

A Multifactor Solution for a Top-Heavy Market

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The dilemma of market concentration is front of mind for asset allocators.

At no point in the last 30 years has the S&P 500 Index been so concentrated in just a handful of names.

The top 10 holdings account for almost 34% of the index's weight, roughly double the weight of the top 10 holdings a decade ago.

S&P 500 Index Weight in Top 10 Holdings



Sources: WisdomTree, S&P, 1/31/1990–2/12/2024. You cannot invest directly in an index.

The growing dominance of a few richly valued companies has elevated S&P 500 valuations—lowering future return forecasts—and reduced the diversification benefits of index-based investing.

The current 21 times forward P/E on the index is well above the historical median valuation of 17 times.

S&P 500 Forward Price-to-Earnings Ratio



Sources: WisdomTree, FactSet, S&P, 12/30/1994–2/12/2024. You cannot invest directly in an index.

For potential solutions for market concentration and elevated valuations, some tend to look to include single factor strategies like small caps or value.

A multifactor approach, on the other hand, can offer a diversified portfolio without having to make a bet on any single factor.

Over the last several years, being factor diversified—as shown with the performance of the multifactor below—has navigated the extremes of performance from single factor indexes.

Factor Index Calendar Year Performance

2018	2019	2020	2021	2022	2023	2024 YTD	Annualized Full Period
1.5% Min Vol	34.4% Quality	29.6% Momentum	29.2% Value	-8.5% Multifactor	31.1% Quality	13.1% Momentum	12.9% Quality
-1.6% Momentum	28.1% Momentum	20.0% Small Caps	27.2% Quality	-9.2% Min Vol	16.9% Small Caps	6.7% Quality	10.9% Momentum
-4.1% Multifactor	28.0% Min Vol	17.1% Quality	21.5% Multifactor	-14.0% Value	14.4% Value	4.7% Multifactor	9.6% Multifactor
-5.6% Quality	27.7% Value	11.9% Multifactor	21.0% Min Vol	-17.4% Momentum	13.3% Multifactor	3.2% Min Vol	9.2% Min Vol
-11.0% Small Caps	25.5% Small Caps	5.8% Min Vol	14.8% Small Caps	-20.3% Quality	9.8% Min Vol	0.4% Value	6.2% Value
-11.1% Value	24.4% Multifactor	-0.2% Value	12.9% Momentum	-20.4% Small Caps	9.5% Momentum	0.4% Small Caps	6.1% Small Caps

Sources: WisdomTree, Russell, MSCI, 12/29/17–2/16/24. Time period start date chosen based on first full year of calendar performance for the WisdomTree U.S. Multifactor Index. Min Vol = MSCI USA Minimum Volatility Index. Momentum = MSCI USA Momentum Index. Multifactor = WisdomTree U.S. Multifactor Index. Quality = MSCI USA Sector Neutral Quality Index. Small Caps = Russell 2000 Index. Value = MSCI USA Enhanced Value Index. You cannot invest directly in an index. Past performance is not indicative of future returns.

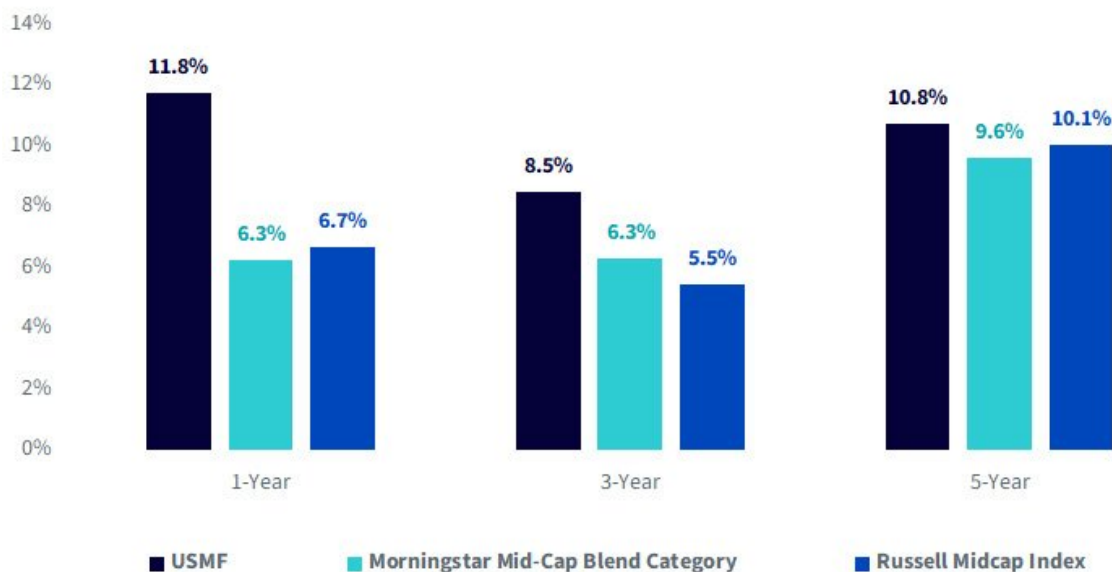
U.S. Multifactor: A Diversified Factor Approach

The [WisdomTree U.S. Multifactor Fund \(USMF\)](#) invests in mid- and large-cap U.S. equities in a fashion that closely resembles equal weighting. [USMF](#) selects 200 securities that have a high combined multifactor score on several widely accepted factors: value, quality, momentum and low correlation.

This multifactor score is used as part of the weighting mechanism, which is complemented by a low-volatility score that gives greater weight to less volatile stocks.

[USMF's](#) modified equal-weighting approach results in a tilt to mid-cap securities. As a result, the Fund is included in Morningstar's Mid-Cap Blend Category where it is rated 5 Stars relative to its category peers.¹

USMF: Morningstar 5-Star Rated



Sources: WisdomTree, Russell, Morningstar, as of 1/31/24. The WisdomTree U.S. Multifactor Fund (USMF) was launched on 6/29/17. Number of investments in Morningstar Mid-Cap Blend Category: 1-Year = 418, 3-year = 382, 5-year = 359. Fund returns measured at NAV. Index returns are total return. Returns greater than 1-year are annualized. You cannot invest directly in an index.

Past performance is not indicative of future results. Investment return and principal value of an investment will fluctuate so that an investor's shares, when redeemed, may be worth more or less than their original cost. Current performance may be lower or higher than the performance data quoted.

For the most recent month-end and standardized performances and to download the Fund prospectus, click [here](#).

Value AND Quality without Sacrificing Momentum

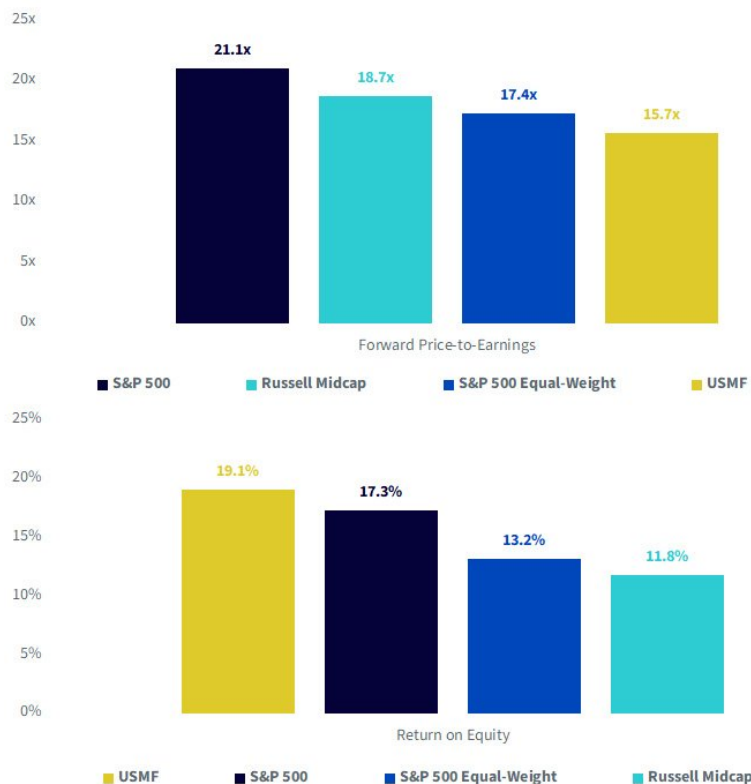
The S&P 500 Equal Weight Index, which gives the same weight to each of the 500 companies in the index, mitigates some of the valuation risk we saw with the S&P 500. Its P/E of 17.4 times is considerably lower than the 21.1 times of the S&P 500.

The S&P 500 Equal Weight also has some drawbacks. One of them is that it has lower profitability than the S&P 500, as measured by return on equity (ROE).

The diversified factor approach of **USMF** helps solve for this trade-off:

- **USMF** also has cheaper valuations than the S&P 500. Its P/E ratio is 15.7 times, which is lower than the 21.1 times of the S&P 500
- **USMF** has higher profitability than the S&P 500. Its ROE is 19.1%, which is higher than the 17.3% of the S&P 500

Fundamental Characteristics



Sources: WisdomTree, FactSet, S&P, Russell, as of 1/31/24. You cannot invest directly in an index.

USMF also has positive exposure to the momentum factor, which looks for stocks that have strong recent performance.

The below bar chart helps illustrate the exposure to the momentum factor. The chart shows the percentage of weight in each of three categories: positive, neutral and negative.

USMF has 49% of its weight in the positive category, which is much higher than the 33% of the S&P 500 and the 23% of the S&P 500 Equal Weight. This means that **USMF** has more exposure to companies with positive trends in momentum.

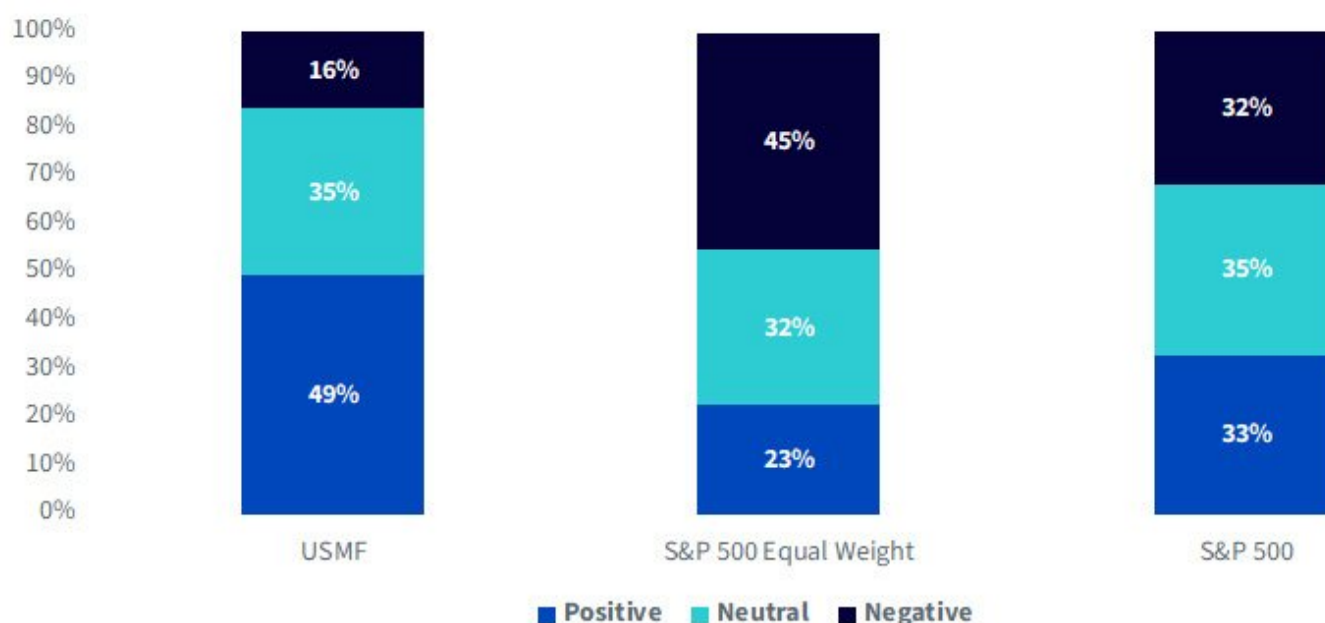
The S&P 500 Equal Weight has a distinct negative momentum tilt. The index has 45% of its weight in the negative category, which is much higher than the 32% of the S&P 500 and the 16% of **USMF**.

The S&P 500 Equal Weight rebalances weights each quarter, which means selling outperformers and buying laggards in a systematic anti-momentum process.

USMF also rebalances every quarter using a rules-based, factor-diversified buy/sell discipline. This approach allows **USMF** to avoid selling winners too soon.

In summary, **USMF** is a diversified factor approach that offers a balanced exposure to academically researched factors that produces a diversified basket of 200 stocks with lower valuations, higher profitability and positive momentum exposure.

Momentum Factor Exposure



Sources: WisdomTree, S&P, as of 1/31/24. You cannot invest directly in an index. Holdings subject to change. Momentum factor measured by trailing 6- and 12-month risk-adjusted returns. "Positive": Represents the highest-ranked one-third of the total market cap. "Neutral": Represents the next ranked one-third of the total market cap. "Negative": Represents the lowest ranked one-third.

1 Category: Mid-Cap Blend. Overall rank based on 382 funds in category, 3-year percentile rank based on 382 funds in category, 5-year percentile rank based on 359 funds in category, as of 1/31/24.

The Morningstar Rating™ for funds, or "star rating," is calculated for managed products with at least a three-year history. Exchange-traded funds and open-ended mutual funds are considered a single population for comparative purposes. It is calculated based on a Morningstar Risk-Adjusted Return measure that accounts for variation in a managed product's monthly excess performance, placing more emphasis on downward variations and rewarding consistent performance.

The top 10% of products in each product category receive five stars, the next 22.5% receive four stars, the next 35% receive three stars, the next 22.5% receive two stars and the bottom 10% receive one star. The Overall Morningstar Rating for a managed product is derived from a weighted average of the performance figures associated with its three- and five-year Morningstar Rating metrics. The weights are: 100% 3-year rating for 36–59 months of total returns, 60% 5-year rating/40% 3-year rating for 60–119 months of total returns.

Important Risks Related to this Article

There are risks associated with investing, including the possible loss of principal. Investing in a Fund exposed to particular sectors increases the vulnerability to any single economic, political or regulatory development. This may result in greater share price volatility. Due to the investment strategy of the Fund, it may make higher capital gain distributions than other ETFs. Please read the Fund's prospectus for specific details regarding the Fund's risk profile.

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