

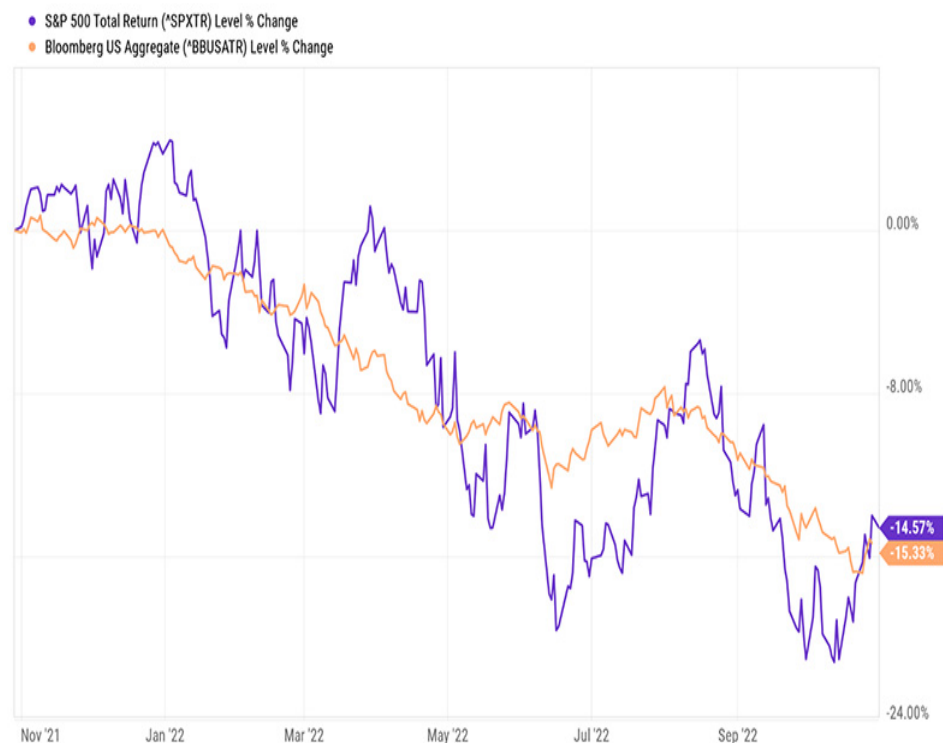
VOLATILITY IS AS VOLATILITY DOES

Scott Welch — Chief Investment Officer, Model Portfolios
11/18/2022

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.

Well, this has been an interesting year, hasn't it? Many investors have not had the "opportunity" to experience a year like this in their professional lives unless they were around for 2000–2001 or 2008–2009. (I'm not counting the COVID-19-induced meltdown in early 2020, which was, to use an increasingly unpopular word these days, "transitory.") Until about a year ago, it was a roughly 10-year market environment of equity [bull](#) markets, [expanding multiples](#), low [interest rates](#) and low [volatility](#).

But here we are, in a quite different environment—equities and [bonds](#) both have fallen, rates are rising, multiples are contracting and volatility is increasing. Most upsetting to many investors is the failure of bonds to provide their historical hedge to equity market risk.

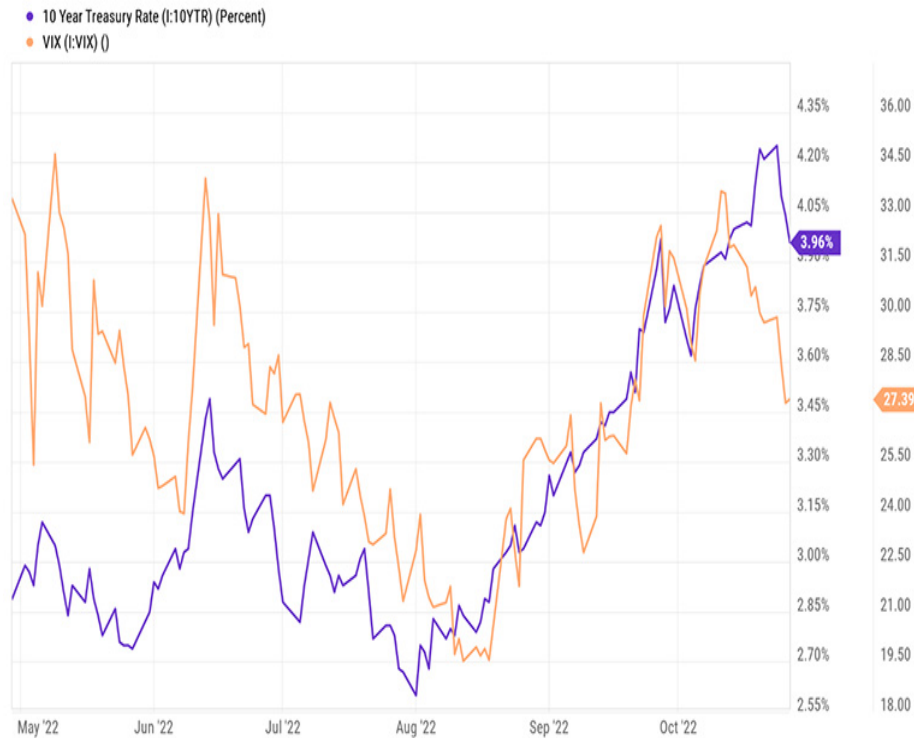


Oct 31 2022, 1:18PM EDT. Powered by **YCHARTS**

Source: YCharts, 12-month data through October 28, 2022. You cannot invest in an index, and past performance does not guarantee future results.

We are receiving an increasing number of inbound calls from advisors asking us, "What else can I put in my portfolio besides stocks or bonds?" The good news is that we have an answer—our **Volatility Management** model.

Before diving into the details of the model, let's remind ourselves of some important historical phenomena—alternative or nontraditional asset strategies tend to work best in rising interest rate and rising market volatility environments, which we certainly would argue represent the current market environment.



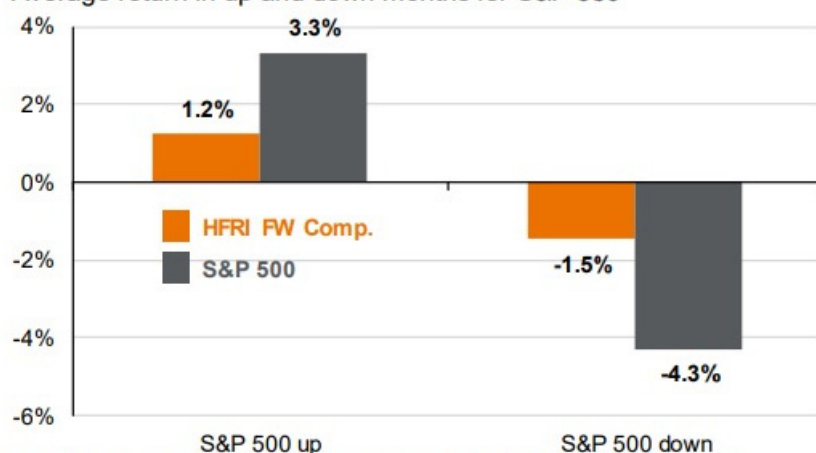
Oct 31 2022, 12:59PM EDT. Powered by **YCHARTS**

Source: YCharts, six-month data as of October 28, 2022. You cannot invest in an index. The Chicago Board of Exchange (CBOE) Volatility Index, or “VIX,” is a calculation designed to produce a measure of constant 30-day expected volatility of the U.S. stock market, derived from real-time, mid-quote prices of S&P 500 Index call and put options. On a global basis, it is one of the most recognized measures of volatility—widely reported by financial media and closely followed by a variety of market participants as a daily market indicator.



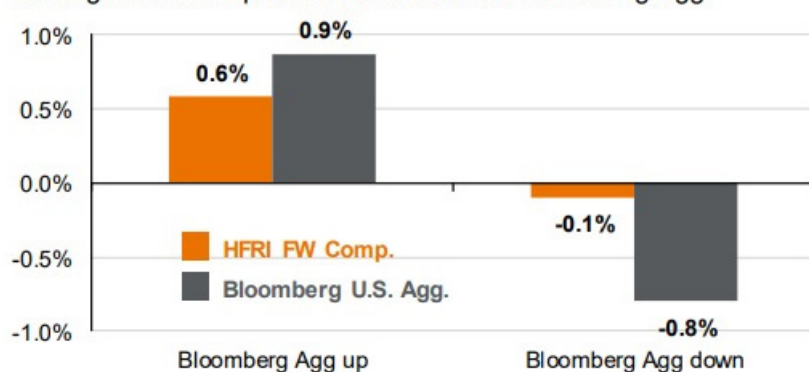
Hedge fund returns in different market environments

Average return in up and down months for S&P 500



Hedge fund returns in different market environments

Average return in up and down months for Bloomberg Agg.



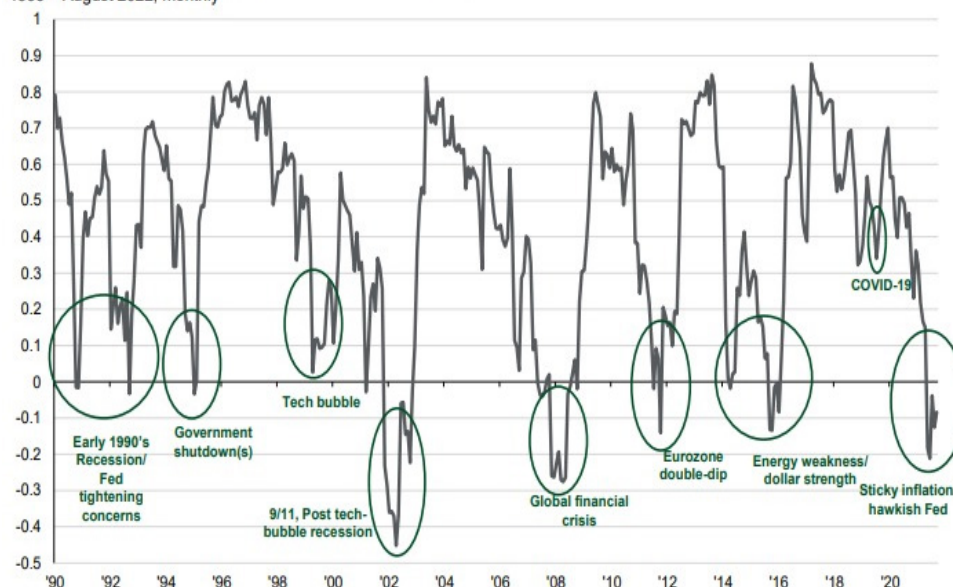
Source: JP Morgan "Guide to the Markets," as of September 30, 2022. You cannot invest in an index, and past performance does not guarantee future results.

These strategies have additional potential benefits: (1) their correlations to traditional stocks and bonds tend to go down in times of [recession](#), and (2) they tend to perform best in higher [inflationary](#) regimes. Again, we think both characteristics are in place in the current market environment.

Hedge funds and traditional portfolios

GTA U.S. 56

Hedge fund correlation with a 60/40 stock-bond portfolio*
1990 – August 2022, monthly



Sources: HFRI, Standard & Poor's, Bloomberg, FactSet, J.P. Morgan Asset Management
*60/40 portfolio is 60% S&P 500 and 40% Bloomberg U.S. Aggregate. Hedge funds are represented by HFRI Macro. Correlation is calculated on a 12-month rolling basis.
Data is based on availability as of August 31, 2022.

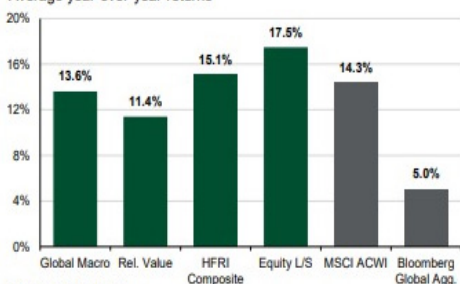
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ASSET MANAGEMENT

Hedge fund returns across inflationary regimes

GTA U.S. 58

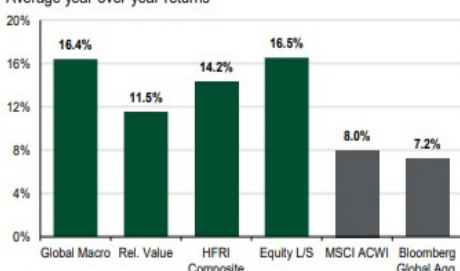
High and rising

Average year-over-year returns



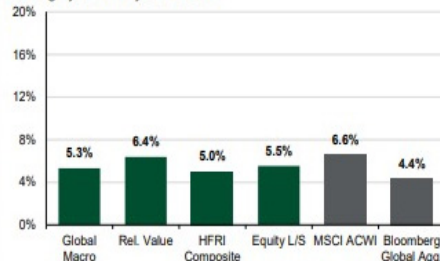
High and falling

Average year-over-year returns



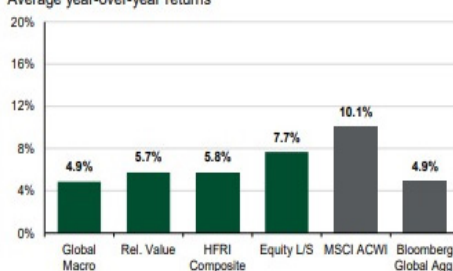
Low and falling

Average year-over-year returns



Low and rising

Average year-over-year returns



Sources: FactSet, HFRI, U.S. Department of Labor, J.P. Morgan Asset Management
All hedge fund returns are from HFRI. HFRI Composite Index. "High" inflation is defined as any year-over-year headline CPI reading above the historical median, while "low" inflation is defined as any year-over-year headline CPI reading below the historical median. The median y/y headline CPI for period between 1991 through July 2022 is 2.44%.
Data is based on availability as of August 31, 2022.

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You cannot invest in an index, and past performance does not guarantee future results.

The WisdomTree Volatility Management Model

With this as background, let's review our Volatility Management ("Vol Man") model.

As with all WisdomTree models, it has certain fundamental characteristics:

1. It is ETF-centric to potentially optimize fees and taxes.
2. It is "open architecture" and contains both WisdomTree and third-party strategies.
3. There is no strategist fee associated with the model—our revenue is generated only from the expense ratios of the WisdomTree strategies contained within the model.

We currently have equal 20% allocations across five different strategies:

1. **Managed Futures**, via our own [WTME](#). We believe all nontraditional or alternative portfolios should start with managed futures, which traditionally have shown almost zero correlation to traditional stocks and bonds, and so may serve as an excellent "anchor position" if the purpose of the portfolio is to improve portfolio diversification and/or add different sources of potential return.
2. **"Hedged Equity/Volatility Premium,"** via our own [put write](#) strategy, [PUTW](#). By selling equity put options, this strategy generates option [premiums](#) used to buffer downside market movement. Since higher levels of premium are generated when equity market volatility is high, this strategy helps to buffer returns of traditional long-only strategies (i.e., the premiums collected help offset negative moves in the market).
3. **Diversified Arbitrage**, via a third-party [mutual fund](#) (the only mutual fund included in any of our publicly available models). These types of strategies attempt to capture market inefficiencies associated with things like corporate mergers, convertibles and other "event-driven" corporate activities. Like managed futures, arbitrage strategies have historically tended to have low correlations to traditional stocks and bonds.
4. **Equity Long/Short**, via a third-party ETF. While these strategies tend to be long the market, their ability to execute short positions may provide mitigation to downside market movement.
5. **Short Biased or "Anti-Beta,"** via a third-party ETF. As the name suggests, these types of strategies are consistently short the market and seek to capitalize on downward market movements. As you might imagine, this strategy is the best-performing allocation within the portfolio so far in 2022.

This collection of strategies has historically tended to not only have a low correlation between the strategies themselves but, more importantly, has had a low correlation to traditional stocks and bonds. It has provided increased portfolio diversification and, therefore, offered a more consistent overall portfolio performance during bearish or volatile market regimes.

This portfolio has performed exactly as expected throughout turbulent 2022, providing a nice buffer against the dramatic decline in both stocks and bonds throughout the year while at the same time kicking off a very respectable portfolio yield. And, at 74 basis points (0.74%), we believe it is very competitively priced versus other solutions available.

WisdomTree Volatility Management Portfolio

1.25%

Model 12-Month Dividend Yield
(As of 10/31/2022)

0.74%

Model Expense Ratio

08/08/2017

Inception date

80% | 20%

Alternative Equity

[Model Performance](#) | [Model Allocations](#) | [Model Exposures](#) | [Fund Performance](#) | [Fund Details](#)

As of 10/31/2022	Cumulative Returns			Average Annual Total Returns				
Name	1-Month	3-Month	YTD	1-Year	3-Year	5-Year	10-Year	Since Inception
WisdomTree Volatility Management Portfolio (NAV)	2.31%	-1.17%	-2.18%	-0.81%	1.90%	0.82%	-	1.04%
WisdomTree Volatility Management Portfolio (MP)	2.37%	-0.89%	-2.25%	-0.83%	1.82%	0.77%	-	1.00%
FTSE 3 Month Treasury Bill Index	0.25%	0.59%	0.87%	0.88%	0.60%	1.16%	-	1.14%

Source: WisdomTree Model Adoption Center, as of 11/17/22. **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.**

The Model Portfolio performance results shown are theoretical and do not reflect any investor's actual experience with owning, trading or managing an actual investment. Thus, the performance shown does not reflect the impact that economic and market factors had or might have had on decision-making if actual investor money had been managed and allocated per the Model Portfolio. The actual performance achieved in seeking to follow the Model Portfolio may differ from the theoretical performance shown for a number of reasons, including the timing of implementation of trades (including rebalancing trades to adjust to Model Portfolio changes), market conditions, fees and expenses (e.g., brokerage commissions, deduction of advisory or other fees or expenses charged by advisors or other third parties to investors, strategist fees and/or platform fees), contributions, withdrawals, account restrictions, tax consequences and/or other factors, any or all of which may lower returns. While the Model Portfolio performance may have been better than the benchmark for some or all periods shown, the performance during any other period may not have been, and there is no assurance that the Model Portfolio performance will be better than the benchmark in the future. The Model Portfolio performance calculations assume reinvestment of dividends, are pre-tax and are net of Fund expenses. ETF shares are bought and sold at market price (not NAV) and are not individually redeemable 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. Model 12-month yield is calculated using the weighted average trailing 12-month distribution yields of the Fund constituents. Funds inception less than 12 months ago do not have a trailing 12-month dividend yield. Model expense ratio refers to the weighted average expense ratios of the Fund constituents.

For the most recent month-end and standardized performance of the model and underlying Funds, please click [here](#).

For the 30-day SEC yield for each of the underlying ETFs, please click the respective ticker: [PUTW](#), [WTMF](#), [BTAL](#), [FTLS](#), [ADAIX](#).

As we noted in a recent blog post on [client conversations in turbulent times](#), these are the market times that try investors' souls—rising rates, increased volatility, a slowing economy, high and “sticky” inflation, a [hawkish Fed](#) and negative investor sentiment. What's not to love, right?

Fortunately, there are things advisors can do to improve portfolio diversification and potentially improve the consistency of performance. Our Volatility Management Model Portfolio is one such potential solution: it was designed to function as a complementary “sleeve” within a traditional stock and bond portfolio with an investment objective of mitigating downside risk.

Financial advisors who register on the WisdomTree website can learn more about this model and how to successfully position it with end clients via our [Model Adoption Center](#).

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

Important Risks Related to this Article

For financial advisors: 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

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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.

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.

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

You cannot invest directly in an index.

DEFINITIONS

Bullish : a position that benefits when asset prices rise.

Multiple expansion : Term for a rising P/E ratio, meaning that share prices are rising faster than earnings are growing.

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

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

Bond : A fixed-income instrument that represents a loan made by an investor to a borrower (typically corporate or governmental).

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

Inflation : Characterized by rising price levels.

PUT Writing : Put writing is an essential part of options strategies. Selling a put is a strategy where an investor writes a put contract, and by selling the contract to the put buyer, the investor has sold the right to sell shares at a specific price. Thus, the put buyer now has the right to sell shares to the put seller.

Premium : When the price of an ETF is higher than its NAV.

Mutual Funds : An investment vehicle made up of a pool of moneys collected from many investors for the purpose of investing in securities such as stocks, bonds, money market instruments and other assets.

Beta : A measure of the volatility of a security or a portfolio in comparison to a benchmark. In general, a beta less than 1 indicates that the investment is less volatile than the benchmark, while a beta more than 1 indicates that the investment is more volatile than the benchmark.

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

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