
"WORD MAN, WE NEED EACH OTHER – WORDS AND MUSIC"

Scott Welch — Chief Investment Officer, Model Portfolios

01/22/2021

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.

"Word man, we need each other. Words and music."

(From the movie Eddie and the Cruisers, 1983)

If you don't know the movie Eddie and the Cruisers (and it's likely that you don't, though I recommend it), the actor Michael Paré plays Eddie Wilson, a talented but troubled musician in the early 1960s—the birth days of rock 'n' roll. Tom Berenger plays Frank Ridgeway, a shy poet, whom Eddie calls "Word Man." Eddie was expressing his belief that you need both words and music to succeed—which was why the two of them got along despite being completely different people.

In late 2020, the WisdomTree Research team built a list of five distinctive investment themes that we believe have a high likelihood of playing out over the course of 2021. That's the "music." The "words" are the WisdomTree Model Portfolios that fit each investment theme.

Here is a summary of those themes (presented alphabetically), why we believe in them and the corresponding WisdomTree Model Portfolio that aligns with that theme.

1. **Cyclical Rotation**

COVID-19 cases are spiking, which may put a damper on economic growth in Q1. At the same time, we believe we are making progress on the vaccination front, and the worst may soon (hopefully) be behind us. Additionally, Congress just passed a substantial [fiscal stimulus](#) package, and with the Biden Administration stepping in and the Democrats in control of both houses of Congress, we believe yet another (perhaps even larger) fiscal stimulus package will be approved before the end of Q1.

This translates into a potentially substantial catalyst to the economy. As we've noted in other blog posts, [small cap](#), [value](#) and [emerging market](#) stocks tend to perform very well as [economic growth recovers](#):

Typical behavior of global business cycle



Value Value stocks are pro-cyclical and have historically performed more strongly coming off the bottom of an economic cycle

Quality Quality stocks are more defensive in nature and have tended to perform best at the peak of an economic cycle or at the beginning of an economic slowdown

Source: NASDAQ, November 2018. This chart is for illustration purposes only and may not reflect actual market behavior. Past performance does not guarantee future results.

We can also see this in “real time” by comparing the recent performance of these three asset classes versus the broader [S&P 500 Index](#):



Source: YCharts, data as of 1/12/21. You cannot invest in an index, and past performance is no guarantee of future results.

Model Portfolio Implications: The WisdomTree [Strategic Core Equity](#), [Siegel-WisdomTree Longevity and Global Equity models](#) all have strategic “tilts” toward small cap and value stocks and are over-weight in emerging markets (EM) compared to the [MSCI ACWI Index](#). They are well positioned to benefit from what we believe will be a continuance of the current cyclical rotation as the economy recovers.

2. Disruptive Growth

While we believe in the current cyclical rotation back toward size, value and EM, we also believe that the COVID-19 pandemic fundamentally and perhaps permanently altered the way we work, socialize and entertain ourselves. We believe this has led to certain “thematic” sectors and industries that are showing huge growth trends. We refer to this as “disruptive growth,” and we think it will be with us for years to come. These industries include (but are not limited to)

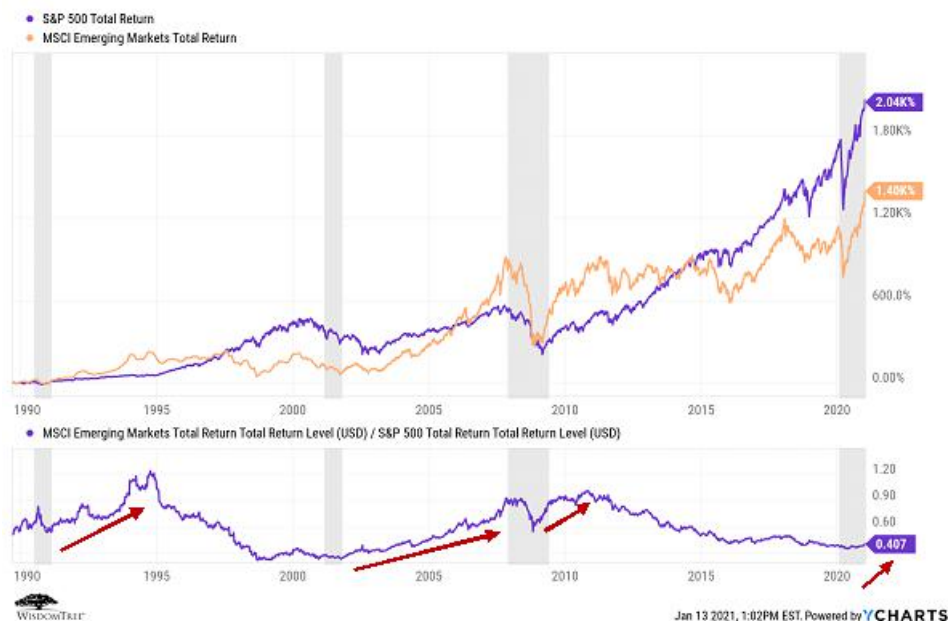
financial technology, cloud-based computing, platform-oriented businesses, human genomics, cybersecurity and online gaming and e-sports.

Model Portfolio Implications: With this growth theme in mind, in mid-2020 we launched the WisdomTree [Disruptive Growth model](#). We identified six specific industry sectors and ETFs that focused on those sectors, and the performance of this model since inception has been exactly what we hoped for, outperforming both broad market indexes (e.g., the S&P 500) and even tech-oriented indexes (e.g., the [NASDAQ](#)). This portfolio carries high valuations corresponding to its high growth rates, and it will be [volatile](#), but for advisors looking to capitalize on a thematic growth trend, we think it may be very interesting.

3. Emerging Markets

Based on our evaluation of fundamentals, economic and earnings growth prospects and our view on the dollar, we made the strategic decision back in late 2018 to go over-weight in emerging markets compared to the MSCI ACWI Index. (We are also over-weight in the U.S. and correspondingly under-weight in developed international, or [EAFE](#) stocks.)

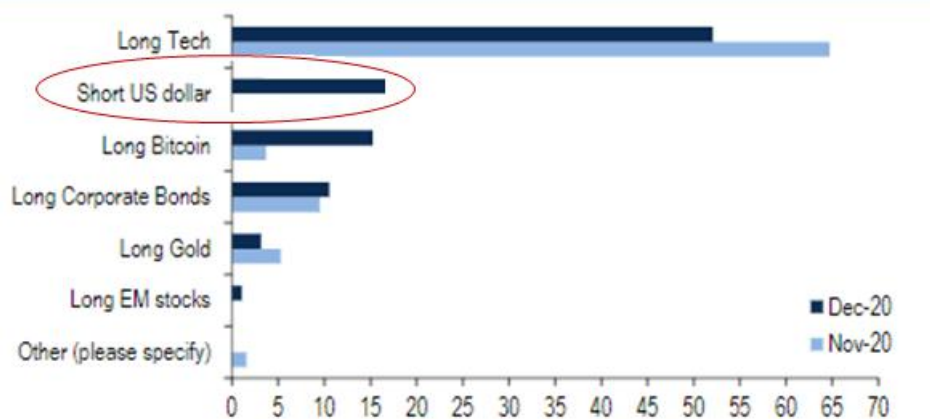
Our conviction to EM remains in place and is perhaps stronger than ever. As we mentioned above, EM historically has outperformed during periods of economic recovery. (The shaded gray areas below show periods of U.S. recession.)



Model Portfolio Implications: All of our [Strategic Core Equity](#) models are strategically over-weight in EM, and we believe they are well positioned to capitalize on the resurgence in EM performance.

While our general market outlook is for a continuation of a weaker dollar, we do recognize that this has become a very “crowded” trade and is perhaps due for somewhat of a reversal:

Exhibit 11: What do you think is currently the most crowded trade?

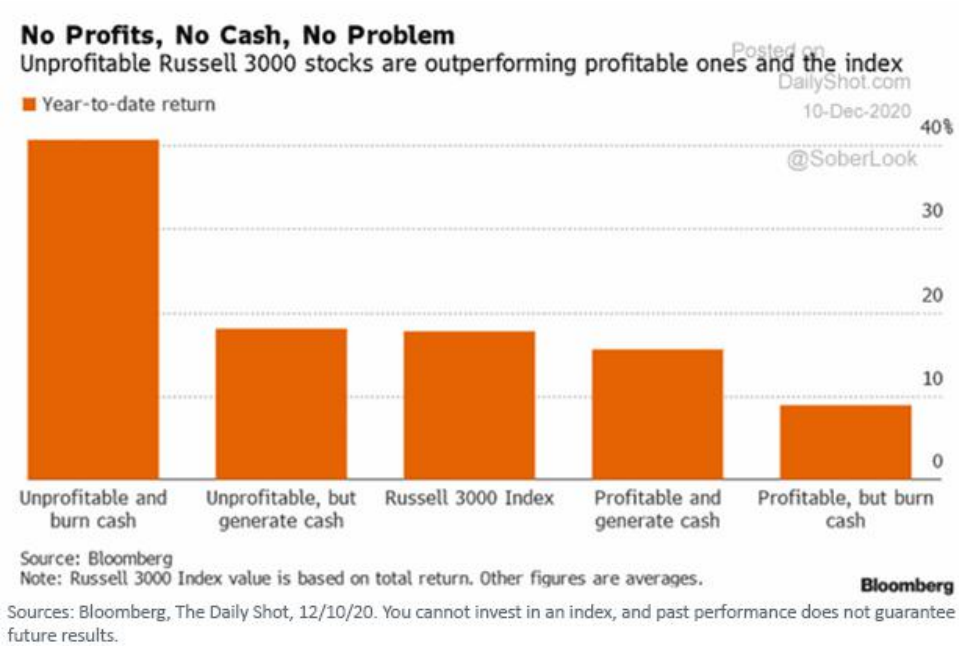


Source: Bank of America Global Fund Manager Survey, December 2020.

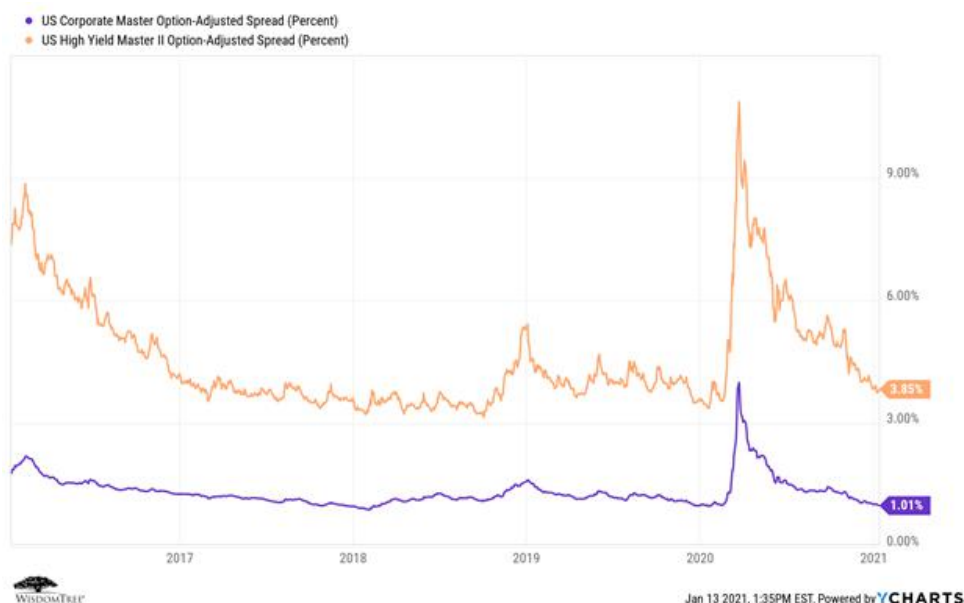
Despite this, we continue to like the fundamental story of emerging markets and remain very comfortable with our current over-weight positioning.

4. Quality and Income

“Quality” companies refer to those with strong [balance sheets](#), [earnings](#) and [cash flows](#). This was a particularly “out of favor” factor throughout most of 2020, as “[junk](#)” companies dominated:



On the income front, we maintain our belief that interest rates will remain lower for longer. We have seen an increase in rates over the past several weeks as economic and COVID-19 vaccine news have hit the headlines, but that is relative—they are still very low, and credit spreads are back to historical averages:



Source: YCharts, data as of 1/12/21. You cannot invest in an index, and past performance does not guarantee future results.

Model Portfolio Implications: We continue to believe that advisors and end clients looking to generate current income out of their portfolios are better served by focusing on high-quality, yield-focused equities versus taking excessive risk in their bond portfolios.

Our [Global Dividend](#), [Global Multi-Asset Income](#) and [Siegel-WisdomTree Longevity](#) models are built explicitly with these themes in mind. They all “tilt” toward higher-quality companies and are currently income-focused but allocate to [yield](#)-oriented equities instead of potentially riskier bond strategies. In a marketplace generally “starved for yield,” we have seen a great deal of advisor interest in these models, and we like how they are positioned in the current environment.

5. Reflation

The last, but not the least, of our investment themes for 2021 is “reflation”—the reappearance of inflationary pressures as the global economy recovers. It is true that, to date, these inflationary pressures have not really materialized, at least in the “headline” indicators:

That said, the recovering global economy, combined with a weak dollar, has put upward pressure on the global commodity complex (i.e., “input prices”)—a trend we expect to continue:

We also believe there is a tremendous level of “pent-up demand” because of the COVID-19 lockdowns. As the vaccinations roll out and additional fiscal stimulus is implemented, we believe we may see a surge in consumption in the second half of 2021.

Model Portfolio Implications: We believe our **Strategic Core Equity** and **Endowment** models are well positioned in the event that we do see “reflation” enter the markets over the course of 2021. Both portfolios have allocations to inflation-sensitive equities, and the Endowment model has an explicit allocation to commodities and other real assets.

Conclusion

All WisdomTree models are built with specific investment objectives in mind and are designed to be “all-weather” portfolios—performing consistently regardless of market conditions.

That said, many of our models do have either strategic or tactical tilts embedded into them. Based on what we believe will be the five primary “investment themes” of 2021—cyclical rotation, disruptive growth, emerging markets, quality and income, and reflation—we are very comfortable with our current positioning and believe our models have the opportunity to perform very well as we move through the year.

For definitions of terms in the blog, please visit our [glossary](#).

Important Risks Related to this Article

WisdomTree Model Portfolio information is designed to be used by financial advisors solely as an educational resource, along with other potential resources advisors may consider, in providing services to their end clients. WisdomTree's Model Portfolios and related content are for information only and are not intended to provide, and should not be relied on for, tax, legal, accounting, investment or financial planning advice by WisdomTree, nor should any WisdomTree Model Portfolio information be considered or relied upon as investment advice or as a recommendation from WisdomTree, including regarding the use or suitability of any WisdomTree Model Portfolio, any particular security or any particular strategy. In providing WisdomTree Model Portfolio information, WisdomTree is not acting and has not agreed to act in an investment advisory, fiduciary or quasi-fiduciary capacity to any advisor or end client, and has no responsibility in connection therewith, and is not providing individualized investment advice to any advisor or end client, including based on or tailored to the circumstance of any advisor or end client. The Model Portfolio information is provided "as is," without warranty of any kind, express or implied. WisdomTree is not responsible for determining the securities to be purchased, held and/or sold for any advisor or end client accounts, nor is WisdomTree responsible for determining the suitability or appropriateness of a Model Portfolio or any securities included therein for any third party, including end clients. Advisors are solely responsible for making investment recommendations and/or decisions with respect to an end client and should consider the end client's individual financial circumstances, investment time frame, risk tolerance level and investment goals in determining the appropriateness of a particular investment or strategy, without input from WisdomTree. WisdomTree does not have investment discretion and does not place trade orders for any end client accounts. Information and other marketing materials provided to you by WisdomTree concerning a Model Portfolio—including allocations, performance and other characteristics—may not be indicative of an end client's actual experience from investing in one or more of the funds included in a Model Portfolio. Using an asset allocation strategy does not ensure a profit or protect against loss, and diversification does not eliminate the risk of experiencing investment losses. There is no assurance that investing in accordance with a Model Portfolio's allocations will provide positive performance over any period. Any content or information included in or related to a WisdomTree Model Portfolio, including descriptions, allocations, data, fund details and disclosures, are subject to change and may not be altered by an advisor or other third party in any way.

WisdomTree primarily uses WisdomTree Funds in the Model Portfolios unless there is no WisdomTree Fund that is consistent with the desired asset allocation or Model Portfolio strategy. As a result, WisdomTree Model Portfolios are expected to include a substantial portion of WisdomTree Funds notwithstanding that there may be a similar fund with a higher rating, lower fees and expenses or substantially better performance. Additionally, WisdomTree and its affiliates will indirectly benefit from investments made based on the Model Portfolios through fees paid by the WisdomTree Funds to WisdomTree and its affiliates for advisory, administrative and other services.

The Siegel-WisdomTree Longevity Model Portfolio seeks to address increasing longevity by shifting the focus to potential long-term growth through a higher stock allocation versus more traditional "60/40" portfolios.

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.

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, 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

Cyclical sectors : Consumer Discretionary, Energy, Industrials, Materials, Financials and Information Technology sectors.

Fiscal Stimulus : Using fiscal policy as a tool to provide economic growth.

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

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.

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.

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

Nasdaq 100 Index : Includes 100 of the largest domestic and international non-financial companies listed on The Nasdaq Stock Market based on market capitalization. The Index reflects companies across major industry groups including computer hardware and software, telecommunications, retail/wholesale trade and biotechnology. It does not contain securities of financial companies, including investment companies.

Volatility : A measure of the dispersion of actual returns around a particular average level.

EAFE : Refers to the geographical area that is made up of Europe, Australasia and the Far East.

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 time.

Balance sheet : refers to the cash and cash equivalents part of the Current Assets on a firm's balance sheet and cash available for purchasing new position.

Core Earnings : Income generated by the company's daily operations rather than one-time events or market fluctuations.

Cash flows : a measure of how much cash a business generates after taking into account all the necessary expenses, including net capital expenditures.

Junk Bond : A high-yield or non-investment grade bond. Junk bonds are fixed-income instruments that carry a rating of 'BB' or lower by Standard & Poor's, or 'Ba' or below by Moody's. Junk bonds are so called because of their higher default risk in relation to investment-grade bonds.

Yield : The income return on an investment. Refers to the interest or dividends received from a security that is typically expressed annually as a percentage of the market or face value.

Reflation : The term is used to describe the first phase of economic recovery after a period of contraction. This period is typically characterized by the act of stimulating the economy through accommodative central bank policies and reducing taxes, to bring growth and inflation back up to the long-term trend.