



Perspective

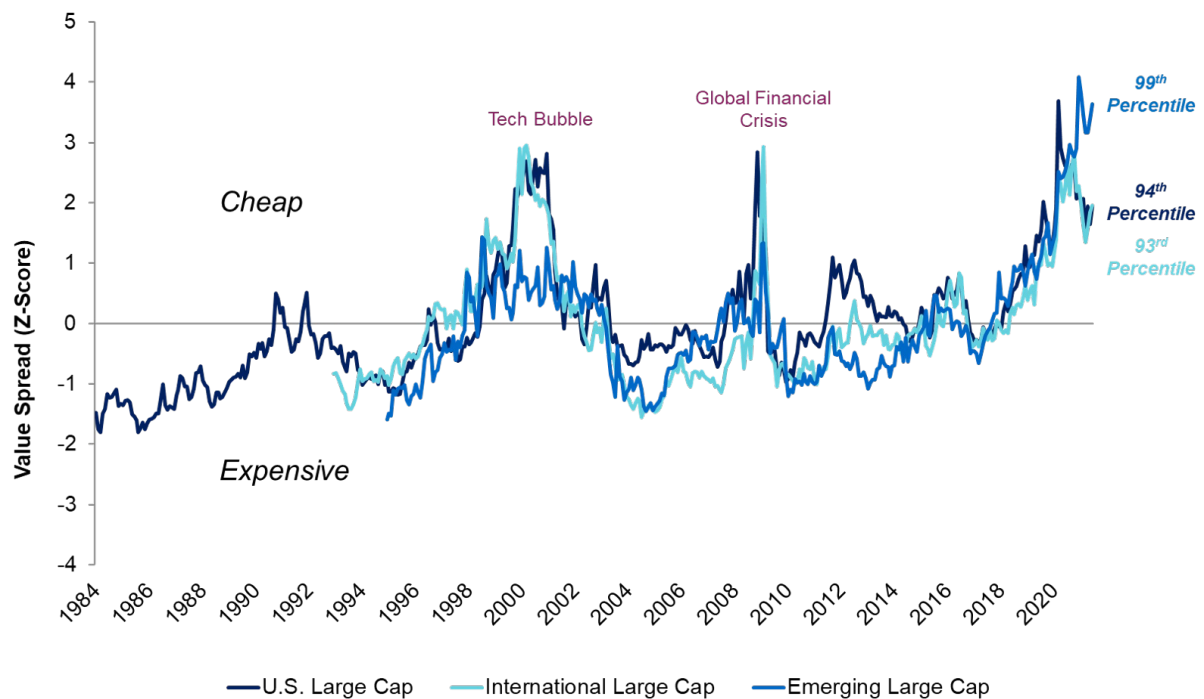
Are Value Stocks Cheap for a Fundamental Reason?

August 30, 2021

We have been discussing the attractiveness of the [value factor](#) for many months based on the unusually high value spread, which compares the valuation multiples of expensive stocks to cheap stocks. This metric is still extremely cheap... 90th + percentile cheap across all regions.

Value Spreads for Hypothetical Industry-and-Dollar-Neutral Value Portfolios*

January 1, 1984 – June 30, 2021



*Spreads are constructed using the Hypothetical Value portfolio as described below, and are adjusted to be dollar-neutral, but not necessarily beta-neutral through time.

Source: AQR. Hypothetical value composite includes four value measures: book-to-price, earnings-to-price, forecast earnings-to-price, and sales-to-enterprise value; spreads are measured based on ratios. To construct industry-neutrality, the value spreads are constructed by comparing the aforementioned value measures within each industry, which are then aggregated up to represent an entire portfolio. Hypothetical data has inherent limitations, some of which are disclosed in the Disclosures. Please see the Hypothetical U.S. Large Cap, International, and Emerging Valuation Theme Model Descriptions in the Disclosures. For illustrative purposes only and not representative of an actual portfolio AQR currently manages. Please read the Disclosures for important disclosures.

We think this signals an unusually attractive forward-looking return for the value factor, but some investors have wondered if value is cheap for a reason. Maybe the fundamental prospects for value stocks are unusually poor today, justifying the high value spread? This is by far the most popular question we get from skeptics. And, yes, we have an answer that doesn't require a four-hour time commitment nor a PhD (though finance PhDs may also be able to follow along). In a recent post, "[Are Value Stocks Cheap for a Fundamental Reason?](#)," we explain why we look at the value spread, and why the current high value spread is forecasting high expected returns, not lower than usual fundamental growth rates for cheap versus expensive stocks. And we cover all of this in five minutes. We encourage all investors, both skeptics and value geeks, to listen to this post, and we welcome any feedback.

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