UNCOVERING VALUE IN EMERGING MARKETS

Wisdomtree EU
16 Dec 2015

WisdomTree Europe

At WisdomTree, a critical way for us to identify valuation opportunities is through our annual index rebalance. Our process is designed to evaluate the underlying fundamentals of index constituents each year. For our dividend indices, this translates to reweighting companies in an index relative to their contribution to the *Dividend Stream®*—the sum total of all dividends paid within a given index. We impart a disciplined focus on valuation, typically by:

- Increasing weight to firms that are growing their dividends—especially in cases where share price performance has not yet responded
- Decreasing weight from firms that see their dividends decrease, especially following runs of strong share price appreciation

Looking at current valuations across the world, some of the lowest-priced stocks are found in the emerging markets, and if you screen and weight these securities based on fundamentals, you can improve the valuation characteristics even further. The WisdomTree Emerging Markets Equity Income Index screens by dividend yield and then weights by dividends, typically resulting in a deep value exposure. The Index provides a dividend yield advantage of almost 400 basis points (bps) and is priced 22% lower on a price-to-earnings (P/E) ratio basis, compared to the MSCI Emerging Markets Index. Figures 1 and 2 provide detailed changes in sector and country exposures for the WisdomTree Emerging Markets Equity Income Index.

- **Country Increases:**Typically EM Equity Income's value-seeking rebalancing process leads to adding weight to countries that underperformed and subtracting weight from countries that outperformed, but dividend growth also plays a role. So although Taiwan exhibited decent relative performance, its relative dividend growth was stronger, ultimately increasing the relationship between dividends and prices, earning a larger weight. Weight was also added to South Korea primarily due to strong dividend growth. More classic examples of where this strategy has typically added weight are Brazil and Indonesia. Both of these countries exhibited poor relative performance and had dividends grow at a higher rate than their price performance.
- **Country Decreases:**Although Russia exhibited poor performance over the period, its dividends contracted even more, decreasing the relationship between dividends and prices, earning a lower weight. Mexico and Malaysia also saw their weights lowered, both resulting from their dividends falling further than their price depreciation.

- **Sector Increases:** Again, typically EM Equity Income's value-seeking rebalancing process leads to subtracting weight from sectors that outperformed, but dividend growth also plays a role. So although the Information Technology sector displayed the highest relative performance, the sector also displayed the highest dividend growth, receiving a larger weight. Although the Materials sector saw dividends contract over the period, they didn't fall as much as the price performance, ultimately earning a higher weight because the relationship between dividends and price improved.
- **Sector Decreases:** It is no surprise to us, given the lower oil prices over the past year, that the Energy sector saw a decrease in weight, primarily driven by dividends decreasing. Financials saw the most significant decrease in weight, but the weight reduction is a result of a 25% sector-capping rule. Financials saw positive relative performance over the year, which allowed its weight to drift higher, so bringing it back in line with the capping rule is part of a rules-based, systematic process.

Investors sharing this sentiment may consider the following UCITS ETF:

WisdomTree Emerging Markets Equity Income UCITS ETF (DEM)

All data is sourced from WisdomTree Europe and Bloomberg, unless otherwise stated.

View the online version of this article here.

Important Information

Marketing communications issued in the European Economic Area ("EEA"): This document has been issued and approved by WisdomTree Ireland Limited, which is authorised and regulated by the Central Bank of Ireland.

Marketing communications issued in jurisdictions outside of the EEA: This document has been issued and approved by WisdomTree UK Limited, which is authorised and regulated by the United Kingdom Financial Conduct Authority.

WisdomTree Ireland Limited and WisdomTree UK Limited are each referred to as "WisdomTree" (as applicable). Our Conflicts of Interest Policy and Inventory are available on request.

For professional clients only. The information contained in this document is for your general information only and is neither an offer for sale nor a solicitation of an offer to buy securities or shares. This document should not be used as the basis for any investment decision. Investments may go up or down in value and you may lose some or all of the amount invested. Past performance is not necessarily a guide to future performance. Any decision to invest should be based on the information contained in the appropriate prospectus and after seeking independent investment, tax and legal advice.

The application of regulations and tax laws can often lead to a number of different interpretations. Any views or opinions expressed in this communication represent the views of WisdomTree and should not be construed as regulatory, tax or legal advice. WisdomTree makes no warranty or representation as to the accuracy of any of the views or opinions expressed in this communication. Any decision to invest should be based on the information contained in the appropriate prospectus and after seeking independent investment, tax and legal advice.

This document is not, and under no circumstances is to be construed as, an advertisement or any other step in furtherance of a public offering of shares or securities in the United States or any province or territory thereof. Neither this document nor any copy hereof should be taken, transmitted or distributed (directly or indirectly) into the United States.

Although WisdomTree endeavours to ensure the accuracy of the content in this document, WisdomTree does not warrant or guarantee its accuracy or correctness. Where WisdomTree has expressed its own opinions related to product or market activity, these views may change. Neither WisdomTree, nor any affiliate, nor any of their respective officers, directors, partners, or employees accepts any liability whatsoever for any direct or consequential loss arising from any use of this document or its contents.