4Q23 Market Review and 1Q 2024 Outlook

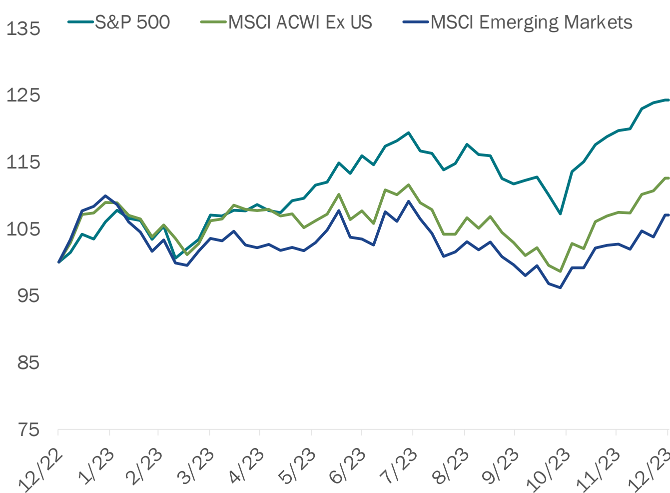
Market Backdrop

The equity markets rallied in the fourth quarter as expectations for further rate hikes declined and the potential for rate cuts in 2024 began to emerge. Continued vigorous rallies across the capital markets followed the announcement.

In the US economy in the fourth quarter, there was incremental softness in hiring despite the resilience of the labor market, oil prices trended lower, and the average US home price remained at historically high levels despite a dearth of activity in both existing home sales and new construction throughout 2023.

Economic growth outside the United States remained muted. In China, the latest residential real estate setback continued to sap the strength of its post-Covid recovery. Ongoing tensions over access to US and international technology led to new restrictions on the purchase of advanced machinery, notably leading-edge semiconductor manufacturing technology, by Chinese enterprises and government agencies. In Europe, growth remained slightly positive to close the year.

Market Index Performance



As of December 31, 2023. Source: Jennison, FactSet, MSCI.

Style Performance

- All major style indices posted strong returns in the fourth quarter. Small cap value and mid cap growth performed the best. Large cap value lagged.
- For the trailing one-year, all style indices also posted double-digit gains but with significant disparity among the different styles. Large cap growth was the best performer by a wide margin. Large cap value also underperformed in this period.
- Large cap leads for the trailing three-years across all styles, while large cap growth remains the best performer for the trailing ten years.

Style Index Performance

4Q23

	Value	Core	Growth
Large	9.5	12.0	14.2
Mid	12.1	12.8	14.5
Small	15.3	14.0	12.7

Trailing 1-year

	Value	Core	Growth
Large	11.5	26.5	42.7
Mid	12.7	17.2	25.9
Small	14.7	16.9	18.7

Trailing 3-Year

	Value	Core	Growth
Large	8.9	9.0	8.9
Mid	8.4	5.9	1.3
Small	7.9	2.2	-3.5

Trailing 10-Years

	Value	Core	Growth
Large	8.4	11.8	14.9
Mid	8.3	9.4	10.6
Small	6.8	7.2	7.2

As of December 31, 2023. Source: Jennison, FactSet, MSCI.

Sector Performance

- In the fourth quarter, all sectors posted solid gains, except for energy, which had a negative return. Real estate advanced the most, followed by information technology.
- Energy was the best performing sector on a three-year basis.
- Information technology leads for the trailing one-and-ten-years.

GICS Sector Performance - S&P® 500 Index

	4Q	One Year	Three Years	Five Years	Ten Years
Real Estate	19	12	7	9	9
Information Technology	17	68	15	27	21
Financials	14	12	11	12	10
Industrials	13	18	11	14	10
Consumer Discretionary	12	42	4	14	12
Communication Services	11	56	4	13	8
Materials	10	13	8	14	9
Utilities	9	-7	4	7	9
Health Care	6	2	8	12	11
Consumer Staples	6	1	6	11	9
Energy	-7	-1	36	13	3
Total	12	26	10	16	12

As of December 31, 2023. Source: Jennison, FactSet, MSCI.

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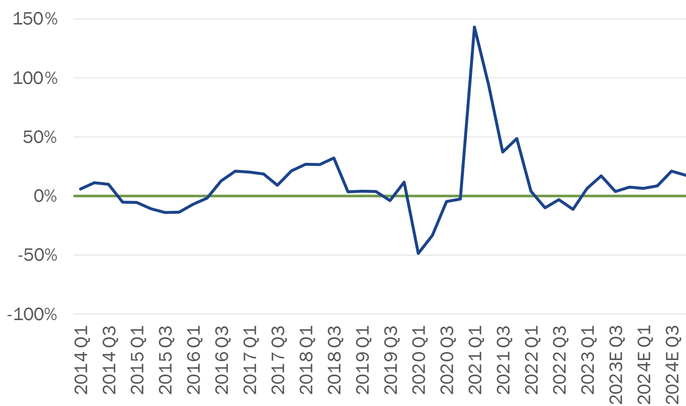
Sector Weights

	S&P 500	MSCI ACWI ex US	Russell 1000 Growth	Russell 10000 Value
Communication Services	9	5	11	5
Consumer Discretionary	11	11	16	5
Consumer Staples	6	8	4	8
Energy	4	6	1	8
Financials	13	21	6	22
Health Care	13	9	11	15
Industrials	9	13	6	14
Information Technology	29	12	44	10
Materials	2	8	1	5
Real Estate	3	2	1	5
Utilities	2	3	0	5

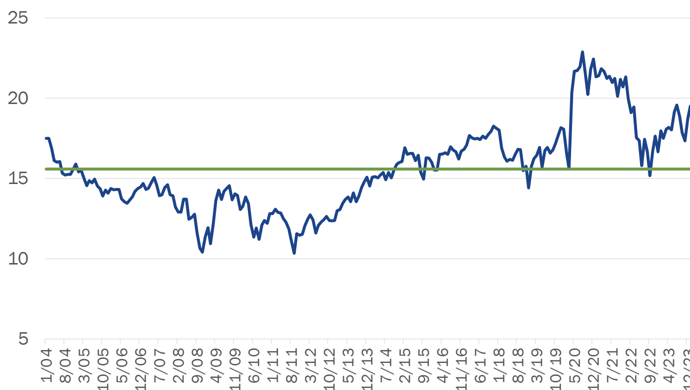
As of December 31, 2023. Source: Jennison, FactSet, MSCI.

S&P 500® Index - YoY EPS Growth



As of December 31, 2023. 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 December 31, 2023. Source: Jennison, FactSet, MSCI.

Outlook from Jennison's Growth Teams

Throughout 2023, we remarked on the resiliency of labor markets and consumption while investors anticipated a significantly greater slowdown and a possible recession that, ultimately, failed to occur. The Fed's expeditious steps following the failure of three major US banks in March provided stability and calm, resulting in a remarkably short-lived period of unease. The ongoing war in Ukraine and the tragedy in Israel and resulting conflict in Gaza have not led to the typical reaction in energy markets. Indeed, the price of energy has declined since October, in line with reduced demand trends and abundant supply.

The continued volatility in capital markets reflected economic and geopolitical realities in different ways throughout the year. The 10-year US Treasury bond began 2023 yielding approximately 3.8%, with an expectation that the federal funds rate would rise as the battle to curb inflation continued. The federal funds rate, which started the year at 4.25%–4.50%, reached a peak of 5.25%–5.50% in July and remained at that level through year-end. Meanwhile, the 10-year US Treasury bond yield peaked at just under 5.0% in late October before declining back to where it began the year, at roughly 3.8%, to close out 2023.

The grudging pace of the US economic slowdown might be the biggest surprise of the year. Consumer resiliency in the face of geopolitical and macroeconomic turbulence is the primary reason, reflecting low unemployment, balance sheet strength, and rising financial asset prices. Uncertainty about the US economy's ability to avoid recession remains a focus entering 2024. We believe the evidence suggests slowing growth but not outright recession ahead. The easing pace of inflation, along with lower borrowing costs, are new tailwinds to activity. Wage rates, one of the last contrary indicators, are no longer rising and, in some cases, entry level pay is now below the pandemic peak. Finally, corporate profits broadly have favorably weathered the post pandemic period despite the demand pull forward and supply chain disruptions.

Taken together, the last two plus years encompassed financial market distress driven by historic inflationary pressures and interest rate increases, followed by a rebound in asset prices to levels that, in some cases, reached near peaks. Valuation has played a significant role in both the decline and rebound of asset prices. This period has been challenging, but we note that many of our growth holdings have meaningfully participated in the recovery. These companies have navigated throughout the environment in strong financial and operational health.

Outlook from Jennison's Sector Teams

Information Technology

After some give-back in Q3, the S&P 500 Index's information technology sector was up 17.2% in the fourth quarter of 2023. The sector finished the year up 57.8%, an impressive recovery from a disappointing 2022. This reflects both better than expected fundamentals across a broad range of business models, along with an improving macro environment (primarily inflation coming down sharply and the consumer holding up well). This has translated to less uncertainty surrounding the forward discounting mechanism for long duration equities.

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Calendar year 2022 produced multiple compression and lowered earnings revisions across the entire sector. Forward consensus on near term fundamentals and growth trajectories had been reset lower in anticipation of further deterioration of the macro environment, with P/E multiples coming down too. Nevertheless, driven by disruptive opportunity for AI and the digital transformation of the consumer and businesses, the longer-term underlying strength in these business models and their secular revenue trends remain solid and were highlighted across the overall sector's reported earnings in 2023.

The U.S. economy stands in better shape than we anticipated when the year began. Solid employment has sustained consumer spending at a solid pace. Consumer confidence currently reflects optimism in the near term despite announced work force reductions. In addition, 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, which weakened earlier last year, have stabilized. 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 a rebound in spending and a return to longer-term investment trends. The strong rebound in the prices of select technology reflects both the depressed nature of valuations when the year began and the first signs of upgrades to near- and medium-term revenue and profit expectations from company managements, a trend we believe will gather pace in the coming quarters.

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.

It is important to recognize that technology is no longer a distinct sector; rather, it is woven through every industry in which we invest. This backdrop 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.

We also see continued acceleration and long duration technology demand from the massive global millennial and Gen-Z population due to their early uptake of so many digital-economy related products that are solving their real-world problems (many of which are driven through the smartphone). 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

- We expect to see generative 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, 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 5G, SaaS, business intelligence (using 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 rates inflecting higher.

Health Care

The health care sector of the S&P 500 Index advanced 6.4% in the fourth quarter, trailing the overall S&P 500 Index's return of 11.7%. Additionally, the Nasdaq Biotechnology Index advanced 10.7%. Over the trailing 12-months, the health care sector's 1.9% return trailed the overall S&P 500 Index's 26.2% gain.

The S&P 1500 healthcare index trailed the broader S&P 500 Index by greater than 20% on a trailing one-year basis, an unprecedented statistic last observed during the internet bubble in the late 1990s. The broad market's return has almost entirely been driven by 7 stocks (Apple, Microsoft, Amazon, Alphabet, Nvidia, Meta and Tesla). As a result, health care stocks are not expensive today and are priced below the broader markets. Slowing global economies call for the resilience that health care companies can offer, yet the sector remains at a 10% discount to global equity markets compared to an average premium of 3% over the past two decades. We believe several factors will drive relative results across multiple health care industries.

Investment Themes & Areas of Focus

Therapeutic Advancements Targeting Massive Total Addressable Markets

- Innovation and spending across drug development, genetic sequencing, data collection and health care service delivery is accelerating and has continued to increase post-COVID. The U.S.

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market alone is approximately $4 trillion and growing at a rapid pace.

- We've seen an unprecedented level of development aimed at some of the world's largest total addressable markets including diabetes, obesity, cardiovascular disease, and cancer.
- Data from this summer's American Diabetes Association conference indicated even greater effectiveness of Eli Lilly and Novo Nordisk's next gen diabetes and obesity drugs (approaching weight loss reduction of over 15% in 32-36 weeks).
- Initial results from NVO's SELECT trial also indicated a 20% reduction in cardiovascular events, which are among the world's deadliest and most costly conditions to treat. We look forward to the full readout at the American Heart Association in November and believe the data can unlock additional catalysts for the industry.
  - For investors, these advancements are creating new opportunities among select pharmaceutical companies that have the depth of resources—including large balance sheets and sizeable manpower—to capitalize on this enormous market for cardiovascular treatments and prevention.
  - Research indicates that these assets will have an even greater comorbidity opportunity, with potential impacts on diseases such as CKD, NASH, and sleep apnea.
- We're witnessing significant advancements in antibody drug conjugate platforms that can directly target various forms of cancer.
- Notable advancements in gene-based therapies have the potential to address 7000 genetic diseases, 95% of which do not currently have treatments.

Increasing Procedural Spend and Utilization

- Health care utilization and procedures have increased post-COVID, with an acceleration over the past 12 months. United and Humana recently released data points citing the increase outpatient and inpatient utilization among seniors. These data points have been confirmed by others, suggesting outpatient hip/knee and cardio procedures have continued to be strong.
- As we look forward, we also expect to see more headwinds for the industry subsiding, including a decrease in inflation, improvements in supply chains and a declining dollar.
- An aging population, more engaged consumers and advancements in tech-enabled procedures and devices should support further upside over the long term.

Improving Capital Markets Activity

- M&A activity, both in terms of count and dollar size, has notably improved. Based on the current run rate for the year, 2023 is on pace to be one of the strongest M&A years in over a decade. We believe the uptick in M&A activity 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.
- Year-to date, 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. The trend of science-led deals has benefited our portfolio as we have owned multiple acquisition targets in 2023. 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 will not double again over next 12-18 months.

Significant Investments in Data Management and AI

- We believe health care will resemble the information technology sector during 2010-2020, with increased digitalization expanding throughout the sector.
- The U.S. 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

While the sector continued to underperform the broader market, utilities finally advanced in 4Q23 after three straight quarterly losses. Rising interest rates weighed on the group throughout the year, but the pullback in the 10-year Treasury and an eye toward the end of Fed tightening finally brought some relief to the utilities sector in 4Q. There were periods this year where recessionary concerns spiked and utilities performed better, but broadly speaking defensives and cyclicals lagged. While retreating, inflation remains a factor for the group, but utilities have shown that they are able to manage the impact of inflationary pressures with efficiency gains, as evidenced in earnings results. Despite the tailwind from the retreat in bond yields, punitive state rate case decisions during the quarter tempered the outlook for next year and the sector underperformed the S&P 500 Index. The utilities sector of the S&P 500 Index gained 8.6% in 4Q23 versus the 11.7% return of the S&P 500 Index.

Despite a meaningful recovery in 2022, the utilities sector had its worst relative performance in over 40 years in 2023. While fundamentals have remained strong, the group's performance versus the broader market has struggled over the past five years and the utilities sector has been one of the weakest. However, even during the economic volatility of the past few years, utility 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, continued recessionary concerns and a flattening yield curve remain tailwinds. Strong fundamentals and macro factors underscore the opportunity in the sector, especially given what remains a lower-than-average interest rate environment by historical standards (even when considering the recent uptick in rates).

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-

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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, in our view.

- Ability to effectively navigate a rising interest rate environment: While rapidly rising rates increase utilities' cost of capital in the near-term, over time they can pass those costs along, resulting in higher ROEs.
- Policy tailwinds: The Inflation Reduction Act (IRA) contains many provisions that are supportive of renewables development over the next decade as the U.S. 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 advanced again in the fourth quarter of 2023, outperforming all other energy sub-sectors but lagging the S&P 500 Index. After a very strong 3Q, the energy sector gave back gains at the end of the year and was the worst-performing sector of the market throughout 4Q. Despite solid demand, oil prices fell steadily during the period as production disagreements within OPEC exacerbated what was already a deteriorating supply outlook. WTI crude fell 21.0% and Henry Hub natural gas was weak as well, falling 14.2%. Despite lagging the broader market, midstream was once again the best-performing energy sub-sector during 4Q and, along with the refiners, the only segment to advance. For the full 3-month period, the Alerian MLP Index (AMZ) gained 5.0%, while the Alerian Midstream Energy Index (AMNA) advanced 6.4%, both lagging the 11.7% return of the S&P 500 Index.

Some of 2022's strong tailwinds dissipated in the first half of the year and macro uncertainties weighed on energy broadly, but the midstream segment bucked the broader trend. In fact, midstream was the leader within energy for 2023. Only the refiners came close to matching the AMZ's 26.6% gain for the year while the broad energy sector of the S&P 500 declined 1.4%. Driven by above-average cash flow yields and volume growth yet trading at a significant valuation discount to the broader market, the group remains well-positioned both near- and long-term. We think this disconnect presents an opportunity given the significant transformation in the sector over the last few years. We believe the capital discipline shown by management teams will continue, the sector will remain free cash flow positive, and companies will continue to return capital to shareholders. Earnings results have been strong and share buybacks continue to provide stock valuation support.

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.
- Utilities with midstream infrastructure assets that can benefit from the broad tailwinds driving the sector.

Financials

- We believe the evidence suggests slowing growth but not outright recession ahead. The easing pace of inflation and lower borrowing costs are new tailwinds to activity. Wage rates, one of the last contrary indicators, are no longer rising and, in some cases, entry level pay is now below the pandemic peak. 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 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 Index returned +14.0% for 4Q23 versus the +11.7% return of the S&P 500 Index. For the full year 2023, the financials sector of the S&P 500 finished up +12.1% vs. the S&P 500 at +26.3%. We continue to see improving news on credit quality and balance sheet trends.
- 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

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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 duration differences between a given bank's assets (loans, securities) and liabilities (deposits and term funding). 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 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 within the sector all industry groups had solid positive returns. The sector was led by consumer finance, banks, and capital markets – all up between 19-28%. The other three industry groups (financial services, insurance, and mortgage REIT's) all finished up 7-9%.

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. 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.
- As a return to normalized growth plays out over the long-term, secular growth companies with defensive attributes (low leverage rates, asset light models, sustainable, high margin, and high free cash flow businesses) should fare better. Several digital payment and financial technology companies meet these criteria.

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Source for Russell® Index data: Mellon Analytical Solutions and FactSet. Source for S&P 500® Index data: Standard & Poor's, FactSet and FT Interactive Data Corporation. Source for Alerian Index: Alerian.

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