

# ClearBridge Opportunity Portfolios

John Goode and Peter Hable  
Senior Portfolio Managers

## Market overview

Over the next six months we expect economic surprises to be on the upside. Gross domestic product ("GDP")<sup>1</sup> may grow by 4%, well above consensus, and job growth could average 100,000-125,000 per month. Inventory levels in many industries have been cut to the bone, and any improvement in the economy could lead to production increases to refill them. Capital expenditures in many sectors have been cut severely. Economic improvement almost certainly will lift capital expenditure levels materially, another factor that could cause economic growth to surprise on the upside.

The Opportunity Portfolio normally has a larger proportion of smaller-cap companies (less than \$2 billion) than it does currently. This is because larger companies appear to be as attractive as at anytime in the last three decades. In addition, many of these companies are multi-national and derive 40% or more of revenues and even higher percentages of their profits from abroad, including emerging markets.

## Opportunity Portfolios - Retail

### Annualized returns gross and net of fees (%) as of December 31, 2009

	Q409	YTD	1-yr	3-yr	5-yr	7-yr	10-yr
Net of fees	-2.28	54.55	54.55	-4.41	0.48	9.35	8.12
"Pure" gross of fees	-1.55	59.04	59.04	-1.52	3.50	12.61	11.36
Russell 3000 Index	5.90	28.34	28.34	-5.42	0.77	6.21	-0.20
Russell 2000 Index	3.87	27.17	27.17	-6.07	0.51	8.65	3.51

For additional performance information please see the GIPS® Performance Endnotes at the end of this document. Quarterly and YTD numbers are not annualized. **Past performance is no guarantee of future results.**

The Opportunity Portfolio had an excellent 2009, appreciating 59.04% (gross of fees) vs. The Russell 3000 advance of 28.34%. However, the fourth quarter saw the account decline a modest -1.55% (gross of fees), whereas the Russell 3000 advanced 5.90%. The Opportunity Portfolio holds a number of smaller, lower-priced stocks that did extraordinarily well between March and September. Over the last three months of the year, many of these stocks consolidated or corrected somewhat. A \$0.50 correction in a lower-priced stock can have a substantial percentage effect even though the yearly appreciation might still be substantial.

After a stellar six months of performance through September 30, our financials, industrials and technology holdings were distinct underachievers, subtracting approximately 3.4% from performance during the quarter. We continue to believe our holdings in these sectors will outperform in the coming quarters.

## Outlook

In order to participate fully in the economic strength we anticipate in coming quarters, our sector emphasis will focus on financials, information technology, industrials, energy, and materials. We are always alert for emerging themes and trends that bode well for companies in a particular area of the stock market. We believe nuclear energy will be an important new theme in 2010. Nuclear energy has been a "pariah" in the United States since the problems at Three Mile Island in 1979. Increased nuclear power generation in this country would reduce dependence on foreign sources, limit carbon emissions, and provide a new source of domestic employment. In the last month we have added two companies we believe could be beneficiaries should nuclear power become a more important source of future power generation in this country.

The president's "State of the Union" address later in January will be important for a number of reasons, including its psychological impact. Many investors continue to be risk averse, which is reflected in individual investors putting nine

<sup>1</sup> Gross domestic product ("GDP") is the market value of all final goods and services produced within a country in a given period of time.

## ClearBridge Opportunity Portfolios

times as much money in bond funds in 2009 as they placed in equities. With more than \$3 trillion still residing in money market funds, any improvement in confidence could cause much more interest to develop in common stocks.

If we are correct about a stronger economy in the coming quarters, it would not be surprising if the U.S. dollar rallied. Although the U.S. economic prospects might still trail those of the emerging markets, they could be considerably more robust than those in Europe and Japan. A stronger dollar would be a magnet for capital flows into U.S. assets.

The bottom line is this: A number of things could improve at a faster rate than expected in the next few quarters. We expect to capture “upside surprise” through our positioning of Opportunity assets.

## ClearBridge Opportunity Portfolios

All opinions and data included in this market commentary are as of the date indicated and are subject to change. The opinions and views expressed herein are those of the portfolio managers specified and may differ from those of other managers or the firm as a whole, and they are not intended to be relied upon as a prediction or forecast of actual future events or performance, or a guarantee of future results, or investment advice. The information contained should not be used as the sole basis to make any investment decisions. The statistics have been obtained from sources believed to be reliable, but the accuracy and completeness of this information cannot be guaranteed. Securities referenced should not be construed as a solicitation or recommendation or be used as the sole basis for any investment decision.

All investments involve risk, including possible loss of principal amount invested. Please refer to [www.leggmason.com/individualinvestors](http://www.leggmason.com/individualinvestors) for more information about the portfolio including objective, risks and investment process. The information presented does not constitute and should not be construed as investment advice with respect to any investment discussed. There is no guarantee that investment objectives will be met. An investor cannot invest directly in an index. Investments are not FDIC insured or guaranteed by any government agency. Values may fluctuate due to market conditions and other factors. **Past performance is no guarantee of future results.**

### Risks

Substantial investments may be made in speculative and/or small-cap and mid-cap companies which involve a higher degree of risk and volatility than investments in larger, more established companies. In addition, because the investments may be concentrated in a limited number of industries and companies, the portfolios may involve heightened risk. Investments may also be made in ADRs and U.S.-traded ordinary shares of non-U.S. companies in developed and emerging markets which involve risks in addition to those

ordinarily associated with investing in domestic securities, including the potentially negative effects of currency fluctuations, political and economic developments, foreign taxation and differences in auditing and other financial standards. These risks are magnified in emerging markets.

### Index/term definitions

The Russell 2000 Index measures the performance of the small-cap segment of the U.S. equity universe. The Russell 2000 Index is a subset of the Russell 3000® Index representing approximately 10% of the total market capitalization of that index. It includes approximately 2000 of the smallest securities based on a combination of their market cap and current index membership.

The Russell 3000 Index measures the performance of the 3,000 largest U.S. companies based on total market capitalization, which represents approximately 98% of the U.S. equity market.

Professional money management may not be suitable for all investors.

©2010 Legg Mason Investor Services, LLC. member SIPC.

Client portfolios are managed based on investment instructions or advice provided by one or more of the following Legg Mason-affiliated investment management firms, as indicated in portfolio names or otherwise: ClearBridge Advisors, LLC, Western Asset Management Company, Brandywine Global Investment Management, LLC, Global Currents Investment Management, LLC and Legg Mason Capital Management, Inc. ("LMCM"). Management is implemented by Legg Mason Private Portfolio Group, LLC or, in the case of certain programs, by the program sponsor or its designee.

FN1010230

**ClearBridge Opportunity Portfolios – GIPS® endnotes (\$USD) — ending December 31**

**Inception date: January 2006**

**Composite creation date: June 2008**

Period	Total return net(%)	Total return (*pure gross)	Russell2000 return (%)	No. of portfolios	% of bundled fee portfolios in the composite	Composite dispersion (%)	Total composite assets at end of period (USD million)	% of firm assets	Total firm assets at end of period (USD million)
2008	-46.44	-44.74	-33.79	280	100	1.68	74.2	0.1	50,615
2007	5.53	8.68	-1.57	294	100	0.92	171.0	0.4	47,112
2006	12.83	16.18	18.37	302	100	0.81	140.0	0.3	54,078
2005	3.92	7.03	4.55	245	100	0.61	-	-	-
2004	14.16	17.55	18.33	220	100	0.62	-	-	-
2003	59.88	64.50	47.25	260	100	1.82	-	-	-
2002	-24.05	-21.58	-20.48	272	100	1.82	-	-	-
2001	3.90	7.04	2.49	260	100	1.67	-	-	-
2000	48.06	52.09	-3.02	253	100	2.49	-	-	-
1999	28.99	32.64	21.26	283	100	2.59	-	-	-
1998	-9.88	-7.08	-2.55	452	100	1.81	-	-	-

\*Pure gross of fee returns do not reflect the deduction of any expenses, including certain transaction costs, and are presented as supplemental to the net of fee returns.

ClearBridge Advisors (also referred to as "CBA") has prepared and presented this report in compliance with the Global Investment Performance Standards ("GIPS®").

For purposes of compliance with GIPS, the "firm" is defined as ClearBridge Advisors, which encompasses all assets managed or advised on a discretionary or non-discretionary basis by ClearBridge Advisors, LLC and ClearBridge Asset Management Inc (collectively, "ClearBridge Advisors"). In June 2008, ClearBridge Advisors combined its separate institutional and retail firms to form a single GIPS firm, CBA. The two predecessor firms were "ClearBridge Advisors Institutional" and "ClearBridge Advisors Retail". ClearBridge Advisors Institutional ("CBA-Inst") encompassed ClearBridge Advisors' mutual fund and other collective investment vehicle businesses and separately managed accounts contracted directly with ClearBridge Advisors. ClearBridge Advisors Retail ("CBA-Retail") was created in 2008 and encompassed separately managed accounts for which ClearBridge Advisors served as sub-advisor under sponsored programs ("retail separately managed accounts"). CBA-Retail's claim of GIPS compliance is effective as of January 2006. In accordance with GIPS, CBA-Retail's historical performance returns prior to January 2006 are presented as non-compliant information. The ClearBridge Advisors entities are wholly-owned subsidiaries of Legg Mason, Inc. ("Legg Mason") and are not affiliated with Citigroup Inc. ("Citigroup").

For the institutional business only, CBA-Inst's predecessor "firm" for GIPS purposes was CAM Institutional ("CAM-NA"). CAM-NA encompassed assets managed by North America-based units of Citigroup Asset Management ("CAM"), the worldwide asset management business of Citigroup that was conducted through various subsidiaries of Citigroup on behalf of certain of its institutional, mutual fund and other collective investment vehicle clients. The CAM-NA "firm" definition was substantially similar to the "firm" definition of CBA-Inst. On December 1, 2005, Citigroup completed the sale of CAM, including CAM-NA, to Legg Mason. In connection with the transaction, ClearBridge Advisors became the manager of a significant portion of the institutional, mutual fund and other collective investment vehicle accounts, including most active equity accounts that were managed by CAM-NA up until the date of the Citigroup-Legg Mason transaction. Assets that were not transitioned to ClearBridge Advisors in connection with the transaction (particularly fixed income and quantitative equity assets) transitioned to other Legg Mason affiliates that were not part of CBA-Inst. Prior to January 2001, CAM maintained three separate AIMR (the predecessor to GIPS) firms. These firms were combined to form CAM-NA effective January 2001.

For the retail separately managed account business only, the performance returns prior to January 2006 represent a composite of accounts from a formerly-affiliated sponsor channel, which historically represented an overwhelming majority of the strategy's retail assets under management. The aforementioned composite returns were calculated on an equal weighted basis, where each portfolio contributed an equal weight to the resulting composite return for the period. As such and in accordance with GIPS, the historical performance returns prior to January 2006 are presented as non-

compliant information. Total firm assets for years ending 2006 and 2007 represent the CBA-Retail firm.

**Composite description**

The ClearBridge Opportunity Account consists of fully discretionary accounts with a minimum net asset value of US \$25,000 (prior to June 2008 the minimum was \$5,000). "Sleeves" of multi-style portfolios and segments of balanced accounts are excluded. Accounts within the composite seek to maximize capital gains. Portfolios may include large, mid and small cap companies, as well as ETFs. When deemed justified by the portfolio managers, substantial cash reserves may be held in accounts, rather than fully investing in stocks.

New accounts enter the composite during the third full month under management. Accounts with external cash flows during a month that are equal to or greater than 10% of an account's market value will cause that account to be excluded from the composite during the month in which the flows occurred. Accounts will be added back to the composite in the following month. Closed accounts are included in the composite rate of return calculations through the completion of the last full month under management. All accounts are valued at calendar month end based on principal market values plus cash and cash accrued income. Account returns are calculated in U.S dollars and utilize the Daily Time Weighted methodology. The composite's monthly rates of return are the asset-weighted averages of the accounts' monthly results, which are then linked to determine the composite's quarterly and annual returns.

Net of fee composite returns are calculated by reducing each monthly composite pure gross rate of return by the highest "bundled" fee charged (3.00%) annually, prorated to a monthly ratio. The "bundled" fee includes transaction costs, investment management, custodial, and other administrative fees. Pure gross returns shown do not reflect the deduction of "bundled" fees and are presented as supplemental information to net returns. Account quarterly and annual returns are calculated by linking individual monthly returns.

Composite dispersion measures represent the consistency of a firm's composite performance results with respect to the individual account returns within a composite. CBA utilizes the Equal-Weighted Standard Deviation measure of dispersion. Only accounts that have been managed within the composite style for a full year are included in the Equal-Weighted Standard Deviation calculation.

No alteration of composites has occurred because of changes in personnel or other reasons at any time. Any material change in the status of an account resulted in the removal of the account from the composite.

Leverage has not been used in any of the accounts included in the composite.

**Composite benchmark description**

The Russell 2000 Index measures the performance of the small-cap segment of the U.S. equity universe. The Russell 2000 Index is a subset of the Russell 3000® Index representing approximately 10% of the total market capitalization of that index. It includes approximately 2000 of the smallest securities based on a combination of their market cap and current index membership