Middle East Dividend Index Reaches New High

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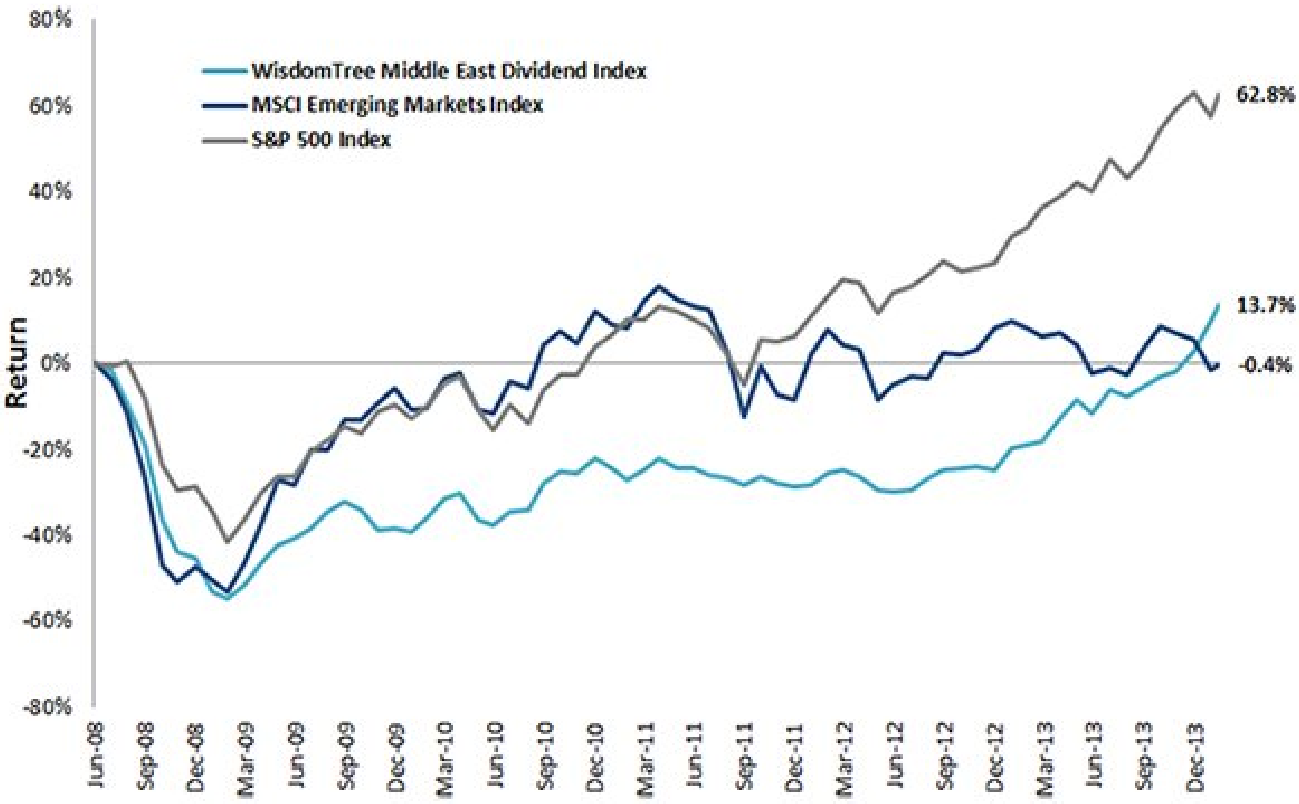
With the emerging markets embroiled in a storm of currency weakness and disappointing recent performance, some investors have decided to abandon the space, as illustrated by recent asset flows. Consequently, I recently wrote here that emerging markets remain some of the cheapest markets around the globe and investors shouldn't abandon the asset class but instead focus on the fundamentals through a rules-based strategy. While it may take time for the negative sentiment to change within traditional emerging markets, I wanted to highlight one standout of relative strength. Interestingly, when one looks at various emerging market countries, a number of the "emerging" emerging markets—or the countries that are often included in frontier market indexes—have diverged from some of the more popular emerging countries. **Middle East Countries Divergence** In May of 2013, I wrote about the divergence of a few Middle East countries during the first half of last year and suggested there could be further potential gains after Qatar and the United Arab Emirates (UAE) were upgraded to emerging market status by Morgan Stanley Capital International (MSCI). Since then, the region has reached new highs and continues to separate from traditional emerging market indexes. To illustrate this point, I will graph the WisdomTree Middle East Dividend Index (WTEMME) since inception against both the MSCI Emerging Markets Index (MSCI EM) and the S&P 500 Index. **Index Performance**



Sources: WisdomTree, Bloomberg (07/01/2008–02/14/2014). You cannot invest directly in an index. Past performance is not indicative of future results.

• **WisdomTree Middle East Dividend Index Reaches New High –** The Index finished the most recent calendar year with a gain of over 37%, putting it at an all-time high and pushing its cumulative return since inception into positive territory for the first time. Year-to-date, WTEMME continues to forge new highs, up close to 10.5%, outperforming both the S&P 500 and MSCI EM by over 10% and almost 16%, respectively.1
• **WTEMME Continues to Diverge from MSCI EM –** Since the start of last year, WTEMME has finally started to trend higher after a few years of sideways consolidation, and this improvement started only after it was announced by MSCI in June of 2013 that Qatar and the UAE would be upgraded to emerging market status in June 2014. It is impossible to know what the new country weights are going to be in the future, but we did know that market participants would need to add exposure to Qatar and the UAE. As a result, it was expected that these markets would converge upon the traditional emerging markets. But the Middle East countries did not stop there; they continued to move higher even as the emerging markets trended lower. I find this relative strength quite impressive, especially considering the year-to-date action, and I believe there is more to these countries than just the upgrade announcement. • While the Middle East Dividend Index went down nearly 1 for 1 with the emerging markets during the 2008 crisis for drops over 50%, the traditional emerging markets rebounded strongly in 2009 – with gains of over 70%, while the Middle East Dividend Index languished. It is making its way back from the crisis, and real estate and banking in particular have been doing well in the UAE. **Further Reasons to Consider the Middle East** Although the region has recently reached new highs, I think it still remains relatively attractive from a valuation perspective. WTEMME had a dividend yield of over 5%, surpassing the S&P 500 and MSCI EM indexes by over 3.1% and 2.3%, respectively. From a price-to-earnings perspective, WTEMME traded

at 11.5x expected earnings, a little above MSCI EM at 9.5x and below the S&P 500 Index at 15.6x.2 • **Valuations Remain Attractive after Strong Performance –** The weighted average performance of stocks within WTEMME domiciled in Qatar and the UAE were up over 29% and 99%, respectively. 3 Yet stocks within Qatar have a dividend yield of 4.36% and an estimated price-to-earnings ratio of 12.2x, while UAE stocks had a dividend yield of 2.8% and an estimated price-to-earnings ratio of 12.9x.4 • **Dividend Growth Supports Valuations –** Firms in the region have recently announced their proposed dividends for the 2013 calendar year, and some of the top weights in WTEMME had signaled for double-digit growth5: o Qatar National Bank – 16.7% increase o Industries Qatar – 29.4% increase o First Gulf Bank – 20.0% increase **Potential Diversification Benefits** Exposure to these Middle East countries represents a different type of emerging market allocation. This can be illustrated through WTEMME's historically low correlation with MSCI EM and S&P 500 Index. • 3-Year Monthly Correlation6: o MSCI EM vs. S&P 500 – 0.77 o WTEMME vs. S&P 500 – 0.56 o WTEMME vs. MSCI EM – 0.45 It is important to remember that regional returns can vary significantly year over year, and it is impossible to time the best-performing region. As a result, we think it is important to remain diversified across the different emerging or frontier countries and not focus just on the traditional countries. The WisdomTree Middle East Dividend Index tracks dividend-paying stocks in countries that tend to be under-weighted in many investors' portfolios. 1Sources: WisdomTree, Bloomberg (12/31/2013–02/14/2014). 2Sources: WisdomTree, Bloomberg (02/14/2014). 3Sources: WisdomTree, Bloomberg (12/31/12–12/31/13). 4Sources: WisdomTree, Bloomberg (02/14/2014). 5WTEMME Index Weight (02/14/14): Qatar National Bank (7.21%), Industries Qatar (7.13%) and First Gulf Bank (6.69%). 6Sources: WisdomTree, Zephyr StyleADVISOR (12/31/10–12/31/13).

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 the Middle East increase the impact of events and developments associated with the region, which can adversely affect performance. Investments in emerging, offshore or frontier markets such as the Middle East 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. Investments focused in Qatar or the United Arab Emirates are increasing the impact of events and developments associated with the region, which can adversely affect performance. Diversification does not eliminate the risk of experiencing investment losses.