FRANKLIN TEMPLETON | ClearBridge

Global Value Improvers Strategy

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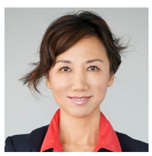

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Key Takeaways

- Global equities rebounded sharply in the second quarter, led by renewed enthusiasm for AI infrastructure, resilient earnings and easing geopolitical stress.
- The Strategy outperformed its benchmark, as strong stock selection in industrials, health care and consumer discretionary more than offset lesser exposure to the quarter's exceptional rally in IT hardware and semiconductors.
- We continue to see durable opportunities across energy security, AI infrastructure, grid modernization and industrial capex, while emphasizing valuation discipline, cash flow durability and balance sheet strength.

Market Overview

Global equities recovered strongly in the second quarter as investors looked through volatility following March's escalation of the U.S.-Iran conflict and refocused on resilient corporate earnings, improving growth expectations and the durability of the AI capital spending cycle. The MSCI World Growth Index returned 18.9%, ahead of the 13.8% gain for the MSCI World Index and the 9.2% return for the MSCI World Value Index. Growth's strong quarter helped it recover from first-quarter weakness; however, value stocks continued to outperform year to date.

Performance was positive across developed markets. Japan remained supported by improving corporate fundamentals, governance reform, exporter strength and a steeper yield curve, while AI demand benefited selected industrial, electronics and automation companies. In Asia, AI supply chain strength and signs of stabilization in China supported sentiment, though consumer demand remained uneven. Continental Europe advanced as Middle East de-escalation, resilient economic sentiment and infrastructure and electrification demand offset still-uneven growth. The U.K. lagged other developed regions, reflecting its defensive index composition, commodity sensitivity and softer domestic growth, while the U.S. contributed to gains as AI-related earnings and capital spending expectations remained supportive.

Energy was a major swing factor: easing geopolitical tensions and the announcement of U.S.-Iran negotiations led to lower oil prices in June, easing some inflation concerns. Even so, central banks remained cautious, with the Federal Reserve and the Bank of England holding rates steady while the ECB and the Bank of Japan tightened policy, reinforcing a higher-for-longer global rate backdrop that we believe favors valuation discipline, cash flow durability and balance sheet strength.

We expect these trends to create durable opportunities across energy production, infrastructure, power management and efficiency.

Portfolio Performance

The ClearBridge Global Value Improvers Strategy outperformed its MSCI World Value Index benchmark in the second quarter. The portfolio participated in the market rebound, supported by strong stock selection across industrials, health care and consumer discretionary, while avoiding weakness in select benchmark constituents also helped. These effects more than offset lesser exposure to the quarter's exceptional rally in information technology (IT) hardware and semiconductors and weakness in energy.

Industrials provided the largest source of relative strength. Vertiv continued to benefit from the buildout of data center and AI infrastructure, which is driving sustained demand for power and cooling solutions, while French power cable manufacturer Nexans advanced on continued demand tied to grid infrastructure, electrification and energy transition projects, as well as the announced Republic Wire acquisition that expands its footprint in the U.S. market. Fortune Brands Innovations also contributed as shares rebounded amid expectations for improved operational execution after the appointment of a new CEO.

Health care represented another area of strong stock selection. Diversified health care company CVS Health rose as stronger first-quarter earnings, raised full-year guidance and better performance in its health benefits business supported confidence in the company's turnaround, while reduced policy uncertainty around exchange subsidies also helped. German pharmaceutical and life sciences company Merck KGaA also benefited from positive earnings results, as its life sciences division emerged strongly from several years of destocking and its electronics division benefited from increased semiconductor demand.

Consumer discretionary also contributed to relative performance, led by food services company Compass Group, as strong first-half results, continued new business momentum and a raised full-year profit outlook supported investor sentiment.

The sharpest sector-level offset came from IT. Microchip Technology was one of the Strategy's strongest holdings, rising alongside greater demand for analog semiconductors tied to AI infrastructure, automotive and industrial applications. However, the Strategy's underweight exposure — and specifically to the exceptional rally in IT hardware and semiconductor stocks — left it unable to keep pace with a benchmark sector that rose by over 50% during the quarter.

Energy weighed on relative results. TotalEnergies and EQT both came under pressure as easing geopolitical tensions in the Middle East and the announcement of negotiations between the U.S. and Iran resulted in a pullback in oil and natural gas prices, pressuring upstream energy producers. For integrated energy companies such as TotalEnergies, the move reduced near-term cash flow support, while for natural gas producer EQT it weighed on sentiment toward commodity-sensitive earnings.

Regionally, Europe Ex U.K. was the largest contributor to relative performance, led by Germany-based industrial technology manufacturer Siemens AG, which advanced on strong order growth, resilient revenue and confirmation of its full-year outlook, while Spanish bank Banco Bilbao Vizcaya Argentaria (BBVA) continued to benefit from improving sentiment. Japan was the largest regional detractor, driven by weakness in Hitachi and our lack of exposure to semiconductor and electronics names that surged in the quarter.

Portfolio Positioning

We repositioned within the industrials sector this quarter, identifying unique opportunities to diversify end market exposure beyond direct AI beneficiaries to those with broader cyclical reach.

We initiated a position in China's Contemporary Amperex Technology (CATL), a global leader in power battery storage products and services. We believe that with its unmatched manufacturing scale and continued innovation driven by forward-looking R&D, CATL can continue to benefit as EV penetration increases and batteries see rising demand from global grid modernization efforts and data center applications. We also initiated a position in Japanese pneumatic equipment manufacturer SMC. We believe SMC is a higher-quality industrial automation business with a strong market position, and that current valuations reflect trough conditions following a prolonged industry downturn. A recovery in demand and lower capital intensity should support improved margins and cash flow over time.

We exited Bureau Veritas in the industrials sector, as execution challenges left the business less resilient to macro pressures than we had expected, while the growth of AI raises additional concerns about revenue models dependent on billable headcount.

Outlook

While macro and geopolitical uncertainty remains elevated, the second quarter reinforced our confidence in several structural themes underpinning our investment approach. Energy security and independence remain multi-decade investment priorities, while AI infrastructure, grid modernization, reshoring and long-overdue infrastructure upgrades continue to support an improving industrial capex cycle. We expect these trends to create durable opportunities across energy production, infrastructure, power management and efficiency, many of which are already represented in the portfolio.

At the same time, given the current degree of market concentration and elevated valuations, maintaining portfolio diversification and finding stocks with adequate margin of safety is paramount. For example, looking outside the narrow set of AI hardware and energy transition beneficiaries that the market is maniacally focused on, we believe many franchise leaders in the out-of-favor sectors such as consumer and health care are trading at very attractive valuations. As interest rates remain higher for longer and macro conditions remain fluid, we believe investors will increasingly appreciate the cash flow durability and balance sheet strength of these businesses. Ultimately, the goal remains to build a portfolio of high-quality businesses with improving fundamentals driven by diversified set of long-term secular themes.

Portfolio Highlights

The ClearBridge Global Value Improvers Strategy outperformed its MSCI World Value Index benchmark during the second quarter. On an absolute basis, the Strategy had gains across eight of the 10 sectors in which it was invested (out of 11 sectors total), with the industrials sector the greatest contributor and the energy sector the largest detractor.

On a relative basis, overall stock selection contributed to performance, but was partially offset by negative sector allocation effects. Stock selection in the industrials, health care, communication services, consumer discretionary, materials and consumer staples sectors, as well as underweights to the consumer staples and consumer discretionary sectors, proved beneficial. Conversely, an underweight and stock selection in the IT sector, stock selection in the financials, utilities and energy sectors and an overweight to the utilities sector weighed on performance.

On a regional basis, stock selection in Europe Ex U.K., the U.K. and North America contributed positively. Stock selection in Japan and an overweight to the U.K. detracted.

On an individual stock basis, CVS Health, Siemens AG, Microchip Technology, BBVA and not owning Microsoft were the greatest contributors to relative performance. The largest relative detractors were TotalEnergies, EQT, Wells Fargo and not owning Micron Technology and Intel.

ESG Highlights: Social Media Under Scrutiny

Social media companies are coming under increasing pressure from state attorneys general, school districts and parents arguing platforms such as Meta Platforms' Facebook and Instagram, Snapchat, TikTok and Alphabet-owned YouTube knowingly designed features that are addictive to young users and failed to adequately warn about mental health risks.

The success of recent lawsuits in California and New Mexico against Meta and YouTube could be impactful for social media broadly, raising regulatory and financial risk and creating the potential for reputational damage.

In New Mexico, a jury awarded $375 million in civil penalties against Meta for misleading the public about predator exploitation on its platforms in violation of state consumer protection law.

Not long after, a jury in Los Angeles became the first to hold social media companies responsible for contributing to a plaintiff's mental health harm via addictive design. The jury determined that Meta and YouTube were liable for negligence and failure to warn related to the plaintiff's alleged social media addiction. The plaintiff was awarded $6 million in damages.

These lawsuits are notable for not seeking action against the content featured on the platforms — for years, such attempts were unsuccessful, largely due to Section 230 of the Communications Decency Act, which protects social media companies from liability related to content posted by their users. Instead, the lawsuits attempt to find fault in the design of the products.

They also follow several milestone national regulations around the world that have involved restrictions on youth access to social media (Exhibit 1). Several U.S. states — such as Utah, Arkansas, Louisiana, Florida, Georgia, Tennessee and Nebraska — have also passed laws restricting minors' use of social media, although many of these are currently being challenged in court.

Exhibit 1: National Restrictions on Youth Access to Social Media

2023	France	Prohibits most social media accounts for children under 14 and parental consent for ages 14-15
2024	Australia	First country to enact nationwide min. age of 16 for social media
2025	Australia	Under 16 ban enters into force
2025	Malaysia	Establishes nationwide min. age of 16 for social media
2025	Portugal	Establishes nationwide min. age of 16 for social media

As of June 30, 2026. Source: ClearBridge Investments.

Social Media Platforms and Active Ownership

ClearBridge owns both Meta and Alphabet in several portfolios, and we are cognizant of the risks to both society from social media and the companies via potential liability. Against this backdrop, we recently engaged with Meta to discuss youth safety. In our conversation in May, we sought to test the real-world effectiveness, credibility and trade-offs of Meta's youth safety efforts, while probing regulatory risk, reputational risk with financial penalties and competitive positioning.

Meta shared that it believes its youth safety measures such as AI-based age verification, content moderation and privacy and parental controls are best-in-class, although this could be challenged. The company also shared that it supports youth safety regulation; its requests for regulation would be for no outright bans, consistency across geographies and equal application to all social media companies.

Meta noted that its Teen Accounts enable the above safety measures by default, it employs AI to screen account content for signs that a user may have lied about his or her age and it automatically age gates as appropriate. In aggregate, these features have led to a "marked improvement" in compliance and outcomes, according to the company. In response to critics that claim these features still let through inappropriate content, the company believes these instances of algorithm failure are exceptions rather than the norm.

We advised the company to disclose the data supporting its claims that its youth initiatives are working and leading to "marked improvement," as it did not provide any during the meeting. Further, we shared our preference that, to lend greater credibility to the claims, this data should be audited by a third party.

ClearBridge's approach focuses on the companies' risk management regardless of the source of risk.

We also explained our difficulty in locating information on these issues on Meta's websites. We noted that information difficult to find for professional investors would likely be even more challenging for everyday users — parents, for example — to locate and to inform their decisions to use the platform. We asked the company to consolidate all its statements on this subject in a single place — rather than spread it out across several different websites — to make it easier for various stakeholders to find and evaluate, similar to what the company does for its environmental disclosures. Meta was receptive to our input.

In June a trust and safety company that helps platforms and AI developers detect and prevent harmful online behavior and unsafe AI outputs published a study in cooperation with Meta that used Meta's content standards to compare the Teen Accounts content experience on Instagram versus a competitor platform. Testing was conducted from mid-December 2025 to mid-January 2026 and found that the safeguards applied to Teen Accounts on Instagram performed better than a competitor platform across several dimensions. While the period may seem short for such a study, Meta has disclosed that Teen Accounts are in the hundreds of millions; as users access the apps multiple times a day, this would aggregate to a statistically significant sample, although ideally the company could disclose time series data showing content moderation improvement over a longer horizon. Also in June, Meta rolled out its Teen Accounts protections globally to all apps as well as parental alert notices for inappropriate content searches by teens.

Conclusion

Content responsibility remains a key component in assessing social media platforms such as those operated by Meta and Alphabet. ClearBridge's approach stresses several components of this topic: rigorous content moderation can potentially limit harmful or illegal content while seeking to maintain platform integrity, and child safety raises questions of regulatory and reputational risk.

Over the years of ClearBridge's ownership with Meta and Alphabet, we have witnessed both companies improving their content responsibility (Exhibit 2). Meta has made progress on its content policy by appointing an independent content oversight board and then growing its scope. After historically having some issues around brand safety and protecting children from sensitive content, YouTube has made significant progress in this area through staffing, technology and policy development. In 2021, YouTube became the first digital platform to receive accreditation for content-level brand safety from the Media Rating Council (MRC), following an independent audit of its content moderation, monetization and ad placement systems.

At the same time, recent litigation with social media suggests the risk profile for these companies is evolving; regulatory risk is shifting from content moderation to product design. ClearBridge's approach focuses on the companies' risk management regardless of the source of risk. As our engagement with Meta shows, we also focus on transparency, as investors need evidence that youth safety initiatives are working in practice, not only descriptions of policies or tools.

Exhibit 2: Content Responsibility Improvement Timeline

Year	Meta	Alphabet
2018	Announces Oversight Board	Expands AI moderation investments
2020	Oversight Board established	COVID-19 misinformation policies
2021	Oversight Board begins issuing decisions	First MRC content-level brand safety accreditation
2022	Updated Community Standards enforcement, explanation and review	Enhanced election misinformation measures
2023	AI content labeling initiatives launched	Generative AI safety commitments
2024–2025	Expanded AI-generated content policies	Gemini AI safeguards and synthetic media labeling

Source: ClearBridge Investments.

Social media is a fast-moving topic involving billions of participants — Meta reports 3.5 billion daily active users, while Alphabet reports over 2 billion signed-in monthly users for YouTube. We continue to educate ourselves on the sustainability factors affecting this industry as we monitor the evolution of litigation and the broader social media bans; we will continue to actively incorporate this analysis into our investment process and stewardship activity.

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