ClearBridge
A Franklin Templeton Company

Large Cap Value ESG Strategy

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Key Takeaways

- During the fourth quarter, quality stocks across the market cap spectrum underperformed the broader market by the widest margin since the late 1990s, which was a headwind for the quality-focused Strategy.
- We believe the shifting market regime offers significant value opportunities, especially as overall market breadth improves and capital flows shift away from high-flying growth stocks toward overlooked, high-quality businesses.
- ClearBridge evaluates environmental and social shareholder proposals on a case-by-case basis, considering whether the ask from the proposal has merit and whether its wording diminishes or enhances shareholder value.

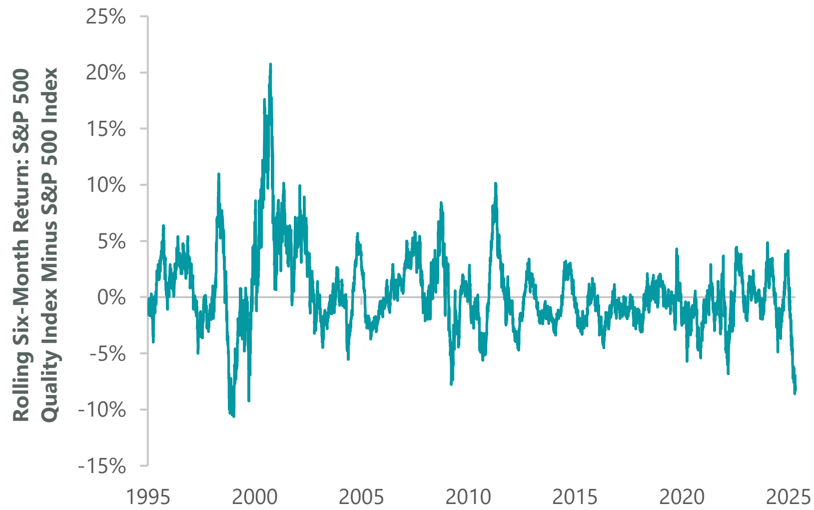
Market Overview

U.S. equites finished a strong 2025 albeit with more subdued gains in the fourth quarter, with the S&P 500 Index rising 2.7% during the period to end the year up 17.9%. Value stocks outpaced growth in the quarter across all market caps as the market pivoted from recent high-momentum AI winners and leadership broadened. The benchmark Russell 1000 Value Index gained 3.8% for the quarter, capping off a 15.9% return for 2025.

During the fourth quarter, quality stocks across the market cap spectrum underperformed the broader market by the widest margin since the late 1990s (Exhibit 1). This was a headwind to the Strategy, which trailed the Russell 1000 Value in the quarter as several high-quality long-term holdings sold off.

Within information technology (IT), long-term portfolio holding Motorola Solutions sold off as its revenue growth rate continued to normalize in its core land mobile radio (LMR) devices business; the company is working off an unusually high backlog created by COVID-era government funding programs. While its LMR devices business is slowing, we think the company has augmented its core franchise with faster-growing adjacencies and increased its mix of software and services. We think Motorola Solutions is a core holding for our strategy that offers attractive risk-reward at current valuation given a sustainable mid-single-digit top-line growth rate with continuously improving profit margins.

Exhibit 1: Quality Stocks' Underperformance at Extremes



As of Oct. 9, 2025. Source: ClearBridge Investments, Bloomberg Finance.

Our high-quality bias applies across the portfolio, including areas of AI. We are more exposed to higher-quality AI exposed stocks such as Broadcom, Taiwan Semiconductor Manufacturing and Microsoft, which lagged this year (although the first two were both up more than 40%) relative to lower-quality more commodity-exposed AI stocks like Micron, Sandisk and Lumentum. While these lower-quality companies are likely to benefit more from supply chain constraints in the near term, we believe that businesses with more sustainable moats are likely to deliver superior returns through the cycle for investors.

In materials, ongoing uncertainty regarding the economics of Air Products and Chemicals' mega projects in Saudi Arabia and Louisiana weighed on the stock through the year. While these projects are longer dated in nature, we believe the company's recent partnership with Yara to provide offtake for its blue ammonia in Louisiana is another point of evidence that the new management team is financially disciplined and focused on returning the business to its core strengths in industrial gases. We have long favored the traditional industrial gas business model, as it is durable during periods of economic weakness and has demonstrated strong pricing power, predictable results and resilient free cash flow.

Financials and health care names were beneficial for the Strategy in the quarter. Strength in consumer spending from the third quarter looked to carry over into the holiday season, helping Capital One and American Express. Capital One reported a large earnings beat driven by lower credit costs and a large reserve release helped by lower charge-offs. The quarter showed very strong operating results from Capital One in its first full quarter following its acquisition of Discovery. The icing on the cake was the announcement of a $16 billion buyback authorization (11%–12% of the market cap) following management's review of post-acquisition capital requirements. American Express also topped earnings estimates and raised the lower end of its guidance helped by strong spending and a bounce back in travel. Its refresh on its Platinum cards is also being well-received.

A fourth-quarter rotation to health care driven by a decline in policy uncertainty, improved earnings, attractive valuations and a pickup in M&A activity helped our holdings in the sector. Thermo Fisher Scientific, a supplier of life science tools and diagnostics, delivered strong earnings driven by its analytical instruments segment and strong operating margins. The company has also benefited from improving results in its growing bioprocessing business and raised revenue and EPS guidance. Consumer health company Haleon rose as it delivered solid results; the stock should continue to benefit from its strong brands in consumer health as it maintains its pricing discipline and gains market share.

Portfolio Positioning

During the quarter we added industrial gas company Linde, which traded down with its industry peers and materials more broadly on caution over the global macroeconomic backdrop. Linde is a durable and high-quality compounder that typically outperforms the market through cycles given its attractive industrial gas business, which offers strong pricing power through the cycle, exposure to non-economically sensitive long-term take or pay contracts, growing backlog of projects, and consistent execution.

At the same time, in the utilities sector, preference for WEC Energy, which has 80% of its assets exposed to some of the most constructive jurisdictions in the country (such as Wisconsin and areas covered by FERC) as well as upside to the data center demand, led us to add to our holding, funding the increase with a trim to Sempra and an exit of Edison International.

Outlook

Our core tenet is to invest in high-quality businesses with underappreciated, sustainable, durable edges, and we remain convinced that this is the path to superior returns through the cycle. In the current frothy market, however, this style has been under pressure. Thanks to our long duration, we see the recent selloff in high-quality businesses as a significant opportunity, and we have recently initiated or added to positions in several — such as Linde, Parker-Hannifin and WEC Energy — at attractive valuations. We believe the shifting market regime offers significant value opportunities, especially as overall market breadth improves and capital flows shift away from high-flying growth stocks toward overlooked, high-quality businesses.

Portfolio Highlights

The ClearBridge Large Cap Value ESG Strategy underperformed its Russell 1000 Value Index benchmark during the fourth quarter. On an absolute basis, the Strategy saw positive contributions from four of 11 sectors. The health care and financials sectors were the main contributors, while consumer discretionary and materials detracted the most.

On a relative basis, overall stock selection detracted from relative results, while sector allocation was positive. In particular, stock selection in the IT, industrials, materials, consumer discretionary and energy sectors detracted, while stock selection in financials, underweights to real estate and consumer staples and a health care overweight were beneficial.

On an individual stock basis, the top relative contributors were Thermo Fisher Scientific, Haleon, Parker-Hannifin, Danaher, and not owning Strategy (formerly known as MicroStrategy). Top relative detractors were Eaton, Air Products and Chemicals, Motorola Solutions, O'Reilly Automotive, and not owning Micron Technology.

ESG Highlights: The Evolving Proxy Landscape

Of the tools public equity investors can use to advocate for sustainable business practices, proxy voting is one of the more visible and powerful. It was vigorously debated in 2025. Throughout the year the SEC tightened parameters for shareholder proposals, strengthening the grounds on which they can be excluded from annual meetings.[1] It announced it would no longer "respond to no-action requests for, and express no views on, companies' intended reliance on any basis for exclusion of shareholder proposals under Rule 14a-8," with minimal exceptions.[2] The likely result will be to enable companies to exclude proposals without having to seek SEC approval, leading to fewer shareholder proposals making it to a vote.

Against this backdrop, the broad trends of the 2025 proxy season were a decline in environmental and social proposals and heightened scrutiny on governance issues. Major topics of environmental proposals filed included emissions disclosures and climate risk and plastic pollution. Social proposals, which were reduced in number, showed continued concern with workforce-related risks like pay equity, workplace safety, and diversity and inclusion. Like environmental proposals, social proposals received less support in 2025 than in previous years, although many of these proposals filed were perhaps "overly prescriptive, duplicative of existing disclosures, or insufficiently tailored to company-specific issues,"[3] a reminder that such proposals need to be judged on a case-by-case basis.

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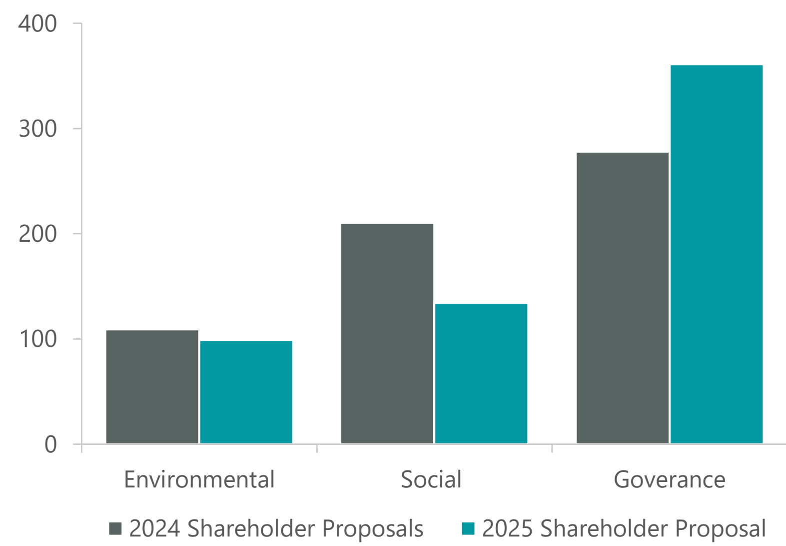
1 Staff Legal Bulletin No. 14M.

2 Statement Regarding the Division of Corporation Finance's Role in the Exchange Act Rule 14a-8 Process for the Current Proxy Season, Nov. 17, 2025. U.S. Securities and Exchange Commission.

3 "2025 Proxy Season Review: From Escalation to Recalibration," Harvard Law School Forum on Corporate Governance. Sept. 15, 2025.

Declines in environmental and social proposals and an increase in governance proposals (which received steady support, all told) were also reflected in ClearBridge's voting activity in 2025 (Exhibit 2).

Exhibit 2: Shareholder Proposals Voted on by ClearBridge



As of December 2025. Source: ClearBridge Investments.

The continued — and apparent increase in — relevance for governance topics reflects our view that good governance is a catalyst for value creation: board and chair independence reduces insular oversight; separating CEO and board chair roles reduces the potential for conflicts of interest; diversity on the board leads to more varied views and strengthens governance; board tenure should balance experience with innovation; linking compensation with sustainability factors could improve environmental stewardship and ensure the social license to operate. We have seen incremental improvements across many of these goals in recent years, and they remain worthy of supportive company dialogue.

Voting on a Case-by-Case Basis

Per ClearBridge's Proxy Voting Policy, we evaluate certain environmental and social proposals on a case-by-case basis. While we would generally be supportive of ESG proposals, we also consider whether the ask from the shareholder proposal has merit and whether the wording in the proposal diminishes or enhances shareholder value.

We also take note if a proposal does not seem to recognize substantial improvements by the issuer on the requests being addressed. This is an important element of ClearBridge's approach to proxy voting and our partnership approach to active ownership: we engage with CEOs, CFOs and other company leaders regularly about all factors that could materially affect value creation. This provides a valuable information component for assessing the merits of shareholder proposals.

Here we offer highlights of some recent ClearBridge votes and our thinking behind them.

Companies Are Making Sustainability Improvements

Amazon.com is a good example of a company that has made substantial improvements in areas where it nevertheless continues to see proposals: in 2025, for example, we examined a shareholder proposal asking the company to report on efforts to reduce plastic packaging. The company has received similar proposals for the past five years but has been making significant progress, addressing the resolutions of the proposals with improvements each year.

We chose not to support this proposal this year on the grounds that the company has already been reporting its plastic packaging reduction efforts and has quantified and published the improvements to the public each year. Such improvements include transitioning away from plastic in its outbound packaging and working with its vendors to let them ship in their own brand packaging via their Ships in Product Packaging (SIPP) program — reducing the use of an Amazon box on top of the product packaging. In addition, as of October 2024, Amazon has removed all plastic air pillows from delivery packaging used in its global fulfillment centers, which to date is the biggest decrease in plastic packaging in North America.

Moreover, through innovation and investment in technologies, processes and materials since 2015, Amazon has been able to reduce the weight of the packaging per shipment by 43% on average and avoided more than three million metric tons of packaging material. There are other achievements in packaging (both plastic and other materials) that the company has reported publicly.

Amazon is advancing partnerships and research to improve recycling infrastructure, engaging with organizations such as the Ellen MacArthur Foundation and The Recycling Partnership and demonstrating its efforts to align with industry peers, even if Amazon is not formally a signatory to the New Plastics Economy Global Commitment. We would still like to see Amazon publish an overall baseline of plastic used across its entire supply chain, to add to its robust reporting levels for outbound packaging practices.

Voting Requires Deep Knowledge of the Company

Our portfolio managers chose not to support a shareholder proposal asking Microsoft to report on the risks of its European Security Program (ESP) being used for censorship of free speech. We thought this proposal appeared to conflate a cybersecurity initiative with speech regulation and could mislead investors on the nature of the ESP. The company launched the ESP in response to the sharp rise in ransomware and cyberattacks involving espionage, data theft and disruption of democratic institutions.

Microsoft's ESP provides structured, limited-scope support to governments by sharing insights into these threats and aligns with Microsoft's Information Integrity Principles, which emphasize trusted information and freedom of expression rather than content moderation, surveillance or speech regulation. The company also participates in the Global Network Initiative (GNI), which independently evaluates its adherence to principles protecting privacy and free expression.

Executive Compensation Should Be Reasonable

We actively engaged UnitedHealth Group's Board of Directors over the course of 2025 about the appropriateness of the compensation for their executive team.

The company serially missed earnings expectations, resulting in underperformance relative to the S&P 500 Index by 20% in both 2023 and 2024. Further, UnitedHealth had a major cybersecurity incident that jeopardized payments throughout the U.S. health care system, and public sentiment toward the company was at historic lows. Despite poor results, United asked investors to support pay increases for the CEO and CFO, while withholding any bonus payment to the family of murdered executive Brian Thompson. We opposed the proposed pay scheme, as did 40% of voting investors, and we accordingly expressed our views to the board.

Following the proxy vote, UnitedHealth announced it would replace both the CEO and the CFO. UnitedHealth's board failed to hold either outgoing executive accountable for poor performance, and it allowed both of them to keep very significant unvested compensation. We again expressed our dissatisfaction to the board about its compensation decision.

Seeking to Enhance Shareholder Value

In voting proxies, we are guided by general fiduciary principles. Our goal is to act prudently, solely in the best interest of the beneficial owners of the accounts we manage. We attempt to provide for the consideration of all factors that could affect the value of the investment and will vote proxies in the manner that we believe are consistent with efforts to maximize shareholder values.

Among these factors would also be issuance of preferred shares. For example, the ClearBridge Emerging Markets Strategy portfolio managers considered a proposal at Localiza, a Brazilian car rental company, which held an out-of-cycle extraordinary general meeting to approve the creation of preferred stock.

Although the issuance of preferred stock adds complexity to common shareholders, the background here was telling: Brazil was to initiate a new dividend tax in January 2026 and companies were advancing dividends and bonus share issues to use up distributable reserves before the year end.

We judged that shareholder voting rights were being maintained and the company was attempting to issue bonus shares before the year-end tax increase. Ultimately, we agreed with management that the share issue was in the interest of shareholders and voted in favor of the proposal.

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