

Introducing the WisdomTree Emerging Markets ex State Owned Enterprises Fund (XSOE)

Published December 10, 2014

Tripp Zimmerman, CFA

Director, Research

When investing in emerging markets, investors always accept a degree of geopolitical risk. But in certain countries and regions, like China, Russia and Brazil, this risk may be even more pronounced. And when companies are partially or wholly owned by the government, known as “state-owned enterprises” (SOEs), the risk may be even more pronounced because the government may influence corporate decisions that are not necessarily in the best interests of investors. Now, for the first time, WisdomTree offers a solution: the WisdomTree Emerging Markets ex-State-Owned Enterprises Fund (XSOE) provides investors with a way to capitalize on the opportunities of emerging markets without the politics involved with state-owned enterprises. The Fund is designed to track the performance of the [WisdomTree Emerging Markets ex-State-Owned Enterprises Index \(EMXSOE\)](#) after costs, fees and expenses. The first step in attempting to avoid SOEs is to understand where they are most common. The concentration of state-owned enterprises tends to be highest in countries like China, Brazil and Russia, which account for approximately 65% of the total state-owned enterprise market cap.¹ On a sector basis, ownership tends to be concentrated among the public good sectors, such as Financials, Energy, Telecom and Utilities, which are among the most systemically important sectors to economic development. The flip side to where the SOEs are, of course, is where they aren't. Currently, governments are less involved in the Consumer Discretionary and Consumer Staples, Information Technology and Health Care sectors, as these are considered less vital to strategic economic development and government welfare. In an attempt to limit any country and sector selection risks after the removal of state-owned enterprises, the Index employs a modified float-adjusted market-capitalization weighting process to target the weights of countries in the universe **prior to the removal of state-owned enterprises** while also limiting sector deviations to 3% of the starting universe float-adjusted market. This unique index weighting process and the sector differential caps provide a type of beta exposure to the emerging markets after the removal of state-owned enterprises. Even with similar sector and country exposure to market cap emerging market exposure, there are still differences in composition, valuations and other characteristics. Comparing the dividend yield and [price-to-earnings \(P/E\) ratios](#) of the WisdomTree Emerging Market ex-State-Owned Enterprises Fund against a market cap-weighted emerging market index showed ex-State-Owned Enterprises to be slightly more expensive. On the other hand, the ex-State-Owned Enterprises Index displayed higher growth expectations.² Firms that have exhibited higher growth typically trade at premium [earnings multiples](#), and they also tend to have lower dividend yields because they reinvest the majority of their earnings. As emerging market countries

have grown and transformed, investors have demanded more ways to gain access to this unique asset class. Recently, some investors have expressed concern over state-owned enterprises, and they have sought tools to limit their exposure, even after understanding the valuation differences. Investors who are interested in concentrating their exposure on the private sector and accessing the higher growth potential should find XSOE a useful tool. For full research on the Emerging Markets ex-State-Owned Enterprises Index [click here](#). 1Sources: WisdomTree, Standard and Poor's, as of 7/31/14. 2Sources: WisdomTree, Bloomberg, as of 9/30/14.

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. Investments in emerging or offshore 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 and intervention or political developments. Funds focusing their investments on certain sectors and/or regions increase their vulnerability to any single economic or regulatory development. This may result in greater share price volatility. Investments in currency involve additional special risks, such as credit risk and interest rate fluctuations. The Fund invests in the securities included in, or representative of, its Index regardless of their investment merit, and the Fund does not attempt to outperform its Index or take defensive positions in declining markets. Please read the Fund's prospectus for specific details regarding the Fund's risk profile.