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Large Cap Growth Strategy

Key Takeaways

- ▶ The Strategy meaningfully underperformed the Russell 1000 Growth Index through one of the most powerful rallies in its history, with underweights to mega cap AI beneficiaries as well as lower-quality AI-related names the largest headwinds. Stock selection in health care also weighed on performance.
- ▶ We acknowledge the need be more proactive and move quickly when a secular theme like AI takes hold. However, we do not believe the current momentum-oriented growth market can sustain itself without interruption, and our priority is positioning the portfolio so sentiment shifts do not impede long-term results.
- ▶ We believe resurgent growth in the economy ex-tech from fiscal stimulus and easing monetary policy will lead to broadening participation within our benchmark. In particular, we are targeting opportunities in health care and short-cycle industrials.

Market Overview

Large cap growth stocks maintained market leadership in 2025 as accelerating spending and enthusiasm related to generative artificial intelligence (Gen AI) and continued strong earnings growth from mega cap companies enabled the benchmark Russell 1000 Growth Index to finish up 18.6%. The technology-heavy NASDAQ Composite rose 20.4% for the year while the S&P 500 Index advanced 17.9%.

After outperforming in a negative first quarter, the ClearBridge Large Cap Growth Strategy trailed the benchmark's powerful 53.9% rally from the post Liberation Day lows in early April through late October. It continued to lose ground through the rest of the fourth quarter, underperforming the benchmark's 1.2% quarterly advance by about 170 basis points (gross of fees). In aggregate, the Strategy underperformed the Russell 1000 Growth Index (RLG) by approximately 900 bps for the year.

Over the history of the index, the RLG's recent rally has only been topped by rebounds from the COVID-19 and Global Financial Crisis in 2020 and 2009, respectively, as well as the run-up to the dot-com bubble in 1999 (Exhibit 1). What surprised us most about this year's surge was the pace of capex increases by cloud hyperscalers, the sudden emergence of privately held OpenAI and Anthropic as sources of billions of dollars in AI spending and the move by Alphabet to start selling custom AI chips to its competitors.

Exhibit 1: Best Six Month Returns for Russell 1000 Growth Index

Year	Russell 1000 Growth Index Returns (%)
2020	62.80
1999	52.20
2009	49.66
2025	47.24
2000	38.53
1997	33.27
2023	31.70
2012	31.64
2019	31.16
2011	31.04

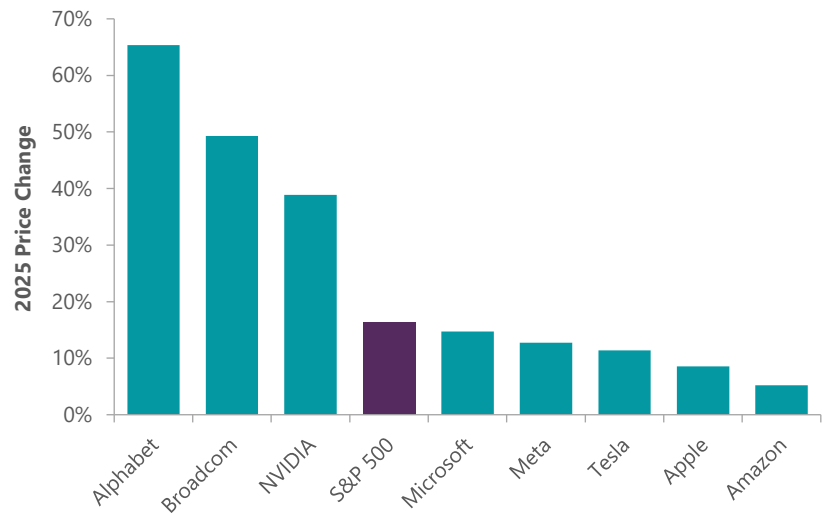
Performance reflects maximum 6-month return of Russell 1000 Growth Index within each year.
Source: FactSet.

Performance Headwinds

The majority of the Strategy's 2025 underperformance — roughly 500 bps — can be attributed to our differentiated AI and mega cap positioning compared to the benchmark (with poor stock selection in health care the second-largest detractor). We were right on Nvidia, a stock we first purchased in 2018 and that has been one of the top portfolio holdings for the last several years. Additionally, we knew an AI revolution was developing, but we underestimated the magnitude of the AI spending growth we witnessed in 2025. We also misjudged the extent to which the market would discount the demise of application software companies in an AI world. Fast moving markets are a challenge for a low-turnover portfolio, although we were quite active from Liberation Day on in seeking to upgrade our AI participation through the purchases of Broadcom, Marvell Technology, Datadog and Oracle, as well as exits from names where we had less confidence in long-term earnings power including Accenture and application software makers Workday and Adobe.

In hindsight, we did not scale up our positions in Broadcom and Alphabet enough. Broadcom shares rose more than 40% for the year but the maker of custom silicon chips for AI workloads was one of the Strategy's largest relative detractors due to our roughly 300 bps underweight. We had been consistently adding to Alphabet since repurchasing the stock in April 2024, as it had been trading at a sub-market multiple, but regret not increasing our exposure more aggressively after the DOJ antitrust case concluded with less onerous penalties than feared. The company's success with its Google Gemini chatbot and TPU chips for AI workloads boosted its shares more than 60% for 2025, causing our ~350 bps underweight to create a significant performance drag.

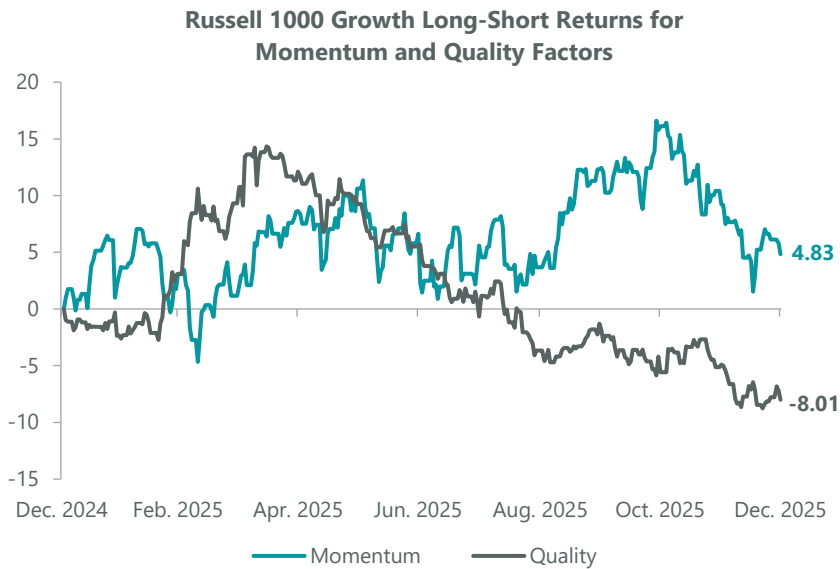
Exhibit 2: Divergence Emerging Among Mega Caps



Data as of Dec. 31, 2025. Sources: FactSet, S&P.

Much of the broadening within IT has occurred among more speculative names in contrast to our buckets approach to portfolio construction, which limits our exposure to this group of holdings. For example, not owning AI operating system software maker Palantir Technologies was a headwind but, at current levels, we think very aggressive future growth assumptions are already factored into the valuation. In fact, we have seen wide dispersion between momentum stocks and quality stocks in 2025, particularly in the second half of the year (Exhibit 3). Our relative overweight to quality and relative underweight to momentum factors negatively affected results.

Exhibit 3: Momentum Stocks Have Dominated Since Liberation Day



As of Dec. 31, 2025. Source: Bloomberg. Momentum performance is FTW RLG Index Momentum Long-Short (High-Low) Total Return; Quality performance is FTW RLG Index Quality Long-Short (High-Low) Total Return.

Meanwhile, the Strategy's more diversified exposure to AI through ownership of Eaton, Accenture and Equinix did not add significant value in 2025. Eaton, a manufacturer of electrical components critical to the operation of data centers, has had supply constraints that limit its ability to vastly exceed its targeted growth rate which may also limit its ability to garner price increases. Accenture, an IT consultant helping enterprise customers deploy AI technologies, was hurt by its association with application software makers and its outsourcing business was deemed at risk of being disintermediated by sophisticated large language models (LLMs). We exited our position in Accenture in the third quarter as part of our AI repositioning. Data center operator Equinix should benefit from the growing importance of sharing data across clouds, but the returns on a large capital spending project will delay revenue growth acceleration until 2027. We view the company as a later stage AI beneficiary, especially if all the current spending begins to produce a positive return on investment.

The performance of our health care holdings was another disappointment. UnitedHealth Group, a consistent contributor in the portfolio's stable bucket for more than a decade, suffered from a combination of negative sentiment and severe mismanagement that caused the stock to lose about half its value in 2025 by the time we exited the position in August. While we had been trimming UnitedHealth consistently since the fourth quarter of 2024, we also believed the company deserved some leeway to turn things around given its long-term track record. In hindsight, UnitedHealth disclosure had always been below average due to the nature of its regulated businesses, as well as the size and scope of the company's operations, but that lack of disclosure also made it hard to assess the execution issues that the company faced in 2025. Ultimately, despite a decade of solid returns, we lost confidence in UnitedHealth's ability to navigate a turnaround under new leadership and exited the position.

We were too early in exiting pharmaceutical maker Eli Lilly, which we sold in July at what we viewed as fair value and due to uncertainty over reimbursements for GLP-1 treatments for diabetes and obesity and the continued prevalence of lower-priced competition. Since then, the U.S. government has struck a deal with Lilly to offer GLP-1s to Medicare and Medicaid patients, opening up millions of additional prescriptions, while readouts on the company's oral GLP-1 treatment indicated a broader market than we had expected. Lilly shares surged in the fourth quarter, causing our lack of exposure to be a drag on relative results.

As with technology, we repositioned our health care exposure with the proceeds of these sales throughout the year by purchasing high-quality biotechnology company Vertex Pharmaceuticals, a leading contributor in the fourth quarter, while adding to our positions in Thermo Fisher Scientific and Intuitive Surgical.

Portfolio Positioning

After a flurry of activity post Liberation Day, our portfolio actions in the quarter were more limited. We closed a position in Starbucks to concentrate our exposure in restaurants into Chipotle Mexican Grill. While we still believe in the turnaround story at Starbucks under CEO Brian Niccol, improvements are taking longer than expected to accelerate the business. Both Starbucks and Chipotle are being impacted by macro headwinds in the restaurant sector due to a challenged low-income consumer; however, we believe Chipotle has faster long-term store growth potential and better unit economics, and we feel more comfortable in Chipotle's price versus value provided to consumers.

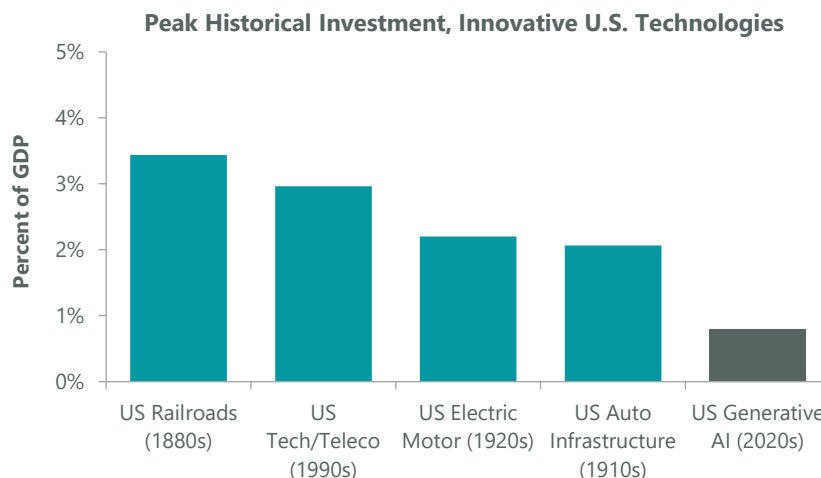
We initiated a position in Arista Networks, a provider of high-speed switches and networking equipment critical to enabling the operation of cloud platforms and data centers. Arista is well-represented among the hyperscalers and benefits from that capex cycle. In the enterprise business, Arista currently has low share but is poised to continue gaining as companies update their campus networking infrastructure.

We will continue to be active in adding to positions or initiating new ones during pullbacks, such as we did with Palo Alto Networks following its announcement of the Cyber Ark acquisition and Netflix when the stock sold off following disclosure of its intent to purchase Warner Bros. Discovery.

Outlook

While AI capex has exceeded expectations thus far, we are still very early in the technology's development.

Exhibit 4: More AI Capex Ahead



Data as of Oct. 20, 2025; latest available as of Dec. 31, 2025.

Source: Bureau of Economic Analysis, Goldman Sachs Global Investment Research.

We see AI as the most transformative technology of our investment careers but, as with past innovations, there will be changes in perceived winners and losers as new LLMs are released, semiconductor innovation evolves and as monetization models become clearer. The growth market right now is momentum oriented and sentiment driven, with the latest data point from an AI bellwether determining near-term direction — similar to what we experienced in 2021. This is not a durable environment, and our challenge is positioning the portfolio so that sentiment shifts do not impede multiyear performance.

This backdrop causes us to be thoughtful in analyzing the potential long-term AI winners and opportunistic in taking advantage of the market volatility that comes with a secular growth trend as it evolves, while remaining cognizant of the downside risks inherent in such emerging trends. Oracle is an example of this volatility. The shares jumped over 30% after our purchase in July but are down 40% from their peak as investors question how soon AI capex will lead to revenue and profitability. While Oracle is a highly levered company, it generates free cash flow and has a large backlog of signed contracts. While there is uncertainty and execution risk with a spending ramp of the size and scale that the company has announced, the market is currently attributing very little value to Oracle being successful in its cloud business.

One of the lessons we have learned this year is the importance of being proactive and moving quickly when a secular theme takes hold. In addition to targeting new ideas at advantageous valuations, we are constantly revisiting the case for owning every holding, moving away from companies with lower visibility and subpar execution and reprioritizing our highest-conviction names. We are currently vetting several ideas in health care and seeing signs of improving activity in areas like short-cycle industrials. These exposures could prove beneficial should growth and earnings revisions in technology-related sectors become more normalized compared to the rest of the market. If not a leadership change from the mega cap names that have dominated RLG performance for the last three years, resurgent growth in the economy ex-tech in 2026 from fiscal stimulus and easing monetary policy would at least support broadening participation within our growth universe.

Portfolio Highlights

The ClearBridge Large Cap Growth Strategy underperformed its Russell 1000 Growth Index benchmark in the fourth quarter. On an absolute basis, the Strategy delivered positive contributions across three of the nine sectors in which it was invested (out of 11 sectors total). The primary contributors to performance were the health care and consumer discretionary sectors while the IT 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 and IT sectors hurt performance. On the positive side, stock selection in the consumer discretionary and consumer staples sectors contributed to performance.

On an individual stock basis, the primary detractors from relative performance for the quarter included Netflix, Eaton, underweights to Alphabet and Apple as well as not holding Eli Lilly. The leading contributors to relative returns were Intuitive Surgical, Thermo Fisher Scientific, ASML, Vertex Pharmaceuticals and an underweight to Microsoft.

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