ANOTHER STRONG YEAR FOR AUSTRALIAN EQUITIES?

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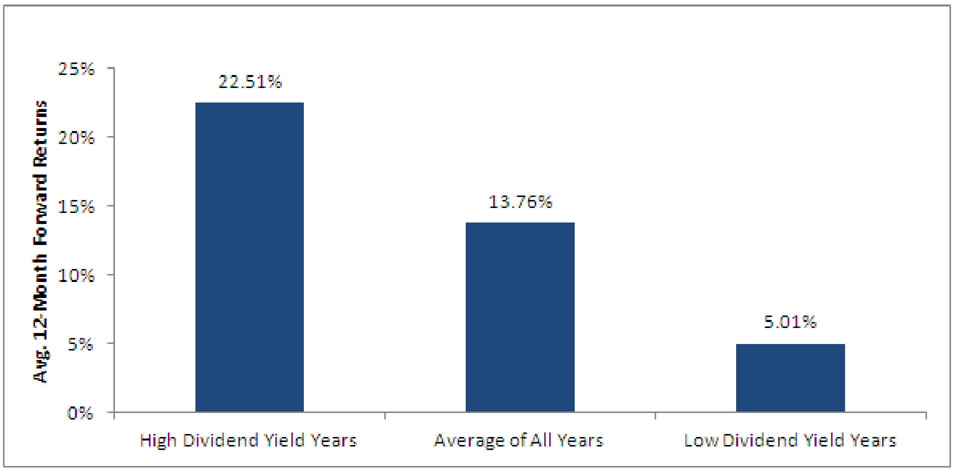
In a recent blog, we detailed our bullish views on the Asia Pacific ex-Japan region, given how a historical analysis showed a favorable return environment following similar price points in the past. In this piece, we conduct a similar analysis for Australian equities (MSCI Australia Index)—a major developed country in this region. Australia is currently noted for two key attributes: • **Natural Resources:** Australia is rich in natural resources, and this fact, combined with a close proximity to China, creates an important economic relationship between the two countries. Australia can supply a significant proportion of China's demand for these resources. • **Strong Sovereign Balance Sheet:** Australia is one of a dwindling number of developed market countries currently maintaining a AAA credit rating from Standard & Poor's[2], partly due to a debt-to-gross domestic product (GDP) ratio of less than 30%, according to the International Monetary Fund's October 2012 estimates. Australian equities have outperformed Asian equities (represented by the MSCI AC Asia Pacific ex Japan Index) by over 10% for the last 12 months (as of 2/28/13). Looking at historical valuations of Australian equities, we conclude that Australian equities are currently selling at relatively low valuations based on historical ranges (which matched our findings for Asian equities in the prior blog), as we will detail in the historical analysis below.

Average 12-Month Returns Following High & Low Dividend Yields



Period studied encompasses 12/31/1970–12/31/2012, which is the full available history of the MSCI Australia Index. Past performance is not indicative of future results.

(For definitions of terms in this chart, please see our Glossary.) • The current trailing 12-month dividend yield for February 28, 2013, is 4.00%, while the median value for all 42 available year-end values for the MSCI Australia Index is 3.71%. Year-end values above this figure were classified as High Dividend Yield Years, and those below this value were classified as Low Dividend Yield Years. This means we are currently in a high dividend yield period relative to the history of Australian equities. • The average return for High Dividend Yield Years was more than 17% better than the average for Low Dividend Yield years, and nearly 9% better than the average of all 42 available calendar

years. Of course, there is no guarantee that this result will repeat itself, but we believe it worth mentioning, especially since it is based on more than four decades of return history. **Particular Risks in Focus: Financials & Materials** While we have outlined a way to look at Australian equities from a positive perspective through the use of the MSCI Australia Index, many might cite the heavy exposure of that Index to financials (49.02%) and materials (21.08%)[2]. While the index is weighted by market capitalization, WisdomTree has created an Index specifically geared to counter the potential sector concentration risk of weighting Australian firms on the basis of their market capitalizations. Instead, the WisdomTree Australia Dividend Index weights the 10 largest qualifying companies from each of the industry sectors on the basis of their dividend yields, resulting in a combined weight to the Financials and Materials sectors of less than 35%[3]. **Australia's Currency** For international investors in Australia, the Australian dollar has also been an important factor in the analysis of equity returns. The Reserve Bank of Australia (RBA) recently stated that the currency is anywhere from 4% to 15% overvalued, a scenario not helpful to the country's export sector. To combat that pressure on the economy, the RBA has lowered its policy rate from 4.75% to 3.00% over the course of 14 months (October 2011 to December 2012). Typically, when a central bank lowers rates, the impact on the currency is an overall weakening—worrisome to equity investors, because it can detract from their returns—but the fact is, from October 4, 2011[4], to March 20, 2013, the Australian dollar appreciated 8.41% on a cumulative basis. The resilient nature of the currency has forced Australian firms, especially exporters, to improve their productivity and become more efficient. One reason for this resilience in the currency could be that many view Australia's AAA-rated[5] debt as a haven for flows during times of uncertainty caused by the trouble in currencies such as the euro and the yen. We believe the Australian currency is more than likely to benefit from these safe-haven flows—especially given the International Monetary Fund's recent classification of the Australian dollar as a reserve currency—until there is evidence of a global growth slowdown or actions taken by the RBA aimed at directly weakening the currency. **Conclusion** While there is truly no way of knowing whether Australian equities can continue their performance run from 2012 and through January 2013, we believe that it makes sense to consider indexes geared toward a more diversified set of sector exposures to the country. **Data source is Bloomberg unless otherwise noted.** [1]Standard & Poor's, March 2013. [2]Source: MSCI, as of 2/28/2013. [3]Sources: WisdomTree, Standard & Poor's, as of 2/28/2013. [4]Reserve Bank of Australia's announcement of initial cut from a 4.75% policy rate. [5]Source: Standard & Poor's, as of March 2013.

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DEFINITIONS

MSCI Australia Index : Market capitalization-weighted index designed to measure the performance of Australian equities.

AAA credit rating : This is the highest issuer credit rating assigned by Standard & Poor's, signaling strong confidence that the issuer will be able to maintain its payment obligations.

MSCI AC Asia Pacific ex Japan Index : The MSCI AC Asia Pacific ex Japan Index captures large and mid cap representation across 4 of 5 Developed Markets countries (excluding Japan) and 8 Emerging Markets countries in the Asia Pacific region. With 683 constituents, the index covers approximately 85% of the free float-adjusted market capitalization in each country. Developed Markets countries in the index include: Australia, Hong Kong, New Zealand and Singapore. Emerging Markets countries include: China, India, Indonesia, Korea, Malaysia, the Philippines, Taiwan and Thailand.

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.

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.

WisdomTree Australia Dividend Index : Index designed to measure the performance of dividend-paying companies in Australia. At maximum the 10-largest Australian dividend-paying companies are selected from each of the 10 sectors on the basis of their market capitalizations. Weighting is by dividend yield.

Reserve currency : A foreign currency held by a central bank or monetary authority as a long-term store of value.