



DANIEL MEGES, MANAGING DIRECTOR, RESEARCH

VALUE VS. GROWTH INVESTING: A NUANCED DEBATE REVISITED

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In the December 2019 edition of ClearPoint, we discussed the various merits and nuances of both value and growth investing, as well as the cases to be made for each of the two styles going forward. Since that time, the equity market landscape has changed dramatically. We experienced the sharp global selloff and subsequent recovery related to COVID-19, while the value investing style came back into vogue at the end of 2020 and into 2021. Given the evolving market environment, we wanted to share our latest thoughts on growth and value investing, as well as their potential paths going forward.

Since the 2020 U.S. Presidential Election, the S&P 500 Value Index has outperformed the S&P 500 Growth Index by 4.8% cumulatively.¹ The rebound in the S&P 500 Value's performance has prompted our clients to ask us the logical question of "is value investing back in style again?" While we cannot definitively answer "yes" or "no," it leads us to first revisit some of the key nuances of value vs. growth investing.

CLEARSTEAD CONTINUES TO BOLSTER TEAM WITH NEW TALENT

We are pleased to announce that we have added talent to the Private Client team with Dave Rubis, Deb Richards, and Kaitlyn Harburg.

Dave Rubis has joined Clearstead as a Senior Managing Director. Dave previously worked for Fairport Wealth as the Director of Client Development. He holds a Master's Degree in Management from North Central College and a Bachelor's Degree in Finance from Miami University.

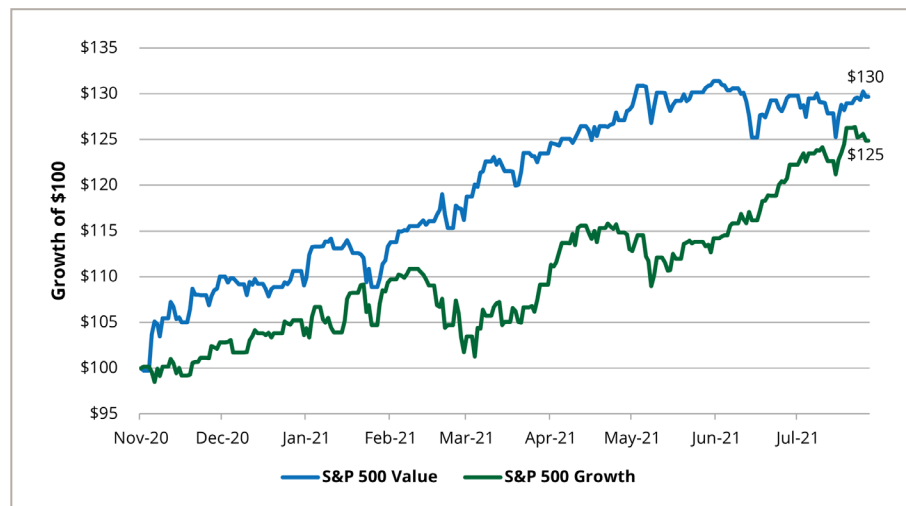
Deb Richards has joined Clearstead as a Senior Planning Associate. Deb recently moved to Cleveland from Chicago where she has spent the last 22 years working in CPA's firms. She has a Master's Degree in Accounting from Kaplan University and a Bachelor's Degree in Liberal Arts from the University of Illinois Urbana-Champaign.

Kaitlyn Harburg has joined Clearstead as a Family Office Professional. Kaitlyn previously worked at Seeb Industrial as an Office Manager and QuickBooks expert.

These changes underscore the firm's commitment to building its investment consulting

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Source: Morningstar Direct: 7/31/2021.

Past performance is not an indicator of future results.

VALUE VS. GROWTH: COMPANY VS. INDEX

Defining value at a company level vs. an index level is an important differentiation and has meaningful implications for shaping our view on value vs. growth investing going forward. At a company level, a value stock typically has some or all the following characteristics: a low valuation relative to its fundamental attributes, recent share price underperformance, and the potential to rebound as investors begin to appreciate the fundamental merits of the company, pushing the share price higher.

Value at an index level contains another layer of nuance, though. When comparing the S&P 500 Value Index to the S&P 500 Growth Index, the reference to value also involves the characteristic differences between the two indexes. On the surface, some of the more apparent differences between the S&P 500 Value Index and the S&P 500 Growth Index are the significantly lower price multiples of the Value Index as measured by trailing twelve-month price-to-earnings, price-to-book, price-to-sales, and price-to-cash flow ratios.² These characteristics align with the typical characteristics of value at a company level.

	S&P 500 Value	S&P 500	S&P 500 Growth
P/E Ratio	21.7x	27.1x	34.6x
P/B Ratio	2.8x	4.6x	10.9x
P/S Ratio	2.0x	3.1x	5.7x
P/CF Ratio	17.6x	20.6x	24.1x

Source: Bloomberg: 7/31/2021.

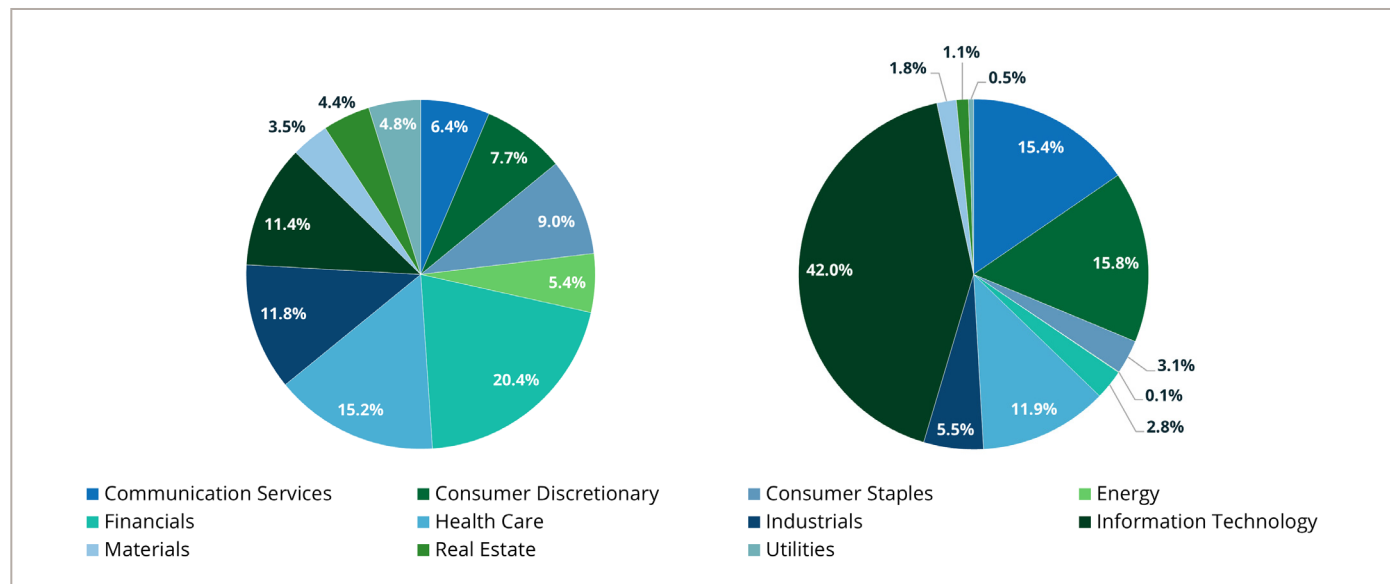
practice, promoting the next generation of leadership, and maintaining a rigorous investment process.

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However, when digging further into that discrepancy, we find meaningful differences in sector composition between the two indexes. Most notably, the S&P 500 Value Index has more exposure to the Financials sector (20.4%) and less exposure to the Information Technology sector (11.4%) relative to the S&P 500 Growth Index (2.8% and 42.0%, respectively).

S&P 500 Value (Left) vs. S&P 500 Growth (Right)



Source: Morningstar Direct: 7/31/2021.

When looking at these sectors in greater depth, we find that, since Q4 2020, the more prominent sectors of the S&P 500 Value Index have generally experienced more robust earnings growth than the more prominent sectors of the S&P 500 Growth Index.² During that time, investors have flocked to companies in sectors like Energy, Financials, Industrials, and Materials, which have experienced year-over-year earnings growth of over 100%² in some cases, exceeding the earnings growth of companies like Microsoft, Amazon, Facebook, Alphabet (Google), and others that had propelled the S&P 500 Growth Index for much of the last decade.

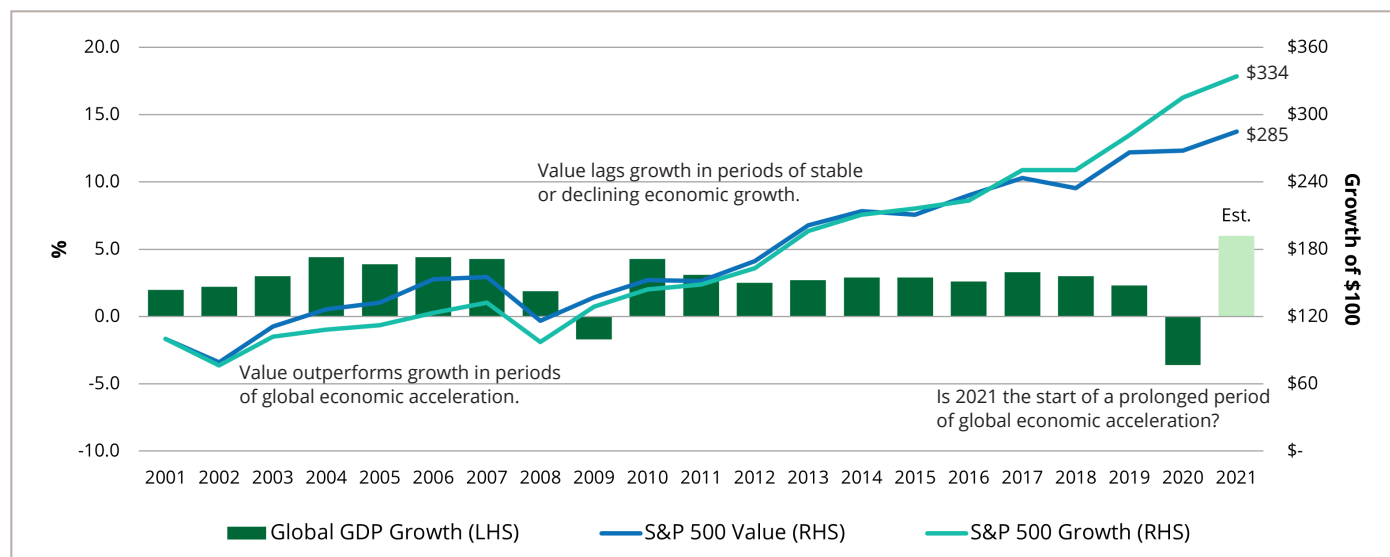
WHAT HELPS THE VALUE INDEX GOING FORWARD?

Given the S&P 500 Value Index’s successes relative to the S&P 500 Growth Index over the last nine months, two final questions we typically receive are “will value (at an index level) stay in favor?” and, if so, “why will value stay in favor?” In short, we do not know if the S&P 500 Value Index will continue the run it has experienced for the last nine months, but our primary thesis for what causes it to do so is a reacceleration in global economic growth accompanied by rising inflation and interest rates.

While the global economy has grown consistently for the last two decades, it has grown at a modest pace of roughly 2.7% annualized.^{2,3} Its modest growth rate has, in Clearstead’s view, led investors to become more willing to pay higher price multiples for companies experiencing more meaningful revenue and earnings growth relative to the global economy, propelling the S&P 500 Growth Index to significant outperformance vs. its value counterpart during that time.

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Sources: Morningstar Direct: 7/31/2021, Bloomberg: 7/31/2021.
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However, if the global economy begins on the path of consistent acceleration of growth, we believe investors will continue to rotate out of Growth Index stocks and into Value Index stocks, as we have seen for much of the last nine months. In an environment where broad-based company-level growth is more robust, we think investors will be more attracted to Value Index companies that offer comparable growth prospects to Growth Index companies but at much more compelling valuations.

If the reacceleration in global economic growth also comes with rising inflation and interest rates, we also think this will benefit Value Index stocks. Conceptually, rising interest rates would increase the discount rate applied to future company-level cash flows. Since several stocks in the S&P 500 Value Index have larger and more visible near-term cash flows, these cash flows would be discounted less relative to the longer-term and often more speculative cash flows of some Growth Index companies.

CONCLUSION

The S&P 500 Value Index has rebounded relative to the S&P 500 Growth Index over the last nine months¹. When digging into the underlying reasons for the performance divergence though, we find the sector differences and accompanying earnings growth differences to be logical reasons for the Value Index's outperformance.

Although the S&P 500 Value Index has rallied, it does not mean value investing is the only path forward to generate positive equity market returns. Value and growth styles have periodically outperformed one another in several instances over the last two decades. Given the uncertainty surrounding the global economic picture and the potential merits of both value and growth investing, we advocate balance between both styles at Clearstead. We believe the new market cycle following COVID-19 is in its early innings and more patience is required before overweighting value or growth stocks in our equity portfolios.

Sources:

- (1) Morningstar Direct: 7/31/2021
- (2) Bloomberg: 7/31/2021
- (3) World Bank: 12/31/2020

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Performance data shown represents past performance. Past performance is not indicative of future results. Current performance data may be lower or higher than the performance data presented.

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MARKET BENCHMARK RETURNS

August 31, 2021		1M	3M	12M	YTD
US Large Cap	S&P 500	3.0%	8.0%	31.2%	21.6%
US Small Cap	Russell 2000	2.2%	0.5%	47.1%	15.8%
Developed Intl	MSCI EAFE	1.8%	1.4%	26.1%	11.6%
Emerging Intl	MSCI Em Mkt	2.6%	-4.1%	21.1%	2.8%
Real Estate	NAREIT	2.1%	9.2%	37.0%	28.7%
Core Fixed	BarCap Agg	-0.2%	1.6%	-0.1%	-0.7%
Short Fixed	BarCap 1-3Yr	0.0%	0.0%	0.4%	0.2%
Long Fixed	BarCap LT G/C	-0.3%	6.1%	-0.8%	-2.3%
Corp Debt	BarCap Corp	-0.2%	2.6%	2.3%	-0.2%

Source: Bloomberg

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