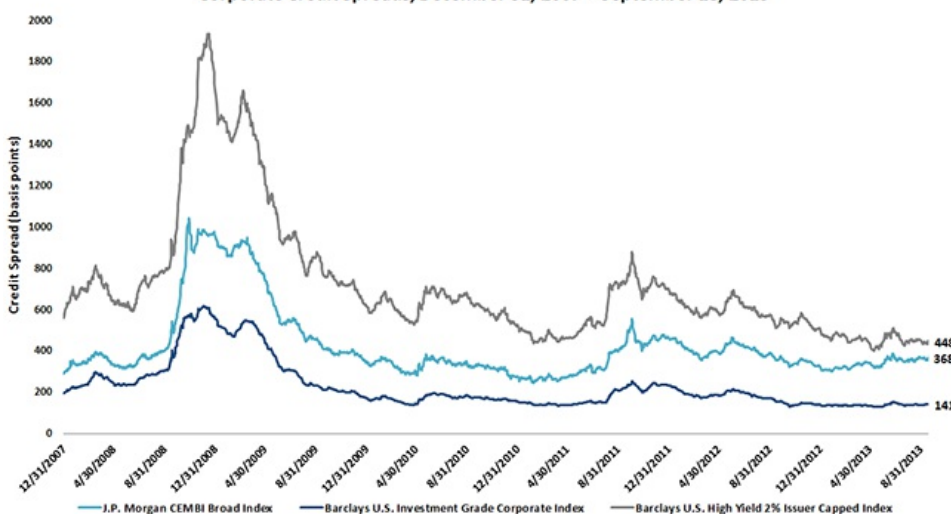


WHERE WE SEE THE GREATEST OPPORTUNITIES IN EMERGING MARKET FIXED INCOME: PART I

Rick Harper — CIO, Fixed Income
09/24/2013

After the Federal Reserve surprised markets by not reducing the pace of their asset purchases, yields on fixed income securities corrected sharply. With the prospect that Chairman Bernanke may now refrain from reducing stimulus before his term expires, sentiment within fixed income markets appears to be improving. In light of these recent events, where does it make sense for investors to add incremental risk to their bond portfolios? In our opinion, investors should consider increasing their exposure to emerging market (EM) fixed income: • **Long-term fundamentals broadly intact:** While a few EM countries seek to reduce external vulnerabilities, the economic fundamentals of many EM countries remain intact from [our perspective](#). • **Sell-off has been overdone:** The extent of the sell-off in recent months has created attractive entry points for both EM currencies and fixed income relative to other sectors. • **China appears resilient:** The combination of stronger growth and improving sentiment contrasts with the headwinds faced earlier this year. Within emerging market fixed income, it is important for investors to determine what risks are worth taking. EM corporate credit and EM local sovereign debt will have very different potential drivers of return going forward. In part one of this two part series, we examine EM corporate credit as an alternative to other U.S. dollar-denominated fixed income. Specifically, • U.S. [corporate bonds](#) are trading at levels near their 12-month average; emerging market corporate bonds have sold off along with other emerging market assets • EM corporate bonds appear attractive compared to U.S. corporate debt • EM [corporate credit](#) touched the closest relative levels to U.S. high yield in its history on September 5, 2013 **EM Corporate Credit** Similar to U.S. corporate bonds, EM corporate bonds are primarily denominated in U.S. dollars and trade at a spread relative to U.S. Treasury bonds. As a consequence, investors are exposed to changes in U.S. interest rates when investing in EM corporate bonds. In an uncertain interest rate environment, the potential value from investing in emerging market corporate credit is achieved through exposure to securities that provide a sizable yield cushion that can potentially dampen principal losses should rates rise.

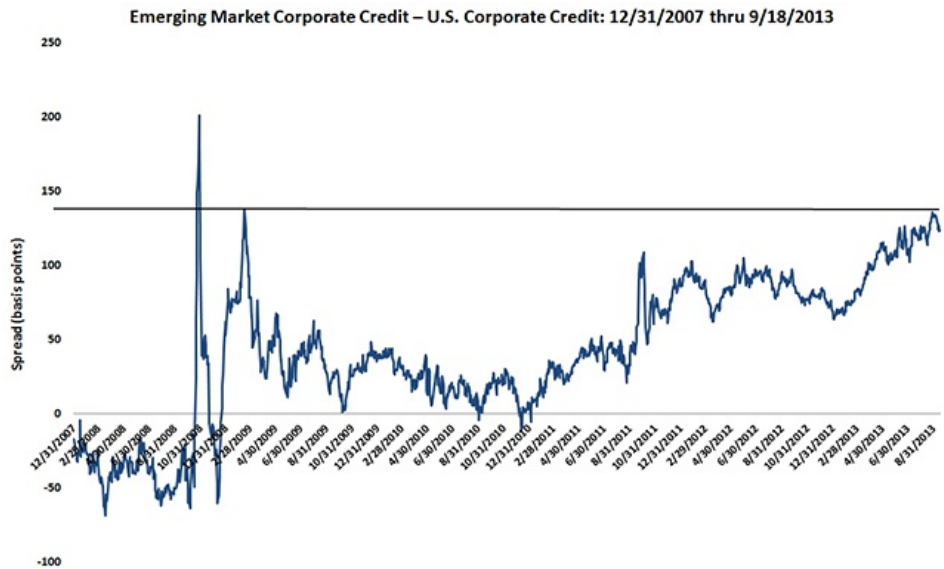
Corporate Credit Spreads, December 31, 2007 – September 18, 2013



Sources: J.P. Morgan, Barclays, Bloomberg, WisdomTree, 2013.

For definitions of terms and indexes in the chart, please visit our [Glossary](#). As shown in the chart above, credit spreads have generally trended lower over the last five years. With a recovering global economy and healthy corporate profits, companies posed less of a risk

to lenders. After a momentary spike in September 2011 (caused by concerns in Europe), [credit spreads](#) continued to [tighten](#) through mid-2013. For much of this period, EM corporate spreads moved largely in concert with those of U.S. companies. However, due to a combination of moderating Chinese growth and better than expected U.S. data, yields in emerging market corporate bonds began to diverge. Even though spreads in U.S. credit continue to trade at or below their 12-month average, spreads in emerging markets have [widened](#) to 368 [basis points](#), currently near their closest relative spread to U.S. high yield in history. Although emerging markets present an additional wrinkle for investors', the narrowing of the spread between EM corporates (an asset class that is currently rated 69% investment grade¹) to an all high-yield portfolio should have EM popping up on more investors' radars. In perhaps an even more interesting development, the so-called "EM premium" is currently trading at levels not seen since the bottoming of the global



financial crisis in early 2009.

Sources: J.P. Morgan, Barclays, Bloomberg, WisdomTree, 2013.

In the chart above, we compare a similarly rated composite of U.S. corporate bonds to the [J.P. Morgan Corporate Emerging Markets Bond Index Broad](#). In the last week, the relative credit spread between emerging markets and the U.S. was trading at all-time wide levels. In our view this implies that either EM corporate bonds are undervalued or that U.S. credit is overvalued, at least when using [credit ratings](#) as a proxy for risk. **Overcoming the EM Stigma** Even though they understand the quantitative advantages of EM credit investing (higher yields for comparable credit quality businesses), the thought of lending to companies headquartered in a foreign country seems to cause some investors concern. However, just like equity investing, by limiting your investable universe to developed markets, you severely restrict your investment opportunity set (and the potential for declining [correlations](#) and excess returns). With EM lagging across virtually all asset classes this year, it might be trendy to decry the end of EM investing. But many of the companies represented in the EM corporate investable universe are multi-billion dollar, multinational corporations with significant track records and credit histories. The combination of solid fundamentals and above market interest rates due to their country of domicile could make for an attractive investment if investors can put their biases behind them. While investor interest has been increasing in recent years, EM corporate credit comprises only 4% of the [Barclays Global Aggregate Corporate Index](#).² At current levels, EM corporate debt appears to be attractively priced compared to U.S. credit. Should investors believe in the long-term opportunity of emerging markets, EM credit may provide an attractive way to generate income in their portfolios while at the same time reducing volatility relative to traditional equity investments in these markets. ¹Source: J.P. Morgan, August 31, 2013. ²Barclays, August 31, 2013

Important Risks Related to this Article

You cannot invest directly in an index.

For standardized performance and the most recent month-end performance click [here](#) NOTE, this material is intended for electronic use only. Individuals who intend to print and physically deliver to an investor must print the monthly performance report to accompany this blog.

For more investing insights, check out our [Economic & Market Outlook](#)

View the online version of this article [here](#).

IMPORTANT INFORMATION

U.S. investors only: Click [here](#) to obtain a WisdomTree ETF prospectus which contains investment objectives, risks, charges, expenses, and other information; read and consider carefully before investing.

There are risks involved with investing, including possible loss of principal. Foreign investing involves currency, political and economic risk. Funds focusing on a single country, sector and/or funds that emphasize investments in smaller companies may experience greater price volatility. Investments in emerging markets, currency, fixed income and alternative investments include additional risks. Please see prospectus for discussion of risks.

Past performance is not indicative of future results. This material contains the opinions of the author, which are subject to change, and should not to be considered or interpreted as a recommendation to participate in any particular trading strategy, or deemed to be an offer or sale of any investment product and it should not be relied on as such. There is no guarantee that any strategies discussed will work under all market conditions. This material represents an assessment of the market environment at a specific time and is not intended to be a forecast of future events or a guarantee of future results. This material should not be relied upon as research or investment advice regarding any security in particular. The user of this information assumes the entire risk of any use made of the information provided herein. Neither WisdomTree nor its affiliates, nor Foreside Fund Services, LLC, or its affiliates provide tax or legal advice. Investors seeking tax or legal advice should consult their tax or legal advisor. Unless expressly stated otherwise the opinions, interpretations or findings expressed herein do not necessarily represent the views of WisdomTree or any of its affiliates.

The MSCI information may only be used for your internal use, may not be reproduced or re-disseminated in any form and may not be used as a basis for or component of any financial instruments or products or indexes. None of the MSCI information is intended to constitute investment advice or a recommendation to make (or refrain from making) any kind of investment decision and may not be relied on as such. Historical data and analysis should not be taken as an indication or guarantee of any future performance analysis, forecast or prediction. The MSCI information is provided on an "as is" basis and the user of this information assumes the entire risk of any use made of this information. MSCI, each of its affiliates and each entity involved in compiling, computing or creating any MSCI information (collectively, the "MSCI Parties") expressly disclaims all warranties. With respect to this information, in no event shall any MSCI Party have any liability for any direct, indirect, special, incidental, punitive, consequential (including loss profits) or any other damages (www.msci.com)

Jonathan Steinberg, Jeremy Schwartz, Rick Harper, Christopher Gannatti, Bradley Krom, Tripp Zimmerman, Michael Barrer, Anita Rausch, Kevin Flanagan, Brendan Loftus, Joseph Tenaglia, Jeff Weniger, Matt Wagner, Alejandro Saltiel, Ryan Krystopowicz, Kara Marciscano, Jianing Wu, Brian Manby and Scott Welch are registered representatives of Foreside Fund Services, LLC.

WisdomTree Funds are distributed by Foreside Fund Services, LLC, in the U.S. only.

You cannot invest directly in an index.

DEFINITIONS

Corporate Bonds : a debt security issued by a corporation.

Corporate Credit : compensation associated with the risk of lending to a corporation.

Credit spread : The portion of a bond's yield that compensates investors for taking credit risk.

Tighten : a decline in the amount of compensation bond holders require to lend to risky borrowers. When spreads tighten, the market is implying that borrowers pose less risk to lenders.

Widen : an increase in the amount of compensation bond holders require to lend to risky borrowers. When spreads widen, the market is implying that borrowers pose greater risk to lenders.

Basis point : 1/100th of 1 percent.

JP Morgan Corporate Emerging Markets Bond Index Broad (CEMBI Broad) : The JPMorgan Corporate Emerging Markets Bond Index Broad (CEMBI Broad) is a market capitalization weighted index consisting of US dollar-denominated Emerging Market corporate bonds. The index serves as a global corporate benchmark representing Asia, Latin America, Europe and Middle East / Africa. US dollar-denominated corporate issues from index-eligible countries are narrowed further by only including issues with more than \$300m current face outstanding and at least five years to maturity (at the time of inclusion into the index).

Credit ratings : An assessment of the creditworthiness of a borrower in general terms or with respect to a particular debt or financial obligation. Credit assessment and evaluation for companies and governments is generally done by a credit rating agency such as Standard & Poor's, Moody's or Fitch.

Correlation : Statistical measure of how two sets of returns move in relation to each other. Correlation coefficients range from -1 to 1. A correlation of 1 means the two subjects of analysis move in lockstep with each other. A correlation of -1 means the two subjects of analysis have moved in exactly the opposite direction.