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# REFLATION, FLATION, WHAT'S YOUR NATION?

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Model Portfolios  
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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.

*Conjunction Junction, what's your function?*

*I got "and," "but," and "or,"  
They'll get you pretty far...*

Conjunction Junction, how's that function?

I like tying up words and phrases and clauses

(From "Conjunction Junction," School House Rock, 1973)

## 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 fixed income;
- A focus on [quality](#) and income, both in equity and fixed income;
- Disruptive growth; and
- [Reflation](#) (higher-than-expected inflation in the second half of the year)

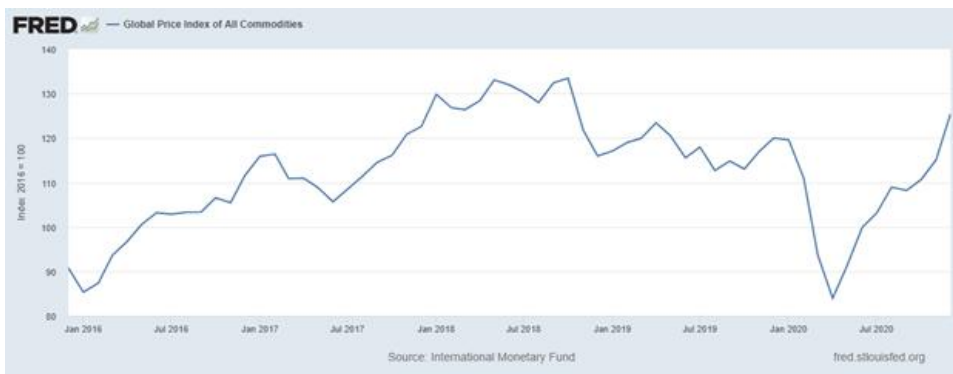
In this blog piece, we want to take a deeper look into this last theme—reflation.

While official inflation indicators, such as the [Consumer Price Index](#) and the [Personal Consumption Expenditures Price Index](#), are not yet showing any signs of a re-emergence of inflation, the U.S. bond market is preparing for a potential shift in the pricing outlook. In our "Inflate-Gate? Don't Tell That to the Bond Market" blog post a couple of weeks ago, we highlighted how [inflation expectations have been noticeably on the rise thus far in 2021](#).



Source: St. Louis Federal Reserve Bank (FRED), data through 2/10/21.

In addition, investors have witnessed rising price trends in purchasing managers' surveys and, perhaps more importantly, in actual commodities. According to data from the International Monetary Fund, the Global Price Index of All Commodities has experienced a rather noticeable V-shaped recovery of its own, finishing 2020 at its highest level in more than two years... And guess what? According to real-time commodity gauges, both [futures](#) and [spot prices](#) have continued this ascending trajectory here into the first two months of the new year.



Source: St. Louis Federal Reserve Bank (FRED), data through 2/16/21.

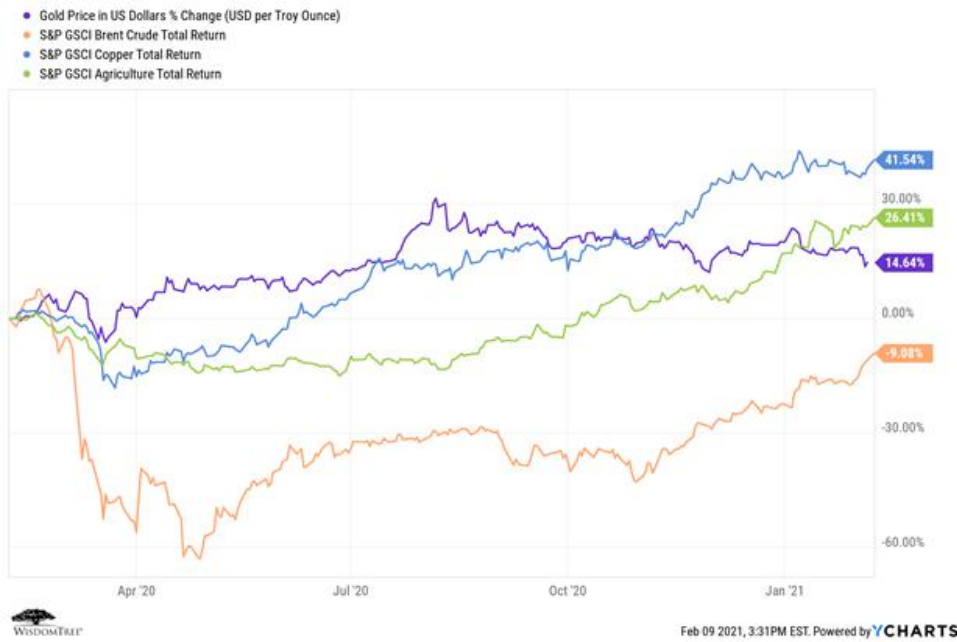
### Product and Portfolio Implications

As we discussed a few weeks ago, WisdomTree offers a variety of fixed income product strategies that can help [navigate inflation/interest rate risks](#). Another approach would be to focus exclusively on the commodity sector.

WisdomTree recently completed the reorganization of the WisdomTree Continuous Commodity Index Fund into the [WisdomTree Enhanced Commodity Strategy Fund \(GCC\)](#). The Enhanced Commodity Strategy Fund is organized under [the Investment Company Act of 1940](#), as amended, with no Schedule [K-1](#) that provides broad exposure to a [diversified](#) basket of commodities.

GCC emphasizes a diversified nature of commodities compared to the traditional well-established commodity indexes like the S&P GSCI Index (SPGSCI), which could have as much as 70%-80% of risk driven by exposure to the energy sector. Our approach maximizes this diversification with strategic weights roughly balanced between precious metals, industrial metals, agriculture and energy. In addition, we dynamically manage the futures contract "[rolls](#)" to potentially mitigate the headwinds faced by the more traditional use of just the [front month](#) contract.

Within the [WisdomTree Model Portfolios](#), specifically within the [Siegel-WisdomTree Longevity Model Portfolio](#) and our Endowment Model Portfolios, we took an explicit gold position last March, and that trade worked well for us, though gold has stabilized over the past 2-3 months.

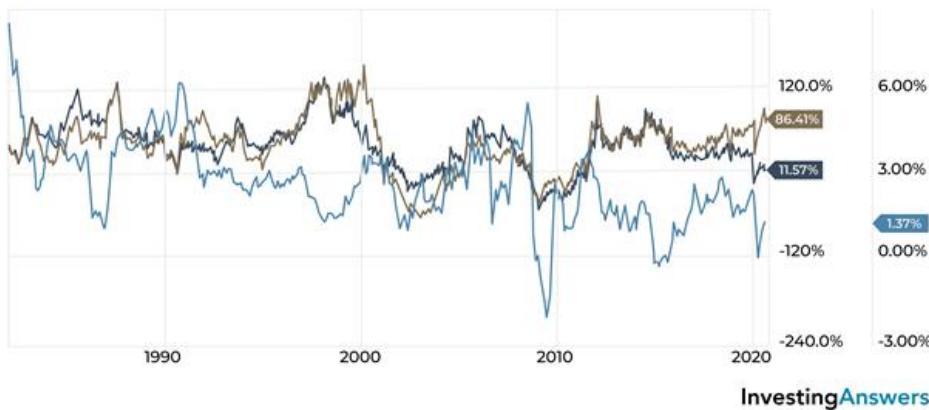


Source: YCharts, data range from 1/1/20–2/9/21. You cannot invest in an index, and past performance does not guarantee future results.

In addition, the Siegel-WisdomTree Longevity Model Portfolio is, by design, over-weight in equities versus fixed income. (We try to maximize current income via [yield](#)-focused equities instead of taking on excessive risk in our fixed income allocation.) Historically, equities have shown to be an effective [hedge](#) against modestly rising [inflation](#):

**Growth vs. Value Stock Performance**

- Russell 1000 Value Total Return 3 Year Total Returns (Daily)
- Russell 1000 Growth Total Return 3 Year Total Returns (Daily)
- US Inflation Rate



Source: ICarelon, Peter. "3 Simple Ways Everyone Can Hedge Against Inflation." InvestingAnswers, updated 1/11/21. You cannot invest in an index, and past performance does not guarantee future results.

In our December Model Portfolio Investment Committee meeting, we made some additional changes. While maintaining our existing gold position within the Siegel-WisdomTree Longevity Model Portfolio, we reallocated from our fixed income position into a broader commodity complex position, specifically GCC. Within our Endowment Model Portfolios, we reallocated out of gold and into GCC to give us a broader exposure to the global commodity complex.

**Conclusion**

If we are correct in our views on global economic recovery, a weak dollar and a general “reflationary” regime in the second half of 2021, we believe WisdomTree has both the strategies and Model Portfolios to meet your needs and help deliver a differentiated end client investment experience.

#### Important Risks Related to this Article

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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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## DEFINITIONS

**Cyclical sectors**: Consumer Discretionary, Energy, Industrials, Materials, Financials and Information Technology sectors.

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

**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.

**Emerging market**: Characterized by greater market access and less potential for operational risks when compared to frontier markets, which leads to a larger base of potentially eligible investors.

**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 time.

**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.

**Consumer Price Index (CPI)**: A measure that examines the weighted average of prices of a basket of consumer goods and services, such as transportation, food and medical care. The CPI is calculated by taking price changes for each item in the predetermined basket of goods and averaging them; the goods are weighted according to their importance. Changes in CPI are used to assess price changes associated with the cost of living.

**Personal Consumption Expenditure (PCE) Price Index**: measure of price changes in consumer goods and services in the U.S. economy.

**Futures price**: the price of a futures contract.

**Spot price**: The current price at which a particular security can be bought or sold at a specified time and place.

**The Investment Company Act of 1940**: An act of Congress which regulates the organization of investment companies and the activities they engage in, and sets standards for the investment company industry.

**K-1**: A tax document used to report the incomes, losses and dividends of a person's interest in an entity.

**Diversification**: A risk management strategy that mixes a wide variety of investments within a portfolio.

**Rolling**: trading out of a security that is close to maturing and into the same or similar security with a later maturity date.

**Front month**: The nearest expiration date for a futures contract. Contracts that have later expiration dates than front month contracts are called back month, or 'far month',

contracts.

**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.

**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.

**Inflation**: Characterized by rising price levels.