Q3 2017 | Putnam Growth Opportunities Fund and Putnam Multi-Cap Growth Fund Q&A

What do stocks need to maintain their strength?

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Industry since 1999

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As we enter the final quarter of 2017, what is your perspective on equity markets?

The behavior of equity markets this year has been unusual in many respects. U.S. economic growth has been underwhelming, inflation is stagnant, and the 10-year Treasury yield has been much lower than we expected it to be at this point. Many investors, myself included, overestimated the ability of the Trump administration to make progress on pro-growth legislation, and the “reflation trade” has gone nowhere. Despite all this, equities in both U.S. and world markets continued to deliver solid gains.

Performance has been dominated by a narrow group of stocks. Do you anticipate a change any time soon?

That has been another unusual characteristic of this year’s market. Like many of our expectations at the start of 2017, the general belief that value would begin to take the lead over growth proved to be incorrect — dramatically so. Growth stocks have outperformed value stocks by a surprisingly wide margin, with most of the gains coming from just two sectors: technology and health care.

I am optimistic that 2018 could bring more balanced performance between growth and value. At some point, sectors such as financials and industrials — and possibly materials and energy — should get back some of the performance advantage they have yielded to technology and health care. It may require a further boost in U.S. economic growth, as well as catalysts such as progress on corporate tax reform, which could encourage businesses to increase their capital expenditures.

Deregulation could be another positive influence. Despite the failings with its legislative agenda, the Trump administration still has the power to directly lower regulatory barriers — and it is doing so. I believe business leaders are still in the process of responding positively to this, which has implications for investment and capital formation in the private sector.

What else could help stocks advance further after such a long run of gains?

Corporate profitability needs to stay strong. Earnings from U.S. businesses have been a key contributor to the strength of equities this year. Earnings growth has improved significantly over 2016, and we just had a second consecutive quarter of double-digit growth for the first time since 2011.

Beyond earnings, I believe the most encouraging factor for equities today may be the impressive level of synchronized global economic improvement. Regional equity markets often stumble as a result of serious economic woes elsewhere — recall the eurozone debt problems of 2010 and 2012 or the China slowdown fears in 2016. Today, however, we have decent economic conditions in the United States, improvement in Europe, and impressive growth in China and many other emerging markets. Global economic variables are more in sync now than at almost any other time since the Great Recession. Positive economic data from most regions worldwide have been a key feature of 2017, and may serve as a catalyst for equities into 2018.

Turning to your portfolios, what helped performance in the third quarter, and where are you focused in the months ahead?

Interestingly, if I had let macro trends drive my decisions, I may have shifted away from the areas that have performed so well in 2017. Instead, I continued my bottom-up focus on the characteristics of individual companies, looking at their growth prospects, the durability of that growth, the end markets they are pursuing, and how their stocks are valued in relation to their growth potential. Macroeconomic factors are part of the analysis, but they are not the dominant part.

Within the fund portfolios in the third quarter, the leaders, by far, were technology and health-care stocks. These holdings benefited from the overall outperformance of the sectors, but my decision to own them was based on fundamental research. One highlight has been stocks of Chinese internet companies. Several of these companies rival the U.S. internet powerhouses in terms of scale and scope, and we continue to expect strong performance from them in the years ahead.

On the flip side of the internet equation, we have seen underwhelming results from a number of consumer staples stocks. I have de-emphasized them throughout the year, and I remain quite cautious about them going forward. In general, many companies are struggling to adapt their business models to the dramatic changes in technology, consumer buying patterns, and online retailing. Through our research, we are working to find companies with niche products or services that may give them a competitive edge over online competitors.

Putnam Growth Opportunities Fund (PGOYX)

Annualized total return performance as of 9/30/17

Class Y shares Inception 7/1/99	**Net asset value**	**Russell 1000 Index**
Last quarter	6.23%	5.90%
1 year	23.18	21.94
3 years	11.63	12.69
5 years	15.90	15.26
10 years	9.78	9.08
Life of fund	7.95	8.42

Total expense ratio: 0.77%

Putnam Multi-Cap Growth Fund (PNOYX)

Annualized total return performance as of 9/30/17

Class Y shares Inception 7/19/94	**Net asset value**	**Russell 3000 Index**
Last quarter	5.80%	5.93%
1 year	22.95	21.87
3 years	11.36	12.65
5 years	15.64	15.18
10 years	8.05	9.03
Life of fund	11.75	9.73

Total expense ratio: 0.80%

Returns for periods of less than one year are not annualized.

Recent performance may have benefited from one or more legal settlements.

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