

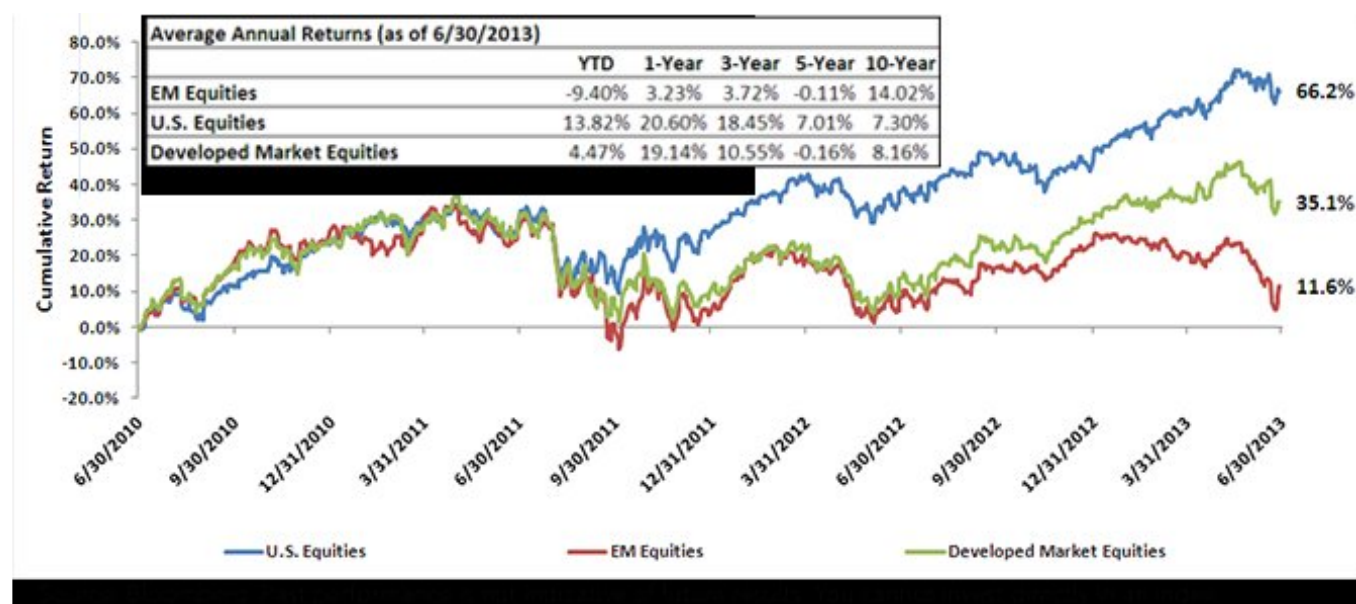
The Search for High Quality and Dividend Growth in the Emerging Markets

Published July 30, 2013

Jeremy Schwartz, CFA

Global Chief Investment Officer

In the last few months, WisdomTree has introduced a new family of dividend growth Indexes that cover a spectrum of different equity markets: from large-cap U.S. stocks to U.S. small caps, to global markets outside the U.S., and now an Index dedicated to the emerging markets. The creation of these dividend growth Indexes falls in a time when the market is digesting news from the U.S. Federal Reserve that its unprecedented accommodative easing may be coming to an end. Investors are beginning to contemplate what a higher interest rate environment could mean for high-dividend-yielding stocks, as these have been some of the top performers of the equity market in the last few years¹. One surprising element of global equity market performance, to us, has been the subpar performance of the MSCI Emerging Markets Index (EM Equities) over the three years ending June 30, 2013. While U.S. equities had a cumulative 66.2% total return from July 1, 2010, to June 30, 2013 (18.5% per year), EM Equities returned only a cumulative 11.6% over that time frame (just 3.7% per year). The MSCI EAFE Index (Developed Market Equities) rests between U.S. Equities and EM Equities (approximately 10.6% per year)². **Figure 1: EM Equities Deliver Lackluster Performance (6/30/2010–6/30/2013)**



We think the fact that EM Equities have been lagging could present a good opportunity to think about new tools, such as baskets of emerging market dividend growth stocks, that could potentially provide differentiated exposure that adds value to traditional portfolio allocations. **Combining a Focus on Dividend**

Growth Stocks with Relative Value Rebalancing WisdomTree believes that a focus on growth-oriented companies must be married with a disciplined focus on valuations, and when we consider dividend growth potential as a component of index methodology, we always marry it with other elements that yield a sensitivity to valuation. Specifically, WisdomTree uses a rules-based rebalancing program that involves tying Index constituent weights back to the *Dividend Stream*® to focus on valuations—as it does in all its dividend-based Indexes. What is unique about this new growth Index methodology are the stock selection factors we have identified as important drivers of dividend growth over time. These factors diverge from a sole focus on past dividend growth behavior to determine potential future dividend growth behavior. **Introducing the WisdomTree Emerging Markets Dividend Growth Index (WTEMDG): Selection Criteria and Rationale**

- Starting universe is stocks in WisdomTree Emerging Markets Dividend Index (WTEMI), a universe of 1,210 stocks with a combined market capitalization of \$7.4 trillion as of June 30, 2013.
- Must have a dividend coverage ratio greater than 1.0x.
- The Index comprises the top 50% of companies with the best combined rank of growth and quality factors from this universe.
- **Growth Ranking 50%:** Long-term earnings growth expectations
- **Quality Ranking 50%:** Evenly split between three-year average return on assets (ROA) and three-year average return on equity (ROE)

Weighting: The Index is dividend weighted to reflect the proportionate share of the aggregate cash dividends. **Single Holding and Sector Caps:** At the annual rebalance, the following caps apply: No single stock can represent more than 5% of the Index, and no sector or country can represent more than 20%. Between annual rebalances, single stocks may fluctuate above 5% and countries or sectors may fluctuate above 20% due to market movement. **Figure 2: Key Characteristics of WTEMDG Index**

Index	Long-Term Earnings Growth Expectations	ROE	ROA	Leverage	Earnings Retention	ROE x Earnings Retention
WisdomTree Emerging Markets Dividend Growth Index	14.8%	22.0%	12.1%	1.8x	68.4%	15.1%
WisdomTree Emerging Markets Equity Income Index	7.6%	16.1%	9.2%	1.8x	45.4%	7.3%
MSCI Emerging Markets Index	11.1%	15.8%	7.3%	2.2x	70.7%	11.2%
MSCI Emerging Markets Value Index	9.5%	14.3%	6.4%	2.2x	68.7%	9.8%
MSCI Emerging Markets Growth Index	12.3%	17.7%	8.2%	2.2x	73.2%	12.9%

For definition of indexes in the chart, please visit our glossary. **The WTEMDG Index Methodology Increases:**

- **Growth Factor:** Long-Term Earnings Growth Expectations.
- **Quality Factor:** ROE & ROA. Companies that show higher ROE and ROA are able to fund growing dividends due to these higher levels of profitability.
- **Earnings Retention:** Earnings that are retained and then reinvested efficiently (through a high ROE) could become future dividend payments.

The WTEMDG Index Methodology Decreases:

- **Exposure to companies with high leverage**

Conclusion: A Differentiated Exposure for Emerging Market Equities WisdomTree has been a pioneer in creating options around the universe of dividend payers in the emerging markets. As of June 30, 2013, over 90% of the market capitalization of emerging market equities is in dividend-paying firms, so we believe a focus on dividend payers in emerging markets doesn't sacrifice any breadth of coverage or representativeness of the universe. While many dividend-focused indexes in emerging markets focus on yield and valuation, there is a dearth of options that focus on dividend growth. We believe that the WTEMDG approach with its flexibility to

respond to growth potential rather than past dividend behavior exhibits greater congruence with actual underlying dividend behavior. Just like the other dividend growth indexes we have created, we believe the WisdomTree Emerging Markets Dividend Growth Index represents the future of dividend growth-oriented indexing. **Unless otherwise stated, data source is WisdomTree.** 1Refers to the S&P 500 Consumer Staples, Health Care, Telecommunication Services and Utilities indexes over the period from 6/30/2010 to 6/30/2013. 2Source: Bloomberg.

Important Risks Related to this Article

Dividends are not guaranteed and a company's future abilities to pay dividends may be limited. A company currently paying dividends may cease paying dividends at any time. Past performance is not indicative of future results. You cannot invest directly in an index.