

## Strategy Matters

# Small caps: can the forgotten factor finally outperform?

European Small caps are down 13% since the end of 2021, while Large caps are up 11%. This has been mostly driven by a derating since central banks embarked on their rate hiking cycle, and Small now trade at a 4% discount to Large caps, one of their lowest relative valuations (based on 12m fwd PE) since the GFC.

**As we approach the first ECB cut, which our economists expect in June, EA Q1 GDP growth has been stronger than expected, and M&A activity is picking up, investors are wondering whether this is time to buy small caps.** Small caps outperformed in Q4 2023, when rate cuts started to be priced. YTD they have given back 2/3 of this outperformance, as markets have postponed cuts. Our economists have just delayed their BoE and Fed first cut forecast to August and September. **Their view is similar to the market, and we doubt that the timid sequential growth acceleration will be enough to support Small caps outperformance.**

**We highlight 4 places where investors can find opportunities within small caps.** (1) **LBO targets as private activity picks up** (Exhibit 23). This strategy is the least dependent on bond yields falling; (2) **Real Estate and Technology laggards** if bond yields fall further (Exhibit 25 and Exhibit 26); (3) **UK small caps**; (4) **Small caps with the highest price upside** based on the 12m target of our equity analysts (Exhibit 31).

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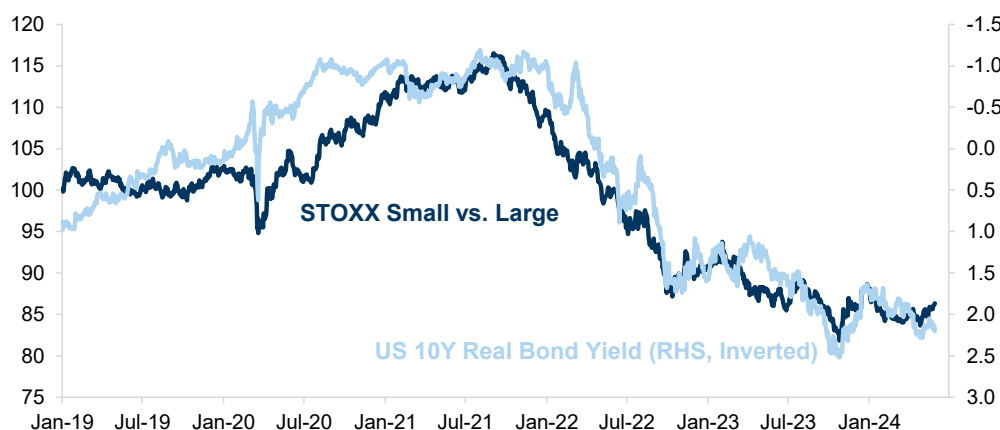
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**Exhibit 1: The relative derating of Small caps has closely tracked the rise in bond yields**  
Price performance STOXX Small vs STOXX Large (indexed to 100 in Jan-19), US 10Y real rates (RHS, Inverted)



Source: Datastream, Goldman Sachs Global Investment Research

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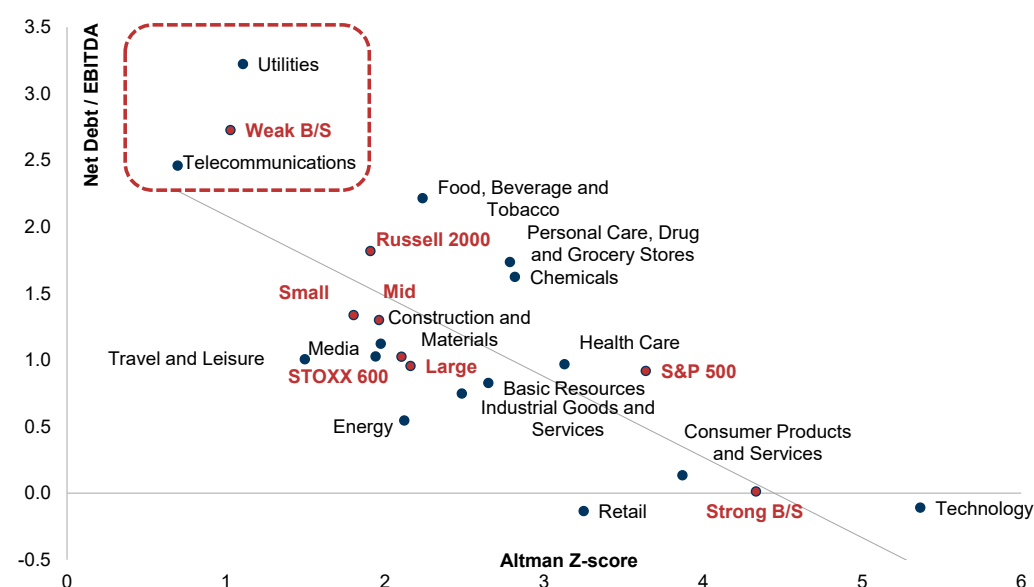
# Small caps: can the forgotten factor finally outperform?

## 1. Small caps need a rate relief

We view the underperformance of small caps being mainly a function of interest rates for two reasons (Exhibit 1):

1. Small caps are not particularly levered, but almost **half of the debt of small caps is floating** (compared with less than 30% for large caps). As a result, their balance sheets are weaker than the market (Exhibit 2) and they are relatively vulnerable to higher interest rates. Their net debt to EBITDA is 1.3x (1x for Large caps), which is small compared with Utilities, Telecoms or our Weak Balance sheet baskets (GSSTWBAL), with a net debt to EBITDA of 2.5x/3x.
2. The negative **sensitivity of small caps to interest rates is also a function of their sector composition**: compared to large caps, they are overweight Real Estate, as well as capital intensive industries such as Industrial Goods & Services and Construction & Materials, all penalised by a high cost of capital. By contrast, they are underweight Banks, Insurance, and Energy, sectors which tend to outperform with rising bond yields and inflation (Exhibit 3).

**Exhibit 2: While not particularly indebted, Small caps have relatively weak balance sheets based on Altman Z-Scores (low score = weak)**



STOXX 600 ex Financials & Real Estate

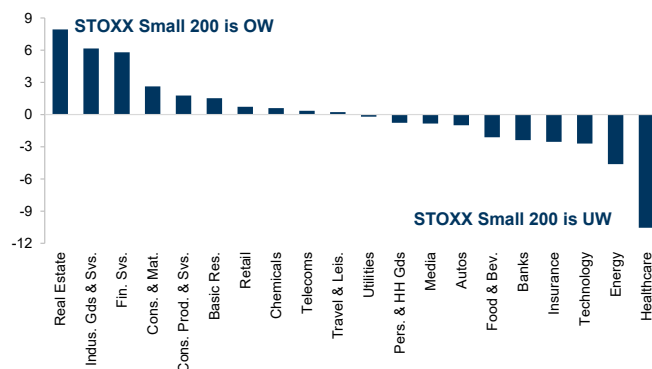
Source: FactSet, Goldman Sachs Global Investment Research

The sensitivity of Small caps to bond yields is new. **Historically, our Small caps model shows that they have been driven by growth expectations rather than bond yields**, because in absolute terms, the level of rates was not a concern for weak balance sheet companies (see *Strategy Matters - Small beginnings: Is it time to buy Small caps?*, 18 January 2024). Since 2022, we find the opposite and growth even

became statistically not significant. A simple correlation exercise shows that Small caps have had close to zero correlation with bond yields over the past 15 years, while they are positively correlated to changes in PMI ([Exhibit 4](#)).

**Exhibit 3: Small caps are overexposed to Real Estate, Industrials and Construction, sectors impaired by the rising rate environment and the manufacturing downturn**

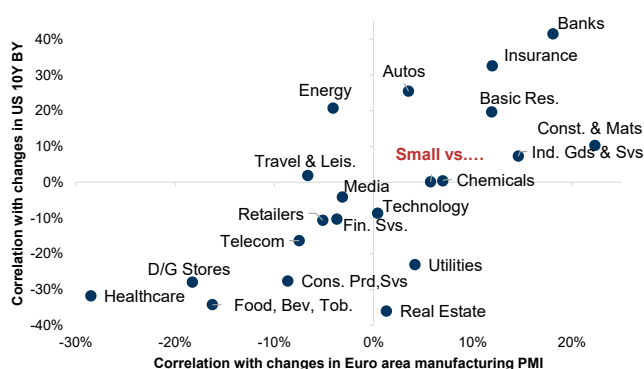
STOXX 200 Small sector weights minus STOXX 200 Large sector weights



Source: FactSet, STOXX, Goldman Sachs Global Investment Research

**Exhibit 4: Small caps, historically, have close to zero correlation with changes in bond yields, but outperform when PMIs rise**

Based on 15y correlations



Source: Haver, Datastream, Goldman Sachs Global Investment Research

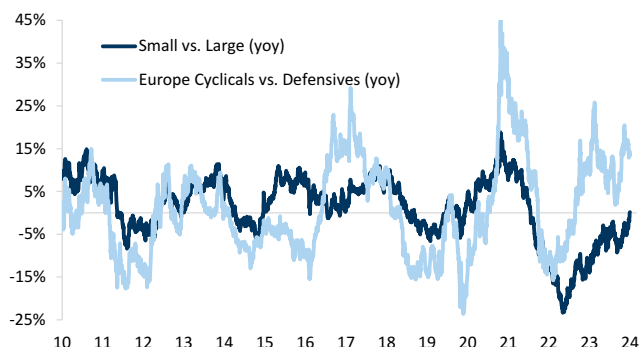
## 2. Small caps have been lagging their cyclical factor

Since the beginning of the year, economic growth has been accelerating in the Euro area (based on Q1 GDP and PMIs) and **cyclical sectors have outperformed Defensive** by 6%, bringing up their valuation discount to -26%, after having dipped to -50% at the end of 2022.

**However, companies with high financial leverage or a disadvantageous debt structure have been left behind: Real Estate, Small caps, Telecoms, our Weak balance sheet basket (GSSTWBAL) and Utilities** are considerably down compared with their end of 2021 level, while Cyclicals (GSSTCYCL) stand 12% above. As [Exhibit 6](#) shows, based on the historical beta of Small caps or Real Estate to economic activity (PMIs), these companies should have outperformed YTD, but they underperformed.

For small caps to catch up with cyclicals, we need to see bond yields coming back down, or sequential growth accelerating more sharply than what our economists expect.

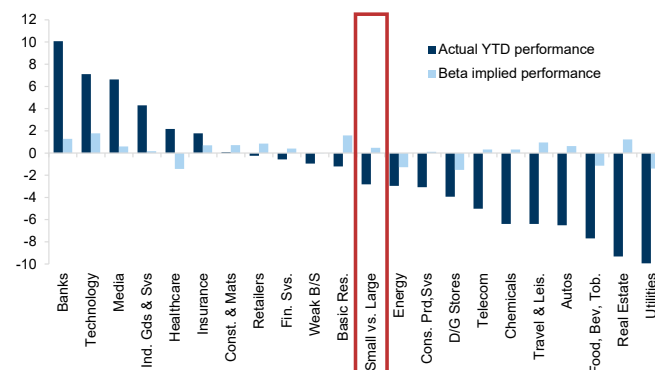
**Exhibit 5: European Small caps have decoupled from Cyclical**  
Europe Stoxx Small vs. Large



Source: Datastream, Goldman Sachs Global Investment Research

**Exhibit 6: As PMIs rose YTD, Small caps should have outperformed just like other cyclicals but they underperformed as bond yields rose**

Relative performance to SXXP. Betas based on changes in Europe manufacturing PMI since 2022

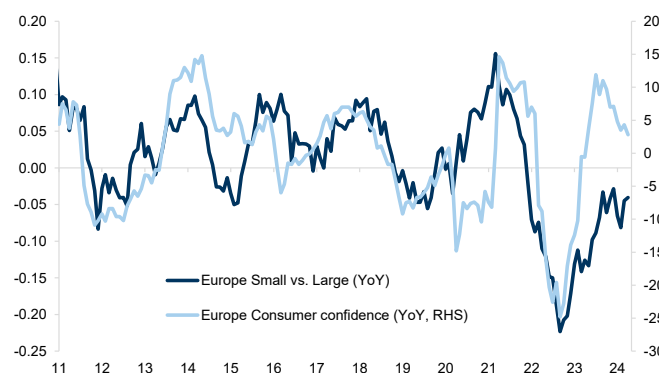


Source: Haver Analytics, Datastream, Goldman Sachs Global Investment Research

On balance, based on their sector mix, **small caps are relatively more cyclical than large caps** (see Exhibits 9 and 10 [here](#)). To give a point of comparison, they are less cyclical than the FTSE MIB and roughly as much as the EURO STOXX 50. Historically, they used to perform closely with cyclical indices and macro indicators of activity, such as Consumer confidence ([Exhibit 7](#)) and economic growth ([Exhibit 8](#)). For more, see [Strategy Matters - What drives European Small caps? Q&A](#).

**Exhibit 7: Small caps tend to outperform with rising consumer confidence**

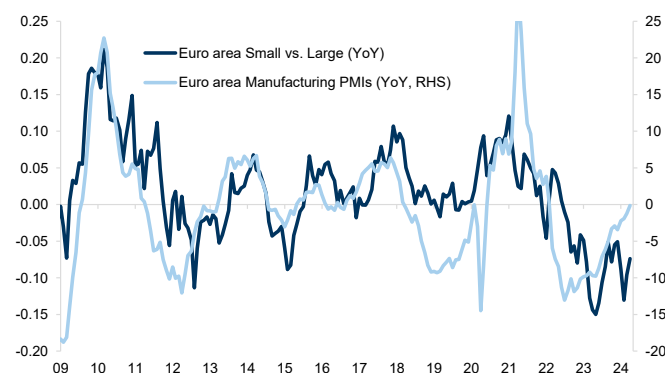
Europe Small vs. Large price index (YoY) and Europe Consumer confidence (YoY, RHS)



Source: Datastream, Bloomberg, Goldman Sachs Global Investment Research

**Exhibit 8: Small caps tend to outperform with improving activity data**

Euro area Small vs. Large price index (YoY) and Euro area Manufacturing PMIs (YoY, RHS)



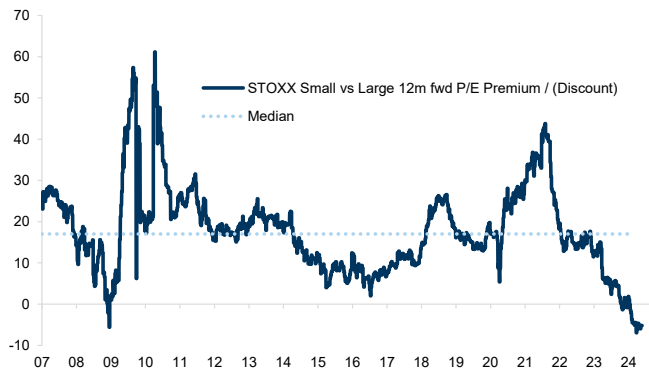
Source: Datastream, Haver Analytics, Goldman Sachs Global Investment Research

### 3. How cheap are small caps?

Small caps trade on a 4% discount to Large caps, one of their **lowest valuations relative to Large caps since the Global financial crisis** ([Exhibit 9](#)).

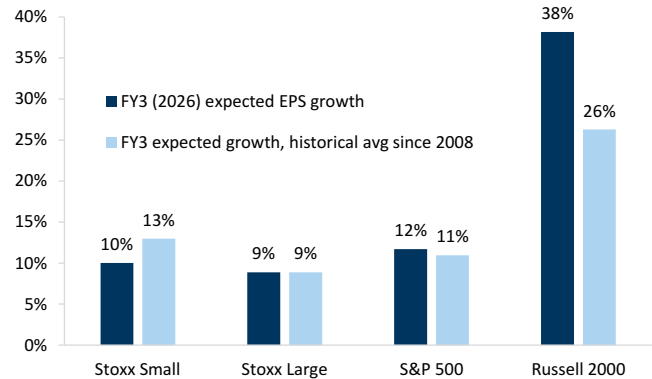
**That said, Small caps' expected earnings growth is lower than usual:** 10% in FY3 (2026), which is only marginally more than large caps, at 9%. This is a much smaller earnings growth differential than usual and much smaller than the expected earnings growth differential between US small caps and the S&P 500 ([Exhibit 10](#) and [Exhibit 19](#)).

**Exhibit 9: Small caps trade at a discount to Large caps for the first time since the Global Financial Crisis**  
12m fwd P/E Premium / (Discount) STOXX Small vs STOXX Large



Source: IBES, Datastream, Goldman Sachs Global Investment Research

**Exhibit 10: FY3 expected EPS growth for European small caps is lower than usual**  
Light blue = median since 2008

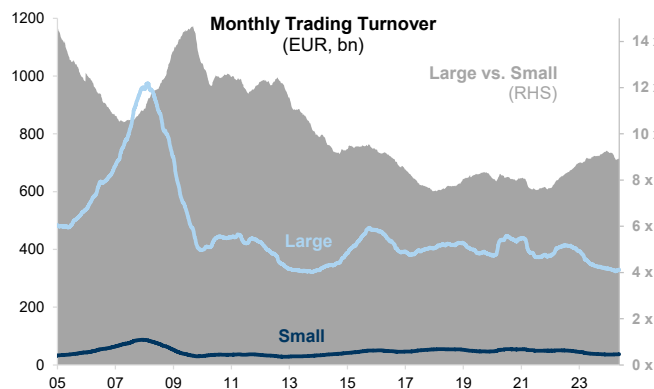


Source: IBES, Goldman Sachs Global Investment Research

#### 4. Small caps can benefit from an M&A pick-up

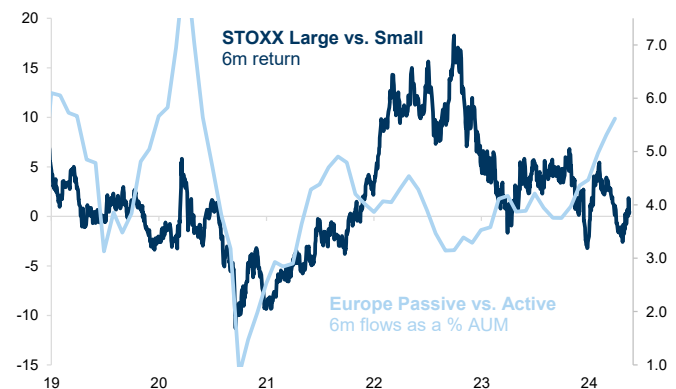
**Small caps suffer from a structural lack of demand, a persistent headwind to their valuations.** Their liquidity is lower ([Exhibit 11](#)), they do not benefit from the surge in passive investment ([Exhibit 12](#)), and small companies do less buybacks than their large counterparts ([Exhibit 13](#)).

**Exhibit 11: Trading volume on the Primary exchange per day is 9x higher for European Large caps than Small caps**  
Monthly Trading Turnover (EUR, bn), Primary exchange



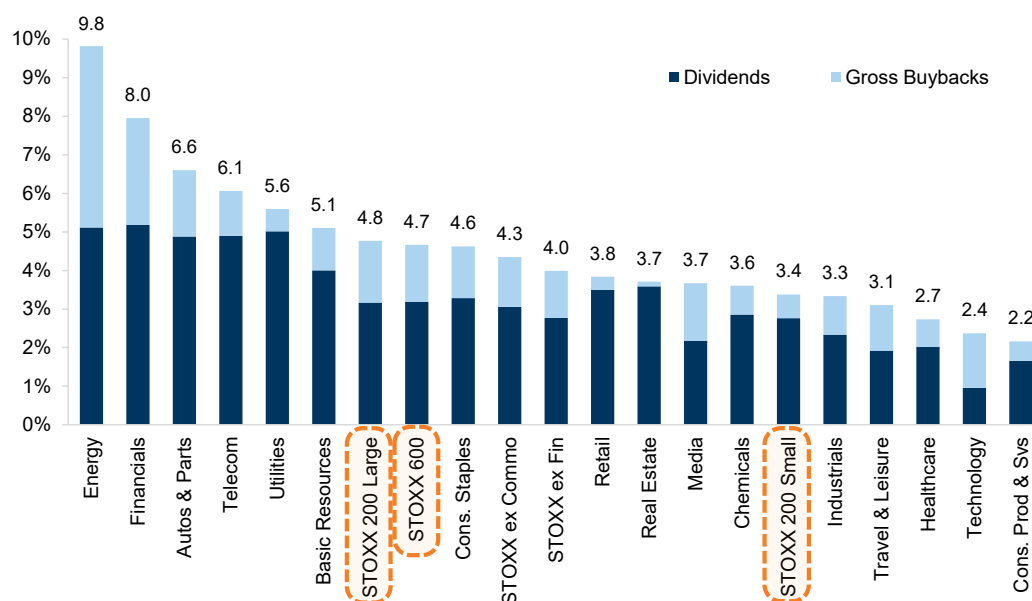
Source: Bloomberg, Datastream, Goldman Sachs Global Investment Research

**Exhibit 12: Small caps tend to underperform when passive funds see more inflows than active**



Source: Datastream, EPFR, Goldman Sachs Global Investment Research

**Exhibit 13: Small caps do less buybacks than Large caps and their total net shareholder return is 3.4%, versus 4.8% for Large caps**  
Last 12 months total shareholder return yield (%)

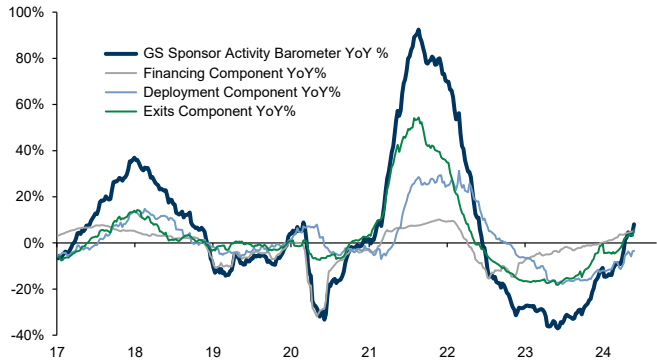


Source: Factset, Datastream, Goldman Sachs Global Investment Research

**One positive though, is that M&A activity should pick up, which tends to support the outperformance of Small caps, typical M&A targets** (Exhibit 16 and Exhibit 17). In addition, **Small caps tend to outperform when alpha opportunities improve** (Exhibit 18), as is currently the case (see *Strategy Espresso: Alpha opportunities to improve further*).

The **Sponsor Activity Barometer** of our equity analysts, which measures dynamism in capital markets, has risen 8% yoy on the back of improving capital availability (Exhibit 14), **M&A deal counts are rising** (after having dropped 30% in 2023, Exhibit 16) as well as Google trends. The number of searches related to M&A in the UK has jumped, up 35% YTD. This should continue as interest rates are meant to be peaking, broad market valuations are below the long-run average, growth is accelerating sequentially and investors' available capital is unprecedentedly high (Exhibit 15).

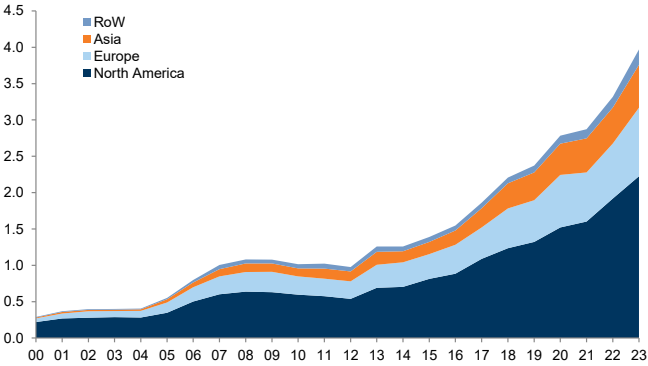
**Exhibit 14: Sponsor Activity Barometer YoY %**  
As of 24 May 2024



Source: Goldman Sachs Global Investment Research

**Exhibit 15: Investors' available capital has increased in recent years**

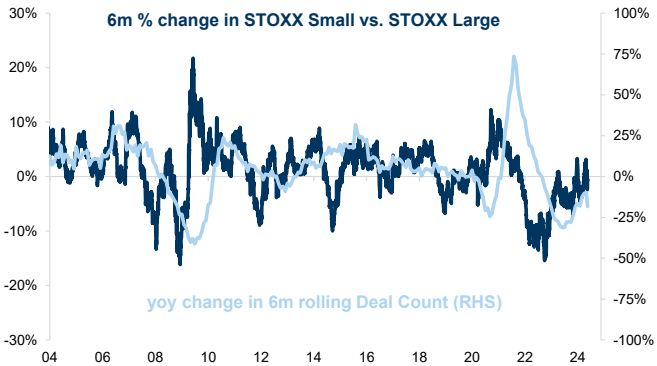
Available capital (capital to be deployed in private markets) by geography, USD tn



Excludes funds of funds and secondaries

Source: Preqin, Goldman Sachs Global Investment Research

**Exhibit 16: Small caps tend to outperform when M&A activity picks up**  
% change in STOXX Small vs. Large and % change in rolling Deal count over 6 months

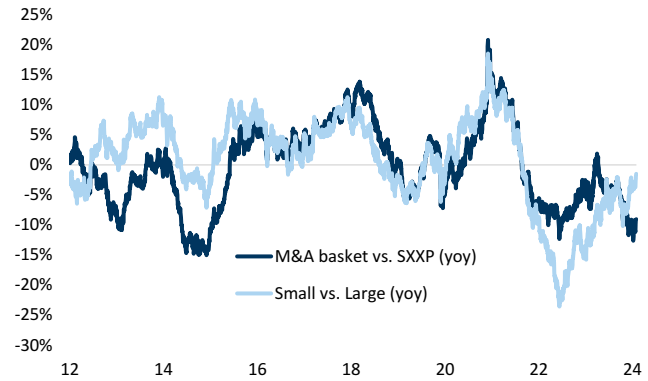


M&A deals in Western Europe, minimum deal value EUR 50 mln.

Source: Bloomberg, Datastream, Goldman Sachs Global Investment Research

**Exhibit 17: Small caps tend to outperform when our M&A basket outperforms**

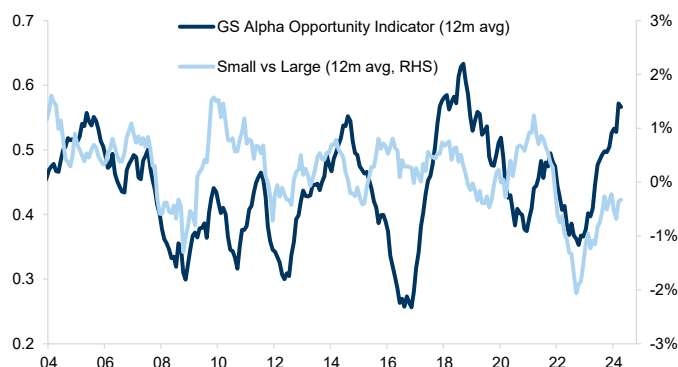
GS European M&A Candidates basket: GSTRACQN Index



Source: Bloomberg, Goldman Sachs Global Investment Research

### Exhibit 18: Small caps generally outperform as Alpha opportunities rise

GS Alpha Opportunity Indicator (12m avg) and Small vs Large (12m avg, RHS)



Source: Bloomberg, Datastream, Goldman Sachs Global Investment Research

## 5. Europe versus US small caps

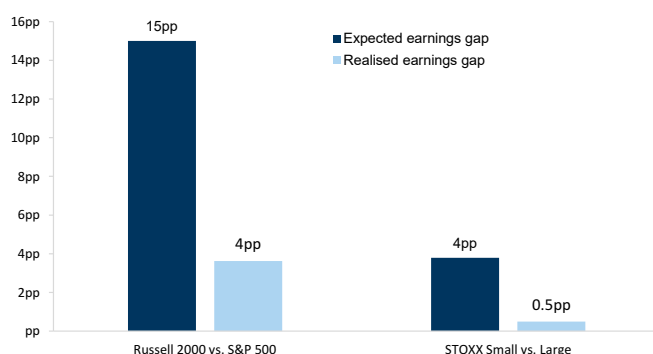
In absolute terms, US and Europe small caps are both 16% below their 2021 peak, but there are significant differences between the two indices:

- **A significant share of US Small caps are probably in the early stages of their business cycle, while a portion of European small caps are former large caps on a structural decline.** In Europe, 6 small caps were actually in the large caps index 10 years ago, and 28 small caps were mid caps. This is consistent with the fact that **almost one third of the Russell 2000 (31%) is expected to be non-profitable over the next 12 months (0% of S&P 500) versus only 2% of European small caps (2% of European Large caps).**
- **The Russell 2000 is more of a Growth index than STOXX Europe Small:** consensus expects its earnings to grow 25% per annum by 2026 (12% for the S&P 500), versus 11% for European small caps (7% for the SXXP). As we show in [Exhibit 19](#), historically, the expected earnings growth differential in FY3 between the Russell 2000 and the S&P 500 is about 15pp, versus only 4pp between European Small and Large caps.
- That said, **revisions to the 2024 EPS estimates have been considerably more negative for the Russell 2000 than for European small caps.** This is also quite typical as, historically, the realised earnings growth differential between the Russell 2000 and the S&P 500 is only 4pp, versus 15pp expected two years ahead.
- In terms of sector composition, US small caps have more Healthcare (Biotech), Tech and Energy than European small caps, and less Real Estate, Financial Services and Industrials ([Exhibit 22](#)). This means that **US Small caps tend to be sensitive to interest rates because of their duration (especially for Biotech and Tech names), while European Small caps tend to be sensitive to interest rates because of their balance sheets.** This probably explains why the valuation premium of European Small caps has dropped more than that of their US counterparts, relative to Large caps ([Exhibit 21](#)).



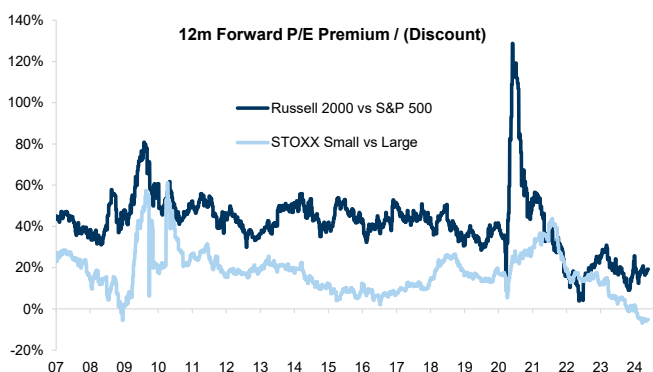
- **Russell 2000 companies are smaller than Stoxx Small companies** with a median market cap of USD 4400 millions versus USD 950 millions, respectively.
- In terms of debt, **Russell 2000 is more indebted than European Small caps**, with a net debt to EBITDA of 1.8x vs. 1.3x, respectively. That said, 30% of the debt structure of the Russell 2000 is based on floating interest rates versus 50% for European small caps. Overall, balance sheets appear of similar strength for the Russell 2000 and European small caps, based on Altman z-scores ([Exhibit 2](#)). We would note that the differential is greater between the Russell 2000 and the S&P 500 which has only 6% of its debt with floating interest rates (30% for the SXXP).

**Exhibit 19: The expected profit growth differential between US Small caps and the S&P 500 tends to be much larger than for European Small caps, but the realised differential is not as large... FY3 EPS growth differential 2y ahead**



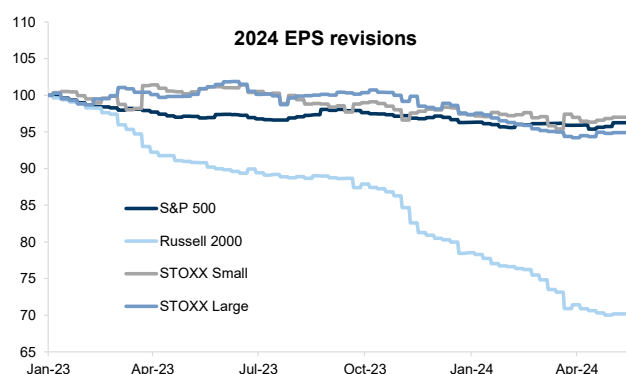
Source: IBES, Datastream, Goldman Sachs Global Investment Research

**Exhibit 21: The relative valuation of European small caps has dropped more than that of US small caps**



Source: Datastream, I/B/E/S, Goldman Sachs Global Investment Research

**Exhibit 20: EPS revisions of the Russell 2000 have been deeply negative while those of European small caps have been resilient 2024 EPS revisions**



Source: Datastream, Goldman Sachs Global Investment Research

**Exhibit 22: US small caps have more Healthcare (Biotech), Tech and Energy than European small caps, and less Real Estate, Financial Services and Industrials**  
Sector Composition

Sector	STOXX 600	STOXX Small	S&P	Russell 2000
Autos	3.0%	1.8%	0.7%	1.4%
Banks	8.7%	7.9%	8.2%	3.3%
Basic Res.	2.7%	3.5%	2.3%	0.5%
Chemicals	2.4%	3.5%	1.3%	1.0%
Cons. & Mat.	3.6%	6.5%	4.7%	0.6%
Cons. Prod. & Svs.	6.5%	6.7%	5.7%	1.5%
Energy	5.8%	2.0%	8.1%	3.7%
Fin. Svs.	4.1%	8.8%	4.5%	4.7%
Food & Bev.	6.2%	5.1%	2.0%	2.7%
Healthcare	16.7%	8.1%	15.1%	10.8%
Indus. Gds & Svs.	13.5%	17.6%	13.7%	10.6%
Insurance	5.0%	3.1%	2.4%	2.0%
Media	1.9%	1.7%	0.9%	1.2%
Pers. & HH Gds	2.7%	1.7%	0.8%	1.8%
Real Estate	1.3%	8.2%	5.5%	2.0%
Retail	0.9%	1.3%	3.4%	7.2%
Technology	7.9%	5.4%	13.8%	38.5%
Telecoms	2.3%	2.4%	1.2%	1.9%
Travel & Leis.	1.1%	1.4%	2.8%	2.1%
Utilities	3.6%	3.4%	2.7%	2.4%

Source: Datastream, Goldman Sachs Global Investment Research

# Where are the places to go in Small caps?

## 1. Which SMIDs are potential LBO targets?

Our analysts' Sponsor Activity Barometer has been picking up to 8% yoy, as investors expect interest rates to come down, stocks are relatively attractively valued, and credit formation is picking up. We derive two screens of SMID companies (market cap < €10bn) which are potential LBO targets as they appear relatively underlevered and undervalued:

- Companies which compared with their sector median have: a lower Net debt to EBITDA, a lower valuation *premium* than usual based on 12m fwd PE, and a higher ROE than usual.
- Companies which compared with their sector median have: a lower Net debt to EBITDA, a lower valuation *discount* than usual based on 12m fwd PE, and a lower ROE than usual.

For additional screens, see the IRR screen of our Tactical Research team.

**Exhibit 23: Our LBO Candidates Screen for SMIDs - High ROE Stocks**

Screen consists of 50 European stocks

Name	Industry	Country	Market Cap (€ bn)	ROE (%)	NTM PE	ND/EBITDA	Rel. Perf. since 2022 (€)
Wise	Industrials	United Kingdom	9.6	33.0	22.2	-0.7	-3%
Carl Zeiss Meditec	Health Care	Germany	8.2	12.9	28.5	0.5	-54%
Puma	Consumer Discretionary	Germany	7.2	10.7	19.3	1.2	-58%
Gea Group	Industrials	Germany	6.6	16.8	14.4	-0.5	-26%
La Francaise Des Jeux	Consumer Discretionary	France	6.3	42.6	14.9	-0.4	-18%
Hargreaves Lansdown	Financials	United Kingdom	6.2	45.8	13.6	-1.2	-24%
Fuchs	Basic Materials	Germany	5.6	15.4	14.3	-0.2	6%
Rightmove	Real Estate	United Kingdom	5.1	289.6	20.5	-0.1	-36%
Darktrace	Technology	United Kingdom	4.9	36.4	40.2	-1.6	30%
Alk-Abello	Health Care	Denmark	4.6	12.6	35.9	0.2	-16%
Soitec	Technology	France	3.9	16.0	22.9	-0.4	-52%
Fielmann Group	Consumer Discretionary	Germany	3.8	14.9	23.6	1.2	-28%
Interparfums	Consumer Discretionary	France	3.3	19.3	24.8	-0.1	-26%
Elekta	Health Care	Sweden	2.8	14.4	17.4	0.9	-37%
Aixtron	Technology	Germany	2.6	20.9	18.0	-0.9	22%
Vusiongroup	Industrials	France	2.5	33.5	31.8	-0.1	98%
Network International Holdings	Industrials	United Kingdom	2.5	13.8	18.0	0.6	24%
Antin Infrastructure Partners	Financials	France	2.3	15.4	17.6	-2.0	-65%
Bridgepoint Group	Financials	United Kingdom	2.2	9.5	14.4	-6.7	-56%
Qt Group	Technology	Finland	2.2	35.0	39.7	-0.2	-40%
Carel	Industrials	Italy	2.0	22.0	28.2	0.3	-36%
AJ Bell	Financials	United Kingdom	2.0	43.6	19.1	-1.3	-2%
Kainos Group	Technology	United Kingdom	1.8	34.0	24.6	-1.3	-40%
Skan	Industrials	Switzerland	1.8	16.1	39.8	-1.2	-10%
Trainline	Consumer Discretionary	United Kingdom	1.8	11.3	22.7	0.4	6%
Gamma Communications	Telecommunications	United Kingdom	1.7	16.6	17.7	-1.0	-18%
Bytes Technology Group	Technology	United Kingdom	1.7	72.6	23.8	-0.9	-4%
Salcef Group	Industrials	Italy	1.6	14.0	17.0	0.1	-4%
Intercos	Consumer Discretionary	Italy	1.5	12.1	20.5	0.6	4%
Rai Way	Telecommunications	Italy	1.3	42.3	14.9	0.6	-12%
Kempower	Industrials	Finland	1.3	29.9	43.6	-1.7	92%
YouGov	Consumer Discretionary	United Kingdom	1.3	14.1	17.9	-0.8	-47%
Secunet Scty.Networks	Technology	Germany	0.9	22.0	30.3	-0.3	-67%
Audax Renovables	Utilities	Spain	0.9	19.6	16.8	2.4	42%
Chemometec	Health Care	Denmark	0.9	30.1	41.9	-1.4	-59%
EL EN	Health Care	Italy	0.8	14.5	13.5	-0.6	-40%
A.G. Barr	Consumer Staples	United Kingdom	0.8	13.7	15.0	-0.7	6%
Alfen	Industrials	Netherlands	0.8	18.0	18.8	0.6	-62%
AO World	Consumer Discretionary	United Kingdom	0.7	23.8	20.8	1.1	-9%
Industrie De Nora	Industrials	Italy	0.7	26.9	27.6	-0.4	NM
Empiric Student Property	Real Estate	United Kingdom	0.6	7.4	19.2	6.5	-3%
Plazza	Real Estate	Switzerland	0.6	2.6	30.4	4.1	-13%
Alfa Financial Software Holdings	Technology	United Kingdom	0.6	56.0	21.6	-0.4	-14%
Fdm Group	Industrials	United Kingdom	0.6	51.0	19.4	-0.7	-68%
Big Technologies	Technology	United Kingdom	0.5	15.4	20.7	-3.0	-54%
Cph Chemie+Papier Hldg.	Basic Materials	Switzerland	0.5	18.9	16.5	-1.9	43%
Sfc Energy	Energy	Germany	0.4	20.2	37.8	-1.9	-16%
Niox Group	Health Care	United Kingdom	0.4	11.5	25.2	-1.3	62%
Elixirr International	Industrials	United Kingdom	0.3	16.0	14.6	-0.4	-24%
Almawave	Technology	Italy	0.1	14.3	12.7	-0.3	-21%
Median			1.7	17.4	20.5	-0.4	-18%

Source: Datastream, FactSet, Goldman Sachs Global Investment Research

**Exhibit 24: Our LBO Candidates Screen for SMIDs - Low ROE Stocks**

Screen consists of 50 European stocks

Name	Industry	Country	Market Cap (€ bn)	ROE (%)	NTM PE	ND/EBITDA	Rel. Perf. since 2022 (€)
Volvo Car	Consumer Discretionary	Sweden	8.3	10.3	4.9	-0.5	-63%
Land Securities Group	Real Estate	United Kingdom	5.6	-4.8	13.3	7.7	-23%
Allfunds Group	Financials	United Kingdom	3.6	3.6	13.9	-4.5	-69%
1&1	Telecommunications	Germany	3.1	5.2	9.6	0.3	-32%
Thyssenkrupp	Industrials	Germany	3.0	-19.1	5.9	-2.5	-53%
Valeo	Consumer Discretionary	France	2.9	6.0	7.3	1.3	-59%
Ubisoft Entertainment Cat	Consumer Discretionary	France	2.7	9.4	13.0	1.1	-54%
Ebro Foods	Consumer Staples	Spain	2.4	8.6	12.9	0.8	-12%
MFE	Consumer Discretionary	Italy	1.9	7.6	7.9	1.0	-40%
Quilter	Financials	United Kingdom	1.9	2.7	11.9	-8.6	-26%
TF1	Consumer Discretionary	France	1.9	10.0	7.8	-0.7	-5%
Playtech	Consumer Discretionary	United Kingdom	1.7	5.9	9.3	0.8	-41%
Centamin	Basic Materials	United Kingdom	1.7	6.9	10.0	-0.2	28%
Hammerson	Real Estate	United Kingdom	1.6	-2.0	13.7	7.7	-23%
Breedon Group	Industrials	United Kingdom	1.6	9.8	11.7	0.6	-23%
Vesuvius	Industrials	United Kingdom	1.5	9.4	9.8	0.8	-2%
Stabilus	Industrials	Germany	1.4	11.2	11.4	0.4	-18%
Assura	Real Estate	United Kingdom	1.4	-10.8	12.0	8.2	-47%
TGS	Energy	Norway	1.4	1.1	10.1	-0.2	19%
Salzgitter	Basic Materials	Germany	1.3	4.1	7.0	0.5	-34%
Naturenergie Holding	Utilities	Switzerland	1.3	11.0	10.3	-0.1	-18%
Kontron	Technology	Germany	1.3	11.9	11.8	-0.3	31%
Eurocommercial Properties	Real Estate	Netherlands	1.2	-0.6	9.3	8.3	13%
Barco New	Technology	Belgium	1.2	10.3	12.4	-1.6	-37%
Supermarket Income Reit	Real Estate	United Kingdom	1.1	0.3	12.1	6.4	-45%
Hochschild Mining	Basic Materials	United Kingdom	1.0	-8.6	9.0	0.7	22%
Hellofresh	Consumer Staples	Germany	1.0	-4.2	9.9	0.7	-92%
SGL Carbon	Basic Materials	Germany	0.9	6.4	11.4	0.6	-15%
Sigmaroc	Industrials	United Kingdom	0.8	2.8	8.3	0.8	-29%
Glenveagh Properties	Consumer Discretionary	Ireland	0.8	6.9	7.9	0.4	3%
RWS Holdings	Industrials	United Kingdom	0.8	-2.7	7.8	0.1	-74%
Bpost	Industrials	Belgium	0.7	5.6	5.4	0.8	-60%
IP Group	Financials	United Kingdom	0.6	-13.3	12.8	-1.6	-62%
NRJ Group	Consumer Discretionary	France	0.6	6.5	13.0	-3.4	29%
Sipef	Consumer Staples	Belgium	0.6	8.7	10.1	0.2	-6%
Brunel Intl.	Industrials	Netherlands	0.6	10.4	11.7	0.1	-9%
PZ Cussons	Consumer Staples	United Kingdom	0.6	-9.9	13.7	0.1	-51%
Jupiter Fund Management	Financials	United Kingdom	0.5	-1.6	8.8	-4.7	-69%
Team 17 Group	Consumer Discretionary	United Kingdom	0.5	-1.5	12.6	-0.9	-65%
Exmar	Industrials	Belgium	0.5	11.2	15.6	0.9	75%
Warehouse Reit	Real Estate	United Kingdom	0.4	-21.5	14.2	8.2	-57%
Gore Street En.Strg.Fd.	Financials	United Kingdom	0.4	8.1	6.7	-2.6	-49%
Deceuninck Ech	Industrials	Belgium	0.4	3.1	8.4	0.6	-29%
Medios	Health Care	Germany	0.3	3.9	9.3	-0.6	-65%
On The Beach Group	Consumer Discretionary	United Kingdom	0.3	9.8	8.7	-4.0	-56%
Forfarmers	Consumer Staples	Netherlands	0.2	-0.3	8.9	0.7	-38%
Groupe Partouche	Consumer Discretionary	France	0.2	5.4	12.6	1.4	4%
Groupe Sfp	Consumer Discretionary	France	0.2	0.5	7.9	-0.4	-47%
Rosetti Marino	Energy	Italy	0.2	5.7	7.3	-0.5	17%
Whats Cooking	Consumer Staples	Belgium	0.1	6.3	9.4	1.1	-40%
Median			1.1	5.5	9.9	0.4	-33%

Source: Datastream, FactSet, Goldman Sachs Global Investment Research

**2. Real Estate and Technology: small sectors set to rally the most as bond yields will fall**

During the first two weeks of May, **German bond yields have fallen more than 20bp and European small caps have outperformed. Sectors rallying the most have been similar among small and large caps: Real Estate, Technology, Utilities and Telecoms**, i.e. sectors with weak balance sheets, or long duration (Technology).

We include two tables highlighting Small caps Tech and Real Estate companies ([Exhibit 25](#), [Exhibit 26](#)). We also include a screen of German small caps, which are overweight Technology, and have underperformed other European small Technology companies ([Exhibit 30](#)).

[Exhibit 32](#) shows YTD sector returns within small caps and the SXXP: Banks have driven

stock returns of Small caps and the SXXP since the beginning of the year. However, Technology is very different among large and small caps: it's been the worst performing sector among small caps (Aixtron, Soitec, Teamviewer), and the best performing one among the SXXP (ASM International, Prosus, SAP). Small healthcare stocks are also among the weakest while they rank among the strongest among the SXXP. By contrast, small Telecoms and Utilities companies have performed better than their large counterparts.

#### Exhibit 25: Real Estate Small Caps rallied the most when bond yields fell in early May

STOXX 200 Small Real Estate. Market Cap and Performance in EUR

Name	Country	Market Cap (€ bn)	NTM PE	Net Debt / Equity	YTD Perf
Hemnet Group	Sweden	2.3	43.6	20.2	15%
Londonmetric Property	United Kingdom	4.8	15.2	2.2	7%
Merlin Properties Reit	Spain	5.1	17.3	0.8	7%
Tag Immobilien	Germany	2.5	14.1	0.9	5%
British Land	United Kingdom	4.5	14.6	0.7	4%
Big Yellow Group	United Kingdom	2.9	21.2	1.0	4%
Safestore Holdings	United Kingdom	2.3	18.3	1.0	2%
Covivio	France	5.5	11.5	0.7	2%
Wihlborgs Fastigheter	Sweden	2.6	17.2	1.3	1%
Derwent London	United Kingdom	3.0	21.7	0.7	-1%
Fastighets Balder	Sweden	6.8	14.4	0.9	-4%
Tritax Big Box Reit	United Kingdom	4.5	17.9	1.2	-6%
Aedifica	Belgium	2.8	12.5	0.8	-7%
Allreal Holding	Switzerland	2.5	20.5	0.9	-7%
Wallenstam	Sweden	2.6	29.9	1.0	-9%
Unite Group	United Kingdom	4.8	19.8	1.0	-10%
Kojamo	Finland	2.5	17.2	0.7	-15%
Cofinimmo	Belgium	2.2	9.3	0.6	-16%
Fabege	Sweden	2.6	21.0	0.7	-20%
<b>Median</b>		<b>2.8</b>	<b>17.3</b>	<b>0.9</b>	<b>-1%</b>

Source: FactSet, Datastream, Goldman Sachs Global Investment Research

#### Exhibit 26: Tech Small Caps are YTD laggards and rallied the most when bond yields fell early May

STOXX 200 Small Technology. Market Cap and Performance in EUR

Name	Country	Market Cap (€ bn)	NTM PE	Net Debt / Equity	YTD Perf
Softcat	United Kingdom	4.0	27.2	13.7	29%
Lagercrantz Group	Sweden	3.1	34.0	10.2	28%
Comet Holdings	Switzerland	2.6	43.6	8.3	19%
Reply	Italy	5.1	23.1	4.6	15%
Sopra Steria Group	France	4.6	11.2	2.5	13%
Fortnox AB	Sweden	3.5	51.8	22.3	7%
Bechtle	Germany	6.0	20.3	3.4	4%
Computacenter	United Kingdom	3.8	15.7	3.5	4%
Just Eat Takeaway	Netherlands	2.7	NM	0.5	-9%
Tietoenvy	Finland	2.3	8.9	1.4	-11%
Teamviewer	Germany	2.1	12.2	25.3	-14%
Soitec	France	4.0	24.0	2.6	-31%
Aixtron	Germany	2.6	17.1	3.3	-41%
<b>Median</b>		<b>3.5</b>	<b>21.7</b>	<b>3.5</b>	<b>4%</b>

Source: FactSet, Datastream, Goldman Sachs Global Investment Research

### 3. UK small caps: the catch-up trade

Since the beginning of the year, **German, Belgium and UK small caps are the bottom 3 performing countries**. By contrast, Danish, Italian and Norwegian small caps are the top 3 performing countries and have outperformed the STOXX Europe 600.

#### When and if bond yields fall, we believe that the FTSE 250 has scope to catch up.

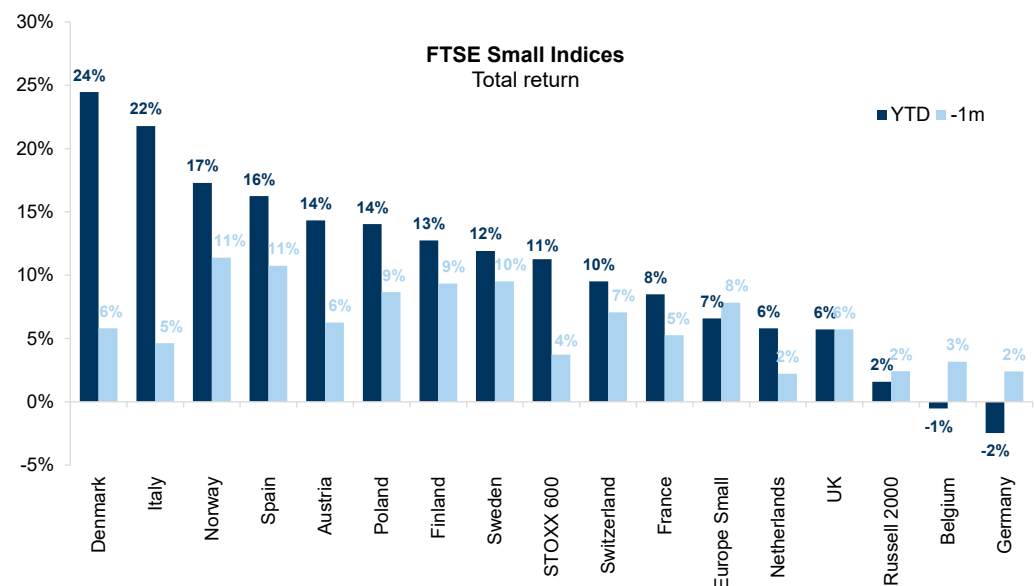
For now, our economists have pushed their first BoE rate cut expectation from June to August. The FTSE 250 is down 12% since the end of 2021, when interest rates started to rise, while Euro area Small caps (SCXE Index) are down 5%. The FTSE 250 has derated by 26pp since then, versus 22pp for Euro area small caps.

UK economic activity has been improving from a low base, positioning is light, and our FX strategists expect GBP/USD to be stable at 1.28 in 12 months (a positive for domestic stocks versus a depreciation). In addition, the FTSE 250 is overweight Real Estate compared with other Small caps, and Consumer discretionary, two sectors which should do well with lower bond yields and a drop in the saving rate. See UK Weekly Kickstart - FTSE 250: The Catch-up Trade, 5 April 2024.

Our Equity analysts' Buy-rated names in the FTSE 250 are Aston Martin, WH Smith, Watches of Switzerland, Direct Line, Man, Supermarket Income REIT, Tritax Big Box, Hiscox, Derwent London, Big Yellow, with a median upside of 30%.

#### Exhibit 27: Danish, Italian, Norwegian, Spanish and Polish small caps are the top 5 performing countries and have outperformed the STOXX Europe 600

YTD and 1-month total return. FTSE Small Cap country indices and SXXP



Source: Datastream, Goldman Sachs Global Investment Research

### Decomposing country performance

Looking at the sector composition of these small cap indices, and the performance of these sectors, we

find that:

- **German small caps have underperformed due to their underweight in Banks** (best performing sector YTD among small caps, included German small banks), **and their overweight in Healthcare, Real Estate and Technology**, 3 sectors which underperformed among European small caps (note that Healthcare and Tech outperformed among large caps). German Healthcare and Tech names underperformed more than other European small caps. We include a screen of German small caps ([Exhibit 30](#)).
- **UK Small caps underperformed due to their overweight in Consumer discretionary**, which underperformed among UK small caps (not among European small caps). Tech and Healthcare UK small caps also considerably underperformed other European small caps.
- **Italian and Spanish small caps have outperformed thanks to their overweight in Banks**. Italian small banks have done much better than others.
- **Danish and Norwegian small caps have outperformed thanks to their overweight in Industrials**, and their companies have done much better than other Industrials in Europe.

#### Exhibit 28: Italian small caps are overweight in Banks

Sector Composition for FTSE Small Cap country indices and STOXX 200 Small

Sector	Denmark	Italy	Norway	UK	Belgium	Germany	Europe
Basic Materials	NM	2%	5%	3%	8%	12%	5%
Consumer Discretionary	NM	16%	0%	20%	2%	11%	13%
Consumer Staples	9%	0%	10%	7%	10%	5%	6%
Energy	NM	6%	24%	3%	0%	4%	4%
Financials	28%	48%	18%	17%	9%	5%	17%
Health Care	33%	0%	0%	2%	4%	12%	7%
Industrials	28%	18%	34%	26%	15%	15%	26%
Real Estate	NM	0%	1%	13%	38%	7%	9%
Technology	3%	4%	8%	7%	9%	19%	9%
Telecommunications	NM	0%	0%	1%	4%	5%	2%
Utilities	NM	6%	0%	2%	0%	5%	2%
<b>Total</b>	<b>100.0%</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>

Belgium includes Luxembourg small caps

Source: FactSet, Goldman Sachs Global Investment Research

#### Exhibit 29: The outperformance of Danish and Norwegian small caps owes to Industrials, that of Italian to Banks, and Tech has dragged German small caps

FTSE Small Cap YTD total return (local currency)

Sector	Denmark	Italy	Norway	UK	Belgium	Germany	Europe small	STOXX 600
Basic Materials	NM	13%	14%	11%	-5%	-2%	5%	8%
Consumer Discretionary	NM	9%	NM	0%	-12%	-3%	2%	10%
Consumer Staples	29%	7%	16%	14%	14%	-13%	9%	3%
Energy	NM	42%	14%	6%	NM	5%	11%	12%
Financials	18%	39%	23%	10%	10%	28%	17%	16%
Health Care	34%	NM	NM	-8%	13%	-8%	6%	12%
Industrials	20%	17%	29%	11%	6%	15%	14%	13%
Real Estate	NM	NM	-4%	0%	-2%	-2%	-1%	3%
Technology	37%	-10%	12%	15%	-11%	-11%	1%	16%
Telecommunications	NM	NM	NM	28%	-3%	-2%	6%	6%
Utilities	NM	-4%	NM	-7%	NM	2%	-6%	2%
<b>Total</b>	<b>25%</b>	<b>23%</b>	<b>19%</b>	<b>7%</b>	<b>0%</b>	<b>-2%</b>	<b>8%</b>	<b>11%</b>

Belgium includes Luxembourg small caps

Source: FactSet, Goldman Sachs Global Investment Research

**Exhibit 30: Germany Small Caps have lagged both YTD and in the last month**

STOXX 200 Small Germany. Market Cap and Performance in EUR

Name	Country	Market Cap (€ bn)	NTM PE	Net Debt / Equity	YTD Perf
Cts Eventim	Consumer Discretionary	8.1	27.6	9.0	32%
Rational	Industrials	9.2	38.2	12.5	18%
Kion Group	Industrials	6.1	12.2	1.1	17%
Talanx Aktgfsf.	Financials	19.0	9.9	1.8	16%
Gerresheimer	Health Care	3.7	18.9	2.5	12%
Fuchs Pref.	Basic Materials	3.1	18.2	1.7	11%
Tag Immobilien	Real Estate	2.5	14.1	0.9	5%
Bechtle	Technology	6.0	20.3	3.4	4%
Hochtief	Industrials	8.1	13.0	6.5	3%
Aurubis	Basic Materials	3.4	9.6	0.8	1%
K S N	Basic Materials	2.4	29.7	0.4	-5%
Carl Zeiss Meditec	Health Care	8.3	27.6	3.8	-6%
Wacker Chemie	Basic Materials	5.5	17.0	1.2	-8%
Freenet	Telecommunications	2.7	9.7	1.9	-9%
Lanxess	Basic Materials	2.2	36.7	0.5	-10%
Teamviewer	Technology	2.1	12.2	25.3	-14%
Thyssenkrupp	Industrials	2.9	5.8	0.2	-25%
Boss (Hugo)	Consumer Discretionary	3.4	10.8	2.6	-28%
Aixtron	Technology	2.6	17.1	3.3	-41%
Evotec	Health Care	1.6	NM	1.5	-57%
Hellofresh	Consumer Staples	1.0	11.3	1.0	-60%
<b>Median</b>		<b>3.4</b>	<b>15.6</b>	<b>1.8</b>	<b>-5%</b>

Source: FactSet, Datastream, Goldman Sachs Global Investment Research

**4. GS small caps with the highest upside**

The screen below shows European small caps with the highest upside based on the 12-month price targets of our equity analysts.

**Exhibit 31: GS-covered small cap stocks with the highest upside**

Companies under €2 bn market cap

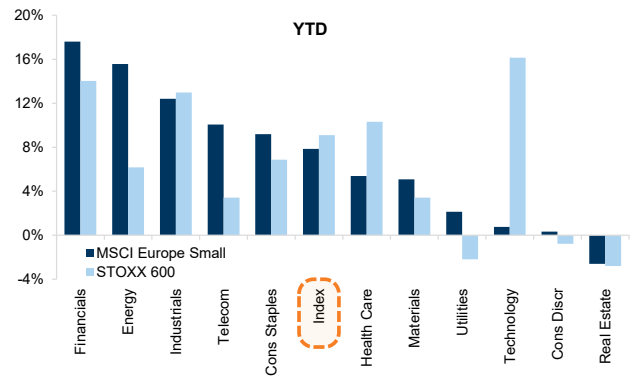
Name	Industry	Country	Price (€)	Market cap (€ bn)	12m Upside	NTM P/E
Aston Martin	Consumer Discretionary	United Kingdom	1.6	1.3	179%	-
ABOUT YOU Holding	Consumer Discretionary	Germany	3.9	0.7	74%	-
AEDAS Homes	Real Estate	Spain	20.2	0.9	71%	9.3
Ferretti	Consumer Discretionary	Italy	3.1	1.0	63%	10.7
Marex Group	Financials	United Kingdom	18.9	1.3	61%	-
BioArctic	Health Care	Sweden	20.2	1.5	51%	96.4
Alamar Foods	Consumer Discretionary	Saudi Arabia	19.7	0.5	49%	24.1
Loomis	Industrials	Sweden	25.5	1.9	49%	9.5
TeamViewer	Technology	Germany	12.2	2.1	48%	14.6
Jahez International	Technology	Saudi Arabia	7.1	1.5	41%	32.9
<b>Median</b>				<b>1.3</b>	<b>56%</b>	<b>14.6</b>

Source: Datastream, Goldman Sachs Global Investment Research



Appendix

**Exhibit 32: Large tech companies have led the rally but small ones underperformed**  
YTD performance



Source: FactSet, Goldman Sachs Global Investment Research

# Disclosure Appendix

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We, Lilia Peytavin, Peter Oppenheimer, Sharon Bell, Guillaume Jaisson and Marcus von Scheele, hereby certify that all of the views expressed in this report accurately reflect our personal views, which have not been influenced by considerations of the firm's business or client relationships.

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