T. Rowe Price®
INVEST WITH CONFIDENCE

Gains still to be found in global equities

Seizing the opportunities that higher volatility and mixed news flow will create

Scott Berg
Portfolio Manager,
Global Growth
Equity Strategy
T. Rowe Price

Equity markets delivered extraordinary returns in 2020, but the first quarter of 2021 will certainly test investors, given the return of uneven and contradictory news flow. Expectations of further monetary and fiscal stimulus, along with positive news on vaccines, have helped support equity markets. However, a new variant of the virus is putting increased pressure on health care systems, and we are seeing more and more countries locking down again. We believe this will have economic repercussions for many and, at a minimum, will defer some of the fundamental rebound investors have been anticipating. We also need to factor in political change. What does the "blue wave transition" in the US mean for companies and policy decisions, especially around taxation and US-China relations?

As we look out to the rest of 2021, we remain optimistic when we analyze the return potential of global equity markets. However, volatility is likely to increase, in part, as higher dispersion within factors, styles, and sectors emerges. For investors to try to make money in this environment, they will have to be more selective and active, which may at times mean taking a more contrarian approach.

"As we look out to the rest of 2021, we remain optimistic when we analyze the return potential of global equity markets."

Navigating through a COVID-On/ COVID-Off environment

We expect the COVID-on/COVID-off trade to continue to flip-flop back and forth as it did through the later stages of 2020. We believe secular growth stocks, at the right price, should continue to compound good returns, but the setup into midyear might imply a continuation of the rotation trade into value, small-caps, and non-US stocks that began toward the end of last year. Certainly, increasing exposure to stocks with earnings sensitivity at this point in the market cycle could potentially reap rewards. But selectivity will remain crucial in a world that remains defined by extreme outcomes.

Further positive news on vaccines would also help those sectors that have been most damaged by the virus, such as travel, leisure, energy, and financials. Indeed, we have been adding individual names to these areas but have been very selective, using our global research platform to identify the best candidates.

"...increasing exposure to stocks with earnings sensitivity at this point in the market cycle could reap rewards."

We have increased our exposure to financials. However, rather than focusing on traditional banks – where zero and negative interest rates continue to hurt balance sheets – we have instead been concentrating on areas such as investment banking, insurance, and investment managers. These are companies that should actually benefit from a lower interest rate environment.

While new vaccines should eventually allow us to exit this pandemic, we believe that many of the trends that have evolved over the course of the past year will endure. COVID-19 has unleashed these trends even further. We expect increased adoption of digital payments, having food delivered to your door, and using technology to connect with each other.

There has been a meaningful step change in the penetration of e-commerce globally, and we believe there is still a long way for this dynamic to go. The advantage for us, as global investors, is that the opportunity set afforded to us allows us to scour all geographies, using our global research platform, to find, in our view, the best investment opportunities.

Looking beyond the US to discover new alpha opportunities

With US equities having performed so strongly, we have been looking for better value elsewhere. Asia-Pacific and Europe are the two places where we have been increasing our exposure. It is our belief that Asia is the place where the gravity of the world is moving toward. It's where markets are deepening the most, where economies have been growing the fastest, and where, currently, the most billionaires are now being created. In that sense, it is where the most unpriced change can be found for investors.

China's recovery from the pandemic has been in stark contrast to developed markets. It is likely to be one of the few countries to see positive economic growth in 2020. More generally, while the emerging market (EM) growth premium has been decelerating for some time and collective earnings have been disappointing, many individual EM economies retain long-term advantages when thinking about potential return generation from equities. Today, our preferred markets are in India, Indonesia, the Philippines, and Peru, while we also have high-conviction positions in Chinese consumer stocks.

We also believe that Europe now looks more attractive. Although it doesn't offer the breadth of high-growth opportunities that the US or China can offer, there are a number of change-driven stocks that we feel confident about in a world that should be marked by improvement, especially from spring 2021 onward – either where stock valuations have fallen sharply, priming them for reversion, or where we have identified fundamental change in a company's earnings profile. Key for us at this point in the equity cycle is the ability to find profits growth, as this remains the most powerful driver of stock prices over the long term.

In a complex macro environment, a stock-specific focus is key

One natural concern is whether equity markets have rebounded too strongly and quickly, especially given the concentration of stock returns. This does create some potential for a broad bubble to form if good news is uninterrupted.

Our view, however, is that although valuations are at a premium in an absolute sense, we are also in a world of unparalleled monetary and fiscal support, which has naturally supported risk assets. Interest rates across the globe are at rock bottom, while at the same time, there is a huge wall of money looking for a home. On that basis, we don't believe that valuations are extreme, and equity markets will continue to offer opportunity, especially relative to alternatives.

"...we don't believe that valuations are extreme, and equity markets will continue to offer opportunity, especially relative to alternatives."

The environment, however, is inherently more stock-specific than it has been for some time. 2021 is likely to present opportunities to invest on bouts of volatility. This is certainly likely if conditions worsen before they get better, and we believe there will certainly be data points for market bears to point to in the coming months ahead.

There are also clear concerns in the market that, beyond monetary support, there is no fundamental improving "bull" case for global equities. However, this aggregate top-down perspective on the world belies the ongoing breadth of stock-specific fundamentals we continue to find, especially in secular growth stocks benefiting from changes in society and in our economy.

A world of dispersed valuations and corporate outcomes is ultimately beneficial to active investors, and we shall look to exploit those factors for our clients in 2021.

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. The portfolio may include investments in the securities of companies listed on the stock exchanges of developing countries.

Important Information

This material is being furnished for general informational and/or marketing purposes only. The material does not constitute or undertake to give advice of any nature, including fiduciary investment advice, nor is it intended to serve as the primary basis for an investment decision. 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.

EEA – 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.

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

ID0003967 (01/2021)

202101-1479563