



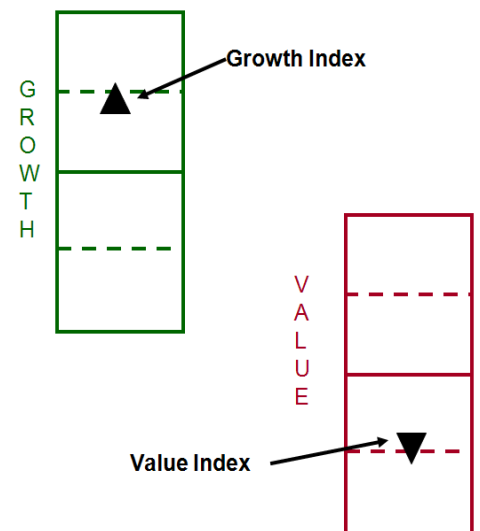
A Prescient Prognostication

July 1, 2012 Ron Surz Ron@PPCA-Inc.com 949/488-8339

Peer group investment performance for periods ending 6/30/12 will be available in about a month. Here is my prediction of what they will say: Growth managers lose. Value managers win.

This prognostication obviously has nothing to do with skill. Flawed indexes and biased peer groups comprise my crystal ball. Peer groups distort the very fabric of performance evaluation in a predictable and troubling way, and lead to a common belief that active managers add the most value when their style is out favor, which is simply not true.

Check me out in a month, when peer groups become available. Most large cap growth managers will underperform their benchmark for the year, three years and five years ending 6/30/12. Most large cap value managers will outperform their benchmark. The picture will look like the graph on the right. Growth managers are losers and value managers are winners.



These results are categorically wrong for two reasons:

1. **The benchmarks are wrong.** Popular indexes use Price/Book as their primary style classification metric. The book values of distressed financials are grossly overstated so these companies are currently misclassified as value. For more details see [Style of Financial Stocks](#).
2. **Peer groups are loaded with biases.** One such bias is particularly problematic because no one knows about it. Classification bias makes winners out of losers and losers out of winners, snatching defeat from the jaws of victory. For more details see [Peer Groups Will Mess You Up](#).

Most importantly, do not make a common mistake. Many, including heads of investment manager research, justify the use of active managers because they shine when their style is out of favor, which is simply not true. The reality is that benchmarks are wrong and peer groups are biased, so performance rankings are worse than useless; they're downright misleading.

Do you use peer groups? Indexes? Were you aware of the myriad problems? Do you care?