

The view from Legg Mason

Legg Mason's investment managers on the outlook for global markets following the recent S&P downgrade in the US.

Standard & Poor's decision to downgrade the credit rating of US long term debt from AAA to AA+ was not unexpected by market-watchers. However, the timing came as a surprise to many, and the decision set off a chain reaction in the markets, including a sell-off in equities.

For insights from Legg Mason investment managers on the impact of the debt downgrade and ongoing market volatility, see the summaries below:

Western Asset Management: Despite the downgrade of the US from AAA to AA+ by Standard & Poors, Western Asset still views US Treasuries as one of the safest and most liquid assets in the world. It believes the fragility in markets and investor sentiment stems more from pessimism about growth in the developed world and concerns with peripheral EU countries than from the downgrade of the US.

ClearBridge Advisors: ClearBridge has been pessimistic about the prospects for material sustained recovery in the US economy for a while. However, it is more sanguine in its views about good companies with sound balance sheets, good business models, and the ability to pay a stream of dividends. Looking ahead, ClearBridge will continue to assess its positions as markets react sporadically to news, but it won't be doing mass movements during emotional upheavals.

Legg Mason Capital Management: LMCM believes the downgrading by Standard & Poors of the credit rating for the US was precipitous, wrong and dangerous. LMCM believes the reasoning was poor, and consequences both short and long term for the global financial system are completely unpredictable. In LMCM's opinion, the US's status as the dominant global economy, sponsor of the world's reserve currency and the world's only military superpower in the world render it sui generis economically. That alone should be worth a rating at least one notch higher than anyone else, it argues.

Royce & Associates: Royce thinks investors are understandably anxious about the US

government's inability to compromise and the effect that this has had on the US credit rating. However, it adds that they're also nervous about a host of other economic issues both in the US and abroad, such as global debt, unemployment, and the rate of growth in developed economies and housing. Royce is using the declines as an opportunity to refresh its portfolios. The indiscriminate selling, it observes, is allowing it to re-enter some of the highest quality names at absolute valuations that it feels very comfortable with.

Batterymarch: The market action last week led to comparisons with the economic situation in 2007 and 2008. While the symptoms may look the same, the manager believes the causes of the recent market sell-off were very different. Batterymarch believes that the market plunge on Monday the 8th of August was not a liquidity driven event that caused forced selling; instead it believes it was a re-pricing of forward growth – a far healthier and more normal reaction than we experienced in 2007 and 2008.

Brandywine: Following the downgrade announcement, the manager observes that prices for risky assets around the globe declined precipitously while US Treasury prices, somewhat ironically, rallied sharply. Brandywine expects Treasuries will continue to trade around current levels in the medium term based on supportive macroeconomic fundamentals, including a high and rising savings rate, low core consumer price inflation, and strong demand for fixed income securities from both the household and banking sector. Elsewhere, thanks to its widespread use as a funding currency for long exposure to global risk assets, Brandywine observes that the US dollar has also benefitted from the recent period of risk aversion.

Batterymarch • Brandywine Global • ClearBridge Advisors • Esemplia • Global Currents • Legg Mason Capital Management • Permal • Royce & Associates • Western Asset Management

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