FTSE Russell
An LSEG Business

Russell US Indexes Spotlight

QUARTERLY REPORT: **APRIL 2023** FOR PROFESSIONAL INVESTORS ONLY

Large-cap and Growth stocks offer refuge from Q1 risk-off storms

Large-caps and Growth dominated US market gains in Q1, with most of their outperformance coming amid a massive flight from risk triggered by serial US bank failures in March, as investors flocked to Tech and other sectors perceived as less vulnerable to potential economic and credit-market shocks. Growth valuations also benefited from the drop in bond yields.

Highlights

Large-caps offer a port in the storm
Stronger rebounds in Tech and Discretionary stocks contributed most to Russell 1000 outperformance vs the Russell 2000 in Q1. (pages 2-4)

Growth shines in March mayhem
Growth trounced Value in Q1, benefiting from the huge rebound in Tech-heavy stocks in March and its lower exposure to selloffs in Financials and Energy. (page 2 & 5)

EPS forecasts drift lower
Forward EPS forecasts continued to see more downgrades than upgrades in Q1, with the Russell 2000 and its style offshoots taking the biggest hits. (page 7-8)

Dividend yields on the rise
Dividend yields have climbed from pandemic lows across the Russell US indexes as corporate profitability has recovered more quickly than stock prices. (page 9)

Valuation re-ratings continue
Forward P/E multiples continued to edge higher across the Russell US indexes amid Q1 price gains. (page 10)

Russell IPOs still in the doldrums
IPO activity remained sluggish in Q1, with the Russell 2000 leading the action. (page 11)

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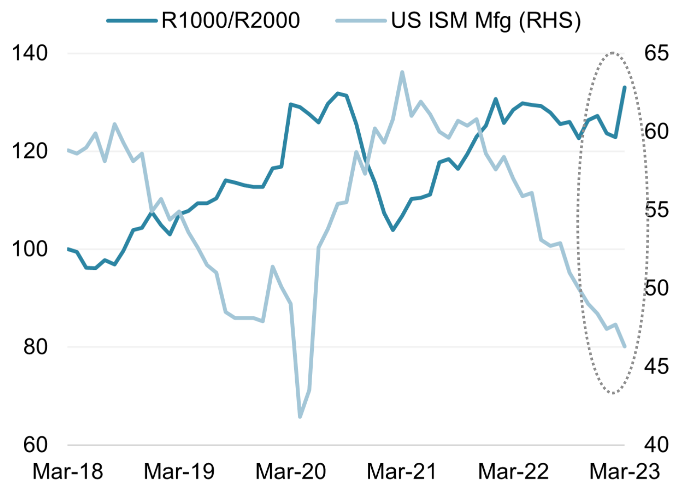
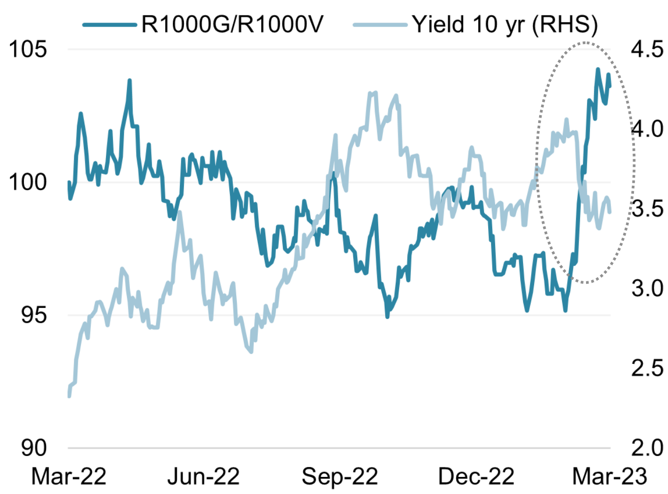
The March banking scare drove a sharp rotation into larger, more economically resilient stocks from more exposed small-cap peers.



Tech-heavy Growth stocks catapulted over financials-tilted Value peers as the banking-sector crisis unfolded in March.



Source: FTSE Russell / Refinitiv. Data as of March 31, 2023. Past performance is no guarantee of future results. This report should not be considered 'research' for the purposes of MIFID II. Please see the end for important legal disclosures. For professional investors only.

Russell US Index Performance – 3M & 12M (%)

Key Observations — First Quarter 2023

US stocks built on their Q4 2022 momentum into the new year, overcoming the ‘higher-for-longer’ rate upheaval in February and a massive flight from risk in March triggered by a series of US bank failures. The Russell 1000 climbed 7.5%, far outstripping the small-cap index’s 2.7% gain, as well as the respective rallies of 6.6% and 3.0% of the FTSE All-World ex US and FTSE Emerging indexes for the quarter. Both size indexes significantly trimmed their 12-month losses, with large-caps making more progress than small-caps (now down 8.4% and 11.6%, respectively).

The Russell 1000 Growth, however, was the hands-down winner of the quarter. The index rose 14.4%, soaring past both Value indexes and small-cap Growth. Amid mounting recession fears, investors piled back into faster-growing companies deemed better able to weather an economic slowdown and potential credit-market stresses — and out of the more cyclical sectors that make up a bigger share of the Value indexes. Growth-stock valuations also benefited from falling interest rates.

The Q1 revival helped most of the style indexes recoup some of their 12-month losses. Russell 1000 Value held its performance edge over its Russell US peers for the longer period, with a decline of 5.9% — or roughly half the double-digit damage endured by the Russell 2000 Value and the two Growth benchmarks.

Chart 1: The Russell 1000 and its Growth offshoot topped the charts in the turbulent Q1 and slashed their 12-month losses. The Russell 2000 and its Value offshoot were the worst performers for the longer period.

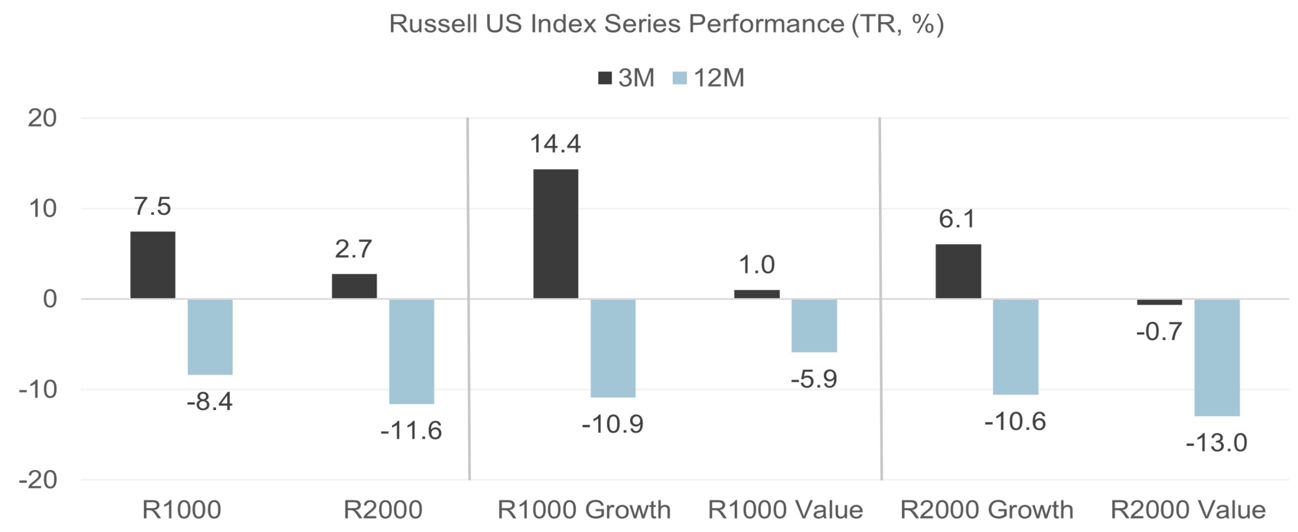
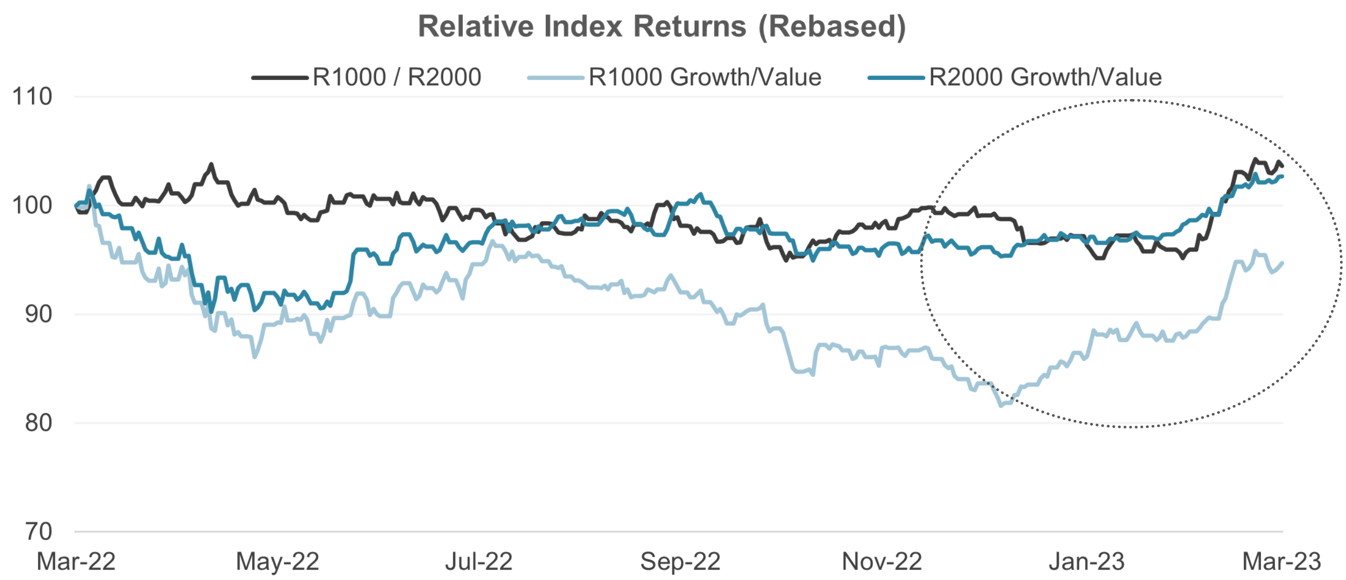


Chart 2: The Russell 1000 outpaced its small-cap peer in Q1, propelled by a robust rebound in growth stocks as investors flocked to sectors deemed better able to withstand an economic slowdown and potential credit-market stresses.



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Macro Drivers – First Quarter 2023

Market anxieties ratcheted to new heights in March as a series of US bank failures ignited fears of a broader financial-market contagion and imminent recession. The US economy's continued resilience in the face of stubbornly high inflation and tighter financial conditions drove dramatic swings in the outlook for rates and future Fed monetary policy.

Though the US Treasury yield curve remain inverted (Chart 1), yields gyrated wildly in Q1, with the 10yr/2yr spread hitting negative 1% in early March at the height of the banking crisis, then recovering by month-end as fears of contagion waned. Worries about the potential economic fallout from lingering credit-market stresses renewed expectations for an earlier end to Fed rate hikes.

Economists continue to expect a sharp slowdown for the US this year and next. However, recent stronger-than-expected economic data prompted many forecasters to raise their GDP growth estimates for 2023, while also lowering their growth expectations for 2024 (Chart 2).

The ISM US Manufacturing Index continued to fall more deeply into contractionary territory (below 50) in Q1 (Chart 3). Weaker economic data, coupled with the banking system pressures that surfaced in March, fueled a robust rotation into large-cap and higher-growth stocks deemed less sensitive to potential economic shocks. Growth valuations also benefited from the recent falloff in bond yields (Chart 4).

Chart 1: While still inverted, the US yield curve flattened slightly with the unfolding banking-sector crisis in March.

Chart 2: Prompted by recent data, economists raised US GDP growth estimates for 2023 but lowered them for 2024.

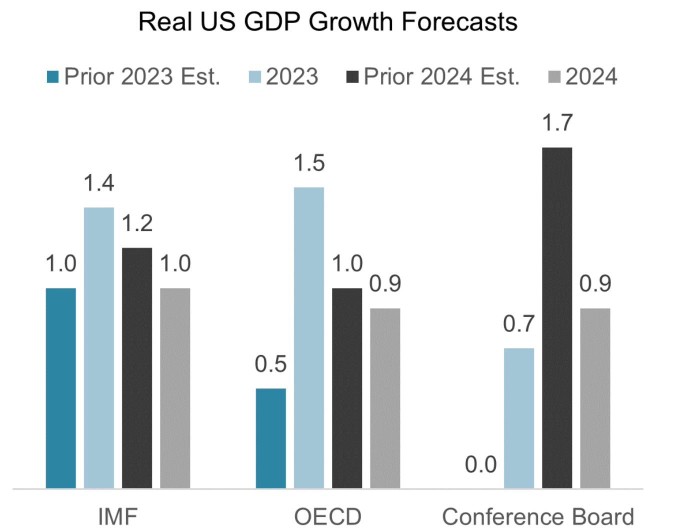


Chart 3: With economic indicators still signaling recession, investors favored larger, less cyclically sensitive stocks.

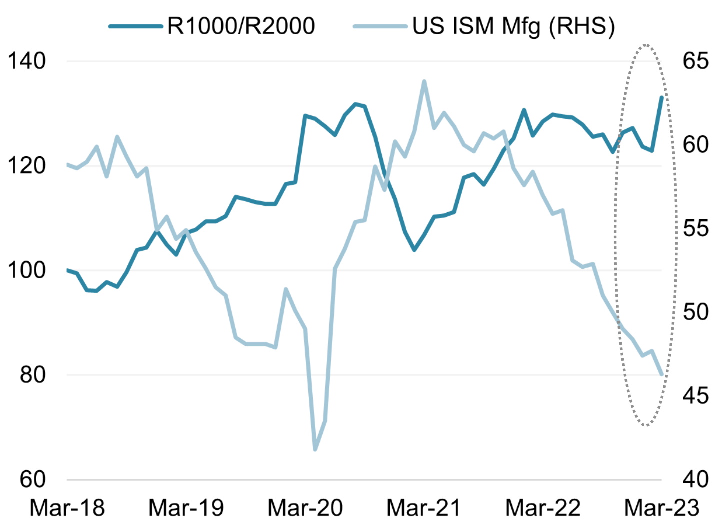
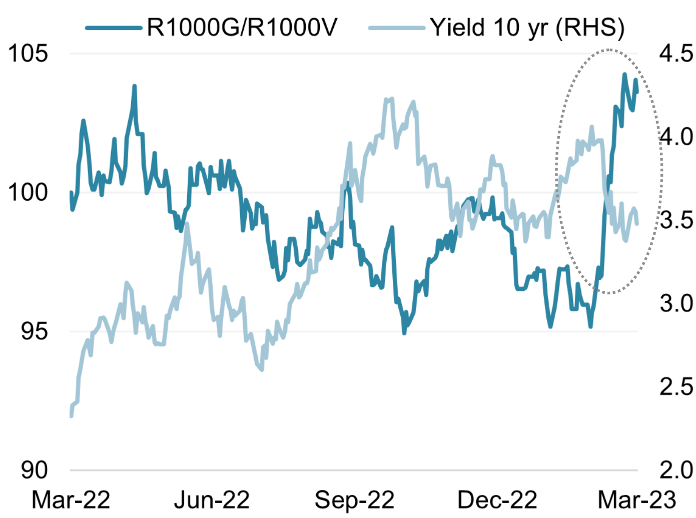


Chart 4: Growth valuations benefitted from the massive 'flight to safety' drop in long bond yields in March.



Source: FTSE Russell / Refinitiv / International Monetary Fund World Economic Outlook Reports / Organization for Economic Cooperation and Development (OECD) and The Conference Board. Data as of March 31, 2023. Past performance is no guarantee of future results. Please see the end for important legal disclosures. For professional investors only.

Industry Returns and Exposures – Russell 1000 & Russell 2000

Key observations

Industry returns diverged widely and narrowed to a few big winners in Q1 2023. Growth-heavy stock groups dominated the gainers, while Financials and Energy dominated the decliners. Losses were bigger for small-cap industries than their large-cap peers for the 12-month period.

- Outperforming Tech, Discretionary and Telecom stocks drove most of Russell 1000's lead vs Russell 2000 in Q1.
- For the 12 months, most large-cap industries held up better than small-cap peers (6 of 11), led by Health Care, Energy and Tech.
- For the quarter, Tech and Discretionary stocks were by far the top performers for both size indexes; Financials, Energy and Health Care stocks were the worst performers for both indexes for the period.
- For the 12 months, large-cap Energy and (less so) Staples were the best performers; Real Estate and Financials suffered the biggest losses, more so for the small-cap index than its large-cap counterpart.

Chart 1: Bigger gains in Tech, Discretionary and Telecom led Russell 1000 outperformance vs the Russell 2000.

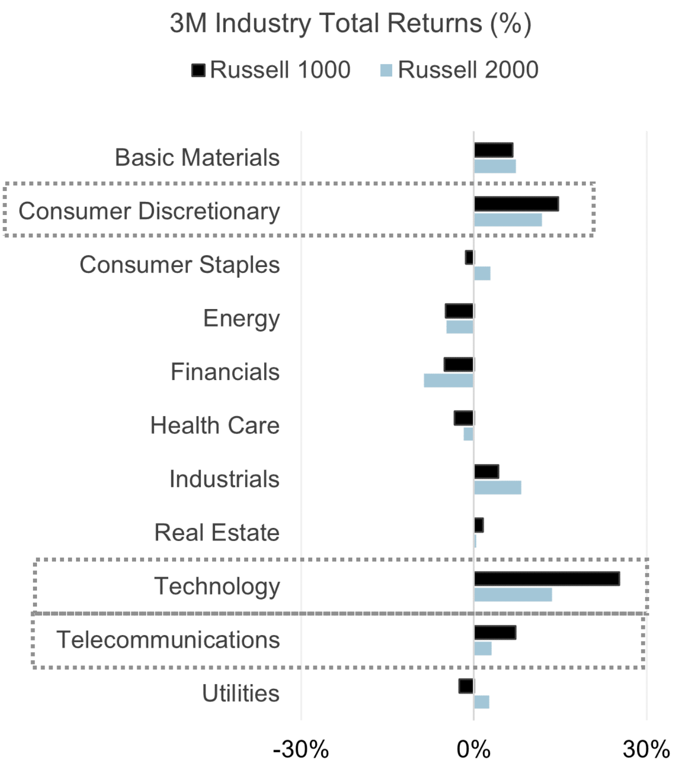
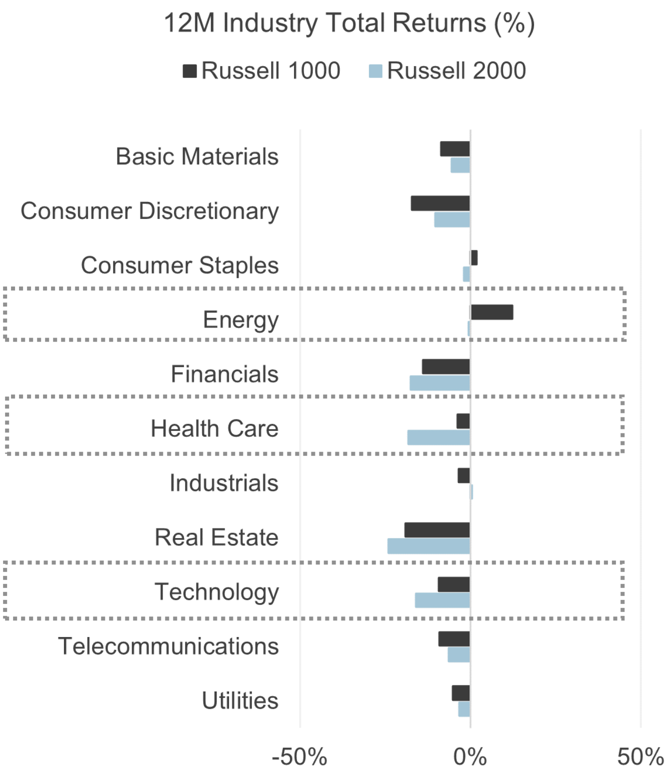
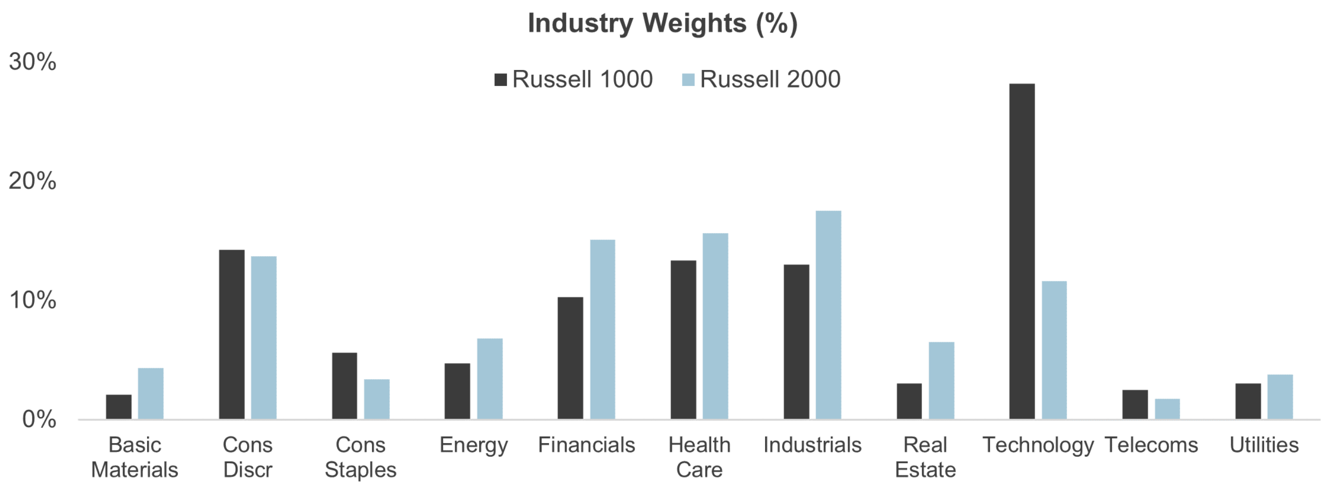


Chart 2: Large-caps fared better than small-caps in most industries, led by Health Care, Energy and Tech.





Source: FTSE Russell / Refinitiv. Based on Industry Classification Benchmark data as of March 31, 2023. Past performance is no guarantee of future results. Please see the end for important legal disclosures. For professional investors only.

Industry Returns & Exposures – Russell 1000 & 2000 Growth & Value

Key observations

Large- and small-cap Growth industries broadly outpaced their Value peers in Q1, spurred by a dramatic rotation into growth-heavy stocks, though most Value industries posted smaller declines than their Growth peers for the 12-month period.

- Within large-caps, Growth beat Value in 9 of 11 industries in Q1, led by Telecom, Discretionary & Financials. But Value continued to hold up better for the 12 months (7 of 11), particularly within Discretionary, Energy & Telecom.
- Within small-caps, Growth outdistanced Value in 8 of 11 industries, with Financials driving most of the performance gap, followed by Utilities & Tech. Value fared better for the 12 months (7 of 11), led by Energy, Real Estate & Utilities.
- For the quarter, Tech & Discretionary tallied the strongest gains across all style indexes, while Energy, Financials & Health Care were the biggest decliners, on average.
- For the 12 months, Energy was by far the top performer, more so for both Value indexes than their Growth counterparts. Staples also fared relatively well, more so for Growth than Value. Real Estate and Financials suffered the biggest losses.

Chart 1: Telecom, Discretionary & Financials drove most of Russell 1000 Growth's lead vs the other style indexes.

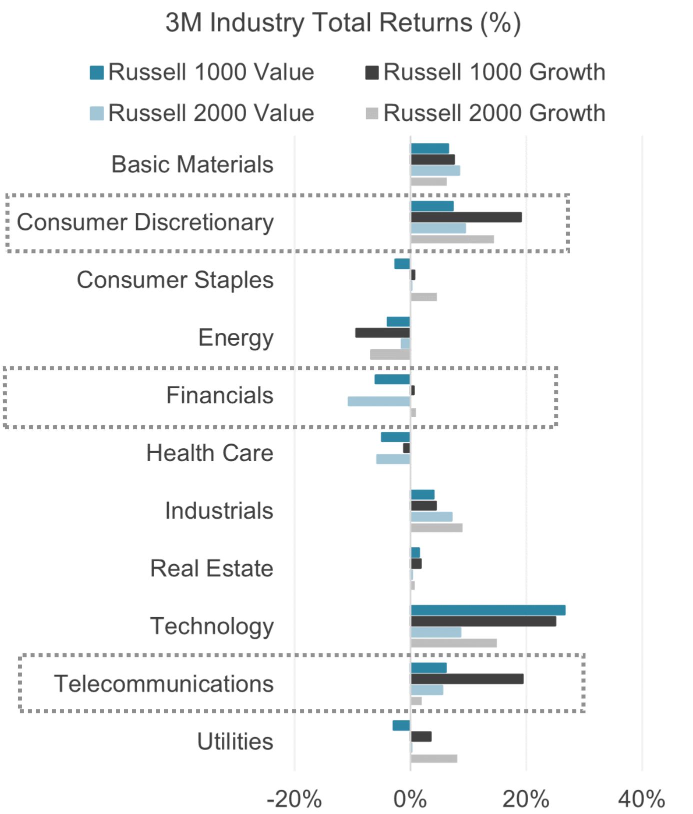
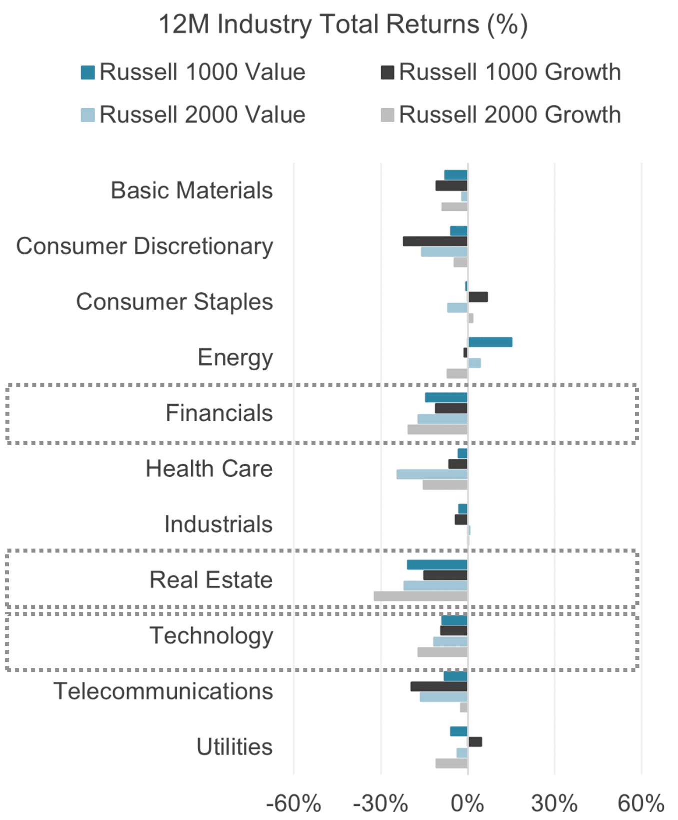
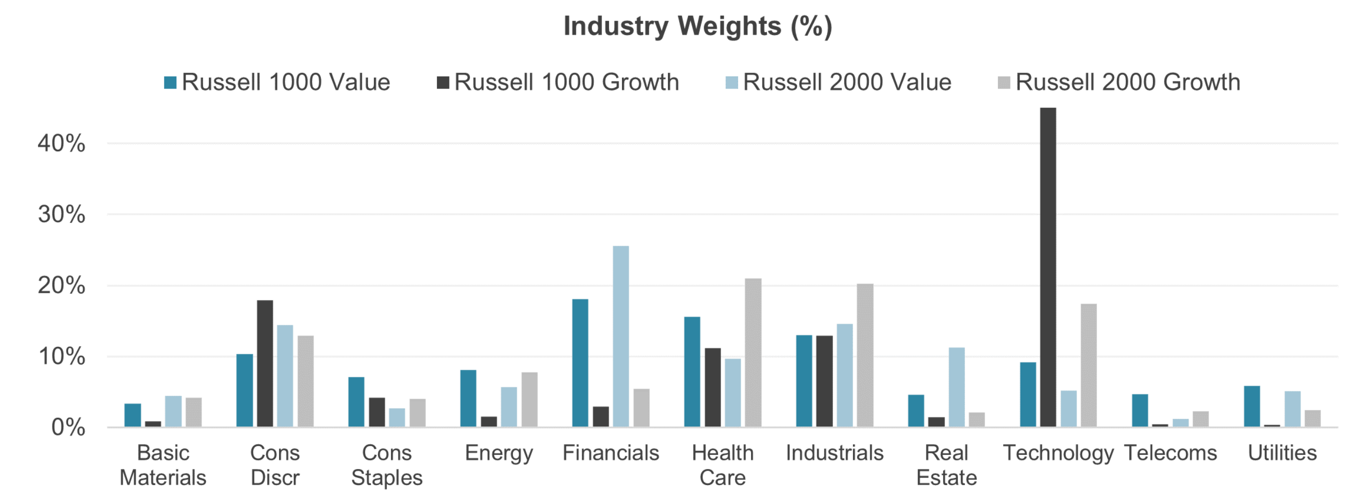


Chart 2: Value fared better than Growth in most industries, particularly among large-caps. Energy was a major driver.





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Russell 1000 Sector Weights & Contributions to Return*

Key observations — First Quarter 2023

Drilling deeper into the sector performances within the 11 Russell 1000 industries in Q1, we highlight the following key points:

- By far the best-performing large-cap industry in Q1, Technology's rebound was powered by similarly robust contributions from both software and hardware components.
- Discretionary was the next best performer, led by the Autos/Auto Parts and Retailers, which together contributed just under 60% of the industry's upsurge for the period.
- For the worst-performing industry in Q1 – Financials – the biggest sector decliners were Banks, which accounted for the bulk of that industry's decline.
- The Oil, Gas & Coal sector contributed nearly all of the losses for the second worst-performing industry, Energy.
- Up next among the biggest decliners, Health Care was hurt most by the selloff in Pharmaceutical & Biotechnology, which accounted for the biggest share of the industry's losses.

Table 1: Both Tech Hardware and Software stocks were the standout sector contributors to large-cap industry returns in Q1, followed by Autos and Retailers. Banks, Oil & Gas and Pharma stocks were by far the biggest drags.

Sector	Avg. Weight	Q1 2023 Contrib.
Basic Material		
Chemicals	63.1%	3.01%
Industrial Materials	4.6%	0.24%
Industrial Metals and Mining	26.0%	3.30%
Precious Metals and Mining	6.2%	0.45%
Consumer Discretionary		
Automobiles and Parts	12.9%	4.53%
Consumer Services	3.5%	0.52%
Household Goods & Home Construction	2.4%	0.32%
Leisure Goods	4.0%	0.43%
Media	10.7%	1.98%
Personal Goods	6.4%	0.37%
Retailers	41.1%	4.01%
Travel and Leisure	19.0%	2.48%
Consumer Staples		
Beverages	29.0%	0.10%
Food Producers	23.1%	0.03%
Personal Care Drug & Grocery Stores	37.1%	-0.98%
Tobacco	10.8%	-0.20%
Energy		
Alternative Energy	3.5%	-0.03%
Oil Gas and Coal	96.5%	-4.91%
Financials		
Banks	32.2%	-3.82%
Finance and Credit Services	6.3%	0.45%
Investment Banking and Brokerage Svcs	38.9%	-0.31%
Life Insurance	4.3%	-0.54%
Mortgage Real Estate Investment Trusts	0.6%	-0.01%
Non-life Insurance	17.6%	-0.44%
Health Care		
Health Care Providers	18.8%	-1.82%
Medical Equipment and Services	31.8%	1.01%
Pharmaceuticals and Biotechnology	49.4%	-2.60%
Industrials		
Aerospace and Defense	13.3%	0.01%
Construction and Materials	5.9%	0.54%
Electronic and Electrical Equipment	8.8%	0.27%
General Industrials	15.9%	0.86%
Industrial Engineering	8.9%	0.05%
Industrial Support Services	34.1%	1.83%
Industrial Transportation	13.2%	0.74%
Real Estate		
Real Estate Investment & Services Dev.	6.4%	-0.17%
Real Estate Investment Trusts	93.6%	1.91%
Technology		
Software and Computer Services	55.1%	11.45%
Technology Hardware and Equipment	44.9%	12.79%
Telecomunications		
Telecommunications Equipment	39.6%	4.14%
Telecommunications Service Providers	60.4%	-0.07%
Utilities		
Electricity	67.2%	-2.28%
Gas Water and Multi-utilities	23.8%	-0.60%
Waste and Disposal Services	9.0%	0.48%

Source: FTSE Russell. *Indexes data shown here are from the Russell Capped Index Series, except for the Real Estate Industry. Data as of March 31, 2023. Past performance is no guarantee of future results. Please see the end for important legal disclosures. For professional investors only.

EPS Growth Outlook and Revision Cycle – Russell 1000 & Russell 2000

The EPS growth outlook for the Russell 1000 and Russell 2000 remains strong but has weakened considerably over the past year as a result of tougher comparisons and increased strains on margins from slowing economic activity, rocketing input costs and higher borrowing rates.

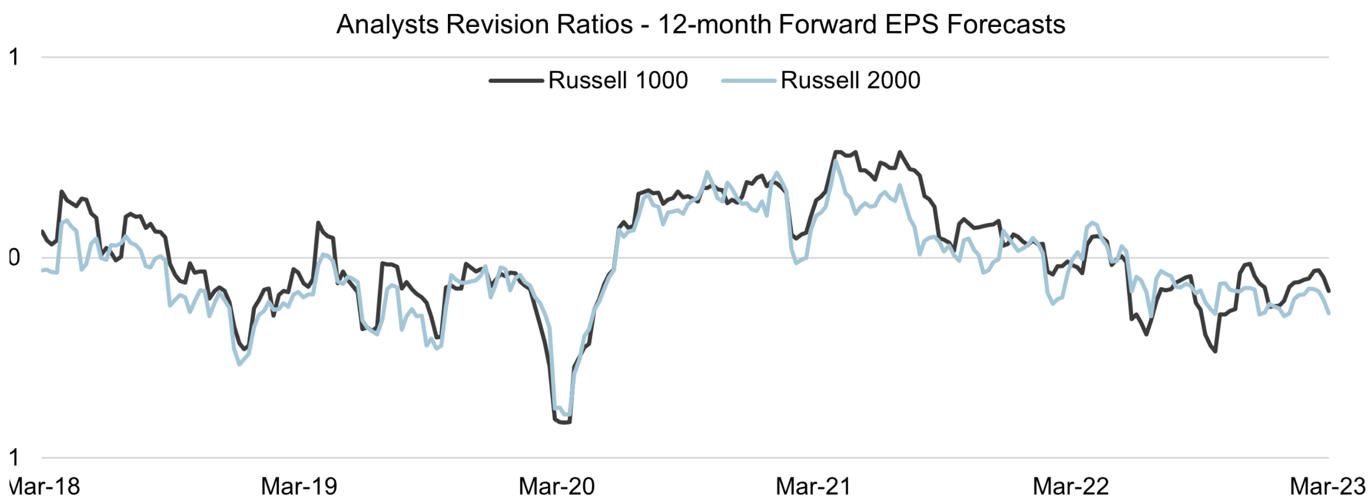
Though the recent revision downtrend appears to have stabilized, consensus forecasts for the Russell 1000 now call for earnings growth of 5% over the next 12 months, down from estimates a year ago of around 10% (Chart 1). The hit to Russell 2000 forecasts has been even harsher (Chart 2), with consensus pegging 12-month forward growth at 12%, down from peak expectations last June for a 40% increase. This is likely in response to diminishing earnings prospects for Energy, Basic Materials, Financials and Real Estate companies, reflecting the continuing easing in commodity prices, tighter lending conditions and the slowing US housing market. Stocks in these industries make up a bigger share of the small-cap index than its large-cap counterpart.

Continuing a pattern that began last June, the number of analysts' downgrades to 12-month-forward EPS forecasts again outnumbered upgrades in Q1 (Chart 3). The downward spiral in this ratio over the past year has been more pronounced for the small-cap index than for its large-cap counterpart.

Chart 1: Forward EPS growth forecasts for the Russell 1000 in Q1 and stands around 5%, or half of its peak a year ago.

Chart 2: Forward EPS growth forecasts continued to edge lower for the Russell 2000 in Q1, to around 12%.

Chart 3: The downward revision cycle for both the Russell 1000 and Russell 2000 that began last June continued into Q1, with analysts' downgrades outnumbering upgrades, but it appears to have stabilized.



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EPS Growth Outlook and Revision Cycle – R1000 & R2000 Growth & Value

As in the case of the two size benchmarks, the earnings growth outlook for the Russell US style indexes has also deteriorated over the past year, far more significantly for large-cap Value and small-cap Growth than for their style counterparts.

Consensus 12-month-forward earnings growth forecasts have fallen sharply for Russell 1000 Value, to just above 1%, down sharply from estimates a year ago of around 9% (Chart 1). This downgrade cycle likely reflects the dimming profit outlooks for Financials, Real Estate and other rate-sensitive constituents (which comprise a larger share of the Value index than the Growth index) as lending standards grow more restrictive and recession fears mount. By contrast, large-cap Growth is expected to deliver earnings gains of around 12%, down from a peak estimate last June of 15%. As Chart 2 illustrates, though analysts downgrades continued to outnumber upgrades for both large-cap style indexes in Q1, revision ratios appear to have stabilized for large-cap Growth, while remaining negative for its Value counterpart.

The roles reversed for the small-cap style indexes. Forward earnings growth forecasts for Russell 2000 Growth have plunged to 13.6% from year-ago estimates (the chart is capped at 50%). This is only moderately faster than the expected earnings growth for its Value counterpart, now forecast at 11.6%, down from a peak estimate of 26% a year ago. As Chart 4 suggests, the downgrade cycle appears to have stabilized for small-cap Growth and took another turn lower for its Value cohort.

Chart 1: Consensus looks for large-cap Value's earnings growth to stall, gapping widely vs 12% for its Growth peer.

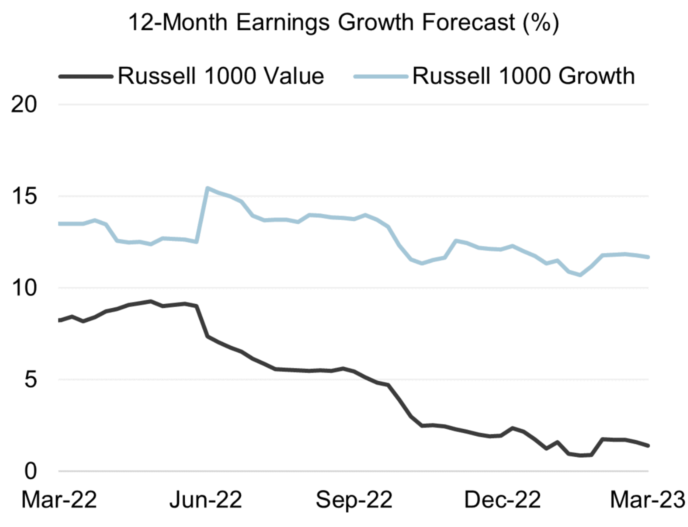


Chart 2: Downgrades continued to outnumber upgrades for both large-cap style indexes, but more so for Value.

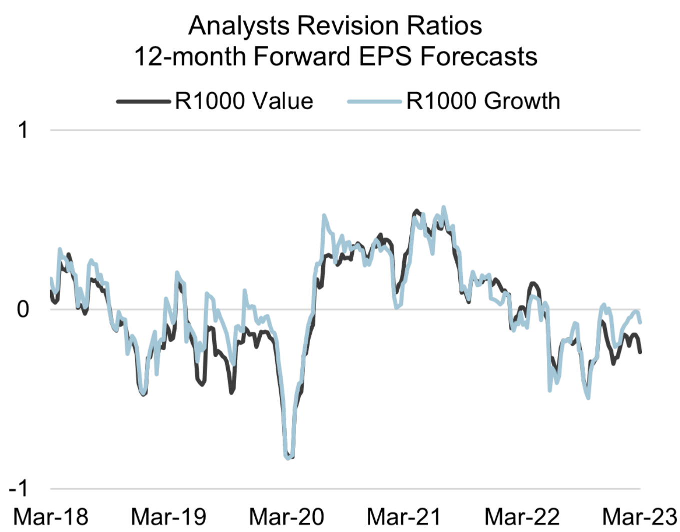


Chart 3: Growth forecasts have ben slashed for both small-cap style indexes in Q1, but the hit to Growth was severe.

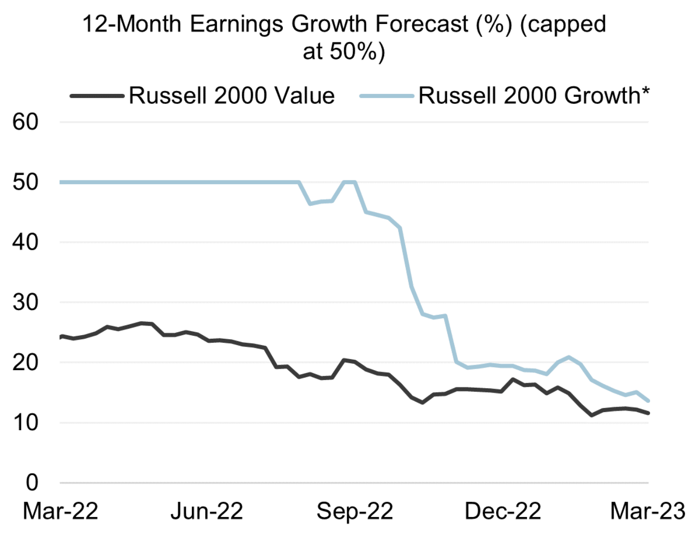
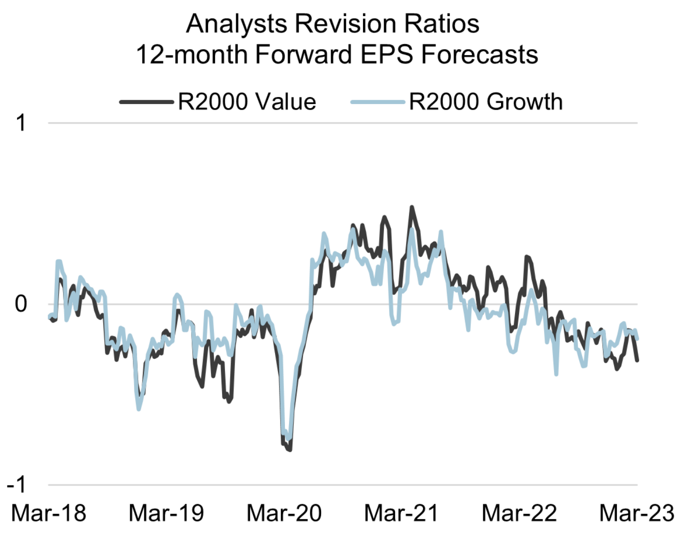


Chart 4: Downgrades continued to outnumber upgrades for both small-cap style indexes, more so for Value.



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Trailing 12-Month Dividend Yields

Dividend yields have been steadily rising across the flagship Russell US Indexes over the past year as corporate profitability and cash flows have normalized from the depressed levels following the Covid-18 outbreak in early 2020. Even so, only Russell 2000 and its Value offshoot have seen their dividend yields return to pre-pandemic levels, reflecting recent underperformance.

Value indexes typically pay higher dividend yields than their Growth counterparts, an outgrowth of the former's bigger weights in traditionally steadier and more generous dividend payers among Telecom, Utilities and Financial companies and far smaller weights in Technology and other higher-growth companies that tend to pay little or no dividends. As Charts 2 and 3 illustrate, dividend yields for both Value indexes have risen far more significantly than for their Growth counterparts since 2021 (particularly among small-caps), despite the strong outperformance of Value stocks over that period. At March-end, the Russell 2000 Value offered a dividend yield of 2.6%, roughly matching its pre-pandemic high. This was only slightly higher than the 2.4% of the large-cap Value index.

Dividend yields have also climbed for the Russell 1000 and Russell 2000 since their 2021 troughs (Chart 1), though not as steeply as those of their style offshoots. At March-end, the large-cap index offered a dividend yield of 1.7% vs 1.6% for the small-cap index.

Chart 1: Both large and small-cap indexes have seen dividend yields climb over the past year (though the gap between the two tightened significantly in Q1) as post-Covid profitability has recovered more rapidly than stock prices.

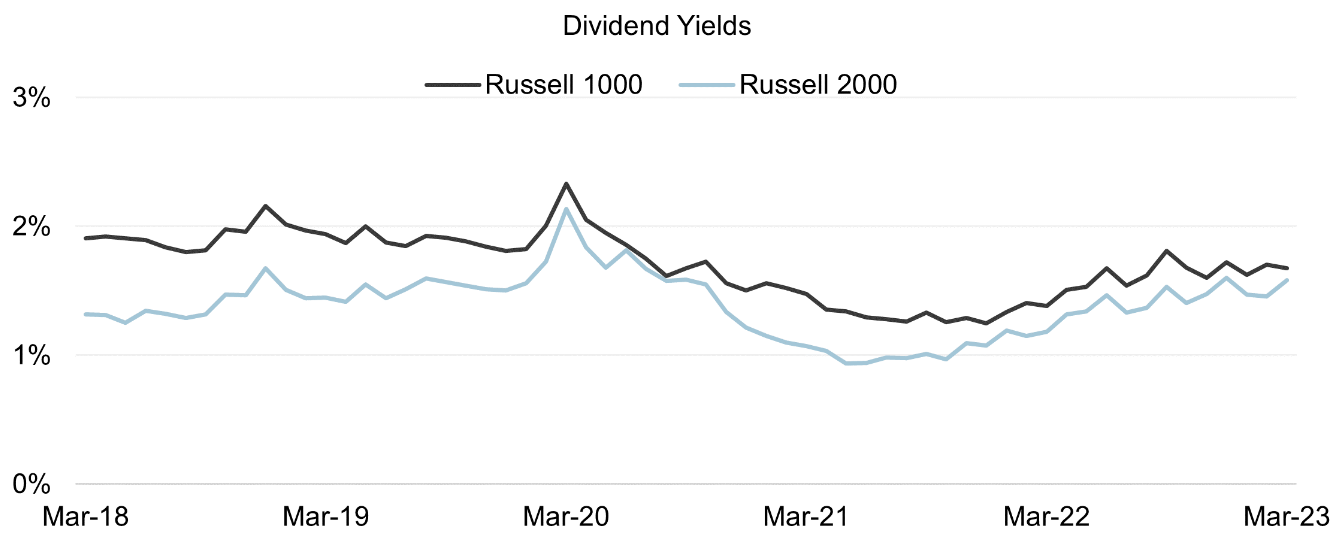


Chart 2: Large-cap Value widened its dividend yield gap vs that of Growth in Q1 reflecting recent underperformance.

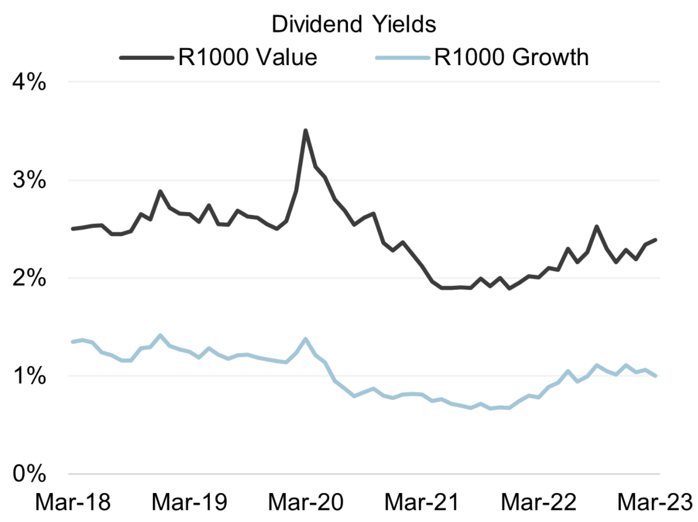
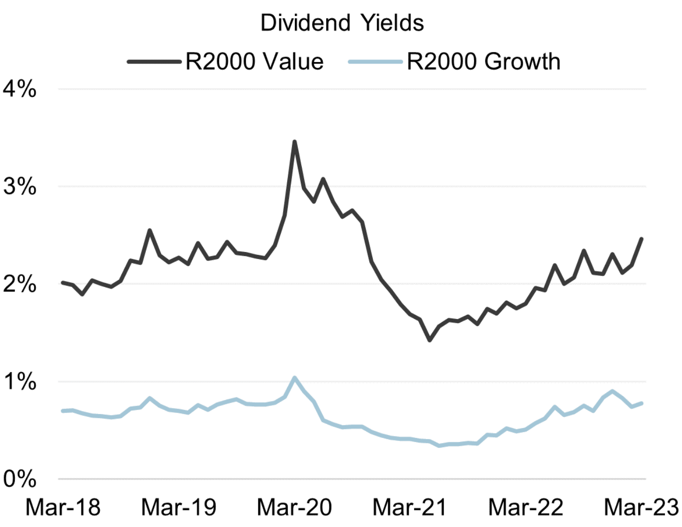


Chart 4: Russell 2000 Value offered a dividend yield of 2.6% at Q1-end, roughly matching its pre-pandemic high.



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Valuation Comparisons – 12-Month Forward P/Es

The multi-year contraction in forward P/Es appears to have stabilized or reversed course along with the broad rallies across the Russell US indexes since late last year, bringing forward multiples for most Russell indexes back to levels in line with pre-pandemic averages — or, in the case of Russell 2000 Growth, below five-year lows. All trade at a premiums to the FTSE All-World ex US, which stood at 12.3 times forward EPS estimates at March-end.

The Russell 2000 currently trades at 21.7 times 12-month EPS forecasts, down sharply from its pandemic peak but up considerably from its low of 16.5 times last June (Chart 1); it's also below its 10-year average of 24.8 times. The Russell 1000 uptick was more modest, ending the quarter at 17.6 times, up from 15.5 in mid-October and roughly in line with its 10-year average. Though the valuation gap between the two indexes has widened considerably over the past year, the small-cap premium remains below its 10-year average, even factoring out its huge upsurge during the reopening euphoria in early 2021.

Forward multiples have also edged higher across the style indexes since Q4 2022 (Charts 2 and 3), more so for Russell 1000 Growth (now 23.2) and Value (now 14.0) than for their small-cap counterparts. All are now modestly above their year-ago levels. Though Growth typically trades at a premium to Value, the gap between the two styles remains modestly above or in line with 10-year averages after factoring out the enormous spike in Growth multiples in the early pandemic years.

Chart 1: The post-pandemic contraction in forward P/Es for both the R1000 and R2000 continued to stabilize in Q1, with both indexes seeing modest re-ratings since last June, more so for the small-cap index than its large-cap counterpart.

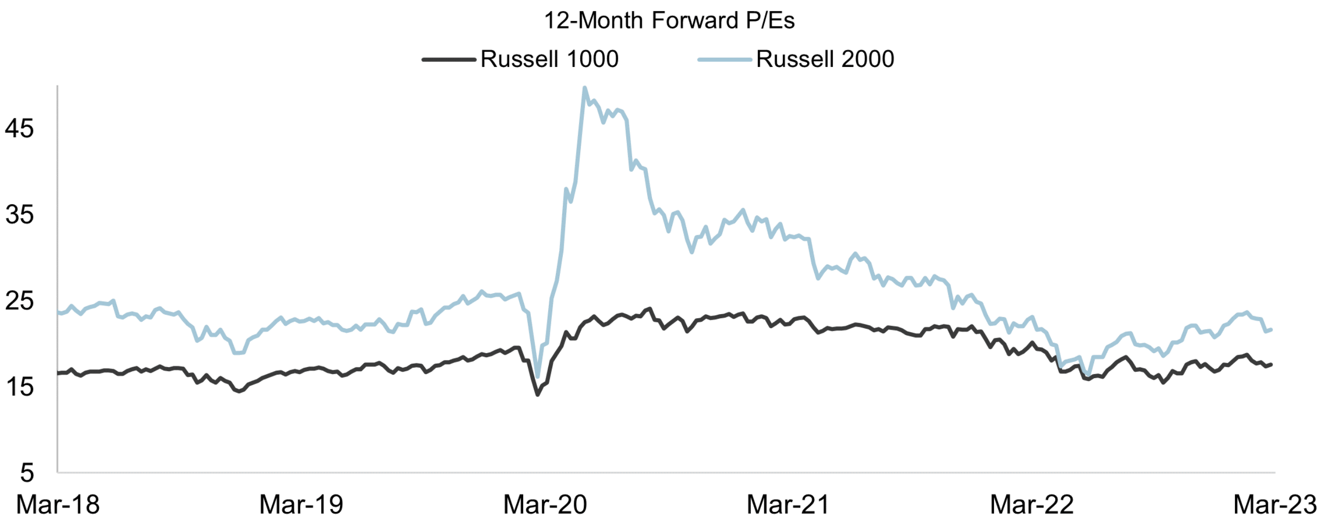


Chart 2: R1000 Growth retains a huge premium to its Value cohort, reflecting its far steeper re-rating in Q1.

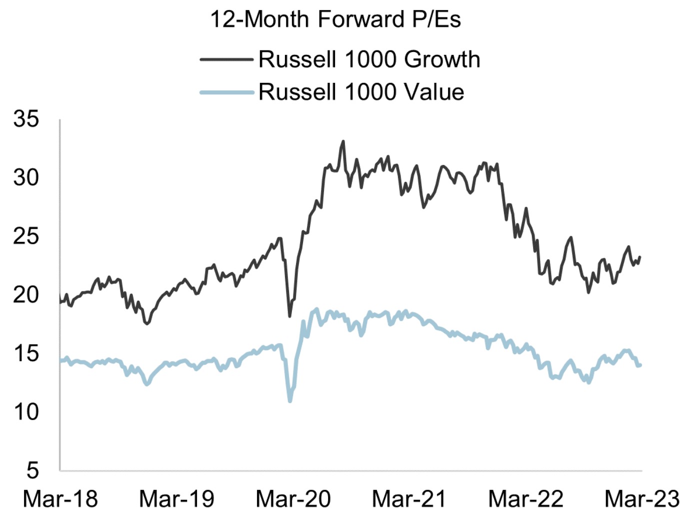
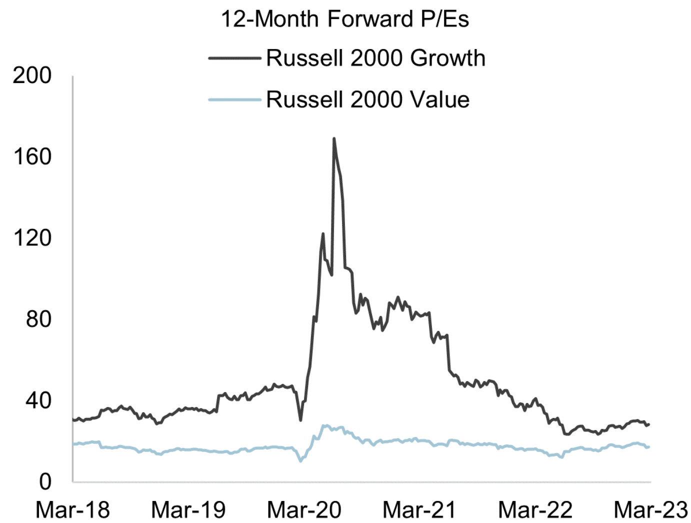


Chart 3: R2000 Growth vs Value premium continued to tighten in Q1 as the Value re-rating exceeded Growth's.



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IPO Additions to Russell US Indexes – First Quarter 2023

FTSE Russell adds eligible initial public offerings (IPOs) to its Russell US Indexes on a quarterly basis, ensuring that the indexes are always an accurate reflection of the markets they are designed to represent. Examining the history of such activity and its industry composition offers insights into market trends and investor sentiment.

While the number of IPOs each quarter tends to ebb and flow, the falloff over the past year has been particularly dramatic, a likely effect of extreme market volatility. IPO activity for the Russell 1000 remains moribund, while the Russell 2000 added four newcomers in Q1 2023, up from two in the prior quarter and eight in the same period a year ago. In keeping with a longstanding trend, Health Care dominated IPO activity in Q1 across the broad Russell US index family (Chart 2), accounting for four (or half) of the total eight new additons. Basic Materials added two, and Energy and Financials each added one. For more information, see Russell US Index IPO additions and reports | FTSE Russell.

Chart 1: The Russell 2000 added four newcomers in Q1 2023 (up from two in Q4 2022 and a total of 30 in 2022. The Russell 1000 IPO activity remained moribund. The US large-cap index has added only one IPO over the past 12 months.

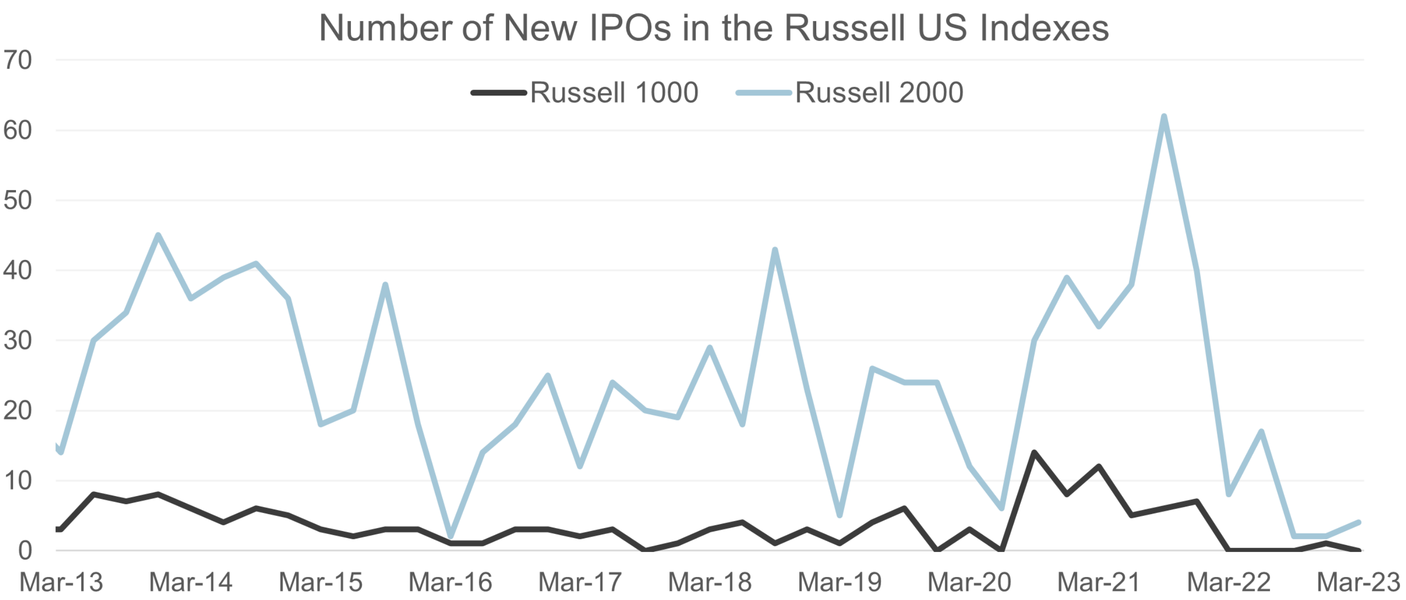
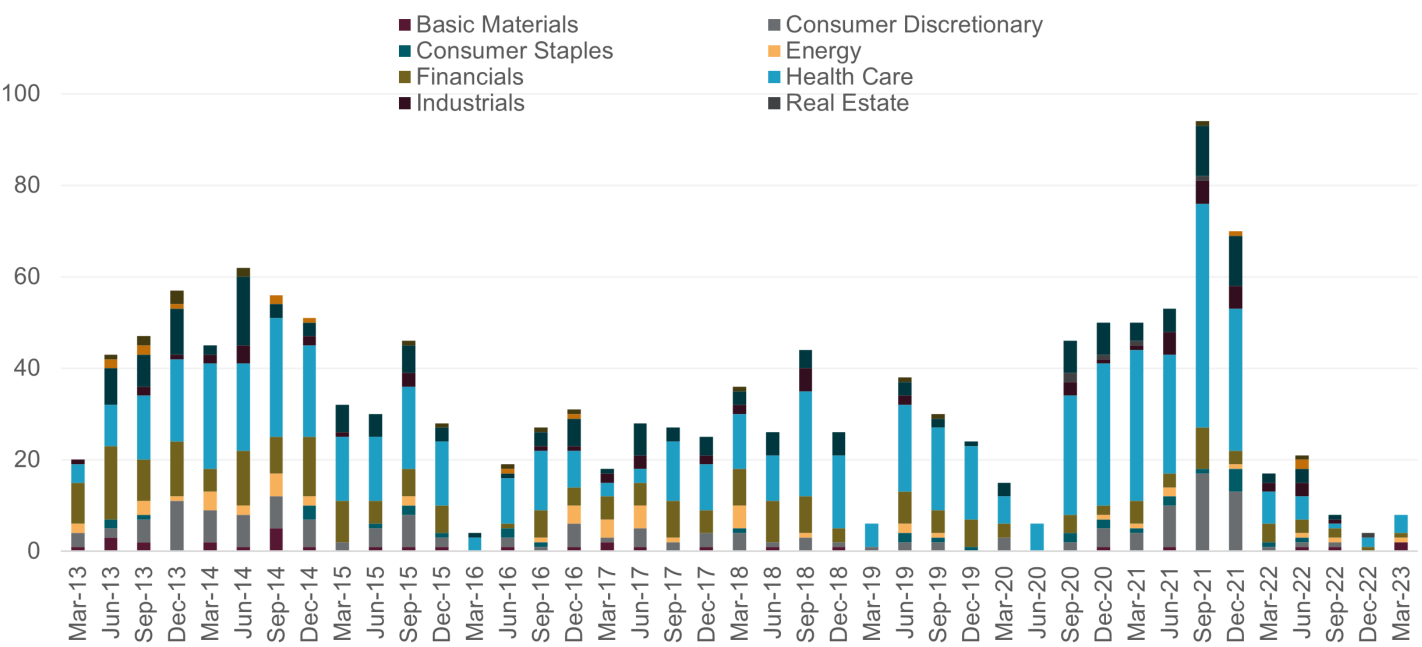


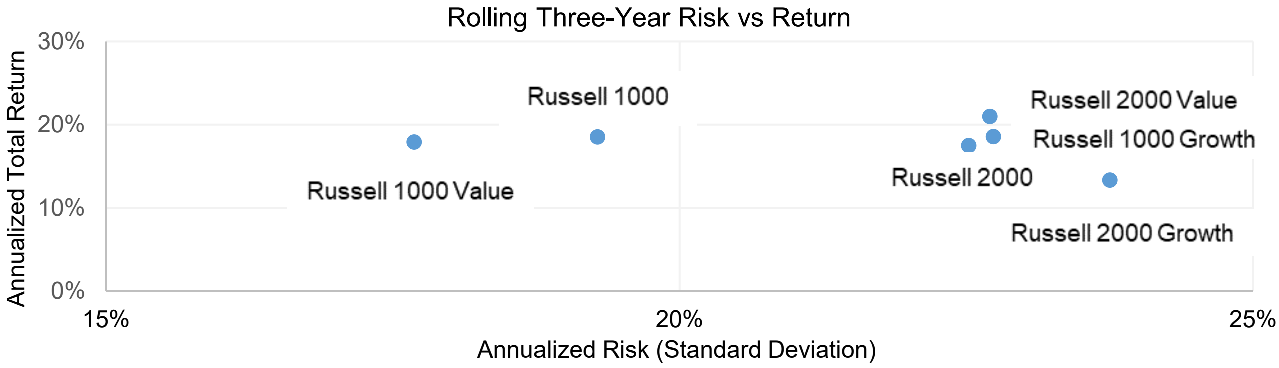
Chart 2: Health Care dominated the IPO activity for the Russell US indexes in Q1 2023, accounting for four (or half) of the total eight new additions. Basic Materials added two companies, and Energy and Financials each added one.



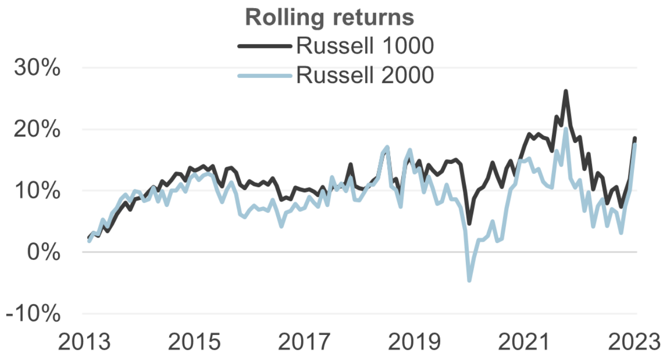
Source: FTSE Russell / Refinitiv. Based on Industry Classification Benchmark (ICB) data as of March 31, 2023. Past performance is no guarantee of future results. Please see the end for important legal disclosures. For professional investors only.

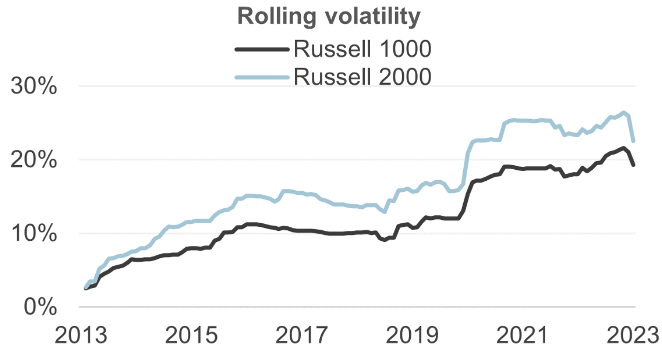
Return & Risk – Rolling Three-Year Patterns

In the most recent 3-year period, the Russell 1000 outpaced the Russell 2000 with far less volatility. Likewise for large-cap Growth and Value vs small-cap peers. The rolling 3-year charts below show return and volatility patterns over time.

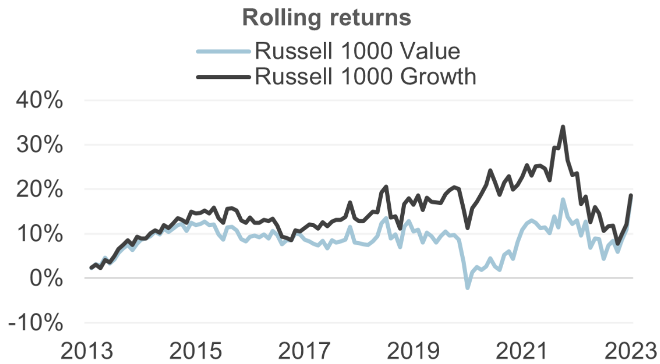


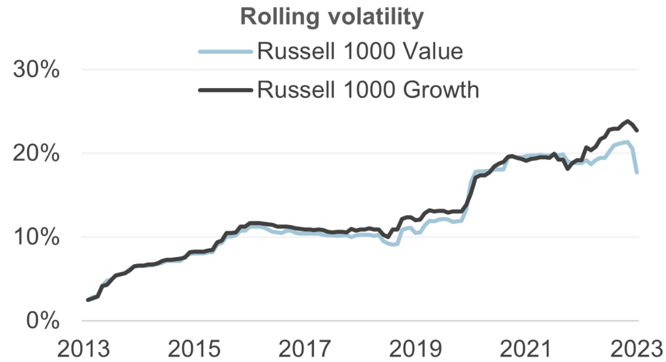
R1000 has slightly outperformed R2000 with far less risk recently, though volatility has risen for both over the Covid era.



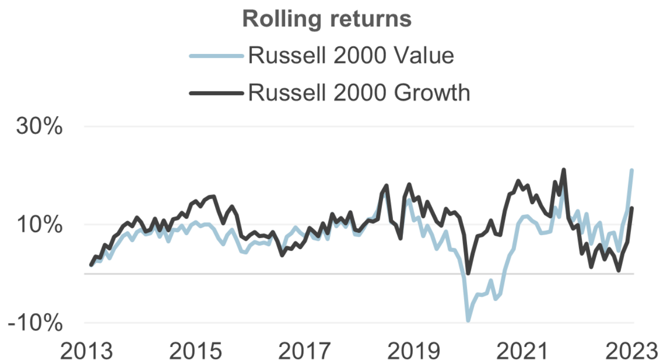


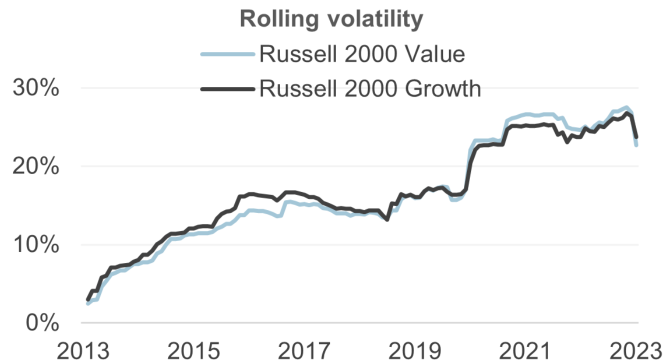
R1000 Growth has outperformed R1000 Value since the Covid outbreak, though it has grown far more volatile recently.





R2000 Value surpassed R2000 Growth in the most recent 3-year period, finishing with comparable volatility.





Source: FTSE Russell / Refinitiv. All data through March 31, 2023. Past performance is no guarantee of future results. Please see the end for important legal disclosures. For professional investors only.

Source: Equity markets data is based on the following: FTSE All-World® (World), FTSE All-Share® (UK), FTSE 100(UK large caps) FTSE 250 (UK mid caps), Russell 2000® (US small caps), Russell 1000® (US large caps), FTSE World ex UK, FTSE Europe ex UK (Eurozone), FTSE World ex US, FTSE Japan, FTSE Asia Pacific ex Japan and FTSE Emerging (emerging markets) Indexes.