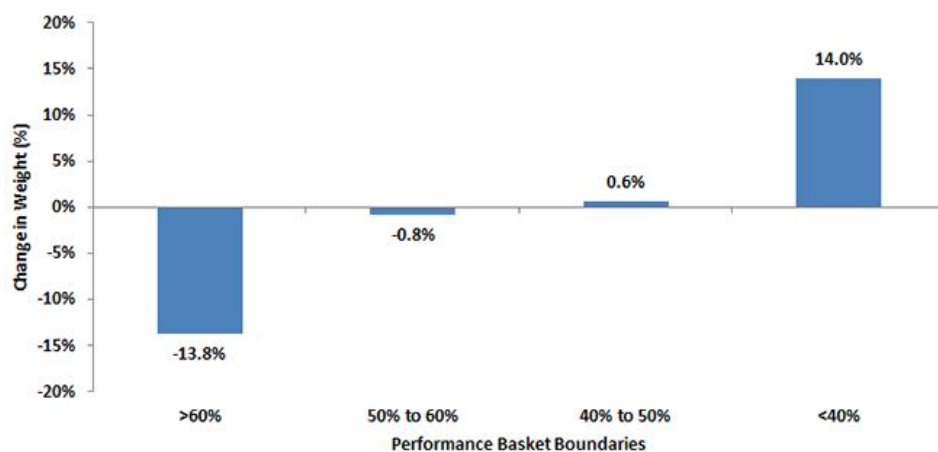


TAKING SOME CHIPS OFF THE SMALL CAP TABLE

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U.S. equity markets¹ performed strongly through much of 2013². And one of the most impressive pockets of performance occurred in the small-cap size segment, with the [Russell 2000 Index](#) up more than 36% compared to the [S&P 500 Index](#), which was up slightly less than 30%. [WisdomTree's SmallCap Earnings Index \(WTSEI\)](#) was up even more over this same period, with a return of more than 40%³. **Decision Time** Due to the futility of trying to time market tops and bottoms for individual stocks on a consistent basis, we believe that there are benefits to undertaking disciplined practices that take some weight away from particularly well-performing positions and reallocating toward areas that may not have kept up.

WTSEI as a Case Study Mapping the Performance Picture While the whole Index was up about 50%⁴ between annual [rebalance](#) screenings, we know that this is an average and not every stock was up by this amount. If we think broadly in terms of sector performance⁵: • **Four Sectors Greater Than 50%:** Consumer Discretionary (57.5%), Industrials (55.1%), Information Technology (52.8%) and Telecommunication Services (51.4%). • **Two Sectors Less Than 30%:** Energy (26.4%) & Utilities (19.3%). We believe that performance dispersion such as this leads to potential opportunities for a [relative value](#) rebalance to go to work. **How Chips Were Taken Off the Table** Shifting to a constituent level, it's important to remember that WTSEI is unique within the U.S. small-cap equity space in that it weights constituent firms by earnings. • **Greater Earnings = Road to Greater Weight:** The typical firm receiving increased weight in WTSEI will have grown or at least maintained its earnings but have had lackluster price performance. Conversely, the typical firm receiving lower weight will have had stronger price performance but earnings growth that did not keep pace. • **Losses Lead to Deletion:** Every constituent of WTSEI must prove its cumulative profitability over the four quarters prior to the November 30 screening. Lack of profits leads to lack of representation. **The Chips Coming**



Performance is measured from 11/30/2012 to 11/30/2013.

Sources: WisdomTree, Standard & Poor's, Bloomberg. Past performance is not indicative of future results. You cannot invest directly in an index.

Off the Small-Cap Table

Over 40% of Weight Returned Over 60%: It was a great year in U.S. small caps, and WTSEI's constituents were no exception. The overall Index returned nearly 50% between annual screening dates. Prior to the November 30, 2013, screening, more than 40% of its weight was in constituents that had returned better than 60%. • **Subtracting from Winners and Adding to Losers:** Regardless of how strong a year it must be to have "losers" defined as those returning less than 40%, we clearly see that weight is taken from those firms with returns greater than 60% over the prior year and redistributed to firms with returns below 40%. • **Accounting for the "Drop-Down" Effect:** Some might correctly point

out the possibility for underperforming firms in the [WisdomTree MidCap Earnings Index \(WTMEI\)](#) to decrease in their [market capitalizations](#) such that they can become constituents of WTSEI. Approximately 11% of the weight of the new constituents of WTSEI were part of WTMEI prior to the November 30, 2013, rebalance. While WTMEI returned over 40% in aggregate, the average performance for these particular firms was below 5%, meaning that they were in fact some of WTMEI's lower performers. **Effectively Taking the "Decision" Off the Table** WTSEI's relative value rebalance, the mechanics of which are seen above, is helpful in that it attacks the market in a disciplined way each and every year. This is especially important after the phenomenal performance of U.S. small caps this year, in that we believe investors might tend to want to hold on to the stronger performers. In sticking to the investment mantra "buy low, sell high," a relative value rebalance may aid in accomplishing this notably difficult action—a key feature of how we think investors can become smarter with their [beta](#) exposures. ¹Refers to the Russell 3000 Index, S&P 500 Index, S&P MidCap 400 Index and Russell 2000 Index. ²Refers to the 12/31/2012 to 11/30/2013 period. ³Source: Bloomberg. ⁴Refers to the 11/30/2012 to 11/30/2013 period, specifically from the 2012 rebalance screen to the 2013 rebalance screen. ⁵Each of the following return figures is sourced from Bloomberg for the 11/30/2012 to 11/30/2013 period.

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You cannot invest directly in an index.

DEFINITIONS

Russell 2000 Index : Measures the performance of the small-cap segment of the U.S. equity universe. The Russell 2000 is a subset of the Russell 3000 Index representing approximately 10% of the total market capitalization of that index. It includes approximately 2000 of the smallest securities based on a combination of their market cap and current index membership.

S&P 500 Index : Market capitalization-weighted benchmark of 500 stocks selected by the Standard and Poor's Index Committee designed to represent the performance of the leading industries in the United States economy.

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.

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.

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

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.

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.

Beta : A measure of the volatility of a security or a portfolio in comparison to a benchmark. In general, a beta less than 1 indicates that the investment is less volatile than the benchmark, while a beta more than 1 indicates that the investment is more volatile than the benchmark.