

# Western Asset Global Multi Sector Fund

## Key Points

- The Western Asset Global Multi Sector Fund posted a return of 7.66%<sup>1</sup> in sterling terms over May. It outperformed its composite benchmark<sup>2</sup>, which returned 4.29% over the month.
- The investment grade corporate sector in Europe and the US had another exceptional month. Financial issues led the rally, with subordinated debt having a very strong month.
- Despite the recent strong performance, the manager believes most non-government sectors still have ample room for improvement and are likely to outperform government bonds over the remainder of 2009 and possibly beyond.
- The manager has eliminated its long-standing overweight exposure to agency mortgage-backed securities, as the attractiveness of the asset class relative to other sectors has faded, and instead shifted exposure into investment grade corporate bonds.

## Market Review

Non-government bonds continued to perform well over May, while government bonds generally recorded negative returns. The investment grade corporate sector in Europe and the US had another exceptional month, after the record performance seen in April. Financial issues led the rally, with subordinated debt having a very strong month. Similarly, high yield corporate bonds recorded a significant outperformance over government issues. Within government bonds, conventional issues struggled, while inflation-linked bonds performed well, as investors shifted their expectations from deflation to inflation.

Monetary policy continued to focus on reinvigorating private lending and stimulating economic activity, rather than on possible pipeline inflationary pressures. The European Central Bank reduced rates by another 25 basis points and announced plans to join the other major central banks in purchasing longer-maturity assets in an effort to ensure that the eurozone economy has enough credit to support a healthy level of activity. The US Federal Reserve (Fed) continued to purchase Treasuries and agency mortgage-backed securities, while the Bank of England expanded the size of its asset purchase plan. The outlook for the major developed economies continued to improve, with signs of a recovery or at least a stabilisation appearing in economic data.

The improving economic outlook and reduced concerns over the recapitalisation needs of financial institutions continued to boost investor confidence over the month. The results of the US bank stress tests led to significant capital raises, and strains in the interbank lending market eased. Most encouragingly, private sector lending to corporate issuers increased across the maturity and ratings spectrum. Despite the large increase in new issuance, spreads over government bonds narrowed significantly in global corporate bond markets.

## Outlook

The manager notes that stabilising economic activity and improving lending activity are now encouraging one another. However, it considers the current recovery fragile and believes central bankers should remain vigilant of further slippage. Although it continues to see forceful headwinds for consumer spending, the manager is confident that economic activity should continue to stabilise and resume positive growth in the near term, even if at a subdued pace. Indeed, the manager believes that the inventory liquidation cycle, which has been the primary detractor from economic growth, is nearing its completion.

The manager has been pleasantly surprised by the strength of the recovery in non-government bond markets over the past two and a half months. It had expected pricing to converge towards fundamental values at a slower pace and is pleased to see market prices rising towards what it had long felt are more accurate valuations. Despite the recent strong performance, the manager believes most non-government sectors still have ample room for improvement and are likely to outperform government bonds over the remainder of 2009 and possibly beyond. Investors fled for the safety of prime money market funds during the crisis. However, with money market investments now generating meagre returns and risk appetite returning, cash is slowly being redeployed in the credit market, helping to support valuations.

Within the non-government sectors, the manager has eliminated its long-standing overweight exposure to agency mortgage-backed securities, taking profits following strong performance. Despite support for the sector from the ongoing purchase programme by the Fed, the manager felt the attractiveness of the asset class relative to other sectors has faded. The manager has instead shifted exposure into investment grade corporate bonds. The manager believes that valuations in both investment grade and high yield

<sup>1</sup> Institutional GBP Hedged Accumulation Shares.

<sup>2</sup> Composite Benchmark: 50% Barclays Capital Global Aggregate Index, 25% Barclays Capital U.S. Corporate High Yield - 2% Issuer Capped Index, 25% JP Morgan EMBI+ Index, Sterling Hedged.

**Source for performance figures** – Legg Mason. Performance is calculated on a NAV to NAV basis. Performance calculations include reinvested dividends, without deduction of withholding tax, and the deduction of the Total Expense Ratio over the calculated period. Sales charges, taxes and other locally applied costs to be paid by an investor have not been deducted.

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corporate debt overstate default risks and therefore offer good value, especially in the financial subsector and non-cyclical industries, including healthcare, telecommunications and utilities.

**This Fund is managed by Western Asset Management.**

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June 2009

Ref: 4661