

THE CASE FOR QUALITY STOCKS IN JAPAN

Jeremy Schwartz — Global Head of Research

03/08/2016

WisdomTree believes Japan could represent one of the best equity markets over the coming years. The Bank of Japan (BOJ) introduced new stimulus tools in January 2016, and we expect it to continue to add to this [easing](#) over the coming months and years. Previously, [we discussed the approach for the WisdomTree Japan Quality Dividend Growth strategies](#) which we offer on both a currency-[hedged](#) and [-unhedged](#) basis: [The WisdomTree Japan Quality Dividend Growth Fund \(JDG\)](#) and the [WisdomTree Japan Hedged Quality Dividend Growth Fund \(JHDG\)](#). Below, we illustrate some of the [fundamental](#) data points that we think are the most important attributes when considering our Japan Quality Dividend Growth exchange-traded funds (ETFs).

The Underlying Index Methodology The Japan Quality Dividend Growth ETFs track the performance of two Indexes:

- JDG is designed to track the performance of the [WisdomTree Japan Quality Dividend Growth Index](#), before fees.
- JHDG is designed to track the performance of the [WisdomTree Japan Hedged Quality Dividend Growth Index](#), before fees.

The sole difference between these Indexes is that one is hedged while the other is unhedged—both select the same 300 companies that rank best on [quality](#) factors (three-year average [return on equity \[ROE\]](#) and three-year average [return on assets \[ROA\]](#)) and a growth factor (based on [long-term earnings growth expectations](#)). These Indexes also include a [dividend](#)-weighting element, which is designed to increase focus on higher-dividend-[yielding](#) stocks.

Higher Dividend Yields: Due to the dividend-weighting component, these two funds have tended to have higher average dividend yields than the [MSCI Japan Index](#) since their earliest common inception date, May 28, 2015. The MSCI Japan Index is a [market capitalization-weighted](#) index and does not have a dividend focus in its methodology.¹

Lower Price-to-Earnings (P/E) Ratios: Neither the MSCI Japan Index nor either of the two WisdomTree Japan Quality Dividend Growth ETFs focus on P/E ratios in their approach, but the Quality Dividend Growth strategy is currently selling at lower P/E ratios.²

Higher Earnings Growth Estimates: The two WisdomTree Japan Quality Dividend Growth ETFs have a considerably higher expected growth estimate than the MSCI Japan Index. This is likely because the selection factor for the methodology includes earnings growth as part of the screening criteria, whereas this is not a factor in the MSCI Japan Index's approach.³

Higher Historical Dividend Growth: While the Quality Dividend Growth strategies' methodology was designed to be a forward-looking dividend model to increase the probability of identifying companies that can raise their dividends at above-average rates, looking historically, the companies in JDG and JHDG as of February 5, 2016, have raised their dividends by more than 5 percentage points faster than the companies in the MSCI Japan Index over the last one-year, three-year and five-year periods. This is an important point: The strategies offer an advantage in current dividend yield as well as past dividend growth rates.⁴ For those investors who believe, like us, that [Japan represents an attractive investment environment](#) in the developed world, there are many options to gain exposure. The case for the Quality Dividend Growth strategies is fundamentally driven: These are companies we currently see selling at relatively attractive [valuations](#) that have good earnings growth prospects. Additionally, the current constituents have shown to be good capital stewards by raising their dividends at above-average rates, and we believe they will continue to do so.

WisdomTree's Focus on Quality

		JDG/JHDG ¹	MSCI Japan Index
Fundamental & Valuation Statistics	Dividend Yield	2.50%	2.14%
	P/E Ratio	15.88x	16.87x
	Long-Term Earnings Growth	15.41%	7.39%
	Total Debt to Common Equity	66.96%	164.53%
Average Annual Dividend Growth of Current Constituents	5-Year	14.87%	9.86%
	3-Year	16.74%	11.87%
	1-Year	16.67%	11.77%

¹Since JDG and JHDG both track Indexes with the same underlying constituents, they have equivalent fundamental and valuation statistics. As of 2/5/16, the SEC yield for both Funds was 1.89%, and the Fund distribution yield was 3.46%.

Source: Bloomberg, data as of 2/5/16.

Performance is historical and does not guarantee future results. Current performance may be lower or higher than quoted. Investment returns and principal value of an investment will fluctuate so that an investor's shares, when redeemed, may be worth more or less than their original cost. Performance data for the most recent month-end is available at www.wisdomtree.com.

WisdomTree shares are bought and sold at market price (not NAV) and are not individually redeemed from the Fund. Total returns are calculated using the daily 4:00 p.m. EST net asset value (NAV). Market price returns reflect the midpoint of the bid/ask spread as of the close of trading on the exchange where Fund shares are listed. Market price returns do not represent the returns you would receive if you traded shares at other times.

Dividend Growth You cannot invest directly in an index. [View the standardized performance for JDG, here.](#) [View the standardized performance for JHDG, here.](#) ¹Source: Bloomberg, for period from 5/28/15 to 2/5/16, the longest period shared by JDG and JHDG.²Source: Bloomberg, with data as of 2/5/16. ³Source: Bloomberg, with data as of 2/5/16.⁴Source: Bloomberg, with data as of 2/5/16. This refers to the current constituents of JDG and JHDG and does not imply that either of these Indexes has one, three or five years of live history.

Important Risks Related to this Article

There are risks associated with investing, including possible loss of principal. Foreign investing involves special risks, such as risk of loss from currency fluctuation or political or economic uncertainty. Funds focusing their investments on certain sectors may be more vulnerable to any single economic, regulatory or sector-specific development. This may result in greater share price volatility.

The Funds focus their investments in Japan, and they may be significantly impacted by events and developments in Japan that can adversely affect performance. Dividends are not guaranteed, and a company currently paying dividends may cease paying dividends at any time. As these Funds can have a high concentration in some issuers, the Funds can be adversely impacted by changes affecting those issuers. The Funds invest in the securities included in, or representative of, their Indexes regardless of their investment merit, and the Funds do not attempt to outperform their Indexes or take defensive positions in declining markets.

The currency-hedged Funds use various strategies to attempt to minimize the impact of changes in the Japanese yen against the U.S. dollar, which may not be successful. Derivative investments can be volatile, and these investments may be less liquid than other securities and more sensitive to the effects of varied economic conditions. Due to the investment strategy of these Funds, they may make higher capital gain distributions than other ETFs. Please read each Fund's prospectus for specific details regarding each Fund's risk profile.

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

Monetary easing policies : Actions undertaken by a central bank with the ultimate desired effect of lowering interest rates and stimulating the economy.

Hedge : Making an investment to reduce the risk of adverse price movements in an asset. Normally, a hedge consists of taking an offsetting position in a related security, such as a futures contract.

Unhedged : Strategy that includes the performance of both the underlying asset as well as the currency in which it is denominated. The performance of the currency can either help or hurt the total return experienced.

Fundamentals : Attributes related to a company's actual operations and production as opposed to changes in share price.

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 time.

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

Return on assets (ROA) : Firm profits (after accounting for all expenses) divided by the firm's total assets. Higher numbers indicate greater profits relative to the level of assets utilized to generate them.

Long-Term Earnings Growth Expectations : Compilation of analyst estimates of the growth in operating earnings expected to occur over the next full business cycle, typically 3 to 5 years, sourced from Bloomberg.

Dividend : A portion of corporate profits paid out to shareholders.

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.

Dividend yield : A financial ratio that shows how much a company pays out in dividends each year relative to its share price.

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

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.

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.