
WHY REBALANCING IS SO CRITICAL TO EXCHANGE TRADED FUNDS (ETFs)

07/01/2014

As we've [discussed previously](#), [smart beta](#) approaches, such as WisdomTree's, have been growing in popularity. Perhaps this is due to the fact that they try to beat the market, rather than be it. But all smart beta approaches may not be created equal. We believe that truly smart beta approaches (as opposed to smart marketing techniques) offer investors:

- High [correlations](#) to established benchmarks
- A rules-based, repeatable methodology that offers broad, representative exposure to an asset class
- Alternative weighting methods
- A proven track record on a total and risk-adjusted return basis

And perhaps one of the most important characteristics, at least in our approaches, is the regular rebalancing back to a relative value. Why is this so important? Rebalancing keeps an eye on relative value

Consider that stock prices can be driven up for many reasons. And when prices are driven up, ETF weightings can be as well. Unless you believe that price is always the best indicator of value, you can appreciate the risks this can add. This is precisely why a [fundamental](#) rebalance is so important to WisdomTree—and should be to all investors. Rebalancing can help reduce the risk of giving too much weight to stocks whose price increases are not supported by improvements in underlying fundamentals. It can provide the opportunity to sell stocks that have become more expensive relative to their underlying fundamentals and buy stocks that have become less expensive relative to their underlying fundamentals. (Please note that stocks are affected by how the market performs. When stock prices fall, you should expect the value of your investment to fall as well.) Put simply, rebalancing to relative value allows us to effectively lower the prices of the markets we invest in*—helping us to:

- Avoid paying too much for growth
- Reduce valuation risk
- Provide the potential for outperformance

So, why don't more ETFs rebalance to relative value—or even rebalance at all? Your guess is as good as ours. **See the [difference rebalancing makes](#) for yourself.** **Ordinary brokerage commissions may apply.*

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.

There are risks involved with investing, including possible loss of principal. Foreign investing involves currency, political and economic risk. Funds focusing on a single country, sector and/or funds that emphasize investments in smaller companies may experience greater price volatility. Investments in emerging markets, currency, fixed income and alternative investments include additional risks. Please see prospectus for discussion of risks.

Past performance is not indicative of future results. This material contains the opinions of the author, which are subject to change, and should not to be considered or interpreted as a recommendation to participate in any particular trading strategy, or deemed to be an offer or sale of any investment product and it should not be relied on as such. There is no guarantee that any strategies discussed will work under all market conditions. This material represents an assessment of the market environment at a specific time and is not intended to be a forecast of future events or a guarantee of future results. This material should not be relied upon as research or investment advice regarding any security in particular. The user of this information assumes the entire risk of any use made of the information provided herein. Neither WisdomTree nor its affiliates, nor Foreside Fund Services, LLC, or its affiliates provide tax or legal advice. Investors seeking tax or legal advice should consult their tax or legal advisor. Unless expressly stated otherwise the opinions, interpretations or findings expressed herein do not necessarily represent the views of WisdomTree or any of its affiliates.

The MSCI information may only be used for your internal use, may not be reproduced or re-disseminated in any form and may not be used as a basis for or component of any financial instruments or products or indexes. None of the MSCI information is intended to constitute investment advice or a recommendation to make (or refrain from making) any kind of investment decision and may not be relied on as such. Historical data and analysis should not be taken as an indication or guarantee of any future performance analysis, forecast or prediction. The MSCI information is provided on an "as is" basis and the user of this information assumes the entire risk of any use made of this information. MSCI, each of its affiliates and each entity involved in compiling, computing or creating any MSCI information (collectively, the "MSCI Parties") expressly disclaims all warranties. With respect to this information, in no event shall any MSCI Party have any liability for any direct, indirect, special, incidental, punitive, consequential (including loss profits) or any other damages (www.msci.com)

Jonathan Steinberg, Jeremy Schwartz, Rick Harper, Christopher Gannatti, Bradley Krom, Tripp Zimmerman, Michael Barrer, Anita Rausch, Kevin Flanagan, Brendan Loftus, Joseph Tenaglia, Jeff Weniger, Matt Wagner, Alejandro Saltiel, Ryan Krystopowicz, Jianing Wu, and Brian Manby are registered representatives of Foreside Fund Services, LLC.

WisdomTree Funds are distributed by Foreside Fund Services, LLC, in the U.S. only. You cannot invest directly in an index.

DEFINITIONS

Smart Beta: A term for rules-based investment strategies that don't use conventional market-cap weightings.

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