



All Cap Growth Strategy



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Key Takeaways

- ▶ The Strategy performed in line with the benchmark in a value-led market, supported by broader participation among our positions in health care and communication services.
- ▶ Guided by valuation, we took advantage of elevated volatility to initiate three new positions while exiting eight positions where confidence in our thesis had waned.
- ▶ Our focus remains on managing the Strategy for a wide range of possible outcomes, relying on companies capable of generating organic growth through a slowing economy and leaning on defensive names through market headwinds.

Market Overview

Volatility rose in the third quarter as a series of weak employment reports caused a growth scare that sent parts of the U.S. equity market into a brief correction. Lifted by the Federal Reserve's ambitious 50 basis point interest rate cut, stocks rallied to finish the period with broad gains. The S&P 500 Index rose 5.89% while the small cap Russell 2000 Index jumped 9.27% as equity leadership broadened beyond the Magnificent Seven.

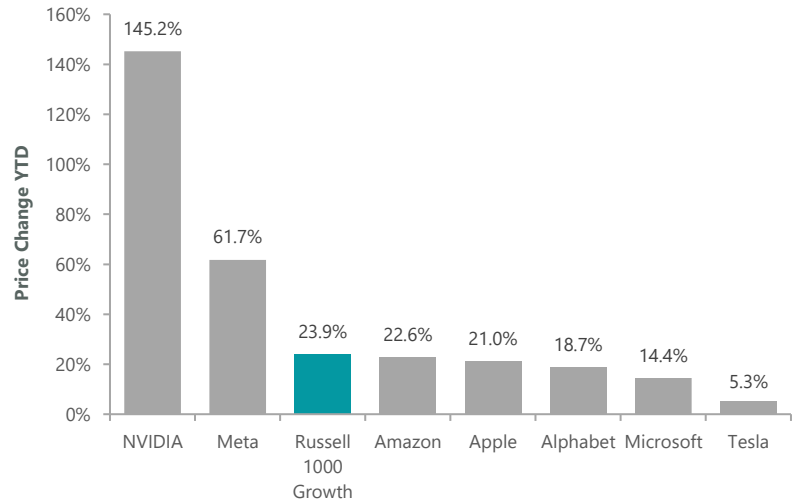
Profit taking among mega caps and early indications of a potential market rotation caused growth stocks to trail value for the quarter. The benchmark Russell 3000 Growth Index advanced 3.42%, underperforming the Russell 3000 Value Index (+9.47%) by over 600 bps.

For most of 2023 and the first half of 2024, momentum-oriented and AI-driven growth stocks led the market. In these environments, the ClearBridge All Cap Growth Strategy saw greater participation from higher-growth and disruptive growth companies. In more balanced markets, like the one that characterized the third quarter, we see broader contributions, with performance driven more by our stable compounder and cyclical growth holdings.

The Strategy performed mostly in line with the benchmark for the period, supported by this emphasis on diversification. On a sector level, relative performance was led by the health care and communication services sectors. On a stock level, the Strategy received meaningful absolute contributions from mega caps Meta Platforms, Apple and Broadcom, durable compounders UnitedHealth Group and Accenture as well as more cyclical holdings such as PayPal, Sherwin-Williams and Grainger.

While the Strategy is benchmarked against a historically concentrated Russell 3000 Growth Index, one of our priorities is managing the portfolio’s mega cap exposure. Since we cannot own the entire Magnificent Seven at market weight, we must evaluate which companies are best positioned to outperform over the next three to five years and, for the past year, we have done an effective job in choosing which companies to overweight and underweight. Magnificent Seven performance has continued to diverge in 2024, making it even more important to deliver solid stock selection both among this group and across the rest of the growth market.

Exhibit 1: The Divergent 7



As of Sept. 30, 2024. Source: ClearBridge Investments, FactSet, Russell.

The Strategy is meaningfully underweight the Magnificent Seven compared to our benchmark. This is by intention, both to prudently manage risk among a small but strong-performing cohort of growth companies as well as to take full advantage of the more attractive growth businesses that our fundamental research uncovers. As a compliment to our larger cap holdings, we continue to see many of these opportunities among companies in the \$10 billion to \$100 billion cap range.

Portfolio Positioning

New addition Builders FirstSource (BLDR), the largest U.S. distributor of building products, prefabricated components and value-added services to professional homebuilders, fits into this “mid cap plus” buy range. An organic share gainer, we see opportunity for BLDR to continue to consolidate share in a fragmented building products distribution market and believe its investments in digital capabilities (3D models and collaboration tools), which smaller competitors do not have the scale to match, can help accelerate share gains.

While the Strategy continues to have a significant position in Nvidia, we are underweight semiconductors versus the benchmark. We added to our semiconductor positioning during the quarter with the

purchase of Taiwan Semiconductor. TSM, an out-of-benchmark name, is the world's fabrication production provider of choice. The criticality and sophistication of its manufacturing footprint powers all of the leading edge fabless global semiconductor companies, including Apple, Nvidia, Qualcomm, AMD and Broadcom. While AI has driven upside in data centers, PCs and handsets are at cycle lows, positioning half of the company's business for a recovery.

On the sell side, we remain disciplined in revisiting our thesis for each underperformer and determining whether we still have high confidence in the company. This analysis led us to exit eight positions during the quarter.

Estee Lauder, a well-known global cosmetics and skin care brand in consumer staples, was purchased as a cyclical turnaround investment in late 2022. At that time, the company had already reduced its earnings outlook due to softness in its high-margin skin care business, primarily driven by bloated inventory in the Asia travel retail distribution channel. Although we appreciated that operating margin improvement was going to be a journey, weak results in China have persisted longer and been more pronounced than we appreciated. Estee Lauder's outlook for fiscal year 2025 points to another year of challenges in its end markets. While we still believe Estee Lauder's long-term profitability is underappreciated, we fully exited the position in the quarter due to lack of visibility on fundamental improvement to the business.

We also exited long-time holding Wolfspeed, a leading global supplier of silicon carbide substrate wafers and devices. After giving management ample time to ramp production at its new Mohawk Valley facility, we closed the position due to continued execution missteps and cyclical headwinds impacting electric vehicle, industrial and energy applications that have repeatedly pushed the company's path to profitability further out.

Workflow and collaboration software maker Atlassian was sold as it continues to experience seat-based spending pressure from end customers rationalizing headcount and re-prioritizing information technology (IT) budgets. The company is also executing upon an on-premise to cloud migration, which has introduced incremental volatility to operating results. We also sold our position in tier 1 automotive parts supplier Aptiv. Part of our original investment thesis for Aptiv was that the company should garner a premium multiple versus competitors as its product portfolio was well-positioned to take share as auto production shifted toward electric vehicles. However, weak global auto demand and slowing mix shift toward EVs has pressured Aptiv's business and the company is capturing share at a slower rate than we anticipated. While Aptiv has executed well on profitability and trades at a cheap valuation, we do not foresee the same level of multiple expansion as the company's growth relative to the market remains weak.

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Outlook

Our focus remains on managing the Strategy for a wide range of possible outcomes. We do this by building some ballast into the portfolio through the ownership of more defensive companies like uniform and business services provider Cintas, off-price retailer TJX Companies and life science tools and diagnostics provider Thermo Fisher Scientific. We view owning these companies as akin to buying an insurance policy; there is a cost to the insurance, as they are likely to trail in momentum markets, but in a market selloff this insurance should pay off in the form of better downside capture.

Volatility and variance are high right now as markets seek to price in several potential presidential election outcomes and gauge the pace of future rate cuts. We have said previously that monetary easing should act to stabilize equities as economic growth slows and the late-cycle expansion seeks its next catalyst. Whether growth reaccelerates or recession risk increases, we feel comfortable with our portfolio construction. If the former scenario occurs, our cyclical exposure should be beneficial while, in the latter, we have confidence that our stable and select names can generate above-market organic growth.

Portfolio Highlights

The ClearBridge All Cap Growth Strategy performed in line with its Russell 3000 Growth Index benchmark in the third quarter. 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 industrials and health care sectors while the consumer staples sector was the main detractor.

Relative to the benchmark, overall sector allocation contributed to performance while stock selection detracted. In particular, stock selection in the health care and communication services sectors, an overweight to industrials and an underweight to IT were the primary drivers of results. Conversely, stock selection in the IT, consumer discretionary and consumer staples sectors detracted from performance.

On an individual stock basis, the leading absolute contributors to performance were Meta Platforms, Apple, UnitedHealth Group, Broadcom and PayPal. The primary detractors were CrowdStrike, Pinterest, e.l.f. Beauty, ASML and Amazon.com.

In addition to the transactions mentioned above, we initiated a position in Tractor Supply in consumer discretionary and exited positions in Marsh & McLennan in financials, Stryker and Alcon in health care and Diageo in consumer staples.

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