

Franklin U.S. Focused Growth SMA

Commentary | as of March 31, 2026

Key Takeaways

- **Markets:** Global equity markets generally declined during the first quarter of 2026 (1Q26) amid heightened volatility, as geopolitical tensions and shifting macroeconomic dynamics weighed on investor sentiment. The conflict in the Middle East emerged as a key destabilizing factor, disrupting energy markets and amplifying inflationary pressures globally. Value stocks outperformed their growth-oriented peers, reflecting a rotation away from high-valuation-multiple sectors amid rising inflation concerns. Large-capitalization equities generally underperformed those in the mid- and small-cap tiers, as investors sought opportunities in more cyclically sensitive areas of the market. Sector rotation saw commodity-linked industries benefit from higher energy prices, while the information technology (IT) and consumer discretionary sectors faced pressure amid concerns over AI-driven disruptions to established business models.
- **Detractors:** Unfavorable stock selection in the industrials, consumer discretionary, financials and health care sectors, plus a lack of exposure to consumer staples, materials, real estate and utilities companies, all of which fared better than the strategy's benchmark index.
- **Contributors:** Effective security selection and overweighting among semiconductor companies; an underweighted exposure to poor-performing software stocks; and beneficial stock selection among pharmaceuticals companies.
- **Outlook:** We are enthusiastic about current and potential productivity gains from AI as its use cases evolve. Generative and agentic AI continue to advance, with returns on investment increasingly visible as deployments scale beyond experimentation toward scaled implementation. We think these developments, alongside progress in other innovation-driven areas, could support a durable backdrop for long-term growth, even as markets experience periodic volatility.

Performance Review

- Although the US Focused Growth strategy (pure gross of fees and net of fees) fared better than the Russell 1000 Growth Index with its core IT sector holdings (averaging 52.3% of total net assets), it underperformed the benchmark across nearly all of the 10 other major equity sectors.
- Industrials holdings (averaging 4% of the portfolio) offered a mix of contributors and detractors but still fell sharply, while industrials stocks tracked by the index appreciated. Aerospace and defense industry declines for Axon Enterprise (overweight) and off-index Kratos Defense & Security Solutions were partially offset by sharp rally in GE Vernova (electrical equipment industry), which saw heightened demand from data center, energy grid and power generation projects.
- Consumer discretionary stocks were weak in both absolute and relative terms. All related holdings traded lower, with the key detractors focused on e-commerce companies such as Amazon.com (overweight) and an off-index consumer internet firm (sold by period-end), though positions in app-based delivery platform providers such as DoorDash (overweight) and online used car sales company Carvana also sustained substantial losses. In the absence of any serious company-specific setbacks, these stocks were broadly impacted by investors rotating away from high-multiple consumer internet names into those perceived as safer, more predictable earnings plays—particularly after a long run of growth stocks outperforming. A surprise announcement of new US tariffs on imported goods further drove broad selling in consumer-facing stocks that rely on global supply chains, as investors began modeling higher costs and lower profit margins. That overall shift from momentum/optimism to fundamental valuation discipline impacted e-commerce and online services disproportionately in the selloff. We're still generally positive on these holdings for the longer term, and Amazon in particular.
- Despite solid rallies for Ascendis Pharma and Jazz Pharmaceuticals, the fund's health care sector allocation (averaging about 6.5% of the portfolio) declined overall, with results versus the index hindered primarily by adverse security selection in the biotechnology industry, mainly due to a lack of portfolio exposure to Amgen, AbbVie and other index components.
- Most of the other major detractors reduced our measure of outperformance in the IT sector, including an underweighted stake in Apple as its share price fell less than the index; substantial losses for Shopify (not an index component) in IT services; and double-digit percentage declines for AppLovin and other overweighted or off-index software stocks.
- Semiconductor and semi equipment holdings (averaging 27.6% of total net assets) were a source of strength in relative terms, as the fund's 3.5% decline compared well to the index's 4.8% drop in the same industry. Some semi stocks posted robust gains, including key contributors Taiwan Semiconductor Manufacturing (TSMC), ASML Holding and Monolithic Power Systems. The semi space was still seeing vigorous structural demand tied to AI infrastructure and advanced computing. Chipmakers with visible 4Q25 earnings "beats," strong 2026 guidance, or clear demand paths linked to AI or data center build-outs tended to separate themselves from selective weakness across the broader IT sector. We also maintained a large yet underweight exposure to Microsoft, which aided results in the software industry as it fell much further than the index. There were a few other, smaller offsetting tech-related contributors, including gains for Cloudflare (overweight) in IT services.
- Aside from the strategy's active investments, its nearly-3% cash position had a larger positive impact on relative performance than all individual contributors cited above except for TSMC and ASML.

Outlook

- **We believe the increasing focus on generative and agentic AI is warranted, as adoption continues to broaden across industries.** At the same time, innovation remains diverse, with advances occurring across areas such as space and defense, robotics, health care, genomics and energy. We view technology, including AI, robotics and hyperscale cloud computing, as inherently disinflationary, with the potential to drive productivity gains across the broader economy.
- **We expect continued technological transformation driven by advances in data, automation and life sciences.** While short-term market movements may reflect valuation shifts or changing sentiment, these do not alter our long-term perspective. As long-term investors, we remain focused on identifying innovative companies whose growth potential and pace of adoption may be underappreciated, consistent with the portfolio's objective of long-term capital growth.

Top Equity Issuers (% of Total)

Holding	Portfolio
NVIDIA CORP	12.91
AMAZON.COM INC	8.92
ALPHABET INC	7.62
MICROSOFT CORP	7.39
BROADCOM INC	5.50
APPLE INC	5.25
META PLATFORMS INC	4.98
TAIWAN SEMICONDUCTOR MANUFACTURING CO LTD	4.54
TESLA INC	3.24
CELESTICA INC	2.45

Average annual total returns (%) - as of March 31, 2026-PRELIMINARY

Composite	3-Mo*	6-Mo*	YTD*	1-Yr	3-Yr	5-Yr	10-Yr	15-Yr	20-Yr	25-Yr	Inception	Inception Date
Net of Fees	-12.58	-14.59	-12.58	15.11	18.13	6.04	—	—	—	—	14.99	3/31/2020
Pure Gross of Fees	-11.90	-13.28	-11.90	18.53	21.63	9.21	—	—	—	—	18.40	3/31/2020
Benchmark	-9.78	-8.76	-9.78	18.81	21.18	12.76	—	—	—	—	19.87	—

*Cumulative total returns

Benchmark(s)

Benchmark = Russell 1000 Growth Index

The strategy returns shown are preliminary composite returns, subject to future revision (downward or upward).

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The **Russell 1000 Growth Index** measures the performance of the large-cap growth segment of the U.S. equity universe.

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Source: FTSE.

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