2Q 2017 | Product Commentary

CLEARBRIDGE VALUE TRUST

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Portfolio Managers

Average annual total returns and fund expenses (%)

as of June 30, 2017

Class C	3-mo	1-yr	5-yr	10-yr	Since Incept. (04/16/82)	Gross	Net
Excluding sales charges	1.99	18.99	13.82	1.57	11.65	1.77	1.77
Including effects of maximum sales charges	1.04	18.04	13.82	1.57	11.65	-	-
S&P 500 Index	3.09	17.90	14.63	7.18	N/A	-	-

Performance shown represents past performance and is no guarantee of future results. *Current performance may be higher or lower than the performance shown. Investment return and principal value will fluctuate, so shares, when redeemed, may be worth more or less than the original cost. Class C shares have a one-year contingent deferred sales charge (CDSC) of 0.95%. If sales charges were included, performance shown would be lower. Total returns assume the reinvestment of all distributions at net asset value and the deduction of all Fund expenses. Total return figures are based on the NAV per share applied to shareholder subscriptions and redemptions, which may differ from the NAV per share disclosed in Fund shareholder reports. Performance would have been lower if fees had not been waived and/or reimbursed in various periods. Returns for less than one year are cumulative. Performance for other share classes will vary. For the most recent month-end information, please visit www.leggmason.com*

Gross expenses are the Fund's total annual operating expenses for the share class(es) shown.

Net expenses are the Fund's total annual operating expenses for the share classes indicated and would reflect contractual fee waivers and/or reimbursements, where these reductions reduce the Fund's gross expenses. These arrangements cannot be terminated prior to December 31, 2018 without the Board’s consent. In periods of market volatility, assets may decline significantly, causing total annual Fund operating expenses to become higher than the numbers shown in the table above.

S&P 500 Index is a market capitalization-weighted index of 500 widely held common stocks. Investors cannot invest directly in an index, and unmanaged index returns do not reflect any fees, expenses or sales charges.

Key takeaways

- Economic data released or updated during the quarter continued to paint a fairly robust picture of the U.S. economy.
- Given our valuation-driven investment process, we believe that good relative and absolute returns come from finding stocks where realized expectations can exceed embedded expectations.
- In all markets, a little lack of love can go a long way in surfacing mispriced opportunities, but you have to have the process discipline to correctly frame an argument that intelligently counters the crowd’s narrative.

Market overview

Major U.S. equity indices continued their record-breaking run in the second quarter, as the S&P 500 Index gained 3.1% during the period. Challenges in implementing health care reform and investigations into the Trump campaign have slowed the Republican agenda, diminishing expectations of Congress passing stimulative fiscal policies that could be market catalysts. Nevertheless, markets have continued to gain on solid earnings reports, the administration’s business-friendly regulatory approach, and reasonably firm economic data. The health care, industrials, financials and information technology (IT) sectors led the market during the quarter, while telecommunication services (telecom) and energy lagged for a second consecutive quarter.

Economic data released or updated during the quarter continued to paint a fairly robust picture of the U.S. economy, providing the equity markets with enough fuel to move higher. First quarter annualized GDP growth was revised up from 1.2% in the Commerce Department's second estimate in May to 1.4% in its final reading in June. While still a relatively weak number, many investors view the first quarter as a short-term aberration, with expectations that second quarter annualized GDP growth will be higher, particularly with rising wages and an economy largely at full employment. June non-farm payroll gains came in at 222,000 and revisions to April and May data added 47,000 jobs, according to the Labor Department. Meanwhile, the unemployment rate continues to remain at low levels, registering 4.4% in the latest measurement; and average hourly earnings growth came in at 2.5% in June, slightly less than expected. Employment and GDP data point to a relatively strong economy that should remain self-sustaining in the near term. With economic and labor market conditions generally strong, the Federal Reserve implemented its second rate hike of the year and provided some guidance for investors on its long-expected balance sheet reduction.

U.S. 10-year Treasury yields were modestly lower, ending the quarter at 2.3%. After peaking in late 2016, the U.S. dollar, as measured by the DXY, continued its slide in the second quarter, falling 4.7% during the period. A weaker dollar should be a tailwind for U.S. multinationals translating profits generated outside the U.S. into dollars. On the commodities front, oil prices continued to exhibit volatility. WTI crude slid to $46.04 at the end of the quarter from $50.60 at the end of March.

The S&P 500 Index closed up 3.1%, while the Dow Jones Industrial Average gained 4.0%. Small-cap stocks underperformed large-caps during the quarter, with the Russell 2000 returning 2.5% versus 3.1% for the Russell 1000. Looking at investment style, growth-oriented stocks outperformed their value counterparts, as the Russell 1000 Value Index returned 1.3% vs. the Russell 1000 Growth's 4.7% during the second quarter.

Fund highlights

During the second quarter of 2017, the ClearBridge Value Trust – Class C shares generated a total return of 1.99%, excluding sales charges. In comparison, the Fund's unmanaged benchmark, the S&P 500 Index, returned 3.09% and the Lipper Multi-Cap Core Funds category average was 2.77% for the same period.

On an absolute basis, seven of the 10 sectors in which the Fund was invested in for the second quarter generated positive returns (out of 11 sectors total). The information technology (IT), financials and health care sectors contributed the most to absolute returns, while the energy sector detracted the most.

Relative portfolio underperformance was driven by stock selection effects, which were partially offset by sector allocation. Stock selection in the consumer discretionary, health care and industrials sectors detracted the most from relative returns. Meanwhile, stock selection in the IT sector and an underweight (no positions) in the telecommunication services sector contributed the most to relative performance for the second quarter.

Oracle, Calpine, Alphabet, Citigroup and Amazon.com were the largest contributors to performance, while the biggest detractors included Synchrony Financial, Devon Energy, AutoZone, Adient and Cisco Systems.

During the second quarter we initiated five new positions: AutoZone, Molson Coors Brewing Company, Pioneer Natural Resources, ServiceMaster Global and TransDigm Group. Four positions were eliminated: Coty, Colgate-Palmolive, PACCAR and Boeing.

Top contributors

Shares of Oracle, which provides products and services for the corporate IT ecosystem, continued their rise in the second quarter, as the company has shown progress in successfully managing its cloud transition. While it is still early innings for Oracle, the company has shifted business to the cloud at a similar rate to Microsoft at a similar point in its transition cycle, and at a faster rate than Adobe, which is perhaps the most successful example of a software provider transitioning to cloud delivery. While Oracle's cloud business is still small relative to its legacy business, the cloud business is large enough and growing fast enough to positively impact earnings. We are positive on the company's transition and products, and anticipate faster adoption of its cloud delivery platform in the near future.

Calpine is a cash-generative unregulated natural-gas utility that had been trading at low levels not seen since the financial crisis. We view the stock as being at a major valuation discount from the market and its own history, but shares jumped in May on news that Calpine may be exploring a sale. The company traditionally benefits when there is high demand and power spikes, but the market has seen excess supply and a lack of power spikes. Yet, Calpine is staying active by using its free cash flow to pay down debt and buy back stock; and we believe that as natural gas prices continue to rise, Calpine should benefit. The company could make a strong takeover target for private equity firms, which could generate attractive returns, given Calpine's high free cash flow yield. We will continue to evaluate the stock's upside, given the possibility of an acquisition and keeping in mind the natural gas supply-demand situation.

Citigroup, one of the largest U.S. money center banks, was a top-performing stock during the second quarter after the company reported strong financial results from the prior quarter and passed the Fed's latest CCAR stress test, which will allow the company to return more capital to shareholders. Citi reported better-than-expected capital markets activity, and it continues to make progress on efficiency and boosting operating leverage. Its international consumer banks have also been performing reasonably well. Additional tailwinds for Citi and other U.S. banks may materialize if industry deregulation is pushed through Congress, and as economic activity picks up and interest rates rise, supporting net interest margin expansion.

Top detractors

Consumer lender Synchrony Financial underperformed the market during the second quarter after lowering credit guidance and on investor worries about a retail-industry slowdown (Synchrony manages credit cards for department stores and other retail outlets). Synchrony may also have been negatively impacted by the market's declining expectations of tax reform being implemented this year, as the company would be a major beneficiary of corporate tax cuts and reform. We believe Synchrony's share price is still well below business value. Additionally, Synchrony has ample excess capital that will allow them to pay out 100% or more of earnings to shareholders for years and grow at a substantial premium to the industry, according to our analysis. Furthermore, our analysis shows there is no relationship between department store sales and Synchrony's loan growth, as Synchrony's growth has accelerated while retailers have struggled. We remain positive on the stock, which is currently one of our highest-conviction names in the financials sector.

Devon Energy traded down in the second quarter on broader commodity price decreases and expectations for larger U.S. crude inventories for the foreseeable future. The company itself continues to improve operationally, and asset sales have helped reduce leverage, and thus alleviate some of the market's concerns of financial distress. Furthermore, management expects meaningful growth this year and into 2018, as they redeploy rigs and increase drilling inventory modestly. While oil prices are likely to remain contained in the near term, the stock at present embeds a reasonable WTI crude price level; and combined with Devon's exposure to the STACK formation, there should be meaningful upside in the stock over the longer term.

Adient, the auto-seat maker spun off from Johnson Controls in October of last year, pulled back from recent highs as concerns about the auto sales cycle in North America caused investors to rotate away from auto stocks more broadly. As a spinoff, the risk of near-term volatility in the stock was high, but from a fundamental perspective, the pullback appears to be overdone. North America represents only a portion of its exposure, with Europe and China being major markets for the company where sales weakness is not expected anytime soon. Adient's opportunities to continue its margin expansion should allow the company to successfully weather relative weakness in North America.

Outlook

The current late-cycle market has revealed two major challenges for active investors: the first is to avoid what is loved and a huge part of the index, which requires behavioral fortitude, and the second is to find value in an environment where most assets and stocks are infected by elevated expectations. Given our valuation-driven investment process, we believe that good relative and absolute returns come from finding stocks where realized expectations can exceed embedded expectations, and capital's growing love for assets and stocks has greatly narrowed the list of attractive candidates. The resulting lack of broad opportunities has created a needle-in-the-haystack market, but that is a great opportunity for truly active managers, like us, to prove our worth.

On the first challenge, we are underweight tech and the so-called FAANG stocks (Facebook, Amazon, Apple, Netflix and Google (Alphabet)), as well as the also-loved bond-proxy stocks that have benefitted from record-low interest rates. The narrative in favor of deflation and extrapolating low rates well into the future is back in full force, after a brief respite as the election-induced hopes of reflation melted away. During the middle of the quarter when capital really flooded into the FAANG stocks and bond proxies, our relative performance suffered, but we were able to gain much of this relative drop back later in the quarter. To be clear, we still own some tech stocks where we believe innovation can extend scaling advantages, and where business values remain above rising prices. However, if exuberance continues to build, our tech and FAANG weighting will keep declining, creating a bigger active gap between our portfolio and the index. We will take near-term relative pain to avoid absolute losses down the road.

On the second challenge, we are still finding mispriced stocks that are either being too aggressively sold by the crowd or are simply being left without the support of the crowd enamored by the FAANGs and the almighty index. In the aggressive crowd selling category, we initiated positions in AutoZone, Molson Coors, Pioneer Natural Resources and Transdigm Group near recent 52-week price lows. In the neglected category, we initiated a position in ServiceMaster Global. In each case, our bottom-up analysis supports business values higher than current prices, assuming reasonable fundamental outcomes, and decent downside support if we are wrong and a nightmare scenario develops. Each stock has a narrative that supports the downside move, but we obviously disagree with all or part of the negative story, or we believe the bad news is more than fully baked into the stock price. Most importantly, none of these companies is in the junk pile, where value investors often get burned hunting for broad opportunities late in market cycles. Even the capital-intensive and oil price-taking Pioneer has an opportunity to generate reasonable returns and actual free cash flow, as it fully exploits its high-quality and extremely low-cost resource base.

In all markets, a little lack of love can go a long way in surfacing mispriced opportunities, but you have to have the process discipline to correctly frame an argument that intelligently counters the crowd’s narrative. As an example, our investment process led us to be heavy buyers of tech stocks, including some of the FAANGs, earlier in this market cycle when Cupid had not yet shot his arrow. At the current stage of the market cycle, however, love for assets is continuing to deepen and capital is freely flowing. When this torrent of capital is widely embracing what is most loved and the blind appeal of indexes, our active approach and investment process discipline is more important than ever.

Top 10 equity holdings (%)	
Alphabet Inc	4.6
Oracle Corp	4.0
Wells Fargo & Co	3.5
Microsoft Corp	3.5
Synchrony Financial	3.4
Citigroup Inc	3.4
Allergan PLC	3.3
Realogy Holdings Corp	3.1
Amazon.com Inc	3.1
Alexion Pharmaceuticals Inc	2.8

Sector allocation (%)	
Financials	18.3
Information Technology	17.4
Consumer Discretionary	16.7
Health Care	16.1
Industrials	9.5
Energy	7.2
Utilities	6.6
Real Estate	4.8
Materials	1.6
Consumer Staples	0.9
Telecommunication Services	0.0
Cash/Other	0.9

Percentages are based on total portfolio as of quarter end and are subject to change at any time. For informational purposes only and not to be considered a recommendation to purchase or sell any security.

Definitions and additional terms:

Please note that an investor cannot invest directly in an index, and unmanaged index returns do not reflect any fees, expenses or sales charges.

Category Average Returns' Source: Lipper Inc. **Past performance is no guarantee of future results.** Lipper returns are based on the three-month period ended June 30, 2017, and they are calculated among 790 funds in the Lipper Multi Cap Core peer group, including reinvestment of dividends and capital gains, if any, and excluding sales charges.

Dow Jones Industrial Average (DJIA) is an unmanaged index composed of 30 blue-chip stocks, each with annual sales exceeding $7 billion. The DJIA is price-weighted, reflects large-cap companies representative of U.S. industry, and historically has moved in tandem with other major market indexes, such as the S&P 500.

The **U.S. dollar index (DXY)** is a measure of the value of the U.S. dollar relative to the value of a basket of currencies of the majority of the United States' most significant trading partners.

FAANG is an acronym for the five most popular and best-performing tech stocks in the market, namely Facebook, Apple, Amazon, Netflix, and Alphabet's Google.

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.

Gross Domestic Product (GDP) is an economic statistic that measures the market value of all final goods and services produced within a country in a given period of time.

S&P 500 Index is an unmanaged index of 500 stocks that is generally representative of the performance of larger companies in the U.S.

Treasury yield is the return on investment, expressed as a percentage, on the U.S. government's debt obligations (bonds, notes and bills).

U.S. Treasuries are backed by the "full faith and credit" of the United States government and offer return of principal value if held to maturity. The U.S. government guarantees the principal and interest payments on U.S. Treasuries when the securities are held to maturity.

Russell 1000 Index measures the performance of the 1,000 largest companies in the Russell 3000 Index, which represents approximately 92% of the total market capitalization of the Russell 3000 Index.

Russell 1000 Growth Index is an unmanaged index of those companies in the large-cap Russell 1000 Index chosen for their growth orientation.

Russell 1000 Value Index is an unmanaged index of those companies in the large-cap Russell 1000 Index chosen for their value orientation.

Russell 2000 Index is composed of the 2,000 smallest companies in the Russell 3000 Index.

West Texas Intermediate (WTI) is light, sweet crude oil, which is commonly referred to as "oil" in the Western world.

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Clarion Partners
ClearBridge Investments
EnTrustPermal
Martin Currie
QS Investors
RARE Infrastructure
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Equity securities are subject to price fluctuation and possible loss of principal. International investments are subject to special risks, including currency fluctuations and social, economic and political uncertainties, which could increase volatility. These risks are magnified in emerging markets. The manager's investment style may become out of favor and/or the manager's selection process may prove incorrect, which may have a negative impact on the Fund's performance. Because this Fund expects to hold a concentrated portfolio of securities, and invests in certain regions or industries, it has increased vulnerability to market volatility.

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Portfolio holdings and sector allocations may not be representative of the portfolio manager's current or future investment and are subject to change at any time.

Percentages are based on total portfolio as of quarter end and are subject to change at any time. For informational purposes only and not to be considered a recommendation to purchase or sell any security.

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