A Growth Style for Two WisdomTree Dividend ETFs

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In the summer of 2013, WisdomTree launched two new exchange-traded Funds (ETFs) to generate exposure to a specific segment of the U.S. dividend-paying equity market: stocks with growth characteristics. Each tracks the performance of an underlying Index focused on a different size segment of the U.S. equity market: large caps and small caps. One question that has been asked: Isn't the U.S. dividend-focused ETF market a crowded and saturated market, with a lot of big ETFs, which makes it tough for newer funds to gain traction? To some extent, parts of the dividend market are indeed very crowded. But there are also segments of the dividend market—particularly those focused on growth-oriented investment strategies—where there is little or no other competition. **In the Large Growth and Small Growth Style Boxes** Nearly half of U.S. dividend-focused ETF assets and half of the dividend-focused ETFs by number (12 out of 24) are categorized as "Large Value" funds by Morningstar. This classification for most of the assets implies a high degree of overlap with various dividend strategies—meaning that their underlying methodologies end up generating portfolios with similar style characteristics. For this analysis, our initial universe consisted of ETFs listed on U.S. exchanges that track the performance of indexes that consist only of U.S. dividend payers. Any ETFs utilizing leverage or sector-specific exposures were excluded because we wanted to focus only on options that were broad based1.

U.S. Equity ETFs Focusing on Dividend Payers: 24 total, with $61.71 billion in assets under management

	Value	Blend	Growth
Large	12 funds $28.43 billion 46.1% of assets	6 funds $18.59 billion 30.1% of assets	1 fund $35.28 million 0.1% of assets
Mid	3 funds $13.85 billion 22.5% of assets	0 Funds	0 Funds
Small	1 fund $797.02 million 1.3% of assets	0 Funds	1 fund $2.50 million 0.0% of assets

Source: Morningstar Direct, July 30, 2013.
The Morningstar style box is a nine-square grid that classifies securities by size along the vertical axis and by style (Value and Growth Characteristics) along the horizontal axis. Morningstar's equity style methodology uses a building block, holdings-based approach. Funds are classified as large, mid, or small based on the market capitalization of its portfolio holdings. Style is determined at the stock level and then those attributes are rolled up to determine the overall investment style of a fund.

For definitions of terms and indexes, visit our Glossary. • There were 24 funds in the universe of broad-based U.S.-listed ETFs, and these had a total of more than $61 billion in total assets. • Approximately 99% of the assets in these 24 ETFs were classified by Morningstar as Large Value, Large Blend or Mid-Cap Value. If new broad-based dividend ETFs come into existence that are classified in these areas of the style box, they might have a more difficult time differentiating themselves from the options already in existence. • The style boxes that are notably “light” fall within the small-cap row as well as along the growth column. The singular funds represented in these areas are both WisdomTree Funds, the WisdomTree SmallCap Dividend Fund (DES) in the Small Value box, the WisdomTree U.S. Dividend Growth Fund (DGRW) in the Large Growth box, and the newest addition to WisdomTree’s lineup of U.S. dividend Funds, the WisdomTree U.S. SmallCap Dividend Growth Fund (DGRS) in the Small Growth box. We believe a major reason asset levels are currently smaller in the small-cap row and the growth column is that investors aren’t aware that dividend-focused options actually exist in these areas of the style box. DGRS was created with a methodology to select dividend-paying stocks with growth characteristics across the spectrum of U.S. small caps. The selection factors of DGRS include a multi-factor ranking process based on long-term earnings growth expectations, historical three-year average return on equity and historical three-year average return on assets. Historically, these variables tend to coincide largely with growth stocks—and stocks we believe have the most potential to grow dividends over time. We believe that many investors may not realize that small-cap U.S. equities are a viable pond in which to fish for companies with dividend growth potential. **Conclusion** As people try to make sense of the myriad investment options that exist within ETFs, our hope is that the above chart might help simplify the dividend-focused picture of U.S. equities. Many options exist, but most of them are categorized within a very limited portion of the style box. We'd encourage investors to recognize that U.S. dividend payers (and ETFs focused on them) can exist within the small-cap row as well as the growth column of the style box, giving the potential to offer differentiated exposure to complement existing dividend-focused strategies. 1The style box classifications and asset levels were sourced from Morningstar Direct, current as of July 30, 2013.

Important Risks Related to this Article

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