

# Top of the Rowe



Photographs by Bill Cramer/  
Wonderful Machine

For more than two decades, Brian Rogers has outpaced the overall market by spotting values for investors in the T. Rowe Price Equity Income fund. Now he sees value in growth stocks.

By Dyan Machan

**B**RIAN ROGERS HAS THE OFFICE you might expect of a midlevel manager, with three standard windows and barely enough room for a visitor or two. But it's messier: A bookcase is overwhelmed with titles and laden with baseball hats. Piles of notebooks teeter in front of framed pictures whose subjects look like they should be running for their

lives. "What, you don't like my Home Depot carpet?" Rogers asks with a boyish smile. "It's a working guy's office."

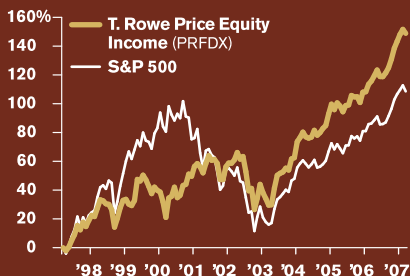
Except that Rogers isn't your average working guy. He's the recently promoted chairman of T. Rowe Price, the rapidly growing Baltimore-based no-load mutual fund house. Rogers not only presides over the

firm's 93 mutual funds, with combined assets of \$345 billion, but he's the unassuming head of its \$24 billion Equity Income fund. The fund was up 19 percent last year, beating the Standard & Poor's 500 by more than three percentage points. But the real story for the fund—and Rogers himself—has been remarkable steadiness. Since 1985 the fund has had a down year only twice, with an annual average return of 10 percent in the past 10 years. "He manages risk better than I do," says Bill Miller, the legendary chief investment officer of rival Legg Mason Capital Management and portfolio manager of the Legg Mason Value Trust.

Rogers does all this with an unwavering commitment to value investing, the philosophy of buying stocks that trade at a discount to the market. But lately, he has also spotted some values in growth stocks, whose sales and earnings grow faster than the overall market. "I think growth is where value was seven years ago," he says. Not that everyone has always loved his approach: In the late 1990s Rogers refused to chase tech stocks even as they marched steadily higher. For three years Equity

### STEADY HAND

By avoiding risky bets, Rogers gives investors less volatility in the short run and hefty gains in the long run.



SOURCE: BLOOMBERG

Income lagged behind the market, leading some investors to send nasty letters. When the market crashed, his fund's investors held up relatively well.

Relaxed and self-assured, Rogers, 51, reflects the firm he oversees—merit over appearances and practicality over flash. Despite an office picture that shows him grinning next to Alan Greenspan and his title of chief investment officer, he says he's "not a market guru." He also dismisses forecasting as a fruitless exercise and isn't much for corporate hierarchy. "We have no king or queen around here," he says. What the firm does have—in the view of its fans—is success. T. Rowe Price's mutual fund assets have nearly doubled since the beginning of 2000.

The son of a teacher and a school principal, Rogers graduated from Harvard in 1977, worked three years as a credit analyst at Bankers Trust and topped that off with a Harvard MBA. In 1982 he signed on with T. Rowe Price, a company that made its name in growth stocks. One of the firm's new ideas was to create a value-oriented fund. Rogers, already a contrarian in the David Dreman mold, jumped at the chance. A \$10,000 investment in his fund in 1985 would be worth \$138,000 today, versus \$123,000 for the S&P 500.

Will it stay strong and steady? We caught up with Rogers in that cluttered office to get his thoughts on his nonmarket market view, what people are missing about big-cap stocks and how you get to be chief investment officer.

**SMARTMONEY:** *You established the worthlessness of market predictions. So what's your market prediction?*

**BRIAN ROGERS:** There's so much you can't forecast. I mean, who would have predicted Britney Spears would

shave her head? [Laughs.] But I think that with earnings growth of 5 to 8 percent, lots of positive dividend and stock buyback activity, and the market multiple being a reasonable 15 or 16 times [earnings], stocks should be able to outperform the risk-free alternative of, say, 5 percent.

**SM:** *By how much?*

**BR:** I think over the long term stock prices will follow earnings growth at 5 to 8 percent. However, if the Fed sees earnings growth slowing too much, it might cut rates. So who's to say you couldn't have a 10 to 15 percent market again?

**SM:** *What do you like in your stocks?*

### Big-Stock Bargains

Whether you call them value stocks or growth stocks, Rogers favors companies with dividends and low P/Es.

Company (Ticker)	Price
<b>3M</b> (MMM)	\$75
<b>Walt Disney Co.</b> (DIS)	34
<b>General Electric</b> (GE)	34
<b>Microsoft</b> (MSFT)	27
<b>Pfizer</b> (PFE)	25

Prices as of 3/9/07.

**BR:** I'm always interested in companies that have gone through a rough spell but, if you look at their histories, were once investor darlings. If investors fall in love with a company, then they're bound to fall in love again. I like lower relative P/Es—10 to 15 times earnings—a solid balance sheet and a good dividend history.

**SM:** *Value has had a great run. Lately, there's more buzz in the growth area.*

**BR:** The buzz probably has basis.

**SM:** *Time to bail out of your fund?*

**BR:** No, but I will make modest adjustments. I would be surprised if over the next two to three years, growth funds don't do better than value funds. You never know when the rubber band is going to snap back.

**SM:** *You're turning into a growth fund?*

**BR:** No, but I want to hedge my bets a bit. Lots of times there are companies like General Electric [his largest holding] in growth funds. Now, you're not going to confuse GE with Google, but GE has a much stronger growth orientation than, say, a steel company. Look at its businesses: media, medical, etc. It's in some good positions.

**SM:** *Many say that with GE you get market performance. There's no way it can double revenue. Nobody believes it can take off.*

**BR:** Absolutely, which is why it's cheap.

**SM:** *But it may be cheap forever.*

**BR:** Few things are cheap forever.

Let's talk about GE. It's one of the half-dozen remaining triple-A-rated companies in the country. There will be times when balance-sheet strength is viewed as an asset again.

GE claims it can grow revenues at basically twice the rate of the global GDP. But arguably, the bottom line can grow faster, say, 12 percent, via intelligent acquisitions,

being the best in a big market and improving margins. It's been reshaping its portfolio and is trading at only 15.8 times earnings, with a 3.2 percent yield.

**SM:** *Enough of GE, already. Besides, I still think it's a value stock.*

**BR:** What about Microsoft? Is it a growth company? Is Walt Disney a growth company? How about Pfizer?

**SM:** *Make your cases.*

**BR:** If the economy grows at 3 or 4 percent, which means 5 or 6 percent in nominal terms, Microsoft can grow at 10 percent. It's the knee-jerk brand with the upgrade cycle working for it. At \$27, it's a buy. I might cut back my position at \$35, depending on what the rest of the market is doing.

Walt Disney is growing sales at more than 8 to 9 percent, but its



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earnings advance at 11 to 13 percent. This company fits into the growth-versus-value debate. It’s at \$34. We bought it at \$22 and would normally lighten up, but if growth stocks start to catch some fire, Disney should benefit. In 10 years there will be Disneylands in India and China. ESPN is one of the most dominant brands. Can they [Disney] continue to produce good films? I bet they can.

**SM:** *Another growth company in value clothes?*

**BR:** Pfizer is a growth company selling at \$25 and not priced as a growth company. Whenever you read research reports saying there is no pipeline activity and the company has lost its R&D edge, you are almost guaranteed to see major product announcements in three years. Plus, it sells at 11 times earnings and has a 4.5 percent yield. If it doesn’t work out and the stock is at \$25 in three years, I

have a 4.5 percent rate of return, and hopefully, something else in the portfolio will make up for it.

**SM:** *What about an old-fashioned value stock in value clothes?*

**BR:** 3M. It was at \$92 two years ago and, after some earnings challenges, is trading at \$75. But I love an invigorated CEO and a company that sells at just 15 times earnings. I see it going back to the \$90 range if it executes well.

**SM:** *The market hates big stocks!*

**BR:** That’s all right. In 1999 our small-cap value fund was the least saleable. Since then the fund had a 17 percent per year return, versus the S&P 500 at 3 percent.

**SM:** *Your sell discipline?*

**BR:** As stock prices perform well, the relative P/E is probably higher. And probably the yield is a lot lower. I sell, as I did with Lockheed Martin last year.

**SM:** *Can we put numbers to it?*

**BR:** Lockheed Martin advanced from \$40 to \$80 in a short period of time. Its P/E was at 10; when it hit \$80, it was 18. The yield dropped from 3 percent to 1.5 percent. That kind of move in a couple years’ period intrigues us to look elsewhere.

**SM:** *Are you concerned about losing the dividend tax cut?*

**BR:** I think it’s likely we will see a Democratic president, and some of the changes of the Bush administration will be reversed.

**SM:** *Will those dividend stocks deflate when taxes go up?*

**BR:** You would see less marginal demand for them. Ironically, it might hurt higher-beta [riskier] stocks even more because it would be viewed as disruptive in the overall market. You would see Google go down faster than a utility stock even though the utility dividend would be more disadvantaged.

**SM:** *How do you become a CIO? Say, I want to be one.*

**BR:** Be careful what you wish for. Back to my life in 1982—one of the reasons I liked T. Rowe Price was I sensed a generational opportunity. There were a lot of people over 40, but not many twentysomethings. That year we hired four MBAs. I’m the last one here.

**SM:** *I see. You were the last one standing. Your white board has something scribbled defining three ways to the top—act the part, build the business or do the dirty work. Which was your path?*

**BR:** I built a business—the fund. When the management position opened up, I made it clear I wanted to stay involved in investing and not get mixed up in managing investment operations.

**SM:** *That would be the dirty work.*

**BR:** There’s nothing un-American about dirty work. But there’s no assurance that I have any skills to do well at that. I know I can be productive on the investment side. **S**