

Legg Mason Western Asset Cash Trust

Objective

The Trust aims to earn a before fees and taxes in excess of the return of the benchmark.

Benchmark

UBS Australian Bank Bill Index.

Value

\$61,146,994

Investment Process Summary

The Trust actively manages investments to ensure that:

- Deposits are readily accessible;
- investments are highly liquid and low risk; and
- returns have limited volatility.

Performance (before fees and taxes)

	Trust %	Benchmark %
1 month	0.40	0.39
3 months	1.24	1.20
1 year	5.03	4.93
3 years p.a.	4.51	4.36
5 years p.a.	5.60	5.49

Past performance is no indication of future performance.

Profile

Sector Allocation	Trust %
Bank obligations	69.5
Corporate	0.0
Asset backed	6.2
Cash	24.3

Market Review

The European sovereign crisis re-emerged after October's brief reprieve as the problems faced there claimed more scalps in the form of governments changing hands. Italian 10-year government bond yields surged past the 7% level, widely considered unsustainable for that country and a potential tipping point for Italian solvency. French government bond spreads over Germany widened further, and even Germany failed to clear a bond auction in late November as markets shied away from European debt.

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. The yield change was more dramatic on Australian government bonds than for corresponding tenors on foreign government bonds, which reflected the focus on 'safe' sovereigns. Equities fell 4.2% and credit spreads widened, mostly on European banks and supranationals.

Earlier in the month, the Reserve Bank of Australia (RBA) cut interest rates by 25 bps for the first time since April 2009. Changes in Australian inflation forecasts—due mainly to a more benign wage-inflation outlook—provided the RBA scope to remove the slight tightening bias to help tackle the softening in the non-commodity-related sectors and the threat that European troubles could dampen domestic economic conditions. Bank bill yields fell, pricing in further aggressive rate cuts by the RBA in coming months, despite broadly favourable domestic economic data, which included larger-than-expected private capital expenditures as Australians took advantage of the strong terms of trade to upgrade capacity and productive resources. The unemployment rate also dipped from 5.3% to 5.2%, thanks to an uptick in full-time employment.

The Australian dollar suffered, as would be expected during bouts of risk-off trading. At one stage, the currency had lost as much as 8% intra-month. However, the late-month surge in confidence helped retrace much of that decline. The Australian dollar finished 2.4% lower relative to the US dollar and 3% lower on a trade-weighted basis.

Performance

The Legg Mason Western Asset Cash Trust returned 0.40% in November, marginally ahead of the UBS Australia Bank Bill Index return of 0.39%. The portfolio's track record continues to be in line with the benchmark.

Outlook

We continue to forecast domestic GDP growth to be around trend level (3.0%–3.5%) in 2012. We recognise the challenges faced in Europe, which, in turn, pose challenges to broader global growth. However, we are constructive on the US economic recovery (albeit at a slow pace), and we believe that Chinese growth will remain solid—factors that are supportive of our domestic growth outlook. Unemployment is currently hovering at 5.2%–5.3%, but we expect it to drift higher and peak at around 5.5% before edging lower as a large uptick of employment begins to take hold in Western Australia and Queensland due to new projects coming on line. An improvement in sentiment for the rest of the economy should further aid the decline in the unemployment rate through 2012.

Inflation is continuing to drift lower at both the headline and core levels, and no longer poses the risk that it did six months ago due to the slowdown in the non-mining sectors. The RBA has signalled that it is comfortable with current levels of inflation, which gives the central bank the scope to further respond to global challenges, particularly those posed by Europe, should the need arise.

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.

Further Information

Credit Quality	Trust %	Maximum %
"AAA" or "A-1+" securities	89.2	100.0
"A-1" securities and cash	10.8	25.0

Maturity Structure	Trust %
1 to 7 days	28.8
8 to 30 days	6.3
31 to 90 days	63.3
91 to 180 days	0.0
181 to 365 days	1.6

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