

Diversified Business Services

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The Global Industry Classification Standard or GICS is a widely recognized industry reference for evaluating the sector components of different indexes. While Weatherbie Capital, an Alger subsidiary, finds it is a helpful tool for evaluating portfolios, we have another internal classification system that we like to use called Dynamic Growth Areas.

We define the Dynamic Growth Areas as meaningful sections of the U.S. stock market; these internal labels help us diversify our holdings. There are six Dynamic Growth Areas and they have been used by Matt Weatherbie, our CEO and co-chief investment officer, across the more than 40 years he has been managing smaller cap portfolios. The dynamic growth areas are: Consumer, Health Care, Information Services, Media & Communications, Technology and Diversified Business Services.

For risk management purposes we invest in at least four of the six at all times. No one Dynamic Growth Area can be larger than 35% of assets under management.

At Weatherbie we identify stocks from a broad universe of smaller cap equities that meet our growth and quality criteria. The result is a focused portfolio of typically 50 stocks, “The Weatherbie 50.” The Dynamic Growth Area that is commonly the largest component of the Weatherbie 50 is Diversified Business Services. This high proportion recognizes that as we look down the

capitalization range at the universe of smaller cap companies, many will have a services business model, often business to business.

What do we look for in a Weatherbie Growth Stock?
 There are six key criteria:

1. Generally earnings per share growth of roughly 20% per year on average over the next three to five years
2. Some maturity to the firm’s business model enabling our team to analyze future growth prospects with some confidence
3. A distinct competitive advantage that is identified by our research and that should lead to superior returns over time
4. Strong Return on Invested Capital, or ROIC, ideally above the cost of capital, indicating what we believe to be a distinct competitive advantage
5. A strong balance sheet and cash flow enabling—to a significant extent—self-funded growth
6. Seasoned management team whom we like and trust and gives us confidence that they have a sensible growth plan that aligns with their interests as well as our clients’.

Identifying the Weatherbie 50 entails a number of steps and while not every stock in this universe will possess all of our criteria, many of the equities we choose from Diversified Business Services demonstrate all of them and often grow to be large positions.

By classifying smaller cap equities according to our own criteria, we are able to identify what we believe will be the most successful Weatherbie Growth Stocks to serve our investors.

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