SMALL CAP EQUITIES PERFORMING STRONGLY ACROSS EUROPEAN COUNTRIES

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02/24/2014

Recently we wrote a blog post discussing the attribution of the WisdomTree Europe SmallCap Dividend Index (WTESC) relative to the S&P Europe 350 Index (European Large Caps). The focus of that post was how small-cap stocks in sectors such as Consumer Discretionary, Industrials and Information Technology benefited more from the cyclically driven recovery in Europe than the more defensive sectors that are often well-represented in large-cap indexes. What we didn't discuss in that attribution piece was a focus on the individual country exposures across these same markets. A recovery in some of the peripheral European markets was also part of the reason why small caps outperformed large caps as part of the European recovery story over the last 18 months. Moreover, small caps outperformed large caps in 14 out of the 15 countries represented in both European indexes,[1] showing that the theme of small caps outperforming on the heels of a cyclical recovery in Europe was not confined to one country or a result of specific country allocations. **Positive Performance Spread across European Countries** From June 2012 to December 31, 2013, every single country equity market represented in WTESC and European Large Caps delivered a positive total return. **Peripheral Recovery:** Within WTESC, the three best-performing equity markets were Ireland (152.53%), Portugal (127.14%) and Italy (116.19%). This demonstrates that WTESC, with its small-cap focus, was able to zero in on the performance of the European periphery recovering post-crisis, whereas European large caps, though performing strongly as well, saw more of the performance coming from the stronger core countries. • Italy was the second most important contributor to the relative performance (WTESC vs. European Large Caps), explaining 9% of the 45% return differential, which was due to Italy's exposure in the WTESC, which is four times as large as it is in the large-cap index.[2] • Portugal, Ireland and Spain were the fifth, sixth and seventh most important contributors to the performance of the European small caps —and each had a return that was over 100%, in other words more than three times the return of traditional large-cap Europe. These three peripheral European markets would have had a greater impact on performance if they had received larger weights, but their collective weight in WTESC was less than 10%, below Italy's weight of 13.5%.[3] While each of these country's equity markets delivered positive performance over the period, we believe that the dispersion warrants special consideration. So, to gain a deeper understanding, we present a look at the country level attribution between these two indexes below. **Bottom Three European Country Equity Markets:** Within WTESC, the three lowest-performing equity markets were Finland (50.75%), the Netherlands (45.78%) and Norway (33.86%)—countries that were viewed as relatively stable through the experience of the 2008–09 global financial crisis.[4] **Highlighting the United Kingdom:** Both WTESC and European Large Caps were heavily exposed to UK equities over the period. But the crucial question concerns which sectors are being captured within which index. Approximately half of WTESC's exposure to United Kingdom equities was in the Industrials and Consumer Discretionary sectors. In other words, WTESC was well positioned to take advantage of improving sentiment in UK equity markets, while avoiding the more defensive sectors (Consumer Staples, Health Care, Telecommunication Services and Utilities), as well as Financials and Energy. These were all areas where European Large Caps had significantly higher exposure. **The Top 10 Contributors to Relative Performance WTESC vs. European Large Caps from (6/29/2012 to 12/31/2013)**

	Average % Weight[1]			Total Returns		Attribution[3]
	WTESC Index	S&P Europe 350 Index	Over-or-Underweight[2]	WTESC	S&P Europe 350	WTESC vs. S&P Europe 350
Index	**100.00%**	**100.00%**	**N/A**	**80.18%**	**34.67%**	**45.51%**
United Kingdom	24.61%	30.34%	-5.73%	80.80%	37.52%	11.27%
Italy	13.51%	3.36%	10.15%	116.19%	48.31%	9.18%
Sweden	11.86%	4.66%	7.20%	65.36%	47.15%	3.55%
Switzerland	3.00%	14.49%	-11.49%	73.75%	47.91%	2.26%
Portugal	2.71%	0.24%	2.47%	127.14%	52.10%	2.09%
Ireland	1.99%	1.01%	0.98%	152.53%	48.31%	1.85%
Spain	4.75%	4.49%	0.26%	104.67%	61.55%	1.56%
Germany	10.41%	13.04%	-2.63%	85.24%	62.55%	1.16%
Austria	1.80%	0.27%	1.53%	101.04%	62.97%	1.08%
Denmark	1.20%	1.61%	-0.41%	61.57%	44.78%	0.65%

[1]Average % Weight: Average weight within the specified sector for each respective Index from 6/29/2012 to 12/31/2013.
[2]Over- or Under-weight: Difference in weight (WTESC minus S&P Europe 350). Positive numbers indicate that WTESC is over-weight.
[3]Attribution: Compares the performance of one index or investment to another, noting particularly the differences in weights or holdings. This analysis quantifies both the positive and the negative effects of selecting or heavily weighting different stocks or sectors.
Source: Bloomberg. Past performance is not indicative of future results. You cannot invest directly in an index. Subject to change.

Average Annual Returns (as of 12/31/2013)

Index Name	WT Index Inception Date	1-Year	3-Year	5-Year	Since WT Index Inception
WisdomTree Europe SmallCap Dividend Index	6/1/2006	47.40%	15.52%	23.99%	6.63%
S&P Europe 350 Index		20.31%	9.15%	13.27%	3.16%

Source: Bloomberg. Past performance is not indicative of future results. You cannot invest directly in an index.

Completion and Complementarity In our prior blog post, which focused on WTESC's sector exposures and their resultant attribution over this same period, we concluded with emphasizing WTESC's potential complementarity to more large-cap-focused approaches. We believe the same can be said for this analysis of country exposures. Within Europe, a focus on large-cap stocks results in different sector exposures across countries than does a focus on small-cap stocks. For example, in the United Kingdom, which we highlighted earlier, a focus on small caps delivered greater economic sensitivity and under-weights to typically defensive sectors (Consumer Staples, Health Care, Telecommunication Services and Utilities), as well as Financials and Energy. In looking at ways to generate European equity exposure, small caps could offer a potentially differentiated approach and performance experience across different country markets. [1]Source: Bloomberg, period 6/29/2012 to 12/31/2013. [2]Source: Bloomberg; refers to average % weight and attribution for period 6/29/2012 to 12/31/2013. [3]Source: Bloomberg; refers to average % weight an attribution for period 6/29/2012 to 12/31/2013. [4]Source: Bloomberg; period 6/29/2012 to 12/31/2013.

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WisdomTree Europe SmallCap Dividend Index : A fundamentally weighted index meant to measure the performance of small-cap European dividend-paying equities weighted by cash dividends paid.

S&P Europe 350 Index : A float adjusted market capitalization-weighted measure of the performance of large cap equities within European markets.

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

Defensive sectors : Consumer Staples, Health Care, Telecommunication Services and Utilities.

Large-Capitalization (Large-Cap) : A term used by the investment community to refer to companies with a market capitalization value of more than $10 billion. Large cap is an abbreviation of the term "large market capitalization". Market capitalization is calculated by multiplying the number of a company's shares outstanding by its stock price per share.