T.RowePrice®
INVEST WITH CONFIDENCE

PRICE POINT
October 2016

Timely intelligence and analysis for our clients.

Global Equities
VOLATILITY, UNCERTAINTY, AND THE AGING BULL MARKET



Scott Berg, CFA
Portfolio Manager, Global Growth Equity Strategy

KEY POINTS

- Top-down macroeconomic and political news is dominating markets like never before.
- The uneven nature of global economic health and a now more uncertain investing environment has raised questions over whether the equity cycle is coming to an end, or are we merely entering a new phase?
- For patient long-term investors, such uncertainty typically creates buying opportunities in durable growth stocks, especially those with perceived cyclicality. Importantly, although profits growth and earnings have been poor at an aggregate level, there remain compelling pockets of growth in the world, and this remains a perennial opportunity throughout a cycle.
- While the rally in oil and commodity prices has brought about a debate on the potential for a value cycle to form, we believe that long-term growth stocks are likely to continue to command a sustainable premium in a challenging macroeconomic environment.

MACROECONOMIC HEADLINES DOMINATE IN 2016

Macro and top-down events are dominating markets like never before in 2016. Rising uncertainty is to be expected when you combine the fact that we are eight years into the second longest bull market in history, in a U.S. election year, and in an environment where so many of the pillars of past return are evolving. The result of the UK referendum on European Union (EU) membership has added to the list of macroeconomic and political risks facing markets.

Realistically, the Brexit result will impact the UK economy in the near term as companies hold back investment in the face of uncertainty surrounding the UK's relationship with Europe. Continental Europe may suffer a similar fate, an unwelcome outcome for a region that is growing slowly and still at the beginning of its economic recovery. Ongoing stimulus from the European Central Bank to support the European economy is highly likely and affirms the view that interest rates are likely to remain low

FOR INVESTMENT PROFESSIONALS ONLY. NOT FOR FURTHER DISTRIBUTION.

for a prolonged period of time, both in Europe and globally. Meanwhile, we have the upcoming U.S. elections in November, which will continue to dominate the headlines.

This adds to investor concerns over an equity bull market, which has become increasingly more complex. This complexity centers on the question of whether global corporates can deliver better earnings in a more modest growth world. As further bottom-up improvement has been called into question, top-down factors—including the outlook for China, concerns over Europe, and volatility in energy and commodity prices—have taken center stage in driving stock prices. On the other hand, those fearful of an aggressive U.S. Federal Reserve tightening cycle may at least have their concerns allayed given rate increases are now likely to be more measured based on Brexit and global growth concerns. Regardless, macroeconomic concerns will persist in the near term, as investors put more weight on these issues rather than the underlying fundamentals of individual companies.

EARNINGS IMPROVEMENT PRESENTS OPPORTUNITY

While the economic picture remains confusing for many, one comforting factor is that we continue to find numerous companies displaying better fundamentals, even in a modest-growth world. In addition, this perspective is set against a starting point where valuations remain reasonable, especially when considering free cash flow-based metrics. The broadening out of the perspective on valuations to include cash-based metrics is important because changes in cash flow trends will help us judge the evolution of the equity cycle over the near and medium terms. It will also help support the return of capital to investors in the form of share buybacks and dividends.

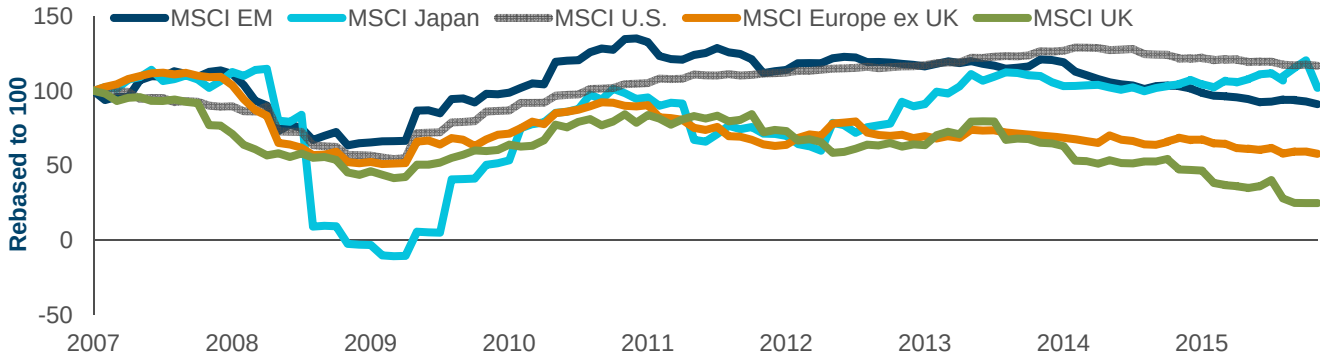
With monetary policy remaining accommodative and inflation still low (although with the potential to turn upward), we believe this is a solid starting point to generate attractive returns from global equities. In particular, it will support stocks with compelling and unrecognized growth characteristics, given the ongoing scarcity of broad-based macroeconomic growth trends.

While the near-term rally in oil and commodities has caused much debate on whether we are seeing the beginning of a value cycle, we do not think this is likely outside of a scenario of a strong upturn in global growth. In fact, the backdrop has created some unusual partnerships including the positive correlation of Value and Growth over the summer. Specifically, Growth and Value seem to have put their historic differences aside, as investors either stay on the sidelines or pile into defensive stocks.

When considering the equity cycle, however, the absence of profit delivery over the past few years remains a legitimate concern (Figure 1). That is important for us when we invest, that we continue to ask ourselves whether we can see clear signs that stocks will begin to deliver on profits after a period of distinctly narrow growth signals.

Figure 1: A Reality Check on Profits Growth—Regional Profits (EPS in USD)

In USD Since Last Cycle Peak (October 2007). As of August 31, 2016.



Sources: FactSet, Citi Research, and MSCI.

MSCI makes no express or implied warranties or representations and shall have no liability whatsoever with respect to any MSCI data contained herein. The MSCI data may not be further redistributed or used as a basis for other indices or any securities or financial products. This report is not approved, reviewed or produced by MSCI.

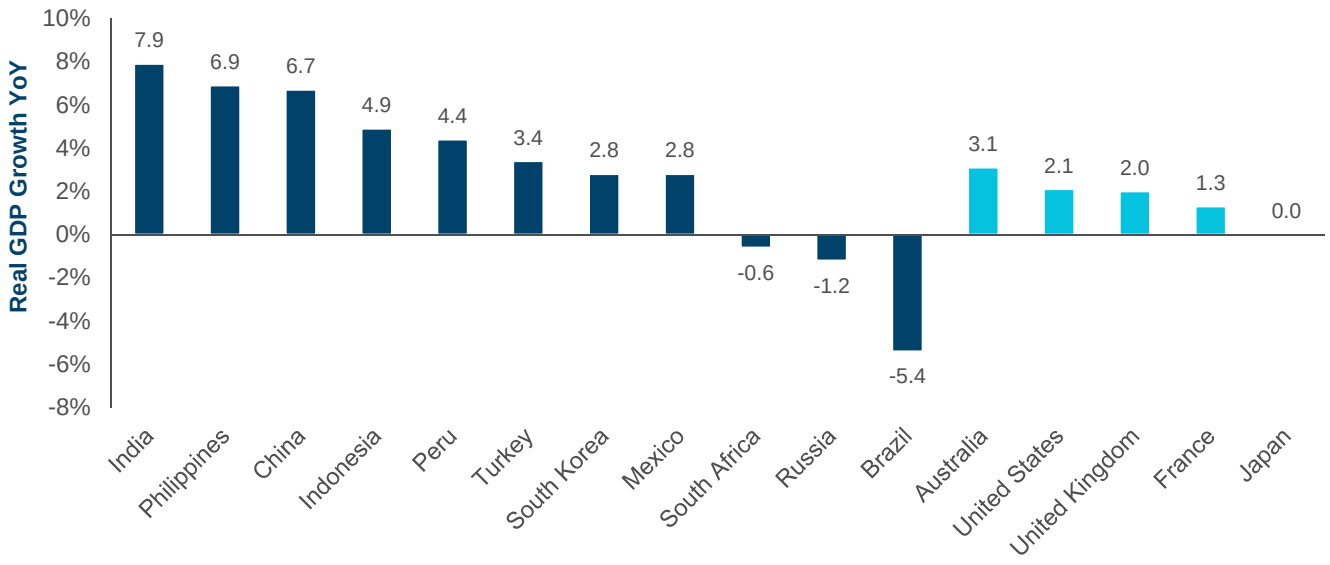
POTENTIAL POCKETS OF GROWTH

Although earnings have been poor at an aggregate level, there remain very interesting pockets of growth. We have identified many stocks that have earnings improvement potential in the next stage of the economic cycle. At the same time, we do not believe that we are headed for a severe contraction of global growth in the near term.

Within the emerging world, there is still huge potential for change and market share gains in particular. Emerging Asia continues to demonstrate strong domestic growth potential, given that many economies remain advantaged by long-term consumption and demographic drivers (Figure 2). Elsewhere, while the developed world growth outlook is subdued, building exposure to select contrarian and cyclical segments of the market, when the opportunity is afforded, can be a sensible approach in our view. This requires a long-term time horizon (as well as a contrarian instinct) in an environment where short-term volatility is inevitable. However, the rewards are real for those willing to buy durable companies with long runways for growth.

Figure 2: Emerging Markets Continue to Drive Global Growth

As of June 30, 2016



Sources: FactSet and Economics.

VALUATIONS ARE REASONABLE BUT WILL NOT DRIVE FUTURE RETURNS

With global equities (including emerging market equities) trading around 15 times 2017 earnings,[1] the days of extremely cheap valuations are clearly over, but valuations remain reasonable in the context of the economic cycle and especially given alternative avenues for capital.

While valuations will not drive aggregate returns moving forward to the extent that they did in the early part of this equity cycle, at the same time, they should not be a barrier to equity markets delivering solid returns over the medium to long terms. Importantly, the lack of bullishness in the world has continued to keep broad-based bubbles at bay, and valuations have, therefore, remained at sensible levels. This provides a generally favorable backdrop for investors and, with all else being equal, likely extends this particular equity cycle.

The environment for equity investing, however, is more nuanced than in previous years. Investors have been cautious of stocks with cyclical characteristics through much of this equity cycle, while continuing to treasure

[1] As of August 31, 2016. Source: FactSet

stocks with defensive qualities and lower-volatility profiles. However, as markets have been shaken by growth concerns, a key opportunity has arisen: the chance to buy high-quality growth and improvement stocks on weakness.

WHERE DO WE GO FROM HERE?

Challenging data points will continue to lie ahead for the global economy, but this will inevitably lead to opportunities in certain areas—including industrials, consumer discretionary and emerging markets—to purchase on weakness. We are still cautious on the commodity price outlook, however, given the long-term changes occurring in China, and this informs much of our positioning in the more cyclical areas.

The major cycle-ending risks are always hard to call, and we should acknowledge that cycles rarely come to an end due to mirror images of previous crises. In short, the world evolves, and so should an investor's perspective on today's risks versus those that have caused significant pain in the past.

Rising political tensions and the impact on economic growth, a prospective deterioration in the credit cycle stemming from lower oil prices, and the likelihood of corporate defaults in China stand out as the most prevalent risks. However, further rate increases are now less likely, and monetary policy around the world remains generally accommodative. Bull markets usually end with a broad-based recession or due to valuation bubbles bursting—we see no signs of either.

Given these factors, we remain constructive, but market returns are likely to be more modest. As we have witnessed during the past few years, sentiment is likely to ebb and flow. This will provide opportunities to invest through periods of stock-specific volatility. But while the outlook is more stock-specific and complex than it has been for some time, patient investors should continue to be rewarded over the long term.

INVEST WITH CONFIDENCE®

T. Rowe Price focuses on delivering investment management excellence that investors can rely on—now and over the long term.

To learn more, please visit troweprice.com.

Important Information

This material, including any statements, information, data and content contained within it and any materials, information, images, links, graphics or recording provided in conjunction with this material are being furnished by T. Rowe Price for general informational purposes only. The material is not intended for use by persons in jurisdictions which prohibit or restrict the distribution of the material and in certain countries the material is provided upon specific request. It is not intended for distribution to retail investors in any jurisdiction. Under no circumstances should the material, in whole or in part, be copied or redistributed without consent from T. Rowe Price. The material does not constitute a distribution, an offer, an invitation, recommendation or solicitation to sell or buy any securities in any jurisdiction. The material has not been reviewed by any regulatory authority in any jurisdiction. The material does not constitute advice of any nature and prospective investors are recommended to seek independent legal, financial and tax advice before making any investment decision. Past performance is not a reliable indicator of future performance. The value of an investment and any income from it can go down as well as up. Investors may get back less than the amount invested.

The views contained herein are as of October 2016 and may have changed since that time.

Australia—Issued in Australia by T. Rowe Price International Ltd. (ABN 84 104 852 191), Level 50, Governor Phillip Tower, 1 Farrer Place, Suite 50B, Sydney, NSW 2000, Australia. T. Rowe Price International Ltd. is exempt from the requirement to hold an Australian financial services licence in respect of the financial services it provides in Australia. T. Rowe Price International Ltd. is authorised and regulated by the UK Financial Conduct Authority under UK laws, which differ from Australian laws. For Wholesale Clients only.

Canada—Issued in Canada by T. Rowe Price (Canada), Inc. T. Rowe Price (Canada), Inc.'s investment management services are only available to Accredited Investors as defined under National Instrument 45-106. T. Rowe Price (Canada), Inc. enters into written delegation agreements with affiliates to provide investment management services.

DIFC—Issued in the Dubai International Financial Centre by T. Rowe Price International Ltd. This material is communicated on behalf of T. Rowe Price International Ltd. by its representative office which is regulated by the Dubai Financial Services Authority. For Professional Clients only.

EEA—Issued in the European Economic Area by T. Rowe Price International Ltd., 60 Queen Victoria Street, London EC4N 4TZ which is authorised and regulated by the UK Financial Conduct Authority. For Professional Clients only.

Hong Kong—Issued in Hong Kong by T. Rowe Price Hong Kong Limited, 21/F, Jardine House, 1 Connaught Place, Central, Hong Kong. T. Rowe Price Hong Kong Limited is licensed and regulated by the Securities & Futures Commission. For Professional Investors only.

Singapore—Issued in Singapore by T. Rowe Price Singapore Private Ltd., No. 501 Orchard Rd, #10-02 Wheelock Place, Singapore 238880. T. Rowe Price Singapore Private Ltd. is licensed and regulated by the Monetary Authority of Singapore. For Institutional and Accredited Investors only.

Switzerland—Issued in Switzerland by T. Rowe Price (Switzerland) GmbH ("TRPSWISS"), Talstrasse 65, 6th Floor, 8001 Zurich, Switzerland. For Qualified Investors only.

USA—Issued in the USA by T. Rowe Price Associates, Inc., 100 East Pratt Street, Baltimore, MD, 21202, which is regulated by the U.S. Securities and Exchange Commission. For Institutional Investors only.

T. ROWE PRICE, INVEST WITH CONFIDENCE and the Bighorn Sheep design are, collectively and/or apart, trademarks or registered trademarks of T. Rowe Price Group, Inc. in the United States, European Union, and other countries. This material is intended for use only in select countries.