US Large-Cap Growth Equity Strategy

EXTRACTING US ALPHA OUTSIDE THE FAANG PHENOMENON

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The much-publicised FAANG stocks – Facebook, Amazon, Apple, Netflix and Google/Alphabet – have been the driving force behind the striking rebound for the US stock market since the depths of the coronavirus panic in March.

Apple has led the way, with its share price climbing 139% since the depths of March, making it the first company to have its market capitalisation reach US$2 trillion. Facebook and Amazon have more than doubled over this period also, rising 108% and 111%, respectively. Meanwhile, Netflix and Google-parent Alphabet have also ridden the recent tech wave, with share price increases of 86% and 63%, respectively.[1]

But the FAANG phenomenon is not just a 2020 story. In our view the sizeable performance of these index heavyweights has helped propel the US stock market to gains far in excess of every other major global index in recent years.

ONLY A QUARTER OF OUTPERFORMANCE

However, as a result of the FAANG dominance, there is a widely held view that alpha generation in the US has solely hinged on whether or not an investor has held active positions in these five tech giants. This is a major misconception.

Of course, as one of the largest active US equity managers in the world, we have shared in the long, medium and short-term success of the FAANG story – with these stocks being a significant driver of performance over the past five years. Indeed, we have been major owners of some of these companies in the T. Rowe Price US Large Cap Growth Equity Strategy for nearly fifteen years.

However, far from just a FAANG play, these five stocks have collectively accounted for only 26% of our outperformance of the benchmark over the past five years – with the vast majority of the alpha generated coming from other sources.[2]

Past performance is not a reliable indicator of future performance.
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.
[1] Source: Financial data and analytics provider FactSet. Copyright 2020 FactSet. All Rights Reserved. % increase from 23 March 2020 to 1 September 2020.
[2] Source T. Rowe Price as at 30 June 2020. Based on analysis of the relative performance of the portfolio versus the indicative benchmark (Russell 1000 Growth Index) as calculated by the FactSet Two-Effect Brinson attribution model. Returns will not match official T. Rowe Price performance because FactSet uses different pricing and exchange rate sources and does not capture intraday trading or fair value pricing. Financial data and analytics provider FactSet. Copyright 2020 FactSet. All Rights Reserved.
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INNOVATION NOT EXCLUSIVE TO FAANGS

The innovative and disruptive FAANGs have transformed industries and rightfully attracted widespread investor attention. These businesses have the characteristics we look for – companies able to take major share within established markets and generate the significant free cash flows that ultimately drive stock prices. In particular, Amazon, Alphabet and Facebook remain among our highest conviction investments.

However, there are many other examples of such innovative companies, aside from the FAANGs, in the technology sector and beyond. Here we highlight three examples from our portfolio:

SNAPCHAT

We have followed Snapchat pre and post IPO and it has continued to innovate and develop its business model – achieving relevance and scale with its target audience. We think Snapchat, which has an impressive 200 million daily active users in the attractive 18-24 age demographic, is well poised to sustain future growth at more attractive margins. It has increased efficiency and margins, with greater scale, through its improved advertiser self-serve toolbox. It also has scope for additional advertisers to join the platform and an opportunity to close the large monetisation revenue gap per user versus the peer group – such as Facebook and Twitter.

CARVANA

Relentless evolution in e-commerce is forcing companies to rethink consumer relationships and the management of image and reputation. We believe the digitally agile Carvana will redefine the buying experience in the highly fragmented US$800 billion US used car market. It uses data to improve the customer experience, while authenticity and trust are drivers of brand engagement.

WIX.COM

We recently took a small position in Wix.com. It is a company we have known for a long time in our small cap portfolios. The company provides website development services to SMBs (small and medium businesses) to establish an online presence to reach and sell to consumers. In our view their disruptive technology, leading market share and innovative customer tools are ready to be monetised. Their freemium offering is experiencing good conversion to paid subscriptions providing good visibility to a high degree of recurring revenue. We expect the total addressable market for these services to grow materially with greater digital adoption and we believe Wix.com’s runway for growth is underappreciated by the market.

While we expect volatility to continue in this uncertain environment, our focus remains on identifying high-quality growth companies that we believe have a competitive advantage. We believe these companies have the potential to generate double-digit earnings growth over time by participating in expanding markets, taking market share, or improving profitability faster than sales. While the FAANGs continue to dominate investor attention, we continue to see numerous stocks well equipped to navigate and thrive in the current unsettled environment.

Performance

US Large-Cap Growth Equity Composite

Figures are calculated in US Dollars

Calendar Years	2015	2016	2017	2018	2019
US Large-Cap Growth Equity Composite (Gross of Fees)	10.74%	3.41%	38.52%	4.89%	29.32%
US Large-Cap Growth Equity Composite (Net of Fees)	10.19	2.90	37.84	4.37	28.68
Russell 1000 Growth IndexΔ	5.67	7.08	30.21	-1.51	36.39
Value Added (Net of Fees)*	4.52	-4.18	7.63	5.88	-7.71

Past performance is not a reliable indicator of future performance.
Gross performance returns are presented before management and all other fees, where applicable, but after trading expenses. Net of fees performance reflects the deduction of the highest applicable management fee that would be charged based on the fee schedule contained within this material, without the benefit of breakpoints. Gross and net performance returns reflect the reinvestment of dividends and are net of all non-reclaimable withholding taxes on dividends, interest income, and capital gains.
Δ Index returns shown with gross dividends reinvested.
* The Value Added row is shown as US Large-Cap Growth Equity Composite (Net of Fees) minus the benchmark in the previous row.

Risks

The following risks are materially relevant to the portfolio.

Small and mid-cap risk - Stocks of small and mid-size companies can be more volatile than stocks of larger companies.

General Portfolio Risks

Capital risk - The value of your investment will vary and is not guaranteed. It will be affected by changes in the exchange rate between the base currency of the portfolio and the currency in which you subscribed, if different.

Equity risk - In general, equities involve higher risks than bonds or money market instruments.

Geographic concentration risk - To the extent that a portfolio invests a large portion of its assets in a particular geographic area, its performance will be more strongly affected by events within that area.

Hedging risk - A portfolio's attempts to reduce or eliminate certain risks through hedging may not work as intended.

Investment portfolio risk - Investing in portfolios involves certain risks an investor would not face if investing in markets directly.

Management risk - The investment manager or its designees may at times find their obligations to a portfolio to be in conflict with their obligations to other investment portfolios they manage (although in such cases, all portfolios will be dealt with equitably).

Operational risk - Operational failures could lead to disruptions of portfolio operations or financial losses.

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