

Mid-cap growth stocks: a middle path to growth potential

Mid-cap companies can combine the beneficial features of larger companies—financial stability, sustainable business models, adaptability—with those of smaller companies—growth potential, niche markets and nimble management. Based on current valuations, historical relative returns and index composition, this may be a favorable time to consider an allocation to mid-cap growth stocks.

Favorable entry point

The valuation gap between the Russell Midcap® Growth Index and the Russell Top 200® Growth Index recently reached a level last observed in late 2001 (Exhibit 1). While that gap has narrowed, valuations still present a favorable potential entry point.

Exhibit 1: Ratio of Russell Midcap® Growth Index vs. Russell Top 200® Growth Index forward P/Es

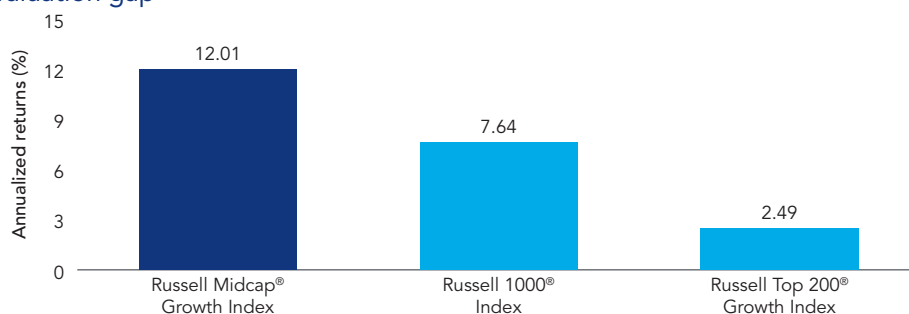


As of 03/31/24. Sources: FactSet, Federated Hermes. This is for illustrative purposes only and is not indicative of any specific investment. Monthly data from 12/31/99 to 03/31/24.

The Russell Midcap® Growth Index outperformed the Russell Top 200® Growth Index by over 9% annualized from October 1, 2001 to September 30, 2006. (Exhibit 2).

Investors in a large-cap growth style that are concerned about valuation or simply a reversion to mean, but still favor growth, may want to consider a tilt toward mid-cap growth stocks given current valuation levels.

Exhibit 2: Five-year index returns following 2001 low in mid-cap/large-cap valuation gap



As of 9/30/06. Sources: FTSE Russell; Federated Hermes. Graph shows five-year returns beginning 10/1/01, when P/E levels were last near current levels.

Past performance is no guarantee of future results.

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Portfolio diversification with reduced technology exposure

A key distinction between the Russell Midcap® Growth Index and the Russell Top 200® Growth and Russell 1000® Growth indexes is the exposure to technology stocks. Some investors may not be aware of the relatively high sector concentration that exists in the large cap growth market segments. This high technology weighting may create performance volatility when market leadership rotates away from tech stocks. Mid-cap growth stocks provide an opportunity to participate in an expanding economy without the higher potential volatility associated with a greater concentration in the technology sector.

Exhibit 3: Index technology sector weights

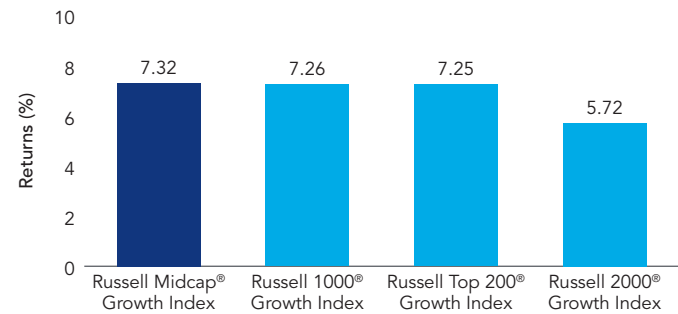
Index	Technology weighting (%)
Russell Midcap® Growth Index	23.4
Russell Top 200® Growth Index	57.6
Russell 1000® Growth Index	53.2

As of 3/31/24. Source: FTSE Russell.

Competitive returns and strong earnings

Large-cap growth companies have dominated market returns of late, but mid-cap growth stocks have demonstrated competitive returns and strong earnings growth over the long run. Mid-cap growth stocks have demonstrated high earnings growth, considered a driver of long-term returns.

Exhibit 4: Competitive long-term returns—annualized returns (%) 1/1/00-3/31/24



As of 3/31/24. Sources: FTSE Russell; Federated Hermes.

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Exhibit 5: High earnings growth

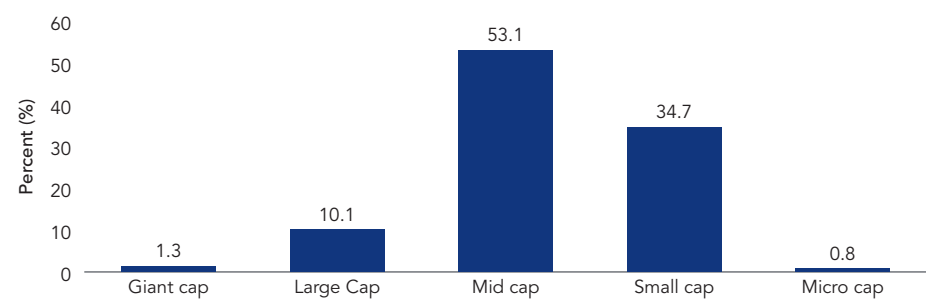
Index	5-year historical EPS growth rate (average)
Russell Midcap® Growth Index	20.23
Russell 1000® Growth Index	19.08
Russell Top 200® Growth Index	19.25
Russell 2000® Growth Index	20.17
S&P 500®	16.30

As of 3/31/24. Sources: Federated Hermes, Factset.

Large pool of stocks + no standard definition = potential market inefficiency

Index providers have clear rules as to how to classify stocks within a particular index, but active fund managers are not obliged to follow those same rules. Managers seeking to outperform their benchmark may look outside the benchmark universe for ideas, which can lead to size or style drift in the portfolio relative to benchmark. A Morningstar analysis of all mid cap funds (Exhibit 6) indicates that many are not pure mid cap funds, and instead also invest in large- and small-cap companies. Choosing a pure mid-cap manager that won't overlap with other strategies may be a challenge. But a mid-cap strategy that adheres to style parameters can help diversify an overall equity portfolio.

Exhibit 6: Morningstar 5-year Mid-Cap Fund category—average fund capitalization breakdown



Sources: Morningstar, Federated Hermes; as of 3/31/24

All Morningstar mid-cap funds: mid-cap blend, mid-cap growth, mid-cap value (not including ETFs & index funds). Capitalization breakdowns follow Morningstar's methodology which evolves over time: Giant: +277,728m; Large: \$53,823m to \$277,728m; Mid: \$2,509m to \$9,754m; Small: \$2,509m to \$9,754m; Micro: Less than \$2,509m.

Definitions

Earnings per share (EPS) is the net income (profit) per share of common stock earned by a company.

Forward price-to-earnings ratio (P/E) is calculated by dividing stock price by an average of 1-year forward earnings estimates for that stock.

Standard deviation is measure of volatility. More formally defined, a statistical measurement of dispersion about an average, which depicts how widely an investment's returns varied over a certain period.

Russell 1000® Index measures the performance of the large-cap segment of the U.S. equity universe. It includes approximately 1,000 largest U.S. stocks, representing 93% of investable U.S. equities by market capitalization. The index comprises the Russell Top 200® and the Russell Midcap® Indexes.

Russell 1000® Growth Index: Measures the performance of the large-cap growth segment of the U.S. equity universe. A subset of the Russell 1000® Index, it includes companies with higher price-to-book ratios and higher forecasted growth values. The Russell 1000® Growth Index is constructed to provide a comprehensive and unbiased barometer for the large-cap growth segment.

Russell Midcap® Growth Index is a subset of the Russell 1000® Growth Index. It includes approximately 300+ securities based on a combination of their market cap and growth characteristics.

Russell Top 200® Growth Index measures the performance of the 200 largest companies in the Russell 1000® Index.

S&P 500® Index: Is an unmanaged capitalization-weighted index of 500 stocks designed to measure performance of the broad domestic economy through changes in the aggregate market value of 500 stocks representing all major industries.

Indexes are unmanaged, have no expenses, and cannot be invested in directly.

A word about risk

Mutual funds are subject to risks and fluctuate in value.

Mid-capitalization companies often have narrower markets and limited managerial and financial resources compared to larger and more established companies.

Due to their relatively high valuations, growth stocks are typically more volatile than value stocks.

Diversification does not assure a profit nor protect against loss.

Investors should carefully consider a fund's investment objectives, risks, charges and expenses before investing. To obtain a summary prospectus or prospectus containing this and other information, contact us or visit FederatedHermes.com/us. Please carefully read the summary prospectus or the prospectus before investing.

Morningstar Category identifies funds based on their actual investment styles as measured by their underlying portfolio holdings over the past three years. If the fund is less than three years old, the category is based on the life of the fund. ©2024 Morningstar, Inc. All Rights Reserved. The information contained herein: (1) is proprietary to Morningstar; (2) may not be copied or distributed; and (3) is not warranted to be accurate, complete or timely. Neither Morningstar nor its content providers are responsible for any damages or losses arising from any use of this information.

Past performance is no guarantee of future results.