



Sustainability Leaders Strategy



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Key Takeaways

- ▶ The third quarter continued the sharp post-Liberation Day rebound for U.S. equity markets, with animal spirits driving the benchmark Russell 3000 Index to record highs.
- ▶ While relative performance has been lagging in recent quarters, we have observed improving relative results in 2025 compared to the prior two years, partly due to recent positioning moves.
- ▶ Recent engagements with ClearBridge portfolio companies have touched on ways they are developing carbon capture and sequestration capabilities across several industries and how in most cases advanced CCS capabilities are driving share gains and improving cash flows.

Market Overview

The third quarter continued the sharp post-Liberation Day rebound for U.S. equity markets, with animal spirits driving the benchmark Russell 3000 Index to record highs. Investor optimism was fueled by better-than-feared tariff outcomes, the passing of the One Big Beautiful Bill Act in July, the Federal Reserve delivering a 25 basis point cut in September and signaling further easing and continued appetite for AI-driven investment.

AI-related names led in a relatively narrow market; the market-cap-weighted S&P 500 Index handily outpaced its equal-weighted counterpart, for example. Expectations and valuations across several AI-exposed names rose sharply even as concerns around “circular funding” (whereby AI hardware providers, for example, invest in their own customers) crept into the market late in the quarter. The momentum factor significantly outperformed the market, while quality, which we favor, underperformed.

Against this backdrop the Strategy underperformed, driven mainly by challenges in information technology (IT), where stocks perceived to not be AI beneficiaries like ServiceNow and Monday.com were left behind. Electronic design automation software company Synopsys, meanwhile, has been benefiting from AI-driven chip design cycles, especially in its IP segment, but guidance came in below consensus due to timing effects, China-related headwinds and a slower than expected ramp up of the foundry business at Intel — a major customer — which adversely impacted the shares. However, the shares began to rebound toward the end of the quarter as investors perceived the initial sharp decline to be an overreaction.

Some of the biggest positive contributors were also in IT among the AI-exposed names such as Broadcom — a large position in the portfolio — which has emerged as a competitor to Nvidia on the custom ASIC chip side. In semis, we also benefited from a rebound in ASML — a high-quality semiconductor chip manufacturing equipment name — as the market focused on the continued need to increase chip manufacturing capacity in the years to come.

PTC was another positive contributor on the back of improving industrial software growth, as macro concerns resulting from Liberation Day tariff announcement eased, and on potential for M&A to affect the company.

The Strategy's financials holdings were strong relative contributors, in particular financial services companies like Morgan Stanley and BlackRock; our underweight to certain payments companies was also additive to relative performance.

In industrials, Deere performed well in the first half of the year, yet tariff headwinds began to take their toll on the farm and construction equipment maker's second-quarter earnings as Deere adjusted its full-year profit outlook. More defensive industrials such as waste disposal company Republic Services were also out of favor in a risk-on quarter despite sound long-term fundamentals. We added to our position on weakness, as well as to testing, inspection and compliance leader UL Solutions, a beneficiary of proliferating electrification. United Rentals was a bright spot in industrials, continuing its strong post-Liberation Day rebound as the rental industry has stabilized; the stock has been gaining share in larger construction projects both data center related and otherwise.

After being out of favor in the first half of the year, Tesla shares rose in the third quarter on the back of increased enthusiasm for its opportunities in AI-enabled autonomous vehicles and humanoid robots. The Strategy does not own Tesla, making the stock's strong performance a detractor to relative performance against the benchmark.

While relative performance has been lagging in recent quarters, we have observed improving relative results in 2025 compared to the prior two years, partly due to recent positioning moves. Large relative contributors in the quarter, for example, include United Rentals, Reddit, Argenx — all new positions in the last 12 months, and we believe we are positioned well for a broadening market with gains more evenly distributed across economic sectors.

Portfolio Positioning

With overweights to industrials and materials and modest underweights to the more defensive utilities, consumer staples and health care sectors, we are focusing on companies that are attractively priced and seeing growth in an environment in which, despite widespread investor enthusiasm, growth is becoming harder

to come by. AI-related names have been dominating in this market as spending levels on data center and related infrastructure as well as demand for emerging AI use cases remain robust. Some of our blue-chip holdings, such as Alphabet, Amazon and Microsoft are beneficiaries of this theme as well.

Repositioning moves in the quarter were focused on investments with exposure to various AI themes. However, given increased expectations, we are being selective and are maintaining a disciplined focus on attaining reasonable valuation and favorable risk-reward. These stocks also provide exposure to attractive sustainability themes.

On this front, we initiated a position in Valmont, a leader in building electricity transmission infrastructure. Increased data center construction is driving new demand for power generation, which goes hand in hand with transmission spending. As utility spending on transmission ramps up in the next couple years, we expect Valmont to capture a meaningful share of this opportunity driving both revenue and margin growth.

Within IT, we added Oracle, which has transformed from a mature software vendor into a high-growth hyperscaler, with a unique position in the AI training market. Access to Nvidia chips and partnership with OpenAI have enabled Oracle to rapidly emerge as the fourth hyperscaler (along with Amazon, Microsoft and Google) with significant growth in its cloud business ahead, and we expect a diversified set of customers beyond OpenAI.

We also bought AppLovin, which runs one of the largest mobile ad networks, matching advertisers with app publishers who have ad space within their free-to-use mobile apps. AppLovin's business model is meaningfully driven by the application of AI technology, which has allowed the company to capture a commanding share of its market. We believe AppLovin has the potential to grow its nascent e-commerce advertising business very significantly in the coming years and is in the early innings of a multiyear growth story as it scales its leading direct response ad platform.

We also purchased Clean Harbors, a major industrial waste management company in the U.S. While not a direct play on AI, Clean Harbors is a high-quality, compounding business trading at an attractive valuation and serving a consolidated end market. Its business is benefiting from reshoring in general, with AI data center construction being a part of this trend. In addition, the company is positively exposed to PFAS ("forever chemicals") disposal due to its irreplaceable incineration asset base. Part of its business is also driven by circularity, as it recycles used motor oil, which reduces the carbon footprint of this product.

Meanwhile, we sold out of PTC, harvesting gains after recent strong performance, partially driven by M&A rumors, which left the risk-reward no longer attractive, in our view.

Outlook

Looking ahead, the macro backdrop is stable but the uncertainty that has persisted all year continues. On the one hand, hiring has slowed and federal deficits remain high. On the other hand, unemployment remains low, tariff uncertainty has declined, consumer spending has remained strong (albeit at the upper end of the income spectrum), credit losses are manageable, the Federal Reserve has started lowering rates and the One Big Beautiful Bill Act is expected to inject stimulus into the U.S. economy starting in 2026.

While these conditions are broadly expected to result in a continued soft landing for the U.S. economy, we continue to construct our portfolio on a bottom-up basis, focusing on long-term compounders with leading sustainability characteristics that we can buy at attractive valuations. Regardless of the near-term macro conditions, we continue to believe that the U.S. market offers attractive long-term investment potential due to a combination of the U.S.'s world-leading innovation, favorable demographics, vibrant capital markets and energy security, among other factors.

Portfolio Highlights

The ClearBridge Sustainability Leaders Strategy underperformed its Russell 3000 Index benchmark in the third quarter. On an absolute basis, the Strategy saw positive contributions from nine of 10 sectors in which it was invested (out of 11 total). The IT and financials sectors led contributors, while the consumer staples sector detracted.

Relative to its benchmark, stock selection and sector allocation detracted. In particular, stock selection in the IT, consumer discretionary and industrials sectors detracted, while stock selection in the financials sector proved beneficial.

On an individual basis, the strongest relative contributors were United Rentals, Reddit, Johnson & Johnson, Broadcom and not owning Meta Platforms. Top relative detractors were Novo Nordisk, Walt Disney, Monday.com, ServiceNow and not owning Tesla.

During the quarter, in addition to activity discussed above, we bought CenterPoint Energy in the utilities sector and TJX in the consumer discretionary sector. We exited Novo Nordisk in the health care sector and Accenture in the IT sector.

ESG Highlights: Innovating Carbon Capture Across Industries

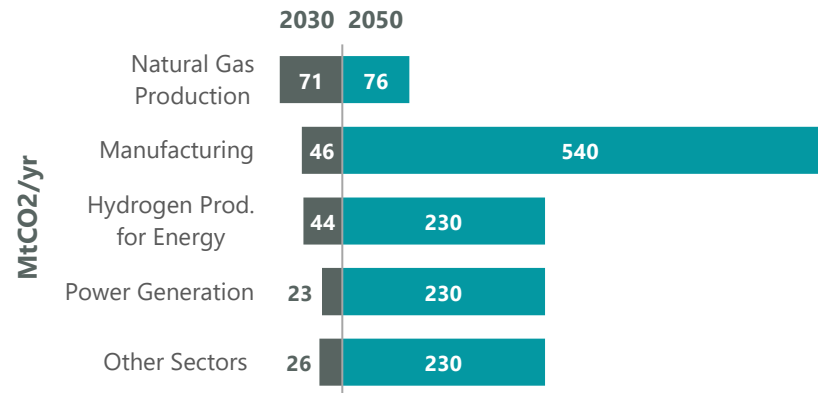
While deployment of renewable energy sources such as solar, wind and hydro will likely play the largest role in the energy transition, carbon capture and sequestration (CCS) remains an important technology for heavy industries that produce unavoidable CO₂ emissions.

There are many types of CCS, and ClearBridge holdings with which we engage regularly represent a diverse portfolio of CCS technologies. Recent engagements with portfolio companies have touched on ways they are developing CCS across several industries and how in most cases CCS capabilities are driving share gains and improving cash flows.

Cleaner Hydrogen Technologies Advancing in Manufacturing

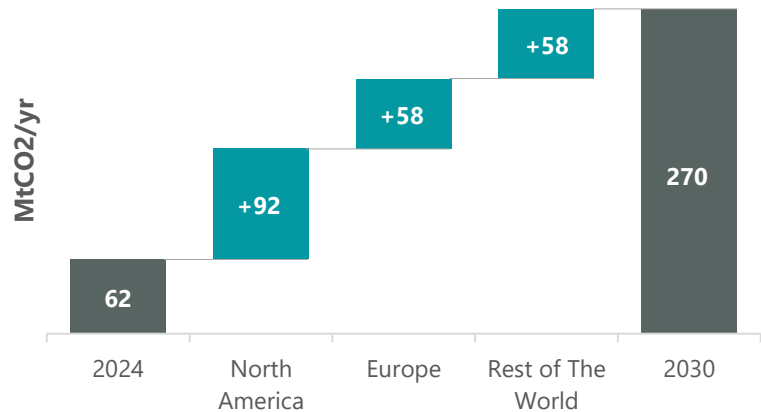
CCS is critical in addressing emissions from manufacturing and will be all the more so as capacity additions ramp up globally in the coming years (Exhibits 1 and 2). In North America, the main applications are hydrogen and ammonia. These were focal points of recent ClearBridge discussions with industrial gas company Linde, which we find is well-positioned to continue taking share in clean hydrogen, specifically blue hydrogen. (Blue hydrogen is produced using fossil fuels but with carbon capture technology preventing emission of CO₂, and is used for various industrial, energy and transport applications.)

Exhibit 1: CCS by Sector 2030 and 2050



As of 2025. DNV, "Energy Transition Outlook CCS to 2050."

Exhibit 2: CCS Capacity Additions to 2030



As of 2025. DNV, "Energy Transition Outlook CCS to 2050."

ClearBridge recently toured Linde's autothermal reformer (ATR) site at its Clear Lake facility in Texas, where Linde provides blue hydrogen and CO₂ to support industrial chemicals supplier and manufacturer Celanese with its methanol and acetyl production.

An ATR is essentially a large chemical reactor that combines natural gas, oxygen and water/steam to produce synthesis gas or syngas (hydrogen plus carbon monoxide/dioxide), a critical input for applications like chemicals production (such as methanol, which is used for paint solvents, antifreeze, fuels, pharmaceutical laboratories and adhesives, among other things). Syngas is also used in power generation, ammonia and fertilizer production for growing crops, and refining (desulfurizing oil, which reduces sulfur dioxide emissions).

Linde's ATR technology is especially attractive as it is more efficient than other methods of producing these inputs given its better energy efficiency, higher CO₂ concentration for better carbon capture, higher product yield and lower maintenance.

Linde has been able to leverage the success of this technology as a proof point to win other projects that support clean hydrogen and ammonia production in the U.S. Other blue hydrogen deals, such as in Nederland, Texas (where Woodside/OCI creates blue ammonia for agriculture, power and marine sectors), in Alberta, Canada (where Dow produces blue hydrogen for ethylene production with two ATRs), and the latest in Modeste, Louisiana (where CF Industries runs a large-scale air separation unit to support blue ammonia).

Linde represents an excellent example of a company where technological expertise in a sustainability practice is driving both emissions savings and growth for the business. In 2024, Linde helped its customers to avoid more than 96 million metric tons of carbon dioxide equivalent, more than twice the emissions that Linde generated from its own operations.

What is Biogenic CO₂?

Green Plains, a U.S.-based agricultural technology and biorefining company based in Nebraska, is one of North America's largest producers of ethanol and bio-based products. It serves several main industries, such as ethanol for fuel, agricultural services (grain management), high-protein feed for livestock and aquaculture and renewable corn oil.

ClearBridge recently met with Green Plains's CFO and Director of Sustainability to discuss the company's carbon capture initiatives and other developments that impact its carbon intensity (CI) and ability to meet its target of net-zero emissions by 2050. The company recently suspended its clean sugar technology (CST) and ultra-high protein (UHP) initiatives to focus on carbon capture, which is more cost-effective under current tax credit structures.

Green Plains considers carbon capture a key tactic in decarbonizing biorefineries by capturing the pure stream of biogenic CO₂ from

fermentation (CO₂ is released from the fermentation process of biological materials such as plants used for biofuels). Initiatives include partnering with Tallgrass Energy on the Trailblazer carbon pipeline, which will initially serve three Green Plains facilities in Nebraska, and is expected to sequester 800k tons of CO₂ annually beginning this year. These facilities are also expected to generate \$150 million in 45Z tax credits (for clean fuel production).

In addition, running other plants in a similar fashion without carbon capture can net another \$50 million under 45Z. Green Plains is raising capital for another deal with startup Carbon Solutions to perform carbon capture on other Midwestern plants. If the 45Z program isn't extended after 2029, Green Plains would drop down to 45Q credits, which are worth one-third of 45Z, until that program ends in 2038.

Overall, however, these credits are valuable programs that get Green Plains past recent liquidity issues after years of capex on plant modernization. With roughly \$50 million left in carbon capture capex, Green Plains has already cut its operating expenses by more than 50%, setting it up to generate ample free cash flow going forward.

Rocks Can Sequester Carbon

In a recent engagement with Vulcan Materials, the largest producer of construction aggregates such as crushed stone, sand and gravel in the U.S. and a name widely owned across ClearBridge, we checked in on Vulcan's goal of 10% absolute reduction in Scope 1 and 2 emissions by 2030. Vulcan shared that its Scope 1 and 2 emissions profile declined by 3% in 2024 versus its 2022 baseline, an improvement on 2023's flat performance. While 3% may seem low, aggregates production already carries a low GHG intensity, so the incremental progress is notable.

Key drivers were increasing renewable adoption (now 14% of total electricity versus a 5% stated goal), upgrades to engines with 20%–50% lower emissions and increased renewable diesel usage in California. Renewable diesel — produced from vegetable oils, waste oils and animal fats and, unlike biodiesel, a “drop-in” fuel that can be used directly in engines without blending or modifications — now accounts for 9% of Vulcan's total diesel usage.

We also touched on Vulcan's operational use of water to wash residue off rocks and to suppress dust. We were encouraged to hear water recycling takes place at roughly 75% of Vulcan's sites and that the company is striving for further improvement.

Increasing water recycling is a win-win from both a sustainability and economic perspective. At the 25% of sites where there is no recycling, Vulcan purchases water and absorbs the cost of trucking it. This seems like an easy target for the company to address over time.

Another interesting facet of Vulcan's environmental profile is that some of its basalt fines (i.e., dust byproduct of rock production) actually help sequester CO₂. We learned the agricultural market can

spread this byproduct on soil to support “enhanced rock weathering” whereby rainwater spurs a chemical reaction that traps atmospheric CO₂ in newly formed, solid material. While sequestering CO₂ with basalt fines is certainly not a core part of Vulcan’s business, it is nonetheless a positive attribute in its environmental profile.

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