WisdomTree Megatrends: Outperforming while thematics are struggling

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Key Takeaways

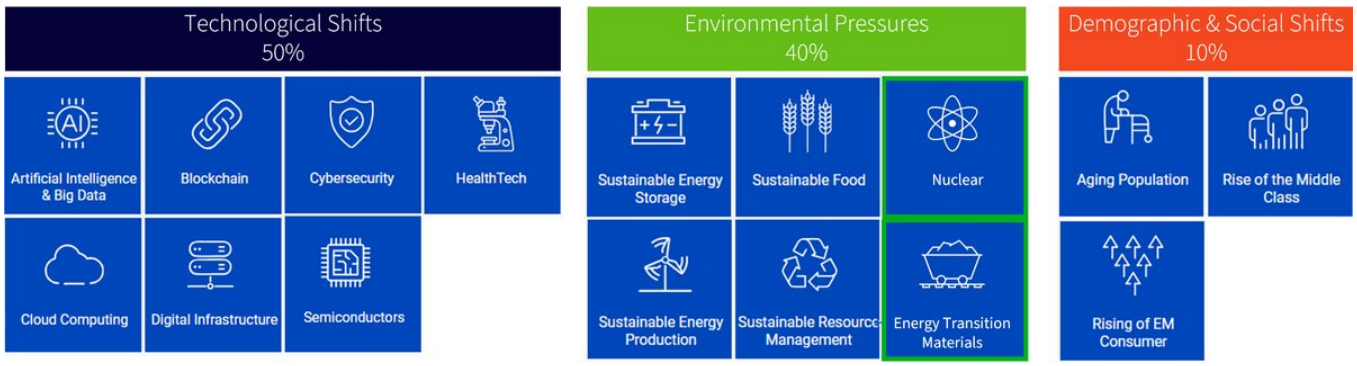
- WisdomTree Megatrends strategy provides a one-stop solution to invest in thematic equities that includes a theme-based tactical overlay to benefit from short-term moves.
- At the latest rebalance, Blockchain was the most favoured theme followed by Semiconductors
- Data centre providers looking to deliver energy independence to their servers could lead to a resurgence in renewable energy, batteries and energy transition materials (miners)

The re-election of Donald Trump in early November sent shockwaves through financial markets, reminiscent of his 2016 victory. As investors digest the implications of Trump's second term, certain thematic equities are already emerging as clear winners. Blockchain equities, for example, delivered strongly in line with President-elect Trump's expected friendliness to the space. Defence stocks are also benefitting from expectations of pressure on NATO's countries to spend more. Conversely, ESG-focused companies have seen declines amid concerns over reduced environmental priorities.

Thanks to its quarterly tactical allocation, the WisdomTree Megatrends Global Equity Index always aims to be positioned to benefit from variations in sentiment around thematics. To do so, the strategy's portfolio is constructed using three successive steps that seek to add value:

- The strategic thematic asset allocation focuses yearly on the most relevant themes in the medium to long term. Currently, the portfolio invests in 16 themes:

Figure 1: WisdomTree global megatrends equity – theme selection



Source: WisdomTree. November 2024

- The tactical asset allocation run quarterly and overweights and underweights themes to position the portfolio to best benefit from periods of exuberance and sluggishness in the various themes.
- The stock selection in each theme leverages WisdomTree thematic investment philosophy, which focuses on:
- Expertise: WisdomTree partners with external experts when constructing their thematic portfolios.
- Purity: Stocks in our thematic portfolios have a business focused principally on one theme.
- Differentiation: Our thematic portfolios are very different from market indices (the overlap between the WisdomTree Multi thematic strategy and the MSCI AC World or the Nasdaq is less than 20%) and very different between themes as well.

WisdomTree thematic tactical overlay: How are we positioned?

As of the latest rebalancing on 18 October, we saw significant changes in the tactical positioning of the portfolio based on our quantitative momentum and mean reversion signals:

- Blockchain remained the most overweighted theme this quarter after delivering strong performance year long. This overweight is already paying off, considering the US election result in early November.
- Semiconductors was the second and only theme to remain overweighted but less so than last quarter. Almost two years into the latest Artificial Intelligence (AI) wave, mean reverting signals have kicked in and led to a reduced overweight.
- AI moved to underweight after moving to neutral last time (mid-July). After strong performance in 2023 and H1, the theme has shown some signs of abating, with some underperformance and outflows in the last few months.
- Nuclear also moved to underweight.
- It is worth noting that quite a few themes that have been underweight for a while moved back closer to neutral. They are still underweight but are showing signs of life. This is the case with Digital Infrastructure, Energy Transition Miners, the Rise of EM Consumers, Sustainable Energy Storage and Sustainable Food.

- This slight rebound in renewable energy-related themes, which suffered from a certain disinterest from the investment community since late 2022, is due to development in the data centre world. Large Language Models consume vast quantities of energy, for example, a ChatGPT request consumes 10 times more than a Google search. Data Center operators are therefore looking for more and more energy while striving to create an independent energy supply that would insulate them from grid issues. This translates into the need for local energy production, i.e. solar, wind and local storage, i.e. batteries and, by extension, energy transition materials, even if this drive is unrelated to climate change.
- All remaining themes continue to suffer from headwinds and remain underweight.

Figure 2: WisdomTree global megatrends equity – tactical overlay

Source: WisdomTree, Bloomberg as of 18 October 2024. You cannot invest directly in an index. Historical performance is not an indication of future performance and any investments may go down in value.

Outperforming the market since inception thanks to its three-layer approach

Looking back, the strategy continues to deliver above-market performance. As of the time of writing (11 November 2024), the strategy had returned 47.2% since its inception on 27 October 20231. This means that the strategy outperformed the MSCI AC World by 7.9% over the period.

Focusing only on the period up to the rebalancing (18 October 2024), the strategy had outperformed by 1.15%. Figure 3 shows how that performance was created.

- First, the strategic asset allocation was detrimental. Overall, 2024 has been challenging for thematics, with 11 themes underperforming the market. This led to -6.96% of relative underperformance from this layer.
- Second, the tactical asset allocation performed very well, creating 6.23% of outperformance. The tactical allocation to Blockchain (overweighted), AI (mostly overweighted), Cybersecurity (oscillating between overweight and underweight) and Semiconductors (overweighted) was particularly positive.
- Finally, our expertise-driven, pure-play stock selection led to a contribution of +1.89% versus the benchmark.

So, overall, despite headwinds in thematic equities, the strategy managed to outperform thanks to the layers used in the portfolio construction.

Figure 3: Performance attribution since the inception of the strategy (by layers)

Source: WisdomTree, Bloomberg. In USD. From 27 October 2023 to 18 October 2024. You cannot invest directly in an index. Historical performance is not an indication of future performance and any investments may go down in value.

What is happening now?

Since the rebalancing, the strategy's relative performance has been very strong. It created 4.8% of outperformance over the MSCI ACWI and 3.1% over the Nasdaq 1002. This is the result of good positioning in light of the US Election results. The rally in blockchain equity was particularly positive for the strategy.

Overall, equities are benefiting from the ‘certainty effect’ (US election results are now in, and uncertainty is reduced), the ‘Trump effect’, the ‘earnings effect’ (as of 7 November, 75 companies in the Nasdaq-100 index had reported their Q3 earnings, with 68% delivering positive revenue surprises), the ‘Fed effect’ (the US Federal Reserve is continuing to cut interest rates) and the ‘inflation effect’ (inflation remain in check). All of these combined could continue to push equities and in particular small cap and tech equities upwards.

1 Source: WisdomTree, Bloomberg. In USD. From 27 October 2023 to 11 November 2024. **You cannot invest directly in an index. Historical performance is not an indication of future performance and any investments may go down in value.**
2 Source: WisdomTree, Bloomberg. In USD. From 18 October 2024 to 11 November 2024. **You cannot invest directly in an index. Historical performance is not an indication of future performance and any investments may go down in value.**

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