

# A Look at the Performance Behind Our Suite of Dynamically Hedged ETFs

Published July 25, 2024

**Liqian Ren**

Director of Modern Alpha

## Key Takeaways

- Dynamic currency hedging has effectively reduced international portfolio risk and added value to non-hedged equity portfolios, especially during periods of U.S. dollar strength.
- Since 2016, the [WisdomTree Dynamic Currency Hedged International Equity Fund \(DDWM\)](#) has outperformed a 50% hedged portfolio with an annual performance of 8.3% and a risk of 12.7%, adding 2% annually over the [WisdomTree International Equity Fund \(DWM\)](#).
- Our dynamic hedging strategy, which includes five components, has seen adjustments in hedge ratios influenced by momentum components, with all components adding value since 2023, and recent monthly rebalancing decreased the developed market hedge to about 20%.

At WisdomTree, we offer numerous suites of Funds. In this blog post, I will focus on two particular suites: one that is dynamically hedged and another that is not hedged.

- **In large caps:** [WisdomTree Dynamic Currency Hedged International Equity Fund \(DDWM\)](#) vs. [WisdomTree International Equity Fund \(DWM\)](#).
- **In small caps:** [WisdomTree Dynamic Currency Hedged International SmallCap Equity Fund \(DDLX\)](#) vs. [WisdomTree International SmallCap Equity Fund \(DLS\)](#).

The only difference between the Funds in each pair is the dynamic currency hedge, allowing for an easy evaluation of the net impact of currency hedging.

Dynamic currency hedging has reduced international portfolio risk while adding value on non-hedged equity portfolios.

Since 2016, [DDLX](#) has added 2% annually over [DLS](#), as it benefited from adapting its hedge during a stronger dollar period for much of the last few years.

Because the U.S. dollar has been strong, it has been difficult to beat a 100% hedged portfolio. However, dynamically hedged [DDLX](#), with a performance of 8.3% and risk of 12.7% since 2016, has been able to beat a 50% hedged portfolio.

The [current dynamic hedging strategy](#) has five components, with a broad market currency trend indicator accounting for 50% of the weight and the other four components (carry, cross asset, low vol and momentum) equal weighted across the remaining 50%.

Since 2023, every component has added some value, with carry and low volatility signals adding the most.

In July, we rebalanced both our developed and emerging markets currency models. Specifically, the hedge for the developed market decreased to about 20%. This change was primarily influenced by the two momentum components of the strategy: the broad trend and cross-sectional momentum, which together account for 62.5% of the weight. As previously mentioned, the increased momentum weight in the new developed market strategy since 2023 has led to more frequent adjustments in hedge ratios.

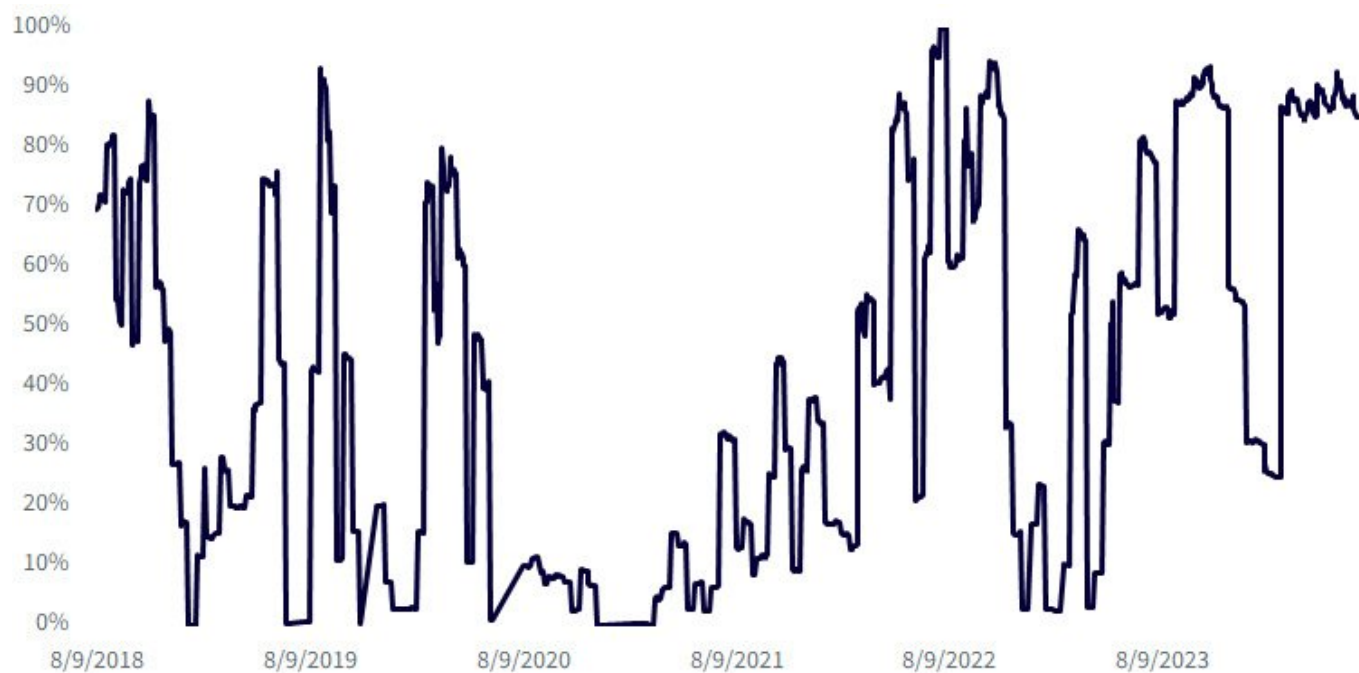
## Figure 1: Historical Dynamic Hedge Ratio in Developed Market



Sources: WisdomTree, FactSet, Refinitiv 1/06/16-7/10/24. Past performance is not indicative of future results.

In July, the currency strategy for the [WisdomTree Emerging Markets Multifactor Fund \(EMMF\)](#) remains similar to June. We are closely monitoring whether the strategy's signal regarding the potential weakening of the dollar is limited to developed markets.

## Figure 2: Historical Dynamic Hedge Ratio in Emerging Markets



Sources: WisdomTree, FactSet, Refinitiv 8/9/18–7/10/24. Past performance is not indicative of future results.

In summary, we maintain our belief that a factor-based dynamic currency strategy can mitigate volatility in international portfolios while potentially enhancing long-term performance.

## Important Risks Related to this Article

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

Foreign investing involves special risks, such as risk of loss from currency fluctuation or political or economic uncertainty. Funds focusing their investments on certain sectors and/or smaller companies increase their vulnerability to any single economic or regulatory development, which may result in greater share price volatility. Investments in derivatives to obtain a dynamic currency hedge exposure can be volatile, less liquid than other securities, and more sensitive to varied economic conditions, and may not perform as intended. Dividends are not guaranteed, and a company currently paying dividends may cease at any time. The composition of the Index underlying the Fund is heavily dependent on quantitative models and data from third parties, which may not perform as intended. Funds that invest in securities included in, or representative of, an Index do not attempt to outperform the Index or take defensive positions in declining markets. Investing involves risk, including possible loss of principal. Investments in non-U.S. securities involve additional political, regulatory and economic risks.

Specific additional risks for EMMF include emerging markets risk, which involves risks relating to political, economic or regulatory conditions not associated with U.S. securities or more developed international markets. The Fund's investment process is heavily dependent on quantitative models that may not perform as intended. Please read the Fund's prospectus for specific details regarding the Fund's risk profile.