

# Franklin Small Cap Growth Fund

Advisor Class: FSSAX Class A: FSGRX

Commentary | as of December 31, 2025

## Key Takeaways

- Markets:** US equities delivered solid gains over the fourth quarter of 2025, maintaining their upward trajectory against a backdrop of generally robust corporate earnings, despite some mixed economic signals and investor concerns about stretched valuations in technology-related stocks. Continued monetary easing by the US Federal Reserve (Fed), along with a constructive shift in US-China relations, also underpinned investor sentiment. The outperformance of the Magnificent Seven mega-capitalization technology stocks during the quarter boosted returns for the S&P 500 Index and the Nasdaq Composite Index, while the relatively strong performance of the Dow Jones Industrial Average reflected the enduring strength of blue-chip companies. By investment style, value investing surpassed growth in the large-, mid- and small-capitalization tiers, with large-cap stocks performing better than their mid- and small-cap counterparts.
- Contributors:** For the quarter, stock selection decisions factored into the fund's relative outperformance. Strong stock selection bolstered relative results in the information technology (IT) sector. Stock selection and an overweight in the industrials sector and stock selection in the energy sector also contributed to a lesser extent.
- Detractors:** Stock selection and an overweight in the consumer staples sector detracted most from relative performance in the fourth quarter. An underweight in the health care sector and stock selection and an underweight in the real estate sector also proved adverse for relative returns.
- Outlook:** The performance of small-cap stocks in general was positive for the fourth quarter and for 2025, supported by broadly favorable valuations, earnings growth and monetary policy. Future performance is likely to depend on the health of the US economy, Fed decisions and overall investor confidence. We believe small-cap growth stocks are attractively valued, both relative to large caps and in light of their own underlying growth potential.

## Performance Review

- The fund's return (Advisor Class without sales charges) was positive and meaningfully outperformed that of the Russell 2000 Growth Index. In the IT sector, Lumentum Holdings was a top contributor to returns. The photonics specialist reported solid fiscal first-quarter 2026 financial results, but it was the company's second-quarter guidance of more than 20% sequential growth that rallied the stock. Increased artificial intelligence (AI) demand benefited its core business, including transceiver components and data center interconnects.
- Olema Pharmaceuticals was a leading contributor in the health care sector. Shares of the clinical-stage biopharmaceutical company jumped after a competitor's breast cancer drug trial succeeded, boosting confidence in Olema's similar therapy. The company is a developer of targeted treatments for breast cancer.
- In contrast, the health care sector was hindered by a position in uniQure (not held by period-end), whose shares fell sharply after the US Food & Drug Administration withdrew its support for the firm's Huntington's disease trial data, raising regulatory uncertainty for the biotechnology company.

## Outlook

- As we enter 2026, our view on US equities remains positive but selective. In an environment where growth is available but not abundant, our focus is on owning high-quality franchises with durable competitive advantages, often supported by secular tailwinds.
- In recent years, a small group of mega-capitalization innovators—dominated by the Magnificent Seven—has driven the majority of index returns, benefiting from scale and AI leadership. Looking toward 2026, we believe conditions should favor a broadening of equity market leadership, with opportunities emerging across sectors beyond IT and companies below the mega-cap threshold, which can offer an advantage for small- and mid-cap companies.
- In 2026, we are focused on structural themes shaped by AI and automation, which are now producing measurable productivity gains not only in the IT sector but also in the health care, financials, industrials and energy sectors. We are also monitoring potential risks for the US economy, including inflation, regulatory pressures, geopolitical friction, infrastructure bottlenecks and unfavorable policy shifts.
- Fiscal and economic conditions appear to be aligning to support growth. We expect continued innovation-led expansion underpinned by quality fundamentals in an environment where we think disciplined, active management has an advantage.

## Top Equity Issuers (% of Total)

Holding	Fund
BWX TECHNOLOGIES INC	2.93
ARCOSA INC	2.72
AAR CORP	2.34
ONTO INNOVATION INC	2.14
GRANITE CONSTRUCTION INC	2.09
NEW YORK TIMES CO/THE	2.03
SERVICETITAN INC	1.99
LATTICE SEMICONDUCTOR CORP	1.99
LUMENTUM HOLDINGS INC	1.97
SITIME CORP	1.97

## Average annual total returns and fund expenses (%) - as of December 31, 2025

Class	CUSIP	Ticker	Without Sales Charge						With Maximum Sales Charge						Expenses		Sales Charges		Inception			
			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	Date	
Advisor Class	354713653	FSSAX	6.08	7.75	7.75	16.86	2.06	10.38		8.19	6.08	7.75	7.75	16.86	2.06	10.38	8.19	0.79	0.79	—	—	5/1/2000
Class A	354713620	FSGRX	6.03	7.50	7.50	16.56	1.81	10.10		7.89	0.20	1.59	1.59	14.38	0.67	9.48	7.66	1.04	1.04	5.50	—	5/1/2000
Benchmark 1	—	—	1.22	13.01	13.01	15.58	3.18	9.57		—	1.22	13.01	13.01	15.58	3.18	9.57	—	—	—	—	—	—
Benchmark 2	—	—	2.66	17.88	17.88	23.00	14.43	14.82		—	2.66	17.88	17.88	23.00	14.43	14.82	—	—	—	—	—	—

## Benchmark(s)

Benchmark 1=Russell 2000 Growth Index

Benchmark 2=S&amp;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 5/1/2000. Performance quotations have been calculated as follows: (a) for Advisor Class periods prior to 5/1/2000, 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. The total annual operating expenses are as of the fund's prospectus available at the time of publication. Actual expenses may be higher and may impact portfolio returns.

## What are the Risks?

All investments involve risks, including possible loss of principal. Small- and mid-cap stocks involve greater risks and volatility than large-cap stocks. The investment style may become out of favor, which may have a negative impact on performance. To the extent the portfolio invests in a concentration of certain securities, regions or industries, it is subject to increased volatility. Liquidity risk exists when securities or other investments become more difficult to sell, or are unable to be sold, at the price at which they have been valued. 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.

## Glossary

**Dow Jones Industrial Average (DJIA)** is an unmanaged index composed of 30 blue-chip stocks, each with annual sales exceeding \$7 billion. The DJIA is price-weighted, reflects large-cap companies representative of U.S. industry, and historically has moved in tandem with other major market indexes such as the S&P 500. Source: © S&P Dow Jones Indices LLC.

The **Magnificent Seven** stocks are Apple, Amazon, Alphabet, Meta Platforms, Microsoft, Nvidia, and Tesla.

**Nasdaq Composite Index** is a market-capitalization-weighted index that is designed to represent the performance of Nasdaq securities and includes over 3,000 stocks. Source: Nasdaq OMX.

## 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 **S&P 500 Index** features 500 leading U.S. publicly traded companies, with a primary emphasis on market capitalization. The **Russell 2000 Growth Index** measures the performance of the small-cap growth segment of the U.S. equity universe.

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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