WIA and WIW Q2 2011 Review

NYSE: WIA & WIW

Q2 2011

Western Asset/Claymore Inflation-Linked Securities & Income Fund (NYSE: WIA) and Western Asset/Claymore Inflation-Linked Opportunities & Income Fund (NYSE: WIW) have made available their quarterly review for the period ended June 30, 2011.

Can you provide a recap of recent economic activity and how WIA and WIW were affected?

The U.S. economy continued to grow during the quarter, but there were numerous indications that the expansion had hit a soft patch. According to the Commerce Department, first quarter 2011 gross domestic product (GDP)[1] growth was a tepid 1.9%. In contrast, the economy expanded 3.1% during the last three months of 2010. Initial second quarter 2011 GDP figures will be released in late July. While an eighth consecutive quarter of growth is expected, a number of headwinds will likely impede a meaningful increase in GDP.

Two factors that negatively impacted the economy were the labor and housing markets. After a modest decline in the first quarter, unemployment moved higher during the second quarter. In April, the Department of Labor reported that unemployment was 9.0%, versus 8.8% at the end of March. The unemployment rate again moved higher in May—to 9.1%—and ended the quarter at 9.2%. Longer-term unemployment trends remain challenging as well. At the end of June, approximately 14.1 million Americans looking for work have yet to find a job, and roughly 44% of these individuals have been out of work for more than six months.[2]

Weakness in the housing market also persisted during the quarter. According to the National Association of Realtors ("NAR"), existing home sales declined 1.8% and 3.8% in April and May, respectively. Hopes for a rebound in housing prices were dashed, as the median existing-home price was $166,500 in May 2011, down 4.6% from May 2010. This weakness was due, in part, to the large overhang of houses on the market. At the end of May, there was a 9.3 month inventory of unsold homes.[3] This is sharply higher than the six to seven months supply that is typical during a healthy housing environment.[4]

Even the manufacturing sector, which had consistently been an area of strength for the economy, faltered somewhat during the second quarter. Based on the Institute for Supply Management's Purchasing Managers Index (PMI), the manufacturing sector has grown 23 straight months since it began expanding in August 2009. However, after reaching 60.4 in April, the PMI fell to 53.5 in May, the lowest level in the previous 12 months. (a reading below 50 indicates a contraction, whereas a reading above 50 indicates an expansion). The PMI then rose modestly to 55.3 in June. More moderate manufacturing activity was partially the result of supply disruptions triggered by the March earthquake and tsunami in Japan.[5]

As expected, the Federal Reserve Board ("Fed")[6] continued to hold interest rates steady within a range of zero to 0.25% during the second quarter. At its meeting in June 2011, the Fed said "To promote the ongoing economic recovery and to help ensure that inflation, over time, is at levels consistent with its mandate, the Committee decided today to keep the target range for the federal funds rate at 0 to 1/4 percent. The Committee continues to anticipate that economic conditions–including low rates of resource utilization and a subdued outlook for inflation over the medium run–are likely to warrant exceptionally low levels for the federal funds rate for an extended period." The Fed also confirmed that it would complete its $600 billion Treasury securities purchase program (dubbed "QE2") at the end of June.

[1] Gross domestic product ("GDP") is the market value of all final goods and services produced within a country in a given period of time.
[2] Source of data in this paragraph: Bloomberg, 7/11.
[3] Source of data in this paragraph: National Association of Realtors, 6/11.
[4] Source: The New York Times, 6/11.
[5] Source of data in this paragraph: Bloomberg, 7/11.
[6] The Federal Reserve Board ("Fed") is responsible for the formulation of policies designed to promote economic growth, full employment, stable prices, and a sustainable pattern of international trade and payments.

Given concerns regarding the economy, both short- and long-term Treasury yields declined during the quarter. The yield on the two- and ten-year Treasury began the period at 0.80% and 3.47%, respectively. Yields initially moved higher as rising food and oil prices fanned inflationary fears. After the yield on the two- and ten-year Treasury peaked at 0.85% and 3.59%, respectively, in April, yields then generally moved lower as economic data were disappointing and oil prices declined. Two- and ten-year Treasuries ended June at 0.45% and 3.18%, respectively. The taxable spread sectors (non-U.S. Treasuries) generated positive returns during the quarter but largely underperformed equal-duration Treasuries given periodic flights to quality.[7]

Headline inflation in the U.S., as measured by the Consumer Price Index for All Urban Consumers (CPI-U), increased, moving up to 3.6% at the end of June 2011 from 2.7% at the end of March, 2011, year over year. Core CPI (which excludes the effects of food and energy) also rose to 1.6%, up from 1.2%, during the same period. Personal Consumption Expenditures (PCE) core deflator, which we believe is the Federal Reserve's favorite inflation measure, also increased to 1.2% from 0.9% over the quarter. Although official inflation measures moved higher, other reflation trades did not fare so well. This was largely driven by weaker economic data which caused downward revisions to growth estimates. Commodities lost nearly 6% as oil prices fell by $11 per barrel over the quarter. The U.S. dollar declined by nearly 2% on a trade-weighted basis while gold only managed to rally by about 0.8%.

U.S. TIPS outperformed treasuries as intermediate maturity real yields rallied. Breakeven rates, the difference between nominal yields and real yields, fell slightly with 10-year TIPS now pricing in average inflation of 2.38% per year at the end of June vs. 2.49% at the end of March 2011.

The 10-year U.S. TIPS real yield rallied 27bps to yield 0.69% at the end of June 2011 from approximately 0.96% at the end of March 2011. Along with coupon and CPI accretion 10-year TIPS generated 4.87% of total return for the second quarter. The 10-year U.S. Treasury, on the other hand, had a total return of 3.59% for the second quarter.

What is your outlook for inflation?

While inflation rose sharply over the first half of the year, at the end of the 2nd quarter inflation data began to moderate, as energy prices were no longer contributing to the gains. With other commodity prices falling recently as well, headline inflation should continue to moderate in coming months, although base effects will still cause year-over-year comparisons to increase. Core inflation continues to rise steadily as rent and shelter components are no longer a drag. While core inflation could reach the Fed's target of 2% by the end of 2011, it does not appear to be going higher without significant reductions in the unemployment rate.

What is your outlook for the Funds' primary investments – U.S. TIPS, inflation-linked securities, high-yield (WIW) and corporate bonds (WIA)?

The recovery remains on-track, albeit at a middling pace. Growth for the remainder of the year is apt to improve despite significant roadblocks at home and abroad. Potential fiscal measures in the US, such as spending cuts to help tame the growing debt, may be beneficial in the long term, but could be detrimental in the short term by biting into growth. Certain global events demand particular attention. Europe has thus far avoided a full-fledged debt crisis contagion—which would likely disrupt global markets—but the possibility of stumbling into one remains. Continued upheaval in North Africa and the Middle East has led to higher energy prices, a decided detriment to an economy struggling to reach firmer footing.

Concerns remained about future demand for TIPS in 2H11 given the end of the Fed's $600 billion QE2 program, a peak in retail gasoline prices, weaker commodities and an uncertain growth outlook. CPI accretion seems poised to fall in 2H11, as well, which will not bode well for TIPS. The $7 billion auction of 30-year TIPS on June 23 was well received, yielding about 1.74%. In the long term, we are still facing an uncertain economic environment given persistent unemployment concerns and a rise in food and gas prices. We believe that we are in an environment in which long-term inflation concerns persist.

Investment Grade Credit

The value of risk assets has cheapened over the past 2 months. The S&P is off 3.09% since the end of April 2011. Investment grade credit hasn't fared much better underperforming similar duration US Treasuries by 3.09% over the same period. Much of the economic data the last 8 weeks has been negative or below market expectations. Clearly the economy had hit a soft-patch, or worse. Investors have sought safety in US Treasuries. 10 year US Treasury rates which were above 3.50% in April have fallen to below 2.90% in early July. In addition to the risk of falling back into another recession other major risks to corporate bonds and risk assets in general include periphery Europe's debt crisis, the US debt ceiling negotiations and uncertainty associated with future bank regulation and capital requirements. Banking institutions with mortgage exposure also face uncertainty as it relates to litigation on the reps and warranties issue. Though BankAmerica (BAC) has reached a tentative accord with a group of investors on mortgages originated by Countrywide (a BAC subsidiary) uncertainty about the potential costs across the industry remain. Our view is that the economy will continue to muddle along with positive growth. We expect GDP growth to exceed 2% for the balance of the year. We believe that Greece will ultimately restructure its debt obligations but the EU will continue to support Greece remaining current on its

[7] Source: Bloomberg, 7/11.

obligations until the systemically important European banks with large periphery Euro exposure build enough capital to be able to absorb the associated losses. We believe the EU will be successful in containing the periphery issue. We believe the US Congress will pass a resolution to increase the debt ceiling. We believe future bank regulation and capital requirements will be supportive of increased bank credit worthiness. We believe the reps and warranties issue is manageable and the BAC agreement may set the blueprint for future agreements. Resolution of these issues will take time and we anticipate markets will remain volatile in the interim.

That said, it appears to us that corporate bond valuations are reasonable, with pockets of opportunity. Though valuations are tending towards the richer side of its historical average, we see corporate fundamentals continuing to strengthen. A low growth environment has historically been good for corporate bond investors. Historically, low growth has discouraged corporate management from engaging in leveraging activities and kept them focused on balance sheet management.

High Yield

The Barclay's 2% Issuer-Constrained US High Yield Index has experienced a sharp sell-off versus similar duration Treasuries over the past 3 months. The option adjusted spread of the index is 100 basis points wider since mid -April. Weak economic data, investor concern regarding how the periphery Europe debt crisis will play out and the acrimonious tone of the debate to raise the debt ceiling have encouraged investors to reduce risk. However, in Western Asset's view we would expect recent worries about the economy to fade in the months to come as the economic backdrop improves, concern regarding an imminent restructuring of Greek debt recedes due to the country receiving monetary support from the EU/IMF and the US Congress and President agree to some form of a pact allowing the debt ceiling to increase. Resolution to these issues and an improving economic environment should result in high yield bonds outperforming similar duration Treasuries in the 2nd half of 2011. The fundamental trajectory of company balance sheets remains positive. In general high yield company cash balances are at all-time highs and leverage continues to decline. As we enter the 2nd quarter earnings period we expect a majority of high yield companies to report minor top-line growth. We will be monitoring closely potential margin erosion due to higher product input costs. We are particularly interested in seeing how successful companies were in passing along these cost increases. The financial metrics of high yield companies have been steadily improving for 6 consecutive quarters which has resulted in the rating agencies issuing almost 2 times as many upgrades than downgrades during the past 12 months. We believe this trend will continue. Under such a scenario, default rates should continue on a downward trajectory and could very well end the year below 2%. At this point we are firmly in the camp that high yield investors are more than fairly compensated for the risks associated with an investment in the asset class.

Outside of U.S. TIPS, where are you finding value in the inflation-linked securities market?

We continue to hold our position in Australia where recent economic data has been mixed, causing the central bank to remain patient with respect to rate increases. As a result, real rates have fallen significantly. If the global situation stabilizes and commodity prices firm up we may look to reduce our position as the central bank would likely resume rate hikes.

We recently added some 5-year French TIPS to the portfolio. We think that the front end of the TIPS market is now fully priced for this year's US inflation and Fed outlook. French linkers, on the other hand, are pricing in a series of rate hikes by the ECB and therefore offer higher real yields than TIPS. French inflation is also expected to be higher than US inflation over the next 6 months. For these reasons we think these bonds offer better relative value than comparable maturity TIPS.

What factors may affect the Funds' dividend rates?

Both WIA and WIW invest at least 80% of their total managed assets in inflation-linked securities. In addition, the Fund's may each invest in non-inflation-linked securities and instruments with the potential to enhance the Fund's income. There are some important differences between investing directly in inflation-linked securities and investing in inflation-linked securities through an actively-managed closed-end fund, such as WIA or WIW. Among these differences are the ways in which investors receive distributions from their investments. Whereas individual inflation-linked securities pay a semi-annual coupon based on a principal value that adjusts for inflation (using CPI-U), WIA and WIW pay monthly dividends based on the income derived from the underlying investments in U.S. TIPS, inflation linked securities and other fixed-income securities.

Historically, CPI-U figures (which are utilized for U.S. TIPS' principal value accretion) have fluctuated from month to month. As a result of this seasonality of inflation, the Funds' monthly distributions may be greater than or less than the amount of income generated by each Fund's underlying portfolio of investments. Although such shortfalls and excesses may occur, the Funds seek to avoid a net return of capital during the course of any given taxable year. In an effort to provide current income and a relatively stable monthly distribution, the Funds attempt to set their dividend rates based on current and projected net investment income at a level that is believed to be sustainable over a period of time.

Each Fund intends to continue to qualify as a regulated investment company for U.S. federal income tax purposes and to meet all other requirements necessary to be relieved of federal taxes on income and gains distributed in a timely manner to shareholders. Each Fund will distribute substantially all of its net investment income and net realized capital gains to its shareholders on a current basis. Accordingly, each Fund will be able to retain for use in the following year very little, if any, of its net investment income and net realized capital gains in excess of its regular monthly distributions for the current year. This means that the Funds may begin each calendar year without a significant "cushion" of undistributed income and gains.

What effect does the seasonality of inflation have on the Funds' income?

U.S. and non-U.S. inflation generally exhibits a normal seasonal pattern of being high in the first half of the year and lower in the second half. The Funds attempt to mitigate the effects of the seasonality of inflation-linked securities. We will look forward to the spring months because we believe they generally provide good inflation accretion for U.S. TIPS holders.

Inflation-linked securities may provide a hedge against inflation. What are some of the hedging strategies the Funds have pursued to address risks not directly associated with inflation?

We again did not implement any hedging strategies during the second quarter, consistent with the quarter ended June 30, 2011. Therefore these strategies did not impact the Funds' yields and had no impact on the total return of WIA and WIW, respectively.

When hedging strategies are implemented in the Funds' portfolios, it is primarily through the use of short futures and long put options. In the past, we have also been opportunistic sellers of calls.

Recall that one of our goals is to maintain a relatively stable NAV – so in bull markets, hedging strategies may cause us to underperform published indices on a total return basis. In bear markets, hedging strategies are designed to help protect the NAV against a significant decline in value. However, there can be no assurance such hedging strategies, if implemented, will be successful.

What are the key reasons you believe investors should hold WIA and WIW in their portfolio?

The key reasons investors should hold WIA and WIW in their portfolio are as follows:

- Current income potential.
- Opportunity for long-term inflation protection: The inflation-linked securities in which WIA and WIW currently invest continue to be one of the few yield-bearing securities that are directly linked to inflation. (The positive effects of inflation on the inflation-linked securities may not necessarily be reflected in the share prices of the Funds.)
- Diversification within investors' fixed-income portfolios.
- Any portion of the Funds' dividends directly attributable to U.S. TIPS principal adjustments is exempt from state and local income tax in certain states.
- An investment in WIA or WIW as compared to a direct investment in individual U.S. TIPS may help avoid the "phantom income"* concern.

We continue to believe that:

- Inflation-linked securities, such as those currently held by the Funds, can be an excellent diversifier for a fixed-income portfolio.

**"Phantom income" is generally any income that is reportable as taxable income but that does not generate cash flow for the investor. In the case of a direct investment in U.S. TIPS, phantom income exists because the investor receives the coupon income in cash but is taxed on both the coupon income and the accretion of principal (resulting from inflation).*

How have the NAVs and share prices of WIA and WIW performed?

Net Asset Value

NAV PER SHARE ($)					NAV PERFORMANCE: TOTAL RETURN				
	Inception	12/31/2009	12/31/2010	6/30/2011	YTD	1-Year	3-Year[1]	5-Year[1]	Since Inception[1]
WIA	$14.33	$12.85	$13.15	$13.57	4.73%	6.11%	4.50%	5.90%	4.46%
WIW	$14.33	$12.94	$13.27	$13.69	4.76%	6.45%	4.74%	6.19%	4.96%

Share Price

MARKET PRICE PER SHARE ($)					MARKET PRICE PERFORMANCE: TOTAL RETURN				
	Inception	12/31/2009	12/31/2010	6/30/2011	YTD	1-Year	3-Year[1]	5-Year[1]	Since Inception[1]
WIA	$15.00	$12.30	$12.83	$12.90	2.10%	5.61%	6.05%	8.26%	3.56%
WIW	$15.00	$12.04	$12.51	$12.52	1.73%	5.33%	5.76%	7.85%	3.56%

[1] Annualized

Inception date of WIA is 9/25/2003; inception date of WIW is 2/24/2004

Since Inception returns assume a purchase of common shares at the initial offering price of $15.00 per share for share price returns and initial net asset value (NAV) of $14.33 per share for NAV returns. Returns for periods of less than one year are not annualized. All distributions are assumed to be reinvested either in accordance with the dividend reinvestment plan (DRIP) for share price returns or NAV for NAV returns. Until the DRIP price is available from the Plan Agent, dividends are assumed to be paid in cash for total return purposes.

Western Asset Management Company
June 30, 2011

RISKS AND OTHER CONSIDERATIONS OF THE FUNDS

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This document is not an offer to sell securities of the Funds and it is not soliciting an offer to buy securities of the Funds.

There can be no assurance that a Fund will achieve its investment objectives. The net asset value of each Fund will fluctuate with the value of the underlying securities. It is important to note that closed-end funds trade on their market value, not net asset value, and closed-end funds often trade at a discount to their net asset value. Past performance is not an indication of future performance.

There can be no guarantee that the Funds' hedging strategies will be employed under all market conditions or will be successful. Additionally, the cost paid for the hedging strategies may result in a reduction of the net asset value of a Fund and, as a result, could make the Fund worse off than if such hedging strategies had not been used.

Certain risks are associated with the leveraging of a Fund's common shares. Both the net asset value and the market value of the common shares may be subject to higher volatility and a decline in value. A Fund's leveraging strategy may not be successful.

An investment in a Fund is subject to certain risks and other considerations. Such risks and considerations include, but are not limited to: Investment Risk, Market Discount Risk, Interest Rate Risk, U.S. TIPS Risk, Credit Risk, Lower Grade and Unrated Securities Risk, Leverage Risk, Issuer Risk, Country Risk, (WIW only) Emerging Markets Risk, Prepayment Risk, Reinvestment Risk, Derivatives Risk, Inflation/Deflation Risk, Mortgage-Related Securities Risk, Management Risk, Turnover Risk, Anti-Takeover Provisions, Smaller Company Risk, and Market Disruption and Geopolitical Risk. Investors should consider the risks, expenses and fees of the Funds prior to investing.

Consider the investment objectives, risks, charges and ongoing expenses of any CEF carefully before investing. The prospectus contains this and other information about the CEF. Please read the prospectus carefully before investing. To obtain a prospectus, visit www.guggenheimfunds.com or contact a securities representative or Guggenheim Funds Distributors, Inc. 2455 Corporate West Drive, Lisle, IL 60532, 800-345-7999.

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