THE DANA VIEWPOINT

September 29, 2020
Dow: 27,452

Growth vs. Value

Growth or value? This question has been a facet of investing for decades, but has come into even more pointed focus in the last few months. Growth stocks have continued a decade-long trend and massively outperformed value stocks for much of 2020, but in recent weeks, performance has been more even. The change suggests many of the factors that propelled growth forward since the pandemic have been fully absorbed by the market. But is that enough to stage a changing of the guard for value investing?

We believe two main factors benefited growth stocks coming out of the pandemic-induced economic slowdown. First, the areas of the economy that the pandemic hurt most tended to be lower-wage, lower-productivity industries that provide person-to-person service. Examples include retail, transportation, airlines, hotel, and restaurant industries. By and large, these are value stock categories. Energy stocks, which are another large component of value indices, were also punished as the economic slowdown dampened demand.

Companies in higher-productivity areas, such as technology, were less affected by the pandemic. These businesses primarily fall into the growth category. Expectations of an extended low inflation environment have also supported growth stocks. Growth stocks' valuation is based largely on the stream of earnings they will earn in the future. Low inflation means the value of those future earnings streams are worth more because they won't be inflated away.

These metrics had helped push growth stock valuations higher in recent months. At some point, markets were bound to reassess extreme valuations. That has happened recently with the tech-heavy NASDAQ falling 10% into correction territory just three days after setting an all-time high at the beginning of September.

Meanwhile, low inflation is a headwind for a value company. These companies generally have more leverage than growth companies. If there's low inflation, a dollar in the future maintains its value. Lower inflation increases the debt burden of leveraged companies in real dollar terms. Low inflation also makes it more difficult for these companies to raise prices or increase revenue to aid in servicing their debt.

The recent slump by growth stocks has put growth and value performance roughly in line with each other since the end of July. Many wonder if extreme valuation differences between growth and value stocks

(CONTINUED ON REVERSE SIDE)

mean value is now due for its own run of outperformance. For this to happen, we think the market will need more signs of economic improvement.

Value stocks are typically more economically sensitive than growth stocks, but that is even more true in the recent downturn. To a large extent, value stocks are associated with companies that primarily benefit when people are moving around and spending money. That just doesn't happen when people are nervous about coming out of their homes and engaging in direct social contact with other individuals.

However, news about the virus has started to sound more encouraging. Although the number of new daily confirmed cases remains high, the infection rate is trending down as the number of confirmed cases divided by the number of tests is falling in many areas. Offices are starting to reopen. For example, JPMorgan recently announced it will call its traders back to their New York offices. Once we see more states reopen and the economy begin to rebound, we wouldn't be surprised to see value outperform growth.

At Dana, our strategies are core equity strategies. We look for investments that have characteristics of both growth and value stocks. We are valuation-conscious, but we don't make directional calls in our portfolio with an intentional shift toward value or growth. However, some of our strategies have started to take advantage of attractive valuations and invest in companies in the hotel, travel, and restaurant industries that would benefit as the economy gradually reopens.

We are also finding opportunity in stocks that have a good "self-help" story. The one silver lining in the recent downturn is that it has forced management teams to re-evaluate costs and think hard about how they can run their business more efficiently. Many have cut their capital expenditures or are looking for ways to deploy them more efficiently. We believe some of these businesses are poised to come out of the downturn running leaner than ever and could see a substantial earnings boost with even a modest economic lift. We will continue to perform our due diligence on these companies in the months ahead and deploy capital where we see opportunities develop.

Random thought: "Leave nothing for tomorrow which can be done today."

- Abraham Lincoln

APPROVED FOR DISTRIBUTION TO CLIENTS. *Dana Investment Advisors welcomes any comments to their newsletter and is more than willing to discuss or explain any aspect of the letter. This newsletter is provided for general information only and is not intended to provide specific advice or recommendations for any individual or entity. This is not an offer, solicitation, or recommendation to purchase any security or the services of any organization. The foregoing reflects the opinions of Dana Investment Advisors.*

If you would prefer to have our newsletter e-mailed, please send your e-mail address to newsletter@danainvestment.com.

20700 SWENSON DRIVE • SUITE 400 • 53186 • P.O. BOX 1067 • BROOKFIELD, WI • 53008-1067 • 262.782.3631 • FAX 262-782-0581
365 ERICKSEN AVENUE.N.E. • SUITE 312 • SEATTLE, WA • 98110-1888 • 206.855.8781 • FAX 800.560.6227

E-Mail: dia@danainvestment.com
Web Site: www.danainvestment.com