Prashant Chandran, CFA
Portfolio Manager

Elliott R. Neumayer
Product Specialist

Webcast Summary

Macro Opportunities Strategy Update: Navigating Rate Cuts and Election Volatility

The global economy is experiencing disinflation and resilient growth, with central banks likely to ease monetary policy in the near term. Inflation continues to decline across developed and emerging market economies, though unevenly. Labor markets are moderating, with job creation slowing and wage pressures easing. Consumer spending remains resilient but shows signs of weakening. Real yields remain high, exerting downward pressure on economic growth. In the current economic environment, the Macro Opportunities strategy favors a long duration bias, especially in US Treasuries (USTs), while selectively maintaining positions in emerging markets and reducing exposure to investment-grade and high-yield credit due to tight valuations. Here are some key takeaways.

Global Outlook

- Global growth is expected to slow, particularly in the eurozone, with real yields remaining high and exerting downward pressure on economic activity.
- US economic growth is projected to moderate, with expectations for 2.0%-2.5% in 2025.
- The US dollar is expected to gradually weaken as the Federal Reserve (Fed) starts its rate-cutting cycle, providing a tailwind for emerging market (EM) currencies.
- EMs are seen as decoupling from China's economic influence, with countries like Mexico, Brazil, India and Indonesia benefiting from increased foreign investment.
- Corporate credit fundamentals remain strong, but valuations are tight with carry expected to drive returns in near term and risks for spreads to widen from current levels.

Inflation

- Globally, inflation is declining across advanced economies, though at different rates and unevenly across CPI baskets.
- US inflation is on a declining trend overall, though the core personal consumption expenditures (PCE) index saw a temporary jump in 1Q24 due to one-off factors like auto insurance and rents.
- The Fed expects inflation to continue moderating toward their target and is waiting for more data confirming declining inflation and jobs.
- The UK is seeing sticky inflation, particularly in services and wages, despite headline CPI nearing the 2% target.
- Japan is experiencing wage pressures that may prompt the Bank of Japan (BoJ) to further hike rates in the near term.
- China is experiencing mild deflation, which is helping to export disinflation to other large economies.

Central Bank Policy

- Central banks, including the European Central Bank and Bank of England (BoE), are anticipated to ease monetary policy the near term with the Fed expected to begin easing in September.
- The BoE is in a tricky situation with high services inflation, but is still expected to start cutting rates, potentially faster than market expectations.
- Real yields remain high, exerting downward pressure on economic growth. This is seen as a reason for central banks to start easing monetary policy later this year.
- The BoJ is an outlier, with wage pressures potentially prompting another 10-basis-point rate hike in the next couple of meetings.
- EM central banks had to pause their rate cutting cycles earlier this year due to inflation concerns, but are expected to resume easing once major central banks begin cutting rates.

Investment Themes

- The Macro Opportunities strategy is positioned to take advantage of global disinflation and prospects for central bank easing. As a result, the portfolio maintains a bias to be long duration and holds select EM currencies, which we believe will benefit in the current environment.
- The strategy provides concentrated exposure to Western Asset's key investment themes. The active trading approach of macro strategies can provide stability during periods of market stress. Historically, the strategy has had low correlation to equities and traditional fixed-income, making it appealing to investors looking for diversification.
- Regarding EM countries, while there could be some negative impacts from US election outcomes, we expect EM overall to hold up relatively well due to factors like foreign direct investment flows.
- To hedge against potential risks, the portfolio maintains long-duration positions, particularly in USTs, as well as short positions in currencies like the euro, British pound and Chinese renminbi.
- We're reducing exposure to both investment-grade and high-yield credit in the strategy through selective trimming of certain names and CDX positions, in an effort to rebalance risk and capitalize on recent market movements, while maintaining significant positions in other areas like EM and tactical positions in agency MBS.
- The strategy's current yield may provide a cushion against adverse scenarios.

Audience Q&A

- Regarding the US election, both Trump and Harris presidencies would likely maintain high budget deficits but differ in their approach to taxes and spending. Trump may renew tax cuts while Harris could increase infrastructure spending.
- A Trump presidency might impose higher tariffs on Chinese imports, potentially keeping inflation higher for longer, but the overall impact on the US economy and inflation may be limited.
- EM countries are expected to demonstrate greater resilience to the US election outcome compared to previous cycles, largely due to their reduced dependence on China. While a Trump presidency could pose challenges for some nations like Mexico, the overall outlook for EM economies remains relatively stable regardless of the election result.

Past performance does not predict future returns. These materials should not be deemed to be a prediction or projection of future performance.

These materials are intended for investment professionals including professional clients, eligible counterparties, and qualified investors only.

These materials have been produced for illustrative and informational purposes only. These materials contain Western Asset's opinions and beliefs as of the date designated on the materials; these views are subject to change and may not reflect real-time market developments and investment views.

Third party data may be used throughout the materials, and this data is believed to be accurate to the best of Western Asset's knowledge at the time of publication, but cannot be guaranteed. These materials may also contain strategy or product awards or rankings from independent third parties or industry publications which are based on unbiased quantitative and/or qualitative information determined independently by each third party or publication. In some cases, Western Asset may subscribe to these third party's standard industry services or publications. These standard subscriptions and services are available to all asset managers and do not influence rankings or awards in any way.

Investment strategies or products discussed herein may involve a high degree of risk, including the loss of some or all capital. Investments in any products or strategies described in these materials may be volatile, and investors should have the financial ability and willingness to accept such risks.

Unless otherwise noted, investment performance contained in these materials is reflective of a strategy composite. All other strategy data and information included in these materials reflects a representative portfolio which is an account in the composite that Western Asset believes most closely reflects the current portfolio management style of the strategy. Performance is not a consideration in the selection of the representative portfolio. The characteristics of the representative portfolio shown may differ from other accounts in the composite. Information regarding the representative portfolio and the other accounts in the composite are available upon request.

Statements in these materials should not be considered investment advice. References, either general or specific, to securities and/or issuers in the materials are for illustrative purposes only and are not intended to be, and should not be interpreted as, recommendation to purchase or sell such securities. Employees and/or clients of Western Asset may have a position in the securities or issuers mentioned.

These materials are not intended to provide, and should not be relied on for, accounting, legal, tax, investment or other advice. The recipient should consult its own counsel, accountant, investment, tax, and any other advisers for this advice, including economic risks and merits, related to making an investment with Western Asset. The recipient is responsible for observing the applicable laws and regulations of their country of residence.

Founded in 1971, Western Asset Management Company is a global fixed-income investment manager with offices in Pasadena, New York, London, Singapore, Tokyo, Melbourne, São Paulo, Hong Kong, and Zürich. Western Asset is a wholly owned subsidiary of Franklin Resources, Inc. but operates autonomously. Western Asset is comprised of six legal entities across the globe, each with distinct regional registrations: Western Asset Management Company, LLC, a registered Investment Adviser with the Securities and Exchange Commission; Western Asset Management Company Distribuidora de Títulos e Valores Mobiliários Limitada is authorized and regulated by Comissão de Valores Mobiliários and Brazilian Central Bank; Western Asset Management Company Pty Ltd ABN 41 117 767 923 is the holder of the Australian Financial Services License 303160; Western Asset Management Company Pte. Ltd. Co. Reg. No. 200007692R is a holder of a Capital Markets Services License for fund management and regulated by the Monetary Authority of Singapore; Western Asset Management Company Ltd, a registered Financial Instruments Business Operator and regulated by the Financial Services Agency of Japan; and Western Asset Management Company Limited is authorised and regulated by the Financial Conduct Authority ("FCA") (FRN 145930). This communication is intended for distribution to Professional Clients only if deemed to be a financial promotion in the UK as defined by the FCA. This communication may also be intended for certain EEA countries where Western Asset has been granted permission to do so. For the current list of the approved EEA countries please contact Western Asset at +44 (0)20 7422 3000.