HOW TO HEDGE YOUR EMERGING MARKET ALLOCATIONS AGAINST A STRONG DOLLAR

Jeremy Schwartz — Global Chief Investment Officer
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2016—until the election—had been the year of emerging market dominance. Commodities came roaring back, and not only was it the year of emerging markets (EM), it was also the year of emerging market currencies (with a weak U.S. dollar) and the commodity sectors within emerging markets. Countries such as Brazil, Russia and Peru led, while commodity importers like India and Korea lagged.

Since the election, however, there has been a new regime. The U.S. dollar started strengthening, and emerging markets faced a setback—although commodities have remained robust in the hope that infrastructure spending will support commodities and discussions of oil production cuts have supported oil.

Valuations Make EM Attractive, but What about Currency Risk?

One of the points supporting emerging markets is that anyone building capital market assumptions that incorporate a valuation factor in setting outlook will tend to be over-weight emerging markets. In the WisdomTree High Dividend Index family, for instance, the Emerging Markets High Dividend Index traded at a 50% price-to-earnings (P/E) discount to the High Dividend U.S. Index , one of the widest margins in last nine years. Of course, emerging markets entail higher risk levels, so they should trade at a discount, but I believe investing is about taking risks that you are compensated to take, so emerging markets look attractive to many.

But emerging markets are also critically reliant today on both China's economy not meaningfully deteriorating and not suffering from too strong of a U.S. dollar. A strong dollar tends to reverberate throughout emerging markets, and that has been the environment over the last five years.

Blending Strong Dollar and Weak Dollar Beneficiaries to Diversify Factor Risk

One idea that could balance this currency risk is to combine a strong dollar beneficiary—a country that sees performance tend to increase on the back of a strong U.S. dollar—with emerging markets that are reliant on a weak U.S. dollar.

A blend I have talked about for this approach looks to DXJ, the WisdomTree Japan Hedged Equity Fund, which I believe is one of the exchange-traded funds (ETFs) most tied to a strong dollar and an improving U.S. economy, and DEM, the WisdomTree Emerging Markets High Dividend ETF, which is reliant on the opposite from a currency side—a weak U.S. dollar.

A 50/50 blend of these two funds makes an interesting comparison to the MSCI AC World ex-US Index over the last five years.

Over the past five years, emerging market currencies generally were under great pressure. Emerging markets and DEM underperformed the MSCI AC World ex-US Index considerably—by more than 5 percentage points per year over this period.

That was a time when Japan outperformed considerably. Over the full period, Japan on a currency-hedged basis outperformed the MSCI AC World ex-US Index by more than 10 percentage points per year.

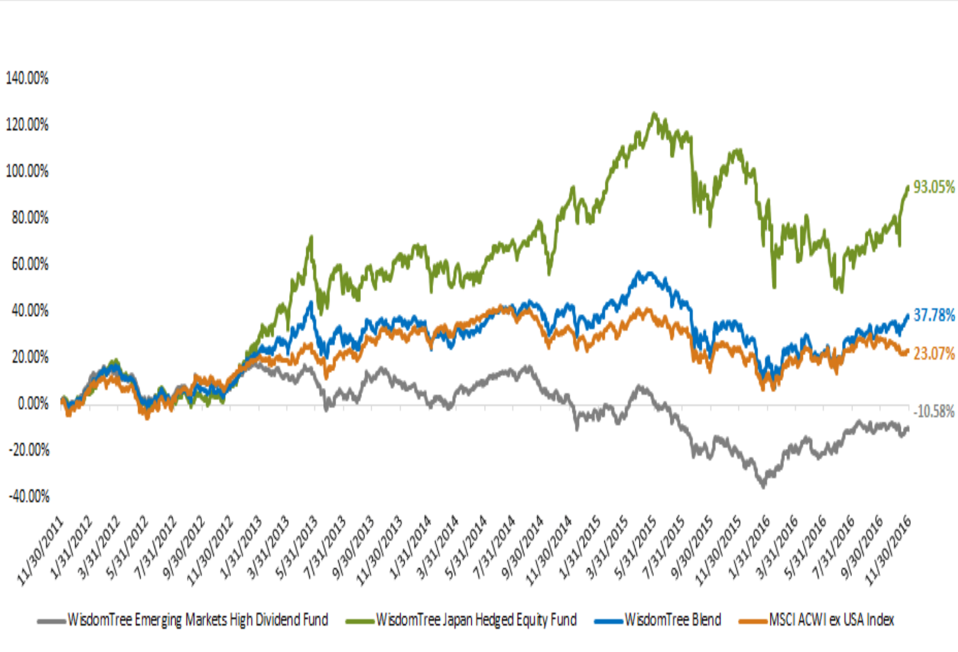
Implementing a blend of these two exposures would have landed investors ahead over five years and also in 2016—a year emerging markets finally began turning around after a dismal five years.

Allocating to a potentially strong dollar exposure—like DXJ, which is also among the lowest valuation countries in the developed world today—therefore has the potential to hedge what I think could be one of biggest risks to emerging market exposures for people who like the valuations presented therein.

The same can be said in reverse: If one is allocated to Japan exposure, perhaps a risk-mitigating strategy is also to allocate toward higher-dividend emerging markets that potentially benefit from a weak dollar and rising commodity prices.

In summary, this 50/50 blend not only has an attractive historical return profile. Looking at bottoms-up valuations of this 50/50 blend in comparison to the international benchmarks below, we believe this valuation profile could continue to look attractive going forward.

Cumulative Return Chart—WisdomTree Blend vs. MSCI ACWI ex—USA Index



Annualized Returns				
	YTD	1Yr	3Yr (Annualized)	5Yr (Annualized)
WisdomTree Emerging Markets High Dividend Fund	19.54%	14.91%	-6.72%	-2.21%
WisdomTree Japan Hedged Equity Fund	-3.91%	-6.37%	5.47%	14.04%
WisdomTree Blend	7.74%	4.27%	0.10%	6.61%
MSCI ACWI ex USA Index	1.73%	-0.03%	-2.31%	4.23%

As of Nov. 30, 2016. Period Covered - Nov. 30, 2011 - Nov. 30, 2016

Source: Bloomberg, as of 11/30/16. "WisdomTree Blend" refers to a 50/50 blend of DEM and DXJ, rebalanced annually. **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.

Click ticker for standardized performance of DEM and DXJ.

Fundamentals Perspective Supportive of WisdomTree 50/50 Blend:

Lower Price-to-Earnings Ratios, Higher Return on Assets (ROA) and Return on Equity (ROE)

Fundamentals and Risk							
	P/E	Fwd P/E	P/B	ROA	ROE	5-Year Beta	5-Year Standard Deviation
WisdomTree Blend	11.66	10.94	1.17	1.55	10.79	0.86	15.67%
MSCI ACWI ex USA Index	17.86	14.42	1.59	1.27	9.00	1.00	13.44%

Source: Bloomberg, as of 11/30/16. Past performance is not indicative of future results. You cannot invest directly in an index.

For definitions of terms in the chart, visit our glossary.

Unless otherwise noted, data source is Bloomberg, as of November 30, 2016.

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 on a single sector 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.

DXJ focuses its investments in Japan, thereby increasing the impact of events and developments in Japan that can adversely affect performance. Investments in currency involve additional special risks, such as credit risk, interest rate fluctuations, derivative investments which can be volatile and may be less liquid than other securities, and more sensitive to the effect of varied economic conditions. As this Fund can have a high concentration in some issuers, the Fund can be adversely impacted by changes affecting those issuers.

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DEFINITIONS

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.

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.

MSCI AC World ex-US Index : Measures the performance of companies incorporated in both emerging markets and developed markets, excluding the United States. Index weighting is by market cap.

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

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.

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