

Markets

T. Rowe's \$1 Trillion Answer to Claims Stock-Picking Is Dead

by Annie Massa and Heather Perlberg

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- Firm's retirement business helped boost revenue and assets
- Narrow focus comes with trade-offs, like missing passive shift

Stock pickers may be under siege after decades of ruling Wall Street, but not every old-school champion of active mutual funds is losing ground to cheaper rivals tracking indexes.

T. Rowe Price Group Inc. is one of the rare winners.

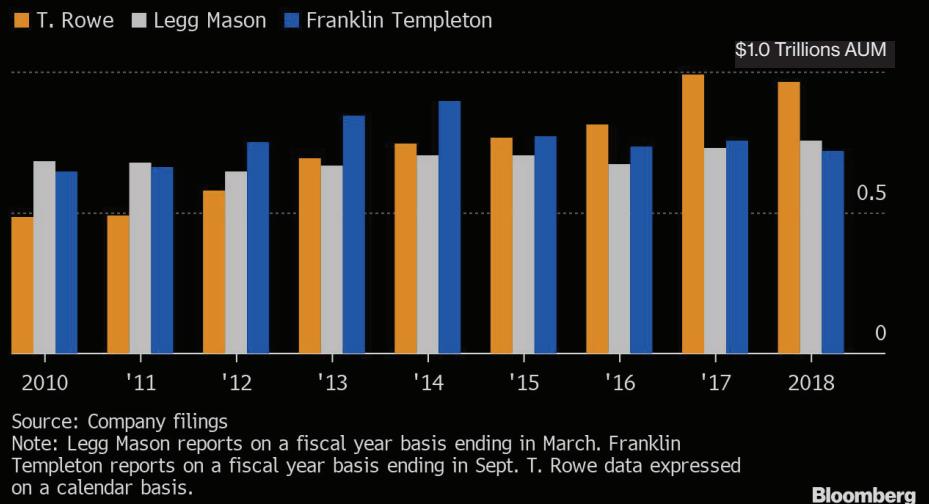
The 82-year-old company, which built its reputation sifting standouts and laggards in U.S. equities, has seen assets under management swell to just over \$1 trillion from around \$400 billion at the start of the decade. That means it stayed abreast of the long bull market even as peers including Franklin Resources Inc. and Legg Mason Inc. suffered outflows and revenue declines.

With its focus on plain old stock funds in retirement accounts, Baltimore-based T. Rowe is an unlikely success in an era when the likes of BlackRock Inc. and Vanguard Group are luring investors looking to make low-cost bets on broadly rising markets. But the firm, whose informal motto is "get rich slow," has thrived by establishing itself in an area that's yet to to embrace exchange-traded funds.

"They decided early on that they'd focus on one niche part of the market, and that's really helped them," said Gregory Warren, an analyst at Morningstar Inc. "Combined with their

Upward Trajectory

T. Rowe's assets under management are growing despite industry hardship



dedication to investment performance, they've done a lot of the right things historically."

About two-thirds of T. Rowe's assets under

management are held in retirement-related products. The firm started offering funds in company-sponsored defined contribution plans in 1974 and today sits among the top 10 providers of recordkeeping services for 401(k)s -- a role tracking employee investments in a company's retirement plan. Its funds are also available on platforms managed by other providers.

"Defined contribution is an important marketplace for us," Chief Executive Officer Bill Stromberg said in an interview.

About 4,600 retirement plan sponsors were using T. Rowe's platform at the end of 2018, according to the company.

"Those are sticky, high quality assets," said Robert Lee, an analyst at Keefe Bruyette & Woods who rates T. Rowe's own shares "market perform."

Index-tracking products such as exchange-traded funds aren't as popular in retirement accounts like 401(k) plans, where their tax advantages aren't relevant.

T. Rowe's strategy has helped the company secure net inflows in all but one of the five

Steady Gains

T Rowe stock has outperformed its rivals



years through 2018; revenue rose 35% over the period. By contrast, Legg Mason saw outflows of more than \$80 billion in its past four fiscal years. Franklin's outflows were even deeper, with clients withdrawing more than \$100 billion in its past four fiscal years.

A Franklin spokesman declined to comment. A spokeswoman for Legg Mason said it "has sought to diversify its investment offerings in fixed income and equity categories, while adding alternative investment capabilities."

T. Rowe keeps a narrow focus on U.S. mutual funds -- a strategy that comes with trade-offs. The fund house obsesses over its cautious, meticulous investment process and long history, to the extent that it called its company mascot -- a bighorn sheep -- "Trusty" on fears that the original name "Lucky" would reflect badly on how it chooses stocks.

One ex-staffer recalled toting a photo of founder Thomas Rowe Price Jr. on sales calls, displaying the image to institutional investors to illustrate the firm's principles and history.

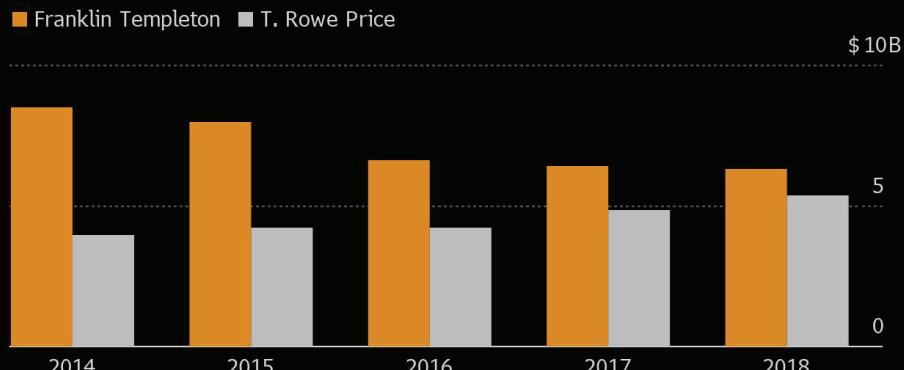
The steady-as-she goes ethos is part of the investment process, and helped about 75% of the firm's U.S. mutual funds do better than the median offering in their class over the past five years, according to Morningstar. It also competes on price, with about half of T. Rowe's funds charging below the industry average, Morningstar data show.

Stromberg has spent more than 30 years at the 7,000-person company, which he joined after a brief stint playing for the Philadelphia Eagles. It's not uncommon to see portfolio managers for T. Rowe funds stay put for decades. Some financial advisers favor that consistency.

The CEO is aware that the years ahead could be challenging, despite the firm's successes.

Diverging Paths

T. Rowe gathers revenue, while rival Franklin Templeton falls



Source: Bloomberg data

Note: Franklin Templeton reports on a fiscal year basis ending in Sept. T. Rowe data expressed on a calendar basis.

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Passive investing continues to gather momentum. In August, assets in U.S. index-based equity mutual funds and exchange-traded funds topped those in active stock funds for the first time: \$4.3 trillion compared with \$4.2 trillion, respectively, according to Morningstar.

While it may help with stock-picking T. Rowe's conservative culture means it can miss out on major industry shifts, such as the growth of index funds. The firm chose not to make a heavy push into such products, said Stromberg, deciding it was too crowded to stand out.

"There wasn't much room for another player," he said.

That stance seems to be changing. Regulators

recently approved partially concealed, actively-managed ETFs from T. Rowe that would reveal their holdings once a quarter, rather than every day as conventional ETFs do. Active strategies account for around 2% of U.S. ETF assets.

Alternative investment strategies could also make sense at some point, said Stromberg, though he didn't give more details. Those investments tend to come with longer time horizons and higher fees.

"We're on our toes," said Stromberg. "We're trying to keep abreast of the changes, and keep an open mind about how we innovate and evolve our business."

— With assistance by Denise Cochran

EXPLANATORY NOTES—ARTICLE REPRINT

Bloomberg, “T. Rowe’s \$1 Trillion Answer to Claims Stock-Picking Is Dead,” December 23, 2019

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80% of our mutual funds with a 5-year track record outperformed their 5-year Morningstar median as of 12/31/19. 122 of our 134 mutual funds had a 5-year track record as of 12/31/19. (Based on primary share class, excluding passives and funds used in insurance products.) 98 of these 122 funds (80%) beat their Morningstar median for the 5-year period. 85 of 133 (64%), 97 of 130 (75%), and 75 of 92 (82%) of T. Rowe Price funds outperformed their Morningstar median for the 1-, 3-, and 10-year periods ended 12/31/19, respectively. Calculations based on cumulative total return. Not all funds outperformed for all periods. (Source for data: Morningstar.) Past performance cannot guarantee future results.

94% of our funds for individual investors have net expense ratios below their peer category averages. 116 of 124 funds more than 6 months old (excluding institutional and bank institutional funds as defined by Morningstar) had net expense ratios below their Morningstar averages based on the most recent prospectus filing available as of 12/31/19.

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Regarding the line chart labeled “Steady Gains: T. Rowe stock has outperformed its rivals,” this chart shows percent growth in stock price indexed to zero on 12/15/14. All data are as of 12/23/19.

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