IT'S YOU, SWEET INCOME

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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.

Honey it's you, sweet baby

Ever lost and captured by your smile, sweet baby
I will always be right there by your side
Right by your side

Lying here alone I'm dreaming
My mind keeps wandering, my thoughts are only you
Looking through the memories in my mind
How could love so real have turned so empty
I just keep wondering why
Will I ever find the love we shared together, you and I?

(From "Sweet Baby" by Stanley Clarke and George Duke, 1981)

Investment Themes for 2021

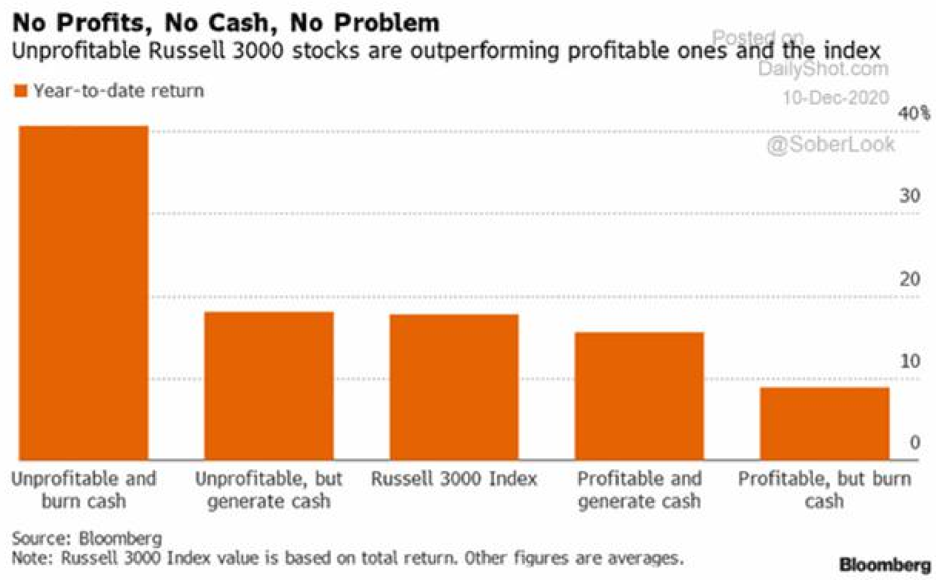
As described in a previous blog post, WisdomTree has identified five primary investment themes that we believe have a high probability of playing out over the course of 2021 and beyond:

- Cyclical rotation back toward small-cap, value and emerging market stocks
- Emerging markets, both in equity and debt
- Reflation (higher than expected inflation in the second half of the year)
- Disruptive growth
- Focus on quality and income, both in equity and debt

In this blog post we take a deeper look into **quality and income** and how our Model Portfolios are aligned with this investment theme.

What Worked in 2020

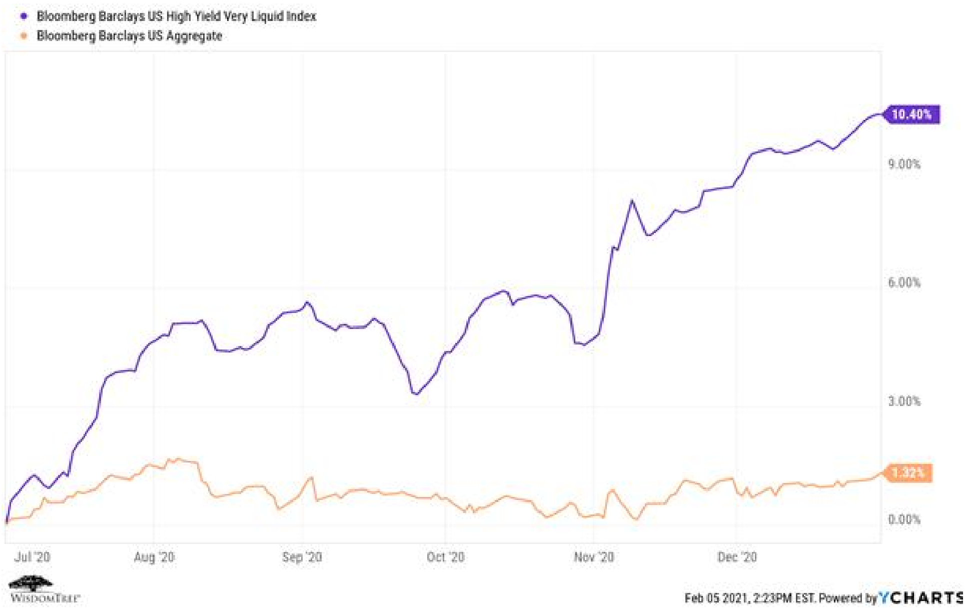
In the equity markets in 2020, neither quality nor income was rewarded by the market as it priced in assumed dividend cuts during the pandemic and rewarded "junk" companies:



Sources: Bloomberg, The Daily Shot, 12/10/20. You cannot invest in an index, and past performance does not guarantee future results.

Source: YCharts, data range 1/1/20–12/31/20. You cannot invest in an index, and past performance does not guarantee future results.

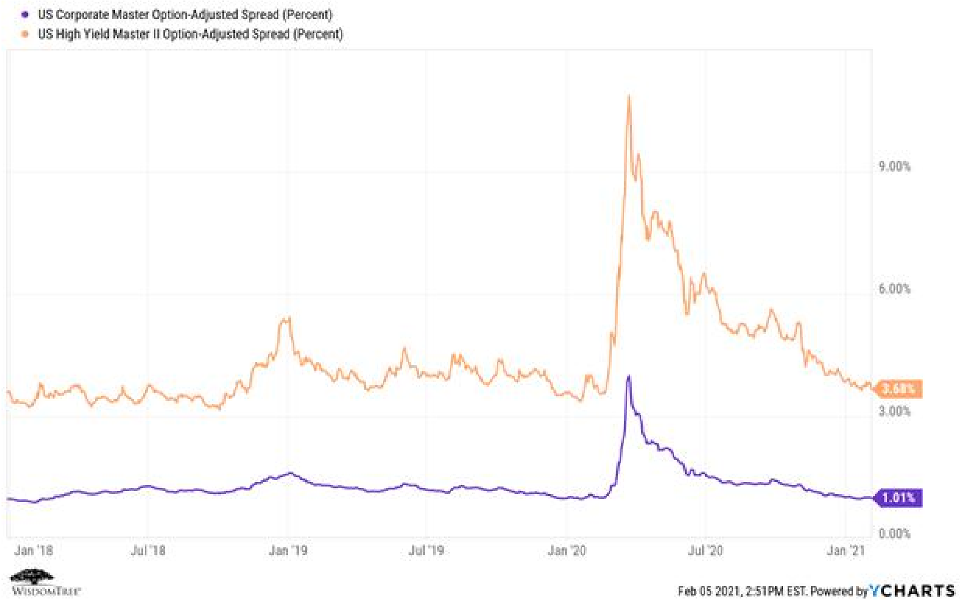
In the bond market, high-yield ("junk") bonds, though much more volatile, outperformed investment-grade bonds, especially in the second half of the year:



Source: YCharts, data range 7/1/20–12/31/20. You cannot invest in an index, and past performance does not guarantee future results.

On the equity side, when we say "quality" we mean screening for companies that have strong [balance sheets](), earnings and [cash flows](). This is a common screen for most WisdomTree equity indexes, and so our Model Portfolios tend to have a distinct quality tilt to them. We never think it is a bad idea to invest in quality companies, even if the market disagrees with us from time to time.

On the fixed income side, we mean companies with solid debt coverage ratios and lower risk of default. Within our core fixed income models, we have for quite some time maintained a strategic positioning of underweight duration and overweight credit. We remain comfortable with that positioning, given our view of future yield curve and spread movements. But, within that overweight credit exposure, we are also highly focused on quality security selection, given current spread levels:



Source: YCharts, data range 1/1/18–2/4/21. You cannot invest in an index, and past performance does not guarantee future results.

While quality and income companies seemingly were out of favor in 2020, we think they are poised for a comeback in 2021. We can see this playing out, at least in small- and m id-cap stocks, if we compare the performance of the S&P 600 Index to that of the Russell 2500 Index since the beginning of the third quarter of 2020 (the S&P indexes typically contain higher quality stocks than the comparable Russell indexes):

Source: YCharts, data range 7/1/20–2/4/21. You cannot invest in an index, and past performance does not guarantee future results.

How does all of this pertain to WisdomTree Model Portfolios? In two primary ways:

1. As mentioned earlier, all of our Models have a distinct quality tilt to them, as that is a common screen we apply in creating the indexes that underly many of our core equity products. On the fixed income side, an excellent example is our WisdomTree High Yield Corporate Bond Fund (WFHY), which screens out companies with negative cash flows.
2. Our Global Dividend, Global Multi-Asset Income and Siegel-WisdomTree Models all have quality and income tilts. A differentiating factor from other income-focused models is that we allocate more heavily to yield and income-oriented equities, versus taking excessive duration or credit risk in the fixed income market. In addition, the Global Multi-Asset Income Model allocates to less traditional sources of income, such as covered call options, master limited partnerships (MLPs) and preferred securities, to enhance current income while increasing portfolio diversification.

Conclusion

With rates and credit spreads where they are, we believe it will be difficult to generate much income from a traditional fixed income allocation without taking excessive risk. Given the quality tilt and diversified nature of the income sources in many of our Model Portfolios, especially the Global Dividend, Global Multi-Asset Income and Siegel-WisdomTree Longevity Models, we believe we are well positioned to capture a quality and income theme in 2021, and thereby help advisors deliver a differentiated end client investment experience.

For definitions of indexes in the charts, please visit our glossary.

Important Risks Related to this Article

There are risks associated with investing, including the possible loss of principal. Fixed income investments are subject to interest rate risk; their value will normally decline as interest rates rise. High-yield or “junk” bonds have lower credit ratings and involve a greater risk to principal. Fixed income investments are also subject to credit risk, the risk that the issuer of a bond will fail to pay interest and principal in a timely manner or that negative perceptions of the issuer's ability to make such payments will cause the price of that bond to decline. While the Fund attempts to limit credit and counterparty exposure, the value of an investment in the Fund may change quickly and without warning in response to issuer or counterparty defaults and changes in the credit ratings of the Fund's portfolio investments. Please read the Fund's prospectus for specific details regarding the Fund's risk profile.

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WisdomTree primarily uses WisdomTree Funds in the Model Portfolios unless there is no WisdomTree Fund that is consistent with the desired asset allocation or Model Portfolio strategy. As a result, WisdomTree Model Portfolios are expected to include a substantial portion of WisdomTree Funds notwithstanding that there may be a similar fund with a higher rating, lower fees and expenses or substantially better performance. Additionally, WisdomTree and its affiliates will indirectly benefit from investments made based on the Model Portfolios through fees paid by the WisdomTree Funds to WisdomTree and its affiliates for advisory, administrative and other services.

Jeremy Siegel serves as Senior Investment Strategy Advisor to WisdomTree Investments, Inc., and its subsidiary, WisdomTree Asset Management, Inc. ("WTAM" or "WisdomTree"). He serves on the Asset Allocation Committee of WisdomTree, which develops and rebalances WisdomTree's Model Portfolios. In serving as a consultant to WisdomTree in such roles, Mr. Siegel is not attempting to meet the objectives of any person, does not express opinions as to the investment merits of any particular securities and is not undertaking to provide and does not provide any individualized or personalized advice attuned or

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The Siegel-WisdomTree Longevity Model Portfolio seeks to address increasing longevity by shifting the focus to potential long-term growth through a higher stock allocation versus more traditional “60/40” portfolios.

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.

For more investing insights, check out our Economic & Market Outlook

View the online version of this article here.

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You cannot invest directly in an index.

DEFINITIONS

Quality : Characterized by higher efficiency and profitability. Typical measures include earnings, return on equity, return on assets, operating profitability as well as others. This term is also related to the Quality Factor, which associates these stock characteristics with excess returns vs the market over tim.

Dividend : A portion of corporate profits paid out to shareholders.

Junk Bond : A high-yield or non-investment grade bond. Junk bonds are fixed-income instruments that carry a rating of 'BB' or lower by Standard & Poor's, or 'Ba' or below by Moody's. Junk bonds are so called because of their higher default risk in relation to investment-grade bonds.

High Yield : Sometimes referred to as "junk bonds," these securities have a higher risk of default than investment-grade securitie.

Volatility : A measure of the dispersion of actual returns around a particular average level. .

Investment grade : An investment grade is a rating that signifies a municipal or corporate bond presents a relatively low risk of default.

Balance sheet : refers to the cash and cash equivalents part of the Current Assets on a firms balance sheet and cash available for purchasing new position.

Cash flows : a measure of how much cash a business generates after taking into account all the necessary expenses, including net capital expenditures.

Debt-to-Asset Ratio : a leverage ratio that defines the total amount of debt relative to assets. .

Duration : A measure of a bond's sensitivity to changes in interest rates. The weighted average accounts for the various durations of the bonds purchased as well as the proportion of the total government bond portfolio that they make up.

Credit : A contractual agreement in which a borrower receives something of value now and agrees to repay the lender at some date in the future.

Yield curve : Graphical Depiction of interest rates on government bonds, with the current yield on the vertical axis and the years to maturity on the horizontal axis.

Small caps : new or relatively young companies that typically have a market capitalization between $200 million to $2 billion.

Mid-Cap : Characterized by exposure to the next 20% of market capitalization (after the top 70% have been removed) within the Value, Blend or Growth style zones with the majority of the fund's weight.

S&P 600 Index : The S&P 600 is an index of small-cap stocks managed by Standard and Poor's. It tracks a broad range of small-sized companies that meet specific liquidity and stability requirements.

Master limited partnership (MLP) : Investment structure where holdings typically must derive most of their cash flows from real estate, natural resources or commodities, combining the tax benefits of a partnership—taxes occur when holders receive distributions—with the liquidity of a publicly traded company.