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WESTERN ASSET UPBEAT ON ASIAN BOND MARKET AS GLOBAL ECONOMIC RECOVERY CONTINUES

- Asian economies to grow at a faster pace due to the combination of domestic and global stimulative policies, and recovery in the US and Europe
- Regional currencies to appreciate faster as Chinese yuan gradually appreciates
- Asian high-yield corporate bonds to perform well in 2010

Singapore – 26 January 2010 – Asian economies should grow at a faster pace in 2010 due to the ongoing impacts of domestic and global macroeconomic policies, and recovery in the US and Europe, says global fixed income manager Western Asset. As policy-makers gain confidence that exports will recover, governments in the region will be less averse to their currencies appreciating to reflect the renewed inflows of foreign capital. Portfolio flows as well as foreign direct investment should continue to increase, as will inflation in the region. Across Asia, there are signs that food prices are climbing again. Rising property prices are also having an impact.

Policy debate has shifted from concern about the sustainability of the recovery to sequencing the exit of various crisis policies.

“While we believe that there is still sufficient economic slack to allow growth to continue at current rates without aggressive tightening of policies, the risk is tilting toward at least a move away from heavily stimulative measures,” said Rajeev De Mello, Head of Asian Investment.

The first series of measures has been administrative measures to contain the rise in housing prices. A combination of reserve requirement tightening, gradual currency appreciation, more aggressive sterilization of currency intervention and policy rate hikes are expected in selected countries this quarter. India and Korea are likely to be the first Asian countries to join the Reserve Bank of Australia, the Bank of Israel and Norges Bank in the global monetary tightening cycle. Other countries may follow in the second quarter.

Most Asian yield curves have already steepened substantially. The financing of government spending programs has led to an increase in expected government bond issuance. Pricing the normalization of monetary policy has also contributed to steepening in the front end of the yield curve. There has also been an increase in the risk premium on longer bonds due to uncertainties about future macroeconomic policies.

“Our strategy is to take advantage of any excessive upward moves in the yield curves to buy back bonds. We continue to like Indonesian bonds as we believe that they already offer a substantial cushion to changes in monetary policy in an environment where inflation has remained remarkably subdued,” said De Mello.

Western Asset expects Asian currencies to benefit from further economic normalization and a change in China's currency policy. For these reasons, it is maintaining an overweight exposure to Asian currencies, particularly the Chinese yuan, Indian rupee, Korean won, Indonesian rupiah and Malaysian ringgit, over the next few months.

"We believe that Chinese policy-makers will wait a few more months before allowing the RMB to strengthen at a gradual pace. Once the Chinese yuan starts appreciating, we should see a faster pace in regional currency appreciation," De Mello added.

The global fixed income manager also continues to favor Asian corporate bonds. Issuance is already picking up as corporates take advantage of low absolute yields but there remains an attractive premium in certain sectors of the credit market. The strong recovery in Asia will be very positive for Asian companies, especially those that depend on the regional and domestic economies. De Mello expects the Asian high-yield corporate bond market to perform well in 2010 but returns this year will likely be lower than last year as most bonds are no longer at distressed prices.

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Note to Editors

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