2Q 2019 | Product Commentary

QS
GLOBAL MARKET NEUTRAL FUND

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Average annual total returns and fund expenses (%)

as of June 30, 2019

Class A	3-mo	1-yr	5-yr	10-yr	Since Incept. (11/30/15)	Expenses Gross	Expenses Net
Excluding sales charges	-2.73	-3.55	N/A	N/A	-0.36	3.42	3.16
Including effects of maximum sales charges	-8.29	-9.10	N/A	N/A	-1.99	3.42	3.16
FTSE 3-Month U.S. Treasury Bill Index	0.61	2.30	N/A	N/A	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 A shares reflect a maximum front-end sales charge of 5.75%. 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. 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, 2020 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.

The FTSE 3-Month U.S. Treasury Bill Index represents monthly return equivalents of yield averages of the last 3-month Treasury bill issues. Please note that an investor cannot invest directly in an index, and unmanaged index returns do not reflect any fees, expenses or sales charge.

Market overview

The MSCI All Country World Index returned 3.8% in U.S. dollar terms for the second quarter of 2019, with all regions posting positive returns. However, global equity markets were quite volatile. The quarter started with a strong rally in April, only to sharply decline in May and rebound dramatically in June. The risk-on/risk-off theme that has dominated financial markets over the past few years was also pervasive during the quarter, as most risky assets appreciated dramatically in April and June but exhibited dismal performance during May. Although risk assets posted generally positive returns for the quarter, gold (typically considered a flight-to-quality asset) rose 9.3%, propped up by the weaker U.S. dollar, a dovish U.S. Federal Reserve and geopolitical concerns. The shifts in investor sentiment were propelled by the perception of a number of risks, including an escalation in the U.S.-China trade tariff war, uncertainty around Brexit, an inversion of the yield curve in the U.S., and soft global growth. These risks overshadowed several sources of investor optimism, which included a pivot to accommodative monetary policies by major central banks, positive economic data, and a post-G20 meeting "tariff freeze" agreement between the U.S. and China.

U.S. equities had a positive quarter, slightly outperforming the index overall with a return of 4.3%. With the exception of energy, which was roiled by volatility in oil prices during the quarter, all sectors posted positive returns. Financials ex banks, banks and materials were the best-performing sectors, while energy, health care and real estate were the laggards. After the Fed meeting in June, Chairman Jerome Powell's comments were perceived as dovish, and the "dots" projections showed that seven policymakers are forecasting 50 basis points of cuts by year end. The projected rate cuts, along with weak U.S. ISM manufacturing data and U.S. non-farm payrolls data, led to the U.S. 10-year yield dropping below 2%.

Continental Europe was the best-performing major region, returning 6.2%. The top-performing sectors were consumer discretionary, information technology and industrials. Real estate, energy and banks were the bottom performers. The European Central Bank (ECB) announced that it will likely keep interest rates unchanged until mid-2020, and it did not rule out future interest rate cuts. European economic data were mixed.

The U.K. had the poorest performance among the regions, with a 0.9% return for the quarter and a wider range of sector returns: the information technology sector was the top performer, returning 8.9%, and real estate was the worst one, with a -5.2% return. While the postponement of Brexit to October 31, 2019 initially led to improved business sentiment and business expansion, uncertainty and fear over a no-deal Brexit continues to impact business activity and equity markets.

Japanese equities underperformed other major regions during the quarter, returning 1.0%, primarily as a result of weakness in May. U.S.-China trade tensions have a direct impact on the Japanese market, as Japanese companies supply many of the electronic components for Huawei. Economic data were mixed for the quarter, with GDP beating consensus expectations. The Bank of Japan left monetary policy unchanged.

Of the smaller regions, resource-based Australia, Canada & New Zealand was the top performer in the index, with a 6% return. Asia Developed ex-Japan had a more modest return of 2.5%.

Emerging markets equities underperformed developed markets while remaining modestly positive for the rest of the quarter. The gap between the developed and emerging market remains notable for 2019 year to date, with the MSCI World Index returning 17% and MSCI Emerging Markets Index 10.6%. Across sectors, financials was the top performer, returning 4.0%; the worst performer was health care, with a return of -6.6%. Argentina (a new addition to the index), Russia and Greece were top performers with double-digit returns, while Pakistan, Chile and Hungary were the worst performers. China was the fourth-worst-performing market, impacted by global trade uncertainty and the mutual increase in tariffs on imported goods. Hopes for a resumption in U.S.-China trade talks and an easing of the trade tariffs following the G20 summit triggered a rebound in Chinese equities in June, up 8.0%.

Fund highlights

The Fund's Class A share underperformed (excluding sales charges) its benchmark in the second quarter of 2019. Stock selection detracted from value across most regions and sectors, especially in continental Europe and the U.S. From a sector perspective, the materials sector was the largest detractor, and that was somewhat offset by strong selection results in industrials. A positive exposure to the energy sector also detracted from relative return.

Outlook

Growth expectations have remained low, and as a result, central banks continue to hint toward more expansionary policies. The U.S. Federal Reserve "dot plot" shows that seven policymakers are forecasting a 50-basis-points cut by year end. In Europe, the ECB will likely keep interest rates unchanged until mid-2020, but it has not ruled out cuts. There is renewed optimism after the U.S. and China meeting at the G20 summit; the U.S. and China agreed to a cease-fire on the trade war, as the U.S. will ease restrictions on Huawei, and it indefinitely postponed tariff increases on Chinese goods. While interest rate differentials and political uncertainty are still cause for concern, we believe that our well-diversified, disciplined strategy is positioned to benefit in this environment.

Top 10 equity holdings - long (%)	
Deckers Outdoor Corp	0.8
Air Canada	0.7
YUM! BRANDS INC	0.7
ASML Holding	0.7
AUTO TRADER GROUP PLC	0.7
ARTIS REAL ESTATE INVESTMENT T	0.7
SIGNIFY NV	0.7
ZEON Corp.	0.7
Kering SA	0.6
Ericsson	0.6

Top 10 equity holdings - short (%)	
AUCKLAND INTL AIRPORT LTD	-0.7
Interxion Holding	-0.7
Transurban Group	-0.7
Taiyo Nippon Sanso Corp.	-0.7
Rakuten Inc.	-0.6
Cellnex Telecom SA	-0.6
Oriental Land Co.	-0.6
MarketAxess Holdings Inc.	-0.6
Axel Springer SE	-0.6
SSR Mining Inc.	-0.6

Regional exposure (%)	Long%	Short%	Net%
United States	28.0	-27.8	0.2
Europe ex. UK	21.1	-21.3	-0.3
Japan	19.6	-19.7	0.0
Australia, New Zealand, Canada	13.0	-13.1	-0.1
United Kingdom	11.9	-11.8	0.0

Sector exposure (%)	Long%	Short%	Net%
Industrials	16.8	-16.6	0.2
Consumer Discretionary	14.5	-14.3	0.2
Materials	12.0	-12.1	-0.1
Technology	8.9	-9.0	0.0
Communication Services	6.8	-7.0	-0.2
Health Care	6.8	-6.7	0.1
Financials	6.7	-6.7	0.0
Energy	6.1	-6.1	0.0
Consumer Staples	4.6	-4.7	-0.2
Real Estate	4.0	-4.3	-0.3
Utilities	3.3	-3.3	0.1
Banks	3.2	-3.1	0.0

Definitions and additional terms

A basis point (bp, or bps) is equal to 1/100th of 1%, or 0.01%.

Brexit is an abbreviation for "British exit," referring to the UK's decision in a June 23, 2016 referendum to leave the European Union (EU).

The **Federal Reserve Board (“Fed”)** is responsible for the formulation of policies designed to promote economic growth, full employment, stable prices, and a sustainable pattern of international trade and payments.

The **Group of 20, or G20,** is a group of finance ministers and central bank governors from 19 of the world's largest economies, including those of many developing nations, along with the European Union.

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

Institute for Supply Management (ISM), formerly known as the National Association for Purchasing Management, is an association representing more than 48,000 purchasing and supply management professionals.

The **MSCI All Country World Index (ACWI)** is designed to provide a broad measure of equity-market performance throughout the world, capturing large- and mid-cap equities representation across 23 Developed Markets and 24 Emerging Markets countries. Please note that an investor cannot invest directly in an index, and unmanaged index returns do not reflect any fees, expenses or sales charges.

The **MSCI Emerging Markets Index** is a free float-adjusted market capitalization index that is designed to measure equity market performance in the global emerging markets.

The **MSCI World Index** captures large- and mid-cap representation across Developed Markets countries

A **yield curve** is a line that plots the interest rates, at a set point in time, of bonds having equal credit quality but differing maturity dates.

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What should I know before investing?

All investments are subject to risk, including the possible loss of principal. The Fund may employ leverage, which increases the volatility of investment returns and subjects the Fund to magnified losses if the Fund's investments decline in value. The Fund may use derivatives, such as options and futures, which can be illiquid, may disproportionately increase losses, and have a potentially large impact on Fund performance. The Fund may employ short selling, a speculative strategy. Unlike the possible loss on a security that is purchased, there is no limit on the amount of loss on an appreciating security that is sold short. The Fund may engage in active and frequent trading, resulting in higher portfolio turnover and transaction costs. There is no assurance strategies used by the Fund will be successful. Equity securities are subject to price fluctuation and 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. Small- and mid-cap stocks involve greater risks and volatility than large-cap stocks. Fixed income securities involve interest rate, credit, inflation and reinvestment risks. As interest rates rise, the values of fixed income securities fall. High-yield bonds possess greater price volatility, illiquidity and possibility of default. Commodity-related investments may be more volatile and less liquid than the underlying commodity, instruments or measures, and their value may be affected by the performance of the overall commodities markets, as well as weather, tax, and other regulatory developments.

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Diversification does not assure a profit or protect against market loss.

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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.

BEFORE INVESTING, CAREFULLY CONSIDER A FUND'S INVESTMENT OBJECTIVES, RISKS, CHARGES AND EXPENSES. YOU CAN FIND THIS AND OTHER INFORMATION IN EACH PROSPECTUS, AND SUMMARY PROSPECTUS, IF AVAILABLE, AT WWW.LEGGMASONFUNDS.COM. PLEASE READ THE PROSPECTUS CAREFULLY.