

TOP OF CLASS EUROPEAN PERFORMANCE

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European markets are dominating headlines this year, from both an economic policy front, with Mario Draghi unleashing a fresh round of [monetary stimulus](#), and a market performance perspective, with European bourses leading indexes higher and the euro tanking¹. As a result, flows are coming into European-focused funds, particularly those that [hedge currency risk](#). In particular, the [WisdomTree Europe Hedged Equity Fund \(HEDJ\)](#) has seen approximately \$13 billion of inflows in 2015 alone.² [Currency hedging](#), which has the goal of neutralizing the effect of [foreign exchange rates](#) on total return, has come into focus for U.S. investors recently, with the last few years showing how critical currency movements can be. **Top-of-Class Performance** Looking at the peer group of European-focused mutual funds and exchange-traded funds (ETFs), HEDJ has ranked No. 1 in its peer group of Morningstar mutual funds and ETFs over the last one- and two-year periods. Interestingly, if one goes back to the inception of HEDJ—when it was first focused on European markets while hedging the euro—which was August 29, 2012, there was only one fund that came out ahead of it³. The one Fund that beat it from this period was another WisdomTree Fund, the [WisdomTree Europe SmallCap Dividend Fund \(DFE\)](#). In 2012, the euro was \$1.26—it fell to \$1.07 by March 31, 2015. Yet, small caps outperformed large caps enough to offset the currency drag that HEDJ was protected from.⁴

Figure 1: Morningstar Peer Group Ranking and Performance

Morningstar Fund Category: European Stock ETF & OE	1-Year			1/1/14–3/31/15			2-Year			9/1/12–3/31/15		
	Total Return	Rank in Peer Group	% of Peer Group Beaten	Total Return	Rank in Peer Group	% of Peer Group Beaten	Total Return	Rank in Peer Group	% of Peer Group Beaten	Total Return	Rank in Peer Group	% of Peer Group Beaten
WisdomTree Europe Hedged Equity Fund	24.02%	1	100%	20.25%	1	100%	19.80%	1	100%	22.08%	2	99%
# of Peers in Fund Category	117			108			102			94		

Fund/Index Name	FUND INFORMATION			TOTAL RETURN NAV (%)					MARKET PRICE (%)				
	Ticker	Expense Ratio	Fund Inception Date	YTD	1-Year	3-Year	5-Year	Since Fund Inception	YTD	1-Year	3-Year	5-Year	Since Fund Inception
WisdomTree Europe Hedged Equity Fund	HEDJ	0.58%	12/31/2009	18.19%	24.02%	18.54%	10.46%	10.35%	18.96%	23.66%	17.82%	10.32%	10.36%
Spliced Cap-Weighted Index Benchmark ¹				18.67%	20.46%	17.60%	9.62%	10.02%	18.67%	20.46%	17.60%	9.62%	10.02%

Sources: WisdomTree, Morningstar, 12/31/09–3/31/15. ¹MSCI EAFE Local Currency Index through 8/29/12; MSCI EMU Local Currency Index thereafter. Morningstar ranking data start date chosen to coincide with HEDJ's investment objective change; after 8/29/12, HEDJ began tracking the WisdomTree Europe Hedged Equity Index. The 1/1/14–3/31/15 date range was chosen to reflect the most recent downward trend in the euro spot rate vs. the U.S. dollar.

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. You cannot invest directly in an index.

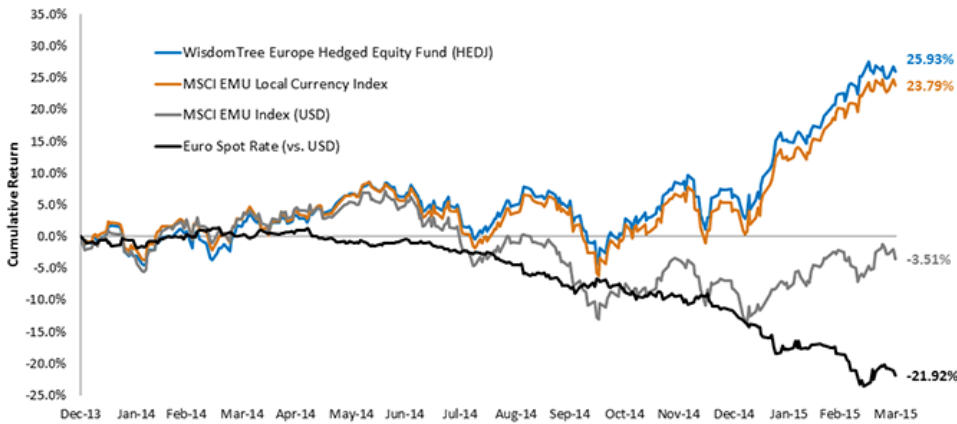
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Data

Accomplishes Goal of Targeting Local Market Returns Typically, traditional unhedged strategies leverage the equity return by layering currency risk on top of it. Hedging is a way to remove this leverage. Put another way: **Unhedged Return = Equity Market Return + Currency Return = Total Return (2 sources of risk/return)** **Hedged Return = Equity Market Return + Currency Return – Currency-Hedged Return Neutralizer = Local Equity Markets Return (1**

Hedging

source of risk/return) Overall, hedged strategies do not typically benefit significantly when currencies go up, nor do they get hurt when currencies go down. It is the unhedged strategies that either see returns increase when the foreign currency is rising or see returns hurt when these foreign currencies are weakening. **Hedging Accomplishing Goals Well** These hedged strategies are accomplishing their goal of achieving those local market returns during periods of significant euro weakness. Note that over the last 1.25 years, when the euro moves really started accelerating downward, HEDJ not only kept pace with the local market return, which was up sharply, but actually provided more than 200 [basis points \(bps\)](#) of cumulative outperformance, even after fees. **Figure 2: Cumulative Performance**



Sources: WisdomTree, Bloomberg, 12/31/13–3/31/15. Start date was chosen to reflect the most recent downward trend in the euro spot rate vs. the U.S. dollar. Past performance is not indicative of future results. You cannot invest directly in an index.

For current performance of HEDJ, visit the [WisdomTree Europe Hedged Equity Fund page](#). **Is It Too Late to Adopt Hedged Strategies?** One

question we are often asked about this currency-hedged European strategy: Has the euro move already been made, and is it too late to move toward a hedged approach? Here I favor the positioning by Andre Perold and Evan Schulman’s paper from the Financial Analysts Journal in 1988, “The Free Lunch in Currency Hedging: Implications for Investment Policy and Performance Standards.” They wrote: *In this article we argue that it is better to formulate long-run investment policy in terms of hedged portfolios than unhedged portfolios. The key to our argument is that, from the perspective of long-run policy, investors should think of currency hedging as having zero expected return. Therein lies the free lunch. On average, currency hedging gives you substantial risk reduction at no loss of expected return. Our prescription does not say the prescient investor should not selectively lift a hedge, just that hedging should be the policy, and lifting the hedge an active investment decision.*⁵

Getting Paid to Hedge If you believe the euro is going to enter a strong rally, lift the hedge as an active decision. But you should realize taking euro risk is equally an active decision—when it is essentially a zero-cost option to get euro risk hedged. In fact, it is currently even better than a zero-cost option, as U.S. investors are being paid a small amount to hedge euro risk based on [interest rate](#) differentials to implement the euro hedge.⁶ Given these dynamics, euro-hedged strategies in many ways offer better long-run policy portfolios, and the unhedged strategies should only be used when an investor has a strong view the euro is going to appreciate. We spoke with analyst Marc Chandler⁷, who believes 0.85 cents per euro is a very real possibility. I am not sure if that level will be reached, but I believe Marc makes just as strong a case as the analysts who say the U.S. dollar move is done and it can head back to \$1.20 per euro. Again, unless an investor has a clear idea the euro is on track to appreciate, the currency risk is just extra noise, and we’d suggest targeting the local equity market returns via [hedged strategies](#).¹

¹Source: Bloomberg, 12/31/14–4/24/15. ²Sources: WisdomTree, Bloomberg, 12/31/14–4/24/15. ³Sources: WisdomTree, Morningstar, 9/1/12–3/31/15 ⁴Sources: WisdomTree, Bloomberg, 9/1/12–3/31/15. ⁵Andre F. Perold and Evan C. Schulman, “The Free Lunch in Currency Hedging: Implications for Investment Policy and Performance Standards,” Financial Analysts Journal, May/June 1988. ⁶Sources: WisdomTree, Bloomberg, 3/31/15. ⁷Marc Chandler is Global Head of Currency Strategy at Brown Brothers Harriman.

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DEFINITIONS

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

Risk : Also standard deviation, which measures the spread of actual returns around an average return during a specific period. Higher risk indicates greater potential for returns to be farther away from this average.

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

Foreign Exchange (FOREX, FX) : The exchange of one currency for another, or the conversion of one currency into another currency.

Basis point : 1/100th of 1 percent.

Nominal interest rate : Interest rate that does not account for the impact of inflation.