

All Cap Value Strategy

3Q11

Market Review

We have maintained a pro-cyclical approach to the stock market, believing that the U.S. and world economies need growth in order to effectively deal with their fiscal problems, which include entitlements and debt. This means that sectors of the market such as industrials and technology have been favored over defensive ones such as utilities and staples.

Although our financials holdings were very poor performers during the quarter, they essentially matched the performance for the benchmark financials sector. Principal reasons for our shortfall during the just completed quarter were utilities, where we are underweight, which caused a negative -1.2% attribution effect; consumer staples, where our underweight position and holdings lagged behind the benchmark by -0.74%; and energy, where our emphasis on oil service companies led to a -1.4% drag on performance. At current prices, oil services companies are one of the most compelling segments within the stock market.

Strategy Highlights

During the third quarter, stock selection and interaction in the consumer discretionary and information technology (IT) sectors contributed positively to relative performance, whereas stock the information technology and industrials sectors. The Strategy's largest relative underweight positions at the end of the period were in the utilities and financials sectors.

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The leading individual contributor to Strategy performance during the third quarter included Cisco Systems Inc. in the IT sector. Leading individual detractors from performance including JPMorgan Chase & Co., Morgan Stanley and Jones Lang LaSalle Inc. in the financials sector and Hess Corp. and Baker Hughes Inc. in the energy sector.

During the quarter, we added new positions to the Strategy's portfolio in Annaly Capital Management Inc. in the financials sector and Apache Corp. in the energy sector. We sold out of

positions in Babcock & Wilcox Co. in the industrials sector, Bank of America Corp. in the financials sector, Enzo Biochem Inc. in the health care sector and United States Steel Corp. in the materials sector.

Outlook

What are the prospects for stocks in the next quarter and year? From time to time we monitor what insiders are doing, and buying vs. selling has reached levels consistent with a market near an important bottom. With these factors in mind, we believe our emphasis on sectors that would benefit from a better stock market is appropriate. The wild card in all of this is Europe. European banks are undercapitalized and need equity

John Goode Managing Director, Senior Portfolio Manager

- 42 years of investment industry experience
- MBA from Stanford's Graduate School of Business
- BA in Economics from Stanford University

Peter Hable Managing Director, Senior Portfolio Manager

- 28 years of investment industry experience
- MBA from the Wharton School at the University of Pennsylvania
- BS in Economics from Southern Methodist University

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injections. Greece has defaulted, for all practical purposes, and if one concludes that “haircuts” and write-downs associated with Greek debt are appropriate, host governments need to inject equity capital in return for partial ownership positions. Existing shareholders are resisting this, which is to be expected. In addition, Europe needs a Eurobond or “umbrella security” to deal with the several trillion dollars of government debt that must be backstopped. If the challenges associated with Europe did not exist, we would be “all in” where our own stock market is concerned.

ClearBridge Advisors

www.clearbridgeadvisors.com

800-691-6960

info@clearbridgeadvisors.com

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