The Case for Small Cap, Quality and Value.

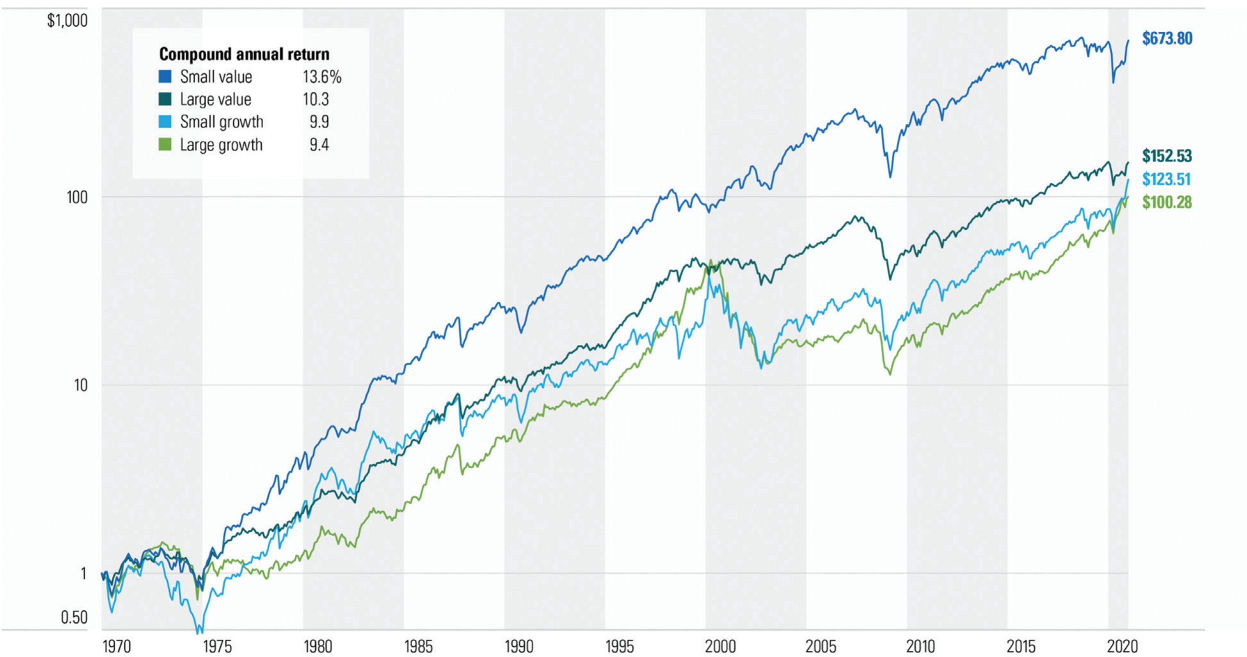
– Michael Mack, Portfolio Manager

One of the most popular asset classes available to investors has been the small cap value space. Small cap companies are those with somewhat smaller market capitalization, which can range from just $300 million to $2 billion.

Large cap companies, on the other hand, are companies with market capitalization of over $10 billion. Small cap and large cap companies can be defined as growth or value companies: growth companies are expected to grow their earnings at above average rates, while value companies are undervalued in price based on fundamentals.

Growth and Value Investing

1970-2020



Past performance is no guarantee of future results. Hypothetical value of $1 invested at the beginning of 1970. Assumes reinvestment of income and no transaction costs or taxes. This is for illustrative purposes only and not indicative of any investment. An investment cannot be made directly in an index.

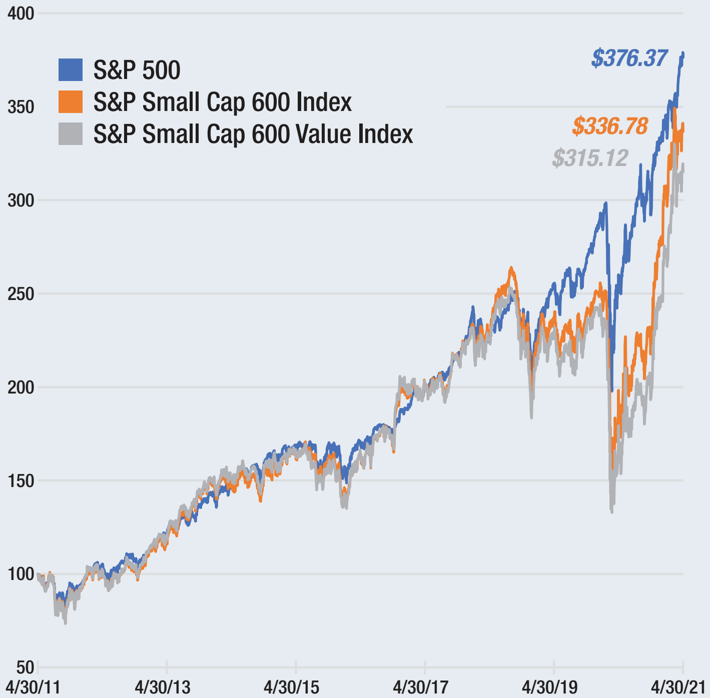
About the data: Growth and value stocks in this example are represented by the Ibbotson Associates Growth and Value Indexes for 1970–97 and the Morningstar Style Indexes thereafter. The Ibbotson Associates Growth and Value Indexes are calculated based on data from the CRSP US Stock and Index Databases, the Center for Research in Security Prices (CRSP®), and the University of Chicago Booth School of Business. Used with permission.

Historically, small-cap stocks have outperformed large-cap stocks, while value stocks have outperformed growth stocks. But within small-cap stocks, the greatest performance differential has been between value and growth.

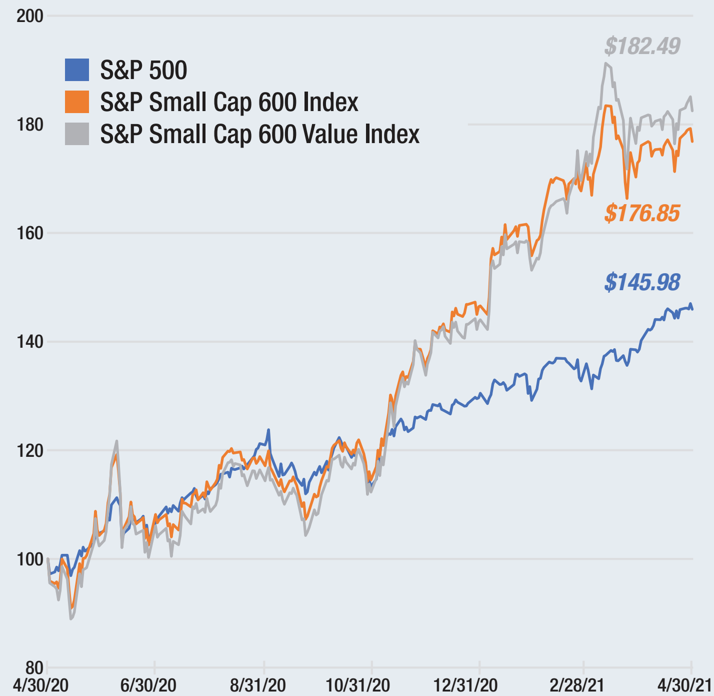
According to Morningstar, small-cap value catapults past small-cap growth, large-cap value, and large-cap growth, ending with nearly 14% compound annual return. Over time, this performance differential would have resulted in an investment value four times that of large cap value. Investors looking to improve their returns may want to consider looking to overweight small-cap value stocks, despite the larger risk.

Small Cap's Performance Then and Now

Growth of $100
4/30/2011 - 4/30/2021



Growth of $100
4/30/2020 - 4/30/2021



Source: Bloomberg. **PAST PERFORMANCE IS NOT INDICATIVE OF FUTURE RESULTS. YOU CANNOT INVEST DIRECTLY IN AN INDEX.**

However, recently small cap has seen a strong turnaround with the heightened market volatility and increased credit concerns. But, given the last 10 years of underperformance, there is still room to grow. As a result, small-cap value stocks have been trading at discounted prices to what their averages have been in the past. This discount may signal an opportunity for investors to shift their portfolio allocations toward small-cap value to take advantage of these attractive valuations.

Current P/E vs 20-year avg. P/E

	Value	Blend	Growth
Large	18.2 / 13.7	21.9 / 15.4	29.2 / 18.5
Mid	18.9 / 14.4	22.5 / 16.3	36.5 / 20.3
Small	**19.1 / 16.8**	30.9 / 21.1	85.6 / 35.2

The chart to the left presents current large, mid and small cap price-to-earnings ratios (P/E) over its 20-year average. P/E ratio is meant to signify a company's current share price compared to its per-share earnings.

This allows investors to easily see the value of a company's shares. Small-cap value currently sits roughly 2 points below its 20-year average, as compared to large-cap value which remains the same.

Source: JP Morgan 3/31/21

Source: FactSet, Russell Investment Group, Standard & Poor's, J.P. Morgan Asset Management.
Data is based on Russell style indices with the exception of the large blend category, which is based on the S&P 500 Index. Past performance is not indicative of future returns. The price to earnings is a bottom-up calculation based on the most recent index price, dividend by consensus estimated for earnings in the next 12 months (NTM), and is provided by FactsSet Market Aggregates.
Guide to the Markets – U.S. Data are as of March 31, 2021.

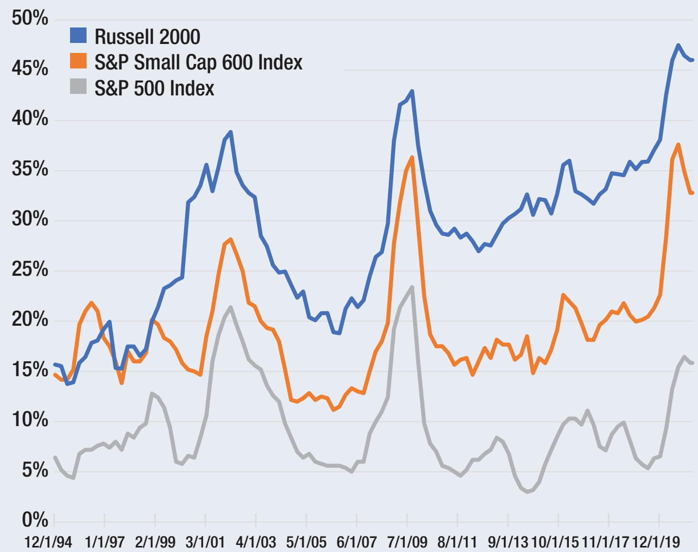
Finding Quality Stocks

Investors must be mindful of the financial health of small cap companies despite the compelling opportunity valuations present. Within small cap, there is a wide dispersion between high-quality and low-quality stocks.

The chart to the right shows that about 45% of companies in the Russell 2000, a popular small cap index, are currently generating negative earnings versus nearly 35% for the S&P SmallCap 600® and just over 15% for S&P 500®. The chart illustrates the benefit of screening companies from the S&P SmallCap 600®, a higher quality index than the Russell 2000.

Source: FactSet

Percentage of Companies with Negative Net Income
12/31/94 - 4/30/21

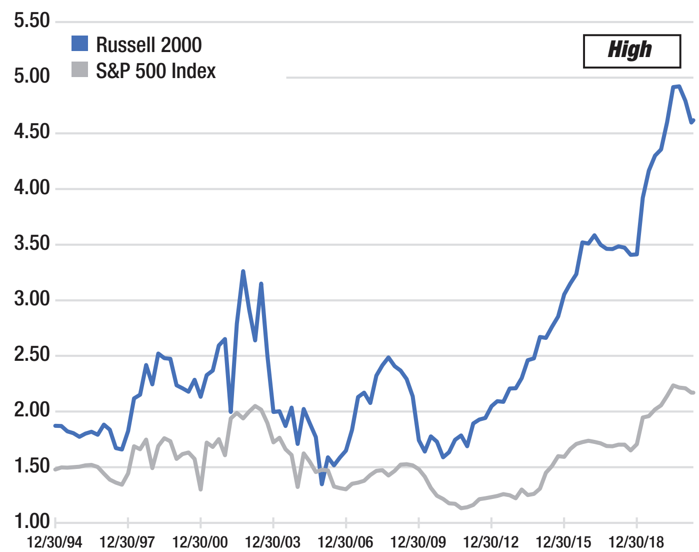


Leverage in Small vs. Large Cap

Small-cap stocks are more leveraged than their large-cap stocks counterpart. Financial leverage is defined as Net Debt/EBITDA, and measures the company's debt level relative to the cash flow available to make debt payments. This is one of the most common ways to measure leverage in the industry.

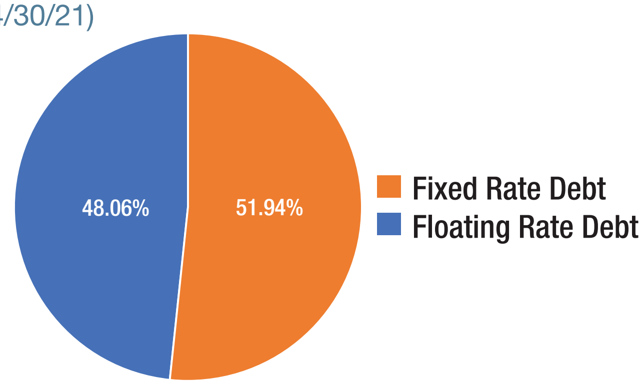
In addition, small cap companies have a much higher percentage of debt based on floating rates. Floating rate debt denotes any form of debt, whether that be a loan or a bond which has a variable rate that can change overtime. Potential problems could present themselves should interest rates resume their upward trend as companies with floating rate debt could see their interest costs increase, making it harder to support debt loads.

Leverage of Small Cap vs Large Cap (Ex-Financials)
12/31/94 - 4/30/21

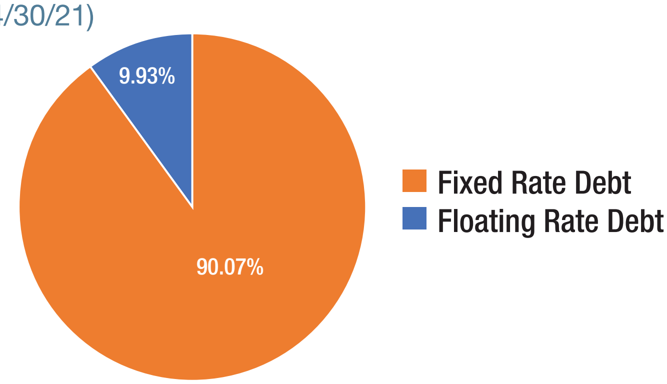


Source: Bloomberg

Russell 2000
(as of 4/30/21)



S&P 500®
(as of 4/30/21)



Source: FactSet. **PAST PERFORMANCE IS NOT INDICATIVE OF FUTURE RESULTS. YOU CANNOT INVEST IN AN INDEX.**

Consider the Pacer US Small Cap Cash Cows 100 Strategy

When it comes to the small cap space, small caps are cheap on a relative and historical basis. **The Pacer US Small Cap Cash Cows 100 ETF (CALF)** consists of 100 small cap stocks that:

- Are all profitable.
- Have higher free cash flow and free cash flow yield than the S&P SmallCap 600®.
- Have lower leverage.

CALF offers investors a way to gain exposure to high-quality companies with high free cash flow yields and strong balance sheets, and now is the time to see if it might fit into your portfolio.

CALF

PACER CASH COWS INDEX® ETF SERIES

Pacer US Small Cap Cash Cows 100 ETF

To learn more, visit **www.paceretfs.com** or call **877-337-0500.**

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EBITDA: earnings before interest, taxes, depreciation and amortization, is a measure of a company's overall financial performance and is used as an alternative to simple earnings or net income in some circumstances.
P/E ratio a fundamental measure commonly used to determine if an investment is valued appropriately. Each holding's P/E is the latest closing price divided by the latest fiscal year's earnings per share. Negative P/E ratios are excluded from this calculation.
S&P 500® Index is a stock market index that tracks stocks of 500 large-cap U.S. companies.
Russell 2000 Index is a small-cap stock market index of the bottom 2,000 stocks in the Russell 3000 Index.

The Pacer US Small Cap Cash Cows Index was released on 5/29/17.

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