

2020: A YEAR FOR STORYTELLERS

Matt Wagner — Associate, Research
03/04/2021

The backbone of any investment is a good story.

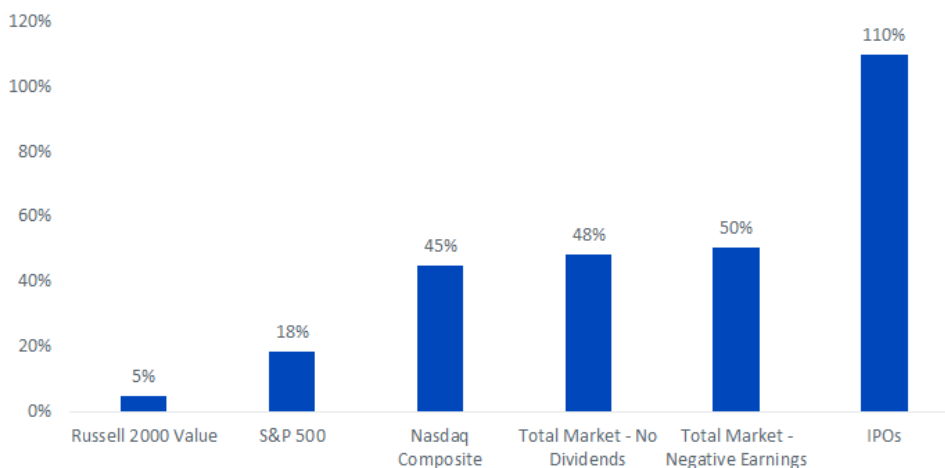
Even quant investors rely on stories—stories of efficient markets where riskier stocks should outperform less risky stocks or where behavioral biases lead investors to systematically undervalue low multiple stocks.

The term “story stock” is commonly attributed to growth stocks—often in technology and biotech—that are on the cutting edge of innovation but have negative earnings today.

2020 was a historic year for the outperformance of story stocks.

The [Russell 2000 Value Index](#) is heavily exposed to regional banks and [small-cap](#) industrial businesses—in many ways, the opposite of story stocks. This Index was up just 5% in 2020, severely lagging stocks with negative earnings (up 50%) and recent [initial public offerings \(IPOs\)](#) (up 110%).

2020 Index Performance

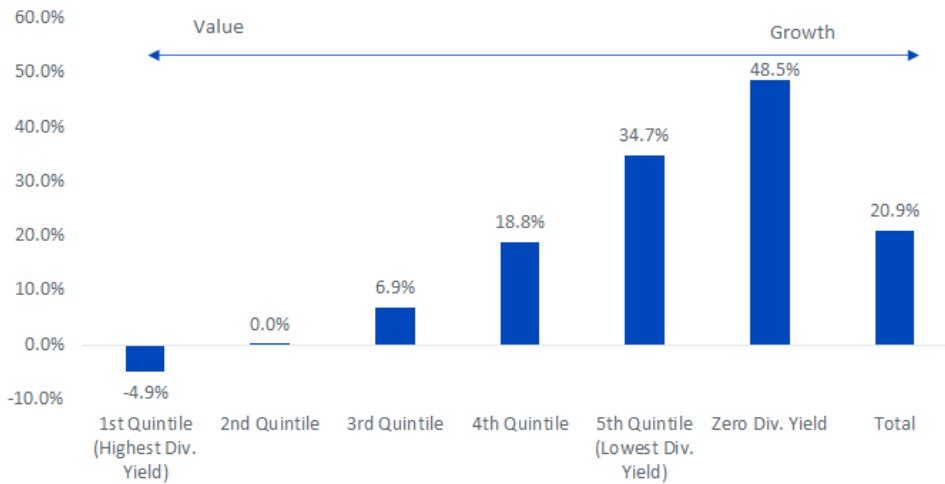


Sources: WisdomTree, Bitwise, Renaissance Capital, Zephyr StyleADVISOR.. IPOs = Renaissance IPO Index. Total Market - Negative Earnings = negative earners in the Russell 3000 Index. Total Market - No Dividends = non-dividend payers in the Russell 3000 Index. You cannot invest directly in an index. Past performance is not indicative of future returns.

Another way of illustrating this trend: The chart below dissects the [Russell 3000 Index](#) constituents into [dividend yield quintiles](#). There was a clear pattern of investors favoring low-yielding or non-dividend-paying companies over the more value-titled high-dividend payers.

Russell 3000 Index Performance

Dividend Yield Quintiles



Sources: WisdomTree, FactSet, 12/31/19–12/31/20. You cannot invest directly in an index. Past performance is not indicative of future returns.

Let’s make two simplifying statements to explain in part why these story stocks took off in 2020:

1. [Risk](#)-free rates plummeted from 1.91% at the start of 2020 to as low as .51%
2. After the initial dramatic dive in risk assets in the spring, investors began to look beyond the COVID-19 pandemic to a faster-than-anticipated return to trend [GDP](#)

These statements tell us that the economy should recover in a relatively short period, and [interest rates](#) appear to be accommodative for the foreseeable future—a combination that should significantly lower the cost of capital for most businesses.

[Growth](#) stocks generally benefit more from this reduced cost of capital compared to value stocks. The reason is that more value from growth stocks comes from cash flows further out in the future, making them more sensitive to fluctuations in discount rates.

Value for Rising Rates

WisdomTree’s [mid](#)- and [small-cap](#) dividend strategies had effectively no exposure to 2020’s skyrocketing story stocks.

Mid- and small-cap Health Care and Information Technology companies were each up more than 35% in the Russell benchmarks. Most of these companies are unprofitable, and even fewer of them pay a dividend.

Sector Weights

Index	Health Care	Information Technology	Combined
WisdomTree U.S. MidCap Dividend	0.94%	6.82%	7.76%
Russell Midcap	10.23%	18.05%	28.28%
WisdomTree U.S. SmallCap Dividend	1.26%	3.14%	4.40%
Russell 2000	18.18%	13.55%	31.73%

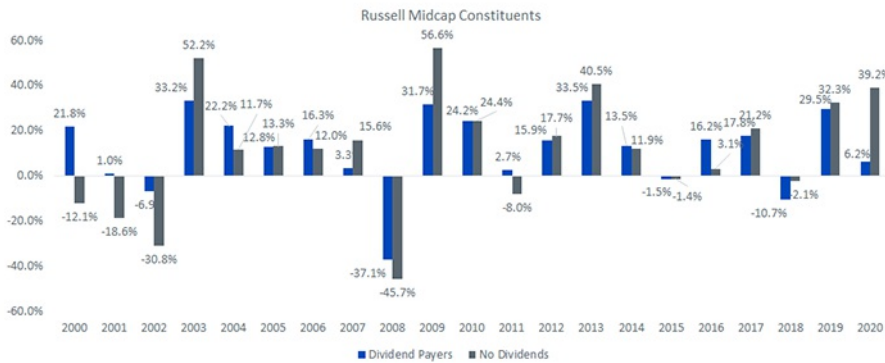
Sources: WisdomTree, FactSet, as of 12/31/19. You cannot invest directly in an index. Weights subject to change.

Over the long run, we have the data to support that mid- and small-cap dividend payers tend to outperform non-dividend payers and tend to do so with significantly less volatility.

Following a year where non-dividend payers outperformed dividend payers by more than 30% in both markets—the widest margin in the past two decades—investors may want to consider that the interest rate environment that was a tailwind to growth stocks in 2020 is unlikely to reoccur in 2021, and it may become a headwind should rates continue to rise.

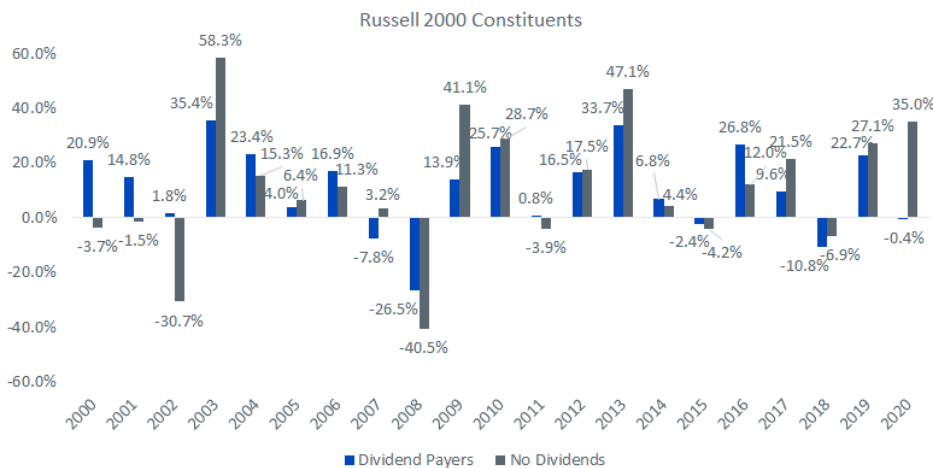
Russell Midcap Index

Annualized	All Constituents	Dividend Payers	No Dividends
Returns	9.11%	10.25%	7.91%
Volatility	19.57%	17.05%	25.86%
Sharpe Ratio	0.47	0.58	0.36



Russell 2000 Index

Annualized	All Constituents	Dividend Payers	No Dividends
Returns	8.65%	9.63%	8.66%
Volatility	19.38%	15.59%	23.90%
Sharpe Ratio	0.45	0.58	0.40



Sources: WisdomTree, FactSet, 12/31/1999–12/31/2020. You cannot invest directly in an index. Past performance is not indicative of future returns.

For definitions of indexes in the charts please visit our [glossary](#).

Important Risks Related to this Article

There are risks associated with investing, including possible loss of principal. Funds focusing their investments on certain sectors and/or smaller companies increase their vulnerability to any single economic or regulatory development. This may result in greater share price volatility. Please read the Fund’s prospectus for specific details regarding the Fund’s risk profile.

For more investing insights, check out our [Economic & Market Outlook](#)

View the online version of this article [here](#).

IMPORTANT INFORMATION

U.S. investors only: Click [here](#) to obtain a WisdomTree ETF prospectus which contains investment objectives, risks, charges, expenses, and other information; read and consider carefully before investing.

There are risks involved with investing, including possible loss of principal. Foreign investing involves currency, political and economic risk. Funds focusing on a single country, sector and/or funds that emphasize investments in smaller companies may experience greater price volatility. Investments in emerging markets, currency, fixed income and alternative investments include additional risks. Please see prospectus for discussion of risks.

Past performance is not indicative of future results. This material contains the opinions of the author, which are subject to change, and should not to be considered or interpreted as a recommendation to participate in any particular trading strategy, or deemed to be an offer or sale of any investment product and it should not be relied on as such. There is no guarantee that any strategies discussed will work under all market conditions. This material represents an assessment of the market environment at a specific time and is not intended to be a forecast of future events or a guarantee of future results. This material should not be relied upon as research or investment advice regarding any security in particular. The user of this information assumes the entire risk of any use made of the information provided herein. Neither WisdomTree nor its affiliates, nor Foreside Fund Services, LLC, or its affiliates provide tax or legal advice. Investors seeking tax or legal advice should consult their tax or legal advisor. Unless expressly stated otherwise the opinions, interpretations or findings expressed herein do not necessarily represent the views of WisdomTree or any of its affiliates.

The MSCI information may only be used for your internal use, may not be reproduced or re-disseminated in any form and may not be used as a basis for or component of any financial instruments or products or indexes. None of the MSCI information is intended to constitute investment advice or a recommendation to make (or refrain from making) any kind of investment decision and may not be relied on as such. Historical data and analysis should not be taken as an indication or guarantee of any future performance analysis, forecast or prediction. The MSCI information is provided on an "as is" basis and the user of this information assumes the entire risk of any use made of this information. MSCI, each of its affiliates and each entity involved in compiling, computing or creating any MSCI information (collectively, the "MSCI Parties") expressly disclaims all warranties. With respect to this information, in no event shall any MSCI Party have any liability for any direct, indirect, special, incidental, punitive, consequential (including loss profits) or any other damages (www.msci.com)

Jonathan Steinberg, Jeremy Schwartz, Rick Harper, Christopher Gannatti, Bradley Krom, Tripp Zimmerman, Michael Barrer, Anita Rausch, Kevin Flanagan, Brendan Loftus, Joseph Tenaglia, Jeff Weniger, Matt Wagner, Alejandro Saltiel, Ryan Krystopowicz, Kara Marciscano, Jianing Wu and Brian Manby are registered representatives of Foreside Fund Services, LLC.

WisdomTree Funds are distributed by Foreside Fund Services, LLC, in the U.S. only.

You cannot invest directly in an index.

DEFINITIONS

Russell 2000 Value Index : measures the performance of small-cap value segment of the U.S. equity universe. It includes those Russell 2000 Index companies with lower price-to-book ratios and lower forecasted growth values.

Small caps : new or relatively young companies that typically have a market capitalization between \$200 million to \$2 billion.

Initial public offering (IPO) : The first sale of stock by a private company to the public.

Russell 3000 Index : Measures the performance of the 3,000 largest U.S. companies based on total market capitalization.

Dividend yield : A financial ratio that shows how much a company pays out in dividends each year relative to its share price.

Quintile : One of the class of values of a variate which divides the members of and batch or sample into equal-sized subgroups of adjacent values or a probability distribution into distributions of equal probability.

Risk : Also standard deviation, which measures the spread of actual returns around an average return during a specific period. Higher risk indicates greater potential for returns to be farther away from this average.

Gross domestic product (GDP) : The sum total of all goods and services produced across an economy.

Interest rates : The rate at which interest is paid by a borrower for the use of money.

Growth : Characterized by higher price levels relative to fundamentals, such as dividends or earnings. Price levels are higher because investors are willing to pay more due to their expectations of future improvements in these fundamentals.

Mid-Cap : Characterized by exposure to the next 20% of market capitalization (after the top 70% have been removed) within the Value, Blend or Growth style zones with the majority of the fund's weight.