

GENERATING YIELD IN A VOLATILE MARKET

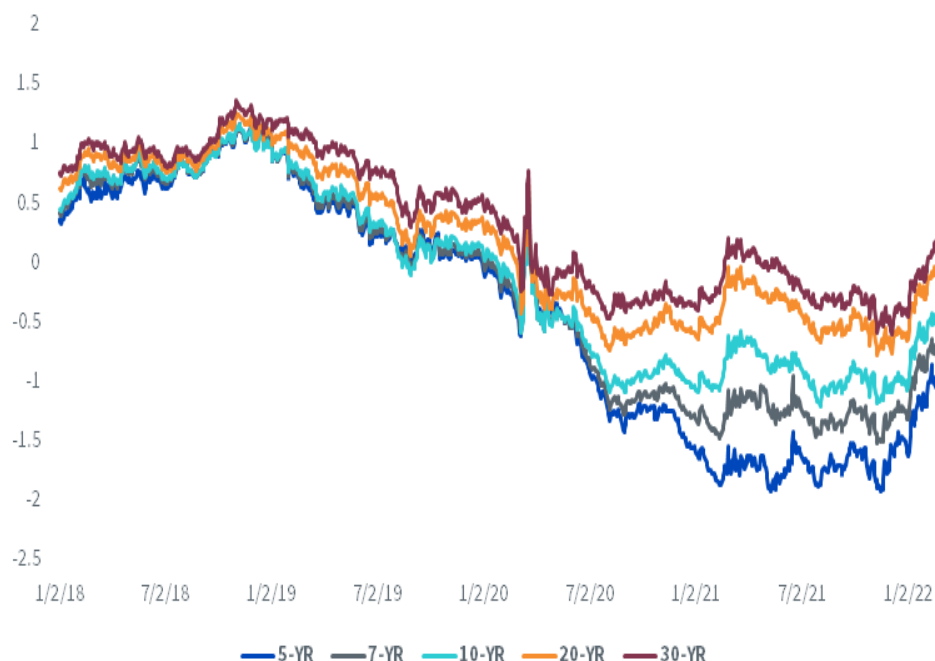
Scott Welch – Chief Investment Officer, Model Portfolios
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This article is relevant to financial professionals who are considering offering Model Portfolios to their clients. If you are an individual investor interested in WisdomTree ETF Model Portfolios,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

It has only been a little more than a month since we last visited the topic of [generating yield in an evolving market](#), but market conditions have changed so rapidly since then it is time to revisit it, and in fact, this will become a recurring topic. The Fed recently began its “[rate hike cycle](#)” as it attempts to balance economic growth against rampant [inflation](#), the stock market has been volatile and geopolitical tensions are as high as they have been in decades.

Let’s begin with rates, starting with the [Treasury yield curve](#). Rates are rising without question as investors anticipate an aggressive Fed rate hike regime, but except for the 30-Year, [Treasury real yields](#) remain negative across the entire maturity spectrum.

U.S. Treasury Real Yields (%)



Source: Treasury.gov, data through 3/21/22. Past performance does not guarantee future results.

While [nominal Treasury](#) rates have also been rising, the real action has been at the short end of the curve, as we now approach a flat and perhaps [inverted yield curve](#) structure (we use the 10-Year minus 2-Year Treasury rates as a proxy for the “shape of the curve”). We think, with fits and starts, this upward trend will continue, but should the yield curve invert, we do not necessarily believe that signals an impending

recession, as it has many times in the past. What is notable is how aggressively the 2-Year rate has risen in recent months even though the Fed has, thus far, only raised rates once.

- 10 Year Treasury Rate (Percent)
- 2 Year Treasury Rate (Percent)
- 10-2 Year Treasury Yield Spread (Percent)



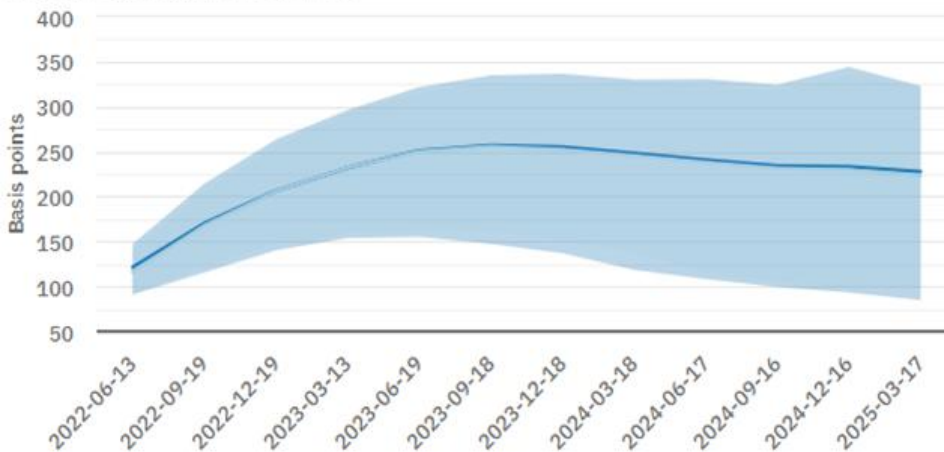
Mar 22 2022, 3:12PM EDT, Powered by YCHARTS

Source: YCharts, 12-month data through 3/21/22. Past performance does not guarantee future results.

Speaking of the Fed, the market is now pricing in at least six rate hikes for the remainder of 2022, meaning at least a 25-basis-point hike in each of the remaining FOMC meetings, resulting in a Fed Funds Rate of at least 2.00% by year-end. There are others, like St. Louis Fed Governor James Bullard and our own Senior Investment Strategy Advisor, Professor Jeremy Siegel, who believe the Fed will have to be even more aggressive than that if it wants to get a handle on inflation.

The Expected Future Path of the Three-Month Average Fed Funds Rate

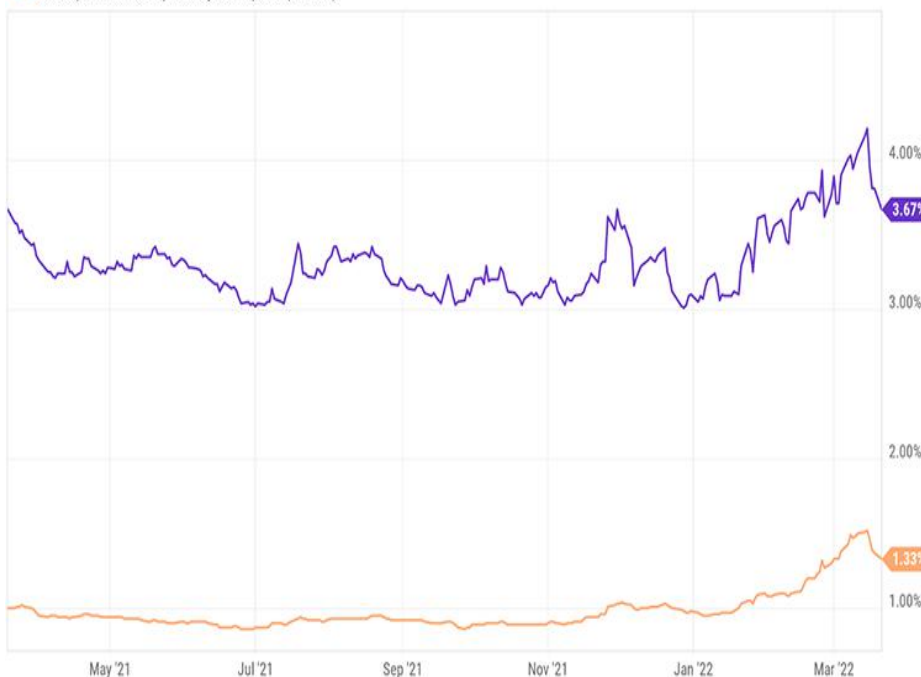
Current target range: 0 basis points



Source: The Atlanta Federal Reserve Bank “Market Probability Tracker,” through 3/18/22. The “Tracker” estimates the market-implied probabilities of various ranges for the three-month average Fed Funds Rate. The methodology uses data on three-month eurodollar futures, options on three-month eurodollar futures from the Chicago Mercantile Exchange (CME), three-month LIBOR/Fed Funds basis swap spreads expiring in 12 months and the Treasury yield curve.

Finally, [credit spreads](#) awakened from their apparent somnambulance and have started to widen.

- US High Yield Master II Option-Adjusted Spread (Percent)
- US Corporate Master Option-Adjusted Spread (Percent)



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Source: YCharts, 12-month data as of 3/21/22. You cannot invest in an Index, and past performance does not guarantee future results.

For definitions of terms in the table, please visit the [glossary](#).

So, What Is a Yield-Seeking Investor to Do?

To summarize the above, we continue to believe rates will grind higher, and inflation remains the story through at least the first half of 2022. Rates are rising, and credit spreads are widening—it’s hard to be optimistic about the total return profile of the broader fixed income markets. We note, however, that corporate balance sheets are in solid shape, so we believe “coupons” (interest payments) have a reduced probability of default.



What about finding yield in the equity markets? Using the information from above, let's compare current nominal fixed income yields to current equity [dividend yields](#).

Instrument	10-Year Treasury	Investment-Grade Credit Spread	High-Yield Credit Spread	Total Nominal Current Yield
IG Bonds	2.14%	1.33%		3.47%
HY Bonds			3.67%	5.81%
S&P 500 Dividend Yield				1.34%
ACWI ex-U.S. Dividend Yield				2.90%

Sources: YCharts, S&P and MSCI, data through 3/21/22. Yields are approximate and security specific. "IG" stands for "Investment grade" and refers to bonds with a BBB- or higher credit rating. Investment-grade bonds are represented by the Bloomberg U.S. Aggregate Bond Index (the "Agg"). "HY" refers to "high yield" and refers to bonds with a credit rating below BBB-. High-yield bonds are represented by the Bloomberg U.S. Corporate High Yield Bond Index. You cannot invest in an Index, and past performance does not guarantee future results.

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Investors can generate higher levels of current nominal income in the bond market than in the equity market (which historically is the more "normal" situation). At the same time, we see increased risk in the fixed income markets and believe that dividends and stock buybacks may represent a more sustainable approach to generating current income.

Our own fixed income Model Portfolios remain short [duration](#) and over-weight in [credit](#), with an explicit focus on quality security selection, relative to the [Bloomberg U.S. Aggregate Bond Index \(the "Agg"\)](#). We are not looking to take excessive risk in our fixed income portfolios in a "reach for yield."

That said, here are some ideas and solutions that may be of interest.

Model Portfolio Ideas

WisdomTree manages four Model Portfolios we think fit nicely into today's yield environment, depending on investor objectives. From the most straightforward to the more complex, they are:

1. **The Short Duration Fixed Income Model Portfolio.** In June 2021, we launched our [Short Duration Fixed Income Model Portfolio](#), which is designed specifically to reduce interest rate (duration) risk while not sacrificing too much in terms of yield relative to the "Agg" Index. It can be used as a stand-alone fixed income Model Portfolio or a complementary sleeve to an existing fixed income allocation as a means of reducing duration risk without disrupting existing allocations. As we write this blog post (March 25th), the effective duration of the Short Duration Fixed Income Model Portfolio is approximately 2.77 years, and the current yield* is approximately 2.81%. This compares to an effective duration of roughly 5.65 years and a current yield of roughly 3.42% in our core Fixed Income Model Portfolio. So, investors are taking a modest reduction in yield to essentially reduce their duration risk by 50%.
2. **The Global Dividend Model Portfolio** is an all-equity model designed specifically to generate optimal yield and current income without taking excessive risk. This can be used as a stand-alone Model Portfolio, but many advisors use it as a complementary sleeve to their existing equity portfolios in an attempt to generate additional income.
3. **The Global Multi-Asset Income Model Portfolio** attempts to optimize risk-controlled current yield and income, but in addition to equities, it includes fixed income and other yield-generating strategies (e.g., preferred securities and energy master limited partnerships (MLPs)).

4. The Siegel-WisdomTree Longevity Model Portfolio. Built and managed in collaboration with our since-inception Senior Investment Strategy Advisor, Professor Jeremy Siegel, this Model Portfolio attempts to “build a better mousetrap” to the traditional [“60/40” portfolio](#) by over-weighting in yield and dividend-focused equities (75% allocation) while using the fixed income allocation (25%) as a source of risk-controlled income and a hedge to the equity risk of the overall portfolio.

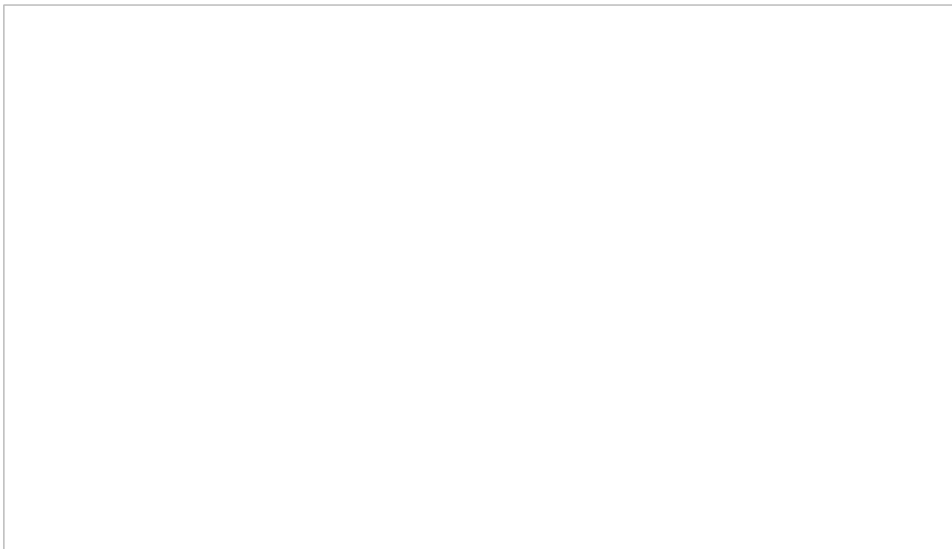
The last three Model Portfolios focus on generating all or much of their current yield from *equity* allocations versus fixed income allocations.

Let’s look at the current yield of these Model Portfolios (as of February 28, 2022).

Model Portfolio	Current Yield/Income*
Siegel-WisdomTree Longevity	3.34%
Global Dividend	3.02%
WisdomTree Global Multi-Asset Income (Moderate)	3.29%

Sources: WisdomTree and FactSet, as of 2/28/22. Past performance does not guarantee future results.

Now let’s examine some hypothetical “typical” client portfolios.



Conclusions

Today’s market environment is fraught with risks for fixed income investors. Despite the pick-up in nominal yields, we continue to believe that taking excessive risk in the fixed income market is not a prudent approach. We believe a more appropriate approach is to focus on the global equity markets to generate yield while still maintaining an adequate fixed income allocation, both to seek income generation and as a potential hedge to equity [beta](#) risk.

In today’s yield-starved world, we believe you can build intelligent portfolios that generate an optimal level of yield without taking excessive risk.

Financial advisors can register with wisdomTree to access fully transparent information (performance, fees, yield, allocations, etc.) via our [Model Adoption Center](#).

**“Current Yield/Income” refers to the Model Portfolio 12-month dividend yield, which is calculated using the weighted average trailing 12-month distribution yields of the Fund constituents. Funds incepted less than 12 months do not have a trailing 12-month dividend yield.*

Important Risks Related to this Article

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Investors and their advisors should consider the investment objectives, risks, charges and expenses of the funds included in any Model Portfolio carefully before investing. This and other information can be obtained in the Fund's prospectus by visiting www.wisdomtree.com for WisdomTree Funds. Visit the applicable third-party website for third-party funds. Please read the prospectus carefully before you invest. WisdomTree Asset Management, Inc., does not endorse and is not responsible or liable for any content or other materials made available by other ETF sponsors.

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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 Model Portfolio Investment Committee for the Siegel-WisdomTree Model Portfolios of WisdomTree, which develops and rebalances WisdomTree's Model Portfolios. In serving as an advisor 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 tailored to the concerns of any person.

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.

Related Blogs

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DEFINITIONS

Federal Reserve: The Federal Reserve System is the central banking system of the United States.

Rate Hike: refers to an increase in the policy rate set by a central bank. In the U.S., this generally refers to the Federal Funds Target Rate.

Inflation: Characterized by rising price levels.

Curve: Refers to the yield curve. Positioning on the yield curve is important to investors, especially during non-parallel shifts.

Real yield: the annual interest rate that an investor demands for holding a bond to maturity including the impact of inflation.

Nominal Treasury: Rate on the treasury security not adjusted for inflation.

Inverted Yield Curve: An interest rate environment in which long-term debt instruments have a lower yield than short-term debt instruments of the same credit quality.

Basis point: 1/100th of 1 percent.

Federal Open Market Committee (FOMC): The branch of the Federal Reserve Board that determines the direction of monetary policy.

Federal Funds Rate: The rate that banks that are members of the Federal Reserve system charge on overnight loans to one another. The Federal Open Market Committee sets this rate. Also referred to as the “policy rate” of the U.S. Federal Reserve.

Credit spread: The portion of a bond’s yield that compensates investors for taking credit risk.

Dividend yields: Refers to the trailing 12-month dividend yield. Dividends over the prior 12 months are added together and divided by the current share price. Higher values indicate more dividends are being generated per unit of share price.

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.

AA+ Credit Rating: The AA+ rating is issued by S&P and is similar to the Aa1 rating issued by Moody's. This rating is of high quality and falls below the AAA ranking. It comes with very low credit risk, even though long-term risks may affect these investments. The AA+ rating is considered one of the rankings for investment-grade debt.

Bloomberg U.S. Aggregate Bond Index: Represents the investment-grade, U.S. dollar-denominated, fixed-rate taxable bond market, including Treasuries, government-related and corporate securities, as well as mortgage and asset backed securities.

60/40 Portfolio: A portfolio of 60% equities and 40% fixed income.

Beta: A measure of the volatility of a security or a portfolio in comparison to a benchmark. In general, a beta less than 1 indicates that the investment is less volatile than the benchmark, while a beta more than 1 indicates that the investment is more volatile than the benchmark.

