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# LOOKING BACK AT EQUITY FACTORS IN Q3 2023 WITH WISDOMTREE

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After two quarters of strong equity performance, markets paused and reversed in the third quarter of the year. The [MSCI World Index](#) lost -3.5% over the quarter, despite gaining 3.4% in July. U.S. equities lost -3.2% and European equities lost -2.1%. Clearly, the change of tone at the [U.S. Federal Reserve \(“Fed”\)](#) played a role in that reversal. After 18 months of being laser-focused on fighting [inflation](#), the Fed is starting to balance the risk of inflation with the risk of over-tightening.

This installment of the [WisdomTree Quarterly Equity Factor Review](#) aims to shed some light on how equity factors behaved in this complicated quarter and how this may have impacted investors’ portfolios.

- [Value](#) and high [dividend](#) posted the strongest returns in developed and European markets.
- In the U.S., [quality](#) performed the strongest.
- Across those regions, [size](#) and [growth](#) suffered.
- In [emerging markets](#), the picture remains quite different from the rest of the world, with most factors outperforming and growth being the standout loser.

Looking to the end of 2023 and beyond, the equity outlook remains quite uncertain. Easy fiscal policy in the U.S. contributed to offset the impact of tightening [monetary policy](#) in 2023. We expect the breadth of the U.S. market to improve, favoring value and dividend stocks. Given the strong manufacturing headwinds facing Europe, we expect weak growth in the eurozone for the remainder of 2023, favoring a tilt toward defensive stocks.

## Performance in Focus: Has the 2023 Bull Run Come to an End?

Despite good performance in July, Q3 saw markets reverse course and post negative returns. After leading for the first seven months of the year, tech mega caps underperformed markets in July and August.

Q3 ended up being a more favorable period for factor investing in developed markets:

- In global developed markets, value and high dividend posted the strongest returns after two difficult quarters.
- In the U.S., quality posted the best return, followed by min [volatility](#), value and high dividend outperformance.
- Size and growth suffered in both developed European and U.S. markets, posting underperformance.
- In Europe, high dividend and value also posted the strongest returns. However, growth and quality underperformed.

- In emerging markets, size continues to dominate, but like in previous quarters, most factors were able to produce outperformance over the quarter. Growth was the standout loser in the region.

Figure 1: Equity Factor Outperformance in Q3 2023 across Regions

	World Q3 2023: -3.5%	USA Q3 2023: -3.2%	Europe Q3 2023: -2.1%	Emerging Markets Q3 2023: -2.9%
High Dividend	1.8%	0.9%	3.8%	3.8%
Minimum Volatility	0.5%	1.0%	0.0%	0.8%
Momentum	0.4%	0.3%	-0.3%	2.3%
Quality	0.6%	1.7%	-1.9%	3.6%
WisdomTree Quality	-1.7%	-1.4%	-0.7%	2.2%
Size	-0.9%	-1.8%	-0.7%	5.9%
Value	3.1%	0.5%	2.4%	0.8%
Growth	-1.4%	-0.3%	-4.2%	-5.7%

Sources: WisdomTree, Bloomberg, 6/30/23-9/30/23. Calculated in U.S. dollars for all regions except Europe, where calculations are in euros. Past performance is not indicative of future results.

### 2023 Has Been Very Consistent Factor-Wise

Looking back at the full year, July and August were not enough to change the overall picture. Growth and quality are the stand-out winners in developed and U.S. markets. All other factors underperformed, with double-digit underperformance for most of them. European markets look quite different, with value dominating and the only factor to outperform. In contrast, growth stocks underperformed for the year. As discussed recently in our equity outlook for 2024, the fundamental difference is that the U.S. is mostly a service-driven economy that benefited from consumer strength in 2023 on the back of strong wage growth, increasing credit card debt and the spending of pandemic savings. Europe, by contrast, is a manufacturing-driven economy that suffered from a weak reopening of the Chinese economy and is now facing the consequences of monetary tightening.

In emerging markets, all factors but momentum did quite well in 2023. Small cap posted the strongest returns, followed by value.

Figure 2: Equity Factor Outperformance in 2023 across Regions

	World YTD: 11.1%	USA YTD: 13.1%	Europe YTD: 8.8%	Emerging Markets YTD: 1.8%
High Dividend	-9.1%	-15.2%	-0.7%	6.6%
Minimum Volatility	-10.4%	-11.7%	-2.2%	0.8%
Momentum	-11.4%	-16.4%	-2.3%	-2.4%
Quality	6.6%	8.1%	-1.8%	1.1%
WisdomTree Quality	-4.9%	-6.7%	-0.1%	4.7%
Size	-8.2%	-9.5%	-6.1%	11.9%
Value	-0.8%	-11.9%	1.3%	7.3%
Growth	9.8%	15.8%	-1.6%	6.9%

Sources: WisdomTree, Bloomberg, 12/31/22-9/30/23. Calculated in U.S. dollars for all regions except Europe, where calculations are in euros. Past performance is not indicative of future results.

### Valuations Decreased in Q3

In Q3 2023, developed markets got less expensive. Most factors saw the price-to-earnings ratio decline over the quarter. Growth saw the biggest decrease across regions, followed by [momentum](#). In emerging markets, however, valuations increased, with momentum [P/E](#) gaining 2.9 and size gaining 2.4. Growth, on the contrary, got cheaper.

Figure 3: Historical Evolution of Price-to-Earnings Ratios of Equity Factors

	World		USA		Europe		Emerging Markets	
	P/E Ratio	Δ3Months	P/E Ratio	Δ3Months	P/E Ratio	Δ3Months	P/E Ratio	Δ3Months
Market	17.5	↓ -0.5	19.7	↓ -0.7	12.8	↓ -0.4	13.3	↑ 0.1
High Dividend	13.2	↑ 0.0	14.8	↓ -0.2	10.1	↑ 0.1	8.2	↑ 0.2
Minimum Volatility	17.2	↓ -0.3	18.3	↓ -0.2	15.9	↓ -0.4	14.3	↓ -0.1
Momentum	18.5	↓ -0.7	23.2	↓ -1.5	14.3	↓ -0.7	12.3	↑ 2.9
Quality	22.1	↓ -0.2	23.0	↓ -0.1	18.0	↓ -0.6	17.1	↑ 1.7
Size	17.4	↑ 0.1	20.6	↑ 0.1	13.0	↑ 0.1	15.3	↑ 2.4
Value	9.5	↓ -0.1	6.9	↓ -0.3	7.9	↓ -0.2	6.4	↑ 0.0
Growth	26.2	↓ -1.2	28.8	↓ -1.7	21.5	↓ -1.6	21.5	↓ -2.2

Sources: WisdomTree, Bloomberg, as of 9/30/23. Past performance is not indicative of future results. "World" is proxied by the MSCI World net TR Index. "USA" is proxied by the MSCI USA net TR Index. "Europe" is proxied by the MSCI Europe net TR Index. "Emerging Markets" is proxied by the MSCI Emerging Markets net TR Index. "Minimum Volatility" is proxied by the relevant MSCI Min Volatility net total return Index. "Quality" is proxied by the relevant MSCI Quality net total return Index. "Momentum" is proxied by the relevant MSCI Momentum net total return Index. "High Dividend" is proxied by the relevant MSCI High Dividend net total return Index. "Size" is proxied by the relevant MSCI Small Cap net total return Index. "Value" is proxied by the relevant MSCI Enhanced Value net total return Index. "WisdomTree Quality" is proxied by the relevant WisdomTree Quality Dividend Growth Index.

### Q4 and Beyond

Positive economic surprises helped push markets higher in the first seven months of the year. However, looking ahead, the outlook remains more uncertain. Easy fiscal policy in the U.S. helped offset the impact of tightening monetary policy. We expect the breadth of the market to improve, favoring value and dividend stocks. Given the strong manufacturing headwinds facing Europe, we expect weak growth in the eurozone for the remainder of 2023, favoring a tilt toward defensive stocks.

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## DEFINITIONS

**MSCI world Index**: Captures large and mid-cap representation across 23 Developed Markets (DM) countries.

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

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

**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.

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

**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.

**Size**: Characterized by smaller companies rather than larger companies by market capitalization. This term is also related to the Size Factor, which associates smaller market-cap stocks with excess returns vs the market over time.

**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.

**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.

**Monetary policy**: Actions of a central bank or other regulatory committee that determine the size and rate of growth of the money supply, which in turn affects interest rates.

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

**Momentum**: Characterized by assets with recent price increase trends over time. This term is also associated with the Momentum Factor which associates these stock characteristics with excess return vs the market over time.

**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.