

# SMALL CAP VALUE

## MARKET COMMENTARY

US small cap company stocks roared in the aftermath of the US Presidential elections as investors focused on the benefits of de-regulation, lower US corporate taxes, re-shoring of supply chains to the US, and a general sense that the US economy was set for accelerating growth. In the first quarter of 2025, the mood has darkened. The prospect of tariffs and the potential for near-term pain, persistently high inflation, and weakening macroeconomic factors have shifted investor sentiment from optimism to concern about a potential recession. Given this backdrop, the Russell 2000 Index declined -9.5% in the first quarter of 2025 while its value counterpart was down less (-7.7%).

The small cap market is down -17% from its post-election high, which suggests investors are already factoring in a good portion of the impact of a typical recession. The sell off was widespread as most non-defensive sectors clocked double digit declines. As a bottom-up manager we search for investment ideas with a bias toward owning good companies with strong balance sheets and attractive valuations. In this environment, that will likely lead us to companies where investors have the greatest concerns about the economy. That said, the valuation of the Russell 2000 Index is in line with its history which suggests small cap stocks could get cheaper from this level.

Ben Graham referred to the stock market as a voting machine in the short-term and weighing machine in the long-term. Eventually stock prices begin to reflect the underlying businesses' fundamentals. The stock market favorites of recent years are likely to reflect more realistic projections rather than be priced for perfection. Conversely, shunned companies operating in very good though perhaps less captivating businesses, are likely to be better appreciated for their true earnings power. Put another way, fundamentals should drive the market. We believe such an environment, which could already be underway, would be very conducive to our investment approach.

## ATTRIBUTION ANALYSIS – 1Q25

The Small Cap Value portfolio outperformed the Russell 2000 Value Index in the first quarter of 2025 (gross and net of management fees). Stock selection in technology was the largest positive contributor in the quarter. Stock selection was also positive in energy, financials, healthcare, and industrials. The underweight position in healthcare also contributed positively. Conversely, stock selection in materials and consumer discretionary detracted in the quarter. The overweight in technology also detracted, as did the underweight positions in financials, real estate, and utilities.

As of 3/31/25, net of fee composite and Russell 2000 Value performance for 1-, 5-, and 10-year periods: -6.62%, 22.68%, 7.01% and -3.12%, 15.31%, 6.07%, respectively. Net performance results are presented after management fees and all trading expenses but before custodial fees; the composite includes all Small Cap Value discretionary accounts. Additional disclosures provided in Endnotes.

Past performance is no guarantee of future results.



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**Endnotes:**

All investments contain risk and may lose value. This commentary is for general information only and should not be relied on for investment advice or recommendation of any particular security, strategy, or investment product.

Portfolio characteristics and attribution are based on a representative Small Cap Value portfolio. Attribution is an analysis of the portfolio's return relative to the index, is calculated using daily holdings information and does not reflect management fees and other transaction costs and expenses; interaction effect is combined with stock selection. Returns can differ from certain client portfolio(s) due to data differences, cash flows, trading, and other activity (data source: Bloomberg, Russell).

The value discipline used in managing accounts in the Small Cap Value strategy may prevent or limit investment in major stocks in the Russell 2000 Value and returns may not be correlated to the index. Composite performance is available at [www.hwcm.com](http://www.hwcm.com), located on the strategy's Performance tab along with important disclosures included in the strategy's [GIPS Report](#); quarterly characteristics and portfolio holdings are located on the Portfolio and Literature tabs. For a list showing every holding's contribution to the overall account's performance and portfolio activity for a given time period, contact H&W at [hotchkisandwiley@hwcm.com](mailto:hotchkisandwiley@hwcm.com). Portfolio information is subject to the firm's portfolio holdings disclosure policy.

The Russell 2000® Index measures the performance of the 2,000 smallest companies in the Russell 3000® Index. The Russell 2000® Value Index measures the performance of those Russell 2000® companies with lower price-to-book ratios and lower forecasted growth values. The Russell 2000® Growth Index measures the performance of those Russell 2000® Index companies with higher price-to-book ratios and higher forecasted growth values. Any indices and other financial benchmarks shown are provided for illustrative purposes only, are unmanaged, reflect reinvestment of income and dividends and do not reflect the impact of advisory fees. It is not possible to invest directly in an index.

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Equity securities may have greater risks and price volatility than U.S. Treasuries and bonds, where the price of these securities may decline due to various company, industry and market factors. Investing in smaller and/or newer companies involves greater risks than those associated with investing in larger companies, such as business risk, significant stock price fluctuations and illiquidity. Investment risk disclosures for the firm's strategies are described in Part 2A of Form ADV of H&W.

A value-oriented investment approach involves the risk that value stocks may remain undervalued or may not appreciate in value as anticipated. Value stocks can perform differently from the market as a whole or from other types of stocks and may be out of favor with investors and underperform growth stocks for varying periods of time.

Information contained in this material may represent or be based on forward-looking statements. Due to various risks and uncertainties, actual events/results or performance of the strategy may differ materially from those reflected or contemplated in such forward-looking statements. Information based on forecasts, proprietary or third-party estimates cannot be guaranteed and are subject to change. Information obtained from independent sources is considered reliable, but H&W cannot guarantee its accuracy or completeness.

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