

Small Cap Stocks to Rebound in 2024?

 westwoodgroup.com/insight/small-cap-for-2024-whgsx/

For seven straight years, large cap stocks have outperformed small-caps – and 2023 was a blowout, as the large-cap Russell 1000 Index beat the small-cap Russell 2000 Index by 9.60%.

But the trend goes even further – nine of the last ten years, even 14 of the last 19 calendar years have ended in favor of large-cap stocks. The last sustained run of small-cap dominance was 1999-2004, when the Internet was still relatively new, the dot-com bubble was breaking, and the Dallas Cowboys had only recently won the Super Bowl.

Small-cap stocks staged a rebound in the fourth quarter to end 2023 on a high note. Does the recovery portend a small-cap renaissance in 2024 and beyond?

Why Small Caps?

It's long been common investment knowledge that small-cap stocks have historically outperformed large-cap stocks.

But is it? The “size premium” that had been part of the lure of small-caps has seemingly been nullified. The domination of large caps is clear: for nearly every trailing five-year period for the past forty-five years, large-cap stocks (measured by the Russell 1000 Index) have outperformed small-cap stocks, represented by the Russell 2000 Index.

If this relationship continues, then it would upend one of the foundational tenets of investing: that investors are compensated for taking on additional risk. Smaller companies are inherently riskier than larger companies, and investors expect to be compensated for that risk.

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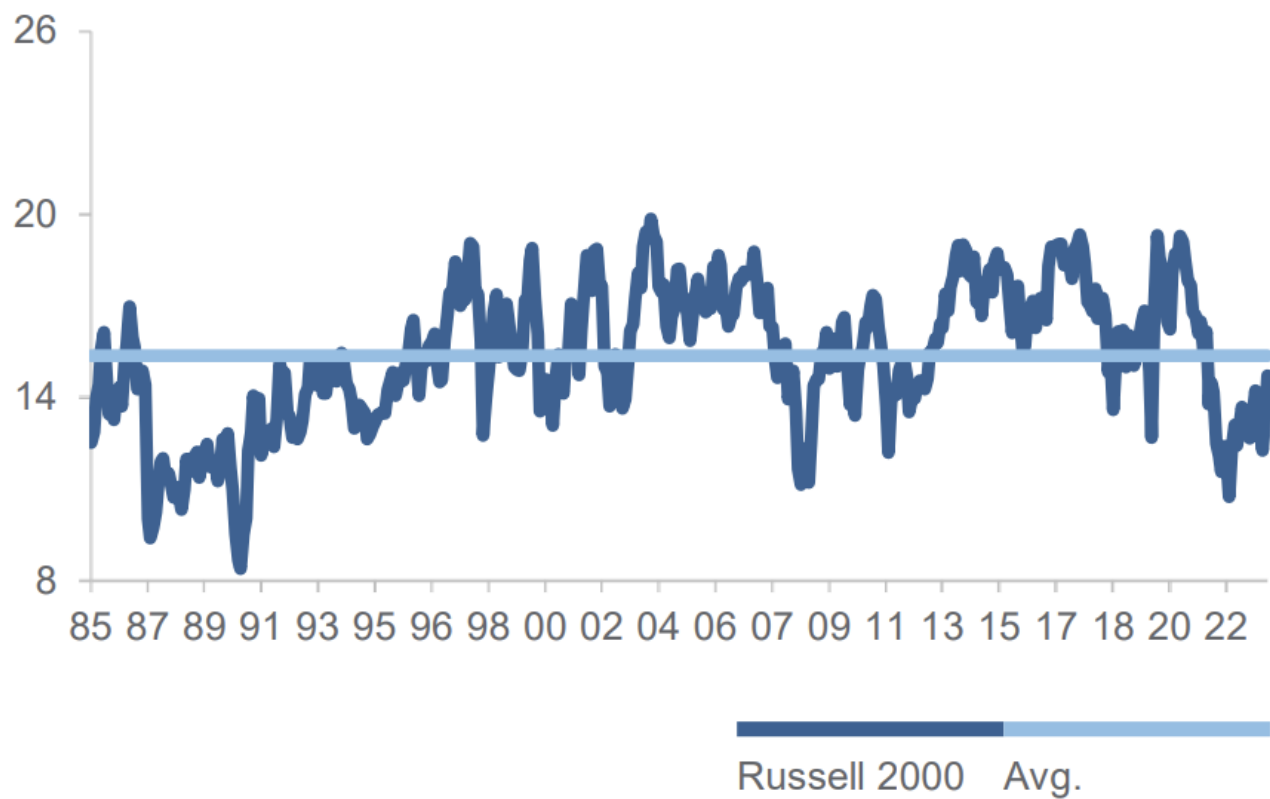
	4Q 23	1 Year	5 Years	10 Years	15 Years	20 Years	25 Years	30 Years	35 Years	40 Years	45 Years
Russell 1000	11.96	26.53	15.52	11.80	14.02	9.78	7.72	10.18	10.83	11.29	11.97
Russell 2000	14.03	16.93	9.97	7.16	11.30	8.11	7.91	8.56	9.32	9.14	10.97
Difference	2.07	-9.60	-5.55	-4.65	-2.72	-1.67	0.19	-1.62	-1.51	-2.15	-1.01

Why Now?

1 Small-Cap stocks are historically undervalued. Relative to large-cap stocks, small-cap stocks are at historical low P/E ratios, providing them ample room for potential appreciation.

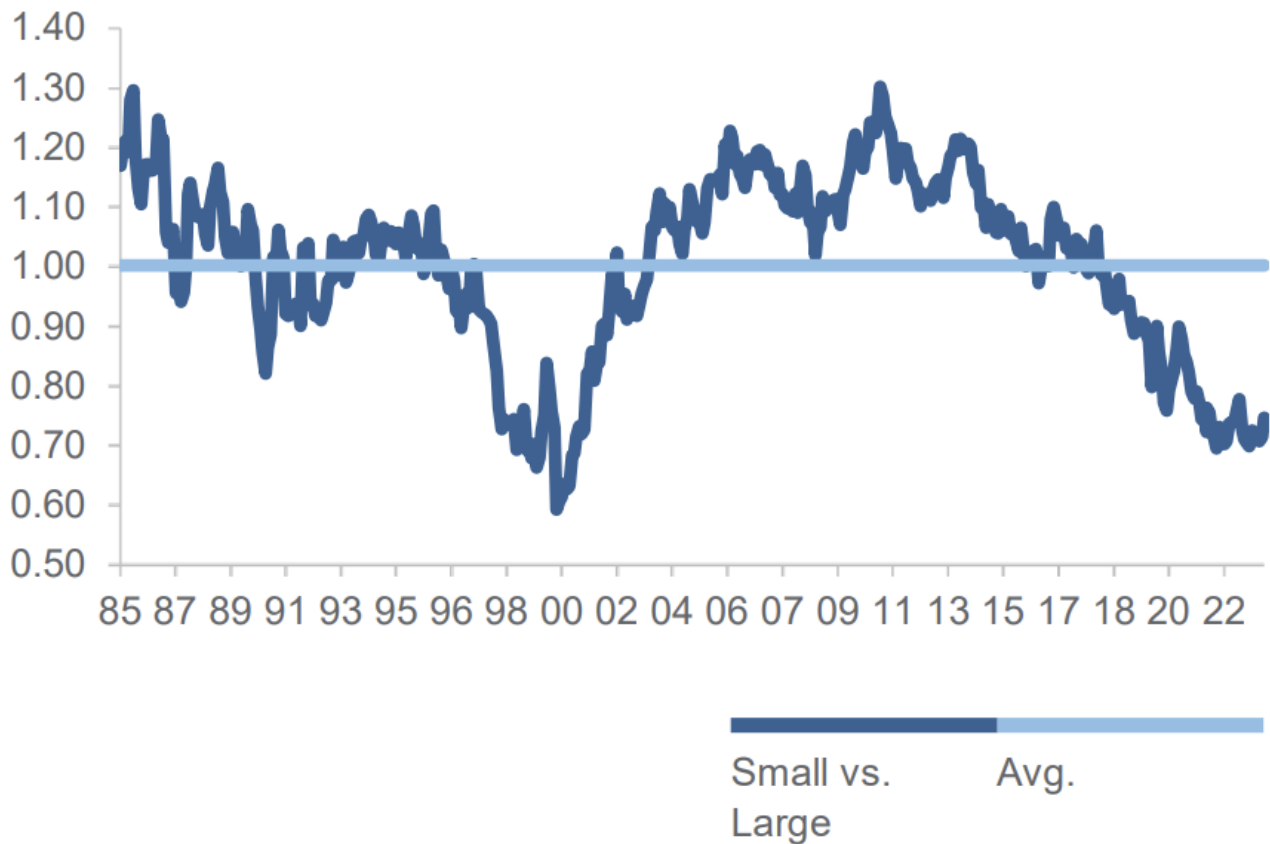
Small cap forward P/E below the long-term average

Russell 2000 Forward P/E, 1985-11/30/2023



Small caps remain historically undervalued vs large caps

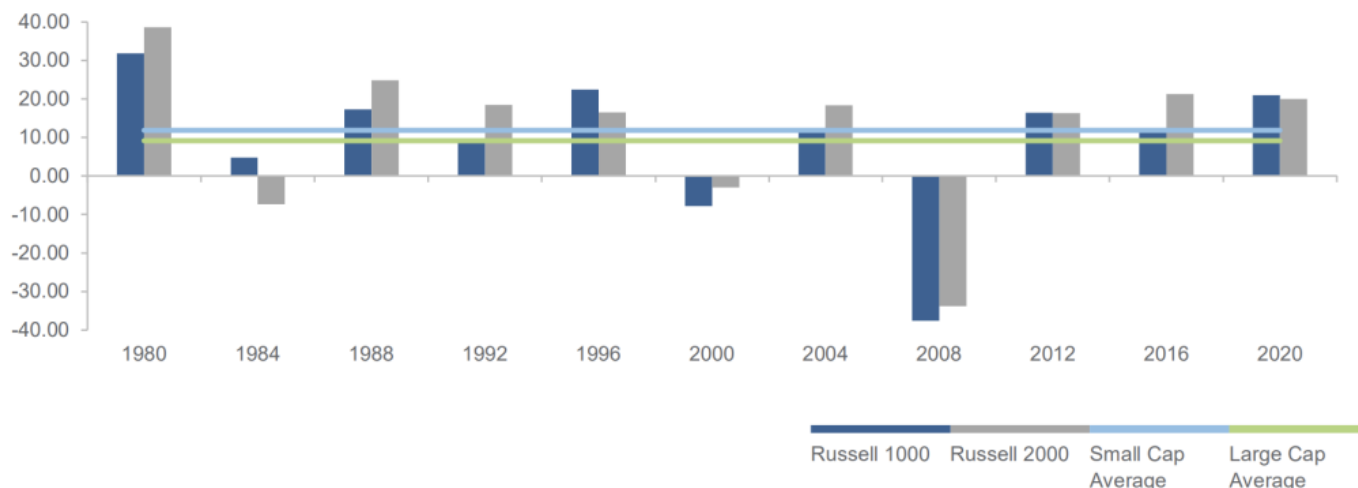
Relative Forward P/E: Russell 2000 vs Russell 1000, 1985-11/30/2023



BofA Global Research, Small/Mid Cap Valuations, 12/13/23. Past performance is not indicative of future results. Indexes are unmanaged, do not incur management fees, costs and expenses, and cannot be invested in directly. The index is unmanaged and is not available for direct investment.

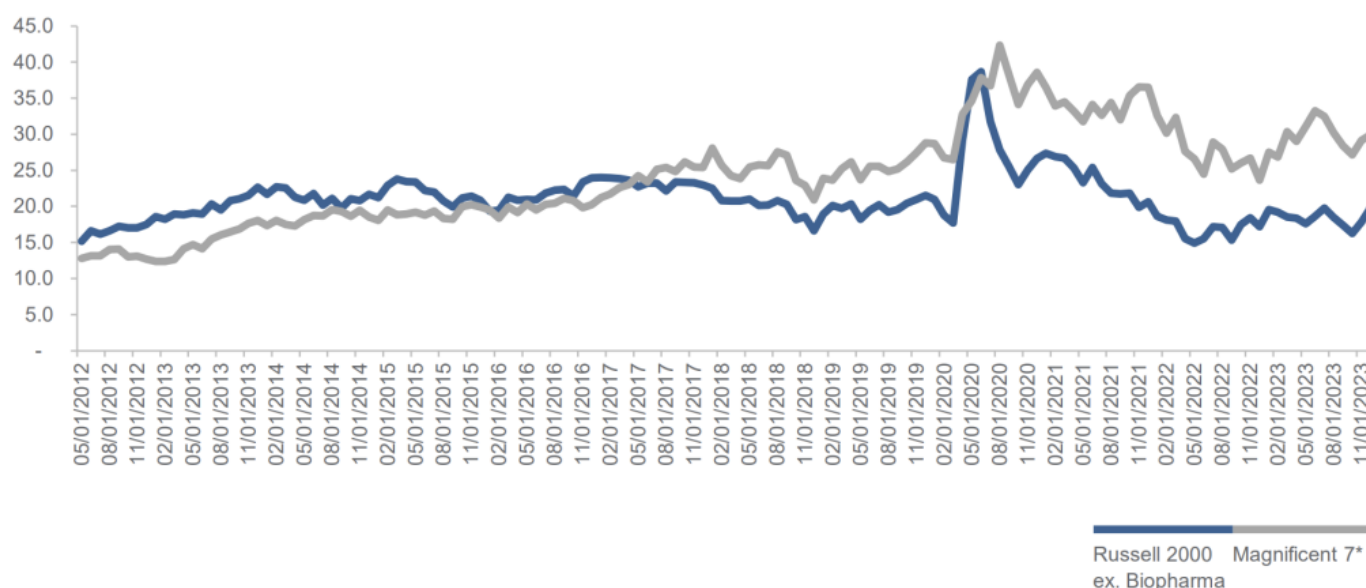
²Presidential election years have been good for small-cap outperformance. Historically, small-caps have outperformed seven of the eleven election years, and by an average of 2.68%.

Large Cap and Small Cap Performance During Election Years 1980 - 2020



Small-Cap (ex-biotech) earnings are expected to grow faster than the Magnificent Seven. The growth case for small caps shows earnings growth the next two years greater than the Magnificent Seven, and at a lower P/E ratio.

Small-cap valuation, by comparison, is more reasonable than Magnificent 7 NTM P/E (Bottom-Up)



Furey Research Partners, 4Q23 Quarter-end and 2023 Year-End Letter, p. 23. Past performance is not indicative of future results. Indexes are unmanaged, do not incur management fees, costs and expenses, and cannot be invested in directly. The index is unmanaged and is not available for direct investment.

Why Westwood Small Cap Value?

The initial phase of a market rebound tends to benefit everyone – a low-quality rally. That’s what happened in the fourth quarter, as lower-quality, high-beta and non-earning companies sparked the fourth-quarter returns in small-cap stocks.

As the bull market matures, investors tend to seek quality and sustainability of earnings. After the initial rising tide lifting all boats, investors typically will start to sort the wheat from the chaff, placing a greater emphasis on earnings, profitability, and sustainability. This is when our investment process tends to shine, as we share that focus on quality.

In 2024, we expect to see small-caps rebound, and we believe that the companies that meet our investment criteria – quality businesses with strong balance sheets and sustainable metrics, and undervalued relative to peers or the market – may have a strong year.

Westwood Quality SmallCap Fund (WHGSX)

Standardized Performance

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	4Q 23	YTD	1 Year	3 Years	5 Years	10 Years	Since Inception
Westwood Quality SmallCap Fund – WHGSX (Inception: 4/2/2007)	15.02%	17.17%	17.17%	9.48%	11.25%	7.72%	7.86%
Russell 2000 Value – Total Return	15.26%	14.65%	14.65%	7.94%	10.00%	6.76%	7.14%

Inception Date: 4/2/2007. Returns less than one year are cumulative. High short-term performance of the fund is unusual, and investors should not expect such performance to be repeated.

The performance data quoted represents past performance. Past performance is not indicative of future results. The investment return and principal value will fluctuate so that an investor’s shares, when redeemed, may be worth more or less than their original cost and current performance may be lower or higher than the performance quoted. For performance data current to the most recent month end, please call [\(877\)-FUND-WHG](tel:877-FUND-WHG).

The total expense ratio for the WHGSX Fund is 1.04% (gross), 0.92% (net). Westwood Management Corp. (the Adviser) has contractually agreed to waive fees and reimburse expenses until March 1, 2024. Absent these waivers, total return would be reduced. Performance Data Source: Ultimus Fund Solutions, LLC. Index returns do not reflect any management fees, transaction costs or expenses. Indexes are unmanaged and one cannot invest directly in an index.

Disclosure

This presentation must be preceded or accompanied by a prospectus. Read the prospectus carefully before investing or sending money. To determine if this Fund is an appropriate investment for you, carefully consider the Fund's investment objectives, risk factors and charges and expenses before investing. This and other information can be found in the Fund's prospectus which may be obtained by calling (877)-FUND-WHG ((877)-386-3944). Please read the prospectus carefully before investing.

Potential Risks

Mutual fund investing involves risk, including possible loss of principal. There can be no assurance that the Fund will achieve its stated objectives. There are specific risks inherent in small cap investing such as greater share price volatility as compared to other funds that invest in stocks of companies with larger and potentially more stable market capitalizations.

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