

Why Investing in S&P 500 Equal Weight (SPW) Might Be a Strategic Move Right Now

The S&P 500's Heavyweight Bias: A Growing Concern

The **S&P 500 Index (SPX)** is one of the most widely followed benchmarks in the world. However, it's important to recognize that this index is **market-cap weighted**, meaning the largest companies, such as Apple, Microsoft, and Nvidia, carry outsized influence on its movements. This structure often leads to periods where a few mega-cap stocks drive returns while smaller companies in the index lag.

One way to measure this imbalance is by looking at the **S&P 500 vs. S&P 500 Equal Weight Ratio (SPX/SPW)**. When this ratio is historically high, it indicates that large-cap stocks have outperformed smaller stocks in the index by a significant margin.

SPX/SPW Ratio is Historically High – A Warning Sign?

Currently, the **SPX/SPW ratio is at historically elevated levels**, suggesting that the dominance of mega-cap stocks is at an extreme. In the past, such levels have often been followed by periods of **underperformance for large-cap stocks** and relative outperformance for smaller names within the index.



Sector Valuation Imbalances: Another Concern for SP500:

Beyond the index-weighting issue, there are also **major sector valuation imbalances** in the S&P 500 right now. Based on historical fair P/E levels:

- **Sectors like Information Technology, Consumer Discretionary, and Communication Services appear overvalued** relative to their historical norms.
- **More cyclical and defensive sectors like Energy and Financials appear more fairly valued or even undervalued.**

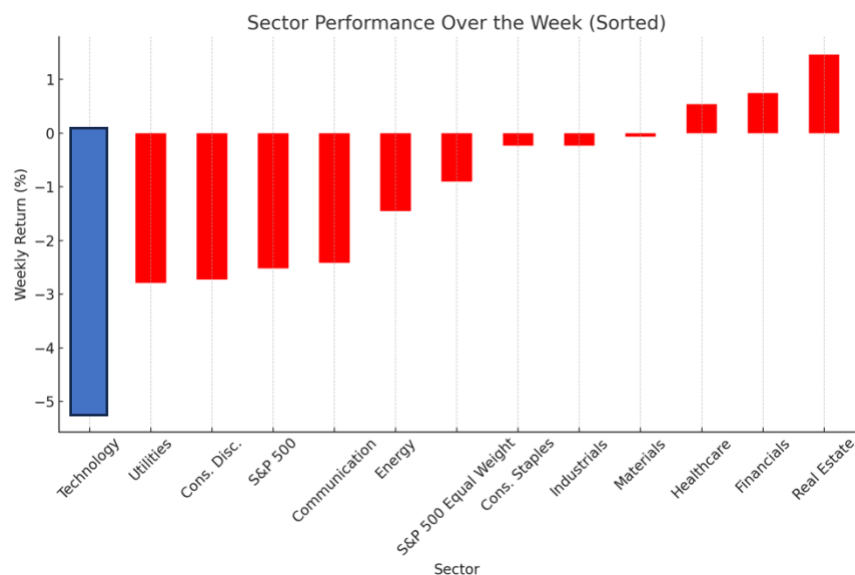
This suggests that **the current rally in SPX is driven by expensive sectors**, while cheaper areas of the market remain overlooked. Since **SPW gives equal weighting to all sectors**, it provides a more balanced exposure, reducing concentration risk.

S&P 500 Sector		Trend	P/E▼	P/E Deviation vs Avg			
				5 Years	10 Years	20 Years	
☐ Real Estate	XLRE	□	37.88	-0.21 σ	-0.05 σ	-	26 Feb
☐ Information Technology	XLK	□	36.76	+2.30 σ	+2.65 σ	+4.27 σ	26 Feb
☐ Health Care	XLV	□	32.12	+2.23 σ	+6.04 σ	+6.10 σ	26 Feb
☐ Consumer Discretionary	XLY	□	27.77	-0.01 σ	+1.21 σ	+2.44 σ	26 Feb
S&P 500 Index	SPY	□	26.72	+2.34 σ	+3.54 σ	+4.66 σ	26 Feb
☐ Industrials	XLI	□	25.89	+1.82 σ	+2.65 σ	+4.43 σ	26 Feb
☐ Materials	XLB	□	24.97	+2.23 σ	+4.27 σ	+4.97 σ	26 Feb
☐ Consumer Staples	XLP	□	23.38	+0.98 σ	+2.21 σ	+2.64 σ	26 Feb
☐ Utilities	XLU	□	21.03	+1.51 σ	+2.21 σ	+2.53 σ	26 Feb
☐ Communication Services	XLC	□	20.64	-0.13 σ	+0.96 σ	+1.99 σ	26 Feb
☐ Financials	XLF	□	16.67	+1.64 σ	+2.99 σ	+3.41 σ	26 Feb
☐ Energy	XLE	□	14.44	+0.02 σ	-0.63 σ	+0.04 σ	26 Feb

US tech showing sign of weakness

This week underperformance of US equities was accompanied with significant return divergence among the sectors. Among them, the Tech sector has been particularly affected by the sell-off, despite Nvidia good earnings. We believe the recent tech downturn could be attributed to several factors. Firstly, concerns over tariffs and export controls have weakened the industry. Nvidia's CFO, recently highlighted uncertainties surrounding potential tariffs and export controls proposed by President Trump, particularly those targeting China. Secondly, despite reporting strong quarterly earnings, Nvidia projected a first-quarter gross margin of approximately 71%, down from the previous 73.5% and below analyst expectations of 72.2%. Finally, the emergence of low-cost AI models from Chinese competitor DeepSeek has intensified market competition.

US Tech lagged the market this week:



Why SPW Might Be a Better Bet:

Given these factors, investors may want to consider **tilting their portfolios toward the S&P 500 Equal Weight Index (SPW)** instead of the traditional market-cap-weighted S&P 500 (SPX). Here's why:

Reduced Concentration Risk – SPW **diversifies** exposure across all 500 stocks equally, reducing reliance on a handful of mega-cap stocks.

Better Value Exposure – With overvalued sectors dominating SPX, SPW **provides a more balanced exposure to cheaper sectors** that could see stronger returns.

Mean Reversion – Historically, when the **SPX/SPW ratio reaches extreme levels**, SPW **tends to outperform in the following periods**.

Potential Rate Cut Tailwind – With the Fed signaling possible rate cuts, **smaller stocks—many of which are more evenly weighted in SPW—could be poised for a rebound**

Conclusion: A Shift in Market Leadership?

While the market has favored **large-cap growth stocks** in recent years, history suggests that this leadership doesn't last forever. With valuations stretched in certain areas of the S&P 500 and the **SPX/SPW ratio at historically high levels**, the case for **investing in the equal-weighted S&P 500 (SPW) over the traditional SPX is growing stronger**.

Furthermore, the possibility of **rate cuts in the coming quarters could provide additional support for smaller stocks**, further strengthening the argument for **a shift away from large-cap dominance**.

For investors looking to **reduce concentration risk, gain exposure to more fairly valued sectors, and potentially benefit from a shift in market dynamics**, SPW presents an attractive alternative in today's market environment.

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