ClearBridge
A Franklin Templeton Company

All Cap Growth Strategy

Evan Bauman
Managing Director,
Portfolio Manager

Erica Furfaro
Director,
Portfolio Manager

Aram Green
Managing Director,
Portfolio Manager

Amanda Leithe CFA
Director,
Portfolio Manager

Margaret Vitrano
Managing Director,
Portfolio Manager

Key Takeaways

- Most growth indexes entered correction territory during the quarter, pressured by the chaotic introduction of tariffs as well as fears of a slowing U.S. economy and higher inflation.
- The Strategy outperformed through this reversal, aided by strong, diversified stock selection and an underweight to the Magnificent Seven.
- We believe the Strategy is well-positioned for a period of heightened uncertainty, with generally lower tariff exposure than the benchmark and holdings beyond the mega caps starting to deliver better earnings growth.

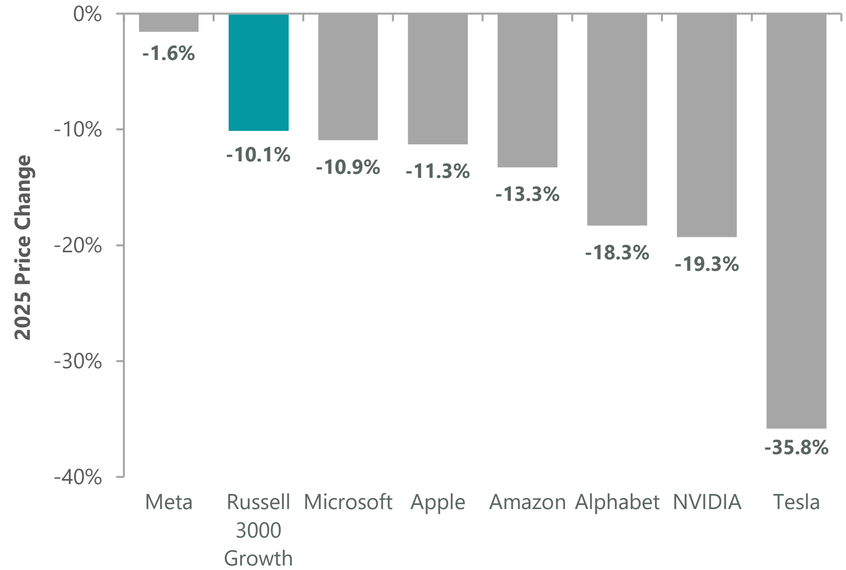
Market Overview

A stall in the mega cap growth trade occurred in the first quarter as the chaotic introduction of tariffs accompanied by fears of a slowing U.S. economy and higher inflation sent stocks to their worst quarterly showing since the 2022 bear market. The S&P 500 Index declined 4.3% while the growth-laden NASDAQ Composite tumbled 10.4% and the benchmark Russell 3000 Growth Index (RLG) fell 10%.

Trump's actions to reorder global trade dominated headlines in his first three months in office, sending the S&P 500 and most U.S. growth indexes into correction territory. The RLG underperformed the Russell 3000 Value Index by over 1,100 basis points. Through March, the U.S. had imposed 25% steel and aluminum tariffs, an additional 20% tariff on China, plus 25% tariffs on most goods from Canada and Mexico not covered by a previous trade deal, with more sweeping levies expected to start the second quarter.

Tariffs were just one of the headwinds impacting the Magnificent Seven as all except Meta Platforms underperformed the index. The surprise emergence in January of DeepSeek, a Chinese large language model (LLM), with capabilities similar to the best LLMs but built with inferior chips and at a lower cost, caused investors to question whether the massive capex being devoted to Gen AI would continue. Shares of Nvidia, supplier of the most advanced GPU chips to power AI applications, fell sharply despite Nvidia continuing to deliver record financial results amid a strong rollout for its newest Blackwell GPU system.

Exhibit 1: The Divergent Seven



Price returns as of March 31, 2025. Source: FactSet.

The ClearBridge All Cap Growth Strategy held up better than the benchmark through this reversal (on a gross basis), aided not only by its underweight to the Magnificent Seven and the information technology (IT) sector but also strong stock selection across communication services and consumer discretionary.

Our active underweight to the Magnificent Seven added more than 130 basis points to relative returns for the quarter, with underweights to EV maker Tesla among the largest relative contributors.

An important but often overlooked component of our diversified approach is the balance provided by more defensive, durable compounder holdings that tend to hold up well in downturns. This was illustrated by longtime health care holdings Vertex Pharmaceuticals and UnitedHealth Group as well as Visa and exchange and financial data provider S&P Global. Two newer positions also held up well: uniform and workplace products provider, Cintas, and off-price apparel retailer, TJX. Cintas delivered strong quarterly results with organic growth and margin improvement ahead of expectations. The company cited several new business wins driven by cost savings, a value proposition that is particularly salient in today’s more uncertain macro environment. TJX also put up a high-quality beat and has become a relative safe haven for investors amid elevated recession fears. The company has historically benefited from trade-down and inventory availability during periods of weaker consumer spending.

This cohort helped offset weakness across mega cap tech names as well as consumer staples holdings e.l.f. Beauty and Target, which could be susceptible to higher costs due to tariffs.

Portfolio Positioning

We took advantage of recent volatility to add two positions in the first quarter while exiting two others.

AppLovin, in the IT sector, is the world's leading mobile game and app advertising platform, providing software for marketing and monetization, powered by its proprietary AI targeting engine (Axon). We see opportunity for AppLovin to continue to expand and grow its share of the market for mobile app marketing, at a time when mobile gaming ad spending is recovering from a higher rate-driven trough. We also see the potential for the company to expand its addressable market to include e-commerce advertising, around which early checks have been encouraging. With strong incremental margins and management keeping expenses controlled, the company should be able to drive significant free cash flow growth as revenue continues to scale.

Ares Management, in the financials sector, is an alternative asset manager offering private credit, real asset and private equity strategies. Ares is a leading player in private credit, a large and growing market that continues to be supported by secular tailwinds such as increased bank regulation, rising retail penetration and the migration of insurance assets. Scaled players such as Ares should take outsize share of industry asset growth and drive fee-related earnings margin expansion over time. Ares also has a balance sheet light strategy and more predictable cash flows, with the vast majority of its realized income from fee-related earnings. Finally, Ares's high underwriting standards and performance in past downturns position the company well to not only manage through a future credit cycle but also emerge stronger versus peers.

We closed out of AbbVie, in the health care sector, a biopharmaceutical company developing treatments for autoimmune diseases and cancer. AbbVie has been a long-term holding but after the recent stock rally, we believe the company's risk/reward appears less attractive from these levels. Growth has slowed in recent years due to the loss of exclusivity of its top-selling drug Humira and the maturing of a number of its existing franchises making pipeline/new product execution key to future success. We have continued to consolidate our exposures within health care toward companies with more attractive/predictable long-term growth prospects.

Charles River Laboratories, a provider of drug discovery services in the health care sector, was sold due to continued weakness among its large cap pharmaceutical customers as well as rhetoric from the Trump administration about cuts at the National Institutes of Health as well as volatile biotech funding trends.

Outlook

The multinational exposure of many of our holdings makes tariffs a key risk we are monitoring. Tariffs could be a headwind to GDP growth with the size of that headwind in the short-term depending on substitutes, ease of shifting production and consumer elasticity of demand.

We have been engaging with management teams of portfolio companies with production outside the U.S. to understand supply change fungibility and the ability to pass through costs to end customers. We are specifically monitoring risks to the consumer sector from tariffs because consumers have already borne the burden of several years of cost inflation pressuring wallets.

We see our holdings outside the Magnificent Seven, including a group of mid cap plus companies in the $10 billion to $100 billion range that provide broad market coverage, starting to deliver better earnings growth. We have positioned the portfolio in anticipation of this broadening in the market. Barring a recession, in 2025 we expect to see earnings growth from industrials and health care companies narrowing the gap compared to the technology universe. While we have entered a period of heightened uncertainty, the general health of the economy entering this phase of the cycle is strong.

Portfolio Highlights

The ClearBridge All Cap Growth Strategy outperformed its Russell 3000 Growth Index benchmark in the first quarter. On an absolute basis, the Strategy delivered positive contributions across four of the nine sectors in which it was invested (out of 11 sectors total). The primary contributor to performance was the health care sector while the IT and consumer discretionary sectors were the main detractors.

Relative to the benchmark, overall sector allocation and stock selection contributed to performance. From a sector allocation perspective, overweights to health care and industrials and an underweight to IT supported results. From a stock selection perspective, strength in communication services, consumer discretionary and industrials offset weakness in consumer staples and real estate.

On an individual stock basis, the leading absolute contributors to performance were Vertex Pharmaceuticals, Visa, Uber, RTX and UnitedHealth Group. The primary absolute detractors were Broadcom, Nvidia, Amazon.com, Apple and Tesla.