

For Immediate Release

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**Western Asset: Korea, Indonesia and Malaysia Most Likely to Suffer
Biggest Repatriation of Foreign Capital Due to Euro Zone Trouble**

Singapore – 8 June 2010 – The deterioration in investment sentiment as a result of troubles in Europe could trigger a repatriation of foreign capital back to investors' home countries, which would adversely impact Asian assets held by foreign investors, according to Legg Mason-owned Western Asset. Despite the European crisis, the ongoing global economic recovery will not be derailed and should continue to benefit Asian bond and corporate markets. Once China decides to allow its currency to appreciate, other Asian currencies will appreciate at a faster pace.

Western Asset believes that Korea, Indonesia and Malaysia are most likely to be impacted because they have been the favourite markets for global investors. Western Asset also believes that Asian markets will be affected by the European crisis through several channels, such as a reduction in the financing activities of European and U.S. banks.

"Interbank rates in US dollars have been increasing since the beginning of the European crisis, and that could continue to adversely impact Asian credit markets," said Rajeev De Mello, Head of Asian Investment at Western Asset.

On the other hand, the deflationary impact of European fiscal tightening could have a positive impact. If European growth recovers at a slower pace due to the crisis, Europe would not contribute to an increase in global inflation and might even help commodity prices stabilize. The initial reaction by commodity markets has been to move lower on fear of weaker demand.

"Since Asia is particularly sensitive to higher inflation, especially imported inflation, this would be positive for most Asian bond markets," said De Mello.

He said that lower inflation could give Asian central banks more leeway in their path toward policy tightening. India and Malaysia have already embarked on the normalization of their policy rates, while other countries are waiting for further confirmation of economic recovery in the U.S., Europe and Japan.

"We continue to believe that China will view the next few weeks as the ideal window to return to its pre-2008 policy of allowing its currency to appreciate at a gradual pace." said De Mello. "Further delays could shift the currency debate to the U.S. Congress, which may want to show its involvement ahead of the mid-term elections in November."

On investment strategy, Western Asset's overall strategy is to favour the longer end of the bond markets as it anticipates government finances to be better-than-expected due to the recovery in

growth. The firm also believes that longer maturity bonds would benefit from policy tightening designed to moderate inflation.

Western Asset says it will continue to underweight on duration in most developed Asian countries and China. The firm is overweight on bonds in India and Malaysia and will look to increase duration in Indonesia if yields rise. It favours Asian credit and has maintained its overweight position to Asian investment-grade and high-yield corporate issuers.

Over the medium term, Asian assets should continue to outperform Europe, Japan and the US assets as the economic fundamentals in the regional are far stronger.

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Notes to Editors

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Western Asset is one of the world's leading fixed income managers with over US\$482.2 billion (December 31, 2009) under management. With offices in the United States, London, Tokyo, Singapore, Hong Kong, Melbourne and Sao Paulo, the company offers clients a full range of local and cross-border fixed income products. By devoting all of its resources to fixed income, Western Asset can provide a full commitment to clients in every area. This focused approach has generated positive long-term returns in a variety of products with varying risk disciplines. Western Asset's long performance track record and global presence has positioned the company to continue its commitment to excellence in fixed income investment management and client service.

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¹ *Legg Mason is the 10th largest asset manager in the world based on worldwide assets under management as of 31 December 2008. Source: Pensions & Investments May 2009 ranking.*

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