



SMID Cap Growth Strategy



Brian Angerame
Managing Director,
Portfolio Manager



Jeffrey Bailin CFA
Managing Director,
Portfolio Manager



Aram Green
Managing Director,
Portfolio Manager



Matthew Lilling CFA
Managing Director,
Portfolio Manager

Key Takeaways

- ▶ Macroeconomic trade concerns and a rotation out of tech stocks spurred a surge of volatility and uncertainty that sent the market lower in the first quarter.
- ▶ The Strategy outperformed its benchmark, largely owing to strong stock selection within the most turbulent sector of the market – information technology.
- ▶ While we anticipate softer near-term results across almost every major sector until macroeconomic and governmental drivers solidify, the speed and magnitude of the recent momentum reversal has likely created attractive long-term opportunities.

Market Overview

The threat of imposition of a myriad of tariffs and trade policy changes and a rotation out of AI-related tech spurred a surge of market volatility and uncertainty sent markets lower in the first quarter. Concerns that small and SMID stocks would incur the brunt of worsening earnings revisions than their larger cap peers manifested in the core Russell 2500 Index returning -7.50% versus the -4.49% of the Russell 1000 Index. The pressure was felt even more acutely within growth stocks, as investors sought defensive protection within value, resulting in the Russell 2500 Growth Index returning -10.80%, nearly 500 basis points worse than the Russell 2500 Value Index.

The first quarter opened with a high level of market optimism, driven by a continued AI rally, the prospect of further interest rate reductions and hopes for a less restrictive regulatory regime under the incoming Trump administration. However, it quickly became apparent that uncertainty would become the hallmark of the first quarter. The unveiling of Chinese AI DeepSeek in late January, with reportedly lower development costs and less need for computing power of comparable AI tools, resulted in a selloff of the information technology (IT) sector and a rotation away from the AI-beneficiaries that had generated strong returns in 2024. Additionally, almost immediately following the inauguration, the Trump administration rapidly pushed through a series of domestic and economic policies including the imposition of tariffs levied on steel and aluminum, imported autos, all goods from China and many from Canada and Mexico. Concerns around the second- and third-order impacts of these rapid and significant changes created business and consumer uncertainty, which weighed on public markets.

Trade wars have weighed on U.S. economic growth and raised inflation expectations.

Portfolio Performance

The ClearBridge SMID Growth Strategy held up better than its benchmark in the first quarter, largely owing to strong stock selection within the most turbulent sector of the market – IT. Our focus on high-quality companies within the software space such as Guidewire Software, which operates a platform for property and casualty insurers, helped to insulate the portfolio from the rotation out of the sector and AI beneficiaries. The sector also included one of our top-performing holdings, Teledyne Technologies, which was rewarded by investors after positive quarterly earnings that showed improvements across some of its more challenged business lines, solid new order data trends and rather conservative and achievable management guidance, which leads us to believe that the company will continue to be a strong performer.

Consumer staples was also a strong contributor to performance thanks to longstanding holdings and steady compounders BJ's Wholesale Club and Casey's General Stores. BJ's share price rose as the company showed strong increases in traffic, execution on its growth initiatives and accelerating store growth. Meanwhile Casey's continues to drive industry-leading growth driven by its prepared food program, loyalty program and private label, with the stock also benefiting from perceived defensiveness amid macroeconomic uncertainty.

Performance across most other sectors was reasonably in-line with benchmark performance, with modest headwinds from stock selection in materials and health care. Within materials, Ashland, a chemicals manufacturer, underperformed due to continued macroeconomic headwinds. In health care, life science tools end markets and biotechnology saw weak performance amid concerns over regulatory environment and forward spending outlooks. Our largest detractor in the sector was infectious vaccine developer Vaxcyte, which saw its share price decline following mixed clinical trial data around its key product and amid greater uncertainty around vaccine development due to new leadership within the Department of Health and Human Services.

Portfolio Positioning

We initiated a new position in Knife River, a diversified construction materials company primarily focused on asphalt paving services in the Pacific Northwest and Midwest. The company has meaningful exposure to public infrastructure investment, which offers resilient volume growth, which the company is augmenting with improving pricing power, M&A and a variety of margin-enhancing initiatives.

We also added two new health care positions in Geron and Glaukos. Geron, a biotech company, focuses on oncology treatments, is launching a new drug to treat blood cancer, which represents an attractive opportunity given the large target market of patients who

must typically cycle through a variety of treatments in combating the disease. Glaukos is a medical device company focused on products used to treat eye conditions such as glaucoma. Given the company's history of launching fast-growing products, we are encouraged that the upcoming debut of its iDose treatment for glaucoma will be similarly successful.

During the period several of our holdings were acquired, including biopharmaceutical company Intra-Cellular Therapies, by Johnson & Johnson, and Paycor, a provider of human capital management solutions, by Paychex.

Outlook

With ever-changing policy priorities out of the new leadership in Washington, D.C., particularly around tariffs, taxes, funding priorities and geopolitical conflicts, we have increased engagement with the management teams of our portfolio holdings. This regular dialogue is vital as the pace of proposed change and lack of clarity around the duration of proposals (particularly tariffs/reciprocal tariffs) have had a chilling impact on general investment and consumer activity.

We anticipate softer near-term results across most sectors until macroeconomic and governmental drivers solidify (in either direction), which can allow companies and investors to reposition as necessary. However, the speed and magnitude of the recent momentum reversal in various corners of the stock market have likely created attractive long-term opportunities. Despite a challenging first quarter for markets, we believe that our relative outperformance speaks to the strength of our investment process – a focus on companies that can compound high levels of growth in large markets without relying on macro tailwinds.

Portfolio Highlights

The ClearBridge SMID Cap Growth Strategy outperformed its Russell 2500 Growth Index benchmark during the first quarter. On an absolute basis, the Strategy had losses across nine of the 10 sectors in which it was invested (out of 11 sectors total). The slightly positive contributor was the communication services sector, while the IT and industrials sectors detracted the most.

On a relative basis, overall stock selection contributed to performance. Stock selection in the IT, communication services and consumer staples sector, as well as an overweight allocation to consumer staples benefited performance. Conversely, stock selection in the health care sector and an overweight to the IT sector weighed on performance.

On an individual stock basis, the biggest contributors to absolute returns during the quarter were Intra-Cellular Therapies, BJ's Wholesale Club, Tradeweb Markets, EQT and TG Therapeutics. The

largest detractors from absolute returns were Globant, Vaxcyte, Wix.com, XPO and Burlington Stores.

In addition to the transactions mentioned above, we initiated a new position in monday.com in the IT sector. We also exited positions in SiteOne Landscape Supply in the industrials sector, CONMED in the health care sector and HubSpot in the IT sector.

Past performance is no guarantee of future results. Copyright © 2025 ClearBridge Investments. All opinions and data included in this commentary are as of the publication date and are subject to change. The opinions and views expressed herein are of the portfolio management team named above and may differ from other managers, or the firm as a whole, and are not intended to be a forecast of future events, a guarantee of future results or investment advice. This information should not be used as the sole basis to make any investment decision. The statistics have been obtained from sources believed to be reliable, but the accuracy and completeness of this information cannot be guaranteed. Neither ClearBridge Investments, LLC nor its information providers are responsible for any damages or losses arising from any use of this information.

Source: London Stock Exchange Group plc and its group undertakings (collectively, the "LSE Group"). © LSE Group 2025. FTSE Russell is a trading name of certain of the LSE Group companies. "FTSE®" and "Russell®" are a trademark of the relevant LSE Group companies and are used by any other LSE Group company under license. All rights in the FTSE Russell indexes or data vest in the relevant LSE Group company which owns the index or the data. Neither LSE Group nor its licensors accept any liability for any errors or omissions in the indexes or data and no party may rely on any indexes or data contained in this communication. No further distribution of data from the LSE Group is permitted without the relevant LSE Group company's express written consent. The LSE Group does not promote, sponsor or endorse the content of this communication.