



VALUE VS GROWTH INVESTING

Whatever your investment style, 'remaining diversified is a key metric for long-term portfolio returns and risk mitigation': Sean Kelly – Paragon Wealth Managers.

Defining the Differences:

Value and growth investing are considered to be two different investing styles and wall street tends to neatly categorize stocks as either value or growth but, the truth is a bit more complicated than this as many companies tend to have elements of both value and growth characteristics.

The main difference is that value investors look for stocks that they perceive to be undervalued to their true (or intrinsic) values relative to their fundamentals such as book values, earnings, and dividends. Thus, they look for shares that typically have relatively low financial ratios such as price-to-earnings (P/E), price-to-book values (P/B) and price-to-earnings growth (PEG). Value investors hunt for hidden gems in the market.

Growth investors look for companies that they believe will deliver better than the market average, growth returns in their revenues or earnings, and therefore have higher ratios such as P/E and PEG. Growth investors often chase the market's highfliers and look for companies that reinvest their earnings or capital for future company development and expansion.

But I think what many investors miss is that although value and growth are the opposite sides of the same coin, one can and should have exposure to both investment styles as historically each style has outperformed the other at some point due to the fact that they tend to cluster in different sectors.

Sectors and Past Performances:

Value stocks are typically linked to solid, well-established sectors such as Financials, Industrials, Energy and Consumer Staples and therefore their profits are more sensitive to economic trends. And as result, they often get hit hard during bear markets and usually rise disproportionately in the initial rebounds of a bull market.

By contrast, Growth stocks are often found in sectors that have a strong potential for growth, such as Emerging Markets, Healthcare, and the of course, Technology.

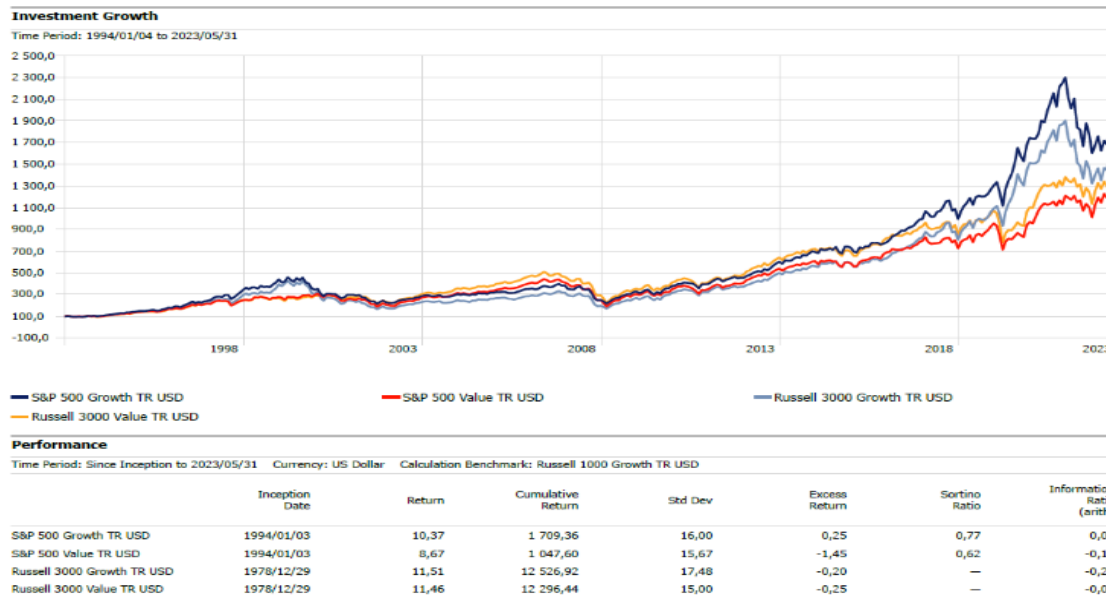
To put this into context, dated back from 1927, value stocks have had an annual outperformance of around 4.1% however, over the past 2 to 3 decades growth stocks have outperformed value.



Source: Dimensional, 2022



To add some more data to this, if we take two indices such as the Russell 3000 Growth and The Russell 3000 Value and compare them over the past 45 years (*dated back 1978*) they both generated almost identical annualized dollar returns whereby Growth returned 11.50% and value 11.46% (as of 31st May 2021):



Source: Morningstar Direct, 2023

BUT, when we start to compare this to more recent times such as a five-, ten- and twenty-year period we see that growth has outstripped value (significantly).

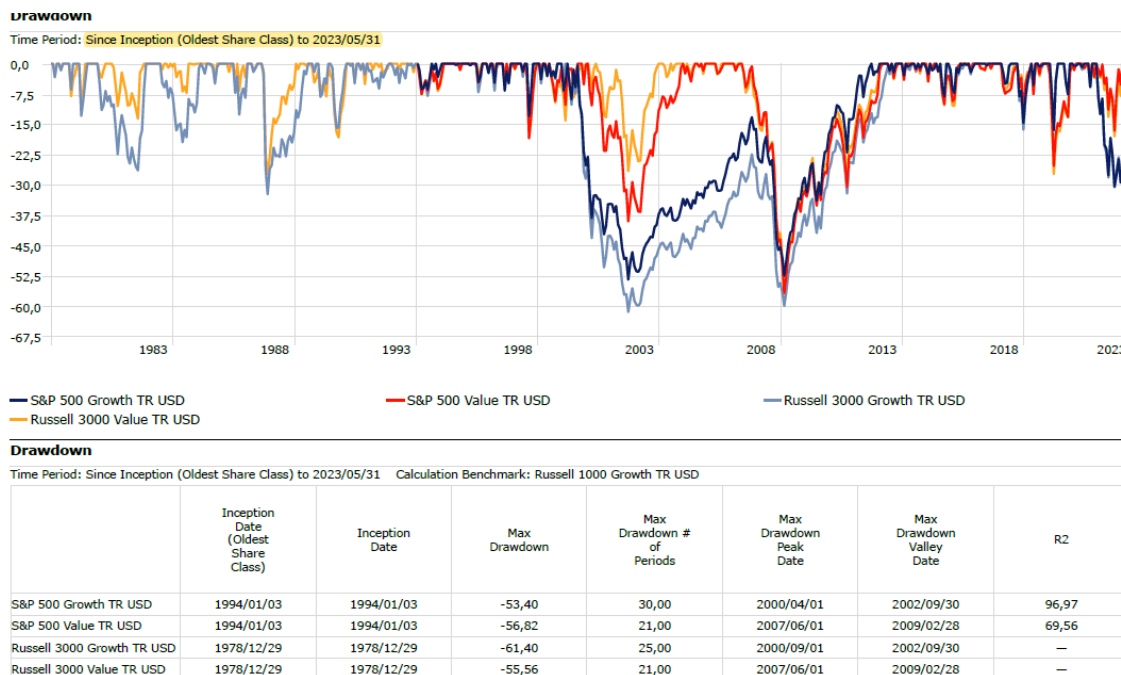
	Russell 3000 Growth	Russell 3000 Value	Outperformance
YTD (13/06/23)	24,03%	1,73%	22,30%
5 Year	13,09%	6,45%	6,64%
10 Year	14,29%	8,29%	6,00%
20 Year	11,06%	8,21%	2,85%

BUT, purely looking at returns never paints the full picture as one must consider the key drivers and risks behind those returns such as volatility and importantly the drawdown of each investment style.



Risks and Diversification:

Although in recent years there's been a notable disconnect between growth and value, Growth has had more volatility and significantly steeper drawdowns.



Source: Morningstar Direct, 2023

To add context, last year the Russell 3000 Growth index finished year down -28,97% whilst the Value Index finished the year down -7,08% (growth was 21% worse off). And the majority drawdown from growth last year came from big company names such as Amazon - 49,62%, Alphabet - 39,09%, Microsoft - 28,02%, Tesla - 65,55% and the list goes on (on a side note, ironically one could argue that those stocks could have been considered as potential value investments given their selloffs).

However, the point is that this pattern tends to repeat itself especially in inflationary environments as there is an inverse correlation between growth stock prices and inflation.

On the other side of the coin, when it comes to value, we see that many investors get caught in a "value trap" whereby investors look for a bargain and buy into a cheap stock which ultimately continues to either remain cheap or drop in price.

So, one needs to remain careful not to fall into this trap. Terry Smith summed it up well when he said "*Cheapness will not transform it into a good business and in the long run it is the quality of the business that you invest in which determines your returns*".

In summary, growth and value investing styles are often pitted against each other as an either-or option. But portfolios do have room for both. Within our own Paragon portfolio allocations we certainly allocate to both investment styles as remaining diversified is a key metric for long-term portfolio returns and risk mitigation.



Currently if you don't have an allocation to growth you will be underweight tech and would have missed most of the large cap AI tech rally. If you don't have an allocation to value and the FED does pivot leading to higher commodity prices will potentially miss that rally.

Historic Returns:

Calendar Year Returns

Data Point: Return	Calculation Benchmark: Russell 1000 Growth TR USD																				
	YTD	2022	2021	2020	2019	2018	2017	2016	2015	2014	2013	2012	2011	2010	2009	2008	2007	2006	2005	2004	2003
S&P 500 Growth TR USD	13,98	-29,41	32,01	33,47	31,13	-0,01	27,44	6,89	5,52	14,89	32,75	14,61	4,65	15,05	31,57	-34,92	9,13	11,01	4,00	6,13	25,66
S&P 500 Value TR USD	4,94	-5,22	24,90	1,36	31,93	-8,95	15,36	17,40	-3,13	12,36	31,99	17,68	-0,48	15,10	21,18	-39,22	1,99	20,80	5,82	15,71	31,79
Russell 3000 Growth TR USD	19,77	-28,97	25,85	38,26	35,85	-2,12	29,59	7,39	5,09	12,44	34,23	15,21	2,18	17,64	37,01	-38,44	11,40	9,46	5,17	6,93	30,97
Russell 3000 Value TR USD	-1,63	-7,98	25,37	2,87	26,26	-8,58	13,19	18,40	-4,13	12,70	32,69	17,55	-0,10	16,23	19,76	-36,25	-1,01	22,34	6,85	16,94	31,14

Source: Morningstar Direct, 2023

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