A Big Change in Small Cap Sentiment… Can it be?

SHAKER investments

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I am breaking no news here, but small-cap stocks broke out to new all-time highs for the first time in nearly four years, ending one of the index's longest drawdowns and finally clearing resistance that halted two past rallies. This breakout removes overhead prior-high resistance and introduces the potential for renewed bullish sentiment, though similar setups have failed before, so cautious optimism is warranted.

Small Cap Price Index (with small-to-large cap ratio)

A six-month rotation from large-caps to small-caps has helped small cap stocks outperform the S&P 500 by over 5% since April, drawing the attention of market participants. The breakout coincided with the second-best day of relative performance against the S&P 500 this year and the small-to-large ratio reaching a seven-month high, underscoring the momentum shift.

Still, this rally may be just a countertrend move as many investors, scarred by years of small-cap underperformance, remain skeptical. My view is that this next phase is crucial for a bullish sentiment shift. Consolidation of small-cap prices in a stable range, alongside lower volatility, is key to shifting sentiment and encouraging active managers to return after years of avoidance. Shaker Investments is ready to deploy additional capital down the cap spectrum and continues searching for underfollowed and fundamentally strong small companies ripe for price discovery, believing persistent bias creates opportunity when sentiment turns.