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BEST ETFS & MUTUAL FUNDS

# Hot Putnam Fund Isn't Afraid Of Fed Regulators Or China's Military Threat

Q&A

**BY PAUL KATZEFF**
INVESTOR'S BUSINESS DAILY

One of the best mutual funds isn't afraid of federal regulators breaking up Google-parent Alphabet **(GOOGL)**, or of China's military threat against a major chipmaker, or of Tesla's **(TSLA)** recent price pullback.

The fund is the $8.3 billion Putnam Growth Opportunities Fund **(POGAX)**. And the reason for its courage in the face of each of those risks is coolheaded logic.

Growth Opportunities co-managers Richard Bodzy and Greg McCullough stick by those stocks — like all of their holdings — because they fit the fund's investment strategy. Crucially, they are a breed of marathon champions.

Not only is their earnings growth above average. That growth is durable.

Why does durability matter? Because rival investors are more likely to misprice stocks' growth the further out in time they're trying to forecast that growth.

That's led Bodzy and McCullough to build a diverse portfolio that includes car and battery maker Tesla **(TSLA)**.

It also includes Taiwan Semiconductor **(TSM)**, arguably the world's most important contract chipmaker.

And the portfolio includes economic recovery plays Walt Disney **(DIS)**, Airbnb **(ABNB)** and DraftKings **(DKNG)**. Unlike many money managers, Bodzy and McCullough don't claim to ignore macro factors as they execute their investment strategy.


**Putnam managers Richard Bodzy and Greg McCullough, right, seek stocks with durable growth like Microsoft.**

Moves like those have worked well for the fund. The fund is a 2021 IBD Best Mutual Funds Awards winner. It won in three categories. In each, it topped the S&P 500 in calendar 2020 as well as over the prior three, five and 10 years on an average-annual-return basis.

In fact, its 2020 return more than doubled the S&P 500's, 38.41% vs. 18.4%.

Bodzy, whose 40th birthday is nearing, and McCullough, whose 43rd birthday is coming up, spoke with IBD about their investment approaches while in South Carolina and New Hampshire, respectively, away from their Boston offices.

**IBD:** What is this fund's investment strategy, in a nutshell?

**Richard Bodzy:** We invest in companies with above-market growth, with durations. And typically these companies are aided by a multiyear secular theme.

**IBD:** Does "duration" mean they must be capable of sustaining their growth long-term?

**Bodzy:** We're looking for companies that can grow at above-market rates, and do so with a multiyear time horizon.

**IBD:** Since you don't seek the very fastest growers, what's the rationale for seeking that long-term growth?

**Greg McCullough:** The market from time to time underestimates the growth capability of a business in the short term. But it underestimates a company's ability to grow over a long period more often.

**IBD:** Which creates buying opportunities for you?

**McCullough:** Exactly.

**IBD:** Which secular themes do you play?

**McCullough:** There are 11. There's 5G connectivity and the Internet of Things, Amazon's influence, autonomous and electric vehicles, and cloud infrastructure and software.

The fifth one is "controlled distribution," which refers to the increasing number of retail-


Alphabet CEO Sundar Pichai testified at a House antitrust hearing.

brand owners that sell products through their own stores or websites. They have few if any third-party sales. They rarely have markdowns. The advantage is that it allows businesses to better control inventory, pricing, promotion and brand presentation. It also leads to a better relationship with end customers.

The sixth is digital marketing. That's related to others, like e-commerce and digital payment processing.

Then there is the humanization of pets. Another is the time that people spend in front of computer and smartphone screens. Personalized medicine is another. Finally, effects of the Covid-19 virus.

**IBD:** How is the fund playing the economic rebound that seems imminent?

**Bodzy:** We're staying within process and investing in some of the best growth companies in the world. Over an appreciable time horizon, call it three-plus years, growth companies are where investors will want to be.

But on the margin, an economic reopening will likely occur throughout 2021. As a result, most recent names added to the fund have not only fit our criteria, but also have a benefit from an economic reopening.

**IBD:** Such as?

**Bodzy:** Disney is a name that we bought in the second half of 2020. Over 35% of their EBIT, earnings before interest and taxes from the theme parks, are temporarily underearning their potential.

We think they'll bounce back as the economy reopens. We also like it for the Disney+ asset, which we think can have over 300 million subscribers "much like Netflix **(NFLX)**" over a few years. In addition, it can be cash flow positive in a couple of years as well.

**IBD:** What's another recent rebound play?

**Bodzy:** We participated in Airbnb's initial public offering in 2020. We've been there the whole time and actually made our stake larger. They're the industry leader in an area that should really benefit from hybrid work environments and workplace flexibility and pent-up demand to travel, which should also help Disney.

Their market-share lead is growing at a fast pace. We think profitability will be very meaningful in a couple years.

**IBD:** What's a third stock that should benefit from the public being able to resume normal activities?

**Bodzy:** DraftKings is a pure play on U.S. sports betting legalization across most of the country in coming years. They have a tremendous platform and meaningful market share. And obviously you need fans being engaged to have more wagering. We think that'll heighten as the economy reopens.

**IBD:** Are you reacting to the prospect of heightened regulation of Big Tech platforms?

**McCullough:** It's fairly clear from the president's comments and folks he's putting in place that technology-sector regulation will be a focus of the administration. We're underweight the FAANG stocks and some other big megacap tech companies. We've been underweight in the FAANG complex for a long period. That underweight has gotten bigger in recent months.

**IBD:** What are your main concerns?

**McCullough:** Not every megacap tech name has the same risk of regulation. We size positions accordingly.

Among its megacap tech peers, Microsoft **(MSFT)**, we view Microsoft as the least likely to be affected by increased antitrust scrutiny.

Microsoft has been reinvented under CEO Satya Nadella. They're far more open to partnerships. That's what's driving growth. They sit at the crossroads of lots of megatrends within technology.

Azure, its cloud business, is the crown jewel. It's a $30 billion business that's growing at nearly 50% a year. We expect that to continue well into the future. Microsoft generates $50 billion of free cash flow a year. They're compounding earnings and free cash flow in the double digits.

**IBD:** I imagine that Alphabet faces greater regulatory risk. The worst-case scenario is breakup. Do you think it faces that?

**Bodzy:** Google's compilation of consumer data and dominant market position do put the company at greater risk of regulation than many businesses and even many other large-cap tech companies such as Microsoft. But we do not, however, believe the company is at serious risk of being broken up. We think it would be very difficult to disentangle the parts of Alphabet in a breakup, and we're not sure that doing so would benefit consumers.

IBD: Name a key driver for Alphabet that many people might not fully appreciate?

**McCullough:** Alphabet's Waymo (Alphabet's autonomous driving technology development company) and Verily (its life-sciences arm) will likely become disruptors over the long-term.

They're like owning call options on Alphabet. They're call options in the sense that they represent a very small part of Alphabet's overall revenue and market value today. But they are disruptors in massive markets — automotive transportation and health care — and they could become much larger contributors in the future if they are able to execute on the business plans.

**IBD:** Tesla's car production rose in 2020. Revenue from China car sales are way up. The firm says its new electric vehicle factory near Berlin will be trendsetting. Yet Tesla share price is off more than 20% since January. Still, you're bullish. Why?

**Bodzy:** Our fundamental view of Tesla hasn't changed. We made our initial purchase in early 2020. We increased our position substantially in the second half.

Tesla is a potential beneficiary of Biden policies. The company has a strong brand and is differentiated from other auto manufacturers. The bet here is that over time the business scales up and battery costs are reduced. Ultimately, there can be meaningful profitability. We've already seen them achieve free-cash-flow positive results. Over the long term, profitability can be enhanced in a significant way.

**IBD:** PayPal **(PYPL)** of course is at the crux of your e-commerce and digital payments theme. What gives it legs?

**McCullough:** We expect high-teens revenue growth and 20%-plus earnings per share growth over the next three to five years.

It has further upside potential from its ability to monetize Venmo (its peer-to-peer payment platform), as well as from its underleveraged balance sheet and from initiatives into buy-now-pay-later arrangements with partners.

**IBD:** Tensions are rising between the U.S. and China. And China keeps threatening Taiwan, where the company Taiwan Semiconductor is based. Given the global computer chip shortage, are you concerned about a possible Chinese invasion of Taiwan for broad political reasons, which incidentally would leave the world's leading semiconductor manufacturer in the hands of China?

**McCullough:** TSM has established itself as the dominant semiconductor outsourcer. It is a critical partner of companies like Apple **(AAPL)**, Qualcomm **(QCOM)**, Broadcom **(AVGO)** and Nvidia **(NVDA)**. The world couldn't function without TSM chips.

The company is doing what we consider prudent by expanding its manufacturing footprint, including a new factory in Arizona.

TSM chips increasingly are part of industrial products and applications. We expect that criticality to be a big driver of growth into the future.

**IBD:** Dynatrace **(DT)** makes computer network monitoring tools. Is its key driver rising demand for those tools as companies move their apps to the cloud?

**Bodzy:** We've owned Dynatrace since its IPO in July 2019. We expect the company to grow its top line 25% to 35% for the next four years. You're right, Dynatrace is a company that's been coming out the other side of the pandemic stronger, and more competitively advantaged.

And what's even more attractive, the company is able to deliver this revenue growth, again, with free cash flow margins well above 25%, due to a highly efficient operating model. Its developer base allows a lower percentage of research and development relative to peers for structurally higher margins.

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Putnam INVESTMENTS

★★★★

The fund received a 4-star Overall Morningstar Rating as of 6/30/21 among 1,138 funds in the Large Growth category (Y shares, based on risk-adjusted returns)

**Richard E. Bodzy**
Portfolio Manager
(industry since 2004)

**Gregory D. McCullough, CFA**
Portfolio Manager
(industry since 2008)

**Objective**
The fund seeks capital appreciation.

**Morningstar category**
Large Growth

**Lipper category**
Large-Cap Growth

**Benchmark**
Russell 1000 Growth Index

**Fund symbols**

| | |
|---|---|
| Class A | POGAX |
| Class B | POGBX |
| Class C | POGCX |
| Class R | PGORX |
| Class R6 | PGOEX |
| Class Y | PGOYX |

**Net assets**
$9,515.33M

**Number of holdings**
55

**Turnover**
45%

**Not FDIC insured**
**May lose value**
**No bank guarantee**

# Putnam Growth Opportunities Fund

## Seeking to harness the growth potential of large U.S. companies

### Seeks above-average growth

The fund focuses on businesses that exhibit both a high level of growth and an above-average duration of growth.

### A thematic approach

The portfolio managers combine top-down investment themes with bottom-up research to select securities that can benefit from growth trends.

### Rigorous analysis

Backed by fundamental research, the managers focus on identifying management teams that act like owners.

### Top ten holdings

| | |
|---|---|
| Microsoft | 9.57% |
| Apple | 8.04 |
| Amazon | 7.43 |
| Alphabet | 5.51 |
| Facebook | 3.87 |
| PayPal | 3.63 |
| NVIDIA | 3.13 |
| Visa | 3.08 |
| Mastercard | 2.88 |
| Adobe | 2.67 |

Holdings represent 49.81% of the portfolio and will vary over time.

### Sector weightings

| | Underweight | Overweight | Portfolio | Benchmark |
|---|---|---|---|---|
| Consumer discretionary | | 2.8 | 21.3% | 18.5% |
| Communication services | | 1.2 | 13.8 | 12.6 |
| Health care | | 0.9 | 10.0 | 9.1 |
| Industrials | | 0.6 | 7.0 | 6.4 |
| Materials | | 0.5 | 1.5 | 1.0 |
| Financials | | 0.3 | 2.6 | 2.3 |
| Utilities | | 0.0 | 0.0 | 0.0 |
| Energy | -0.3 | | 0.0 | 0.3 |
| Real estate | -0.4 | | 1.3 | 1.7 |
| Consumer staples | -2.6 | | 1.3 | 3.9 |
| Information technology | -3.8 | | 40.3 | 44.1 |

Cash and net other assets represent 1.1% of the portfolio.

Allocations will vary over time. Due to rounding, percentages may not equal 100%.

The unclassified sector, where applicable, includes exchange-traded funds and other securities not able to be classified by sector

### Top active weights

| Top 5 overweights | Portfolio | Benchmark | Over/under |
|---|---|---|---|
| PayPal | 3.6% | 1.6% | 2.0% |
| UnitedHealth | 1.6 | 0.1 | 1.5 |
| Danaher | 1.5 | 0.0 | 1.5 |
| Mastercard | 2.9 | 1.5 | 1.4 |
| Adobe | 2.7 | 1.3 | 1.4 |

| Top 5 underweights | Portfolio | Benchmark | Over/under |
|---|---|---|---|
| Apple | 8.0% | 10.2% | -2.2% |
| AbbVie | 0.0 | 0.9 | -0.9 |
| Broadcom | 0.0 | 0.9 | -0.9 |
| Netflix | 0.2 | 1.1 | -0.9 |
| PepsiCo | 0.0 | 0.8 | -0.8 |

### Risk

| | Beta | Tracking error | Up capture ratio | Down capture ratio |
|---|---|---|---|---|
| Y share (as of 6/30/21) | 0.95 | 2.82% | 100.51% | 92.37% |

The Russell 1000 Growth Index is an unmanaged index of those companies in the large-cap Russell 1000 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.

**Capture ratios** are used to evaluate how well an investment manager performed relative to an index during specific periods (periods of positive return in the case of up capture, negative return in the case of down capture). The ratio is calculated by dividing the manager's returns by the returns of the index during the period and multiplying that factor by 100. **Turnover** is the rate at which the fund buys and sells securities each year. For example, if a fund's assets total $100 million and the fund bought and sold $100 million of securities that year, its portfolio turnover rate would be 100%. **Beta** is defined as a fund's sensitivity to market movements and is used to evaluate market related, or systematic, risk. It is a historical measure of the variability of return earned by an investment portfolio. Risk statistics are measured using a 5-year regression analysis. For funds with shorter track records, Since Inception analysis is used. **Tracking error** assesses how closely a fund's performance tracks that of the fund's benchmark by calculating the standard deviation of the difference between the fund's returns and its benchmark returns over a given time period, typically 5 years.

Not all share classes are available on all platforms.

**Morningstar rankings**

(Y shares, based on total return)

| | |
|---|---|
| 1 year | 87% (1081/1239) |
| 3 years | 21% (243/1138) |
| 5 years | 15% (145/1024) |
| 10 years | 20% (142/761) |

**Total expense ratio**

(Y shares)
0.80%

(A shares)
1.05%

**Adjustable management fee examples**

(Y shares, based on performance versus benchmark)

| | |
|---|---|
| Base fee | 0.54% |
| Higher fee after 1% outperformance | 0.57% |
| Lower fee after 1% underperformance | 0.51% |
| Maximum performance adjustment | +/-0.12% |

**Market-cap breakdown**

| | |
|---|---|
| Over $95B | 74.50% |
| $22B–$95B | 21.70% |
| $4.7B–$22B | 2.72% |
| $1.5B–$4.7B | 0.00% |
| Less than $1.5B | 0.00% |
| Cash and other assets | 1.08% |

"Cash and other assets" includes cash, short-term securities, ETFs, bonds excluding convertible bonds, and other securities not able to be classified by market capitalization.

## Annual performance (all distributions reinvested)

| | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 YTD |
|---|---|---|---|---|---|---|---|---|---|---|
| Y shares at net asset value | 18.0% | 36.9% | 13.9% | 1.3% | 6.6% | 31.3% | 2.6% | 36.7% | 38.8% | 11.7% |
| A shares before sales charge | 17.7 | 36.6 | 13.6 | 1.1 | 6.3 | 31.0 | 2.3 | 36.4 | 38.4 | 11.6 |
| Benchmark | 15.3 | 33.5 | 13.1 | 5.7 | 7.1 | 30.2 | -1.5 | 36.4 | 38.5 | 13.0 |

## Annualized total return performance

| | 1 year | 3 years | 5 years | 10 years | Life of fund |
|---|---|---|---|---|---|
| Y shares (Inception 7/1/99) | 35.41% | 25.47% | 25.14% | 17.82% | 10.30% |
| A shares (Inception 10/2/95) before sales charge | 35.09 | 25.16 | 24.82 | 17.53 | 10.05 |
| A shares after sales charge | 27.32 | 22.71 | 23.35 | 16.84 | 9.80 |
| Benchmark | 42.50 | 25.14 | 23.66 | 17.87 | 10.61 |

**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 A and Y shares assumes reinvestment of distributions and does not account for taxes. After-sales-charge returns for class A reflect a maximum 5.75% load. Returns for class Y shares prior to their inception are derived from the historical performance of class A shares, which have not been adjusted for their lower expenses; had they, returns would have been higher. 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. For the most recent month-end performance, please visit putnam.com.**

Because the dollar amount of the monthly performance fee adjustment is based on the fund's average assets during the rolling performance period, the amount of any dollar adjustment as a percentage of a fund's current assets could exceed the "maximum annualized performance adjustment rates." Performance fee adjustments will not commence until a fund has been operating under a shareholder-approved management contract with a performance fee adjustment for at least 12 months.

The Morningstar Rating™ for funds, or "star rating," is calculated for managed products (including mutual funds, variable annuity and variable life subaccounts, exchange-traded funds, closed-end funds, and separate accounts) with at least a three-year history. Exchange-traded funds and open-ended mutual funds are considered a single population for comparative purposes. It is calculated based on a Morningstar Risk-Adjusted Return measure that accounts for variation in a managed product's monthly excess performance, placing more emphasis on downward variations and rewarding consistent performance. The top 10% of products in each product category receive 5 stars, the next 22.5% receive 4 stars, the next 35% receive 3 stars, the next 22.5% receive 2 stars, and the bottom 10% receive 1 star. The Overall Morningstar Rating for a managed product is derived from a weighted average of the performance figures associated with its three-, five-, and 10-year (if applicable) Morningstar Rating metrics. The weights are: 100% three-year rating for 36-59 months of total returns, 60% five-year rating/40% three-year rating for 60-119 months of total returns, and 50% 10-year rating/30% five-year rating/20% three-year rating for 120 or more months of total returns. While the 10-year overall star rating formula seems to give the most weight to the 10-year period, the most recent three-year period actually has the greatest impact because it is included in all three rating periods. Ratings do not take into account the effects of sales charges and loads. Putnam Growth Opportunities Fund received 4, 4, and 4 stars for the 3-, 5-, and 10-year periods among 1,138, 1,024, and 761 Large Growth funds, respectively.

Morningstar rankings for class Y shares are based on total return without sales charge relative to all share classes of funds with similar objectives as determined by Morningstar. Morningstar rankings may differ significantly from Morningstar's risk-adjusted star ratings. Past performance is not indicative of future results.

**Consider these risks before investing:** 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. 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.

**Request a prospectus or a summary prospectus, if available, from your financial representative or by calling Putnam at 1-800-225-1581. These prospectuses include investment objectives, risks, fees, expenses, and other information that you should read and consider carefully before investing.**

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