

ALGER

Inspired by Change, Driven by Growth.

Spring 2021

Capital Markets: Observations and Insights

Grand Reopening



Alger is committed to sustainability and is a signatory to the PRI.

Grand Reopening

Unprecedented stimulus, high savings rates, pent-up demand and vaccines may come together to make this season a very grand reopening of the economy, potentially boosting growth this year to the highest in many decades.

With strong economic growth comes the temptation to buy equity in lower quality businesses with heavy operating or financial leverage. It seems easy enough. As an investor, you can “rent” these cyclical stocks when the going is good and sell at the right time to boost your returns, right? In practice, we doubt it. Yes, theoretically it is possible, but we believe the digital revolution is only accelerating, disrupting companies on the wrong side of change, no matter how great the macroeconomic tailwind.

When we speak to strong company management teams who are thoughtful and focused on the long term, they don’t say they are trying to gain more exposure to cyclical forces. Rather, they talk about the desperate need to digitally transform their businesses in order to increase their productivity, delight their customers and gain market share in this ever-changing world. Long-term investors should take heed—good business managers are focused on the accelerating pace of change and the investments needed to keep up and thrive. We believe business owners and shareholders, should be of the same view—stay focused on long-term secular forces transforming the economy. In other words: own, don’t rent; invest, don’t trade.



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Key Observations and Themes

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Grand Reopening

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Unprecedented stimulus, high savings rates, pent-up demand and vaccines may come together to create strong growth and a grand reopening of the economy.

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Secular investment trends may transcend economic volatility, politics and central bank actions, producing compelling investment opportunities over the long term.

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With the non-U.S. valuation discount historically large, investors may be able to find the growth they crave at the values they want outside of the U.S.

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While elevated relative to history using traditional metrics, equity valuation looks more attractive after accounting for low interest rates and changing business models.

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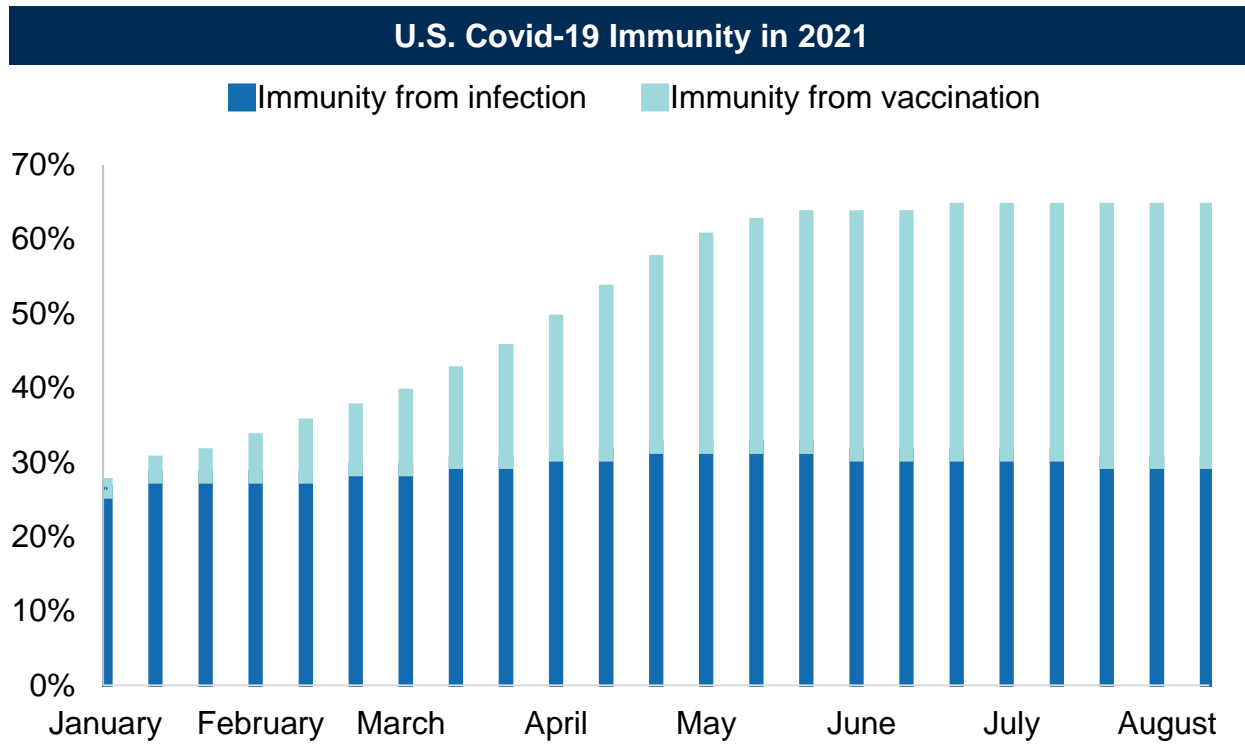
Style Wars

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Value stocks have regained some lost ground, but powerful structural forces may keep the long-term trend of Growth outperformance intact, in our view.

Grand Reopening A Shot in the Arm

- Strong progress in the vaccination effort, combined with existing immunity resulting from infection, should create a large proportion of the U.S. population resistant to Covid-19

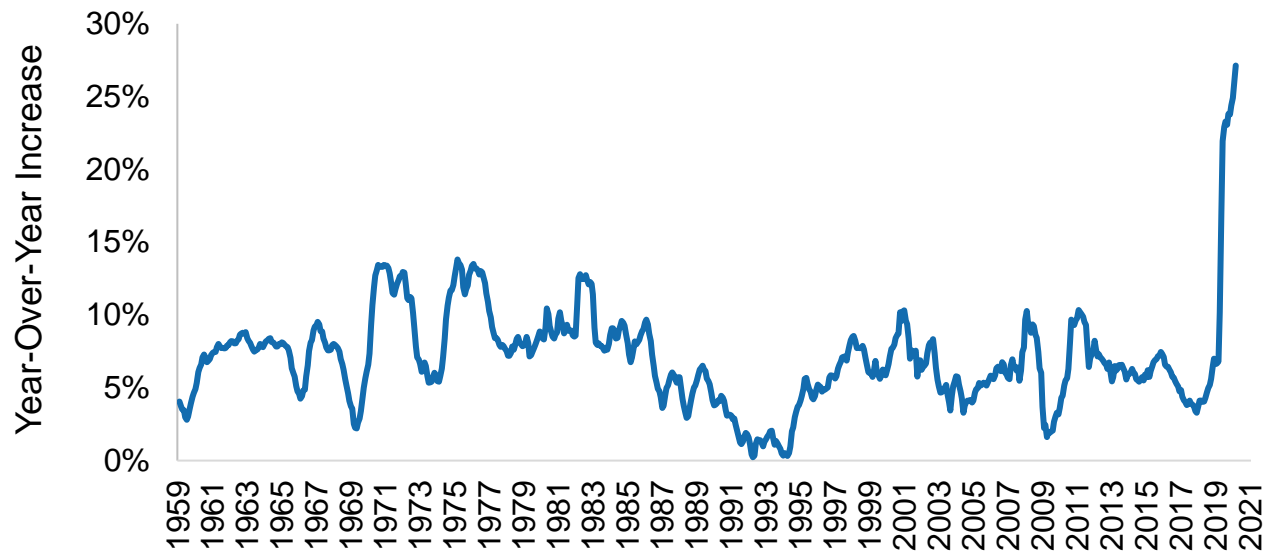


Source: CDC; covid19-projections.com. March onward are projections.

Grand Reopening Hot Off the Press

- Recent monetary stimulus in the U.S. has been unprecedented
- Explosion in the money supply is still working its way into the real economy

Massive Increase in Money Supply



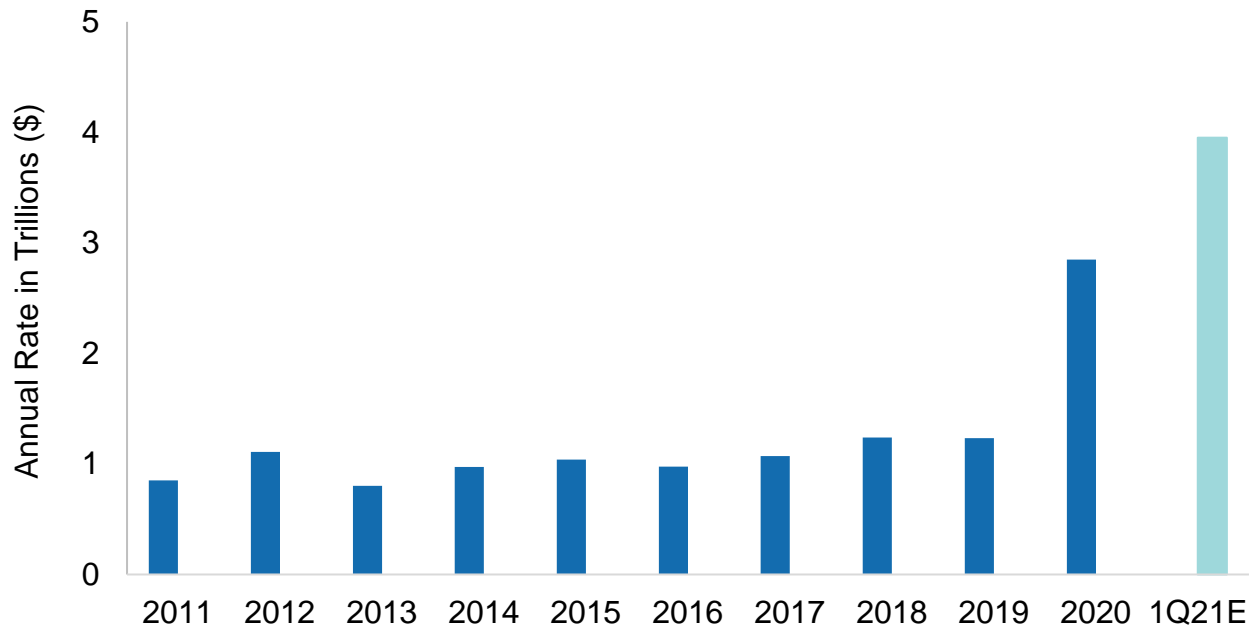
Massive increase of \$4 trillion may drive robust economic growth

Source: Federal Reserve as of 3/31/21. Money supply is "M2," a measure of the money supply that includes, generally, cash, checking deposits, savings deposits, shares in retail money market mutual funds.

Grand Reopening Surging Savings

- Stimulus has driven very high savings levels, a portion of which will ultimately be spent and may drive very strong consumer spending, in our view

U.S. Personal Savings Explodes Higher



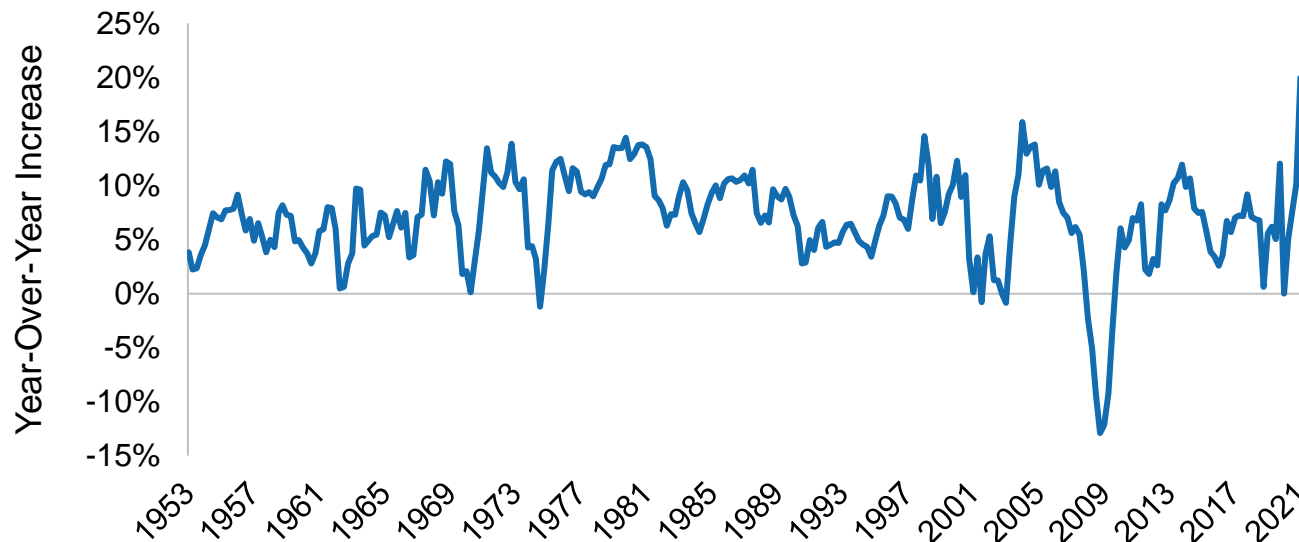
Trillions of dollars of recent *incremental* savings could come back to the economy

Source: U.S. Bureau of Economic Analysis. Last datapoint for 1Q21 is seasonally adjusted annual rate estimate by Cornerstone Macro.

Grand Reopening Feeling Wealthier?

- With strong equity and housing markets, household net worth is increasing rapidly
- Given the academic estimates of propensity to spend, this surge in net worth could lift spending by several hundred billion dollars

Household Net Worth Surges



Americans may spend a portion of the large aggregate increase in wealth

Source: Federal Reserve's most recent data as of 3/31/21. Last data point is 1Q21 estimate by ISI Evercore.

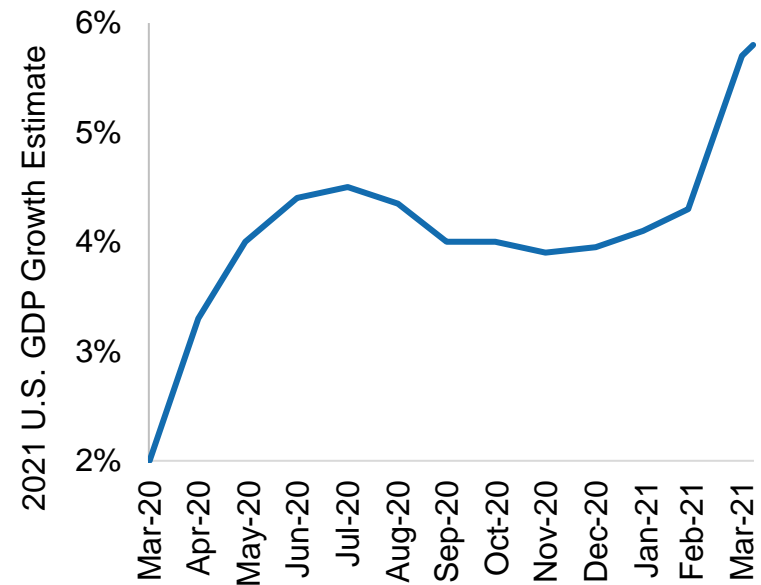
Grand Reopening Economic Excitement

- Unprecedented stimulus, high savings rates, pent-up demand and vaccines may come together to boost economic growth this year to the highest in many decades

OECD U.S. GDP Tracker Shows Acceleration



Economists Still Catching Up

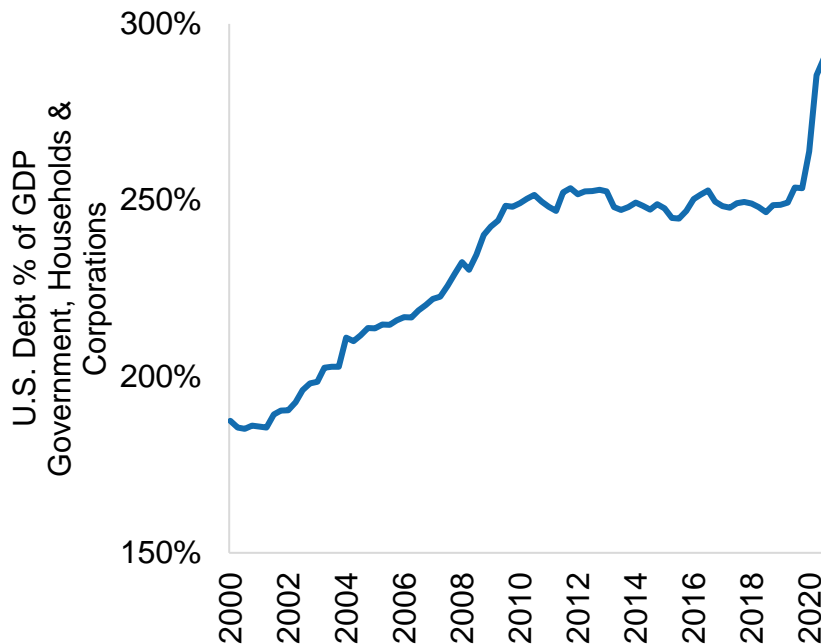


Source: OECD and FactSet. OECD indicator provides a real-time high-frequency measure of economic activity using machine learning and Google Trends data. Two-year stacked data sums current and last year's year-over-year change.

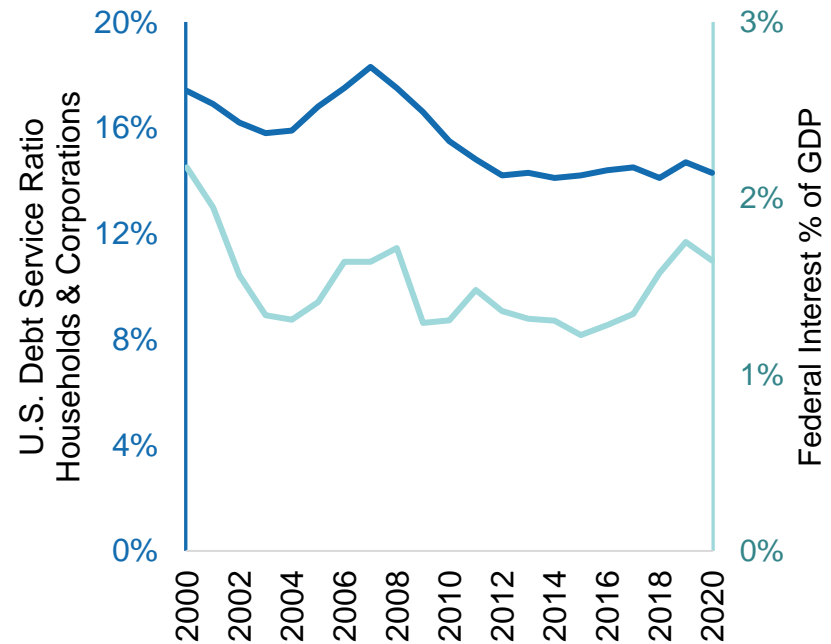
Grand Reopening No Debt Hangover Yet?

- Huge fiscal stimulus and easy financial conditions have caused a surge in U.S. debt
- However, the cost to service the private and federal debt is not high relative to history

U.S. Debt Levels Are Very High...



...But The U.S. Debt Service Burden Is Not

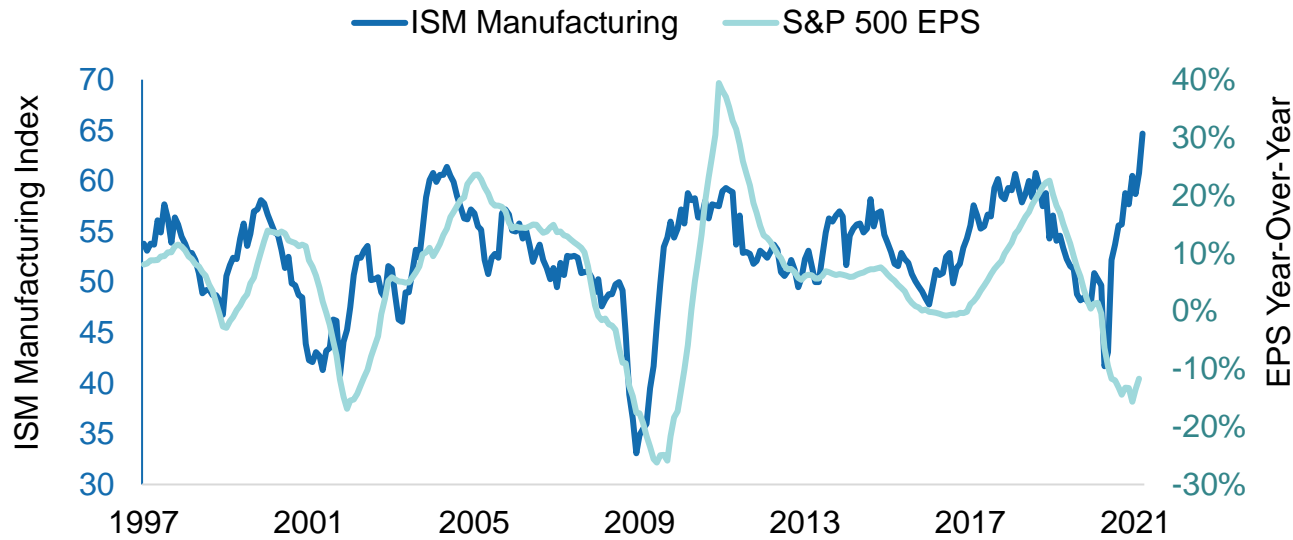


Source: Bank for International Settlements, March 2021 and Federal Reserve Bank of St. Louis. Debt Service Ratio is the share of income used for interest payments and amortizations in the non-financial private sector.

Grand Reopening Earnings Extravaganza?

- Historically, the ISM Manufacturing Index has led S&P 500 EPS growth by about seven months with an 80% correlation
- We believe the recent 37-year high in the index may imply massive earnings growth this year, potentially above the consensus estimate of 25%

Leading Indicator Portends Very Strong EPS Growth



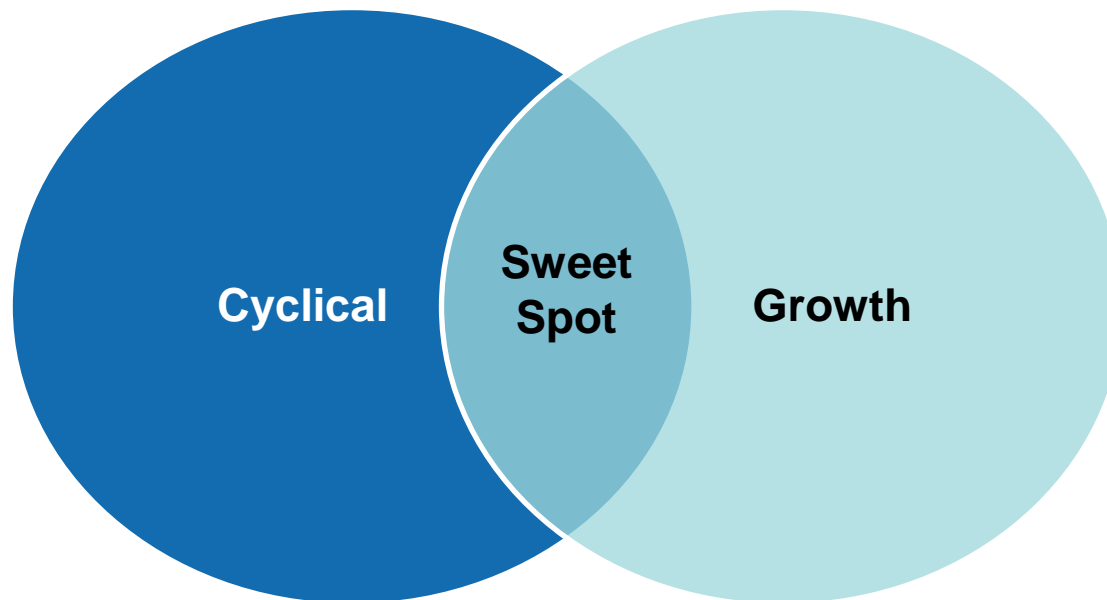
**Leading
indicator
suggests
huge future
EPS growth**

Source: Institute for Supply Management®, FactSet, and Alger as of 4/1/21. The ISM Manufacturing Index is an indicator of U.S. economic activity based on a survey of purchasing managers at manufacturing firms.

Grand Reopening

Where to Invest?

- Growth stocks with cyclical/depressed end-market exposure are attractive, in our view
 - Many investors use “Value” stocks as a shorthand for cyclicals, but we believe “Value” has structural problems (see Style Wars section at end of this presentation)
 - Several key value industries may also be negatively impacted by new behavior, such as changes in business travel and office space, arising from the pandemic

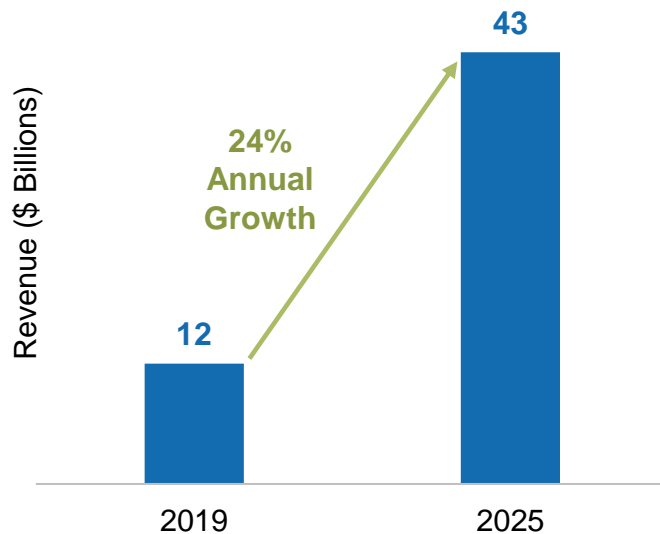




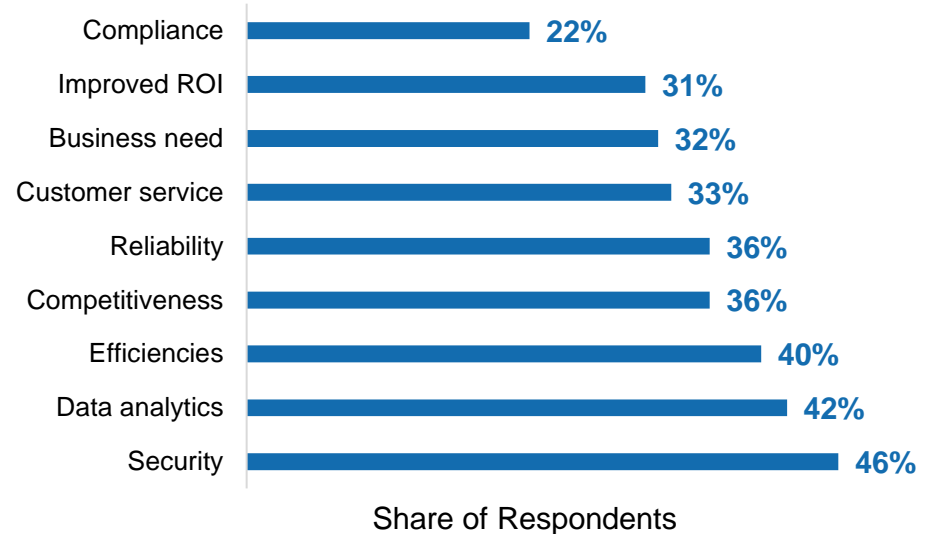
Enduring Themes Internet of Things

- The explosion in connected devices is creating the “Internet of Things” or IoT, transmitting valuable and actionable information
 - Applications include industrial monitoring and automation, health care, security, agriculture, inventory management, smart cities, utility metering and connected cars

IoT Sensor Market Worldwide



Drivers of IoT Spending

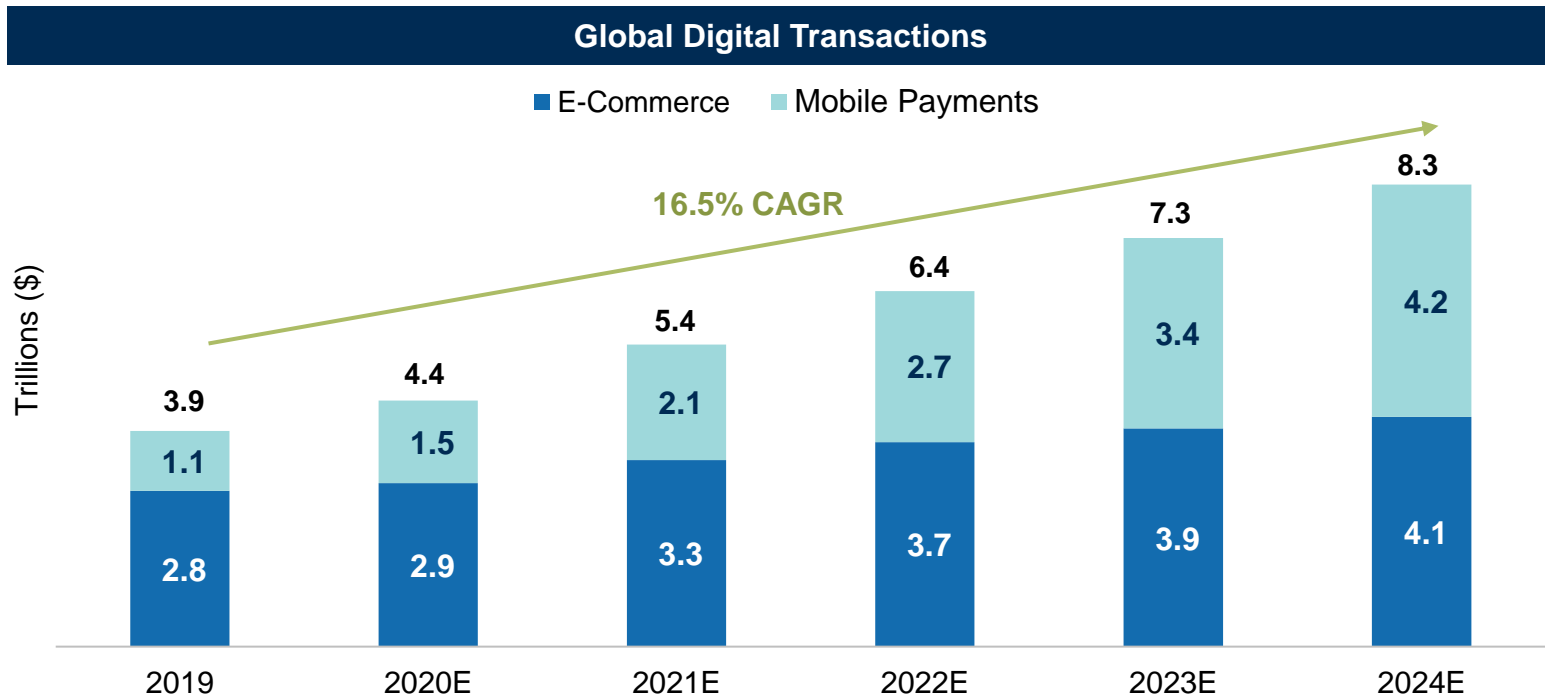


Source: Sensor market forecast from MarketWatch, July 2020, and drivers of IoT spending from 451 Research survey, December 2019.



Enduring Themes Digital Payments

- Digital payments continue to outgrow the broad economy as they gain penetration, driven by increasing e-commerce and mobile payments
 - China has the largest volume of digital payments and Europe is growing fastest
- Payment networks, processors and software companies can capitalize on the trend



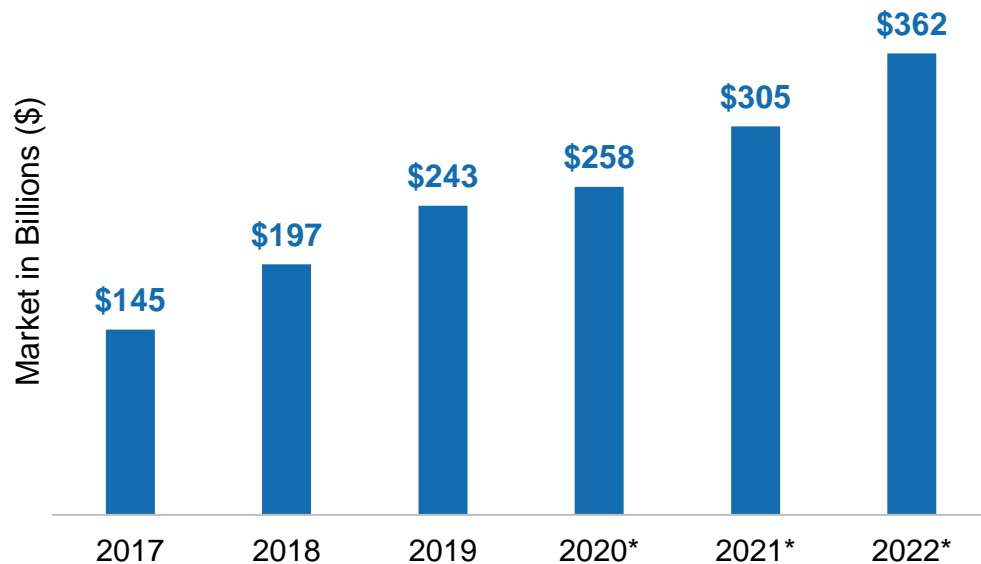
Source: Statista Digital Market Outlook 2020. CAGR is compound annual growth rate, the rate of return required for a quantity to grow from its beginning balance to its ending balance. Mobile payments occur when smartphones are used to process transactions using wireless communication or scan QR barcodes.



Enduring Themes Cloud Computing

- Cloud computing optimizes IT assets, reducing costs and improving flexibility and accessibility
 - The growth in online streaming entertainment, e-commerce, work from home, telehealth, e-sports, and virtual learning are all enabled by cloud computing

Cloud Computing Market Is Growing Rapidly



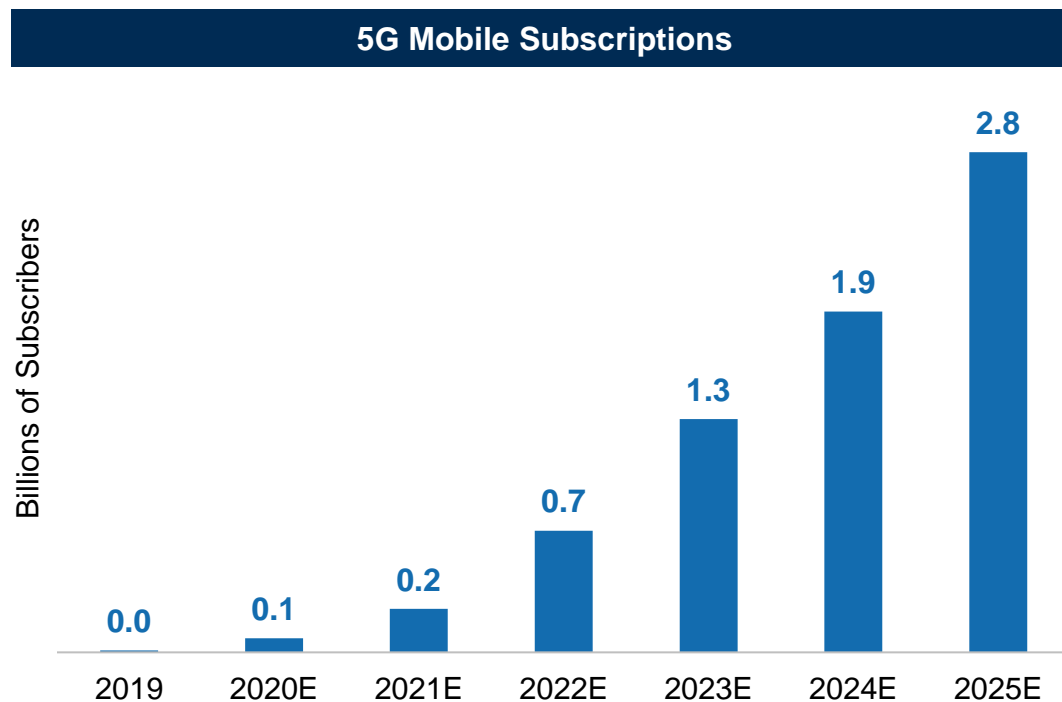
Source: Gartner, November 2020. *Forecast. Market includes cloud application services, infrastructure services, business process services, and security.



Enduring Themes

5G Wireless

- The next generation of wireless technology, 5G, is bringing faster speeds, increased capacity, much lower latency and more efficient spectrum utilization
 - 5G helps enable telematics, advanced health care monitoring, remote work, augmented/virtual reality and autonomous driving applications



Source: Ericsson, July 2020.

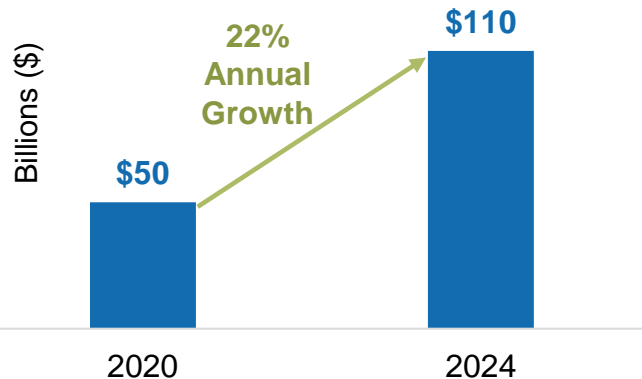


Enduring Themes

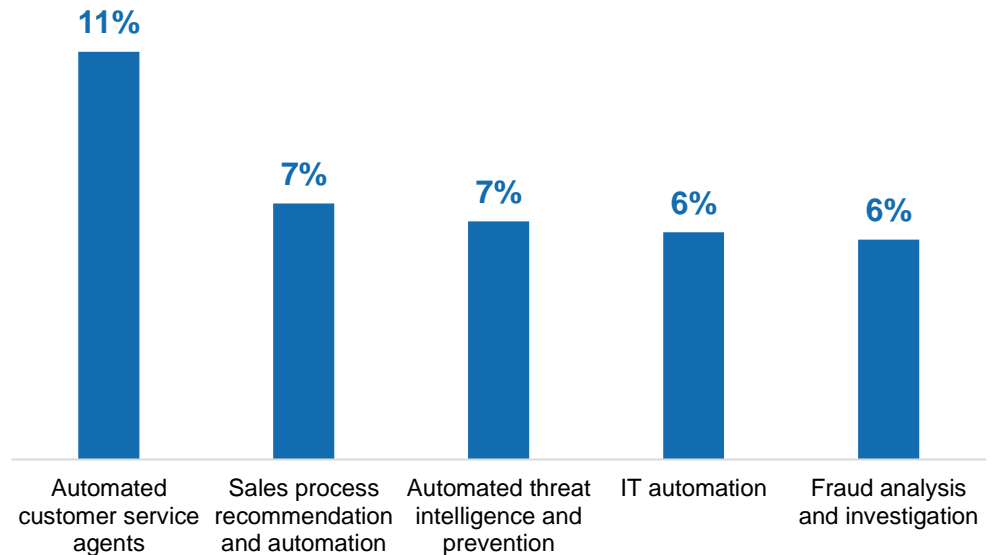
Artificial Intelligence

- “AI systems can now compose text, audio, and images to a sufficiently high standard that humans have a hard time telling the difference.” – Stanford University AI Report 2021
- Investment in AI has been most prolific in drug development, autonomous driving, education, software development, speech, fraud detection/prevention*

Global AI Spending



Leading AI Use Cases



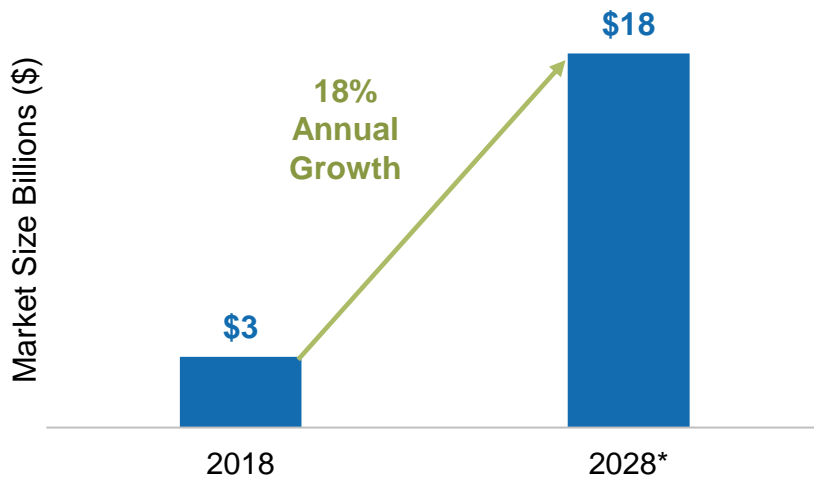
Source: AI spending and use cases from IDC, August 2020. *Stanford Artificial Intelligence Index, 2021 annual report.



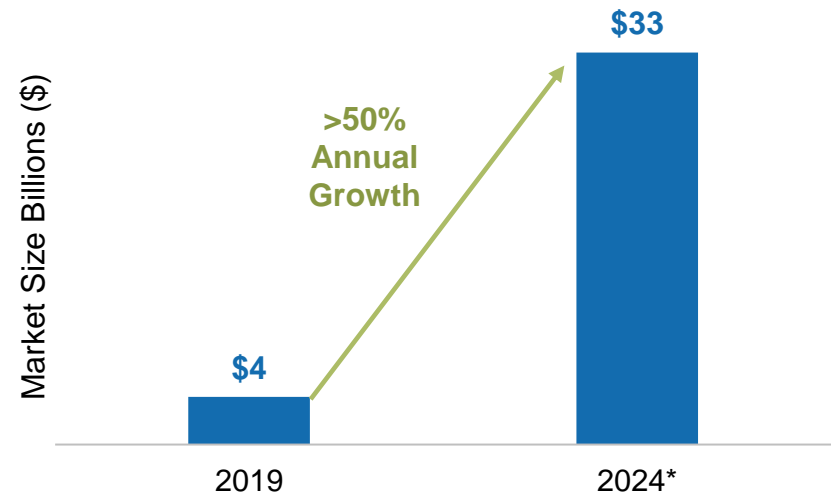
Enduring Themes Genomics Innovation

- Genetic analysis and manipulation will increasingly impact the practice of health care
 - Turning sick care into preventive health care by giving insight into predisposed diseases
 - Delivering more efficacious treatments via targeted therapies (e.g., immuno-oncology)

The Genetic Sequencing Market Expected to Grow



Genetic Advances Drive Cell / Gene Therapies

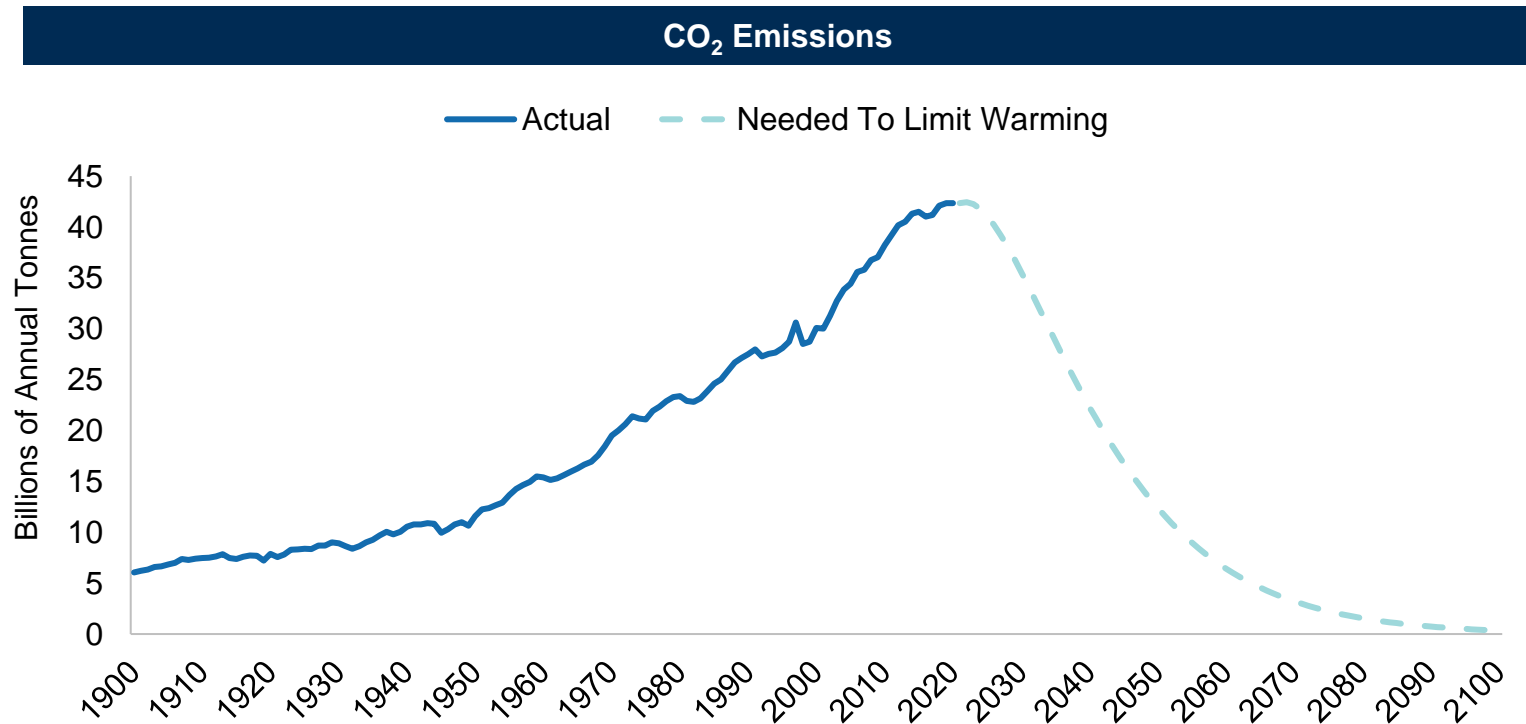


Source: Sequencing based monitoring and diagnostic test market from BIS Research. Cell & gene therapy market data from Cryoport. *Estimated.



Enduring Themes Emission Reductions

- The rate of CO₂ emissions is not sustainable in our view
- Reducing emissions may provide opportunities in alternative energy sources and in electric vehicles and related products and services

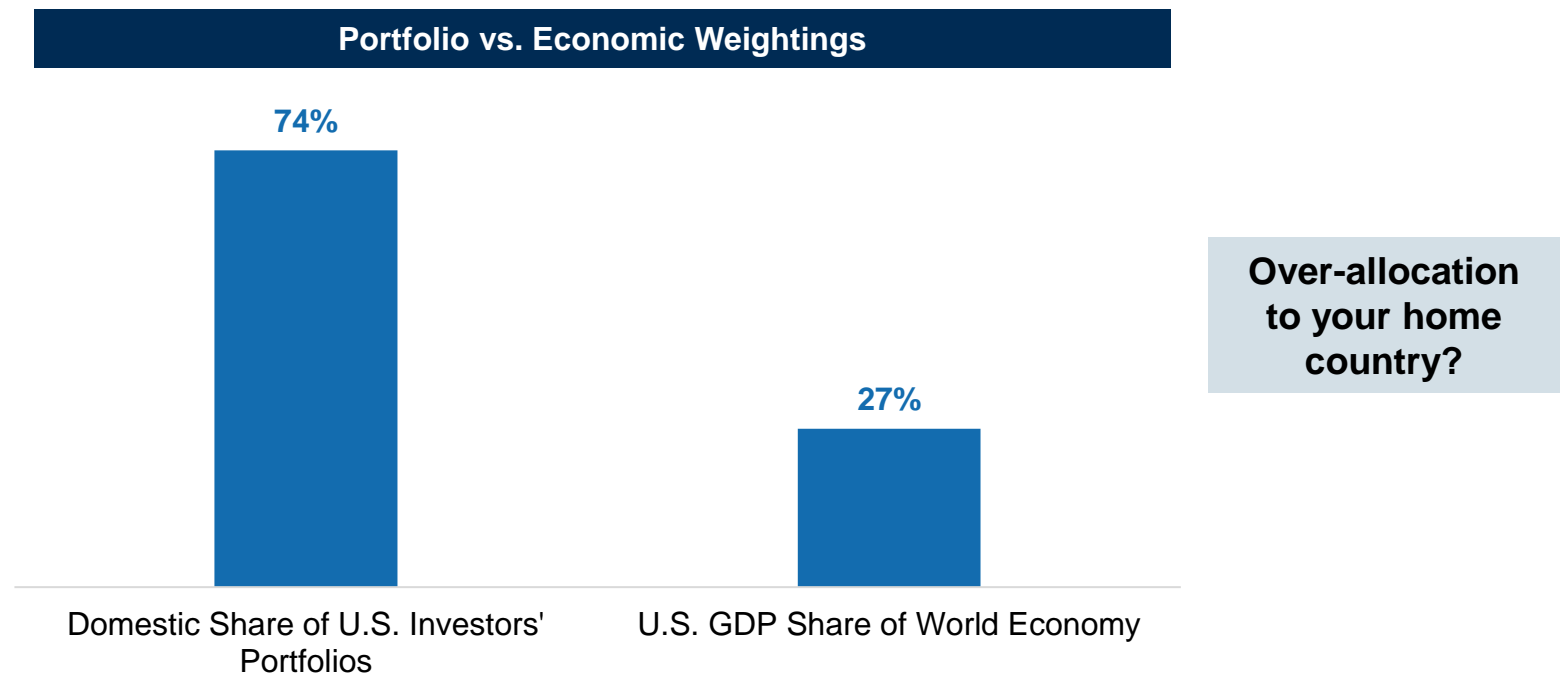


Source: Robbie Andrews (2019) based on Global Carbon Project & IPCC SR15. Carbon budget based on >66% probability of staying below 2°C warming, beginning in 2021.



Looking Abroad Home Country Bias

- People tend to gravitate to what they know. In investing, this phenomenon is known as home country bias
 - Americans generally invest in U.S. companies, Europeans invest their own region, etc.

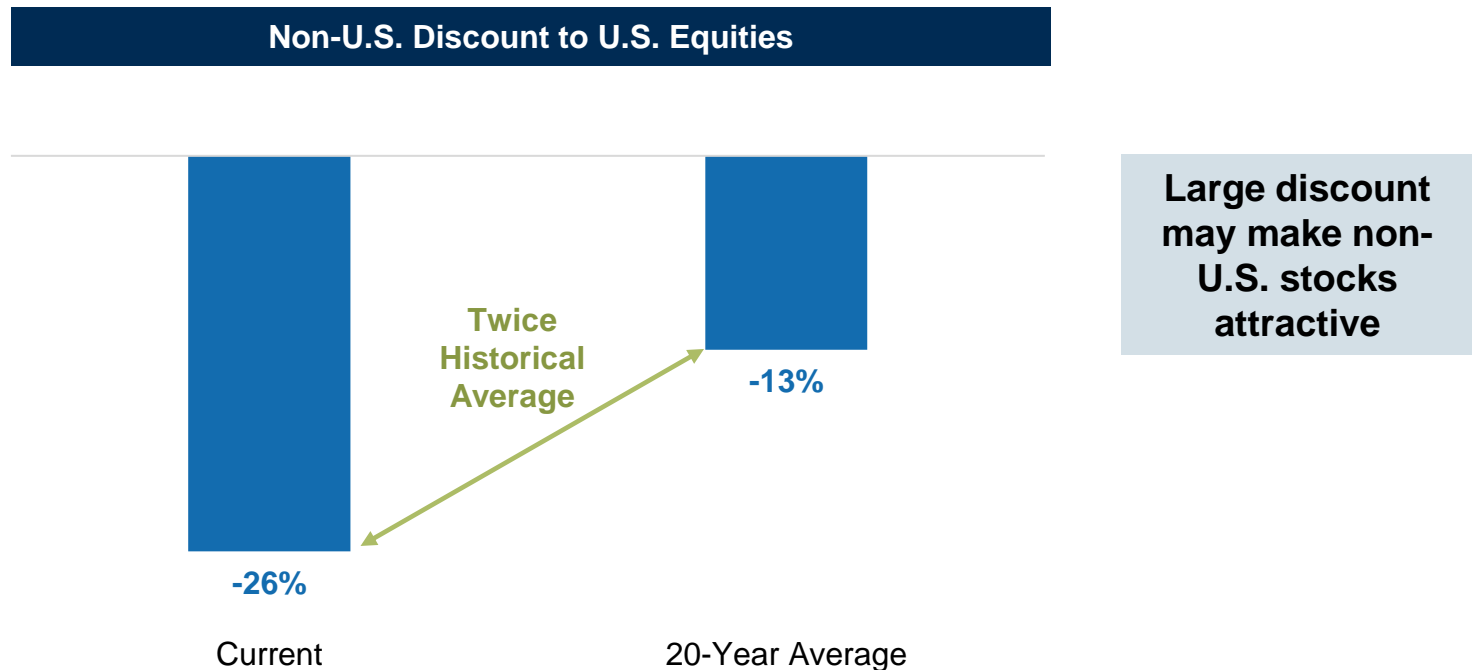


Source: Morningstar, J.P. Morgan and Alger. Note: Domestic share of U.S. investors' portfolios calculated by comparing U.S. Equity and International Equity Morningstar categories as of 3/31/21.



Looking Abroad On Sale

- Non-U.S. stocks typically trade at a discount to U.S. equities but that discount is twice as large as it has been historically



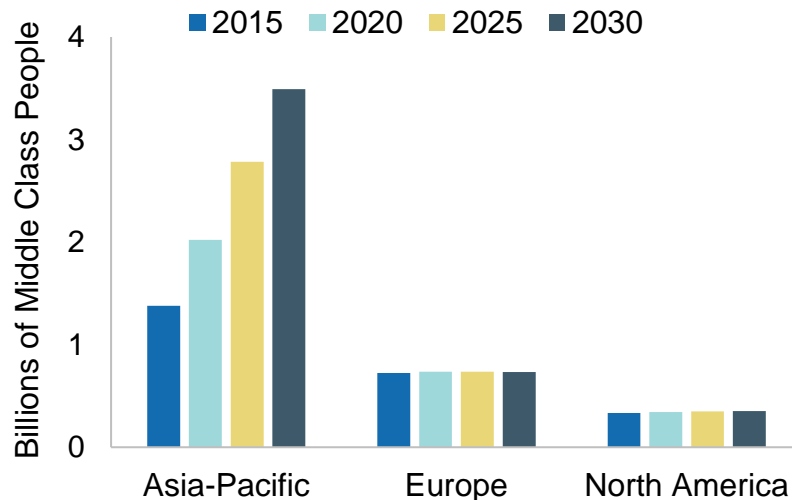
Source: FactSet and Alger as of 3/31/21.



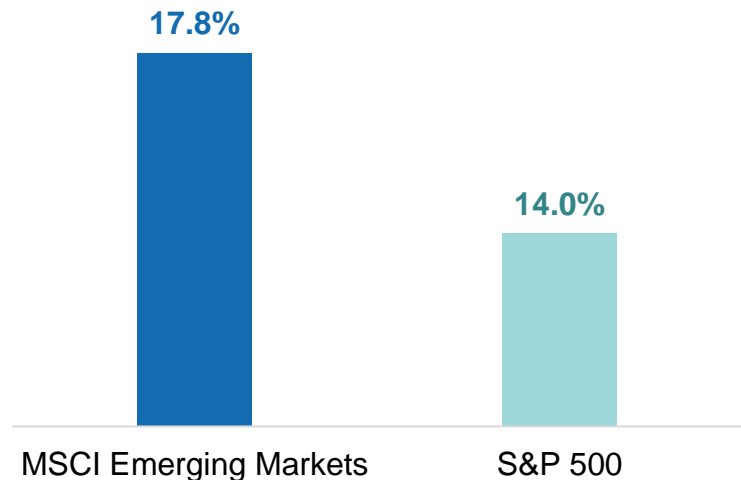
Looking Abroad Emerging Market Growth

- The demographics in emerging markets is a significant growth factor
- Drives materially stronger long-term earnings growth within emerging markets

The Asian Middle Class Is Expected to Grow



Long-Term EPS Growth Greatest in EM



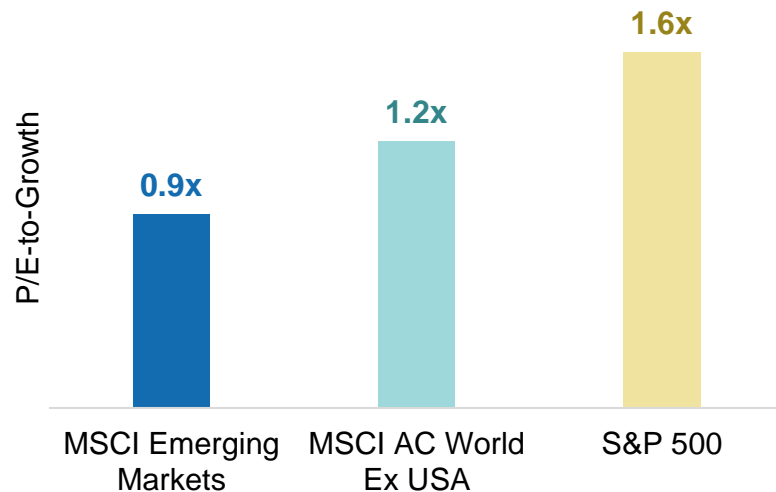
Source: Middle class estimates from Brookings Institution. A middle-class family has an approximate income of \$16,000 to \$160,000 in purchasing power parity terms. EPS growth estimates from FactSet as of 3/31/21.



Looking Abroad Innovation for Less?

- Investors may be able to find the innovation they crave at the values they want in non-U.S. stocks
- Equities in key innovation categories often trade for much cheaper valuations in foreign markets as compared to those within the U.S.

Growth is Cheaper Outside of the U.S.



Innovative Themes Available For Less in Non-U.S.

Industry	Large Non-U.S. Discount?
Communication Platform as a Service	✓
E-Commerce	✓
Solar	✓
Business Process Automation	✓

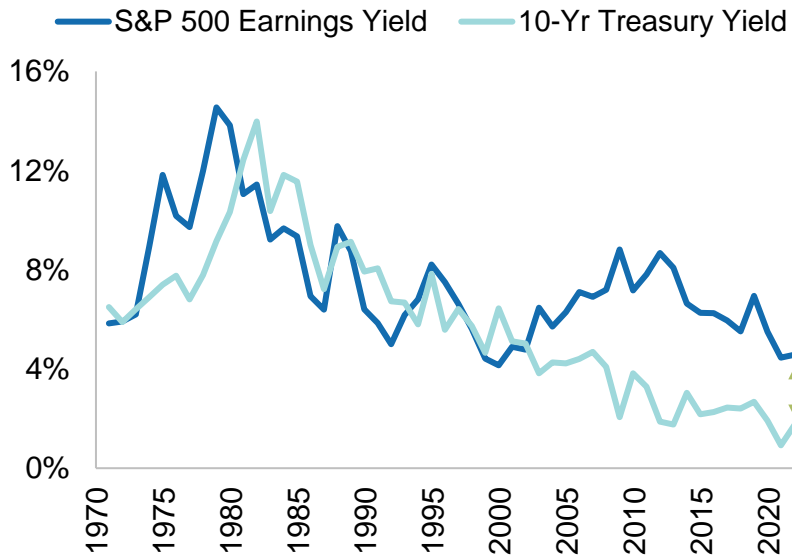
Source: FactSet and Alger as of March 31, 2021. For more information on non-U.S. discount in innovative themes see Brad Neuman, "Where to Find Growth For Less," Alger, 2021.

IV

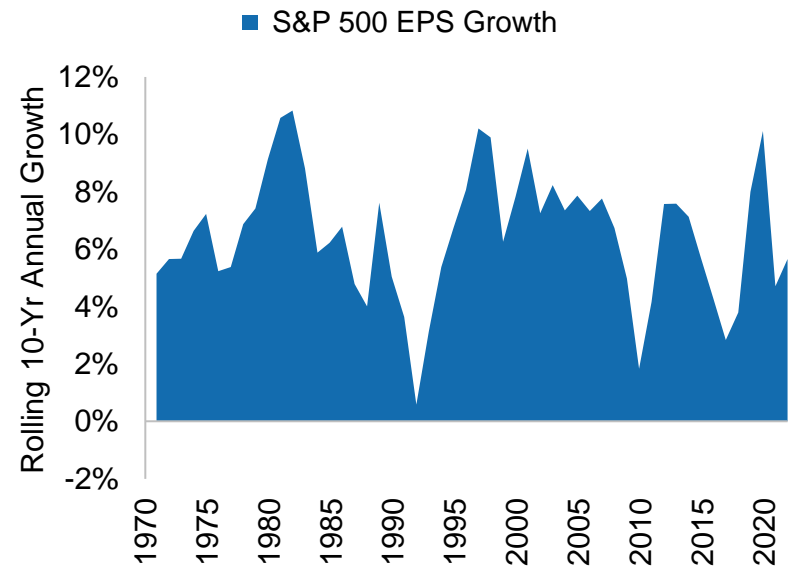
Valuation Equities Attractive Relative to Bonds

- Investors are accepting lower “yields” for the safety of Treasuries relative to equities
 - Over 10-year periods in the past half century, S&P 500 EPS has always grown (even through this pandemic), averaging nearly 7% annually, while bond coupons do not grow

Equity “Yield” Is Attractive Relative to Treasuries...



...And Equity EPS Can Grow!

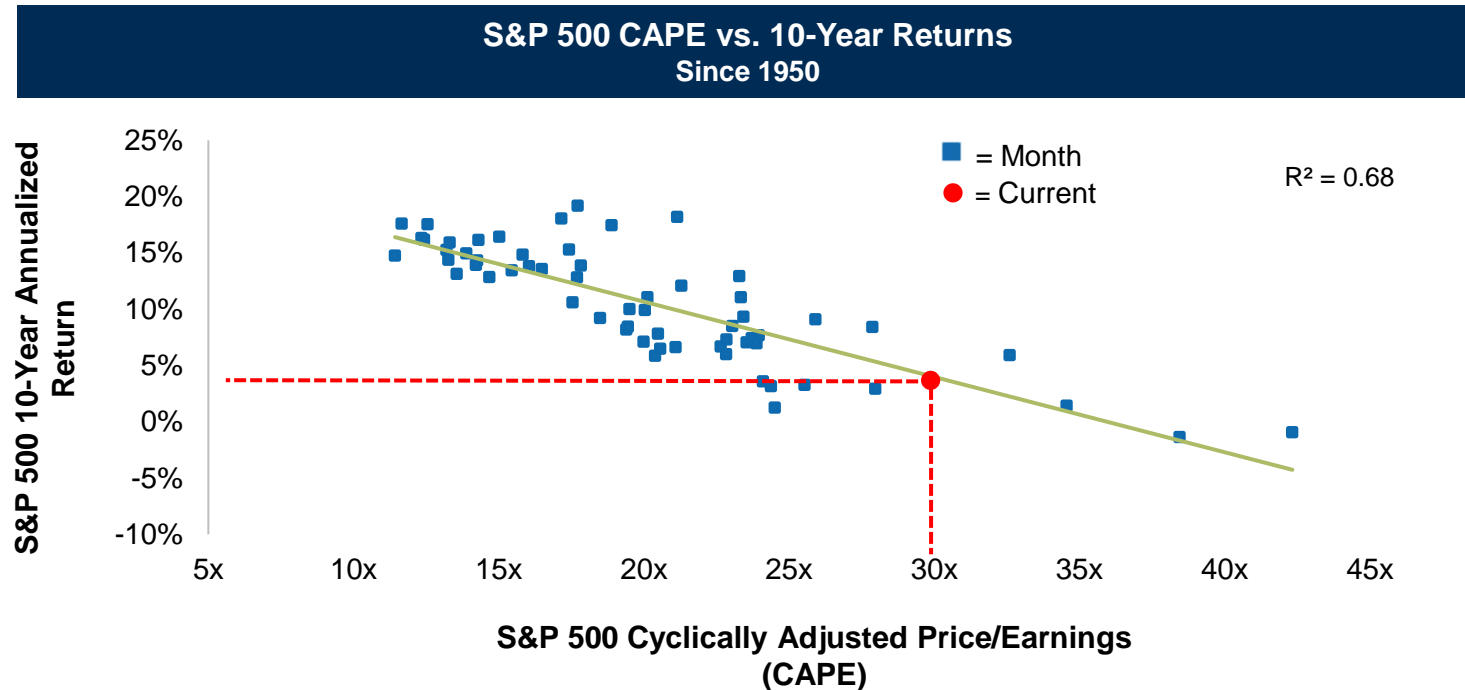


Source: FactSet, Robert Shiller, Alger. Notes: periods used were annual. Equity yield is NTM EPS / Price. Earnings per share (EPS) is the portion of a company's earnings or profit allocated to each share of common stock.

IV

Valuation More Modest Returns?

- Strong relationship between starting valuations and ensuing 10-year returns suggest modest equity returns over the coming decade, but still better than bonds
 - Note that low real interest rates and stronger free cash flow generation imply higher multiples relative to history (see pages 24 & 25)



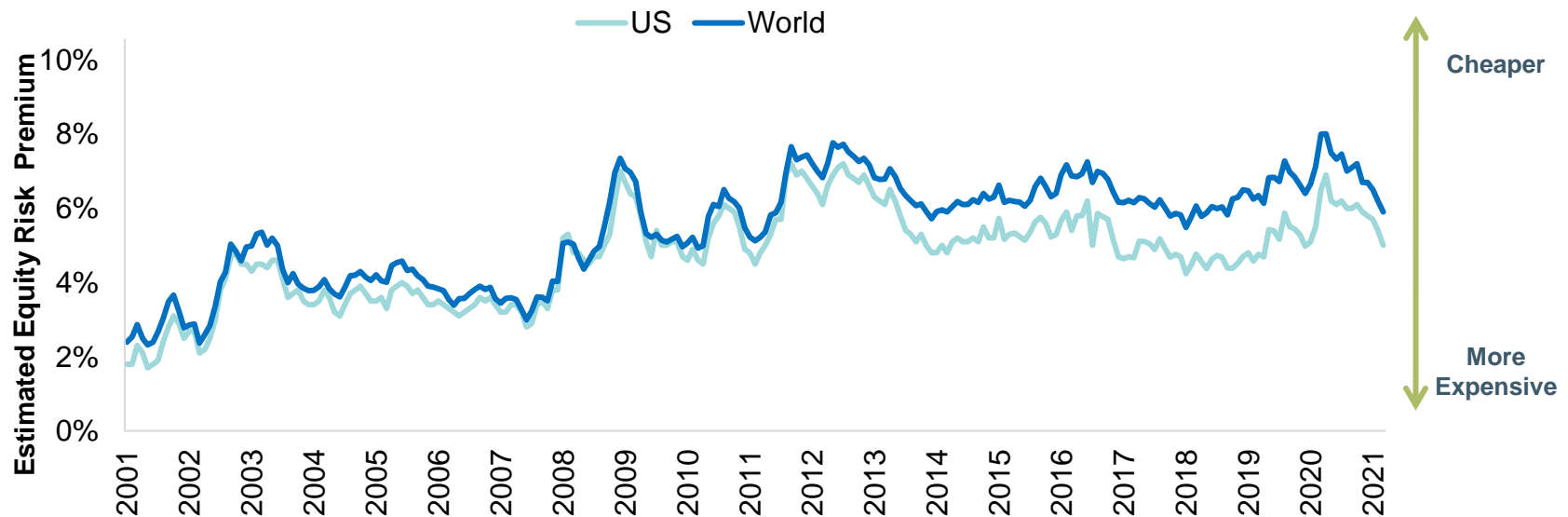
Source: FactSet. Each dot represents the P/E during that year and the returns generated over the subsequent 10 years. The starting CAPE ratio is the price divided by the cyclically adjusted EPS, which is the average of the EPS over the last decade at the start of each 10-year period measured. Annual data utilized from 1950 through 2020; "current" is as of 3/31/21. R-squared is a statistical measure used to analyze how differences in one variable can be explained by the difference in a second variable. **The performance data quoted represents past performance, which is not an indication or a guarantee of future results.**

IV

Valuation Reasonable Relative to Interest Rates

- One good way to incorporate interest rates into valuation is to calculate investors' required rate of return above the prevailing risk-free interest rate
 - Using the so-called Equity Risk Premium shows stocks are attractively valued relative to their historical average

Equity Risk Premiums Show Stocks Are Inexpensive



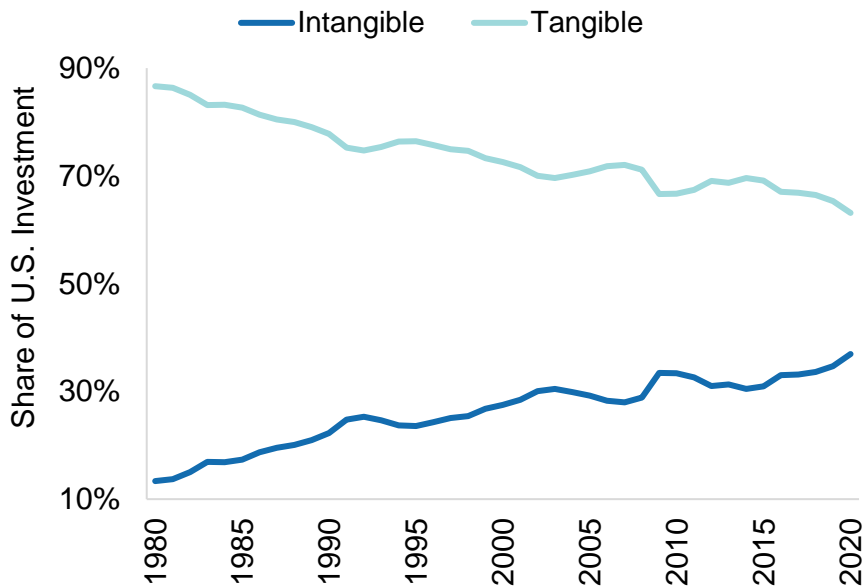
Source: Goldman Sachs. Note: The market implied equity risk premium (ERP) is the rate that at each point in time makes the theoretical value from GS Dividend Discount Model equal to the observed market price. U.S. equities are represented by the S&P 500. World equities are represented by a weighted average of MSCI Asia Pac ex-Japan (20%), TOPIX (10%), Stoxx 600 (30%), and S&P 500 (40%).

IV

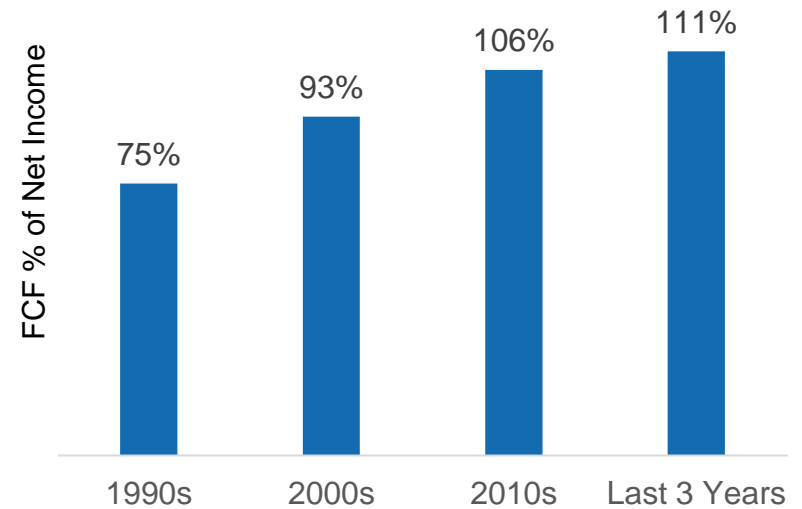
Valuation More than Meets the Eye

- Companies are increasingly investing more in intangible assets (e.g., R&D), that are expensed rather than capitalized causing earnings to decline relative to free cash flow
- The trend of higher free cash flow conversion has made stocks appear cheaper on a Price-to-Free Cash Flow basis as compared to Price-to-Earnings, relative to history

Rising Intangible Investment



Free Cash Flow Conversion Increasing



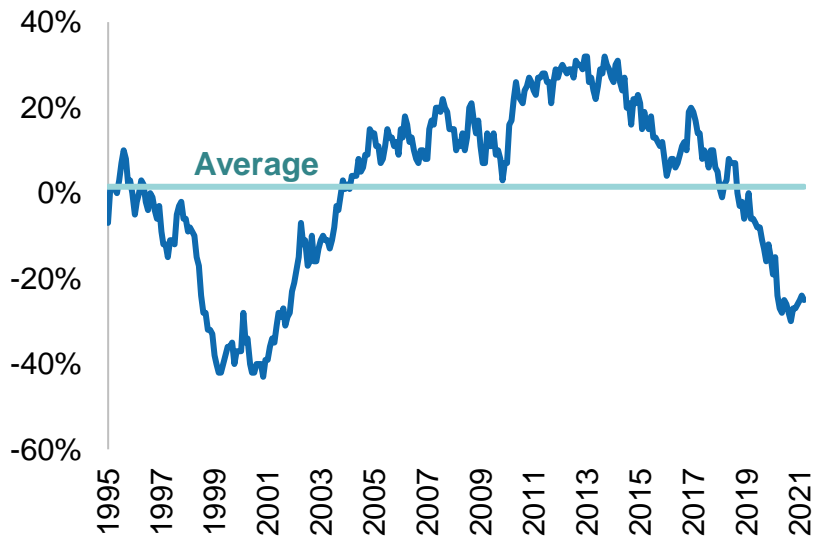
Source: Share of U.S. investment is based on gross private nonresidential domestic investment from the Bureau of Economic Analysis. FCF conversion is from FactSet as of 3/31/2021.

IV

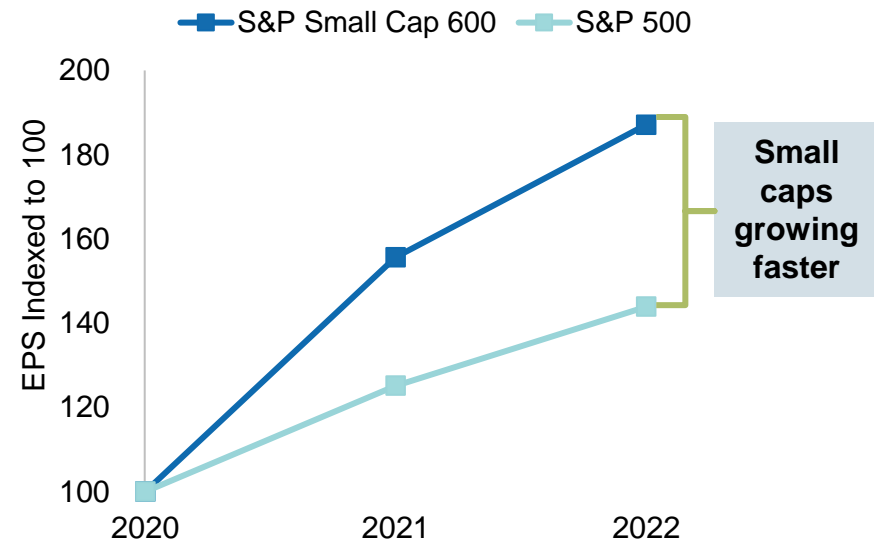
Valuation Smaller Capitalization Stocks Look Attractive

- Small cap equity valuations relative to large caps are depressed as compared to history
- Small caps are expected to grow much faster than large caps

Price-to-Earnings
S&P Small Cap 600 / S&P 500



Estimated Earnings Per
Share Trajectory



Source: FactSet as of 3/31/21. P/E is price divided by earnings per share over last 12-months. Estimated EPS trajectory based on consensus estimates from FactSet.

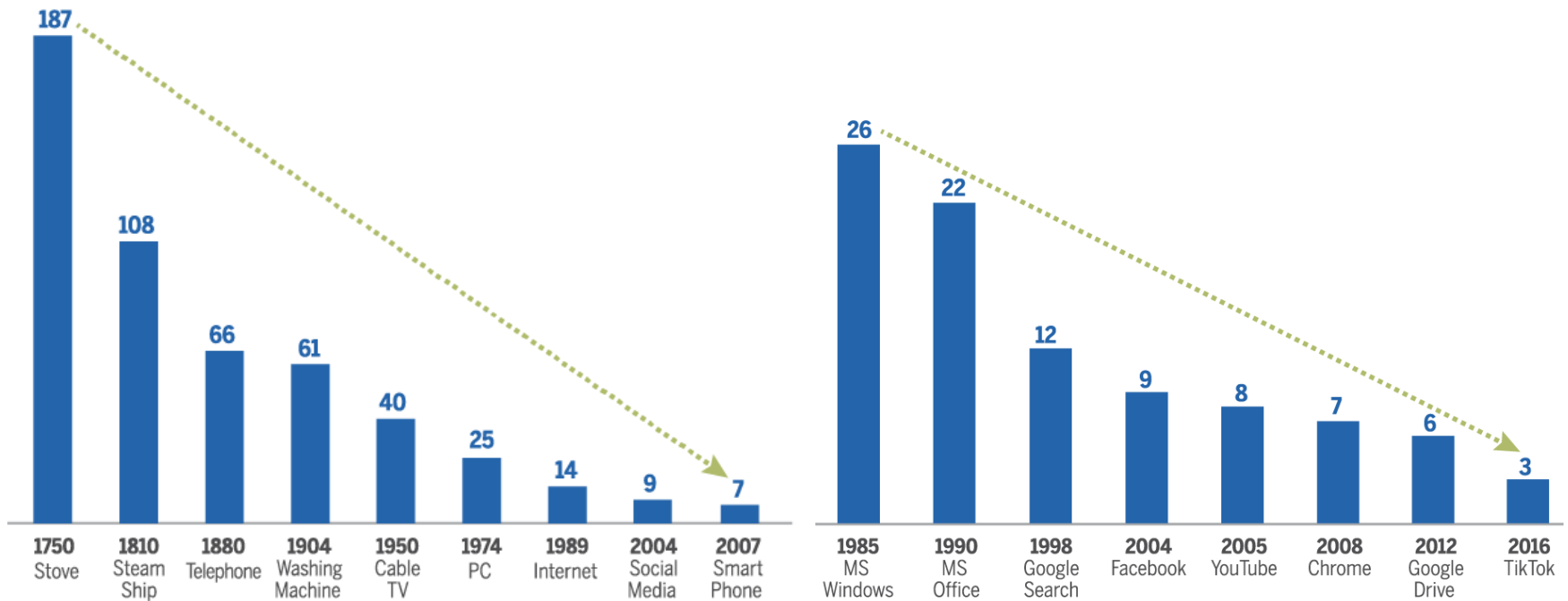
V

Style Wars Accelerating Change

- Innovation is accelerating across many areas of the economy, causing new products and services to diffuse through society faster and disrupt businesses at a greater pace
- This may be a tailwind to growth companies, which we believe are the drivers of innovation, and a headwind to value stocks, which may be victims of change

Years from Market Entry to 50% Penetration

Years to Reach 1 Billion Users

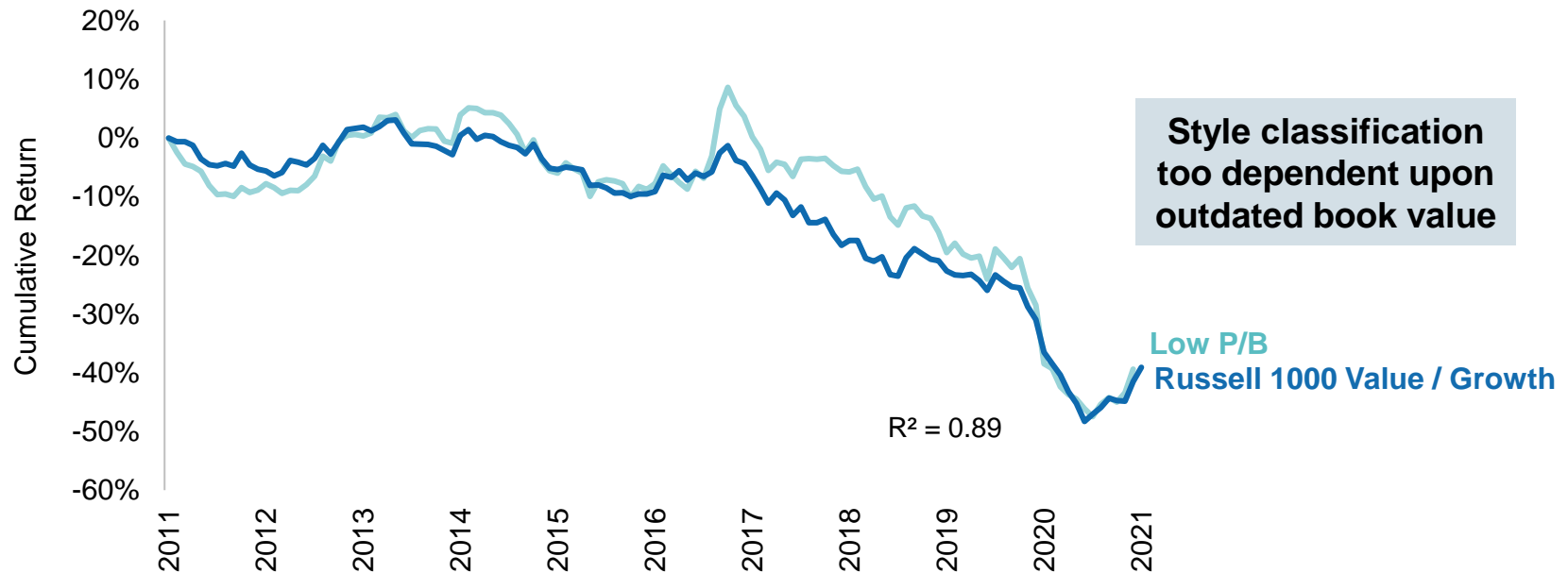


Source: Asymco, Visual Capitalist, company disclosures, Alger estimates.

V

Style Wars Structural Issues Driving Growth vs. Value

- Growth stocks have dramatically outperformed Value stocks over the past decade
- The driver has been the very weak performance of the Price-to-Book valuation metric, which is used heavily in index classifications of Growth vs. Value stocks
- As accounting fails to keep up with the changing economy, book value may no longer be as relevant (e.g., R&D is not capitalized in book value)

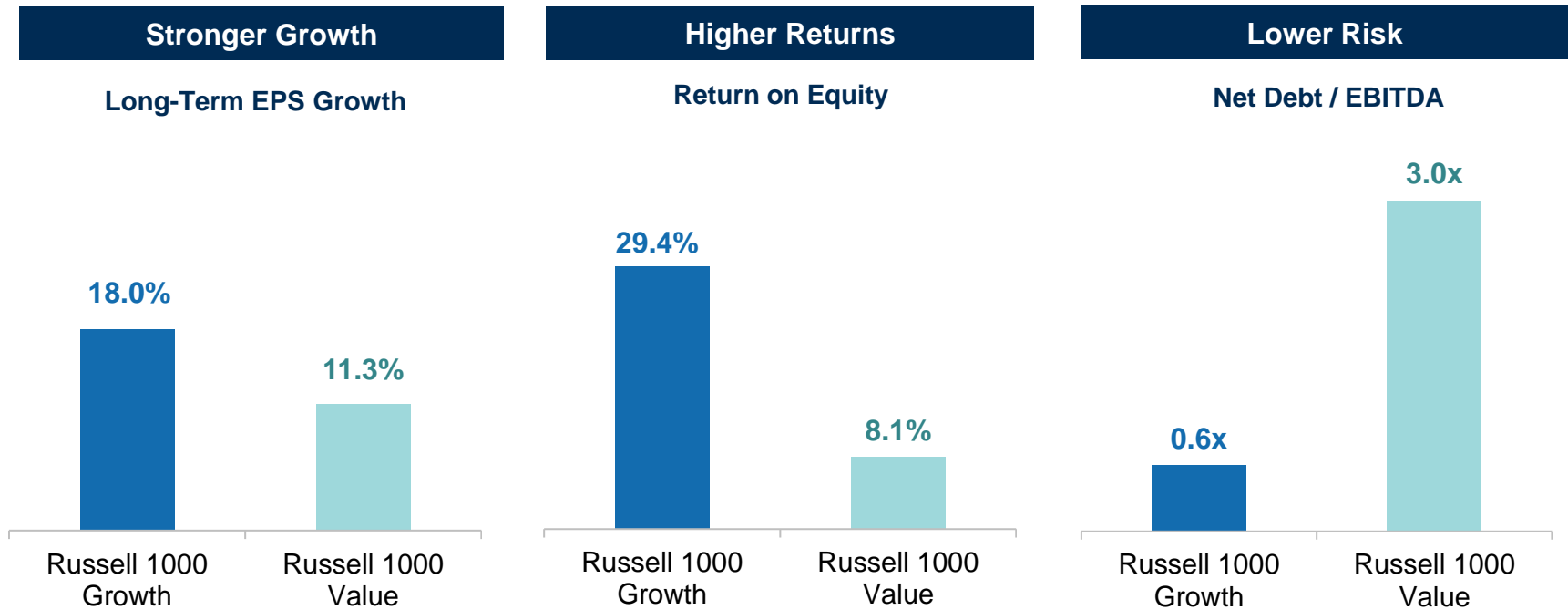


Source: FactSet, Kenneth R. French, and Alger as of 3/31/21. Low price-to-book returns are based on the B/P Fama/French factor for the CRSP universe which includes US firms listed on the NYSE, AMEX, or NASDAQ. The performance data quoted represents past performance, which is not an indication or a guarantee of future results.

V

Style Wars The Growth Advantage

- Three variables drive P/E multiples: growth, return on capital, and risk
- The Russell 1000 Growth Index has higher expected EPS growth, higher return on equity, and lower risk in the form of better balance sheets as compared to the Russell 1000 Value Index



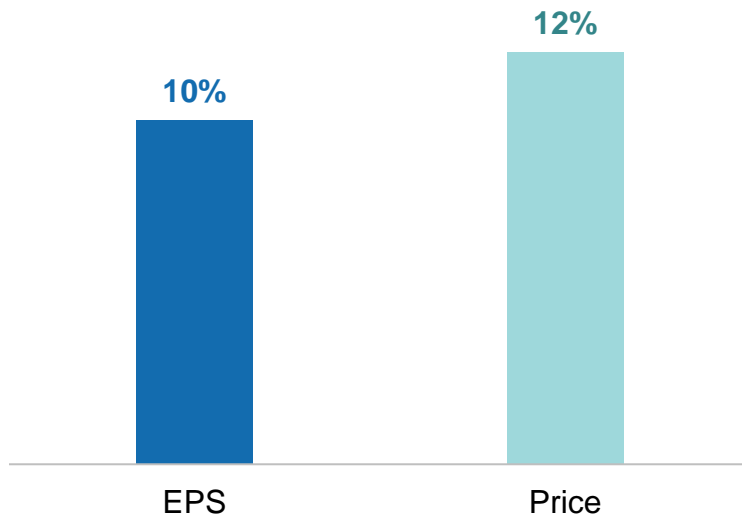
Source: FactSet as of 3/31/21. Growth represents consensus long-term analyst estimates and actual future EPS growth rates might be materially different than the forecasts shown.

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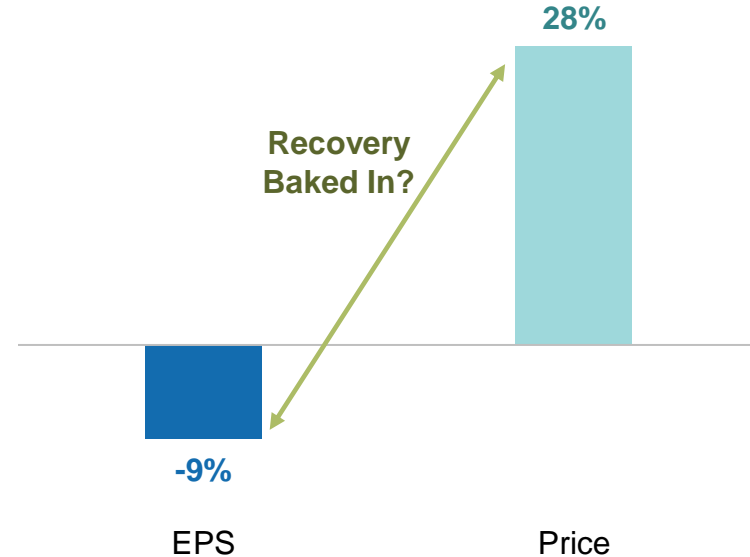
Style Wars Great Expectations

- Growth stocks have appreciated in-line with their fundamentals
- Value stock prices have far outpaced their earnings, indicating lofty expectations

Russell 1000 Growth Six Month Change



Russell 1000 Value Six Month Change



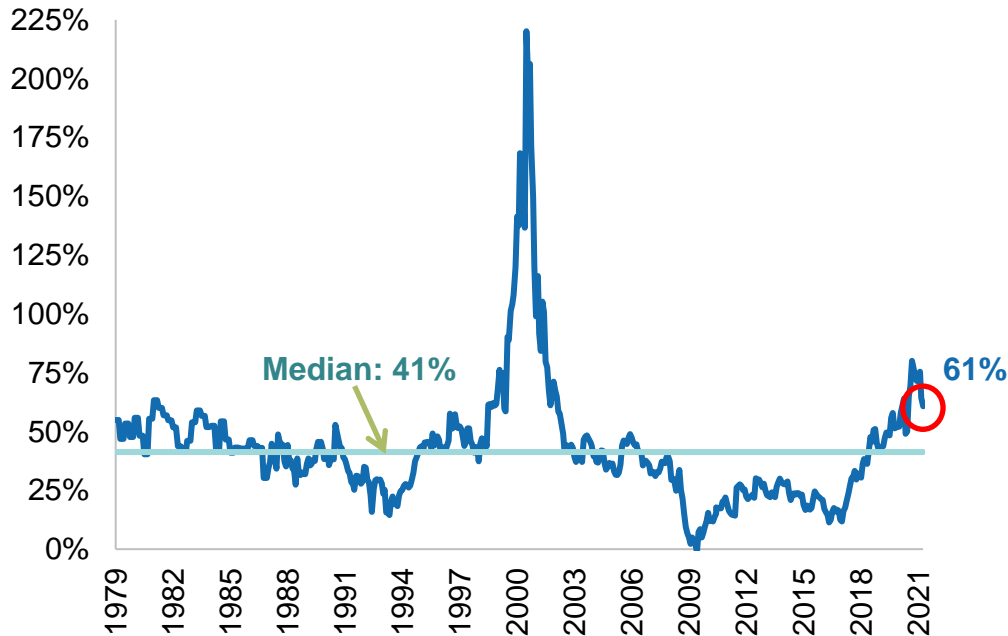
Source: FactSet as of 3/31/21. The performance data quoted represents past performance, which is not an indication or a guarantee of future results.

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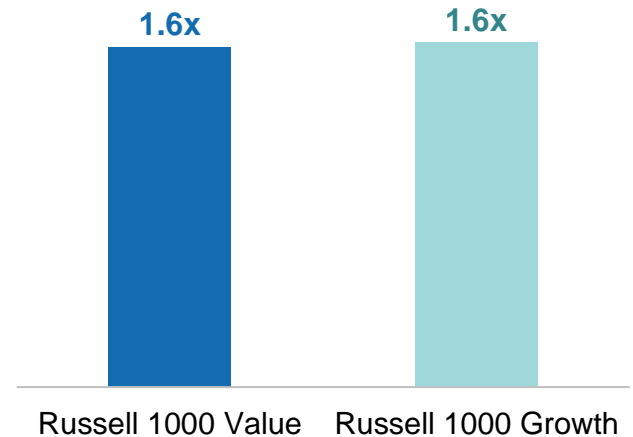
Style Wars What Does Growth Cost?

- Recent Value stock appreciation has lowered the premium at which Growth stocks trade

Russell 1000 Growth Relative to Russell 1000 Value P/E



Russell 1000 Growth vs. Russell 1000 Value PEG Ratio



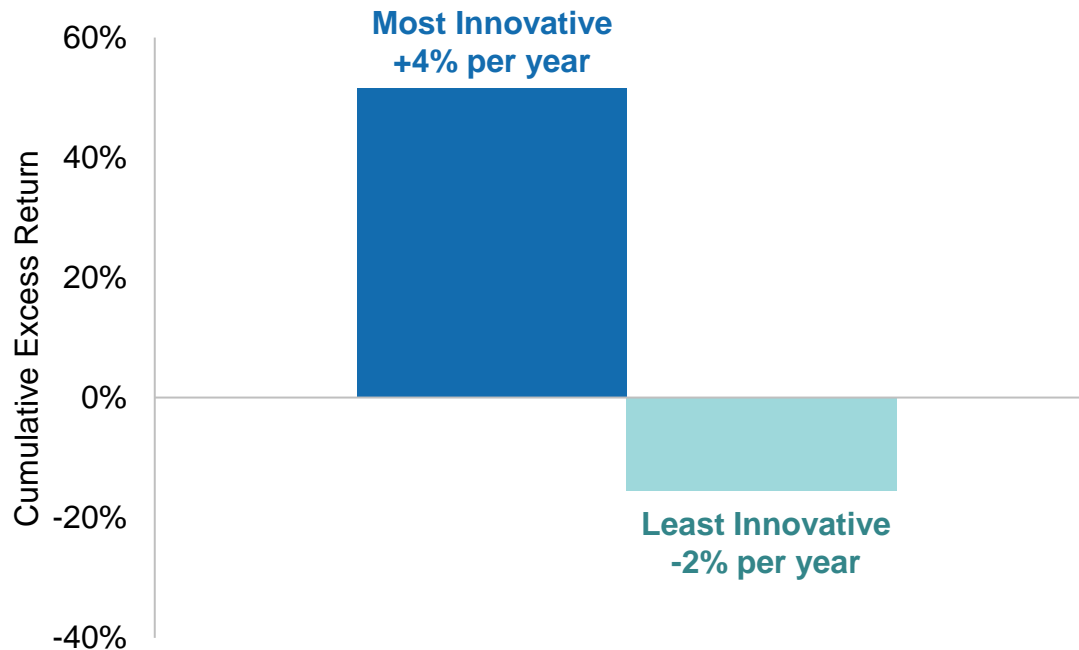
Source: FactSet as of 3/31/21. PEG ratio is P/E divided by long-term growth rate. The performance data quoted represents past performance, which is not an indication or a guarantee of future results.

Style Wars

A Powerful New Investing Factor?

Studies have shown and our research demonstrates that the most innovative companies grow their sales, earnings, and stock prices faster*

Innovative Companies Have Outperformed Over the Past Decade



Source: FactSet. Most/least innovative stock excess performance is derived from highest and lowest S&P 1500 quintiles based on R&D as % of sales, normalized for market value, using one month returns for 10 years ending February 2021. *Baruch Lev and Suresh Radhakrishnan, "The Stock Market Valuation of R&D Leaders." **The performance data quoted represents past performance, which is not an indication or a guarantee of future results.**

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The following positions represented the noted percentages of Alger assets under management as of December 31, 2020: Microsoft Corp., 4.54%; Facebook, Inc., 2.14%; and Alphabet, Inc. 2.24%.

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