

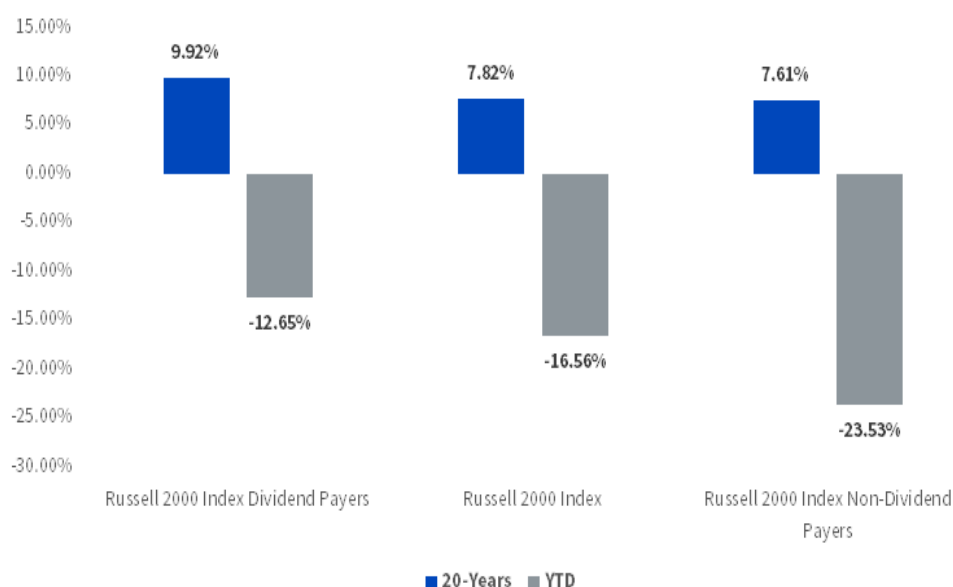
# MANAGING RISK VIA SMALL-CAP DIVIDEND GROWERS

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So far in 2022, the biggest determinant of total returns has not been [value](#) versus [growth](#) but rather [dividend](#) versus non-dividend payers. While much of the attention has been focused on [large-capitalization](#) equities, we've noticed an even more marked dispersion among [small caps](#).

The outperformance of small-cap dividend payers in 2022 is also not a new phenomenon—over the last 20+ years, dividend payers in the [Russell 2000](#) have outperformed non-dividend payers by more than 2% per year.



Sources: WisdomTree, Bloomberg, 5/31/00–5/31/22. Dividend portfolios rebalanced annually and market cap-weighted. You cannot invest directly in an index. Past performance is not indicative of future returns.

With [valuations](#) near all-time lows and a strong dollar potentially weighing on large-cap profitability, we believe now may be the time to increase exposure to small caps, as long as you're looking through the lens of dividend growth.

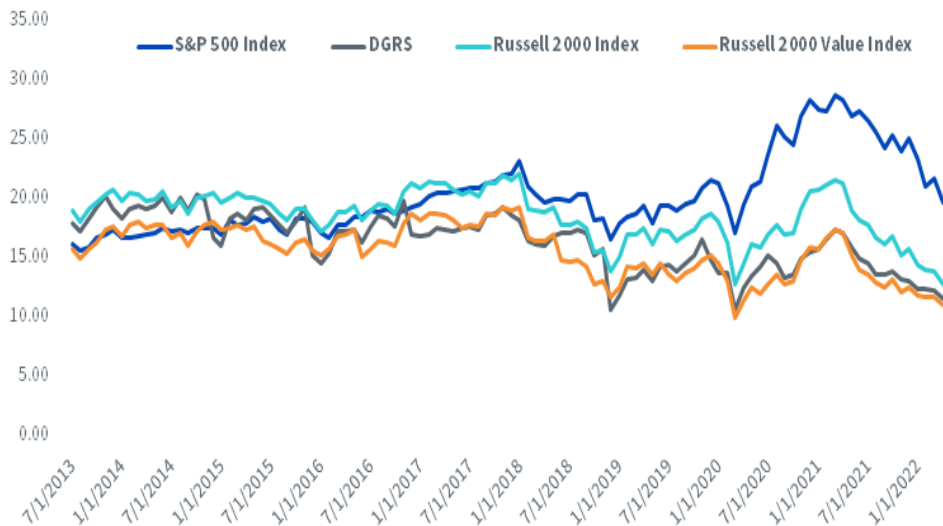
The [WisdomTree U.S. SmallCap Quality Dividend Growth Index \(WTSDG\)](#) selects dividend-paying companies with the best combined rank of earnings growth and [quality](#) factors, such as [ROE](#) and [ROA](#), and weights by their dividend stream. The [WisdomTree U.S. SmallCap Quality Dividend Growth Fund \(DGRS\)](#) seeks to track WTSDG, before fees and expenses.

WTSDG methodology tilts the portfolio to what we believe are well managed, high-quality, profitable companies with strong [balance sheets](#), better valuations and lower [leverage](#).

## Valuations

While technically classified by Morningstar as a small-cap blend strategy, [DGRS](#) has historically traded at similar valuations to small-cap value. At present, that means [P/Es](#) approaching levels not seen since the market lows of March 2020.

## Price-to-Earnings

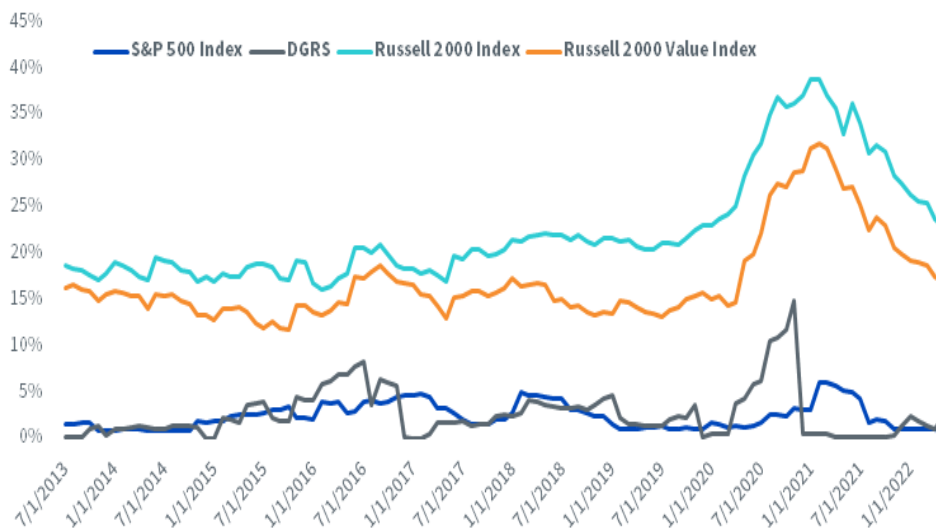


Sources: WisdomTree, FactSet, S&P, Russell, 5/31/22. Price-to-earnings excludes negative earners. You cannot invest directly in an index. Past performance is no guarantee of future results.

### Quality Stocks

Despite compelling valuations, investors remain concerned about earnings quality as the risk of recession rises. As of May 31, 2022, small-cap indexes such as Russell 2000 and [Russell 2000 Value](#) had more than 22% and slightly above 17% exposure to companies with negative earnings. Compare that to [DGRS](#), our quality small-cap Fund, which only had 2.5% invested in unprofitable companies.

### Percentage of Companies with Negative Earnings



Sources: WisdomTree, FactSet, S&P, Russell, 5/31/22. You cannot invest directly in an index. Past performance is not indicative of future results.

### Anchoring to Dividends

Small caps have been susceptible to significant [drawdowns](#) when the risk of a recession rises. In the current environment, which rewards dividend payers, [market cap-weighted](#) small-cap benchmarks have come under significant pressure, given that only 36% of the Russell 2000 Index currently pays a dividend. We contrast this with a strategy like [DGRS](#) that is not only comprised of dividend payers but also focuses on companies WisdomTree believes are best positioned to grow their dividends over time.

In fact, the median constituent in [DGRS](#) has grown its dividends by 8.4% over the last year, nearly double the rate of the [S&P 500](#). Since the Russell Indexes are comprised of a significant number of non-dividend payers, the median issuer is around zero. However, when looking at weighted averages, constituents in [DGRS](#) have not only been outpacing small-

cap peers but large caps as well.

Characteristics (as of 5/31/22)	Median Dividend Growth			Weighted Average Dividend Growth		
	1-Year	3-Year	5-Year	1-Year	3-Year	5-Year
DGRS	8.40%	5.90%	6.79%	35.34%	15.88%	13.34%
Russell 2000 Index	0.00%	0.00%	0.00%	3.18%	1.77%	2.60%
Russell 2000 Value Index	0.00%	0.00%	0.00%	4.22%	2.41%	3.54%
S&P 500 Index	4.48%	4.39%	5.79%	14.99%	5.58%	5.93%

### Tying It All Together

Characteristics (as of 5/31/2022)									
	Price/Earnings (Trailing)	Price/Earnings (Forward)	Dividend Yield	% Negative Earners	Net Buyback Yield	Shareholder Yield	Return on Equity	Return on Assets	Leverage
DGRS	11.98	10.90	2.83	2.50	2.77	5.60	15.42	4.03	3.83
Russell 2000 Index	12.57	12.21	1.21	22.88	-0.95	0.26	8.44	1.90	4.43
Russell 2000 Value Index	11.09	10.79	1.78	17.05	-0.25	1.53	8.77	1.89	4.64
S&P 500 Index	19.50	17.92	1.47	0.87	2.28	3.75	19.69	4.32	4.56

Sources: WisdomTree, FactSet, S&P, Russell, 5/31/22. You cannot invest directly in an index. Past performance is not indicative of future results.

For the most recent standardized performance, 30-day SEC yield and month-end performance, click [here](#).

For investors looking to diversify away from U.S. large caps, we believe small-cap dividend growers may be a compelling option. With dividend yields and growth rates nearly 2x the S&P 500, P/Es near single digits and historic lows, we believe [DGRS](#) may offer compelling value in an environment where dividend payers and dividend growth remain top of mind in investor portfolios.

### Important Risks Related to this Article

There are risks associated with investing, including the possible loss of principal. Funds focusing their investments on certain sectors and/or smaller companies increase their vulnerability to any single economic or regulatory development. This may result in greater share price volatility. Please read the Fund's prospectus for specific details regarding the Fund's risk profile.

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

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.

### Related Funds

+ [WisdomTree U.S. SmallCap Quality Dividend Growth Fund](#)

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.

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You cannot invest directly in an index.

## DEFINITIONS

**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.

**Growth** : Characterized by higher price levels relative to fundamentals, such as dividends or earnings. Price levels are higher because investors are willing to pay more due to their expectations of future improvements in these fundamentals.

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

**Large-Capitalization (Large-Cap)** : A term used by the investment community to refer to companies with a market capitalization value of more than \$10 billion. Large cap is an abbreviation of the term "large market capitalization". Market capitalization is calculated by multiplying the number of a company's shares outstanding by its stock price per share.

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

**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.

**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.

**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.

**Balance sheet** : refers to the cash and cash equivalents part of the Current Assets on a firm's balance sheet and cash available for purchasing new position.

**Leverage** : Total assets divided by equity. Higher numbers indicate greater borrowing to finance asset purchases; leverage can tend to make positive performance more positive and negative performance more negative.

**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.

**Russell 2000 Value Index** : measures the performance of small-cap value segment of the U.S. equity universe. It includes those Russell 2000 Index companies with lower price-to-book ratios and lower forecasted growth values.

**Drawdowns** : Periods of sustained negative trends of return.

**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.

**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.