
THIS IS HOW WE DID IT

Alejandro Saltiel – Head of Indexes, U.S.
01/27/2020

Financial markets experienced one of their best years in recent history in 2019. All major asset classes had positive returns and in most cases exceeded their trailing 15-year average¹.

Investors might assume that investing in the “market” would’ve been the best way to reap the benefits of such an environment.

But WisdomTree, through its systematic approach of seeking higher [risk-adjusted returns](#) by deviating from traditional [market cap weighting](#), was able to exploit certain investment [factors](#) (or themes) that outperformed in 2019.

How did we do it? Below are some of the key themes we implement in our strategies that resulted in outperformance.

1. Removing [State-Owned Enterprises \(SOEs\)](#) in Emerging Markets (EM)

The [WisdomTree Emerging Markets ex-State-Owned Enterprises Fund \(XSOE\)](#) had a whopping 576 [basis points \(bps\)](#) at NAV outperformance versus the [MSCI Emerging Markets Index](#). For standardized performance of XSOE, please click [here](#).

XSOE identifies and removes from its universe EM companies that can be subject to management conflicts of interest as a result of the local government having an ownership stake in excess of 20% (SOEs).

By removing these companies and reweighting those remaining using a [modified market cap](#), XSOE accesses regional growth and governance being over-weight in the Consumer Discretionary and Information Technology sectors and under-weight in the Financials and Energy sectors.

XSOE’s methodology is the main driver of its outperformance, since last year non-SOE companies within MSCI EM Index outperformed the overall index by 200 bps² while SOEs lagged by more than 600 bps. Staying away from state-owned enterprises has proven to lead to excess return since the Fund’s inception more than five years ago.

XSOE seeks to track the price and yield performance before fees and expenses of [WisdomTree Emerging Markets ex-State-Owned Enterprises Index](#), shown below

EMXSOE - WisdomTree Emerging Markets ex-State-Owned Enterprises Index VS. MXEF - MSCI Emerging Markets Index

State-Ownership Attribution As of: 12/31/2019

MTD QTD 1Y 3Y 5Y Since Inception*

EXPORT EXCEL

Category ^	Attribution Component				Average Category Weight			Category Performance	
	Allocation	Stock Selection	Interaction	Total Attribution	Index Weight	Benchmark Weight	+/- Wgt	WT Index Return	Benchmark Return
SOE	1.59%	0.00%	0.00%	1.59%	0.00%	24.56%	-24.56%	0.00%	12.19%
XSOE	0.52%	3.03%	1.00%	4.55%	100.00%	75.44%	24.56%	24.58%	20.47%
Total	2.12%	3.03%	1.00%	6.14%	-	-	-	24.58%	18.44%

Source: WisdomTree. Data from 12/31/18 to 12/31/19. Past performance is not indicative of future results. You cannot invest directly in an index. Index performance does not represent actual fund or portfolio performance. A fund or portfolio may differ significantly from the securities included in the index. Index performance assumes reinvestment of dividends but does not reflect any management fees, transaction costs or other expenses that would be incurred by a portfolio or fund, or brokerage commissions on transactions in fund shares. Such fees, expenses and commissions could reduce returns.

2. Over-weighting Profitability (Quality)

The [WisdomTree International Hedged Quality Dividend Growth Fund \(IHDG\)](#) outperformed its benchmark, the [MSCI EAFE Local Index](#), by 11.05% at NAV last year. For standardized performance of IHDG, please click [here](#). IHDG seeks to invest in developed international companies that have strong profitability metrics and foreseeable growth-quality companies.

Using [return on equity \(ROE\)](#) as a proxy for quality, the highest [quintile](#) of [quality](#) companies in the international developed market³ last year outperformed the MSCI EAFE Index by 12 percentage points in local currency terms. Those with lowest quality underperformed by 5%.

IHDG’s significant over- and under-weights in these categories (in reference to the highest quintile in the table below), along with its [currency hedge](#), has allowed it to generate significant excess returns.

IHDG seeks to track the price and yield performance, before fees and expenses of the [WisdomTree International Hedged Quality Dividend Growth Index](#), shown below.

WTIDGH - WisdomTree International Hedged Quality Dividend Growth Index VS. MMEA - MSCI EAFE Local Currency Index

Return on Equity Attribution As of: 12/31/2019

MTD QTD 1Y 3Y 5Y Since Inception*

EXPORT EXCEL

Category	Attribution Component				Average Category Weight			Category Performance	
	Allocation	Stock Selection	Interaction	Total Attribution	Index Weight	Benchmark Weight	+/- Wgt	WT Index Return	Benchmark Return
1st Quintile (Highest ROE)	5.02%	1.22%	2.16%	8.41%	67.80%	25.54%	42.26%	38.58%	33.61%
2nd Quintile	0.07%	1.08%	0.17%	1.31%	18.09%	20.81%	-2.72%	24.11%	19.96%
3rd Quintile	0.23%	2.62%	-1.27%	1.58%	9.56%	20.51%	-10.95%	33.00%	20.55%
4th Quintile	1.24%	1.26%	-2.32%	0.18%	3.47%	19.27%	-15.80%	16.65%	13.91%
5th Quintile (Lowest ROE)	0.61%	-2.90%	2.71%	0.42%	0.59%	10.90%	-10.31%	-3.82%	15.98%
Negative Return	0.18%	0.24%	-0.24%	0.17%	0.09%	2.02%	-1.93%	11.72%	12.72%
N/A	0.00%	0.15%	-0.22%	-0.06%	0.40%	0.96%	-0.55%	41.40%	17.99%
Total	7.35%	3.67%	0.98%	12.00%	-	-	-	33.67%	21.67%

Source: WisdomTree. Data from 12/31/18 to 12/31/19. Past performance is not indicative of future results. You cannot invest directly in an index. Negative Return category represents companies with negative trailing 12-month net income. N/A category represents unavailable Return on Equity data.

3. Controlling Valuation

The [WisdomTree U.S. LargeCap Fund \(EPS\)](#), which weights the 500 largest profitable companies in the U.S. market by the proportion of their earnings, outperformed the [S&P 500 Index](#) by 1.12% at NAV in 2019.

EPS’s methodology results in a lower aggregate valuation [price-to-earnings \(P/E\)](#). For standardized performance of EPS, please click [here](#).

In 2019, the most expensive companies (shown in the first quintile of the table below) in the S&P 500 underperformed the overall index by close to 500 bps, while the cheapest companies outperformed by 200 bps. EPS’s under- and over-weights in these respective categories translated to excess returns.

EPS seeks to track the price and yield performance before fees and expenses of [WisdomTree U.S. LargeCap Index](#), shown below.

WTEPS - WisdomTree U.S. LargeCap Index VS. 500 - S&P 500 Index

Earnings Yield Attribution As of: 12/31/2019

MTD QTD **1Y** 3Y 5Y 10Y Since Inception*

EXPORT EXCEL

Category	Attribution Component				Average Category Weight			Category Performance	
	Allocation	Stock Selection	Interaction	Total Attribution	Index Weight	Benchmark Weight	+/- Wgt	WT Index Return	Benchmark Return
1st Quintile (Lowest P/E)	0.25%	-0.02%	-0.07%	0.16%	24.91%	14.37%	10.54%	32.98%	33.57%
2nd Quintile	-0.09%	0.33%	0.09%	0.33%	24.91%	19.78%	5.14%	30.23%	28.50%
3rd Quintile	0.02%	0.39%	0.02%	0.43%	21.51%	21.61%	-0.11%	35.65%	33.66%
4th Quintile	-0.06%	-0.00%	-0.01%	-0.08%	18.72%	24.31%	-5.59%	32.75%	33.09%
5th Quintile (Highest P/E)	0.32%	0.24%	-0.14%	0.41%	9.32%	18.42%	-9.10%	29.96%	27.81%
Negative Earners	0.06%	0.17%	-0.09%	0.14%	0.54%	1.31%	-0.78%	50.39%	38.76%
N/A	0.03%	0.02%	-0.01%	0.03%	0.09%	0.19%	-0.11%	6.82%	-2.33%
Total	0.51%	1.13%	-0.22%	1.43%	-	-	-	32.91%	31.49%

Source: WisdomTree. Data from 12/31/18 to 12/31/19. Past performance is not indicative of future results. You cannot invest directly in an index. Negative Return category represents companies with negative trailing 12-month net income. N/A category represents unavailable Return on Equity data.

4. Weighting by Dividends

WisdomTree pioneered [fundamentally weighted](#) funds in emerging markets.

The [WisdomTree Emerging Markets SmallCap Dividend Fund \(DGS\)](#), launched in 2007, weights all [small-cap dividend](#) payers by the proportion of their U.S. dollar dividend payments. This results in DGS being over-weight in the highest dividend yield quintile in the EM small-cap space, while under-weighting the lowest dividend quintile along with non-dividend payers.

In 2019, the highest-yield quintile of DGS outperformed the broad [MSCI Emerging Market Small Cap Index](#) by 11.5% at NAV while the lowest [dividend yield](#) and non-dividend paying group lagged by 11% and 3.5%, respectively. This was the main driver to DGS beating its benchmark by 7.41% over the year.

DGS seeks to track the price and yield performance before fees and expenses of the [WisdomTree Emerging Markets SmallCap Dividend Index](#), shown below. For standardized performance of DGS, please click [here](#).

WTEMSC - WisdomTree Emerging Markets SmallCap Dividend Index VS. MXEFSC - MSCI Emerging Markets Small Cap Index

Dividend Yield Attribution As of: 12/31/2019

MTD QTD 1Y 3Y 5Y 10Y Since Inception*

EXPORT EXCEL

Category	Attribution Component				Average Category Weight			Category Performance	
	Allocation	Stock Selection	Interaction	Total Attribution	Index Weight	Benchmark Weight	+/- Wgt	WT Index Return	Benchmark Return
1st Quintile (Highest Div. Yield)	3.07%	0.21%	0.41%	3.68%	43.14%	15.62%	27.52%	24.39%	23.13%
2nd Quintile	0.65%	-0.25%	-0.10%	0.29%	26.18%	17.65%	8.53%	16.82%	18.57%
3rd Quintile	0.08%	0.13%	0.07%	0.28%	16.80%	15.85%	0.95%	13.32%	12.34%
4th Quintile	0.11%	0.34%	-0.16%	0.29%	9.12%	15.41%	-6.30%	11.73%	9.53%
5th Quintile (Lowest Div. Yield)	1.68%	1.46%	-1.17%	1.98%	2.96%	16.46%	-13.50%	8.56%	-0.29%
Zero Div. Yield	0.59%	-3.39%	3.36%	0.55%	0.21%	18.54%	-18.33%	-11.33%	8.19%
N/A	-0.29%	0.25%	0.19%	0.16%	1.60%	0.46%	1.13%	29.18%	-16.52%
Total	5.89%	-1.27%	2.60%	7.22%	-	-	-	18.73%	11.51%

Source: WisdomTree. Data from 12/31/18 to 12/31/19. Past performance is not indicative of future results. You cannot invest directly in an index. Zero Div. Yield category represents companies that do not pay dividends. N/A category represents unavailable Dividend Yield data.

What Lagged? Small Value

WisdomTree’s fundamental-weighting approach to U.S. small caps faced a more challenging environment.

Companies with negative earnings—which do not get included in the [earnings-weighted WTSD I](#)—outperformed the broader [Russell 2000 Index](#) by over 1,000 bps. The lowest P/E quintile, on the other hand, lagged by about 250 bps. For EES standardized performance please click [here](#).

During a year when small-cap profit growth was negative, investors seemed to be reaching for growth out of unprofitable biotech and tech companies.

With a potential reacceleration in economic growth in 2020, a rotation into small value has become a popular theme across [sell-side research](#)⁴ in year-ahead forecasts.

EES seeks to track the price and yield performance before fees and expenses of the [WisdomTree U.S. SmallCap Index](#), shown below.

WTSEI - WisdomTree U.S. SmallCap Index VS. RU2000 - Russell 2000® Index

Earnings Yield Attribution As of: 12/31/2019

MTD QTD **1Y** 3Y 5Y 10Y Since Inception*

EXPORT EXCEL

Category	Attribution Component				Average Category Weight			Category Performance	
	Allocation	Stock Selection	Interaction	Total Attribution	Index Weight	Benchmark Weight	+/- Wgt	WT Index Return	Benchmark Return
1st Quintile (Lowest P/E)	-0.92%	-0.69%	-1.30%	-2.91%	34.34%	12.15%	22.19%	16.81%	21.99%
2nd Quintile	0.34%	0.04%	0.08%	0.46%	24.62%	15.07%	9.55%	28.96%	29.32%
3rd Quintile	-0.04%	0.17%	0.11%	0.24%	18.01%	16.36%	1.65%	23.58%	23.00%
4th Quintile	0.49%	0.34%	-0.18%	0.65%	12.09%	16.68%	-4.59%	20.76%	19.63%
5th Quintile (Highest P/E)	0.62%	-0.48%	0.20%	0.34%	6.93%	18.27%	-11.34%	18.40%	21.32%
Negative Earners	-2.11%	-0.74%	0.86%	-1.99%	3.97%	21.24%	-17.27%	31.40%	35.61%
N/A	-0.09%	0.13%	-0.10%	-0.05%	0.03%	0.23%	-0.20%	37.40%	51.67%
Total	-1.70%	-1.23%	-0.32%	-3.26%	-	-	-	22.27%	25.52%

Source: WisdomTree. Data from 12/31/18 to 12/31/19. Past performance is not indicative of future results. You cannot invest directly in an index.. N/A category represents unavailable Price-to-Earnings data.

Conclusion

What works one year can sometimes be a good harbinger of the year to come—or not.

The whole 2010s seemed in favor of high P/E ratio growth companies. By the end of 2019, there seemed to be a modest shift away from high-P/E large caps, perhaps a sign of a shift toward value.

Small-cap growth continued on a tear last year. For bargain hunters, we believe 2020 may offer a good entry point for small-cap value stocks.

Internationally, companies with higher profitability could continue demonstrating solid performance as European and Far East markets look to sustained growth. While in EM, we believe non-state-owned Enterprises will continue outperforming the broad market, taking advantage of their solid governance and growth.

Unless otherwise stated, all data is from WisdomTree and FactSet as of December 31, 2019.

¹Bloomberg, as of January, 24 2020

²This refers to the category of state-owned companies within XSOE.

³The universe is: Companies incorporated in Japan, the 15 European countries, Australia, Israel, New Zealand, Hong Kong and Singapore.

⁴Research published by brokerage firms.

Important Risks Related to this Article

There are risks associated with investing, including the possible loss of principal. Foreign investing involves special risks, such as risk of loss from currency fluctuation or political or economic uncertainty. Funds focusing on a single sector and/or smaller companies generally experience greater price volatility. Investments in emerging, offshore or frontier markets are generally less liquid and less efficient than investments in developed markets and are subject to additional risks, such as risks of adverse governmental regulation, intervention and political developments. Funds focusing

their investments on certain sectors and/or regions increase their vulnerability to any single economic or regulatory development. This may result in greater share price volatility. The Funds invest in the securities included in, or representative of, their respective Index regardless of their investment merit, and each Fund does not attempt to outperform its Index or take defensive positions in declining markets. Please read each Fund's prospectus for specific details regarding the Fund's risk profile.

Dividends are not guaranteed, and a company currently paying dividends may cease paying dividends at any time. Derivative investments can be volatile, and these investments may be less liquid than other securities, and more sensitive to the effect of varied economic conditions. The Funds invest in the securities included in, or representative of, their Index regardless of their investment merit, and each Fund does not attempt to outperform its Index or take defensive positions in declining markets. Due to the investment strategy of DGS, this Fund it may make higher capital gain distributions than other ETFs.

For the top 10 holdings of XSOE please visit the Fund's fund detail page at <https://www.wisdomtree.com/investments/etfs/equity/xsoe>

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, Jianing Wu, and Brian Manby 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

Risk-adjusted returns: Returns measured in relation to their own variability. High returns with a high level of risk indicate a lower probability that actual returns were close to average returns. High returns with a low level of risk would be more desirable, as they indicate a higher probability that actual returns were close to average returns.

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.

Factor: Attributes that based on its fundamentals or share price behavior, are associated with higher return.

State-owned enterprise: Companies in which governments have a significant ownership stake and the potential to influence the firms' actions over time.

Basis point: 1/100th of 1 percent.

MSCI Emerging Markets Index: a broad market cap-weighted Index showing performance of equities across 23 emerging market countries defined as "emerging markets" by MSCI.

MSCI EAFE Local Currency Index: A market cap-weighted index composed of companies representative of the developed market structure of developed countries in Europe, Australasia and Japan, with performance measured in local currency term.

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

Quintile: One of the class of values of a variate which divides the members of and batch or sample into equal-sized subgroups of adjacent values or a probability distribution into distributions of equal probability.

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.

Currency hedging: Strategies designed to mitigate the impact of currency performance on investment returns.

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.

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.

Price-to-earnings (P/E) ratio: Share price divided by earnings per share. Lower numbers indicate an ability to access greater amounts of earnings per dollar invested.

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

Small caps: new or relatively young companies that typically have a market capitalization between \$200 million to \$2 billion.

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

MSCI EM Small Cap Index: Includes small cap representation across 21 Emerging Markets countries. The small cap segment tends to capture more local economic and sector characteristics relative to larger Emerging Markets capitalization segments.

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

Value: Characterized by lower price levels relative to fundamentals, such as earnings or dividends. Prices are lower because investors are less certain of the performance of these fundamentals in the future. This term is also related to the Value Factor, which associates these stock characteristics with excess returns vs the market over time.

100% Passively Hedged Approach: Strategy designed to have the full currency exposure hedged, regardless of any changes in market conditions.

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.