

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 natural asset allocation of the Trust.

Benchmark

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

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
5% Cash	UBS Australian Bank Bill Index
3% Alternative investments	UBS Australian Bank Bill Index

Value

\$234,984,859

Performance (Before fees and taxes)

	Trust* %	Benchmark %	Trust**%
1 month	-1.95	-0.67	-1.96
3 months	-0.85	0.13	-0.98
1 year	-2.04	-0.76	-2.47
3 years p.a.	6.87	4.56	6.05

* Before fees and taxes.

** After fees and taxes.

Past performance is no indication of future performance.

Market Review

In November, equity markets were once again weak, on the back of concerns around a potential European financial meltdown. Increasing yields on Italian Government bonds contributed to increase solvency concerns of the larger European economies. Equities plummeted through the month before rallying near month-end on renewed speculation that the European Central Bank was preparing a new plan to solve the sovereign debt issue.

In Australia, the AGM season continued and most of the companies indicated that the operating environment is still challenging. Defensive names outperformed more cyclical names. A-REITs, Information Technology and Utilities sectors outperformed, while Financial, Resources and Consumer Discretionary were the laggards. The Australian equity market finished the month down 3.48%, as measured by the S&P/ASX 200 Accumulation Index.

The Australian Real Estate Investment Trusts (A-REIT) sector was up 2.65 % over the month, as measured by the S&P/ASX 300 A-REIT Accumulation Index. A-REITs outperformed the broader Australian equity market by 6.1% during the period.

Global equities experienced significant volatility during November as markets declined for the majority of the month and then rallied in the final week, leaving investors down and out in terms of performance. The evolving Eurozone crisis weighed on investors during the month and fed the volatility in stocks. Steps taken by the world's central banks to make it less costly for European banks to borrow U.S. dollars bolstered markets at month's end and supported the equity rally.

Yields on Australian government bonds saw their largest decline since late 2008. Three-year bonds reached their lowest level since March 2009, having declined an extraordinary 76 basis points (bps), while 10-year bond yields moved to their lowest level since May 2009, which resulted in the curve steepening 18 bps.

Australian economic data released during the month were mixed. The Reserve Bank of Australia announced a 25 basis points rate cut on November 1, in line with market expectations. The market has priced in several more potential rate cuts by June 2012.

The Australian dollar continued to reflect the increase in risk aversion and lost ground against the U.S. dollar. After reaching a low of US0.969 cents during the period, it ended the month at US0.998 cents, down US5.5 cents.

Performance

The Legg Mason Balanced Trust underperformed its benchmark by 1.3% (before fees and taxes) over the month. The overseas equities sector added value last month, while the overweight allocation to Australian shares detracted value. Australian bonds outperformed and contributed positively to performance, while global bonds detracted. The Australian listed property sector outperformed its benchmark and contributed positively to last month's performance.

In Australian equities, most of the underperformance came from the underweight to defensive sectors like Healthcare, Property, Telecommunications and Gold and from the overweight to Banks.

In developed market global equities, stock selection benefited the portfolio chiefly due to stock selection in the US. Selection was modestly positive in most regions and flat in Asia ex-Japan. The impact of region/sector allocations added value due to an underweight in Asia ex-Japan and in continental Europe. In emerging market equities overweight positioning in India and China were the main detractors but on a general note underperformance was fairly broad across sectors.

In A-REITs, the portfolio outperformed its benchmark over the month. Portfolio's holdings that aided performance included Stockland (+7.3%) and the underweight positions to Goodman Group (-4.8%), Investa Office (-4.8%) and CFS Retail (+1.1%).

In Australian bonds, the short duration position relative to benchmark was the main source of underperformance, as bond yields fell to their lowest level since early 2009. Corporate spread-widening also detracted due to the portfolio overweight to that sector. However, this was largely neutralised by an underweight position in the supranational sector, a judicious selection of supranational issuers (such as EIB, KfW and Rentenbank) and the careful management of the overall credit spread duration within those sectors.

Outlook

The international environment is clearly the focus of investment markets at the current time. Volatile markets always expose excellent long term investment opportunities and now should not be any different. Given current valuations, we believe the portfolio is well positioned to participate in the eventual recovery.

Abundant cash levels in corporate Australia should lead to higher dividends, merger and acquisition activity, capital expenditure and strong employment levels. This further underpins the case for Australian equities at this time.

At the overall market level, A-REITs are considered to be attractively valued based on implied value relative to unlisted property, global REITs, the broader Australian equity market as well as Australian and global bonds.

At the security level, the investment opportunity for selected A-REITs continues to be attractive. The valuation spread between the most attractive and least attractive securities in the investment universe remains at around two times historical averages.

In the global equities asset class the investment team anticipates making strategic purchases with a focus on low valuations, low expectations, the value proposition of the franchise and a margin of safety.

In the bond sector, duration positioning will be tactical, with a short duration bias relative to the benchmark. Volatility is likely to remain high while markets consider the fragile state of developed-nation economies and continue to test the eurozone's resolve to stand by its member countries and their financial systems.

The portfolio is expected to maintain an overweight position in corporate bonds, with an emphasis on large financials, as market valuations and increased regulation continue to appeal.