

THE BOND MARKET'S SELL-OFF IS TAKING OUT THE STOCK MARKET'S LEADERS

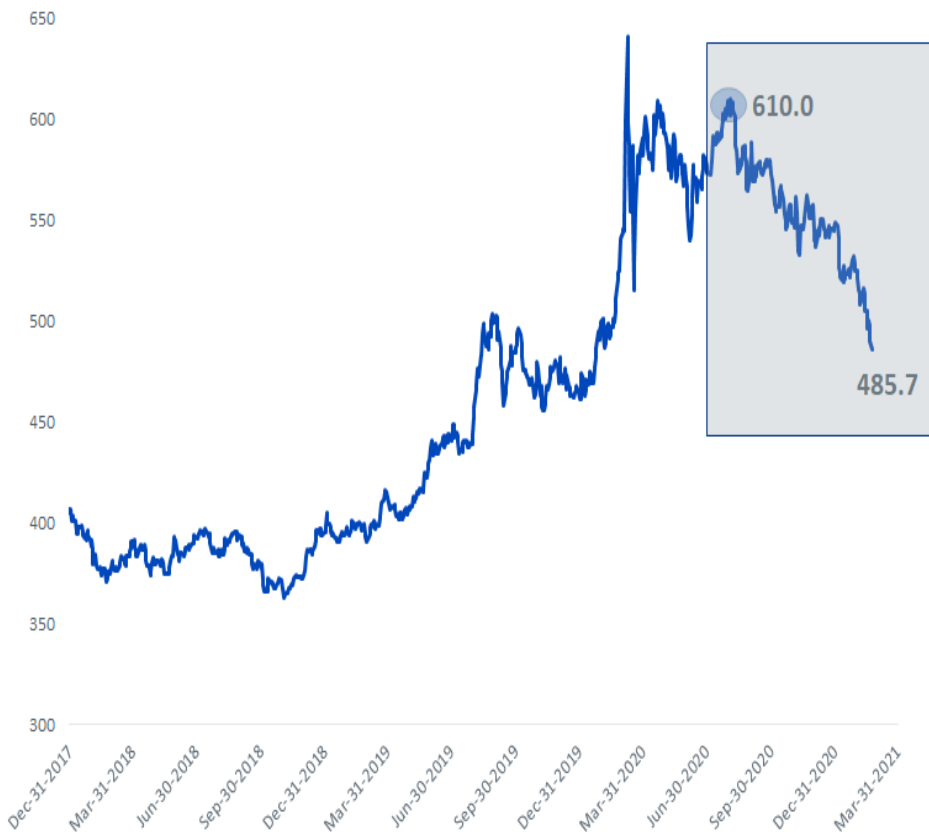
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This is part 1 of a two-part blog series. In part 2, “Plenty of Price, Not Much Sales,” we will take a look at the growing list of companies that are trading at extraordinary [valuations](#).

Long [duration](#) bonds are witnessing some ugly price action.

It came so quickly that you could be forgiven for not fully appreciating the extent of the pain—the 30-Year U.S. [Treasury](#) is officially in a [bear market](#), defined as a loss of more than 20% (figure 1).

Figure 1: Ryan Labs U.S. 30-Year Treasury Total Return Index



Sources: Thomson Reuters Refinitiv, Ryan Labs, as of 2/22/21. Past performance is not indicative of future results. You cannot invest directly in an index.

My suspicion is that rising [yields](#)—bond market pain—amount to a greater headwind for [growth](#) stocks than [value](#) stocks, owing to the effect that higher discount rates have on

distant cash flows.

Focus on the bold fonts in figure 2, which show the correlation to the [S&P 500 Growth](#) of some of our major U.S. [large-cap](#) value-tilted Funds.

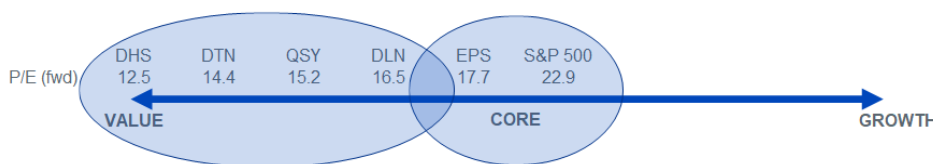
Figure 2: WisdomTree Large Cap Core & Value Correlations

Indexes & Funds	S&P 500 Growth	S&P 500 Value	QSY	EPS	DLN	DHS	DTN
S&P 500	0.96	0.92	0.94	0.99	0.97	0.88	0.92
S&P 500 Growth	1.00	0.78	0.80	0.94	0.91	0.74	0.78
S&P 500 Value	0.78	1.00	0.95	0.94	0.95	0.98	0.97
QSY	0.80	0.95	1.00	0.96	0.94	0.88	0.92
EPS	0.94	0.94	0.96	1.00	0.97	0.89	0.93
DLN	0.91	0.95	0.94	0.97	1.00	0.96	0.97
DHS	0.74	0.98	0.88	0.89	0.96	1.00	0.97
DTN	0.78	0.97	0.92	0.93	0.97	0.97	1.00

Sources: Thomson Reuters Refinitiv, WisdomTree. Correlations are for 10 years, monthly, ending 1/31/21. EPS = WisdomTree U.S. LargeCap Fund, DLN = WisdomTree U.S. LargeCap Dividend Fund, QSY = WisdomTree U.S. Quality Shareholder Yield Fund, DTN = WisdomTree U.S. Dividend ex-Financials Fund, DHS = WisdomTree U.S. High Dividend Fund.

On a value-core-growth spectrum, the five Funds look something like figure 3. [DHS](#), [DTN](#) and [QSY](#) give a deeper value bias than [DLN](#), which is a more traditional value. [EPS](#) is more of a core Fund that has a value flavor.

Figure 3: WisdomTree Funds' Value-Core-Growth Positioning



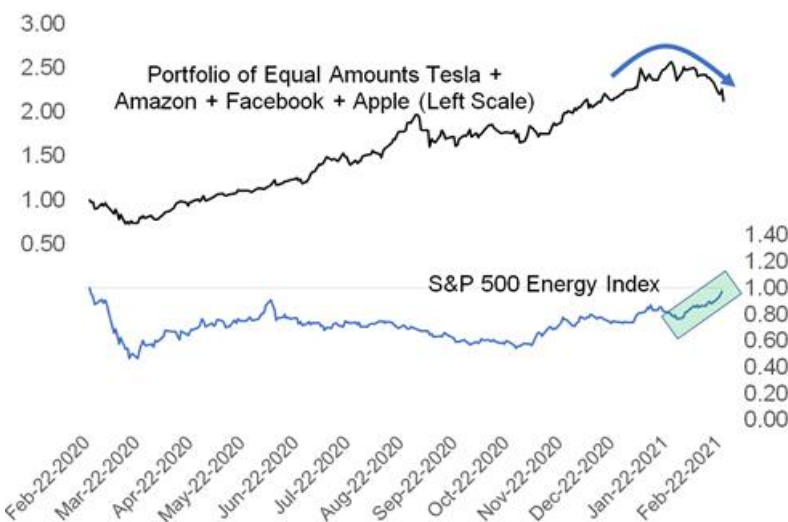
Source: WisdomTree. P/E ratios as of 1/31/21.

It's still early days, but the stock market's response to the bond sell-off has been to take out growth stocks. For sure, not all of the market's leaders are in trouble: Google-parent Alphabet is still near its highs, while Microsoft's decline since mid-February is just a blip on the long-term chart. Then again, I am not sure many people consider that one to be a growth stock anymore.

But things are looking ugly with some of the market's "generals," with Tesla, Amazon, Facebook and Apple acting sickly of late. That is a sharp contrast to the surge in the [reflation](#)-themed Energy sector.

Figure 4 is the 2021's reflation thesis in one exhibit: disinflation beneficiaries are "off," and inflation beneficiaries are "on."

Figure 4: Old Leaders vs. New Leaders



Source: Thomson Reuters Refinitiv, as of 2/25/21. Past performance is not indicative of future results. You cannot invest directly in an index.

The "value-lite" EPS tends to under-weight in high flyers because its 500-stock

methodology weights components by their earnings as a proportion of all stocks' earnings. It only has 1% in Energy, owing to that group's low profits. If the goal is to have more in that sector, maybe something like QSY is the angle.

DLN requires a dividend for inclusion, so it is a course that can be taken to completely exclude a handful of the market's darlings. Similar concepts are found in DTN and DHS, which have their own twists on dividend screens.

Figure 5: Fund & Index Weights

Ticker	Name	Tesla	Amazon	Facebook	Apple	Energy
SPX	S&P 500	1.60%	4.02%	1.89%	5.96%	2.88%
EPS	WisdomTree U.S. Large Cap Index Fund	--	1.63%	2.03%	4.63%	1.18%
DLN	WisdomTree U.S. Large Cap Dividend Fund	--	--	--	4.14%	0.45%
QSY	WisdomTree U.S. Quality Shareholder Yield Fund	--	--	--	1.12%	6.07%
DTN	WisdomTree U.S. Dividend ex-Financials Fund	--	--	--	--	3.42%
DHS	WisdomTree U.S. High Dividend Fund	--	--	--	--	0.96%

Sources: Thomson Reuters Refinitiv, WisdomTree, as of 2/26/21. Weights subject to change

In part 2 of this two-part blog series, we look at the abundance of companies in the S&P 500 that are trading at a price-to-sales ratio above 10—and what may happen to them if rising interest rates hinder growth stocks.

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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.

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.

Treasury: Debt obligation issued by the U.S. government with payments of principal and interest backed by the full faith and credit of the U.S. government.

Bear market: A sustained downturn in market prices, increasing the chances of negative portfolio returns.

Yield: The income return on an investment. Refers to the interest or dividends received from a security that is typically expressed annually as a percentage of the market or face value.

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.

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.

Reflation: The term is used to describe the first phase of economic recovery after a period of contraction. This period is typically characterized by the act of stimulating the economy through accommodative central bank policies and reducing taxes, to bring growth and inflation back up to the long-term trend.