
WISDOMTREE QUARTERLY THEMATIC REVIEW: SEEING THE GLASS HALF-FULL

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2022 was a tumultuous year for equity markets, shaped by macro and geopolitical factors. Monetary tightening that started with the Federal Reserve (Fed) in the United States spread to other regions. The war in Ukraine and zero-COVID policy in China added further pressure to the global growth outlook, elevating fears of recession. In this general risk-off environment, we have seen global rotation into value stocks. Thematics, being the new face of growth, felt more pain in this rotation. Thematic assets in Europe lost 26% from their peak (as of 31 December 2021), driven by the negative performance move of 28.9%, as flows in contrast remained positive at \$12.1 billion for the year¹.

Buoyed by the positive performance move in Q4, thematic assets in Europe rebounded from the previous quarter to \$283.4 billion. Aided by positive returns throughout October and November, Q4 was the only quarter in 2022 when assets in both exchange-traded funds (ETFs) and open-ended funds experienced a positive performance impact of around 7%-7.5%. In total, 15 themes beat the broad global equity benchmark, MSCI ACWI, as November saw optimism prevailing in the equity markets on the back of cooler Consumer Price Index (CPI) data and a resilient job market. In contrast, a more hawkish Fed outlook in the FOMC meeting, alongside some signs of a weakening US economy, weighed on the markets in December. Net flows in Q4 were subdued, but continued to remain positive with \$1.5 billion assets gathered across both wrappers.

Performance-wise, 2022 was an ugly year for growth stocks and even more so for thematic strategies. Nevertheless, three themes managed to outperform MSCI ACWI that dropped 18.36%, with the best performing theme showing 8.2% return differential against the benchmark. Notably, in such a difficult year, thematic ETFs in Europe captured 48% of flows that went into open-ended funds with only 12.2% share of the European thematic market at the end of 2021. Thematic launches were defying the performance downturn as the pipeline of newly introduced strategies broke the record in ETFs and was only 14 strategies behind last year's figure across both wrappers.

In this quarterly thematic review, we will look at the space and analyse the fourth quarter, as well as the full 2022 through the lens of performance, flows, and new launches. For all of our calculations, we will use the [WisdomTree Thematic Classification](#) that we have previously introduced in a series of blogs in which we discussed [how to classify](#) and [select thematic funds](#). More insights on the thematic space in Europe can be found in our [quarterly thematic update](#).

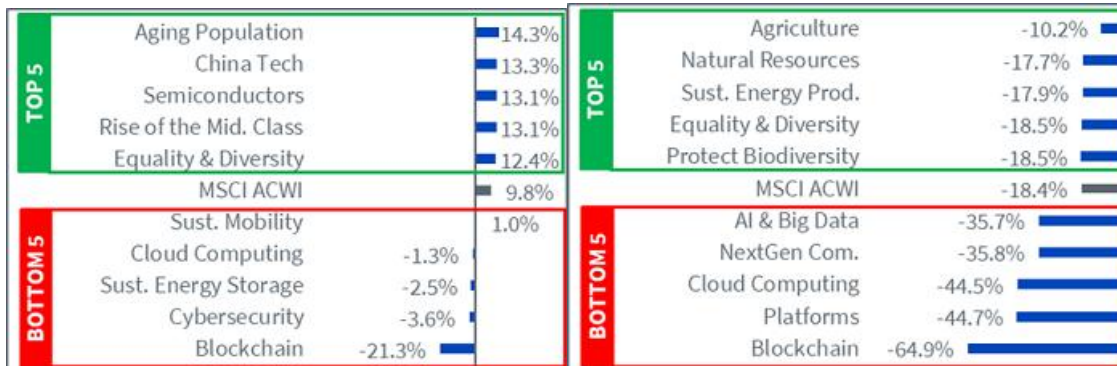
Winners and losers

As noted in our research paper on [thematic investments](#), themes tend to rotate in flows and performance over time due to their individual narratives. Our quarterly tracking of theme returns shows no lack of evidence in the performance rotation. China-centred themes were one example in 2022, while tech-focused growth themes, more sensitive to the changes in interest rates, were another. Thus, the ‘Blockchain’ theme, after claiming top in Q3 with 2.8% return, fell to the bottom in Q4 with -21.3% return respectively.

In comparison to Q3, more themes managed to beat MSCI ACWI in Q4: 15 vs. 11. However, dispersion in performance between themes and between strategies inside themes remained elevated. Themes from the ‘Demographic and Social Shifts’ made a notable appearance in the top 5 with ‘Aging Population’ leading the pack. Q4 was the only quarter in 2022 when ‘green’ themes did not make it to the top 5. After a dismal Q3, ‘China Tech’ posted a strong return of 13.3%, claiming second place. Following a 2-month rebound streak from its year-to-date bottom in October, ‘Semiconductors’ clawed back some losses posted in 2022, delivering the third strongest return in Q4 at 13.1%.

The bottom 5 themes continued to be dominated by the tech-focused themes showing higher sensitivity to interest rate changes. In Q4, ‘Blockchain’ suffered another blow with the collapse of FTX. Cybersecurity stocks were hurt by longer sales cycles and slowing demand, especially from the mid- and small-sized businesses, revealing that the space is not as immune to the recessionary risks. Green themes such as ‘Sustainable Mobility’ and ‘Sustainable Energy Storage’ made a surprising appearance in the bottom 5, most likely impacted by the concerns over economic slowdown and softening demand for electric vehicles (EVs), especially in light of a looming end of a decade-long EV subsidy in China at the start of 2023.

Figure 1. Q4 (left) and 2022 (right) performance of the top 5 and the bottom 5 themes vs MSCI ACWI



Source: WisdomTree, Morningstar, Bloomberg. All data as of 30 December 2022 and based on WisdomTree's internal classification of thematic funds. Performance is based on monthly returns from Morningstar. Please refer to Footnote 1 for the details around the calculation of performance for a given theme.

Historical performance is not an indication of future performance, and any investments may go down in value.

Q4 performance hasn't changed the ranking of the top three losing themes on a year-to-date basis – ‘Blockchain’, ‘Platforms & Digital Markets’ and ‘Cloud Computing’ claimed the title for the year. ‘Blockchain’ was hurt by a series of high-profile events happening in the cryptocurrency space in 2022, such as the Terra-Luna crisis, the blow-up of Three Arrows Capital and, most recently, FTX's collapse. Cloud Computing stocks, largely characterised by higher revenue growth rates and negative profits, were hurt by interest rate hikes, resulting in a heavier discount of companies' future cash flows and lower present value. Aside from the general macro factors, the ‘Platforms & Digital

Markets’ theme suffered from slowing online spending and consumers heading back to brick-and-mortar.

Only three themes beat MSCI ACWI in 2022, which goes to show the depth of the correction in the space and its sensitivity to interest rate hikes. On the bright side, it is worth highlighting the temporary nature of the macro headwinds that drove underperformance across many themes. We expect a stronger response in the space, with the general risk-on sentiment returning to the markets. Another positive sign lies in the magnitude of outperformance posted by the top-performing theme vs. MSCI ACWI. ‘Agriculture’, which drew a lot of attention amidst food supply chain disruptions and shortages caused by the war in Ukraine, returned 8.2% in excess of MSCI ACWI in 2022.

Flows subdued but remain positive

Despite continued pressure on growth stocks, net flows into thematics have remained positive in Q4, with \$1.5 billion across ETFs and open-ended funds. That makes four quarters of positive flows for 2022, totalling \$12.1 billion, despite the general risk-off environment.

‘Green’ themes dominated flows in open-ended funds in Q4, with 4 themes in the top 5 flow gatherers raising more than \$0.6 billion. ‘Artificial Intelligence & Big Data’ is the only standout in that top 5. In ETFs, Technological themes fared better, with ‘Cybersecurity’ gathering the most flows and ‘Semiconductors’ in fourth place. Jointly, these three themes gathered around \$0.5 billion across both wrappers.

Technological themes generally continued to remain out of favour with net negative flows of -\$0.6 billion in Q4. ‘Robotics & Automation’ and ‘HealthTech’ were the common denominators in the top outflows across both ETFs and open-ended funds.

Looking back at 2022, the ‘Environmental Pressures’ themes have dominated the thematic space, delivering the best performance and raising the most assets with more than \$14.6 billion of net flows. ‘Climate Change and Sustainability’ themes continued to resonate the most with investors and have gathered the bulk of the flows in Europe with \$12.9 billion inflows year-to-date and \$2.26 billion in Q4. This highlights the role thematic investing might play in financing the transition to a low- or zero-carbon world, especially against the backdrop of a year that hasn’t favoured innovative emerging companies.

Figure 2. Q4 (top) and 2022 (bottom) flows in Europe of the top 5 and the bottom 5 themes - ETFs (dark blue) vs open-ended (OE) funds (teal)

| | | | | | |
|-----------------|----------------------|-------|-----------------|----------------------|--------|
| TOP 5 | Cybersecurity | \$144 | TOP 5 | Sust. Energy Prod. | \$230 |
| | Sust. Resource Mgt | \$104 | | AI & Big Data | \$217 |
| | Protect Biodiversity | \$97 | | Sust. Food | \$201 |
| | Semiconductors | \$87 | | Sust. Resource Mgt | \$112 |
| | Natural Resources | \$65 | | Natural Resources | \$94 |
| | | | | | |
| BOTTOM 5 | Blockchain | -\$32 | BOTTOM 5 | Fintech | -\$117 |
| | Equality & Diversity | -\$55 | | HealthTech | -\$117 |
| | Sust. Energy Storage | -\$64 | | Aging Population | -\$146 |
| | HealthTech | -\$66 | | Equality & Diversity | -\$233 |
| | Robotic & Automat. | -\$77 | | Robotic & Automat. | -\$366 |
| | | | | | |



Source: WisdomTree, Morningstar, Bloomberg. All data as of 30 December 2022. Data based on WisdomTree's internal classification of thematic funds.

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At the theme level, in 2022, 'Sustainable Energy Production' continued to dominate flows with \$1.6 billion in ETFs and \$2.3 billion in mutual funds. Other 'green' themes that regularly appeared in the top 5 and gathered flows above \$1 billion each were 'Sustainable Resource Management', 'Sustainable Food' and 'Agriculture'. In a difficult year for tech, 'Cybersecurity', 'Semiconductors' and 'Artificial Intelligence & Big Data' still gathered \$1.1 billion, \$366 million and \$218 million respectively.

The bottom 5 themes by net flows in 2022 are mostly represented by tech-focused themes. 'Fintech & Digitalisation of Finance', 'Robotics & Automation', 'HealthTech' and 'Digital Health' all saw around \$1 billion of outflows.

Overall, we saw positive flows across 20 out of 37 themes that we interpret as a sign of thematic allocations for the long term. Moreover, flows into ETFs remained positive across all four clusters in our thematic classification, in contrast to open-ended funds that saw outflows in the 'Technological Shifts' and the 'Demographic & Social Shifts' clusters. This was especially true in the 'Equality, Inclusion & Diversity' theme.

ETF launches breaking another record

Asset managers continued to grow thematic offerings in Europe, suggesting they see the potential of increasing adoption of thematic strategies in investors' portfolios.

Despite a slowdown in Q4 (and only 6 new ETF launches) the total 2022 figure, at 62 new ETFs, surpassed the 2021 record by 17 ETFs. In the mutual fund space, Q4 saw the launch of 26 new strategies. In 2022, active asset managers introduced 106 new thematic strategies, behind last year's figure of 137 but above the launches in all prior years.

Notably, ETF launches in 'Technological Shifts' were just 2 strategies ahead of the launches in 'Environmental Pressures', 31 vs. 29. For open-ended funds, the picture reversed with 35 and 45 new launches in the respective clusters. 'Sustainable Energy Production', 'Sustainable Resource Management' and 'Metaverse' were the most popular themes by the number of launches. However, it was strategies targeting broad themes within the 'Climate Change & Sustainability' sub-cluster that saw the highest number of launches, at 17.

We will continue to closely watch the space in Q1 2023, and we will summarise our findings in the next WisdomTree Quarterly Thematic Review. Stay tuned.

Footnotes

1. All figures are based on the WisdomTree's internal classification of thematic funds and WisdomTree's calculations using the underlying data from Morningstar and Bloomberg.

2. **Performance of a theme.** For any given theme, we consider each month all the ETFs and open-ended funds classified in that specific theme that have published a monthly return for that month in Morningstar. We then calculate the average of all those monthly returns to compute the average monthly return for that theme. So, the monthly return for January 2020 for the theme may include 19 funds, while the February 2020 return may comprise 21 funds (if two funds classified in that theme have been launched in the meantime). By collating monthly returns for the theme, we get the theme's average historical performance. Therefore, the theme's average historical performance incorporates every ETF, and open-ended fund focused on this theme. The theme's average historical performance is not biased towards surviving funds or successful funds. Every fund alive in a given month is included irrespective of its future survival or success. Investments that try to focus on multiple themes and, therefore, classified either at Cluster or Sub-Cluster Level are not included.

Sources

¹ All figures throughout this blog (unless stated otherwise) are based on WisdomTree's internal classification of thematic funds and WisdomTree's calculations using the underlying data from Morningstar and Bloomberg.

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