High Dividends: Shortening Equity Duration

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The Fed may not be pulling away the punch bowl just yet, but it's also not adding more juice to it.

At the conclusion of last week's FOMC meeting, Fed Chair Powell announced that the committee anticipates three rate hikes in 2022.

Indications that the Fed will more seriously act to combat rampant inflation has led the policy-sensitive 2-Year yield to spike higher.

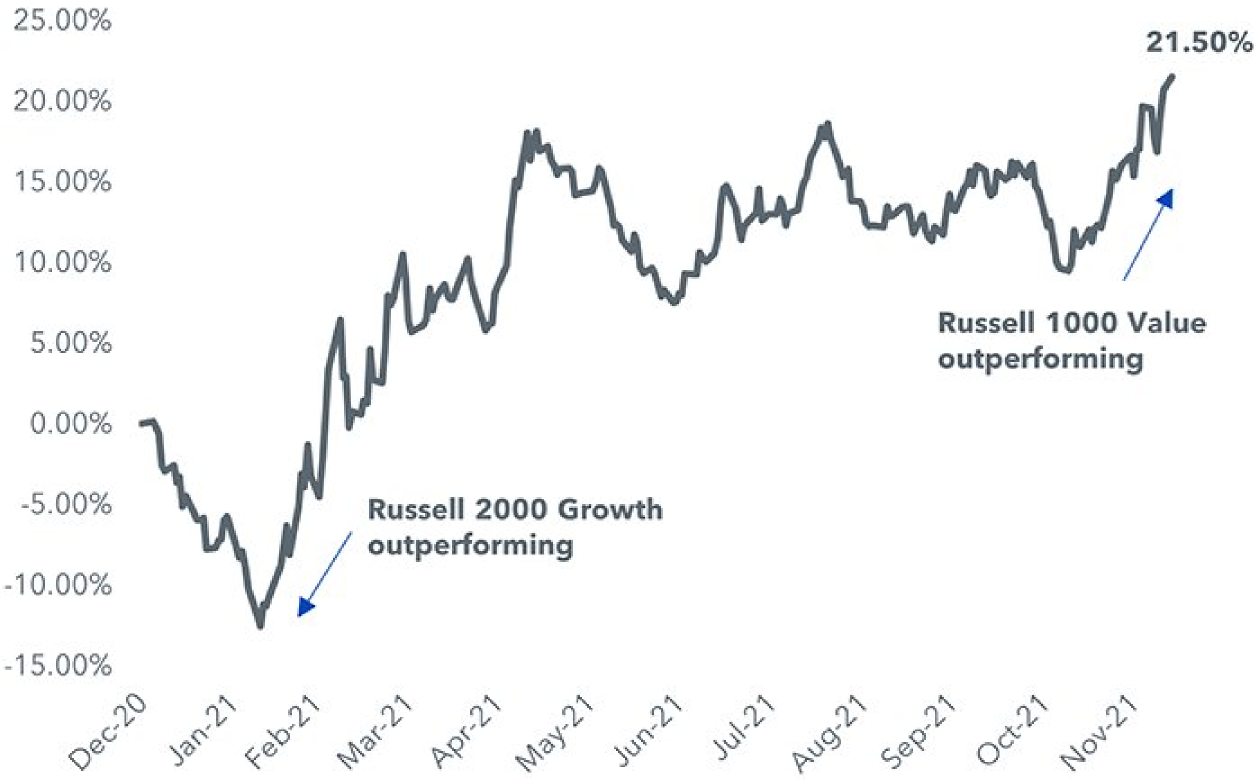
2-Year U.S. Treasury Yield

Sources: WisdomTree, Barclays, 12/31/20–12/10/21 .

Higher rates have caused unprofitable, high-growth companies to fall into a tailspin as far-out cash flows get discounted at higher rates.

This trend can be seen in the significant outperformance of the Russell 1000 Value Index relative to the Russell 2000 Growth Index over the past several weeks.

Russell 1000 Value vs. Russell 2000 Growth



Sources: WisdomTree, Russell, 12/31/20–12/10/21. You cannot invest directly in an index. Past performance is not indicative of future returns.

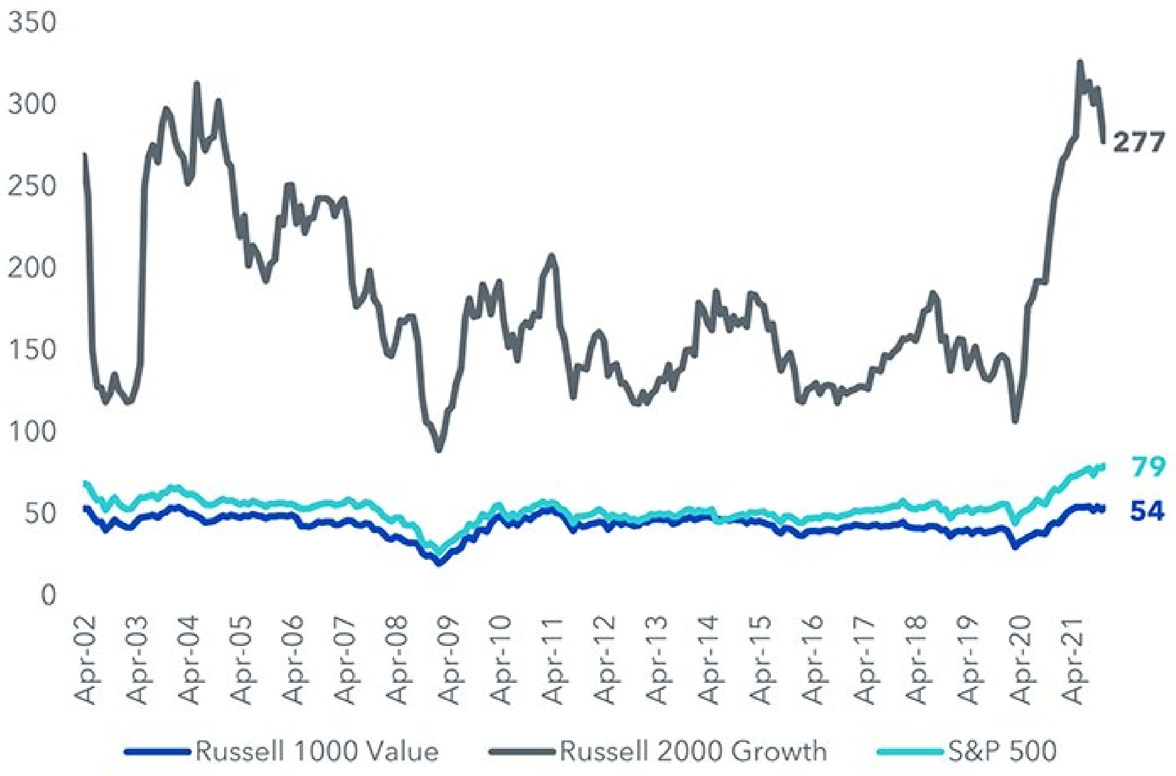
The interest rate sensitivity, or duration, of equities can be measured by the inverse of the dividend yield of an index (1/dividend yield), or the number of years of dividends it would take to recover the current price.

An index with a higher duration (low-dividend yield) may be more ***negatively impacted*** by a move higher in rates. Conversely, a company with a lower duration (high-dividend yield) may be more ***positively impacted*** by a move higher in rates.

Since March 2020, the rate sensitivity of high-growth stocks has substantially increased. The equity duration of the Russell 2000 Growth Index has skyrocketed from 107 years to more than 300.

The duration of value stocks has also increased but at a more subdued rate.

Equity Duration (Years)



Sources: WisdomTree, Russell, S&P, 4/30/02–11/30/21. Equity duration = 1/dividend yield. You cannot invest directly in an Index. Past performance is not indicative of future returns.

High Dividends Can Lower Rate Risk

On December 14, the WisdomTree U.S. High Dividend Index executed its annual rebalance. It had a modest impact on the characteristics of the Index.

The Index has a dividend yield greater than 4%—well over twice that of the Russell 1000 Value Index. That equates to a duration of 25 versus the duration of 54 for the Russell 1000 Value.

And the Index also has higher profitability metrics (ROE/ROA) than the Russell 1000 Value Index.

Fundamentals

Characteristics	Pre-Rebalance	Post-Rebalance	Russell 1000 Value	S&P 500
Size				
Weighted Average Market Cap ($bn)	$109.98	$117.26	$140.37	$617.52
Median Market Cap ($bn)	$2.96	$4.09	$12.70	$31.98
Over $10 billion	86.46%	89.30%	92.29%	99.26%
$2 billion - $10 billion	10.90%	8.54%	7.69%	0.74%
Under $2 billion	2.64%	2.16%	0.02%	0.00%
Valuation & Other Characteristics				
Price/Earnings (Trailing)	14.25	14.36	18.65	24.92
Price/Earnings (Forward)	12.11	12.17	15.83	21.23
Price/Book	2.62	2.51	2.64	4.87
Price/Sales	2.04	1.87	1.95	3.07
Dividend Yield	4.21%	4.07%	1.92%	1.28%
Return on Equity	15.87%	15.21%	13.37%	18.16%
Return on Assets	2.92%	3.05%	2.68%	3.95%
Number of Holdings	313	387	849	505

Sources: WisdomTree, Russell, FactSet, as of 11/30/21. The Index rebalance took place after the close on December 14, 2021. You cannot invest directly in an index.

From a sector perspective, the Index added heavily to Energy (+14) and Health Care (+4%) while trimming from Info Tech (-10%) and Comm Services (-4%).

Sector Weights

Sector	Pre-Rebalance	Post-Rebalance	Russell 1000 Value
Health Care	14.21%	18.49%	17.52%
Consumer Staples	18.90%	17.51%	7.10%
Financials	17.67%	16.60%	21.46%
Energy	1.00%	15.03%	5.23%
Utilities	13.03%	12.53%	4.95%
Communication Services	9.37%	5.00%	7.42%
Real Estate	5.76%	5.00%	4.95%
Information Technology	13.22%	3.40%	10.16%
Industrials	3.52%	3.01%	11.66%
Materials	2.23%	2.34%	3.79%
Consumer Discretionary	1.08%	1.09%	5.76%

Sources: WisdomTree, Russell, FactSet, as of 11/30/21. The Index rebalance took place after the close on December 14, 2021. You cannot invest directly in an index.

The oil majors Exxon and Chevron were added back to the Index after being removed at last year's rebalance based on a proprietary screen of dividend riskiness. Combined, these two holdings make up nearly 10% of the 14% addition to the Energy sector.

Broadcom, a steady dividend payer/grower, was removed, as its more than 40% return since last year's rebalance dropped its dividend yield from 3.24% to 2.55%, removing it from the high-dividend-yield universe.

AT&T (8.71% yield), IBM (5.34% yield) and Lumen Technologies (7.72% yield) were all screened out of the Index based on the Index risk screen. Dropping these names contributed to modestly lowering the overall Index yield from 4.21% to 4.07%, as the Index aims to hold more sustainable dividend payers as opposed to merely the highest yielders.

Top Adds/Drops

Top 5 Additions		
Name	Weight	Sector
Exxon Mobil	5.39%	Energy
Chevron	4.26%	Energy
Merck	2.88%	Health Care
Morgan Stanley	2.07%	Financials
Bristol-Myers Squibb	1.80%	Health Care

Top 5 Drops		
Name	Weight	Sector
Broadcom Inc.	4.08%	Information Technology
AT&T Inc.	3.66%	Communication Services
IBM	3.11%	Information Technology
Lumen Technologies	0.76%	Communication Services
Public Storage	0.65%	Real Estate

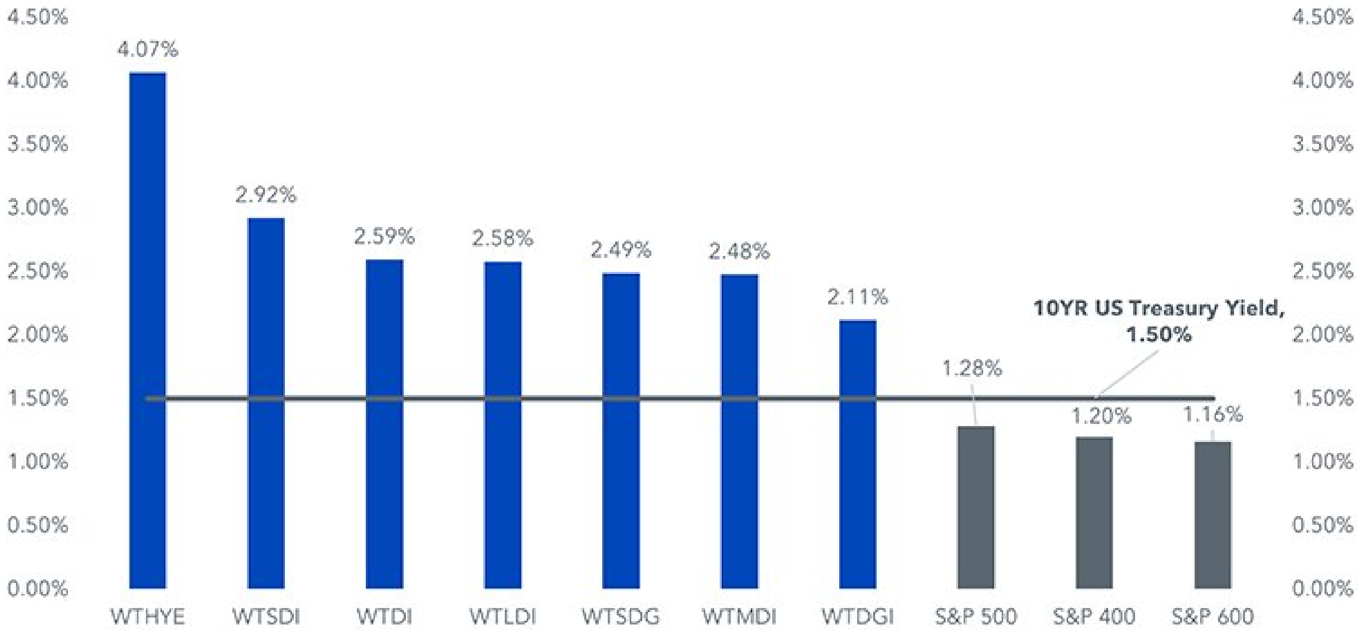
Sources: WisdomTree, Russell, FactSet. The Index rebalance took place after the close on December 14, 2021. You cannot invest directly in an Index.

WisdomTree has a family of dividend-weighted Indexes, several of which have more than 15 years of live track record.

Style	WisdomTree Index	Index Ticker	Index Inception Date	Related WisdomTree ETF
Broad Dividends	U.S. Dividend	WTDI	6/1/2006	U.S. Dividend (DTD)
	U.S. LargeCap Dividend	WTLDI	6/1/2006	U.S. LargeCap Dividend (DLN)
	U.S. MidCap Dividend	WTMDI	6/1/2006	U.S. MidCap Dividend (DON)
	U.S. SmallCap Dividend	WTSDI	6/1/2006	U.S. SmallCap Dividend (DES)
Quality Dividends	U.S. Quality Dividend Growth	WTDGI	4/12/2013	U.S. Quality Dividend Growth (DGRW)
	U.S. SmallCap Quality Dividend Growth	WTSDG	4/12/2013	U.S. SmallCap Quality Dividend Growth (DGRS)
High Dividends	U.S. High Dividend	WTHYE	6/1/2006	U.S. High Dividend (DHS)

A Fed hiking cycle is likely to favor value as shorter-duration/high yielders become more attractive with increases in short-term rates. Among WisdomTree's family of domestic dividend Indexes, the WisdomTree

U.S. High Dividend Index fits the bill as having the greatest value/income tilt with a yield advantage of nearly 280 basis points (bps) relative to the S&P 500.



Sources: WisdomTree, FactSet. Data as of 11/30/21 using post-rebalance Index weights for WisdomTree Indexes. You cannot invest directly in an Index. WTDI = WisdomTree U.S. Dividend Index; WTLDI = WisdomTree U.S. LargeCap Dividend Index; WTMDI = WisdomTree U.S. MidCap Dividend Index; WTSDI = WisdomTree U.S. SmallCap Dividend Index; WTDGI = WisdomTree U.S. Quality Dividend Growth Index; WTSDG = WisdomTree U.S. SmallCap Quality Dividend Growth Index; WTHYE = WisdomTree U.S. High Dividend Index.

Important Risks Related to this Article

Investing involves risk, including loss of principal. Dividend-focused funds may underperform funds that do not limit their investment to dividend-paying stocks. Stocks held by funds may reduce or stop paying dividends, affecting the fund's ability to generate income. Performance may also be affected by risks associated with non-diversification, including investments in specific countries or sectors. Each individual investor should consider these risks carefully before investing in a particular sector or strategy.