
SURPRISE: HOW A EUROPE-FOCUSED ETF BEAT THE S&P 500 OVER THE LAST THREE YEARS

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05/02/2024

U.S. market leadership has been well established for much of the last 15 years, but it might surprise a number of readers to learn some European ETFs outperformed the U.S. over the last three years—so long as those ETFs employed a currency-hedged approach.

The dollar has been strong, and we think it offers a [nice diversifier to portfolios](#). But if there is a place where it matters the most, it likely is Europe, which we see as having long-term structural issues with its economy.

But low growth can lead to opportunities for low [valuations](#) in companies that participate in revenue growth around the world, not just in Europe.

U.S. equity markets are richly priced. While valuation by itself has rarely caused a [market correction](#), there are wide concerns that U.S. equities could be ripe for a downturn.

European equities are perceived to be among the global laggards in performance. From the top down:

- While the U.S. has energy security, fulfillment of Europe's energy needs has been at greater [risk](#) ever since Russia invaded Ukraine. Germany, Europe's manufacturing center, became dependent on Russian natural gas and had to make significant shifts.
- There is a perception that Europe leads on regulation, whereas the U.S. tends to lead on innovation. Using AI as an example, Europe has taken steps to secure these technologies on the regulatory front,¹ but most of the companies pushing the newest AI technologies forward are not operating out of Europe.²

Many tend to assume that the U.S. must be crushing Europe on an equity market performance basis.

European vs. U.S. Equities: A Few Performance Surprises

To give a better sense of how different types of equities are performing, we can delve into the broad ETF toolkit including³:

- [WisdomTree Europe Hedged Equity Fund \(HEDJ\)](#): The WisdomTree Europe Hedged Equity Fund is designed to track the total return performance, before fees and expenses, of the [WisdomTree Europe Hedged Equity Index](#). The Index consists of dividend-paying companies incorporated in the eurozone and traded on eurozone stock exchanges that derive more than 50% of their revenue from sources outside Europe, tilting toward companies with a more global revenue base. The Index also [hedges](#) exposure to fluctuations in the exchange rate between the euro and U.S. dollar.
- [iShares MSCI Eurozone ETF \(EZU\)](#): The iShares MSCI Eurozone ETF is designed to track the total return performance, before fees and expenses, of the [MSCI EMU Index](#). The index provides exposure to large-cap and mid-cap equities within the eurozone. Currency exposure between the euro and U.S. dollar is not hedged.

- **iShares Currency Hedged MSCI Eurozone ETF (HEZU):** The iShares Currency Hedged MSCI Eurozone ETF is designed to track the total return performance, before fees and expenses, of the [MSCI EMU 100% Hedged to USD Index](#). This index hedges exposure to fluctuations in the exchange rate between the euro and U.S. dollar. The index also provides exposure to large-cap and mid-cap equities within the eurozone.
- We use the [S&P 500 Index](#) to show the performance of the U.S. equity market.

In recent years, investors have become so used to U.S. equities outperforming European equities that the question of which region is winning in a given period has almost faded away. Few, if any, assume that European equities would be outperforming those in the U.S.

Figure 1a: Standardized Performance

Fund Name	Fund Ticker	Fund Inception Date	Fund Gross Expense Ratio	Fund Net Expense Ratio	1-Year	3-Year	5-Year	10-Year	Since Fund Inception
WisdomTree Europe Hedged Equity Fund (NAV)	HEDJ	Dec 31, 2009	0.58%	0.58%	21.63%	12.98%	11.49%	9.30%	8.72%
WisdomTree Europe Hedged Equity Fund (MP)	HEDJ	Dec 31, 2009	0.58%	0.58%	21.84%	13.03%	11.53%	9.31%	8.75%
iShares MSCI Eurozone ETF (NAV)	EZU	Jul 25, 2000	0.51%	0.51%	16.17%	5.91%	8.58%	4.57%	3.50%
iShares MSCI Eurozone ETF (MP)	EZU	Jul 25, 2000	0.51%	0.51%	16.36%	5.97%	8.59%	4.58%	3.51%
iShares Currency Hedged MSCI Eurozone ETF (NAV)	HEZU	Jul 9, 2014	1.12%	0.53%	19.57%	11.40%	11.77%	N/A	8.95%
iShares Currency Hedged MSCI Eurozone ETF (MP)	HEZU	Jul 9, 2014	1.12%	0.53%	19.57%	11.42%	11.79%	N/A	8.95%
S&P 500 Index					34.42%	11.49%	15.21%	13.05%	N/A

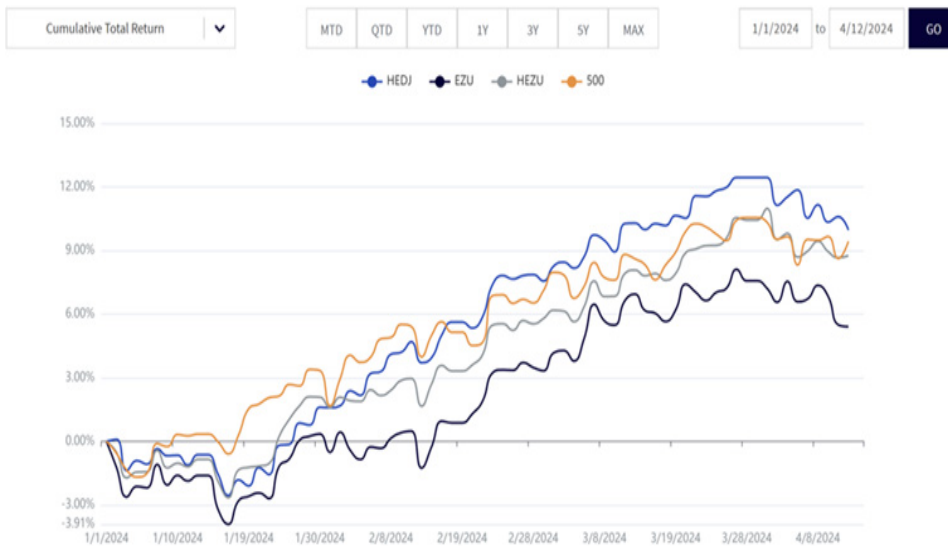
Sources: WisdomTree, PATH Fund Comparison Tool and FactSet, as of 3/31/24. NAV denotes total return performance at net asset value. MP denotes market price performance. **Past performance is not indicative of future results. Investment return and principal value of an investment will fluctuate so that 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.**

Performance data for the most recent month-end for HEDJ is available [here](#).

In Figure 1b, we see:

- EZU underperformed HEZU, indicating euro weakness against the U.S. dollar.
- HEZU delivered similar performance over the period to that of the S&P 500 Index—many wouldn't have realized that eurozone stocks, currency hedged, were keeping up with U.S. stocks.
- [HEDJ](#) performed better than HEZU over the period.

Figure 1b: Performance Year-to-Date 2024



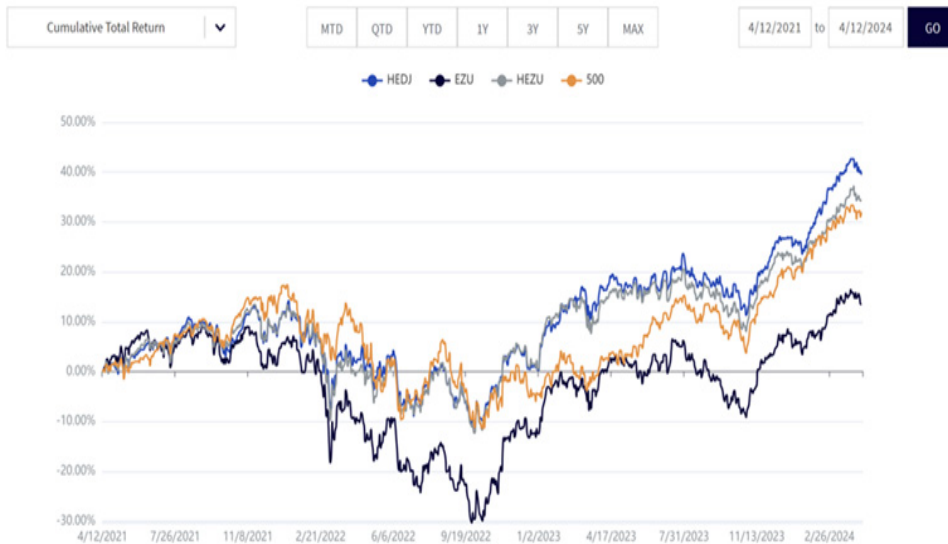
Sources: WisdomTree, PATH Fund Comparison Tool and FactSet, for the period 1/1/24–4/12/24. Total return shown are based on NAV. An investment cannot be made directly into an index. **Past performance is not indicative of future results. Investment return and principal value of an investment will fluctuate 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.**

If we think of the past three years (figure 2), we can see a mix of big equity market events in our mind's eye:

- In the second half of 2021, the market was running up to a near-term peak, buoyed by central bank policy interest rates at or near zero and record printing of money.
- 2022 was rough for equities, except those focused on the energy sector, as central bank policy interest rates in many developed countries were raised quickly to combat [inflation](#).
- 2023 surprised many investors and there was a marked shift back to [large-cap growth](#), which certainly favors a lot of U.S. stocks over, for instance, European stocks.

In this environment of growth over [value](#) and with Europe having a reputation for being so anti-growth, we can see a case for why we might expect U.S. stocks to beat European stocks over the past three years...and yet, [HEDJ](#) outperformed.

Figure 2: It Has Been a Volatile Three Years



Sources: WisdomTree, PATH Fund Comparison Tool and FactSet, for the period 4/12/21–4/12/24. Total return shown are based on NAV. An investment cannot be made directly into 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.**

U.S. vs. Europe—A Very Different Sector Picture

The evolution of the U.S. equity market has led to big platform companies attaining primacy. The Magnificent 7 in 2023—Apple, Alphabet, Meta Platforms, Amazon.com, Microsoft, Tesla and Nvidia—share a common thread of a massive base of users that subscribe to certain services.

Looking to Europe, one big group of companies is the auto makers. These firms are very capable and longstanding, but at the core are viewed as car companies, whereas Tesla is able at times to be perceived as more of an AI or software company.

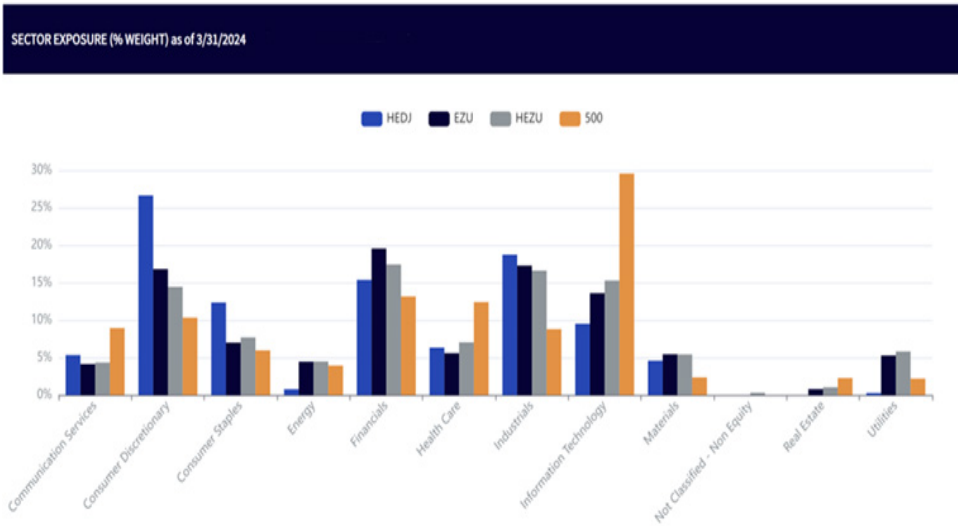
Another big company is ASML. Nvidia’s most advanced chips are being fabricated by Taiwan Semiconductor Manufacturing Co. (TSMC) on machines developed and maintained by ASML.

Then, there is the luxury market, represented by LVMH, which has some of the best brand recognition in the world, but is still making physical products.

The bottom line: there are great companies in Europe but not the same number of clear cases of firms that can break a trillion or trillions of U.S.-dollar [market capitalization](#) in the near term. Notably, many of the [Magnificent 7](#) firms do in fact garner significant revenues from Europe.

In figure 3, we see that the S&P 500 Index has roughly 30% exposure to what we think of as ‘tech’ and [HEDJ](#) places much more weight into Consumer Discretionary. A big reason an export-oriented strategy has so much discretionary exposure is in fact the auto makers.

Figure 3: Differences in Sector Distribution across European Equity ETFs vs. the S&P 500 Index



Sources: WisdomTree, PATH Fund Comparison Tool and FactSet, as of 3/31/24. Weights are subject to change.

Valuations vs. Growth—A Bottom Line Measure of Risk

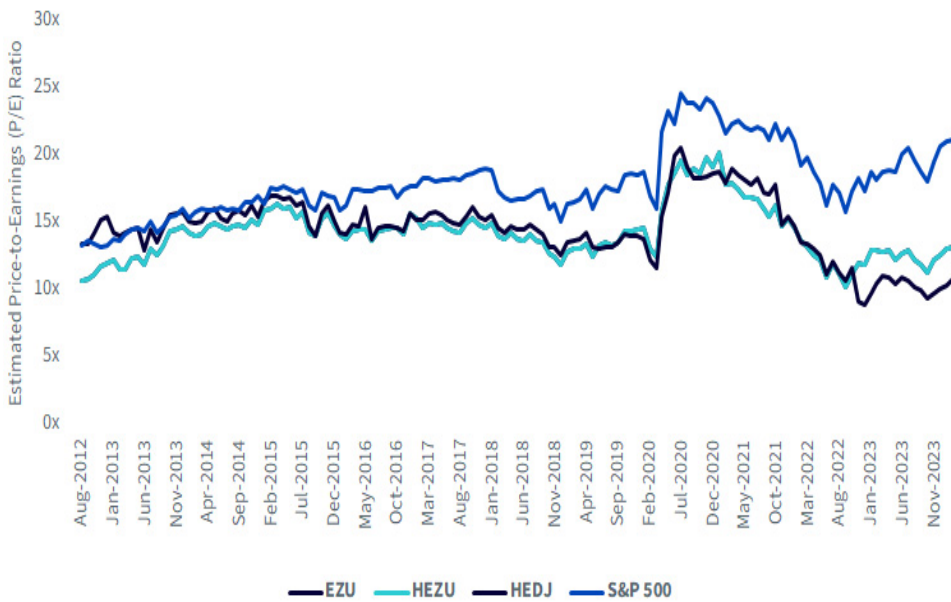
We frequently come back to valuations here in 2024.

The U.S. equity market has been driven forward by large-cap growth and it is at the more expensive end of its range. While an expensive valuation is rarely the reason why an equity market will drop, it does create a greater susceptibility to risk if earnings ever disappoint.

When we look at the performance of European exporters, there are periods when they have outperformed the U.S. and they have certainly not lagged as much as many might think. With that said, on a [forward price-to-earnings ratio \(P/E\)](#) basis, the S&P 500 Index is above 20x, whereas [HEDJ](#) is at approximately a 50% discount and closer to 10x.

We'd note that in figure 4, since HEZU and EZU have the same underlying stock exposures, the forward P/E ratio data is the same for each of the relevant historical time series.

Figure 4: European Equities' Valuation Discount to the U.S. Has Widened



Sources: WisdomTree, FactSet, for the period August 2012 to March 2024. Due to EZU and HEZU having exposure to the same underlying stocks, in a chart like this we would only ever see a single line, in this case HEZU. Fundamental data based on underlying stocks is the same.

Forward Looking Growth Expectations

We think a lot about the nexus between how an equity market is currently priced relative to its future growth expectations. We also try to get beyond the current year and think a bit ahead. Figure 5 takes a measure of 2025 operating income and compares that to the current enterprise value of the different ETFs. Since EZU and HEZU contain the same underlying stocks, we only show one of them here.

Our conclusion: [HEDJ](#), EZU, HEZU and the S&P 500 Index have very different risk profiles. If one wants exposure to U.S. large-cap growth—there is not substitute for a U.S. exposure. However, many investors we speak to look at the U.S. market and have seen very good performance of late.

They are concerned about valuation. Figure 5 shows that [HEDJ](#) is currently trading at about half the ratio of the S&P 500 Index if one is comparing EV/2025 operating income.⁴ In our opinion, this discount could allow investors to feel more comfortable with the increased risk of investing outside the U.S.

Figure 5: The Valuation Discount of European Equities vs. U.S. Equities



Sources: WisdomTree, FactSet, as of 3/31/24.

Figure 6: Other Important Information Regarding ETFs in this Piece



If you are a financial professional and interested in diving further into the comparison of these Funds, please check out our [Fund Comparison Tool](#).

¹ Source: AI Act, European Commission, <https://digital->

strategy.ec.europa.eu/en/policies/regulatory-framework-ai

² Source: Nestor Maslej, Loredana Fattorini, Erik Brynjolfsson, John Etchemendy, Katrina Ligett, Terah Lyons, James Manyika, Helen Ngo, Juan Carlos Niebles, Vanessa Parli, Yoav Shoham, Russell Wald, Jack Clark, and Raymond Perrault, "The AI Index 2023 Annual Report," AI Index Steering Committee, Institute for Human-Centered AI, Stanford University, April 2023.

³ EZU is the largest ETF within the U.S. ETF Europe Stock category for Morningstar, measured on the basis of assets under management (AUM), that has only eurozone equity exposure, i.e., no exposure to the UK, Switzerland, Norway, Sweden or any other country that does not use the euro currency. Calculations were run as of 4/22/24. HEZU is the currency-hedged version of the same strategy.

⁴ Refers to a measure of current enterprise value over 2025 operating income, meaning that company estimates of 2025 operating income are aggregated for each strategy. The source is FactSet, which aggregates all analyst estimates.

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For the top 10 holdings of HEDJ please visit the Fund's fund detail page at <https://www.wisdomtree.com/investments/etfs/equity/hedj>

For standardized performance and the most recent month-end performance click [here](#) NOTE, this material is intended for electronic use only. Individuals who intend to print and physically deliver to an investor must print the monthly performance report to accompany this blog.

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DEFINITIONS

Valuation: Refers to metrics that relate financial statistics for equities to their price levels to determine if certain attributes, such as earnings or dividends, are cheap or expensive.

Correction: A drop of 10% or greater in an Index or stock from a recent high.

Risk: Also standard deviation, which measures the spread of actual returns around an average return during a specific period. Higher risk indicates greater potential for returns to be farther away from this average.

Hedge: Making an investment to reduce the risk of adverse price movements in an asset. Normally, a hedge consists of taking an offsetting position in a related security, such as a futures contract.

MSCI EMU Index: A free float-adjusted market capitalization-weighted index designed to measure the performance of the markets in the European Monetary Union.

MSCI EMU 100% Hedged to USD Index: represents a close estimation of the performance that can be achieved by hedging the currency exposure of its parent index, the MSCI EMU Index, to USD, the “home” currency for the hedged index. The index is 100% hedged to USD by selling the EUR forward at the one-month forward rate. The parent index is composed of large and mid-cap stocks across 10 Developed Market countries.

S&P 500 Index: Market capitalization-weighted benchmark of 500 stocks selected by the Standard and Poor’s Index Committee designed to represent the performance of the leading industries in the United States economy.

Inflation: Characterized by rising price levels.

Large-Capitalization (Large-Cap): A term used by the investment community to refer to companies with a market capitalization value of more than \$10 billion. Large cap is an abbreviation of the term “large market capitalization”. Market capitalization is calculated by multiplying the number of a company’s shares outstanding by its stock price per share.

Growth: Characterized by higher price levels relative to fundamentals, such as dividends or earnings. Price levels are higher because investors are willing to pay more due to their expectations of future improvements in these fundamentals.

Value: Characterized by lower price levels relative to fundamentals, such as earnings or dividends. Prices are lower because investors are less certain of the performance of these fundamentals in the future. This term is also related to the Value Factor, which associates these stock characteristics with excess returns vs the market over time.

Market Capitalization: $\text{Market cap} = \text{share prices} \times \text{number of shares outstanding}$. Firms with the highest values receive the highest weights in approaches designed to weight firms by market cap.

Magnificent 7: Refers to a group of high-performing U.S. stocks including Microsoft (MSFT), Amazon (AMZN), Meta (META), Apple (AAPL), Google parent Alphabet (GOOGL), Nvidia (NVDA), and Tesla (TSLA)

Price-to-earnings (P/E) ratio: Share price divided by earnings per share. Lower numbers indicate an ability to access greater amounts of earnings per dollar invested.