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MARKETS

How Big Tech Has Powered Global Stocks

Profits at Facebook, Alibaba and others are boosting stocks that got walloped last year

Alibaba Group is among the tech companies whose shares have risen more than 25% this year. **PHOTO:** GILLES SABRIE/BLOOMBERG NEWS

By Akane Otani

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Booming profits are driving a fresh rally in technology shares from New York to Hong Kong, helping boost stock markets and showing the allure of rapidly growing companies even as the global growth outlook dims.

Companies including Facebook Inc., Netflix Inc., Alibaba Group Holding Ltd. and Rakuten Inc. have risen more than 25% this year, well outpacing the gains of the stock indexes on which they are listed. The advance is a marked turnaround from the final months of 2018, when tumbling technology shares wiped out trillions of dollars from the global stock market.

Fund managers have credited some of the advance to the group's record of generating robust and, in many cases, record profits as broader earnings growth has cooled. Earnings are a key driver of stock prices, making industries delivering high growth like technology an appealing bet for investors who are worried about slowing growth across the global economy.

“Big tech is looking far more interesting now than it has any time over the past year,” said Jim Tierney, chief investment officer of U.S. concentrated growth at AllianceBernstein, which owns shares of Google parent Alphabet Inc., Facebook and Microsoft Corp. As the growth outlook becomes more murky, “if you can find companies that can grow a heck of a lot faster, they’re looking attractive,” Mr. Tierney said.

Stocks broadly have gotten a lift from the Federal Reserve’s pivot from signaling further rate increases to keeping rates on pause as it gauges a slowdown in the global economy, as well as easing trade tensions. The World Bank and the International Monetary Fund slashed their forecasts for 2019 and 2020 growth in recent months, citing risks including weakening industrial production, a potential “no-deal” Brexit and cooling earnings growth.

Fears about a global slowdown sent stock indexes in the U.S., Europe and Shanghai to their biggest one-week slide since December on Friday, although all three remained up at least 9% for the year.

Investors seeking growth have turned to tech giants whose profits are driving higher. Facebook delivered its best-ever earnings in its most recent quarter, showing investors that advertisers continued to flock to the platform despite public scrutiny over how it handles users’ privacy. Chinese e-commerce giant Alibaba grew sales by 41% and profit by 37% in its latest quarter, while media and internet firm Naspers Ltd., Africa’s largest publicly traded company, posted a 39% climb in earnings as its classifieds unit turned a profit for the first time.

Four tech stocks—Microsoft, Facebook, Apple Inc. and Amazon.com Inc. —have accounted for about 12% of the S&P 500’s total advance in the first two months of the year, according to S&P Dow Jones Indices. They were four of the five biggest contributors during that period, along with Boeing Co.

Still, even after the rally of the past couple of months, a number of large technology stocks have yet to return to record levels. The iShares global tech exchange-traded fund is up 12% this year, on track for its best quarter since 2012, but still below its 2018 record.

Many investors have said the recent rally appears to have more conviction behind it than previous ones, which some had described as melt-ups: rapid rises in prices driven more by a fear of missing out on gains than by confidence in a company’s earnings. That is partially because valuation multiples for a number of technology behemoths have fallen from recent highs, pulled down by a combination of higher earnings and the end-of-year rout that pummeled global stocks.

Facebook, for instance, trades at around 22 times its past 12 months of earnings, well below its level of 34 times from the start of last year, according to FactSet. Shenzhen-based Tencent Holdings Ltd. is trading at 32 times trailing earnings, versus around 55 times earnings in the beginning of 2018, while Dutch semiconductor firm ASML Holding NV is trading at 26 times earnings, versus around 31 then.

Still, discounted shares haven't been enough to win over all investors.

Firms including RBC Capital Markets and Morgan Stanley have advised clients this year to limit their exposure to technology stocks, citing the potential for disappointing growth ahead, as well as regulatory risks that could crimp profits.

That is a scenario that already has begun to play out in China, where the fortunes of two internet giants have diverged in recent months. Shares of Alibaba have surged 28% this year, more than double Tencent's gains.

Analysts blame the split on China's increased scrutiny of the videogame industry, a key source of revenue for Tencent. Officials have approved new games at a slower pace and have given the green light to fewer high-profile titles that promise to be big moneymakers, denting the company's outlook, said David Dai, a senior analyst at Bernstein in Hong Kong.

Even with technology companies facing increasing scrutiny by regulators and lawmakers, a number of investors say the reward appears to outweigh the risk for now.

Many firms remain relatively early on in their growth cycles, offering the potential for several more years of robust returns before reaching what some analysts may consider to be the late stages of a cycle.

"Investors should look at Chinese tech stocks, not because they have 'China' or 'tech' in their names but because they offer long-term upside," said Bin Shi, head of China equities at UBS Asset Management, adding that he believes valuations for the group still look reasonable.

Fund managers also are reassured by signs that technology stocks haven't become a so-called crowded trade—something held widely by investors that is vulnerable to sharp reversals.

Investors surveyed by Bank of America had ranked global tech stocks the most crowded trade across markets for 10 consecutive months through November. Since then, they have pointed to other areas of the markets as being overextended, including bets on a strengthening U.S. dollar and on emerging markets.

"It feels more healthy than the go-go momentum we saw in 2017 and 2018," said Dave Donabedian, chief investment officer at CIBC Private Wealth Management. "We're in a global slow patch, so the earnings growth that growth stocks bring to the table looks more precious."

—Saumya Vaishampayan contributed to this article.

Write to Akane Otani at akane.otani@wsj.com