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- Investors should read and understand the Fund's most current offering document, including details of risk factors relevant to the Fund before making an investment in the Fund.
- The Fund may take significant, long-term positions that the Investment Manager believes are undervalued by the market. Companies in which such Funds invest may remain out of favour with the market for extended periods of time. Such Funds may continue to hold, and in some cases add to, a declining position so long as the relevant Investment Manager continues to view the market as incorrectly valuing the security. As a result, the Fund may face the risk of mis-estimation by the Investment Manager in its fundamental analysis regarding the companies in which the Fund invests. The performance of the Fund may not closely correlate to specific market indices over time and may include extended periods of underperformance as compared to the broader market.
- An investment in the Fund may not be suitable for all investors. The investment decision is yours but you should not invest in the Fund unless the intermediary who sells it to you has advised you that it is suitable for you and has explained why, including how buying it would be consistent with your investment objectives.
- The Fund is a sub-fund of Legg Mason Global Funds plc, an open-ended umbrella investment company constituted in Ireland. The Fund seeks to achieve long-term capital appreciation principally through investing in securities of U.S. issuers that the Investment Manager believes to be undervalued in relation to their intrinsic value.

Legg Mason Capital Management Value Fund

Key Points

- The Fund continues to be overweight in sectors of the market that the manager considers to be among the cheapest, namely healthcare, financials, and technology.
- The Fund's overweight position in healthcare is a notable change from its positioning a year ago when it was underweight in the sector. In the financials sector, meanwhile, the manager has diversified the Fund's holdings to include more exposure to life insurance groups and asset managers in addition to its holdings in banks.
- The manager expects to see this year's high correlations in equity markets come down in 2012 with the result that stock picking and valuation should again be the key performance drivers.

This Q&A is based on a teleconference call that took place on 8th December 2011 with Sam Peters (SP), who in April 2012 will become sole manager of Legg Mason Capital Management's value equity strategy which underlies the Legg Mason Capital Management Value Fund.

Q: How has the portfolio changed since you joined as its co-manager?

SP: I joined the firm six years ago and became co-portfolio manager of the Fund in November last year so there is a lot of continuity with my current transition to being the sole manager of the strategy with effect from 1st April 2012.

Looking at the portfolio now compared to 12 months ago, one highlight is that we were underweight in healthcare but we are now nicely overweight in the sector. In fact, it's our second largest overweight position. I used to run a global healthcare team globally for a different firm, so it was a natural place for me to start. The sector has done very well because of its defensive characteristics, but we're more excited about the long-term valuation opportunity of healthcare.

Another area that Bill Miller, Mary Chris Gay, and I really thought was attractive was mega-cap US stocks. Bill had been talking about that prior to me joining the portfolio and we both agreed the key was not just buying the big stocks which in the US are cash rich and not discounting any growth, but buying the mega-

cap US stocks that have good capital allocation and management teams that understand how to allocate capital. A lot of this came through going overweight in healthcare, because we bought some of the big names in the sector like Pfizer. We also increased our consumer staples weighting with stocks that had underperformed for about two-and-a-half years, so there was a valuation opportunity there. Elsewhere we bought some of the integrated oil companies, and changed around some of our holdings in the technology and financials sectors.

The result of this was that we improved the dividend growth opportunities of the Fund, and by buying dividends we expected to improve our performance during risk-off, or downside, market periods. Overall, we wanted to be overweight in what we viewed as the cheapest parts of the market, namely healthcare, technology, and financials, and that's what we have done. We wanted to have better fundamentals and characteristics in the Fund than in the S&P500 Index, and obviously much better valuations, and that's also what we think we have done.

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Legg Mason Capital Management

Value Fund

Q: What changes did you make to the Fund's exposure to the financials sector and why?

SP: The key issue here is that people say financials are cheap for a reason. They cite factors such as new regulations and the new normal which means that the US is going to be Japan and in Japan there is this deflationary de-levering cycle. The claim is also made that if you just short financials and go overweight in exporters, you're going to pick up huge alpha. My counter to that is the financials that we hold, such as BlackRock, Aflac, JP Morgan, and American Express, means that we own franchise financials spread across the life insurance, banks, and asset management sectors. Balance sheets in the financials sector are in great shape, the best shape in fact I've ever seen in 20 years both from a liquidity and solvency standpoint. Dividend yields are attractive and most of the financial stocks that we hold we bought below tangible book value.

A year ago we were just overweight in the big money centre banks such as Citibank and Goldman Sachs, but because all the financials were equally cheap for the most part, I wanted to sprinkle in some other holdings to the portfolio. So I pulled back from some of the pure brokerage names, which are going to have more regulatory pressure.

We bought life insurers like MetLife in a big way, for example, which is now our largest financial holding. We bought it close to half of tangible book value, which we view as an extremely low valuation.

We also bought BlackRock, the asset management group, at a double-digit free cash flow yield. So we spread our financials exposure around, but without having to give up attractive valuations.

Also noteworthy is that we swapped Bank of America for PNC Financial, which is a super-regional in the US. It's a swap that has worked well so far. We sold Bank of America at around half the tangible book and we bought PNC at 0.8 times tangible book with a 3% dividend yield. We think Bank of America is going to be a great stock at some point and may re-invest in the company but it's just not right to do that today, in my opinion.

Q: What macro environment would you expect to be most advantageous for the Fund?

SP: We'd expect the big macro win for us to be a US recovery, especially around housing. I don't know exactly when that will come, but clearly there are some signs that the US is doing a lot better than a lot of places in the world. I think we have some huge inherent advantages in the US. At the same time, ironically, we think we're well positioned if there is a global growth scare. Europe is the centre of attention for this now. We think we would actually pick up ground because we're underweight global cyclicals. Oil prices are up 15% a year over

the last ten years and gold has compounded even better, up 17% a year over the last ten years. If you think these two situations are going to repeat themselves, then this is not the portfolio for you.

Taking the other side, if Europe infects the world, brings down global growth and hurts Asia, we would actually expect to pick up nice relative ground because investors are still very much overweight global cyclicals and not overweight in the areas where we are overweight. But the macro backdrop we want most is US recovery.

Q: How worried are you about the situation in Europe?

SP: US exports to Europe are 2% of GDP, so there are not a lot of downside multipliers on that. The S&P 500's exposure to European revenues is about 18%, so Europe matters, but we believe based on such considerations that it doesn't present the macro risks for the US that some people think. The key for 2012 to be a reasonably good year and more friendly to valuation, which I think it will be, is that we can't have a complete disaster in Europe where the euro dissolves, etc. Some of the fear of this is clearly priced into the market, but we think we'll avoid that outcome.

Q: What are your main challenges in the current environment?

SP: For me and every other active portfolio manager, one of the key challenges is that we've got a highly correlated market with more and more things being thrown into the 'risk-on' bucket. As well as this, valuation spreads are very low with a lot of stocks being priced the same. So for us, finding cheap stocks isn't the problem, rather it's how you put them together in the portfolio. Coming back to financials, for example, we think they're the most attractive part of the portfolio but I also know they're going to drive a lot of volatility. So the question becomes how do you put very cheap financials together with other things to smooth out the ride while at the same time making sure you do not sacrifice valuation.

Q: How does this affect your outlook for the Fund in 2012?

SP: At the moment a lot of people are just thinking of equities as a risk asset, like a correlated risk asset or as a lump of risk assets, so we're getting these high volatility periods. I think that should start to abate as some of the macro issues recede. As a result, correlations should come down, which would be a big help for stock pickers. If that happens, it should be beneficial to us. We don't need it to come down a lot. Currently, correlations are at 80%, which is a historic high. If they came down to 60%, which is still historically high, we should be set up to do much better. So we are encouraged as we expect to see correlations come down and stock picking and valuation to matter more in 2012.

Legg Mason Capital Management Value Fund

IMPORTANT INFORMATION

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The Fund may invest in certain types of derivative instruments for efficient portfolio management purposes. Please refer to the prospectus for more information.

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