Franklin Templeton Investments
(Asia) Limited
富蘭克林鄧普頓投資(亞洲)有限公司
17/F, Chater House
8 Connaught Road Central
Hong Kong
t +852 2877-7733
f +852 2877-5401
www.franklintempleton.com.hk

This letter is important and requires your immediate attention.

If you are in doubt, please consult your legal, financial or professional advisers.

13 June 2014

Dear Shareholder,

Franklin Floating Rate Fund plc (the "Company")
- **Appointment of AIFM**
- **Appointment of Depositary**
- **Revisions to Investment Objectives and Policies of the Master Fund**
- **Revisions to the Master Fund's Policies on the Use of Investment Techniques, Swaps, Repurchase Agreements and Reverse Repurchase Agreements**
- **Disclosure in relation to Securities Lending Agent**
- **Revisions to the Investment Manager's Policy on Selection of Brokers and Dealers**
- **Adoption of a Policy on Equalisation Payments by the Company**
- **Disclosure in relation to Dividend Distribution Policy**
- **Provisions on "Prohibited Persons"**

The purpose of this letter is to inform you of (1) the appointment of Franklin Templeton International Services S.à r.l. as the alternative investment fund manager (the "**AIFM**") of the Company; (2) the appointment of J.P. Morgan Bank (Ireland) plc as the depositary (the "**Depositary**") of all the assets of the Company; (3) revisions to the investment objectives and policies of Franklin Floating Rate Master Trust (the "**Master Fund**"), in which the Company invests up to 100% of its net assets; (4) revisions to the Master Fund's policies on the use of investment techniques, swaps, repurchase agreements and reverse repurchase agreements; (5) disclosure in relation to the use of a securities lending agent (if any) by the Master Fund; (6) revisions to the policy of Franklin Advisers, Inc., the investment manager of the Company (the "**Investment Manager**") on the selection of brokers and dealers for the Company; (7) adoption of a policy on equalisation payments by the Company; (8) disclosure of the Company's dividend distribution policy in relation to the payment of dividends out of its capital; and (9) measures which the Company may take in order to restrict or prevent the ownership of shares of the Company by "Prohibited Persons" (as explained below).

Unless otherwise defined herein, terms and expressions used in this letter shall have the same meanings as those defined in the Prospectus dated October 2009, as amended, of the Company (the "**Current Prospectus**").

1. Appointment of AIFM

The Company is currently organized as a self-managed investment company whereby the directors of the Company (the "**Directors**") are responsible for managing the business affairs of the Company in accordance with its articles of association. Under this structure, the Directors have delegated the day-to-day administration of the Company's affairs to the Administrator, and the management of the cash and other assets and investments of the Company to the Investment Manager.

Recent European regulations, including the Alternative Investment Fund Managers Directive (Directive 2011/61/EU) ("**AIFMD**"), have had the effect of reinforcing management and administration requirements for the Company. As a consequence, and in order to centralize the management and administration functions in one "central" entity, it is envisaged that on 17 July 2014, the Company will appoint its existing Shareholder Services Agent, Franklin Templeton International Services S.à r.l. (formerly known as "Franklin Templeton International Services S.A.") as its AIFM.

The AIFM is part of Franklin Templeton Investments. The AIFM was incorporated in Luxembourg on 17 May 1991 as a company subject to general company law. The corporate object of the AIFM is to provide investment management, administration and marketing services to undertakings for collective investment. The AIFM has been authorised by its home regulator (the *Commission de Surveillance du Secteur Financier*) to act as an AIFM pursuant to the Law of 12 July 2013 and will be appointed by the Company as alternative investment fund manager to perform portfolio and risk management functions as well as activities related to the assets of the Company.

The AIFM will be responsible for the portfolio management and the risk management function of the Company. The AIFM is also responsible for ensuring compliance with the AIFMD, to which the Company is subject. The AIFM shall ensure compliance of the Company with the investment restrictions and oversee the implementation of the Company's strategies and investment policy.

As the AIFM will, in turn, at all times delegate portfolio management of the Company to the existing Investment Manager (which will have discretionary investment management powers), the appointment of the AIFM will not have any impact on the way the Company is managed.

Rest assured, there will be no change to the investment objective, policies or restrictions of the Company as a result of the proposed appointment of the AIFM. For the avoidance of doubt, the appointment of the AIFM will not result in the Company adopting an alternative investment strategy.

The AIFM will be remunerated by the Investment Manager out of the investment management fee received from the Company and the appointment of the AIFM will not result in any change in the fee levels and costs borne by the Company.

The AIFM will employ a risk management process which enables it to monitor and measure at any time the risk of the positions of the Company.

The AIFM will maintain a liquidity management process to monitor the liquidity risk of the Company, which includes, among other tools and methods of measurement, the use of stress tests under both normal and exceptional liquidity conditions. The liquidity management systems and procedures allow the AIFM to apply various tools and arrangements necessary to ensure that the portfolio of the Company is sufficiently liquid to normally respond appropriately to redemption requests.

The Current Prospectus will be updated to reflect this change if and when implemented.

2. Appointment of Depositary

Pursuant to the requirements under the AIFMD, the Company will be appointing its existing Custodian, J.P. Morgan Bank (Ireland) plc, as Depositary of all the assets of the Company with effect on or about 17 July 2014.

The Depositary was incorporated in Ireland as a limited liability company on 30 November 1926. The Depositary is ultimately a wholly-owned subsidiary of J.P. Morgan Chase & Co. of Delaware, U.S.A. One of the principal activities of the Depositary is to act as depositary and trustee of collective investment schemes.

The Depositary’s primary responsibilities are in general wider than those which are presently performed by the Custodian and include ensuring the safekeeping of the cash and assets of the Company, fiduciary oversight of the operation of the Company and reporting to investors in relation to the same on an annual basis. The Depositary will also perform additional daily cashflow monitoring duties under AIFMD in respect of the operation of the Company. The Depositary's duties will include, amongst others, the following:

(i) ensuring that the Company’s cash flows are properly monitored, and that all payments made by or on behalf of investors upon the subscription of Shares have been received;

(ii) safekeeping the assets of the Company, which includes (a) holding in custody all financial instruments that can be registered in a financial instrument account opened in the Depositary's books and all financial instruments that can be physically delivered to the Depositary; and (b) for other assets, verifying the ownership of such assets and maintain a record accordingly;

(iii) ensuring that the sale, issue, re-purchase, redemption and cancellation of Shares are carried out in accordance with applicable Irish law and the Articles;

(iv) ensuring that the value of the Shares is calculated in accordance with the applicable laws and the Articles;

(v) carrying out the instructions of the Company and the AIFM, unless they conflict with the applicable Irish law or the Articles;

(vi) ensuring that in transactions involving the Company’s assets any consideration is remitted to the Company within the usual time limits; and

(vii) ensuring that the Company’s income is applied in accordance with the applicable Irish law and the Articles.

J.P. Morgan Bank (Ireland) plc will continue to receive the same fee that it received as Custodian after its appointment as Depositary and the change in appointment of J.P. Morgan Bank (Ireland) plc from Custodian to Depositary will not result in any change in the fee levels and costs borne by the Company. The Depositary will also continue to comply with Chapter 4.2 to Chapter 4.4 of the Securities and Futures Commission of Hong Kong’s (the “**SFC**”) Code on Unit Trusts and Mutual Funds (the “**UT Code**”) and there is nothing which would affect its ability to act or perform as the depositary of the Company in compliance with Chapter 4 of the UT Code.

The Current Prospectus will be updated to reflect this change if and when implemented.

3. <u>Revisions to Investment Objectives and Policies of the Master Fund</u>

We would like to inform you that the investment objectives and policies of the Master Fund, under the sub-section headed “Investment Considerations - Investment Objectives and Policies of the Master Fund” on pages 8 and 9 of the Current Prospectus (the “**Investment Objectives and Policies of the Master Fund**”), will with effect from 17 July 2014 be revised and restated as set out below.

For the avoidance of doubt:

- the appointment of the AIFM (as described in paragraph 1 above) and the clarifications and elaborations to the Investment Objectives and Policies of the Master Fund that are set out below will not result in any change to the extent of the Master Fund’s use of financial derivative instruments for investment purposes (which will remain in compliance with Chapter 7 of the UT Code); and

- for such time as they remain authorised by the SFC, each of the Company and the Master Fund shall not invest more than 10% of its net asset value in securities issued and/or guaranteed by any single sovereign issuer (including its government and a public or local authority of that country) with a credit rating below investment grade, including unrated sovereign issuers, and the Current Prospectus shall be amended accordingly.

A. Investment goal of the Master Fund

To reflect the existing investment goal of the Master Fund and to ensure the same is brought to your attention, the following paragraph on the investment goal of the Master Fund will be inserted immediately following the first paragraph of the Investment Objectives and Policies of the Master Fund on page 8 of the Current Prospectus:

> "*The Master Fund's investment goal is to provide as high a level of current income and preservation of capital as is consistent with investment primarily in senior secured corporate loans and corporate debt securities with floating interest rates.*"

Rest assured, there will be no change to the way that the Company is currently managed or to the investment strategy of the Company.

To disclose the risks arising out of the Company's investment in the Master Fund and to ensure that the same is brought to your attention, the following risk disclosure will be inserted immediately following the risk disclosure on "Sales Charges" under the section headed "Risk Factors" on page 13 of the Current Prospectus:

> "***Feeder Fund***
>
> *Due to the Company's investment in the Master Fund, Shareholders will be subject to fees and expenses arising from the layered investment structure. See "Fees and Expenses". The Company may also bear, indirectly through its investment in the Master Fund, a proportion of the offering, organisational and operating expenses of the Master Fund.*
>
> *The Master Fund may be permitted in certain circumstances to redeem its shares in-kind. Thus, upon the Company's withdrawal of all or a portion of its interest in the Master Fund, the Company may receive securities that are illiquid or difficult to value. In these circumstances, the Company would seek to dispose of these securities in an appropriate manner including obtaining the consent of Shareholders.*"

B. Elaboration of the credit analysis process of the Investment Adviser

To elaborate on the credit analysis process employed by the Investment Adviser of the Master Fund, Franklin Advisers, Inc., the fourth paragraph of the Investment Objectives and Policies of the Master Fund on page 8 of the Current Prospectus shall be deleted in its entirety and replaced by the following paragraph:

> "*The Investment Adviser of the Master Fund performs its own independent credit analysis of each borrower, and of the collateral structure securing the Master Fund's investment. The Investment Adviser of the Master Fund generally will determine the value of the collateral backing the Master Fund's investment by customary valuation techniques that it considers appropriate, including reference to financial statements, independent appraisal, or obtaining the market value of collateral (e.g., cash or securities), if it is readily ascertainable. The Investment Adviser of the Master Fund also will consider the nature of the industry in which the borrower operates, the nature of the borrower's assets, and*

the general quality and creditworthiness of the borrower. The Investment Adviser of the Master Fund evaluates the credit quality of the Master Fund’s investments on an ongoing basis. The value assigned to the collateral by the Investment Adviser of the Master Fund may be higher or lower than the value at which the borrower values the collateral on the borrower's books.”

The revisions are being made to:

- explain how the Investment Adviser will make use of customary valuation techniques in determining the value of the collateral securing the Master Fund’s investments; and

- elaborate on the factors that the Investment Adviser will consider in performing its own independent credit analysis of each borrower.

Rest assured, there will be no change to the way that the Company is currently managed or to the investment strategy of the Company.

C. Elaboration on the Master Fund’s floating rate investments

To elaborate on the Master Fund’s floating rate investments:

(i) the fifth paragraph of the Investment Objectives and Policies of the Master Fund on page 8 of the Current Prospectus shall be deleted in its entirety and replaced by the following paragraph:

“*The Master Fund's floating rate investments will, in most instances, hold the most senior position in the capitalization structure of the company and be secured by specific collateral. Such senior position means that, in case the company becomes insolvent, the lenders or security holders in a senior position like the Master Fund will typically be paid before other creditors of the corporation from the assets of the company. When a company pledges specific collateral, it has agreed to deliver, or has actually delivered, to the lenders or security holders assets it owns that will legally become the property of the lenders or security holders in case the company defaults in paying interest or principal.*”; and

(ii) the twelfth paragraph of the Investment Objectives and Policies of the Master Fund on page 9 of the Current Prospectus will be revised and restated as set out below. The relevant revisions are marked up for your ease of comparison.

“*Floating interest rate loans and securities are generally credit-rated less than investment grade and may be subject to restrictions on resale. The Master Fund may invest up to 100% of its portfolio in ~~senior secured debt obligations~~floating interest rate loans and securities that may be high yield, high risk, debt securities ~~that~~and are rated less than investment grade (i.e., less than BBB~~). See “Risk Factors”. However~~, sometimes called junk bonds) or unrated. ~~u~~Under normal conditions, the Master Fund invests at least 65% of ~~the Master Fund’s~~its total assets ~~will be~~in floating in~~v~~terest~~ed~~ ~~in debt obligations~~rate loans and securities that are rated ~~by a NRSRO with the equivalent of a~~ B or higher by a nationally recognized statistical rating ~~by Moody’s or S&P~~organization (“NRSRO”) or, if unrated, are determined to be of comparable ~~credit~~ quality by the Investment Adviser of the Master Fund. Under normal conditions, t~~T~~he Master Fund may~~,~~ ~~however,~~ invest up to 35% of its total assets in ~~debt obligations~~floating interest rate loans and securities that are rated ~~less than such a~~below B ~~rating~~ by an NRSRO or, if unrated, are determined to be of comparable ~~credit~~ quality by the Investment ~~Adviser of the Master Fund~~Manager.~~Please see the Appendix for a description of ratings of Moody’s and S&P.~~*”

The revisions are being made to:

- elaborate on the senior secured position (in most instances) of the floating rate investments held by the Master Fund;

- explain the significance to investors of such investments holding (in most instances) the most senior position in the capitalization structure of the issuing company and being secured by specific collateral;

- provide investors with general credit rating information on floating rate investments;

- clarify that the Master Fund may invest up to 100% of its portfolio in floating interest rate loans and securities that are rated less than investment grade; and

- clarify that under normal conditions, the Master Fund will seek to invest at least 65% of its total assets in floating interest rate loans and securities which are rated B or higher or which are determined to be of comparable credit quality by its Investment Adviser, and may invest up to 35% of its total assets in floating interest rate loans and securities that are of a lower credit quality.

Rest assured, there will be no change to the way that the Company is currently managed or to the investment strategy of the Company.

D. Elaboration on the Master Fund's investments in corporate loans and corporate debt securities

To elaborate on the Master Fund's investments in corporate loans and corporate debt securities:

(i) the third, sixth and seventh paragraphs of the Investment Objectives and Policies of the Master Fund on page 8 of the Current Prospectus shall be deleted in their entirety and replaced by the following paragraph:

> "*The Master Fund normally invests at least 80% of its net assets, plus the amount of any borrowings for investment purposes, in corporate loans and corporate debt securities that are made to, or issued by, borrowers that are U.S. companies, non-U.S. borrowers and U.S. subsidiaries of non-U.S. borrowers and that have floating interest rates (floating interest rate loans and securities). Shareholders in the Master Fund will be given 60 days advance notice of any change in this 80% policy. Certain of the Master Fund's floating interest rate investments may permit the borrower to select an interest rate reset period of up to one year. A portion of the Master Fund's investments may consist of loans with interest rates that are fixed for the term of the loan. Investment with longer interest rate reset periods or fixed interest rates may increase fluctuations in the Master Fund's share price as a result of changes in interest rates. Fixed rate corporate loans and debt securities that are converted from fixed rate investments to floating rate investments through interest rate swaps or other derivative transactions will be considered to be floating interest rate loans and securities for purposes of the Master Fund's policy of normally investing at least 80% of its net assets in income-producing floating interest rate corporate loans and corporate debt securities made to or issued by U.S. companies, non-U.S. entities and U.S. subsidiaries of non-U.S. entities. Some of the Master Fund's floating interest rate loans and securities may have the additional feature of converting into a fixed rate instrument after certain periods of time or under certain circumstances. Upon conversion of any such floating interest rate loans and securities to fixed rate instruments, the Investment Adviser of the Master Fund will rebalance the Master Fund's investments, if needed, to meet the 80%*

level described above, as promptly as is reasonable. Generally, corporate loans and corporate debt securities require that the borrower or issuer comply with various restrictive covenants that accompany the loan or security although some available in the market from time to time are ‘covenant lite’ in that they contain fewer or no restrictive covenants.”; and

(ii) the ninth paragraph of the Investment Objectives and Policies of the Master Fund on pages 8 and 9 of the Current Prospectus will be revised and restated as set out below. The relevant revisions are marked up for your ease of comparison.

“*~~While the~~The Master Fund ~~will~~normally invests primarily in ~~debt obligations of U.S.~~ corporat~~ions~~e loans or securities of U.S. entities, ~~the Master Fund may also~~but may invest up to 65% of its assets in ~~debt obligations of non-U.S.~~ corporat~~ions~~e ~~located~~loans or corporate debt securities of entities in developed ~~market~~ countries other than the U.S. The Master Fund may from time to time invest in ~~non-U.S.~~ corporat~~ions~~e debt securities of entities in emerging market countries, but currently does not intend to invest more than 35% of its ~~net~~ assets ~~in debt obligations issued by corporations~~ in emerging market countries. The Master Fund considers a country to be an emerging market country if it is defined as a country with an emerging or developing economy by any one or more of the following: the International Bank for Reconstruction and Development (commonly known as the World Bank), the International Finance Corporation, or the United Nations or its agencies or authorities.*”

The revisions are being made to:

- provide more details on the Master Fund’s primary investments, including:

  (a) the level in percentage terms (*i.e.*, at least 80%) of the Master Fund’s net assets that are normally invested in its primary investments;

  (b) the nature of the primary investments; and

  (c) the nature and geographical location of the issuers of the primary investments (*i.e.*, U.S. companies, non-U.S. borrowers and U.S. subsidiaries of non-U.S. borrowers);

- elaborate on certain of the features of the Master Fund's floating interest rate investments, including:

  (x) investments with longer interest rate reset periods or fixed interest rates;

  (y) investments which convert into a fixed rate instrument after certain periods of time or under certain circumstances; and

  (z) restrictive covenants; and

- clarify that the issuers of the primary investments of the Master Fund are normally primarily U.S. entities, but the Master Fund may invest up to 65% of its assets in corporate loans or corporate debt securities of entities in developed countries other than the U.S. The Master Fund also invest in corporate debt securities of entities in emerging market countries, but currently does not intend to invest more than 35% of its assets in emerging market countries.

Rest assured, there will be no change to the way that the Company is currently managed or to the investment strategy of the Company.

To disclose the risks arising out of the Master Fund’s investment in ‘covenant lite’ loans and debt securities and to ensure that the same is brought to your attention, the following risk disclosure will be inserted immediately following the risk disclosure on "Limitations On Availability Of Corporate Loans, Participation Interests, Assignments And Corporate Debt Securities" under the section headed "Risk Factors" on page 14 of the Current Prospectus:

> "***Covenant Lite Risks***
>
> *Covenant lite loans and debt securities generally entail higher risk, since they lack certain restrictions that serve as early warning signs of a borrower's financial troubles. This risk is offset to varying degrees by the fact that the same financial and performance information is available with or without covenants to lenders and the public alike and can be used to detect such early warning signs as deterioration of a borrowers financial conditions results. With such information, the portfolio managers are normally able to take appropriate action without the help of covenants in the loan agreements or debt securities. Covenant lite corporate loans and debt securities, however, may foster a capital structure designed to avoid defaults by giving borrowers or issuers increased financial flexibility when they need it the most.*
>
> *The substantially increased issuance of covenant-lite loans and high-yield bonds with weak investor protections in the current market may signal the emergence of a "covenant bubble" that potentially could leave investors vulnerable if a credit cycle downturn in the market occurs.*"

E. Elaboration on risks arising from the Master Fund's future obligations

To elaborate on the risks arising from the Master Fund's future obligations, the eighth paragraph of the Investment Objectives and Policies of the Master Fund on page 8 of the Current Prospectus will be revised and restated as set out below. The relevant revisions are marked up for your ease of comparison.

> "*The debt obligations may be structured to require the Master Fund to contribute additional capital to the corporate issuer or obligor~~, but the~~. If the Master Fund's ~~intends to limit investments in any such debt~~future obligations ~~to amounts that would not require commitments for future investments to exceed 20% of the~~are not met for any reason, including the failure of an intermediate participant to fulfil its obligations, the Master Fund's ~~total assets~~interests may be harmed. The possible exposure of the Master Fund resulting from these requirements will be aggregated to ensure that prior to becoming subject to a requirement to contribute additional capital the Master Fund will be satisfied the requirements will not result in a breach of its investment restrictions.*"

The revisions are being made to clarify that the 20% limit on the Master Fund's commitments for future investments no longer applies. For the avoidance of doubt, the Master Fund will not acquire any asset which involves the assumption of any liability which is unlimited.

Rest assured, there will be no change to the way that the Company is currently managed or to the investment strategy of the Company.

F. Elaboration on the Master Fund's use of derivative instruments

To elaborate on the Master Fund's use of derivative instruments, the tenth paragraph of the Investment Objectives and Policies of the Master Fund on page 9 of the Current Prospectus shall be deleted in its entirety and replaced by the following paragraphs:

> "*The Master Fund currently invests predominantly in corporate loans or corporate debt securities that are U.S. dollar-denominated or otherwise provide for payment in U.S. dollars. For the purposes of pursuing its investment goals,*

the Master Fund may enter into interest rate and credit-related transactions involving certain derivative instruments, including interest rate and credit default swaps (including loan and high yield credit default swaps) or other derivative transactions. The Master Fund may use such interest rate or credit-related derivative transactions to hedge risks relating to changes in interest rates, credit risks and other market factors. The Master Fund may also use interest rate or credit-related derivative transactions for the purposes of enhancing fund returns, increasing liquidity, and/or gaining exposure to particular instruments or interest rates in more efficient or less expensive ways.

When the Investment Adviser of the Master Fund believes market or economic conditions are unfavorable for investors (for example, in times of market failure), the Investment Adviser of the Master Fund may invest up to 100% of the Master Fund's assets in a temporary defensive manner by holding all or a substantial portion of its assets in cash, cash equivalents or other high quality short-term investments. Temporary defensive investments generally may include money market fund shares (including shares of an affiliated money market fund), U.S. government securities, high-grade commercial paper, repurchase agreements and other money market instruments. The Investment Adviser of the Master Fund also may invest in these types of securities or hold cash while looking for suitable investment opportunities or to maintain liquidity. In these circumstances, the Master Fund may be unable to achieve its investment goals."

The revisions are being made to:

- elaborate on the types of derivative instruments that the Master Fund may enter into and the purposes of entering into such transactions; and

- elaborate on how the Master Fund may invest its assets when market or economic conditions are unfavourable, or while the Investment Adviser of the Master Fund is looking for suitable investment opportunities or to maintain liquidity.

Rest assured, there will be no change to the way that the Company is currently managed or to the investment strategy of the Company. For such time as the Master Fund remains authorised by the SFC, the Master Fund does not intend to invest in financial derivative instruments (including interest rate swaps, credit default swaps and currency swaps) for investment purposes (other than in accordance with Chapter 7 of the UT Code). To clarify this, the following new paragraph will be inserted at the end of the Fundamental Investment Policies of the Master Fund on page 11 of the Current Prospectus:

"*For such time as it remains authorised by the SFC, the Master Fund will not invest in financial derivative instruments (including interest rate swaps, credit default swaps and currency swaps) for investment purposes (other than in accordance with Chapter 7 of the SFC's Code on Unit Trusts and Mutual Funds). The Master Fund may amend its policy with respect to investments in financial derivative instruments subject to the SFC's prior approval and by giving not less than one month's prior notice to investors.*"

G. Clarification on the Master Fund's investments in short-term debt securities and obligations

To provide clarification on the Master Fund's investments in short-term debt securities and obligations, the eleventh paragraph of the Investment Objectives and Policies of the Master Fund on page 9 of the Current Prospectus will be revised and restated as set out below. The relevant revisions are marked up for your ease of comparison.

"*In addition to the Master Fund main investments, the Master Fund may, under normal conditions hold ancillary liquid assets and invest up to 20% of its net* *assets in certain other types of short term debt securities and obligations including unsecured debt obligations, U.S. government securities, U.S. government agency securities (some of which may not be backed by the full faith and credit of the United States), bank money market instruments (such as certificates of deposit), bankers acceptances and corporate and commercial obligations (such as commercial paper and medium-term notes) and for efficient portfolio management purposes re-purchase agreements.* ~~*These short-term debt securities or obligations purchased by the Master Fund will be rated within the four highest rating categories assigned by a nationally recognized statistical rating organization ("NRSRO") or, if unrated, determined to be of comparable quality by the Investment Adviser of the Master Fund. None of these short term debt securities and obligations are required to be backed by collateral. Short-term debt obligations purchased by the Master Fund, however, will be (or counterparties associated therewith will be) investment grade. This means that they will be rated Baa, P-3 or higher by Moody's Investors Services ("Moody's") or BBB, A-3 or higher by Standard & Poor's Ratings Group ("S&P") or, if unrated, determined to be of comparable quality by the Investment Adviser of the Master Fund.*~~ *These short-term debt securities or obligations will not exceed 20% of the Master Fund's total assets except (i) during interim periods pending investment of the net proceeds of Common Share sales; (ii) pending reinvestment of proceeds of the sale of debt obligations of the Master Fund; and (iii) during temporary defence periods when, in the opinion of the Investment Adviser of the Master Fund, suitable senior secured debt obligations are not available or prevailing market or economic conditions warrant.*"

The revisions are being made to clarify to investors that the existing investment objective and policies of the Master Fund do not limit its investments in short-term debt securities and obligations to those which are rated within the four highest rating categories assigned by a nationally recognized statistical rating organization or of investment grade.

Rest assured, there will be no change to the way that the Company is currently managed or to the investment strategy of the Company.

H. Elaboration on the Master Fund's anticipated portfolio maturity and prepayment considerations

To elaborate on the Master Fund's anticipated portfolio maturity and prepayment considerations, the thirteenth paragraph of the Investment Objectives and Policies of the Master Fund on page 9 of the Current Prospectus will be revised and restated as set out below. The relevant revisions are marked up for your ease of comparison.

"*The Master Fund has no restrictions on portfolio maturity* ~~*but*~~*. The Master Fund anticipates, however, that a majority of* ~~*the debt obligations in which it will invest*~~*its investments will have stated maturities ranging from three to ten years. This means that the borrower is required to fully repay the obligation within that time period. The Master Fund also anticipates that* ~~*such debt obligations will*~~*its investments will generally have an expected average life of* ~~*three to*~~ *five years or less. The expected average life of most floating rate investments is less than* ~~*the*~~*their stated maturities because the* ~~*corporate issuers or obligors*~~*borrowers may choose to pay off such obligations early. Such obligations usually permit the borrower to elect to prepay. Also, prepayment is likely because such corporate obligations generally provide that the lenders will have priority in prepayment in case of sales of assets of the borrowers, or from excess cash flow.*"

The revisions are being made to:

- elaborate on the Master Fund's anticipated portfolio maturity; and
- elaborate on the repayment period for the Master Fund's investments and the impact on the repayment period arising from prepayment by borrowers.

Rest assured, there will be no change to the way that the Company is currently managed or to the investment strategy of the Company.

To disclose the risks arising out of prepayment and to ensure that the same is brought to your attention, the following risk disclosure will be inserted immediately following the risk disclosure on "Risks From Fluctuations In Interest Rates" under the section headed "Risk Factors" on page 15 of the Current Prospectus:

> "***Prepayment***
>
> *Debt securities are subject to prepayment risk when the issuer can "call" the security, or repay principal, in whole or in part, prior to the security's maturity. When the Master Fund reinvests the prepayments of principal it receives, it may receive a rate of interest that is lower than the rate on the existing security, potentially lowering the Master Fund's income, yield and its distributions to shareholders. Securities subject to prepayment may offer less potential for gains during a declining interest rate environment and have greater price volatility. Prepayment risk is greater in periods of falling interest rates.*"

4. <u>Revisions to the Master Fund's policies on the use of investment techniques, swaps, repurchase agreements and reverse repurchase agreements</u>

We would like to inform you that the Master Fund's policies on the use of investment techniques, swaps, repurchase agreements and reverse repurchase agreements, under the section headed "Investment Techniques" on pages 11 to 13 of the Current Prospectus, will with effect from 17 July 2014 be revised and restated as set out below.

A. Clarification on treatment of revenues from efficient portfolio management techniques

To clarify the treatment of revenues from efficient portfolio management techniques not received directly by the Master Fund and to ensure the same is brought to your attention, the following paragraph will be inserted immediately following the first paragraph of the sub-section headed "Investment Techniques - Investment Techniques of the Master Fund" on page 11 of the Current Prospectus:

> "*Any revenues from efficient portfolio management techniques not received directly by the Master Fund, net of direct and indirect operational costs and fees, will be returned to the Master Fund.*"

B. Clarification on use of currency swaps

To clarify that the Master Fund currently does not intend to enter into foreign currency swap arrangements and to ensure the same is brought to your attention, the third paragraph of the sub-section headed "Investment Techniques – Use of Interest Rate and Currency Swaps" on page 11 of the Current Prospectus shall be deleted in its entirety.

C. Use of credit default swaps

To clarify that the Master Fund may enter into credit default swap arrangements and to ensure the same is brought to your attention:

(i) the following paragraphs will be inserted immediately before the first paragraph of the sub-section headed “Investment Techniques – Use of Interest Rate and Currency Swaps” on page 11 of the Current Prospectus:

“*The Master Fund may enter into credit default swaps, including loan credit default swaps and interest rate swaps. The use of such derivative transactions may allow the Master Fund to obtain net long or net short exposures to selected interest rates, durations or credit risks. The Master Fund may use these interest rate or credit-related derivative transactions for the purposes of enhancing returns, increasing liquidity, gaining exposure to particular instruments or interest rates in more efficient or less expensive ways and/or hedging risks relating to changes in interest rates, credit risks and other market factors. The Master Fund currently does not intend to enter into currency swaps.*

Swap agreements, such as interest rate and credit default swaps, are contracts between the Master Fund and, typically, a brokerage firm, bank, or other financial institution (the swap counterparty) for periods ranging from a few days to multiple years. In a basic swap transaction, the Master Fund agrees with its counterparty to exchange the returns (or differentials in rates of return) earned or realized on a particular “notional amount” of underlying instruments. The notional amount is the set amount selected by the parties as the basis on which to calculate the obligations that they have agreed to exchange. The parties typically do not actually exchange the notional amount. Instead, they agree to exchange the returns that would be earned or realized if the notional amount were invested in given instruments or at given interest rates.

For credit default swaps, the “buyer” of the credit default swap agreement is obligated to pay the “seller” a periodic stream of payments over the term of the agreement in return for a payment by the “seller” that is contingent upon the occurrence of a credit event with respect to an underlying reference debt obligation. Generally, a credit event means bankruptcy, failure to timely pay interest or principal, obligation acceleration, or modified restructuring of the reference debt obligation. The contingent payment by the seller generally is the face amount of the debt obligation in exchange for the physical delivery of the reference debt obligation or a cash payment equal to the then current market value of that debt obligation. By way of example, the investment manager might "buy" credit default swaps to help protect against the risk of default by the issuer of one or more debt securities held by the Master Fund. Alternatively, the Master Fund may "sell" a credit default swap to gain exposure to an asset class more efficiently or less expensively than by purchasing the related debt security outright.”;

(ii) the second paragraph of the sub-section headed “Investment Techniques – Use of Interest Rate and Currency Swaps” on page 11 of the Current Prospectus will be revised and restated as set out below. The relevant revisions are marked up for your ease of comparison.

“*Except as noted above, there is no limit on the amount of <u>credit risk or</u> interest rate hedging transactions that may be entered into by the Master Fund. The <u>risk of loss with respect to credit risk hedges is limited to the amount of periodic streams of payments over the term of the agreement. If the other party to a credit default swap defaults, the Master Fund’s risk of loss consists of the net payment of the face amount of the debt obligation. Similarly, the</u> risk of loss with respect to interest rate hedges is limited to the net amount of interest payments that the Master Fund is obligated to make. If the other party to an interest rate swap defaults, the Master Fund’s risk of loss consists of the net amount of interest payments that the Master Fund is entitled to receive. The Master Fund will only enter into an interest rate swap after the Investment Adviser of the Master Fund* *has evaluated the creditworthiness of the other party to the swap in accordance with the requirements set out below.*";

(iii) the first sentence of the fourth paragraph of the sub-section headed "Investment Techniques – Use of Interest Rate and Currency Swaps" on page 12 of the Current Prospectus will be revised and restated as set out below. The relevant revisions are marked up for your ease of comparison.

"*Interest rate and ~~currency~~credit default swaps may be bought or sold by the Master Fund on a Recognised Market or off-exchange on an over-the-counter market ("OTC Contracts").*"; and

(iv) the sub-section headed "Investment Techniques – Use of Interest Rate and Currency Swaps" on page 11 of the Current Prospectus will be renamed as "Investment Techniques – Use of Credit Default and Interest Rate Swaps".

To disclose the risks arising out of the Master Fund's use of derivative instruments and to ensure that the same is brought to your attention, the following risk disclosure will be inserted immediately following the risk disclosure on "Highly Leveraged Transactions" under the section headed "Risk Factors" on page 16 of the Current Prospectus:

"***Derivative Instruments***

The performance of derivative instruments depends largely on the performance of an underlying instrument or index and derivative instruments often have risks similar to their underlying instrument in addition to other risks. Derivatives involve costs and can create economic leverage in the Master Fund's portfolio which may result in significant volatility and cause the Master Fund to participate in losses (as well as enable gains) in an amount that exceeds the Master Fund's initial investment. Other risks include illiquidity, mispricing or improper valuation of the derivative instrument, and imperfect correlation between the value of the derivative and the underlying instrument so that the Master Fund may not realize the intended benefits. Successful use of derivatives will usually depend on the Investment Adviser of the Master Fund's ability to accurately forecast movements in the market relating to the underlying instrument. Should a market or markets, or prices of particular classes of investments move in an unexpected manner, especially in unusual or extreme market conditions, the Master Fund may not achieve the anticipated benefits of the transaction, and the Master Fund may realize losses, which could be significant. If the Investment Adviser of the Master Fund is not successful in using such derivative instruments, the Master Fund's performance may be worse than if the Investment Adviser of the Master Fund did not use such derivative instruments at all. To the extent that the Master Fund uses such instruments for hedging purposes, there is the risk of imperfect correlation between movements in the value of the derivative instrument and the value of the underlying investment or other asset being hedged. There is also the risk, especially under extreme market conditions, that an instrument, which usually would operate as a hedge, provides no hedging benefits at all.

Use of these instruments could also result in a loss if the counterparty to the transaction (particularly with respect to OTC instruments, such as swap agreements and forward currency contracts) does not perform as promised, including because of such counterparty's bankruptcy or insolvency. This risk may be heightened during volatile market conditions. Other risks include the inability to close out a position because the trading market becomes illiquid (particularly in the OTC markets) or the availability of counterparties becomes limited for a period of time. In addition, the presence of speculators in a *particular market could lead to price distortions. To the extent that the Master Fund is unable to close out a position because of market illiquidity, the Master Fund may not be able to prevent further losses of value in its derivatives holdings and the Master Fund's liquidity may be impaired to the extent that it has a substantial portion of its otherwise liquid assets marked as segregated to cover its obligations under such derivative instruments. The Master Fund may also be required to take or make delivery of an underlying instrument as a transaction that the investment manager would otherwise have attempted to avoid. Some derivatives can be particularly sensitive to changes in interest rates or other market prices. Investors should bear in mind that, while the Master Fund intends to use derivative strategies on a regular basis, it is not obligated to actively engage in these transactions, generally or in any particular kind of derivative, if the Investment Adviser of the Master Fund elects not to do so due to availability, cost or other factors.*

The use of derivative strategies may also have a tax impact on the Master Fund. The timing and character of income, gains or losses from these strategies could impair the ability of the Investment Adviser of the Master Fund to utilize derivatives when it wishes to do so."

D. Clarification on use of repurchase agreements and reverse repurchase agreements

To clarify the conditions under which the Master Fund may enter into repurchase or reverse repurchase agreements and to ensure the same is brought to your attention, the second to fourth paragraphs of the sub-section headed "Investment Techniques – Use of Repurchase/Reverse Repurchase Agreements" on page 12 of the Current Prospectus will be revised and restated as set out below. The relevant revisions are marked up for your ease of comparison.

"*The Master Fund may enter into repurchase or reverse repurchase agreements ("repo contracts") only in accordance with normal market practice and provided that collateral obtained under the repo contract is in the form of ~~(i)~~ cash or~~; (ii) government or other public~~ liquid securities and~~; (iii) certificates of deposit issued by a credit institution authorised in the European Economic Area (EEA) (European Union Member States, Norway, Iceland, Liechtenstein), a credit institution authorised by a signatory state, other than a Member State of EEA, to the Basle Capital Convergence Agreement of July 1988 (Switzerland, Canada, Japan, United States), or a credit institution authorised in Jersey, Guernsey, the Isle of Man, Australia or New Zealand, ("Relevant Institutions"); (iv) bonds/commercial paper issued by Relevant Institutions or by non-bank issuers where the issue and issuer are rated A1 or equivalent; (v) letters of credit with a residual maturity of three months or less, which are unconditional and irrevocable and which are issued by Relevant Institutions; or (vi) equity securities traded on a stock exchange in the EEA, Switzerland, Canada, Japan, the United States, Jersey, Guernsey, the Isle of Man, Australia or New Zealand.~~ complies with the following criteria: liquidity: collateral must be sufficiently liquid so that it can be sold quickly at a robust price that is close to its pre-sale valuation; valuation: collateral must be capable of being valued on at least a daily basis and must be marked to market daily; issuer credit qualify: where the collateral issuer is not rated A-1, or equivalent, conservative haircuts must be applied. Any incremental income generated from repo contracts will be accrued to the Master Fund. Investors should note that the Master Fund may utilise up to 100% of its assets for repo contracts.*

Until the expiry of a repo contract, the collateral obtained under such contract (a~~) must be marked to market daily; (b~~) must equal or exceed in value at all times the value of the amount invested or securities loaned by the Master Fund; (~~c~~b) must be transferred to the trustee of the Master Fund or its agent (except where the Master Fund uses tri-party collateral management services of International

Central Securities Depositaries and Relevant Institutions which are generally recognised as specialists in this type of transaction and the Master Fund's trustee is a named participant to the collateral arrangements); and (~~d~~c) must be immediately available to the Master Fund without recourse to the counterparty in the event of a default by that entity.

Non-cash collateral (i) cannot be sold or pledged by the Master Fund; (ii) must be held at the risk of the counterparty; ~~and~~ (iii) must be issued by an entity independent of the counterparty; and (iv) must be diversified to avoid concentration in any one country, sector or issue."

5. Disclosure in relation to Securities Lending Agent

For the purpose of clarification and to comply with legal and regulatory requirements, the following paragraph will be inserted immediately following the fifth paragraph of the sub-section headed "Investment Techniques – Lending of Portfolio Securities" on page 13 of the Current Prospectus:

"*To the extent that the Master Fund engages in securities lending it may appoint a securities lending agent which may receive a fee in relation to its securities lending activities. Any such securities lending agent is not expected to be an affiliate of the Depositary of the Master Fund or Investment Adviser of the Master Fund. Any operational costs arising from such securities lending activities shall be borne by the securities lending agent out of its fee.*"

The wording on the securities lending agent is being added for disclosure purposes to comply with applicable regulatory requirements and do not reflect any change to the fee structure of the Company. The additional disclosure on the securities lending agent will not result in any change in the fee levels and costs borne by the Company.

6. Revisions to the Investment Manager's Policy on Selection of Brokers and Dealers

To disclose changes to the Investment Manager's policy on the selection of brokers and dealers for the Company and the potential conflicts of interest that may arise from such policy, paragraph 16 of the sub-section headed "Management and Administration – The Directors" on page 27 of the Current Prospectus shall be deleted in its entirety and replaced by the following paragraph:

"*The Investment Manager may refer transactions for the Company's account to brokers or dealers that refer advisory clients to the Investment Manager or that recommend the purchase of shares of the Fund, provided that in each case, the Investment Manager reasonably seeks and believes the broker or dealer will provide best execution for the transaction. This practice may result in a potential conflict of interest between the Company's interest in obtaining best execution and the Investment Manager's interest in obtaining client referrals and selling additional Shares of the Company. A similar conflict of interest may arise when the Investment Manager causes transactions for the Company to be executed through brokers that provide research services to the Investment Manager and who may charge higher commissions than other brokers. The AIFM shall ensure that the identified potential conflicts of interest be managed and monitored pursuant to the AIFM's Conflicts of Interest Policy, including (where relevant) separate chains of command for, and information barriers between, persons responsible for selecting brokers or dealers and fund distribution personnel.*"

7. Adoption of a policy on equalisation payments by the Company

We wish to inform you of the adoption of a policy on equalisation payments by the Company.

From time to time, there may be subscriptions and/or redemptions in the Shares of the Company. Significant subscriptions or redemptions of relevant Shares during any month can give rise to a significant impact on the net investment income of the relevant class of Shares which would otherwise be available for distribution.

To protect Shareholders' interests from the effects of significant subscriptions or redemptions (as explained above), the Company may adopt a policy on equalisation payments with effect from 17 July 2014. The details of the policy, which will be added as a new paragraph immediately following paragraph 2 of the risk disclosure on "Dividend Distribution Policy of the Company" under the section headed "Risk Factors" on page 19 of the Current Prospectus, are as follows:-

> "*The Directors may from time to time, and in their sole discretion, determine that the Company shall apply an equalisation formula in respect to any relevant class of Shares for any month in which it is expected that significant subscriptions or redemptions of relevant Shares during that month might have a significant impact on the net investment income of the relevant class which would otherwise be available for distribution on the relevant Dividend Declaration Date. In such circumstances, the subscription price of the Shares in the relevant class will be deemed to include an equalisation amount which represents a portion of the accrued income of the relevant class up to the point of subscription, and the first distribution in respect of the Shares in the relevant class will include a payment of capital usually equal to the amount of such equalisation payment. The redemption price of each Share in the relevant class will also include an equalisation payment in respect of the accrued income up to the Dealing Day on which the relevant Shares are redeemed.*"

8. Disclosure in relation to Dividend Distribution Policy

We wish to inform you of the adoption of a policy on payment of dividends out of capital by the Company.

To disclose the Company's policy on the payment of dividends out of capital and the potential effect on the net asset value per share of the Company that may arise from such policy, the following paragraph shall be added as a new paragraph immediately following the last paragraph of the sub-section headed "Dividend Distribution Policy of the Company" on page 19 of the Current Prospectus:

> "*Subject to applicable legal and regulatory requirements, the Company may at its discretion pay dividends out of the capital of the Company. Investors should note that:-*
>
> *(i) payment of dividends out of capital amounts to a return or withdrawal of part of an investor's original investment or from any capital gains attributable to that original investment;*
>
> *(ii) any distributions involving payment of dividends out of the Company's capital (as the case may be) may result in an immediate reduction of the net asset value per share;*
>
> *(iii) the compositions of the dividends (i.e. the relative amounts paid out of (a) net distributable income and (b) capital) for the last 12 months are made available by the Hong Kong Representative on request and also on the Hong Kong Representative's website; and*
>
> *(iv) the Company may amend the policy with respect to such distribution policy subject to the SFC's prior approval and by giving not less than one month's prior notice to investors."*

The disclosures in this paragraph are made in compliance with the clarification published by the SFC regarding the requirements for disclosures on capital distribution by existing SFC-authorized funds.

As disclosed in the Company's financial statements, the Company has been making income equalization adjustments for calculating its net distributable assets. According to the abovementioned clarification published by the SFC, the Company is required to determine the composition of its dividend payment without making such adjustments and is thereby considered as paying dividend out of its capital. As a result, the Company is required to amend the Current Prospectus to include the disclosures in this paragraph.

Please be assured that the disclosures in this paragraph will not bring any negative impact on the shareholders of the Company.

9. <u>Measures to restrict or prevent the ownership of shares by Prohibited Persons</u>

The Company may need to restrict or prevent its Shares from being owned by a person, firm or corporate body in cases where (in the opinion of the Company) such ownership may be detrimental to the Company or its shareholders, may result in a breach of any applicable law or regulations or may expose the Company or its Shareholders to liabilities or any other disadvantages that it or they would not have otherwise incurred or been exposed to. Such persons, firms or corporate bodies are herein referred to as "Prohibited Persons".

To protect the Company and its Shareholders from the detrimental effects of ownership of Shares by Prohibited Persons, the Company will adopt measures in order to restrict or prevent the ownership of Shares of the Company by Prohibited Persons. The measures are intended to protect existing Shareholders of the Company who are not Prohibited Persons, and are not expected to have an adverse impact on the holdings of such Shareholders.

A summary of the measures (which will also be disclosed in the Current Prospectus) is provided below:-

> "***PROHIBITED PERSONS***
>
> *The Company may restrict or prevent the ownership of Shares by any person, firm or corporate body if in the opinion of the Company such holding may be detrimental to the Company or its Shareholders, may result in a breach of any applicable law or regulations or may expose the Company or its Shareholders to liabilities or any other disadvantages that it or they would not have otherwise incurred or been exposed to. Such persons, firms or corporate bodies are herein referred to as "Prohibited Persons".*
>
> *The actions that the Company may take in order to restrict or prevent the ownership of Shares by Prohibited Persons include (in summary):*
>
> *1) declining to issue Shares and/or register transfers of Shares;*
>
> *2) requiring the furnishing of representations and warranties and/or information, supported by affidavit;*
>
> *3) redeeming all or part of the Shares held by a relevant Shareholder; and*
>
> *4) declining to accept the vote of any Prohibited Person at any meeting of Shareholders of the Company.".*

* * * * * *

The Directors of the Company accept full responsibility for the accuracy of the information contained in this letter as at the date of its publication and confirm, having made all reasonable enquiries, that to the best of their knowledge and belief there are no other facts the omission of which would make any statement misleading.

If you require further information please do not hesitate to contact your investment consultant or call our Investor Hotline at +852 2805 0111.

Yours faithfully,

For and on behalf of
Franklin Templeton Investments (Asia) Limited (富蘭克林鄧普頓投資(亞洲)有限公司)

David Chang
Director