banks will remain extraordinarily accommodative

Fiscal policy will continue to ramp up to provide relief efforts

Even after recovery begins, central banks will keep rates ultra low

Spread products ultimately should be primary beneficiaries of recovery

The timing and slope at eventual recovery remains the largest uncertainty

Questions & Answers



Thank you.

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期限日のお知らせ： 金融商品取引法(以下、「法」)の以下の規定による期限日は、いずれも毎年9月30日(休日の場合は、前営業日)とします。
法第34条の2により、特定投資家を特定投資家以外の顧客とみなす場合。法第34条の3により、特定投資家以外の顧客である法人を特定投資家とみなす場合。
法第34条の4により、特定投資家以外の顧客である個人を特定投資家とみなす場合。

個人情報の取り扱いについて： 当社はその業務に関連して、お客様及びお客様の役職員の個人情報を取得する場合があります。当社は取得した情報を、当社からのご連絡、セミナーのご案内などの営業活動に利用することがあります。

ウエスタン・アセット・マネジメント株式会社について： 業務の種類： 金融商品取引業者(投資運用業、投資助言・代理業、第二種金融商品取引業)
登録番号： 関東財務局長(金商)第427号 加入協会： 一般社団法人日本投資顧問業協会(会員番号 011-01319)、一般社団法人投資信託協会