

Legg Mason Brandywine Global Fixed Income Trust

Objective

The Trust aims to earn a before fees and taxes return of 2% p.a. in excess of the benchmark over a complete market cycle of three to five years.

Benchmark

Citigroup World Government Bond Index, hedged into Australian dollars.

Value

\$93,609,374

Performance (before fees and taxes)

	Trust %	Benchmark %
1 month	-0.01	0.06
3 months	2.19	1.34
1 year	9.87	8.31
3 years	14.82	7.50

Past performance is no indication of future performance.

Profile

Portfolio Characteristics

Modified duration (years)	7.08
Average credit quality (Standard & Poor's)	A-

Sector Allocations

	%
Government sovereign	60.64
Government regional agencies	9.82
Municipal bonds	1.91
Corporate bonds	13.66
Mortgage backed securities	1.62
Cash and currency	12.35

Market Review

Developed Global Bond Markets

Concerns related to the European sovereign debt crisis elevated volatility in November. Performance varied markedly across the developed-market universe with all euro-denominated sovereign markets producing negative absolute returns, but all other markets producing positive absolute returns. European countries already receiving support from policy institutions, like Portugal, Italy and Ireland sharply underperformed, but even core countries like Austria, Finland, France and Belgium experienced weakness. Standard & Poor's downgraded Belgium's debt rating from AAA, calling into question the broader ability of core European countries to finance future bailout efforts if necessary. In contrast, northern-European sovereigns continued to benefit from investors seeking non-euro sovereign alternatives. The U.K. gilts market notably has produced the strongest returns of any index country over the prior three months. The market has a strong technical backdrop given tight fiscal policy, expansionary monetary policy and demand from investors seeking a liquid alternative to euro-denominated sovereigns.

Australian debt produced the best performance of any sovereign market in November. In response to a deteriorating global macroeconomic backdrop, the country lowered short-term interest rates during the month, which benefits existing holders of fixed-rate debt. U.S. and Canadian sovereign markets produced positive, but more modest returns than other countries in the index. Polish and Mexican sovereign markets produced slightly positive absolute returns. While both countries benefit from strong fundamental borrowing profiles, the recent increase in systemic risk moderates investor demand in markets that offer less liquidity. The Malaysian sovereign bond market produced only modestly positive returns. Yields climbed after government figures showed the economy expanded at a faster-than-expected rate over the prior three months.

Currencies

The U.S. dollar outperformed all major currencies except the Japanese yen (up 0.49%) in November. The euro fell sharply (down 3.57%) in reaction to a loss of investor confidence in Europe's policy makers to resolve the sovereign debt and banking crisis. U.K. sterling (down 2.59%) also fell against the dollar, but outperformed all other European currencies due to investor demand for a safe and liquid regional alternative to the euro. Commodities fell during the period and weighed on the exchange rates of commodity-linked currencies like the Australian dollar (down 3.27%), New Zealand dollar (down 4.23%) and Norwegian krone (down 4.34%). North American currencies like the Canadian dollar (down 2.32%) and the Mexican peso (down 3.45%) produced modestly better performance than similar-beta currencies due to their proximity to the relatively stable U.S. economy. The Chinese renminbi (down 0.31%) reversed its typical bias toward slow appreciation against the dollar this month. Flexible Asian currencies like the South Korean won (down 2.55%), Malaysian ringgit (down 3.20%), and Singapore dollar (down 2.32%) remained better supported than other non-Asian export-oriented peers.

Corporate Bonds

European concerns pushed credit spreads substantially higher in November, driving negative absolute returns in investment-grade and high yield corporate credit. Spreads on the Barclays Capital U.S. investment-grade credit index widened 38 basis points (bps), pushing yields to 3.73%. Financials were by far the worst performing major sector, reflecting the sensitivity of banking and insurance names to deterioration in the European banking system. Since most of the large banks and insurers issue A rated debt, this quality segment underperformed higher-quality segments as well as the lower-rated BBB quality segment. Spreads on the Barclays Capital U.S. High Yield index widened 67 bps, pushing yields to 8.87%. Also illustrating the stress in Europe, spreads for the Pan-European High Yield Index widened 145 bps, pushing yields above 10% by the end of the month.

Mortgage Bonds

European sovereign debt concerns continued to elevate market volatility and limit investors' risk appetites during the month. This caused the amount of bidding activity in the non-agency and structured mortgage market to be relatively light, evidenced by 60% to 70% of dealers posting "do-not-trade" notices on certain days this month. Many market participants are still concerned about the possibility of a flood of distressed supply from European banks, which would mostly be distressed Alt-A / subprime floaters. Performance in credit has been stagnant due to the still-distressed housing market. We expect the weak housing market will limit price upside in the future. Investors continue to favour higher credit-quality jumbo and alt-A fixed rate bonds.

Housing demand has been disappointing in 2011, even with ultra-low mortgage rates and favourable affordability metrics. At the current pace of existing-home sales, we expect housing price values will fall an additional 5% to 10% in 2012 and stabilizing in late 2013.

Emerging Markets

Most emerging-market currencies weakened in November due to the systemic risks posed by a deteriorating outlook for Europe. Commodity-linked emerging currencies like the Brazilian real (down 6.48%) suffered the worst depreciation given their higher sensitivity to commodity prices.

Brazil's 10-year government bonds produced near-zero but slightly negative absolute returns.

The Hungarian forint (down 3.89%) also fell, but avoided a deeper decline by rallying when the finance minister announced Hungary would open talks with the International Monetary Fund. Although a possible IMF financing backstop would be designed to preserve the country's investment-grade rating, Moody's downgraded Hungary's sovereign debt rating near the end of the month. Benchmark 10-year bonds lost more than 4% in local currency terms in November.

The Indonesian rupiah (down 2.63%) fell in response to the central bank's unexpected 50 bps cut in policy rates, but also in response to the systemic risk fears that weighed on most emerging-market currencies in November. Rising global uncertainty drove negative absolute returns in the Indonesian government bond market.

Performance

The Legg Mason Brandywine Global Fixed Income Trust slightly underperformed its benchmark over the month. Performance in the last 12 months is 1.6% ahead of benchmark.