

GROWTH VS. VALUE: AN UNFINISHED DEBATE IN STYLE INVESTING

Brian Manby, CFA, Senior Associate, Research

Key Takeaways:

- Despite Growth's dominance since 2017, historical data underscores the resilience and long-term potential of Value investing during market reversals.
- Growth's leadership over the past decade has been fueled by sentiment-driven multiple expansion, which entails greater risks should investor optimism waver.
- The valuation gap between Growth and Value suggests a compelling opportunity for portfolio rebalancing in anticipation of a potential shift in market leadership.

2024 delivered yet another knockout for Growth over Value in the realm of U.S. style investing. For the second consecutive year, the Russell 3000 Growth Index eclipsed its Value compatriot by double digits, widening the cumulative performance gap to nearly 60% since the end of 2022.

The drastically different fortunes exacerbate the lopsided recent history between the two, prompting many investors to wonder whether the style spectrum has encountered an inflection point.

Should the Growth-versus-Value debate even continue? Perhaps Growth is the unanimous victor.

But decades of market history should suppress these myopic conclusions. Growth's superiority is a more recent phenomenon than most investors realize. Its leadership materialized within the past decade, driven by several fundamental and sentiment-based advantages that simultaneously discredited Value.

However, a longer-term view proves Value's merit. More importantly, it dispels the notion that Growth's outperformance is evidence of an enduring trend. **Instead, it reinforces that Value investing should not be dismissed as obsolete but utilized for any anticipated reversal in Growth leadership.**

THE EXTENDED HISTORY OF VALUE

Over the past century, Value's performance record makes a declarative statement about its efficacy. Using Eugene Fama and Ken French's data library, which amasses nearly a century of monthly return data points for various investment factors, Value disproportionately outperformed Growth dating back to 1926.

The chart below indexes the returns for two of their U.S. Value and Growth portfolios beginning years ago. Plotting the two relative to each other shows that extrapolations about Growth based solely on its recent winning streak may be flawed.

Figure 1: Value Maintains a Long-Term Advantage Over Growth Over Past 50 Years



Sources: WisdomTree, Fama-French Data Library, as of 12/31/2024, which represents the latest available data. Growth is represented by returns from U.S.-listed companies from the Center for Research on Securities Prices (CRSP®) database within the bottom 30th percentile based on the book value of equity-to-market value of equity (book-to-market). Value is represented by securities from the same geographic universe, within the top 30th percentile based on the book value of equity-to-market value of equity.

But starting points matter, so any value verdict needs to consider performance measured from various reference dates. The Fama-French dataset begins in the mid-1920s and offers more than nine full decades of return observations to test value's merit.

Figure 2: Annualized Growth vs. Value Total Returns by Decade

Decade	Growth	Value	Difference
July 1926 - Dec. 1929	20.0%	17.2%	-2.8%
1930s	1.6%	-3.2%	-4.8%
1940s	6.9%	17.3%	10.4%
1950s	17.7%	22.1%	4.4%
1960s	8.0%	12.2%	4.2%
1970s	3.8%	13.8%	10.0%
1980s	15.1%	20.7%	5.6%
1990s	19.2%	16.1%	-3.1%
2000s	-1.2%	5.6%	6.8%
2010s	15.1%	11.2%	-3.9%
2020 - 2024	18.2%	15.2%	-3.0%

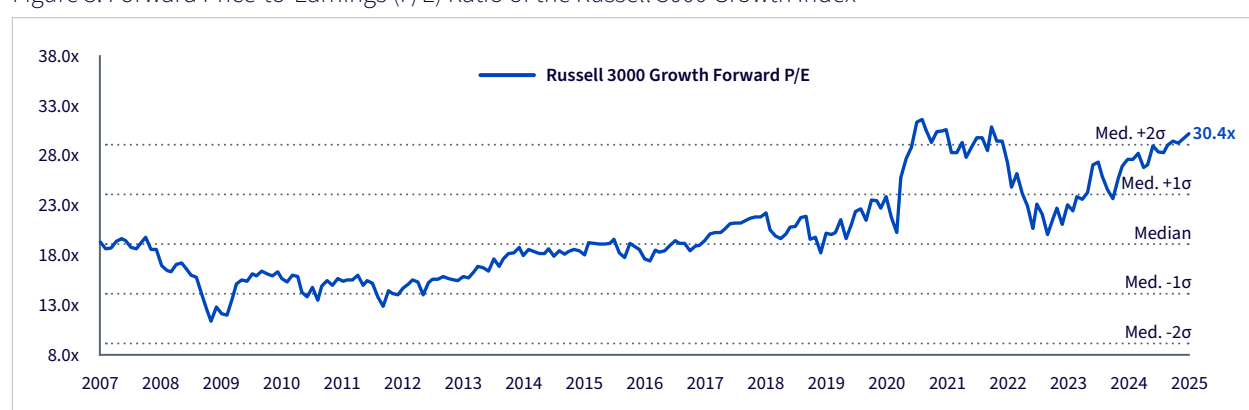
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Fortunately, its extended history is more convincing than recent returns suggest. It had 50 years of consistent success versus Growth in the mid-20th century, which confirms the core tenet of value philosophy: **Valuations matter over the long term and significantly affect returns.**

That point is especially relevant today, when investors confront extended U.S. Growth valuations with little indication that they will soon retrace. Not only does this threaten existing allocations by introducing downside risk if earnings or fundamentals disappoint, but it also creates challenging entry points for those pursuing new investments.

Growth multiples are currently two standard deviations above their median valuation since the beginning of our data availability in 2007. The forward price-to-earnings (P/E) ratio of the Russell 3000 Growth Index is above 30, which is its highest since October 2021 and a 96th percentile observation over this timeframe.

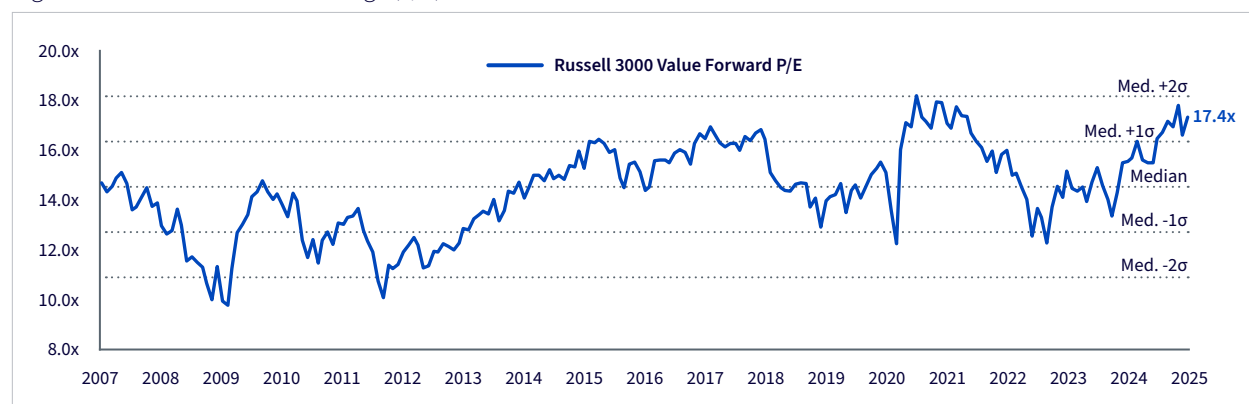
Figure 3: Forward Price-to-Earnings (P/E) Ratio of the Russell 3000 Growth Index



Sources: WisdomTree, FactSet, as of 1/31/2025. You cannot invest directly in an index.

Meanwhile, value multiples are more subdued. The Russell 3000 Value Index currently trades at 17x next year's earnings, which is slightly more than one standard deviation above its median multiple since 2007. This may be somewhat expensive relative to its own history, but it's more palatable than corresponding Growth multiples. It's also in line with the S&P 500's median forward P/E over the past 30 years, which is also 17x forward earnings.

Figure 4: Forward Price-to-Earnings (P/E) Ratio of the Russell 3000 Value Index

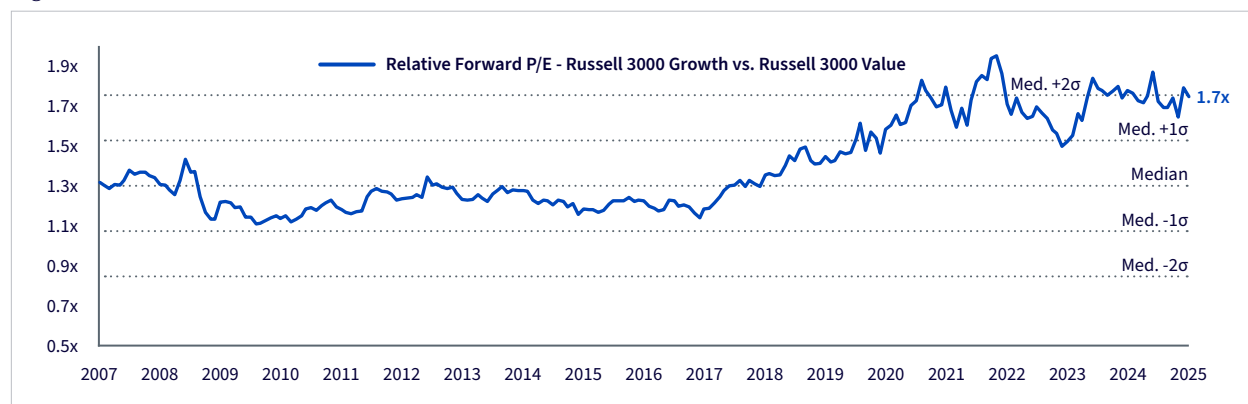


Sources: WisdomTree, FactSet, as of 1/31/2025. You cannot invest directly in an index.

Evidently, there’s a valuation discrepancy between Growth and value markets today, proven further by the relative multiple between the two styles. **Growth’s forward P/E remains at a steep premium to value and two standard deviations above its median relative multiple.**

This is an 87th percentile observation, and the rise in valuations coincides perfectly with Growth’s ascent, starting in 2017. Relative multiples have remained in this territory for virtually the entire post-pandemic environment. The most recent nadir was during 2022’s bear market, where it remained a full standard deviation above its historical median.

Figure 5: Relative Forward P/E Ratio of Russell 3000 Growth Index vs. Russell 3000 Value Index



Sources: WisdomTree, FactSet, as of 1/31/2025. You cannot invest directly in an index.

Return attribution since the start of the Growth cycle in 2017 illustrates the valuation divergence and its performance effects as well.

Figure 6: Annualized Total Return Attribution: 2017 - 2024



Sources: WisdomTree, FactSet, Russell, as of 12/31/2024. Past performance is not indicative of future results. You cannot invest directly in an index. Figures represent the contribution to index-level total returns attributable to each factor. Earnings growth is the collective contribution of profit margin expansion and sales growth.

Unsurprisingly, Growth trounced Value by 10% per year due to superior earnings growth and multiple expansion. The latter, however, differs significantly from the former, especially over this timeframe.

While earnings growth is based on improvements in underlying business health and efficient operations, such as margin and sales growth, multiple expansion is sentiment-driven and a fluid indication of investor attitudes. It represents the extent to which investors are willing to pay more per dollar of earnings, which can be volatile and prone to sudden reversal.

This 6.6% gap between Growth and Value explains a significant portion of their return differential. But it also suggests that there's a speculative spirit prevailing within Growth, which is inherently risky. If investors are willing to pay more for profits, then companies will be pressured to report increasingly impressive results to confirm investors' prescribed valuations. If they falter or underwhelm, Growth leadership could rapidly unwind.

Despite the speculative fervor, however, Growth's fundamental advantages over Value for most of the past decade still cannot be ignored: **Earnings growth added nearly 11% per year, which is about 5% more than its impact for Value.** Surely, this accentuated the effects from multiple expansion.

But the past eight years are still a subset of market history. Extending the analysis beyond Growth's recent leadership period balances the argument.

Figure 7: Annualized Total Return Attribution: 1996-2016



Sources: WisdomTree, FactSet, Russell, as of 12/31/2024. Past performance is not indicative of future results. You cannot invest directly in an index. Figures represent the contribution to index-level total returns attributable to each factor. Earnings growth is the collective contribution of profit margin expansion and sales growth.

The two decades preceding today's Growth cycle belonged convincingly to Value. From 1996 through 2016, Value outperformed by about 1.6% per year. This timeframe coincides with the Tech bubble of the early 2000s, when Growth last dominated in a similar fashion, and the collapse of U.S. markets during the global financial crisis (GFC).

Despite these obstacles, Value was supported by fundamental improvements and performed admirably.

Earnings growth lagged but kept better pace with Growth than it has for the past eight years, but the gap was partially offset by another pillar of Value investing. **Dividends contributed an extra 2.5% per year, or a 1.3% advantage over Growth.** Valuations were relatively stable across both styles, but Growth's multiple contraction again illustrates how investors can punish companies over time for falling short of lofty earnings aspirations.

But even this 20-year period can be segmented into separate regimes that delivered drastically different fortunes for Growth and Value, demonstrating how quickly markets can reward one factor, punish another and suddenly reverse.

GROWTH'S DOMINANCE FORESHADOWS THE TECH BUBBLE

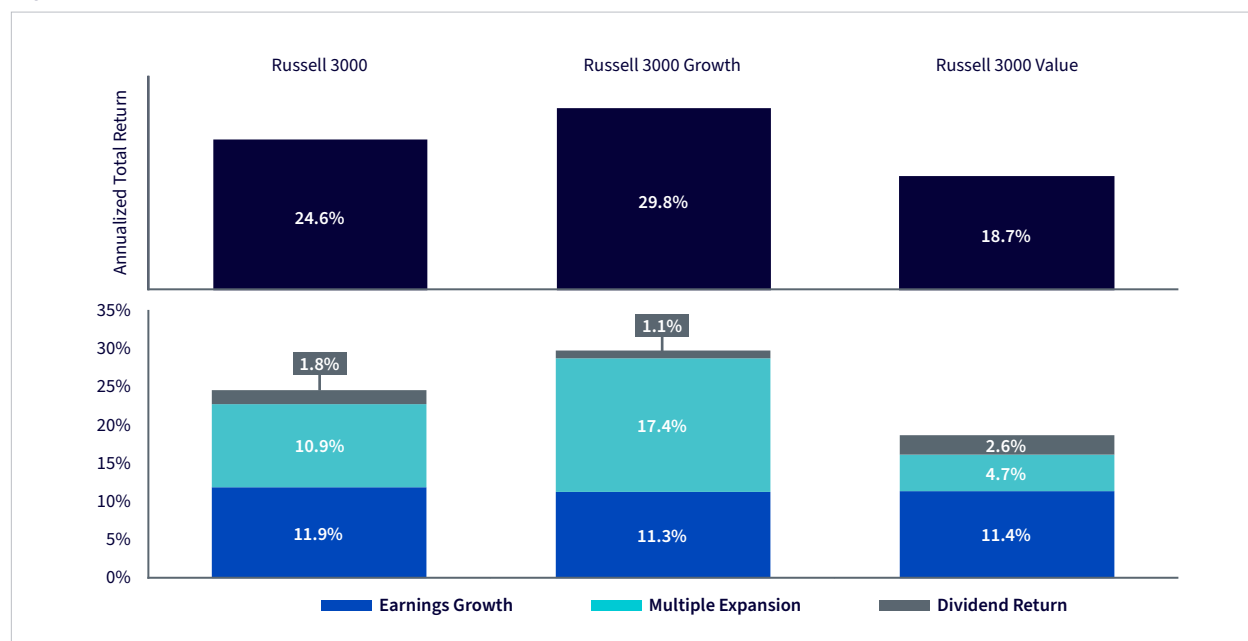
The final four years of the 20th century provided a raging bull market that laid the foundation for the Tech bubble. Growth trumped Value by more than 11% per year from 1996 through 1999, falling just shy of 30% annualized gains.

"Animal spirits" prevailed as multiple expansion was the largest contributor to Growth's ascent. Nearly two-thirds of Growth's performance was attributable to investors' insatiable demand for promising stocks with stellar earnings growth, no matter the cost. Price-to-earnings ratios ballooned as a result, climbing from 23x at the end of 1995 to 42x four years later.

Value rode the bull market as well, but with tempered results. It matched the earnings growth of the Russell 3000 Growth Index through a healthy mix of margin and sales growth, yet investors only rewarded it with modest multiple expansion. Its P/E rose less than three points in four years, climbing from 15x to 18x.

In hindsight, the drastically different attitudes toward earnings valuation were evidence of a bubble. Both styles were propelled by impressive earnings growth, yet investors rewarded Growth's results more favorably than Value's, which explains its entire outperformance before the bubble's imminent burst.

Figure 8: Annualized Total Return Attribution: 1996-1999



Sources: WisdomTree, FactSet, Russell, as of 12/31/2024. Past performance is not indicative of future results. You cannot invest directly in an index. Figures represent the contribution to index-level total returns attributable to each factor. Earnings growth is the collective contribution of profit margin expansion and sales growth.

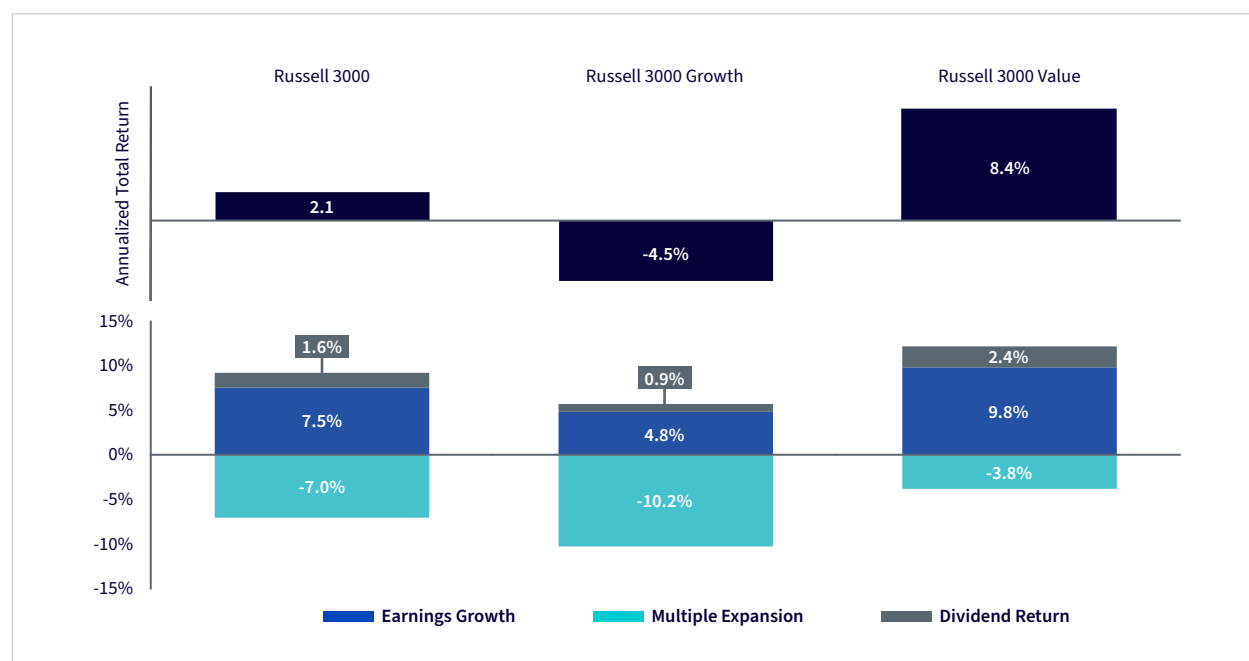
VALUE'S RESILIENCE AMID GROWTH'S RECKONING

When the bubble burst at the start of the 21st century, it introduced a painful cycle for Growth. Over the next seven years, it fell 4.5% annually as investors recalibrated their earnings valuations and licked their wounds. Its P/E fell by more than half, from 42x to 20x by the end of 2006.

Meanwhile, Value remained robust and maintained impressive results amid Growth's meltdown. It returned 8.4% per year, outperforming Growth by nearly 13%, with steady contributions from earnings growth and dividends.

Multiples contracted for both styles during the seven-year period, but since Value was relatively less affected by the preceding Growth mania, it required little correction from investors. Growth's valuation retracement was more severe and punished returns.

Figure 9: Annualized Total Return Attribution: 2000-2006



Sources: WisdomTree, FactSet, Russell, as of 12/31/2024. Past performance is not indicative of future results. You cannot invest directly in an index. Figures represent the contribution to index-level total returns attributable to each factor. Earnings growth is the collective contribution of profit margin expansion and sales growth.

Once again, valuation changes delivered diverging fortunes with drastic performance effects. The Growth implosion was a powerful example of how suddenly markets can reverse when sentiment shifts.

More importantly, however, it proved an important lesson for investors spurned by Growth. When stability was needed most, Value provided its very premise: a trifecta of **superior earnings growth, modest valuations and a dividend advantage**.

STYLE PERFORMANCE IN THE GFC'S AFTERMATH

The next decade featured mixed results that muddied the Value-versus-Growth debate. The GFC emerged in late 2007 and devastated the U.S. equity market with no impunity or concern for investment styles. The 18-month peak-to-trough decline from September 2007 through March 2009 roiled markets and threatened the global financial system, sending Growth and Value down 40% to 50% apiece. However, the volatility ultimately helped rebalance the style scale during the ensuing recovery.

Figure 10: Annualized Total Return Attribution: 2010-2016



Sources: WisdomTree, FactSet, Russell, as of 12/31/2024. Past performance is not indicative of future results. You cannot invest directly in an index. Figures represent the contribution to index-level total returns attributable to each factor. Earnings growth is the collective contribution of profit margin expansion and sales growth.

From 2010 through 2016, Growth and Value kept approximately equal pace and were propelled by similar results. Growth outperformed Value by about 30 basis points per year, primarily due to an earnings growth advantage compounded by multiple expansion. Value's earnings contribution fell short, but its multiple expanded proportionally to Growth's. Once again, dividend return helped offset the shortfall.

In GFC's aftermath, it's notable that the two diametrically opposite investment styles both performed so well that it only enriched the Value-versus-Growth debate rather than settle it. Normally, after an economic calamity, investors might expect an inflection point to emerge with a definitive signal about the market's direction, yet the aftermath of the global financial crisis provided anything but.

BALANCING OPTIMISM WITH A HISTORICAL PERSPECTIVE

Growth's outperformance over Value for the past eight years has certainly been justified by fundamentals and compounded by investor optimism. But, recent results should not be extrapolated into future conclusions. In our view, today's style debate has grown too dismissive of Value despite contrary evidence across decades of market history and recent performance regimes.

Today, Growth investors remain unbothered by historically high multiples, no doubt infatuated by the perceived limitless potential of AI and companies' willingness to spend handsomely to harness it. But over the past few decades, valuations demonstrated a two-way influence on returns. They may gradually increase before anyone expresses concern, but when fortunes turn, they often rapidly reverse and harm portfolios. As the 21st century has already proven, subsequent market recoveries are often uneven and unpredictable.

We encourage investors to be cautious and discerning of prevailing Growth valuations, especially if they're neglecting Value allocations in the process. Any change in sentiment could unwind the Growth leadership cycle, and valuations may be the catalyst.

If that materializes, Value may be more resilient for the long term, just as decades of market history reliably suggest.

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