BEATING THE S&P 500 IS HARD! HERE IS HOW OUR ETF DID IT.

Pierre Debru — Head of Quantitative Research & Multi Asset Solutions at WisdomTree in Europe,Christopher Gannatti — Global Head of Research

01/27/2023

2022 proved to be a particularly challenging year for investors across the world. The S&P 500 closed 18.51% down despite a relatively good fourth quarter. In that context, many investors could have found solace in the fact that their investment at least outperformed the market. Unfortunately, this would not have been the case for many of them. As highlighted semiannually by the SPIVA scorecard, the majority of active managers underperform their benchmark over the medium to long term, and this is particularly true for U.S. equities. In the U.S., 9.97% of funds outperformed the S&P 500 after fees over the last 10 years, and 15.5% did so over the last five years. So, what could explain such poor results, and how could investors go about finding the diamond in the rough that will deliver this elusive outperformance?

Are Markets Too Efficient?

One often-mentioned explanation for the difficulties of active managers is the increasing efficiency of markets across the world and in the U.S. in particular. However, academics have demonstrated once and again that systematically investing in factor portfolios would have outperformed the market over the long term. Investing in high-dividend stocks, high-quality stocks or cheap stocks in a systematic manner should, we believe, give managers one of the keys to outperforming the market. It is worth noting that academic research has shown that the historical outperformance yielded by such factor investing strategies has not meaningfully decreased since their discoveries, even if markets have become more efficient. Of course, "systematic" is the keyword in this approach, and this is where active fund managers may be struggling.

The WisdomTree U.S. Quality Dividend Growth Fund (DGRW) is a good example of how using this decade-long research can help investors seeking to outperform the S&P 500. Our ETF has outperformed since its inception in May 2013 and in many periods since then, as highlighted in figure 1 (5Y, 3Y, 2022). We believe one of the reasons for this success is that the ETF's investment process is rooted in this academic literature and focuses on a systematic selection of a diversified b asket of highly profitable companies with solid dividend-paying credentials, leaning heavily into the quality and high-dividend factors.

Figure 1: Historical Annualized Outperformance of DGRW vs. the S&P 500

	2022	3Y	5Y	SI
WisdomTree U.S. Quality Dividend Growth Fund	-6.36%	9.87%	10.24%	11.92%
S&P 500 net TR Index	-18.51%	7.14%	8.85%	10.52%
Annualized Outperformance	12.15%	2.73%	1.41%	1.40%

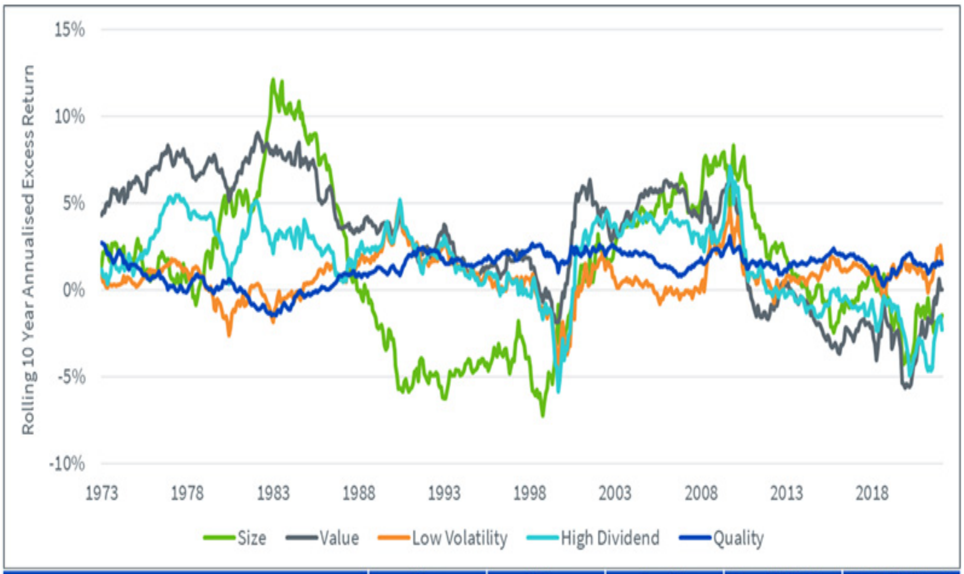
Sources: WisdomTree, Bloomberg. Period from 5/23/13 to 12/31/22. Calculations are based on daily NAV in USD. The inception date for the WisdomTree U.S. Quality Dividend Growth Fund is May 22, 2013. Performances over periods longer than a year are annualized. You cannot invest directly in an index. **WisdomTree shares are bought and sold at market price (not NAV) and are not individually redeemed from the Fund. Total returns are calculated using the daily 4:00 p.m. EST net asset value (NAV). Market price returns reflect the midpoint of the bid/ask spread as of the close of trading on the exchange where Fund shares are listed. Market price returns do not represent the returns you would receive if you traded shares at other times.**

Performance is historical and does not guarantee future results. Current performance may be lower or higher than quoted. Investment returns and the principal value of an investment will fluctuate so that an investor's shares, when redeemed, may be worth more or less than their original cost. Performance data for the most recent month-end is available above.

Click here for the most current month-end and standardized performance.

Of course, factors are not infallible, either. They do not outperform the market every single day or even every single year. While they tend to outperform over the long term, they also tend to ebb and flow between periods of relative underperformance and outperformance, depending on the cycle. But strategically, some factors exhibit higher consistency than others. This is the case for quality, which tends to outperform the most consistently with the lowest volatility, as shown in figure 2.

Figure 2: Historically, Quality Has Delivered the Most Consistent Outperformance over 10-Year Periods



	Size	Value	Quality	Low Volatility	High Dividend
Percentage of Outperforming periods	61%	75%	88%	77%	73%
Best Outperformance	12.1%	9.0%	3.1%	5.0%	7.1%
Worst Underperformance	-7.2%	-5.7%	-1.5%	-4.4%	-5.9%

Sources: WisdomTree, Ken French, data as of 7/31/22 and represents the latest date of available data. Value: High 30% Book-to-Price portfolio. Size: Low 30% portfolio. Quality: High 30% portfolio. Low Vol: Low 20% portfolio. High Div: High 30 portfolio. Market: All CRSP firms incorporated in the U.S. and listed on the NYSE, AMEX or NASDAQ. Past performance is not indicative of future results, and any investments may go down in value. You cannot invest directly in an index.

Over rolling 10-year periods, we can see that the quality factor has exhibited outperformance most often (88% of the time versus the market) and has the smallest "worst underperformance" number of all factors. It suggests that quality is a true "all-weather" factor, and that is the reason why WisdomTree decided to build its "core" equity exposure ETF around that specific factor with the success I just described.

Is There a Tech Curse in the U.S.?

Another often-mentioned explanation is that the U.S. market is increasingly concentrated in large-cap tech stocks and active managers suffer from underinvestment in those stocks. This would imply that it is not possible to outperform the S&P 500 without taking even bigger bets on tech stocks and, in particular, non-dividend-paying tech stocks like Amazon, Tesla, Meta and Alphabet. Extending this premise further, it is possible to wonder if only growth strategies have any chance to outperform in the U.S. Isn't the incredible run of growth versus value over the last 10 years proof of that?

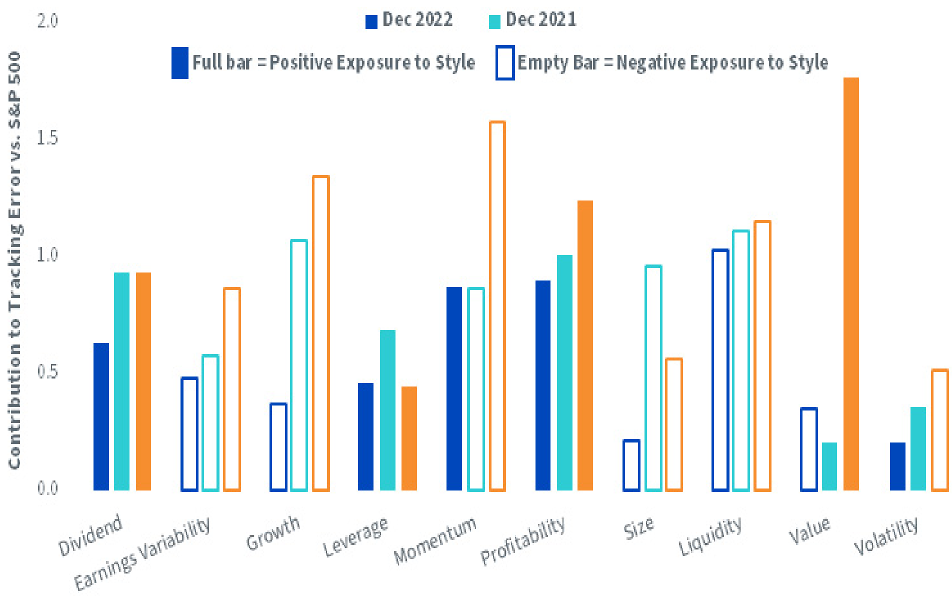
DGRW is a great example to show that neither of those things is, in fact, fundamentally true.

- First of all, the ETF focuses on dividend-paying, dividend-growing stocks, meaning that it does not invest in companies that don't pay a dividend. This means no investment in Amazon or the like. The average weight of Information Technology in the ETF in the last three years was 24.2%: i.e., under-weight to the 27.1% of the S&P 500.

- Furthermore, the ETF has been consistently positively exposed to the high dividend factor and negatively exposed to the growth factor, as illustrated in figure 3.

Both of these facts did not stop the ETF from outperforming its benchmark over the medium to long term, as illustrated in figure 1.

Figure 3: Factor Exposure of Returns in Excess of the S&P 500 over Time



Sources: WisdomTree, Bloomberg. Data as of 12/31/22. Analysis is run on holdings of the ETF using PORT in Bloomberg. Factor definitions and calculations are explained in "US Equity Fundamental Factor Model," which is available in PORT Help in Bloomberg. Past performance is not indicative of future results, and any investments may go down in value. You cannot invest directly in an index.

Do Highly Profitable Companies Rule the Market?

A final, intriguing explanation comes from a paper published in 2018 by Professor Hendrik Bessembinder that shows that only around 4% of stocks explain the totality of the excess wealth created by U.S. equities between 1926 to 2016. In other words, a handful of the most successful companies create most of the outperformance. Looking back at which companies those are, we find Apple, Microsoft, General Electrics, IBM and so on. This, again, would speak to an approach where the focus is on companies that are growing, profitable and high quality, leaning into the main principles that WisdomTree uses with its quality dividend growth strategies.

What Is the Conclusion Then?

Whatever the reason for the failings of active managers when it comes to delivering consistent outperformance, at WisdomTree, we believe a robust, research-driven, systematic investment process focusing on high-quality stocks is the cornerstone of an equity portfolio and the key to building resilient portfolios that can help investors build wealth over the long term and weather the inevitable storms along the way.

The ETF's portfolio is constructed around 300 dividend payers with the best-combined rank of earnings growth, return on equity and return on assets within a universe of companies with sustainable dividend policies. Stocks are also risk-tested using a proprietary risk screen (composite risk score), which uses quality and momentum metrics to rank companies and screen out the riskiest companies and potential value traps. Each company is then weighted based on its cash dividend paid (market capitalization x dividend yield), which introduces valuation discipline into the portfolio. Those steps, in combination, deliver a thoughtfully blended exposure to quality and high dividend. We believe the outperforming track record of the WisdomTree U.S. Quality Dividend Growth Fund over the last nine and a half years is a testament to that.

Looking forward to 2023, recession risk continues to hang over the market like the sword of Damocles. The International Monetary Fund (IMF) is warning of a recession in the U.S., a deep slowdown in Europe and a drawn-out recession in the United Kingdom. While inflation has shown signs of easing, we expect central banks to remain hawkish around the globe as inflation is still very meaningfully above targets. With markets facing many of the same issues in 2023 that they faced in the second half of 2022, it looks like resilient investments that tilt to the quality and high dividend factors that have done particularly well in 2022 could continue to benefit.

[1] Source: S&P, SPIVA Report, as of 6/30/22.

[2] Hendrik (Hank) Bessembinder, "Do Stocks Outperform Treasury Bills?" Journal of Financial Economics (JFE), Forthcoming, 5/28/18. Available at SSRN: https://ssrn.com/abstract=2900447 or http://dx.doi.org/10.2139/ssrn.2900447

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Click here for a full list of DGRW's Fund holdings. Holdings are subject to change and risk.

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Pierre Debru is an employee of WisdomTree UK Limited, a European subsidiary of WisdomTree Asset Management Inc.'s parent company, WisdomTree Investments, Inc.

For definitions of terms in the charts above, please visit the glossary.

For the top 10 holdings of DGRW please visit the Fund's fund detail page at https://www.wisdomtree.com/investments/etfs/equity/dgrw

For standardized performance and the most recent month-end performance click here NOTE, this material is intended for electronic use only. Individuals who intend to print and physically deliver to an investor must print the monthly performance report to accompany this blog.

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DEFINITIONS

S&P 500 Index : Market capitalization-weighted benchmark of 500 stocks selected by the Standard and Poor's Index Committee designed to represent the performance of the leading industries in the United States economy.

SPIVA Scorecard : S&P Indices versus Active (SPIVA) scorecards are semiannual reports published by S&P Dow Jones Indices that compare the performance of active equity and fixed income mutual funds against their benchmarks over different time horizons.

Dividend : A portion of corporate profits paid out to shareholders.

Baskets : The composition of an ETF in terms one creation/redemption unit.

Quality : Characterized by higher efficiency and profitability. Typical measures include earnings, return on equity, return on assets, operating profitability as well as others. This term is also related to the Quality Factor, which associates these stock characteristics with excess returns vs the market over tim.

Large-Capitalization (Large-Cap) : A term used by the investment community to refer to companies with a market capitalization value of more than $10 billion. Large cap is an abbreviation of the term "large market capitalization". Market capitalization is calculated by multiplying the number of a company's shares outstanding by its stock price per share.

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.

Value : Characterized by lower price levels relative to fundamentals, such as earnings or dividends. Prices are lower because investors are less certain of the performance of these fundamentals in the future. This term is also related to the Value Factor, which associates these stock characteristics with excess returns vs the market over tim.

Return on Equity (ROE) : Measures a corporation's profitability by revealing how much profit a company generates with the money shareholders have invested.

Return on assets (ROA) : Firm profits (after accounting for all expenses) divided by the firm's total assets. Higher numbers indicate greater profits relative to the level of assets utilized to generate them.

Momentum : Characterized by assets with recent price increase trends over time. This term is also associated with the Momentum Factor which associates these stock characteristics with excess return vs the market over time.

Market Capitalization : Market cap = share prices x number of shares outstanding. Firms with the highest values receive the highest weights in approaches designed to weight firms by market cap.

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

Recession : two consecutive quarters of negative GDP growth, characterized generally by a slowing economy and higher unemploymen.

International Monetary Fund : international organization for global monetary cooperation, secure financial stability, facilitate international trade, promote high employment and sustainable economic growth around the world.

Inflation : Characterized by rising price levels.

Central bank : Refers to the the monetary authority of any country.

Hawkish : Description used when worries about inflation are the primary concerns in setting monetary policy decisions.