

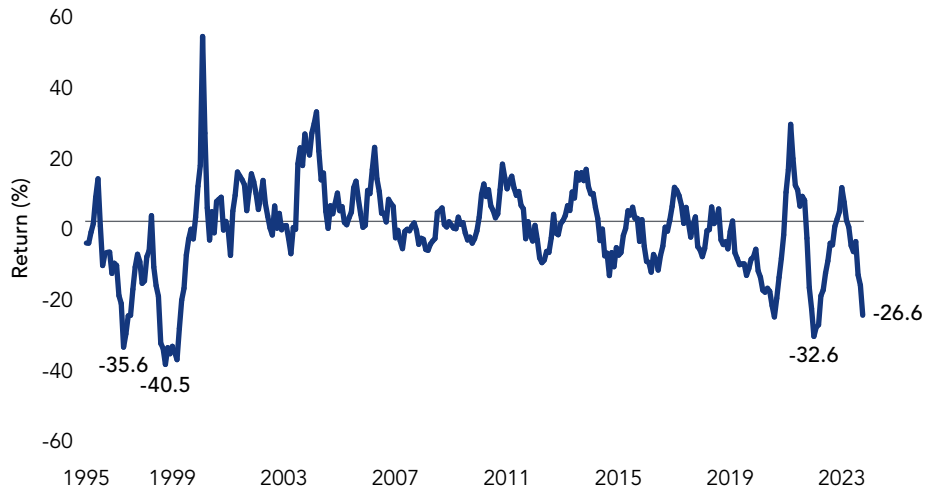
# Is a big opportunity in small cap growth approaching?

- Small caps have outperformed large caps over the long term<sup>1</sup>
- Recent small cap growth underperformance relative to large appears likely near a bottom
- We believe small cap growth should perform well in a recovery

## Small cap growth offers a potentially historic opportunity vs. large

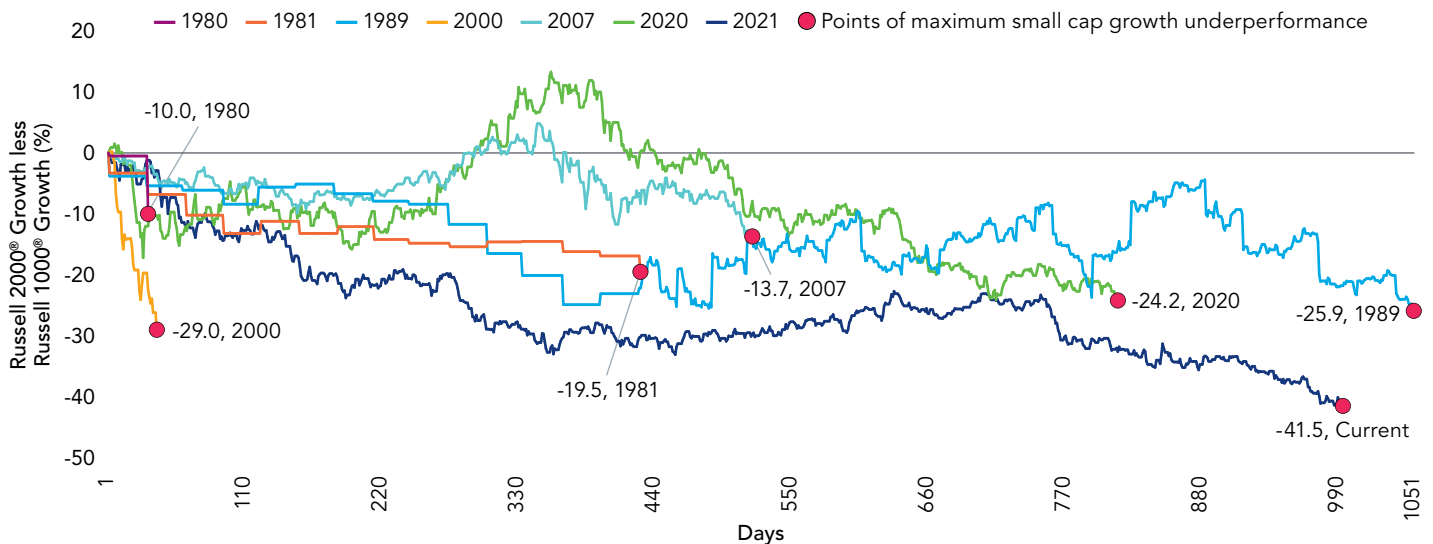
- Relative performance vs. large caps is near record lows. History suggests this trend could reverse
- When looking at peak-to-trough returns, including periods near recessions, recent small cap growth performance relative to large cap growth is the lowest since before 1980, as shown below

**Russell 2000® Growth Index - Russell 1000® Growth Index relative 12-month return**



As of 10/31/23. Sources: Russell, Federated Hermes analysis. **Past performance is not indicative of future results.**

## Peak-to-trough relative returns around past recessions, Russell 2000® Growth vs. Russell 1000® Growth



As of 10/31/23. Peak points are marked at zero months and begin the last day of small cap growth peaks around past recessions. Trough points are points of maximum small cap growth underperformance vs. large following the peak. Graph shows the relative return trajectory from peak to trough. Peak-to-trough dates are: 2/28/80 to 3/31/80, 6/29/81 to 8/31/82, 10/30/89 to 9/14/92, 3/9/00 to 4/17/00, 10/10/07 to 3/11/09, 2/19/20 to 5/11/22 and 2/9/21 to 10/30/23. Sources: Russell, Federated Hermes analysis. **Past performance is not indicative of future results.**

**The above charts are for illustrative purposes only and not representative of any specific investment.**

Not FDIC Insured • May Lose Value • No Bank Guarantee

- A wide dispersion in returns has some promising securities currently trading at beaten-down prices
  - › 42% of Russell 2000® Growth stocks are down year-to-date (YTD); 56% are down since 1/1/22<sup>2</sup>
  - › 30% of small caps are trading below their book value, the most since 2009 and second most since before 2000<sup>3</sup>
- We believe current conditions present attractive opportunities for our experienced teams

**Small cap growth stocks by decile of performance - YTD**

	Average return
Highest	101.0
2nd	40.0
3rd	22.1
4th	8.3
5th	-2.4
6th	-12.0
7th	-21.0
8th	-30.8
9th	-44.0
Lowest	-67.5
<b>Average</b>	<b>-0.7</b>

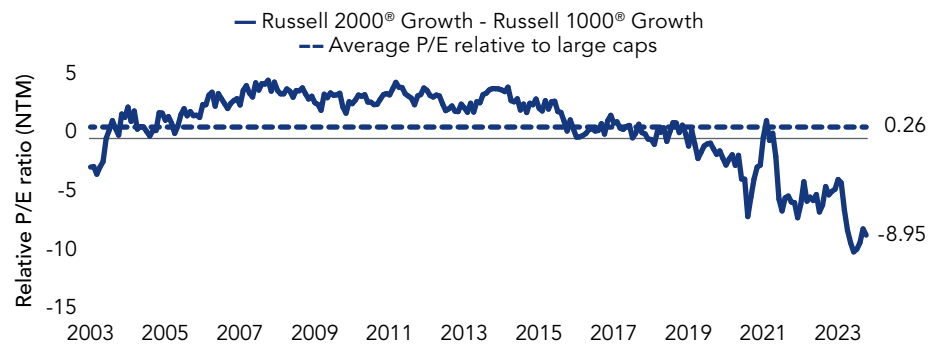
**Small cap growth stocks by decile of performance - since 1/1/22**

	Average return
Highest	123.1
2nd	25.3
3rd	4.8
4th	-9.3
5th	-22.3
6th	-33.9
7th	-45.8
8th	-57.2
9th	-70.2
Lowest	-84.7
<b>Average</b>	<b>-17.3</b>

As of 10/31/23. Sources: Russell, Federated Hermes analysis. **Past performance is not indicative of future results.**

- A return to normal, average P/E levels vs. large caps could increase small cap growth prices
- On an absolute basis, Russell 2000® Growth P/E next twelve months (NTM) was 17.01 at 10/31/23, 14% below its 19.82 average since 2003

**Small cap growth relative price/earnings ratio (NTM)**

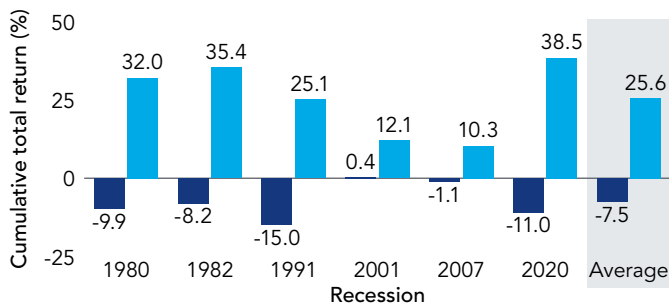


As of 10/31/23. Sources: Russell, Federated Hermes analysis.

**Most of the bad news may already be priced in, leaving attractive upside potential from here through a recovery**

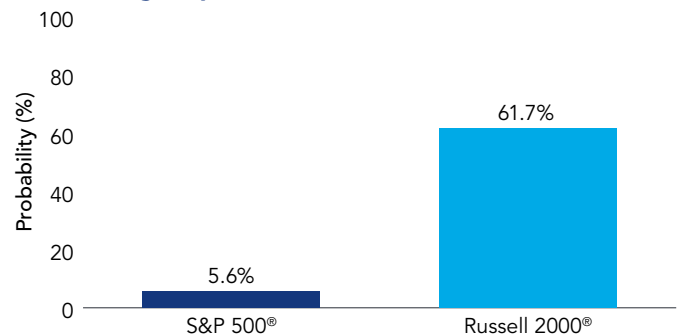
**Small cap vs. large cap relative returns during and after recessions**

- Russell 2000® underperformance from S&P 500® peak to trough
- Outperformance one year later



As of 11/30/23. Sources: S&P, Russell, Federated Hermes analysis. Dark blue bars show Russell 2000® minus S&P 500® return during peak to trough performance of S&P 500® around past National Bureau of Economic Research recessions. Light blue bars show the relative return from the trough over the next 12 months. **Past performance is not indicative of future results.**

**Probability of a U.S. recession as currently priced across small and large caps**



As of 11/30/23. Sources: S&P, Russell, Federated Hermes analysis. To calculate the probability, we divided the indexes' current drawdowns from their most recent peaks, by their average max drawdowns around the last 6 recessions.

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# Is a big opportunity in small cap growth approaching?

## Portfolio Constructions Solutions insight

Our PCS team analyzes hundreds of financial professional's portfolios each year. As a result, the team has a deep understanding of the typical allocations and intended exposures within portfolios.

- In 3Q23, the average equity portfolio reviewed by our PCS team contained a 9.9% allocation to small caps. Of these portfolios, 78% obtained small cap exposure through at least one dedicated small cap fund (and on average, 1.5 funds).
- In portfolios that held a fund within the Morningstar Small Growth category, the average allocation was 4.7% of the overall equity allocation.
- From 2Q to 3Q, the average percent allocated to large cap growth increased, and the average allocation to small cap growth was unchanged.

## Portfolio implementation considerations

- We believe small cap growth should perform well in a post-recession market environment, as it has in the past. Small caps could also benefit when/if the Federal Reserve transitions to cutting rates
- While there may be downside risk, history suggests that the reward-to-risk ratio may be tilted disproportionately to the upside, particularly relative to large cap growth
- We believe now may be a good time to review exposures to growth stocks, and consider increasing small cap growth allocations

## Discover Federated Hermes U.S. small cap growth funds

Call [1-888-400-7838](tel:1-888-400-7838) to learn more

Views are as of 12/6/23 and are subject to change based on market conditions and other factors.

<sup>1</sup> Sources: Fama French, Federated Hermes analysis. Fama French Small Neutral Portfolio annualized total return 1970 to 2022: 15.07%; Large Neutral: 12.18%.

<sup>2</sup> Sources: Russell, Federated Hermes analysis of Russell 2000® Growth constituents.

<sup>3</sup> Bloomberg Finance L.P., J.P. Morgan. Based on U.S. and Canadian small caps.

The information and data contained herein are provided solely for informational purposes. Accordingly, this communication does not represent specific investment advice and should not be construed as an investment recommendation.

Although the information provided in this document has been obtained from sources which Federated Hermes believes to be reliable, it does not guarantee accuracy of such information and such information may be incomplete or condensed.

There is no guarantee that any specific investment approach will be successful.

**Fama French equity style portfolios** are formed on size and book-to-market value and include NYSE, AMEX, and NASDAQ stocks for which market equity data and (positive) book equity data for exists. The portfolios, which are constructed at the end of each June, are the intersections of 2 portfolios formed on size (market equity, ME) and 3 portfolios formed on the ratio of book equity to market equity (BE/ME). The size breakpoint for year t is the median NYSE market equity at the end of June of year t. BE/ME for June of year t is the book equity for the last fiscal year end in t-1 divided by ME for December of t-1. The BE/ME breakpoints are the 30th and 70th NYSE percentiles. Fama French "Neutral" or core portfolios contain both value and growth stocks.

**Price-to-earnings ratio (P/E ratio)** is a valuation ratio of a company's current share price compared to its per-share earnings. The P/E ratio helps investors determine the market value of a stock as compared to the company's earnings. A low P/E ratio might indicate that a stock that has the potential for significant growth is undervalued. P/E ratios are only one indicator of a company's financial well-being.

**Russell 1000® Growth Index** measures the performance of the large-cap growth segment of the U.S. equity universe. It includes those Russell 1000® Index 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.

The Index is completely reconstituted annually to ensure new and growing equities are included and that the represented companies continue to reflect growth characteristics.

**Russell 2000® Growth Index** measures the performance of the small-cap growth segment of the U.S. equity universe. It includes those Russell 2000® Index companies with higher price-to-value ratios and higher forecasted growth values. The Russell 2000® Growth Index is constructed to provide a comprehensive and unbiased barometer for the small-cap growth segment. The index is completely reconstituted annually to ensure larger stocks do not distort the performance and characteristics of the true small-cap opportunity set and that the represented companies continue to reflect growth characteristics.

**S&P 500®** 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 and cannot be invested in directly.

### Risk considerations

Mutual funds are subject to risks and fluctuate in value.

International investing involves special risks, including currency risk, increased volatility, political risks and differences in auditing and other financial standards.

Investing in IPOs involves special risks such as limited liquidity and increased volatility.

Small-cap companies may have less liquid stock, a more volatile share price, unproven track records, a limited product or service base and limited access to capital. The above factors could make small-cap companies more likely to fail than larger companies and increase the volatility of the fund's portfolio, performance and share price. Suitable securities of small-cap companies also can have limited availability and cause capacity constraints on investment strategies for funds that invest in them.

**Past performance is no guarantee of future results.**

**Investors should carefully consider the 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](https://FederatedHermes.com/us). Please carefully read the summary prospectus or the prospectus before investing.**