

Q3 2021 | Putnam Small Cap Growth Fund Q&A

Fund outperforms in challenging quarter for small caps



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Industry since 1996

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How did the fund perform in the third quarter?

For the quarter, the fund outperformed its benchmark, the Russell 2000 Growth Index. The fund also outperformed for the 1-, 3-, 5-, and 10-year periods ended September 30, 2021. Third-quarter outperformance was almost entirely driven by stock selection. Holdings in healthcare and information technology contributed most to returns while financials and energy stocks detracted by modest amounts.

How did small-cap growth stocks perform relative to other styles?

During the quarter, we saw continued gyrations in the small-versus-large and growth-versus-value performance trends. Among small-cap stocks, value outperformed growth for the quarter.

How were investing conditions overall in the quarter?

There was limited good news in the marketplace during the third quarter. While there is always a list of things to worry about, this quarter's seemed longer and more severe than most. Leading the list were rising cases of the Delta variant of Covid-19 around the globe. In addition, the Chinese investing landscape remained a bit unsettled due to fears of a large potential bankruptcy in the real estate area. This compounded prior concerns about the regulatory oversight of many Chinese technology companies. In the United States, we saw surging transportation costs and shipping delays as well as ongoing microchip shortages. The chip shortages will affect many businesses, but the pain seems especially acute in auto production. Other challenges included labor shortages in areas like homebuilding and restaurants, which slows the economic recovery.

On top of these issues, we also saw “normal” disruptive events like hurricanes and flooding. These seemed to put added stress on supply chains, which were too tight to handle such disturbances. With this backdrop, we saw a minor flight to quality. Large-cap stocks that were perceived as safer tended to outperform small-cap stocks.

What is your outlook for the months ahead?

As we enter the final quarter of 2021, we are starting to see negative earnings revisions, which we haven't seen in a while. Coming out of the pandemic-induced disruptions, companies had been routinely beating conservative earnings assumptions. The market is now faced with the prospect that the “reopening upside” may not be as great as many anticipated, at least in select areas of the economy.

However, we believe most of these issues are somewhat temporary in nature. They should get worked out with the passage of time, and in our view, the future remains quite bright. In this environment, we continue to focus on what drives stock prices over longer time periods, which is the long-term growth in profits. We then apply that to our active, fundamental research of individual companies.

Putnam Small Cap Growth Fund (PSYGX)

Annualized total return performance as of 9/30/21

	Class Y shares Inception 11/3/03	Russell 2000 Growth Index
Last quarter	4.00%	-5.65%
1 year	36.12	33.27
3 years	21.60	11.70
5 years	22.81	15.34
10 years	18.99	15.74
Life of fund	12.80	7.84

Total expense ratio: 0.99%

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

Current performance may be lower or higher than the quoted past performance, which cannot guarantee future results. Share price, principal value, and return will vary, and you may have a gain or a loss when you sell your shares. Performance of class Y shares assumes reinvestment of distributions and does not account for taxes. Class Y shares, available to investors through an asset-based fee program or for institutional clients, are sold without an initial sales charge and have no CDSC. Performance for class Y shares before their inception are derived from the historical performance of class A shares (inception 12/31/97), which have not been adjusted for the lower expenses; had they, returns would have been higher. Recent performance may have benefited from one or more legal settlements. For the most recent month-end performance, please visit putnam.com.

The Russell 2000 Growth Index is an unmanaged index of those companies in the small-cap Russell 2000 Index chosen for their growth orientation. Frank Russell Company is the source and owner of the trademarks, service marks, and copyrights related to the Russell Indexes. Russell® is a trademark of Frank Russell Company. You cannot invest directly in an index.

For informational purposes only. Not an investment recommendation.

The views and opinions expressed are those of the portfolio manager, as of September 30, 2021. They are subject to change with market conditions and are not meant as investment advice.

Consider these risks before investing: Investments in small and/or midsize companies increase the risk of greater price fluctuations. Growth stocks may be more susceptible to earnings disappointments, and the market may not favor growth-style investing.

The value of investments in the fund's portfolio may fall or fail to rise over extended periods of time for a variety of reasons, including general economic, political, or financial market conditions; investor sentiment and market perceptions;

government actions; geopolitical events or changes; and factors related to a specific issuer, geography, industry, or sector. These and other factors may lead to increased volatility and reduced liquidity in the fund's portfolio holdings. These risks are generally greater for small and midsize companies. From time to time, the fund may invest a significant portion of its assets in companies in one or more related industries or sectors, which would make the fund more vulnerable to adverse developments affecting those industries or sectors.

Our investment techniques, analyses, and judgments may not produce the outcome we intend. The investments we select for the fund may not perform as well as other securities that we do not select for the fund. We, or the fund's other service providers, may experience disruptions or operating errors that could have a negative effect on the fund. You can lose money by investing in the fund.

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Request a prospectus or summary prospectus from your financial representative or by calling 1-800-225-1581. The prospectus includes investment objectives, risks, fees, expenses, and other information that you should read and consider carefully before investing.