



Mid Cap Growth Strategy



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Key Takeaways

- ▶ Despite an optimistic start to the year, headlines around potential tariffs/global trade friction and a rotation out of AI-related tech stocks sent equities lower in the first quarter.
- ▶ The Strategy underperformed as detractors in technology and greater uncertainty in industrials overcame a handful of positive contributors across the financials, consumer staples and energy sectors.
- ▶ While we did not emerge unscathed from the equity correction, such market shocks are opportunities to acquire and add to high-quality companies with attractive growth opportunities at compelling prices.

Market Overview

Despite an optimistic start to the year, tariff threats and trade policy changes under the new Trump administration and a rotation out of AI-related stocks spurred volatility and uncertainty that sent equity markets lower for the first quarter. Amid the decline, mid growth stocks broadly outperformed other areas of the market with the Russell Mid Cap Growth Index declining -7.12% compared to the -9.97% and -11.12% declines of the Russell 1000 Growth and Russell 2000 Growth Indexes, respectively. However, the swing from market optimism to risk-off sentiment propelled value and core stocks ahead of their growth counterparts, with the Russell Midcap Value Index (-2.11%) holding up the best among mid caps, followed by the Russell Midcap Index, which declined -3.40%.

For growth investors, the surprise emergence in January of DeepSeek, a China-based low-cost large language model, stoked fears about the returns to be expected from the massive investment being made in the AI ecosystem. This sentiment shift took down information technology (IT) stocks and those indexed to AI buildouts in other sectors.

Portfolio Performance

The ClearBridge Mid Cap Growth Strategy underperformed its benchmark in the first quarter, as the rotation out of IT and AI stocks weighed on several of our fourth-quarter winners. This included Marvell Technology, a networking and storage semiconductor company with a strong presence in data centers, as high expectations for data center spending were questioned in the wake of the DeepSeek reveal. The fallout spilled over to industrials holding Vertiv,

which manufacturers thermal management systems for data centers. However, regardless of the DeepSeek impact, we believe that large AI hyperscalers will continue to need to develop and build new and more intensive data centers, providing both Marvell and Vertiv with a long-term opportunities to capitalize on their positions as preferred partners in new data center construction.

Another significant detractor was AI-enabled advertising company AppLovin, although this was largely due to AppLovin being a victim of its own success. Shares came under pressure from several short seller reports during the quarter, which sought to capitalize on a reversal in the company's positive momentum and strong run-up last year amid the broader tech retreat. We believe that the company continues to be one of the best AI opportunities within the mid cap market, and that strong positive channel indicators for its e-commerce business points toward a solid and persistent future of attractive returns.

Our top contributor during the period was Tradeweb Markets, an operator of electronic financial markets, which saw increased demand for its data and analytics, trade execution and trader processing services as the rapid increase in uncertainty spurred greater trading activity. The Strategy also benefited from continued strong execution from companies in more traditionally defensive sectors, such as Casey's General Stores in the consumer staples sector and Steris in the health care sector. Steris also received added tailwinds from the resolution of a liability lawsuit that had previously weighed on the company's long-term growth projections.

In energy, EQT, North America's largest natural gas producer, continued its upward trajectory from the fourth quarter as the U.S. endured its coldest winter since 1988, upping demand. Additionally, EQT continues to capitalize on strong operational performance, making additional progress on its goal of deleveraging and extending its lead as the lowest-cost producer in the basin.

Portfolio Positioning

During the quarter we participated in the IPO of SailPoint, which offers identity security solutions to help companies manage and secure access to critical data and applications. Having known the company for a long time and previously owned it in its prior publicly traded form, we believe the incorporation of AI has swelled the company's attractive total addressable market — already growing at a high pace — as companies will need to begin addressing what data and functions their new AI agents can access across their enterprise.

We also refined our health care exposure, swapping Sarepta Therapeutics for a new position in Alnylam Pharmaceuticals. Alnylam is a biopharmaceutical company focused on RNA interference therapeutics for genetic diseases. We like Alnylam due to its broad, robust and repeatable drug development process and pipeline, and

believe the anticipated 2025 launch of its new product designed to treat heart failure represents a substantial growth opportunity within an underpenetrated market.

Our largest sale during the quarter was of alternative investment manager KKR, which focuses on private equity and real estate investments. While we continue to like the company and believe it to be a leader within the alternative investment space, we exited the position as the company outgrew our target mid cap market.

Outlook

While we did not emerge from the first quarter unscathed, we see these market shocks as opportunities to acquire and add to high-quality companies with attractive growth opportunities at compelling prices. As the global economic outlook grows murkier, we feel strongly that our companies will continue to invest in their businesses from positions of balance sheet strength. In the past, this has enabled our companies to take market share from smaller or weaker-capitalized companies.

Portfolio Highlights

The ClearBridge Mid Cap Growth Strategy underperformed its benchmark during the first quarter. On an absolute basis, the Strategy had positive contributions across three of the 11 sectors in which it was invested. The leading contributor was the energy sector, while the IT and industrials sectors detracted the most.

On a relative basis, overall stock selection detracted from performance. Specifically, stock selection in the IT, industrials, consumer discretionary and health care sectors weighed on performance. Conversely, stock selection in the real estate and consumer staples sectors benefited performance.

On an individual stock basis, the biggest contributors to absolute returns during the quarter were Tradeweb Markets, EQT, Casey's General Stores, MercadoLibre and Steris. The largest detractors from absolute returns were Trade Desk, AppLovin, Marvell Technology, Datadog and HubSpot.

In addition to the transactions mentioned above, we initiated new positions in Verisk Analytics in the industrials sector, CAVA in the consumer discretionary sector, Ryan Specialty and Ares Management in the financials sector and Jones Lang LaSalle in the real estate sector. We exited a position in Celsius in the consumer staples sector.

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