Volatility Is as Volatility Does

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This article is relevant to financial professionals who are considering offering model portfolios to their clients. If you are an individual investor interested in WisdomTree ETF Model Portfolios, please inquire with your financial professional. Not all financial professionals have access to these model portfolios.

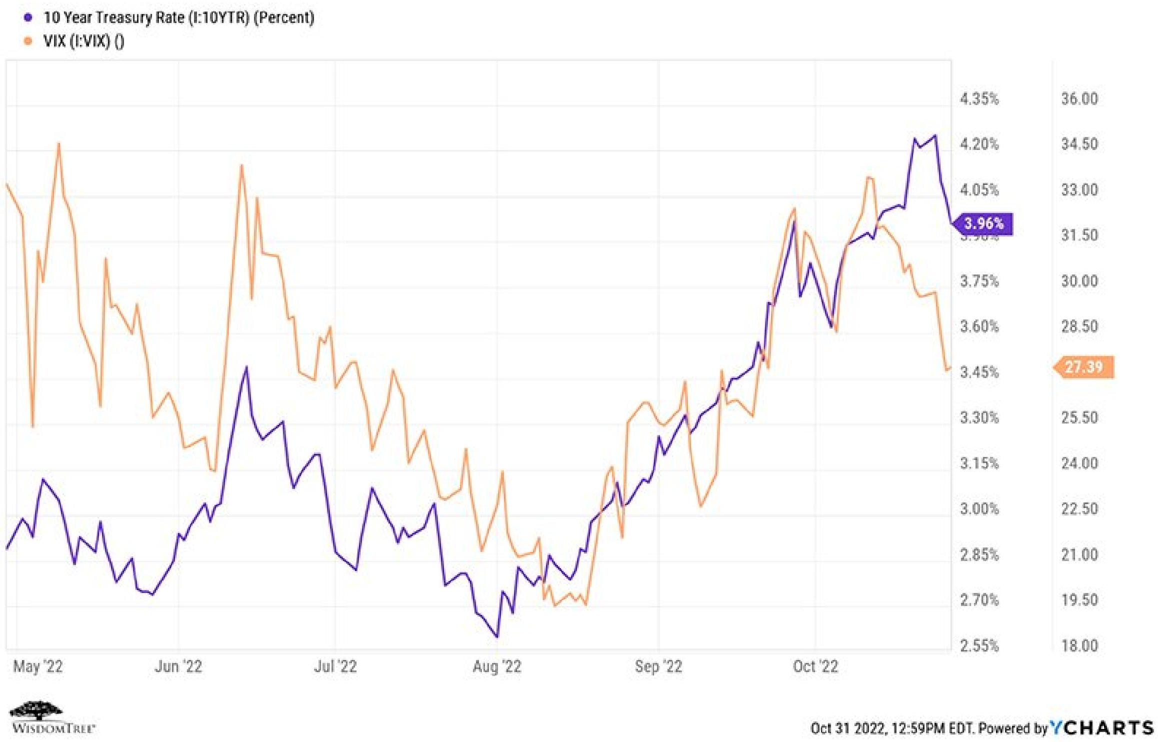
Well, this has been an interesting year, hasn't it? Many investors have not had the "opportunity" to experience a year like this in their professional lives unless they were around for 2000–2001 or 2008–2009. (I'm not counting the COVID-19-induced meltdown in early 2020, which was, to use an increasingly unpopular word these days, "transitory.") Until about a year ago, it was a roughly 10-year market environment of equity bull markets, expanding multiples, low interest rates and low volatility.

But here we are, in a quite different environment—equities and bonds both have fallen, rates are rising, multiples are contracting and volatility is increasing. Most upsetting to many investors is the failure of bonds to provide their historical hedge to equity market risk.

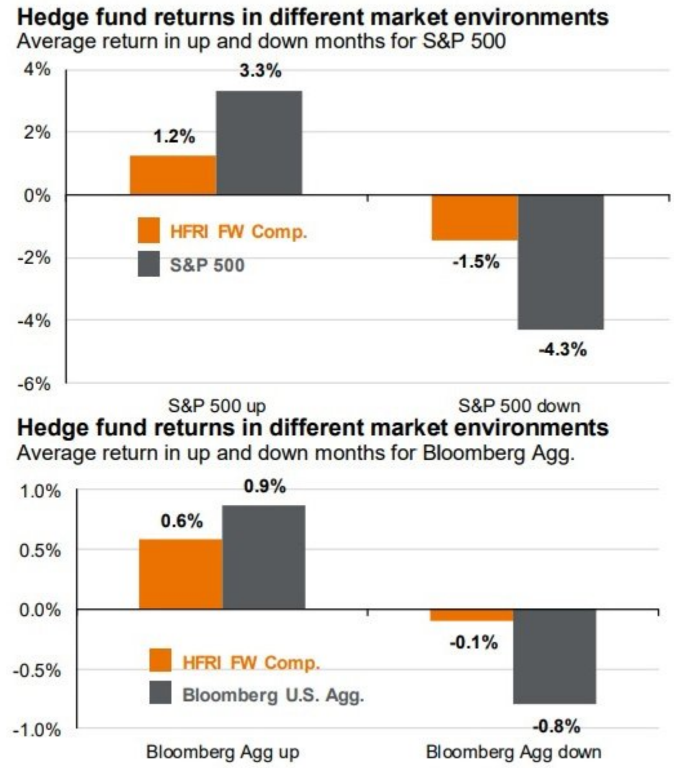
Source: YCharts, 12-month data through October 28, 2022. You cannot invest in an index, and past performance does not guarantee future results.

We are receiving an increasing number of inbound calls from advisors asking us, “What else can I put in my portfolio besides stocks or bonds?” The good news is that we have an answer—our **Volatility Management** model.

Before diving into the details of the model, let’s remind ourselves of some important historical phenomena—alternative or nontraditional asset strategies tend to work best in rising interest rate and rising market volatility environments, which we certainly would argue represent the current market environment.

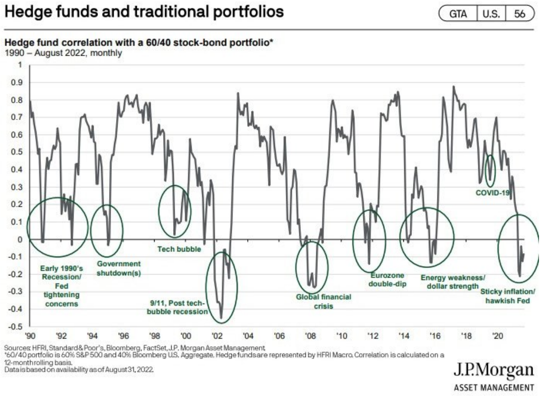


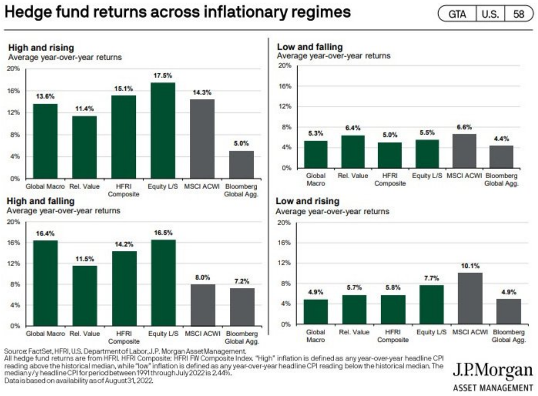
Source: YCharts, six-month data as of October 28, 2022. You cannot invest in an index. The Chicago Board of Exchange (CBOE) Volatility Index, or “VIX,” is a calculation designed to produce a measure of constant 30-day expected volatility of the U.S. stock market, derived from real-time, mid-quote prices of S&P 500 Index call and put options. On a global basis, it is one of the most recognized measures of volatility—widely reported by financial media and closely followed by a variety of market participants as a daily market indicator.



Source: JP Morgan "Guide to the Markets," as of September 30, 2022. You cannot invest in an index, and past performance does not guarantee future results.

These strategies have additional potential benefits: (1) their correlations to traditional stocks and bonds tend to go down in times of recession, and (2) they tend to perform best in higher inflationary regimes. Again, we think both characteristics are in place in the current market environment.





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The WisdomTree Volatility Management Model

With this as background, let's review our Volatility Management ("Vol Man") model.

As with all WisdomTree models, it has certain fundamental characteristics:

1. It is ETF-centric to potentially optimize fees and taxes.

2. It is "open architecture" and contains both WisdomTree and third-party strategies.

3. There is no strategist fee associated with the model—our revenue is generated only from the expense ratios of the WisdomTree strategies contained within the model.

We currently have equal 20% allocations across five different strategies:

1. **Managed Futures**, via our own WTMF. We believe all nontraditional or alternative portfolios should start with managed futures, which traditionally have shown almost zero correlation to traditional stocks and bonds, and so may serve as an excellent "anchor position" if the purpose of the portfolio is to improve portfolio diversification and/or add different sources of potential return.

2. **"Hedged Equity/Volatility Premium,"** via our own put write strategy, PUTW. By selling equity put options, this strategy generates option premiums used to buffer downside market movement. Since higher levels of premium are generated when equity market volatility is high, this strategy helps to buffer returns of traditional long-only strategies (i.e., the premiums collected help offset negative moves in the market).

3. **Diversified Arbitrage**, via a third-party mutual fund (the only mutual fund included in any of our publicly available models). These types of strategies attempt to capture market inefficiencies associated with things like corporate mergers, convertibles and other "event-driven" corporate activities. Like managed futures, arbitrage strategies have historically tended to have low correlations to traditional stocks and bonds.

4. **Equity Long/Short**, via a third-party ETF. While these strategies tend to be long the market, their ability to execute short positions may provide mitigation to downside market movement.

5. **Short Biased or "Anti-Beta,"** via a third-party ETF. As the name suggests, these types of strategies are consistently short the market and seek to capitalize on downward market movements. As you might imagine, this strategy is the best-performing allocation within the portfolio so far in 2022.

This collection of strategies has historically tended to not only have a low correlation between the strategies themselves but, more importantly, has had a low correlation to traditional stocks and bonds. It has provided increased portfolio diversification and, therefore, offered a more consistent overall portfolio performance during bearish or volatile market regimes.

This portfolio has performed exactly as expected throughout turbulent 2022, providing a nice buffer against the dramatic decline in both stocks and bonds throughout the year while at the same time kicking off a very respectable portfolio yield. And, at 74 basis points (0.74%), we believe it is very competitively priced versus other solutions available.

WisdomTree Volatility Management Portfolio

1.25%	0.74%	08/08/2017	80% | 20%
Model 12-Month Dividend Yield (As of 10/31/2022)	Model Expense Ratio	Inception date	Alternative | Equity

Model Performance | Model Allocations | Model Exposures | Fund Performance | Fund Details

As of 10/31/2022	Cumulative Returns			Average Annual Total Returns				
Name	1-Month	3-Month	YTD	1-Year	3-Year	5-Year	10-Year	Since Inception
WisdomTree Volatility Management Portfolio (NAV)	2.31%	-1.17%	-2.18%	-0.81%	1.90%	0.82%	-	1.04%
WisdomTree Volatility Management Portfolio (MP)	2.37%	-0.89%	-2.25%	-0.83%	1.82%	0.77%	-	1.00%
FTSE 3 Month Treasury Bill Index	0.25%	0.59%	0.87%	0.88%	0.60%	1.16%	-	1.14%

Source: WisdomTree Model Adoption Center, as of 11/17/22. **Performance is historical and does not guarantee future results. Current performance may be lower or higher than quoted. Investment returns and the 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.**

The Model Portfolio performance results shown are theoretical and do not reflect any investor's actual experience with owning, trading or managing an actual investment. Thus, the performance shown does not reflect the impact that economic and market factors had or might have had on decision-making if actual investor money had been managed and allocated per the Model Portfolio. The actual performance achieved in seeking to follow the Model Portfolio may differ from the theoretical performance shown for a number of reasons, including the timing of implementation of trades (including rebalancing trades to adjust to Model Portfolio changes), market conditions, fees and expenses (e.g., brokerage commissions, deduction of advisory or other fees or expenses charged by advisors or other third parties to investors, strategist fees and/or platform fees), contributions, withdrawals, account restrictions, tax consequences and/or other factors, any or all of which may lower returns. While the Model Portfolio performance may have been better than the benchmark for some or all periods shown, the performance during any other period may not have been, and there is no assurance that the Model Portfolio performance will be better than the benchmark in the future. The Model Portfolio performance calculations assume reinvestment of dividends, are pre-tax and are net of Fund expenses. ETF shares are bought and sold at market price (not NAV) and are not individually redeemable from the Fund. Total returns are calculated using the daily 4:00 p.m. EST net asset value (NAV). Market price returns reflect the midpoint of the bid/ask spread as of the close of trading on the exchange where Fund shares are listed. Market price returns do not represent the returns you would receive if you traded shares at other times. Model 12-month yield is calculated using the weighted average trailing 12-month distribution yields of the Fund constituents. Funds incepted less than 12 months ago do not have a trailing 12-month dividend yield. Model expense ratio refers to the weighted average expense ratios of the Fund constituents.

For the most recent month-end and standardized performance of the model and underlying Funds, please click here.

For the 30-day SEC yield for each of the underlying ETFs, please click the respective ticker: PUTW, WTMF, BTAL, FTLS, ADAIX.

As we noted in a recent blog post on client conversations in turbulent times, these are the market times that try investors' souls—rising rates, increased volatility, a slowing economy, high and "sticky" inflation, a hawkish Fed and negative investor sentiment. What's not to love, right?

Fortunately, there are things advisors can do to improve portfolio diversification and potentially improve the consistency of performance. Our Volatility Management Model Portfolio is one such potential solution: it was designed to function as a complementary "sleeve" within a traditional stock and bond portfolio with an investment objective of mitigating downside risk.

Financial advisors who register on the WisdomTree website can learn more about this model and how to successfully position it with end clients via our Model Adoption Center.

For definitions of indices and terms in the charts above, please visit the glossary.

Important Risks Related to this Article

For financial advisors: WisdomTree Model Portfolio information is designed to be used by financial advisors solely as an educational resource, along with other potential resources advisors may consider, in providing services to their end clients. WisdomTree's Model Portfolios and related content are for information only and are not intended to provide, and should not be relied on for, tax, legal, accounting, investment or financial planning advice by WisdomTree, nor should any WisdomTree Model Portfolio information be considered or relied upon as investment advice or as a recommendation from WisdomTree, including regarding the use or suitability of any WisdomTree Model Portfolio, any particular security or any particular strategy.

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