



A Franklin Templeton Company



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All Cap Growth Strategy

Key Takeaways

- ▶ The Strategy underperformed, hurt by allocation differences among our mega cap growth holdings as well as weak stock selection in communication services and health care.
- ▶ We added new positions during the quarter across the industrials, materials and consumer discretionary sectors.
- ▶ Disciplined portfolio management and opportunistic capital allocation continue to reinforce our long-term investment philosophy in a fast-moving market environment.

Market Overview

U.S. equities delivered resilient but volatile performance in the fourth quarter. Momentum-driven themes tied to artificial intelligence (AI) and technology extended into the early part of the quarter before reversing, resulting in heightened volatility and greater stock-level dispersion.

The S&P 500 Index returned 2.7% during the quarter, while the benchmark Russell 3000 Growth Index advanced 1.1%. As volatility increased, investors became more selective, rewarding companies with durable fundamentals, innovation-driven growth and strong execution, while penalizing stocks where expectations had moved ahead of near-term fundamentals.

The ClearBridge All Cap Growth Strategy underperformed the benchmark for the quarter, hurt by allocation differences among our mega cap growth holdings as well as weak stock selection in communication services and health care.

An underweight to Alphabet was a primary detractor. We had been consistently adding to Alphabet since repurchasing the stock in April 2024, as it had been trading at a sub-market multiple, but we regret not increasing our exposure more aggressively after the DOJ antitrust case concluded with less onerous penalties than feared. The company's success with AI-supported digital advertising, its Google Gemini chatbot and TPU chips for AI workloads boosted its shares more than 25% for the quarter. An underweight to the outperforming Apple also weighed on results.

Netflix fell due to investor uncertainty and concerns over its proposed \$72 billion acquisition of Warner Bros. Discovery's studio assets, a move complicated by a rival bid from Paramount/Skydance, potential regulatory hurdles and integration risks, muddling its previously clear growth narrative.

In health care, Eli Lilly rose strongly after striking a deal with the U.S. government to offer its GLP-1 treatments to Medicare and Medicaid patients while readouts on the company's oral GLP-1 treatment indicated a broader market than expected. This caused our lack of exposure to be a drag on relative results.

Partially offsetting this weakness, Vertex Pharmaceuticals benefited from growing optimism around its kidney disease pipeline; Thermo Fisher Scientific was up on improved sentiment toward the health care sector while Natera was higher on positive results in its oncology business and raised financial guidance.

Portfolio Positioning

We initiated three positions during the quarter, the largest being European aerospace and defense contractor Airbus. The long-term demand for commercial aircraft to support air travel is increasing, with much of the growth from China and other parts of Asia, while aging of the existing fleet provides a robust pipeline of replacement demand for years to come. With the A320 family providing a durable and scalable platform, Airbus is entering a favorable period for free cash flow growth before it needs to invest in a next-generation aircraft. Additionally, Airbus's relatively smaller defense segment stands to benefit from the EU ramping up defense spending as the U.S. pulls back on its overseas security commitments. With the company's multiyear backlog and robust industry demand for planes, we believe the long-term backdrop for Airbus remains robust.

New addition Linde is a well-run company operating in an attractive, consolidated end market of industrial gas, a key input in many industries including technology, chemicals, manufacturing, health care and electronics. Both the company and the industry are highly disciplined in terms of price and contracting structure, providing downside protection in periods of slower economic growth. We believe an overlooked feature of Linde's business is its role as primary provider of gases for rocket propellant and coatings used by companies operating space and satellite businesses.

Hilton is one of the world's largest and fastest-growing hospitality companies with a portfolio of over 8,500 properties and more than 1.25 million rooms across 24 brands. Hilton's business is asset-light, with the majority of its revenue and profits derived from franchised and managed properties rather than company-owned and operated hotels. We believe the hotel operator has a long runway for growth supported by continued mid- to high-single-digit net unit expansion. The company also has strong margins and free cash flow conversion, enabling consistent return of capital through share buybacks. We believe Hilton should remain a relative share gainer irrespective of the macro backdrop.

Outlook

Our outlook remains consistent with what we articulated earlier in the year — and importantly, what played out in the fourth quarter. Markets remain resilient, but volatility has increased as momentum-driven areas cooled and stock-level dispersion widened, reinforcing the importance of disciplined stock selection and a balanced approach to portfolio construction.

AI continues to represent a powerful long-term opportunity, though early beneficiaries such as semiconductors and infrastructure have already seen significant gains. We are focused on making sure we have not only the right exposure within the AI complex but also other offensive bets in the portfolio to position the Strategy well should market leadership broaden further. At the same time, we continue to emphasize balance, owning companies not only with offensive growth potential but also defensive characteristics built on strong free cash flow, clean balance sheets and proven management teams, which should help to protect the portfolio should the environment weaken.

Portfolio Highlights

The ClearBridge All Cap Growth Strategy underperformed its Russell 3000 Growth Index benchmark in the fourth quarter. On an absolute basis, the Strategy delivered positive contributions across four of the 10 sectors in which it was invested (out of 11 sectors total). The primary contributor to performance was the health care sector while the main detractor was the communication services sector.

Relative to the benchmark, stock selection detracted from performance. In particular, stock selection in communication services and health care weighed on returns. Conversely, stock selection in consumer discretionary and materials contributed to performance.

On an individual stock basis, the leading relative contributors to performance were Vertex Pharmaceuticals, Freeport McMoRan and Natera as well as underweights to Microsoft and Oracle. The primary relative detractors were Netflix and Doximity as well as an underweights to Alphabet and Apple and not holding Eli Lilly.

CLEARBRIDGE ALL CAP GROWTH STRATEGY

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