

I'VE GOT FRIENDS IN LOW PLACES

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*Well, I guess I was wrong
I just don't belong
But then, I've been there before
Everything's all right
I'll just say goodnight
And I'll show myself to the door
Hey, I didn't mean
To cause a big scene
Just give me an hour and then
Well, I'll be as high as that ivory tower
That you're livin' in
'Cause I've got friends in low places
Where the whiskey drowns
And the beer chases my blues away
And I'll be okay
I'm not big on social graces
Think I'll slip on down to the oasis
Oh, I've got friends in low places...*

(From "Friends in Low Places," performed by Garth Brooks, 1990)

We recently wrote about the investor demand for "[low volatility](#)" positions within their portfolio. Let's update our chart from that blog for year-to-date (it ain't pretty):

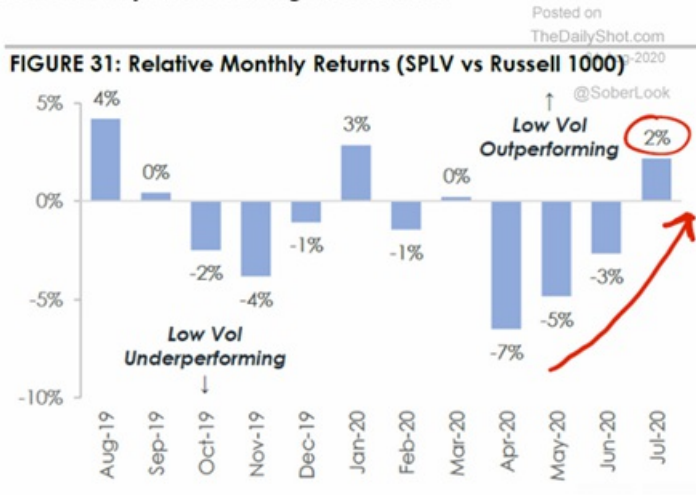


Source: YCharts, data as of 8/11/20. You cannot invest in an index. Past performance does not guarantee future results.

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

If we broaden our horizons (i.e., compare "low vol" to the [Russell 1000 Index](#) instead of the [S&P 500](#), which is dominated by the [mega-cap](#) tech stocks), however, "[low vol](#)" seems to be making a bit of a comeback.

Low Volatility Factor Making a Comeback?



MarketDesk Research | Factor Views

Sources: MarketDesk Research and The Daily Shot, 8/6/20. You cannot invest in an index. Past performance does not guarantee future results. SPLV is the Invesco S&P 500 Low Volatility ETF. SPLV tracks the S&P 500 Low Volatility Index, which is a volatility-weighted index of the 100 least-volatile stocks in the S&P 500.

Furthermore, despite relatively anemic relative performance, investor demand for “low volatility” positions within their portfolios seems to be increasing, given the rise in overall market volatility due to the ongoing coronavirus pandemic and corresponding economic uncertainty. First, let’s illustrate the potential “regime change” in volatility:

CBOE S&P 500 Volatility Index VAL 23.76 CHG +1.63 % CHG +7.37%

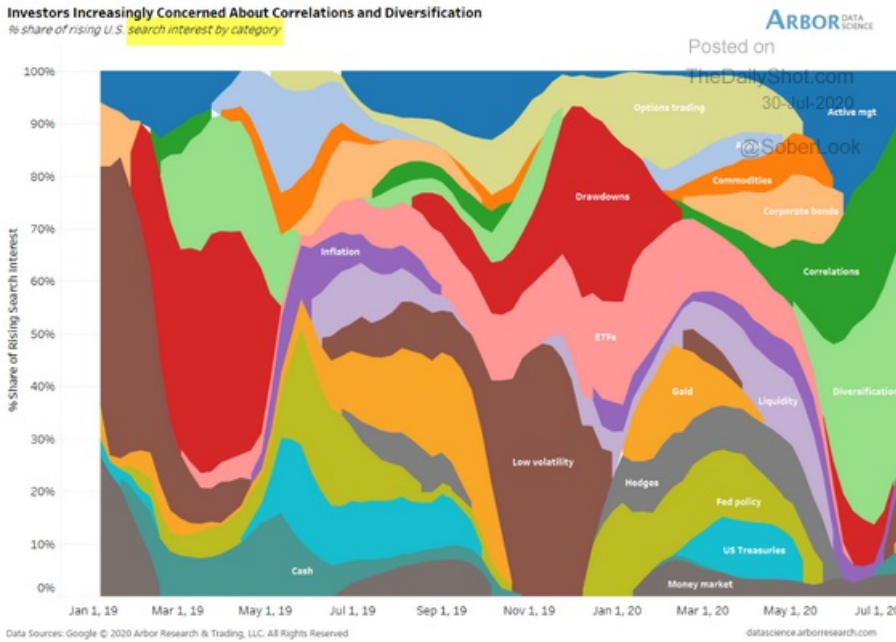


Aug 11 2020, 3:56PM EDT. Powered by YCHARTS

Source: YCharts, data as of 8/11/20. You cannot invest in an index. Past performance does not guarantee future results. CBOE Volatility Index® (VIX®): a key measure of market expectations of near-term volatility conveyed by S&P 500 stock index option prices. It is the premier benchmark for U.S. stock market volatility.

Now, let’s examine how investors are reacting to this potential volatility “regime change.” This next chart somewhat resembles a surrealist painting, but it illustrates an interesting point—investors increasingly are seeking “diversification” within their portfolios:

Investors Increasingly Concerned About Correlations and Diversification
% share of rising U.S. search interest by category



Sources: Arbor Data Science and The Daily Shot, 7/30/20.

Finally, let's remind ourselves of the importance of [factor diversification](#) as well as asset class [diversification](#) when attempting to build a truly diversified portfolio. Just like asset classes, risk factors rotate in and out of favor. In this busy "risk factor performance quilt," focus your eyes on the dark green "multifactor" index box—notice how it tends to "cluster" around the middle, suggesting more consistent and stable historical performance relative to the other, more individual, risk factors:

2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020 YTD
Momentum (-1.8%)	Value (6.32%)	Correlation (3.04%)	Quality (1.1%)	LowVol (19.30%)	Quality (30.93%)	LowVol (-23.10%)	Value (2.1%)	Quality (25.67%)	LowVol (12.31%)	Quality (18.82%)	Value (6.52%)	LowVol (17.2%)	Momentum (7.46%)	Value (18.44%)	Quality (25.42%)	LowVol (-4.2%)	Size (28.23%)	Correlation (8.52%)
LowVol (-2.50%)	WTUSMFU (38.36%)	Multifactor (21.63%)	Value (25.26%)	Momentum (17.42%)	Correlation (7.38%)	Momentum (-25.75%)	WTUSMFU (40.14%)	WTUSMFU (23.23%)	Momentum (12.08%)	Value (17.72%)	Size (35.77%)	Multifactor (26.96%)	LowVol (5.32%)	WTUSMFU (11.4%)	Size (22.21%)	Momentum (-2.36%)	Quality (7.92%)	Size (-0.83%)
Multifactor (-2.87%)	Correlation (34.08%)	Value (36.62%)	Correlation (15.0%)	Value (17.30%)	Size (7.18%)	Multifactor (-32.59%)	Quality (8.07%)	Value (20.57%)	Multifactor (10.60%)	WTUSMFU (17.26%)	WTUSMFU (3.33%)	Correlation (15.2%)	Quality (1.7%)	Quality (13.23%)	WTUSMFU (16.63%)	Correlation (-3.07%)	Value (7.75%)	Momentum (-1.86%)
Correlation (-7.12%)	Quality (12.91%)	LowVol (2.13%)	Multifactor (5.82%)	Multifactor (15.42%)	Multifactor (5.45%)	Quality (-25.03%)	Correlation (2.82%)	Correlation (20.12%)	Correlation (6.43%)	Size (25.7%)	Correlation (36.82%)	Momentum (15.2%)	Size (0.60%)	LowVol (13.02%)	Value (19.1%)	Multifactor (-4.82%)	LowVol (7.67%)	Quality (2.47%)
Quality (-3.27%)	Multifactor (30.67%)	Quality (21.48%)	WTUSMFU (21.07%)	WTUSMFU (14.4%)	WTUSMFU (5.77%)	Size (-36.67%)	Size (2.78%)	Momentum (27.56%)	Quality (3.4%)	Multifactor (15.47%)	Quality (31.78%)	Size (31.20%)	Multifactor (10.5%)	Size (11.59%)	Momentum (18.77%)	Size (-4.38%)	WTUSMFU (27.1%)	WTUSMFU (-4.76%)
Value (-45.47%)	Size (30.15%)	WTUSMFU (21.44%)	Size (7.59%)	Size (13.39%)	Momentum (5.39%)	Value (-36.47%)	Multifactor (26.58%)	Multifactor (17.38%)	Size (0.05%)	Correlation (15.52%)	Multifactor (12.73%)	Value (13.92%)	WTUSMFU (-1.31%)	Momentum (6.96%)	Multifactor (17.52%)	Quality (-4.87%)	Momentum (20.13%)	Multifactor (-5.55%)
WTUSMFU (-17.97%)	LowVol (27.01%)	Momentum (17.02%)	Momentum (5.55%)	Quality (12.57%)	LowVol (1.94%)	WTUSMFU (-38.80%)	LowVol (29.27%)	LowVol (25.94%)	WTUSMFU (10.12%)	Momentum (13.15%)	Momentum (27.99%)	Quality (23.22%)	Value (-5.94%)	Multifactor (17.7%)	LowVol (17.29%)	WTUSMFU (-7.82%)	Correlation (23.15%)	LowVol (-7.10%)
Size (-22.22%)	Momentum (25.57%)	Size (13.18%)	LowVol (5.07%)	Correlation (11.44%)	Value (0.27%)	Correlation (-8.07%)	Momentum (25.13%)	Size (14.5%)	Value (-1.34%)	LowVol (12.04%)	LowVol (21.76%)	WTUSMFU (12.2%)	Correlation (-7.79%)	Correlation (7.5%)	Correlation (13.51%)	Value (-43.2%)	Multifactor (20.11%)	Value (-24.97%)

Source: WisdomTree Asset Management, data through 7/31/20. You cannot invest in a factor. Past performance does not guarantee future results.

All of this focus on "low volatility" diversification brings us to what we think might be an interesting WisdomTree solution set—our U.S., EAFE (Europe, Australasia and the Far East) and Emerging Markets (EM) [multifactor strategies](#). All of these strategies screen for multiple risk factors, including [quality](#), [value](#), [momentum](#) and [low correlation](#) relative to the broader market.

The result is a "low vol" strategy (or, more specifically, a strategy that seeks to lower overall portfolio volatility by increasing the risk factor diversification), but at much more attractive [valuations](#) than the much-sought-after "low volatility" strategies.

As a point of comparison, as of mid-August a very popular ETF that tracks the performance of the S&P 500 Index currently trades at a [price-to-earnings \(P/E\) ratio](#) of ~24.9%. Another popular ETF that tracks the performance of the S&P 500 Low Volatility Index currently trades at a P/E ratio of ~23.3%—barely a discount for an Index that includes the hyper-valued mega-cap tech stocks.

But the [WisdomTree U.S. Multifactor Fund \(USMF\)](#) currently trades at a P/E ratio of ~18.2%—and it also carries lower

valuations on a [price/sales](#), [price/cash flow](#) and [price/book basis](#). Additionally, the securities within USMF show significantly higher quality characteristics (e.g., [return on equity](#), [return on assets](#) and [leverage](#)) than those other two ETFs.

The bottom line? If you are seeking smarter diversification within your overall portfolio, the WisdomTree multifactor strategies may be able to help you get there without overpaying for the benefit of “low volatility.”

Important Risks Related to this Article

Diversification does not eliminate the risk of experiencing investment losses.

There are risks associated with investing, including possible loss of principal. Investing in a Fund exposed to particular sectors increases the vulnerability to any single economic, political or regulatory development. This may result in greater share price volatility. Due to the investment strategy of the Fund, it may make higher capital gain distributions than other ETFs. Please read the Fund’s prospectus for specific details regarding the Fund’s risk profile.

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.

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You cannot invest directly in an index.

DEFINITIONS

Russell 1000 Index : A measure of the performance of the 1,000 largest companies by market capitalization in the Russell 3000 Index.

Mega Cap : Market Capitalization over \$100 Billion.

Low Volatility : Characterized by lower standard deviation of price over time. This term is also associated with the Low Volatility Factor, which associates lower volatility stocks with better risk-adjusted returns vs the market over time.

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

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

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.

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.

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.

Low Correlation : Characterized by assets that have a relatively lower correlation vs the market over time. This term is also associated with the Low Correlation Factor which associates these stock characteristics with excess returns vs the market over time.

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.

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.

Price-to-sales (P/S) ratio : share price divided by per share revenue.

Price-to-cash flow (P/CF) ratio : Share price divided by cash flow per share. Lower numbers indicate an ability to access greater amounts of cash flows per dollar invested.

Price-to-book ratio : Share price divided by book value per share. Lower numbers indicate an ability to access greater amounts of earnings per dollar invested.

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.

Leverage : Total assets divided by equity. Higher numbers indicate greater borrowing to finance asset purchases; leverage can tend to make positive performance more positive and negative performance more negative.