

ALGER

Inspired by Change, Driven by Growth.

Spring 2023

Capital Markets: Observations and Insights

Inflation in Retreat?



Alger is a signatory to the PRI and carbon neutral.

Inflation in Retreat?

We believe that several massive tailwinds to inflation have recently reversed with important economic and investing implications. First, the huge expansion of the money supply has now turned into contraction as we had anticipated.* Second, fiscal policy is no longer stimulative and hawkish political sentiment is building. Third, supply chain constraints have eased significantly. These developments may contribute to a decline in inflation and help maintain relatively low interest rates over the next year, in our view.

While there are important structural drivers of longer-term inflation, such as the move to supply chain reliability over efficiency, increased focus on environmental priorities, and labor supply issues, we believe they may be offset by an acceleration in innovation driving higher productivity and increased price transparency.

If we are correct, and inflation falls and interest rates stay low, that may remove a headwind that so-called long duration, or growth stocks, have experienced over the past couple of years. In our view, without valuation compression to contend with, growth stocks are well-positioned, as they may benefit from the increased pace of innovation that we see in the economy, in areas such as artificial intelligence, the internet of things, genomics, and new surgical technologies.



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* Alger, Capital Markets: Observations and Insights, Autumn 2022.

Key Observations and Themes

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With several massive tailwinds to inflation having recently reversed, we discuss the possible economic and investing implications.

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The lagged impact of tightening monetary policy is working to slow the economy, in our view. We explore leading indicators, housing, bank lending, debt levels, and more.

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Although the short-term macroeconomic environment may be challenging, the long-term future of the economy and investing is very bright, in our view.

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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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Powerful structural forces may keep the long-term trend of growth outperformance intact, in our view.

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Making Better Decisions

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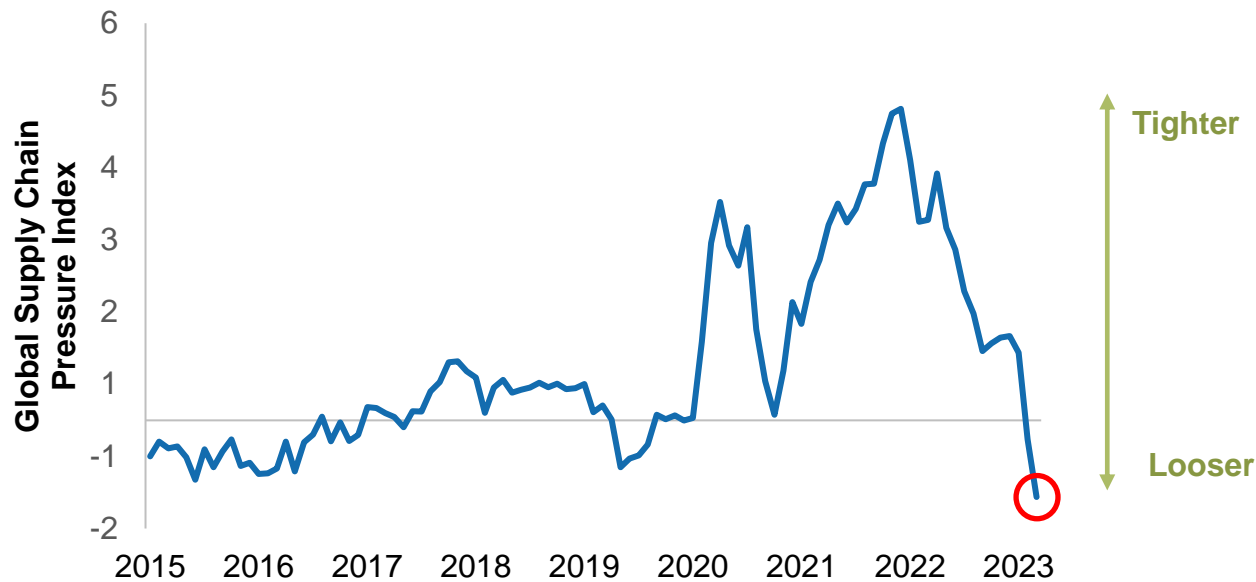
We provide tools that we believe can be used for better decision making in both investing and life.

Inflation in Retreat?

No More Kinks in the Supply Chain

- As Covid restrictions have been eliminated globally, inventories of raw materials, components, and finished goods have become more plentiful, transportation costs have come down, and supplier delivery times have sped up

Global Supply Chain Pressures Have Eased

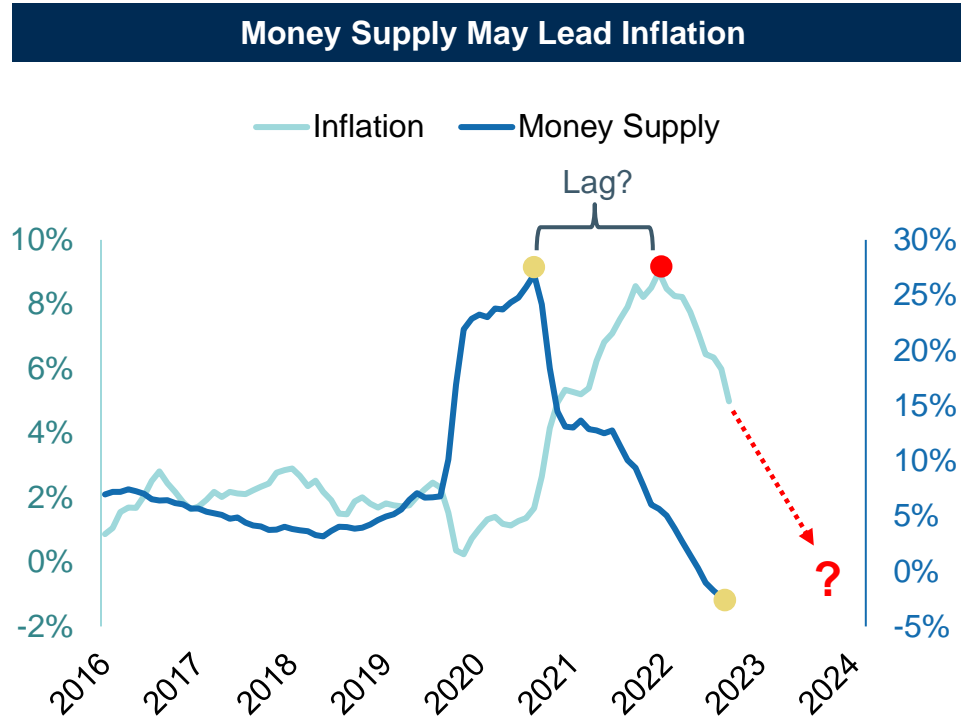


Supply chain constraints have been removed

Source: Federal Reserve Bank of New York Liberty Street Economics. The Global Supply Chain Pressure Index (GSCPI) is global measure that encompasses several indicators used to capture supply chain disruptions. Last data point is March 2023.

Inflation in Retreat? Money Drain

- According to the U.S. Federal Reserve, monetary policy works with a long lag
- We believe the reduction in the money supply may lead to a decline in inflation over the next year



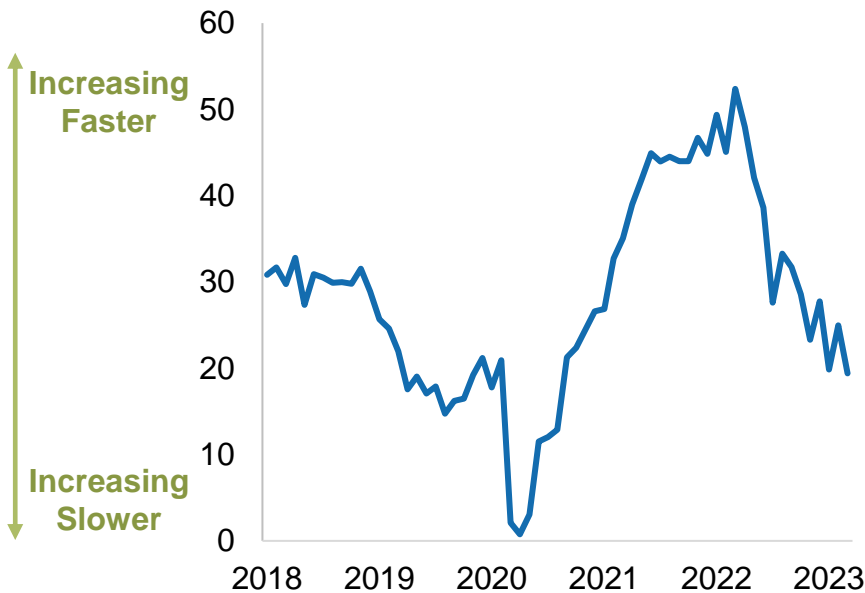
**Lower money supply
= lower inflation?**

Source: U.S. Bureau of Labor Statistics and Federal Reserve. Money Supply is M2. Inflation is the Consumer Price Index (CPI), which measures the monthly change in prices paid by U.S. consumers. The dots represent the high and low points of each data set.

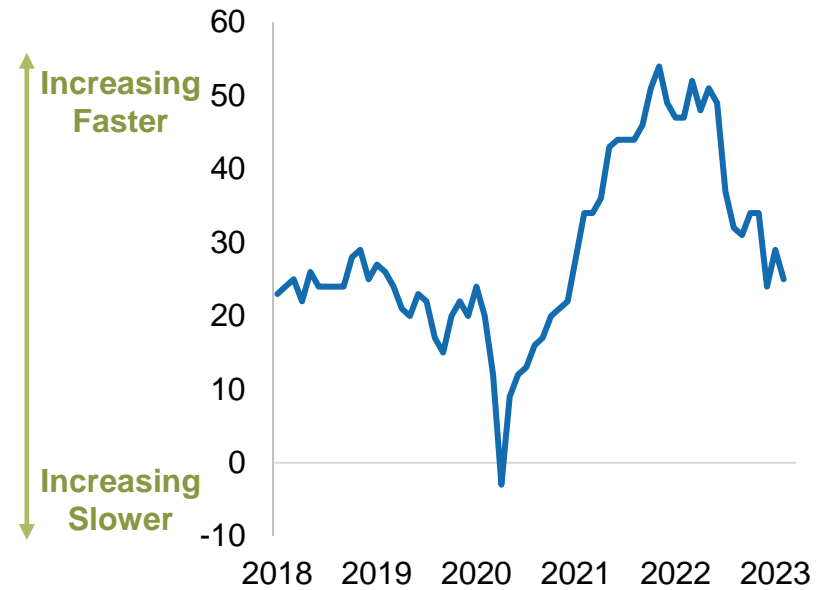
I Inflation in Retreat? Pricing Power Waning

- Companies are expecting to see less rapid selling price increases to customers
- Businesses are planning more moderate price increases

Next 6-Months Expected Prices Received at Manufacturers



Next 3-Month Price Plans at Small Businesses

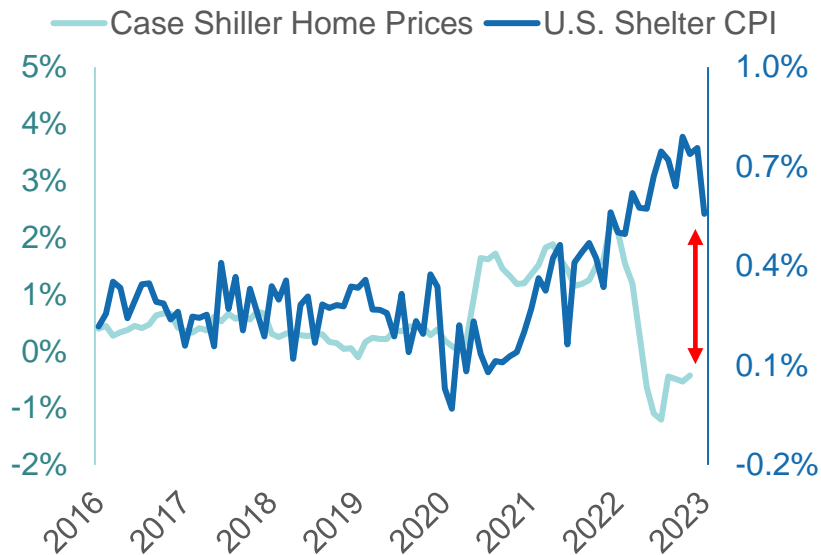


Source: Prices received is average of Philadelphia, Dallas, New York, Kansas City, and Richmond Federal Reserve manufacturing surveys through March 2023. Next 3-month pricing plans at small businesses is from National Federation of Small Business through February 2023.

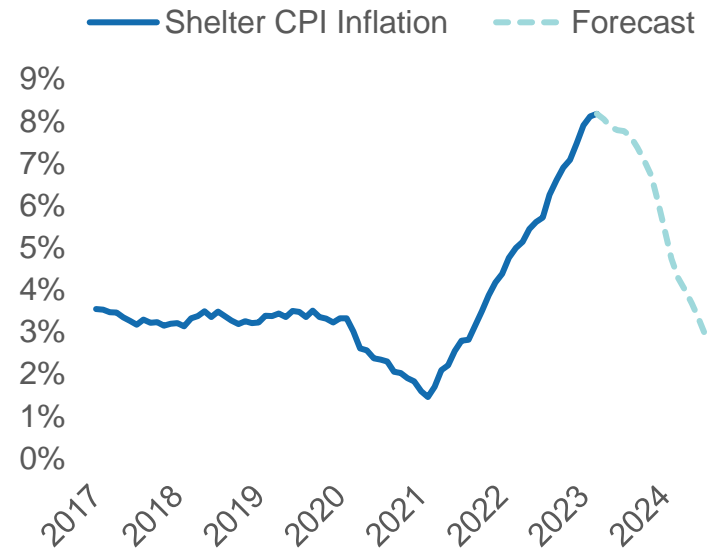
Inflation in Retreat? Will Shelter Costs Collapse?

- U.S. government data shows high shelter inflation, but it lags real-time housing data that shows deflation
- If shelter inflation, which is more than one-third of CPI, follows home prices, then we believe it will fall precipitously over the next year

Month-Over-Month Change in Home Prices



Year-Over-Year Change in Home Prices

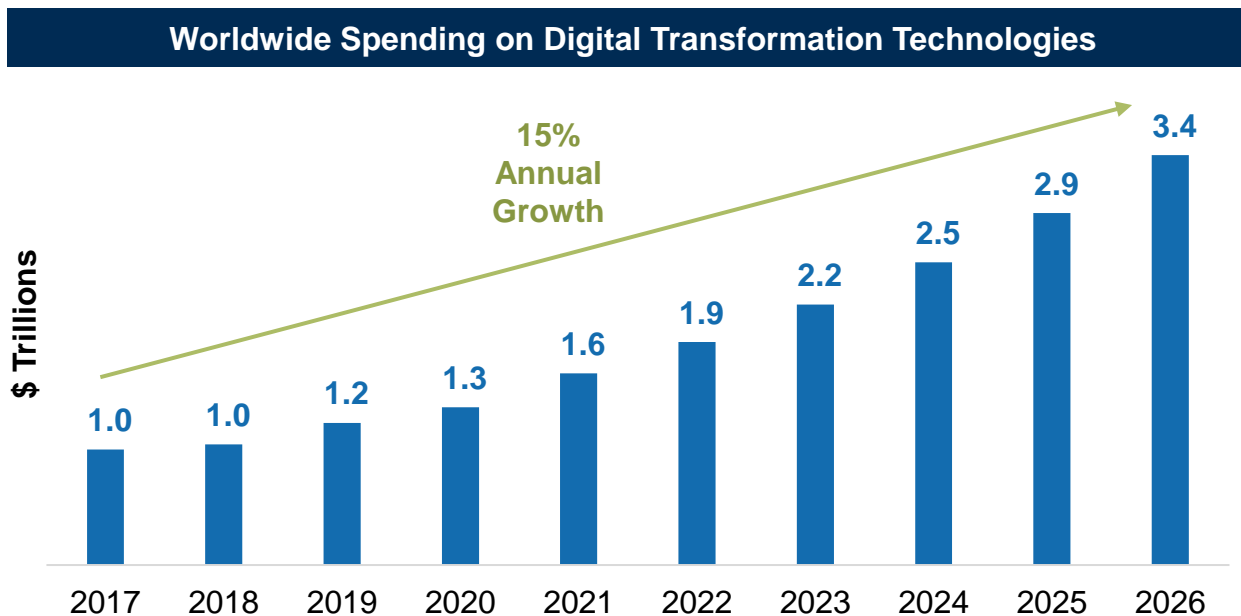


Source: U.S. Bureau of Labor Statistics (Consumer Price Index for Shelter, which is owners' equivalent rent of residences and rent of primary residence) through March 2023, S&P (Case-Shiller Home Price index measures the price level of existing single-family homes in the U.S.) through January 2023, Zillow. CPI Shelter forecast based on historical Zillow home prices.

Inflation in Retreat?

Long-term Deflationary Force: Digital Transformation

- Digital transformation refers to the act of adopting technology and processes to enable businesses to operate digitally
 - Areas of transformation include accounting & finance, HR, legal, security, production, design, supply chain, R&D, marketing, sales, and customer service
- Digitalization may reduce costs, improve productivity, and increase price transparency



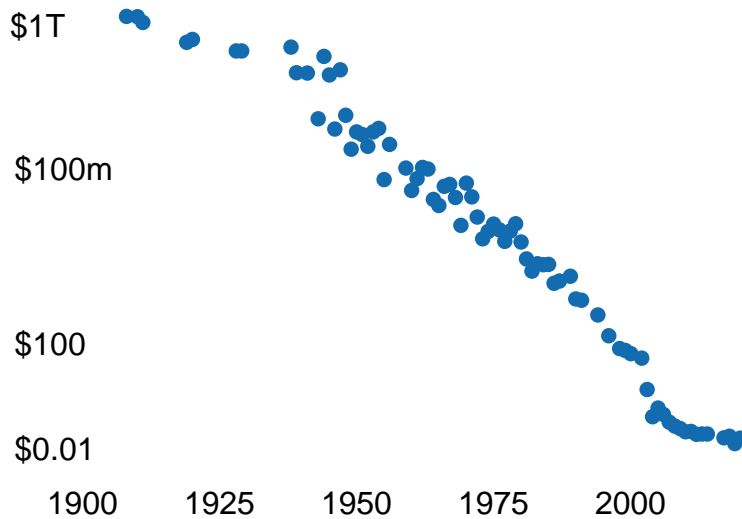
Source: IDC, Statista, October 2022. 2022-2026 data is forecasted.

Inflation in Retreat?

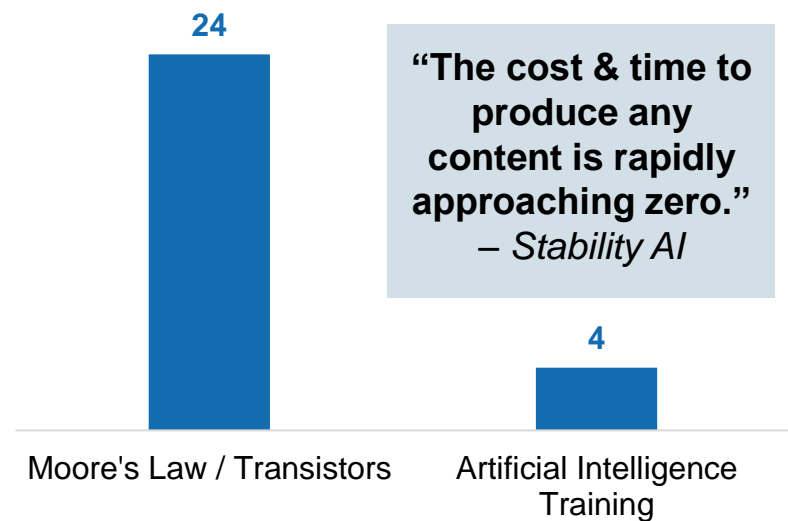
Long-term Deflationary Force: Artificial Intelligence

- The declining cost of computing has been a huge deflationary force in the economy, in our view
- We believe the incredible speed of artificial intelligence will be an even greater driver of cost reduction

Cost of Computing Over Time
\$/ Million Instructions per Second



Doubling Time
(in Months)

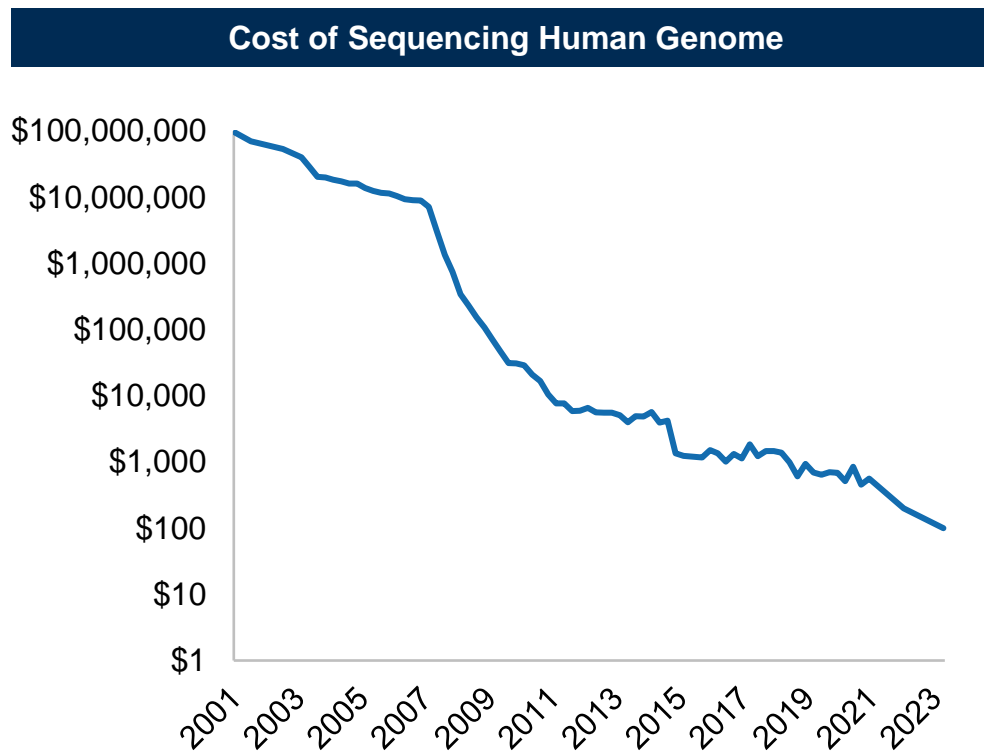


Source: Cost of computing from Luke Muehlauser and Lila Rieber, “Exponential and non-exponential trends in information technology” and Alger, in real terms (2004 dollars). Doubling time from Intel, Our World in Data, Alger. Doubling time refers to the amount of compute or “training” utilized by AI programs, while Moore’s Law refers to length of time that it takes for the number of transistors per integrated circuit to double. Evaluation periods vary.

Inflation in Retreat?

Long-term Deflationary Force: Genomics

- As the cost of DNA sequencing comes down, the ability to predict which diseases will strike whom and how best to attack those diseases will be greatly improved, in our view



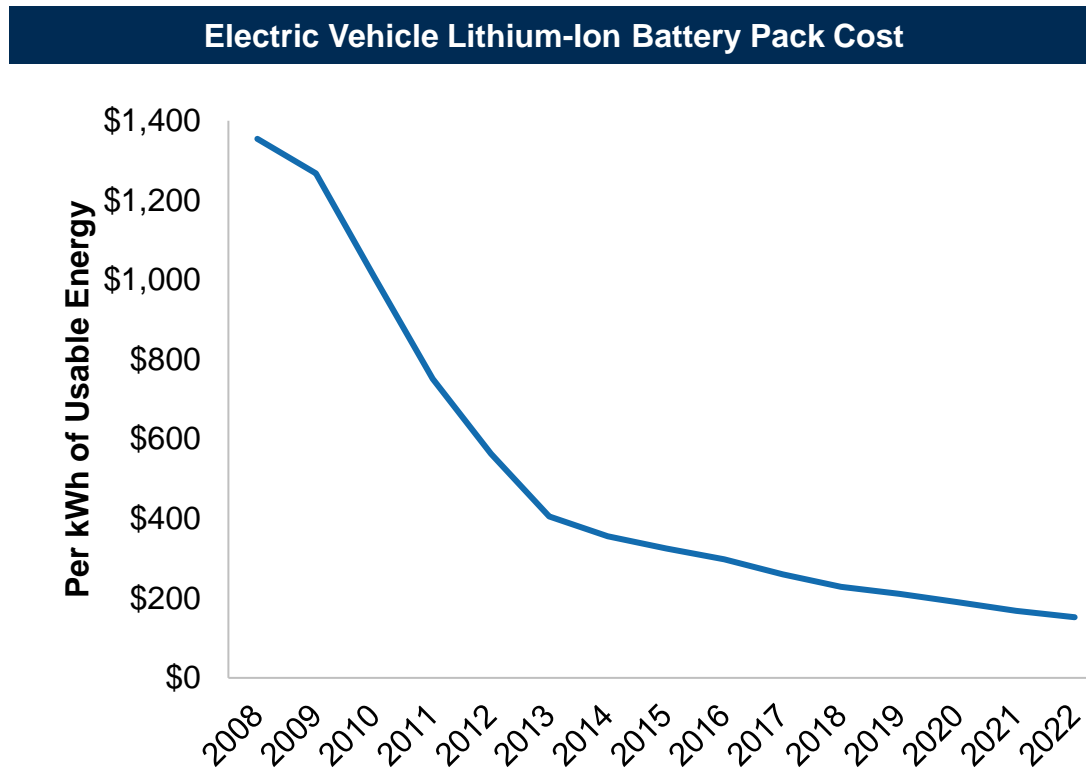
DNA sequencing cost has come down even faster than Moore's Law would have suggested

Source: National Human Genome Research Institute through 2021. 2022 and 2023 data based on comments from Illumina and Complete Genomics, respectively.

Inflation in Retreat?

Long-term Deflationary Force: Electric Vehicles

- The cost of a lithium-ion battery pack, which powers an electric vehicle, continues to decline and in our view will drive automobile and transportation costs significantly lower



Lower battery prices driving down EV costs

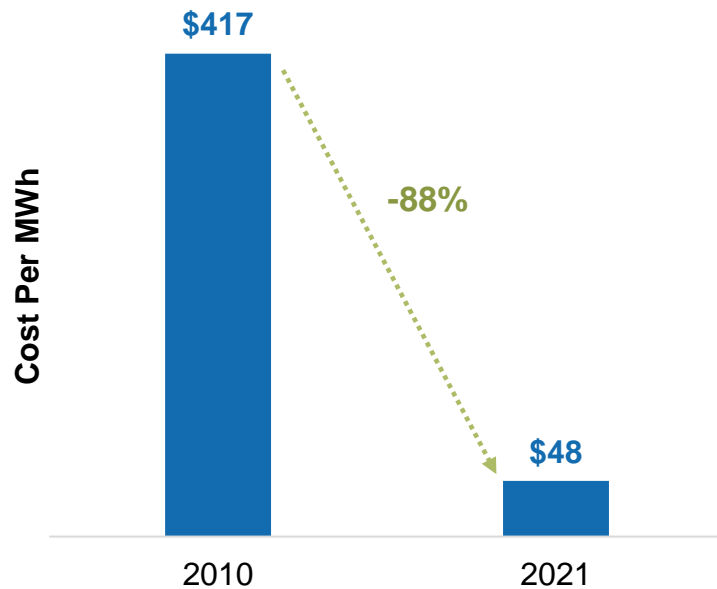
Source: U.S. Department of Energy Office of Energy Efficiency & Renewable Energy. Data is adjusted for inflation or in constant dollars.

Inflation in Retreat?

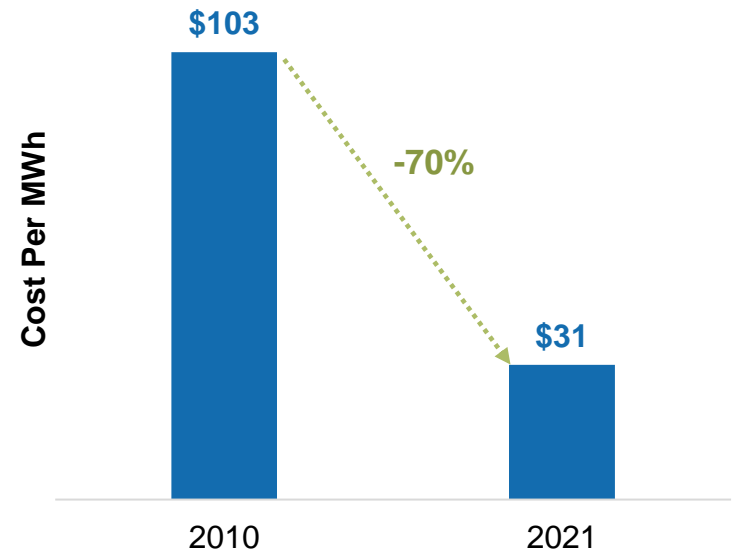
Long-term Deflationary Force: Energy

- The innovation seen in design and manufacturing optimization is expected to continue to drive down the costs of renewable energy sources, which in many cases are already cheaper than fossil fuels

Solar Costs Plummeting



Wind Costs Plummeting

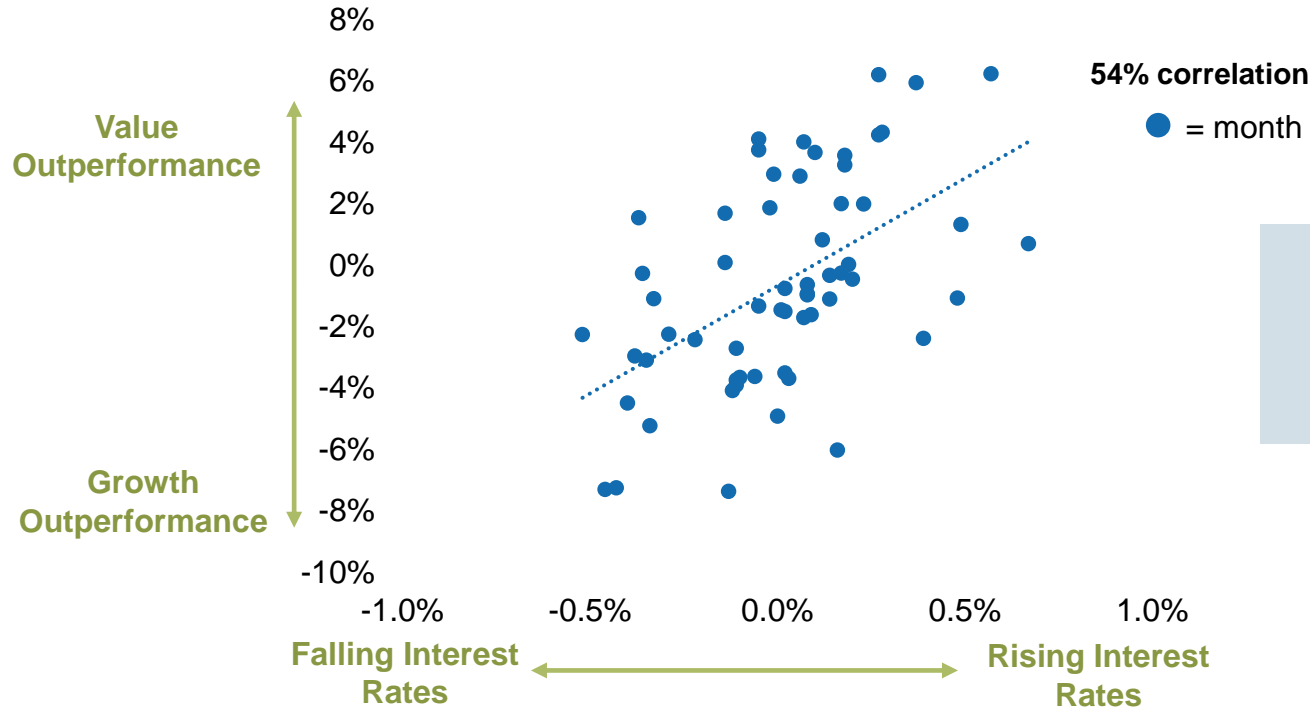


Source: IRENA renewable cost database. Levelized cost of energy for solar is global based on utility scale projects and wind is based on North America cost.

Inflation in Retreat? Style Implications

- Lower inflation and subdued interest rates may eliminate the headwind that long duration assets, such as growth equities, have encountered over the previous couple of years as interest rates have risen

Value and Growth Historical Performance vs. Interest Rates Monthly Change



Will lower inflation help growth equity performance?

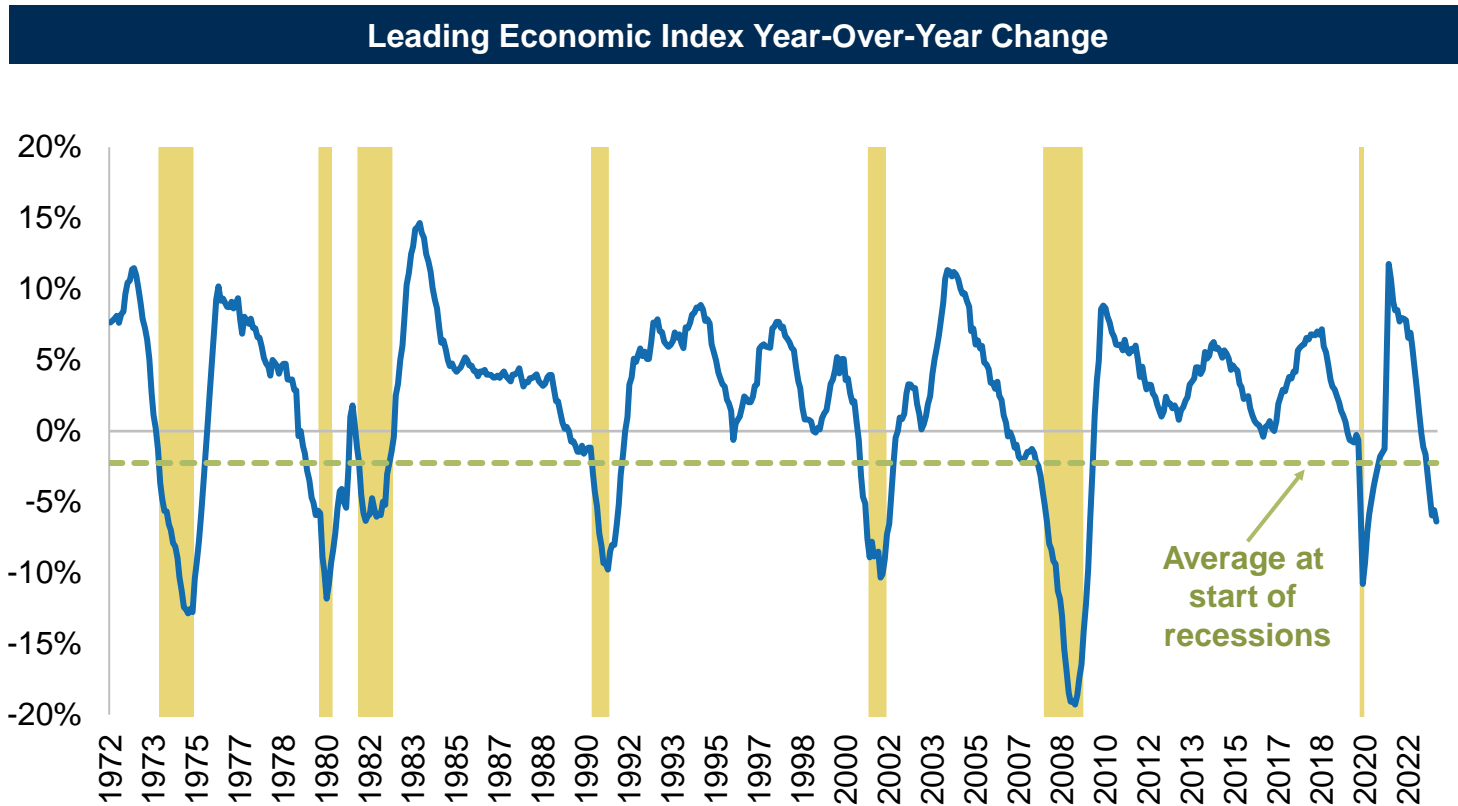
FactSet. Y-axis is monthly return of Russell 3000 Value less Russell 3000 Growth return. X-axis is monthly change in 10-year U.S. Treasury bond yield. Monthly data spans March 2018-March 2023. Correlation is a statistical measure that shows how two variables are related to each other. Chart data as of January 2023. **The performance data quoted represents past performance, which is not an indication or a guarantee of future results.**



Economic Outlook

The Leading Edge

- The Leading Economic Index has historically declined preceding recessions



Source: The Conference Board with last data point for February 2023, NBER. The Leading Economic Index (LEI) is a monthly index of 10 economic components used to predict the direction of global economic movements in future months. Average at start of recessions utilizes data going back to 1960.



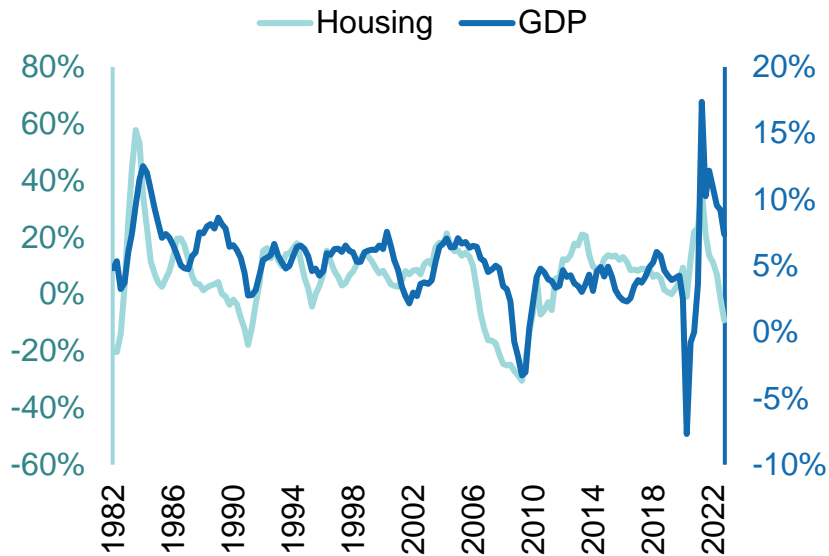
Economic Outlook

Housing's Message

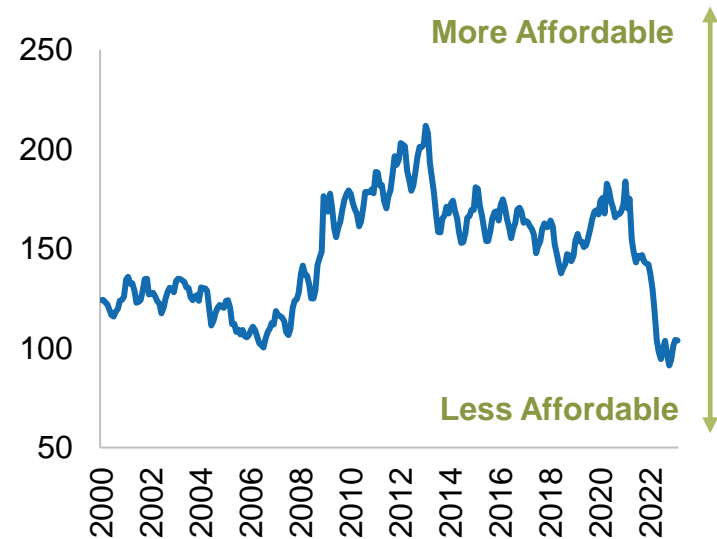
- Changes in housing have historically led growth in the overall economy

- Even after its recent weakness, U.S. housing prices still look expensive and are set for continued softness, in our view

Housing vs. Gross Domestic Product (GDP) Year-over-Year Change



Housing Affordability Index



Source: U.S. Bureau of Economic Analysis (Housing is fixed residential investment). Housing Affordability Copyright ©2023 "Housing Affordability Index" NATIONAL ASSOCIATION OF REALTORS®. All rights reserved. Reprinted with permission. Housing Affordability Index measures whether or not a typical family earns enough income to qualify for a mortgage loan on a typical home at the national and regional levels based on the most recent price and income data).

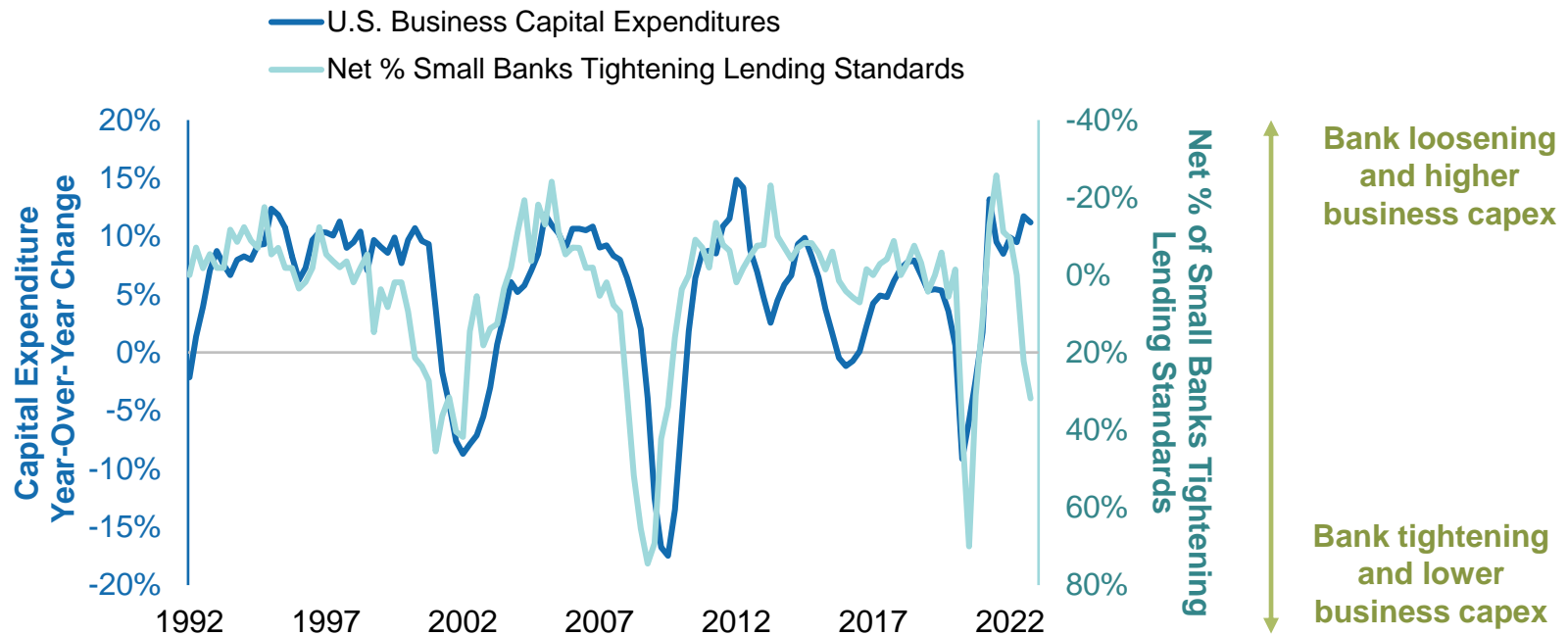


Economic Outlook

Lower Lending?

- There is a strong relationship between small bank lending standards and U.S. corporate business spending (-73% correlation with two quarter lead)
- The issues within the small bank industry may serve to further constrict lending and therefore capital expenditures

Lending Standards Have Historically Impacted Capital Expenditures



Source: Net percentage of small banks tightening lending standards from the Federal Reserve. U.S. business capital expenditures (“capex”) is nonresidential gross domestic fixed investment from the U.S. Bureau of Economic Analysis. Correlation is a statistical measure that shows how two variables are related to each other. Chart data as of January 2023.

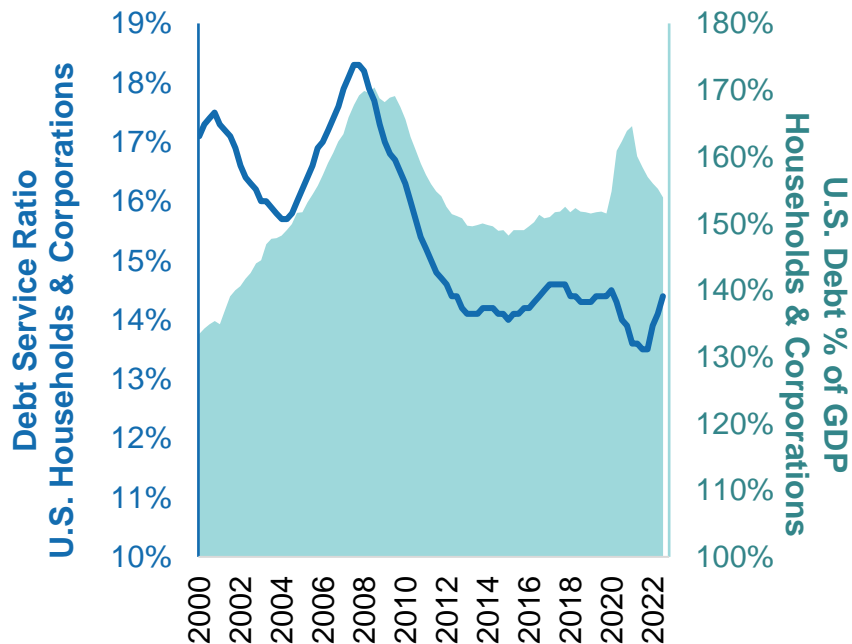


Economic Outlook

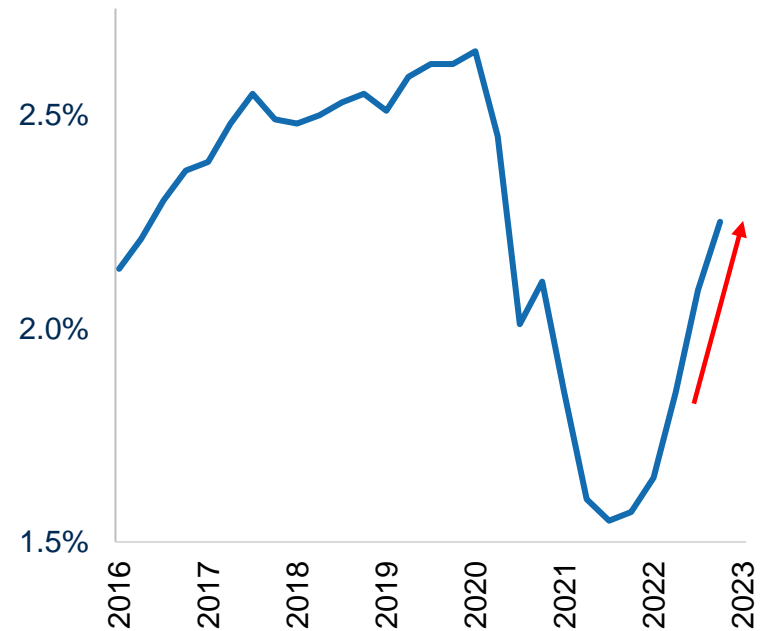
Degrees of Debt

- While U.S. private sector debt servicing ratios are low, debt balances are not...
- ...and rising borrowing rates and decelerating income growth could trigger increased delinquencies

Debt Service Ratio and Debt Relative to GDP



Credit Card Delinquency Rate at U.S. Banks



Source: Debt and debt service from Bank for International Settlements. The debt service ratio reflects the share of income used to service debt (interest and principal). Last data point for debt and delinquencies are 3Q22 and 4Q22, respectively. Delinquency rate from Board of Governors of the Federal Reserve System.

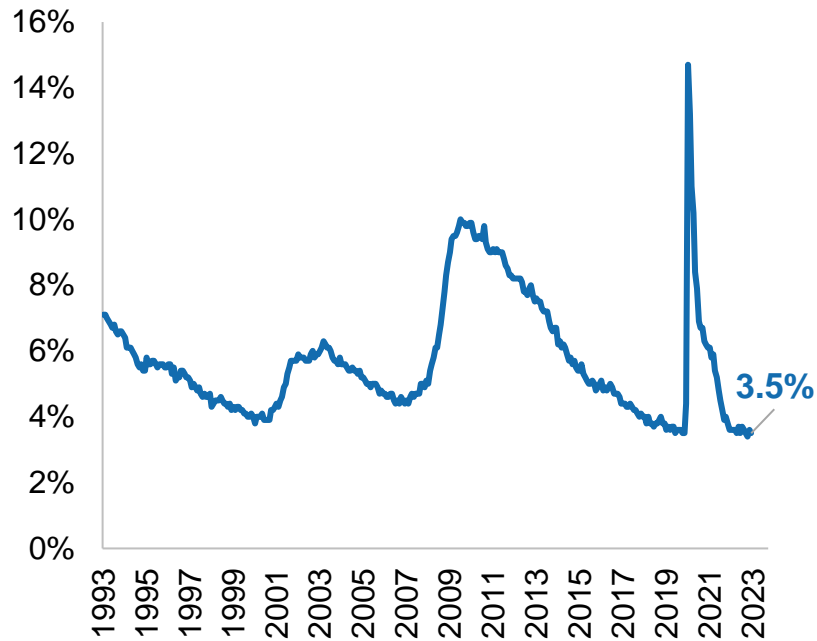


Economic Outlook

Does Solid Employment Prevent Recession?

- The unemployment rate has been historically low...
- ...but that has not necessarily prevented the onset of recession, in the past

U.S. Unemployment Rate



Unemployment Rate and Recessions

Date	Unemployment Rate	Months to Recession
June 1953	2.5%	2
Dec. 1969	3.5%	1
Feb. 2020	3.5%	1
July 1948	3.6%	5
Aug. 1957	3.7%	1
Dec. 2000	3.9%	4
Oct. 1973	4.6%	2
Aug. 2007	4.6%	5

Source: U.S. Bureau of Labor Statistics (March 2023), National Bureau of Economic Research. Table displays lowest unemployment rates within six months of recessions since 1948.



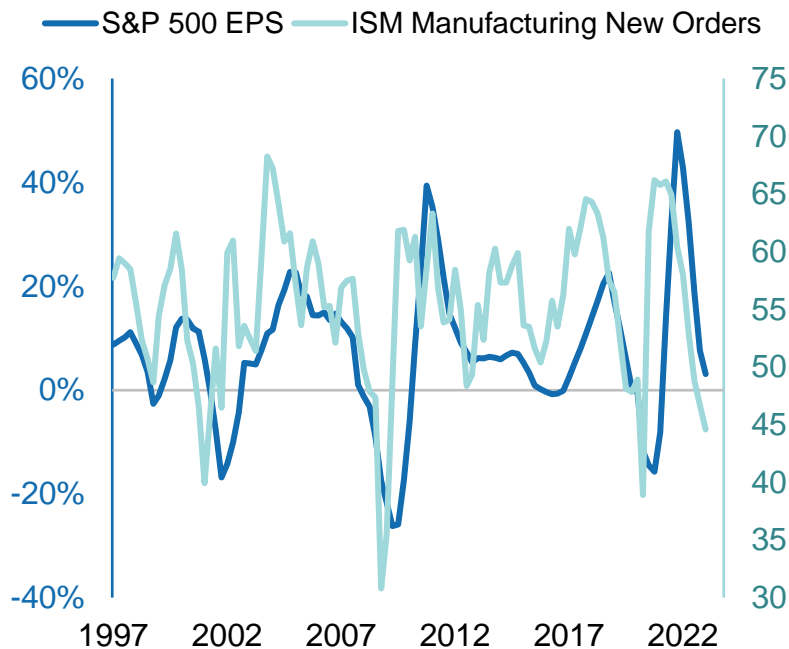
Economic Outlook

Yearning For Earnings

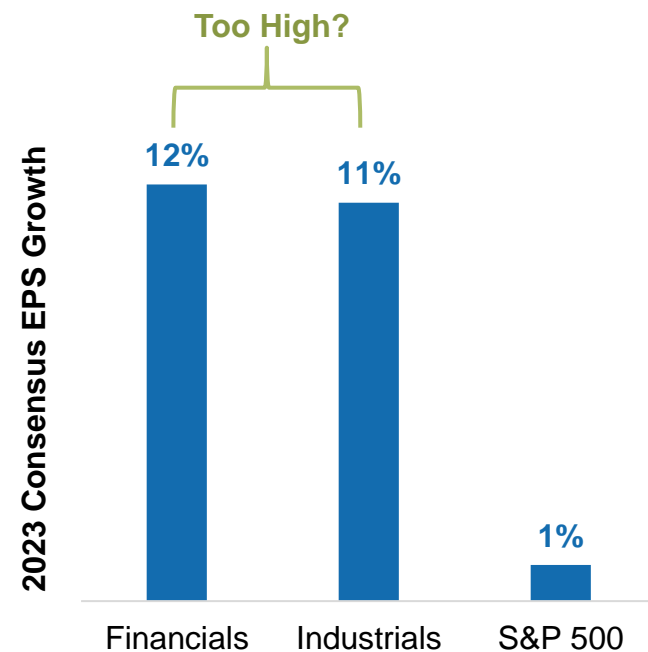
- The corporate earnings recession is in full swing with S&P 500 EPS down in 4Q22 and 1Q23, but leading indicators suggest further declines may be coming

- Earnings estimates may still be too optimistic, particularly for more economically sensitive sectors, in our view

Manufacturing Orders Indicate Declining EPS



Select S&P 500 Sector Estimated EPS Growth



Source: S&P 500 EPS is year-over-year change from FactSet. ISM® Manufacturing New Orders (which indicates the magnitude of growth or decline in new orders from customers of manufacturing firms reported by survey respondents compared to the previous month) from The Institute of Supply Management ISM® Report On Business® – Manufacturing (PMI®). S&P 500 sector EPS is from FactSet, which is aggregating bottom-up consensus analyst estimates. Earnings per share (EPS) is the portion of a company's earnings or profit allocated to each share of common stock.

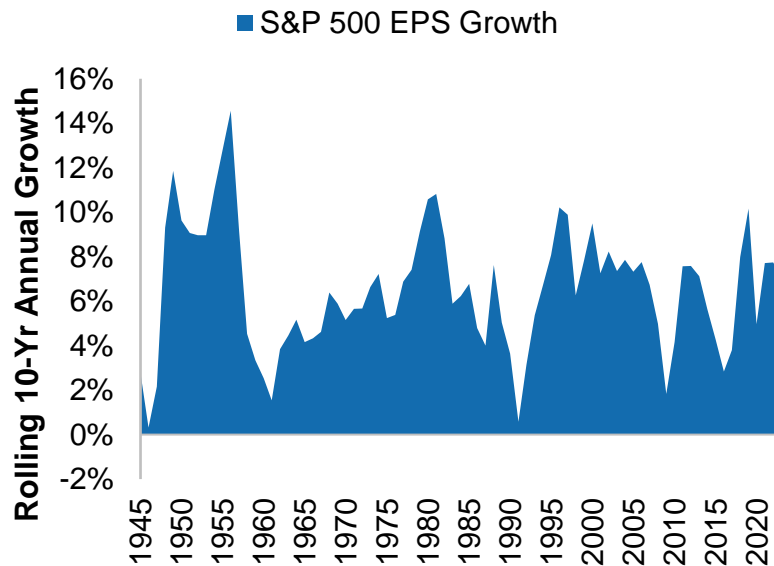


The Long Run

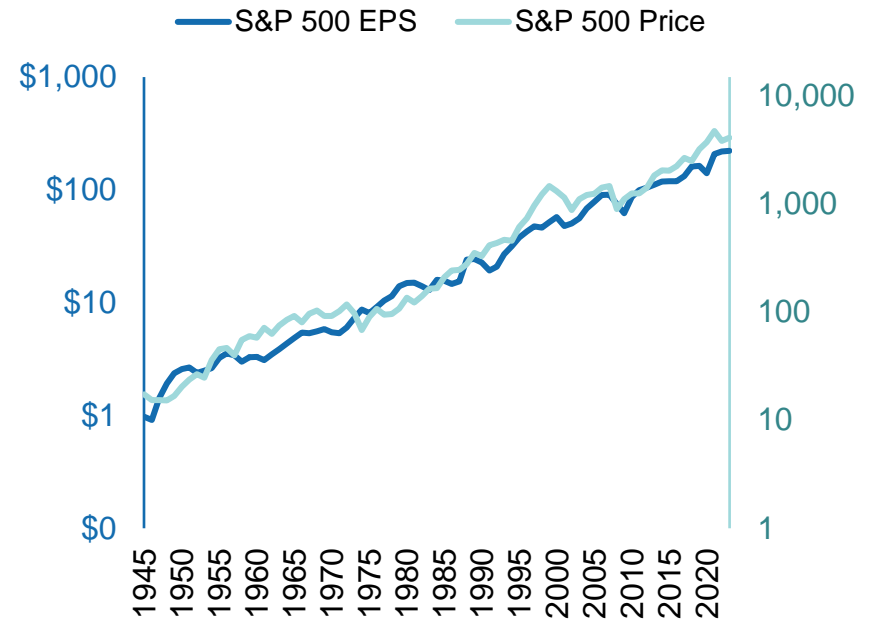
Powerful Long-Term Trends

- Earnings have historically grown over full cycles
- Post WWII, S&P 500 EPS has always grown over 10-year periods
- The S&P 500 price has increased in-line with the 7% annual growth in earnings
- Huge wealth creation despite 12 recessions and several wars

Earnings Have Historically Grown...



...Driving Stocks Prices Upward at a Similar Rate



Source: FactSet. EPS and Price data through 3/31/23. The performance data quoted represents past performance, which is not an indication or a guarantee of future results.



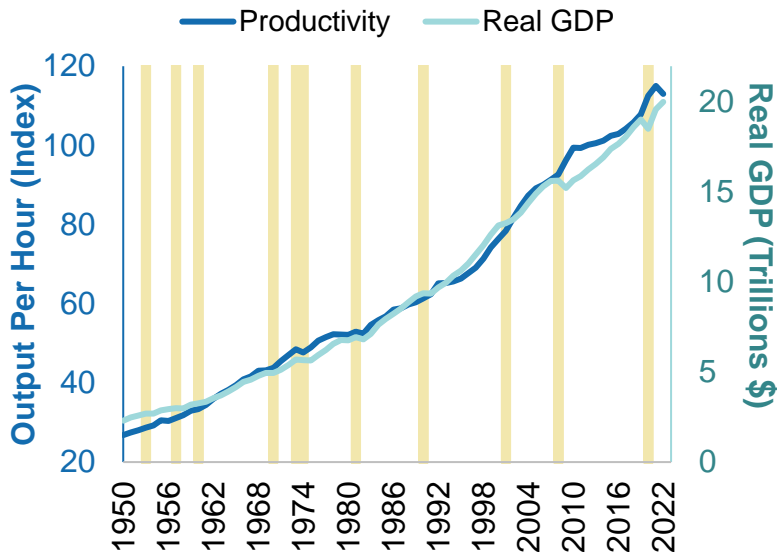
The Long Run

The Engine of Growth

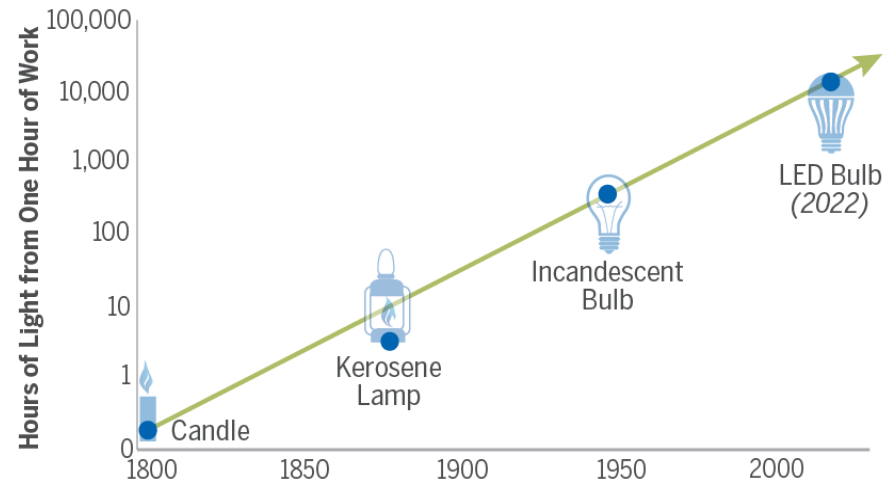
- If earnings drive stock prices and GDP drives corporate earnings, what propels GDP?
 - *Answer:* productivity (output per hour)

- If increasing output per hour is the main ingredient to better living standards over time, what drives productivity higher?
 - *Answer:* innovation

Productivity Improvements Increase GDP



Innovation Drives Productivity

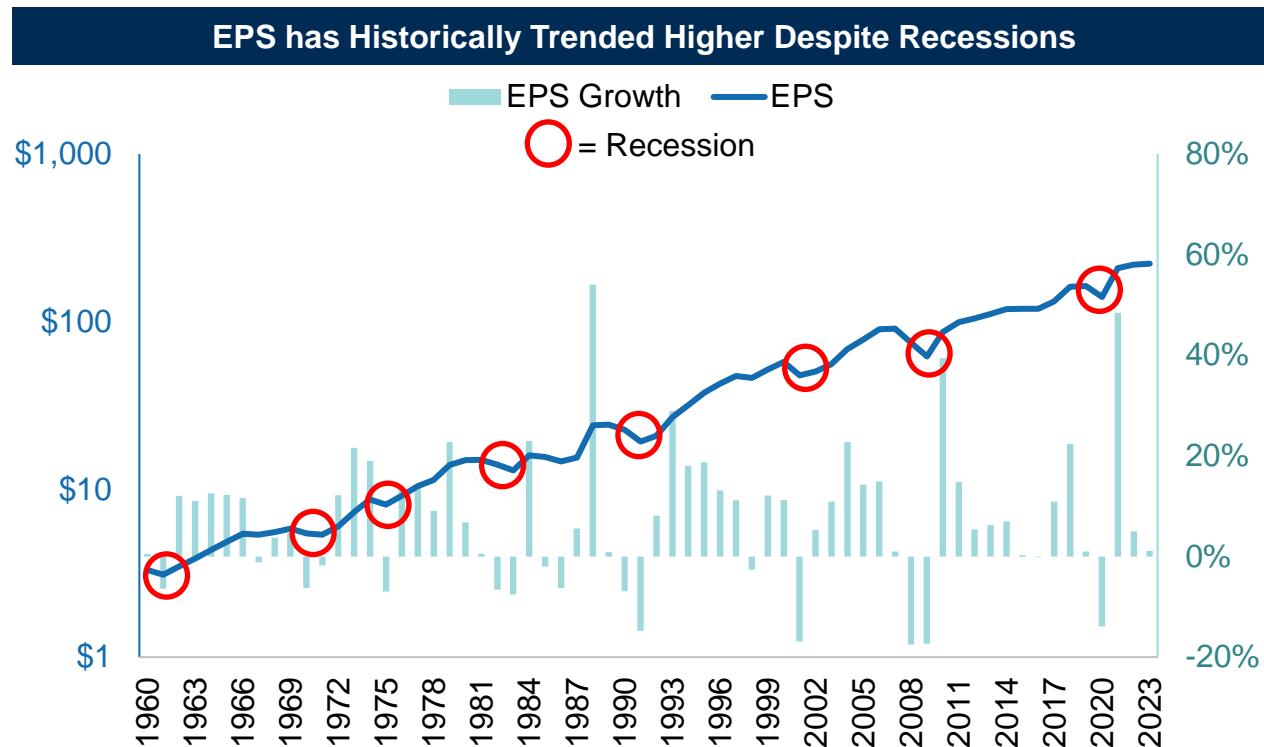


Source: Data for left chart from U.S. Bureau of Labor Statistics and U.S. Bureau of Economic Analysis through 2022. Shaded regions denote U.S. recessions as determined by the National Bureau of Economic Research. Data for right chart from William D. Nordhaus, "Do real output and real wage measures capture reality? The history of lighting suggests not," in "The Economics of New Goods" ed. T.F. Breshnahan and R. Gordon, Chicago University Press, and Alger estimates. Investing in innovation is not without risk and there is no guarantee that investments in research and development will result in a company gaining market share or achieving enhanced revenue.



The Long Run Recessions and Recoveries

- S&P 500 earnings have declined in past recessions, but historically, EPS has reached or nearly reached a new high in the first or second year after the recession ended
 - Temporary EPS declines shouldn't theoretically impact long-term value significantly

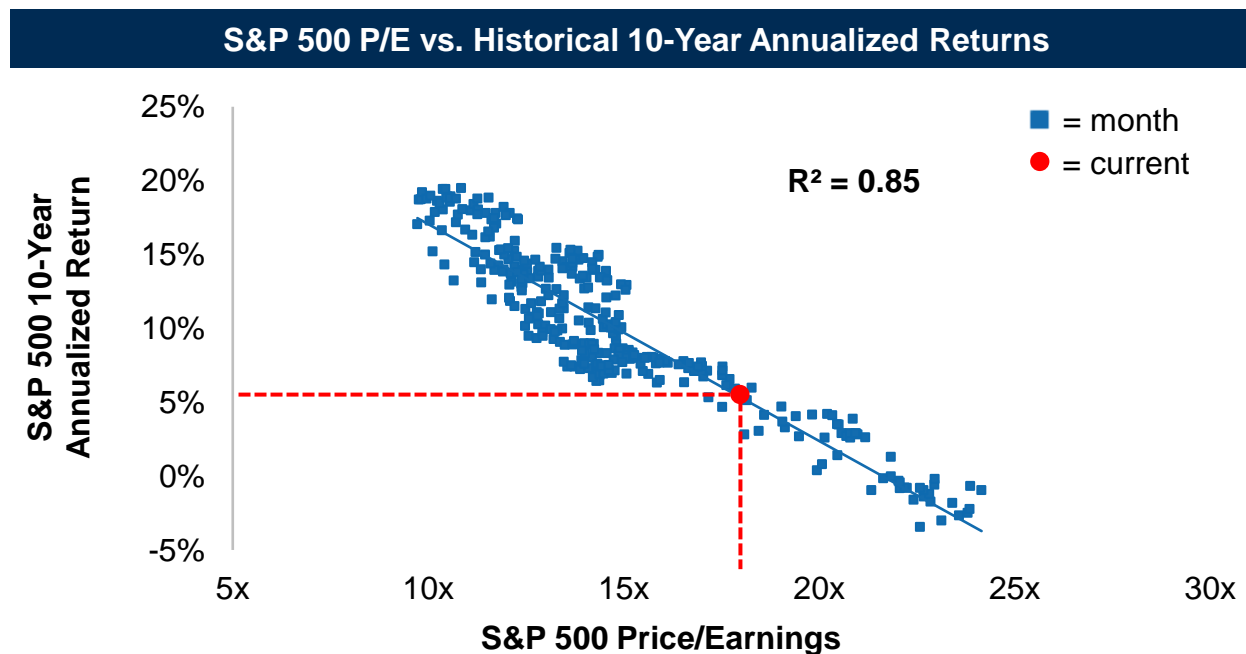


Source: S&P reported EPS 1960-1987. S&P operating EPS 1988-1995, FactSet S&P 500 Operating EPS 1996 to present.



The Long Run Many Happy Returns?

- There is a strong historical relationship between starting equity valuations and subsequent 10-year annualized returns



Source: FactSet. Each dot represents the P/E during that month and the returns generated over the subsequent 10 years. The starting P/E ratio is the price divided by the next 12-month earnings per share estimate at the start of each 10-year period measured. Monthly data through March 2023 and beginning in January 1986. R-squared is a statistical measure used to analyze how differences in one variable can be explained by the difference in a second variable. In the context of the chart, it measures the proportion of the variability of the dependent variable (subsequent 10-year annualized return) that can be explained by the independent variable (price-to-earnings). An R-squared value of 1.00 means that the independent variable (price-to-earnings) perfectly explains the variability in the dependent variable (subsequent 10-year annualized return), while a value of 0.00 means that the independent variable cannot explain any of the variability. In the chart, the R-squared of 0.85 means that 85% of the variability in subsequent 10-year annualized returns can be explained by the price-to-earnings multiple. **The performance data quoted represents past performance, which is not an indication or a guarantee of future results.**

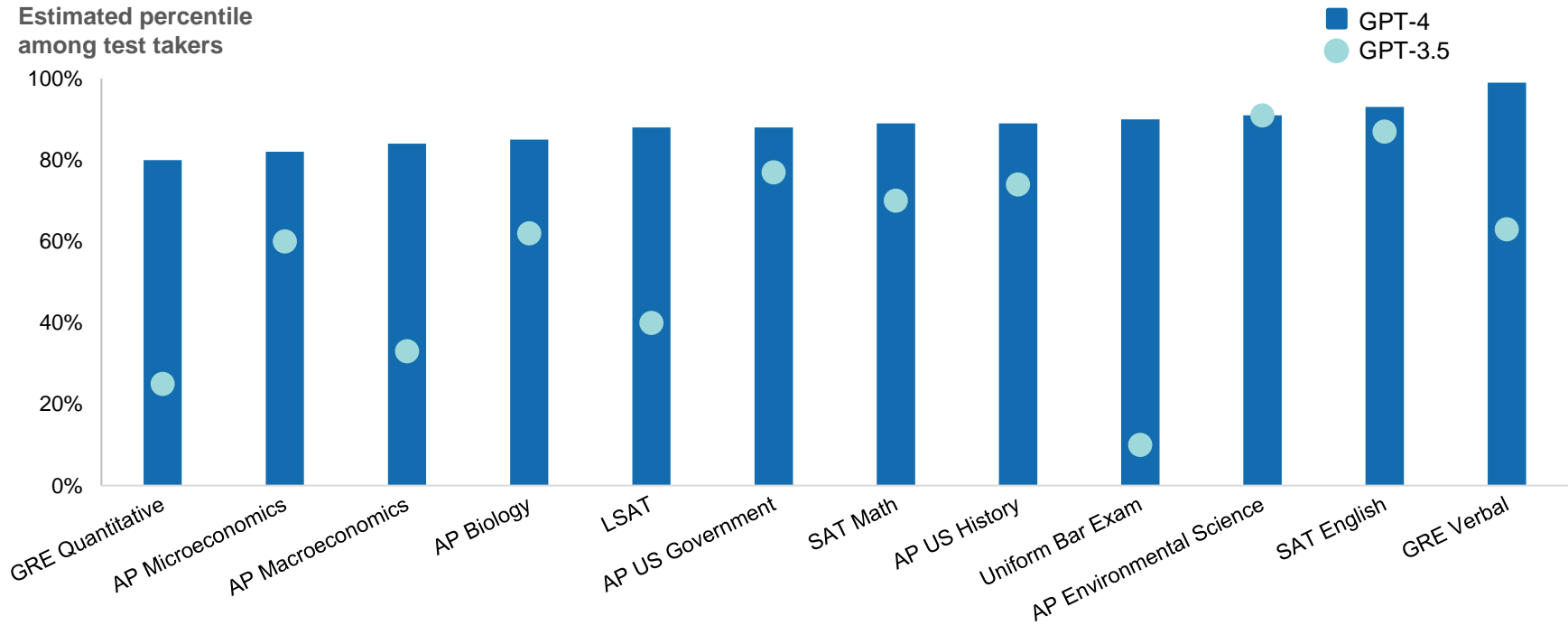
IV

Enduring Themes Artificial Intelligence

- With AI growing much faster than Moore's Law, tremendous progress is being made quickly
- Companies providing AI-based software or hardware have a large opportunity, in our view

AI is Smart and Getting Smarter

Estimated percentile
among test takers



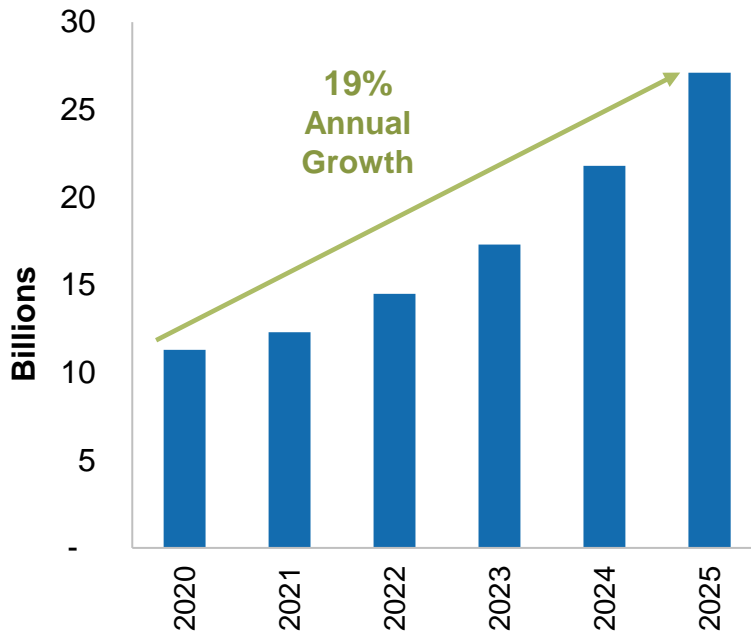
Source: OpenAI (2023). Chat GPT-4, which launched March 13, 2023, is a more advanced language model than Chat GPT-3.5.

IV

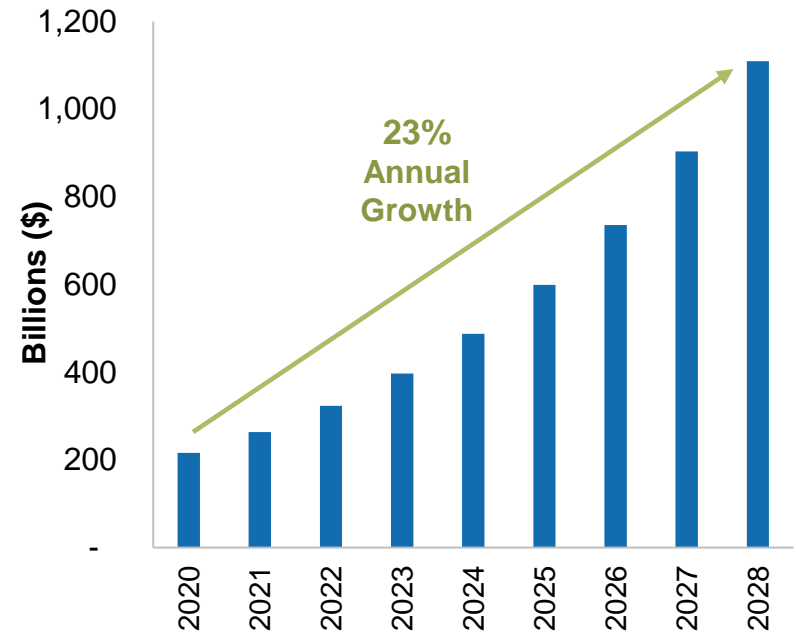
Enduring Themes Internet of Things

- The explosion in connected devices is creating the “Internet of Things” or IoT, transmitting valuable and actionable information
 - Drivers of IoT spending include security, data analytics, efficiencies, reliability, customer service, improved ROI and compliance

Global IoT Connected Devices



Global Industrial IoT Market Size



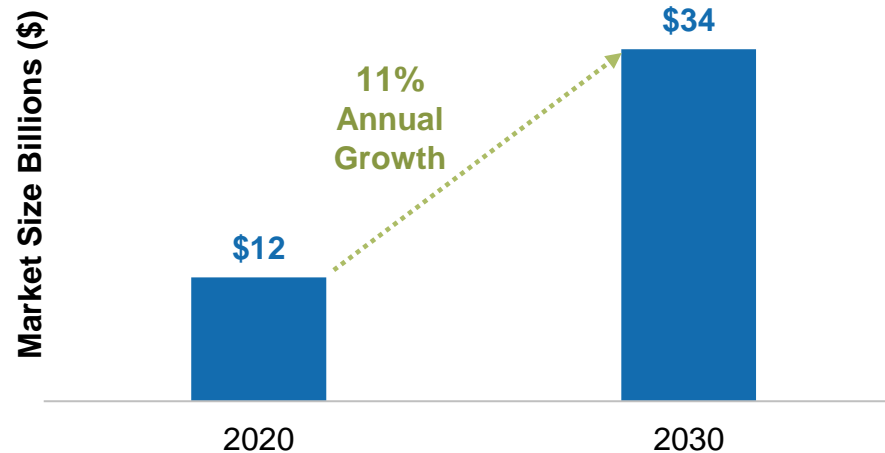
Source: IOT Analytics, September 2021 (2021 – 2025 are estimates), and Grand View Research, March 2022 (2021 – 2028 are estimates).

IV

Enduring Themes Advances in Surgical Technologies

- Improvements in surgical procedures owing to advances in bioengineering and biomaterials should drive improved outcomes for patients and revenue opportunities for innovative companies in our view
 - Robotic surgery
 - Minimally invasive structural heart interventions
 - Organ preservation for transplants

Worldwide Minimally Invasive Surgical Technologies

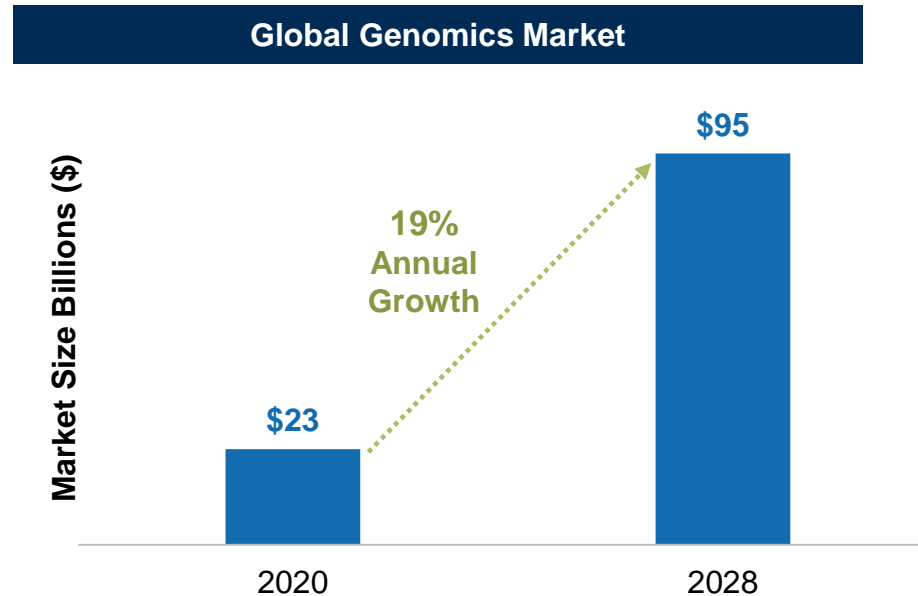


Source: Alger analysis. 2030 is an estimate. Market consists of surgical robotics, percutaneous heart valve repair, and minimally invasive technologies.

IV

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 (e.g., liquid biopsy for early multi-cancer detection)
 - Delivering more efficacious treatments via targeted therapies (e.g., mRNA therapies)

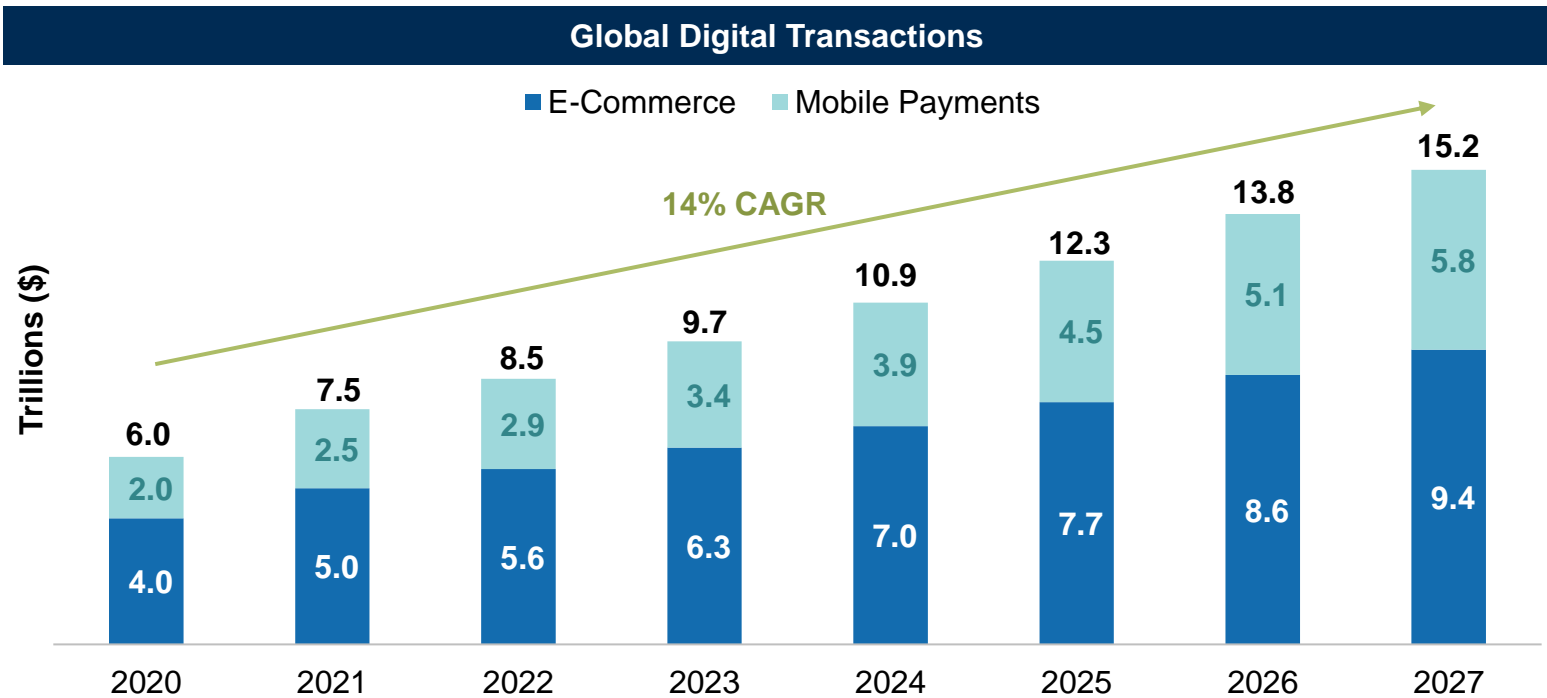


Source: Fortune Business Insights, January 2022. 2028 is an estimate.

IV

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

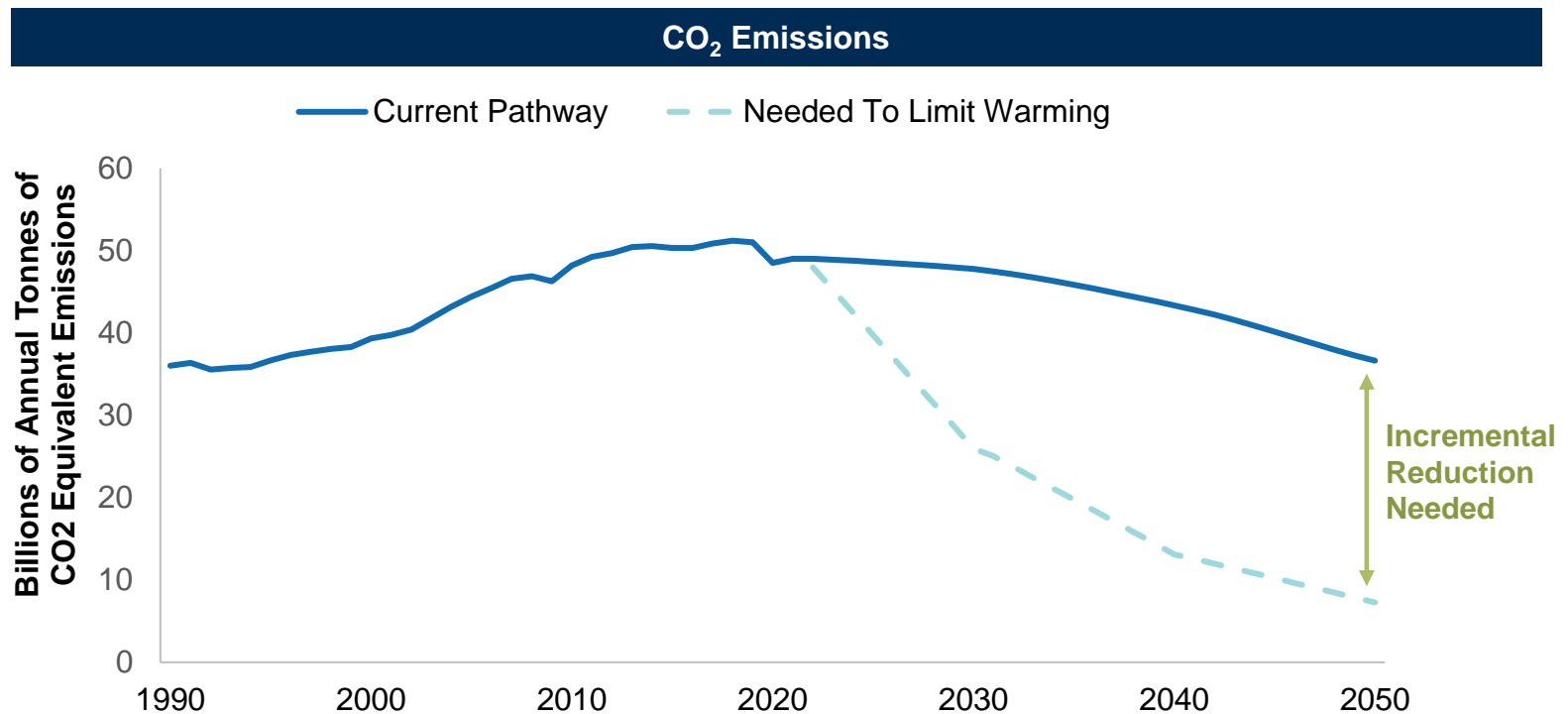


Source: Statista, August 2022 (2022 – 2027 are estimates). E-commerce includes digital remittances. CAGR is compound annual growth rate, the rate of return required for a quantity to grow from its beginning balance to its ending balance. Mobile payments occur when smartphones are used to process transactions using wireless communication or scan QR barcodes.

IV

Enduring Themes Emission Reductions

- The rate of CO₂ emissions is not sustainable in our view and current emission targets need to be reduced further
- Reducing emissions may provide opportunities in alternative energy sources and in electric vehicles and related products and services



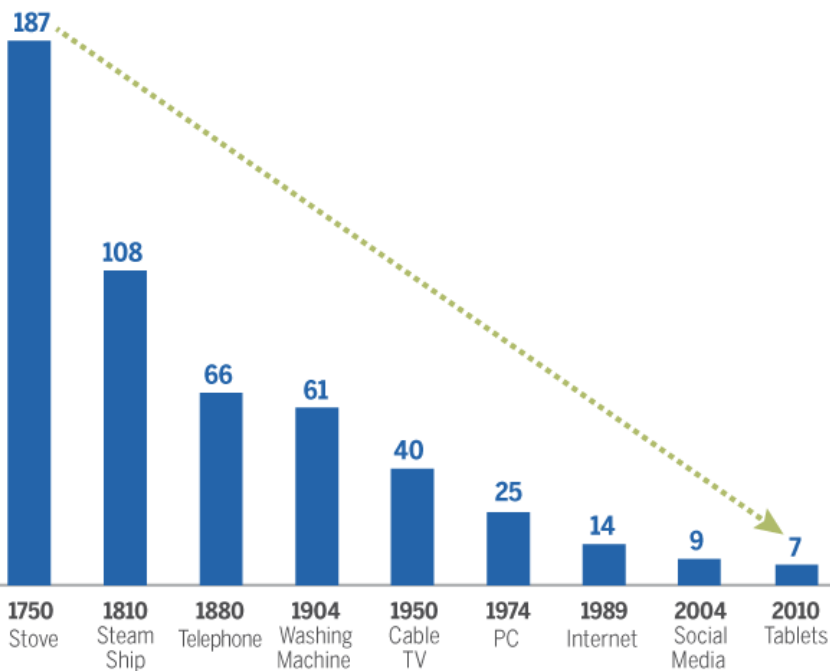
Source: Climate Action Project, May 2021. Current pathway represents average of high and low “pledges and targets” scenario while needed to limit warming is based on median to achieve 1.5 degrees Celsius warming.

V

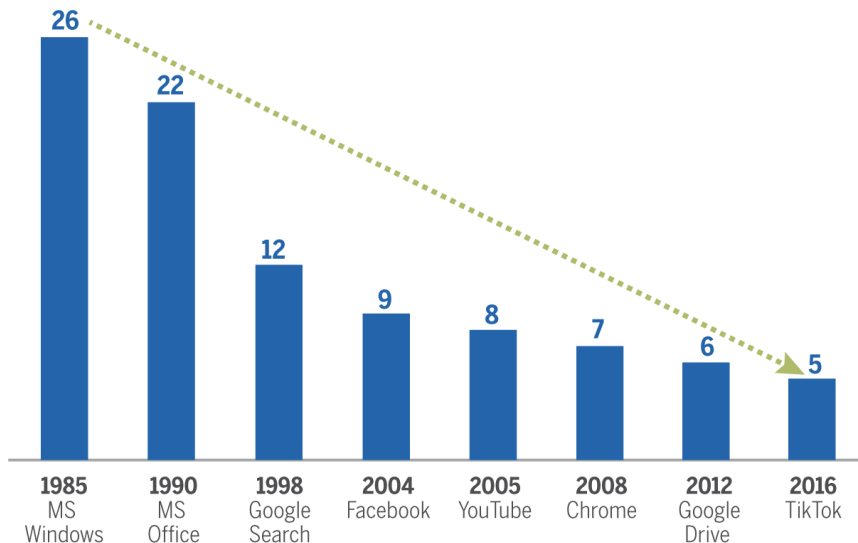
Style Wars Accelerating Change

- 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



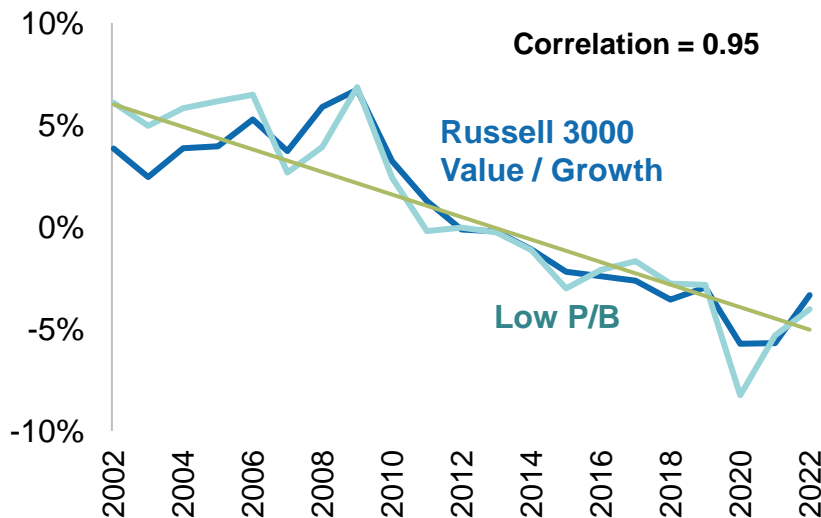
Source: Asymco, Visual Capitalist, company disclosures, Alger estimates.

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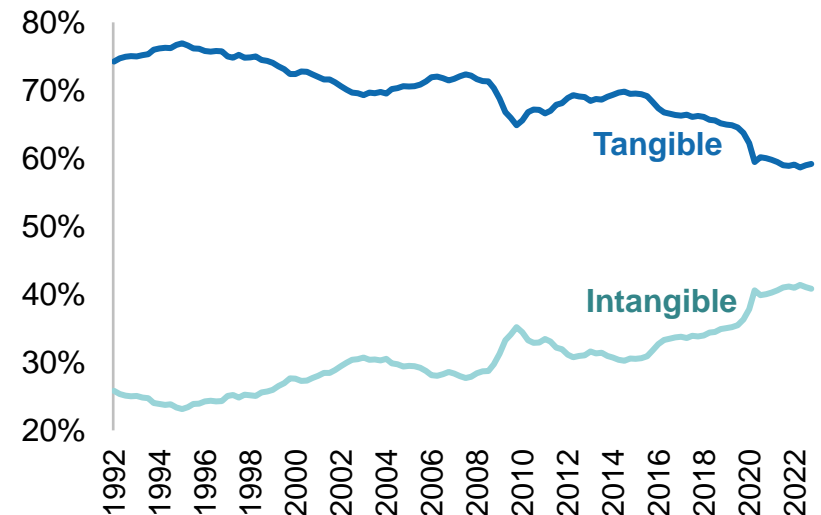
Style Wars Structural Issues Driving Growth vs. Value

- Despite recent outperformance, value stocks have underperformed over the long-term
 - Driven by the very weak performance of the price-to-book valuation metric
- Book value may no longer be as relevant, making current style classification flawed
 - As a result of increasing use of intangible assets that are expensed rather than capitalized

**Value/Growth vs. P/B Cumulative Return
10-Year Rolling Return**



**Business Investment
Intangible vs. Tangible**

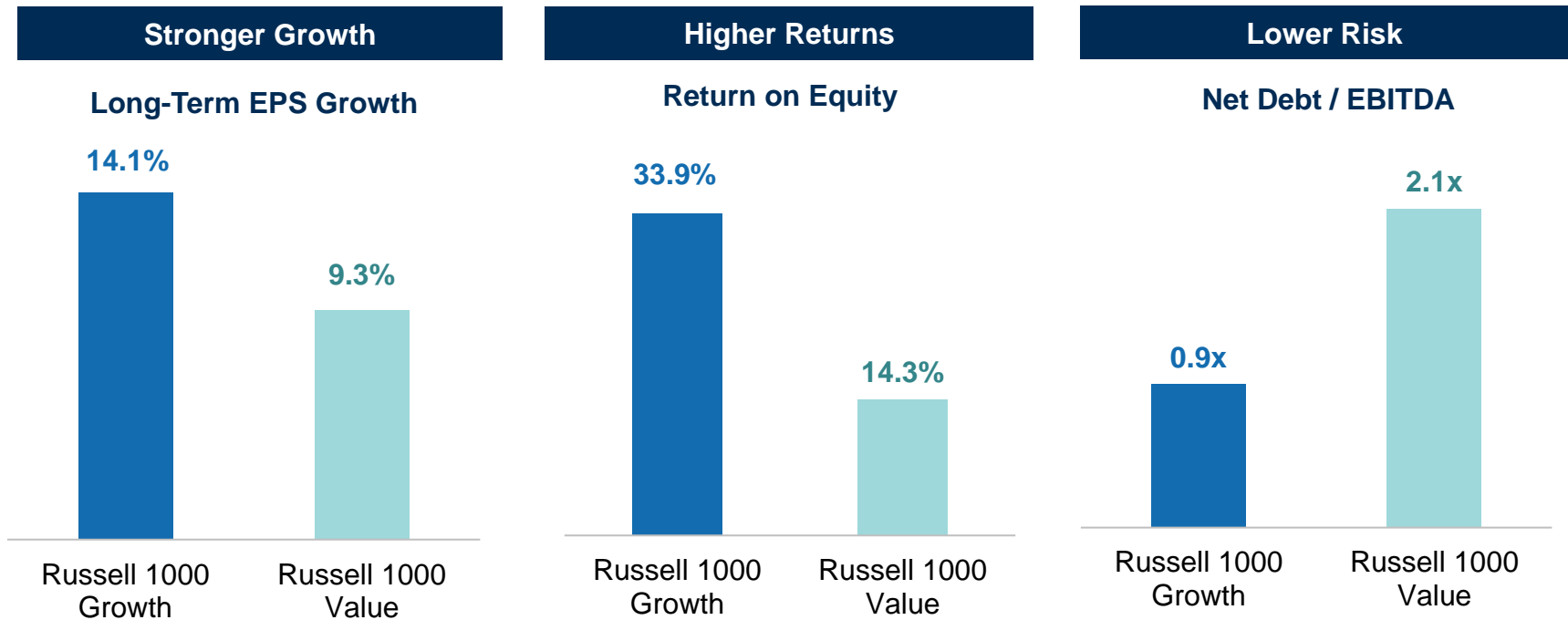


Source: FactSet, Kenneth R. French, FactSet, Bureau of Economic Analysis. Low price-to-book returns are based on the B/P Fama/French factor for the CRSP universe which includes US firms listed on the NYSE, AMEX, or NASDAQ. Correlation measures a relationship estimate between two variables. **The performance data quoted represents past performance, which is not an indication or a guarantee of future results.**

V

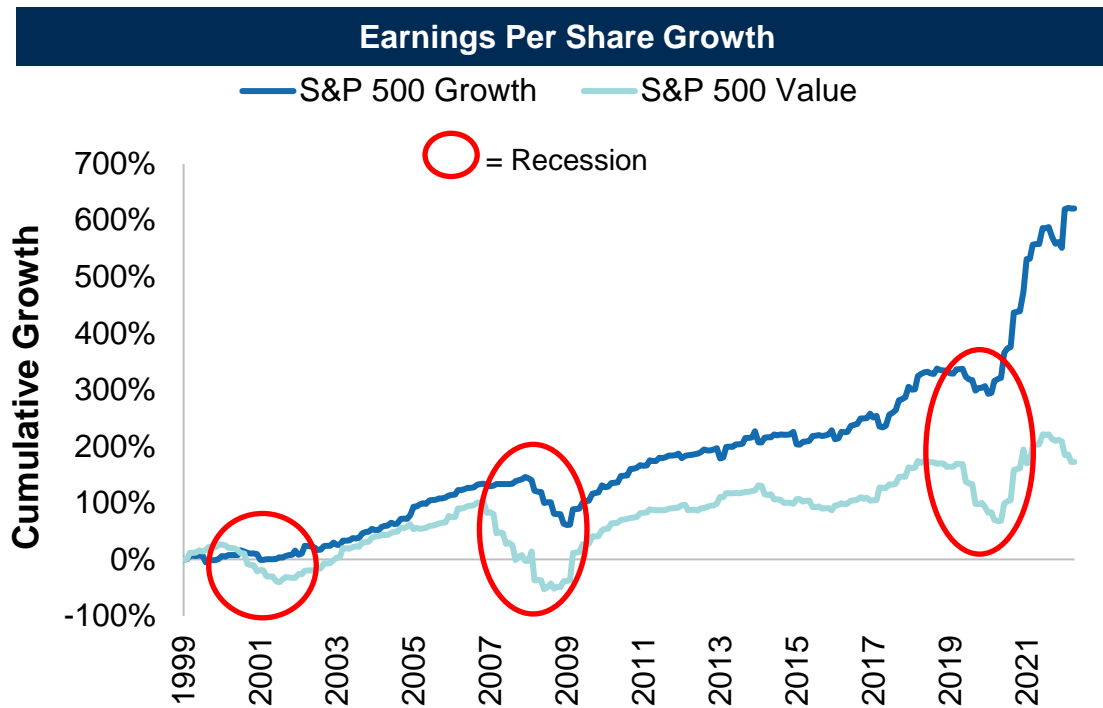
Style Wars The Growth Advantage

- 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 3/31/23. Growth represents consensus long-term analyst estimates and actual future EPS growth rates might be materially different than the forecasts shown.

- Market share gains have enabled growth stocks to post better fundamentals in past recessions than more economically sensitive value stocks

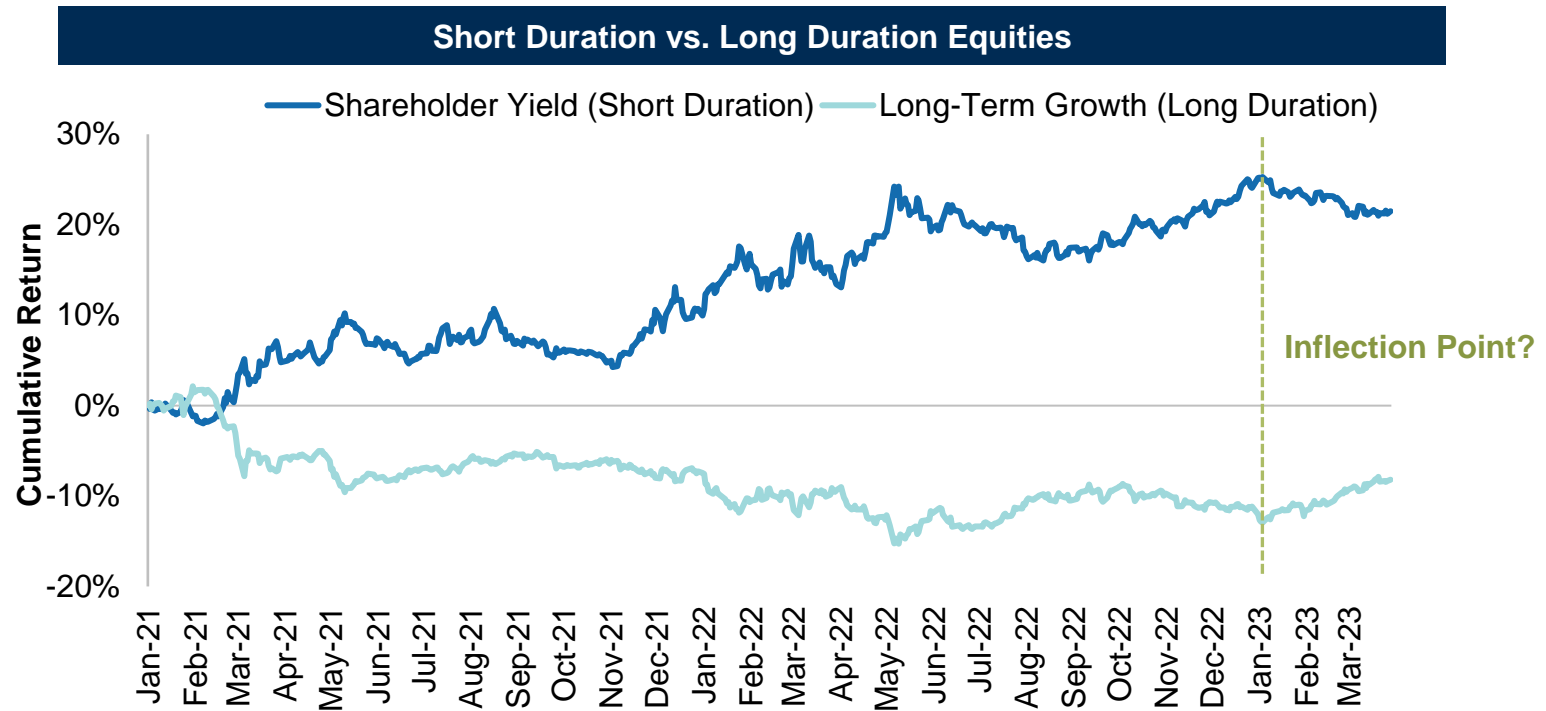


Growth stock fundamentals have fared better in recessions

V

Style Wars The Duration Trade

- Over the past couple of years, we believe rising interest rates hurt those securities with cash flows furthest in the future or those with higher “durations”
- While it has begun to reverse, the duration trade has driven investors to seek more current cash flows at the expense of growth



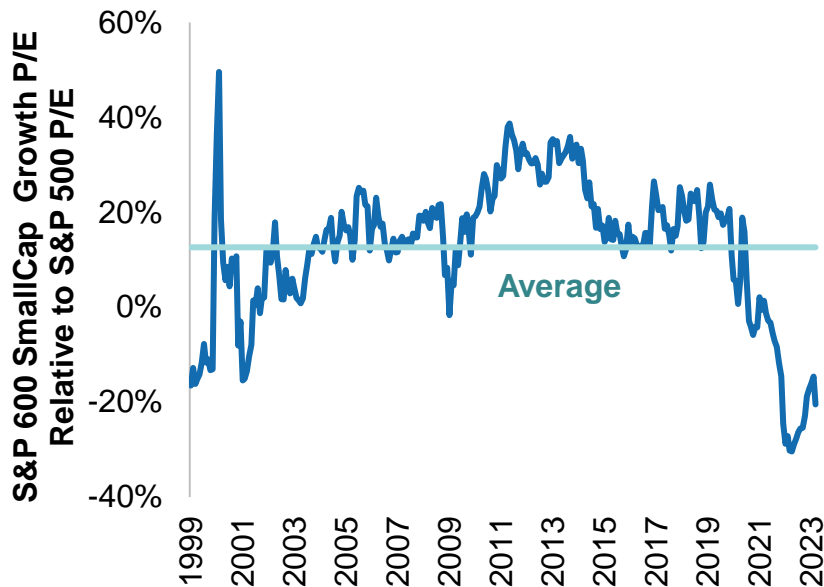
Source: Piper Sandler and FactSet as of 3/31/23. Factor performance relative to the S&P 1500, which is sector neutral and is calculated by taking the relative performance of the top quintile of stocks against the bottom quintile of stocks for each factor. The constituents in the quintiles are rebalanced monthly. Shareholder Yield is [LTM Common and Preferred Stock Purchased - LTM Common and Preferred Stock Sold + LTM Total Common Dividends] / Market Capitalization. Long-term Growth is mean estimated 5-year EPS growth.

V

Style Wars Long Duration Appears Attractive

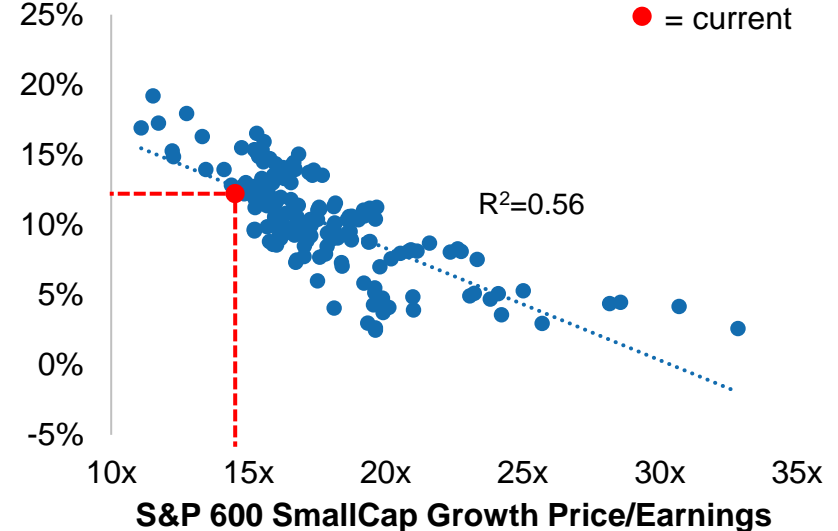
- Small cap growth stocks are trading at historically inexpensive valuations relative to the broader stock market
- While past performance is not necessarily indicative of future results, similar valuations have historically led to strong returns

Small Growth Valuation Relative to History



Valuations & Historical Returns

S&P 600 SmallCap Growth P/E vs. Historical 10-Year Annualized Returns



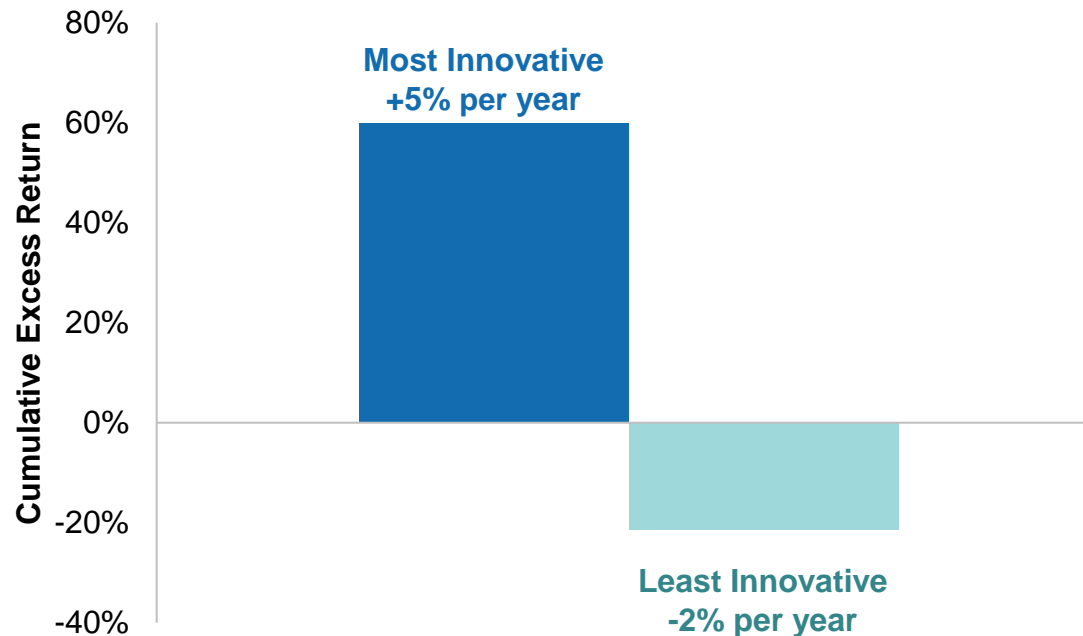
Source: FactSet. Each dot represents the P/E during that month and the returns generated over the subsequent 10 years. The starting P/E ratio is the price divided by the next 12-month earnings per share estimate at the start of each 10-year period measured. Monthly data through March 2023 and beginning in September 1998. In the context of the chart, it measures the proportion of the variability of the dependent variable (subsequent 10-year annualized return) that can be explained by the independent variable (price-to-earnings). An R-squared value of 1.00 means that the independent variable (price-to-earnings) perfectly explains the variability in the dependent variable (subsequent 10-year annualized return), while a value of 0.00 means that the independent variable cannot explain any of the variability. In the chart, the R-squared of 0.56 means that 56% of the variability in subsequent 10-year annualized returns can be explained by the price-to-earnings multiple. **The performance data quoted represents past performance, which is not an indication or a guarantee of future results.**

V

Style Wars A Powerful New Investing Factor?

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

Innovative Companies Have Outperformed Over the Past Decade



Source: FactSet. Excess performance of the quintiles of R&D as a percentage of revenue with the most innovative being top quintile and the least innovative being bottom quintile of the stocks in the S&P 1500 index. Stocks were divided into quintiles based on R&D spending-to-revenue and calculated monthly for the 10-year period ended February 2023. *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.** Innovative companies may be defined as those companies with a high ratio of annual R&D investment to revenue. Investing in innovation is not without risk and there is no guarantee that investments in research and development will result in a company gaining market share or achieving enhanced revenue.

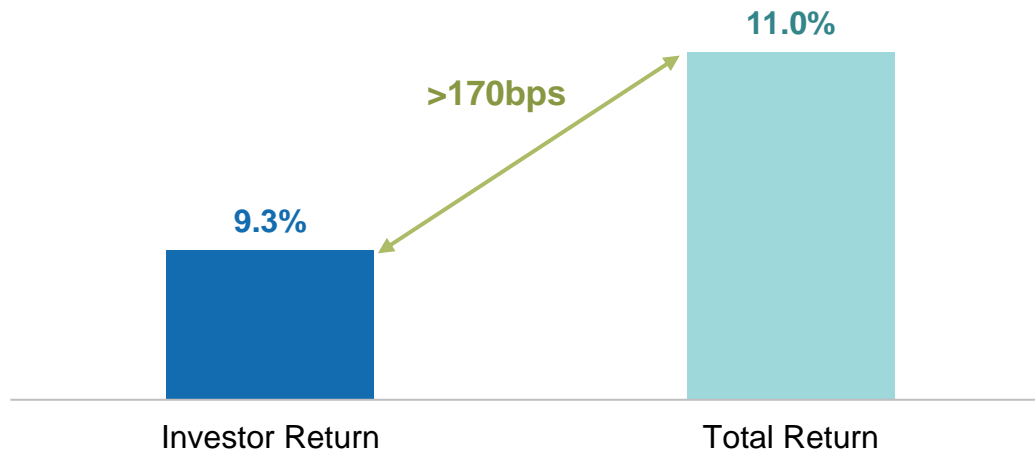
VI

Making Better Decisions Sub-Optimal Results

- Studies demonstrate investors have significantly underperformed because of less-than-optimal decisions, which drive poor timing of purchases and sales of investments
 - Potentially a result of biases such as herding, loss aversion, or confirmation bias

The Average Investor has Underperformed

Annual Returns for 10 Years Ending 2021 of U.S. Mutual Funds and ETFs



Source: Morningstar Mind The Gap 2022. The annual total return calculation is time-weighted, where a lump-sum investment made at the beginning of the period and held throughout the entire measurement term. The investor return calculation is the internal rate of return that accounts for timing of all cash flows. **The performance data quoted represents past performance, which is not an indication or a guarantee of future results.**

VI

Making Better Decisions Behaving Better Checklist

- How can investors take tangible actions to “behave better” and try to make better investing decisions?

DO...

- Put your investment goals in writing
- Assign short- and long-term timeframes to your goals
- Evaluate several scenarios as potential outcomes. What happens in a weak return environment compared to one with strong returns?
- Build your portfolio using an agreed-upon asset allocation framework. This may help remove emotional bias.
- Implement, and stick to, a game plan.

DON'T...

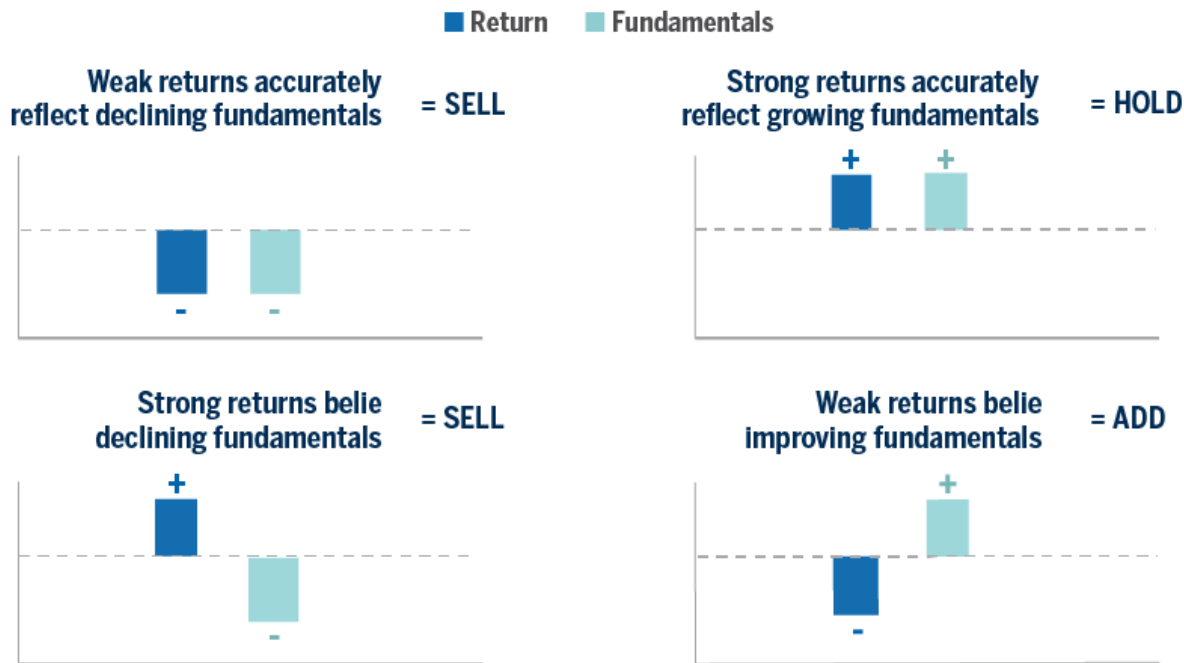
- Chase recent returns. You'll likely be disappointed as recent past performance may not be indicative of future results.
- Make investments outside of the framework you established.
- Use your “gut” to make decisions. Even if successful, it is unlikely to be sustainable because process, not results, should be evaluated and optimized to ensure repeatability.

VI

Making Better Decisions Evaluating Funds

- By assessing the fundamentals of a portfolio's positions, investors may be able to gain a better understanding of whether a manager's performance is a result of an accurate view of the sales and earnings power of their holdings or if the strategy is just in or out of style

Four Potential Scenarios for Holding, Selling or Adding to a Portfolio



Source: Alger. This chart is for illustrative purposes only. The chart above describes four potential investment scenarios an investor may consider when focusing on the fundamentals of a portfolio's positions. Company fundamentals typically refer to the financial and operational information about a company that investors use to assess its overall health and potential for future growth. This includes considerations around the company's revenue, earnings, assets and liabilities, and cash flow.

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