LEGG MASON
GLOBAL ASSET MANAGEMENT

Legg Mason
Balanced Trust

Objective

The Trust aims to earn a before fees and taxes return (over rolling three year periods) in excess of a benchmark constructed in accordance with the neutral asset allocation of the Trust.

Benchmark

The performance of the Trust is measured against a benchmark comprising the following sectors:

Sector	Index
35% Australian equities	S&P/ASX 200 Accumulation Index
10% Property securities	S&P/ASX 200 A-REIT Accumulation Index
23% Global equities	MSCI All Country (ex-Australia) World Index, net dividends reinvested, expressed in AUD
12% Australian bonds	UBS Australian Composite Bond Index
12% Global bonds	Barclays Capital Global Aggregate Index, hedged into AUD
5% Cash	UBS Australian Bank Bill Index
3% Alternative investments	UBS Australian Bank Bill Index

Value

$224,561,773.

Performance (before fees and taxes)

	Trust* %	Benchmark %	Trust ** %
1 month	3.09	2.04	2.92
3 months	-2.25	-1.93	-2.16
1 year	11.37	8.93	11.14
3 years p.a.	-5.46	-4.01	-5.74

* Before fees and taxes.
** After fees and taxes.
Past performance is no indication of future performance.

Market Review

Equity markets around the world recovered ground during July as improved sentiment for risk assets reflected diminished concerns over the sovereign debt issues in Europe and the extent of the slowdown in China. The Australian equity market gained 4.5% over the month, as measured by the S&P/ASX 200 Accumulation Index.

Consistent with a more risk tolerant environment, Australian equity investors rewarded the more cyclical sectors, particularly those that had borne the brunt of the recent sell-down. The Banks, Industrials and Materials sectors all outperformed, while investors reduced their exposures to some of the more defensive names, particularly in the Telecommunication Services, Consumer Staples and Property Trust sectors. Smaller capitalised securities generally outperformed the large cap Australian equity market. In a further sign of optimism, merger and acquisition activity continued this month, with bids made for Intoll Group (+41.4%), Centennial Coal Company (+34.7%) and Healthscope (+15.6%).

The Australian real estate investment trust (“A-REIT”) market gained 1.5% over the month, as measured by the S&P/ASX 200 A-REIT Accumulation Index. The A-REITs relatively defensive characteristics held the sector back relative to the broader Australian equity market.

Global equity markets reversed course in July, as the MSCI World (ex Australia) Index, expressed in Australian dollars, rose 0.7% over the month. Company earnings announcements were generally better than analyst estimates and investors began to see equity markets as oversold.

Emerging markets rebounded in July with a return of 1.1%, as measured by the MSCI Emerging Markets Index, expressed in Australian dollars.

Bond yields moved higher over the month as the flight to quality in bond markets eased. This was tempered by the revised outlook for cash rate rises over the coming 12 months and questions over the speed of global growth. As a result, bond yields are still well below April levels.

On the economic front, employment growth remained strong while consumer price inflation came in a little weaker than the market had expected. The Reserve Bank of Australia left the target cash rate on hold at 4.50%, while the Australian dollar gained US4.63 cents against the U.S. dollar to end the month at US89.86 cents.

Issued and approved by Legg Mason Asset Management Australia Limited, ABN 76 004 835 849, AFSL No. 240827. Level 47, 120 Collins Street, Melbourne VIC 3000.

Performance

The Legg Mason Balanced Trust outperformed its benchmark by 1.0% over the month. Portfolio performance over the past year was 2.4% ahead of benchmark Performance this month was aided by choices in the Australian equities, A-REITs, emerging market equities and bond sectors. Asset allocation decisions between Australian equities and bonds also added value.

In Australian equities, portfolio performance was aided by stock selection decisions across a range of sectors. In particular, the portfolio's tilt towards securities leveraged to a growing economy in the Financials ex Banks & Property, Metals & Mining and Energy sectors added significant value.

In A-REITs, the portfolio's overweight exposures to EDT Retail and Valad Property Group added value this month.

Exposure to developed market global equities detracted from performance largely as a result of stock selection decisions, chiefly in the U.S. Selections in continental Europe and Japan were also weak.

In emerging market equities, the portfolio's overweight exposure to Brazil contributed positively to performance, as did portfolio holdings in Brazil and Taiwan.

In Australian bonds, an overweight position to the corporate sector was the major source of value added through a higher running yield and tighter credit spreads. The portfolio's exposure to lower-rated investment grade debt provided some additional benefit.

At the asset allocation level, the portfolio was overweight Australian equities and underweight bonds. This position added value over the month as domestic equities outperformed domestic bonds. The portfolio remained overweight Australian equities and underweight bonds at month end to benefit from an expected return to more normal relative equity and bond market valuations.

Outlook

Our view was that the Australian equity and A-REIT market weakness experienced during the June quarter was overdone and that it may partially be explained by memories of 2008. The gains over the past month are an encouraging indicator of the significant value that we believe is still on offer in selected underlying securities.

As such, we remain of the view that the Australian equity and A-REIT sectors should be able to move higher on a medium term time horizon. This view is supported by evidence that Australian firms have reduced their risk profiles post the global financial crisis. As a result, a number of firms are poised to produce strong margin expansion once revenue growth returns.

In developed market global equities, the portfolio has a slightly cyclical tilt and is positioned for global recovery over the next 12 months. Portfolio exposures relative to the benchmark remain moderate.

In emerging market equities, earnings expansion should be well supported by strong domestic demand growth across most regions, while inflation is far from calling for drastic action by emerging market central banks.

In Australian bonds, portfolio duration is expected to be tactically managed as volatility is likely to remain high while markets debate the speed of the global recovery, the possible return of inflation and sovereign risk issues. We maintain an overweight position in corporate bonds, with emphasis on Financials, as market valuations and increased regulation provide appeal despite spreads tightening over the past year. We are also selectively buying primary corporate deals in industries that will benefit from an economy that has returned to growth and those that have reduced their level of leverage, namely property trusts and infrastructure.