LMP REAL ESTATE INCOME FUND INC.
Form N-CSR
March 01, 2012

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM N-CSR

CERTIFIED SHAREHOLDER REPORT OF REGISTERED MANAGEMENT INVESTMENT COMPANIES

Investment Company Act file number 811-21098

LMP Real Estate Income Fund Inc.
(Exact name of registrant as specified in charter)

620 Eighth Avenue, 49th Floor, New York, NY — 10018
(Address of principal executive offices) — (Zip code)

Robert I. Frenkel, Esq.

Legg Mason & Co., LLC

100 First Stamford Place

Stamford, CT 06902
(Name and address of agent for service)

Registrant s telephone number, including area code: (888)777-0102

Date of fiscal year end: December 31

Date of reporting period: December 31, 2011

ITEM 1. REPORT TO STOCKHOLDERS.

The **Annual** Report to Stockholders is filed herewith.

December 31, 2011

Annual Report

LMP Real Estate Income Fund Inc.

(RIT)

INVESTMENT PRODUCTS: NOT FDIC INSURED • NO BANK GUARANTEE • MAY LOSE VALUE

Fund objectives

The Fund s primary investment objective is high current income and the Fund s secondary investment objective is capital appreciation.

What s inside

Letter from the chairman

Dear Shareholder,

We are pleased to provide the annual report of LMP Real Estate Income Fund Inc. for the twelve-month reporting period ended December 31, 2011. Please read on for a detailed look at prevailing economic and market conditions during the Fund s reporting period and to learn how those conditions have affected Fund performance.

As always, we remain committed to providing you with excellent service and a full spectrum of investment choices. We also remain committed to supplementing the support you receive from your financial advisor. One way we accomplish this is through our website, www.leggmason.com/cef. Here you can gain immediate access to market and investment information, including:

- Fund prices and performance,

- Market insights and commentaries from our portfolio managers, and

- A host of educational resources.

Special shareholder notice

Effective August 15, 2011, Legg Mason Partners Fund Advisor, LLC (LMPFA), the Fund s investment manager, assumed primary responsibility for the day-to-day management of the Fund s portfolio. LMPFA continues to provide management and administrative services to the Fund. Mark McAllister serves as senior portfolio manager and John Baldi as co-portfolio manager to the Fund. Following LMPFA s assumption of the day-to-day management of the Fund s portfolio, the Fund no longer has a subadviser. Prior to August 15, 2011, AEW Capital Management, L.P. served as the Fund s subadviser.

We look forward to helping you meet your financial goals.

Sincerely,

R. Jay Gerken, CFA

Chairman, President and Chief Executive Officer

January 27, 2012

Investment commentary

Economic review

Economic growth in the U.S. accelerated over the twelve months ended December 31, 2011. However, the pace of the expansion was less robust than during most other periods exiting a severe recession. U.S. gross domestic product (GDP)i growth, as reported by the U.S. Department of Commerce, was 0.4% and 1.3% in the first and second quarters of 2011, respectively. Third quarter GDP growth then rose to 1.8%. The economy then gathered further momentum late in the year, as the Commerce Department s initial estimate for fourth quarter GDP growth was 2.8% the fastest pace since the second quarter of 2010. This was attributed, in part, to higher consumer spending, which rose 2.0% in the fourth quarter, versus 1.7% and 0.7% gains in the third and second quarters, respectively.

Two factors holding back the economy were the weak job market and continued strains in the housing market. While there was some improvement in early 2011 and late in the reporting period, unemployment remained elevated. When 2011 began, unemployment, as reported by the U.S. Department of Labor, was 9.4%. After dipping below 9.0% in March 2011 (to 8.9%), unemployment moved back to 9.0% in April. Unemployment stayed above 9.0% over the next five months before declining to 8.9% in October. Unemployment then fell to 8.6% in November and 8.5% in December, the latter being the lowest rate since February 2009. The housing market showed some encouraging signs, although home prices still appear to be searching for a bottom. Looking back, existing-home sales moved somewhat higher in January 2011, according to the National Association of Realtors (NAR). Existing-home sales then fluctuated over the next eight months before rising during each of the last three months of the year. In addition, the year ended with the lowest inventory of unsold homes since April 2006. However, existing-home prices remained weak versus a year ago, with the NAR reporting that the median existing-home price for all housing types was $164,500 in December 2011, down 2.5% from December 2010.

While the manufacturing sector continued to expand, it experienced a soft patch during a portion of the reporting period. Based on the Institute for Supply Management s PMI (PMI)ii, in February 2011, the manufacturing sector expanded at its fastest pace since May 2004, with a reading of 61.4 (a reading below 50 indicates a contraction, whereas a reading above 50 indicates an expansion). The PMI then generally moderated over the next several months and was 50.6 in August 2011, its lowest reading in two years. However, the manufacturing sector gained some momentum late in the period and ended December at 53.9, its highest reading in the last six months.

The Federal Reserve Board (Fed)iii took a number of actions as it sought to meet its dual mandate of fostering maximum employment and price stability. As has been the case since December 2008, the Fed kept the federal funds rateiv at a historically low range between zero and 0.25%. In addition, in August 2011, the Fed declared its intention to keep the federal funds rate steady until mid-2013. Then, in September 2011, the Fed announced its intention to purchase $400 billion of longer-term Treasury securities and to sell an equal amount of shorter-term Treasury securities by June 2012 (often

Investment commentary (cont d)

referred to as Operation Twist). At its meeting in December, the Fed potentially opened the door to another round of quantitative easing in 2012, saying it is prepared to employ its tools to promote a stronger economic recovery in a context of price stability. Finally, in January 2012 (after the reporting period ended), the Fed extended the period it expects to keep rates on hold, saying economic conditions including low rates of resource utilization and a subdued outlook for inflation over the medium run are likely to warrant exceptionally low levels for the federal funds rate at least through late 2014.

As always, thank you for your confidence in our stewardship of your assets.

Sincerely,

R. Jay Gerken, CFA

Chairman, President and
Chief Executive Officer

January 27, 2012

All investments are subject to risk including the possible loss of principal. Past performance is no guarantee of future results.

i Gross domestic product (GDP) is the market value of all final goods and services produced within a country in a given period of time.

ii The Institute for Supply Management s PMI is based on a survey of purchasing executives who buy the raw materials for manufacturing at more than 350 companies. It offers an early reading on the health of the manufacturing sector.

iii The Federal Reserve Board (Fed) is responsible for the formulation of policies designed to promote economic growth, full employment, stable prices and a sustainable pattern of international trade and payments.

iv The federal funds rate is the rate charged by one depository institution on an overnight sale of immediately available funds (balances at the Federal Reserve) to another depository institution; the rate may vary from depository institution to depository institution and from day to day.

Fund overview

Q. What is the Fund s investment strategy?

A. The Fund s primary investment objective is high current income with capital appreciation as a secondary investment objective. The Fund has a fundamental policy of concentrating its investments in the U.S. real estate industry and not in any other industry. The Fund primarily invests in income-producing common shares, preferred shares, convertible preferred shares and debt securities issued by real estate companies, including real estate investment trusts (REITs)i. Real estate companies are companies that generally derive at least 50% of their revenue from the ownership, construction, financing, management or sale of commercial, industrial and residential real estate, or have at least 50% of their assets invested in such real estate.

Our investment process focuses on finding securities with sustainable, high or growing distributions that are covered by a company s operating cash flows. We also look for securities that are trading at a discount to what we believe is the intrinsic value of the company. We feel this provides the Fund with additional capital appreciation potential, as well as superior defensive characteristics. Sector allocation is largely an outgrowth of our fundamental securities analysis.

Under normal market conditions, the Fund invests at least 90% of its total assets in income-producing common shares, preferred shares, convertible preferred shares (preferred shares that, upon the passage of time or the happening of certain events, automatically convert into common shares) and debt securities issued by real estate companies, including REITs. At least 80% of the Fund s total assets will be invested, under normal market conditions, in income-producing securities issued by REITs.

It is the Fund s intention to invest approximately 60% to 80% of its total assets in common shares issued by real estate companies and 20% to 40% of its total assets in preferred shares, including convertible preferred shares, issued by real estate companies. The actual percentage of common, preferred and convertible preferred shares and debt securities in the Fund s portfolio may vary over time based on our assessment of market conditions. Our use of leverage is also based on our current view of the risk/return profile of the market. While we do not expect to change the amount of leverage we use frequently, it will be managed in accordance with market conditions and will not be held static if we believe it makes sense to make an adjustment.

Q. What were the overall market conditions during the Fund s reporting period?

A. While returns for most domestic equity indices were essentially flat during the period, the REIT market broadly generated solid returns. With the equity market experiencing historic levels of volatility, the S&P 500 Indexii produced a total return for the period of 2.11%, which was driven almost entirely by dividend income, while the benchmark MSCI U.S. REIT Indexiii returned 8.69% for the same period. We believe that much of the performance for REITs was driven by investors desire for shares with substantial dividend yields in a period of economic and market volatility and very low interest rates on many fixed-income alternatives. In addition, some of those REITs which had reduced or frozen the

Fund overview (cont d)

level of their dividends during the 2008 2009 financial crisis began to increase them as operating fundamentals began to improve.

REITs also raised a record amount of capital in the public markets in 2011, including a record amount of equity. REITs raised $51.3 billion in public equity and debt in 2011 more than the $49 billion raised in the previous record year of 2006.[iv]

Q. How did we respond to these changing market conditions?

A. Since we assumed management of the Fund in mid-August 2011, we have made some moderate changes in its composition. The biggest changes were meaningful reductions in our exposures to the Retail-Free Standing and Apartments sectors. We felt that the Apartments sector s valuation was less compelling and we were less optimistic than many other observers about rental growth prospects going forward. We have also meaningfully added to our holdings in the Shopping Centers and Regional Malls sectors, as we believed that many of them offered good dividend yields and were trading at attractive discounts to their net asset values (NAVs)[v].

The Fund has maintained an emphasis on commercial REITs during the reporting period. The Fund did own one mortgage REIT during the period we managed it. We do not expect to have a large allocation to this area of the market in the near term; however, we may selectively add to our mortgage REIT weighting in the future if we can make purchases of well-managed companies at a discount to their underlying book value.

Prior to our assumption of management of the portfolio, interest rate swaps were used to manage the Fund s exposure to interest rate fluctuations. Overall, these derivative positions detracted from performance during the period.

Performance review

For the twelve months ended December 31, 2011, LMP Real Estate Income Fund Inc. returned 4.02% based on its NAV and -1.44% based on its New York Stock Exchange (NYSE) market price per share. The Fund s unmanaged benchmark, the MSCI U.S. REIT Index, returned 8.69% for the same period. The Lipper Real Estate Closed-End Funds Category Average[vi] returned 2.16% over the same time frame. Please note that Lipper performance returns are based on each fund s NAV.

During the twelve-month period, the Fund made distributions to shareholders totaling $0.72 per share. The performance table shows the Fund s twelve-month total return based on its NAV and market price as of December 31, 2011. **Past performance is no guarantee of future results.**

Performance Snapshot as of December 31, 2011

Price Per Share	**12-Month Total Return***
$10.70 (NAV)	4.02%
$9.25 (Market Price)	-1.44%

All figures represent past performance and are not a guarantee of future results.

*** Total returns are based on changes in NAV or market price, respectively. Total returns assume the reinvestment of all distributions in additional shares in accordance with the Fund s Dividend Reinvestment Plan.**

Q. What were the leading contributors to performance?

A. On an absolute basis, the Fund had in excess of 98% of its assets invested in REITs during the period, which produced positive returns for the year. In terms of individual Fund holdings, leading contributors to performance for the period included positions in Camden Property Trust, DCT Industrial Trust Inc., Excel Trust Inc., Strategic Hotels & Resorts Inc. Series B Preferred Shares and Primaris Retail Real Estate Investment Trust.

Q. What were the leading detractors from performance?

A. Relative to the MSCI U.S. REIT Index, the Fund s overall stock selection detracted from relative performance. In terms of individual Fund holdings, leading detractors from performance for the period included positions in Getty Realty Corp., First Potomac Realty Trust, CommonWealth REIT, Mack-Cali Realty Corp. and LBA Realty Fund II WBP I Public.

Q. Were there any significant changes to the Fund during the reporting period?

A. In addition to the broader changes made to the Fund that were announced via press release over the course of the reporting period (including changing the portfolio management team), there were a number of specific changes made to the portfolio over the course of the reporting period.

Among the largest additions to the Fund s portfolio were new positions in Westfield Group Australia, Campus Crest Communities Inc., DCT Industrial Trust Inc., Hospitality Properties Trust, and Excel Trust Inc. Some of the largest existing holdings that were sold over the course of the period were positions in Camden Property Trust, American Campus Communities Inc., National Retail Properties Inc., and Realty Income Corp.

Looking for additional information?

The Fund is traded under the symbol RIT and its closing market price is available in most newspapers under the NYSE listings. The daily NAV is available on-line under the symbol XRITX on most financial websites. *Barron s* and the *Wall Street Journal s* Monday edition both carry closed-end fund tables that provide additional information. In addition, the Fund issues a quarterly press release that can be found on most major financial websites as well as www.leggmason.com/cef.

In a continuing effort to provide information concerning the Fund, shareholders may call 1-888-777-0102 (toll free), Monday through Friday from 8:00 a.m. to 5:30 p.m. Eastern Time, for the Fund s current NAV, market price and other information.

Thank you for your investment in LMP Real Estate Income Fund Inc. As always, we appreciate that you have chosen us to manage your assets and we remain focused on achieving the Fund s investment goals.

Sincerely,

Mark McAllister

Portfolio Manager
Legg Mason Partners Fund Advisor, LLC

Fund overview (cont d)

John Baldi

Portfolio Manager
Legg Mason Partners Fund Advisor, LLC

January 17, 2012

RISKS: *Funds that invest in securities related to the real estate industry are subject to the risks of real estate markets, including fluctuating property values, changes in interest rates and other mortgage-related risks. In addition, investment in funds that concentrate their investments in one sector or industry may involve greater risk than more broadly diversified funds. Leverage may result in greater volatility of NAV and the market price of common shares and increases a shareholder s risk of loss. The Fund may make significant investments in derivative instruments. Derivative instruments can be illiquid, may disproportionately increase losses, and have a potentially large impact on Fund performance.*

Portfolio holdings and breakdowns are as of December 31, 2011 and are subject to change and may not be representative of the portfolio managers current or future investments. The Fund s top ten holdings (as a percentage of total investments) as of this date were: Urstadt Biddle Properties Inc., Cumulative, Series C, 8.500% (4.2%), Macerich Co. (4.0%), OMEGA Healthcare Investors Inc. (3.7%), Kilroy Realty Corp. (3.5%), Kimco Realty Corp., Series G, 7.750% (3.4%), First Potomac Realty Trust (3.4%), Westfield Group (3.3%), Public Storage Inc., Cumulative Redeemable, Series L, 6.750% (3.2%), HCP Inc. (3.1%) and Liberty Property Trust (3.1%). Please refer to pages 6 through 8 for a list and percentage breakdown of the Fund s holdings.

The mention of sector breakdowns is for informational purposes only and should not be construed as a recommendation to purchase or sell any securities. The information provided regarding such sectors is not a sufficient basis upon which to make an investment decision. Investors seeking financial advice regarding the appropriateness of investing in any securities or investment strategies discussed should consult their financial professional. The Fund s top five sector holdings (as a percentage of total investments) as of December 31, 2011 were: Shopping Centers (19.1%), Health Care (13.1%), Office (12.7%), Diversified (11.7%) and Regional Malls (10.6%). The Fund s portfolio composition is subject to change at any time.

All investments are subject to risk including the possible loss of principal. Past performance is no guarantee of future results. All index performance reflects no deduction for fees, expenses or taxes. Please note that an investor cannot invest directly in an index.

The information provided is not intended to be a forecast of future events, a guarantee of future results or investment advice. Views expressed may differ from those of the firm as a whole.

i Real estate investment trusts (REITs) invest in real estate or loans secured by real estate and issue shares in such investments, which can be illiquid.

ii The S&P 500 Index is an unmanaged index of 500 stocks and is generally representative of the performance of larger companies in the U.S.

iii The MSCI U.S. REIT Index is a free float-adjusted market capitalization weighted index that is comprised of equity REITs that are included in the MSCI U.S. Investable Market 2500 Index, with the exception of specialty equity REITs that do not generate a majority of their revenue and income from real estate rental and leasing operations. The Index represents approximately 85% of the U.S. REIT universe.

iv NAREIT News Release; January 4, 2012.

v Net asset value (NAV) is calculated by subtracting total liabilities and outstanding preferred stock (if any) from the closing value of all securities held by the Fund (plus all other assets) and dividing the result (total investments) by the total number of the common shares outstanding. The NAV fluctuates with changes in the market prices of securities in which the Fund has invested. However, the price at which an investor may buy or sell shares of the Fund is the Fund s market price as determined by supply of and demand for the Fund s shares.

vi Lipper, Inc., a wholly-owned subsidiary of Reuters, provides independent insight on global collective investments. Returns are based on the twelve-month period ended December 31, 2011, including the reinvestment of all distributions, including returns of capital, if any, calculated among the 9 funds in the Fund s Lipper category.

Fund at a glance (unaudited)

Investment breakdown (%) as a percent of total investments

The bar graph above represents the composition of the Fund s investments as of December 31, 2011 and December 31, 2010 and does not include derivatives, such as swap contracts. The Fund is actively managed. As a result, the composition of the Fund s investments is subject to change at any time.

Schedule of investments

December 31, 2011

LMP Real Estate Income Fund Inc.

Security	Shares	Value
Common Stocks 57.4%		
Apartments 1.9%		
Campus Crest Communities Inc.	308,220	$ ***3,100,693***(a)
Diversified 5.4%		
Digital Realty Trust Inc.	45,000	3,000,150(a)
Dundee Real Estate Investment Trust	125,000	4,008,589
Starwood Property Trust Inc.	85,000	1,573,350
Total Diversified		***8,582,089***
Health Care 11.5%		
Cogdell Spencer Inc.	205,000	871,250
HCP Inc.	119,800	4,963,314(a)
Health Care REIT Inc.	83,000	4,525,990(a)
OMEGA Healthcare Investors Inc.	300,000	5,805,000(a)
Senior Housing Properties Trust	90,000	2,019,600(a)
Total Health Care		***18,185,154***
Industrial 5.2%		
DCT Industrial Trust Inc.	557,830	2,856,090(a)
First Potomac Realty Trust	410,000	5,350,500(a)
Total Industrial		