

# WisdomTree Barclays Yield Enhanced U.S. Short-Term Aggregate Bond Fund

# SHAG

In today's fixed income markets, the ability for investors to maintain the appropriate balance between risk and return remains extremely challenging. While stronger economic growth may boost the returns of credit, this could also lead to an increase in nominal interest rates. At the same time, core fixed income benchmarks have experienced a dramatic shift from their historical composition over the last 20 years. Given that many investors often follow market capitalization<sup>1</sup>-weighted benchmarks, their holdings of U.S. Treasuries have increased markedly, often at the cost of their ability to generate sufficient income from core portfolios.

In our view, a more intuitive approach to indexing may focus on the ways an investor can enhance the yield of his or her portfolio while dialing down the interest rate risk profile of a familiar benchmark. Through its relationship with Bloomberg Barclays as index provider, WisdomTree helped develop an approach for SHAG that draws on the same investable universe as the Bloomberg Barclays U.S. Aggregate Index (the Agg) but focuses on ways to reduce interest rate risk<sup>2</sup> while at the same time boosting yield potential. As a result, this approach may serve as a powerful tool for investors seeking to navigate the opening stages of a rising rate environment.

## **BLOOMBERG BARCLAYS U.S. SHORT AGGREGATE ENHANCED YIELD INDEX (SHORT AGG ENHANCED YIELD)**

- 1. Divide the Agg constituents maturing in one to five years in 13 subcomponents**
- 2. Screen and apply constraints**
- 3. Determine index weights**

<sup>1</sup> Market capitalization: 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.

<sup>2</sup> Interest rate risk: The risk that an investment's value will decline due to an increase in interest rates.

### 1) Divide the Agg constituents maturing in one to five years into 13 subcomponents

In the first step, the Agg is divided into 13 buckets across sector, maturity<sup>3</sup> and credit quality.<sup>4</sup> While each component retains a suitable size for investment and liquidity<sup>5</sup> purposes, each bucket may present unique opportunities for risk and reward. The strategy draws on the one- to five-year segment of the market (Short Agg Composite<sup>6</sup>) in order to mitigate interest rate risk.

		Years to Maturity	
		1-3 Years	3-5 Years
Sector	Government	Treasury 1-3	Treasury 3-5
		Agency 1-3	Agency 3-5
	Credit	Credit 1-3 Baa	Credit 3-5 Baa
		Credit 1-3 A	Credit 3-5 A
		Credit 1-3 Aaa-Aa	Credit 3-5 Aaa-Aa
	Securitized	Commercial Mortgage-Backed Securities WAL 1-5	
		Asset-Backed Securities WAL 1-5	
		Conventional MBS 15 ys	

Source: Bloomberg, as of 3/31/2018. Credit rating determined using Bloomberg Barclays' index rating methodology. Commercial mortgage-backed security (CMBS): A security whose value is composed of a pool of commercial mortgages. Asset-backed security (ABS): A fixed income security whose value or cash flows depend on the value of another asset, such as a loan, lease or receivable. Mortgage-backed security (MBS): A fixed income security that is composed of multiple underlying mortgages. WAL represents weighted average life of the security.

<sup>3</sup> Maturity: the amount of time until a loan is repaid.

<sup>4</sup> Credit quality: A measure of a borrower's potential risk of default.

<sup>5</sup> Liquidity: The degree to which an asset or security can be bought or sold in the market without affecting the asset's price. Liquidity is characterized by a high level of trading activity. Assets that can be easily bought or sold are known as liquid assets.

<sup>6</sup> Short Agg Composite represents the 1-5 year segment of the Agg.

## 2) Screen and apply constraints.

The following constraints are added; these serve to control risk and concentration while limiting turnover:

- + **Tracking Error Constraints:** Tracking error volatility (TEV)<sup>7</sup> of the Short Agg Enhanced Yield relative to the Short Agg Composite should be less than .175% (17.5 basis points [bps]) each month.
- + **Duration<sup>8</sup> constraints:** The duration of the Index generally will not be more than half a year greater than that of the Short Agg Composite.
- + **Sector and Subcomponent Constraints:** The weight of major and minor sectors (Treasuries, Credit and Securitized Bonds) cannot deviate by more than 30% from their weights in the Short Agg Composite. The total notional weight of the Baa subcomponents (U.S. Credit 1–3 Year Baa, U.S. Credit 3–5 Year Baa) cannot deviate from their weights in the Short Agg Composite by more than 30%.
- + **Turnover Constraints:** Portfolio turnover due to monthly rebalancing<sup>9</sup> is capped at 5%. When this condition cannot be met, the turnover limit is increased incrementally by 1% until a solution is found.

## 3) Determine Index Weights

On a monthly basis, weights of the Index are reallocated across the 13 subcomponents to help maximize yield, while adhering to the four constraints. These weights are then applied at the individual issue level, so that the weight is the product of the subcomponent's determined weight and the security's weight within the subcomponent.

For example, if a Treasury note maturing in three years has a 10% weight within the 1–3-Year Treasury subcomponent, the calculated weight of 12% allocated to the 1–3-Year Treasury subcomponent would result in a weight of 1.2% at month-end. Returns and statistics are calculated based on the constituents for the coming month. The Short Agg Enhanced Yield Index is rebalanced each month.

## THE RESULT

The Short Agg Enhanced Yield currently yields 3.03%<sup>10</sup> and is intended to deliver additional yield relative to the Short Agg Composite with a similar volatility profile. In our view, this mechanical approach enhances the desirable characteristics, while also enhancing the income potential of the strategy. For investors needing to hit minimum income targets, this modification could help them achieve their objectives. For managers currently concerned about the high-yield bond market, this approach also provides higher income potential in an investment-grade portfolio.

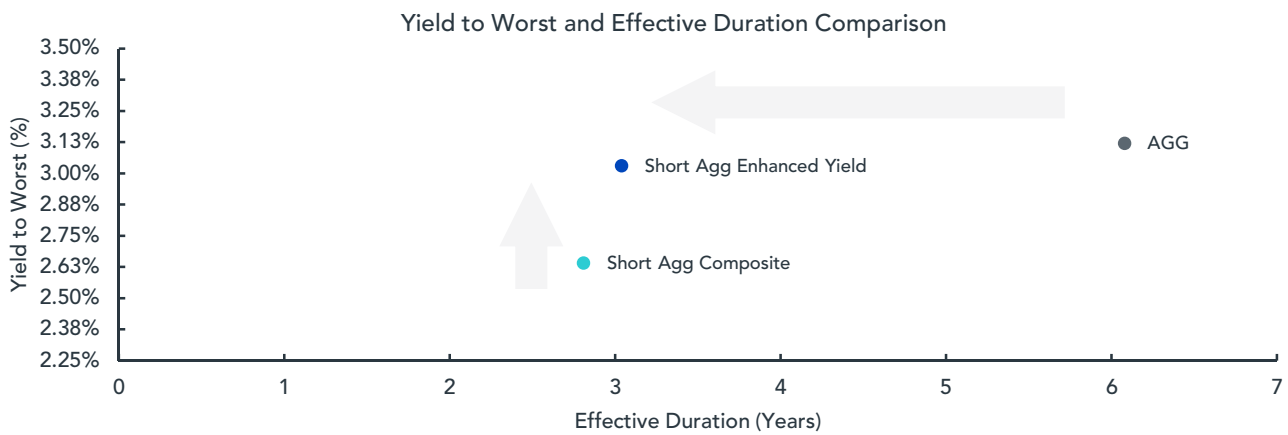
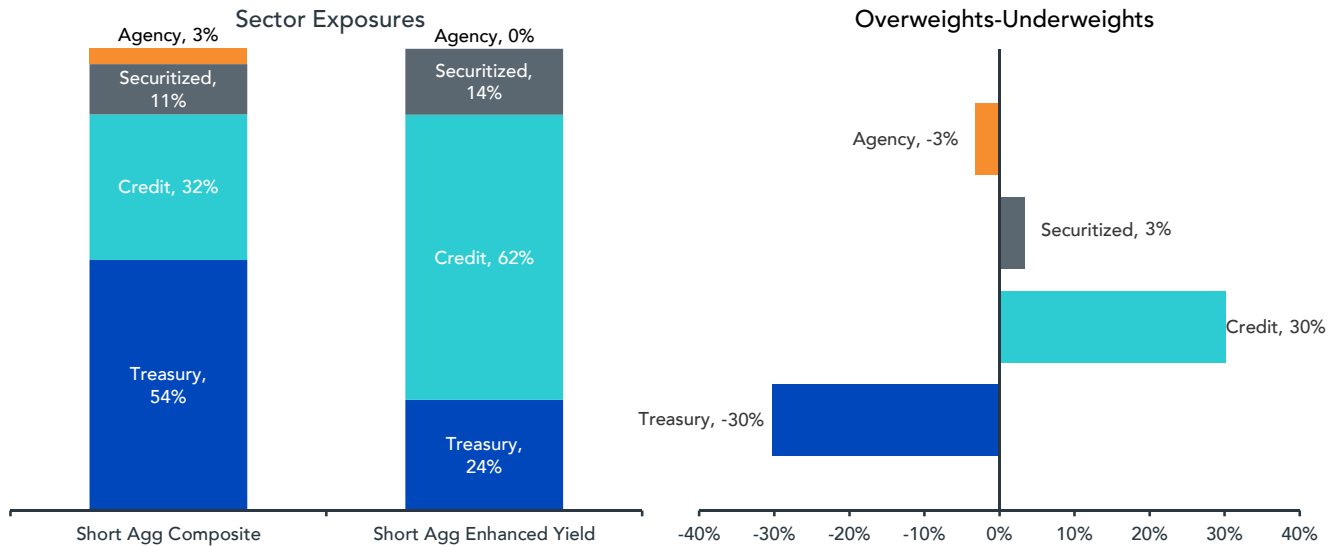
<sup>7</sup> Tracking error volatility: The volatility of the difference between the performance of a portfolio and its benchmark. In this case, the portfolio is the Short Agg Composite.

<sup>8</sup> Duration: A measure of a bond's sensitivity to changes in interest rates. The weighted average accounts for the various durations of the bonds purchased as well as the proportion of the total government bond portfolio that they make up.

<sup>9</sup> Rebalance: An index is created by applying a certain set of selection and weighting rules at a certain frequency.

<sup>10</sup> Source: Bloomberg, as of 3/31/2018.

**SHORT AGG ENHANCED YIELD VS. SHORT AGG COMPOSITE [ As of 3/31/2018 ]**



**For core investors, one could expect diversified exposure with significantly less rate risk and only a small sacrifice in income. For more conservative investors, one could expect as sizable yield enhancement with only slightly more rate risk.**

Source: Bloomberg, as of 3/31/2018. Past performance is not indicative of future results. You cannot invest directly in an index. Yield to worst: The rate of return generated assuming a bond is redeemed by the issuer on the least desirable date for the investor. Effective duration: This statistic provides a measure of the sensitivity of the fund's price to changes in interest rates and is calculated as the weighted average of the individual bond effective durations. Effective duration recognizes that changes in interest rates may also change the expected cash flows generated by any underlying bonds with embedded options. The calculation is expanded to incorporate the contribution of derivatives to the overall interest rate risk sensitivity to the portfolio. 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.

**INTRODUCING WISDOMTREE BARCLAYS YIELD ENHANCED U.S. SHORT-TERM AGGREGATE BOND FUND (SHAG)**

To provide tradable access to the Short Agg Enhanced Yield, WisdomTree launched the **WisdomTree Barclays Yield Enhanced U.S. Short-Term Aggregate Bond Fund (SHAG)**. By sourcing opportunities within the Agg, SHAG offers the opportunity to enhance the income potential of a core bond portfolio, while continuing to benefit from the diversification of a multisector portfolio.

**WisdomTree Barclays Yield Enhanced U.S. Short-Term Aggregate Bond Fund  
Quick Facts**

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**Ticker:** SHAG

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**Exchange:** BATS

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**Expense Ratio:** Net expense ratio, amount charged to shareholder\*: .12%

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**Gross expense ratio:** .20%

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**Structure:** Open-end ETF

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**Target Exposure:** U.S. dollar-denominated, investment grade short-term fixed income

At WisdomTree, we do things differently. We build our ETFs with proprietary methodologies, smart structures and/or uncommon access to provide investors with the potential for income, performance, diversification and more.

**For more information about SHAG, contact your WisdomTree representative or visit [WisdomTree.com](http://WisdomTree.com)**

\*The net expense ratio reflects a contractual waiver of .08% through 12/31/18.

This Fund is new and has limited operating history. You cannot invest directly in an index.

**Investors should carefully consider the investment objectives, risks, charges and expenses of the Fund before investing. To obtain a prospectus containing this and other important information, please call 866.909.9473 or visit [wisdomtree.com](http://wisdomtree.com). Investors should read the prospectus carefully before investing.**

There are risks associated with investing, including possible loss of principal. Fixed income investments are subject to interest rate risk; their value will normally decline as interest rates rise. Fixed income investments are also subject to credit risk, the risk that the issuer of a bond will fail to pay interest and principal in a timely manner or that negative perceptions of the issuer's ability to make such payments will cause the price of that bond to decline. Investing in mortgage- and asset-backed securities involves interest rate, credit, valuation, extension and liquidity risks and the risk that payments on the underlying assets are delayed, prepaid, subordinated or defaulted on. Due to the investment strategy of the Fund, it may make higher capital gain distributions than other ETFs. Please read the Fund's prospectus for specific details regarding the Fund's risk profile.

Diversification does not eliminate the risk of experiencing investment losses.

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Bloomberg Barclays U.S. Aggregate Bond Index: Represents securities that are SEC-registered, taxable and dollar denominated. The index covers the U.S. investment-grade, fixed-rate bond market, with index components for government and corporate securities, mortgage pass-through securities and asset-backed securities. These major sectors are subdivided into more specific indexes that are calculated and reported on a regular basis. Bloomberg Barclays U.S. Short Aggregate Enhanced Yield Index: A constrained, rules-based approach that reweights the sector, maturity and credit quality of the Barclays U.S. Aggregate Index across various subcomponents in order to enhance yield maturing in one to five years.

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