T. ROWE PRICE INSIGHTS
ON GLOBAL EQUITIES

Crisis Playbook (Part II)—The Power of “Stop Getting Worse”

Looking beyond to find the best outcomes for clients.

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We believed the coronavirus would spread, so we acted early. We moved to reduce risks in the portfolio that weren’t conducive to the deteriorating backdrop, and we neutralized balance sheet issues as much as possible. We leveraged our global research platform to focus on the stocks we want to own as this crisis deepens, but also for when we come out on the other side.

If you are going to de-risk, you need to do it early. Why? Because as any crisis unfolds, the longer-term opportunities become potentially compelling. This crisis is no different.

We believe the Global Focused Growth Equity Strategy is a tool that offers exposure to compelling investment ideas, always balancing conviction at the stock level with risk mitigation individually and collectively. We have made changes to the strategy in the past few weeks and, importantly, feel good about how it is positioned today for the medium to long term.

Short-Term Pain

We believe the world will enter a recession in the next one to two quarters. The freezing of economic activity is too powerful for the global economy to withstand without a significant impact. But I believe it will be a different kind of recession. It will involve a fundamental disconnect between longer-term economic value (the present value of free cash flow) and the acute impact of short-term financial obligations (rent, interest and principal payments, payrolls, etc.). This is not a debt crisis, or in any way a normal economic cycle, because of the root cause.

Stocks typically bottom when the economic environment “stops getting worse,” not when economic or earnings data are trending better. Given this, we need to focus on signs that indicate when it will “stop getting worse” as opposed to focusing on the elimination of all risk until things get better.

We believe there are three key signposts to look out for:

1. **Massive and virtually unconstrained fiscal and monetary stimulus.**

   Already, we are seeing this scenario rapidly unfold globally. Governments and policymakers have learned the

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lessons of the global financial crisis. Stimulus is necessary to bridge the gap between longer-term economic value and short-dated financial obligations. In the same way I will personally support my local restaurant through this crisis, we expect governments to support jobs in their individual countries. To this end, huge fiscal and support packages are being planned or announced around the world. Crisis causes change, and fiscal and monetary support is needed along with lower interest rates. Governments have the will and the balance sheets to do this.

2. **Treatment and testing for the virus.**

   Although a vaccine is not likely in the short term, treatments should begin to improve over the coming months, and testing will become more ubiquitous. Our health care research team has been doing amazing work analyzing progress in these areas and mapping out likely outcomes.

3. **Peaking infection rates.**

   Things will get worse, especially for the developed world that is behind China and the rest of Asia. For some countries, the "peak of this virus" is yet to come, and we will see more and more restrictive measures implemented. However, there should be a strong correlation between peaking infection rates and troughing stock prices. U.S. infection rates should peak in the next couple of months, based on an acceleration of quarantine restrictions and social distancing. If people take this seriously, we know that infection rates will peak, with the experience in Asia providing a useful guide.

All three of these signposts are indicators that can signal the emergence of a "stop getting worse" period—the peak of the crisis. Stocks are likely to bottom as these factors align, and we want to be positioned appropriately.

Look to the Future

Looking beyond the immediate disruption to the global economy, we must imagine dealing with this virus over the longer term and how the world might change. We believe there is a high probability that a vaccine will be developed. We have faith in science and human ingenuity. But this could be 12 months or more away. In the meantime, some businesses will recover quickly as the crisis normalizes, while others will take longer. It is important to be focused on those that can recover fastest, but at the same time, we need to understand the real value of companies that may take longer and then pick our spots for investment.

We also want to be focused on companies that see accelerated fundamental momentum within their industries directly resulting from the coronavirus shock. This crisis is going to allow for experimentation that could potentially translate to longer-lasting behavioral changes within society. If we can use our global research platform to identify companies that will benefit from this, we can be ahead of the curve. Many of these companies are likely to be in the technology and health care space.

Finally, what does massive fiscal and monetary stimulus mean for interest rates and the financials sector? Do we begin to see crowding out? Do government demand for cash and friction in the economy lead to inflation and higher interest rates, contrary to the forces of technology unlocking capacity and demographics pressuring deflation? This all needs to be worked out.

As I noted in my last blog, T. Rowe Price Insights: *Crisis Playbook—The Fear of Loss and Regret*, my experience is that investors often regret not buying

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great assets in times of crisis. While being respectful of risk control, both our experience and investment framework tell us that if we focus on great assets on the right side of change, we can potentially reap rewards over the long term.

The recession will cause economic hardship, and its origin is clearly frightening. The question we face day to day is how to invest around the circumstances to best help our clients.

Our aim remains the same—to provide our clients with a vehicle to capitalize on the long-term value creation of great companies while at the same time balancing risk and reward.

This is the time for active management to shine, both in mitigating risk on the downside, but also in creating value as we work our way through this crisis to the other side.

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