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WEALTH MANAGEMENT

Market Capitalization: What are Large Cap and Small Cap Stocks?

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Your financial advisor may mention that your portfolio includes small cap stocks or large cap stocks. Understanding the difference is an important aspect of managing potential risks and expected returns for your investments.

The world of equity investing can be overwhelming. There are many classifications of equities that investors may consider when investing: one of which being the market capitalization of stocks (commonly referred to as "market cap"), which is used to designate the size of a company. A company's market cap is an important consideration that can have a meaningful impact on the performance of your portfolio. The stability of business operations and end market exposures are just a few important factors that vary depending on the size or market cap of a company.

What is Market Capitalization?

Market capitalization is a dollar value commonly used to indicate the size of a company. It is calculated by multiplying the number of total outstanding shares of a company by the market price of a share. Intuitively, large cap stocks are those with higher dollar value market caps and small cap stocks are those with lower dollar value market caps. There is not a universal rule of a certain number of shares or a certain price of a share that makes a company large cap or small cap, only the relationship between the number of shares and price. The market cap of a publicly traded company on a major exchange can range from as high as $1 trillion to as little as $25 million. Generally, companies with a market cap of at least $10 billion are classified as "Large Cap" while companies with a market cap of less than $2 billion are considered "Small Cap."

Highly recognized companies such as Apple (market cap of over $850 billion) or ExxonMobil (market cap of over $300 billion) are examples of Large Cap companies. While many may not be as familiar with Small Cap companies since they have smaller footprints or do not touch the end consumer as much as Large Caps, many are still familiar with companies like Shake Shack (market cap of slightly under $2 billion) or GameStop (market cap of over $800 million), both of which are considered Small Caps.[1]

[1] Quoted Market Caps as of 05/21/2019.

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A MOMENT OF CLARITY

Why Does Market Capitalization Matter?

Understanding the market cap of a company is important as it can lead to a better understanding of the risks and return expectations of your investment. Large cap companies are typically considered more "stable" than small cap companies, as they have more diversified streams of revenue and a greater amount of sales. Additionally, large cap companies typically have a greater global reach, so they are more likely to have exposure to international markets. Small cap companies don't have the same type of global scale, so sales will generally be driven more by regional or broad U.S. demand.

Should you Invest in Large or Small Cap Companies?

One is not necessarily better or worse than the other. While most portfolios will have a greater allocation to Large Cap stocks for stability, the addition of Small Cap stocks can benefit returns in an expanding U.S. economy. Conversely, Small Cap stocks may hinder performance if the economy is slowing. Either way, it is important to have a discussion with your advisor to understand the exposures and associated risks within your portfolio. If you are unsure how your portfolio is allocated or what allocation is most appropriate for you, please reach out to Round Table Wealth Management for a review.

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