



## SMALL CAP ADVANTAGE

### Portfolio Comments

March 31, 2024

#### Distinguishing Features

GIM builds the [Small Cap Advantage](#) portfolio from the bottom-up; sector weightings are secondary to stock selection. As of March 31, 2024, the Small Cap Advantage portfolio was overweight its Russell 2000 Growth benchmark in Technology, Health Care, Real Estate, and Financials. We are equal weight in Utilities and Basic Materials and underweight the benchmark in all other sectors. The portfolio has no exposure to Energy or Consumer Staples.

#### Commentary

##### Market Environment

Recent economic data highlight that the U.S. economy remains resilient. Commodity prices and yields have increased in response to the underlying strength of the economy. Geopolitical risks have risen as trade tensions with China have increased and the continuation of conflicts in Ukraine and Israel cause trepidation. These dynamics have created volatility within the financial markets especially as investors debate the Federal Reserve’s position on inflation, and when and whether they will cut rates. A strong job market and elevated wage inflation could delay the Federal Reserve’s first cut in interest rates from current expectations for a June cut. While small caps saw a meaningful recovery off the October lows, we expect continued volatility until there is more clarity on the economy.

Given the economic strength, the strongest performing sectors in the quarter were Technology, Energy, and Industrials. Without a doubt, the most notable storyline this quarter centered around two Technology companies, Super Micro Computers (SMCI) and Micro Strategy (MSTR), representing the largest single-stock weights ever in the Russell 2000 Growth Index and the largest combined weight of any two stocks ever. These two stocks drove about half of the performance of the Index: SMCI driven by AI demand and MSTR a bitcoin play, both with larger market caps. Excluding both companies, the Russell 2000 Growth 1Q24 return would have been + 3.4% versus the actual index return of +7.6%.

##### Performance

The Granahan Small Cap Advantage strategy returned +1.3% in Q1, underperforming the +7.6% return of its Russell 2000 Growth benchmark. Selection in Financials, Utilities, and Real Estate contributed positively for the quarter along with our overweight in Technology, but it was not enough to outweigh the penalties from stock selection in Technology, Health Care, Consumer Discretionary, and Industrials.

With respect to LifeCycles this quarter, Core Growth, Special Situation, and Pioneer categories all lagged.

#### Top Contributors

1. Kinsale Capital (Financials, Core Growth)
2. Edgewise Therapeutics (Health Care, Pioneer)
3. Toast (Technology, Pioneer)
4. Pure Storage (Technology, Core Growth)
5. Zeta Global Holdings (Financials, Pioneer)

#### Top Detractors

1. 10x Genomics (Health Care, Pioneer)
2. Genius Sports (Industrials, Pioneer)
3. Smartsheet (Technology, Pioneer)
4. Globant (Technology, Core Growth)
5. SI-BONE (Health Care, Pioneer)



## **Outlook**

Since Granahan's inception in 1985, relative valuation of small cap companies versus large has only been lower one other time, which was at the bottom of the Covid bear market. Despite the recent rise in yields adding pressure to small cap growth stocks, fundamentals in the companies we own remain compelling, with the prospect of normalizing interest rates and improving financial conditions providing an additional tailwind for performance. We believe this supports a strong growth outlook over the next couple of years.

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