

# INTERNATIONAL SMALL CAPS IN FOCUS

Jeremy Schwartz — Global Chief Investment Officer  
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On May 13, 2013, we wrote a blog entitled "[International Mid and Small Caps Offer Size and Sector Diversification](#)" -a piece highlighting the fact that although many focus strictly on the [MSCI EAFE Index](#) outside the United States, there might be benefits to looking at indexes outside the large-cap end of the capitalization spectrum. Today we address how WisdomTree's May 31, 2013, annual rebalance screen impacted the [WisdomTree International SmallCap Dividend Index \(WTISDI\)](#), an Index built to measure the performance of small-cap dividend payers in developed international markets.

**How WisdomTree Rebalances** It is important to note that [WisdomTree](#) adheres to a strict focus on [relative value](#) at its annual index rebalance. 1. Companies whose share prices have appreciated significantly but whose dividends haven't kept pace typically see their weights reduced. 2. Companies whose share prices have fallen but whose dividends have stayed constant or increased typically see their weights increased. When we look at the changes in exposures as well as the numbers relative to the MSCI EAFE Index, it's important to note that there are no views being taken—weighting is based on price performance relative to dividends. This rules-based rebalance program is an important part of the WisdomTree Index methodology's added value. Throughout this piece we use the MSCI EAFE Index for comparison purposes due to its broadness of exposure to international equity markets. **The Country Picture**

Top 10 Country Weights & Regional Breakdowns: WTISDI After 5/31/2013 Rebalance Screen

Country	WTISDI (as of 5/31/2013)			MSCI EAFE Index	WTISDI Weight (after Rebalance Screen) minus MSCI EAFE Index Weight
	Before Rebalance Screen	After Rebalance Screen	Change		
Japan	23.9%	25.1%	1.2%	21.4%	3.7%
Australia	13.0%	17.3%	4.2%	8.2%	9.1%
United Kingdom	14.9%	14.9%	0.0%	19.2%	-4.3%
Sweden	5.0%	5.1%	0.1%	3.2%	1.9%
Singapore	4.0%	4.5%	0.5%	1.7%	2.8%
Italy	6.0%	3.9%	-2.2%	2.1%	1.8%
Germany	3.9%	3.6%	-0.3%	8.7%	-5.1%
Hong Kong	2.8%	3.4%	0.6%	3.1%	0.3%
New Zealand	2.8%	3.1%	0.2%	0.1%	2.9%
Israel	2.6%	2.9%	0.3%	0.5%	2.4%
Europe <sup>1</sup>	53.5%	46.8%	-6.8%	64.7%	-17.9%
Asia & Pacific <sup>2</sup>	46.5%	53.2%	6.7%	34.5%	18.8%

Sources: WisdomTree, Bloomberg. Subject to change.

<sup>1</sup> Europe: Includes United Kingdom, Sweden, Italy, Germany, Israel, Finland, France, Switzerland, Belgium, Norway, Netherlands, Ireland, Spain, Austria, Portugal, Denmark and Greece.

<sup>2</sup> Asia & Pacific: Includes Japan, Australia, Singapore, Hong Kong and New Zealand.

## • Changes at 5/31/2013 Rebalance:

Australia saw the biggest absolute change—a 4.2% increase in weight. On the opposite end of the spectrum, Italy lost approximately 2.2% of its weight. Overall, WTISDI's exposure to Europe decreased approximately 7%, while its exposure to Asia & Pacific increased approximately 7%. In fact, all Asia & Pacific countries (Japan, Australia, Hong Kong, Singapore and New Zealand) saw weight increases. **• WTISDI Weights Compared to MSCI EAFE Index:** It is interesting that there are no double-digit under- or over-weights on the country side. Australia is the biggest over-weight at 9.1%, while Switzerland, France and Germany were some of the biggest under-weights at -7.6%, -6.8% and -5.1%, respectively. However, if one considers the exposures to Europe vs. the exposures to Asia & Pacific, a different picture emerges. WTISDI is nearly 20% under-weight in Europe and nearly 20% over-weight in Asia & Pacific compared to the MSCI EAFE

Sector Exposures & Defensive vs. Cyclical Breakdowns: WTISDI After 5/31/2013 Rebalance Screen

Sector	WTISDI (as of 5/31/2013)			MSCI EAFE Index	WTISDI Weight (after Rebalance Screen) minus MSCI EAFE Index Weight
	Before Rebalance Screen	After Rebalance Screen	Change		
Consumer Discretionary	24.7%	21.1%	-3.6%	11.5%	9.6%
Consumer Staples	6.6%	7.4%	0.8%	11.8%	-4.5%
Energy	2.3%	2.0%	-0.3%	7.2%	-5.1%
Financials	17.6%	16.2%	-1.4%	25.0%	-8.8%
Health Care	4.4%	3.4%	-1.0%	10.4%	-6.9%
Industrials	22.1%	25.0%	2.9%	12.5%	12.5%
Information Technology	8.5%	9.8%	1.3%	4.4%	5.4%
Materials	9.1%	10.6%	1.5%	8.5%	2.1%
Telecommunication Services	2.1%	2.4%	0.3%	5.0%	-2.6%
Utilities	2.6%	2.1%	-0.5%	3.8%	-1.7%
Defensive Sectors <sup>1</sup>	15.7%	15.3%	-0.4%	31.0%	-15.7%
Cyclical Sectors <sup>2</sup>	58.2%	58.7%	0.5%	39.6%	19.1%

Sources: WisdomTree, Bloomberg. Subject to change.

<sup>1</sup> Defensive sectors: Consumer Staples, Health Care, Telecommunication Services and Utilities.

<sup>2</sup> Cyclical sectors: Consumer Discretionary, Energy, Industrials and Materials.

Index. **The Sector Picture**

• **Changes**

**at the 5/31/2013 Rebalance:** Consumer Discretionary saw the biggest absolute change, with its weight decreasing by 3.6%, while Industrials gained the most (2.9%). Most of the other sector changes were quite small. • **WTISDI Weights Compared to MSCI EAFE Index:** The sector weights of WTISDI compared to the MSCI EAFE Index exhibit a much wider dispersion than does the country picture. Industrials are the standout—a 12.5% over-weight. But at 9.6%, Consumer Discretionary is also a rather large over-weight. We often describe the small-cap stocks as being more sensitive to the economic environment than large-cap stocks, and these two sector over-weight positions are part of that tilt. The under-weights in small caps compared to large caps come from the defensive sectors—Consumer Staples, Health Care, Telecommunication Services and Utilities. Collectively, the defensive sectors received 15.7% less weight in WTISDI than in the MSCI EAFE Index. On the other hand, cyclical sectors see almost 20% more weight in WTISDI than in the MSCI EAFE Index. **Conclusion** We believe that the [WisdomTree International SmallCap Dividend Index](#) rebalance affords a further opportunity to build on the picture of developed international small caps relative to the MSCI EAFE Index. In the near future, we shall turn our focus to the WisdomTree International MidCap Dividend Index in similar fashion.

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## **DEFINITIONS**

**MSCI EAFE Index** : is a market cap-weighted index composed of companies representative of the developed market structure of developed countries in Europe, Australasia and Japan.

**WisdomTree International SmallCap Dividend Index** : A fundamentally weighted index measuring the performance of the small-capitalization segment of the US dividend-paying market. The Index is comprised of the companies that compose the bottom 25% of the market capitalization of the WisdomTree Dividend Index after the 300 largest companies have been removed. The index is dividend weighted annually to reflect the proportionate share of the aggregate cash dividends each component company is projected to pay in the coming year, based on the most recently declared dividend per share.