

**2023**  
**ECONOMIC**  
**& MARKET**  
**OUTLOOK**



**ACTIONABLE IDEAS**  
Q4/2023

# Macro Insight: Volatility Remains a Market Constant

## + Economic backdrop: Volatility quotient remains elevated

- Inflation is expected to continue cooling for the rest of the year, though we have a plot twist with resurgent crude oil
- The U.S. economy has remained surprisingly resilient in the wake of historic Fed rate hikes, but a negative quarter or two for real GDP in 2024 should not be ruled out
- Labor market data will hold the key to Fed actions; softening is anticipated
- Broad stock market earnings could be vulnerable
- Treasury yields are expected to remain elevated before falling in 2024

## + Fed policy and global central banks will continue to take centerstage

- The Fed appears to be at, or close to, the end of this rate hike cycle
- Upon concluding its rate hikes, it should then go on extended pause
- Rate cuts are expected to come into focus by mid-2024
- Equity and bond markets seem to be in better alignment with the Fed narrative
- Still keeping our eye on banks and the funding markets

# Taking Precaution in Quality: U.S. Equities

**Outlook:** Our primary concern for the S&P 500's earnings outlook is that the stage of the credit tightening cycle is manifesting in tough responses in the Fed's Senior Loan Officer Survey. However, we were particularly worried a half year ago that what we called the "bank walk," whereby deposits were to flow out of banks and maybe bring some other regional banks down the path that was taken by Silicon Valley Bank (SVB), could be a multi-year overhang. Fortunately, that has not happened.

The market has been selling off since July 31, but with little conviction either way with respect to Growth or Value in U.S. equities (though Value has been trouncing Growth in many overseas markets). Some groups that have been characterized by speculative fervor, such as solar and wind companies and other unprofitable or "story" stocks have been hard hit. Still, it is tough to draw conclusions, as there are also some new 52-week lows being made in traditionally stodgy groups such as food companies and utilities. This is a stock market in flux.

- + **What We Like:** We are concerned that the market does not fully appreciate the game changer that a 5.5% Fed funds rate may well bring to this economy. Owning baskets of high-quality companies at reasonable valuations seems a prudent course of action, as any reincarnation of 2022's ugly stock market environment would necessitate a posture that errs on the side of mitigating downside.
- + **What Could Go Wrong:** The market has been no stranger to sudden, bold up-moves in speculative stocks that have no earnings in recent years. What if that happens again? Though we do not suspect anything like that, such a market would leave many WisdomTree strategies behind.

## Actionable Idea:

- DGRW: WisdomTree U.S. Quality Dividend Growth Fund

# Taking Precaution in Quality: International DM Equities

**Outlook:** We have been heartened by Japan in particular. The economic data in that country has held up, while the collapsed yen has created a generational corporate competitiveness set-up. To some extent, a similar situation has occurred with sterling and the euro.

- + **What We Like:** Japan's 2024 NISA program expansion, which is akin to a traditional IRA, may help pull retail investors into the stock market. Additionally, we believe the Tokyo Stock Exchange's push for corporate governance reform may have some staying power. In broad developed markets, we are routinely seeing our baskets showing up at multi-year valuation lows across much of our dividend business. Some of our overseas quality screens are showing up with return on equity (ROE) results that are double those of the broad market.
- + **What Could Go Wrong:** We must remember that Mother Nature gave Europe a gift last winter, in that temperatures did not necessitate heavy use of Russia-provided natural gas for home heating. Not every winter will be balmy. Additionally, global stocks have been having a rough couple of months, after having surged relentlessly during the year's first seven months. The key risk is that central banks went too far, too fast.

## Actionable Ideas:

- IHDG: WisdomTree International Hedged Quality Dividend Growth Fund
- DXJ: WisdomTree Japan Hedged Equity Fund

# Taking Precaution in Quality: Emerging Markets Equities

**Outlook:** We continue to believe China is investable, though the central government's further concentration of political power breeds risk in equities. However, there's significant inefficiency in the market's pricing of China risk; overreactions to both good and bad news are common. We continue to assess very low risk of U.S.-China conflict over Taiwan, though the constant cloud is problematic for investor sentiment in the region. India may be a beneficiary, as it appears to be leveraging its membership in the so-called BRICs while at the same time maintaining friendly relations with the likes of the U.S. and Japan.

- + **What We Like:** Many deep value and quality-oriented value mandates have dividend yields that are near double digits. Emerging Markets Value is also a contrarian play, owing to years of historical underperformance. We are hopeful that indications of Value trumping Growth this autumn, which we have witnessed in both developed markets (DM) and emerging markets (EM), can persist into a 2024 regime that battles a tightened global credit environment.
- + **What Could Go Wrong:** China could continue to forge closer ties with Russia or saber-rattle Taiwan. In panics, investors often sell emerging markets first and ask questions later. A source of pessimism from somewhere in the developed world could end up causing underperformance in the emerging world, at no fault of its own. India is in the middle of a diplomatic feud with Canada that may hinder U.S. relations, though we have trouble seeing how this could adversely affect equity valuations near term.

## Actionable Ideas:

- DEM: WisdomTree Emerging Markets High Dividend Fund
- EPI: WisdomTree India Earnings Fund

# Fixed Income: A Return to Normalcy

**Outlook:** The narrative for the U.S. fixed income arena has experienced a ‘sea-change’ in attitude due to the surprising resiliency in economic growth and a subsequent restrictive Fed policy. Treasury yields have risen to new high watermarks not seen in sixteen years. Until the U.S. economy begins to reveal signs of a significant slowing in activity, it would appear as if interest rates will remain at elevated levels. We expect rates to be ‘higher for longer’, with volatility continuing to be a part of the broader bond market investment landscape.

This development has created an interesting phenomenon: there’s “income back in fixed income.”

- + **What We Like:** Yields have risen to (normal) levels that a generation of advisors and investors have never seen before, returning fixed income to its more traditional role in portfolios.
- + **What Could Go Wrong:** We could see no recession, with inflation remaining ‘sticky’. As a result, the Fed (global central banks) either continue to raise rates more than expected, or don’t cut them until mid to late 2024.

Or we could see a deep recession where the U.S. economy (labor market) rolls over and the Fed cuts rates sooner than expected. Other concerns include geopolitical developments (such as Ukraine, China/Taiwan and/or Middle East escalation).

## Actionable Ideas:

- USFR: WisdomTree Floating Rate Treasury Fund
- WFHY: WisdomTree U.S. High Yield Corporate Bond Fund
- AGGY: WisdomTree Yield Enhanced U.S. Aggregate Bond Fund

# Glossary

**Central bank:** An institution that manages the currency and monetary policy of a state or formal monetary union and oversees their commercial banking system.

**Dividend yield:** A financial ratio that shows how much a company pays out in dividends each year relative to its share price.

**Fed Funds Rate:** The rate that banks that are members of the Federal Reserve system charge on overnight loans to one another. The Federal Open Market Committee sets this rate. Also referred to as the “policy rate” of the U.S. Federal Reserve.

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

**Gross Domestic Product (GDP):** The sum total of all goods and services produced across an economy. Real GDP is a macroeconomic statistic that measures the value of the goods and services produced by an economy in a specific period, adjusted for price changes.

**Growth stocks:** Stocks whose share prices are higher relative to their earnings per share or dividends per share. Investors are willing to pay more because of their earnings or dividend growth expectations going forward.

**NISA:** A Nippon individual savings account (NISA) is an account that is meant to help residents in Japan save money with tax-exempt benefits.

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

**Return on Equity (ROE):** Measures a corporation’s profitability by revealing how much profit a company generates with the money shareholders have invested.

**S&P 500 Index:** Market capitalization-weighted benchmark of 500 stocks selected by the Standard and Poor’s Index Committee designed to represent the performance of the leading industries in the United States economy.

**Treasury:** Debt obligation issued by the U.S. government with payments of principal and interest backed by the full faith and credit of the U.S. government.

**Valuations:** 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.

**Value stocks:** Stocks whose share prices are lower relative to their earnings per share or dividends per share. Investors pay less for these stocks because their earnings or dividend growth expectations going forward are lower.

**Yield:** The income return on an investment. Refers to the interest or dividends received from a security that is typically expressed annually as a percentage of the market or face value.

# Important Information

**Investors should carefully consider the investment objectives, risks, charges and expenses of the Funds before investing. To obtain a prospectus containing this and other important information, please call 866.909.9473, or visit [WisdomTree.com/investments](https://www.wisdomtree.com/investments) to view or download a prospectus. Investors should read the prospectus carefully before investing.**

There are risks associated with investing, including the possible loss of principal.

**DGRW:** Funds focusing their investments on certain sectors increase their vulnerability to any single economic or regulatory development. This may result in greater share price volatility. Dividends are not guaranteed and a company's future abilities to pay dividends may be limited. A company currently paying dividends may cease paying dividends at any time.

**IHDG:** Foreign investing involves special risks, such as risk of loss from currency fluctuation or political or economic uncertainty. To the extent the Fund invests a significant portion of its assets in the securities of companies of a single country or region, it is likely to be impacted by the events or conditions affecting that country or region. Dividends are not guaranteed and a company currently paying dividends may cease paying dividends at any time. Investments in currency involve additional special risks, such as credit risk and interest rate fluctuations. Derivative investments can be volatile and these investments may be less liquid than other securities, and more sensitive to the effect of varied economic conditions. As this Fund can have a high concentration in some issuers, the Fund can be adversely impacted by changes affecting those issuers. The Fund invests in the securities included in, or representative of, its Index regardless of their investment merit and the Fund does not attempt to outperform its Index or take defensive positions in declining markets. Due to the investment strategy of this Fund it may make higher capital gain distributions than other ETFs.

**DXJ:** Foreign investing involves special risks, such as risk of loss from currency fluctuation or political or economic uncertainty. The Fund focuses its investments in Japan, thereby increasing the impact of events and developments in Japan that can adversely affect performance. Investments in currency involve additional special risks, such as credit risk, interest rate fluctuations, derivative investments which can be volatile and may be less liquid than other securities, and more sensitive to the effect of varied economic conditions. As this Fund can have a high concentration in some issuers, the Fund can be adversely impacted by changes affecting those issuers. Due to the investment strategy of this Fund it may make higher capital gain distributions than other ETFs. Dividends are not guaranteed, and a company currently paying dividends may cease paying dividends at any time.



# Important Information

**DEM:** Foreign investing involves special risks, such as risk of loss from currency fluctuation or political or economic uncertainty. Funds focusing on a single sector generally experience greater price volatility. Investments in emerging, offshore or frontier markets are generally less liquid and less efficient than investments in developed markets and are subject to additional risks, such as risks of adverse governmental regulation, intervention and political developments. Due to the investment strategy of this Fund it may make higher capital gain distributions than other ETFs.

**EPI:** Foreign investing involves special risks, such as risk of loss from currency fluctuation or political or economic uncertainty. This Fund focuses its investments in India, thereby increasing the impact of events and developments associated with the region which can adversely affect performance. Investments in emerging, offshore or frontier markets such as India are generally less liquid and less efficient than investments in developed markets and are subject to additional risks, such as risks of adverse governmental regulation and intervention or political developments. As this Fund has a high concentration in some sectors, the Fund can be adversely affected by changes in those sectors. Due to the investment strategy of this Fund it may make higher capital gain distributions than other ETFs.

**USFR:** Securities with floating rates can be less sensitive to interest rate changes than securities with fixed interest rates, but may decline in value. The issuance of floating rate notes by the U.S. Treasury is new and the amount of supply will be limited. Fixed income securities will normally decline in value as interest rates rise. The value of an investment in the Fund may change quickly and without warning in response to issuer or counterparty defaults and changes in the credit ratings of the Fund's portfolio investments. Due to the investment strategy of this Fund it may make higher capital gain distributions than other ETFs.

**WFHY:** Fixed income investments are subject to interest rate risk; their value will normally decline as interest rates rise. High-yield or “junk” bonds have lower credit ratings and involve a greater risk to principal. Fixed income investments are also subject to credit risk, the risk that the issuer of a bond will fail to pay interest and principal in a timely manner or that negative perceptions of the issuer's ability to make such payments will cause the price of that bond to decline. While the Fund attempts to limit credit and counterparty exposure, the value of an investment in the Fund may change quickly and without warning in response to issuer or counterparty defaults and changes in the credit ratings of the Fund's portfolio investments.

# Important Information

**AGGY:** Fixed income investments are subject to interest rate risk; their value will normally decline as interest rates rise. Fixed income investments are also subject to credit risk, the risk that the issuer of a bond will fail to pay interest and principal in a timely manner, or that negative perceptions of the issuer's ability to make such payments will cause the price of that bond to decline. Investing in mortgage- and asset-backed securities involves interest rate, credit, valuation, extension and liquidity risks and the risk that payments on the underlying assets are delayed, prepaid, subordinated or defaulted on. Due to the investment strategy of the Fund, it may make higher capital gain distributions than other ETFs.

Please read each Funds' prospectus for specific details regarding the Funds' risk profiles.

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