

DOES YOUR MID-CAP INDEX MEASURE UP?

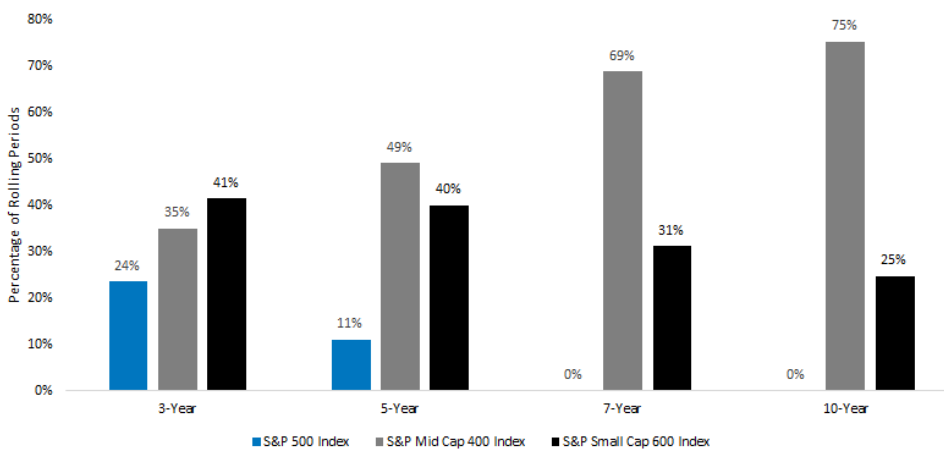
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We frequently discuss allocations that focus on large caps, small caps and all sorts of different [factor](#) exposures. Considering the persistence of their outperformance, we don't tend to hear enough about mid-caps.

Size Spectrum Analysis for Standard & Poor's Size Cuts

To define that persistence of outperformance, we looked at rolling periods of average annual returns.

Was There Any Consistency of Leadership Across Large Caps, Mid-Caps or Small Caps?



Sources: WisdomTree, Bloomberg, with data from 10/31/1994 to 3/31/2017, due to the live calculation for the S&P SmallCap 600 Index beginning on 10/28/94. Past performance is not indicative of future results. You cannot invest directly in an index. Percentage of Rolling Periods of Specified Lengths in Which the Index of Large Caps (S&P 500 Index), Mid-Caps (S&P MidCap 400 Index) or Small Caps (S&P SmallCap 600 Index) Was the Top-Performing Size Segment.

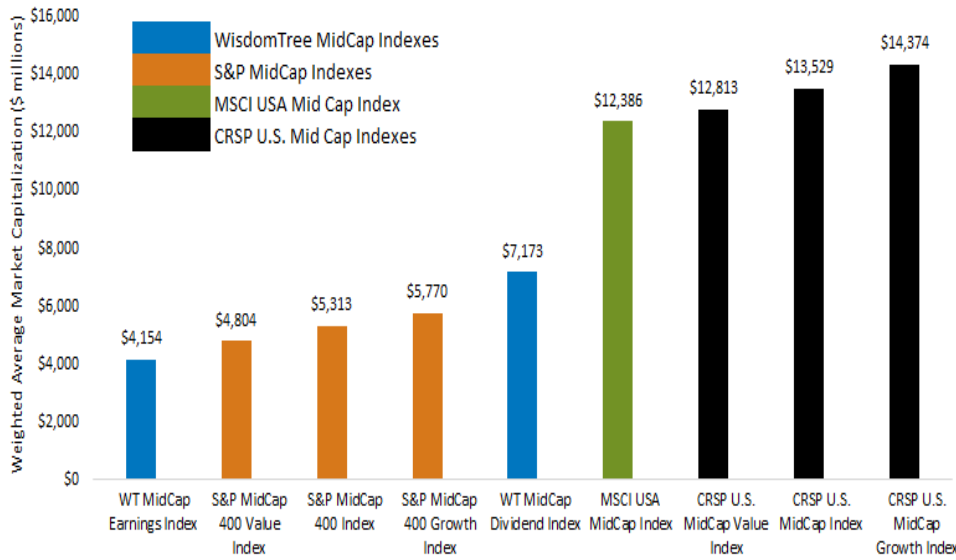
For definitions of indexes in the chart, visit our [glossary](#).

- The S&P analysis indicated an advantage to the [S&P MidCap 400 Index](#) over the rolling 5-, 7- and 10-year periods. The longer the horizon, the greater the apparent persistence of this result.

What Is a Mid-Cap, Anyway?

There are no universally accepted definitions for large caps, mid-caps or small caps. WisdomTree's view is that stocks with [market capitalizations](#) below \$2 billion constitute small caps, while stocks between \$2 billion and \$10 billion constitute mid-caps and stocks above \$10 billion constitute large caps. [We recently published a similar analysis for small-cap indexes.](#)

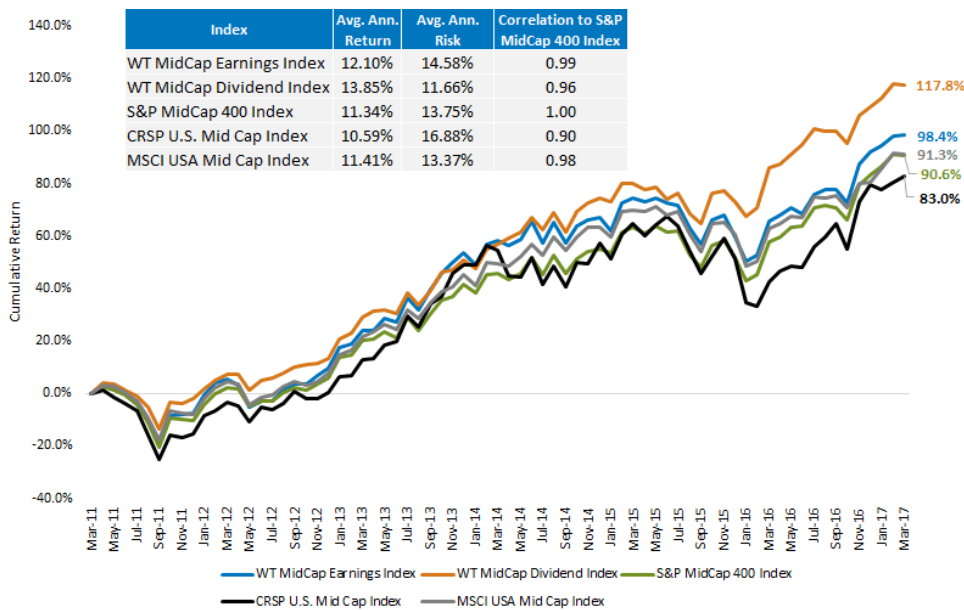
How Different Are Commonly Followed U.S. Mid-Cap Indexes?



Sources: WisdomTree, Bloomberg, with data as of 3/31/17. Due to data access, Russell indexes are not shown. You cannot invest directly in an index.

- Weighted Average Market Capitalization:** This is an important metric to consider, in that it combines the actual market capitalization size of the firms with the weighting mechanism of the indexes. The [WisdomTree MidCap Earnings Index](#) is weighted by earnings, whereas the [WisdomTree MidCap Dividend Index](#) is weighted by dividends. Stocks that are 1) included and then 2) weighted more highly would have the greatest influence.
- WisdomTree MidCap Earnings Index Was the Smallest Among Mid-Caps:** In terms of weighted average market capitalization, the WisdomTree MidCap Earnings Index was the smallest, at approximately \$4.2 billion.
- WisdomTree & S&P MidCap 400 Indexes:** It's clear to us that the WisdomTree Indexes and the S&P MidCap 400 indexes shown in this chart all generally find themselves in that "between \$2 billion and \$10 billion" category. This is distinctly different than the MSCI and CRSP indexes—notable in that the CRSP indexes have weighted average market capitalizations approaching the \$13 billion to \$14 billion range.

Does Size Exposure Matter in Mid-Caps?



Sources: WisdomTree, Bloomberg, with period start determined by the 3/31/11 start of live calculation for the CRSP indexes. Past performance is not indicative of future results. You cannot invest directly in an index.

- 35% Spread in Cumulative Performance:** What this 35% really tells us is not which of the mid-cap indexes shown will outperform over the next six years—as that is impossible to know today—but rather that the selection of the mid-cap index is enormously important. All of these indexes have “mid-cap” in their name, but as is clearly shown, performance was quite different.
- Measuring Exposure to the Asset Class:** In our experience, clients tend to put a lot of work into determining their asset allocation frameworks. If mid-cap equities in the U.S. are decided upon, it’s important to select an exposure that actually generates that return experience. It’s interesting that the [CRSP U.S. Mid Cap Index](#) had a .90 correlation of monthly returns to the S&P MidCap 400 Index over this period—both indexes are market capitalization-weighted and both seek to generate broad exposure to U.S. mid-caps. The WisdomTree MidCap Dividend Index, which includes solely mid-cap dividend payers, had a significantly higher correlation with this important benchmark, measured at .96 over this period.

WisdomTree’s Indexes Hit 10 Years of Live History

If people asked us what our strongest mid-cap strategy would be if the corporate tax reform proposed by President Trump passes in some version, we would cite the WisdomTree MidCap Earnings Index. This Index has 10 years of live calculation and includes only profitable companies—in other words, the ones that would benefit from a reduction in taxes as opposed to those with negative earnings. It also addresses one of the key challenges in the market place today—that many feel the market is selling at high valuations—This Index has a [price-to-earnings \(P/E\) ratio](#) today of 17–18x that could see a reduction to range of 14–15x under a corporate tax reduction scenario. Why the reduction? Tax cuts would lead to earnings growth.

The WisdomTree MidCap Dividend Index also has been a steady generator of strong returns for almost 11 years. In our opinion, it has been a “category creator,” fulfilling an income-generating need in a low interest rate environment within mid-cap stocks. Prior to this strategy’s existence, dividends were thought to be a large-cap equity phenomenon.

For standardized performance and the most recent month-end performance click [here](#) NOTE, this material is intended for electronic use only. Individuals who intend to print and physically deliver to an investor must print the monthly performance report to accompany this blog.

For more investing insights, check out our [Economic & Market Outlook](#)

View the online version of this article [here](#).

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You cannot invest directly in an index.

DEFINITIONS

Factor : Attributes that based on its fundamentals or share price behavior, are associated with higher return.

S&P MidCap 400 Index : provides investors with a benchmark for mid-sized companies. The index covers over 7% of the U.S. equity market, and seeks to remain an accurate measure of mid-sized companies, reflecting the risk and return characteristics of the broader mid-cap universe on an on-going basis.

Market Capitalization : Market cap = share prices x number of shares outstanding. Firms with the highest values receive the highest weights in approaches designed to weight firms by market cap.

Dividend : A portion of corporate profits paid out to shareholders.

CRSP U.S. Mid Cap Index : Market capitalization-weighted measure of the performance of mid cap equities within the United States.

Correlation : Statistical measure of how two sets of returns move in relation to each other. Correlation coefficients range from -1 to 1. A correlation of 1 means the two subjects of analysis move in lockstep with each other. A correlation of -1 means the two subjects of analysis have moved in exactly the opposite direction.

Price-to-earnings (P/E) ratio : Share price divided by earnings per share. Lower numbers indicate an ability to access greater amounts of earnings per dollar invested.