Value vs. Glamour: A Study of the Indices

As described in the Brandes Institute research "Value vs. Glamour," value stocks have outperformed glamour stocks over the long term in both U.S. and non-U.S. markets. The Institute's research used valuation measures such as price-to-book, price-to-earnings, and price-to-cash flow ratios to distinguish between value and glamour stocks. The approach replicates and expands upon the methodology originally developed by Professors Lakonishok, Shleifer, and Vishny in their landmark study, "Contrarian Investment, Extrapolation, and Risk," published in 1994.

But what about commonly used benchmarks? Over the long term, aren't glamour stocks just growth stocks, and aren't returns for growth and value indices about the same?

While the Brandes Institute research used 5-year horizon measurements, questions have been raised as to whether similar differences occur on an annual basis, when measured by traditional value and growth indices. Using Russell Value Indices as a proxy for U.S. value stocks and the Russell Growth Indices as a proxy for U.S. growth stocks, we compared returns since the indices' inception in 1979.

	Large Cap		Small Cap	
	Russell 1000 Value Index	Russell 1000 Growth Index	Russell 2000 Value Index	Russell 2000 Growth Index
Annualized Return*	14.60%	11.89%	15.92%	10.32%
Difference (Value minus Growth)	2.71%		5.60%	

*since inception on Jan. 1, 1979 through Dec. 31, 2006

For large- and small-cap stocks, value outperformed growth over the 28-year period ending December 31, 2006. Using calendar years, we measured how often value outperformed growth. Of the 28 years in this study, the large-cap Russell 1000 Value Index ended ahead of the Russell 1000 Growth Index 16 times, or 57% of the years. The smaller-cap Russell 2000 Value Index outperformed its growth counterpart 64% of the years, or 18 out of 28.

Using annual returns data we also measured returns over rolling[1] 5-year periods since 1979:

	Large Cap		Small Cap	
	Russell 1000 Value Index	Russell 1000 Growth Index	Russell 2000 Value Index	Russell 2000 Growth Index
Average of Rolling, 5-Year Periods*	14.32%	11.91%	14.89%	8.52%
Difference (Value minus Growth)	2.41%		6.37%	

*since inception on Jan. 1, 1979 through Dec. 31, 2006

[1]Rolling periods represent a series of overlapping, smaller time periods within a single, longer-term time period. A hypothetical example is the 20-year time period from 12/31/82 through 12/31/02. This long-term period consists of 16 smaller five-year "rolling" segments. The first segment is the five-year period from 12/31/82 to 12/31/87. The next rolling segment is the five-year period from 12/31/83 to 12/31/88, and so on.

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During the 24, rolling 5-year periods in our study, among large-cap stocks, the Russell 1000 Value Index ended ahead of the Russell 1000 Growth Index 16 times, representing 67% of the 5-year periods. For small caps, the Russell 2000 Value Index outperformed the Russell 2000 Growth Index in 22 of the 24 5-year periods, or 92% of the time.

Similarly compelling results were uncovered in a study of non-U.S. indices. Using the MSCI EAFE Value Index as a proxy for non-U.S. value stocks, and the MSCI EAFE Growth Index as a proxy for non-U.S. growth stocks, we compared returns during the same period used for the Russell Indices.

On an annual basis, our study found that the value component of the MSCI EAFE outperformed the growth component during 21 of the 28 years studied, or 75% of the period under review. In addition to this persistent outperformance, value stocks averaged a 4.3% performancepremium annually over their growth counterparts. Examining performance on a rolling 5-year basis, the value component of the MSCI EAFE outperformed the growth component in 23 of the 24 5-year rolling periods, or 96% of the time.

To investigate these results among large- and small-cap non-U.S. stocks, we used the Citigroup EMI (Extended Market Index) and PMI (Primary Market Index) World ex-U.S. Indices asproxies, and examined the growth and value components of each index. Although annual performance data is only available beginning 1990, we found a convincing value premium across both large- and small-cap non-U.S. stocks. On an annual basis, large-cap non-U.S. value stocks outperformed their growth equivalents in 12 out of the 17 years reviewed, or 71% of the time. Parallel results were found among small-cap non-U.S. value stocks.

	Large Cap		Small Cap	
	Citigroup PMI World ex-U.S. Value Index	Citigroup PMI World ex-U.S. Growth Index	Citigroup EMI World ex-U.S. Value Index	Citigroup EMI World ex-U.S. Growth Index
Annualized Return*	7.99%	5.88%	8.23%	5.33%
Difference (Value minus Growth)	2.11%		2.90%	

*Jan. 1, 1990 through Dec. 31, 2006

We also measured returns over rolling 5-year periods since 1990:

	Large Cap		Small Cap	
	Citigroup PMI World ex-U.S. Value Index	Citigroup PMI World ex-U.S. Growth Index	Citigroup EMI World ex-U.S. Value Index	Citigroup EMI World ex-U.S. Growth Index
Average of Rolling, 5-year Periods*	7.97%	5.91%	7.94%	4.83%
Difference (Value minus Growth)	2.07%		3.11%	

*Jan. 1, 1990 through Dec. 31, 2006

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These findings demonstrate:

- Value stocks have outperformed growth stocks over the long term.
- Value stocks generally have delivered *consistent* outperformance.
- Value stocks' advantages appear evident for both large caps and small caps.
- Value stocks have outperformed growth stocks in non-U.S. markets.

The information provided should not be considered a recommendation to purchase or sell any particular security. It should not be assumed that any security transactions, holdings, or sectors discussed were or will be profitable, or that the investmentrecommendations or decisions we make in the future will be profitable or will equal the investment performance discussed herein. International and emerging markets securities entail risk such as currency fluctuation and political instability. Please note that all indices are unmanaged and are not available for direct investment. Past performance is not a guarantee of future results. No investment strategy can assure a profit orprotect against loss.

The Citigroup Extended Market Index (EMI) World ex-U.S. Growth Index is an unmanaged index that tracks small capitalization companies from developed markets around the world excluding the United States, that have a growth style. The style is determined by the equal weighted relative magnitude of three growth and four value variables: 5-year historical EPS growth rate, 5-year historical sales per share growth, 5-year average annual internal growth rate, book value per share, price to sales, price to cash flow and dividend yield. It includes the reinvestment of dividends and income but does not reflect fees, brokerage commissions, withholding taxes, or other expenses of investing.

The Citigroup Extended Market Index (EMI) World ex-U.S. Value Index is an unmanaged index that tracks small capitalization companies from developed markets around the world excluding the United States, that have a value style. The style is determined by the equal weighted relative magnitude of three growth and four value variables: 5-year historical EPS growth rate, 5-year historical sales per share growth, 5-year average annual internal growth rate, book value per share, price to sales, price to cash flow and dividend yield. It includes the reinvestment of dividends and income but does not reflect fees, brokerage commissions, withholding taxes, or other expenses of investing.

The Citigroup Primary Market Index (PMI) World ex-U.S. Growth Index is an unmanaged index that tracks large capitalization companies from developed markets around the world, excluding the United States, that have a growth style. The style is determined by the equal weighted relative magnitude of three growth and four value variables: 5-year historical EPS growth rate, 5-year historical sales per share growth, 5-year average annual internal growth rate, book value per share, price to sales, price to cash flow and dividend yield. It includes the reinvestment of dividends and income but does not reflect fees, brokerage commissions, withholding taxes, or other expenses of investing.

The Citigroup Primary Market Index (PMI) World ex-U.S. Value Index is an unmanaged index that tracks large capitalization companies from developed markets around the world, excluding the United States, that have a value style. The style is determined by the equal weighted relative magnitude of three growth and four value variables: 5-year historical EPS growth rate, 5-year historical sales per share growth, 5-year average annual internal growth rate, book value per share, price to sales, price to cash flow and dividend yield. It includes the reinvestment of dividends and income but does not reflect fees, brokerage commissions, withholding taxes, or other expenses of investing.

The Morgan Stanley Capital International (MSCI) EAFE Growth Index is an unmanaged index consisting of equities from Europe, Australasia, and the Far East. The index is generally considered to be representative of international growth stock market activity and often used as a benchmark for international growth equity portfolios. The MSCI EAFE index includes dividends and distributions net of corresponding withholding taxes, but does not reflect fees, brokerage commissions, or other expenses of investing.

The Morgan Stanley Capital International (MSCI) EAFE Value Index is an unmanaged index consisting of equities from Europe, Australasia, and the Far East. The index is generally considered to be representative of international value stock market activity and often used as a benchmark for international value equity portfolios. The MSCI EAFE index includes dividends and distributions net of corresponding withholding taxes, but does not reflect fees, brokerage commissions, or other expenses of investing.
The Russell 1000 Value Index is an unmanaged index that measures the performance of those Russell 1000 Index companies with lower

price-to-book ratios and lower forecasted growth rates. It includes the reinvestment of dividends and income, but does not reflect fees, brokerage commissions, or other expenses of investing.

The Russell 1000 Growth Index is an unmanaged index that measures the performance of those Russell 1000 Index companies with higher price-to-book ratios and higher forecasted growth rates. It includes the reinvestment of dividends and income, but does not reflect fees, brokerage commissions, or other expenses of investing.

The Russell 1000 Index is an unmanaged index that measures the performance of the largest 1000 securities in the Russell 3000 Index. It includes the reinvestment of dividends and income, but does not reflect fees, brokerage commissions, or other expenses of investing.

The Russell 2000 Growth Index is an unmanaged index that measures the performance of those Russell 2000 Index companies with higher price-to-book ratios and higher forecasted growth rates. It includes the reinvestment of dividends and income, but does not reflect fees, brokerage commissions, or other expenses of investing.

The Russell 2000 Value Index is an unmanaged index that measures the performance of those Russell 2000 Index companies with lower price-to-book ratios and lower forecasted growth rates. It includes the reinvestment of dividends and income, but does not reflect fees, brokerage commissions, or other expenses of investing.

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11988 El Camino Real
Suite 500
P.O. Box 919048
San Diego, CA 92191-9048
858.755.0239
800.237.7119
Fax 858.755.0916
brandesinstitute@brandes.com
www.brandes.com/institute

0907