

PHILLIP MUTUAL BERHAD

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Large Cap vs. Small Cap: Understanding the Differences and When Size Matters

Large-cap stocks are stocks of established, well-known companies with high market capitalisation. These companies have a proven business model, a stable earnings outlook, and a long operating history. They typically have a more extensive trading volume and a significant institutional investor base due to their established reputation, which results in a more stable price performance.

Small-cap stocks, on the other hand, are stocks of newer players or companies that operate in new growth industries. These companies have a smaller revenue base but may potentially generate higher growth rates than large-cap companies. However, their earnings tend to be less predictable and more susceptible to economic slowdowns. Furthermore, with a smaller institutional investor base and lower trading volume, small-cap stocks may experience significant price swings, making them riskier investments than large-cap stocks but also provides opportunities for potentially higher returns.

Performance of FBM KLCI and FBM Small Cap Index

In comparison to the FBM KLCI Index, the price performance of the FBM Small Cap Index appears to be relatively volatile. This was particularly evident in 2020, where the small cap index experienced more significant declines during the sell-off but subsequently saw stronger rebounds during market recoveries (see Figure 1).

Figure 1: FBM KLCI and FBM Small Cap Index Price Performance (1 Jan 2013 to 31 Dec 2022)



Source: Bloomberg

Although there have been some years where the FBM KLCI Index has performed better than the Small Cap Index and vice versa, over a period of 10 years, the FBM Small Cap Index has recorded a total return (including capital appreciation and dividend) of 66.9%, which is significantly higher than the FBM KLCI's return of 23.3%. See Figure 2.

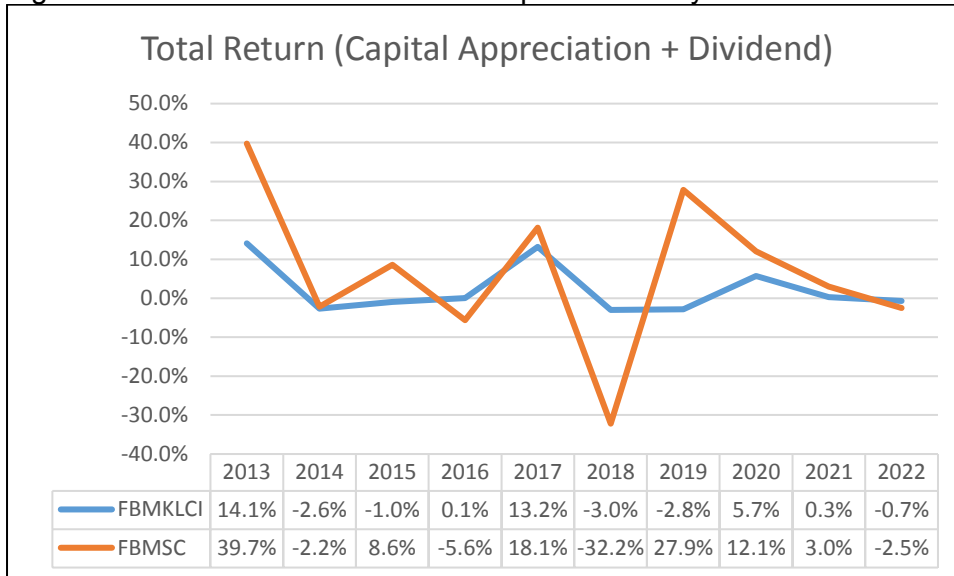
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Figure 2: FBM KLCI and FBM Small Cap Index Yearly Return



Source: Bloomberg

Assessing Stock Market Performance in 2023

At the time of writing, FBM KLCI Index, which is largely dominated by banking, plantation and oil and gas (O&G) sectors, slips close to 5% year-to-date following the sudden burst of turmoil in the global banking sector. FBM Small Cap Index, in contrast, is now up 2% year-to-date, erasing some gains made early this year.

As banking contagion worries ebb, we anticipate that the outlook for Malaysia's economy and equity market will improve, driven by several factors. These include the accelerating recovery of laggard sectors, as China's reopening boosts trade, tourism, and commodities demand, benefiting Malaysia as a commodities exporter. While we expect the market to remain challenging in the first half of 2023, due to rising operating costs, higher interest rates, and slower global growth, we believe the downside will be limited by the local bourse's undemanding valuations and China's reopening of the border.

On the economy front, Malaysia's growth fundamentals remain encouraging, with firm domestic consumption, a stable labour market, sustained current account surplus, revival of construction projects, and expansion of primary sectors thanks to elevated global commodity prices and modest external trade activities.

Another notable factor supporting the market is the low foreign shareholding in the Malaysia equities market (Feb'23: 20.4%), which is close to its historical low of 20.1% in Aug'22. This suggests that the downside risk from potential foreign selling may be limited. Furthermore, the market seems to be confident with the new unity government led by Prime Minister Anwar, which we believe is unlikely to implement any negative policy changes, particularly relating to subsidies and taxes, as it focuses on cost-of-living issues. Additionally, as the state elections in Selangor, Kelantan, Terengganu, Negeri Sembilan, Kedah, and Penang are expected to take place in June 2023, it is unlikely that significant policy reforms will be announced.

Overall, these factors bode well for the future growth prospects of Malaysia's economy and equity market in 2023. We continue to focus on sufficient liquidity to take advantage of market weakness with medium-term investment objectives.

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Strategies for Navigating Volatility as an Investor

Whether small-cap or large-cap stocks are better for an investor depends on their individual investment goals, risk tolerance, and investment horizon. Here are some factors to consider when comparing small-cap and large-cap stocks:

1. **Potential for returns:** Small-cap stocks have a higher potential for returns but also come with higher risks due to their volatility and the potential for business failures. Large-cap stocks may have lower potential returns but also offer more stability and a track record of successful performance.
2. **Risk tolerance:** Investors with a higher risk tolerance may choose to invest in small-cap stocks. In contrast, investors with a lower risk tolerance may prefer the stability of large-cap stocks.
3. **Market conditions:** During periods of market strength and positive investor sentiment, small-cap stocks may outperform large-cap stocks. Conversely, during market downturns or periods of uncertainty, large-cap stocks may be more resilient due to their established reputation and institutional investor support.
4. **Diversification:** Diversification across various sectors, market capitalisations, and asset classes is an essential aspect of portfolio management. A well-diversified portfolio may include a mix of small-cap and large-cap stocks to balance risk and potential returns.

Our Investment Approach and Offerings

Our investment strategy prioritises stocks that have strong fundamental characteristics, such as resilient earnings and sustainable business models, regardless of their market capitalisation. Apart from valuation (a small-cap stock can be undervalued too and present a great investment opportunity), we place a significant emphasis on evaluating the quality of the company's management team. We believe that competent and visionary leaders are critical to a company's long-term success, and we only invest in businesses that we believe have capable and trustworthy management.

This investment approach allows us to navigate through the challenging periods of market volatility and unexpected events, while maintaining a focus on delivering consistent returns to our investors over the long term. We strive to build resilient portfolios that can weather the storms and provide stable growth for our investors.

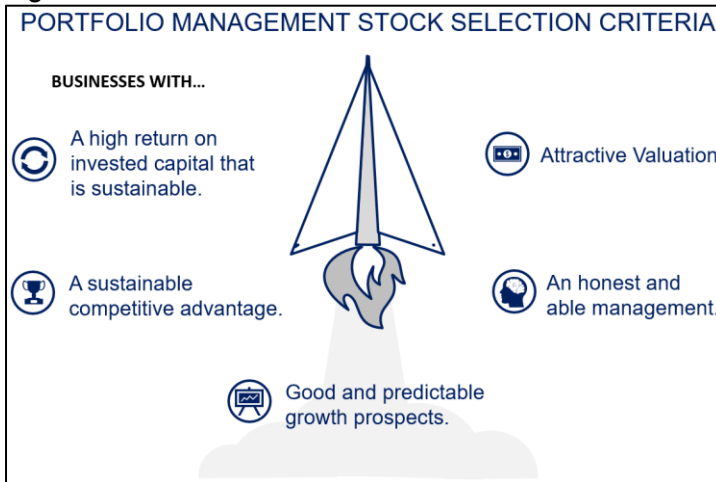
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Figure 3: Stock Selection Criteria



Source: PMB

Phillip Mutual Berhad offers a comprehensive list of local and global unit trust funds that may suit your investment preferences and financial goals. For local funds, our recommendation is as below:

Lipper Category	PMB Funds
Equity Malaysia Income	Phillip Dividend
Equity Malaysia	Phillip Recovery Phillip Dana Aman * Phillip Master Equity Growth
Equity Malaysia Sm&Mid Cap	Phillip Pearl

Note: * indicates Syariah

Our investment portfolio focuses on companies that possess strong fundamentals, including stable earnings and a promising future outlook, and are led by capable management teams. We have allocated a greater portion of our investments in the Technology, Industrial, and Consumer sectors as we anticipate these industries will experience growth due to the reopening of borders and the overall improvement in economic conditions.

Please click on the [link](#) to learn more or email us at phillipmutual@phillipcapital.com.my if you require any further information.