

## **Soft landing possibility makes small caps even more appealing**

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The most anticipated recession in recent history may never happen, and even if it does it may likely be short and shallow. Key risks stemming from elevated interest rates remain, but the global disinflation combined with remarkable strength of labour markets increase the probability of a soft landing.

The first half of the year saw a robust rally from large caps. However, investors may feel uneasy with their elevated valuations especially given the increased attractiveness of bond yields. As long as the global economy manages to avoid a systemic shock, small cap companies may be an attractive position for the coming months thanks to their more domestic profiles, relatively low valuations vs history and bound for a significant catch up potential.

### **What does Small Cap mean?**

The definition of small cap companies is naturally all about the market capitalization. Nevertheless, the notion of “small cap” varies across regions and can also evolve over time. The median size of a company within the MSCI World Small Cap Index is \$992mn while for MSCI Emerging Market Small Cap Index the median market cap is \$432mn<sup>(1)</sup>.

One misconception is that small cap stocks are only companies in an early stage of life, while in reality these companies often have well established businesses but with a significant growth potential ahead.

Small caps tend to be relatively domestic and cyclical. However, there is a variety of strategies available with specific risks and opportunities associated with investing in each region.

### **US Small & Mid Caps**

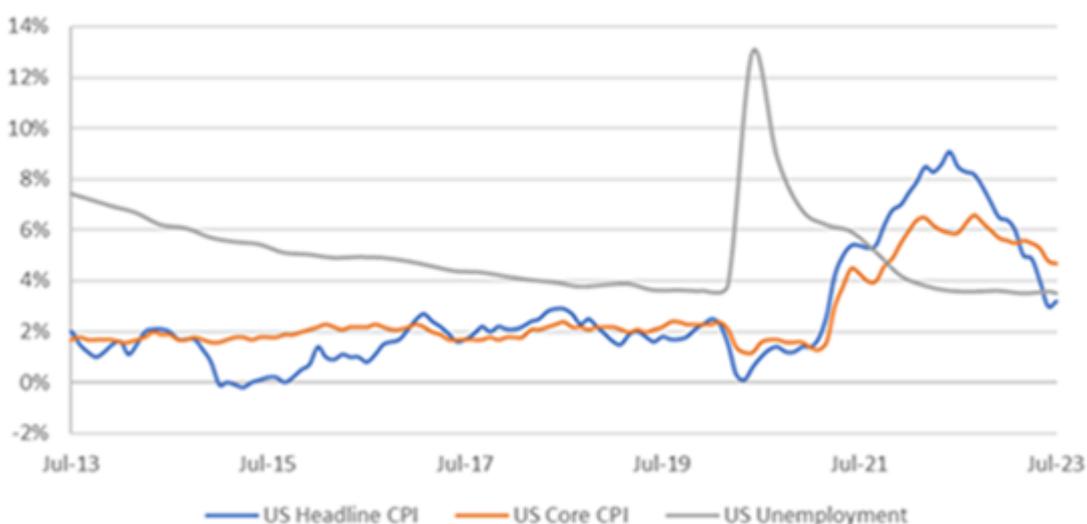
Russell 2000 Index and S&P MidCap 400 Index both outperformed US large caps since the resolution of debt ceiling disputes in early June<sup>(2)</sup>. We continue to see an investment case for US Small and Mid Caps as the July CPI at 3.2.% allows to believe that the recent rate hike may have been the last one in this cycle. Is the battle against inflation being won? At least for now it has been going in the right

direction and yet, this has been achieved without destroying the labour market. Indeed US unemployment (U3) stood at 3.5% and average hourly earnings increased by 0.4% in July. Tight labour market drives US consumer resiliency which in turn supports more domestic companies within the Russell 2000 Index and the S&P MidCap 400 Index, as they generate 80% and 76% of revenue within the US, respectively<sup>(3)</sup>. This allows them to keep going during the current economic slowdown.

In the longer run, initiatives such as the Infrastructure Investment and Jobs Act, CHIPS and Science Act, Inflation Reduction Act and broad reshoring efforts are likely to benefit more domestic and industrial heavy SMID companies.

Unlike large caps, Russell 2000 Index trade at relatively undemanding, 14x positive earnings, below a 17x 10y average <sup>(4)</sup>. Investors wanting to obtain an additional value tilt may turn towards the MSCI USA Small Cap value weighted index.

### US Inflation & Unemployment



Source: Bloomberg Finance L.P. as of 31 July 2023.

### SPDR® Russell 2000 U.S. Small Cap UCITS ETF

Fund Name	SPDR® Russell 2000 U.S. Small Cap UCITS ETF
ISIN	IE00BJ38QD84
Base Fund Currency	USD
Primary Ticker	ZPRR GY
Other Tickers	R2SC LN, R2US LN, R2US SE, R2US FP, R2US IM, R2USN MM
Total Fund Assets (\$mn)	2,102
TER	0.30%
Index Name	Russell 2000 Index

Annualised Net Performance	3M	YTD	1Y	3Y	5Y	Since Inception* (%)
SPDR <sup>®</sup> Russell 2000 US Small Cap UCITS ETF	5.01%	7.79%	11.66%	10.45%	3.81%	6.31%
Russell 2000 Net 30% Return	5.09%	7.85%	11.82%	10.43%	3.81%	6.13%
Difference	-0.08%	-0.06%	-0.15%	0.02%	0.00%	0.18%

\*Inception date is 30 June 2014. Performance data as of 30 June 2023 in USD. Other Datapoints as of 31 July 2023. Past performance is not a reliable indicator of future performance. Performance returns for periods of less than one year are not annualized. The performance figures contained herein are provided on a net of fees basis and reflect the deduction of advisory or other fees. The performance includes the reinvestment of dividends and other corporate earnings and is calculated in USD. Index returns are unmanaged and do not reflect the deduction of any fees or expenses. Index returns reflect all items of income, gain and loss and the reinvestment of dividends and other income as applicable. Visit [www.ssga.com](http://www.ssga.com) for most recent month-end performance.

## SPDR<sup>®</sup> S&P<sup>®</sup> 400 U.S. Mid Cap UCITS ETF

Fund Name	SPDR <sup>®</sup> S&P <sup>®</sup> 400 U.S. Mid Cap UCITS ETF
ISIN	IE00B4YBJ215
Base Fund Currency	USD
Primary Ticker	SPY4 GY
Other Tickers	SPY4 LN, SPX4 LN, SPY4 IM, SPY4 SE, SPY4 FP, SPY4N MM
Total Fund Assets (\$mn)	1,785
TER	0.30%
Index Name	S&P MidCap 400 <sup>®</sup> Index

Annualised Net Performance	3M	YTD	1Y	3Y	5Y	10Y	Since Inception* (%)
SPDR <sup>®</sup> S&P <sup>®</sup> 400 US Mid Cap UCITS ETF	4.68%	8.56%	16.87%	14.77%	7.16%	9.57%	10.51%
S&P 400 Net Total Return Index	4.71%	8.56%	16.99%	14.93%	7.28%	9.69%	10.64%
Difference	-0.03%	0.00%	-0.12%	-0.16%	-0.11%	-0.13%	-0.13%

\*Inception date is 30 January 2012. Performance data as of 30 June 2023 in USD. Other Datapoints as of 31 July 2023. Past performance is not a reliable indicator of future performance. Performance returns for periods of less than one year are not annualized. The performance figures contained herein are provided on a net of fees basis and reflect the deduction of advisory or other fees. The performance includes the reinvestment of dividends and other corporate earnings and is calculated in USD. Index returns are unmanaged and do not reflect the deduction of any fees or expenses. Index returns reflect all items of income, gain and loss and the reinvestment of dividends and other income as applicable. Visit [www.ssga.com](http://www.ssga.com) for most recent month-end performance.

## SPDR<sup>®</sup> MSCI USA Small Cap Value Weighted UCITS ETF

Fund Name	SPDR <sup>®</sup> MSCI USA Small Cap Value Weighted UCITS ETF
ISIN	IE00BSPLC413
Base Fund Currency	USD
Primary Ticker	ZPRV GY
Other Tickers	USSC LN
Total Fund Assets (\$mn)	390
TER	0.30%
Index Name	MSCI USA Small Cap Value Weighted Index

Annualised Net Performance	3M	YTD	1Y	3Y	5Y	Since Inception* (%)
SPDR® MSCI USA Small Cap Value Weighted UCITS ETF	5.11%	7.08%	13.94%	22.31%	7.52%	7.51%
MSCI USA Small Cap Value Weighted Index	5.13%	7.09%	13.98%	22.48%	7.69%	7.71%
<b>Difference</b>	-0.02%	-0.02%	-0.04%	-0.17%	-0.18%	-0.20%

\*Inception date is 18 February 2015. Performance data as of 30 June 2023 in USD. Other Datapoints as of 31 July 2023. Past performance is not a reliable indicator of future performance. Performance returns for periods of less than one year are not annualized. The performance figures contained herein are provided on a net of fees basis and reflect the deduction of advisory or other fees. The performance includes the reinvestment of dividends and other corporate earnings and is calculated in USD. Index returns are unmanaged and do not reflect the deduction of any fees or expenses. Index returns reflect all items of income, gain and loss and the reinvestment of dividends and other income as applicable. Visit [www.ssga.com](http://www.ssga.com) for most recent month-end performance.

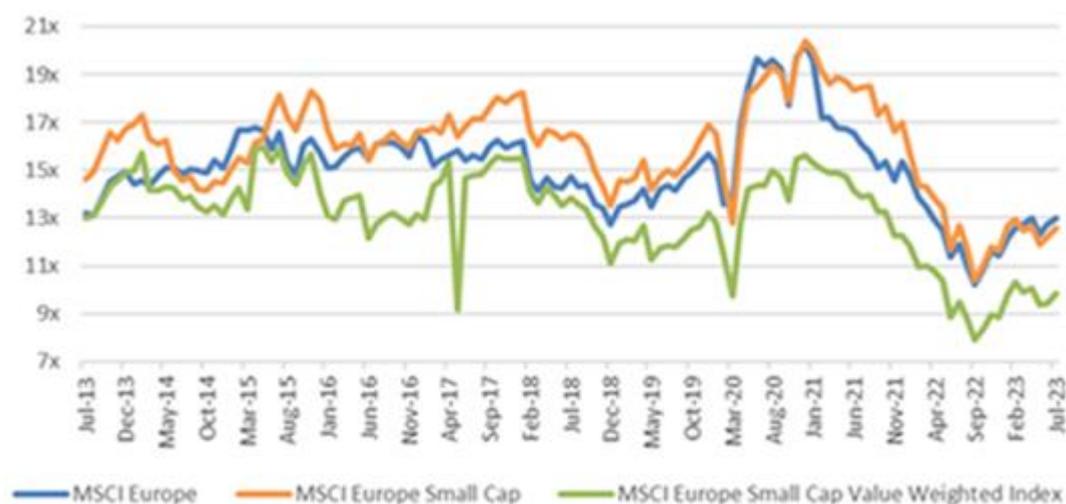
## Europe Small Caps

Europe, just like the rest of the world is having to grapple with a slowing economy and particularly tight financial conditions since the ECB abandoned its negative interest rate policy and brought their main Refi rate to levels last seen pre-GFC. However, both the MSCI Europe and the MSCI Europe Small Cap indices reflect this slowdown in their valuations, trading at Forward P/E ratios of 13.0x and 12.6x, respectively<sup>(5)</sup>. Although the ECB is lagging the FED, the inflation in Europe is moderating too and the unemployment remains in check benefitting more local companies.

Indeed, companies within the MSCI Europe Small Cap Index are more domestic generating 64% of revenue within Europe while the corresponding number for the large caps index is only 41%<sup>(6)</sup>. This allows to mitigate the impact stemming from weaker than expected China trade numbers as well as potential Euro strengthening against the US dollar.

The MSCI Europe Small Cap index does not trade on materially lower multiples compared to the large cap index, simply because MSCI Europe has become a value trade in itself. In order to find a value tilt within European small caps investors may consider the MSCI Europe Small Cap Value Weighted Index.

## MSCI Europe Small & Large Caps P/E using FY1 Est



Source: FactSet as of 31 July 2023. Availability of estimates for small cap companies may be limited.

## SPDR® MSCI Europe Small Cap UCITS ETF

Fund Name	SPDR® MSCI Europe Small Cap UCITS ETF
ISIN	IE00BKWQ0M75
Base Fund Currency	EUR
Primary Ticker	SMC FP
Other Tickers	SMCX SE, SMCX IM
Total Fund Assets (€mn)	138
TER	0.30%
Index Name	MSCI Europe Small Cap Index

Annualised Net Performance	3M	YTD	1Y	3Y	5Y	10Y	Since Inception* (%)
SPDR® MSCI Europe Small Cap UCITS ETF	-0.01%	5.87%	6.94%	8.08%	2.97%	8.56%	7.52%
MSCI Europe Small Cap Index	-0.17%	5.69%	6.74%	7.92%	2.86%	8.63%	7.72%
<b>Difference</b>	0.16%	0.18%	0.20%	0.16%	0.11%	-0.08%	-0.20%

\*Inception date is 31 March 2005. Performance data as of 30 June 2023 in EUR. Other Datapoints as of 31 July 2023. Past performance is not a reliable indicator of future performance. Performance returns for periods of less than one year are not annualized. The performance figures contained herein are provided on a net of fees basis and reflect the deduction of advisory or other fees. The performance includes the reinvestment of dividends and other corporate earnings and is calculated in EUR. Index returns are unmanaged and do not reflect the deduction of any fees or expenses. Index returns reflect all items of income, gain and loss and the reinvestment of dividends and other income as applicable. Visit [www.ssga.com](http://www.ssga.com) for most recent month-end performance. The SPDR® MSCI Europe Small Cap UCITS ETF was previously known as the streetTRACKS® MSCI Europe Small Cap ETF.

## SPDR® MSCI Europe Small Cap Value Weighted UCITS ETF

Fund Name	SPDR® MSCI Europe Small Cap Value Weighted UCITS ETF
ISIN	IE00BSPLC298
Base Fund Currency	EUR
Primary Ticker	ZPRX GY
Total Fund Assets (€mn)	147
TER	0.30%
Index Name	MSCI Europe Small Cap Value Weighted Index

Annualised Net Performance	3M	YTD	1Y	3Y	5Y	Since Inception* (%)
SPDR® MSCI Europe Small Cap Value Weighted UCITS ETF	0.36%	7.10%	10.24%	14.19%	3.63%	4.35%
MSCI Europe Small Cap Value Weighted Index	0.23%	7.03%	10.12%	14.42%	3.71%	4.48%
<b>Difference</b>	0.13%	0.06%	0.12%	-0.22%	-0.08%	-0.13%

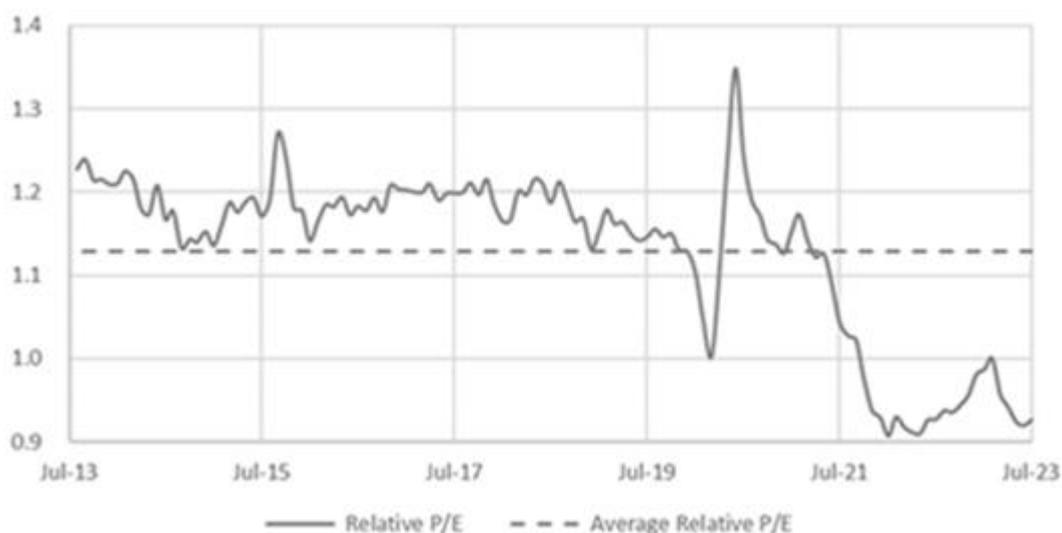
\*Inception date is 18 February 2015. Performance data as of 30 June 2023 in EUR. Other Datapoints as of 31 July 2023. Past performance is not a reliable indicator of future performance. Performance returns for periods of less than one year are not annualized. The performance figures contained herein are provided on a net of fees basis and reflect the deduction of advisory or other fees. The performance includes the reinvestment of dividends and other corporate earnings and is calculated in USD. Index returns are unmanaged and do not reflect the deduction of any fees or expenses. Index returns reflect all items of income, gain and loss and the reinvestment of dividends and other income as applicable. Visit [www.ssga.com](http://www.ssga.com) for most recent month-end performance.

### World Small Caps

The MSCI World Small Cap Index allows investors to gain a global developed and cyclical exposure, combining the specific merits of smaller companies across the US (60% of the index) and Europe (18%). The global index also provides access to Japan (11%), which is itself a cyclical economy<sup>(7)</sup>.

As the soft landing narrative is taking a stronghold among strategists, global small caps may also present an appealing opportunity given the relative P/E to MSCI World is 0.93x which resides in the bottom 10<sup>th</sup> percentile within a ten year range, while the performance potential remain since MSCI World Small Cap Index rallied only 9.6% year to date lagging the MSCI World Index by more than 6%<sup>(8)</sup>.

## MSCI World Small Cap Index 12m fwd P/E relative to MSCI World Index



Source: Bloomberg Finance L.P. as of 31 July 2023. P/E is Bloomberg BEST\_PE ratio.

## SPDR® MSCI World Small Cap UCITS ETF

<b>Fund Name</b>	SPDR® MSCI World Small Cap UCITS ETF
ISIN	IE00BCBJG560
Base Fund Currency	USD
Primary Ticker	ZPRS GY
Other Tickers	WOSC LN, WDSC LN, WOSC SE, WDSCN MM
Total Fund Assets (\$mn)	834
TER	0.45%
Index Name	MSCI World Small Cap Index

Annualised Net Performance	3M	YTD	1Y	3Y	5Y	Since Inception* (%)
SPDR® MSCI World Small Cap UCITS ETF	3.23%	7.74%	12.84%	10.35%	4.29%	6.47%
MSCI World Small Cap Index	3.22%	7.64%	12.94%	10.45%	4.44%	6.63%
<b>Difference</b>	0.02%	0.10%	-0.10%	-0.10%	-0.15%	-0.15%

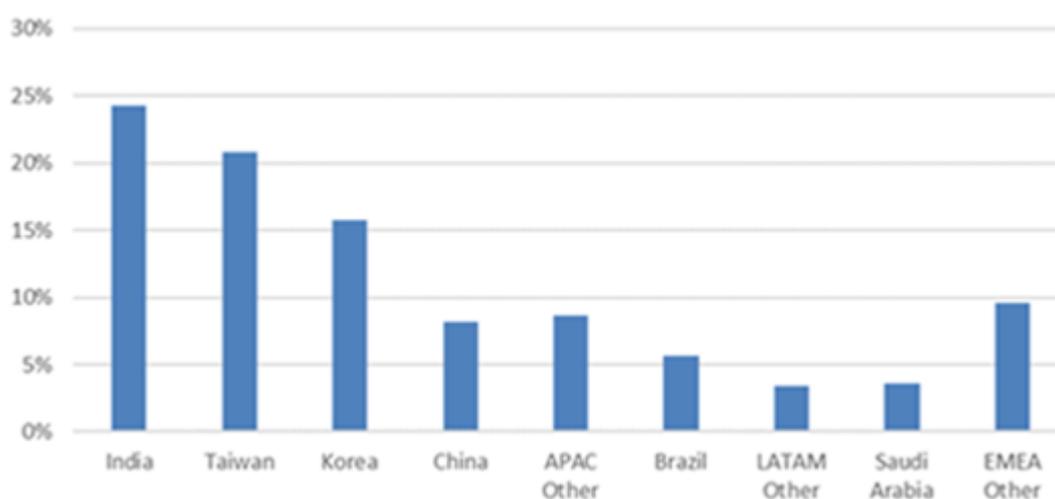
\*Inception date is 25 November 2013. Performance data as of 30 June 2023 in USD. Other Datapoints as of 31 July 2023. Past performance is not a reliable indicator of future performance. Performance returns for periods of less than one year are not annualized. The performance figures contained herein are provided on a net of fees basis and reflect the deduction of advisory or other fees. The performance includes the reinvestment of dividends and other corporate earnings and is calculated in USD. Index returns are unmanaged and do not reflect the deduction of any fees or expenses. Index returns reflect all items of income, gain and loss and the reinvestment of dividends and other income as applicable. Visit [www.ssga.com](http://www.ssga.com) for most recent month-end performance.

## Emerging Markets Small Caps

The MSCI Emerging Market Small Cap index allows to access growing economies of South-East Asia although with a more limited exposure to China. Indeed the

Middle Kingdom accounts only for 8% of the MSCI EM Small Cap index. While we remain constructive on EM large caps, investors who are more sceptical about prospects of the Chinese economy due to its slower than expected import and export data or issues related to its real estate sector may find that EM small caps could be an interesting alternative. The index is more exposed towards India (24%), one of the key engines of the global growth, as well as Taiwan (21%) and South Korea (16%)<sup>(9)</sup> with their technology heavy network of companies.

### MSCI Emerging Market Small Cap Index regional breakdown



Source: FactSet, State Street Global Advisors as of 31 July 2023.

### SPDR® MSCI Emerging Markets Small Cap UCITS ETF

Fund Name	SPDR® MSCI Emerging Markets Small Cap UCITS ETF
ISIN	IE00B48X4842
Base Fund Currency	USD
Primary Ticker	SPYX GY
Other Tickers	EMSM LN, EMSD LN, EMSDN MM
Total Fund Assets (\$mn)	240
TER	0.55%
Index Name	MSCI Emerging Markets Small Cap Index

Annualised Net Performance	3M	6M	1Y	3Y	5Y	10Y	Since Inception* (%)
SPDR® MSCI Emerging Markets Small Cap UCITS ETF	6.47%	10.65%	13.46%	13.48%	4.71%	4.48%	2.51%
MSCI Emerging Markets Small Cap Index	6.39%	10.50%	13.28%	13.73%	4.94%	4.63%	2.67%
<b>Difference</b>	0.08%	0.15%	0.18%	-0.25%	-0.23%	-0.15%	0.08%

\*Performance Inception date is 16 May 2011. Performance data as of 30 June 2023 in USD. Other Datapoints as of 31 July 2023. Past performance is not a reliable indicator of future performance. Performance returns for periods of less than one year are not annualized. The performance figures contained herein are provided on a net of fees basis and reflect the deduction of advisory or other fees. The performance includes the reinvestment of dividends and other corporate earnings and is calculated

in USD. Index returns are unmanaged and do not reflect the deduction of any fees or expenses. Index returns reflect all items of income, gain and loss and the reinvestment of dividends and other income as applicable. Visit [www.ssga.com](http://www.ssga.com) for most recent month-end performance.

<sup>1)</sup> Source: MSCI as of 31 July 2023.

<sup>(2)</sup> Source: Based on returns from 1 June 2023 to 10 August 2023 for S&P 500; S&P MidCap 400 Index and Russell 2000 Index.

<sup>(3)</sup> Source: FactSet, FTSE Russell. Revenue breakdown for S&P MidCap 400 Index calculated using index breakdown as of 30 June 2023 and revenue data available as of 18 July 2023. Russell 2000 Index revenue breakdown as of 30 June 2023 (source: FTSE Russell).

<sup>(4)</sup> Source: FTSE Russell as of 30 June 2023. Russell 2000 Index 1y forward positive P/E is 14x while the 10y average is 17x.

<sup>(5)</sup> Source: FactSet as of 31 July 2023. Availability of estimates for small cap companies may be limited.

<sup>(6)</sup> Source: FactSet. Revenue breakdown calculated using index breakdown as of 31 July 2023 and revenue data available as of 8 August 2023.

<sup>(7)</sup> Source: FactSet as of 31 July 2023.

<sup>(8)</sup> Source: Bloomberg Finance L.P. as of 10 August 2023. Valuation percentiles based on monthly time series of 12m forward Bloomberg BEST\_PE ratios as of 31 July 2023.

<sup>(9)</sup> Source: FactSet as of **31 July 2023**.

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