

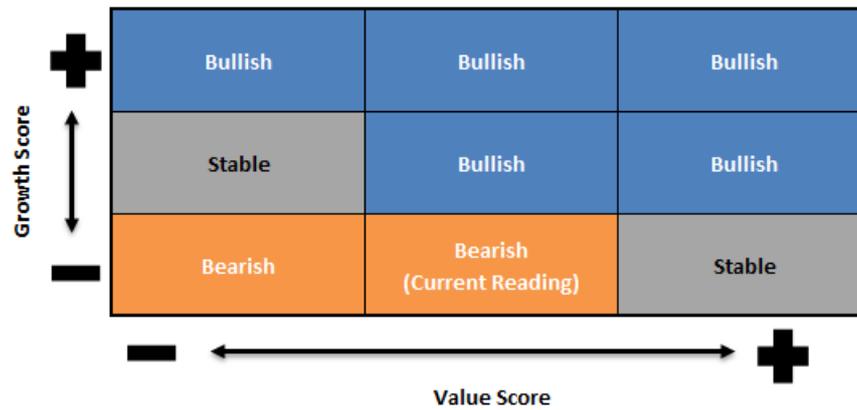
# ARE YOU HAVING TROUBLE TIMING THE MARKET?

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A simple, well-known adage says that successful investing is all about “time in the market, rather than timing the market.” Unfortunately, many investors lack investment discipline and have trouble staying invested when [volatility](#) increases, and as a result, tend to time the market wrong by selling at adverse times. Timing is also notoriously difficult for market professionals. But if you are ready to give up trying to time the market yourself, we have created a rules-based market indicator that strives to determine a tactical timing indicator for you, and we’ve made it available in exchange-traded funds (ETFs). **Timing the Market** We believe it makes sense for many investors to invest for the long term using a strategic asset allocation model with periodic rebalances. That being said, there are investors who want to take a more tactical approach to asset allocation and by doing so try to time the market. Some popular market timing indicators use a security’s or index’s price, by comparing various short-term [moving averages \(MA\)](#) against longer-term moving averages, and one of the most popular signals, often referred to as the ["golden cross"](#) which occurs when the 50-day MA crosses above the 200-day MA.<sup>1</sup> Historically, [technical indicators](#) like the golden cross have proven to add value, mostly by buffering investors from substantial drawdowns. WisdomTree has differentiated a timing indicator to be determined based on market [fundamentals](#), rather than technical indicators and market prices. [This dynamic indicator incorporates trends](#) in well-known [growth](#), [quality](#) and [value](#) factors.

- **Growth/Quality Indicators**–These include trends in [operating](#) and [net income margins](#), as well as profit quality. Profits are a key driver of the market, so when the bottoms-up profits of a broad cross section of the U.S. markets are deteriorating, the indicator would look to be more [bearish](#) and [hedge](#) the portfolio.
- **Value Indicators**–These consider the [price-to-book \(P/B\)](#) and [price-to-cash flow \(P/CF\)](#) of the universe, to determine if valuations are stretched compared to their history. When price appreciation outpaces fundamental growth, the indicator would look to hedge because rising [valuations](#) typically signal there is more downside risk in the market. Combining both growth/quality and value indicators results in a signal that can provide guidance on when to become more [bullish](#) or bearish.

**What Signals Suggest Today: Hedge Your Market Risk** Recently we have seen both net and operating profits margins deteriorate in the market, resulting in a negative growth/quality score. Also, after large price gains in the market during recent years, the value indicator signaled relatively high numbers, resulting in a neutral value score. As of December 31, 2015, the [dynamic hedging indicator](#) was positioned in one of the two bearish buckets, signaling a 100% [hedge ratio](#). **Dynamic Hedging**



Net Equity Exposure		
Regime	WisdomTree Dynamic Long/Short U.S. Equity Fund (DYLS)	WisdomTree Dynamic Bearish U.S. Equity Fund (DYB)
Bullish	100%	25%
Stable	50%	0%
Bearish	0%	-100%

Sources: WisdomTree, Alpha Vee, as of 12/31/15. The above chart references the possible ranges of net equity exposures.

**Indicator Results**

**Implement? How to** wisdomTree recently launched two [liquid](#) alternative [long/short](#) strategies in the ETF structure: the [WisdomTree Dynamic Long/Short U.S. Equity Fund \(DYLS\)](#) and the [WisdomTree Dynamic Bearish U.S. Equity Fund \(DYB\)](#). These liquid alternative solutions follow rules-based [passive](#) Indexes that use the dynamic hedging indicator to decide the short position (or hedge ratio), which rebalances monthly based on growth, quality and value conditions of the broad market. Since each Fund has different possible ranges of net equity exposure, they can be used separately or together, depending on the view of the market. The net equity position was 0% (or [market neutral](#)) for DYLS and -100% (or net short equity) for DYB.<sup>2</sup> It is important to note that these Funds are designed to be dynamic, and the hedge ratio (or net equity position) can change on a monthly basis. **When would Hedge Ratios Change: If Profit Margins Stop Deteriorating** In order to move to another box and for DYLS to go from market neutral to unhedged, we would have to see changes in the growth or value score, which can happen if profit margins stop deteriorating (or improve) and/or prices fall more rapidly than fundamentals, which would improve valuation readings. Remember, although prices change rapidly, equities report earnings only quarterly. As the latest quarterly earnings data starts getting evaluated, the dynamic hedging indicator will reassess conditions monthly. While our hedging indicator will certainly not get every market downdraft timed perfectly, the indicator did start getting more bearishly positioned in 2015. The early results show the merits of including a strategy that aims to hedge market risk (or go net short, as is happening in DYB). These Funds certainly merit a look as a volatility-reduction part of asset allocation models or as part of a core alternatives allocation bucket.

<sup>1</sup>Other moving averages may be used, the above reference is just used as an example

<sup>2</sup>Source: WisdomTree, as of 12/31/15

**Important Risks Related to this Article**

There are risks associated with investing, including possible loss of principal. The Fund invests in derivatives, including as a substitute to gain short exposure to equity securities. Derivative investments can be volatile, and these investments may be less

liquid than other securities, and more sensitive to the effects of varied economic conditions. Derivatives used by the Funds to offset their exposure to market volatility may not perform as intended. The Funds may engage in “short sale” transactions and will lose value if the security or instrument that is the subject of a short sale increases in value. A Fund that has exposure to one or more sectors may be more vulnerable to any single economic or regulatory development. This may result in greater share price volatility. The composition of the Index is heavily dependent on quantitative models and data from one or more third parties, and the Index may not perform as intended. The Funds invest in the securities included in, or representative of, their Indexes regardless of their investment merit, and the Funds do not attempt to outperform their Indexes or take defensive positions in declining markets. Please read each Fund’s prospectus for specific details regarding the Fund’s risk profile.

Using an asset allocation strategy does not ensure a profit or protect against loss. Investors should consider their investment time frame, risk tolerance level and investment goals.

For standardized performance and the most recent month-end performance click [here](#) NOTE, this material is intended for electronic use only. Individuals who intend to print and physically deliver to an investor must print the monthly performance report to accompany this blog.

For more investing insights, check out our [Economic & Market Outlook](#)

View the online version of this article [here](#).

**IMPORTANT INFORMATION**

**U.S. investors only:** Click [here](#) to obtain a WisdomTree ETF prospectus which contains investment objectives, risks, charges, expenses, and other information; read and consider carefully before investing.

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## DEFINITIONS

**Volatility**: A measure of the dispersion of actual returns around a particular average level.

**Moving Average**: is a calculation to analyze data points by creating a series of averages of different subsets of the full data set.

**Golden cross**: Generally referenced when a shorter-term moving average crosses above a longer-term moving average and is a bullish indicator. When a shorter-term moving average crosses below a longer-term moving average, it may be referred to as a “death cross” and is a bearish indicator.

**Technical indicators**: Type of analysis that tries to determine future price patterns using historical price patterns.

**Fundamentals**: Attributes related to a company’s actual operations and production as opposed to changes in share price.

**Growth**: Characterized by higher price levels relative to fundamentals, such as dividends or earnings. Price levels are higher because investors are willing to pay more due to their expectations of future improvements in these fundamentals.

**Quality**: Characterized by higher efficiency and profitability. Typical measures include earnings, return on equity, return on assets, operating profitability as well as others. This term is also related to the Quality Factor, which associates these stock characteristics with excess returns vs the market over time.

**Value**: Characterized by lower price levels relative to fundamentals, such as earnings or dividends. Prices are lower because investors are less certain of the performance of these fundamentals in the future. This term is also related to the Value Factor, which associates these stock characteristics with excess returns vs the market over time.

**Operating margin**: Operating income divided by total sales. Higher numbers indicate higher profitability.

**Profit margins**: Net income divided by total sales. Higher values indicate a greater fraction of each dollar of sales being left to the firm and its owners after expenses are accounted for.

**WisdomTree Dynamic Bearish U.S. Equity Index**: A rules-based long/short index that includes long equity positions or long U.S. Treasury positions and short equity positions. The Long Equity Index consists of approximately 100 U.S. large- and mid-capitalization stocks that meet Index eligibility requirements and have the best combined score based on fundamental growth and value signals. Stocks are weighted in the Long Equity Index according to their volatility characteristics. The Short Equity Index consists of short positions in the largest 500 U.S. companies, weighted by market capitalization, designed to act as a market risk hedge. The Index provides a dynamic allocation of exposure to the Long Equity Index ranging from 100% to 0% while employing a variable monthly hedge ratio ranging from 75% to 100% exposure to the Short Equity Index based on a quantitative rules-based market indicator that scores growth and value market signals. During times when the market indicator shows unattractive readings on valuation and growth characteristics, the Index can move to 100% exposure to the Long Treasury Index (and accordingly no exposure to the Long Equity Index).

**Hedge**: Making an investment to reduce the risk of adverse price movements in an asset. Normally, a hedge consists of taking an offsetting position in a related security, such

as a futures contract.

**Price-to-book ratio**: Share price divided by book value per share. Lower numbers indicate an ability to access greater amounts of earnings per dollar invested.

**Valuation**: Refers to metrics that relate financial statistics for equities to their price levels to determine if certain attributes, such as earnings or dividends, are cheap or expensive.

**Bullish**: a position that benefits when asset prices rise.

**Dynamic Hedge**: Strategy in which a currency hedge can be varied (as opposed to targeting a constant level) and change over the course of time.

**Hedge Ratio**: The specified percentage of currency exposure being hedged, with 0% indicating that none of the currency exposure is being hedged and 100% indicating that all of the currency exposure is being hedged.

**Liquidity**: The degree to which an asset or security can be bought or sold in the market without affecting the asset's price. Liquidity is characterized by a high level of trading activity. Assets that can be easily bought or sold are known as liquid asset.

**Long (or Long Position)**: The buying of a security such as a stock, commodity or currency, with the expectation that the asset will rise in value, the opposite of Short (or Short Position).

**Short (or Short Position)**: The sale of a borrowed security, commodity or currency with the expectation that the asset will fall in value, the opposite of Long (or Long Position).

**Passive**: Indexes that take a rules-based approach with regular rebalancing schedules that are not changed due to market conditions.

**Market neutral**: Strategy that seeks to avoid market risk by hedging a percentage equal to total long exposure.