JAPAN IS INEXPENSIVE—WHERE TO LOOK FOR PERFORMANCE

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Yes, this is a very good time to re-engage with Japan, in our view. The Brexit capitulation trade forced TOPIX down to almost 30% below its August 2015 peak,[1] which in turn makes Japanese equities the most attractively valued equity market in the world. More importantly, Japan is not a "value trap." In coming weeks, both micro and macro forces that should trigger a positive inflection point for Japanese large-cap performance will begin to align, in our view: On the micro side, dividend growth and share buyback momentum is likely to be maintained at the upcoming earnings season, despite negative earnings growth. On the macro side, a coordinated demand boost by the Ministry of Finance (MoF) and the Bank of Japan (BOJ) is on its way, with the BOJ poised to finance an ¥8 trillion to ¥10 trillion extra budget that includes "helicopter money" cash transfers to Japan's working poor. In short, attractive valuations + concrete triggers = time to re-engage in Japanese large caps. **Deep Value It Is…** In our view, this is true both from an absolute and relative perspective: MSCI Japan trades on a 1.1x price-to-book (P/B) ratio, which is in the bottom 10% range against its long-term history and well below the 2.0x for the MSCI World Index Japan's trailing price-to-earnings (P/E) ratio now stands at 14.2x. This is at the very bottom 2% against its history and well below the 20.2x for MSCI World. These are just the highlights. We see below in the more detailed global valuation matrix that by whichever metrics you choose, Japan is clearly winning the global valuation beauty contest. **Global Valuation Matrix: Japan Is Looking More and More Attractive** Overview of MSCI Equity Market Valuations by Region: MSCI Market Capitalization-Weighted Benchmarks

Sector	Price-to-Book Ratio		Price-to-Sales Ratio		Price-to-Earnings Ratio (Trailing)		Price-to-Earnings Ratio (Forward)		Price-to-Earnings Ratio (before extraordinary items)[3]		EV/EBIT[1]		EV/Sales[2]		Return on Equity		Dividend Yield		Free Cash Flow Yield	
		%-ile vs. History		%-ile vs. History		%-ile vs. History		%-ile vs. History		%-ile vs. History		%-ile vs. History		%-ile vs. History		%-ile vs. History		%-ile vs. History		%-ile vs. History
MSCI ACWI Index	1.9x	27%	1.4x	78%	19.3x	52%	15.8x	70%	22.0x	58%	17.2x	62%	1.8x	49%	9%	22%	2.8%	89%	7.5%	88%
MSCI World Index	2.0x	26%	1.4x	77%	20.2x	51%	16.3x	58%	23.3x	55%	17.9x	65%	1.8x	48%	9%	18%	2.8%	88%	7.1%	84%
MSCI USA Index	2.8x	39%	1.8x	81%	19.5x	67%	17.7x	71%	24.0x	65%	18.4x	61%	2.2x	47%	12%	21%	2.2%	88%	5.4%	58%
MSCI EMU Index	1.3x	16%	0.9x	46%	20.6x	48%	13.5x	57%	20.6x	50%	14.3x	43%	1.1x	29%	7%	27%	3.9%	84%	12.4%	90%
MSCI Japan Index	1.1x	10%	0.7x	39%	14.2x	2%	12.3x	2%	14.2x	2%	12.8x	0%	1.0x	11%	8%	65%	2.5%	93%	12.6%	99%
MSCI United Kingdom Index	1.7x	14%	1.2x	50%	47.7x	89%	16.2x	96%	47.6x	90%	29.6x	96%	1.5x	48%	4%	10%	4.6%	91%	5.8%	69%
MSCI Emerging Markets Index	1.4x	37%	1.1x	61%	14.2x	67%	12.4x	70%	14.9x	75%	13.0x	70%	1.5x	67%	11%	24%	2.9%	87%	11.0%	88%
MSCI EM Asia Index	1.4x	16%	1.1x	49%	12.7x	31%	12.4x	58%	12.9x	35%	12.5x	33%	1.4x	51%	12%	37%	2.7%	84%	9.1%	94%
MSCI EM Europe Index	0.9x	22%	0.9x	32%	18.3x	92%	8.2x	37%	25.8x	94%	9.6x	81%	1.1x	37%	8%	10%	4.1%	93%	51.1%	99%
MSCI EM Latin America Index	1.7x	52%	1.3x	55%	30.6x	99%	14.9x	82%	35.4x	99%	18.0x	99%	2.1x	69%	6%	5%	2.9%	61%	4.4%	33%

Sources: WisdomTree, Bloomberg. Historical percentile (%-ile) ranks based on data calculated from 1/31/1995 to 6/28/2016. Past performance is not indicative of future results. You cannot invest directly in an index.

[1] EV/EBIT: Refers to enterprise value (EV) to earnings before interest and taxes. Higher numbers indicate higher valuations compared to this specific depiction of earnings.

[2] EV/sales: Refers to enterprise value (EV) to sales. Higher numbers indicate higher valuations compared to a company's sales figures.

[3] Price-to-earnings ratio (before extraordinary items): Share price divided by earnings per share calculated without taking unusual or infrequent events that can impact earnings per share into account.

Note: For the price-to-book, price-to-sales, the three distinct price-to-earnings ratio measures, the EV/EBIT and the EV/sales ratios, the lower the percentile rank, the better the valuation opportunity compared to history. For the return on equity, dividend yield and free cash flow yield, the higher the percentile rank, the better the current figure looks compared to history.

…But Is Japan a "Value Trap"? While valuations are very attractive, performance ratios appear less so: Japan's return on equity (ROE) stands at 8%, which is not just below the 9% of the MSCI World but also at the 68% percentile mark—high by historical standards measured against its own history. Ditto for the dividend yield, 2.5% currency, which is in the 93rd percentile compared to its history. This is where our key pillar of the Japan bull thesis comes in: Corporate governance has fundamentally changed, and capital stewardship is now a principal focus for corporate managers. Equity returns and dividends are on a structural up-trend, in our view. The economic dynamic here is Japan's declining savings rate, forcing higher rates of return, with the newly introduced Stewardship Code[2] and Governance Code[3] helping to engender management behavior. The fact that Japan boasts a 12.6% free cash flow yield—MSCI World is 7.1%—suggests there is ample room for a structural rise in shareholder returns. **Trigger One: "Show Me the Money" at Upcoming Earnings Season** Here, the upcoming earnings results season should prove key to convincing investors that capital stewardship is really changing for the better: The April–June period is expected to be a second consecutive quarter of earnings declines. We will want to see confirmation that dividends will be maintained or even increased and share buybacks continue. The upcoming results season will be all about "show me the money" (from a shareholder perspective). If, as we suspect, dividend growth and share buyback momentum can be maintained, this should be the first concrete trigger to help overcome Japanese value trap fears (the April–June earnings results season will peak in early August). **Trigger Two: Coordinated Monetary & Fiscal Stimulus** A second positive performance trigger is poised to come from, yes, "Abenomics." Specifically, a pro-growth boost to aggregate demand is on its way, likely to be delivered by end-August/early September, in our view. Prime Minister Shinzo Abe has already instructed technocrats to prepare a supplementary fiscal boost. Here, an added ¥4 trillion to ¥5 trillion of public infrastructure investment for the reconstruction of the Kumamoto earthquake devastation is bound to be the mainstay. Added elements are expected to bring fiscal support for regional enterprises as well as a new round of cash transfers to the working poor. How exactly helicopter money will be administered is heavily debated, but the helicopter money question appears to have moved from "should" to "how?" In our view, a one-off gift from the treasury to the working poor has become likely. Most importantly, Team Abe is very focused on coordinating added fiscal spending with the Bank of Japan. Specifically, there is great awareness of the diminishing returns from monetary policy. The focus is on linking the central bank balance sheet more directly to aggregate demand. In practical terms, this means that the financing of the coming fiscal boost is poised to come from the BOJ. In our view, the BOJ will increase its quantitative easing by basically the same amount that the MoF will need to fund the extra budget. We expect a deficit-bond-funded extra budget of ¥8 trillion to ¥10 trillion and a boost in the BOJ's balance sheet growth target from the current ¥80 trillion to between ¥88 trillion and ¥90 trillion. For Japanese large-cap equities, we are approaching a positive turning point, in our view. Valuations are now very attractive, and concrete performance triggers are likely from both micro and macro dynamics unfolding. The time has come to re-engage in Japanese large caps, in our view. [1]Source: Bloomberg, with data measured from 8/10/15 to 6/28/16. [2]Stewardship Code: "Principles for Responsible Institutional Investors, Japan's Stewardship Code: To Promote Sustainable Growth of Companies through Investment and Dialogue," Financial Services Agency, 2/26/14.[3]Governance Code: "Japan's Corporate Governance Code: Seeking Sustainable Corporate Growth and Increased Corporate Value over the Mid- to Long-Term," JPX: Tokyo Stock Exchange, 6/1/15.

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DEFINITIONS

Brexit : an abbreviation of “British exit” that mirrors the term Grexit. It refers to the possibility that Britain will withdraw from the European Unio.

Tokyo Stock Price Index (TOPIX) : A free float-adjusted market capitalization-weighted index that is calculated based on all the domestic common stocks listed on the Tokyo Stock Exchange First Section.

Dividend growth : The growth in trailing 12-month dividends for the specified universe.

Buyback : When a company uses its own cash to purchase its own outstanding shares; may positively impact the share price.

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.

MSCI Japan Index : A market cap-weighted subset of the MSCI EAFE Index that measures the performance of the Japanese equity market.

Price-to-book ratio : Share price divided by book value per share. Lower numbers indicate an ability to access greater amounts of earnings per dollar invested.

MSCI World Equity Index : The MSCI World Index is a free float-adjusted market capitalization weighted index that is designed to measure the equity market performance of developed markets.

Return on Equity (ROE) : Measures a corporation’s profitability by revealing how much profit a company generates with the money shareholders have invested.

Dividend yields : Refers to the trailing 12-month dividend yield. Dividends over the prior 12 months are added together and divided by the current share price. Higher values indicate more dividends are being generated per unit of share price.

Bullish : a position that benefits when asset prices rise.

Free Cash Flow : A measure of how much cash is left in the company after taking into account all the necessary expenses, including net capital expenditures.

Yield : The income return on an investment. Refers to the interest or dividends received from a security that is typically expressed annually as a percentage of the market or face value.

Monetary stimulus : refers to attempts to use monetary policy like lowering interest rates or quantitative easing to stimulate the economy.

Abenomics : Series of policies enacted after the election of Japanese Prime Minister Shinzo Abe on December 16, 2012 aimed at stimulating Japan’s economic growth.

Helicopter money : has been proposed as an alternative to Quantitative Easing (QE) when interest rates are close to zero and the economy remains weak or enters recession. Economists have used the term ‘helicopter money’ to refer to two very different policies. The first set of policies emphasizes the ‘permanent’ monetization of budget deficits. The second set of policies involves the central bank making direct transfers to the private sector financed with base money, without the direct involvement of fiscal authorities.

Quantitative Easing (QE) : A government monetary policy occasionally used to increase the money supply by buying government securities or other securities from the market. Quantitative easing increases the money supply by flooding financial institutions with capital, in an effort to promote increased lending and liquidity.