# ARE INVESTORS IGNORING IMPORTANT DIVIDEND PAYERS?

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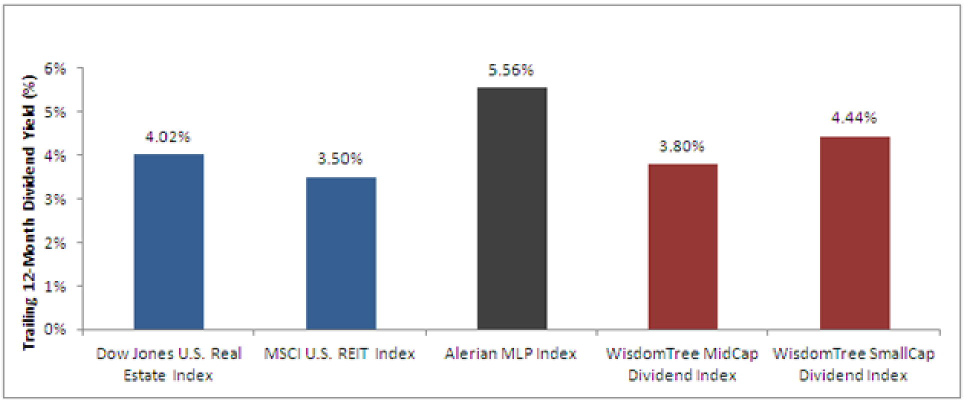
Income is the story of the day—notably the lack of any reasonable levels of income from such traditional sources as bonds and money market investments. This has caused many to search for income in a variety of asset classes; from large-cap, blue-chip dividend payers to real estate investment trusts (REITs) to preferred stocks to master limited partnerships (MLPs)—if it produces a good income stream, it has been in high demand in recent years. There is a big part of the U.S. equity market that I believe has—to a significant extent—been glossed over and ignored in this hunt for income, and that is mid- and small-cap dividend payers in the United States. **The Forgotten Dividend Payers** While there are a large number of dividend-based exchange-traded funds (ETFs) that concentrate on the large-cap segment of the market, I believe there are only two indexes (and ETFs designed to track them) in the United States focused exclusively on stocks outside this size segment: the WisdomTree MidCap Dividend Index (with the WisdomTree MidCap Dividend Fund—DON—designed to track it) and the WisdomTree SmallCap Dividend Index (with the WisdomTree SmallCap Dividend Fund—DES—designed to track it). Mid- and small-cap ETFs in general represent a very large category of traditional asset allocation models for U.S. equities and two of the biggest market segments within ETFs. There are almost $60 billion invested in small-capitalization ETFs and close to another $60 billion invested in mid-capitalization ETFs. Collectively, these two market segments represent over 20% of the approximately $514 billion invested in U.S.-based equities focused on broad market indexes. Yet while U.S.-based dividend ETFs collectively represent almost $49 billion in assets, or about 9% of U.S. equity assets under management, there are less than $1 billion combined in the mid- and small-cap dividend category. Based on the investable opportunity sets, I believe these mid- and small-cap dividend funds should be much larger. Consider this: **Market Capitalization as a Measure of Potential Opportunity**

As Of 1/31/2013

| Index | Market Capitalization |
|---|---|
| Dow Jones U.S. Real Estate Index | $578.35 Billion |
| MSCI U.S. REIT Index | $497.59 Billion |
| Alerian MLP Index | $294.23 Billion |
| WisdomTree MidCap Dividend Index | $1.52 Trillion |
| WisdomTree SmallCap Dividend Index | $511.37 Billion |

(For Index definitions, go to Glossary.) There are more than $10.5 billion invested in either ETFs or exchange-traded notes tracking the performance of the Alerian MLP Index, and more than $20 billion in ETFs designed to track the Dow Jones U.S. Real Estate Index and the MSCI U.S. REIT Index. Based on the aforementioned market capitalization statistics, I believe the biggest investment opportunity set by far exists in the ETFs that track the WisdomTree MidCap and SmallCap Dividend Indexes—and there is less than $1 billion invested in these funds. Moreover, the dividend yields have recently been fairly competitive with these smaller market segments. **Indexes Indicate Similar Yield Levels:** Trailing 12-Month Index Dividend Yields, As of 1/31/2013




Source: Bloomberg

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.

We recognize the inherent differences in methodology and market segments between these particular indexes, but we feel that the one common element—that many people consider these types of asset classes, be it real estate, REITS, MLPs and dividends--as income generators. Through the common theme of "income generation," we believe there is merit to the comparison, but we acknowledge that people should consider the differences in potential risk profiles between these asset classes when conducting any analysis. **How Much to Allocate?** What would be an appropriate allocation to the mid- and small-cap dividend segments within an income-focused allocation? We believe that a good place to start could be an analysis of the exposure of mid- and small-cap stocks in broad market capitalization-weighted indexes. Of course, every investor will have different investment needs and should work with their investment advisor to determine the right balance for their needs. **Percentage of Market Cap Index:** If we look at the Russell 3000 Index—one of the most often-cited measures of large-, mid- and small-cap equities in the United States—17.5% of the index comprises mid-cap stocks (defined here as those with market caps between $2 billion and $10 billion), while 6.6% is in small-cap stocks (defined here as those with market caps below $2 billion), for a combined mid- and small-cap weight of approximately 23%. This is a similar share as what we saw earlier in terms of the proportion of mid- and small-cap allocations across U.S.-focused ETFs. **Percentage of Dividend Index:** Within the universe of U.S. dividend payers, and using the same market capitalization breakpoints as the Russell 3000 Index, 13% of the WisdomTree Dividend Index comprises mid-cap stocks and 4% is small-cap stocks. We believe that these could be good starting baseline allocations. Many people often over-weight mid- and small-cap segments when it comes to their breakdown vs large caps in asset allocation. and the same can be done compared to large-cap dividend ETFs. ***WisdomTree's Jeremy Schwartz discusses the case for investing in Emerging Markets equities with Michael Johnston of ETF Database. Hear the podcast.*** **Source for data in this article:** Bloomberg, as of 1/31/2013.

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You cannot invest directly in an index.

## DEFINITIONS

**Real estate investment trust (REIT)** : Investment structure containing a basket of different exposures to real estate, be it directly in properties or in mortgages. Returns predominantly relate to changes in property values and income from rental payments.

**Master limited partnership (MLP)** : Investment structure where holdings typically must derive most of their cash flows from real estate, natural resources or commodities, combining the tax benefits of a partnership–taxes occur when holders receive distributions–with the liquidity of a publicly traded company.

**Exchange-traded notes** : Different from exchange-traded funds in that they are a direct obligation of a financial entity–typically a bank–where the contract specifies that the bank will pay the holder of the note according to the returns of an underlying index minus applicable fees. Exchange-traded funds hold the underlying assets of the index and their returns represent the returns of the assets held.

**Trailing 12-month dividend yield** : Dividends over the prior 12-months are added together and divided by the current share price. Higher values indicate more dividends are being generated per unit of share price.