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WisdomTree Europe

Is the Traditional 60/40 Dead? Redefining Diversification with Efficient Core Solutions

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March 2025

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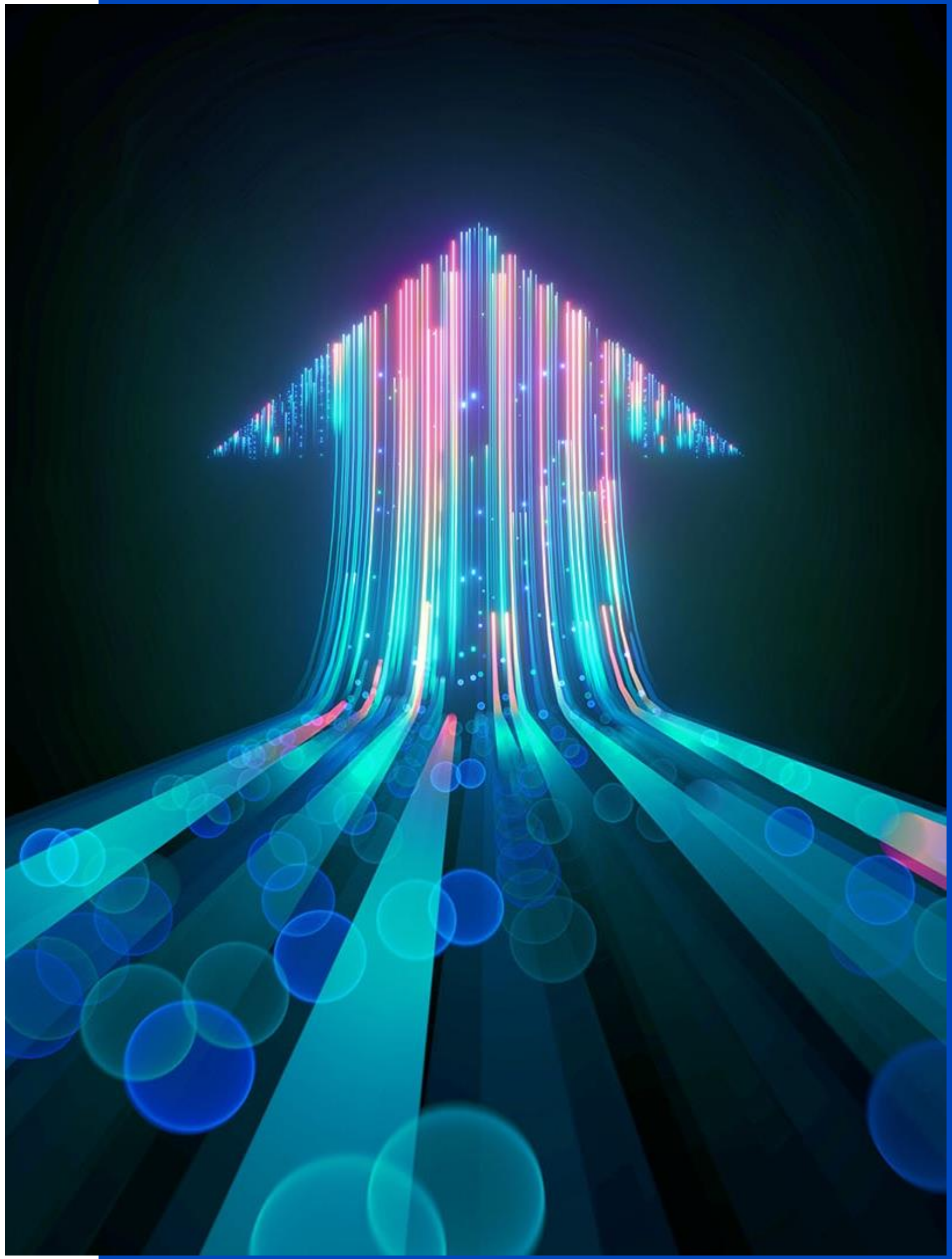
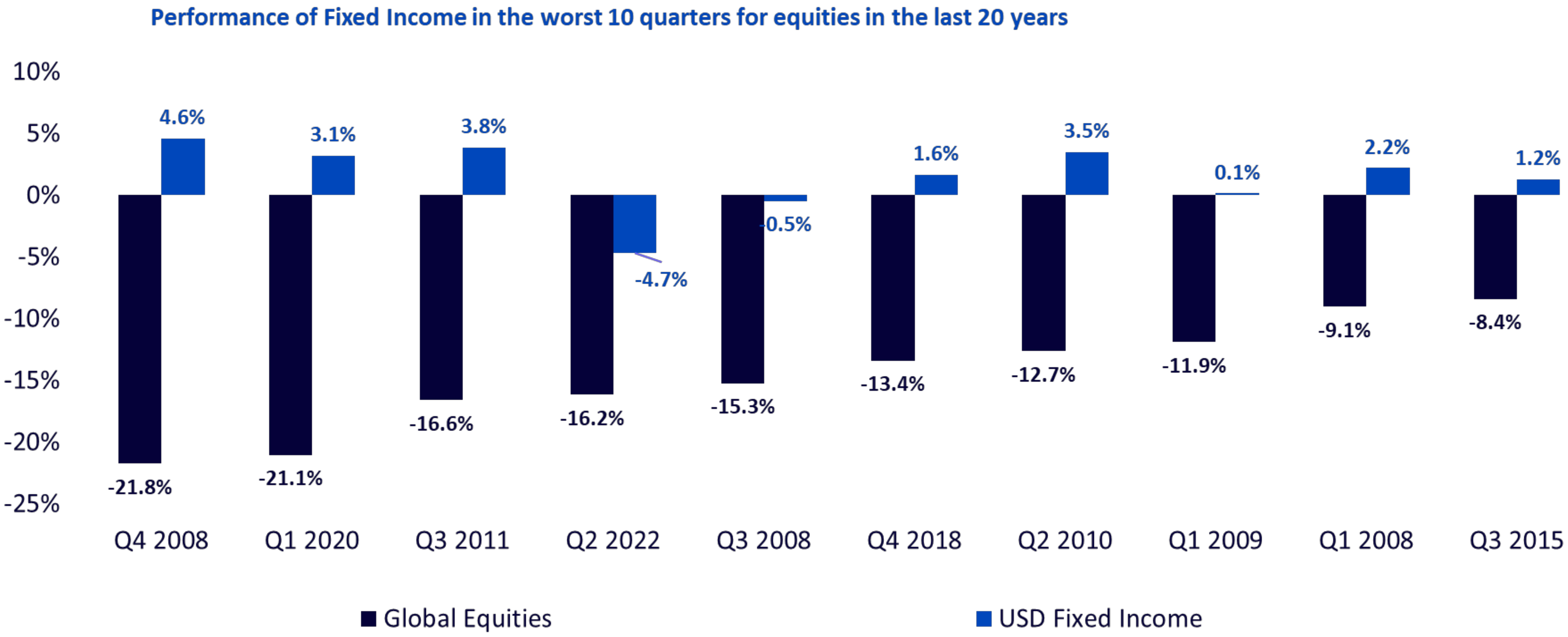


1.

Is the 60/40 still relevant today?

Equity and Bonds behave differently. Bonds can help when equities suffer



Source: Bloomberg, WisdomTree. 31st December 2004 to 31st December 2024. Quarterly data in USD. Global equities = MSCI World TR, USD Fixed Income= Bloomberg US Aggregate TR. **Historical performance is not an indication of future performance and any investments may go down in value..**

The origin of the 60/40 Portfolio
A multi-asset portfolio can reduce the impact of market volatility

- The 60/40 portfolio emerged as a response to the need for a balanced approach to portfolio construction that could provide both capital appreciation and risk mitigation.
- The 60/40 portfolio benefits from the fact that equity and bonds behave differently across the business cycle leading to low correlation between the 2 assets.
- The diversification effect between two assets with low correlation results in the volatility of the portfolio being reduced.

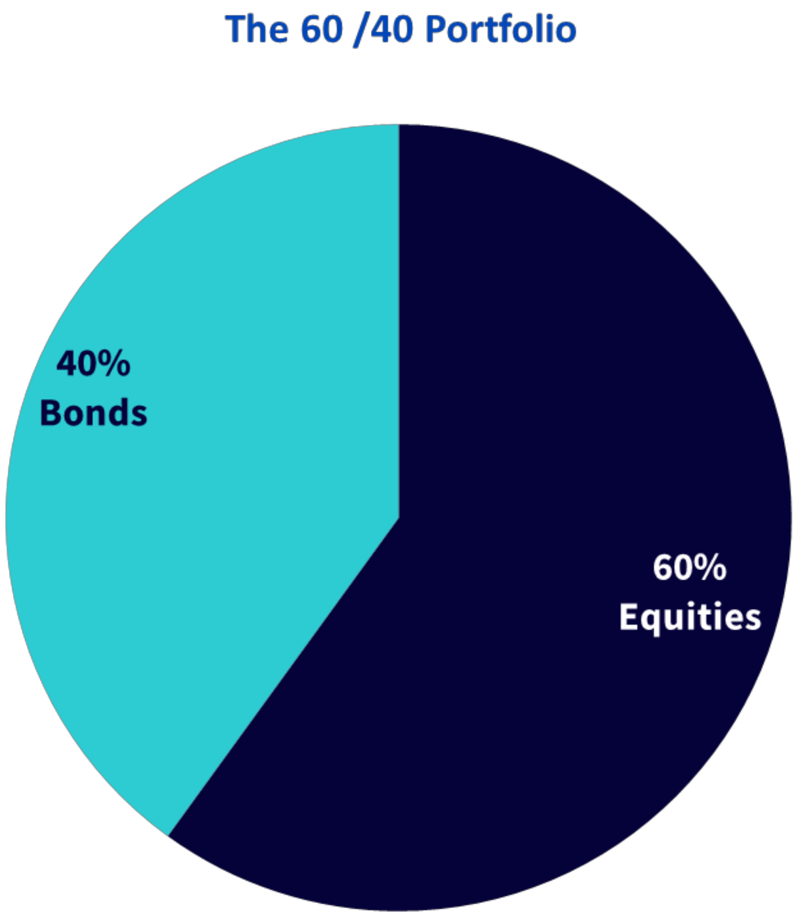


Illustration Only

The limits of the 60/40 in today's world
The risk balance is better but the long term returns are lower

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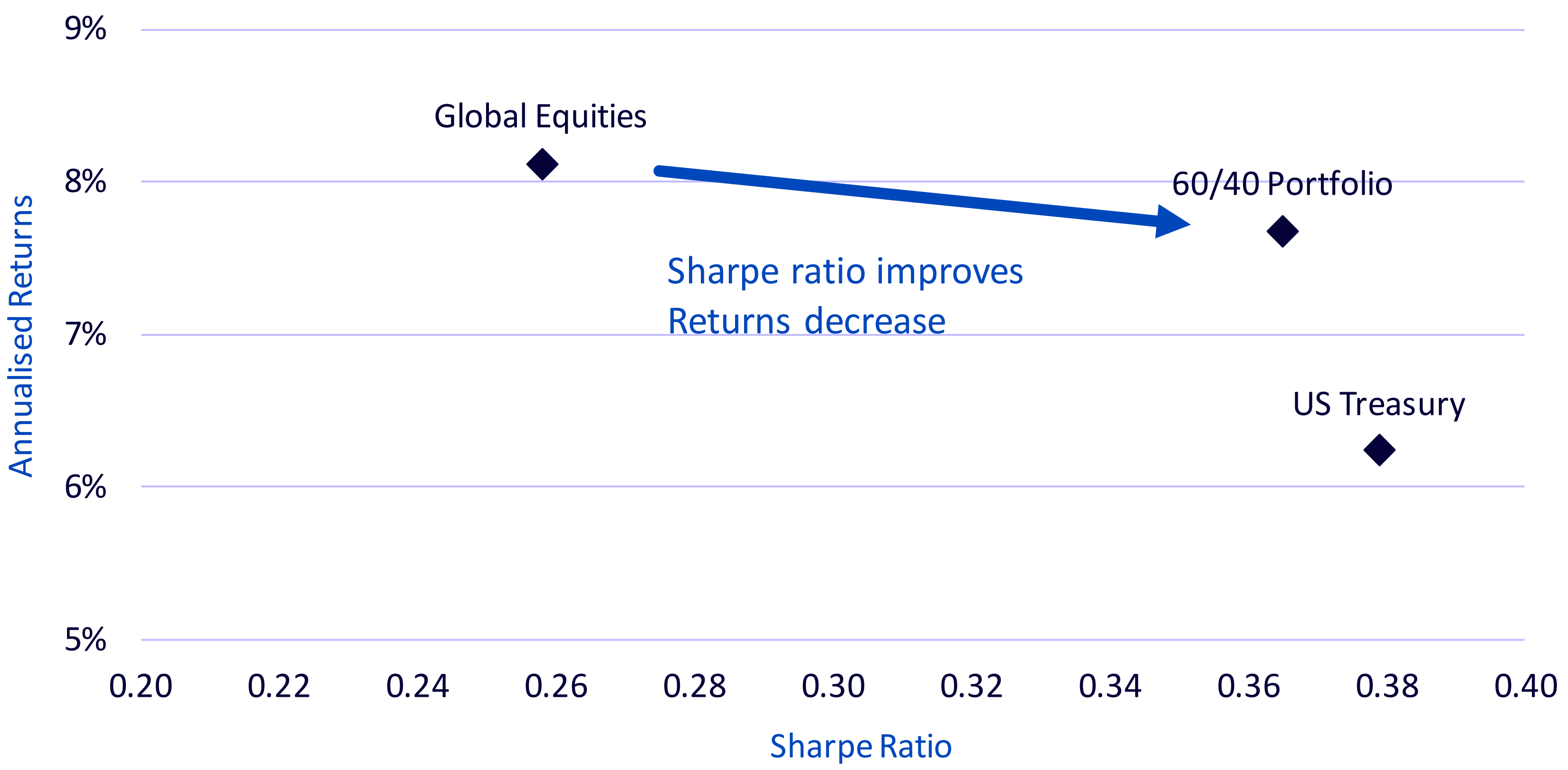
+ Whether saving for retirement or a future home, investors are typically looking for strong returns, without taking on too much risk.

+ Investing in a 60/40 portfolio does lower risks but also lowers returns and therefore may not be sufficient to create enough growth to fund investors' goals.

Long Term Returns and Sharpe Ratios of Global Assets



Source: Morningstar Ibbotson, Bloomberg, WisdomTree. As of 31st January 2025. Monthly data in USD. Analysis started on 31st January 1973. Global equities = MSCI World TR, government Bonds = Bloomberg US Treasury TR. **Historical performance is not an indication of future performance and any investments may go down in value..**

The limits of the 60/40 in today's world

Many asset classes are now available easily to investors. The 60/40 does not have space for them

+ Diversification is the only free lunch in investing
+ Nowadays, investors have access to a large range of diversifiers:
  - Broad Commodities
  - Gold
  - Real Estate
  - Infrastructure
  - Hedge Funds
  - Alternatives
+ Modern portfolio construction indicates that using many of those would lead to better overall results but that means creating space for them in the portfolio

2.

An Innovative concept: A new era of smart portfolio construction

AQR's C. Asness' Thought Experiment

An out-of-the-box solution to the Portfolio Paradox

C. Asness proposed a solution in "Why Not 100% Equities".

Asness shows how the use of leverage, when applied to a traditional 60/40 strategy, could achieve a similar volatility of the 100% equity exposure but could help improve the return.

In this analysis, the Levered 60/40 is composed of 155% exposure to the 60/40 portfolio and the cost of financing is proxied by the one-month t-bill rate

Foundational results from "Why Not 100% Equities" – 1926 - 1993

EXHIBIT 3
Effect of Leverage (%)

Portfolio	Compound Return	Standard Deviation
100% Stocks	10.3	20.0
100% Bonds	5.6	6.8
60% Stocks, 40% Bonds	8.9	12.9
Levered 60/40	11.1	20.0

Stocks are represented by the S&P 500. Bonds are represented by the Ibbotson total return series for long-term corporates. The 60/40 portfolio is a combination of 60% the S&P 500 and 40% long-term corporates, rebalanced back to 60/40 every month. The levered 60/40 portfolio invests 155% each month in the 60/40 portfolio, and –55% each month in the one-month T-bill.

A diversified portfolio provides more expected return per unit of risk

Clifford S. Asness
Founder, Managing Principal and Chief Investment Officer at AQR Capital Management

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Source: The Journal of Portfolio Management. Volume 22 Number 2. Winter 1996

An Innovative concept
A new era of smart portfolio construction

Better than 100% equities?

The illustrative Strategy would aim to deliver:

- 90% exposure to large-cap equities
- 60% to government bond Futures

Many advantages:

- **Enhanced risk-adjusted return** while preserving broad exposure to equities
- **Reduced drawdowns** via a government bond futures overlay
- **Improved** capital efficiency, allowing for allocations in alternatives and diversifiers

A low-fee, Core, equity solution

- A core equity exposure offering return enhancement, improved risk management and diversification potential compared to a 100% equity portfolio.
- A low fee, core equity solution designed to replace existing core passive or active equity exposures.

A capital efficient tool

- A unique and innovative strategy to increase portfolio efficiency
- By delivering equity and bond exposure in a capital-efficient manner, the strategy can free up space in the portfolio for alternatives and diversifiers.

Illustrative Strategies
3 Key Exposures

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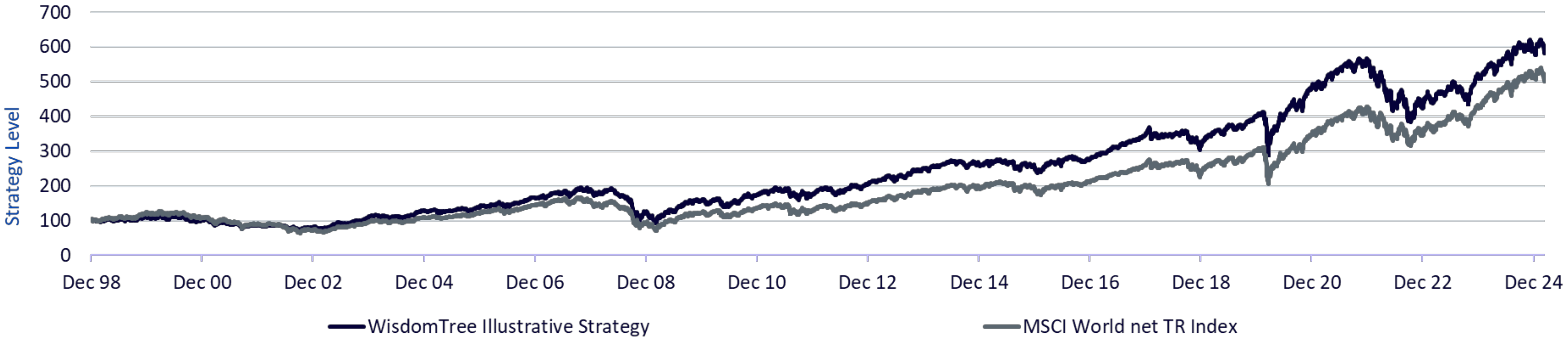
01	02	03
90% Large Cap Equities	**60% Government bond Future Contracts**	**10% Cash Collateral**
The strategy would invest in an ESG diversified basket of large capitalisation companies.	The strategy would invest in a diversified basket of government bond futures contracts with maturities ranging from 2 to 30 year. + Currency weight matches the weight in equity + Quarterly rolled	The strategy would have roughly 10% exposure in cash, which serves as collateral for the government bond future contracts.

Rebalancing

The strategy is rebalanced on a quarterly basis on the last business day of February, May, August and November.
If Equity or Bond exposure deviates by more than 5% between rebalancing dates, the index will rebalance back to target weights.

WisdomTree Illustrative Strategy
Illustrative Backtest (without the ESG Filter)



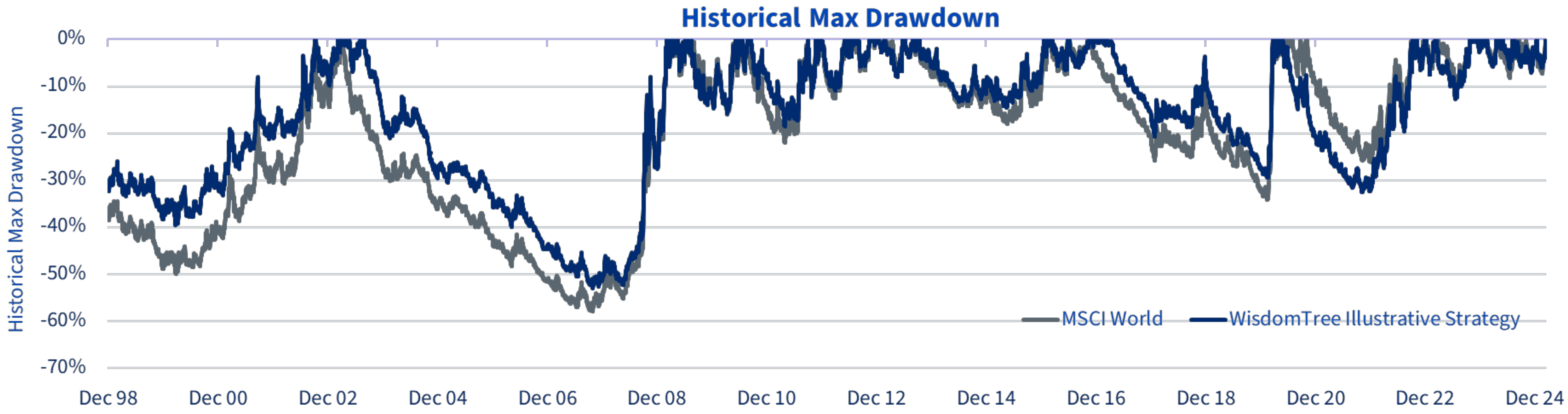
	WisdomTree Illustrative Strategy	MSCI World net TR
Total Return (Annualised)	7.0%	6.4%
Standard Deviation (annualised)	15.0%	16.2%
Daily VaR 95%	-1.4%	-1.6%
Tracking Error (Annualised)	4.2%	
Sharpe Ratio	0.33	0.27
Information Ratio	0.14	
Beta (ex post)	89.3%	100.0%
Correlation	96.6%	

Source: Bloomberg, WisdomTree. From December 1998 to 31st January 2025. Daily data in USD. **Backtest Data has been used. Historical performance is not an indication of future performance and any investments may go down in value.**

Reduced Historical Max Drawdown

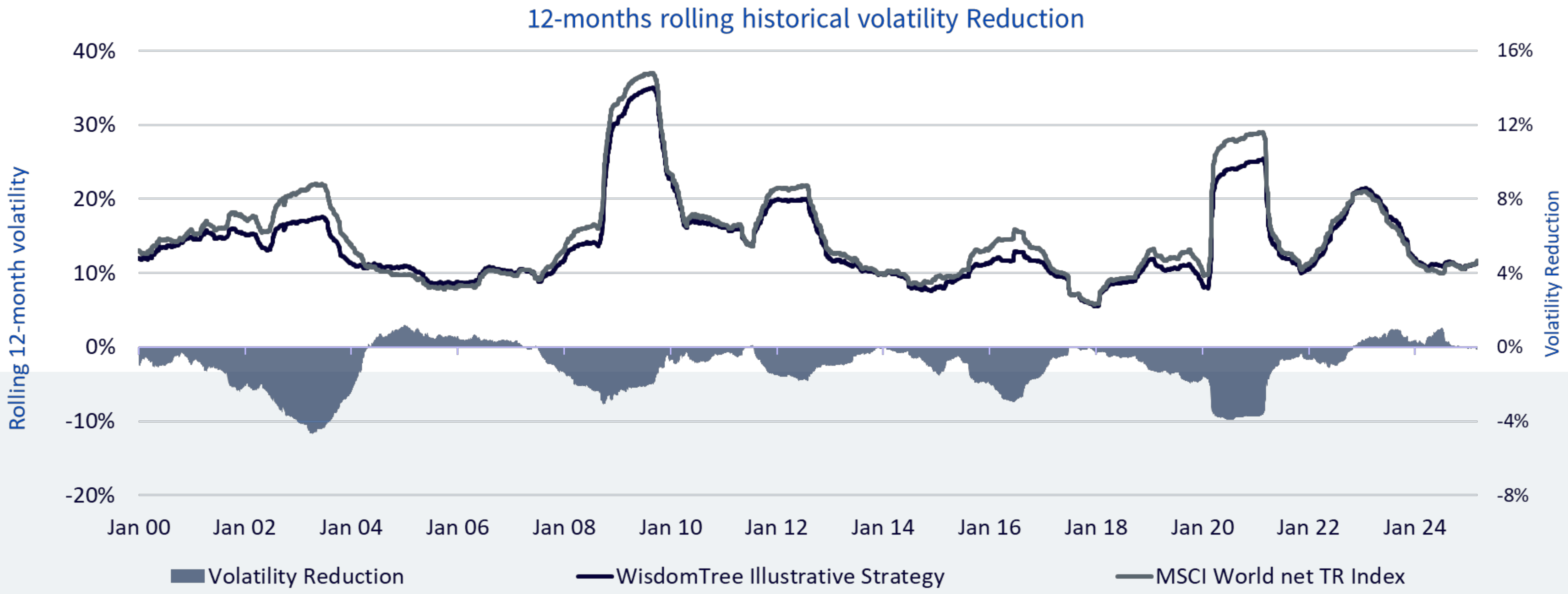
Reduced Drawdown in 2001, 2008 and 2020

Drawdowns are significantly reduced in the main crisis historically, with the exception of 2022.



Source: Bloomberg, WisdomTree. From December 1998 to 31st January 2025. Daily data in USD. **Backtest Data has been used. Historical performance is not an indication of future performance and any investments may go down in value.**

Consistent volatility reduction versus Global Equities



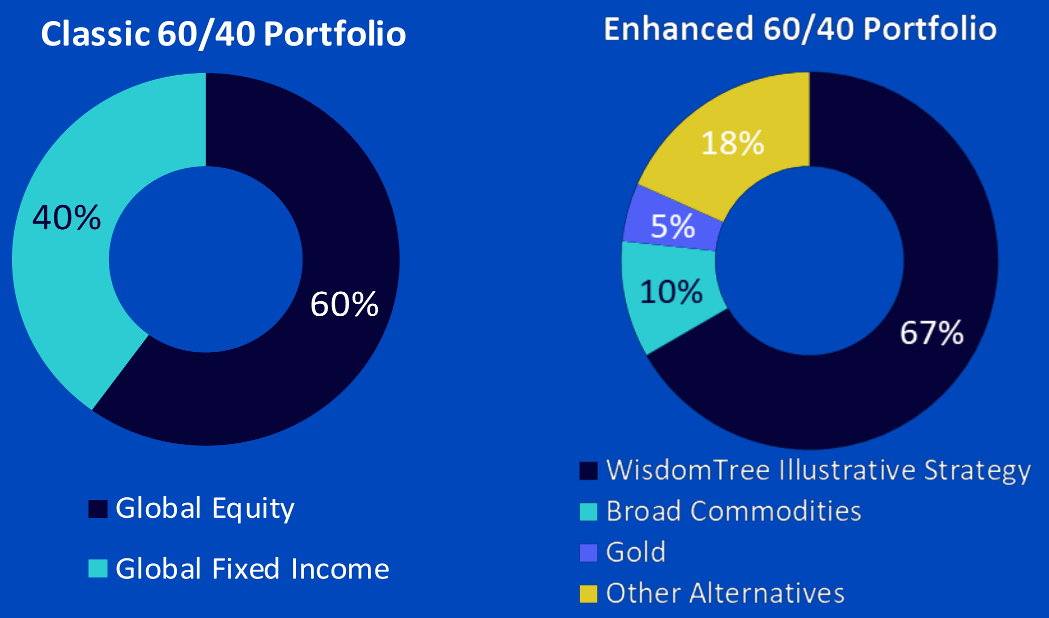
Source: Bloomberg, WisdomTree. From December 1998 to 31st January 2025. Daily data in USD. **Backtest Data has been used. Historical performance is not an indication of future performance and any investments may go down in value.**

In a portfolio: Improving asset allocation via capital efficiency

A capital efficiency tool

WisdomTree Illustrative Strategy can help free up space in portfolios for alternatives and diversifiers.

As an illustrative example, by allocating 10% of a portfolio to this concept, investors would get 9% exposure to Global equities and 6% exposure to government bonds, freeing 5% to invest in alternative assets.



Source: Bloomberg, WisdomTree. From December 1998 to January 2025. Daily data in USD.
Historical performance is not an indication of future performance and any investments may go down in value.

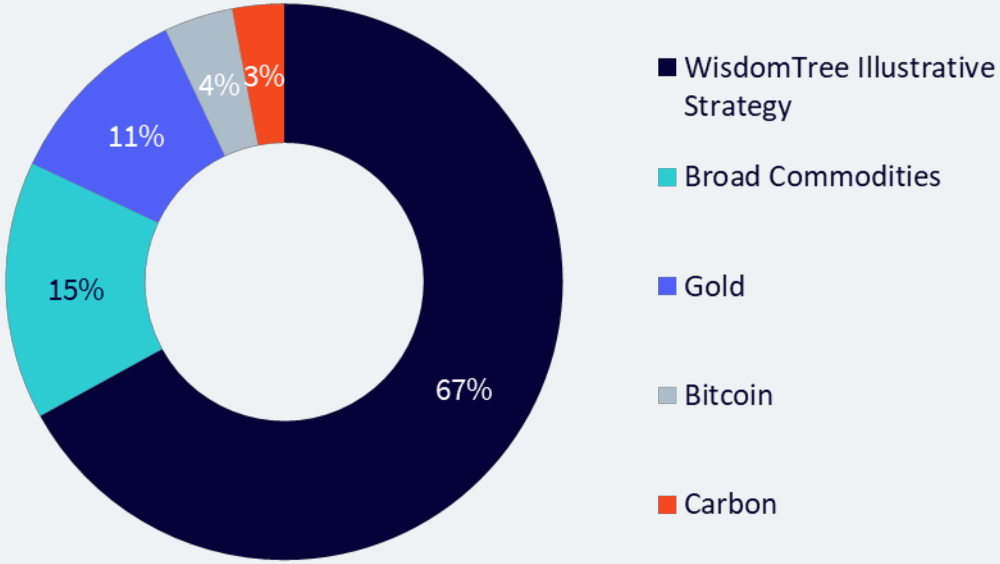
Illustrative Model Portfolio

Creating Space with this new concept

Using this new concept in portfolios creates a big difference between capital allocation and exposure

+ With 40% capital allocation to WisdomTree Illustrative Strategy, 60% of equity and bond exposure are created.
+ This creates 20% of space for alternatives and diversifiers.

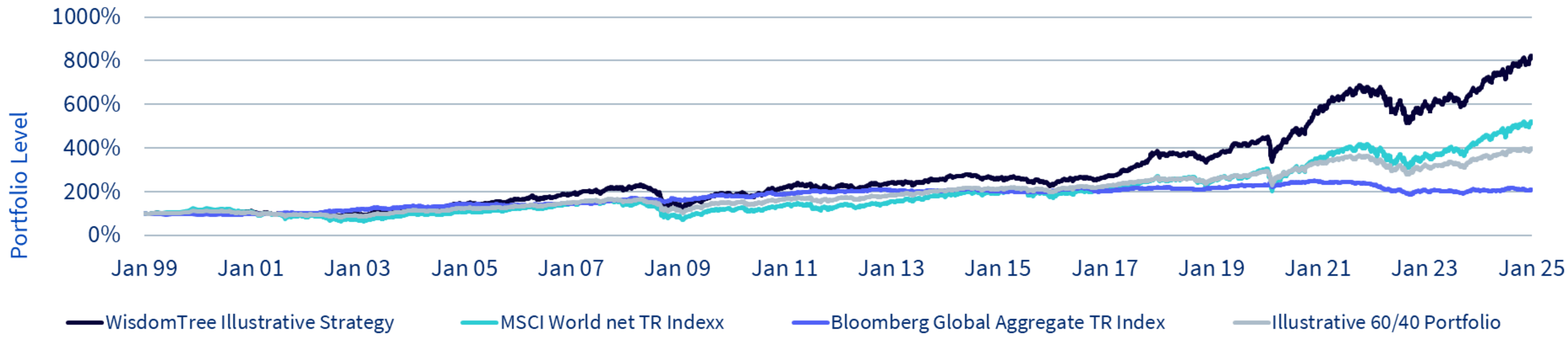
Capital Allocation



	Capital Allocation	Exposures			
		Equity	Fixed Income	Commodities	Digital Assets
WisdomTree Illustrative Strategy	67%	60%	40%		
Broad Commodities	15%			15%	
Gold	11%			11%	
Bitcoin	4%				4%
Carbon	3%			3%	
Total	**100%**	**60%**	**40%**	**29%**	**4%**

Source: WisdomTree. Illustrative Only

Illustrative Model Portfolio



	WisdomTree Illustrative Strategy	Illustrative 60/40 Portfolio	MSCI World net TR Indexx	Bloomberg Global Aggregate TR Index
Annualised Returns	8.41%	5.42%	6.53%	2.85%
Annualised Volatility	13.06%	10.17%	16.58%	5.60%
Sharpe Ratio	0.49	0.34	0.28	0.16
Max Drawdown	-47.3%	-39.0%	-57.8%	-25.7%

Source: Bloomberg, WisdomTree. From January 2002 to 31st January 2025. Daily data in USD. **Backtest Data has been used. Historical performance is not an indication of future performance and any investments may go down in value.**

In Summary

Benefit from Diversification without lowering long-term returns

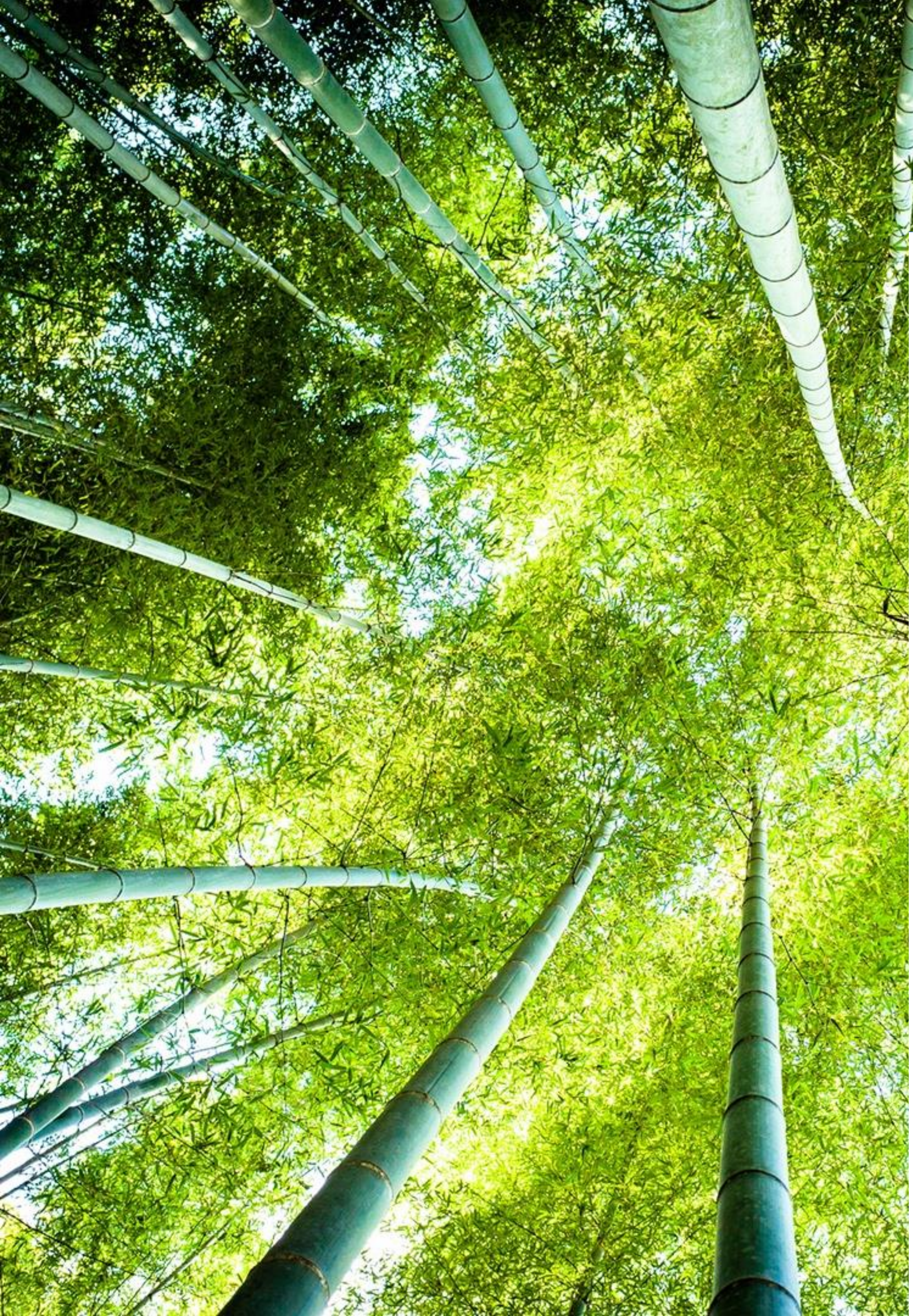
Diversification increases risk-adjusted returns of the portfolio

Aim for higher returns and higher Sharpe ratio

Investing in a levered portfolio with high Sharpe ratio portfolio allows to benefit from the diversification without reducing long-term returns

Improve portfolio diversification

Leverage creates capital efficiency which in turn creates space for diversifiers such as alternatives, commodities, and crypto in the portfolio



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Thank you.

For more information, please visit:

WisdomTree.eu/Efficient-Core

Questions

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wisdomtree.eu/global-quality-dividend-growth

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ETPedia

The educational guide to Exchange Traded Products (ETPs)

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