JAPAN VS. SOUTH KOREA: WHAT SHOULD INVESTORS CONSIDER

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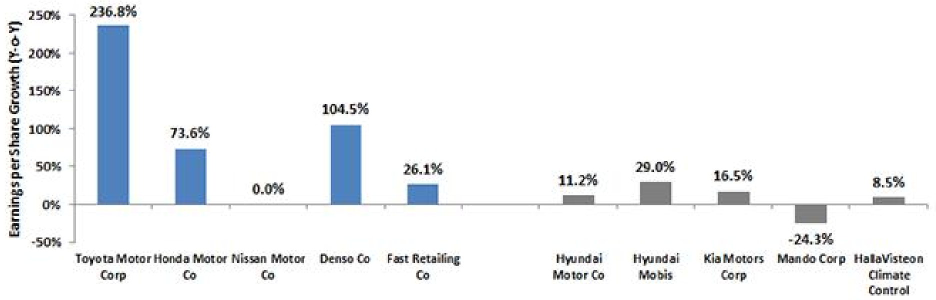
South Korea is a vibrant economy that is widely known for its high literacy rate and exporting prowess. In 2012, South Korea's gross domestic product (GDP) was nearly twice that of many developed nations, including Switzerland, Sweden and Norway.[1] Over the years, South Korea has shifted toward exporting higher-end technological innovations that focus on cutting-edge technology as well as automobiles from global leaders such as Samsung, LG, Hyundai and Kia Motors.[2] South Korea's economy, particularly its export industry, has been highly resilient throughout the years. As of December 31, 2012, almost 60% of South Korea's GDP came from exports.[3] From that perspective, changes in exchange rates can impact its economy and companies—in particular the cross rate with Japan. **Competitive Landscape Japan vs. South Korea** To illustrate the importance of this currency discussion, consider this story: In his first month on the job (April 2013), South Korean minister of Strategy and Finance Hyun Oh-Seok was faced with a sharply depreciating Japanese yen as well as escalating political tensions with North Korea that could have erupted in war. While the threat of a potential nuclear event may have had significant ramifications, Hyun said, "Compared to the North Korea risk, a sliding yen is having a considerable impact on the real economy of South Korea.[4]" This is a testament to just how important the cross currency rates of the won and the yen are to these two Asian countries and their leaders. From the time Japan's prime minister Shinzo Abe was elected on December 16, 2012, to May 22, 2013, the Korean won gained (and the yen weakened) almost 20% against the yen and has barely moved since then.[5] It is clear that Korean firms were impacted by the yen weakness. For the past year (from September 30, 2012 to September 30, 2013), the Japanese TOPIX generated earnings per share (EPS) growth of over 87.1%, while the KOSPI (South Korea) has EPS contraction of 4.6% over the same period.[6] The chart below details the top five Japanese and Korean consumer discretionary companies. **Year-over-Year Growth in the 12-Month Trailing EPS before Extraordinary Items of the Top Five Consumer Discretionary Companies in Japan and Korea (October 25, 2013)***



Sources: Bloomberg, Standard & Poor's. Past performance is not indicative of future results. Subject to change. You cannot invest directly in an index.

* "Top five" refers to the top five companies in the Consumer Discretionary sector by weight in the WisdomTree Japan Hedged Equity Index and WisdomTree Korea Hedged Equity Index, as of 10/25/2013.

For current holdings of the WisdomTree Japan Hedged Equity Index, please click here. For current holdings of *the WisdomTree Korea Hedged Equity Index, please click here.* • The top five Japanese consumer discretionary companies have recorded an average EPS growth of 88.2% on a year-over-year basis, with a range of 0% to 236.8%. • In comparison, the top five Korean consumer discretionary companies recorded a much lower average EPS growth of 8.2% on a year-over-year basis, with a range of -24.3% to 29%. Below are a few anecdotes that speak to the change in the competitive landscapes of major Korean and Japanese exporters: • **Hyundai vs. Toyota:** Given that Hyundai earns over 50% of its revenue outside South Korea, sells 87% of its vehicles abroad and ships auto parts to facilities internationally, a Hyundai executive has recently named the simultaneous weakness of the yen accompanied by won appreciation "…a double torture situation."[7] Hyundai estimates that its balance sheet sensitivity to a 5% appreciation in the Korean won sets it back by approximately 32 billion won.[8] Meanwhile, Toyota Motor Corporation (TMC) in its latest quarterly earnings release reported a net revenue increase of 13.7% and a 93.6% net income increase from ¥290 billion to ¥562 billion from one year ago. TMC's managing officer Takuo Sasaki attributed the company's operating income increase in part to "…the impact of foreign exchange rates and our global efforts for profit improvement, through cost reduction activities such as companywide value analysis…"[9] To be more precise, TMC attributed ¥260 of its ¥271.8 billion net income increase (95% of total) to effects of foreign exchange (forex) rates or yen depreciation against most of its trading partners. • **Samsung Electronics vs. Sony:** With over 85% of Samsung's total revenue coming from abroad, the company suffered approximately 350 billion won in foreign exchange losses in the fourth quarter of last year.[10] Further, Samsung estimates that the yen will cost it as much as 3 trillion won in 2013—estimates are that the firm lost 1.2 trillion won based on foreign exchange fluctuations in 2012.[11] Sony on the other hand, has seen 3.5 billion yen in net income for the second quarter of 2013—a number that beat expectations of 2.6 billion yen over this period.[12] While currency isn't the only factor in the competitive mix, it can be an important headwind for South Korean exporters and a tailwind for Japanese exporters. If Abenomics continues to lead to further yen weakness, South Korea could have to respond in ways to weaken its currency to improve its export competitiveness. If Abenomics falters, these South Korean firms—many of which make very similar products as their Japanese counterparts—could be in a prime position to benefit as the winds of currency performance shift. [1]Source: World Bank, 2012. [2]Source: Korean International Trade Association, 2012. [3]Source: World Bank, 2012. [4]Cynthia Kim, "South Korea's Hyun Says Yen Bigger Issue Than North Korea," Bloomberg, April 19, 2013. [5]Source: Bloomberg, as of 10/25/13. [6]Computations based on the change in trailing 12-month earnings per share from 9/30/2012 to 9/30/2013. [7]Investor Campus, 9/25/13. [8]Hyundai Consolidated Financial Statements, 6/30/13. [8]Toyota Motor Corporation Quarterly Financial Report 8/2/13. [10]Source: Samsung IR Presentations, Annual Report 2013. [11]Source: Kim Yoo-chul, "Samsung Expects Forex Losses to Reach W3 Tril. in 2013," The Korea Times, 5/12/13. [12]Source: Bloomberg, "Sony Rides Weak Yen to Beat Profit Estimates," The Japan Times, 8/1/13.

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DEFINITIONS

Gross domestic product (GDP) : The sum total of all goods and services produced across an economy.

Tokyo Stock Price Index (TOPIX) : A free float-adjusted market capitalization-weighted index that is calculated based on all the domestic common stocks listed on the Tokyo Stock Exchange First Section.

Earnings per share : Total earnings divided by the number of shares outstanding. Measured as a percentage change as of the annual Index screening date compared to the prior 12 months. Higher values indicate greater growth orientation.

KOSPI (Korea Composite Stock Price Index) : A market capitalization-weighted index built to measure the performance of all common shares on the Korean stock exchanges.

12 month trailing EPS : 12 month trailing earnings per share is the sum of a company's earnings per share for the previous four quarter.

Foreign Exchange (FOREX, FX) : The exchange of one currency for another, or the conversion of one currency into another currency.

Abenomics : Series of policies enacted after the election of Japanese Prime Minister Shinzo Abe on December 16, 2012 aimed at stimulating Japan's economic growth.