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Select Strategy

Key Takeaways

- ▶ The Strategy outperformed, drawing strength from the balance we have created through our pyramid portfolio construction across companies and sectors with distinct growth drivers.
- ▶ Our wide-ranging exposure in health care as well as AI-focused companies across IT and industrials enabled the Strategy to thrive despite the market's return to mega cap growth leadership.
- ▶ We believe more clarity on tariffs will open the logjam of capital, both in capital markets and that held by companies for future investment. A reopening of the IPO market is a positive sign, and we are looking at a number of new ideas among companies planning to go public.

Market Overview

U.S. equities rebounded strongly from tariff and geopolitical scares to deliver healthy gains in the second quarter. The S&P 500 Index returned 10.9%, swinging from a near bear market to an all-time high, while the benchmark Russell 3000 Index advanced 11.0% as risk-on sentiment took hold after tariff implementation was delayed. Growth stocks led across market caps, with the Russell 3000 Growth Index (+17.6%) outperforming its value counterpart by more than 1,300 basis points. The Russell 2500 Growth Index, home to many of the small and mid cap companies we target in the ClearBridge Select Strategy, rose 11.3% for the quarter, slightly outpacing the broader market but not enough to offset the significant underperformance in the first quarter.

The Strategy outperformed the benchmark for the period, drawing strength from the balance we have created through our pyramid portfolio construction across companies and sectors with distinct growth drivers. It's a testament to that balance that we were able to stay ahead of our large cap heavy benchmark in a return to AI-driven mega cap leadership and in a quarter where stock selection among our information technology (IT) and industrials holdings, the Strategy's two largest sector weights, were the main detractors from relative performance.

Our health care exposure was a particular standout in a quarter that saw the sector overall struggle due to tariff fears and challenges in the Medicare Advantage market. Insulet, a developer of insulin pumps for the treatment of diabetes, which was already seeing robust margin growth, is benefiting from Omnipod sales among the type 2 diabetes population, a market it received FDA approval for last

summer. HealthEquity, a provider of health savings accounts (HSA), saw its shares rise on better than expected quarterly revenue and raised full-year guidance driven by strong growth in HSAs and assets.

The Strategy also saw strong performance from Caris Life Sciences, an AI-driven company in cancer care and genetic profiling. We have owned the company for several years in the private investment area of the strategy. Caris went public late in the quarter and offers a differentiated molecular profiling services to biopharmaceutical companies using machine learning algorithms.

We did see good results from AI-ecosystem holdings in IT and industrials. Within IT, ServiceNow remains a leader among its software peers in the monetization of generative AI, with a target of \$1 billion in annual contract value from AI-related products by 2026. AppLovin delivered exceptional first-quarter results, highlighted by outsize product-led share gains with ad revenue growing 71% year over year driven by the AI-driven advertising algorithm provider's continued strength in gaming and rising traction in e-commerce.

Vertiv and Comfort Systems continue to benefit from the growing focus on AI and the underlying infrastructure investments required to support it. Vertiv delivers power and thermal management systems critical for data center operations, while Comfort Systems provides HVAC and electrical systems installation and maintenance. These names helped offset weakness across our more cyclical industrial positions that have yet to see a meaningful upturn in economic activity. Detractors included auto salvage company Copart, which fell sharply after its fiscal third-quarter revenue missed investor expectations for the first time in many quarters. Willscot and Trex, holdings tied to commercial and residential construction, also underperformed, as did LTL trucking provider Saia due to delays in recovery from a multiyear freight recession.

Within IT, weakness in SMID software companies HubSpot, whose latest results failed to beat high expectations by a significant amount amid slowing customer additions, and DocuSign, which failed to benefit from early renewals by customers, weighed on performance. The Strategy was also penalized by an underweight to Microsoft in a strong quarter for the cloud and early AI software adopter.

Portfolio Positioning

We initiated seven new positions in the quarter while exiting four others. Our largest purchase was Verisk Analytics, a data and software solutions provider to the insurance industry. Verisk's modern solutions are powerful and sticky, making them a must-have for major insurance companies. Through new products and raising prices, the company should continue growing high single digits and drive margins and free cash flow higher.

We exited Monolithic Power Systems in the IT sector, rolling the proceeds into newer semiconductor additions, Lattice Semiconductor

and Qorvo. Lattice makes programmable logic devices used in a wide range of applications including PC/servers, industrial, automotive and communications equipment. The volumes in most of its end markets have been depressed since the 2022 supply chain shock, but we believe declines have stabilized and volumes should start to grow late this year into 2026. Lattice is the best positioned company in the industry, taking share from other players through innovation, and its new CEO delivered remarkable returns for investors at a prior company owned in the Select portfolio.

Qorvo is a communications semiconductor company primarily selling into mobile phones, with heavy iPhone exposure, and defense devices. The stock, which we view as an evolving opportunity, has been depressed as sales of iPhones have been disappointing, and the current management team has made poor capital allocation decisions. We believe new shareholders who have obtained board seats will improve operation, capital allocation and pursue strategic activity to unlock value, while we wait for future iPhone upgrade cycles.

In health care, Sartorius is a premier manufacturer of consumable products and services used in the development of biopharmaceutical production such as cell culture media, bioreactors and systems for separation, purification and concentration of biological products. This area has grown rapidly with the increase in new biologics and cell and gene therapies. Post-COVID, sales slowed due to excess inventory built up in the system. That has been worked down over the last three years and growth is reaccelerating, which should propel the multiple higher.

Penumbra is a name we are familiar with from owning across other portfolios at ClearBridge. The company's products use an aspirator to remove clots from the brain, heart, lungs and peripheral circulation. With this new innovation quickly becoming a best-in-class approach among physicians, Penumbra is continuing to develop new products to serve this large and growing market, and we anticipate a major product release later this year.

The Portfolio sold Chinese e-commerce and payment platform Alibaba Group after its stock price rose rapidly incorporating new enthusiasm for its AI-cloud offerings. We also exited Fox Factory, which makes components that go into high-priced trucks and bicycles, due to concerns over tariffs and large ticket consumer purchase activity.

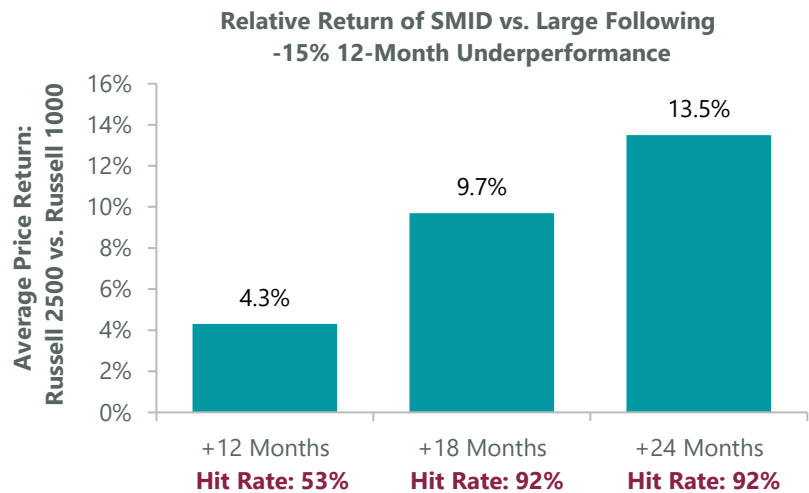
Mindful of the ongoing risks and position sizes, we trimmed disruptors AppLovin in IT and MercadoLibre in consumer discretionary following strong recent performance.

Outlook

The market's rally off the early April lows on improving trade sentiment validates our view that the solution to the global tariff problem rests in the hands of the President, whose stance can quickly be reversed. Similarly, much lower rates are not needed for a

broadening of performance in equity markets; rates just need to gradually move to a normal level with lower levels of volatility, and business activity needs more clarity on tariffs. Large cap stocks have continued to outperform smaller caps, with the rolling 10-year annualized return gap the largest on record dating back to the 1930s, and relative valuations in the bottom decile. SMID stocks have historically recovered following such periods of sizeable underperformance versus large cap stocks (Exhibit 1).

Exhibit 1: SMID-Cap Snapback



Russell 2500, Russell 1000, reflective of period from 1979 – present, as of June 30, 2025.
Sources: FactSet, Russell.

Economic data points like a tariff-induced contraction in first-quarter GDP, range-bound inflation and job growth without wage spikes suggest the Fed is likely to move forward with rate cuts in the second half of the year. What is needed is more clarity on tariffs, which would open the logjam of capital, both in capital markets and that held by companies for future investment. We are starting to see a reopening of the IPO market and are looking at a number of new ideas among companies planning to go public, as well as late-stage high-growth innovators.

We expect the macro backdrop to remain bumpy but have positioned the portfolio to perform well in a variety of market and economic scenarios. With a balanced approach, we own stocks with organic growth drivers and strong management teams that have the proven ability to execute regardless of macro conditions. Unlike certain “style-pure” peers, we have the flexibility to own companies over long periods of time and through business cycles as they compound cash flows significantly and grow from emerging disruptors into larger and steadier compounders. The portfolio features a number of examples of this from Monster Beverage in consumer staples to Shopify in e-commerce and Fortinet in information security.

Portfolio Highlights

The ClearBridge Select Strategy outperformed its Russell 3000 Index benchmark during the second quarter. On an absolute basis, the Strategy saw contributions across eight of the 10 sectors in which it was invested. The main contributor was the IT sector while primary detractor was the energy sector.

Relative to the benchmark, overall sector allocation contributed to performance. In particular, an overweight to IT, an underweight to financials and stock selection in the health care, consumer staples, financials and real estate sectors aided results. Conversely, stock selection in IT and industrials and an underweight to communication services detracted from performance.

On an individual stock basis, the primary relative contributors were MercadoLibre, ServiceNow, Vertiv, Comfort Systems and AppLovin. The leading detractors were positions in Copart, Microsoft, Baker Hughes, Waste Connections and ICON.

In addition to the transactions mentioned above, we added positions in Chime Financial in financials and Medpace Holdings in health care. We also sold Workday in IT.

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