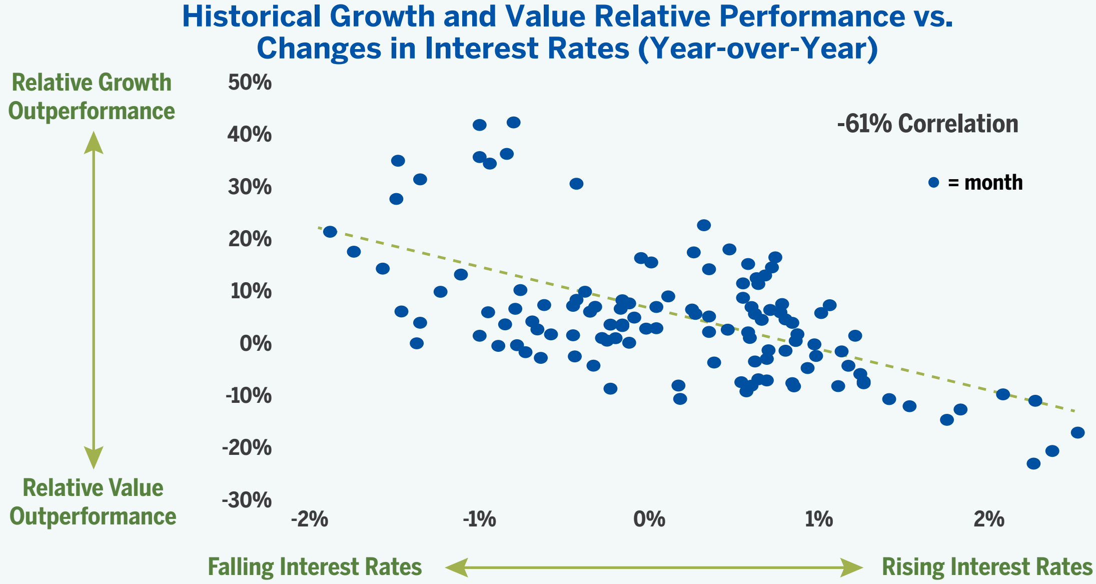
ALGER

Alger On the Money

Rate Swings and Style Shifts

For the better part of a year, investors have been grappling with the Federal Reserve's (Fed) aggressive monetary policy designed to bring down inflation. As a result of the largest interest rate hikes seen since 1980, growth stocks experienced meaningful valuation compression and underperformed value stocks in 2022 (see Laggards to Leaders?). While past performance is not indicative of future results, what has historically happened to growth stocks when interest rates fall?



Source: FactSet. 1-year performance for Growth stocks are Russell 3000 Growth, Value stocks are Russell 3000 Value, and Interest rates are U.S. 10-year Treasury Bond. Monthly data from March 2013 to March 2023. Correlation is a statistical measure that shows how two variables are related to each other.[1] **The performance data quoted represents past performance, which is not an indication or a guarantee of future results. There is no guarantee that any historical trend illustrated in this commentary will be repeated in the future, and there is no way to predict precisely when such a trend will begin.**

- Growth stocks have historically underperformed value stocks when interest rates rise and outperform value stocks when interest rates fall, as illustrated in the chart above. Generally, when interest rates rise, investors discount the future cash flows of a security using a higher rate. For long-duration securities (i.e., those whose cash flows are expected to be received further out in the future), such as growth stocks, higher interest rates have historically tended to have a greater impact on valuations compared to short-duration securities (i.e., cash flows expected to be received in the near-term), such as value stocks.
- We believe that several forces that have contributed to inflation over the past year could be reversing: 1) the U.S. money supply has been in contraction since December 2022, 2) fiscal policy is no longer stimulative, and 3) supply chain bottlenecks have been considerably alleviated. In our view, these factors may contribute to a decline in inflation and help maintain relatively low interest rates over the next year.
- While interest rates may be an important short-term consideration, we believe that productivity and innovation are the key drivers of corporate earnings growth which determine stock performance over the long-term. Moreover, we believe growth stocks may be well-positioned to potentially benefit from the increased pace of innovation in areas such as artificial intelligence, the internet of things, genomics, and cutting-edge surgical technologies.

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[1] Correlation is a statistical measure that shows how two variables are related to each other. If two variables are correlated, it means that they tend to move together in some way. The strength of the correlation is measured by a number called the correlation coefficient, which ranges from -1 to 1. A value of 0 indicates no correlation, a value of 1 indicates a perfect positive correlation (i.e., as one variable increases, the other increases as well), and a value of -1 indicates a perfect negative correlation (i.e., as one variable increases, the other decreases). In this example, if there is a -61% correlation between relative growth vs. value 1-year stock performance and 1-year change in US interest rates, it means that as interest rates rise, growth stocks tend to underperform value stocks, and vice versa. The negative sign indicates a negative correlation, which means that as one variable increases (US interest rates), the other tends to decrease (growth underperforms value). This calculation took data from March 2013 through March 2023. This information is for illustrative purposes and should not be considered investment advice. **Past performance is not indicative of future performance.**

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