

# Franklin Biotechnology Discovery Fund

Advisor Class: FTDZX Class A: FBDIX

Commentary | as of March 31, 2025

## Key Takeaways

- **Markets:** After starting 2025 on a strong note, global equities collectively declined during the rest of the first quarter (1Q25) due to investor concerns about US economic growth, President Donald Trump's trade policy and a broadening trade war. Despite the overall weakness, eight out of 11 global equity sectors still managed to advance, including a fifth-place finish for health care. The sector's better-than-average result was driven by several key factors, including (1) interesting valuations after underperforming in 2024; (2) continued advancements in medical technology and new drug approvals; and (3) strong fourth-quarter 2024 earnings reports from major health care companies.
- **Detractors:** Stock selection in the biotechnology industry and a small, off-benchmark exposure to the managed health care industry.
- **Contributors:** An overweight in the health care services industry, positioning in the pharmaceuticals industry, and stock selection and an underweight in the life sciences tools and services industry.
- **Outlook:** We are carefully monitoring emerging 2025 risks related to global tariffs, health care regulation and US Food & Drug Administration (FDA) staffing. We also remain cognizant of risks to biopharma innovation and stock performance linked to persistent inflation and the potential for only minimal interest-rate cuts in the United States in 2025.

## Performance Review

- Most of the fund's performance gap versus the benchmark NASDAQ Biotechnology Index was due to unfavorable stock selection in the biotechnology industry, which comprised 82.28% of the portfolio at March-end. Overweighted or off-index positions in Vaxcyte, UniQure, Praxis Precision Medicines, Day One Biopharmaceuticals, Jasper Therapeutics, Crinetics Pharmaceuticals, Dyne Therapeutics and several other biotech detractors sold off sharply and saw their equity values reduced by more than 30%, which in most cases was due to clinical trial setbacks.
- In general, the new US administration's unconventional appointments to key health care posts raised concerns about the direction of US biotech regulation. This uncertainty generally soured investor sentiment toward US-based biotech companies. The persistently high interest-rate environment in the United States has also been a disadvantage for domestic biotech companies, which typically have long drug development cycles. This has made it more challenging to secure funding and maintain profitability. The complex impact of the Inflation Reduction Act on drug pricing has added to the uncertainty. Global market dynamics were also at play: non-US biotech companies, particularly those in Europe and Asia, have benefited from more stable regulatory environments and favorable or improving economic conditions. Additionally, these regions have seen significant private and public funding rounds, which have bolstered investor confidence.
- Although pharmaceuticals holdings (11.15% of the portfolio at March-end) added to both relative and absolute returns, there were several detractors that shed considerable value, including off-index Contineum Therapeutics, which faced delays in its Phase 2 trial for PIPE-307, a treatment for relapsing-remitting multiple sclerosis.
- Among contributors, pharmaceuticals industry results were driven by a stellar gain for Intra-Cellular Therapies (not held at quarter-end) and a rally in Eli Lilly (not an index component). Johnson & Johnson (not a fund holding) agreed to acquire all outstanding shares of Intra-Cellular for \$132 per share in cash, totaling about \$14.6 billion.
- In biotech, the aforementioned relative-return setbacks were diminished by a host of notable contributors that included robust rallies in Ascendis Pharma, PTC Therapeutics and Mineralys Therapeutics (all overweighted). The fund was also aided by a lighter-than-index exposure to Regeneron Pharmaceuticals as its share price declined, and our avoidance of several index component companies that sold off.
- In the health care services industry, an overweighted investment in Guardant Health appreciated solidly. Guardant, which is seeing exceptional demand for its products, focuses on cancer treatment through advanced diagnostics. Elsewhere in the portfolio, relative returns in the life sciences tools and services industry were aided foremost by our limited exposure to Illumina's steep selloff as we liquidated the position ahead of the worst of it.

## Outlook

- Recent developments related to FDA staffing and global tariffs add to near-term uncertainty. We are closely monitoring the impact of recent senior departures at the FDA, as well as the agency's larger workforce reductions. Individual company exposure to tariffs will depend on whether the fees are paid on active pharmaceutical ingredients (mostly imported) or finished goods (as a lot of the final product manufacturing facilities are in the United States). We are also focused on transfer pricing and taxation, direct-to-consumer advertising, and most-favored nation pricing as these appear to be additional focal points for the Trump administration. Companies with existing commercial drug franchises tend to have less exposure to FDA risks, on average, but they also have higher exposure to tariff uncertainties at this time.
- Health care sector merger-and-acquisition (M&A) activity is more or less on hold these days as businesses work through a period of heightened uncertainty tied to the FDA and tariffs. However, as clarity on regulations and trade policy returns, we think M&A could switch back to a market tailwind as capital constraints put pressure on smaller or early-stage companies and as intensifying drug reimbursement pressures and patent-exclusivity losses impact larger commercial enterprises.
- Alongside the biotech and pharma spheres, we are encouraged by what we are seeing in background processes, as novel discovery tools and the adoption of artificial intelligence (AI) and machine learning (ML) technologies are enabling faster and more rational drug discovery and development. While still in the early stages, the adoption of AI/ML tools in drug discovery is expected to grow rapidly in the near term. We believe AI/ML offers the potential to identify novel targets that were previously thought to be "undruggable," as well as improve drug design by simulating molecular behavior and interactions.

## Top Equity Issuers (% of Total)

Holding	Fund
AMGEN INC	8.12
GILEAD SCIENCES INC	7.83
VERTEX PHARMACEUTICALS INC	7.75
REGENERON PHARMACEUTICALS INC	5.50
ASCENDIS PHARMA A/S	4.42
JAZZ PHARMACEUTICALS PLC	4.10
ARGENX SE	3.81
PTC THERAPEUTICS INC	3.13
MERUS NV	2.93
BENITEC BIOPHARMA INC	2.77

## Sector Allocation (% of Total)

Industry	Fund
Biotechnology	82.28
Pharmaceuticals	11.15
Life Sciences Tools & Services	2.88
Health Care Services	1.92
Managed Health Care	0.16
Cash & Cash Equivalents	1.60

## Average annual total returns and fund expenses (%)

Class	CUSIP	Ticker	Without Sales Charge							With Maximum Sales Charge							Expenses		Sales Charges		Inception Date
			3-Mo	YTD	1-Yr	3-Yr	5-Yr	10-Yr	Inception	3-Mo	YTD	1-Yr	3-Yr	5-Yr	10-Yr	Inception	Gross	Net	Initial Charge	CDSC	
Advisor Class	354713398	FTDZX	-4.51	-4.51	-10.75	4.47	4.88	1.50	9.44	-4.51	-4.51	-10.75	4.47	4.88	1.50	9.44	0.81	0.80	—	—	9/15/1997
Class A	354713844	FBDIX	-4.57	-4.57	-10.97	4.21	4.61	1.25	9.28	-9.82	-9.82	-15.86	2.26	3.44	0.67	9.06	1.06	1.05	5.50	—	9/15/1997
Benchmark 1	—	—	-1.54	-1.54	-4.19	0.62	4.58	1.67	—	-1.54	-1.54	-4.19	0.62	4.58	1.67	—	—	—	—	—	—
Benchmark 2	—	—	-4.27	-4.27	8.25	9.06	18.59	12.50	—	-4.27	-4.27	8.25	9.06	18.59	12.50	—	—	—	—	—	—

## Benchmark(s)

Benchmark 1=NASDAQ Biotechnology Index

Benchmark 2=S&P 500 Index

**Performance data quoted represents past performance, which does not guarantee future results.** Current performance may be lower or higher than the figures shown. Principal value and investment returns will fluctuate, and investors' shares, when redeemed, may be worth more or less than the original cost. Performance would have been lower if fees had not been waived in various periods. Total returns assume the reinvestment of all distributions and the deduction of all fund expenses. Returns with sales charge reflect a deduction of the stated maximum sales charge. An investor cannot invest directly in an index, and unmanaged index returns do not reflect any fees, expenses or sales charges. Returns for periods of less than one year are not annualized. All classes of shares may not be available to all investors or through all distribution channels. For current month-end performance, please visit [franklintempleton.com](http://franklintempleton.com).

The fund began offering Advisor Class shares on 9/1/2009. Performance quotations have been calculated as follows: (a) for Advisor Class periods prior to 9/1/2009, a restated figure is used based on the fund's Class A performance. The performance was adjusted to take into account differences in class-specific operating expenses and maximum sales charges. (b) For periods after share class offering, performance for the specific share class is used, reflecting the expenses and maximum sales charges applicable to that class.

Gross expenses are the fund's total annual operating expenses as of the fund's prospectus available at the time of publication. Actual expenses may be higher and may impact portfolio returns. Net expenses reflect contractual fee waivers, expense caps and/or reimbursements, which cannot be terminated prior to 08/31/2025 without Board consent. Additional amounts may be voluntarily waived and/or reimbursed and may be modified or discontinued at any time without notice.

## What are the Risks?

**All investments involve risks, including possible loss of principal.** The portfolio is **non-diversified** and may invest in a relatively small number of issuers, which may negatively impact the fund's performance and result in greater fluctuation in the value of the fund's shares. To the extent the portfolio invests in a **concentration of certain securities, regions or industries**, it is subject to increased volatility. **Small- and mid-cap stocks** involve greater risks and volatility than large-cap stocks. **International investments** are subject to special risks, including currency fluctuations and social, economic and political uncertainties, which could increase volatility. These risks are magnified in **emerging markets**. The manager may consider **environmental, social and governance (ESG) criteria** in the research or investment process; however, ESG considerations may not be a determinative factor in security selection. In addition, the manager may not assess every investment for ESG criteria, and not every ESG factor may be identified or evaluated. These and other risks are discussed in the fund's prospectus.

## Important Information

The information provided is not a complete analysis of every material fact regarding any country, market, industry, security or fund. Because market and economic conditions are subject to change, comments, opinions and analyses are rendered as of the date of this material and may change without notice. A portfolio manager's assessment of a particular security, investment or strategy is not intended as individual investment advice or a recommendation or solicitation to buy, sell or hold any security or to adopt any investment strategy; it is intended only to provide insight into the fund's portfolio selection process. Holdings are subject to change.

The **NASDAQ Biotechnology Index** is a modified capitalization-weighted index designed to measure performance of all NASDAQ stocks in the biotechnology sector. Source: Nasdaq OMX. The **S&P 500 Index** features 500 leading U.S. publicly traded companies, with a primary emphasis on market capitalization. Source: © S&P Dow Jones Indices LLC. All rights reserved.

Important data provider notices and terms available at [www.franklintempletondatasources.com](http://www.franklintempletondatasources.com). All data is subject to change.

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**Before investing, carefully consider a fund's investment objectives, risks, charges and expenses. You can find this and other information in each prospectus, or summary prospectus, if available, at [www.franklintempleton.com](http://www.franklintempleton.com). Please read it carefully.**



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