

# RECENT U.S. EQUITY OUTPERFORMANCE VS. REST OF WORLD: NOT JUST LARGE-CAP TECH

Andrew Okrongly — Director, Model Portfolios  
11/21/2022

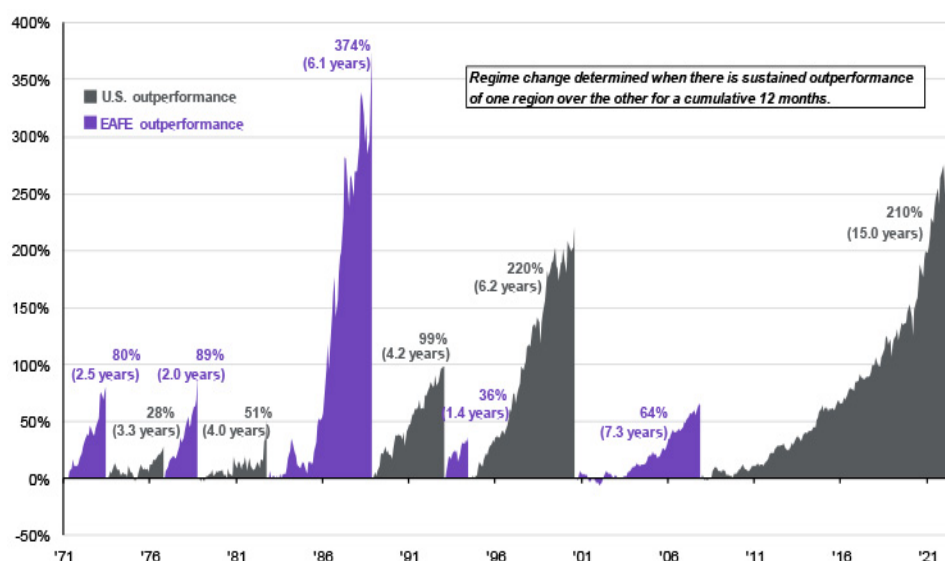
*This article is relevant to financial professionals who are considering offering model portfolios to their clients. If you are an individual investor interested in WisdomTree ETF Model Portfolios, please inquire with your financial professional. Not all financial professionals have access to these Model Portfolios.*

## A Decade-Plus-Long Run for U.S. Equity Markets

By some measurements, we are now more than 15 years into one of the most pronounced, long-lasting periods of U.S. equity outperforming international stocks in recent history.

Since the 1970s, the relative performance of U.S. versus international equities has been cyclical, and these cycles have lasted, on average, around five years. While it is impossible to predict the exact timing for when the current trend will reverse, one could certainly make the argument that international stocks may soon have their moment in the sun.

## U.S. Equity vs. International Equity Cumulative Outperformance Cycles



Sources: FactSet, MSCI, J.P. Morgan Asset Management, as of 9/30/22. U.S. Equity represented by the MSCI USA Net Total Return Index. International Equity represented by the MSCI EAFE Net Total Return Index (USD). A regime change is called when there is sustained outperformance of one region over the other for a cumulative 12 months. Past performance is not indicative of future returns. You cannot invest directly in an index.

Regardless of the market cycle, investors, in aggregate, tend to have a “home country bias.” Following this decade-plus-long run for domestic stocks, many U.S. investors are now questioning the need for international [diversification](#) altogether.

Despite the prevalence of home country and recency biases, our [Model Portfolios](#) reflect WisdomTree’s conviction in the long-term risk and return advantages of global diversification. Accordingly, we tend to utilize the [MSCI All Country World Index \(ACWI\)](#) as our reference benchmark from a regional exposure standpoint.

However, a notable caveat to the above is that our preference for [dividend-paying](#), [small-cap](#) equities extends to both [developed](#) and [emerging markets](#) outside the United States.

Contrary to popular belief, these smaller, [value-oriented](#) companies have lagged their U.S. equivalents to nearly the same extent as the larger, [market cap-weighted](#) benchmarks.

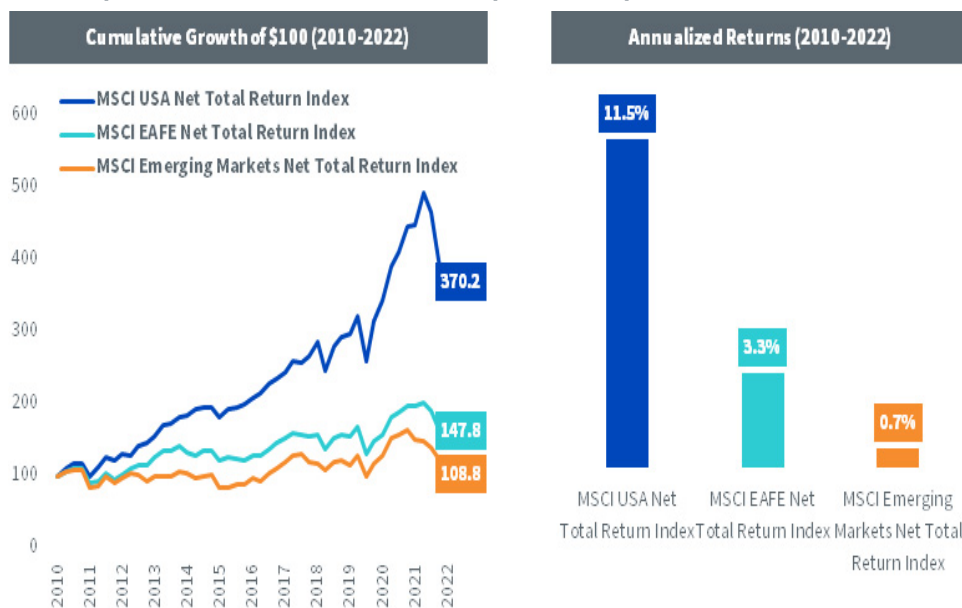
For those investors who may now be contemplating a move into international equities and are focused on [valuations](#), we believe small-cap dividend payers are an interesting area to consider.

### U.S. Outperformance: Not Just Large-Cap Tech

U.S. equities delivered an 11.5% annualized return during the 12-year period ended September 30, 2022, as measured by the [MSCI USA Index](#).

This compares to returns on international developed equities ([MSCI EAFE Index](#)) of 3.3% and only 0.7% for emerging markets ([MSCI Emerging Markets Index](#)).

### U.S. Outperformance vs. Rest of World (Sep 2010–?Sep 2022)

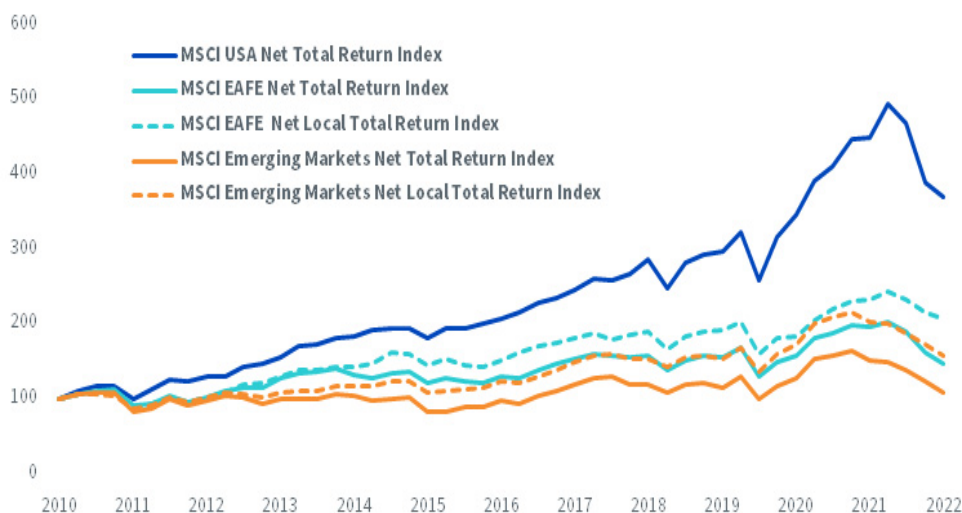


Sources: WisdomTree, FactSet, 9/30/10–9/30/22. Past performance is not indicative of future returns. You cannot invest directly in an index.

This period of U.S. dominance is often explained by a strengthening dollar or the significant appreciation of U.S. [large-cap](#) tech stocks. But these factors do not tell the entire story.

Below we show that U.S. equities have dramatically outperformed even the local market returns of international stocks.

### U.S. Outperformance vs. Rest of World USD and Local Indexes (Sep 2010–?Sep 2022)



Sources: WisdomTree, FactSet, 9/30/10–9/30/22. Past performance is not indicative of future returns. You cannot invest directly in an index. US equity is represented by the MSCI USA Net Total Return Index. EAFE represented by MSCI EAFE Net Total Return Index. EM represented by MSCI Emerging Markets Net Total Return Index. Past performance is not indicative of future returns. You cannot invest directly in an index.

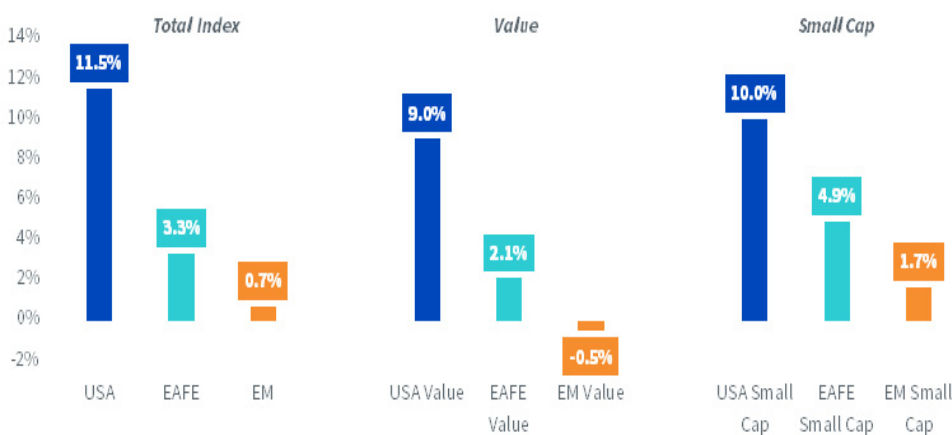
Based on the performance of local equity markets over this same period, [foreign exchange](#) moves explain approximately 30%–40% of international developed and emerging equity underperformance. Clearly, a majority of the relative outperformance of U.S. equities was not solely currency related.

Many market commentators have also pointed to the [FAANG](#) stocks (Facebook/Meta, Amazon, Apple, Netflix and Google) to explain this recent relative performance cycle.

While the weight of these companies within traditional market cap-weighted indexes is significant, the U.S. outperformance story extends well beyond large-cap tech.

In fact, there has been a similar degree of relative outperformance over the past 12 years in U.S. value and small-cap stocks.

#### U.S. vs. Rest of World Annualized Returns (2010–2022)



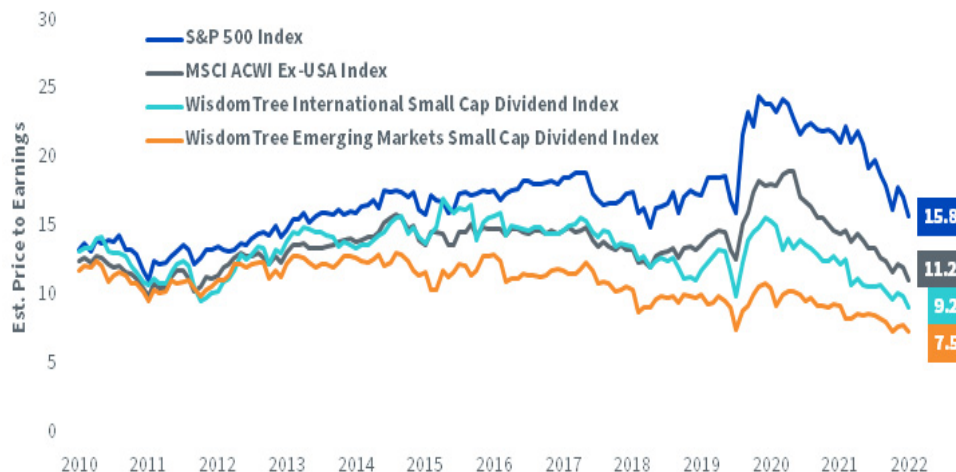
Sources: WisdomTree, FactSet, 9/30/10–9/30/22. Past performance is not indicative of future returns. You cannot invest directly in an index. U.S. Equity is represented by the MSCI USA Net Total Return Index, MSCI USA Value Net Total Return Index, and MSCI USA Small Cap Net Total Return Index. EAFE represented by MSCI EAFE Net Total Return Index, MSCI EAFE Value Net Total Return Index, and MSCI EAFE Small Cap Net Total Return Index. EM represented by MSCI Emerging Markets Net Total Return Index, MSCI Emerging Markets Value Net Total Return Index, and MSCI Emerging Markets Small Cap Net Total Return Index. Past performance is not indicative of future returns. You cannot invest directly in an index.

#### A Potential Opportunity in Small-Cap Value outside the U.S.

These international small-cap value stocks, battered in recent years compared to their U.S. counterparts, now offer a compelling value and income opportunity.

Over the same 12-year period of U.S. outperformance ended September 30, 2022, the gap between the estimated [Price/Earnings \(P/E\) ratio](#) of the [S&P 500 Index](#) and [MSCI ACWI Ex-USA](#) Index has widened by more than 400%.

## Estimated Price to Earnings (Sep 2010–?Sep 2022)

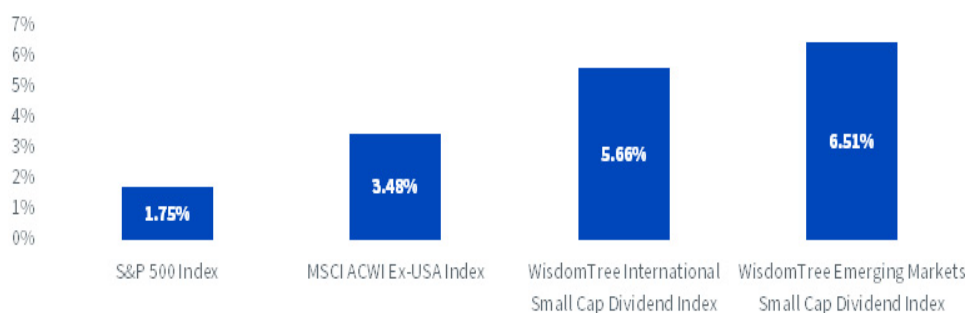


Sources: WisdomTree, FactSet, 9/30/10–9/30/22. Past performance is not indicative of future returns. You cannot invest directly in an index.

What's even more striking is how inexpensive value-oriented small caps outside the U.S. have become relative to the S&P 500 Index. The WisdomTree International and Emerging Markets SmallCap Dividend Indexes now offer P/E multiples in the single digits!

In addition to attractive valuations, the income offered by small-cap dividend payers outside of the U.S. is considerably higher than core U.S. equities.

### Dividend Yield as of 9/30/22



Sources: WisdomTree, FactSet, 9/30/10–9/30/22. Past performance is not indicative of future returns. You cannot invest directly in an index.

### Investing in Small-Cap Dividend Payers Abroad

The [WisdomTree International SmallCap Dividend Fund \(DLS\)](#), one of WisdomTree's initial ETFs launched in 2006, tracks the [WisdomTree International SmallCap Dividend Index](#), providing exposure to small-cap dividend-paying companies in the developed international world, ex-U.S. and Canada.

The [WisdomTree Emerging Markets SmallCap Dividend Fund \(DGS\)](#), launched in 2007, tracks the [WisdomTree Emerging Markets SmallCap Dividend Index](#) and provides exposure to small-cap dividend-paying companies in emerging markets.

Both Funds are value-oriented and provide the following enhancements to traditional market cap-weighted indexes:

- Screen the eligible universe of stocks to only include dividend-paying companies
- Remove those companies most at risk of cutting their dividend based on quantitative risk screens
- Take a [dividend-weighted](#)-to-index construction based on each underlying company's [Dividend Stream®](#)

### Conclusion

Perfectly timing the start of a new outperformance cycle for international stocks may be a fool's errand. But we are now 15+ years into a prolonged period of U.S. leadership that has historically been quite cyclical.

While the strength of the dollar and the performance of large-cap tech companies have often been cited as drivers of recent U.S. outperformance, international small-cap and value stocks are now equally inexpensive relative to their U.S. counterparts.

For investors interested in diversifying outside the U.S. but focused on risk mitigation in the form of valuations and income, small-cap dividend payers in developed and emerging international markets offer a compelling investment case.

#### Important Risks Related to this Article

**DLS:** There are risks associated with investing, including the possible loss of principal. Foreign investing involves special risks, such as risk of loss from currency fluctuation or political or economic uncertainty. The Fund invests in derivatives in seeking to obtain a dynamic currency hedge exposure. Derivative investments can be volatile, and these investments may be less liquid than other securities, and more sensitive to the effects of varied economic conditions. Derivatives used by the Fund may not perform as intended. A Fund that has exposure to one or more sectors may be more vulnerable to any single economic or regulatory development. This may result in greater share price volatility. The composition of the Index underlying the Fund is heavily dependent on quantitative models and data from one or more third parties, and the Index may not perform as intended. The Fund invests in the securities included in, or representative of, its Index regardless of their investment merit, and the Fund does not attempt to outperform its Index or take defensive positions in declining markets. Please read the Fund's prospectus for specific details regarding the Fund's risk profile.

**DGS:** There are risks associated with investing, including the possible loss of principal. Foreign investing involves special risks, such as risk of loss from currency fluctuation or political or economic uncertainty. Funds focusing on a single sector and/or smaller companies generally experience greater price volatility. Investments in emerging, offshore or frontier markets are generally less liquid and less efficient than investments in developed markets and are subject to additional risks, such as risks of adverse governmental regulation, intervention and political developments. Due to the investment strategy of this Fund, it may make higher capital gain distributions than other ETFs. Dividends are not guaranteed, and a company currently paying dividends may cease paying dividends at any time. Please read the Fund's prospectus for specific details regarding the Fund's risk profile.

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

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

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.

#### Related Funds

+ [WisdomTree Emerging Markets SmallCap Dividend Fund](#)

+ [WisdomTree International SmallCap Dividend Fund](#)

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](http://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, 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

**Diversification** : A risk management strategy that mixes a wide variety of investments within a portfolio.

**MSCI ACWI Index** : A free-float adjusted market capitalization-weighted index that is designed to measure the equity market performance of developed and emerging markets.

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

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

**Developed market** : A country that is most developed in terms of its economy and capital markets.

**Emerging market** : Characterized by greater market access and less potential for operational risks when compared to frontier markets, which leads to a larger base of potentially eligible investors.

**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 time.

**Market capitalization-weighting** : 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.

**Valuation** : Refers to metrics that relate financial statistics for equities to their price levels to determine if certain attributes, such as earnings or dividends, are cheap or expensive.

**MSCI USA Index** : is designed to measure the performance of large and mid cap segments of the US market.

**MSCI EAFE Index** : is a market cap-weighted index composed of companies representative of the developed market structure of developed countries in Europe, Australasia and Japan.

**MSCI Emerging Market Index** : The MSCI Em (Emerging Markets) Index is a free-float weighted equity index that captures large and mid cap representation across Emerging Markets (EM) countries.

**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.

**Foreign Exchange (FOREX, FX)** : The exchange of one currency for another, or the conversion of one currency into another currency.

**FAANG** : An acronym referring to the stocks of the five most popular and best-performing American technology companies: Facebook, Amazon, Apple, Netflix and Alphabet (formerly known as Google).

**Price-to-earnings (P/E) ratio** : Share price divided by earnings per share. Lower numbers indicate an ability to access greater amounts of earnings per dollar invested.

**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.

**MSCI ACWI ex-U.S. Index** : A free-float adjusted market capitalization-weighted index that is designed to measure the equity market performance of developed and emerging markets excluding companies based in the United States.

**Dividend weighted** : Constituent securities represented within the Index in proportion to their contribution to the



dividend stream of the Index.

**Dividend Stream** : Refers to the regular dividends per share multiplied by the number of shares outstanding.