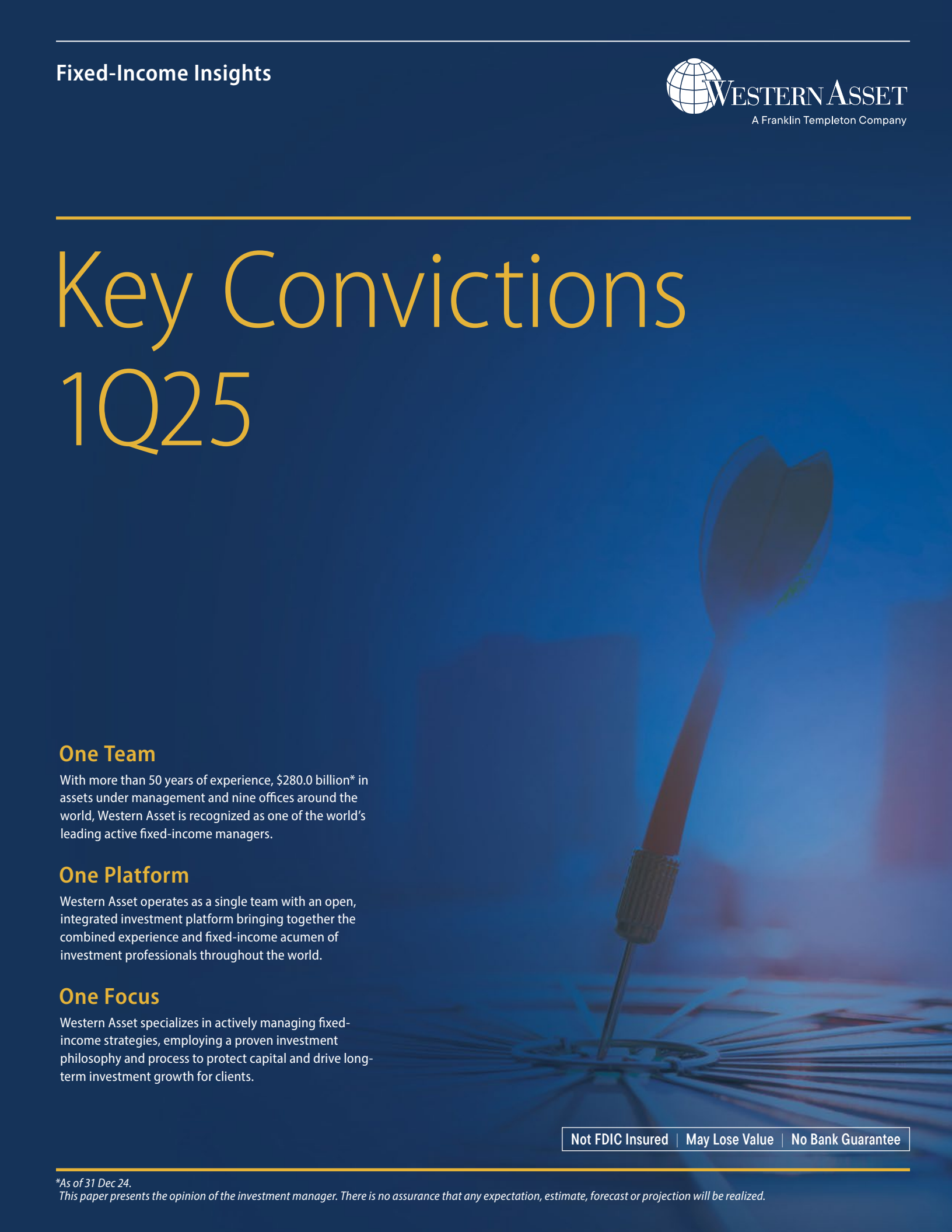
Fixed-Income Insights

WESTERN ASSET
A Franklin Templeton Company

Key Convictions 1Q25



One Team

With more than 50 years of experience, $280.0 billion* in assets under management and nine offices around the world, Western Asset is recognized as one of the world's leading active fixed-income managers.

One Platform

Western Asset operates as a single team with an open, integrated investment platform bringing together the combined experience and fixed-income acumen of investment professionals throughout the world.

One Focus

Western Asset specializes in actively managing fixed-income strategies, employing a proven investment philosophy and process to protect capital and drive long-term investment growth for clients.

Not FDIC Insured | May Lose Value | No Bank Guarantee

*As of 31 Dec 24.

This paper presents the opinion of the investment manager. There is no assurance that any expectation, estimate, forecast or projection will be realized.

Market Insights at a Glance

We anticipate a favorable environment for fixed-income investments in 2025 driven by strong global growth, overall progress on inflation and select opportunities arising from market volatility. While the US is likely to continue outpacing other developed market (DM) economies, we anticipate a narrowing growth gap and selective opportunities across various credit markets.

This summary is intended to aggregate the Firm's current overall views and present an at-a-glance dashboard.*



Growth

Convictions

- We expect global growth to remain positive but slow down somewhat from recent levels.
- The US should continue to outpace other DM economies, though the gap will likely narrow.
- The eurozone and China will face ongoing struggles, though the former may see some improvement as monetary policy easing drives investment activity.

Rationale

The US consumer remains resilient, manufacturing in the eurozone is weak and China continues to struggle with inadequate policy responses to its economic challenges.

Inflation

Convictions

- We expect global inflation to continue its downward trend, nearing central banks' 2% target.
- The US will continue to face more stubborn inflation compared to other DM economies. Historically, the US has experienced stickier inflation when the rate has approached 2%.
- We anticipate services inflation to grind lower, contributing to the overall decline in headline inflation.

Rationale

Central banks have made significant progress in reducing inflation. Service inflation remains tenacious but is expected to continue to moderate.

Rates

Convictions

- We anticipate shorter-term rates will likely decline, providing a more stable source of duration, as they tend to align with potential central bank rate cuts.
- Yield curves are likely to steepen, not just in the US but globally, due to ongoing fiscal concerns.
- We are monitoring opportunities in DM rates and remain overweight duration, particularly in the eurozone, the UK and Australia.

Rationale

Fiscal concerns and strong fundamentals in spread sectors influence rate movements. The front end of the US yield curve and certain other DM countries may present attractive opportunities for investors.

Monetary Policy

Convictions

- We expect central banks to have room to cut rates further, though the magnitude and timing will vary globally.
- The Federal Reserve's (Fed) goal of achieving 2% inflation in the US remains challenging due to inconsistent progress and the stickiness of services inflation.
- The European Central Bank (ECB) has cut its deposit rate by 100 basis points since last summer, but policy rates are still high relative to historical averages.

Rationale

Central banks have made significant progress on inflation, but the US faces more challenges in reaching its target. The ECB has loosened policy, but rates remain elevated compared to historical norms.

Credit Markets

Convictions

- We believe that corporate credit fundamentals are strong, given encouraging free cash flow generation and balance sheet health.
- Despite tight spreads, we believe there are still opportunities in specific sectors such as financials and European utilities.
- We expect pockets of volatility to provide opportunities to add to credit positions at more attractive valuations.

Rationale

Strong corporate credit fundamentals and selective opportunities in specific sectors, combined with anticipated market volatility, create a favorable environment for credit market investments.

Geopolitics

Convictions

- Trump's trade policies, particularly tariffs, are likely to cause temporary market disruptions.
- Other geopolitical factors include Trump's border and immigration policies, protectionist rhetoric and aggressive international negotiating tactics.

Rationale

The new administration's approach to tariffs and other geopolitical issues will introduce volatility into the markets, impacting both rates and spreads.

Embracing Volatility

"We think 2025 is going to be an interesting year … a good year for fixed-income. We're going to see some periods of volatility—but we're actually excited about being ready to take advantage of those."

— **Michael Buchanan, CFA,** Chief Investment Officer



*As of 31 Dec 24.

Trump, Tariffs and Protectionist Policies

As featured in our new Macro Market Trends publication, the kickoff of Trump's second term is almost certain to cause bouts of market volatility, as he made tariff threats a central part of his campaign. The proposed tariffs, particularly targeting China, the eurozone and Mexico, are expected to have significant global economic implications. While the exact timing and severity of any actual tariffs remain uncertain, the shift toward protectionism is clear. The potential tariffs could lead to higher inflation while dampening economic activity for key trading partners. The broader impact likely includes weaker global growth and potential retaliatory measures from affected countries. Latin America, particularly Mexico, could face economic pressures from a stronger dollar and lower oil prices. Japan and the eurozone may experience modest disinflation and weaker growth due to reduced exports. Asian economies, especially China, may mitigate impacts through fiscal and monetary measures. Australia, with its strong trade ties to China, could see softer economic growth and inflation.

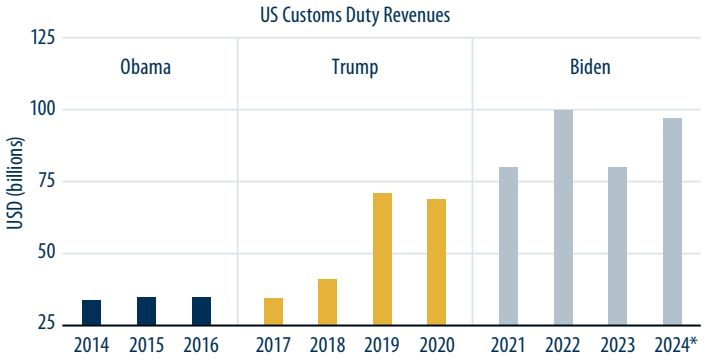
Even before Trump 2.0, US trade policy had become increasingly protectionist.

- The executive branch can independently drive trade policy, unlike fiscal policy, which requires legislative approval.
- Trump's approach is blunt compared with Biden's sector-specific tariffs.

The 10% tariffs Trump proposed risk a broader disruption to trade and markets.

- Exchange rates, prices paid by consumers and exporter margins would likely absorb the brunt of across-the-board tariff increases.
- Larger tariffs applied to China could divert some production to other countries, risking scrutiny on re-imports.
- We expect US trading partners to respond with reciprocal tariffs, which could increase geopolitical tensions.

Exhibit 1: US Policy and Trade Implications



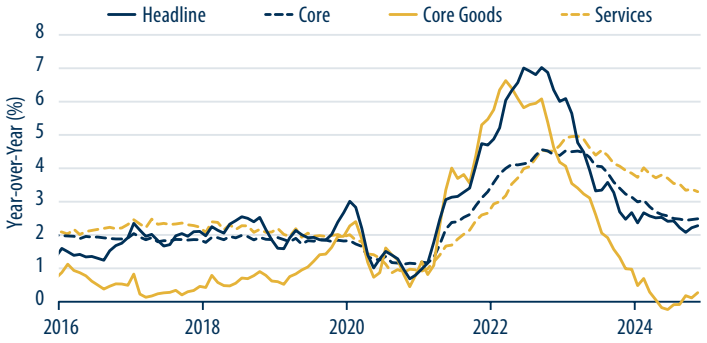
*Source: Statista. *Forecast. As of 30 Nov 24.*

Optimism Amid Volatility

Western Asset expects 2025 to be a good year for fixed-income investments, primarily supported by the following views:

- **Primary Driver of Returns:** Income and yields will be the main contributors to returns, rather than dramatic rate moves. Yields are currently at attractive levels, and the US yield curve has normalized (disinverted) to an upward slope.
- **Economic Expectations:** We expect global growth to remain positive but to slow from current levels. The US is expected to outperform other DM economies, although the gap may narrow.
- **Anticipated Volatility:** We expect a spike in volatility episodes over 2025, primarily due to the incoming Trump administration's posturing related to trade and tariffs. But only time will tell if the rhetoric matches the results. Regardless, volatility this year should create investment opportunities that reinforce the value of working with an active investment manager.
- **Inflation:** The fight against inflation should continue to make good progress, though it will be inconsistent across regions. While trending lower, inflation in the US—especially compared to other DM countries—remains sticky, particularly within the services sector.

Exhibit 2: Global Disinflation Is Broad-Based and Ongoing



*Source: Citigroup, Haver Analytics. *Headline and core inflation cover 15 economies; goods and services cover 12 economies. As of 30 Nov 24.*

Western Asset Investment Themes

Asset Class	Our View
Overall Spread Sectors	We expect spread sectors to face periods of volatility due to geopolitical and economic uncertainties, including the new Trump administration policies and ongoing fiscal concerns. However, strong fundamentals and technicals in sectors like corporate credit and structured products provide opportunities for selective investment, with a focus on maintaining flexibility to capitalize on market dislocations.
Investment-Grade Credit	We are focusing on sectors with strong fundamentals and attractive relative value, such as financials, while being mindful of the tight spreads and positioning portfolios to take advantage of any market dislocations that may arise.
High-Yield Credit	We are maintaining exposure to sectors with good fundamentals and strong technicals, while being prepared to opportunistically add to positions during periods of market volatility, leveraging our sector teams' insights to identify attractive opportunities.
Structured Product	We see attractive opportunities in commercial mortgage-backed securities (CMBS) and collateralized loan obligations (CLOs), where spreads remain wider compared to investment-grade corporate bonds. Fundamentals remain strong, supported by high-quality new issuance and manageable supply.
EM Debt	With nominal rates at decade highs and real yields averaging close to 4%, we see attractive local market rate opportunities in select countries like Mexico.
Geopolitical and Economic Risks	Key risks that could impact financial markets and fixed-income strategies include fiscal concerns in the US and other countries like France and the UK, along with the potential for central banks to stay too restrictive or for growth to be too strong.

DEFINITIONS

Disinflation is a temporary slowing of the pace of price inflation and is used to describe instances when the inflation rate has reduced marginally over the short term.

Emerging markets (EM) are nations with social or business activity in the process of rapid growth and industrialization. These nations are sometimes also referred to as developing or less developed countries.

Spread sectors refers to sectors of the bond market, such as taxable bonds that are not Treasury securities, and includes securities such as agency securities, asset-backed securities, corporate bonds, high-yield bonds and mortgage-backed securities.

WHAT ARE THE RISKS?

All investments involve risks, including possible loss of principal. Past performance is no guarantee of future results. Please note that an investor cannot invest directly in an index. Unmanaged index returns do not reflect any fees, expenses or sales charges.

Fixed-income securities involve interest rate, credit, inflation and reinvestment risks and possible loss of principal. As interest rates rise, the value of fixed income securities falls. **Low-rated, high-yield bonds** are subject to greater price volatility, illiquidity and possibility of default.

International investments are subject to special risks, including currency fluctuations and social, economic and political uncertainties, which could increase volatility. These risks are magnified in emerging markets. Investments in companies in a specific country or region may experience greater volatility than those that are more broadly diversified geographically. The government's participation in the economy is still high and, therefore, investments in **China** will be subject to larger regulatory risk levels compared to many other countries. There are special risks associated with investments in **China, Hong Kong and Taiwan,** including less liquidity, expropriation, confiscatory taxation, international trade tensions, nationalization, and exchange control regulations and rapid inflation, all of which can negatively impact the fund. **Investments in Taiwan** could be adversely affected by its political and economic relationship with **China.**

Commodities and currencies contain heightened risks that include market, political, regulatory, and natural conditions and may not be suitable for all investors.

US Treasuries are direct debt obligations issued and backed by the "full faith and credit" of the US government. The US government guarantees the principal and interest payments on US Treasuries when the securities are held to maturity. Unlike US Treasuries, debt securities issued by the federal agencies and instrumentalities and related investments may or may not be backed by the full faith and credit of the US government. Even when the US government guarantees principal and interest payments on securities, this guarantee does not apply to losses resulting from declines in the market value of these securities.

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