



Aram Green
Managing Director,
Portfolio Manager

Select Strategy

Key Takeaways

- ▶ The Strategy outperformed in a narrow, momentum-driven market as our small and mid cap growth holdings exhibited continued strength.
- ▶ We added six new positions in the quarter while exiting four others. Buying was balanced across the portfolio, highlighted by a disruptor in communication services and durable compounders in financials and health care. We also trimmed and/or exited several disruptors to manage risk.
- ▶ While the market rotation has experienced fits and starts, we believe this cycle of wider leadership is still in the early innings. The Trump administration should support lighter regulation and improved M&A activity, conditions particularly beneficial to companies down the market cap spectrum.

Market Overview

A market broadening in the fourth quarter sparked by Donald Trump's election victory and further interest rate cuts from the Federal Reserve proved momentum-driven with relatively narrow leadership. The S&P 500 Index advanced 2.41% in the quarter to finish 2024 up 25.02%, completing the best back-to-back years for the index since 1998, while the benchmark Russell 3000 Index rose 2.63% for the quarter and 23.81% for the year.

While small cap, value and cyclical shares were bid up in the aftermath of Trump's win, growth stocks reasserted control by quarter's end. The Russell 3000 Growth Index jumped 6.83% for the quarter, outperforming the Russell 3000 Value Index by 877 basis points, while the Russell Midcap Growth Index was the best quarterly performer overall, rising 8.14%. Growth outperformed among smaller capitalization stocks as well although the advantage was less pronounced.

The ClearBridge Select Strategy considers small and mid cap growth stocks its most attractive target market and outperformed the benchmark in the fourth quarter as these companies exhibited continued strength.

Disruptors residing mostly in the information technology (IT) sector were leading contributors, highlighted by triple-digit gains for AppLovin, 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 purchased AppLovin in the first quarter and see opportunity for the company to continue to grow its share of the market for mobile app marketing, at

a time when mobile gaming ad spend is recovering from a higher-rate-driven trough. While we also see the potential for the company to expand its addressable market to include e-commerce advertising, we took some profits during the quarter to deploy into other positions at less full multiples.

E-commerce enablement software maker Shopify continued to see its shares rate higher following a strong third-quarter showing that further illuminated the improved financial stability and capital allocation mindset guiding the business. The company is a much different story than it was even two years ago. Gone is the poorly conceived Shopify Fulfillment Network, which changed the capital intensity of the business dramatically. We are also encouraged by the fundamental maturity of long-time holding DocuSign, which is seeing good traction with its new AI-powered intelligent agreement management platform rollout.

The Strategy also saw significant contributions from new addition Reddit in communication services and e-commerce platform Global-E Online in the consumer discretionary sector. Reddit is a unique destination for community and conversation on the internet. The company's latest quarterly results showed strong gains in daily average users while advertising and data licensing revenues also ramped aggressively. Reddit operates a very high margin business and we believe the company is still early in its engagement, monetization and profitability journey.

These results offset weakness among our consumer discretionary holdings. After rising more than 30% through November, the Latin America e-commerce platform MercadoLibre gave back gains in a broad final month selloff. Footwear retailer Crocs also retraced stronger gains earlier in the year as financial conditions appeared to tighten in the fourth quarter. Health care holdings Surgery Partners and ICON were pressured by negative post-election sentiment toward the sector. We believe the fundamentals of these companies remain robust and are maintaining existing exposures.

Portfolio Positioning

Besides the Reddit purchase, we added five common stock positions in the quarter. Among durable compounders, we bought Charles Schwab in the financials sector, a leading online brokerage and bank catering primarily to individual investors. Schwab's cash shorting issues are trailing into the past and a new more favorable regulatory regime should be positive for the returns of this durable compounder. The addition of UnitedHealth Group was driven by overreaction to a recent event that caused shares of the country's largest managed care provider to derate. The company was hurt by a combination of negative investor sentiment and the increasing risk of regulatory scrutiny of its health insurance business following the surprising public reaction to the tragic murder of the company's

benefits group CEO in early December. We believe the company is part of the solution to improving the outcomes and lowering the costs of the U.S. health care system, and that its business model will prove resilient.

We also purchased Grocery Outlet, a high-growth, off-price supermarket chain. The company, which we view as an evolving opportunity with scope for fundamental improvement, is going through a management change, and issues from a failed ERP implementation should be behind it.

Our disruptor holdings represent the highest risk/reward exposure in the portfolio, causing us to pay close attention to position sizes to manage risk and maintain diversification. The Strategy sold disruptor Marvell Technology into strength as shares of the chipmaker whose products are essential to powering the data centers that enable AI computing had nearly doubled during the year. We exited Progyny, in the health care sector, a provider of fertility services offered as benefit for companies, after the company missed quarterly estimates and lowered full-year earnings guidance due to weakening utilization trends. We also sold Clear Secure, a provider of identity and security software in the IT sector, after it hit our target valuation and deployed the proceeds from the sale into existing positions that provide more attractive risk/reward dynamics.

Outlook

While the market broadening that began over the summer has experienced fits and starts, we believe this cycle of wider leadership beyond the Magnificent Seven is still in the early innings. The economic leadership in the Trump administration brings capital markets experience to policy making, which we believe will lead to lighter regulation and improve the environment for M&A activity, conditions particularly beneficial to companies down the market cap spectrum.

With the election behind, managements of small and mid cap companies have a clearer path forward around deploying capital. This is where the animal spirits get stoked, with business managers having the confidence to continue to invest in their business and make acquisitions. We have already started to see a pickup within business and capital markets activity. We think there's a big backlog for IPOs heading into next year. We believe this is an opportune time for active managers, like ourselves, to be evaluating these things in real time and making the necessary changes within their portfolios.

Regarding opportunities in this improving environment, we remain bullish on e-commerce and the enablers of the digital economy. Penetration levels are still very low, particularly for niche e-commerce and digital media companies, and a number of companies in these areas still trade at what we view as very attractive valuations with above-average long-term growth rates. Another area that has been generally overlooked is off-price retailers. With inflation proving

stubbornly high, we expect the cost of living will keep rising, causing more consumers to seek out bargains. Finally, with AI, e-commerce and other technologies creating a more digital economy, we see rising demand for cybersecurity technologies across consumer, corporate and government markets.

Portfolio Highlights

The ClearBridge Select Strategy outperformed its Russell 3000 Index benchmark during the fourth quarter. On an absolute basis, the Strategy posted positive contributions across eight of the 11 sectors in which it was invested. The primary contributors came from the IT sector while consumer discretionary and health care detracted the most.

Relative to the benchmark, overall stock selection contributed to performance. In particular, stock selection in the IT, health care, materials, communication services, energy and consumer staples sectors drove results, more than offsetting negative selection in the consumer discretionary sector. From an allocation standpoint, an overweight to IT and an underweight to health care were beneficial while underweights to financials and communication services and an overweight to industrials detracted from performance.

On an individual stock basis, the leading contributors were positions in AppLovin, ServiceNow, Nvidia, Shopify and HubSpot. The primary detractors were MercadoLibre, ICON, Crocs, Surgery Partners and Monolithic Power Systems.

In addition to the transactions mentioned above, we added positions in TG Therapeutics in the health care sector Coherent in the IT sector and exited Exxon Mobil in the energy sector.

Past performance is no guarantee of future results. Copyright © 2024 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.

Performance source: Internal. Benchmark source: Russell Investments. Frank Russell Company ("Russell") is the source and owner of the trademarks, service marks and copyrights related to the Russell Indexes. Russell® is a trademark of Frank Russell Company. Neither Russell nor its licensors accept any liability for any errors or omissions in the Russell Indexes and/or Russell ratings or underlying data and no party may rely on any Russell Indexes and/or Russell ratings and/or underlying data contained in this communication. No further distribution of Russell Data is permitted without Russell's express written consent. Russell does not promote, sponsor or endorse the content of this communication.

Performance source: Internal. Benchmark source: Standard & Poor's.