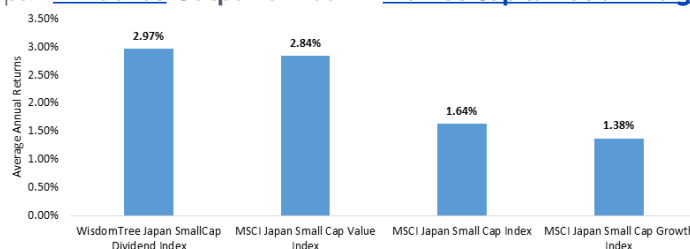


VALUE OUTPERFORMED GROWTH IN JAPANESE SMALL CAPS

Christopher Gannatti — Global Head of Research
07/15/2016

The [value](#) style has tended to outperform the [growth](#) style. This is something that many just assume to be true, and it fits with the behavioral aspect of finance as well. Growth stocks can be exciting, thereby getting bid up in price and leading many to invest well above an appropriate measure of [fair value](#). The result: future underperformance. **Past 10 Years Were a “Growth” Decade** While there is nothing wrong with the aforementioned logic and it has proved true over long periods, it was not true over the most recent 10 years in many markets. In fact, in both the United States and developed international equities, growth outperformed value. **Japanese Small Caps: The Opposite, Value over Growth Market** Japan, as has tended to be the case over the past few decades, exhibited a rather differentiated picture compared to developed international markets and the United States. Value outperformed growth. This was true for Japanese large caps, mid-caps and small caps. **Dividends Outperformed All Market Capitalization-Weighted Styles over 10-Year**



Sources: WisdomTree, Bloomberg, MSCI, with data from 6/1/06 to 6/1/16. 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.

Period in Japan Small Caps

How did WisdomTree’s dividend-focused approach to Japanese small caps outperform the other market capitalization-weighted approaches to small caps over this period? The key: The [WisdomTree Japan SmallCap Dividend Index](#) is not a very selective index—the main measure of stock selection is actually zeroing in on the small-cap size segment in Japan. Beyond that, the approach seeks to include every regular dividend payer. **Japan’s Small-Cap Income Factor** [Japan Small-Cap Income Factor](#)

Small-Cap Income Factor Shows Lower Market Sensitivity: The margin is not large, but it is true that the WisdomTree Japan SmallCap Dividend Index did exhibit market sensitivity below 1.0 for this period. This means that the WisdomTree Japan SmallCap Dividend Index would have the potential to go up less than Japan’s market in upward-trending markets and down less than Japan’s market in downward-trending markets. Given, however, that this was only a 0.03 difference from the [How term is in blog](#) target=“_blank”>MSCI Japan Small Cap Value Index, any difference in performance would be difficult to explain via this metric. • **Japan’s Small-Cap Income Factor Had Same Sensitivity to Size as Japan Small Cap Value Index:**

It is interesting that the sensitivity to size was basically equal between the WisdomTree Japan SmallCap Dividend and MSCI Japan Small Cap Value Indexes. The difference in performance would be tough to explain with this metric. • **Japan’s Small-Cap Income Factor Was a Bit Less Sensitive to Value:** Companies in Japan tend to initiate dividends sooner over their life cycles than companies in the U.S., so it is not surprising that the WisdomTree Japan SmallCap Dividend Index did not exhibit that extreme of a sensitivity toward value. This would be one area that might explain the difference in performance between the WisdomTree Japan SmallCap Dividend and MSCI Japan Small Cap Value Indexes. • **Japan’s Small-Cap Income Factor Was Less Tilted to Weak Operating Profitability:** If we had to hypothesize the critical difference between the WisdomTree Japan SmallCap Dividend and MSCI Japan Small Cap Value Indexes, this would be it this: The MSCI Japan Small Cap Value Index is much more tilted

toward companies that exhibited weak operating profitability over this period. Among Japanese small caps generally, robust operating profitability did exhibit outperformance over weak operating profitability during this period. WisdomTree's first Index family just celebrated its 10-year anniversary. The WisdomTree Japan SmallCap Dividend Index represents one of these very first Indexes that has a 10-year track record of demonstrating added value versus other major benchmarks for its space. The factor analysis above suggests that the quality tilt that came with the dividend-weighted income factor was a key driver and value-add versus the traditional value indexes. This helps demonstrate long-term attractiveness of this strategy. In the shorter term, our [Japan CEO, Jesper Koll](#), believes small caps represent a [secular growth](#) opportunity for the local economy, based on a shortage of workers at the young side of the population. This shortage of workers is pushing up wages for recent graduates and supporting a new middle class of Japanese workers who are getting more full-time jobs. The small-cap category for Japan is a great way to access this more local Japanese option, and we have now provided both [hedged](#) and [unhedged](#) versions of these Indexes to access this segment of the market. ***Unless otherwise noted, data source is Bloomberg.***

Important Risks Related to this Article

Investments focused in Japan increase the impact of events and developments associated with the region, which can adversely affect performance.

Investments focusing on certain sectors and/or smaller companies may be more vulnerable to any single economic or regulatory development.

Dividends are not guaranteed, and a company currently paying dividends may cease paying dividends at any time.

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

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.

Fair value : Also known as "eNAV." It is essentially an indicative value (IV) that is made in real time by calculating the basket value on every underlying tick and by adjustments that account for updated market news.

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

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.

Secular Growth : Long term positive trend where the longer-term positive movements cancel out any shorter-term negative movements.

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.