Large Cap Growth ESG Strategy

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Key Takeaways

- Momentum carried markets higher on strong earnings and easing geopolitical concerns, while the Russell reconstitution and SpaceX's historic IPO significantly reshaped large cap growth benchmarks.
- Although the Strategy underperformed for the quarter, we believe benchmark changes, broader market participation and continued AI infrastructure leadership create a strong setup for alpha generation in the second half of 2026.
- As the regulatory landscape evolves for social media platforms, active stewardship on youth safety, content moderation and disclosure can help assess whether companies are managing emerging legal, reputational and operational risks effectively.

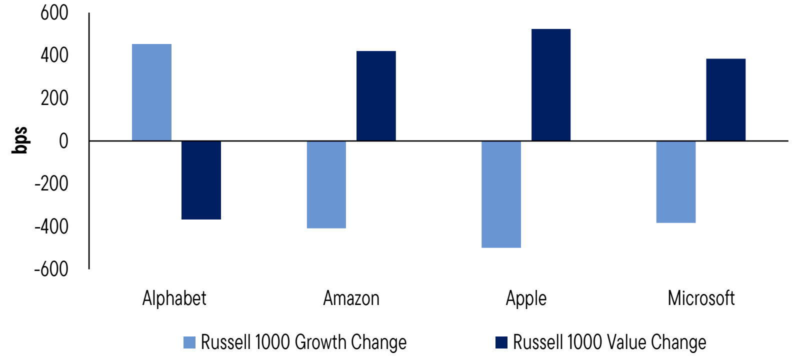
Market Overview

Equity markets rallied in the second quarter, fueled by robust corporate earnings and optimism that a U.S.-Iran ceasefire would bring down commodity prices and temper geopolitical risk. Despite wavering sentiment for AI investments late in the period, the S&P 500 Index finished up 15.2%, its best quarterly showing since 2020, while the benchmark Russell 1000 Growth Index advanced 16.7%.

While markets are constantly evolving, we witnessed an acceleration of those normal fluctuations in June, highlighted by unprecedented changes to large cap benchmarks in the Russell U.S. Indexes Reconstitution and SpaceX completing the largest initial public offering in history.

The Russell rebalance substantially reduced the weighting of the Magnificent Seven in the Russell 1000 Growth Index (RLG), with Apple, Microsoft and Amazon shifting toward the Russell 1000 Value Index while Alphabet's weight increased (Exhibit 1). Factoring in the net effect of these changes, the index saw a reduction in top-heavy concentration, which we view as a welcome change. At the same time, the rebalance has caused the index to become more momentum-oriented. We began repositioning the portfolio for these changes in advance of the rebalance and, although we are confident in our positioning entering the third quarter, we will continue to refine our exposures as the market evolves. Our objective remains to express our highest-conviction ideas while also appropriately managing risk among benchmark holdings.

Exhibit 1: Significant Mega Cap Benchmark Changes



Changes measure weighting of each stock on June 26 in each index. Source: FactSet.

Portfolio Positioning

During the quarter we added meaningfully to Alphabet, in anticipation of the Russell rebalance, as well as several other existing positions: Arista Networks, a leading maker of high-speed switches enabling high-speed data transfer within server racks; Blackstone, an alternative asset manager; and Tesla, an EV and battery storage manufacturer.

Our participation in the SpaceX IPO also keeps the portfolio in step with a risk-on benchmark. A diversified aerospace and communications company, SpaceX competes in several large addressable markets with a significant technology lead versus peers. Its core competitive advantage is its proven ability to reuse rockets, which materially lowers the cost of delivering payloads into orbit. This capability is supported by the company's vertically integrated approach to rocket design, manufacturing and launch operations. By combining SpaceX's operations with Starlink, the dominant satellite Internet provider, the company plans to extend this playbook into AI infrastructure scaling orbital data center compute. SpaceX also has demonstrated the ability to lower the cost of scaling data center compute terrestrially through innovative techniques like onsite battery power generation. Moving forward, key questions are around execution as SpaceX scales its next generation of large payload rockets, enabling the company to unlock multiple new end markets.

Supporting diversified growth exposure outside technology, we initiated a position in Boston Scientific, a medical technology company developing minimally invasive devices to treat cardiovascular, oncological and a range of other conditions. We believe the market underestimates the company's durability of growth beyond its headline drivers — WATCHMAN for stroke prevention and electrophysiology to treat atrial fibrillation — as many treatment areas remain underpenetrated. We see a consistent pipeline of internal innovation and tuck-in M&A supporting durable, high-single-digit organic growth and low-teens earnings growth through the cycle, which we view as not fully reflected in the stock's current valuation.

To enable these moves, we substantially trimmed exposure to Amazon.com and Microsoft.

The Strategy also exited a position in Intuit due to growing concerns that AI could commoditize parts of its tax business. In order to maintain competitiveness, management appears to recognize the need to reinvest in the TurboTax platform, which we believe could weigh on forward guidance. We also see rising competition to Intuit's QuickBooks small business finance software platform from both traditional and AI peers. Our sale follows similar logic applied to other software companies over the past few years: exiting companies with weak or weakening core businesses that do not have a clear AI strategy to compete in an increasingly complex environment.

Outlook

Amid this rapidly evolving market, the ClearBridge Large Cap Growth ESG Strategy underperformed its benchmark for the quarter. Despite recent headwinds, the transformation of the RLG and the greater investment flexibility we have gained through the Strategy's transition to a non-diversified mandate gives us renewed confidence in our ability to deliver alpha for shareholders. While maintaining a well-rounded portfolio in a concentrated market with a focus on valuation, longer-term ownership and delivering consistent results through the business cycle, we have gained a more effective structure to capitalize on our best ideas. Being non-diversified will also allow us to better manage heightened volatility, especially at the top of the portfolio, with more potential mega cap IPOs on the horizon and the RLG now going through a reconstitution every six months.

In the second half of 2026, we will continue to recalibrate our portfolio exposures and evaluate the best ways to represent AI. One way to do this is by assessing the AI lifecycle: the first beneficiary in 2024 was GPU leader Nvidia; 2025 saw Broadcom take market share in custom silicon for AI applications; in 2026 leadership has shifted to AI infrastructure — the picks and shovels providers of memory and various needs for data centers. These companies are leading an information technology (IT) sector generating earnings growth that is twice as fast as the overall market. Such earnings power allays the risks of a growth stock bubble, although we remain concerned about when massive hyperscaler capex will produce a compelling return on investment.

We entered the year expecting a broadening market, a development sidelined by war in the Middle East. With the conflict nearing a resolution and commodity prices down, we believe the Fed could look past recent upticks in inflation and cut interest rates in the second half of 2026. We would expect such an easing of financial conditions to promote greater market participation and benefit focus areas like industrials.

Portfolio Highlights

The ClearBridge Large Cap Growth ESG Strategy underperformed its Russell 1000 Growth Index benchmark in the second quarter. On an absolute basis, the Strategy delivered positive contributions across six of the eight sectors in which it was invested (out of 11 sectors total). The primary contributor to performance was the IT sector while the health care and communication services sectors were the main detractors.

Relative to the benchmark, overall stock selection and sector allocation detracted from performance. In particular, stock selection in the communication services, health care and industrials sectors, overweights to the communication services and materials sectors and an underweight to the IT sector weighed on results. On the positive side, stock selection in the IT, consumer discretionary and consumer staples sectors, along with an underweight to consumer staples, contributed to performance.

On an individual stock basis, the largest relative detractors included Netflix and Intuit, as well as not holding Advanced Micro Devices, Lam Research and KLA. The largest relative contributors were Palo Alto Networks, ASML, Taiwan Semiconductor Manufacturing, Datadog and an underweight to Microsoft.

In addition to the transactions mentioned above, we gained shares of Honeywell Aerospace following its spinoff from existing holding Honeywell International. We also closed out S&P Global in the financials sector.

ESG Highlights

Social media companies are coming under increasing pressure from state attorneys general, school districts and parents arguing platforms such as Meta Platforms' Facebook and Instagram, Snapchat, TikTok and Alphabet-owned YouTube knowingly designed features that are addictive to young users and failed to adequately warn about mental health risks.

The success of recent lawsuits in California and New Mexico against Meta and YouTube could be impactful for social media broadly, raising regulatory and financial risk and creating the potential for reputational damage.

In New Mexico, a jury awarded $375 million in civil penalties against Meta for misleading the public about predator exploitation on its platforms in violation of state consumer protection law.

Not long after, a jury in Los Angeles became the first to hold social media companies responsible for contributing to a plaintiff's mental health harm via addictive design. The jury determined that Meta and YouTube were liable for negligence and failure to warn related to the plaintiff's alleged social media addiction. The plaintiff was awarded $6 million in damages.

These lawsuits are notable for not seeking action against the content featured on the platforms — for years, such attempts were unsuccessful, largely due to Section 230 of the Communications Decency Act, which protects social media companies from liability related to content posted by their users. Instead, the lawsuits attempt to find fault in the design of the products.

They also follow several milestone national regulations around the world that have involved restrictions on youth access to social media (Exhibit 2). Several U.S. states — such as Utah, Arkansas, Louisiana, Florida, Georgia, Tennessee and Nebraska — have also passed laws restricting minors' use of social media, although many of these are currently being challenged in court.

Exhibit 2: National Restrictions on Youth Access to Social Media

2023	France	Prohibits most social media accounts for children under 14 and parental consent for ages 14-15
2024	Australia	First country to enact nationwide min. age of 16 for social media
2025	Australia	Under 16 ban enters into force
2025	Malaysia	Establishes nationwide min. age of 16 for social media
2025	Portugal	Establishes nationwide min. age of 16 for social media

As of June 30, 2026. Source: ClearBridge Investments.

Social Media Platforms and Active Ownership

The Large Cap Growth ESG Strategy owns both Meta and Alphabet, and we are cognizant of the risks to both society from social media and the companies via potential liability. Against this backdrop, we recently engaged with Meta to discuss youth safety. In our conversation in May, we sought to test the real-world effectiveness, credibility and trade-offs of Meta's youth safety efforts, while probing regulatory risk, reputational risk with financial penalties and competitive positioning.

Meta shared that it believes its youth safety measures such as AI-based age verification, content moderation and privacy and parental controls are best-in-class, although this could be challenged. The company also shared that it supports youth safety regulation; its requests for regulation would be for no outright bans, consistency across geographies and equal application to all social media companies.

Meta noted that its Teen Accounts enable the above safety measures by default, it employs AI to screen account content for signs that a user may have lied about his or her age and it automatically age gates as appropriate. In aggregate, these features have led to a "marked improvement" in compliance and outcomes, according to the company. In response to critics that claim these features still let through inappropriate content, the company believes these instances of algorithm failure are exceptions rather than the norm.

We advised the company to disclose the data supporting its claims that its youth initiatives are working and leading to "marked improvement," as it did not provide any during the meeting. Further, we shared our preference that, to lend greater credibility to the claims, this data should be audited by a third party.

We also explained our difficulty in locating information on these issues on Meta's websites. We noted that information difficult to find for professional investors would likely be even more challenging for everyday users — parents, for example — to locate and to inform their decisions to use the platform. We asked the company to consolidate all its statements on this subject in a single place — rather than spread it out across several different websites — to make it easier for various stakeholders to find and evaluate, similar to what the company does for its environmental disclosures. Meta was receptive to our input.

ClearBridge's approach focuses on the companies' risk management regardless of the source of risk.

In June a trust and safety company that helps platforms and AI developers detect and prevent harmful online behavior and unsafe AI outputs published a study in cooperation with Meta that used Meta's content standards to compare the Teen Accounts content experience on Instagram versus a competitor platform. Testing was conducted from mid-December 2025 to mid-January 2026 and found that the safeguards applied to Teen Accounts on Instagram performed better than a competitor platform across several dimensions. While the period may seem short for such a study, Meta has disclosed that Teen Accounts are in the hundreds of millions; as users access the apps multiple times a day, this would aggregate to a statistically significant sample, although ideally the company could disclose time series data showing content moderation improvement over a longer horizon. Also in June, Meta rolled out its Teen Accounts protections globally to all apps as well as parental alert notices for inappropriate content searches by teens.

Conclusion

Content responsibility remains a key component in assessing social media platforms such as those operated by Meta and Alphabet. ClearBridge's approach stresses several components of this topic: rigorous content moderation can potentially limit harmful or illegal content while seeking to maintain platform integrity, and child safety raises questions of regulatory and reputational risk.

Over the years of ClearBridge's ownership with Meta and Alphabet, we have witnessed both companies improving their content responsibility (Exhibit 3). Meta has made progress on its content policy by appointing an independent content oversight board and then growing its scope. After historically having some issues around brand safety and protecting children from sensitive content, YouTube has made significant progress in this area through staffing, technology and policy development. In 2021, YouTube became the first digital platform to receive accreditation for content-level brand safety from the Media Rating Council (MRC), following an independent audit of its content moderation, monetization and ad placement systems.

At the same time, recent litigation with social media suggests the risk profile for these companies is evolving; regulatory risk is shifting from content moderation to product design. ClearBridge's approach focuses on the companies' risk management regardless of the source of risk. As our engagement with Meta shows, we also focus on transparency, as investors need evidence that youth safety initiatives are working in practice, not only descriptions of policies or tools (Exhibit 3).

Social media is a fast-moving topic involving billions of participants — Meta reports 3.5 billion daily active users, while Alphabet reports over 2 billion signed-in monthly users for YouTube. We continue to educate ourselves on the sustainability factors affecting this industry as we monitor the evolution of litigation and the broader social media bans; we will continue to actively incorporate this analysis into our investment process and stewardship activity.

Exhibit 3: Content Responsibility Improvement Timeline

Year	Meta	Alphabet
2018	Announces Oversight Board	Expands AI moderation investments
2020	Oversight Board established	COVID-19 misinformation policies
2021	Oversight Board begins issuing decisions	First MRC content-level brand safety accreditation
2022	Updated Community Standards enforcement, explanation and review	Enhanced election misinformation measures
2023	AI content labeling initiatives launched	Generative AI safety commitments
2024–2025	Expanded AI-generated content policies	Gemini AI safeguards and synthetic media labeling

Source: ClearBridge Investments.

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