

How to organise the thematic universe? Introducing the WisdomTree thematic classification

Published 22 April 2021

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Thematic investments promise to harness long-term growth by turning structural, world-changing shifts into potentially compelling investment opportunities. They enable investors to link their vision of the world and its evolution directly to their investment strategies. Historically, equity funds and Exchange Traded Funds (“ETFs”) would end up being classified by the geography in which they invest, the sector in which they specialise, the size of their target companies or the type of stocks they focus on. Quite logically, they would end up in a very well-defined box, like, for example, US Large-cap Value or European Consumer Discretionary. Thematic strategies sit outside of such classification. This is part of what makes thematic investing exciting, as there is a feeling of ‘stepping outside’ from the conventional framework in an attempt to add value. However, this also means that existing classification methods are not relevant for thematic investing, and it is necessary to find new ways to classify and organise those funds. Unfortunately, there is no universally approved classification. This is the gap that the WisdomTree Thematic Classification aims to fill.

Thematic or not Thematic, that is the question

The first step in creating a Thematic classification for investment funds is to define if a fund is indeed thematic. While developing our WisdomTree Thematic Classification, we are using a combination of two definitions to weed out non-thematic funds and focus on the funds that lean into the thematic space:

- A positive definition states that a thematic fund has to deliver a value proposition based on a potential for growth linked directly to one or more Megatrends. The strategy needs to invest proactively in a group of stocks that reflect similar values, beliefs, or objectives. The connection to that ‘big story’ must be there.
- A negative definition states that any fund that ends up easily in one of the “classic” boxes, such as sector, country or small-cap, is not thematic. It is worth mentioning that adding an environmental, social and governance (ESG) screen to a non-thematic fund (like a sector fund) would not make it thematic. In our judgement, the focus of the strategy would remain the same with or without the ESG screen.

Introducing the WisdomTree Thematic Classification: 4 Clusters, 35 Themes

The second steps in creating the WisdomTree Thematic Classification is to list and organise the different investment Themes. Academics, consultants, international organisations (like the World Economic Forum),

or think-tanks have all been publishing lists or scans of megatrends that are impacting or will impact the world in the long term. While those lists all differ from one another, they still share some commonality. Collating a range of those reports, we have highlighted four areas of consensus, leading to the creation of four thematic Clusters:

- **Technological Shifts:** This Cluster focuses on the different Themes that originate from the introduction of new technologies and innovation. It incorporates disruptive and emerging technologies as well as their impact on societies and economies, such as the increasing digitalisation and connectivity of the world.
- **Demographic and Social Shifts:** This Cluster focuses on the different Themes that originate from changes in population and societies alike. It incorporates, for example, changes in the world's pyramid of age, the impact of the growing, younger, wealthier populations in emerging markets, as well as changes to societal values and lifestyles.
- **Environmental Pressures:** This Cluster focuses on the environment and, more importantly, on the impact of human activities on the planet. It incorporates changes driven by sustainability issues, the increasing scarcity of resources and the need to address Global Warming and Climate Change.
- **Geopolitical Shifts:** This Cluster focuses on the Themes driven by the globalisation and the changes in the global geopolitical order with the rise of new geopolitical powers like China. It also taps into the increasing polarisation of modern societies as a counterforce to globalisation.

Within the classification, all thematic ETFs and Open-ended funds can be organised into a coherent universe. They can be classified into:

- Diversified Thematics, if they try to harness a large number of Megatrends in one go. Those funds tend to have a very diluted focus, which could mean that it might be harder to find sources of potential differentiation against a broad market benchmark.
- A specific Cluster, if they try to harness multiple Themes across Sub-Clusters but within one particular Cluster. For example, a fund investing in Artificial Intelligence, Robotics, Cloud, and Cybersecurity would be classified as a 'Technological Shifts' fund.
- A particular Sub-Cluster, if a strategy aims to invest in most of the Themes within that Sub-Cluster. For example, a fund investing in Cloud Computing, Platforms, Cybersecurity, and Fintech would be classified as a 'Hyperconnectivity & Digitalisation' fund.
- A Theme, if the investment strategy is focused on a specific, clear Theme.

Figure 1: The WisdomTree Thematic Classification

Diversified Thematics							
DEMOGRAPHIC AND SOCIAL SHIFTS		TECHNOLOGICAL SHIFTS		GEOPOLITICAL SHIFTS		ENVIRONMENTAL PRESSURES	
Demographic Shifts	Social Shifts	Disruptive Technologies	Hyper Connectivity & Digitalisation	Globalisation	Multi-polarity	Climate Change & Sustainability	Limited Resources
Millennials	Equality, Inclusion & Diversity	Artificial Intelligence	Cloud Computing	Global Logistics	China's Rise	Decarbonisation	Agriculture
Aging Population	Rise of the Middle Class	Robotics & Automation	Cybersecurity		Polarisation	Sustainable Mobility	Natural Resources
	Rise of EM Consumer	Health Tech	Digital Infrastructure		Rise of Tension	Sustainable Energy Production	
	Wellness	Industry 4.0	Platforms & Digital Markets			Sustainable Energy Storage	
		Next Gen Communications	Internet of Things			Sustainable Food	
		Blockchain	Social Media & Media			Sustainable Cities	
		Nano Tech	Gaming & Entertainment			Sustainable Resource Mgt	
		Space	Fintech & Digitalisation of Finance				

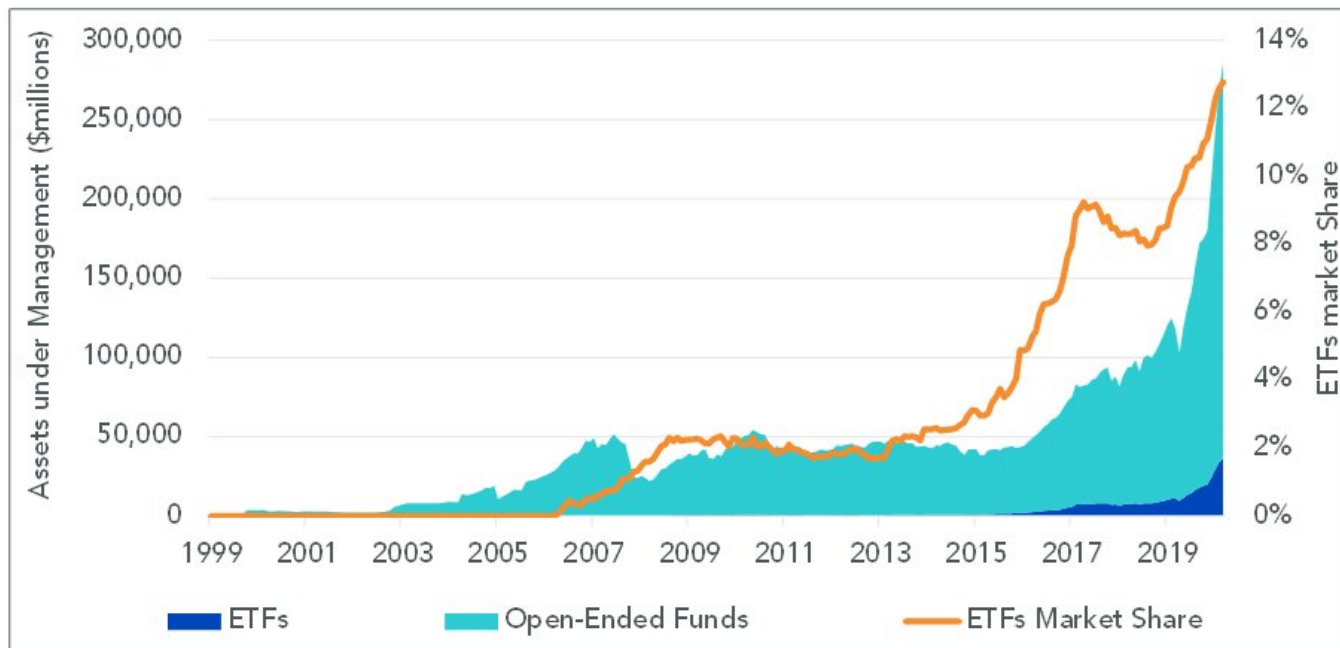
Source: WisdomTree, Morningstar, Bloomberg. As of 31st March 2021.

When populated with all Thematic Exchange Traded Funds globally and Europe-domiciled Thematic open-ended Funds (more than 1000 investment products live and terminated as of our last count¹), the WisdomTree Thematic Classification allows us to make better sense of the thematic space by bringing structure to it.

Thematic ETFs - late entrants with exponential growth

One example of using the classification is to look at the assets under management (AUM)'s evolution in the thematic space. In upcoming blogs and publications, we will show many more examples. In Europe, active managers used to be the only players in the thematic space, while ETF providers used to focus on market access and classic beta exposures. However, with ETFs growing in Europe, this has changed dramatically. Index construction has evolved, and an index can now comprise a mixture of many different stock selection and weighting parameters. It can be far more specific than what was previously accepted. With these changes, the number of thematic ETFs started to pick up around 2015, and AuM started to move. ETFs went from representing 3%² of the European thematic AuM with only 1.1bn² under management five years ago to 12.8% and \$36.4 bn on 28th February 2021² as illustrated in Figure 2.

Figure 2: Assets under management in Europe-domiciled thematic funds by wrappers since 2000.



1As of February 2021

2 WisdomTree, Morningstar, Bloomberg. From February 2016 to February 2021. In US Dollars.

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