2Q24 Market Review and 3Q 2024 Outlook

Market Backdrop

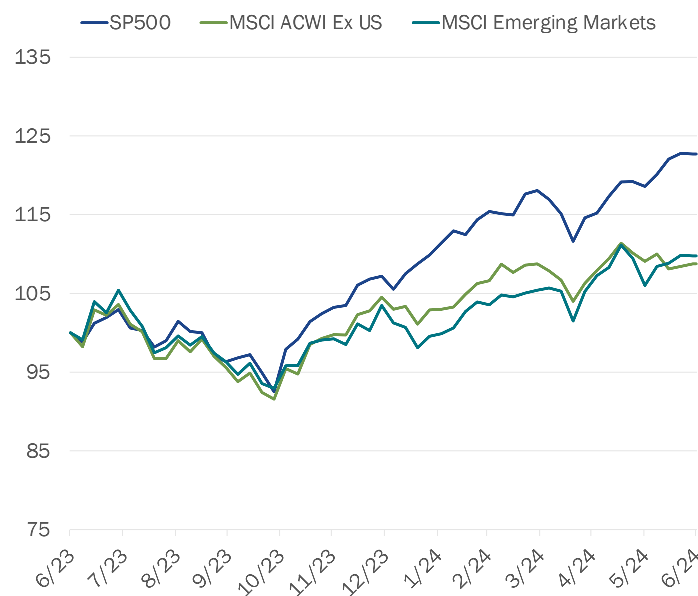
The second quarter of 2024 saw continued resilience in US economic activity as it exceeded the pace of most economies outside the United States. Evidence of an anticipated deceleration in growth began to emerge with consumer sentiment declining and the unemployment rate gaining slightly through quarter end. The level of the Federal Reserve's current federal funds rate remained steady, reflecting ongoing strength of the economy with policymakers awaiting further evidence of softening to emerge before acting.

Meanwhile, around the globe, important elections in India and Mexico produced unexpected outcomes. Political leadership in France and the United Kingdom called snap elections, leading to uncertainty and market weakness into quarter end.

The US dollar continued its strong relative performance, most notably against the weakening Japanese yen. The relative decline in the Japanese currency and stubbornly high inflation led to the first interest rate increase in Japan in 17 years, but it did little to halt the yen's weakness.

The ongoing conflict in Ukraine coupled with expanded Israeli military activity in the West Bank and Gaza kept geopolitical tensions high. The repercussions of a weak property market and trade restrictions on technology goods saw Chinese economic activity stagnate.

Market Index Performance



As of June 30, 2024. Source: Jennison, FactSet, MSCI.

Style Performance

- There was significant disparity among market capitalizations and styles in the second quarter. Large cap growth dominated, and large cap core also posted a solid positive return. All other major style indices were negative in the second quarter.
- Large cap growth has also led market returns for the trailing one, three, and ten years.
- Small caps were the worst performing market segment for all time periods, but with mixed results for growth versus value.

Style Index Performance

2Q24

	Value	Core	Growth
Large	-2.2	3.6	8.3
Mid	-3.4	-3.3	-3.2
Small	-3.6	-3.3	-2.9

Trailing 1-Year

	Value	Core	Growth
Large	13.1	23.9	33.5
Mid	12.0	12.9	15.1
Small	10.9	10.1	9.1

Trailing 3-Year

	Value	Core	Growth
Large	5.5	8.7	11.3
Mid	3.7	2.4	-0.1
Small	-0.5	-2.6	-4.9

Trailing 10-Years

	Value	Core	Growth
Large	8.2	12.5	16.3
Mid	7.6	9.0	10.5
Small	6.2	7.0	7.4

As of June 30, 2024. Source: Jennison, FactSet, MSCI.

Sector Performance

- In 2Q, there was also substantial disparity among sector returns. Information technology was the best performer, followed by communication services. Materials and industrials were the weakest sectors.
- Information technology leads for the trailing three-, five-, and ten-years, while communication services is modestly ahead for the one-year period.
- Real estate was the weakest sector for all longer time periods.

GICS Sector Performance - S&P 500® Index

	2Q	One Year	Three Years	Five Years	Ten Years
Information Technology	14	42	20	27	23
Communication Services	9	45	6	15	10
Utilities	5	8	6	6	8
Consumer Staples	1	8	7	9	9
Consumer Discretionary	1	13	2	11	12
Health Care	-1	12	7	12	11
Real Estate	-2	6	-1	4	7
Financials	-2	24	6	11	11
Energy	-2	16	24	13	3
Industrials	-3	16	8	12	10
Materials	-4	9	5	11	8
Total	4	25	10	15	13

As of June 30, 2024. Source: Jennison, FactSet, MSCI.

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466 Lexington Avenue, New York, NY 10017 T: 212-421-1000

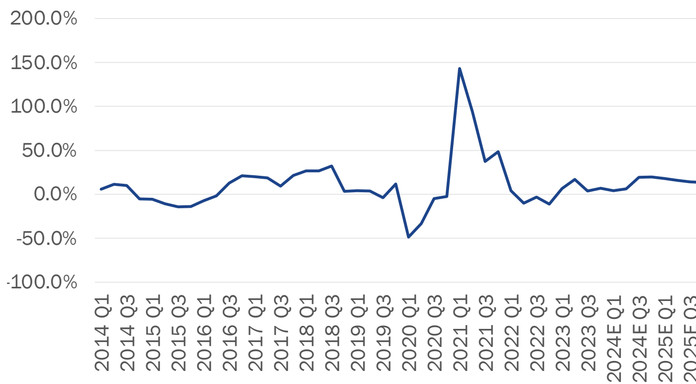
One International Place, Suite 4300, Boston, MA 02110 T: 617-345-6850

Sector Weights

	S&P 500	MSCI ACWI ex US	Russell 1000 Growth	Russell 10000 Value
Communication Services	9	5	13	4
Consumer Discretionary	10	11	14	5
Consumer Staples	6	7	4	8
Energy	4	6	0	8
Financials	12	22	6	23
Health Care	12	9	10	14
Industrials	8	14	5	14
Information Technology	32	14	47	10
Materials	2	7	1	5
Real Estate	2	2	1	5
Utilities	2	3	0	5

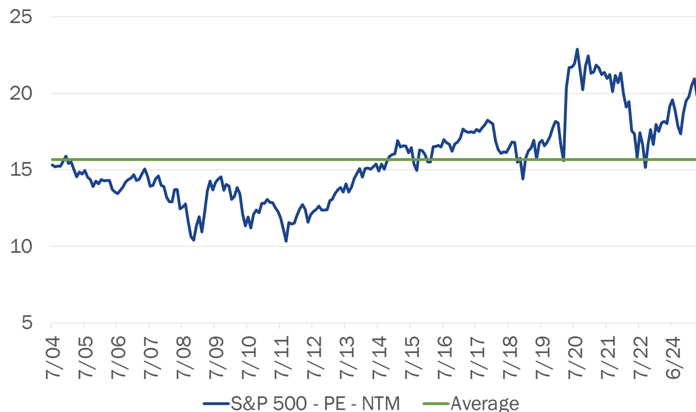
As of June 30, 2024. Source: Jennison, FactSet, MSCI.

S&P 500® Index - YoY EPS Growth



As of June 30, 2024. YoY = Year over Year. Source: FactSet. Forecasts may not be achieved and are not a guarantee or reliable indicator of future results.

S&P 500® Index - NTM P/E



As of June 30, 2024. Source: Jennison, FactSet, MSCI.

Outlook from Jennison's Growth Teams

As we reach the year's halfway point, markets continue to focus on and reward companies that are generating growth at above-average rates. Profits generally are growing at a faster rate than the previous year and the economy has remained largely resilient. The federal funds rate, as a result, remains unchanged from the start of the year. We continue to believe that the trajectory of short rates is lower, though the timing of the movement remains uncertain. The consumer slowdown is gathering pace but does not suggest acute distress. Strong employment and growing wages will likely continue to support a positive backdrop, though with moderating gains over the balance of the year.

Outlook from Jennison's Sector Teams

Information Technology

Following up on a strong start for the year, the S&P 500 Index's information technology sector was up double-digits at +11.4% in the second quarter of 2024. This reflects continued better-than-expected fundamentals across a broad range of business models (mainly the AI leaders), along with an improving macro environment (primarily lower inflation and the consumer holding up well). Additionally, we are seeing ongoing improvement in the forward discounting mechanism (i.e., less uncertainty) for long duration equities.

Fundamentals are being driven by the disruptive opportunity for AI and the digital transformation of consumers and businesses, especially the mega cap companies in the space who can invest heavily to stay ahead with innovation and disruption. The longer-term underlying strength in these business models and their secular revenue/profit trends remain solid and were highlighted across the overall sector's reported earnings these past few quarters.

The US economy continues to hold-up. Solid employment has sustained consumer spending at a steady pace. Consumer confidence currently reflects optimism in the near term despite announced work force reductions. Interest rates have stabilized at a higher level, and the Fed has tightened liquidity and succeeded in reducing credit availability in the financial system. It therefore seems likely that the slope of the economy's slowing trajectory will remain shallower while employment remains healthy. Additionally, inflationary pressures, while still evident, will likely continue to moderate. Consensus thinking leans towards the bulk of the rate increases being behind us for this cycle.

Trends in technology spending continue to improve. A combination of easing year-over-year comparisons and the priority of the digital transformation, with an emerging impetus from AI (primarily driven by productivity opportunities) increasingly suggest an ongoing rebound in spending and a return to longer-term investment trends. Nevertheless, management guidance has been cautious given the high levels of macro uncertainty that remain along with more elevated consensus forward fundamental expectations for the sector.

Longer term we believe the market will continue to favor companies with asset-light business models, high incremental gross profit margins, subscription model revenue streams, disruptive products, large total addressable markets (TAM), and faster organic growth with long runways of opportunity.

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One International Place, Suite 4300, Boston, MA 02110 T: 617-345-6850

It is important to recognize that technology is no longer a distinct sector; rather, it is woven through every industry in which we invest; a backdrop that creates an attractive environment for long-term champions of innovation. For example, we expect continued accelerated long-term CAPEX spend on tech, software, and R&D, especially since these expenditures have now become a "necessity for survival" for businesses instead of a way to reduce costs and a "nice to have." This can be seen across multiple fronts: technology-heavy capital expenditures; AI/deep-learning, ecommerce strategies; health care and medical technology, the enterprise transition to the cloud; direct-to-consumer business models; and software applications that extend across businesses. The long-term implications of this change in CAPEX spend will likely be profound, again with AI the dominant driver.

We also see continued acceleration and long duration technology demand from the massive global millennial and Gen-Z population, given their early uptake of so many digital-economy related products (many of which are driven through the smartphone) that are solving their real-world problems. We believe these large, global-oriented total addressable markets provide an ample runway for long-duration top-and bottom-line growth, with many disruptive trends expected to double over the next 4-5 years. Historically, earlier stages of mass adoption have spurred more innovation, greater ease of use, and an expansion of the ecosystem, which in turn has kept the virtuous cycle spinning with yet greater adoption.

Investment Themes & Areas of Focus

- AI and the super high speed computing processing that it requires continues to drive accelerating demand across a broad range of chip and silicon companies (especially the most advanced). This also includes the software architecture players and cloud platform leaders, along with the high-end design and manufacturing/ fabrication providers.
- We expect to see AI use cases and applications spread from technology providers and developers to a wide variety of industries and companies that use these tools to increase competitive positioning through improved time to market, streamlined customer service, and accelerated efforts to harness data in increasingly sophisticated ways.
- The use of digital technologies to create new (or alter existing) business processes, cultures, and customer experiences has become a strategic imperative as enterprises seek to meet changing business and market needs. This digital transformation has been driven by technologies such as social media platforms, mobile devices, artificial intelligence, and cloud computing.
- We look for companies positioned to benefit from increased business CAPEX spending on technology. This includes investing in industries such as business intelligence (AI), semiconductors, cloud storage and software, and life sciences tools.
- We think the continued ramping-up of data/information/ entertainment usage across a broad range of devices and applications, along with digital payments, are among the areas that offer long-duration opportunities and huge addressable markets for companies with the right technologies. Business and consumer behaviors have clearly changed, with adoption and uptake continuing to inflect higher.

Health Care

The health care sector of the S&P 500® Index declined 1.0%, trailing the overall S&P 500 Index's 4.3% return during the second quarter. Additionally, the Nasdaq Biotechnology Index advanced 2.8%. Over the trailing 12-months, the health care sector's 11.7% return trailed the S&P 500 Index's 24.6% gain.

We believe the current set up for the sector is extremely favorable. Health care is one of few sectors that offers access to open ended total addressable markets. Presently, the combination of several drug/therapies in both late stage and pre-commercialization in large markets (Obesity, Asthma, Cholesterol, COPD, Multiple Sclerosis, Lupus) coupled with a broad recovery in utilization offers an attractive runway for sustainable growth. Our focus is on those companies that provide a significant benefit to the patient, improving the human condition and thus offering the highest rate of return to the health care system which in turn garners the highest and most sustainable level of reimbursement from the various payees across the globe.

Investment Themes & Areas of Focus

- **Therapeutic Advancements Targeting Massive Total Addressable Markets - Catalyst rich calendar going forward.**
  - Many companies came to the public markets at too early of a stage, (over the last 5 years), their data was too immature (or non-existent) to garner proper multiples/valuation in the public markets. Over the past 3 years we have seen a broad deflation in valuations and thus stock prices of many therapeutics companies resulting from investor disinterest in the space broadly. As stock prices collapsed these same companies have made significant progress on their pipelines and are finally hitting the "investable" part of the curve, providing, on our view, a fertile ground for stock selection and thus performance over the next 12 months.
  - A few of the catalysts we are excited to see data for include the FCRNs in myositis, COVID-POTS, Sjogren's, Graves and TED, additional data for AstraZeneca's ADC platform in breast cancer, Krystal Biotech's aesthetics pipeline, data from several new targets in various forms of epilepsy, data from new mechanisms in neuropsychiatric diseases as well as data for Crinetics Pharmaceutical in several endocrine disorders. In the new product launch side, we are closely following Arcutis Biotherapeutic's launch of Vtama in seb derm and atopic dermatitis, Krystal Biotech's launch in DEB, Argenx's launch in CIDP, Eli Lilly and Novo Nordisk's continued launch in obesity, Merck & Co's launch in in PAH and several more!
- **Above historic trend growth for broad healthcare utilization.**
  - We believe we have entered a period of above trend utilization. Our view continues to be that of gradual recovery in procedural volumes as the last vestiges of COVID-related headwinds abate and the broad system returns to its normal rhythm. As nurse shortages end and hospitals look to accelerate profitable growth, certain areas of devices should experience above historical market growth in 2024.
- **Innovation in the sector expands beyond biotech and biopharma companies.**
  - A shift towards a value-based care model where costs are directly associated with the quality of the result is encouraging

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technology investments to increase efficiencies. Healthcare service providers are guiding this evolution through access to patient data and developing methods to monitor and optimize the delivery of care.

- **Improving Capital Markets Activity.**
  - Capital market activity, specifically M&A has picked up since 2023 as it was one of the best years in over a decade both in terms of count and dollar size. As the trends for deals have been evolving, we believe the uptick is sustainable as cash rich larger cap biopharma companies continue to look to replace the greater than $200 billion loss in revenues from commercial drugs that are scheduled to come off patent in the coming years. Over the past year the pace of activity has been driven by the availability of clinical data as bolt-on and in-licensing deals have outpaced cost synergy driven acquisitions. In addition, rates have been more stable and as pharma looks to make deals, they may be more comfortable because the cost of capital potentially won't double again over next 12-18 months.
- **Significant Investments in Data Management and AI.**
  - We believe healthcare will resemble the information technology sector from 2010-2020, with increased digitalization expanding throughout the sector.
  - The US health care economy is undergoing a generational transformation to a value-based system, which will be further supported by technological advancements.
  - In our view, select HMOs will benefit from this dynamic as they are the backbone of these efforts over the medium to long term.

Utilities

The utilities sector of the S&P 500 Index advanced again this quarter, outperforming the broader S&P 500 Index. The lack of Fed rate cuts has been a headwind to the sector after initially benefitting from the end of Fed tightening in late 2023. A handful of Independent Power Producers and Utilities with the ability to grow generation have been the biggest beneficiaries. Continued investor enthusiasm for the strong outlook for generative AI-related data center power demand growth propelled shares of our utilities sector and energy midstream holdings higher during 2Q24 due to rising expectations for forward power prices, regulated utilities electricity load growth, renewable energy development activity, and natural gas demand for gas-fired generation. We believe strong long-term fundamentals and still-reasonable valuations underscore the opportunity in the utilities sector. The utilities sector of the S&P 500 gained 4.7% in 2Q24, slightly ahead of the 4.3% return of the S&P 500.

While absolute performance has steadily improved in 2024, the utilities sector had its worst relative performance in over 40 years in 2023 and the utilities sector has been one of the weakest sectors over the last five years. However, even during the economic volatility of the past few years, the companies have continued to execute operationally and deliver strong earnings while also de-risking their portfolios. Continued solid execution, along with the potential growth opportunities from renewable energy investments, should help to drive the sector's earnings going forward. In addition, the increase in power demand growth driven by AI presents both a challenge to meet that demand but also supports underlying earnings growth potential. Strong fundamentals and macro factors underscore the opportunity in the sector, especially given what remains a lower-than-average interest rate environment.

Utilities are a compelling defensive growth proposition for investors for several reasons, both sector-specific and macro-related:

- The Renewables Opportunity: Improving economics in wind and solar power continue to remain a growth driver for the overall sector; companies are only now beginning to incorporate renewables into their capex plans, allowing them to earn a regulated rate of return on their renewable investments.
- Predictable cash flow and earnings: Utilities are by nature a defensive sector and those companies with regulated or quasi-regulated (renewables) businesses generate long-duration cash flows and predictable rate base earnings; in addition to providing stable dividends even in periods of uncertainty, growth in renewables should help drive earnings above the sector's historical 3%-5% growth rate.
- More favorable interest rate environment provides relief: Rapidly rising rates increase utilities' cost of capital in the near-term, but the end of Fed tightening and potential rate cuts could be tailwinds.
- Policy tailwinds: The Inflation Reduction Act (IRA) contains many provisions that are supportive of renewables development over the next decade as the US aims to lower carbon emissions and should help to sustain dividend growth.

Investment Themes & Areas of Focus

- Regulated Utilities - companies operating in favorable regulatory environments and geographies, with above-average projected earnings and/or dividend growth driven by regulatory rate-base investment.
- Renewable Electricity – the energy transition is driving ongoing investment and usage of renewables and should continue to provide unique investment opportunities over the long-term.
- Water Utilities – a focus on improving water quality, as well as pipeline replacement and maintenance, provides 10 years of transparency into spending and income plans.
- Midstream Energy - specifically companies with exposure to natural gas, a critical bridge fuel.
- Communications Infrastructure - tower operators provide critical infrastructure and strong free cash-flow generation due to multi-year contracts; data centers are well-positioned to benefit from generative AI, as well as increased pricing power driven by specialization.

Midstream Energy Infrastructure

Midstream energy continues to advance, outperforming both the broad energy sector and the S&P 500 in 2Q24. After being one of the best performing sectors in the prior quarter, the energy sector was negative in the second quarter, underperforming the broader market. Oil prices dipped mid-quarter on worries of new OPEC+ supply coming on in 4Q24, which is earlier than expected. However, prices rebounded later in the quarter reiterating that OPEC+ will re-assess supply quota increases if prices are too low. Natural Gas spiked off multi-year lows as seasonal electricity demand expectations along with the long-term need for new electricity generation will benefit natural gas—the most environmentally friendly

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fossil fuel. For the full 3-month period ending June 30, 2024, the Alerian MLP Index (AMZ) gained 3.4%, underperforming the 4.3% return of the S&P 500. The more diversified Alerian Midstream Energy Index (AMNA) advanced 5.4%

Thus far in 2024, midstream continued its strong relative performance from last year, where it had the best returns within the energy sector and matched the gains of the S&P 500. The energy sector at large (including midstream infrastructure companies) is in the midst of an historic period of financial strength, shareholder friendly corporate discipline, and high capital returns. The midstream sector in particular is well-positioned for continued financial success, both in fundamental earnings drivers and equity performance. The sector continues to generate well above average free cash flow yields yet trades at a significant valuation discount to the broader market. We think this disconnect presents an opportunity given the significant transformation in the sector and the market appears to now be taking notice; 2024 is off to a strong start with companies reporting steady growth in cash flows during Q1 earnings and management teams reiterating shareholder friendly capital policies.

We believe that, over the longer-term, midstream energy companies will play an important role in our energy future. The global energy transition will require multiple sources of energy to be successful and hydrocarbons – especially natural gas - will continue to have a role, driving future demand not just for the commodities but for the essential logistical systems that move them. With physical steel in the ground, midstream energy infrastructure companies have difficult-to-replicate asset networks with high barriers to entry, and whose adaptability to transport other energy sources is underappreciated. Management teams are increasingly aware of the role they will play in our energy future, focusing not just on the environmental impact of their operations but also on how their asset bases can and will be part of a greener future.

Investment Themes & Areas of Focus

- "Reformed" companies – those companies exhibiting greater capital discipline, and healthier, more conservative balance sheets that can withstand a downturn, along with improving ESG metrics such as solid corporate governance.
- Integrated business models – the larger, more integrated companies with multiple touch points along the energy value chain, higher barriers-to-entry, and steady cash-flows.
- Firms with exposure to the natural gas liquid (NGL), liquefied natural gas (LNG), and natural gas demand export themes.
- Companies with liquids exposure that will benefit from volume growth.

Financials

Market consensus continues to coalesce around slowing growth but not outright recession ahead. The easing pace of inflation, along with stable financial conditions are now mildly supportive to activity. Wage rates, one of the last contrary indicators, have stabilized along with a slight improvement in productivity. Finally, corporate profits broadly have favorably weathered the post pandemic period despite the demand pull forward and supply chain disruptions.

Nevertheless, there is still a possibility of a hard landing recession due to the inherent time lags following aggressive Fed tightening (key here will be to what extent that the unemployment increases) and uncertainty around the level and timing of the terminal inflation rate. The financial sector would be negatively impacted if this would occur, specifically around higher credit losses and slowing consumer/business lending activity.

The financials sector of the S&P 500 returned -2.0% for 2Q24 versus the +4.3% return of the S&P 500 index. Overall, the current credit quality and balance sheet trends are holding up for the sector.

Another positive is the slowing pace of the Federal Reserve's monetary policy adjustment. Commentary from Fed board members in the past three months emphasized the need to remain vigilant in the ongoing process of fighting inflation. At the same time, they acknowledged the diminishing pace of gain in the headline inflation rate year over year, coupled with the lagging impacts of the rate increases of the past 12 months that have yet to fully reveal themselves.

The sector's focus continues to be directed toward liquidity and the forward yield curve dynamics. In addition to liquidity, we believe another key risk to banking health is the status of loan quality. Banks carry significant exposure to commercial real estate (CRE), which is experiencing significant secular (post Covid) and cyclical challenges. As this economic cycle potentially turns, asset quality will need to be watched closely.

Future income statement pressure will also come from continued labor cost pressures, but this is being offset by improved tech driven efficiencies and generally better overall operation of the businesses by management. For the quarter, the sector was led by banks (the only industry in positive territory). Insurance and financial services were the worst performers.

Investment Themes & Areas of Focus

- Overall, the large money center, consumer finance, and super-regional banks are significantly better positioned today than they were in the 2008-2009 financial crisis across a broad range of balance sheet, capital, and risk management metrics.
- Valuations in the sector have normalized. We believe that tailwinds for future earnings growth will be primarily driven by solid revenue trends and credit controls; stabilizing net interest margins; ongoing expansion of their fee-based business opportunities; and continued efficiency improvements through better use of technology.
- Global alternative asset management business models have attractive valuations, especially given their strong recurring revenue businesses and consistent ability to raise fee-based assets to fund their ongoing deal-making activity along with optimizing their spread-based revenue streams.
- Fundamentals for P&C insurance companies are solid (driven by favorable pricing dynamics) and valuations remain attractive. This industry group continues to be a defensive safe-haven for investors.
- Secular growth companies with defensive attributes (low leverage rates, asset light models, sustainable, high margin, and high free cash flow businesses) continue to attract investors looking for both quality and durability of growth. Several digital payment and financial technology companies meet these criteria.

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