



Market Uncertainty— Never Comfortable But Potentially Profitable

Bouts of uncertainty have historically created opportunities to generate alpha.

November 2019

KEY INSIGHTS

- A range of factors, both at a broad market level as well as company-specific concerns, are contributing to a general sense of market uncertainty. And with uncertainty comes weakening investor confidence.
- However, for U.S. large-cap growth investors, these periods of market uncertainty have historically provided some of the best opportunities to generate alpha.
- Beyond any short-term uncertainty, U.S. large-cap companies are driving much of the innovation that we are seeing in the market today. This remains an ongoing attraction.



Taymour Tamaddon

*Portfolio Manager, T. Rowe Price US
Large-Cap Growth Equity Strategy*

Any number of factors can combine to generate a broader sense of market or stock-specific uncertainty for investors. These can be macroeconomic or geopolitical concerns, such as the current U.S.-China trade tensions, the moderating growth environment, or a shift in central bank policy. Or they can be more stock specific, with disruptive industry trends as well as operational, regulatory, and competitive factors all coming into play. Ultimately, any uncertainty can lead to an erosion of confidence and weigh on stock market performance.

However, in the U.S. large-cap space—the most efficient part of the most efficient market in the world—these periods of uncertainty have historically provided strong alpha-generating potential. While never exactly comfortable, we see uncertainty as an opportunity.

Seizing Opportunity From Uncertainty

Market uncertainty creates potential pricing dislocation opportunities, as investors will frequently overreact in response to bad news. Whether it is at a broad market level, or specific to certain stocks, uncertainty creates short-term opportunities for long-term investors to potentially take advantage of this dislocation.

Importantly, for the T. Rowe Price US Large-Cap Growth Equity Strategy, we are constantly trying to identify and invest in innovative businesses—companies that, by virtue of their novel ideas, services, or products, have the potential to deliver long-term, compounded growth. These types of companies create potentially industry-disruptive uncertainty, and this is the kind we rush toward.

USD 8 billion+

Market cap of
companies included
within the U.S.

Large-Cap Growth
Equity universe—
equating to roughly
500 stocks.¹

Identifying companies that have these capabilities and potential demands research that goes beyond the day-to-day headlines. News stories create pockets of opportunity; however, it is difficult to make a lot of money from this kind of approach in the large-cap arena. It might be possible to achieve a 1% or 2% gain following a major news story. However, rarely is anything significant gleaned from this short-term “noise” that is ultimately useful in gaining a deeper insight into the company’s long-term growth or profit profile. In our experience, the only way to consistently try to capitalize on uncertainty in the U.S. large-cap sector, is by having a deep understanding of companies’ fundamental businesses and the distinctiveness of proposition they offer.

Looking Beyond the Short-Term Market “Noise”

Facebook is a great example of our approach. The stock fell from USD 210 in mid-2018, to USD 125 over the next six months, largely due to concerns about its approach to data privacy. Poor decision-making in the first instance and a distinct lack of transparency in communications once the issue arose weighed heavily on the stock.

However, looking beyond the immediate negative market reaction, we sought to revisit and retest our initial investment thesis. This involved further analysis into why so many companies use Facebook for their advertising, its principal revenue source. During a series of visits to companies across the country, most confirmed that advertising with Facebook represented the first or second most significant return on their investment. Understanding this, it became clear that the data privacy breach would not, of itself, see companies withdraw what is

effectively their most profitable avenue for growth.

As a long-term investor in Facebook, we also had a good understanding of the potential impact of major issues on daily/monthly average users. In this instance, despite the very public backlash, we observed only a relatively small negative impact on average user numbers.

The combination of these two factors meant that, when the stock price fell sharply, not only were we comfortable holding, but we added to our position during this period of weakness.

Dedicated, Fundamental Research Underpins Conviction Decision-Making

Boeing is another example where we have backed our conviction view through a period of heightened uncertainty for the company. Boeing faced a crisis in the wake of tragic incidents involving its new 737 MAX model aircraft. Through comprehensive research and insights into the sector, we were confident that Boeing could withstand the impact of the crisis.

Our dedicated sector analysts have a deep understanding of the aerospace industry, which is effectively structured as a duopoly. Our research highlighted that a heavy order backlog faces its main competitor, which is unlikely to be able to deliver on any new aircraft orders until around 2024/25. As a result, we felt confident to build our position in Boeing through the period of weakness.

Innovation Remains a Compelling Theme

We continue to field questions from investors and prospects alike, essentially asking if we still feel the U.S. large-cap growth environment is a good place to invest right now. All bias aside, one of the ongoing attractions is the innovation

¹ Source: FTSE/Russell (see Additional Disclosure), as of 30 September 2019. Universe is represented by the Russell 1000 Growth Net 30% Index.

(Fig. 1) U.S. Large-Cap Companies are Driving Innovation

This trend has been reflected in market returns

As of October 11, 2019



Past performance is not a reliable indicator of future performance.

U.S. large-cap growth versus U.S. small-cap cumulative 5-year index performance. Indexes rebased to 100. U.S. Large-Cap = Russell 1000 (EOD) Growth - Price Index, U.S. Small-Cap = Russell RAFI US Small Co - Price Index. Price returns are shown and do not reflect reinvestment of dividends and income. Source: Refinitiv, © 2019 Refinitiv. All rights reserved, analysis by T. Rowe Price.

“...it is predominantly larger companies that are driving today’s market innovation.”

and potential market disruption that is coming from the large-cap area of the U.S. equity market, particularly from companies that are utilizing large data sets to their advantage. And we are not talking about any potential data privacy issues here but rather the analysis of vast sets of accumulated data to improve the consumer experience, for example.

Historically, market disruption has generally started with smaller companies leveraging a new and innovative product or service. However, today data is driving much of the innovation in the market. It takes very large data sets to drive the kind of disruption we are seeing. Given that this volume of data tends to be less available to smaller companies, it is predominantly larger companies that are driving today’s market innovation. This is a trend that has played out significantly over the last five years, with the influence reflected in relative market performance (Fig. 1).

Any use of data must be appropriate and within regulations, but the ability to beneficially utilize data is driving better targeting of advertising, leading to happier customers and improved revenues.

Market uncertainty is likely to remain prominent for the foreseeable future. Macroeconomic and political risks represent potential headwinds to negotiate, while at a company level, disruptive innovation as well as operational, regulatory, and competitive challenges will all continue to be impactful, creating stock-specific uncertainty. Nevertheless, we believe that there are sufficient market drivers in place to continue to support U.S. equities, while any increase in volatility could present attractive buying opportunities as investors will often overreact in this environment, both on the downside and the upside. For strategic, long-term investors, we believe this is a rich landscape.

WHAT WE’RE WATCHING NEXT

The U.S.-China trade dispute continues to weigh on investor sentiment, erode business confidence, and constrain capital spending. In our view, how this dispute evolves over the coming year will play a large part in determining the near-term performance of the U.S. equity market.

The specific securities identified and described do not represent all of the securities purchased, sold, or recommended for the portfolio, and no assumptions should be made that the securities identified and discussed were or will be profitable.

Key Risks—The following risks are materially relevant to the strategy highlighted in this material: Transactions in securities of foreign currencies may be subject to fluctuations of exchange rates which may affect the value of an investment. The portfolio is subject to the volatility inherent in equity investing, and its value may fluctuate more than a portfolio investing in income-oriented securities.

Additional Disclosure

London Stock Exchange Group plc and its group undertakings (collectively, the “LSE Group”). © LSE Group 2019. All rights in the FTSE Russell indexes or data vest in the relevant LSE Group company which owns the index or the data. Neither LSE Group nor its licensors accept any liability for any errors or omissions in the indexes or data and no party may rely on any indexes or data contained in this communication. No further distribution of data from the LSE Group is permitted without the relevant LSE Group company’s express written consent. The LSE Group does not promote, sponsor or endorse the content of this communication.

INVEST WITH CONFIDENCESM

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

T.RowePrice®

Important Information

This material is being furnished for general informational purposes only. The material does not constitute or undertake to give advice of any nature, including fiduciary investment advice, and prospective investors are recommended to seek independent legal, financial and tax advice before making any investment decision. T. Rowe Price group of companies including T. Rowe Price Associates, Inc. and/or its affiliates receive revenue from T. Rowe Price investment products and services. **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 material does not constitute a distribution, an offer, an invitation, a personal or general recommendation or solicitation to sell or buy any securities in any jurisdiction or to conduct any particular investment activity. The material has not been reviewed by any regulatory authority in any jurisdiction.

Information and opinions presented have been obtained or derived from sources believed to be reliable and current; however, we cannot guarantee the sources' accuracy or completeness. There is no guarantee that any forecasts made will come to pass. The views contained herein are as of the date written and are subject to change without notice; these views may differ from those of other T. Rowe Price group companies and/or associates. Under no circumstances should the material, in whole or in part, be copied or redistributed without consent from T. Rowe Price.

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.

Australia—Issued in Australia by T. Rowe Price Australia Limited (ABN: 13 620 668 895 and AFSL: 503741), Level 50, Governor Phillip Tower, 1 Farrer Place, Suite 50B, Sydney, NSW 2000, Australia. 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 ex-UK—Unless indicated otherwise this material is issued and approved by T. Rowe Price (Luxembourg) Management S.à r.l. 35 Boulevard du Prince Henri L-1724 Luxembourg which is authorised and regulated by the Luxembourg Commission de Surveillance du Secteur Financier. For Professional Clients only.

Hong Kong—Issued in Hong Kong by T. Rowe Price Hong Kong Limited, 6/F, Chater House, 8 Connaught Road Central, Hong Kong. T. Rowe Price Hong Kong Limited is licensed and regulated by the Securities & Futures Commission. For Professional Investors only.

New Zealand—Issued in New Zealand by T. Rowe Price Australia Limited (ABN: 13 620 668 895 and AFSL: 503741), Level 50, Governor Phillip Tower, 1 Farrer Place, Suite 50B, Sydney, NSW 2000, Australia. No Interests are offered to the public. Accordingly, the Interests may not, directly or indirectly, be offered, sold or delivered in New Zealand, nor may any offering document or advertisement in relation to any offer of the Interests be distributed in New Zealand, other than in circumstances where there is no contravention of the Financial Markets Conduct Act 2013.

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.

South Africa—T. Rowe Price International Ltd (“TRPIL”) is an authorised financial services provider under the Financial Advisory and Intermediary Services Act, 2002 (FSP Licence Number 31935), authorised to provide “intermediary services” to South African investors.

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

UK—This material is issued and approved 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.

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.

© 2019 T. Rowe Price. All rights reserved. T. ROWE PRICE, INVEST WITH CONFIDENCE, and the Bighorn Sheep design are, collectively and/or apart, trademarks of T. Rowe Price Group, Inc.