



## THE MISSING PIECE | Mid Caps

# Growth Potential of Mid Caps

An advantage of investing in mid-cap stocks is that midsized companies may still have plenty of growth potential. Mid-caps can give investors a way to gain an early position in companies that might become tomorrow's blue-chip stocks. Since growth often drives share price, it's not surprising that this asset class has done well over the years. Mid-caps historically have outperformed other asset classes since the inception of the Russell indices in 1979 (see Figure 1).<sup>1</sup>

"Mid-cap managers are well-schooled in developing strategic long-term plans, versus being focused on short-term gains," says Christopher Sassouni, D.M.D., Eagle Asset Management Portfolio Co-Manager. "At the same time, they can be more nimble than large-cap managers, who may require more time to effect change. Mid-cap managers also are focused on creating shareholder value over raising cash. It's the quality of the management teams that I believe contributes to the relative historical outperformance of mid-cap stocks compared to small-caps."<sup>2</sup>

## ATTRACTIVE ACQUISITIONS?

Midsized companies can also become attractive targets for acquisition by larger companies. It's often easier for companies to purchase a particular innovation or product line through acquisition than it is to build that competency internally.

"Mid-cap companies tend to have fewer lines of business than large-caps, which allows management teams to focus their attention," says John Indellicate, CFA, Scout Investments Portfolio Co-Manager. "We believe this focus is also a contributor to why mid-cap companies get acquired at similar rates to small-cap companies, adding to the historical outperformance of mid-cap stocks. Mid-cap balance sheets are generally stronger than those of small-caps, and historically mid-caps have exhibited faster cash flow growth than large- and small-caps."<sup>3</sup>

## TAX CUTS SPUR GROWTH

Another key factor favorable for mid-cap growth was the federal government's passage of corporate tax cuts. The tax cuts freed up cash flow that has been used for two important drivers of growth: share buybacks and capital expenditures.

The corporate tax cuts made it attractive for companies to buy back shares of their own stock. These buybacks may help investors because they increase one key measure of a stock's success – earnings per share.



Figure 1. As of 6/30/2019. Source: Morningstar Direct

\* Small Cap: Russell 2000® Index  
 SMID Cap: Russell 2500™ Index  
 Mid Cap: Russell Midcap® Index  
 Large Cap: Russell Top 200® Index

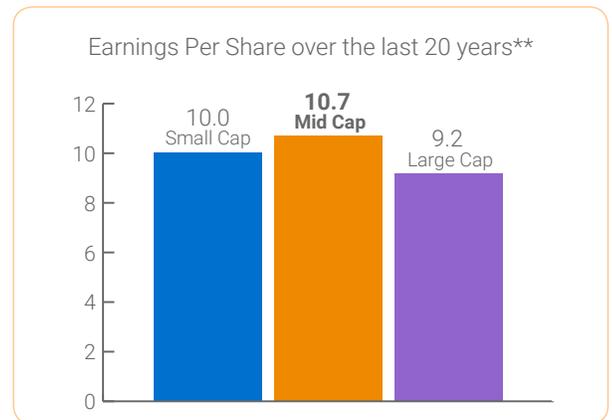


Figure 2. As of 3/29/2019. Source: FactSet

\*\* Small Cap: Russell 2000® Index  
 Mid Cap: Russell Midcap® Index  
 Large Cap: Russell 1000® Index

Based simply on supply and demand, this buyback reduces supply, thus increasing demand which can drive the share price higher. Buybacks for the S&P 500® reached record levels in 2018 and are on pace to set new records in 2019.<sup>4</sup>

In addition, U.S. companies are finally investing not just to maintain, but also to expand capacity. U.S. capital expenditures initially jumped dramatically just prior to the corporate tax cuts to levels not seen since the late 1980s (see Figure 3). Capital expenditures have since dropped to a historically normal range.

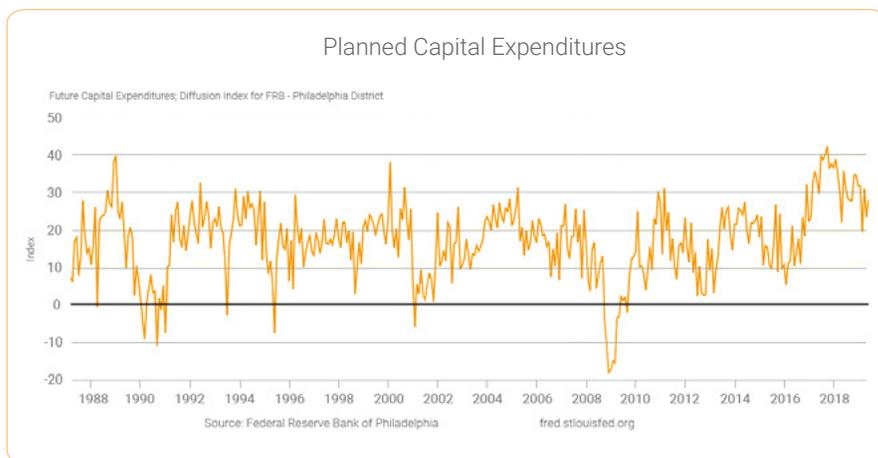


Figure 3. Source: Federal Reserve Bank of Philadelphia

In a nutshell, investors can use mid-caps to help solve the puzzle of growth potential while owning an asset class that has historically provided outperformance. If you are seeking to diversify your portfolio across small, midsized and large companies, mid-caps might deserve a closer look.

<sup>1</sup>As represented by the Russell 2000® Index, the Russell Midcap® Index and the Russell 1000® Index.

<sup>2,3</sup>2019 Mid Cap Outlook | Innovation, Trade, and Timing." Copyright 2019 Carillon Tower Advisers. Accessed July 26, 2019.

[https://www.carillontower.com/-/media/rj/affiliate-sites/carillon-tower/insights-and-commentary/pdfs/2019\\_mid\\_cap\\_outlook.pdf](https://www.carillontower.com/-/media/rj/affiliate-sites/carillon-tower/insights-and-commentary/pdfs/2019_mid_cap_outlook.pdf)

<sup>4</sup>Erney, R. "Stock Buybacks Surge." Kiplinger. May 9, 2019. Accessed July 26, 2019. <https://www.kiplinger.com/article/investing/T052-C000-S002-stock-buybacks-surge.html>.

**Risk Considerations:** Investing in mid-sized companies is based on the premise that relatively smaller companies will increase their earnings and grow into larger, more valuable companies. Historically, mid-cap stocks have experienced greater volatility than other equity asset classes, and they may be less liquid than larger cap stocks. Thus, relative to larger, more liquid stocks, investing in mid-cap stocks involves potentially greater volatility and risk. In addition, mid-cap stocks have experienced greater volatility than other classes of securities. Mid-cap stocks can also be less liquid than those of large companies, and illiquidity increases the potential for volatility. As with all equity investing, there is the risk that a company will not achieve its expected earnings results, or that an unexpected change in the market or within the company will occur, both of which may adversely affect investment results. The biggest risk of equity investing is that returns can fluctuate and investors can lose money.

Past performance does not guarantee or indicate future results. The information presented is for illustrative purposes only and should not be used as the sole basis for an investment decision. This information should not be construed as a recommendation to buy, sell or hold any particular security. Investors cannot invest directly in an index and unmanaged index returns do not reflect any fees, expenses or sales charges.

Contact us for more information on our active mid-cap solutions.

Financial professionals: 800.521.1195 | Investing public: contact your financial advisor | [carillontower.com](http://carillontower.com)

**CARILLON**  
TOWER ADVISERS

880 Carillon Parkway | St. Petersburg, FL 33716

CFD19-0446 Exp. 10/31/2019

Carillon Tower Advisers, Inc. is the investment advisor.

©2019 Carillon Tower Advisers, Inc. All rights reserved.

Carillon Fund Distributors, Inc., Member FINRA