

On Top of the

WORLD

David Alger's Spectra fund gained more than 900 percent in the 1990s, making him the decade's top-performing diversified fund manager.

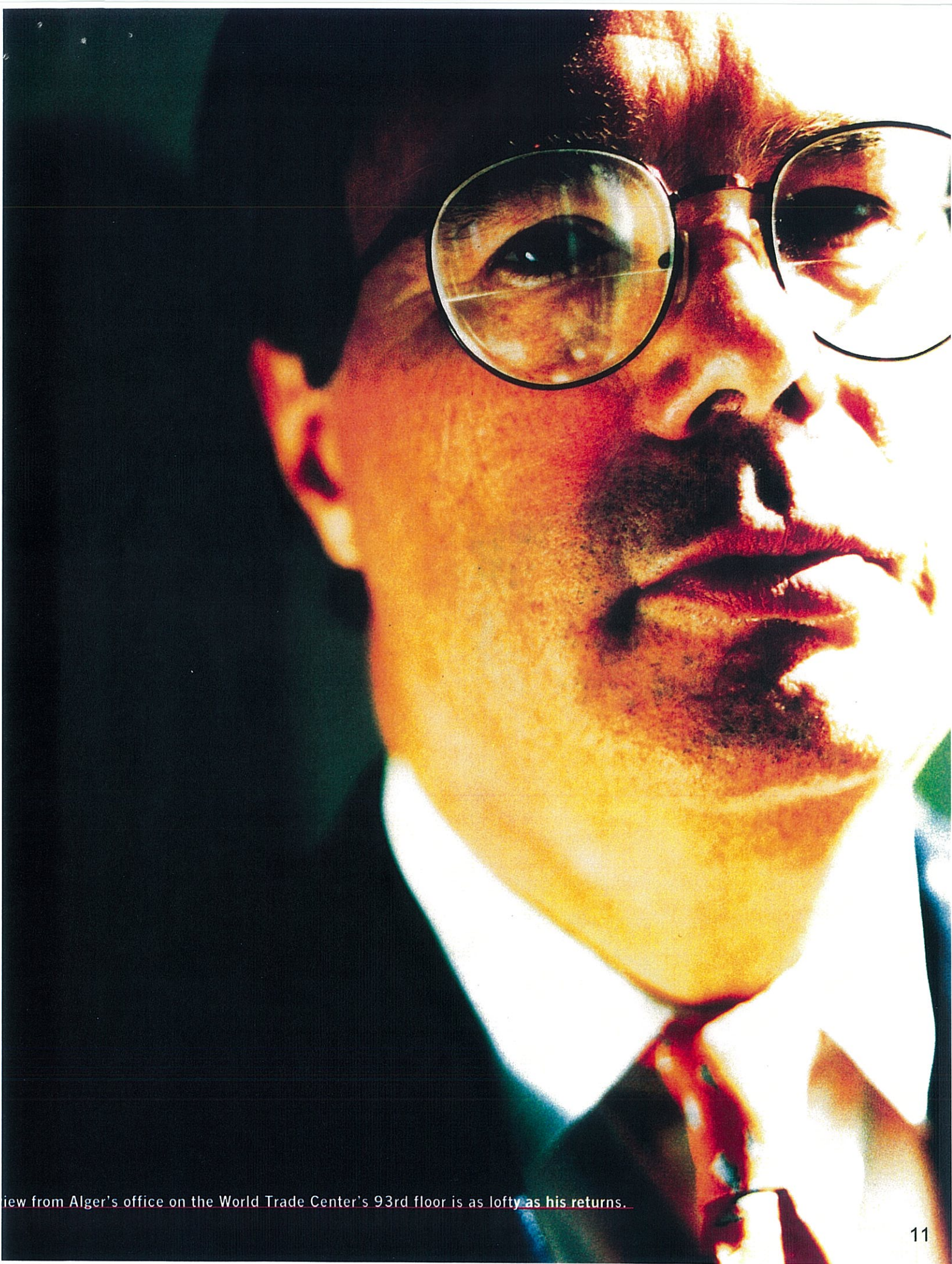
Will he fly as high in Y2K? *By Lauren Young*

PHOTOGRAPHS BY CHARLES GULLUNG

Spectra Fund was ranked number 1 out of 871 domestic equity funds for

SMART MONEY

JANUARY 1999



View from Alger's office on the World Trade Center's 93rd floor is as lofty as his returns.

ONE DAY, BACK IN OCTOBER 1998, DAVID Alger, president and chief investment officer of the mutual fund company Fred Alger Management, assembled his entire investment team in the conference room of his firm's downtown Manhattan office. Alger's funds had been doing dimly: His no-load Spectra fund had plummeted nearly 29 percent since the summer, his flagship Growth fund had lost more than 25 percent over the same period, and his Small Capitalization fund had done even worse—it was down 34 percent from its July peak.

Not surprisingly, morale was terrible. "Everybody was walking around like they were dead," says Alger, 56. "They were so morose." More important, he says, people were afraid to pick stocks: "We were getting to be wimpy. Everybody was second-guessing themselves." So with all of his 15 analysts and three fund co-managers gathered before him, Alger wheeled a 20-inch television and VCR on a cart to the center of the room and hit the play button. Were they watching a rousing compilation of speeches from Federal Reserve Chairman Alan Greenspan, or listening to then Treasury Secretary Robert Rubin trumpet the power of the American economy? Hardly. On screen, in front of an enormous American flag, appeared actor George C. Scott in the opening scene from *Patton* when General Patton speaks to the Third Army during World War II.

of all diversified U.S. stock funds.

Alger's funds followed up their roaring '98 with another great year in 1999—Spectra, for instance, was up 45 percent through late November. Now, as the year 2000 dawns, Alger is arguably the hottest diversified-fund manager on the planet. When it comes to performance, no other domestic equity fund equals Alger's Spectra. The portfolio has delivered a total annualized return of nearly 26 percent for the past decade. Think index funds have been the place to invest in the 1990s? Forget it. Spectra, which has focused on large-company growth stocks, outperformed the S&P 500 by more than eight percentage points annually for the 10 years ending Oct. 31, 1999. (There are some who might quibble with these results because Spectra began life as a closed-end fund with a fixed number of shares.)

Spectra is not Alger's only winning fund: Alger Growth, which also invests in large caps, has been a top-quartile performer over the past decade. The younger Alger Capital Appreciation and Alger Balanced funds both have ranked in the top 5 percent of their peer groups for the past five years. And year to date, all six Alger funds are beating the S&P 500.

Putting David Alger's achievement into context is simple: Say you invested \$10,000 in an S&P index fund on Jan. 1, 1990; it would now be worth \$48,712. Not bad. If you'd put that same money into Alger's closest competitor, RS Emerging Growth, you'd have \$83,449. Even better. But if you'd given the cash to David Alger to

'I don't like hanging around with anyone who is bearish,' says Alger of his management methods. 'Sometimes people need to be shaken up and have their asses kicked.'

"Americans love a winner and will not tolerate a loser," the "general" admonished both his own troops and Alger's. "Americans play to win all the time." Alger let the tape run till the end of the five-minute opening scene, then hit the stop button. His troops sat there silent, stunned. "We need to focus on being aggressive," he told them. "You shouldn't sit there in your foxhole being scared."

Analyst Ginger Risco, who covers consumer stocks for Alger, was convinced her boss had lost his mind. "I thought, 'Oh my God—he couldn't be more out of it,'" she says.

But there was a method to Alger's madness. His people needed a pep talk, not a seminar on interest rates, he says. "And I couldn't rouse Patton back from the grave" to give it. His odd rally seems to have worked: Alger's analysts bulked up on beaten down financial-services names; they also bet heavily on companies in the cable, semiconductor, Internet and personal computer sectors. By year-end Spectra had soared 56 percent, Alger Growth had jumped 43 percent, and Alger Small Cap had gained 45 percent. Five of the six Alger stock funds ended up beating the Standard & Poor's 500-stock index's 29 percent gain in 1998, a feat achieved by just one in five

handle, you'd have \$96,624. Says Don Phillips, president of Chicago fundtracker Morningstar, "You could make a good case that David Alger is the mutual fund manager of the decade."

Other so-called superstar managers have come and gone. Remember Gary Pilgrim? (His PBHG Growth fund soared by more than 50 percent in 1995, but it's been plagued by bad performance since then.) Or how about Ken Heebner? (His CGM Capital Development returned a breathtaking 99 percent in 1991 but has steadily faded ever since.) What about those ubiquitous Kaufmann managers, Hans Utsch and Lawrence Auriana? (They've failed to beat the S&P 500 for the past five years running.) But David Alger has hung on when others faltered.

Indeed, while the average stock fund manager's tenure is a mere four years (of the 871 stock funds that have even been around 10 years, just 233, or 27 percent of them, have been managed by the same person for the past decade), Alger has been running Spectra since 1974, the year Fred Alger Management acquired it. Sure, Alger has hit some rough patches. But he's quick to tweak the investment formula if the magic potion isn't working. "Look at all the other once-

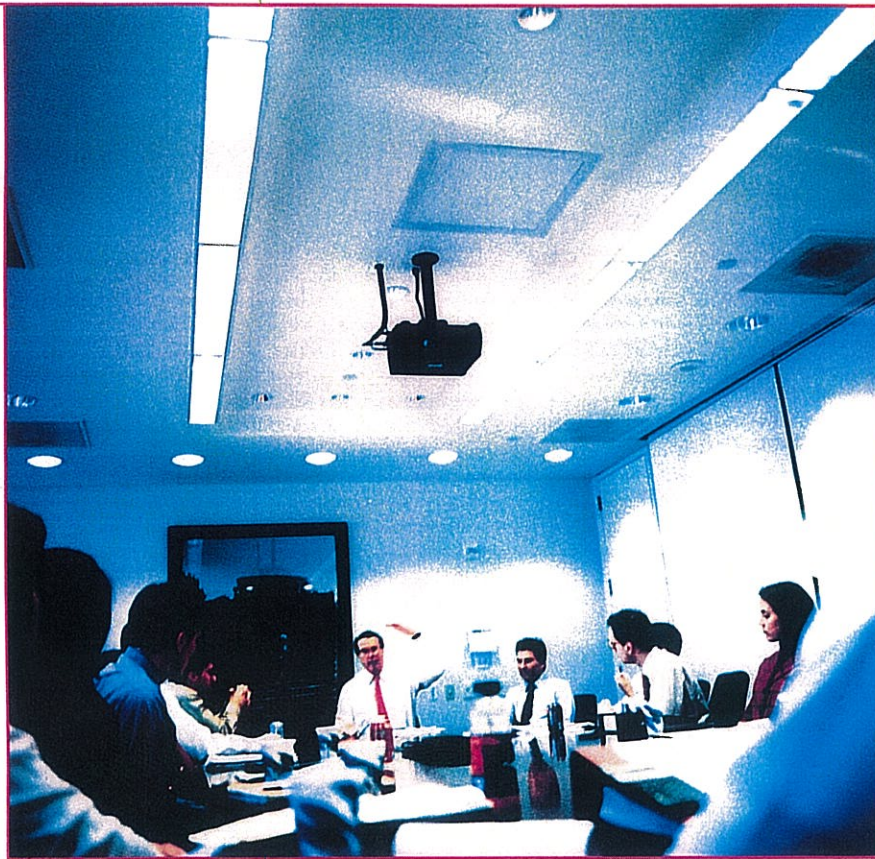
successful managers who have stumbled badly during the past decade," says Morningstar's Phillips. "Alger simply navigated the same terrain better."

What's his secret? Rigorous analysis, a hair-trigger trader's finger and a real affection for the market's hottest sector: technology stocks. Eighties supermanager Peter Lynch's favorite aphorism was "know what you own," but Alger's personal mantra is "know everything." Alger analysts are expected to speak not only to management, but also to suppliers, customers—anyone who might know anything about the company. They'll even check help-wanted ads to see who is hiring. The training clearly pays off: Alger has turned out some of the decade's hottest portfolio managers, including Thomas Marsico, whose Marsico Focus fund was up 23 percent for 1999 through Oct. 31, and overseas-markets superstar Helen Young Hayes, whose Janus Worldwide fund was up 24 percent.

His firm's attention to detail has helped Alger get into stocks at the right moment. He bought Cisco Systems just after it went public. (His cost basis in some accounts is a little more than \$2, giving him a 4,300 percent return.) In the early '80s he organized one of the first groups of cellular analysts on Wall Street. That research helped Alger stake a claim in such hot cellular stocks of the early 1990s as Centel, Metro Mobile, McCaw Cellular and Vanguard Cellular—all of which have since been merged out of existence.

But there are downsides to Alger's methods. He trades *a lot*: Spectra's portfolio turnover is 191 percent, more than double that of the average U.S. stock fund. As a result, the fund's tax-efficiency rate over the past five years is far from ideal. As evidenced by 1998's roller-coaster ride, Alger's funds can be extremely volatile. And they have higher-than-average expenses: A \$1,000 investment in Spectra costs investors \$19 a year; the average U.S. diversified stock fund costs about \$13 annually.

And Alger recently hired IBM to create artificial-intelligence models called Deep Green to analyze stocks for all his accounts. The program is fed a cocktail of technical information including more than 20 ingredients, such as historical price and volume data. In trial runs this past year, Deep Green spotted problems in iVillage,



Alger and the analysts: He hires them young to "brainwash them into our way of thinking."

Charles Schwab, Office Depot and NorthPoint, all of which later stumbled. Deep Green, says Alger, "is going to put a turbocharger on our stock-picking process."

DAVID ALGER HAD BIG PLANS FOR HIMSELF WHEN HE JOINED elder brother Fred's money-management firm back in 1971. At that point, David had graduated from Harvard and the University of Michigan's business school, and he was working at a boutique Wall Street research firm. He'd had one big, winning stock pick—a modem manufacturer called Milgo Electronics that was one of the American Stock Exchange's best-performing equities in 1969. "I thought I'd sashay in as his partner," says David. "His thought was that after five years of beating me up, I might actually learn something." Fred won: David started out as an analyst, making about \$25,000. Several years later, when Fred's partner wanted out, David bought his share of the company for about \$400,000. "It took me 15 years of bonuses to pay it off," says David. "I was living on dust for a long time." David, who now runs the company day to day, currently owns 20 percent of Alger Associates, the holding company



With one of his ever-present rubber bands: Alger's funds are volatile, and so is he.

that controls Fred Alger Management. Fred, who moved to Switzerland in 1995, controls the other 80 percent with his family.

The Alger investment philosophy is founded on the belief that superior returns are produced by purchasing rapidly growing companies. Ideally, he's after companies in the midst of a major "life cycle change"—a new management team, restructuring, a mushrooming business line—that can spark a spurt in growth.

His current batch of 17 analysts, who cover a total of 1,400 stocks, are charged with finding those companies. Alger likes his recruits young and hungry. "We tend not to hire people with experience—so we can brainwash them into our way of thinking," he says. He particularly likes prospects who've played college sports, because they are highly disciplined, competitive people, he says. Newcomers usually start at Alger as research associates. Ordinarily, it takes at least four years to advance from associate to junior analyst to analyst. By the time they've honed their stock-picking skills, analysts must be able to convey the reasons to buy a company in 15 minutes. For further incentive Alger runs a stock-picking derby, with the \$50,000 prize going to the analyst with the best picks each quarter.

A few years after he joined his brother's firm, Alger came across a small computer manufacturer named Apple. He bought the stock, but first he bought one of the company's Apple II computers, which featured a spreadsheet program called VisiCalc. Alger thought it would let him improve on the stock models he'd started running. He

was right. Computer modeling remains a key component of the Alger way that's drummed into each new analyst. Whereas many buy-side analysts are spoon-fed Wall Street research, Alger requires analysts to do the homework themselves, then to use models to forecast financial variables such as revenue growth, profit margins, cash flow and earnings per share.

Take Bank One, a stock that's been followed by Alger financial analyst Craig Smith. Back in the summer of 1998, management was claiming potential earnings growth of 15 percent as a result of the Midwest bank's mergers with First Chicago NBD and First USA. Wall Street was in love. But Smith's model for the company told a different story. Analyzing data on the company's banking and credit card revenue, he couldn't figure out how it was going to grow faster than 11 or 12 percent. Bank One had been telling the Street that its combined credit card businesses would drive growth, but Smith stuck to his model. In August 1999, Bank One admitted it was going to fall short of projected earnings in—where else?—its credit card unit, and the stock has since lost 34 percent of its value.

Just as important as modeling at Alger is plain, old-fashioned legwork. Several Christmases ago, Alger sent analysts disguised as "graduate students working on term papers" to check out the holiday traffic at Toys "R" Us stores. They noted that dozens of shoppers complained about the merchandise, and Alger sold the stock before it tumbled.

EVERY MONDAY AT 8 A.M., THE 20-PERSON ALGER INVESTMENT team gathers to go over stocks in the firm's conference room on the 93rd floor of the World Trade Center. The performance of the firm's top 150 stock holdings is updated twice daily, with the list circulated among the analysts and portfolio managers. Before each weekly meeting, Alger reviews the one-year performance chart of every stock the firm owns, grading them from 1 (worst) to 5 (best). For the analyst covering those stocks with losing grades, Monday is *not* a good day. "I don't like hanging around with anyone who is bearish," says Alger by way of explaining his motivational methods. "Sometimes people need to be shaken up and have their asses kicked." On this particular August morning, Jeff Kwit is first to be put in the hot seat. Alger wants to know why Sonic Automotive, an auto retailer that Kwit follows, is down about 40 percent for the year. "This chart really sucks," Alger says.

Kwit explains that two big momentum funds have pulled out. "This is by far the best auto retailer in the group," Kwit argues.

Alger isn't impressed. "You can get so hung up on some of these stocks by trying to be right," he says.

Sara Manley, one of the firm's telecom analysts, is next to bear the brunt of Alger's displeasure. As of this morning's meeting, MCI WorldCom has lost 22 percent of its value in a little more than two

months. Alger's mutual funds and private accounts collectively own about \$241 million worth of the stock, making it one of the firm's top holdings. "This is a piece of garbage!" Alger yells, his hands furiously making a car's cradle of one of the ever-present red rubber bands he carries. "We are sitting here, la-di-da, like Nero while Rome is burning. It's a company nightmare."

Manley pulls out her calculator. "I see them earning \$2.80 to \$2.85 a share [next year]," she counters. "With a P/E of 32, they're selling at a discount to their 42 percent growth rate."

In the end, Alger sells a million of his shares in MCI WorldCom. But through early November he is still holding Sonic—and still urging Kwit to sell. "No excuses anymore—we've got to get rid of it,"

ley Dean Witter Health Sciences fund. Other Algerites have followed the hedge fund route, including Shelton Swei, whose two Sapphire Management hedge funds both rose 94 percent in 1998 and are up more than 100 percent through November 1999. And Wall Street has its own Alger camp, including *Wall Street Journal* All-Stars David Togut, who covers computer services at Morgan Stanley, and Amy Ryan, who follows retailers for Prudential Securities.

"I'm amazed at how many great people have come out of Alger," says Morningstar's Phillips. "But just think if they could have kept them all."

Why *has* Alger had such a hard time holding on to its stars-in-the-making? "It's a pyramid," Alger says. "Most people can't jump

The numbers don't lie, and putting Alger's achievement into context is simple: \$10,000 invested in Spectra on Jan. 1, 1990, would now be worth \$96,624.

he tells him. Kwit says his recalcitrance hasn't harmed his relationship with his boss. "The good thing about David is that he doesn't hold a grudge. Five minutes later, he's your best friend again."

Which is not to say Alger takes a missed call calmly. In the summer of 1997, Alger decided it was time to unload his firm's \$117 million position in the HMO Oxford Health Plans. Oxford was—and still is—Alger's insurance provider, and he was waging his own personal war with the company because it wouldn't cover a procedure for his wife, Josie. Every time Alger called to ask a question, he encountered more red tape. The dismal customer service and confusion about Alger's account only reinforced his gut feeling that something was wrong, so he told analyst Ron Reel about his qualms.

On the morning of Oct. 27, 1997, the day Oxford reported that it had an astonishing third-quarter loss of \$78 million, Alger appeared outside Reel's office. "What the hell is going on? I told you this was a terrible company," Alger screamed, pounding the table.

Without waiting to hear Reel's opinion, Alger yelled, "We're going to sell it," and marched off to the trading desk. He lost about 52 percent on the stock, which ultimately lost 62 percent that day.

"When I get mad, I really get mad," Alger says.

Despite Alger's temper, most of the people who have survived his analyst program say the time they spent there was invaluable. "Although it was painful at times, I learned a great deal from that experience," says Thomas Marsico, who admits he patterned his own approach to research—both at Janus and at his own firm—after that of the Algers. The financial industry is littered with former Algerites (one of the reasons David Alger ranked 17th on the 1999 "SmartMoney 30" list of the most influential people in the mutual fund industry). In addition to Hayes and Marsico, other Alger alums now running mutual funds include Warren Lammert and Jim Goff, both at Janus; Tony Weber, whose Alleghany Veredus Aggressive Growth is one of the best new funds of 1999; Rob Lyon, president of Institutional Capital; and Teresa McRoberts, now the manager of the Morgan Stan-

ahead unless they leave. As long as we are incubating people as smart as the people who are leaving, then I'm happy."

Until 1995, when Alger appointed two portfolio co-managers to help run the Growth, Capital Appreciation, MidCap and Small Cap funds, he ran all the company's money himself. There was simply no place for a stock picker to go. "The name of the firm is Fred Alger Management," notes Institutional Capital's Rob Lyon, who spent seven years at Alger. "Blood is thicker than water. I knew no one else but an Alger would be president of that firm."

DAVE ALGER LIKES TO BE ON TELEVISION. HE REALLY, really likes to be on television. Last year alone he made close to 35 appearances, on CNN, CNBC, CNNfn, you name it. And each time, rather than doing the usual remote interview from his office, Alger jumped in his car and battled his way through Manhattan traffic to the network headquarters. Why? He thinks the lighting in the studio is more flattering—"it's not good to look like you're dead when you're in front of 10 trillion investors," he says. Alger's more than a tad vain. His inevitable attire consists of a custom-made pinstripe suit from Bergdorf Goodman, Hermès tie and custom Lobb shoes from London.

For someone so interested in marketing his image, Alger still doesn't manage all that much money. Fred Alger Management runs \$13 billion. By contrast, Alger alumnus Thomas Marsico manages \$12 billion—and his company is just two years old. If he's so smart, why isn't Alger richer? (Not that he's doing badly: In addition to their Upper East Side apartment, the Algers own a house on 15 acres in pricey Tuxedo Park, N.Y.)

Mutual fund consultant Geoff Bobroff says the problem has been the way the Alger brothers have sold their funds. "Alger has really missed the boat in terms of marketing and distribution," he says. Until 1994, Alger's load funds were distributed by American Skandia, which focused mainly on selling variable annuities. And



For television, Alger always goes to the studio—the lighting's more flattering.


promoting the no-load Spectra to the public is a delicate matter because the firm doesn't want to anger the brokers who sell its five load funds. But the bigger problem, Alger says, was his brother's laissez-faire approach to marketing. "Fred was not exactly user-friendly. His attitude is 'I'm brilliant. Now give me your money,'" says David.

The elder Alger admits that his brother is a better salesman. "I was more of the entrepreneur. David is the corporate manager," Fred Alger explains. On David's watch, the amount of money flowing in has dramatically increased. While other fund companies have had a dismal 1999, the Alger funds' net inflows were at an astounding \$1 billion.

The question for those new investors is, can Alger do as well in the 21st century as he's done at the close of the 20th? Much of the answer, at least in the short term, hinges on what happens to technology stocks. Rarely has the firm's weighting in tech dipped below 25 percent—right now it's near 45 percent—and that enthusiasm has served Alger well in the '90s market. His fortunes became linked to the Internet, thanks in great part to the urging of Dan Chung, Fred's son-in-law and next in line to run the firm, who pushed Alger to buy America Online back in October 1995. (That initial position has since climbed 3,073 percent.)

Today Alger's funds are fueled by such Net stocks as Ama-

zon.com, eBay, Yahoo! and Excite@Home. Since 1998, Alger has made at least three major moves into and out of the sector. In June 1999, for example, the firm started to cut its Internet stake in half when eBay began experiencing service outages and Yahoo! seemed overextended. But Alger returned to the sector with gusto in late August, buying up more than 5 million shares of Web companies in the belief that e-commerce would explode come the holiday shopping season. In November more than 15 percent of the firm's assets were tied up in Internet stocks.

How will Alger know when it's time to get out again? Despite his elaborate computer models, his Monday morning yell-fests with the analysts, despite even Deep Green, Alger admits that, finally, it'll come down to intuition. "This is like car racing," says Alger. "Brake too soon, you lose. Brake too late, you die." 

SmartMoney.com

Check out how your mutual funds compare with Alger's. Click on the Mutual Funds button.

Performance and other information referenced in this reprint may no longer be accurate as this article was printed in January 2000. Past performance is no guarantee of future results. Spectra Fund was ranked number 15 out of 814 domestic equity funds for the ten year period ended 9/30/00. Spectra Fund was ranked number 1,833 out of 5,871 domestic equity funds for the one year period ended 9/30/00 and number 256 out of 2,439 domestic equity funds for the five year period ended 9/30/00. Spectra Fund portfolio turnover is shown for the fiscal year ended 10/31/98. Portfolio Turnover for the six months ended 4/30/00 is 40.19%. Investment return and principal value of an investment will fluctuate and the Fund's shares, when redeemed, may be worth more or less than the original cost. The views expressed herein are subject to change and there can be no guarantee that the views and opinions expressed in this reprint will come to pass. The returns indicated include reinvestment of all distributions. Fred Alger & Company, Incorporated is the distributor of The Alger Fund and Spectra Fund.

The holdings mentioned in this reprint are subject to change and the individual stocks listed may no longer be owned by the Fund. At 9/30/00, The Alger Fund Portfolios and Spectra Fund did not own iVillage, Apple Computers, North Point, Sonic Automotive, Amazon.com, Office Depot, Excite@Home or MCI WorldCom. At 9/30/00, the Alger Fund or Spectra Fund did own stock in the following companies; they are shown as a percentage of total assets in the portfolio:

	Small Cap	Mid Cap Growth	LargeCap Growth	Balanced	Cap App	Spectra
America Online Inc.	0.00%	0.00%	1.52%	1.70%	1.98%	2.05%
Cisco Systems, Inc.	0.00%	0.00%	2.80%	2.49%	2.91%	3.05%
eBay Inc.	0.00%	3.16%	2.86%	2.71%	3.63%	3.24%
Charles Schwab Corp.	0.00%	0.00%	1.13%	0.86%	0.12%	0.13%
Yahoo Inc.	0.00%	0.00%	0.61%	0.53%	0.61%	0.00%

Spectra Fund Average Annual Returns Through 9/30/00*

Spectra Fund Class N	1 Year	5 Years	10 Years	20 Years
	27.80%	25.15%	29.21%	21.04%

* Performance is for Class N shares. The Fund also offers Class A shares. Class A and Class N shares differ only in that Class A shares are subject to a sales charge, whereas Class N shares are out. Because of the sales charge, returns will be lower for Class A shares.

The Alger Fund Average Annual Returns Through 9/30/00 Class B Shares**

	1 Year	5 Years	10 Years	Since Inception
Alger Capital Appreciation B	31.92%	25.06%	n/a	29.56% (incept. 11/1/93)
Alger MidCap Growth B	56.57%	21.97%	n/a	25.68% (incept. 5/24/93)
Alger LargeCap Growth B***	19.75%	19.90%	22.86%	17.97% (incept. 11/1/86)
Alger Small Capitalization B	11.98%	6.68%	16.37%	15.72% (incept. 11/1/86)
Alger Balanced B	17.94%	16.58%	n/a	14.10% (incept. 6/1/92)

**Performance does not reflect a contingent deferred sales charge of 5% declining to 0% after 6 years associated with Class B Shares.

*** Prior to 11/1/00, the Alger LargeCap Growth Portfolio was named the Alger Growth Portfolio.

S&P 500 Index	13.29%	21.69%	19.44%	16.69% (9/30/80 - 9/30/00)
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