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PRESENTATION

Alan Magleby *- Legg Mason, Inc. - Managing Dir., Head of IR & Corp. Communications*

Good afternoon, my name is Alan Magleby, Director of Investor Relations and Corporate Communications for Legg Mason. On behalf of the Company I would like to welcome you to today's call.

This presentation contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. These forward-looking statements are not statements of facts or guarantees of future performance and are subject to risks, uncertainties and other factors that may cause actual results to differ materially from those discussed in the statements.

For a discussion of these risks and uncertainties please see Risk Factors in management's discussion and analysis of financial condition and results of operations in the Company's annual report on Form 10-K for the fiscal year ended March 31, 2016 and in the Company's subsequent filings with the Securities and Exchange Commission.

During the call today we will also discuss non-GAAP financial information. Reconciliations of the non-GAAP financial information to the comparable GAAP financial information can be found in materials for this call, which are available in the Investor Relations section of our website. The Company undertakes no obligations to update the information contained in this presentation to reflect subsequently occurring events or circumstances.

Today's call will include remarks by Mr. Joe Sullivan, Legg Mason's Chairman and CEO, and Mr. Pete Nachtwey, Legg Mason's CFO. There will be at live questions in the room and those on the call who have questions can email them to me via the IR website at LeggMason.com and I will ask them if time permits. Now I would like to turn the call over to Mr. Joe Sullivan.

Joe Sullivan *- Legg Mason, Inc. - Chairman & CEO*

Al, thank you. And welcome, everyone; I want to welcome the people in the room today. Hopefully you have enjoyed lunch and we are sitting in the 49th floor Board conference room of Legg Mason in the New York Times building, a room that has spectacular views although today it is a little bit hazy out there. So I think we will have everybody's full attention on us hopefully.

I would also like to thank all of those listening in on the webcast. We have about an hour; we are going to try to march this pretty quickly because, as Al said, we do want to leave time for questions.

I hope you realize and appreciate that we always try to be transparent and, frankly, increasingly so. We have worked hard to help you to understand Legg Mason by providing an increasing amount of information around the Company. And today we intend to discuss four things which we are highlighting on the agenda page on slide 2.

First of all I will very briefly review our strategic progress and I will share some thinking on the balance sheet and how we think about capital allocation. Pete will then discuss and introduce some new non-GAAP financial measures, again, that we hope will help you to better evaluate Legg Mason. And then he will talk a little bit about our thinking on the value of our tax shield and then we will move into Q&A.

So if you turn to slide 4, let me just start by saying it was 4 years ago next week that I was appointed interim CEO and I was elected as permanent CEO about 3.5 years ago. And it has been quite the journey for me and for Legg Mason since that time. But at that time between really 4 years ago and 3.5 years ago when we did some important strategic work with our Board, it was the consensus of our executive team and, importantly, it was also the mandate of our Board that we needed to embark on a journey and aggressively reposition Legg Mason for the future.

Now to be clear, it was not our intent to abandon the existing businesses that we had, but rather to expand choice for clients as we saw demand evolving. And to become and remain an increasingly relevant Company for our clients. And I want to highlight this and emphasize this for everybody listening. This is our fundamental strategy, which is to expand choice for clients through diversification. It is very straightforward, very simple, expand choice for clients through diversification.

So if you look -- as you look on slide 4, we embarked on that repositioning by focusing on three priorities. Number one, enhancing our existing legacy strengths in three ways: our investment capabilities, our product and vehicle capabilities and our global distribution capabilities. That was number one, enhance our existing legacy strengths.

Secondly, we needed to rationalize our portfolio at that time by closing, by divesting or by merging affiliates that were either underperforming or subscale or nonstrategic.

And then finally, and importantly, we needed to add critical new investment product and vehicle or access capabilities in what we envisioned and believed at the time to be high-growth areas.

Now we are not completely done but we have made incredible progress along all of these fronts. We have executed -- and I think this slide really highlights and emphasizes it -- we have executed I would call a breathtaking level of activity in a very short period of time. We have remained Legg Mason along the way and I just want to pause and thank and congratulate all of my colleagues at both Legg Mason and our affiliates for what has been a great accomplishment.

Now I want to focus on that last piece, adding new capabilities accomplished through what has been an extraordinary and ambitious M&A agenda as depicted on slide 5. I want you to notice really the strategic nature of all of our M&A. And I talk about that frequently. We are not a financial holding acquirer or M&A firm, we are a strategic -- we do strategic M&A. Again, all of which has been done to fill what we acknowledge to be business gaps for us, be it again in asset class investment capability, be it in products and vehicles or access.

Now I want to just comment that while onboarding a new affiliate is a relatively straightforward process for us and we do it and have done it very, very well, commercializing a new affiliate always takes time and it's frankly subject to many factors. It can be regulatory requirements or various approvals, it can be internal product and marketing planning or sales training. And then always the market status in terms of investment performance of the affiliate that we've acquired, client demand and product acceptance. All of those things kind of factor in.

And what we have seen and what we have experienced over the last few years is that some of our acquisitions have actually hit quite quickly and quite well, QS being a great example where they are playing into a theme, an investment theme at that time and obviously we are thrilled with that. And others sometimes take a little bit more time and that is not necessarily unexpected. Martin Currie would be an example of that.

While we have had some real success with Martin Currie, Martin Currie had a very significant emerging-market capability that we acquired. And shortly after we acquired it investment performance for them in that strategy was challenged and the entire market was pretty challenge. So we haven't benefited yet from what they do in emerging markets, but we are benefiting in other areas.

But I think if you look on slide 6, what you see is a depiction of how we have evolved to become a more streamlined, a more focused and a more relevant Company over the last -- just over the last few years.

Now I would like to move on to slide 8 and talk a little bit about -- I have some comments about our balance sheet and how we have thought about debt, because I know that that has been a point of discussion with a number of people. And I think you will note if you look at this slide that we have used that thoughtfully over the years to accomplish a variety of initiatives or objectives. Three main points about debt with us.

Number one, our use of debt relies on what has always been a very robust cash generation capability. And what is now, and Pete will get into this, because of our tax shield, a very robust cash realization capability.

Secondly, we have a history of using debt and then delevering as able and appropriate, you can see it over time.

And our approach today is no different where we think we are being opportunistic in terms of what we are doing by using debt now -- and that is really the third point -- as opposed to equity capital to support our growth.

We are using debt now because rates, as we all know, remain at or near historical lows and credit spreads are reasonable, demand for fixed income remains high, especially on the long end of the curve. And if you think back, it was not that long ago that companies like asset managers really couldn't access debt investors on the long end of the curve, we have been able to.

And we have been able to issue debt at low rates on the long end of the curve and on very, very favorable terms. And so, we believe that what we have done is to thoughtfully source attractive capital to support our growth.

I want to talk for just a minute and highlight a couple important points about our last raise in particular. As you know, we did a series of transactions in the spring to finance a few of the transactions that we had recently done and then we termed out our revolver debt here in August by tapping the retail junior subordinated debt market again on what I think to be extraordinarily favorable terms.

And I have to just remind you, I cut my teeth in the industry on the debt side; I spent 28 years in debt capital markets. And so, I look at these things with a sense of history and a sense of where we've been and I don't project where we are today in perpetuity. And so seeing the opportunity, the pricing and the terms on which we could access the debt capital markets for 40 years, and on the terms was to me extraordinary.

The structure of the securities that we issued both in the spring, the $250 million Junior sub debt raise and the $500 million sub debt raise of a month ago or so, the structure of those securities provides us with incredible optimality. We have issued 40-year paper with only five years of call protection or lockout. That kind of optionality is extraordinary.

If rates are lower five years from now or are as slow or are lower five years from now we can simply call those securities at par and we can either -- and we can delever or we could in theory reissue those securities then or at any time over the next 35 years.

Now candidly I am hard-pressed to envision us actually calling this paper because I think it is just very, very attractive paper. But we have that optionality. We can call it at par in five years and any time for the next 35 years on 30 days notice we can call it at par and either delever, pay it off or reissue. No call premium, no prepayment penalty.

And then also as you all know, on this particular structure we do receive partial equity credit toward our leverage ratios from both our bank lenders and our rating agencies. And when you think about our overall debt structure, and again I have a history of starting in the business in 1979 with double-digit interest rates -- I know we are not there now, I know it looks like we are never going to get back there, but again I would not personally project in perpetuity where we are today.

We have an average coupon of less than 5% -- it is just a little less, so call it 5% -- 5% on our entire debt capital structure with an average tenor of 23 years. That is a debt structure that we are very happy about and with which we can live very comfortably.

I think if you look at slide 8 also just very quickly, I think it really tells an incredible story related to our cash flow. So over that period of time while we have navigated and used debt, raised it and then delivered along the way, you can also see we have since 2000 -- just since 2011, basically over the last five years or so, we have returned capital to shareholders in terms of our share repurchase and dividends in excess of $3 billion.

And we have also invested $1.5 billion into our business. So, that is a pretty powerful use of our cash generation and, as Pete will get into and talk about, our cash retention.

Finally what I want to speak to is our capital allocation priorities. Because many of you -- almost all of you when we meet frequently ask as to restate it and I want to talk about that on slide 9.

I want to be clear though, there is no static answer to this, no permanent answer to this and there never will be because our priorities change as the facts change. That said, the way I think about capital allocation right now, I like to keep things very simple and very straightforward.

Our first priority with cash integration is obviously to cover our current ongoing business requirements. Broadly speaking those requirements include things like CapEx, interest expense and taxes. We think about those in an amount circa $180 million a year.

Secondly, we focus on our dividend. And as you know, it is not a formal commitment on our part, it is something that is needed to be voted on and approved by our Board on a quarterly basis. But it is something -- our dividend is something about which we feel very strongly and we want to be a very reliable and enduring return of capital to our shareholders.

The current annual spend on our dividend is approximately $90 million, so $180 million in CapEx and interest expense and taxes, another $90 million in terms of our dividend.

The next thing we look at when we think about the allocation of our excess EBIT is investment in the business. And again, this is all about facts and circumstances. And if and as we and our Board see attractive opportunities to invest in the business we have plenty of cash to do so. But that is the number three thing.

And the swing piece, the variable piece of our allocation has always been and will always continue to be our share repurchase. With our stock being undervalued as it has been we have attempted to be intentionally consistent with respect to our repurchase activity. We intend to continue to be consistent and measured.

We have done work with many of our equity investors who say a consistent measured approach rather than stepping in and out and accelerating at times and backing off of others, the market appreciates a level set of consistent repurchase and that is what we have sought to do and we intend to continue to do. Again it is subject to facts and circumstances such as, as we have talked about, our stock continuing to be undervalued in our view and not having alternative investments to make into our business.

Last slide I will go over really quick -- very quickly is slide 10. Probably my favorite slide in the deck. Really highlights what our capital return story has looked like over the last several years. It has been an industry leading shareholder payout ratio. We have reduced our share count by 36% since 2010.

And if you look at the right side of the chart, we have tried to depict what potentially our share count would look like at the end of fiscal 2018, our fiscal 2018, if we were able to continue our repurchases at the current $90 million a quarter and at this price or at roughly where we are right now net of issuance of annual employee stock awards.

Along the way, while we have reduced our share count dramatically, we have restored and increased our dividend by a factor of 6 times. So, I think it is a pretty powerful slide in terms of shareholder return. We are proud of that and we want to continue to share -- return a robust level of capital to shareholders, but also balance that against our investment in the business. So I am going to pause there. Pete, the floor is yours.

Pete Nachtwey - *Legg Mason, Inc. - CFO*

All right, great, thanks, Joe. And again, thanks everybody who is here in the room and enjoying the view from the New York Times. But also thanks very much to everybody who is on the call with us today.

So my section starts on page 12. And as always we are looking to try and provide more transparency and more ways for you to understand our business and our financials, which we understand are in little more complicated than a normal integrated firm.

So in that light I am really going to hit on three things today, one is a couple new -- well, one tweaked but another new non-GAAP measure. Second is an update on our tax shield because we have recently affectively recharged that with the two acquisitions we have just done. And then third is to take a fresh look at how we view the valuation of Legg Mason whenever we are making this share buyback decision as Joe pointed out.

So we think it is very, very helpful not only you in the room but investors to kind of a see inside our heads both as management but also inside our Board room as to what we are thinking about, what kind of data and information are we using when we are making capital decisions.

So page 12 itself on the non-GAAP front, so we are making some tweaks to a number that we already disclosed called adjusted EBITDA. And then I ought to back up one second, all of you I am sure have followed the press over the last six months. The SEC has taken a much renewed interest in non-GAAP. And primarily due to people who abuse it.

We don't think we are in that camp, even remotely and that camp. But we want to stay well outside of that camp. So we are always very, very thoughtful about what we put out there from a non-GAAP perspective, cover that with our Board or our audit committee with our auditors. So you'll probably see us be a bit less aggressive probably than our -- than some of our peers and certainly some folks in other industries.

But having said that, we recognize and the SEC recognizes that non-GAAP information is very often helpful and we are going to give you as much of that as we can making sure we stay within the rules. So making some tweaks to EBITDA, and then we are rolling out a new concept we are calling parent operating margin, it is actually kind of in the form of a many parent level P&L which we will speak to in a couple of minutes. So, I will spend a couple minutes on each of them as to why we think they matter, how they are derived and then how we intend to disclose them in the future.

So, starting with adjusted EBITDA, the SEC views this as a liquidity measure. So they really sanction two types of non-GAAP measures, one is liquidity, the other is performance. Quite frankly I think many of the folks around this table and many users of financial statements think of EBITDA more as a performance measure than a liquidity measure. But there is some pretty well trotted guidelines in the SEC on this one that it is a liquidity measure, period.

So frankly, that is probably a nuance only an accountant or a lawyer could love. But what it means as a practical matter is we have to reconcile it to our cash flow statement as opposed to our income statement and we will get into that in terms of how we do that.

We currently show this on a quarterly basis with some of the tweaks we will talk about. We continue to intend to show it to you quarterly. But also to help you really digest it we are going to provide a bridge quarter over quarter similar to what we do with EPS so you can see what are the one time or unusual items that are hitting in a quarter that impact EBITDA.

And we will also show you in one place all the things that we as capital for, as Joe has showed you on the earlier slide. That is all in our current filings but you have got to hunt and peck for them all over our Qs and Ks; we will put that on one page as we go forward. So that will be every quarter.

Turning to page 13, this shows a couple things. First, again, making sure we are following the strict interpretation of the rules, GAAP number always needs to be provided first, so that is what is in the row up top. And as you can see that can bounce around a bit, particularly given last quarter it went negative. And it is not because we didn't have any earnings, it is because that is when we pay our bonuses.

And so, the GAAP rules will show a bonus as a negative cash -- negative use of cash only when they are paid, not as they are accrued during the year which is effectively how EBITDA looks at it. So that is one of the reasons we think EBITDA again is a more useful measure than GAAP cash flows from operating activities where we will get a benefit from delaying paying vendors or accelerating getting receivables in that don't really impact the long-term earnings power of cash generation of the Firm.

As you can see just in terms of absolute dollars it is a bit lower starting in December due to challenging markets that kind of carried over into March. And then you see it improving. And again, what we are looking at, the blue bars are the actual calculation, the dotted lines are the one-time items that went through that quarter. So if you add the two together you can kind of get to a run rate adjusted EBITDA number.

So again carrying over to the new calendar year, markets weren't that great in the first calendar quarter, but second-quarter they obviously improved. We also started to see the results of having a partial quarter in for Clarion and EnTrust.

Flipping ahead page 14, so this is the roll forward that we will give you every quarter. And as you can see it breaks out, similar to what we do in an earnings per share bridge, fiscal Q4 items of $51 million, the second column on the left; fiscal Q1 items in the red column, $41.5 million.

And then what is left in the middle is what really happened to run rate EBITDA during the quarter. And it improved through a combination of better markets, having a first partial quarter of EnTrust and Clarion in our numbers, but those were also partially offset by the fact we had higher sales commissions, I think it was virtually a record sales quarter for LMGD.

So, for the long term that is really good. For the instant quarter we get the sale we have got a commission to pay and that impacted last quarter. We also had lower performance fees as you are seeing across the alternative space versus the prior quarter. And we have some seasonal comp impacts that we always kind of talk about in the June quarter. But this will be a bridge that again we'll provide you every quarter and hopefully be helpful as you try and understand this metric.

Page 15 shows the required reconciliation to the most relevant GAAP number which is the cash provided by or use -- either provided by or used for operating activity, so that is the first bucket in the cash flow statement and the GAAP set of financial statements.

So of course we are going to add back to that to get the EBITDA, we are going to add back interest and taxes. But you won't see an adjustment on this page for depreciation and amortization because that has already been added back in the GAAP number.

The biggest add back, and just focusing on the June 16 column, is in other assets and liabilities. And again, that is virtually all related to just our bonus accruals effectively now being paid out in cash. But that will be an add back to get to adjusted EBITDA.

Then at the bottom, this is where you can see the uses in each quarter. And all of these again are readily available in various parts of our public filings but we will pull them together in one place.

And then I guess as a reminder before I leave a adjusted EBITDA, we always talk about the fact that it is a higher-quality EBITDA. It is not like somebody saying, well my kid is better than the neighbor's kid. No, this is actually mathematically better because we have cash taxes that we pay at about a 6% rate now versus the majority of our peers who are more full taxpayers at the 35% to 40% rate.

So any time you are thinking of EBITDA and using it particularly as a leverage multiple or assessment of leverage you have got to keep in mind a lot more of our EBITDA goes to bottom-line cash that we can use to service debt and invest in the business or payout to shareholders.

So page 16 -- now we are on to parent operating margin. Given the majority of our affiliates are on revenue shares and then the new ones, virtually all of which have minority interests and also have locked in bonus formulas that effectively combine to operate the same way as a revenue share. There is X amount of revenues that go to the affiliates and X amount of revenues that come to the parent.

What that means is that effectively those revenues going to the affiliates are a pass-through. We don't get to manage that day to day, they know exactly what percentage of every dollar of revenue they get and we know what percentage we get. So it is much more like a pass-through similar to our third-party [DNS] expenses that you are used to seeing us adjust whenever we calculate our operating margin as adjusted that you see every quarter.

So what is left over is what is available for us to manage on behalf of shareholders and that is what we will be referring to as kind of parent level revenues. So the graphic here at the bottom is really designed to just demonstrate that simplistically but we will walk through a couple more pages of detail.

So the total business economics that come into the consolidated Legg Mason, slightly more than half of that goes to the affiliates to run all of their businesses and platforms. So 100% of that that goes to the affiliates is actually an expense because they pay it all out; whatever they don't pay for heat, light, power, facilities, research, etc., they pay in their bonus pools.

So 0% margin on that because the affiliates are using it to run their businesses and fill up their bonus pools. The remainder comes to Legg, and that is what we get to manage, as I said, on behalf of shareholders.

So this is a new metric. We intend to disclose it at least annually so you can kind of see the progress. It is obviously not a metric that is widely used in our industry because most of our peers aren't structured the way we are other, although you certainly can find a lot of industries where people publish parent level financials particularly for holding company type operations.

Page 17 kind of gets to how do we get at parent margins. So again, since it is a non-GAAP measure we are required to first show you the GAAP calculation at the top of the page, but the meat of this is really below that first big solid line. And what we are showing you below that solid line is really a mini parent only P&L.

So basically it is the similar information, almost virtually the same information that we show to our Board every quarter when we talk to them about our financial results and how we are doing. So it starts with operating revenues on a GAAP basis of $700 million for the quarter. That is fully consolidated before any pass-throughs to third parties.

We then make the normal adjustment, as we have always done, to get down to operating revenues as adjusted. We back out third-party DNS expense. We also have a new item which are the performance fees at Clarion and EnTrust that stay with the affiliates. And you may recall the way those deals were structured any legacy kind of carrier performance fees stayed with them, we will start participating --.

Joe Sullivan - *Legg Mason, Inc. - Chairman & CEO*

And we did not pay for those.

Pete Nachtwey - *Legg Mason, Inc. - CFO*

And we did not pay for those, exactly. So those go into getting to this operating revenue as adjusted. Then after that we back out the affiliate share of revenues. So, effectively as a similar pass-through to DNS. So the revenue that comes to the parent that we get to manage in the last quarter was $237.4 million. And then we show you where we spent that.

And so, we spent $90 million of it in distribution. You can see that is up quite a bit from the December quarter. Virtually all of that is commission related. And then corporate, and this is the cost of the financial holding Company and all the costs of being a public Company were $31 million.

So after our parent expenses of $121 million we are left with an operating income from the parent operations of $116 million. And when you calculate the parent margin what level of income did we generate on the revenues that came to the parent, it is basically 48%.

Now we are not just showing that to you to just to artificially show you a bigger number than our normal one that is down in the mid-20s%. The point of showing this to you is so that you can see better where the operating leverage is in the system that we get to manage. And I think we will see that a bit more in the next couple pages.

So slide 18, as you can see again with GAAP number first at the top. The bullets at the bottom disclose the one-time or unusual items that are excluded from the parent margin calc just to give you a better sense of kind of a normalized run rate on this metric. And then you can see that it has increased nicely over the prior quarter.

And as we said on last quarter's earnings call, we expect our consolidated margin to go up this next quarter and we obviously would therefore expect the parent margin to go up as well. And it is going up because of, again, this operating leverage of the parent and the fact that we have added additional earning streams from Clarion and EnTrust.

Page 19 I guess kind of shows a little more clearly -- I know there is a lot of bars here and we will dissect those. But a little more clearly how this leverage at the parent level works. So, what the graph is at the bottom, you will see the X axis has $10 million, $20 million, $30 million. So those are assumed increases in top-line revenue.

And what the bars are is -- the blue is what would happen to our fully consolidated GAAP margin. The orange bar is the way we currently calculate operating margin as adjusted after pass-throughs and then the green is the parent margin.

And so you can see on the left hand side -- but first of all we don't normally show you, we never show you fully consolidated GAAP margin because no one in the industry calculates it that way. That is fully consolidated before backing out third-party distribution expenses. But again because we are in non-GAAP land here it is important we show you that even though nobody else in our industry is going to show it to you.

The real important bars are the orange and the green. And you can see the orange for every $10 million -- or for a $10 million increase in revenue we get a 30 basis point increase in the margin on a consolidated basis. For every $10 million increase at the top line we get a 40 basis point increase in the parent margin.

Again these are based on some hypothetical assumptions that are outlined in the footnotes. But kind of reasonably representative of our business in terms of the proportion of mix between institutional revenues versus retail revenues. Because on institutional dollar revenue comes to the affiliate; at the parent level we have virtually zero cost for that. Retail dollar revenue we do have the sales commission and that is reflected in here in terms of the mix as to how we are thinking about the impact on margin.

But if you look at the green bar, so we increase from $10 million to $20 million to $30 million the steepness of the curve because of the operating leverage at the parent is much more apparent when you look at things just kind of on a parent only basis.

So again, probably going to be a lot of questions on this but we want to get as much facts out as possible. Alan and I are happy to walk people through details of the calculations with all the information that is in here -- either we can do that in Q&A or we'll do it at a later point.

So, enough said on non-GAAP measures. It is still going to be an area we are going to continue to look at as SEC guidance evolves and we watch what peers do and if there is more we can do to provide you non-GAAP information we will do that.

And then wrap up on two items, tax shield and then enterprise value. So if you look at slide 21, this is something you see us pretty much every quarter. I think now we put it back in the appendix in our earnings decks. But every once in a while we like to do a deep dive on this so you understand how all the pieces and parts move.

So on the left-hand side shows the tall bars are GAAP tax rate, 31%. That is a little bit lower this year, that is projected for full 2017. And it is a little bit lower this year just due to some vagaries of the deal related costs. But that is typically going to run 35%-36% range.

The cash tax rate on the other hand is at 6%, that won't fluctuate because of some of these other items that are impacting the GAAP rate. And we do expect it to stay under 10% for the rest of this decade. So this year it is 6%, last year I believe for the full year it was 4%.

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On the right-hand side we show you the level of earnings that we can shield from taxes first, which is $3.5 billion. And then the related estimated cash tax savings. So over the life of the shield we anticipate saving $1.4 billion of extra cash to invest in the business or return to shareholders after tax.

Joe Sullivan - *Legg Mason, Inc. - Chairman & CEO*

Or delever.

Pete Nachtwey - *Legg Mason, Inc. - CFO*

Or delever. And then if you went back to three years ago at the last investor event where we went through this in a little more detail, the similar numbers were the [$3.5 billion] going back to 2013 was [$3.8 billion]. That worked down before these new deals to [$2.8 billion].

And then on the cash tax savings side go back three years ago that number was $1.5 billion, right before the new acquisitions it had worked its way down to $1.1 billion meaning we had realized $400 million of cash tax savings that went to doing a lot of things that were back on the capital slide that Joe showed you.

So we now, with the new acquisitions, built it back up almost to the same level that it was three years ago. So we are back up to $3.5 billion in terms of --.

Joe Sullivan - *Legg Mason, Inc. - Chairman & CEO*

Done so with debt.

Pete Nachtwey - *Legg Mason, Inc. - CFO*

Exactly. And so the refresh of this tax shield has been paid for 100% with debt. So the shareholders are going to get the benefit of that tax savings, that incremental going from $1.1 billion to $1.4 billion of tax savings. So tax savings before these deals, $1.1 billion is what we expected, after the deals $1.4 billion. That all goes to the shareholder not to the debt holders.

So it is kind of another nuance to how you think about the power of the debt because it is already very, very long-term, it's already very low cost. Just after tax -- Joe mentioned its average below 5% on a blended basis.

If you just deduct interest expense it is below 4%, it is now at a low 3%, I think, Gregg -- on an after-tax basis, before taking into account the $300 million of cash savings we get from the goodwill and intangible amortization. So it is we think a very powerful way these businesses have been financed on behalf of the shareholder.

And then last couple of things on this, slide 22 is basically an illustration of the additional cash that we will have available on an after-tax basis. So the top line, the $400 million for either Legg or a full taxpayer, that is -- we don't give earnings guidance but we will take Thomson ONE consensus for the year of $400 million.

And then just apply our cash tax rate versus a normal company's. And we end up paying $24 million of tax on that $400 million versus a normal company paying something in the $160 million range. So it gives us an extra $136 million of cash after-tax to be able to run the business or return to shareholders.

Joe Sullivan - *Legg Mason, Inc. - Chairman & CEO*

This is also something we talk to the rating agencies about to help them to really appreciate the fact that when they evaluate us from a ratings perspective the quality of our EBIT and ability to repay our debt is much greater than our (multiple speakers).

Pete Nachtwey - *Legg Mason, Inc. - CFO*

Exactly. I think the first time we pointed that out to the agency, not that they are not very smart people and do a great job of modeling and understanding our business, but that was one that gave them pause. I said, yes, we can't -- we use EBITDA as a basis for the leverage ratios that we kind of set whereas a BBB or a AAA or whatever. But those leverage ratios use EBITDA without taking into account a firm like ours that is paying very little out in the way of taxes.

And they have kind of said, geez, we are going to give you quality credit for that, it is hard to put it into their ratios. But certainly you could, you could find a way to do that.

Page 23, some of you will recall -- for those of you who were at our investor event three years ago, for the first time we try to show you a time line as to how the tax shield might get used. Because people were struggling with, okay, how do you think about putting a value on it if you don't know how fast it is going to be used? And then we don't give you earnings guidance so you can't come up with a way to do that.

So, we are still not giving you earnings guidance, but what we are doing is using some reasonable assumptions that are listed out in the note in terms of what normal markets, equity returns of 6%, fixed returns of about 2%, alternatives of 6% and a conservative organic growth rate of 2%. So if you just call those assumptions -- generic assumptions you can plug in whatever you would like. But we are just setting those out as something that is reasonable.

Then this gives you a picture of how fast the shield will get used. The green bar -- the green portion of the bar relates to the purchased goodwill and intangibles. The NOLs and foreign tax credits are in the blue. And frankly we don't start using the blue stuff until we become a taxpayer. Right now we are not a taxpayer even though we are earning tremendous amount of cash earnings. The tax shield has been almost -- in the US has been fully shielding us from any federal tax and most state taxes.

So you will see in 2019 though that is when we start becoming a federal taxpayer, that is when -- and when we will start using the NOL and foreign tax credits and then they get used going all the way out to 2032.

But when you look at this chart, you can calculate the average but we have done that for you already, it is six years. So this shield has an average life of six years. Take that fact and then a discount rate which we didn't put in the body but the very last page of the appendix does a buildup of a hypothetical discount rate.

And this is something we have worked with our bankers on, several of them, just to triangulate as the same what would -- if we were selling the firm, which we are not, but if we were what should we expect to get paid for our shareholders for this tax shield? And they said, well, somebody -- a buyer or seller would probably be using a junior debt rate to discount this.

And the reason being you have got to cover all your other expenses plus your senior debt interest expense before you are earning any income to start using the shield. So it really would fit in the junior part of the capital structure.

We obviously now have junior debt, so we kind of know what that is other than our junior debt is 40 year life not 6. So what you will see back in the build up, we start with a 6 year senior note rate which is right off the curve of where we are trading today, it is somewhere around 3.4%. And then we add in kind of two notches, the bankers would typically say 75 basis points for each layer down you go in terms of more junior debt.

So we have rounded that up, instead of saying 75 we did 80 basis points, so at 80 we already have junior debt so you have got to get there. And then another 80 before you get to where this is. So it rounds out to a 5% number. And that kind of feels like, Joe, I wasn't a debt trader for 20 years. Thank goodness I always have a wing man or a boss who has done it for 20 years every time we are doing debt.

But I have been in business for 40 years and the idea that you would use a 5% discount rate for something like this seems incredibly low. On the other hand, interest rates have been where they've been for the last six years and nobody is forecasting them coming off the bottom. I mean they may start ramping up in 25 bp increments but they are not going up very steeply in the next six years.

So, again, you guys can do your own math, but when we do this math average life six years, discount rate of 5%, we get about $1.1 billion in value. So and I will show you that in terms of what -- how does that fit into our thinking and then we will go to Q&A.

But if you go to page 25, enterprise EBITDA value calc, and we are not trying to do your guys jobs for you, you guys do a great job at that already. But we did think it would be helpful to show you what we show to our Board and our finance committee every quarter just as we continue to talk about is buying back stock the right use of shareholder capital.

So you have seen this before, the left-hand side starts with our equity market cap at the end of August, it hasn't really changed much since then. We add in our total debt and then we back out the three things that we would expect to get paid for in a transaction over and above somebody buying the business, excess cash, the majority of our seed capital that is liquid and then the capitalized value of our tax shield. So that gets to an implied enterprise value of $4.2 billion.

And then you look further down, we actually give you a projected adjusted EBITDA number for September. So you did hear me say projected for a firm that never gives guidance, but we aren't not going too far out on a limb, we only have three weeks to go. But we have basically said we have used that projected number as opposed to trying to pro forma prior quarter because this effectively shows you now a full quarter of EnTrust and Permal.

It still has some transition and acquisition costs of about $15 million that are reducing it and it also doesn't show a full amount of EnTrust and Permal savings yet. But the $155 million is kind of a good number, adjusted then further for the $15 million of transition costs that are in here that will go away. And then we have got another $4 million roughly of EnTrustPermal savings that we will get in future quarters.

So you kind of look and say, if we were doing a future run rate it is more like $170 million, but we have used the $155 million just to be conservative. Use that, annualize it, $620 million, we come up with an enterprise value to EBITDA multiple of 6.8 versus the average of our peer group is 9.2, top quartile 9.7. And frankly three years ago, four years ago when Joe took over we wouldn't have been arguing for a premium multiple to the midpoint but I think now we are.

As you saw earlier in all the strategic things that we have done. Is it top quartile, top decile? You guys can judge. But I think it ought to be at least above the median. But that is 2.4 times $620 million. So when we get that map our Board and we feel we are undervalued by roughly $1.4 billion, $1.5 billion as a minimum. And that is what gives us the confidence to be buying stock back as a priority use of capital unless there is some other opportunity to invest in a business that comes along.

So why don't I stop there, Kevin has got some microphones. We would be happy to take any and all questions. Al, I think people can email ones to you and we will turn it over. So the first one will be from Chris Harris once he gets his mic.

QUESTIONS AND ANSWERS

Chris Harris - *Wells Fargo Securities - Analyst*

Okay, a question for Joe. You had mentioned repositioning Legg Mason and we have seen you do that now the last couple of years. You mentioned in the comments there you don't think you are quite done yet. I'm just wondering if you could expand on that a little bit. What else do you think needs to get done? And maybe what are your major strategic priorities over the course of next year or two?

Joe Sullivan - *Legg Mason, Inc. - Chairman & CEO*

So, look, I think -- first of all I think, Chris, maybe the number one strategic priority we have is kind of pulling all this together and making it work. We like what we have in terms of different asset classes and different investment capabilities. But now we've need to bring it together.

This industry is going- - Mike has written extensively about it and others have as well, others of you have written about it -- this industry is undergoing substantial change, disruptive change. We do believe that increasingly the business is moving towards solutions and we feel good about the different pieces that we have to be able to contribute to providing more solution, multi-asset class solutions.

So, I would say the number one strategic priority that we have right now is to make all of this that we have put together work, not just work on an individual basis but work together with distribution, with products and vehicles and in a solutions type context. And we have got the capability to do that through QS. So, QS has been a multi-asset class manager in the past. They are today. They do manage products today that are multi-asset class.

I think in terms of what other M&A we might do, look, I think we feel like we have got a significantly greater part of the landscape covered today than we did only three, four years ago. From a big picture standpoint we might like private equity at some point or something more related to private equity energy or something like that. But I don't see anything big on the horizon. I want to be very clear about that. I don't see any major transactions on the horizon.

Again, when we think of M&A we think about it in terms of investment capabilities and we are pretty well set there. Again PE or energy or something like that, we think about it in terms of products and vehicles and we have done the acquisition -- or the investment in Precidian. We like where we are; we have added and invested, added an ETF capability, we have got ETFs out in the market. So we feel good there, we don't see anything there.

I would say there could be some investments, continued investments in access. And what do I mean by that? We have done a couple of things, we did iVEZT which was a portal for people who didn't have access to 401(k)s, corporate 401(k)s. We invested in that. We invested -- acquired Financial Guard, we are excited about that. We will be open to smaller kind of technology complementary acquisitions that strengthen our distribution capability particularly around technology.

I think on the investment side, just to close out on that, I think the M&A around that I think will more be about strengthening our existing affiliates. And we have more discussions right now about teams or smaller firms that could strengthen an existing affiliate. That is really where our M&A is focused on right now. We are really not focused on bigger transactions right now. Is that helpful?

Chris Harris - *Wells Fargo Securities - Analyst*

Yes, thank you.

Unidentified Audience Member

Thanks. I guess my question is going down the same path and it ties into the usage of capital. Now that you have transactions in house and still early days where you have lived with them for a while and -- I mean how do you think about the need to actually increase maybe seed capital that you are deploying towards these new affiliates and new strategies?

Because that is I guess the other piece of the growth puzzle that maybe you didn't touch on too much in this. So, could we see an increase in seed capital usage with new affiliates or as you look on how to accelerate leveraging them?

Joe Sullivan - *Legg Mason, Inc. - Chairman & CEO*

Pete, you can jump in as well. But I think that is a good question. And I think we are looking at increasing our seed capital. But I think we are also -- one of the things Gregg Gorman, who is with us here, and our Treasurer, has done a great job at is managing our seed portfolio. We are a very aggressive recycler of seed capital. And so, we tend to fund a lot of our new seed capital requests by virtue of recycling.

But I do think over time, and particularly with new affiliates, I think the request for seed will continue to go up, we know that. I would expect that is why those are some of the uses of capital that I think could come into play that would be kind of investments in the business.

And I think the other thing, one of the things that we are thinking a lot about is our fund range. And our fund range has -- like a lot of funds has kind of grown significantly over time and we are left with a lot of funds that we are questioning now that maybe were good ideas and have a small amount of AUM. And the question is what do we do with those and is there some seed that we can repatriate through that. But, Pete, do you have anything to add?

Pete Nachtwey - *Legg Mason, Inc. - CFO*

No, that's a good summary. And again Gregg -- Gregg Gorman, for those who are on the phone, sitting immediately to my left, does a fantastic job kind of running day-to-day our capital committee, which consists of a host of folks at the parent level. Including product through Tom Hoops, including M&A folks with Jeff Nattans, including some of the other compliance and risk people that need to be around the table.

It also includes a couple of affiliates. If we are going to be investing shareholder money why don't we get some of the guys that actually do it for a living for third parties. So it is a pretty robust process and, as Joe indicated, we've been very aggressive about recycling. We set targets -- every one of our seeds is looked at every six months to see if it is on track to what they thought they were going to be able to do, how is it performing on a relative basis, etc.

And when things -- stuff sometimes just doesn't pan out, maybe because there really wasn't a market for it, we thought there might be but there ended up not being. Or performance wasn't there or whatever, we pull the plug pretty quickly. So we have recycled, I don't know, $100 million probably of our existing $371 million the last two years or less.

And then the other thing we encourage our affiliates to do is go find partners. So, very often they will have clients who are interested in a certain area and they will go cut a very favorable deal with them on fees and so forth because they are placing a bet on something that is untested. But very often affiliates are coming up with their own seed. So I do think over time, yes, as we grow the natural --.

Joe Sullivan - *Legg Mason, Inc. - Chairman & CEO*

And you can do that with distribution partners, too. When we launched recently -- actually the week after the Brexit vote we launched a fund -- a UK fund for RARE Infrastructure in London. And it was all done with client money. So it had been worked on coming into Brexit, into the Brexit vote. And I have to be honest, I was shocked that we could actually get it launched and it launched I think with about $25 million in client money and grew pretty quickly.

I think it is up near $50 million right now in a pretty short period of time. But that was all done with client money. So, there are certain times when you go and you have a client actually -- one client or two seeded, but in this particular case it was seeded among a large number of clients that then launched it into the market with like $25 million or thereabouts in seed.

Pete Nachtwey - *Legg Mason, Inc. - CFO*

And the other thing that will give us a little more juice of what is in there today, back when we acquired Permal we acquired a number of very long-term products that -- while we call it seed it is actually GP kind of co-investment type money. And those things have a life and over time we will be able to get some of that back.

So, we basically kept the seed capital flat I think for like three years, even though we have been growing. But I do think the natural tendency is going to be for it to grow, but it shouldn't grow by leaps and bounds.

Alan Magleby - *Legg Mason, Inc. - Managing Dir., Head of IR & Corp. Communications*

Mike?

Unidentified Audience Member

Yes, just a couple questions. First, Pete, just on I guess slides 17 through 19, just on the parent margin, I guess just a few things. One is on the revenue sensitivity is that on operating revenue or that parent revenue number and does it depend on the margin?

Pete Nachtwey - *Legg Mason, Inc. - CFO*

No, so it is total. So we basically had to keep it apples-to-apples, it was $2 million on a GAAP consolidated basis for all three.

Unidentified Audience Member

Okay, all right, got it. And then I think in the past when we thought about your margin, there was always somewhat of a limit or a peak maybe just given the structure. So just wanted to get any update based on whether it is the equity incentives or anything structurally that is changed with the new affiliates?

Pete Nachtwey - *Legg Mason, Inc. - CFO*

Yes, I mean obviously the margin can't grow to the sky, it takes something to be able to run the business. I think again you are seeing our kind of legacy margin marching up based on the operating leverage that we have. But you will definitely see the parent margin move faster than that because it has got a smaller base. And also we are able to control costs at the parent level fairly aggressively.

So, should that number be north of [50], yes, I think that is -- assuming normal markets just given the new affiliates that we've added given the full EnTrustPermal saves, etc., we certainly see a path to getting north of there. And can it go higher? Sure. But again, we have to grow the business to do it.

Unidentified Audience Member

Right. Okay, and then just a quick one for Joe. Just on the strategy, the affiliates that you have added, I think when you look at the buckets or the needs, it does fill a lot of the categories where if you look at the industry there is demand. I think when we look at the results, and some of these are very soon, meaning they have just occurred. But some of them you do you have modest outflows, nothing that significant.

But just wanted to get a sense, when you look at the transactions that you have done, are there any where the demand picture is changing or is it just a timing factor in terms of integrating them, getting the products out into the sales force? And I understand it has been quite a year or last 12 months for flows for all categories. But just wanted to get an update there.

Joe Sullivan - *Legg Mason, Inc. - Chairman & CEO*

Yes, I would say -- good question and fair question. First of all I think when it comes to transactions, we take kind of a longer-term view of it, we don't take a quarter or even a year because, as I mentioned, things can happen.

So, for example, we acquired EnTrust merged it with Permal, at a time when that space -- when the hedge fund space is under a lot of pressure. So we have had some outflows that were deal related, but also just outflows there that are more just sector related right now.

Now we don't -- does that mean that, gosh, we shouldn't have invested in EnTrust? No. We actually think that EnTrust helped to diversify us from both a client standpoint and from a product standpoint. But we are going through a period here where that space is under pressure.

Conversely, we are going through a period when I think demand for real estate is increasing. We are seeing Clarion continue to drive positive net flows. I know a lot of people -- or there are some people who have subscribed to a narrative that commercial real estate prices are peaking. We don't necessarily see that.

Not to say it is in the first inning of the game, but we don't think it is in the ninth inning either, it is probably in the sixth or seventh inning. Cap rates are still low with rates being -- interest rates being low and will probably for a while. That probably implies continued low cap rates. The demand side of the equation for real estate is increasing. What did we just see, Al, that it is being included as a separate category in for (multiple speakers)?

Alan Magleby - *Legg Mason, Inc. - Managing Dir., Head of IR & Corp. Communications*

Index being broken out of financials into a separate sector.

Joe Sullivan - *Legg Mason, Inc. - Chairman & CEO*

That is only positive, that only reinforces that investors are going to need to have an allocation and a robust allocation to real estate. So all of those demand factors play in favor of Clarion kind of offsetting what are some pressured factors for EnTrust. But we love the EnTrust acquisition in combination with Permal because long-term we believe that the kind of uncorrelated returns that a firm like EnTrustPermal can deliver are going to be important.

Away from that whether it be RARE or whether it be Martin Currie or whether it be any of our acquisitions, it is just ebbs and flows, it is just kind of markets. As I mentioned, we acquired Martin Currie, we are very pleased with that team and with that affiliate. But of course as soon as we did they had a reasonably robust emerging-market book and that sector got under pressure. It happens.

But the good news is other things that they are doing are working well for us. So, we try to take kind of a longer-term measured approach to it. I would say the only two demand questions that you are asking, one is positive in real estate with Clarion, but the one that is under pleasure is EnTrustPermal. Those are more sector related.

Alan Magleby - *Legg Mason, Inc. - Managing Dir., Head of IR & Corp. Communications*

[Mike, thank you].

Unidentified Audience Member

Great, thanks, and thanks for hosting today's event. So two questions here, first for Joe. You had mentioned certainly QS big success, Martin Currie some challenges there. So just curious as you are thinking about Martin Currie, what sort of lessons learned do you have from that transaction?

And how has that impacted your thinking in terms of doing future deals, even some of the deals that you have done most recently, whether it is in terms of what you are willing to pay, how you go about structuring them, views on synergies, payback period, return expectations and so forth?

Joe Sullivan - *Legg Mason, Inc. - Chairman & CEO*

Look, we -- actually it is interesting you ask, Mike. We do on a regular basis review the transactions that we have done with our Board and what the underwriting was and what the results have been. And our Board recognizes, as we do, that things that -- you project and then the markets happen and then performance can happen and things like that.

I want to be clear, if I am suggesting Martin Currie has been a disappointment it hasn't been as robust as we would like. But we are, for example, in this particular month, and we have been seeing decent flows in different parts of Martin Currie. So we combine Martin Currie with our Legg Mason Australian equities unit. And they have added some support to that business and we have combined them and so Martin Currie in total is actually growing and recently seeing some inflow.

So I wouldn't characterize Martin Currie as a huge disappointment. It is just that when you look at it compared to QS, I mean QS for all intents and purposes doubled their size within a year. But remember, they were in the sweet spot.

I think we felt like when we added Martin Currie one of the things we said is we think this is a good team to get on the field with and that we could do things with them in terms of bringing their products to market in the US and expanding their product capabilities.

I think if there is a lesson -- it is a fair question, if there is a lesson and I am guilty of this, this is my -- and not just with Martin Currie but probably with all of our affiliates -- is that the time it takes -- we understand how to onboard them but the time it takes to do some of the stuff is typically greater than I expect.

So, for example, merging their fund range into ours in the cross-border space took a tremendous amount of not only time but work and effort and focus on the part of Martin Currie. It was important to get done, it saved Martin Currie and us a fair amount of money. But it takes longer and more work and more focus than I probably fully appreciate.

In a couple of cases if you think about QS, it is rather extraordinary because when we acquired QS we immediately combined it with Batterymarch and with an internal affiliate called Legg Mason Global Asset Allocation. So we basically brought three businesses together. And just having one business join us -- again, we can do the onboarding pretty easily, but there is still some transition and adjustment period from a firm that has been on its own to becoming part of a corporate enterprise.

You start bolting and putting other affiliates together and that gets even more complex. We did the same thing with Martin Currie. So as I mentioned, I don't think this got a lot of play. We added Martin Currie so we had to have them kind of connect with us and plug with us. Again, we do this stuff well. You have never heard about us fumble an integration. We don't call it integration, we call it onboarding, but you haven't heard about us fumble this because we do it quite well. But there is a lot of work to it.

Oh, by the way, we then connected Legg Mason Australian equities into them. Again a lot of work. Meanwhile we are merging Martin Currie's fund range -- cross-border fund range into ours. So, there is just -- I am ambitious and I want to get it done and let's keep going. And so, I probably tend to underestimate frankly the distraction factor and the impact of that. And that is a lesson.

Unidentified Audience Member

Great, thanks. And just the second question for Pete, two-part question. I just wanted to touch upon some of the adjusted EBITDA numbers that you provided. So first, Pete, just wanted to understand a little bit how that differs from your adjusted earnings numbers that you have given historically?

And then the second part is you have given some reconciliations here on the adjusted EBITDA versus cash flow. Just wanted to understand how we should think about the adjusted EBITDA number versus say pretax earnings. And maybe some sort of walk from pre-tax on the income statement to the adjusted EBITDA?

Pete Nachtwey - *Legg Mason, Inc. - CFO*

Yes. The primary difference is between the old adjusted EBITDA. The old adjusted EBITDA exactly mimicked something we call bank EBITDA so it was a way the EBITDA was defined in our revolver for debt covenant purposes. And as we took a look at that particularly with, again, the SEC's renewed focus on this, we said, well, the problem is EBITDA is a liquidity measure and you can't adjust out things that are going to be cash settled.

So our bank revolver gave us a $100 million bucket for one-time transition and related costs that we could add back. Well, under the SEC rules in terms of liquidity measure we shouldn't be adding that back. So what we were trying to do was find a way to thread that needle, not be adding it back overtly but through the ways that we are highlighting here with the dotted lines in the bar graphs, etc., to be able to give you a path to -- how do you think about kind of a normalized EBITDA number.

In terms of getting it down to earnings, I mean at the end of the day the key adjustments of backing out interest, taxes, depreciation and amortization. But if you are really trying to get to a cash -- more or less a cash earnings number, if you are starting with that number and you are backing out our cash interest expense and you are backing at our cash taxes that is probably going to get you as close to that as we can.

And I would love to be able to just do that math for you, but that actually is verboten again under the SEC rules in terms of -- and again, it is not because it is not useful to you guys, etc., it is because people have abused these things in the past. And we are a little frustrated; we have never been an abuser but unfortunately we get boxed in by the rules that are targeted at those types of folks.

Eric Berg - *RBC Capital Markets - Analyst*

Thanks, Eric Berg from RBC. Joe, I think you made it pretty clear to me at least that the most important work with respect to acquisitions is really what happens after the acquisition is completed, the adding of distribution, the developing of new products and so forth.

But I guess what I would like to know is you talked at the beginning about diversification, no doubt about it, Legg is a profoundly more diversified Company than it was when you began.

My question, do you think that diversification in and of itself -- and this is a topic that people have debated, I'm not sure if there is a right answer -- in and of itself creates value? Just being in more businesses, does it in and of itself create value?

Joe Sullivan - *Legg Mason, Inc. - Chairman & CEO*

I think that it -- look, it is our -- first of all I think it helps to keep us more relevant with clients over market cycles. And as a result kind of spreads our bets across a variety of businesses all designed I think individually. So the way we sort of think about where the business is going is, as I mentioned earlier, sort of increasingly to solutions. We actually think that is where the business should go.

I think longer-term -- I think what has been an individual product or fund pushing -- pushing, I don't like that -- but fun sales business is going to evolve we think to more of a solutions models type business. And so the good news is we have got more -- we think of that or the imagery that we have been using is that of a tapestry, right. Weaving and investment tapestry, individual tapestries for individual client objectives. And we have an increasing number of threads to be able to help weave that tapestry.

Now as we like to say, we will continue to offer individual threads but we would much rather sell tapestries. And that is how we think about it. So the diversification plays into being able to do a better job of weaving it. We may use in some cases ETFs or other things if we don't have a capability. But I think it is all about kind of multi-asset class. And we have more of those asset classes today to offer.

And so if you think about, for example, income. If we are dealing -- if we are trying to create and weave an income solution today we can bring together Western or what Brandywine does or what Clarion does or certain things that EnTrustPermal can do or what RARE can do. So we have got -- or our equity managers and dividend equity income.

So we have got many sources of income that we can try to optimize in a way that meets an investor's objective. And so, it is not just diversification for diversification's sake, but diversification to create more choice for our investors. I think ultimately that will yield a benefit -- a greater benefit to our shareholders as well. It should serve to smooth earnings and not have us completely -- all of our chips in one particular asset class.

(Technical difficulty) tried to diversify this Company, we talk about it over and over again, not just in terms of investment capabilities but in terms of products and vehicles. So now we are not just in the mutual fund business, not just in the cross-border space, we are not just in -- we are also now in ETFs. We have also been trying to diversify our distribution.

We have institutional distribution, retail distribution, we have US distribution, we have international distribution. We are now moving into the traditional kind of distribution and now with Financial Guard we are moving into a capability that is digital. And so, we are constantly trying to diversify and cover as many potential choices and markets and channels as we can.

Pete Nachtwey - *Legg Mason, Inc. - CFO*

And as it goes to -- the earnings volatility aspect, as Joe mentioned, and volatility is a good thing if you are valuing an option. It is not necessarily a good thing if you are trying to value a stock, particularly if the stock is one that over the intermediate to longer term we would like to have people think of us as a very steady dividend payer and one that can grow that dividend.

But if you have got very volatile earnings streams that is tough to grow the dividend as much as we like. So, we think from the financial guys' perspective and think about how our stock gets valued, we think that diversification is actually helpful there too.

Eric Berg - *RBC Capital Markets - Analyst*

And just one quick question, financial question for you, Pete. Your new measure, parent operating income, would that be literally identical to the penny to which you are currently considering operating income available to Legg shareholders? Would that be the same?

Pete Nachtwey - *Legg Mason, Inc. - CFO*

It would be although we are adding back to that parent margin a number of the one-time charges. So once we get past the one-time costs, yes, theoretically parent operating income should equal our consolidated operating income.

Eric Berg - *RBC Capital Markets - Analyst*

Thank you.

Unidentified Audience Member

Yes, just wondering if you guys could provide us with an update and what you saw in the month of August in terms of AUM or flows?

Joe Sullivan - *Legg Mason, Inc. - Chairman & CEO*

Sure. I think first of all we -- I am going to say this before -- I will answer the question but I went to say this. I would always ask you -- you know it is interesting, we are talking about this this morning. I know you went to know and, by the way, we are I think still the only firm out there that actually provides flows on a monthly basis. I am surprised you guys let everybody else get away with that but that is your battle to fight.

We actually feel good about providing flows. The downside of that is you get in some cases too myopically focused on, uh oh, this month. And so, for example, I can tell you absolutely I have things that I see coming up, and Pete, we all see things coming up, reallocations where we see things that we know are going out at one of our clients that are also going to be replaced by this. Or sometimes things are going out here and they are coming in here. But timing moves around a little bit.

So we would love to have every single month flows going up, but the reality is they go in and out. And I would caution you about putting too much emphasis on any given month's flows positive or negative. So that is my disclaimer urging you all to kind of stay measured.

I am thinking, Rob, of your thing that I read every week I guess where you say don't put too much weight into these mutual fund flows because there are things that we don't know. Well, there are things that you don't know. So I would urge you not to put too much on monthly either.

That said, I think August was -- I think because we don't -- it keeps changing by the day. So that is why we are loathe to kind of put out numbers and I am not going to actually put out a number today. But what I will tell you is that I think it is -- we expect it to be a solidly positive month. We saw good activity in fixed income particularly at Western.

I am really pleased with the progress I am seeing at Western, not a rocket ship, not straight up, but Western continues to make progress and I am encouraged by that. So good activity with Western and positive in fixed income. We were out -- it looks like we are going to be out in equities but a slowing redemption rate there.

Again, as I mentioned earlier, a nice month at Martin Currie, that really relates to our Japanese business and what we are doing with LMJ, Legg Mason Japan, and our Martin Currie Australian business which is really a real asset type business. And then also I would characterize it as flat.

We saw some -- looks like we will have some inflows at both RARE and Clarion and slight outs at EnTrustPermal. So I think it is going to -- it looks like it should be a solidly positive month and we'll know Tuesday, right? Or we'll release it Tuesday.

Alan Magleby - *Legg Mason, Inc. - Managing Dir., Head of IR & Corp. Communications*

Rob.

Unidentified Audience Member

My turn again? Okay, thanks, guys. Two questions. The first, Pete, you kind of touched on the dividend. Could you maybe elaborate a little bit on how you do think about the dividend? Should we -- obviously it has grown at a very high rate the last five, six years.

But from here forward depending -- obviously be a function of earnings growth or cash flow growth. But should we think of it at least growing at pace with your share count reduction at a minimum from here and then hope -- I mean do have like a target payout ratio or how do you think --?

Pete Nachtwey - *Legg Mason, Inc. - CFO*

Actually we have espoused in the past a 20% payout ratio on a GAAP number which is not all that relevant because, as you know, our GAAP number has a lot of non-cash expenses in it, etc. But just to give people guidance. We have been well above that 20% actually. In part because of some of the transaction and other related costs.

And what we've said is, look, we want to grow more towards at least the peer median. And then maybe, depending on demand for income, which we think is going to remain strong really over the course of coming decades given what is going on in Western world in terms of demographics, etc., that higher yielding stocks are going to be rewarded.

And if that is the case then we want our shareholders to be rewarded and, oh, by the way, when we pay them a dividend they get rewarded in a meaningful way, take it to Starbucks that they can't when we just buy stock back.

But we are going to -- looked at the two, at some point the lines will cross. When we feel we are more fully valued is when you could see us more aggressively increase the dividend. But I would have to say we have been aggressive, it has been double-digit percentage increases ever since I have been here. Not because it was my decision but because we are very confident in doing that.

Unidentified Audience Member

I guess my next question kind of -- I guess also plays off I guess a theme today of how -- as, Joe, you have mentioned, it kind of takes some time once you have an acquisition come on board just to kind of get them into the system, get new products out.

And when I think about the remake of the Company launching an ETF business, Financial Guard acquisition, all kinds of new products. I mean how does your distribution force even absorb all of this? I mean what kind of -- are there more changes needed there? I mean is that really the big kind of --?

Joe Sullivan - *Legg Mason, Inc. - Chairman & CEO*

I think the -- you raise a good point. I think distribution broadly in the industry is under -- like everything is under a fair amount of disruption right now. Actually I believe that our US retail leadership team is sort of rolling out kind of the evolution of distribution -- an initiative internally right now working with their teams.

I am not going to get into it but they have been working for a long time on how kind of the traditional belly to belly just selling a fund and this and that, it is a different ballgame now.

And so, yes, there is pressure not so much from a how much can these salespeople understand but really this move, again, away from kind of individual fund sales to models, things like that. I think there is an evolution that is underway. And our teams are all over it.

Jack Hueler - *Citigroup - Analyst*

[Jack Hueler], Citigroup. I think this one is probably for you, Pete. As we think about EnTrustPermal, can you give us an update on the synergies? And then maybe where the adjusted margin could go once you realize those synergies?

Pete Nachtwey - *Legg Mason, Inc. - CFO*

Yes, sure, Jack. So last quarter being the June quarter we had about $3 million of the synergy savings and when I say synergy -- well synergies, there was a lot of opportunity there between the two. We said on an annualized basis we expect that to grow to $35 million when it is all said and done pretty much by the end of this calendar year.

But we had $3 million in the June quarter; in this projection that is in here we are anticipating $5 million for the current quarter. So there will still be another $4 million per quarter to go.

And so, in terms of -- when you said adjusted earnings or adjusted EBITDA, so that will ultimately get reflected in that number down the road. And then obviously go to the question earlier about the margin. Obviously that will add significantly to the parent margin as well.

Jack Hueler - *Citigroup - Analyst*

And then just a follow up on that. As I think through adjusted EBITDA with those savings and the one timers rolling off, that I think if I did 65% of that, which was your historical metrics, the $90 million for the buyback I get to a number much higher than $90 million. Is there any thought over time if the stock price stays where it is that you would maybe juice up the buyback pass to $90 million you have historically done?

Pete Nachtwey - *Legg Mason, Inc. - CFO*

Well, I will take the first stab, the boss here is going to have a view too. What we have said and we have talked to pretty much all of our CIOs at our equity affiliates to say, when you are looking at a buyback program, so [Chuck Royce] and the stock you own or Scott Glasser and the stock you own, etc., how do you like to see it? Do you want to see it opportunistically, do you want to see it level percentage, a level dollar amount?

Pretty much what they have told us is, look, a level dollar amount, don't try and outsmart the market, send a signal to your investors that they can count on. And we view that while the 65% was a ceiling we set with the rating agencies to make sure that they were comfortable, we always said once we set that that $90 million was still the absolute dollar amount of what we felt appropriate to deploy. Now opportunistically my --.

Joe Sullivan - *Legg Mason, Inc. - Chairman & CEO*

And that has given us an industry-leading capital return. So I don't feel pressured like we are behind the curve in this, we are already industry-leading. I think candidly I would like to build a little bit of cash. I think there are things that we could see to invest in a little bit. We are comfortable that at that $90 million level that we are returning quite a bit of capital. We may increase our dividend as we have talked about -- all kinds of things.

So I wouldn't look for us -- look if our EBITDA goes significantly higher, then, yes, we will revisit it, facts and circumstances, stock remains cheap. Yes, we may revisit it. We may increase that from $90 million to $95 million or something, we will see. But today and what we are seeing looking forward I think $90 million is a fair amount and building a little bit of cash (multiple speakers) and we have got some delevering ahead of us in three years. So we may build some cash to take care of that.

Pete Nachtwey - *Legg Mason, Inc. - CFO*

Well, we think it is a smart decision for the long-term shareholder and all of us up here are big, long-term shareholders. The flipside is nobody is going to give you a multiple on buying stock back, that is just a wasting kind of thing. So we are also very focused on how do we grow -- how do we grow the business, grow the platform.

But in the meantime we are not going to go out and overpay for things in order to just get growth. So, we are trying to balance all those things as we think about buyback, dividend and what we invest in the business.

Joe Sullivan - *Legg Mason, Inc. - Chairman & CEO*

So, Al, our 1 hour call is now 1 hour and 20 minutes. Is there anything that has come in email wise?

Alan Magleby - *Legg Mason, Inc. - Managing Dir., Head of IR & Corp. Communications*

No.

Joe Sullivan - *Legg Mason, Inc. - Chairman & CEO*

Was there anybody -- is there any less question here? I think we should probably keep going -- I mean, look, we really appreciate your interest and your time and we'll be happy to engage further if you have further questions. Clearly Al is always available and Pete and I as appropriate, happy to answer any questions. Anything kind of burning in the room here that we can answer for you before we call it a call?

Pete Nachtwey - *Legg Mason, Inc. - CFO*

What is for dessert maybe?

Joe Sullivan - *Legg Mason, Inc. - Chairman & CEO*

We've got cookies and stuff (laughter). Well, thank you for you here in the room and then for everyone listening on the webcast. Look, we are absolutely focused on trying to do our best to be as transparent as we can and help you with everything we can. We are respectful of what the SEC requires and not only the letter of the law there and letter of the rules but the spirit of them. So we are trying to thread that needle, as Pete said.

On the other hand, many of you have said we need more information, we would like more transparency and more insight. We are trying to do that. So hopefully this has been helpful. And again, if there are other questions that come up along the way please call Al and, if necessary, Pete and I can join in. So, thank you very much for joining us today and we look forward to talking again soon. Thanks.