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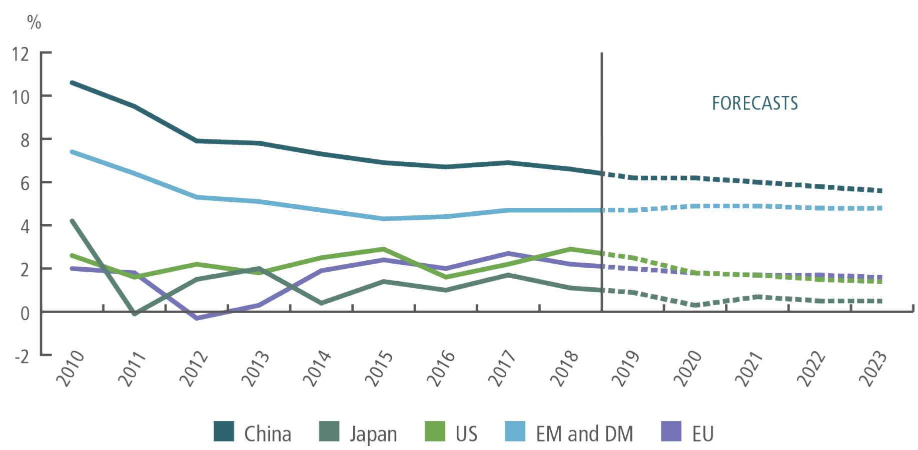
A LEGG MASON COMPANY

Adjusting Portfolio Positioning Amidst Transitioning Growth

2017 marked an unprecedented year for equity investors; all three major regional indices rose over 20% and realized historically low volatility levels amidst an environment of unusually low interest rates and generally synchronized global economic growth. 2018 was the year of US exceptionalism; US equities appeared to be insulated from broader macroeconomic and political risks affecting other regions — Brexit negotiations, slowdown in China, USD strength, among others — on the back of tax stimulus and continued deregulation, rising over 11% until late September. US equities retreated during the last months of 2018, down over 19% from September's highs through December amidst growing concerns regarding stretched valuations and mounting macroeconomic risks. As US equities "catch down" with the rest of the world, it appears that global growth may be converging again, this time slowing down in unison as future GDP growth is anticipated to soften over the next few years.

While many economic fundamentals remain strong, it is important to consider the impending risks of tighter financial conditions and slower growth on investment portfolios.

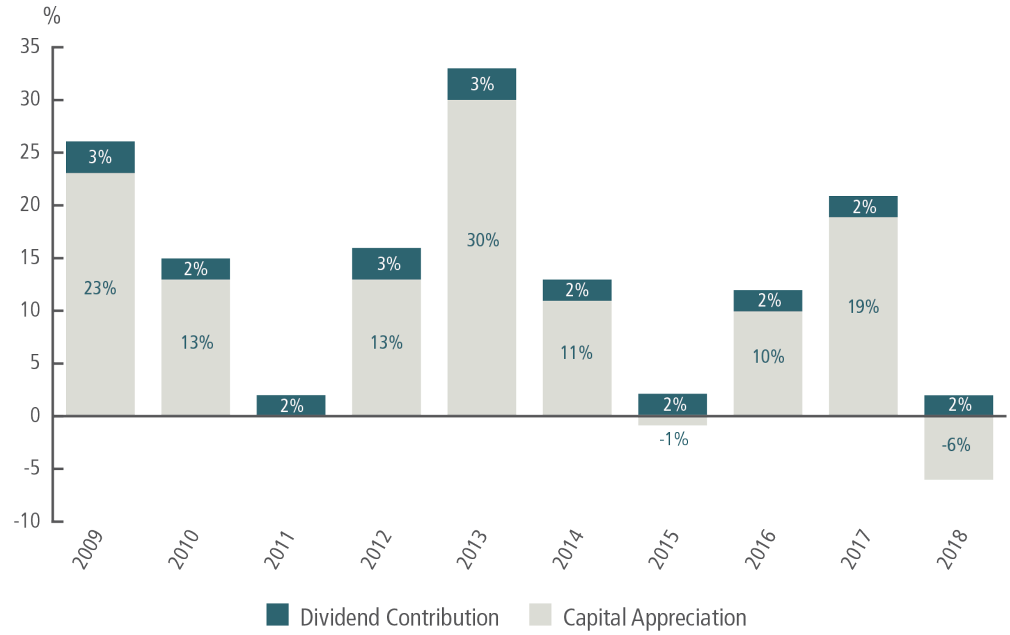
SYNCHRONIZED SLOWDOWN



Source: Real GDP Growth, Annual Percentage Change IMF, 2018.

Where does this leave investors as we move into 2019? While global economic growth is slowing, we do not see eminent signs of a recession in the near term. Even amidst the recent gloom, US jobless claims remain stable while US unemployment rates hover near 50 year lows. US wages continue to rise while taxes and oil prices fall on average. This, combined with US household incomes growing at a solid pace should support continued spending, thus providing an engine for global growth. While many economic fundamentals remain strong, it is important to consider the impending risks of tighter financial conditions and slower growth on investment portfolios. During low equity return environments, dividends play an integral role in investors' portfolios as they become a larger and more stable component of total return.

DECOMPOSITION OF S&P 500 TOTAL RETURN INDEX



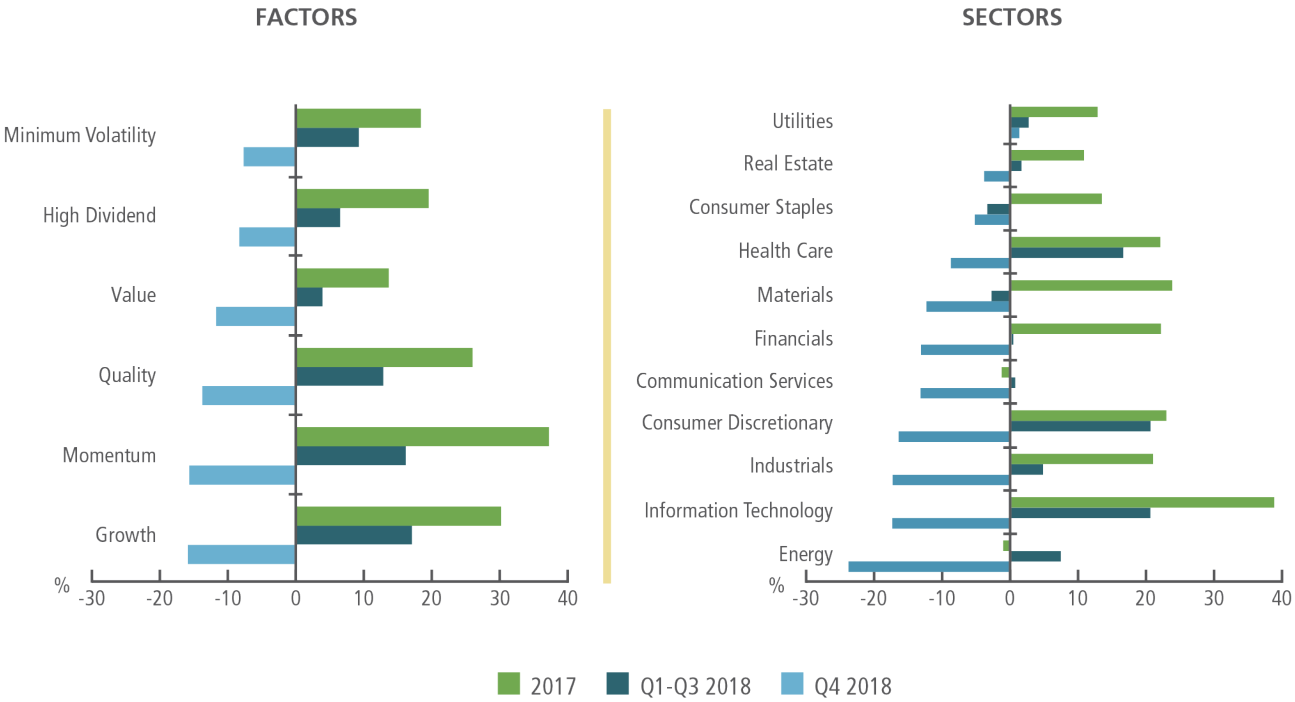
Source: Bloomberg, MSCI, Standard & Poor's.

Going forward we believe it is important for investors to continue to maintain equity market participation; however, it is important for investors to position their portfolios to weather more frequent bouts of volatility.

The crucial role of dividends for investors seeking a steady stream of returns was evident during the most recent US correction where Low Volatility and Dividend factors drew down significantly less than their Value and Momentum counterparts. Similarly, those less cyclical, historically dividend paying sectors such as Utilities, Real Estate and Consumer Staples proved to be much more resilient than their more cyclical, growth oriented peers. Going forward we believe it is important for investors to continue to maintain equity market participation; however, it is important for investors to position their portfolios to weather more frequent bouts of volatility.

While it is always tempting to try and time the markets, reducing equity allocations amidst sharp drawdowns may leave investors at risk of missing some of the best trading days, which history shows often follow some of the worst, as we have seen in December and January of this year. Tilting portfolios to favor high conviction, income yielding companies who have the earnings power to support their dividends may mitigate such risks. Exposure to these quality companies will likely reduce volatility and drawdowns, resulting in a more palatable portfolio risk/return profile, protecting investors from selling at adverse times and locking in losses, allowing investors to consistently maintain equity market exposure.

Q4 2018 ROTATION IN SECTOR AND FACTOR PERFORMANCE



Source: Bloomberg, MSCI, Standard & Poor's.
Minimum Volatility (MSCI USA Minimum Volatility Index), High Dividend (MSCI USA High Dividend Index), Value (Russell 1000 Value Index), Quality (MSCI USA Quality Index), Momentum (MSCI USA Momentum Index), Growth (Russell 1000 Growth Index). Sectors based on S&P Sectors based on GICS classifications.

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