



Large Cap Growth Strategy



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Market Overview

U.S. equity markets extended their rally in August, with major indexes reaching new record highs amid robust corporate earnings, an increasing likelihood of interest rate cuts and continued optimism around AI. The S&P 500 Index climbed 2.0% while the NASDAQ Composite Index advanced 1.6%. Value stocks outperformed growth, with the Russell 1000 Value Index returning 3.2% and the benchmark Russell 1000 Growth Index returning 1.1%.

Minutes from the Federal Reserve's July meeting revealed a divided committee, with some members advocating for rate cuts to support employment, while others emphasized the need to guard against upside inflation risks. Chair Powell's Jackson Hole speech underscored the Fed's cautious stance, noting that while inflation has moderated, it remains above target, and the labor market is showing signs of cooling. Following the speech, futures markets pegged the likelihood of a rate cut at the Fed's September meeting at 87%.

U.S. Treasury yields declined during the month, falling from 4.4% to 4.2%, reflecting market uncertainty over the Fed's next moves and the broader economic outlook.

Portfolio Highlights

The ClearBridge Large Cap Growth Strategy underperformed its Russell 1000 Growth Index benchmark in August. On an absolute basis, the Strategy delivered positive contributions across six of the nine sectors in which it was invested (out of 11 sectors total). The primary contributors to performance were the materials and financials sectors while the information technology (IT) sector was the main detractor.

Relative to the benchmark, overall stock selection detracted from performance while sector allocation effects proved beneficial. In particular, stock selection in the IT, consumer discretionary and communication services sectors detracted from performance. On the positive side, stock selection in the consumer staples sector and an overweight to the materials sector contributed to performance.

On an individual stock basis, the primary detractors from relative performance for the month included Apple, Intuit, Eaton, Marvell Technology and Meta Platforms. The leading contributors to relative returns were Microsoft, Palo Alto Networks, Sherwin-Williams, ASML and Netflix.

Portfolio Positioning

We made several changes to the portfolio to better participate in the market's most attractive growth areas. Prompted by our recent re-examination of our health care holdings, we exited UnitedHealth Group and Novo Nordisk. The health care sector is facing a myriad of questions around underlying spending levels, tariff concerns and regulatory risks. After trimming managed care provider UnitedHealth regularly over the last three quarters, we took returning CEO Stephen Helmsley's turnaround plan released at the end of July to indicate that the profitability issues at UnitedHealth are very far reaching and the path to recovery will be protracted, prompting our exit.

We purchased Novo in December believing the stock was more undervalued compared to GLP-1 competitor Eli Lilly and that the market was underappreciating the company's potential share gains. Our optimism was predicated on a robust pipeline and indications that the negative impacts from compounders entering the GLP-1 market were set to abate. While Novo has pipeline potential, we believe it will take time for incremental data to prove this out. At the same time, the compounder issue, which has had a material impact on Novo's growth, is taking longer to abate than previously anticipated. Without a clear path for the company to retake market share versus Lilly — a position we closed in July — and given our more muted view of the GLP-1 market, we sold the position to fund better growth opportunities elsewhere. At the same time, we upgraded our biopharmaceutical exposure with the purchase of Vertex Pharmaceuticals, a high-quality biotech with a leading franchise in cystic fibrosis. We have been following Vertex for some time and see pain as its next big opportunity. Some disappointments in the timing of clinical trials for chronic pain enabled us to establish a position at what we view as a moderate valuation relative to its pipeline.

One of the more compelling segments of technology right now is support for generative AI buildouts. Here we initiated a position in Datadog, which operates a monitoring, observability and data security platform for cloud applications. We believe large language model (LLM) observability, a rapidly growing market due to the acceleration of Gen AI workloads, creates a new vector for growth not reflected in fundamental estimates. The company's end-to-end platform is positioned to consolidate multiple observability vendors, increasing cross-selling opportunities and support high teens to low 20s revenue growth for multiple years. While Datadog trades at a premium valuation, we believe the mission critical nature of its offering and its flexible, consumption-based model should enable it to maintain pricing power in an increasingly competitive observability market.

The Strategy also added a position in Parker-Hannifin, a diversified manufacturer in industrials. One of the company's two main segments is aerospace, a resilient growth area in an otherwise challenged economy. We have been optimistic about the durability of growth in aerospace as expressed through portfolio holdings RTX and Airbus. Parker-Hannifin is also exposed to short-cycle industrial businesses

where orders are stabilizing back to growth. While it is still too early to definitively call a positive inflection in the industrial economy, we see green shoots here and want portfolio exposure to improving trends.

Outlook

We are preparing for a potentially volatile second half of 2025 but feel better about an improving fundamental setup next year. Consumer spending has been resilient and consumer confidence has bounced back off the early 2025 lows. Several positive catalysts for the economy should be apparent in the medium term and we will continue to position the portfolio to participate. The One Big Beautiful Bill Act could add an estimated 50 bps to 2026 GDP growth thanks to immediate expensing of R&D and domestic capital spending. Companies are also becoming more confident about getting on with decisions despite lingering uncertainty as evidenced by an uptick in recent M&A activity. At the same time, weaker recent jobs reports and downward revisions to prior months show a slowing labor market. We are also cognizant that tariff impacts could be more pronounced through the rest of the year.

Market performance has been bolstered by robust corporate earnings. For the second quarter, with 98% of S&P 500 companies having reported, 81% of them delivered positive earnings and revenue growth, per FactSet. The estimated earnings growth rate of 11.9%, would mark the third consecutive quarter of double-digit earnings growth. This backdrop contributes to our view that growth companies beyond the mega caps present the most attractive opportunities in what remains a highly valued market.

We continue to carefully calibrate our mega cap exposure to participate in the secular trends of Gen AI buildouts, cloud computing and digital advertising while also promoting diversification. When our active weight positions (Meta, Amazon) outperform, the Strategy is better able to keep pace with our highly concentrated benchmark. However, when our most significant underweight exposures outperform, as was the case in August with Apple up 12%, relative performance can be challenged.

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