Thematic Tactical Rotation: how are we doing so far?

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Key Takeaways

- Multi-thematic strategies offer a better way to invest in growth than traditional growth funds, but it takes a lot of expertise to successfully construct those strategies
- Multi-thematic strategies should offer three clear value-add propositions: theme selection, capital allocation between themes and expert-driven stock selection for each theme
- The tactical overlay in the WisdomTree Global Megatrends Equity Index correctly overweighted or underweighted 11 themes in its first rebalancing period and 10 in its second.
- The tactical overlay in the WisdomTree Global Megatrends Equity Index created 8.1% outperformance in its first four months of live performance

Thematic investing offers investors a new way to gain exposure to growth. Thematics provide a forward-looking grid that allows investors to select growth stocks not based on backwards-looking growth fundamentals but based on companies' forward-looking use cases and how this aligns with long-term structural shifts in our society and our world. In many ways, thematic strategies have become growth strategies 2.0.

When investing in thematics, investors have two main choices: single-theme strategies if they want to keep control of this part of their portfolio or multi-thematic strategies. Multi-thematic strategies offer investors a one-stop solution to participate in long-term equity growth across different megatrends as they develop, while delegating the decisions around the selection of the most relevant themes, the capital allocation between themes and the stock selection. Throughout 2023, in Europe, we have seen many investors make that second choice. Despite outflows in the thematic space, multi-thematic strategies gathered over $4 billion1.

After six years of thematic research, two whitepapers, and ten single-theme ETFs, WisdomTree launched a new multi-thematic strategy, the WisdomTree Global Megatrends Equity index, on 27 October 2023, followed in December by the launch of an ETF, the WisdomTree Megatrends UCITS ETF.

The WisdomTree megatrends strategy

Our strategy offers a unique approach that allows investors to get access to long-term growth through a curated portfolio of themes and expert-driven stock selection. Investors also benefit from tactical allocation to the different themes over time to adapt to current market environments. Investors benefit from three layers of value creation:

1. Strategic thematic asset allocation

First, WisdomTree delivers a curated selection of promising themes (around 15) out of all the available themes in the investment space. Each year, the selection focuses on high-conviction themes with a high diversification potential and alignment with the UN Sustainable Development Goals (SDGs).

2. Tactical thematic asset allocation

WisdomTree also applied a proprietary, momentum-based, tactical overlay to overweight and underweight themes every quarter. The objective is to benefit from virtuous cycles in themes, like Cloud in 2020 around the remote working craze or AI and Semiconductors in 2023, following the launch of ChatGPT.

3. Thematic stock selection

Finally, regarding the stock selection in each theme, WisdomTree focuses on pure-play companies, meaning those with more direct exposure to the theme rather than tangential exposure. To do so, the portfolio for each theme is built independently in partnership with a theme-specific expert.

A closer look at the tactical overlay

More than four months after the strategy's launch, it is time to take stock of the performance of the tactical overlay in the WisdomTree Global Megatrends Equity Index. Since we rebalanced the portfolio on 19 January 2024, we can look at two distinct periods with their specific overweights and underweights:

- Figure 1 – 25 October 2023 to 19 January 2024
- Figure 2 – 19 January 2024 to 29 February 2024

In the first rebalancing periods, the portfolio was overweighting five themes: AI, Blockchain, Cloud Computing, Cybersecurity and Semiconductors. Over the period considered, all five of those themes outperformed the MSCI ACWI. Four of them outperformed by double-digit numbers and AI outperformed by only 9.6.%, so the overweighting worked well.

Of the nine themes we underweighted, six underperformed MSCI ACWI. The Rise of EM Consumer underperformed by 23.2%, and Sustainable Resource Management by 14.5%, for example. Only three themes that we underweighted outperformed the market: Rise of the Middle Class, HealthTech, and Digital Infrastructure but they did so narrowly with +4.2%, +1.7% and +6.1% (respectively).

Overall, the tactical overlay got 11 out of 14 themes right in that first period – so the tactical overlay added 5.77% to the performance.

Figure 1: WisdomTree thematic tactical overlay's performance up to 19 January 2024

Source: WisdomTree, Morningstar, Bloomberg. From 23 October 2023 to 19 January 2024. Historical performance is not an indication of future performance and any investments may go down in value. You can not invest in an index.

On 19 January, the strategy was rebalanced. While the same five themes remained overweighted, the overweights were slightly smaller. As a result, the underweight in Digital Infrastructure, HealthTech, and Sustainable Resource Management was reduced.

Only three of our five overweights have worked as of the end of February. Cloud Computing and Cybersecurity have been underperforming the market slightly over the period. However, Blockchain is up 30.2%, and Semiconductors are up 6.9% on a relative basis, which more than compensates for the small underperformance of the other two themes.

Out of the nine underweight, seven themes did underperform. So-called "green themes" continue to suffer, leading to much of that underperformance. This means that the tactical overlay only got HealthTech and Rise of the EM Consumer wrong this time.

Overall, the tactical overlay got 11 out of 14 themes right in that second period so far, adding 2.35% to the performance.

Figure 2: WisdomTree thematic tactical overlay's performance from 19 January 2024

Source: WisdomTree, Morningstar, Bloomberg. From 19 January 2024 to 29 February 2024. Historical performance is not an indication of future performance and any investments may go down in value. You can not invest in an index.

Conclusion

Creating a multi-thematic strategy is a difficult endeavour that requires lots of research and experience in the thematic space. Investors expect to receive the benefit of intelligent theme selection, theme weighting, stock selection and to see a portfolio that offers a lot of differentiation to tech indices or the Nasdaq 100. After six years of research, WisdomTree launched its own multi-thematic strategy that offers innovative solutions to these challenges. In the first four months of the live track record, the theme selection (i.e., the strategic allocation) delivered 1.6% of outperformance versus the MSCI ACWI, with the tactical overlay adding 8.1% of outperformance.

Sources

1 Source: WisdomTree, Morningstar, Bloomberg. From 30 December 2022 to 31 December 2023. The list of Europe-Domiciled ETFs and Open-ended mutual funds has been compiled by WisdomTree as part

of the WisdomTree's own thematic classification. Historical performance is not an indication of future performance and any investments may go down in value.

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