GETTING PAID TO HEDGE

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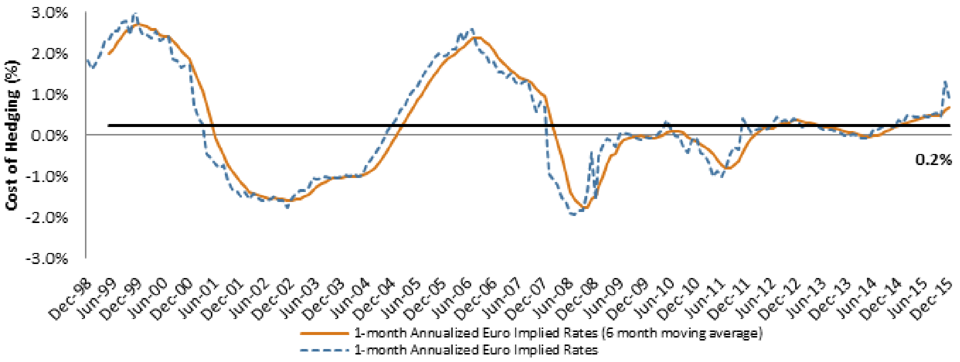
Last year, one of the most important investment themes was currency hedging, particularly for euro-denominated stocks. Many investors believed the euro was going to weaken on the back of quantitative easing by the European Central Bank (ECB)—and that's exactly what happened. Versus the U.S. dollar, the euro started 2015 at 1.21 and closed the year at 1.09. With such a big move, many investors are wondering if they missed the boat. From our perspective, to the contrary. The case to hedge the euro has gotten stronger by one very important measure: how much you are now being paid to hedge. An important element of currency-hedged strategies involves the use of forward contracts to neutralize currency exposure. The pricing of these forward contracts is based on relative interest rate differentials. In some countries like Brazil, short-term interest rates are very high, so it can cost U.S. investors upward of 14% per year to hedge exposure to currencies like the Brazilian real. That creates an incredibly high hurdle for how much the currency has to decline before an investor breaks even on paying that hedge cost. But the actions the ECB took in December 2015 make hedging the euro different. The ECB took its deposit rate more negative—cutting rates to -30 basis points (bps). The U.S. Federal Reserve (Fed) hiked interest rates for the first time in nine years and now has a band on its short-term rate of 25–50 bps; the midpoint of the range would be 37.5 bps. This means currency hedging is not only inexpensive—investors are actually getting paid to hedge the euro. And if/when the Fed increases rates in 2016, that "payment" will increase further. **Historical Cost of Hedging the Euro (1-Month Currency Forward Implied Rates as of 12/31/15)**



Source: Bloomberg. Past performance is not indicative of future results.

From a tactical perspective, when we look at what factors can help improve the returns from a purely passive hedging standpoint, interest rate differentials are the most powerful long-run signal. Given that an investor is starting to get paid more than 50 basis points a year from the differential in interest rates, this offers a boost to returns to hedged strategies over unhedged strategies, even if the euro does not move. Of course, if the euro appreciates, the hedged strategies will not participate in those gains, but they will be hedged against further losses in the euro if those were to occur. WisdomTree has three exchange-traded fund (ETF) options to target euro-area stocks with a currency hedge: 1) **WisdomTree Europe Hedged Equity ETF (HEDJ)**: Provides access to the dividend-paying exporters of Europe, which can be positioned to benefit from a decline in the euro with their goods becoming more competitively priced in the global markets. We believe these companies have not fully benefited from the fall in the euro yet, as many of them also have large amounts of business coming from the emerging markets, which have also been weak in the last year. This is our flagship ETF for euro-area-hedging strategies. 2) **WisdomTree Europe Hedged SmallCap Equity ETF (EUSC)**: Provides access to small-cap companies of the euro area and offers exposure to a more local side of European stocks. This fund can pair nicely with the large-cap multinationals to diversify size exposure and geographic revenue mixes of the companies. 3) **WisdomTree Dynamic Currency Hedged Europe Equity ETF (DDEZ)**: Provides access to a broad cross-section of dividend payers from the euro area and implies a dynamic currency hedge. For investors who do not want to rotate between hedged and unhedged strategies, but want to have some currency exposure when the environment is supportive of it, this fund can adapt and provide that type of tactical hedging solution.

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DEFINITIONS

Currency hedging : Strategies designed to mitigate the impact of currency performance on investment returns.

Quantitative Easing (QE) : A government monetary policy occasionally used to increase the money supply by buying government securities or other securities from the market. Quantitative easing increases the money supply by flooding financial institutions with capital, in an effort to promote increased lending and liquidity.

Forward contracts : Agreements to buy or sell a specific currency at a future date at an agreed upon rate.

Interest rates : The rate at which interest is paid by a borrower for the use of money.

Short-term rates : the rate of interest on a debt instrument maturing in two years or less.

Basis point : 1/100th of 1 percent.

Federal Reserve : The Federal Reserve System is the central banking system of the United States.

1-Month Currency Forward : A binding one month contract in the foreign exchange market that locks in the exchange rate for the purchase or sale of a currency on the following one month.

Implied interest rate : The annualized interest rate implied by forward currency contracts relative to spot rates.

Dividend : A portion of corporate profits paid out to shareholders.

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.