Q1 2021 | Putnam Large Cap Value Fund Q&A

# Value rally continues in first quarter

**Darren A. Jaroch, CFA**
*Portfolio Manager*
Industry since 1996

**Lauren B. DeMore, CFA**
*Assistant Portfolio Manager*
Industry since 2002

***The fund outperformed the benchmark for the 1-, 3-, 5-, and 10-year periods ended March 31, 2021.***

***Despite their recent outperformance, value stocks continue to trade at a significant discount to growth stocks.***

***Over the next 12 months, we believe we should see assets flowing into the economy due to a burst of spending from both businesses and consumers.***

Effective March 30, 2021, the fund's name changed from Putnam Equity Income Fund.

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

### How has the fund performed?

**Darren:** For the first quarter, the fund slightly underperformed its Russell 1000 Value benchmark. From a longer-term perspective, the fund outperformed the benchmark for the 1-, 3-, 5-, and 10-year periods ended March 31, 2021.

### Value stocks have outperformed growth stocks for several months. What are the drivers of this market rotation?

**Darren:** A key development that sparked the value rally was the announcement last November of impressive efficacy results in Covid-19 vaccine trials. At the same time, valuation spreads in the market — the difference between the cheapest and most expensive stocks — had reached historic wide levels. This set the market up for the rotation into value stocks that has continued into 2021. The rally was boosted further by the rollout of three effective Covid-19 vaccines, optimism about the reopening of economies, and significant government stimulus, including a $2.3 trillion infrastructure plan announced at the close of the quarter.

### Do you believe the value rally is sustainable?

**Lauren:** We believe we're still in the early innings of the rally for a number of reasons. First, despite their outperformance since last September, value stocks continue to trade at a 40% discount to growth. This is a significantly wider gap than we've seen historically. Also, once these style rotations occur, the cycles tend to last for several years. Value has lagged growth for about a decade, so we believe value stocks are likely to fare well over the course of 2021.

Also worth noting are the very strong consumer balance sheets. That is, households across a range of income levels have built up significant savings. Throughout 2020, there were very few opportunities for consumers to spend money. Today, total savings equal approximately 65% of U.S. GDP, which is higher than the pre-pandemic level and significantly higher than it was following the global financial crisis. As vaccine distribution accelerates along with the pent-up demand for "normal" activities, we should see consumer spending accelerate as well.

**Darren:** For businesses, inventory levels are at historic lows across many industries, and companies that had been reluctant to pursue capital expenditure plans are now moving forward with them. Over the next 12 months, we believe we should see assets flowing into the economy due to a burst of spending from both businesses and consumers. This broadening macroeconomic growth is one of the most important ingredients for a sustained value rally.

### Inflation expectations rose in the first quarter. What does this mean for value stocks?

**Darren:** We are seeing two other key ingredients for a prolonged value rally — modest inflation and modestly higher interest rates. During the first quarter, the yield on the 10-year Treasury note reached its highest level in more than a year. Industries that are most correlated to rising bond yields — banking, commodities, industrials — make up the bulk of the value benchmark. Stocks in these cyclically sensitive sectors tend to perform well with higher inflation. For many growth sectors, on the other hand, inflation can be a significant headwind. Spending and demand are starting to increase, and the Federal Reserve has indicated that it will keep its easy monetary policy in place despite rising inflation expectations. This environment is another reason we believe value can take a meaningful lead over growth.

### With these changing conditions, how are you positioning the portfolio?

**Lauren:** Over the past 12 months, we have been able to take advantage of significant dislocations in the market. In the challenging markets of 2020, we focused on companies that we believed were being unfairly punished. As a result, we were able to add many fundamentally strong companies to the portfolio at attractive prices. In addition, we have been carefully monitoring holdings that have outperformed significantly, in areas like the technology sector. We are proceeding with caution toward any stocks with price-to-earnings multiples that we believe are too high, and we are selling or trimming those that we believe have become too expensive.

When stocks sold off sharply at the start of the pandemic, then later rallied through the remainder of 2020, and as the sector rotation continues today, our relative value approach has not changed. Our goal, as always, is to prepare the fund for a range of scenarios with a balanced structure for the portfolio. We plan to maintain a mix of cyclical and defensive holdings, investing in our best ideas with a focus on the fundamentals of the businesses.

## Putnam Large Cap Value Fund (PEIYX)

Annualized total return performance as of 3/31/21

| **Class Y shares** Inception 10/1/98 | **Net asset value** | **Russell 1000 Value Index** |
|---|---|---|
| Last quarter | 11.22% | 11.26% |
| 1 year | 57.62 | 56.09 |
| 3 years | 12.95 | 10.96 |
| 5 years | 13.77 | 11.74 |
| 10 years | 11.99 | 10.99 |
| Life of fund | 10.55 | — |

Total expense ratio: 0.65%

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 assumes reinvestment of distributions and does not account for taxes. For the most recent month-end performance, please visit putnam.com. Class Y shares before their inception are derived from the historical performance of class A shares (inception 6/15/77), which have not been adjusted for the lower expenses; had they, returns would have been higher. For a portion of the periods, this fund may have had expense limitations, without which returns would have been lower. Class Y shares are generally only available for corporate and institutional clients and have no initial sales charge.*

The Russell 1000 Value Index is an unmanaged index of those companies in the large-cap Russell 1000 Index chosen for their value 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. There are no guarantees that a company will continue to pay dividends.

For informational purposes only. Not an investment recommendation.

The views and opinions expressed here are those of the portfolio managers as of March 31, 2021, are subject to change with market conditions, and are not meant as investment advice.

**Consider these risks before investing:** Value stocks may fail to rebound, and the market may not favor value-style investing. Income provided by the fund may be reduced by changes in the dividend policies of, and the capital resources available at, the companies in which the fund invests. 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. 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.

A world of investing.®

Putnam INVESTMENTS

**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.**

Putnam Retail Management

**Putnam Investments | 100 Federal Street | Boston, MA 02110 | putnam.com**

TL020 325332 4/21