The Truth About Investment Styles. What Determines Value and Growth?

- Is Apple a growth stock or a value stock?
- Why are Russell style indexes so popular?
- Did you know there's a new third generation of style analysis?

Like politics, most investment managers have a declared party affiliation that they call either Value or Growth. But life is rarely that simple. All value managers are not alike, nor are all growth managers. Importantly, the distinctions are complicated by a lack of standardization. For example, the following table shows how style index firms currently disagree on three popular stocks:

	Russell	S&P	Surz
Johnson & Johnson	Value	Growth	Core
General Electric Corporation	Value	Value	Growth
Apple	Growth	Growth	Value

Good chance you've picked the style you agree with, but do you know why? Apple is not a growth stock if you use its current Price/Earnings ratio of 11, but it is growth if you use its 4-times Price/Book.

<u>Choosing your style provider</u>

As you can see, style providers can disagree, so how can you decide which one you like? You could start by learning their rules by visiting these websites:

- S&P
- Russell
- Surz

I'll spare you some time and pain by summarizing the key classification variables used by these firms:

	Russell	S&P	Surz
Primary Classification	Price/Book	Price/Book	Price/Earnings
Secondary	Earnings Growth	Price/Earnings	Yield
Third		Earnings Growth	Price/Book

So it really boils down to a choice between Price/Book and Price/Earnings. The rationale for Price/Book is that a stock trading at a price near or below its cost basis is inexpensive, a good value. But as Laurence Siegel states in a CFA Research Foundation monograph, "*Book value is mostly a* ***historical accident****. It is the accounting profession's estimate of the company's value; it reflects what the company paid for assets."* Siegel calls Book Value a "stock variable" in contrast to Earnings, which are a "flow variable." Earnings are about today, whereas book value is history. Serious distortions can be caused by the use of book value. During the financial crisis in 2009, the prices of distressed banks fell while their book values remained unchanged, so these very risky stocks became deep value by the Russell and S&P Price/Book definition. By contrast, these very same banks were classified as aggressive growth by the Surz definition because their earnings plummeted much faster than their prices.

It wouldn't surprise me if you haven't heard of the Surz Style Pure© Indexes that I created in 1986. Other than being imitated by Morningstar, they're an undiscovered treasure that features "Core", defined as the stocks in between value and growth – ideal for core-satellite investing. I'm making them available to you in a way you'll like. You can actually "see" the styles of the stocks you own in an X-Y graph that shows size and style.

A free tool

Style analysis is in its third generation and the good news is that it's interactive. You can play with the results and choose various options. Simply enter your holdings into the portal and see what you see. It's particle finance.