HOW TO REPOSITION IN LESS EXPENSIVE STOCKS

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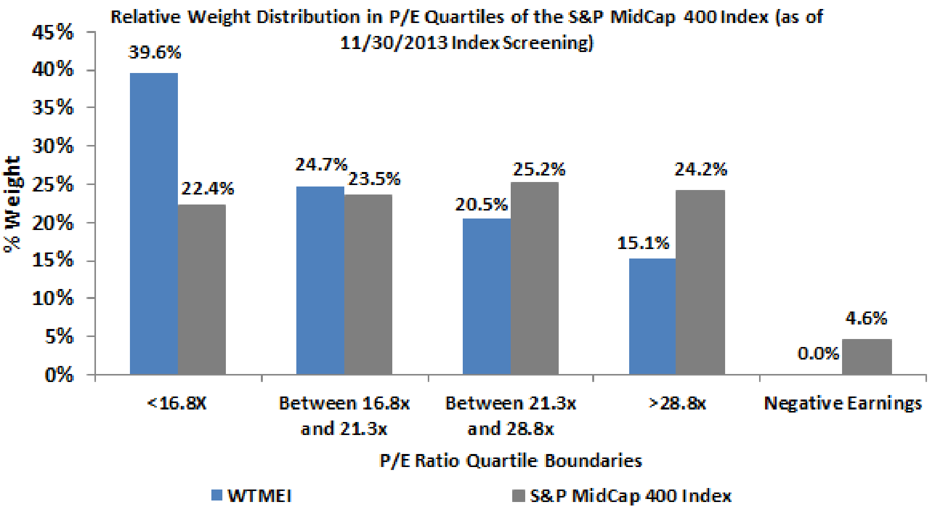
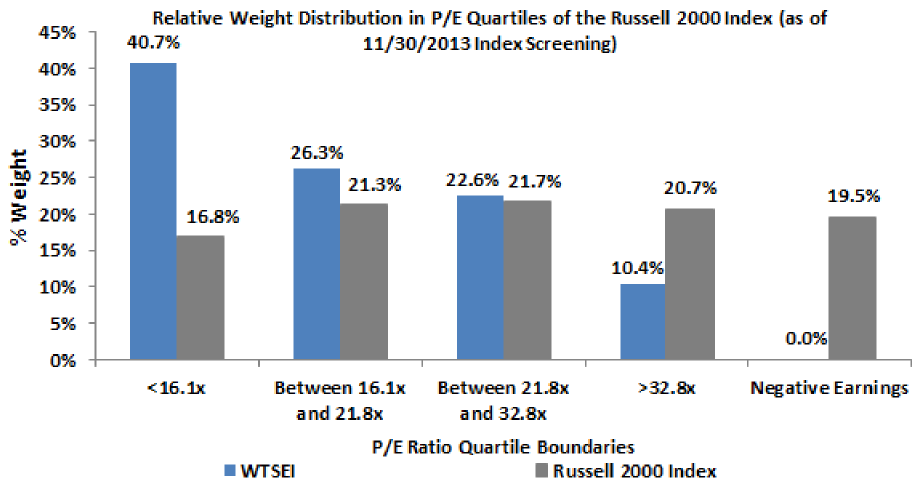
We've been heavily focused on why we believe there is a need for a relative value rebalance in 2013. Equity markets[1] have touched new record highs[2], and performance has been strong. We've also seen in prior blog posts how two of our Indexes, WisdomTree MidCap Earnings Index (WTMEI) and WisdomTree SmallCap Earnings Index (WTSEI) have trimmed weight from some of their top-performing constituents and reallocated it to firms that did not perform as well. What we haven't quite done as of yet is magnify the valuation impact of this rebalance. **Framing the Analysis Price-to-Earnings Ratio (P/E) Quartiles**: The first step in this analysis is defining the boundaries. For mid-caps, we will use the S&P MidCap 400 Index as the benchmark and set up the P/E ratio quartiles based on the values of its constituents as of November 30, 2013. For small caps, the Russell 2000 Index will serve in this capacity, with values measured as of the same date. **Weighting by Earnings vs. Market Capitalization (and Requiring Positive Profits):** In essence, WTMEI and WTSEI weight constituents by earnings and require all their constituents to have positive profits over the four quarters prior to the annual November 30 screening date. Relative to market capitalization-weighted approaches an earnings-weighted approach has the potential to lower the P/E ratio of a similar universe of stocks. **WTMEI Pushes Weight into the Lowest P/E Quartile (as of 11/30/2013 Index Screening)**



Sources: WisdomTree, Standard & Poor's, Bloomberg. You cannot invest directly in an index. Subject to change.

WTSEI Pushes Weight into the Lowest P/E Quartile (as of 11/30/2013 Index Screening)



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• **Two-Thirds' Weight in Lower P/E Quartiles:** Both WTMEI and WTSEI have approximately two-thirds of their constituent weight in firms in the two lower P/E ratio quartiles. Effectively, this illustrates an important impact of an earnings-weighted approach. The market capitalization-weighted indexes show much different positioning. • **Valuation Expansion Doesn't Impact All Firms Equally:** We have indicated in a prior blog post that an important driver of the returns witnessed in 2013 has been the expansion, or increase, of the P/E multiple. At face value, some may look at changing index-level P/E multiples and conclude that U.S. small- or mid-cap stocks have become expensive. However, we believe that some more appropriate conclusions could be: o **P/E Ratios Have Increased for Some Firms:** One important reason for this has been earnings contractions, as there have been firms that have lost money over the prior year. o **Opportunities Still Abound:** What these charts tell us is that there are small- and mid-cap firms with lower P/E ratios and not all mid- and small-cap companies are expensive. **Dealing with Negative Earnings** Each of the indexes featured in these charts has a different objective, which determines how they deal with firms with negative earnings over the prior year. The Russell 2000 Index, seeking broadness of exposure, allows constituents to be initially included with negative earnings, which explains why it has almost a 20% weight in such firms. The S&P MidCap 400 Index requires four quarters of positive, cumulative earnings prior to initial index inclusion—it thus has less exposure to firms with negative earnings over the prior 12 months than the Russell 2000 Index. Finally, the WisdomTree Indexes (both WTMEI and WTSEI) require four quarters of cumulative positive earnings leading up to every screening date. That's why it has a zero exposure within these charts. Minimizing (or eliminating) exposure to firms with negative earnings can also help lower the P/E ratio of a broader index. **Concluding the 2013 WisdomTree Earnings Family Rebalance Series** This blog post concludes our series on the 2013 Earnings Family rebalance. We believe the crucial takeaways are: • U.S. equity market performance[3] has been strong as of late, driving the potential for stocks to become more expensive. • A relative value rebalance can help trim weight from strong performers and reallocate it to those that haven't kept pace. • Weighting by earnings can potentially tilt more weight toward firms with lower P/E ratios. While none of this can in any way guarantee future performance, we believe it can potentially provide a disciplined approach that's lacking in market capitalization-weighted indexes. [1]Refers to the Russell 3000 Index, S&P 500 Index, S&P MidCap 400 Index and Russell 2000 Index. [2]Source: Bloomberg, as of 11/30/2013. [3]Refers specifically to the Russell 3000 Index, S&P 500 Index, S&P MidCap 400 Index and Russell 2000 Index all performing well from 12/31/2012 to 11/30/2013; source: Bloomberg, as of 11/30/2013.

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You cannot invest directly in an index.

DEFINITIONS

Relative value : The relationship between a particular attribute, e.g., a dividend, and the firm's share price compared to that of another firm.

Rebalance : An index is created by applying a certain set of selection and weighting rules at a certain frequency. WisdomTree rebalances, or re-applies its rules based selection and weighting process on an annual basis.

WisdomTree MidCap Earnings Index : Fundamentally-weighted index that measures the performance of the top 75% of the market capitalization of the WisdomTree Earnings Index after the 500 largest companies have been removed.

WisdomTree SmallCap Earnings Index (WTSEI) : measures the performance of earnings-generating companies within the small-capitalization segment of the U.S. Stock Market. The index is comprised of the companies in the bottom 25% of the market capitalization of the WisdomTree Earnings Index after the 500 largest companies have been removed.

Valuation : Refers to metrics that relate financial statistics for equities to their price levels to determine if certain attributes, such as earnings or dividends, are cheap or expensive.

Quartile : Statistical measure that groups a series of values into four groups after ranking them from lowest to highest. The first quartile will have the lowest values, whereas the fourth quartile will have the highest.

S&P MidCap 400 Index : provides investors with a benchmark for mid-sized companies. The index covers over 7% of the U.S. equity market, and seeks to remain an accurate measure of mid-sized companies, reflecting the risk and return characteristics of the broader mid-cap universe on an on-going basis.

Market Capitalization : Market cap = share prices x number of shares outstanding. Firms with the highest values receive the highest weights in approaches designed to weight firms by market cap.

Market capitalization-weighting : Market cap = share prices x number of shares outstanding. Firms with the highest values receive the highest weights in approaches designed to weight firms by market cap.

Earnings-weighted : Earnings for all constituents in an index are added together, and individual constituents are subsequently weighted by their proportional contribution to that total.