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Where Are We in the Small-Cap Cycle?

Please refer to important disclosures on pages 14 and 15. Analyst certification is on page 14.

Investors pay so much attention to the macroeconomic picture because they know that financial market returns are ultimately driven by corporate profits. Those profits, in turn, are inherently linked to nominal GDP growth, which itself moves in cycles (both longer-term secular changes and shorter-term cyclical shifts). Investors also know that changes in these cycles are often synonymous with significant rotations in investing style across asset classes, which for the equity market include both sector and size. Hence, gauging the relative performance of smaller caps to larger-cap stocks is often a good barometer of where we are (or at least where the market thinks we are) in the economic cycle. **In this *Economics Weekly*, we take another look at small caps and their relationship with the economic cycle, and why this currently unloved area of the market should be piquing the interest of investors.**

Small Caps and the Economic Cycle

History shows that smaller-cap stocks tend to be significantly more volatile than larger-cap stocks, but also over time generate higher returns to compensate. This volatility is down to the fact that smaller-cap stocks are less widely covered by Wall Street research analysts, are often younger and less established, and have less-experienced management teams, which tend to create greater opportunities for positive and negative surprises. They also tend to be more highly correlated to the domestic economic cycle relative to the larger-cap stocks, which normally have more diverse revenue streams in terms of both products and geography.

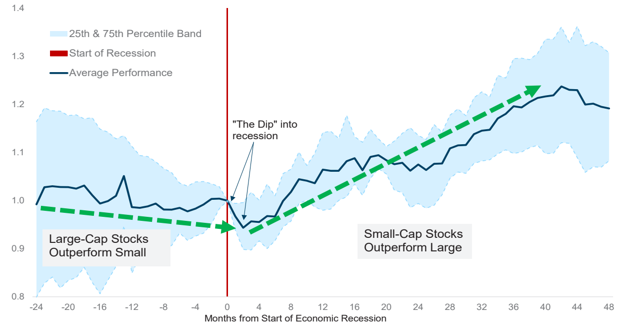
Importantly, smaller caps are far more sensitive to the credit cycle. This is not only because they are more highly leveraged than the large caps, which may have moved out of their growth phase, but small-cap stocks also tend have less access to credit compared to the large-cap stocks that can more easily tap capital markets, bank loans, private capital, and various lines of credit at any one point in time.

Because of this greater economic and credit sensitivity, smaller caps can generally be viewed as the speedboats of the equity world, compared to the larger-cap supertankers. Smaller caps tend to feel the first impulses of a new credit cycle as well as the drag when interest rates start to increase and financial conditions tighten. For large caps, it takes much longer to feel these effects and then respond.

This highly cyclical behavior is highlighted in exhibits 1 and 2, which show a steady underperformance of smaller-cap stocks in the later stages of the economic cycle as domestic growth opportunities fade and interest rates start to rise. Performance is then normally followed by an even sharper contraction in relative growth just as the recession gets underway. They then start to sharply outperform from very early on in the recession and continue to do so for the following three to four years.

Exhibit 1.

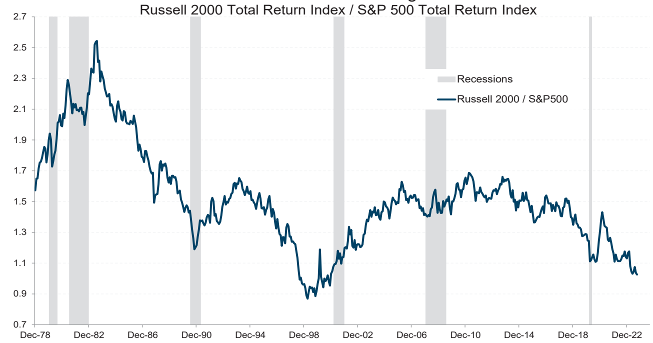
Relative Performance of Russell 2000 vs S&P 500 Index Around Recessions
(Average Relative Performance for Last 6 Recessions Starting From 1980 to 2023, Indices Rebased to 100 at Start of Recession)



Sources: Bloomberg, NBER, William Blair Equity Research

Exhibit 2

Small Stocks vs Large
Russell 2000 Total Return Index / S&P 500 Total Return Index



Sources: Bloomberg, S&P, William Blair Equity Research

Recent Performance—Struggling for Traction

The last time we wrote about smaller caps was in July 2022 ([Economics Weekly: Time to Start Looking at Small Caps Again?]). As exhibit 3 shows, this coincided with the start of a strong outperformance for the smaller-cap stocks up to March 2023, before it came to an abrupt halt due to: 1) the surge in interest in a small handful of AI-related stocks, and 2) the collapse of Silicon Valley Bank.

Exhibit 3.

Relative Performance Russell 2000 versus S&P 500

Sources: Bloomberg, William Blair Equity Research

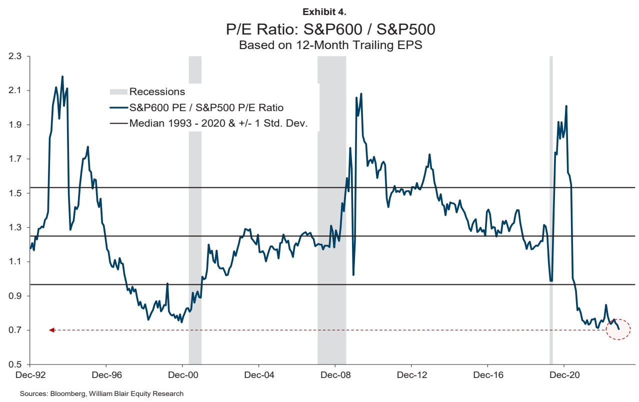
As these banking issues were settled, another mini-rally ensued through June and July, before then giving way to another shift in sentiment. At this point, investors collectively lowered their expectations for a hard landing and increased their expectations that the Fed might achieve its ultimate goal of lowering inflation without causing a recession—the so-called "immaculate disinflation"—but at the cost of continued tighter financial conditions or higher interest rates for longer.

Today, we are at a point where the market no longer views a recession as being imminent. It feels interest rates, or credit conditions more generally, are not about to ease anytime soon. In such an environment, it is normally better to tilt toward larger-cap stocks than the smaller caps. There is perhaps also a sense that from a timing perspective there is no great hurry to slide down the market cap scale given "the dip," which often takes place at the start of most recessions (depicted in exhibit 1).

Why It Is Still Worth Taking a Look at Smaller Caps Today

To the extent that valuation still matters—which we strongly feel is still the case, despite the proliferation of valuation-agnostic passive investment—the small-cap narrative is particularly attractive.

Exhibit 4, for example, shows that on a relative P/E basis over the last three decades small caps have never been as inexpensive as they are now. Furthermore, a comparison of this relative P/E with the relative performance of the smaller caps over the following three years (the best fit, with r = -47%) suggests that current valuations should be consistent with strong outperformance in the coming years (exhibit 5).



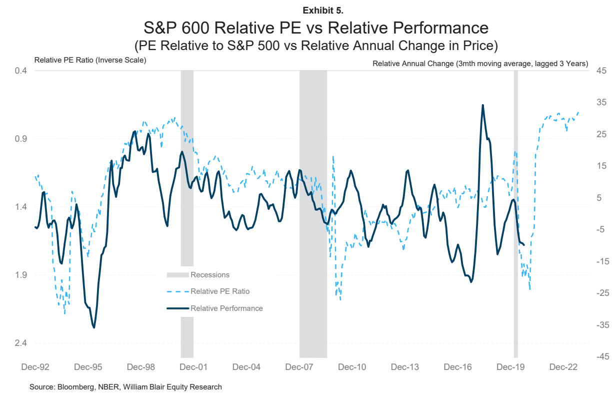
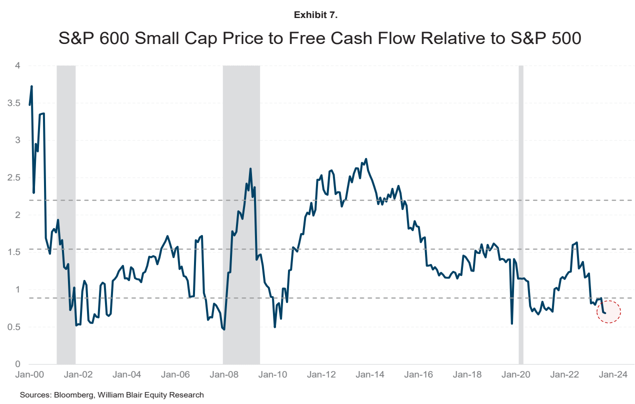
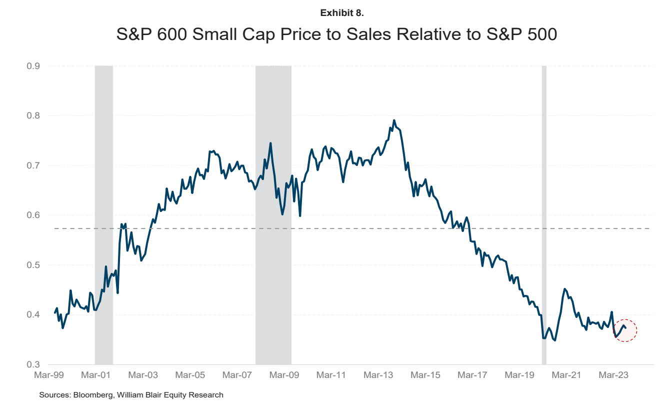
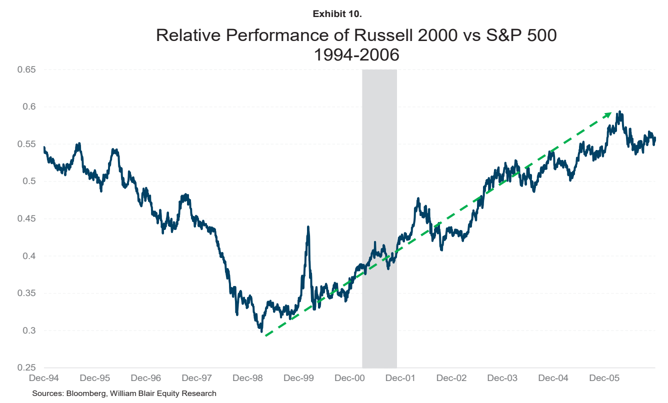


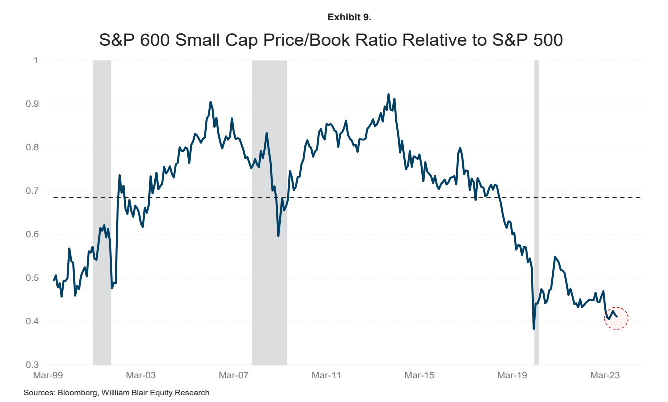
Exhibit 6 shows that even on an absolute basis, they have only ever been less expensive in the midst of the GFC in 2009. Similarly, the current forward P/E for the S&P 600 is 12.8 versus 18.0 for the S&P 500. As the question of negative earnings pops up frequently, it is worth noting that the S&P P/E *includes* negative earnings. The P/E ratio is taken as total market cap/total earnings (with appropriate divisors), where total earnings is the sum of all company earnings both positive and negative.

The more attractive relative valuations can similarly be seen across various other metrics, as shown in exhibits 7-9.









Late 1990s as a Historical Parallel?

While no two periods perfectly match, it is worth examining what happened around a previous period that shares some similarities with today. During the late 1990s, the market breadth had similarly thinned to only a handful of tech-heavy stocks driving the market on the back of an innovation boom with the internet.

Back then, and importantly despite still being late in the economic expansion (i.e., not yet having the catalyst of an economic recession), the smaller-cap stocks began to steadily outperform in a rotation that didn't blink during the internet bubble burst nor at the onset of the economic recession. That smaller-cap outperformance ultimately continued until April 2006, before yet again late-cycle dynamics came back into play (exhibit 10).

We attribute this cyclically inconsistent outperformance to three factors. The first is that valuations, like today, were exceptionally inexpensive, which meant that for many investors the margin of safety (or the price relative to the intrinsic value) for investing in many of these names was extremely high. This increasingly enticed many investors to start to nibble away at these stocks, despite rising interest rates and widening credit spreads.

The second factor to help support a pre-recession bottoming and outperformance of the smaller caps was that the ongoing sharp increases in the price of many of those larger-cap internet stocks were increasingly blowing out portfolio-weighting restrictions. This forced money managers to diversify those excess funds into other areas of the market, including the attractively valued smaller-cap stocks.

Lastly, the consumer was also heading into the 2001 recession in relatively good shape. This meant that unlike the GFC, for example, consumer spending remained solid and ultimately the 2001 recession turned out to be a relatively mild downturn by historical standards. Back then, and again similar to today, the unemployment rate was as low as 3.8% in 2000; and while it eventually rose to 6.3% by 2003, this would still be classified as a below-average increase by recessionary standards.

The Hurdles

Perhaps the biggest structural impediment to a recovery in the small-cap sector is the global power that the largest-cap stocks seem to wield these days. Many industries have become oligopolized, driven by globalization, brand power, huge network effects, political influence, and perhaps most importantly, very deep and wide technology moats, making it extremely difficult for smaller upstarts to compete.

Private markets are also much bigger players in financial markets than they have ever been previously. One reason cited for the steady de-rating of the smaller-cap stocks has been the possibility that they have already been heavily picked over and taken private by these players—leaving only the underperformers to the public markets.

Lastly, due to their greater interest rate sensitivity, investors are concerned that if interest rates stay higher for longer and/or there is no recession, smaller-cap stocks will not feel much of the bounce that they might normally get in the early stages of a recession, when the Fed starts to aggressively cut rates.

While these are all very real concerns, they are also not new. The sharp rise in rates has increased the risk of "breaking something" and suggests investors should focus on the highest-quality areas of this spectrum; however, the extreme de-rating in valuations that has taken place over the last few years would also suggest that many of these fears may already have been discounted in the price.

Conclusion

History shows that smaller-cap stocks are much more closely tied to the domestic economic cycle than larger-cap stocks. As a result, economic recessions have often represented exceptional buying opportunities for these equities once the cathartic final "dip" at the start of most recessions is out of the way.

The fact that the economy today is still not in recession is making investors wary that either it continues to expand, limiting the potential for any expected future rate cuts, or that higher rates will eventually "break something" and drag down the more volatile smaller-cap stocks with it. Adding to these woes is the sheer dominance and market power of many of the largest-cap stocks today, as well as the introduction of private equity as a major player in the smaller-cap space, which may have already squeezed the market for these stocks. In short, it is not hard to see why investors have shunned smaller caps.

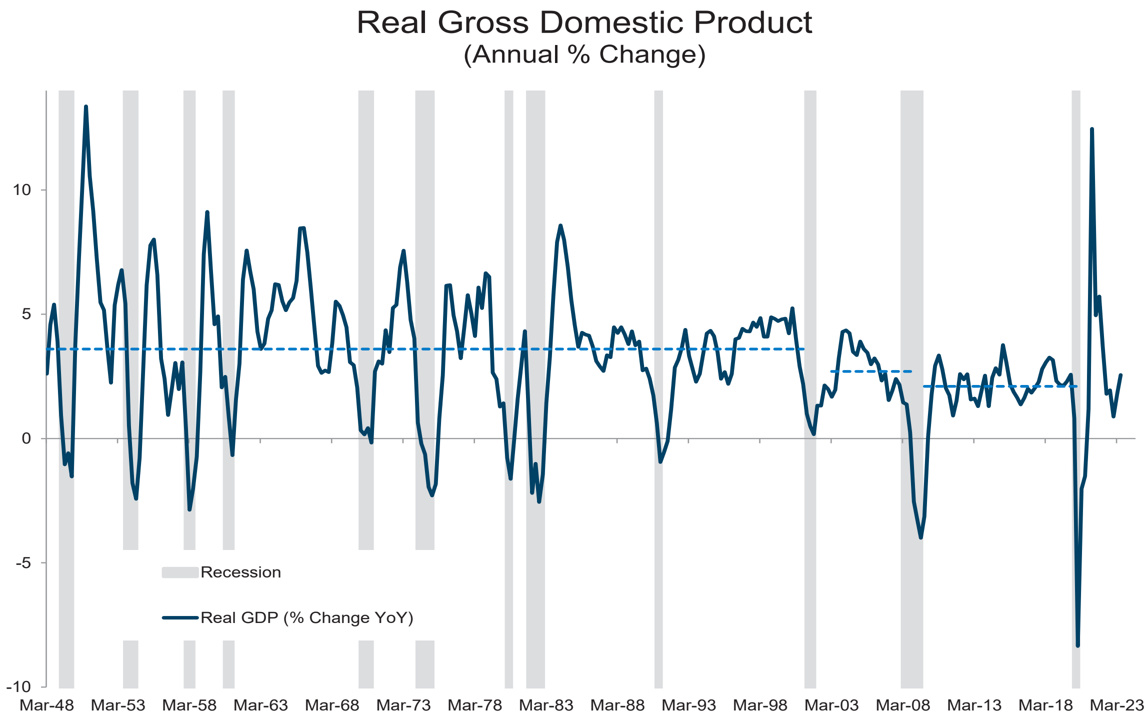
Nevertheless, while neither the economic cycle nor the expected rate environment would seem to currently support a small-cap rotation, there are similar parallels between the start of the 1998-2006 small-cap cycle and today. Only today, there is at least a strong probability that interest rates have already peaked, while valuations are even more attractively priced across just about all available metrics. This would suggest that many of the fears investors have been harboring about smaller-cap stocks have already been priced in, helping to provide a wider margin of safety and interesting opportunity for more valuation-conscious investors at the higher-quality end of this market.

Highlights in the Week Ahead

Date	Time (EDT)	Indicator	Last	Consensus	WB Estimate	Actual
25 Oct	10:00 a.m.	New Home Sales (Sep)	-8.7%	1.3%	0.6%	
26 Oct	8:30 a.m.	GDP (Q3 Advance)	2.1%	4.0%	4.5%	
26 Oct	8:30 a.m.	Durable Goods Orders (Sep)	0.1%	1.0%	1.4%	
		Orders Less-transportation	0.4%	0.3%	0.5%	
27 Oct	8:30 a.m.	Personal Income (Sep)	0.4%	0.4%	0.4%	
		Personal Spending	0.4%	0.4%	0.4%	

Sources: Bloomberg, William Blair Equity Research

Indicator of the Week: Third-Quarter GDP



Source: Bureau of Economic Analysis, William Blair Equity Research

Economic Scorecard

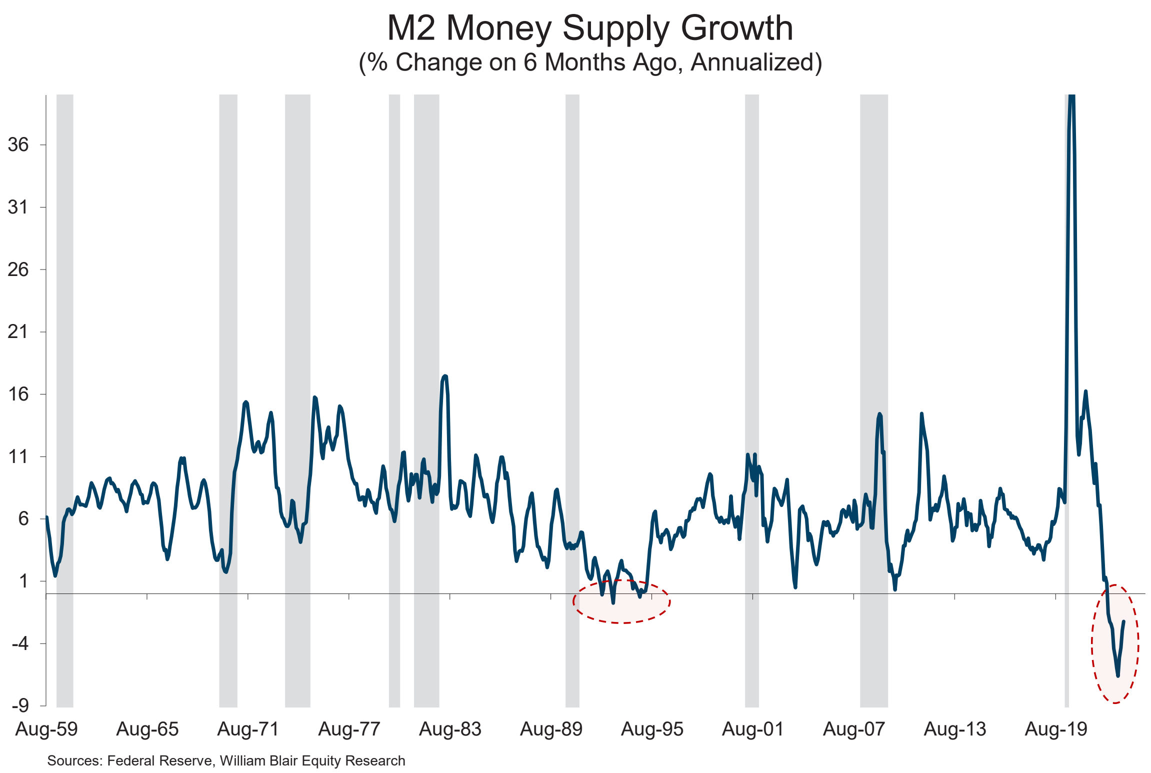
Rolling monthly heat map, % Change on Year Ago (unless otherwise noted)

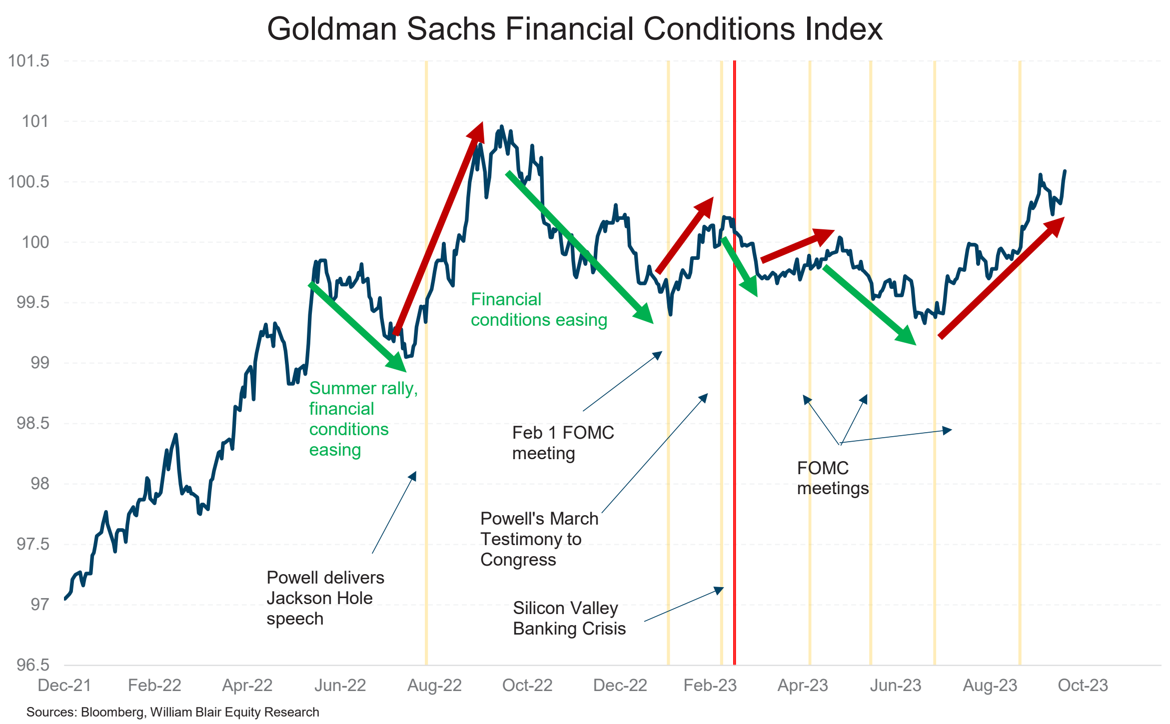
	Apr-22	May-22	Jun-22	Jul-22	Aug-22	Sep-22	Oct-22	Nov-22	Dec-22	Jan-23	Feb-23	Mar-23	Apr-23	May-23	Jun-23	Jul-23	Aug-23	Sep-23	Oct-23
Growth																			
US Leading Indicators	4.4	2.8	1.3	-0.3	-1.1	-1.6	-3.2	-4.6	-6.0	-6.0	-6.8	-7.9	-8.1	-7.9	-7.8	-7.5	-7.7	-7.8	
US Coincident Indicators	2.6	2.4	1.8	2.0	2.2	2.4	1.9	1.4	1.5	1.5	1.3	1.4	1.3	1.7	1.8	1.7	1.4	1.5	
US Lagging Indicators	4.8	5.5	6.7	6.6	7.4	7.5	7.4	7.6	7.5	6.7	6.7	5.6	5.0	3.9	3.0	2.5	1.9	1.3	
Consumer																			
Total Retail Sales	8.9	9.7	9.5	10.4	10.1	9.2	8.8	6.1	6	7.4	5.3	2.2	1.3	2.1	1.5	2.8	2.9	3.8	
Personal Income	1.3	3.6	3.9	3.6	3.9	5.1	4.9	4.6	4.5	5.8	5.7	5.8	5.7	5.7	5.5	5	4.8		
Real Disposable Personal Income	-7.4	-4.7	-4.6	-4.3	-3.8	-2.3	-2	-1.6	-0.9	3.2	3.5	4.4	4.5	5	5.4	4.2	3.7		
Real Personal Consumption	2.4	2.5	1.7	1.9	1.8	1.9	1.4	0.9	1.3	2.3	2.3	1.7	1.6	1.8	2.1	2.7	2.3		
Personal Saving Rate (%)	3.1	3.1	2.7	3.5	3.2	3	3	3.3	3.4	4.4	4.7	5.2	5.2	5.3	4.9	4.1	3.9		
Consumer Confidence (Conference Board)**	108.6	103.2	98.4	95.3	103.6	107.8	102.2	101.4	109	106	103.4	104	103.7	102.5	110.1	114	108.7	103	
Employment																			
Employment Growth	4.9	4.8	4.5	4.4	4.2	4.0	3.7	3.4	3.2	3.3	2.8	2.7	2.6	2.6	2.4	2.2	2.1	2.1	
ASA Temporary Staffing Index	11.6	11.2	9.2	9.3	9.3	5.4	1.1	0.2	1.0	-2.1	-6.1	-6.5	-6.8	-5.9	-6.6	-4.7	-4.8	-5.5	
ISM Employment Index Manufacturing*	51.2	50.2	48.1	49.8	54.2	49.3	49.9	48.9	50.8	50.6	49.1	46.9	50.2	51.4	48.1	44.4	48.5	51.2	
ISM Employment Index Services*	49.7	50.3	48.7	49.5	50.2	52.3	49.2	50.6	49.4	50	54	51.3	50.8	49.2	53.1	50.7	54.7	53.4	
Unemployment Rate, %	3.6	3.6	3.6	3.5	3.7	3.5	3.7	3.6	3.5	3.4	3.6	3.5	3.4	3.7	3.6	3.5	3.8	3.8	
Average Hourly Earnings	5.8	5.5	5.4	5.4	5.4	5.1	4.9	5	4.8	4.4	4.7	4.3	4.4	4.3	4.4	4.3	4.3	4.2	
Initial Jobless Claims (avg. wkly. chg. '000s)	216	212	217	216	210	191	202	213	209	200	219	238	239	230	254	228	238	209	
Jop Openings	26.6	16.3	8.9	4.6	-7.0	-0.3	-7.9	-4.3	-5.0	-8.0	-14.0	-19.0	-12.2	-16.0	-16.4	-21.6	-5.8	-11.5	
Layoff Announcements	6	-15.8	58.8	36.3	30.3	67.6	48.3	416.5	129.1	440	410.1	319.4	175.9	286.7	25.2	-8.2	266.9	58.2	
Housing Market																			
Housing Starts	21.5	-3.6	-6	-13.9	-4.5	-6.2	-8.9	-16.6	-24.1	-19.7	-18.9	-19.4	-25.2	2.6	-9.2	5.8	-15.7	-7.2	
New Home Sales	-24.6	-11	-21.4	-28.6	-7.5	-23.6	-15.1	-24.6	-23.4	-19.9	-19.1	-9.5	11.1	11.6	21.5	36.1	5.8		
Existing Home Sales	-6.5	-8.9	-14.8	-19.9	-20.2	-24.0	-28.2	-35.2	-34.0	-36.9	-23.1	-22.1	-23.0	-20.4	-18.9	-16.6	-15.3	-15.4	
Median House Price (Existing Homes)	21.7	15.4	15.5	17.8	8.9	15.6	16.3	7.4	17	0.4	1.4	0.7	-8.9	-6.5	-3.7	-8.7	-2.3	-2.3	
Existing Homes Inventory (Mths' supply)	2.2	2.4	2.7	2.9	3	3	3.2	3.4	3.5	3.4	2.9	2.8	2.8	2.8	2.8	2.9	3	3.3	
New Homes Inventory (Mths' supply)	8.5	8.3	9.5	10.1	8.7	9.7	9.7	9.4	8.5	8.1	8.4	8.1	7.6	7.2	7.5	7	7.8		
NAHB Homebuilder Sentiment*	77	69	67	55	49	46	38	33	31	35	42	44	45	50	55	56	50	44	40
Inflation																			
Consumer Price Index	8.3	8.6	9.1	8.5	8.3	8.2	7.7	7.1	6.5	6.4	6	5	4.9	4	3	3.2	3.7	3.7	
CPI Less-food & energy	6.2	6	5.9	5.9	6.3	6.6	6.3	6	5.7	5.6	5.5	5.6	5.5	5.3	4.8	4.7	4.3	4.1	
Producer Price Index	11.2	11.1	11.2	9.7	8.7	8.5	8.2	7.4	6.4	5.7	4.7	2.7	2.3	1.1	0.2	1.1	2	2.2	
PPI Less-food & energy	9	8.6	8.3	7.6	7.2	7.2	6.9	6.3	5.7	5	4.6	3.3	3.1	2.8	2.5	2.7	2.5	2.7	
PCE Price Index	6.6	6.7	7.1	6.6	6.5	6.6	6.3	5.9	5.4	5.5	5.2	4.4	4.4	4	3.2	3.4	3.5	3.5	
PCE Prices Less-food & energy	5.3	5.1	5.2	5.0	5.2	5.5	5.3	5.1	4.9	4.9	4.8	4.8	4.8	4.7	4.3	4.3	3.9	3.9	
Business Activity - US																			
Industrial Production	4.6	3.7	3.2	3.0	3.1	4.5	3.1	1.9	0.6	1.5	0.9	0.2	0.4	0.1	-0.4	0.2	0.1	0.1	
New Cap Gds Orders less-aircraft & parts	4.8	9.5	7.6	6.3	8.2	5.6	5	3.2	1	5.6	2.7	1.9	1	3.2	1.4	0.4	0.6		
Business Inventories	17.9	19	20.1	20.6	19.8	19.5	18.3	16.8	15.1	12.6	10.7	8.8	6.2	5.2	3.3	1.8	1.4	1	
ISM Manufacturing PMI*	55.9	56.1	53.1	52.7	52.9	51	50	49	48.4	47.4	47.7	46.3	47.1	46.9	46	46.4	47.6	49.0	
Markit US Manufacturing PMI*	59.2	57	52.7	52.2	51.5	52	50.4	47.7	46.2	46.9	47.3	49.2	50.2	48.4	46.3	49	47.9	49.8	
ISM Services Index*	57.5	56.4	56	56.4	56.1	55.9	54.5	55.5	49.2	55.2	55.1	51.2	51.9	50.3	53.9	52.7	54.5	53.6	
Markit US Services PMI*	55.6	53.4	52.7	47.3	43.7	49.3	47.8	46.2	44.7	46.8	50.6	52.6	53.6	54.9	54.4	52.3	50.5	50.1	
Business Activity - International																			
Germany Manufacturing PMI Markit/BME*	54.6	54.8	52	49.3	49.1	47.8	45.1	46.2	47.1	47.3	46.3	44.7	44.5	43.2	40.6	38.8	39.1	39.6	
Japan Manufacturing PMI Jibun Bank*	53.5	53.3	52.7	52.1	51.5	50.8	50.7	49	48.9	48.9	47.7	49.2	49.5	50.6	49.8	49.6	49.6	48.5	
Caixin China Manufacturing PMI*	46	48.1	51.7	50.4	49.5	48.1	49.2	49.4	49	49.2	51.6	50	49.5	50.9	50.5	49.2	51	50.6	
China Manufacturing PMI*	47.4	49.6	50.2	49	49.4	50.1	49.2	48	47	50.1	52.6	51.9	49.2	48.8	49	49.3	49.7	50.2	
UK Manufacturing PMI Markit/CIPS*	55.8	54.6	52.8	52.1	47.3	48.4	46.2	46.5	45.3	47	49.3	47.9	47.8	47.1	46.5	45.3	43	44.3	
France Manufacturing PMI Markit*	55.7	54.6	51.4	49.5	50.6	47.7	47.2	48.3	49.2	50.5	47.4	47.3	45.6	45.7	46	45.1	46	44.2	
Currencies***																			
Euro (EUR/USD)	-12.3	-12.2	-11.6	-13.9	-14.9	-15.4	-14.5	-8.2	-5.8	-3.3	-5.7	-2.1	4.5	-0.4	4.1	7.6	7.8	7.9	
Renmimbi (USD/CNY)	2.1	4.7	3.8	4.4	6.7	10.4	14.0	11.4	8.5	6.2	9.9	8.4	4.7	6.5	8.3	5.9	5.3	2.6	
Yen (USD/Yen)	18.7	17.4	22.1	21.5	26.3	30.1	30.5	22.0	13.9	13.0	18.4	9.2	5.1	8.3	6.3	6.8	4.7	3.2	
Sterling (GBP/USD)	-9.0	-11.3	-12.0	-12.5	-15.5	-17.1	-16.2	-9.3	-10.7	-8.4	-10.4	-6.1	-0.1	-1.3	4.3	5.5	9.0	9.2	
Canadian $ (USD/CAD)	4.6	4.8	3.8	2.6	4.1	9.1	10.0	5.0	7.3	4.7	7.7	8.1	5.5	7.3	2.9	3.1	2.9	-1.8	
Mexican Peso (USD/MXN)	0.9	-1.5	0.9	2.5	0.3	-2.4	-3.7	-10.2	-5.0	-8.7	-10.6	-9.2	-11.9	-10.0	-14.9	-17.8	-15.4	-13.5	
US Equities																			
S&P 500	-1.2	-1.7	-11.9	-6.0	-12.6	-16.8	-15.9	-10.7	-19.4	-9.7	-9.2	-9.3	0.9	1.2	17.6	11.1	14.0	19.6	
S&P 400 Midcap	-8.3	-7.8	-15.8	-7.1	-11.7	-16.6	-12.9	-4.8	-14.5	0.7	-2.3	-6.7	-0.4	-4.3	15.6	8.6	8.8	13.6	
S&P 600 Smallcap	-9.7	-9.9	-18.0	-7.6	-13.4	-20.0	-13.1	-7.4	-17.4	-2.5	-5.1	-10.4	-5.5	-8.9	7.8	3.4	3.6	8.1	
Russell 2000	-17.8	-17.8	-26.1	-15.3	-18.9	-24.5	-19.6	-14.2	-21.6	-4.8	-7.4	-12.9	-5.1	-6.1	10.6	6.3	3.0	7.2	

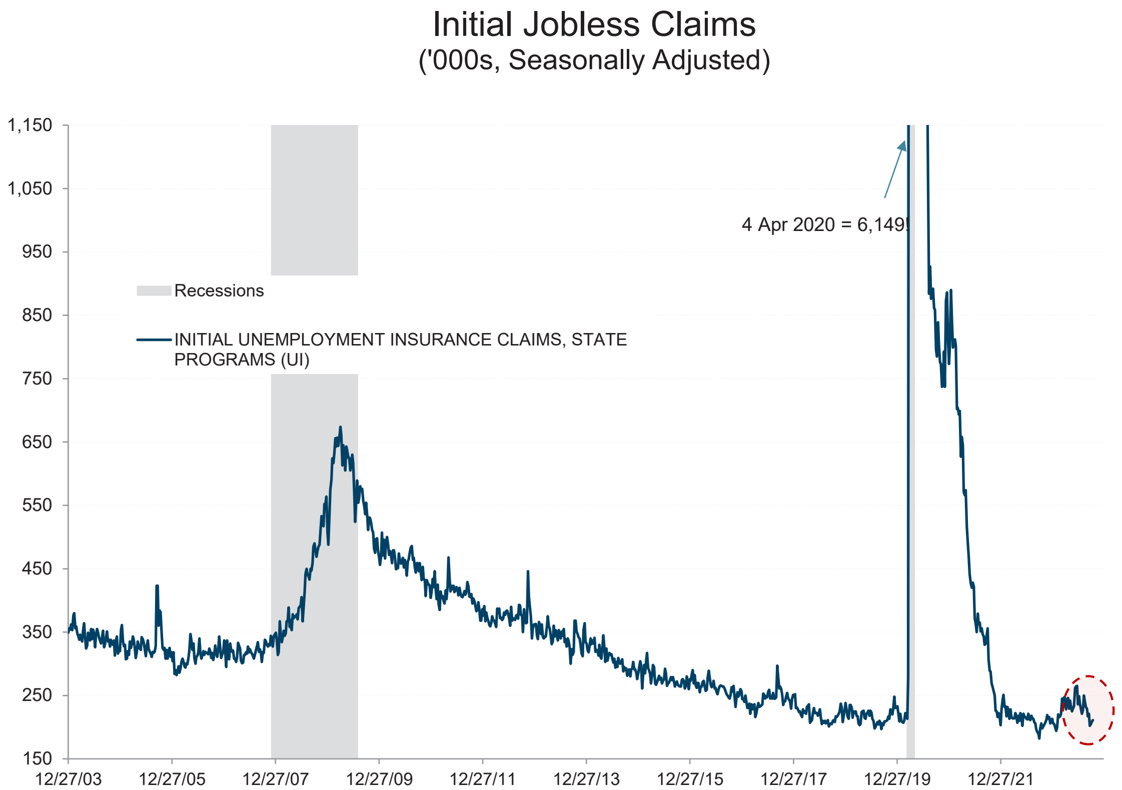
* Diffusion Index, **1985=100, ***Currencies - green/red = strengthening/weakening foreign currency vs dollar

Source: ISM, Federal Reserve, Census Bureau, Bureau of Labor Statistics, Conference Board, Bloomberg, William Blair

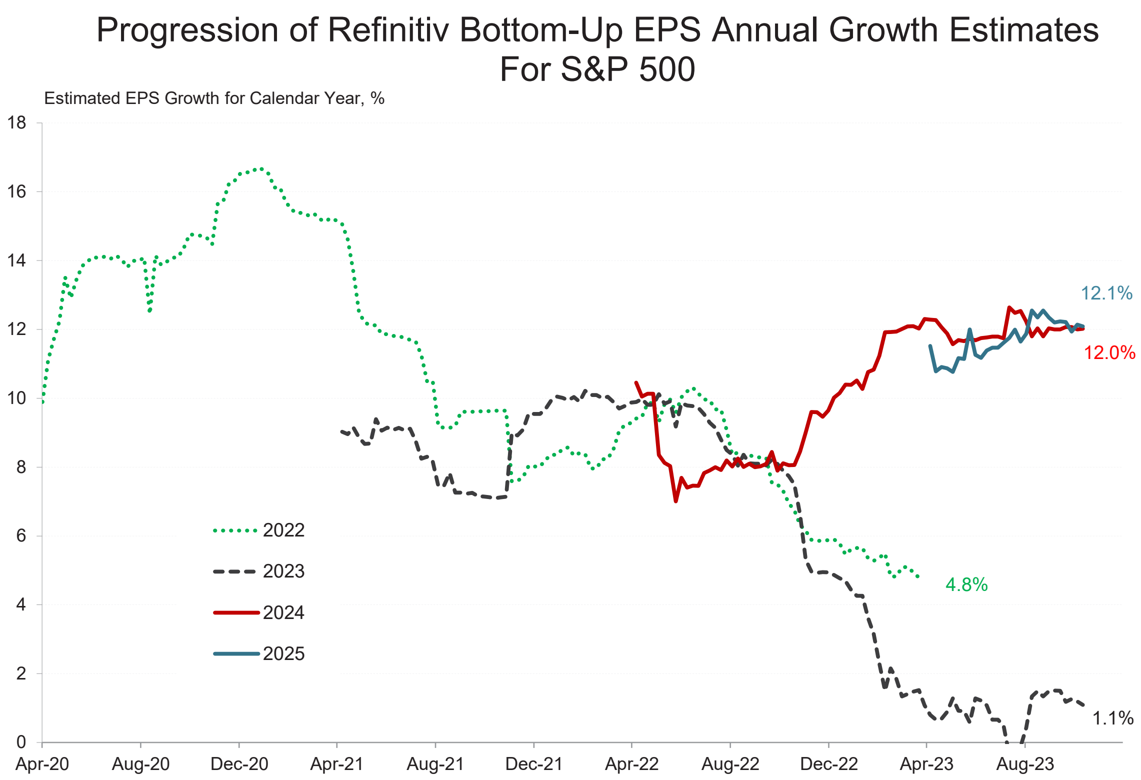
Other Economic Indicators





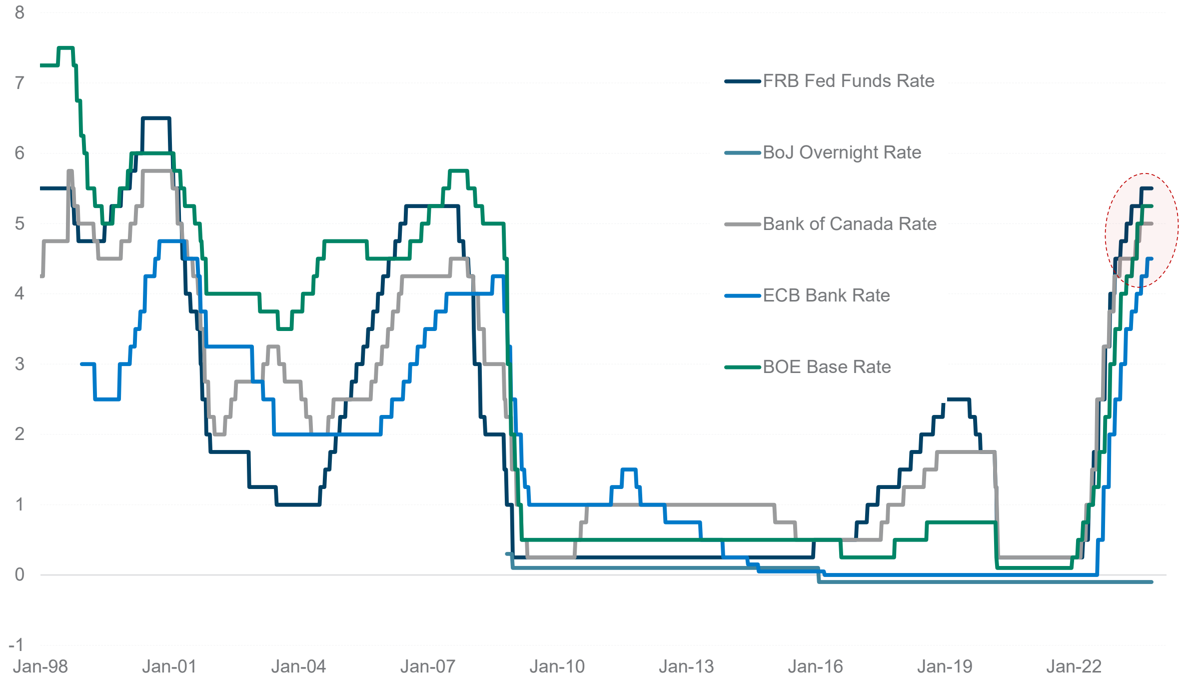


Source: Department of Labor, Bloomberg, William Blair Equity Research



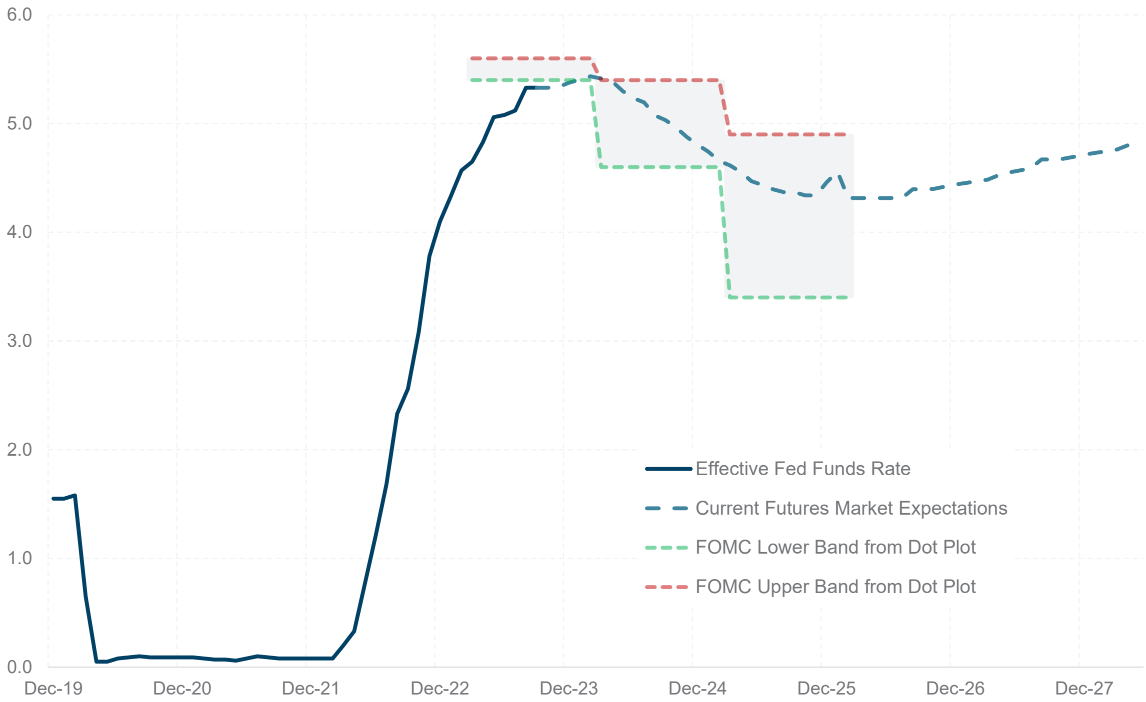
Sources: LSEG, William Blair Equity Research

Central Bank Target Short-term Interest Rates, %



Sources: Bloomberg, William Blair Equity Research

Fed Funds Rate, Futures Market Expectations & FOMC Projections, %



Sources: Bloomberg, William Blair Equity Research

S&P 500 Sector Performance

Global Industry Classification System	Current Weight* 19-Oct-23	Week Ago 12-Oct-23	Month Ago 19-Sep-23	Qtr-to-Date 29-Sep-23	Year-to-Date 30-Dec-22
S&P 500 Index	**100.00**	**-1.65**	**-3.73**	**-0.23**	**11.42**
S&P400 MidCap Index		**-1.52**	**-5.41**	**-3.28**	**-0.42**
S&P600 SmallCap Index		**-1.71**	**-5.94**	**-3.88**	**-4.40**
Dow Jones Industrials		**-0.65**	**-3.20**	**-0.28**	**0.81**
Nasdaq Composite		**-2.86**	**-3.60**	**-0.25**	**25.98**
Communication Services	**9.45**	**-0.71**	**-0.16**	**3.47**	**44.26**
Advertising	0.07	-2.00	-4.39	-0.38	-11.36
Broadcasting	0.06	0.37	-7.06	-3.78	-11.69
Cable & Satellite	0.66	-2.04	-5.28	-2.48	22.81
Integrated Telecommunication Services	0.66	3.69	-2.93	-0.73	-18.64
Interactive Home Entertainment	0.16	-2.26	0.98	0.63	17.71
Interactive Media & Services	6.34	-1.74	0.65	4.91	77.66
Movies & Entertainment	1.02	4.38	0.49	3.79	13.86
Publishing & Printing	0.03	3.78	8.36	7.62	19.38
Wireless Telecommunication Svcs	0.44	-2.34	-3.25	-1.58	-1.54
Consumer Discretionary	**10.98**	**-4.26**	**-8.60**	**-3.75**	**20.99**
Apparel Retail	0.39	1.48	-0.94	1.58	9.01
Apparel & Accessories & Luxury Goods	0.18	7.21	-2.95	-1.23	-23.30
Auto Parts & Equipment	0.09	-5.94	-10.90	-7.73	0.61
Automobile Manufacturers	2.14	-13.71	-16.64	-11.67	59.80
Automobile Retail	0.30	-2.90	-3.90	-2.33	-0.49
Broadline Retail	3.69	-2.95	-6.65	0.86	24.18
Casinos & Gaming	0.18	-2.98	-8.82	-3.53	1.61
Computer & Electronics Retail	0.04	-1.25	-2.72	0.04	-13.35
Consumer Electronics	0.05	-3.03	-1.97	-0.83	13.05
Distributors	0.12	-7.66	-8.20	-7.16	-12.74
Footwear	0.34	3.83	8.91	7.77	-11.93
Home Furnishings	0.01	-0.52	-13.75	-7.78	-22.59
Home Improvement Retail	1.08	-2.45	-9.88	-6.03	-7.85
Homebuilding	0.26	-2.98	-10.39	-6.19	21.05
Hotels, Resorts & Cruise Lines	0.82	-6.03	-10.36	-8.24	30.09
Household Appliances	0.02	4.55	-5.89	-3.40	-8.70
Housewares & Specialties	0.01	3.53	-27.07	-22.14	-46.26
Leisure Products	0.02	1.77	-14.57	-14.39	-7.19
Restaurants	1.12	4.00	-4.98	-0.53	0.43
Other Specialty Retail	0.13	0.18	-7.46	-4.29	-17.19
Consumer Staples	**7.14**	**1.95**	**-5.51**	**-1.90**	**-8.42**
Agricultural Products	0.15	1.71	-7.08	-2.71	-19.20
Brewers	0.03	0.48	-8.63	-8.26	13.24
Hypermarkets	2.13	1.13	-1.39	0.69	5.38
Distillers & Vintners	0.16	2.75	-10.51	-6.42	-3.20
Drug Retail	0.05	-13.35	-4.86	-5.76	-43.90
Food Distributors	0.09	4.74	-6.88	-0.59	-14.11
Food Retail	0.09	0.54	-3.45	-0.56	-0.18
Household Products	1.33	3.58	-3.21	1.38	-3.30
Packaged Foods & Meats	0.83	2.84	-10.12	-7.20	-18.36
Personal Products	0.19	1.08	-7.22	-2.56	-46.75
Soft Drinks	1.49	2.48	-8.87	-4.52	-12.46
Tobacco	0.59	-0.51	-4.85	-0.86	-9.13
Energy	**4.79**	**4.77**	**0.37**	**1.32**	**4.61**
Integrated Oil & Gas	2.24	5.61	-1.66	-2.01	-0.58
Oil & Gas Equipment & Services	0.53	2.87	0.24	3.30	13.32
Oil & Gas Exploration & Production	1.29	5.16	4.88	7.24	7.38
Oil & Gas Refining & Marketing & Transportation	0.43	4.10	-3.39	-2.98	15.79
Oil & Gas Storage & Transportation	0.38	1.70	2.40	5.37	4.92
Financials	**12.38**	**-1.21**	**-5.89**	**-1.43**	**-4.47**
Asset Management & Custody Banks	0.81	-3.58	-11.17	-5.96	-13.22
Consumer Finance	0.49	-2.74	-6.97	-1.69	-2.59
Diversified Banks	2.70	0.02	-4.28	-0.70	-4.81
Financial Exchanges & Data	1.15	-2.03	-4.06	0.65	9.72
Insurance Brokers	0.68	-0.94	-4.27	-0.23	10.89
Investment Banking & Brokerage	0.90	-3.21	-13.41	-7.82	-21.46

Life & Health Insurance	0.42	-0.61	-3.54	0.11	-6.07
Multi-line Insurance	0.20	0.94	-1.28	1.42	-1.87
Multi-Sector Holdings	1.21	-2.03	-8.59	-3.32	9.63
Property & Casualty Insurance	0.89	4.22	2.90	5.60	3.54
Regional Banks	0.28	-2.57	-5.26	-4.06	-40.94
Reinsurance	0.05	2.02	3.40	8.11	21.30
Health Care	**13.41**	**-0.64**	**-2.41**	**-0.22**	**-5.52**
Biotechnology	2.09	-2.06	-1.59	0.01	-4.85
Health Care Distributors	0.36	-0.54	4.19	4.10	15.83
Health Care Equipment	2.36	3.22	-7.27	-3.88	-6.79
Health Care Facilities	0.20	3.76	-3.50	-0.47	0.04
Health Care Services	0.60	2.18	1.83	3.52	-14.80
Health Care Supplies	0.12	2.44	-10.34	-6.19	10.18
Life Sciences Tools & Services	1.43	-2.61	-8.21	-6.32	-15.50
Managed Health Care	1.98	1.66	9.41	5.74	-1.83
Pharmaceuticals	4.28	-3.03	-3.74	0.64	-3.34
Industrials	**8.41**	**-2.83**	**-4.36**	**-1.60**	**1.50**
Aerospace & Defense	1.65	-0.07	0.11	3.29	-9.14
Agricultural & Farm Machinery	0.30	-0.24	-4.34	1.06	-11.05
Air Freight & Logistics	0.54	-2.47	-3.42	-4.01	0.67
Building Products	0.40	-7.26	-8.77	-7.40	2.13
Construction & Engineering	0.07	-5.15	-13.97	-9.80	18.41
Construction Machinery & Heavy Trucks	0.60	-4.93	-7.63	-5.79	6.02
Data Processing & Outsourced Services	0.06	-2.94	-5.31	-1.76	30.03
Diversified Support Svcs	0.26	-2.89	-1.54	3.75	25.09
Electrical Components & Equipment	0.60	-6.50	-6.74	-5.06	9.30
Environmental & Facilities Services	0.39	-0.84	-6.19	-1.99	-0.56
Human Resource & Employment Services	0.49	-0.85	0.16	2.48	10.84
Industrial Conglomerates	0.78	-2.38	-8.36	-3.11	2.55
Industrial Machinery	0.82	-4.54	-5.46	-3.02	5.55
Passenger Airlines	0.16	-6.42	-17.01	-11.87	-12.46
Railroads	0.64	-0.01	-0.86	1.90	-3.81
Research & Consulting Svcs	0.23	-3.17	-4.30	-1.23	8.13
Trading Companies & Distributors	0.26	-4.81	-0.07	0.47	22.02
Information Technology	**28.20**	**-2.97**	**-1.55**	**1.59**	**35.89**
Application Software	2.50	-1.47	-0.30	4.05	44.16
Communications Equipment	0.92	-1.28	-3.26	0.03	14.91
Electronic Components	0.20	-3.45	-8.74	-5.69	-0.90
Electronic Equipment & Instruments	0.17	-3.19	-8.62	-7.07	-15.37
Electronic Manufacturing Services	0.10	-4.21	-6.00	-3.38	3.96
Internet Software & Services	0.10	0.41	3.12	2.58	12.78
IT Consulting & Services	1.09	-1.23	-5.07	-1.64	4.99
Semiconductor Equipment	0.80	-7.41	-2.59	-2.80	15.26
Semiconductors	6.32	-6.86	-2.46	-1.70	68.52
Systems Software	8.19	-0.09	0.45	4.54	37.62
Technology Distributors	0.07	-4.13	-2.79	0.54	13.59
Technology Hardware, Storage & Peripherals	7.72	-2.91	-2.03	2.34	34.18
Materials	**2.38**	**-2.12**	**-5.84**	**-2.91**	**-1.92**
Commodity Chemicals	0.18	-0.81	-6.02	-3.28	3.19
Construction Materials	0.14	-4.15	-3.14	0.20	18.49
Copper	0.14	-2.33	-9.25	-5.52	-7.29
Diversified Chemicals	0.02	-2.19	-9.12	-6.77	-12.17
Fertilizers & Agricultural Chemicals	0.20	2.65	-3.04	0.11	-17.14
Gold	0.09	1.73	-2.09	6.76	-16.42
Industrial Gases	0.66	-1.96	-5.35	-0.69	6.78
Metal & Glass Containers	0.04	2.99	-10.66	-9.28	-11.69
Paper Packaging	0.18	-2.34	-3.54	-3.97	-8.73
Specialty Chemicals	0.61	-4.03	-7.74	-5.56	-5.25
Steel	0.14	-3.72	-6.58	-7.88	6.55
Real Estate	**2.28**	**-4.15**	**-8.83**	**-3.45**	**-11.16**
Health Care REITs	0.19	-1.99	-3.26	0.00	4.88
Hotel & Resort REITs	0.03	-1.93	-3.49	-1.99	-1.87
Industrial REITs	0.26	-6.45	-15.62	-8.58	-9.00
Office REITs	0.07	-3.37	-15.80	-6.41	-30.28
Real Estate Service	0.14	-6.86	-9.86	-5.38	-11.18
Residential REITs	0.32	-2.51	-5.55	0.21	-2.85
Retail REITs	0.27	-1.24	-7.62	-1.61	-15.43
Specialized REITs	0.13	-2.19	-7.85	-2.02	-1.90

Utilities	**2.36**	**0.00**	**-8.49**	**-0.48**	**-16.94**
Electric Utilities	1.55	-0.10	-9.09	-0.71	-17.13
Gas Utilities	0.04	-0.92	-3.49	3.94	-1.76
Independent Power Producers & Energy Traders	0.03	6.05	-17.42	-8.94	-51.88
Water Utilities	0.06	-1.11	-14.94	-5.50	-23.23
Multi-Utilities	0.67	0.22	-6.37	0.62	-14.34

*Current Weight is market cap based, based on calculations by William Blair Intl. Ltd.

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DOW JONES: 33414.20
S&P 500: 4278.00
NASDAQ: 13186.20

Additional information is available upon request.

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Coverage Universe	Percent	Inv. Banking Relationships *	Percent
Outperform (Buy)	72	Outperform (Buy)	7
Market Perform (Hold)	28	Market Perform (Hold)	2
Underperform (Sell)	1	Underperform (Sell)	0

*Percentage of companies in each rating category that are investment banking clients, defined as companies for which William Blair has received compensation for investment banking services within the past 12 months.

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