ClearBridge Investments
A Legg Mason Company

2Q 2019 | Product Commentary

CLEARBRIDGE SELECT FUND

Aram Green
Portfolio Manager

Average annual total returns and fund expenses (%)

as of June 30, 2019

Class A	3-mo	1-yr	5-yr	10-yr	Since Incept. (09/23/13)	Expenses Gross	Expenses Net
Excluding sales charges	4.32	11.16	15.94	N/A	15.38	1.68	1.59
Including effects of maximum sales charges	-1.67	4.78	14.57	N/A	14.19	1.68	1.59
Russell 3000 Index	4.10	8.98	10.19	N/A	N/A	-	-

Performance shown represents past performance and is no guarantee of future results. *Current performance may be higher or lower than the performance shown. Investment return and principal value will fluctuate, so shares, when redeemed, may be worth more or less than the original cost. Class A shares have a maximum front-end sales charge of 5.75%.Total returns assume the reinvestment of all distributions at net asset value and the deduction of all Fund expenses. Total return figures are based on the NAV per share applied to shareholder subscriptions and redemptions, which may differ from the NAV per share disclosed in Fund shareholder reports. Performance would have been lower if fees had not been waived in various periods. Returns for less than one year are cumulative. For the most recent month-end information, please visit www.leggmason.com.*

Gross expenses are the Fund's total annual operating expenses for the share class(es) shown. **Net expenses** are the Fund's total annual operating expenses for the share classes indicated and would reflect contractual fee waivers and/or reimbursements, where these reductions reduce the Fund's gross expenses. These arrangements cannot be terminated prior to December 31, 2020 without the Board's consent. In periods of market volatility, assets may decline significantly, causing total annual Fund operating expenses to become higher than the numbers shown in the table above.

The Gross and Net Expenses listed include 0.02 of Acquired Fund Fees and Expenses (AFFE) that are required to be shown in the Fund's prospectus. AFFE reflects the Fund's pro rata share of fees and expenses relating to its investments in acquired funds; however, AFFE are not incurred directly by the Fund. Therefore, AFFE are not reflected in the Fund's audited financial statements or financial highlights.
The **Russell 3000 Index** is a market-capitalization-weighted equity index maintained by the FTSE Russell that provides exposure to the entire U.S. stock market. Investors cannot invest directly in an index, and unmanaged index returns do not reflect any fees, expenses or sales charges.

Key takeaways

- Solid fundamentals and robust multiple expansion caused fast-growing companies to lead in an exceptional first half for equities.
- We took advantage of an open IPO window, participating in four new issues with attractive, long-term growth profiles.
- A higher-than-normal cash position, a reflection of high valuations for the companies we target and portfolio mergers and acquisitions (M&A) activity, was a drag on relative performance.

Market overview and outlook

Investors expressed a strong preference for the fastest-growing stocks in the market in the second quarter, extending a first-half run for growth. The Russell Midcap Growth Index was the best performer for the quarter, with a 5.40% return, and it's up 26.08% year to date, while the Russell 3000 Growth Index advanced 4.50% for the quarter and is up 21.41% for the year. Both indexes handily outperformed their value counterparts over each period. In addition, the S&P 500 Index added 4.30% in the second quarter to cap its best first-half showing (+18.54%) since 1997.

The Select Fund maintains significant exposure to the fastest-growing segments of the market by targeting stocks that we categorize as disruptors. These are companies like e-commerce platforms Shopify and MercadoLibre, which are enabling the growth of new markets – in this case turning small businesses into competitive online merchants – through innovative sales, fulfillment and payment solutions. MercadoLibre is also the dominant player in a burgeoning Latin American market early in the secular growth of consumer spending.

Strong-performing stocks like these have benefited from multiple expansion on top of upward earnings revisions. Shopify, for example, has seen its enterprise value-to-sales multiple zoom from 7X at the end of 2018 to a current 19X. A more accommodative environment has also fueled multiple expansion. As interest rates decline (the 10-year U.S. Treasury yield fell 40 basis points in the second quarter), the present value of a company's future earnings and cash flows rise.

Capital market activity has provided further confirmation of the desire for growth. The initial public offering (IPO) market saw its best quarter for deal volume in four years and best quarter for capital raised in nearly five years. We participated in four IPOs in companies we consider disruptors: Zoom Video, a cloud-based provider of video conferencing that topped revenue forecasts in its first post-IPO earnings report; CrowdStrike Holdings, a cloud-based cybersecurity provider; Pinterest, an already profitable social platform where users can express their interests and discover ideas through images they "pin" to their pages; and the RealReal, an online marketplace for used luxury merchandise, a growing niche for both millennial and Baby Boomer consumers. We also added a new position in Farfetch, a high-conviction disruptor that went public in 2018 and operates an online luxury goods marketplace where both well-known brands and small boutiques can sell their merchandise.

Strategic acquirers are also seeking sources of above-average growth, leading to the proposed takeout of two portfolio companies: cloud-based biopharmaceutical data and analytics software maker Medidata Solutions (by French technology conglomerate Dassault Systemes) and data analytics provider Tableau Software (by Salesforce.com).

The intensity of the growth stock rally has pushed the valuations of some disruptors to the point where we have become more selective in sourcing new ideas and adding to existing positions. This, combined with a busy period of M&A in the first quarter, has caused the portfolio to accumulate higher-than-normal levels of cash. We have been redeploying some sale proceeds into compounders like OUTFRONT Media, a new addition that is a leader in the established billboard and outdoor advertising business, and evolving opportunities – companies we consider temporarily mispriced and possessing changing dynamics, like ride-share provider Lyft after its disappointing first-quarter IPO. Despite these moves, cash was a drag on relative performance for the quarter.

Many of the indicators we follow, including operating margins, employment and the trend in interest rates, suggest a late cycle equity market. Earnings revisions are another key indicator, with negative revisions currently outnumbering positive ones. Reductions in guidance are skewed to cyclical stocks dependent on a strong economy for growth or tied to end markets with weakening demand. The Select Strategy is underweight these companies, as well as those carrying heavy debt loads. Portfolio weakness during the quarter was centered in portfolio holdings such as specialty hospital operator Surgery Partners and ATM provider Cardtronics, which have higher levels of financial leverage, which the market has not been favoring.

As trade issues persist and business confidence falls, organic growers are being recognized for their ability to outperform in most market environments. We are confident in the range of opportunities available to our portfolio companies.

Fund highlights

For the quarter ended June 30, 2019, the ClearBridge Select Fund — Class A shares had a cumulative return of 4.32%, excluding the effects of sales charges. In comparison, the Fund's unmanaged benchmark, the Russell 3000 Index, returned 4.10%.

On an absolute basis, the Fund had gains in eight of the nine sectors in which it was invested (out of 11 total) during the quarter. The main contributors to performance were the information technology (IT) and industrials sectors.

On a relative basis, stock selection in the industrials and real estate sectors and a lack of exposure to the energy sector contributed the most to relative results. On the negative side, stock selection in the communication services sector, an underweight to the financials sector and the Strategy's cash position detracted from relative results.

On an individual stock basis, the largest contributors to absolute returns in the second quarter were Shopify, Zoom, Copart, MercadoLibre, and Insulet. The greatest detractors from absolute returns were positions in comScore, Cardtronics, Surgery Partners, ForeScout Technologies and Lyft.

The Fund initiated six new positions in the second quarter and closed two positions, Casa Systems, in the IT sector, and Grubhub, in the consumer discretionary sector.

Top contributors

Shopify (SHOP), in the IT sector, is a Canadian e-commerce software provider that enables small businesses to establish an online store and manage all aspects of the sales, marketing and fulfillment process. The stock was propelled higher by quarterly results that beat estimates on strong growth in subscriptions and its merchant solutions business.

Copart (CPRT), in the industrials sector, is an essential service provider to the insurance industry, recycling or disassembling (for parts) vehicles that have been totaled. Copart has an irreplaceable real estate network of over 200 yards, and the logistics to process/scrap/tow/sell. The company reported very strong trends in its first quarter, with non-U.S. markets maturing well (+13% units) and U.S. volumes continuing to be strong (+3%).

Insulet (PODD), in the health care sector, is a medical device manufacturer that develops insulin infusion systems for diabetes patients. The stock was lifted by quarterly results that topped forecasts and an upward revision to full-year earnings guidance.

Top detractors

comScore (SCOR), in the communication services sector, is a media measurement provider, tracking consumer behavior and advertising across media platforms. The stock sold off following the resignation of two top executives and the announcement of a cost reduction plan.

Cardtronics (CATM), in the IT sector, operates a network of automatic teller machines and financial kiosks. Despite solid results that topped estimates, the stock was hurt by its increasing financial leverage.

Surgery Partners (SGRY), in the health care sector, is a leading surgical facility operator specializing in ambulatory surgery centers, a fast-growing segment in health care. Interest in Surgery Partners has grown as the vertical integration trend in health care has begun to value ambulatory surgery centers as potential acquisitions due to their flexible operating model, cheaper costs and well-entrenched market positioning. The stock trended lower after results missed estimates and the company increased its financial leverage.

Top 10 equity holdings (%)	
Shopify Inc	3.5
SBA Communications Corp	3.4
ServiceNow Inc	2.8
Ross Stores Inc	2.6
Copart Inc	2.5
Wix.com Ltd	2.5
MercadoLibre Inc	2.4
Syneos Health Inc	2.3
Trex Co Inc	2.1
Adobe Inc	2.0

Sector allocation (%)	
Information Technology	35.3
Consumer Discretionary	17.9
Health Care	12.0
Industrials	8.7
Real Estate	5.7
Communication Services	4.6
Consumer Staples	3.7
Financials	1.5
Materials	1.2
Other	0.0
Utilities	0.0
Energy	0.0
Cash/Other	9.4

Percentages are based on total portfolio as of quarter end and are subject to change at any time. For informational purposes only and not to be considered a recommendation to purchase or sell any security.

Definitions and additional terms:

Please note that an investor cannot invest directly in an index, and unmanaged index returns do not reflect any fees, expenses or sales charges.

A **basis point (bp, or bps)** is equal to 1/100th of 1%, or 0.01%.

An **initial public offering (IPO)** is the process of offering shares in a private corporation to the public for the first time.

Russell 3000 Index is an unmanaged index of the 3,000 largest U.S. companies

Russell 3000 Growth Index is a market capitalization-weighted index based on the Russell 3000 index. The Russell 3000 Growth Index includes companies that display signs of above-average growth.

The **Russell Midcap Index** is a complete subset of both the Russell 1000 and the Russell 3000.

S&P 500 Index is an unmanaged index of roughly 500 stocks that is generally representative of the performance of larger companies in the U.S.

U.S. Treasurys are backed by the "full faith and credit" of the United States government and offer return of principal value if held to maturity.

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- A broad mix of equities, fixed income, alternatives and cash strategies invested worldwide
- A diverse family of specialized investment managers, each with its own independent approach to research and analysis
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What should I know before investing?

Equity securities are subject to price fluctuation and possible loss of principal. 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. Fixed income securities involve interest rate, credit, inflation and reinvestment risks; and possible loss of principal. As interest rates rise, the value of fixed income securities falls. High-yield bonds are subject to greater price volatility, illiquidity and possibility of default. Derivatives, such as options and futures, can be illiquid, may disproportionately increase losses, and have a potentially large impact on Fund performance. As a non-diversified fund, the Fund is permitted to invest a higher percentage of its assets in any one issuer than a diversified fund, which may magnify the Fund's losses from events affecting a particular issuer.