Jeremy Schwartz has served as WisdomTree’s Executive Vice President, Global Head of Research since November 2018 and leads WisdomTree’s investment strategy team in the construction of WisdomTree’s equity indexes, quantitative active strategies and multi-asset model portfolios. Mr. Schwartz joined WisdomTree in May 2005 as a Senior Analyst, adding to his responsibilities in February 2007 as Deputy Director of Research and thereafter, from October 2008 to October 2018, as Director of Research. Prior to joining WisdomTree, he was head research assistant for Professor Jeremy Siegel and helped with the research and writing of Stocks for the Long Run and The Future for Investors. Mr. Schwartz also is co-author of the Financial Analysts Journal paper, What Happened to the Original Stocks in the S&P 500? He received his B.S. in Economics from The Wharton School of the University of Pennsylvania and hosts the Wharton Business Radio program Behind the Markets on SiriusXM 132. Mr. Schwartz is also a member of the CFA Society of Philadelphia.

Rick Harper serves as the Head of Fixed Income and Currency for WisdomTree Asset Management, where he oversees the firm’s suite of fixed income and currency exchange-traded Funds. Rick has over 22 years of investment experience in strategy and portfolio management positions at prominent investment firms. Prior to joining WisdomTree in 2007, Rick held senior-level strategist roles with RBC Dain Rauscher, Bank One Capital Markets, ETF Advisors and Nuveen Investments. At ETF Advisors, he was the Portfolio Manager and developer of some of the first fixed income exchange-traded funds. His research has been featured in leading periodicals, including the Journal of Portfolio Management and the Journal of Indexes. He graduated from Emory University and earned his MBA at Indiana University.

As part of WisdomTree’s Investment Strategy group, Kevin Flanagan serves as the Head of Fixed Income Strategy. In this role, he contributes to the asset allocation team, writes fixed income-related content and travels with the sales team, conducting client-facing meetings and providing expertise on WisdomTree’s existing and future bond ETFs. In addition, Kevin works closely with the fixed income team. Prior to joining WisdomTree, Kevin spent 30 years at Morgan Stanley, where he was most recently a Managing Director. He was responsible for tactical and strategic recommendations and created asset allocation models for fixed income securities. He was a contributor to the Morgan Stanley Wealth Management Global Investment Committee, primary author of Morgan Stanley Wealth Management’s monthly and weekly fixed income publications and collaborated with the firm’s Research and Consulting Group Divisions to build ETF and fund manager asset allocation models. Kevin has an MBA from Pace University’s Lubin Graduate School of Business and a B.S. in finance from Fairfield University.
MACRO BACKDROP

With Q1 now in the rearview mirror, our U.S. outlook—for some softening in economic activity—appears to be on track. Our base case scenario does not involve a potential recession, but rather a slowing from the roughly 3.0% real gross domestic product (GDP)\(^1\) print of 2018. The question now becomes, just what type of slowdown should investors expect in 2019?

The mixed data that investors have witnessed thus far for Q1 should not come as a surprise. The economy was confronted with a variety of challenges to begin 2019, with the government shutdown, polar vortex and a tightening in financial conditions all standing out as potential negative influences. Consensus forecasts for Q1 real GDP are centered around the 1.5% level, but some estimates are as low as 0.5%.

In our opinion, the opening three-month frame will represent the trough in this year’s economic activity, with growth returning to a more balanced 2.0%–2.5% range for the remainder of the year. The three aforementioned “negative influences” have been removed, potentially lifting the cloud of uncertainty as a result. The government shutdown and inclement winter weather are certainly behind us, but perhaps more importantly, financial conditions have eased considerably (more on this later).

Growth is expected to slow on a global basis as well, and economic forecasts for this outlook also do not include any imminent downturns. The two areas that are being watched closely are China and the eurozone. With respect to China, recent economic data could be providing a hint that policy-related stimulus measures may be bearing some fruit, but with respect to the eurozone, the outlook remains less promising. In fact, the European Commission downgraded their 2019 GDP estimate for the region to 1.3%, similar to consensus forecasts. On a specific country basis, Italy entered into a technical recession while Germany is barely above water.

FED WATCH

Without a doubt, the Fed outlook changed considerably during Q1. The Fed’s own “blue dot” forecast for two rate hikes at its December meeting has now been revised down to zero increases for this year.

It has become increasingly apparent that Chair Powell & Co. are operating with an overabundance of caution, and are truly letting their data-dependent mantra play out. With inflation expectations relatively muted, the Fed can afford to be patient, even though Powell has stated more than once that the economy is “in a good place.”

At this point, we will take the Fed at its word regarding 2019 rate hikes. However, if our base case growth scenario continues to play out for the remainder of 2019, we will not rule out one rate increase in December. Given that Federal Funds Futures, as recently as late March, were priced for a rate cut later this year and for two more in 2020, the Fed will have its work cut out for it, if in fact it does have to switch gears. Remember, the blue dots made NO mention of rate cuts, and, in fact, still had a rate hike scheduled for 2020.

\(^1\) Gross domestic product (GDP): The sum total of all goods and services produced across an economy.
THE YIELD CURVE INVERTS

In late March, the big news was that the U.S. Treasury (UST) 3-month/10-year yield curve became inverted for the first time since 2007. It was certainly a noteworthy development in bond-land, but as of this writing, the closely watched UST 2s/10s spread has yet to invert and is still at 17 basis points (bps). In fact, the UST 3-month/10-year inversion may have been one of the shortest on record, lasting only five days before going back to the positive side. The magnitude of the inversion, about 6 bps at its peak, pales in comparison to the prior two episodes, of more than 50 bps and nearly 100 bps, respectively.

Notably, the recent decline in Treasury yields essentially served as a quarter-point rate cut for the Fed, without the policymakers having to lift a finger. In effect, one of the Fed’s primary concerns of late—a tightening in financial conditions—has been removed. First, we had the bounce back in equities and credit spreads, but now a whole new dynamic has entered into the equation: a stealth rate cut.

APPROACHING FIXED INCOME ALLOCATIONS

The second half of Q1 seemed to see more of an interest in longer-duration fixed income products, at the expense of short-term instruments. A dovish Fed, combined with a more bearish economic outlook were the primary culprits, but it does raise the question: are investors being compensated for such an approach?

With the Fed hiking nine times in this tightening cycle, short rates have soared above the level of typical investment manager fees. Treasury Bill positions are no longer a net cost to performance and can offer a strategic source of return. Combined with the recent decline in longer-dated yields, higher short rates change the calculus of positioning portfolios. Investors need a higher level of conviction when taking on interest rate risk. The flat and/or inverted 3-month/10-year curve underscores this point. At post-Federal Open Market Committee March meeting levels, longer duration yields leave little, if any, margin for error, and highlight the relative value opportunities at the shorter end of the yield curve.

Beyond domestic interest rate markets, valuations in many sectors remain full, or nearly so.

We are neutral on investment-grade (IG) credit and mortgage-backed securities. Diversifying across alpha sources and raising the fundamental profile of investments will be essential in delivering absolute returns as we move forward.

The health of the credit market remains a hot topic for both investors and the financial media this year. Increasing leverage and weakening covenants, amid a backdrop of rising rates, aging expansion and escalating trade tensions, have heightened investors’ concerns. The dominance of BBB issues has become the focus for the IG universe. Leveraged loans and the funds that package them have come under similar scrutiny, with structural considerations augmenting concerns about the explosion of issuance since the financial crisis.

These concerns came to a head in Q4, during the markets’ risk-off period. The widening in both IG and high-yield (HY) spreads reached their crescendo on January 3 of this year. On that day, IG spreads peaked at 157 bps, while HY hit a highwater mark of 537 bps. These were the highest levels since 2016 and represented a total widening of 52 bps and 234 bps, respectively, from the lows printed in early October.

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2 Basis point: 1/100th of 1 percent.
3 Investment grade: A rating given to a municipal or corporate bond. It is a relatively favorable rating, by either Moody’s or Standard & Poor’s, indicating a higher chance an issuer performs interest and principal obligations as promised by the terms of the debt issuance.
4 Mortgage-backed securities: Fixed income securities that are composed of multiple underlying mortgages.
5 High yield: Sometimes referred to as “junk bonds,” these securities have a higher risk of default than investment-grade securities.
Since these peak readings were printed, IG differentials have managed to come in by almost 40 bps, a nearly 75% reversal. HY spreads have narrowed by a little more than 160 bps, recouping more than two-thirds of their prior widening.

We anticipate corporate fundamentals will continue to be supported for the rest of the year as the domestic economy continues to expand. We do, however, acknowledge that corporate credit fundamentals have likely peaked for this expansion. Additionally, we anticipate a greater dispersion across issuer fundamentals going forward. With a period of inexpensive financing behind us, there will likely be a greater focus on corporations deleveraging their balance sheets.

Investors may want to focus on issuers with more attractive fundamentals and a greater ability to deleverage. Combining the “up in quality” approach with a tilt toward value should best position credit portfolios for the coming year. With rate positioning remaining a challenge, we prefer HY securities over more rate-sensitive IG corporate issues.

Given trade tensions with China and the recent risk-off sentiment, local emerging markets debt might seem like an odd choice as a potential source of alpha in fixed income portfolios. Timing and sentiment remain critical in unlocking value from local debt investments. If our base case is realized, some of the most pressing fears regarding emerging markets are likely to dissipate. Reduced fears of soaring U.S. rates, a more stable China and a de-escalation of trade tensions could create a better backdrop for local emerging markets debt to contribute to fixed income portfolio performance.

WHAT IS WISDOMTREE’S OUTLOOK FOR GLOBAL EQUITY MARKETS IN 2019?

Our equity model portfolios go into Q2 2019 with the same positioning we started 2019 with, particularly for the U.S. markets. The Q4 market swoon transitioned to a Q1 boom—for risk market prices, if not for underlying economic gauges. The dire-looking global manufacturing gauges may have bottomed in Q1, particularly for those economies suffering from a China trade oriented slow down. Chinese stimulus in Q1 may percolate further into growth for global markets and economies in the rest of 2019.

We have expressed concern that rising volatility, especially during Q4, was over-extending valuations in low-volatility stocks. As of March 31, 2019, the MSCI USA Minimum Volatility Index had price-to-earnings (P/E) ratios that were a few points higher than those of the S&P 500 Index, despite this segment of the market being concentrated in slower-growing, lower-profitability companies.

When we sort the MSCI USA Index into volatility quintiles, we find that the lowest-volatility quintile has typically been priced at a P/E discount to the broad index, and has also been more profitable as measured by return-on-equity (ROE). As of March 31, 2019, however, the lowest-volatility quintile had a P/E ratio of 19.44x, a bit higher than that of the MSCI USA Index, while historically this quintile has traded at a discount. This widening P/E multiple premium for the least volatile stocks is accompanied by deteriorating quality metrics. Historically, the ROE of low volatility stocks has been 2.3% higher than the average stock, but now it is 2.5% lower.

Above-normal valuations, with below-normal quality tilts, does not make an attractive fundamental combination, in our view.

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6 Price-to-earnings (P/E) ratio: Share price divided by earnings per share. Lower numbers indicate an ability to access greater amounts of earnings per dollar invested.

7 Return-on-equity (ROE): Measures a corporation’s profitability by revealing how much profit a company generates with the money shareholders have invested.
These poor fundamental attributes imply hidden risk in this very popular and crowded factor. This “low vol” factor was the best-performing factor in 2018, outperforming the market by over 500 bps. Despite the worries of rising volatility and the inverted yield curve, we’d be cautious about this factor.

Our favorite three exposures to the U.S. markets for 2019 offer compelling valuations and are well positioned for rising volatility. The three funds are:

+ **DGRW**: WisdomTree U.S. Quality Dividend Growth Fund (P/E: 15.0x, ROE: 24.0%)
+ **USMF**: WisdomTree U.S. Multifactor Fund (P/E: 14.5x, ROE: 17.7%)
+ **EES**: WisdomTree U.S. SmallCap Fund (P/E: 11.3x, ROE: 14.8%)

The equally weighted combination of these three ETFs sell at 13.4x forward earnings and are of a generally higher quality than most, with a 19% ROE. For reference, the S&P 500 sells at a forward P/E of 16.7x and an ROE of 16.6%.

Quality at reasonable price: While there are concerns that quality stocks are expensive, DGRW’s approach shows lower forward-looking valuations than the S&P 500, with a meaningful improvement in ROE profitability gauges. We continue to prefer that trade-off.

Similarly, given EES’s P/E ratio of 10x–11x for trailing and estimated 2019 earnings, we believe fears of overvaluation in equities can be managed with this basket of 900 stocks. These small-cap stocks are definitely more cyclical in nature and fears of recession, or at the very least profit margin compression, are keeping their valuations low. However, if a recession does not materialize this year, we think there is still opportunity in this segment.

Sources: WisdomTree, FactSet. Past performance is not indicative of future results. You cannot invest directly in an index.

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### Price-to-Earnings Ratio (1/31/02—3/31/19)

<table>
<thead>
<tr>
<th></th>
<th>Low-Vol Quintile</th>
<th>MSCI USA Index</th>
<th>Low Vol Discount/Premium</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Current P/E</strong></td>
<td>19.44x</td>
<td>19.23x</td>
<td>101.1%</td>
</tr>
<tr>
<td><strong>Historical Median P/E</strong></td>
<td>16.14x</td>
<td>17.48x</td>
<td>94.0%</td>
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<tr>
<td><strong>Difference</strong></td>
<td>3.30x</td>
<td>1.75x</td>
<td>7.1%</td>
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</table>

### Return-on-Equity (1/31/02—3/31/19)

<table>
<thead>
<tr>
<th></th>
<th>Low-Vol Quintile</th>
<th>MSCI USA Index</th>
<th>Low Vol Discount/Premium</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Current ROE</strong></td>
<td>13.9%</td>
<td>16.4%</td>
<td>84.7%</td>
</tr>
<tr>
<td><strong>Historical Median ROE</strong></td>
<td>17.4%</td>
<td>15.1%</td>
<td>116.4%</td>
</tr>
<tr>
<td><strong>Difference</strong></td>
<td>-3.5%</td>
<td>1.4%</td>
<td>-31.7%</td>
</tr>
</tbody>
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8 Unless otherwise noted, valuations in the section are as of 3/29/19. Data from WisdomTree, FactSet.
<table>
<thead>
<tr>
<th>Fund Information</th>
<th>Total Return NAV (%)</th>
<th>Market Price (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Fund</strong></td>
<td><strong>Ticker</strong></td>
<td><strong>Exp. Ratio</strong></td>
</tr>
<tr>
<td>WisdomTree U.S. Quality Dividend Growth Fund</td>
<td>DGRW</td>
<td>0.28%</td>
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<td>WisdomTree U.S. SmallCap Fund</td>
<td>EES</td>
<td>0.38%</td>
</tr>
</tbody>
</table>

Performance is historical and does not guarantee future results. Current performance may be lower or higher than quoted. Investment returns and principal value of an investment will fluctuate so that an investor’s shares, when redeemed, may be worth more or less than their original cost. Performance data for the most recent month-end is available at wisdomtree.com. WisdomTree shares are bought and sold at market price (not NAV) and are not individually redeemed from the Fund. Total returns are calculated using the daily 4:00 p.m. ET net asset value (NAV). Market price returns reflect the midpoint of the bid/ask spread, as of the close of trading on the exchange where Fund shares are listed. Market price returns do not represent the returns you would receive if you traded shares at other times. 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.

Finally, USMF can anchor a portfolio with a combination of fundamental and technical screening factors. We expect to see a continuation of its strong returns, with reduced volatility compared to broad market benchmarks, for some time.

International markets bore the brunt of investor angst and selling in 2018. We still generally favor the U.S. over Europe. But we also suggest over-weight positions in Japanese small caps, which typically benefit from low valuations, improved corporate governance impacting shareholder returns and generally lower correlations to U.S. markets.

Emerging markets, which tend to perform well when global growth accelerates, declined in lockstep with Chinese markets in 2018 and led the markets higher in Q1. Expectations and market prices reflect a trade deal with China being signed during Q2—and if those negotiations fall apart, that is certainly a risk to our bullish thesis.

Emerging markets valuations are the lowest among the major regions. In many ways, their growth profiles and long-run opportunities are the best. We also think fiscal stimulus by China during Q1 will help revitalize parts of the global economy under stress and that the dire global trade stats may bottom out during Q2.

Our preferred emerging markets allocation combines long-run growth opportunities—exemplified by our ex-state-owned strategy that over-weights consumer, technology, and internet companies—and a multifactor strategy that is more defensive. This emerging markets strategy incorporates a currency-factor model that raises and lowers the beta profile dynamically, based on currency momentum signals. This is a powerful combination to balance the risk-reward tradeoff we see in the emerging markets: accessing the opportunity offered by favorable valuations while mitigating the short-term risks associated with a stronger dollar and more widespread volatility.
HOW IS WISDOMTREE THINKING ABOUT CURRENCY RISK?

A primary risk to our view that emerging markets look poised to outperform global markets in 2019 is another year of continued U.S. dollar strength. Entering 2018, the consensus forecast was for a weaker U.S. dollar. But the dollar rose nearly 5%, as measured by the Bloomberg Dollar Total Return Index. In 2019, many strategists are again forecasting a weaker dollar.

Our core thesis remains that investors take on too much uncompensated currency risk by always being long foreign currency and betting strategically on the dollar’s demise when they invest internationally. We believe a 50/50 hedge ratio is a more neutral international benchmark, while being fully hedged in the developed world can help minimize unrewarded volatility.

WisdomTree found that interest rate differentials often have a significant impact on the relative pricing of currencies. Today, U.S.-dollar-based investors are picking up nearly 3% by hedging the euro, and just over 2.6% by hedging the yen. In other words, foreign currencies must appreciate by at least these amounts in order to break even with hedging these currencies.

Bottom line: far from being expensive to hedge, as many assume, in the developed world, investors are paid a large and increasing amount of carry to be neutral on foreign currency risk. That is a trade-off we believe more investors may want to take.

On a more tactical view, our aggregate hedge ratio in the last three years, based on a three-factor model, was 60% hedged. But the latest hedge ratios in March were over 67% hedged—a higher hedge ratio than average. Our research suggests when our hedge ratios are higher than average, they have a higher probability of paying off more than average. This would imply a good possibility of another gain in the dollar in 2019, which is a dynamic most are not prepared for.

Investors should carefully consider the investment objectives, risks, charges and expenses of the Funds before investing. To obtain a prospectus containing this and other important information, please call 866.909.9473, or visit WisdomTree.com to view or download a prospectus. Investors should read the prospectus carefully before investing.

There are risks associated with investing, including possible loss of principal. Funds focusing their investments on certain sectors increase their vulnerability to any single economic or regulatory development. This may result in greater share price volatility. Due to the investment strategy of some Funds, they may make higher capital gain distributions than other ETFs. Please read each Fund’s prospectus for specific details regarding each Fund’s risk profile.

MSCI USA Minimum Volatility Index: Aims to reflect the performance characteristics of a minimum variance strategy applied to the large- and mid-cap segments of the U.S. market. MSCI USA Index: Designed to measure the performance of the large- and mid-cap segments of the U.S. equity universe. MSCI USA Minimum Volatility Index: Aims to reflect the performance characteristics of a minimum variance strategy applied to the large- and mid-cap segments of the U.S. market. MSCI USA Index: Designed to measure the performance of the large- and mid-cap segments of the U.S. equity universe. MSCI USA Minimum Volatility Index: Aims to reflect the performance characteristics of a minimum variance strategy applied to the large- and mid-cap segments of the U.S. market. MSCI USA Index: Designed to measure the performance of the large- and mid-cap segments of the U.S. equity universe. MSCI USA Minimum Volatility Index: Aims to reflect the performance characteristics of a minimum variance strategy applied to the large- and mid-cap segments of the U.S. market. MSCI USA Index: Designed to measure the performance of the large- and mid-cap segments of the U.S. equity universe.

Sources: WisdomTree, Bloomberg. Returns 12/29/17–12/31/18, as measured by Bloomberg Dollar Total Return Index.