

# TIME TO DIVE DEEP INTO VALUE

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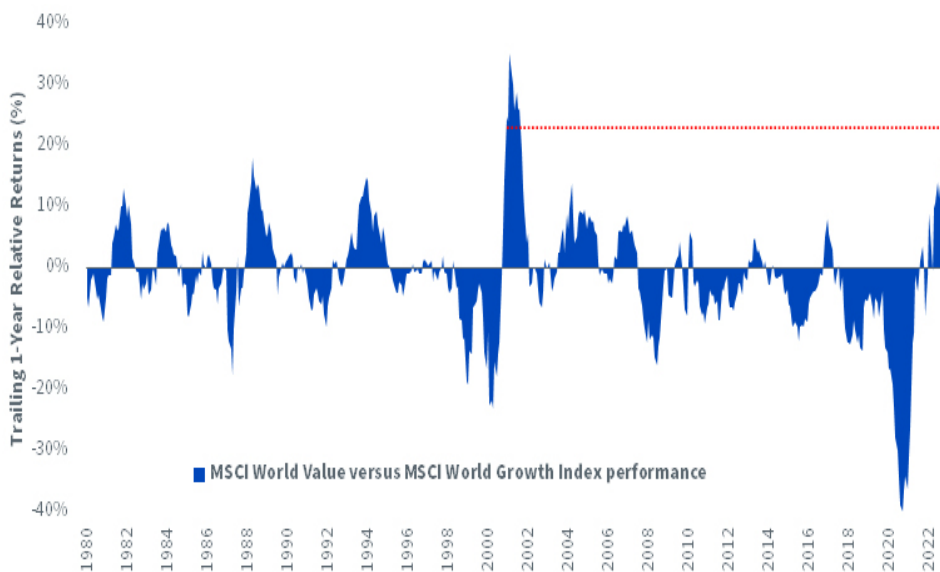
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2023 is off to a cautious start, heralded by the [International Monetary Fund \(IMF\)](#). It has warned that the upcoming recession will likely leave the global economy fundamentally damaged—with a [recession](#) in the U.S., a deeper slowdown in Europe and a drawn-out recession in the United Kingdom. This is quite possible; however, the current downturn may not look like downturns of the past as it's supported by a more resilient labor market. As we transition to 2023, three questions from 2022 remain unanswered:

1. How sticky will the underlying [inflation](#) be?
2. How intense will the recession be?
3. Will we find a solution to Europe's energy crisis?

2022 was a tough year for equities, as evident by the 20% decline in the global stock market capitalization to \$96.6 trillion<sup>1</sup>. Expensive growth stocks that had driven markets higher over the past decade began to correct sharply as the interest rate regime changed. In contrast, [value](#) stocks, while down for the year, were relative outperformers. The [MSCI World Value Index](#) outperformed its growth counterpart by 21% this year.<sup>1</sup> The rising rate environment had a strong role to play in the higher [relative performance](#).

## Rotation from Growth into Value Stocks



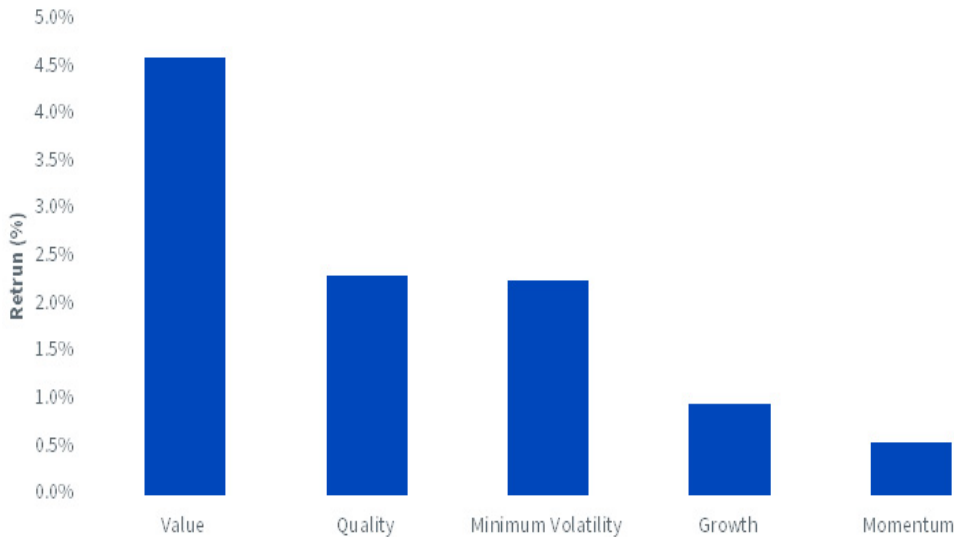
Sources: WisdomTree, Bloomberg, as of 12/30/22. You cannot invest directly in an index. Past performance is not indicative of future results. The red line indicates the last time the Trailing 1-year relative returns were at this level.

## Central Banks Turn up the Hawkish Rhetoric

While inflation has begun showing signs of easing globally, [central banks](#) in the U.S., Europe and the UK continue to remain [hawkish](#). The [Federal Open Market Committee's \(FOMC\)](#) new forecasts for the economy and policy showed few signs that the inflation picture is improving meaningfully. [Federal Reserve \(Fed\)](#) Chair Powell made clear in the December meeting that he wanted to see "substantially" more progress on inflation before the hiking would stop. The Fed is pointing out that there is no Fed put left while markets continue to misprice what the Fed is going to do.

The latest European Central Bank (ECB) projections show inflation is unlikely to reach the 2% target until late 2025. At its December meeting, the ECB took a hawkish turn, and we think it is likely to hike by 50 [basis points \(bps\)](#) at least twice more, in February and March 2023. Similarly, in the UK, the [Monetary Policy Committee \(MPC\)](#) will need to see core [consumer price index \(CPI\)](#) inflation slow materially before the MPC stops its rate hike cycle. The key question in 2023 remains how sticky inflation will be on the upside (how soon it will approach the central bank’s targets), as it will determine the likelihood of central banks maintaining their hawkish stance on [monetary policy](#). Historically, the value factor has demonstrated resilience during periods of interest rate [volatility](#).

**Factor Performance during Periods of Above-Average Interest Rate Volatility**



Sources: WisdomTree, Bank of America Securities, Bloomberg. Data from 1/1/1990 to 1/31/2022; annualized relative performance versus equal-weighted index. You cannot invest directly in an index. Past performance is not indicative of future results.

**De-risking Your Equity Portfolio with the High-Dividend and Value Factors**

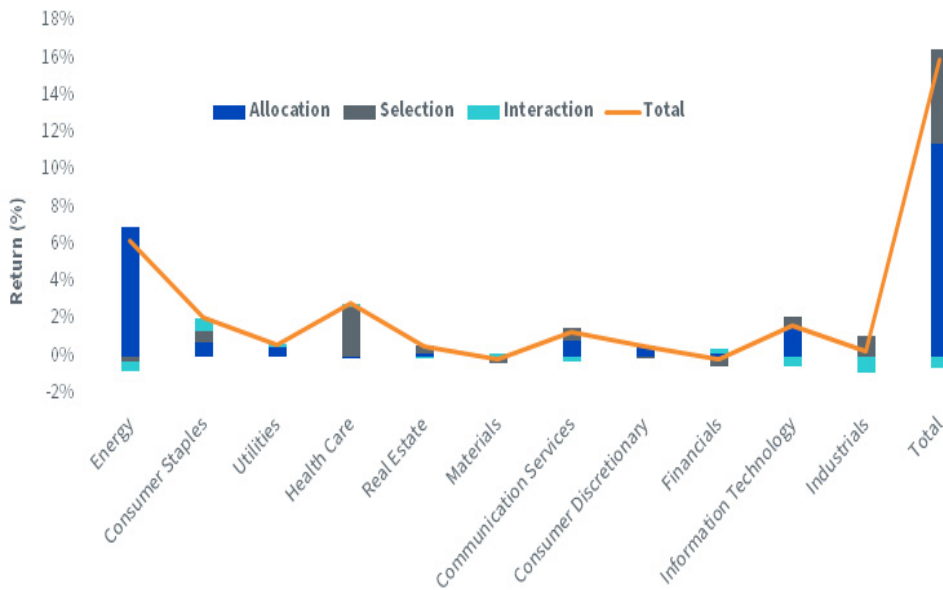
As interest rate volatility is poised to remain high, value-oriented stocks such as Financials, Energy, Utilities, Health Care and Industrials may be in better shape to withstand a slowdown. This is because value companies tend to make their money in the near term, owing to which earnings for these companies are less discounted than for growth companies whose significant profits and cash flow are expected to occur far in the future. Value stocks also have a better chance of defending and/or growing their operating margins than growth stocks.

The high-[dividend](#) factor is synonymous with an investment strategy that gains exposure to companies that appear undervalued and have demonstrated stable and increasing dividends. The strong performance of the dividend factor in 2022 has been a function of its close relationship with stocks with more stable fundamentals alongside the rising rate environment.

**What Worked in 2022?**

Our approach to blending the high-dividend factor alongside the value factor helped the [WisdomTree U.S. High Dividend Index \(WTHYE\)](#) outperform the [Russell 1000 Value Index \(RLV Index\)](#) by 15.9% in 2022. As illustrated in the sector attribution (below), the allocation has been positive, contributing to the tracking difference by +11%. The over-weight in Energy, Information Technology and Consumer Staples benefited performance by +7%, 2% and 1%, respectively, last year.

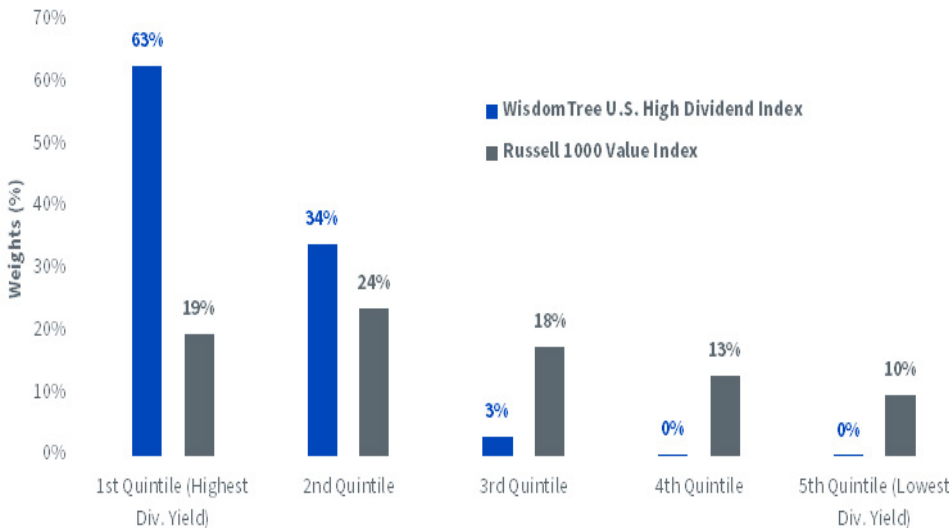
**Sector Attribution – 2022**



Sources: FactSet, WisdomTree, as of 12/31/22. You cannot invest directly in an index. Past performance is not indicative of future results.

More importantly, the higher allocation of the [WisdomTree U.S. High Dividend Index](#) to the higher-yielding dividend quintiles also contributed to the higher relative performance versus the Russell 1000 Value Index.

**Allocation within Dividend Yield Quintiles**



Sources: FactSet, WisdomTree, as of 12/31/22. You cannot invest directly in an index. Past performance is not indicative of future results.

<sup>1</sup> Source: Bloomberg, as of 12/30/22.

For definitions of terms/indexes in the charts above, please visit the [glossary](#).

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

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You cannot invest directly in an index.

## DEFINITIONS

**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.

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

**Inflation** : Characterized by rising price levels.

**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.

**MSCI World Value Index** : Captures large and mid cap securities exhibiting overall value style characteristics across 23 Developed Markets (DM) countries.

**Relative performance** : Comparing the performance outcome measures of one agency to the performance outcome measures of the other agencies performing the same service.

**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.

**Federal Open Market Committee (FOMC)** : The branch of the Federal Reserve Board that determines the direction of monetary policy.

**Federal Reserve** : The Federal Reserve System is the central banking system of the United States.

**Basis point** : 1/100th of 1 percent.

**Monetary Policy Committee (MPC)** : A committee of the Bank of England, which meets for three and a half days, eight times a year, to decide the official interest rate in the United Kingdom (the Bank of England Base Rate).

**Consumer Price Index (CPI)** : A measure that examines the weighted average of prices of a basket of consumer goods and services, such as transportation, food and medical care. The CPI is calculated by taking price changes for each item in the predetermined basket of goods and averaging them; the goods are weighted according to their importance. Changes in CPI are used to assess price changes associated with the cost of living.

**Monetary policy** : Actions of a central bank or other regulatory committee that determine the size and rate of growth of the money supply, which in turn affects interest rates.

**Volatility** : A measure of the dispersion of actual returns around a particular average level.&nbsp;nbsp;.

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

**Russell 1000 Value Index** : A measure of the large-cap value segment of the U.S. equity universe, selecting from the Russell 1000 Index.