THE WISDOMTREE PHILOSOPHY: PORTFOLIO CONSTRUCTION AND BUILDING "ALL-WEATHER" PORTFOLIOS

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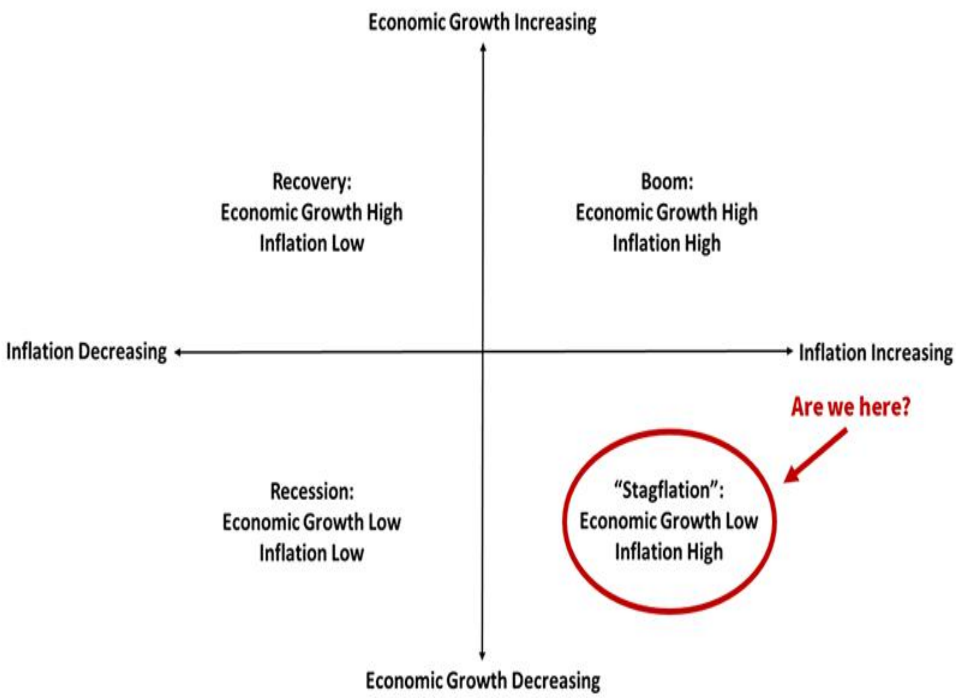
This article is relevant to financial professionals who are considering offering Model Portfolios to their clients. If you are an individual investor interested in WisdomTree ETF Model Portfolios, please inquire with your financial professional.

The WisdomTree Investment Philosophy

At any given time, the economy is either expanding or contracting, and inflation is either rising or falling, creating a four-quadrant "economic regime" framework for designing and managing investment portfolios:



Source: WisdomTree. This chart is for illustration purposes only.

The economy tends to rotate through these four quadrants (to varying degrees) over full market cycles (typically 6–8 years, although this time frame perhaps is truncated in today's economic and policy landscape), and different investment strategies tend to perform better (i.e., either generate positive performance or help mitigate downside risk) depending on which economic regime quadrant we may be in at any given time.

This "economic regime" structure provides a logical framework for building full market cycle Model Portfolios. WisdomTree refers to this as building "all-weather" portfolios. The goal is to build portfolios that perform consistently regardless of where we are in the economic cycle.

Investment Philosophy, Point 1: ***Build portfolios that are diversified at both the asset class and risk factor levels***

to optimize the potential for more consistent performance throughout evolving economic regimes.

The WisdomTree Investment Process

Given that no single investment approach consistently performs at all times and under all market conditions, successful portfolio management depends on several factors:

1. An investment philosophy that is logical, rational and quantitatively defensible;
2. A track record of success over full market cycles; and
3. Discipline to the approach over those full market cycles.

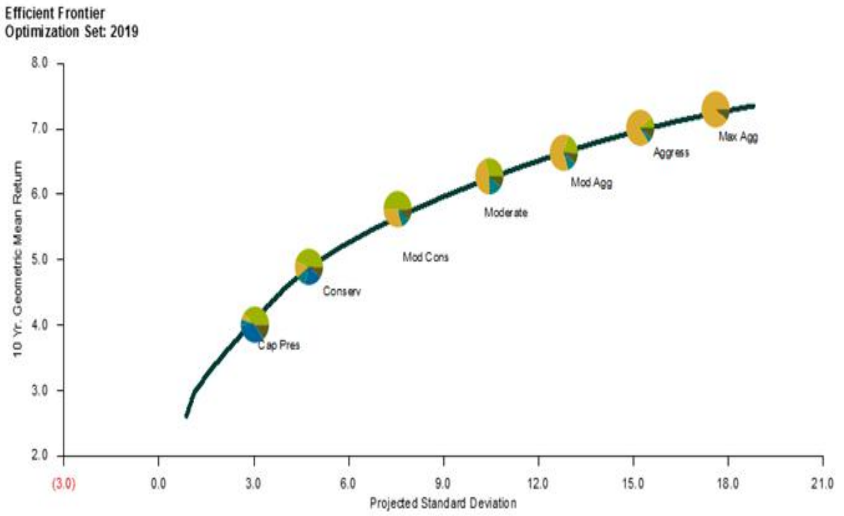
- **Logical, Rational and Quantitatively Defensible:** Within reason, we adhere to many accepted investment principles, including:
  - **Modern Portfolio Theory (MPT):** The idea that there is a relationship between risk and return and that risk can be reduced through appropriate diversification;
  - **Capital Market Theory (CMT):** The notion that markets are rational over time and there is an "efficient frontier" that represents a series of portfolios that optimize expected returns for various levels of risk; and
  - **The Power of Asset Class and Risk Factor Allocation:** The belief that asset and risk factor allocation decisions, not individual security selection, are the primary determinants of portfolio performance over time.

- The implementation of these investment principles into actual portfolio construction requires:
  - **Capital Market Assumptions (CMAs):** Forward-looking assumptions as to what levels of expected risk and return different asset classes and investment strategies may generate over a given period (typically 5–10 years), as well as the relationship (correlations) between the different asset classes—that is, how they move or change in value relative to one another. WisdomTree aggregates multiple third-party sources on a regular basis to help us develop appropriate CMAs; and
  - **Portfolio Construction Tools:** More commonly known as "Mean-Variance Optimizers" (MVOs), these are algorithmic and analytical tools that take CMA inputs and generate efficient frontiers—the set of portfolios that, based on the assumed CMAs, optimize expected returns for any assumed level of risk. This then allows WisdomTree to create Model Portfolios that fit different "risk profiles," from "conservative" (lower risk) to "aggressive" (higher risk).

A typical "efficient frontier" might look like this.

Strategic Asset Allocation

2019 efficient frontier and sample model portfolios



Portfolio Component	Cap Pres	Conserv	Mod Cons	Moderate	Mod Agg	Aggress	Max Agg
Hedge Funds	15	10	10	10	10	10	10
Cash Equivalents	35	20	0	0	0	0	0
Real Assets	5	10	10	15	10	5	0
Capital Growth	5	15	30	45	60	75	90
Income	40	45	50	30	20	10	0
Totals	100	100	100	100	100	100	100
10 Yr. Geometric Mean Return	4.11%	4.77%	5.68%	6.24%	6.64%	6.97%	7.24%
Projected Standard Deviation	3.25%	4.93%	7.67%	10.44%	12.79%	15.19%	17.62%
10 Yr. Simulated Sharpe Ratio	0.48%	0.45%	0.40%	0.35%	0.31%	0.29%	0.26%

Source: Callan, LLC, data through 2019. You cannot invest in an index, and past performance does not guarantee future results. This graph is for illustration purposes only and does not represent investment advice.

The theories of MPT, CMT and asset allocation are well-established and supported by academic work that resulted in Nobel Prizes for many thought leaders in the respective areas. That said, WisdomTree recognizes that these are all just theories based on assumptions and are not to be adhered to blindly.

This is the primary role of the WisdomTree Asset Allocation and Model Portfolio Investment Committees—we start with and are informed by the quantitative output of the various assumptions and tools. We then apply our collective knowledge and practical experience to arrive at portfolios we believe are defensible quantitatively but which also reflect our understanding of client expectations, as well as when and where the theories may not always hold true.

Specifically, most of these theories are based on necessarily simplified assumptions. While they present a robust framework for conceptualizing portfolio construction over full market cycles, they are not necessarily predictive of market conditions at any given time.

We believe this combination of rigorous quantitative analytics and extensive practical experience helps us in creating robust portfolios that (a) investors are comfortable maintaining over their preferred time horizon and (b) have the best opportunity to succeed over full market cycles.

Investment Philosophy, Point 2: *WisdomTree applies quantitative and qualitative analysis to both long-term forecasts and current market conditions to build strategic, longer-term portfolios.*

WisdomTree Portfolio Construction

WisdomTree believes in taking a longer-term approach to building globally diversified portfolios based on the process described above.

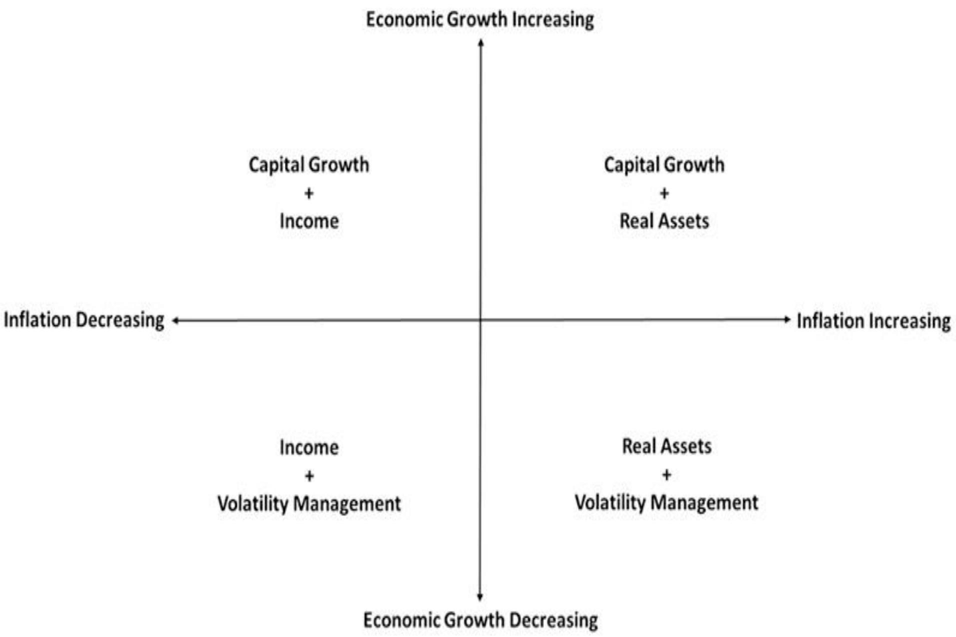
We further believe that the two portfolio characteristics advisors have the most control over are fees and taxes.

As such, we are ETF-centric in our portfolio construction process, as we believe that the ETF is a superior investment structure versus mutual funds and their use helps optimize portfolio fees and taxes.

We use four "building block" strategy categories, the combination of which we believe has the potential to build multiple and diversified portfolios that can meet a variety of investment mandates and generate consistent performance under all economic regimes and in all market conditions:

- **Global Equities, or "Capital Growth":** We access ETFs across all major geographies, asset classes and asset styles. These strategies include both passive "cap-weighted beta" strategies and (as is typical with WisdomTree products) "factor-tilted" strategies (i.e., screened for dividends, value, size, quality, etc.). Using both types of products allows us to build "core-satellite" portfolios using primarily ETFs.
- **Fixed Income:** We access a wide variety of ETFs, both U.S. and non-U.S., inclusive of most major fixed income sectors (rates, credit, high yield, securitized, both fixed and floating rate, preferreds, municipals, etc.).
- **Alternatives, or "Volatility Management":** Strategies may include but are not limited to equity long/short, global macro, managed futures, event-driven, short-bias, inflation hedge and options based. In the portfolios where we include these strategies, they are designed to (a) provide additional diversification to portfolio equity, interest rate and inflation risk, (b) access a more diverse set of potential sources of return and (c) reduce the volatility of the overall portfolio over time.
- **Real Assets:** These types of strategies historically have proven to be sensitive to longer-term changes in inflation, and when we incorporate them, we are attempting to (a) provide still more diversification to the portfolio equity risk, (b) access additional sources of potential return and (c) provide purchasing power protection to the portfolio against rising inflation. These strategies may include but are not limited to gold, broad-basket commodities, real estate, energy Master Limited Partnerships (MLPs) and diversified inflation-sensitive products.

If we overlay these four product strategy categories onto our economic regime quadrants, in terms of when we might expect each "building block" to "help most" with respect to delivering consistent risk-adjusted returns over time, it might look like this:



Source: WisdomTree. This chart is for illustration purposes and does not represent investment advice.

We take a generally strategic approach to our portfolio construction and ongoing management—we do not try to "time the market" and rotate in and out of strategies based on the regime we believe we might be in.

Instead, depending on the underlying investment mandate, our models are diversified across all or most of the strategy building blocks in an attempt to deliver consistent performance regardless of which regime we may be in or evolving to. We may make marginal dynamic allocation or strategy decisions as changing market conditions warrant, but we build our portfolios with a longer-term time horizon in mind.

Investment Philosophy, Point 3: ***In building Model Portfolios, we are (1) ETF-centric in nature to optimize both fees and taxes, (2) global in nature and (3) "open architecture"—we use both WisdomTree and third-party models in all of our portfolios to help us deliver better asset class and risk factor diversification, as well as access "best in class" investment solutions, and (4) we take a "core-satellite" portfolio construction approach.***

Summary and Conclusions

The WisdomTree Investment Philosophy and Portfolio Management approach is grounded in both academic research and practical experience. Over full market cycles and in varying economic and investment regimes, we strive to deliver consistent and positive risk-adjusted net-of-fee performance. By doing so, we attempt to help advisors and their end client investors meet their long-term investment goals and objectives.

Important Risks Related to this Article

Neither asset allocation nor diversification assures a profit or protects against loss in a given market environment. Investors should consider their investment time frame, risk tolerance level and investment goals.

For Retail Investors: WisdomTree's Model Portfolios are not intended to constitute investment advice or investment recommendations from WisdomTree. Your investment advisor may or may not implement WisdomTree's Model Portfolios in your account. The performance of your account may differ from the performance shown for a variety of reasons, including but not limited to: your investment advisor, and not WisdomTree, is responsible for implementing trades in the accounts; differences in market conditions; client-imposed investment restrictions; the timing of client investments and withdrawals; fees payable; and/or other factors. WisdomTree is not responsible for determining the suitability or appropriateness of a strategy based on WisdomTree's Model Portfolios. WisdomTree does not have investment discretion and does not place trade orders for your account. This material has been created by WisdomTree, and the information included herein has not been verified by your investment advisor and may differ from the information provided by your investment advisor. WisdomTree does not undertake to provide impartial investment advice or give advice in a fiduciary capacity. Further, WisdomTree receives revenue in the form of advisory fees for our exchange-traded Funds and management fees for our collective investment trusts.

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You cannot invest directly in an index.

DEFINITIONS

Inflation : Characterized by rising price levels.

Risk : Also standard deviation, which measures the spread of actual returns around an average return during a specific period. Higher risk indicates greater potential for returns to be farther away from this average.

Modern Portfolio Theory (MPT) : A financial theory that seeks to juxtapose investors' attitudes toward risk and return by maximizing the expected returns of a portfolio for a given level of risk, since greater expected returns usually involve absorbing additional risk.

Capital Market Theory (CMT) : A generic term for the analysis of securities.

Capital Market Assumptions (CMAs) : Beliefs about the future performance of available asset segments that incorporate theories, observations and experience.

Mean-Variance Optimization : The process of measuring an asset's risk against its likely return and investing based on that risk/return ratio.

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 tim.

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.

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 tim.

Credit : A contractual agreement in which a borrower receives something of value now and agrees to repay the lender at some date in the future.

High Yield : Sometimes referred to as "junk bonds," these securities have a higher risk of default than investment-grade securitie.

Securitized : a debt security whose value is backed by an asset or pool of assets such as a mortgage.

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

Interest rates : The rate at which interest is paid by a borrower for the use of money.

Purchasing Power : The value of a currency expressed in terms of the number of goods or services that one unit of money can buy.