

Aggressive Growth Strategy

4Q11

Market Review

Despite significant volatility, the equity markets ended 2011 essentially flat on the year, with the S&P 500 closing down less than 1%. The first half of the year saw stocks rally sharply with major averages hitting multi-year highs in May before retreating sharply into August amid global economic fears. After testing the August lows in early October, the markets rebounded toward the end of the year due to improving economic conditions and increased investor optimism that the worst of the macro fears were either priced into stocks or behind us.

Our performance, much like the market, was choppy over 2011. After two strong years in 2009 and 2010, solid results continued into the first half of the year on both an absolute and relative basis. As the macroeconomic headlines turned negative in the third quarter and equity correlations neared record highs, we saw many of our holdings sell off sharply. The year's early gains evaporated, and we had sharply negative third quarter performance on an absolute and relative basis. Performance recovered strongly in the final three months of the year, leaving our Strategy slightly behind the benchmark for the year. Despite the volatility, many of our companies made significant progress fundamentally throughout the year, growing both top and bottom lines and improving their balance sheets.

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- 15 years of investment industry experience
- BS in Mathematics from Duke University

Richard Freeman, **Managing Director, Senior Portfolio Manager**

- 35 years of investment industry experience
- MBA in Finance from New York University
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We remain convinced that the severe correction that the broad market experienced, which reached its nadir in early August, was a pause to refresh the primary bull market that we think has been in place since early 2009. Typically, rising markets lead to improving investor confidence, yet while the S&P 500 Index is more than 80% above its 2009 lows, investor sentiment ranges somewhere between complacency and outright pessimism. This has led to a highly correlated market, with the headlines dominating the market’s direction. As we detail below, we expect this to change as confidence starts to return.

We expect that consolidation will be a major theme in 2012. In our experience, this type of market – one that fails to recognize the value many companies are offering – will eventually compel companies to take their own future in their hands. Undervalued companies with strong balance sheets

have the opportunity to increase share buyback programs, merger and acquisition deal activity, or both. The discrepancy between what a growth company is worth to a third party, and where many stocks are trading in the open market, is sizeable. This has led to large premiums (over public share price) in deals that have been announced. Cash on corporate balance sheets in the U.S. remains at record levels (approaching \$3 trillion). We believe the limiting factor holding this wave of consolidation in check has been a lack of confidence in market conditions, but this should change as the economy shows signs of improvement.

At the end of 2011, we feel very comfortable with our portfolios. While many investors have become short sighted and hyper-focused on the macroeconomic situation, we feel that much of the news is backward looking and

already reflected in the stock prices at current valuation levels. We continue to be focused on finding companies with unique competitive advantages over competition and those with balance sheet strength that allow them to invest during downturns. Whereas highly correlated markets can be frustrating shorter term, they tend to produce inefficiencies that can be exploited by those with longer-term investment time horizons. We were able to take advantage of the market's downside volatility this summer to hold and/or increase positions in businesses that we believe have the opportunity to grow significantly, both in the short and long term.

Strategy Highlights

In terms of absolute performance, the Strategy had gains in all seven sectors in which it was invested (among 10 in total) for the quarter. The greatest contributors to returns were the energy, health care and consumer discretionary sectors, while the smallest contributors were the financials, materials and industrials sectors. The Strategy had no holdings in the consumer staples, utilities or telecommunications services sectors.

Relative to the benchmark index, stock selection in the health care, energy, information technology (IT), and consumer discretionary sectors contributed significantly to performance for the quarter. An overweight to the energy sector and underweights to the IT and consumer staples sectors also contributed meaningfully to relative performance. Significant detractors from relative performance included an overweight to the health care sector, underweights to the materials and industrials sectors, and stock selection in the financials sector.

Leading individual contributors to Strategy performance during the fourth quarter included Biogen Idec Inc., Amgen Inc. and UnitedHealth Group Inc. in the health care sector, and Anadarko Petroleum Corp. and Core Laboratories NV in the energy sector. The bottom individual contributors to Strategy performance included Vertex Pharmaceuticals Inc. and Human Genome Sciences Inc. in the health care sector, Broadcom Corp. and Cree Inc. in the IT sector and Cablevision Systems Corp. in the consumer discretionary sector.

Over the course of the quarter, we made just one significant change to our portfolio, closing our existing position in Nokia Corp. in the IT sector.

Market Outlook

Looking ahead, we still believe that many of the factors that had been driving the secular bull market over the past two years should remain in place. Liquidity remains high, as balance sheets are generally healthy and short-term interest rates remain historically low. Based on statements from the Federal Reserve, rates should continue to be historically low until the economy shows signs of expansion. Stock valuations, in general, are still very low by historical standards, especially in comparison to fixed-income assets.

Furthermore, the buildup of cash reserves on the part of individual investors and corporate America, which could move into equities, has continued. At the same time, equity risk premiums remain at a 60-year high, reflecting investor distaste for stocks and concerns over the macroeconomic environment. In conclusion, we maintain our bottom-up, benchmark-agnostic and fundamentals-focused approach to portfolio management, and feel that we are well positioned for 2012.

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