

Institutional Large Cap Value Strategy

4Q09

Market Overview

Over the past two years, we have experienced an unprecedented economic slowdown and one of the most severe financial crises on record. While the worst might be behind us, it will likely take a prolonged period of time to unwind leverage and repair consumers' balance sheets. After collapsing spectacularly in 2008, the U.S. equity market finished 2009 with its third straight quarterly advance as the S&P 500 Index gained nearly 6% in the fourth quarter and 26% for all of 2009, its best year since 2003 and a tremendous turnaround from the previous year's 37% loss.

The market's recovery since the lows of the past spring was remarkable, with the S&P 500 gaining 65% from its 12-year low on March 9 through the end of the year. Perhaps more notable, however, was the fact that stocks closed the decade below where they began it, with the S&P 500 dropping 24% over the last 10 years for an average decline (including dividends) of 0.9% a year since 1999, the first decade of negative annualized returns for the S&P 500 since its inception in 1927.

Portfolio Highlights

On an absolute basis, the Strategy had positive returns in nine out of 10 sectors for the fourth quarter, with the greatest contributions to returns coming from the consumer discretionary, healthcare and consumer staples sectors and the only negative return coming from the financials sector.

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Robert Feitler, Jr. Managing Director, Portfolio Manager

- 15 years of investment industry experience
- MBA in Finance from the University of Wisconsin
- BA in Economics from Haverford College

Dmitry Khaykin Managing Director, Portfolio Manager

- 13 years of investment industry experience
- MBA in Finance and Accounting from the Wharton School at the University of Pennsylvania
- BA in Economics and Computer Science from New York University

Relative to the benchmark Russell 1000 Value Index, the Strategy's overall stock selection contributed to performance for the quarter, while the overall impact of sector allocation was negligible. Stock selection in the consumer staples, IT and financials sectors made significant contributions to relative performance, while selection in the energy sector detracted from it. The Strategy's overweight to the consumer discretionary sector and its underweight to the financials sector helped relative performance, but this was offset by negative impacts from the underweighted materials and utilities sectors.

During the fourth quarter, we added positions to the Strategy in Johnson & Johnson, CVS Caremark Corp. and Hewlett-Packard Co. and closed our existing positions in both PNC Financial Services Group Inc. and Boeing Co.

The leading individual contributors to Strategy performance for the fourth quarter included our positions in Total S.A. (ADS) in the energy sector, Microsoft Corp. in the IT sector, DISH Network Corp. (Class A) in the consumer discretionary sector, Sempra Energy in the utilities sector and American Express Co. in the financials sector. The bottom individual contributors to Strategy performance for the quarter included Bank of America Corp., State Street Corp. and Marsh & McLennan Cos., all in the financials sector, as well as General Electric Co. and Boeing Co., both in the industrials sector.

Outlook

During the fourth quarter, we continued to see signs of economic stabilization, albeit tenuous and largely supported by the government's deficit spending. Housing, which has been at the center of the current economic woes, remained one of the main areas receiving government support. Artificially low mortgage rates, tax credits, and the government's effort to reduce foreclosures have stabilized home prices for the past three months. The private sector continued to demonstrate impressive resilience by aggressively controlling expenses in an effort to restore profitability. While investors welcomed corporate managements' focus on profitability, it has come at the expense of workforce reduction. Although unemployment remained elevated, first-time jobless claims continued to decline to its lowest level since July 2008. It will likely take several years to regain the millions of jobs lost during the recession, but we remain optimistic that as the economy improves, the private sector will start adding net new jobs.

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The U.S. government continues to play an unusually active role in many sectors of the economy, including financial services and healthcare. Various support programs helped to restore confidence in the viability of major financial institutions, enabling them to improve their balance sheets by raising equity. During the fourth quarter, Bank of America and Wells Fargo raised over \$19 billion and \$12 billion of equity, respectively, and were allowed to repay TARP. We participated in both offerings, and we continue to believe that these companies offer attractive risk-adjusted returns for long-term investors. In the health care area, both the House and the Senate passed their versions of the health care legislation. While there are still meaningful differences between the two versions of the bill, it looks increasingly likely that some form of health care reform will be enacted and that

it will have a profound impact on the way health care services are delivered in the U.S.

During the past two years, a challenging economic environment combined with unprecedented government intervention created an extraordinary level of investor uncertainty. We believe that periods of high uncertainty often create the best investment opportunities and that 2009 was no different. During the year, we found multiple opportunities to establish positions in what we felt were high-quality franchises at very attractive valuations. While the recent stock market rebound anticipates some level of economic recovery, we remain optimistic that investors with multi-year time horizons will benefit from current and future opportunities.

Past performance is no guarantee of future results.

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