

WisdomTree Yield Enhanced Canada Short-Term Aggregate Bond Index ETF

CAGS

In today's bond market, the ability for investors to maintain the appropriate balance between risk and return remains a challenge. While an acceleration in global economic growth may boost the returns of credit, it could also lead to an increase in nominal interest rates. At the same time, fixed income benchmarks at the core of many investors' portfolios are dominated by large exposures to low-yielding government securities. An investor's ability to generate sufficient income in their core portfolios could be hampered when following a market capitalization-weighted benchmark.

In our view, a more intuitive approach to indexing may focus on the ways investors can enhance the yield of their portfolios while dialing down the interest rate risk profile of their performance benchmark. By partnering with Bloomberg Barclays, WisdomTree helped develop an approach that draws on the same investable universe as the Bloomberg Barclays Canadian Aggregate Index (CAD Agg), but focuses on ways to reduce interest rate risk while boosting yield potential. As a result, this approach may serve as a powerful tool for investors seeking to navigate the opening stages of a rising rate environment.

[Bloomberg Barclays Canadian Short Aggregate Enhanced Yield Index \(CAD Short Agg Enhanced Yield\)](#)

THE INDEX'S THREE STEP METHODOLOGY:

1. Divide the CAD Agg constituents maturing in one to five years into eight subcomponents
2. Screen and apply constraints
3. Determine Index Weights

1. Divide the CAD Agg constituents maturing in one to five years into eight subcomponents

In the first step, the CAD Agg is divided into eight buckets across sector, maturity¹ and credit quality². While each component retains a suitable size for investment and liquidity³ purposes, each bucket may present unique opportunities for risk and reward. The strategy draws on the one- to five-year segment of the market (CAD Short Agg Composite) in order to mitigate interest rate risk.

		Years to Maturity	
		1-3 Years	3-5 Years
Sector	Treasury	Treasury 1-3	Treasury 3-5
	Credit	Credit 1-3 A & Above	Credit 3-5 A & Above
		Credit 1-3 BBB	Credit 3-5 BBB
	Gov Related	Gov Related 1-3	Gov Related 3-5

Source: Bloomberg, as of 6/30/2018. Credit rating determined using Bloomberg's index rating methodology. CAD Short Agg Composite represents the one- to five-year segment of the CAD Agg.

¹ Maturity: the amount of time until a loan is repaid.

² Credit quality: A measure of a borrower's potential risk of default.

³ Liquidity: The degree to which an asset or security can be bought or sold in the market without affecting the asset's price.

2. Screen and Apply Constraints

The following constraints are added, which serve to control risk and concentration while limiting turnover:

- + **Tracking Error Constraints:** Tracking Error Volatility (TEV)⁴ of the CAD Short Agg Enhanced Yield Index relative to the CAD Short Agg Composite would be less than 0.175% (17.5 basis points [bps]) each month.
- + **Duration Constraints:** The duration of the Index generally will not be more than half a year greater than that of the CAD Short Agg Composite.
- + **Sector and Subcomponent Constraints:** The weight of major and minor sectors (Treasuries, credit and government-related bonds) cannot deviate by more than 30% from their weights in the CAD Short Agg Composite. The total notional weight of the Baa subcomponents (Credit 1–3 Year Baa, Credit 3–5 Year Baa) cannot deviate from their weights in the CAD Short Agg Composite by more than 30%.
- + **Turnover Constraints:** Portfolio turnover due to monthly rebalancing⁵ is capped at 5%. When this condition cannot be met, the turnover limit is increased incrementally by 1% until a solution is found.

3. Determine Index Weights

On a monthly basis, weights of the Index are reallocated across the eight subcomponents to help maximize yield, while adhering to the four constraints. These weights are then applied at the individual issue level, so that the weight is the product of the subcomponent's determined weight and the security's weight within the subcomponent.

For example, if a Treasury note maturing in three years has a 10% weight in the 1–3-Year Treasury subcomponent, the calculated weight of 12% allocated to the 1–3-Year Treasury subcomponent would result in a weight of 1.2% at month end. Returns and statistics are calculated based on the constituents for the coming month. The CAD Short Agg Enhanced Yield Index is rebalanced each month.

THE RESULT

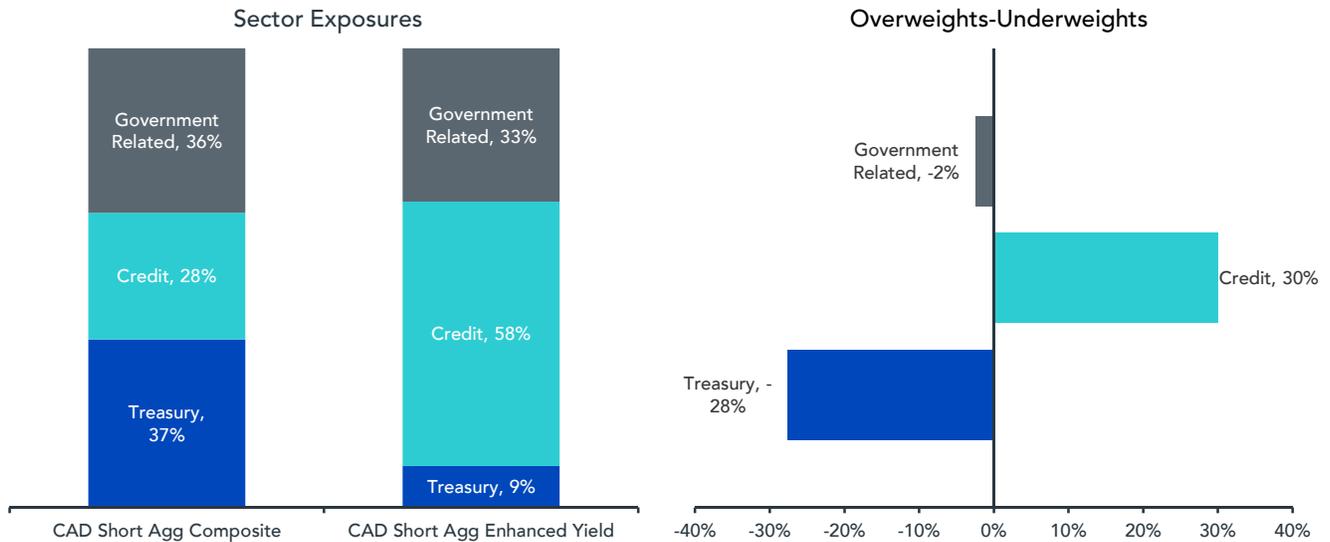
The CAD Short Agg Enhanced Yield currently yields 2.66%⁶ and is intended to deliver additional yield relative to the CAD Short Agg Composite with a similar volatility profile. In our view, this mechanical approach enhances the desirable characteristics while also enhancing the income potential of the strategy. For investors needing to hit minimum income targets, this modification could help them achieve their objectives. For managers concerned about the high-yield bond market, this approach also provides higher income potential in an investment-grade portfolio.

⁴ Tracking Error Volatility: the volatility of the difference between the performance of a portfolio and its benchmark. In this case, the portfolio is the CAD Short Agg Enhanced Yield.

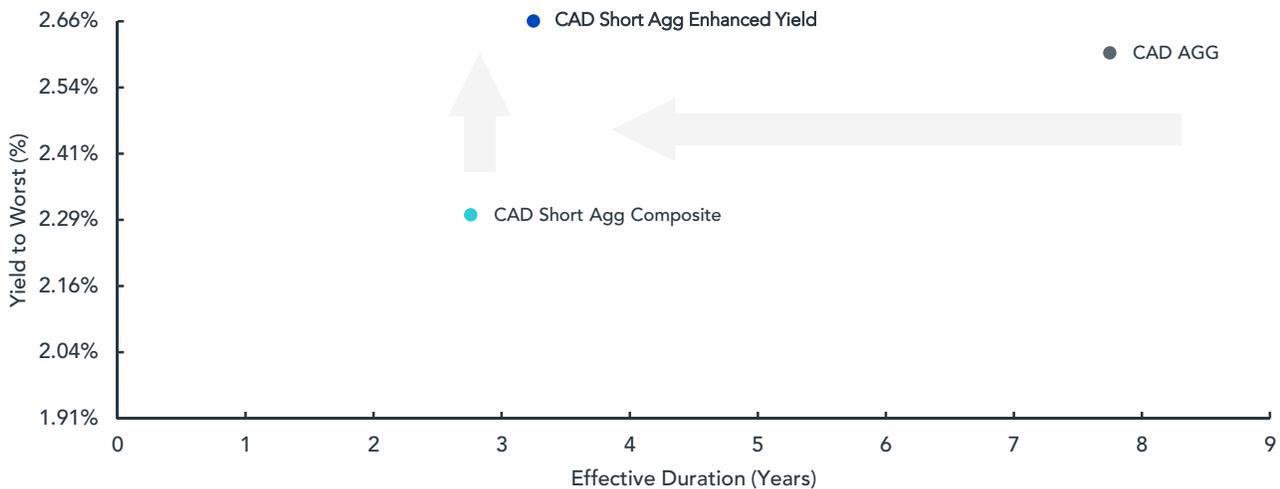
⁵ Rebalance: An index is created by applying a certain set of selection and weighting rules at a certain frequency.

⁶ Source: Bloomberg, as of 6/30/2018. Yield is calculated as income return on an investment, and refers to the interest or dividends received from a security that is typically expressed annually as a percentage of the market or face value.

CAD SHORT AGG ENHANCED YIELD VS. CAD SHORT AGG COMPOSITE [As of 6/30/2018]⁷



Yield to Worst and Effective Duration Comparison



For core investors, one could expect diversified exposure with significantly less rate risk and only a small sacrifice in income. For more conservative investors, one could expect as sizable yield enhancement with only slightly more rate risk.⁷

⁷ Source: WisdomTree, Bloomberg, as of 6/30/2018. Yield to Worst: the rate of return generated assuming a bond is redeemed by the issuer on the least desirable date for the investor. Portfolio Yield to Worst represents the weighted average yield to worst of a fund's investments in fixed income securities as of a specified date. Effective duration: A measure of the sensitivity of the index's price to changes in interest rates, calculated as the weighted average of the individual bond effective durations. Effective duration recognizes that changes in interest rates may also change the expected cash flows generated by any underlying bonds with embedded options.

INTRODUCING THE WISDOMTREE YIELD ENHANCED CANADA SHORT-TERM AGGREGATE BOND INDEX ETF (CAGS)

To provide tradable access to the CAD Short Agg Enhanced Yield, WisdomTree launched the WisdomTree Yield Enhanced Canada Short-Term Aggregate Bond Index ETF (CAGS). By sourcing opportunities in the CAD Agg, CAGS offers the opportunity to enhance the income potential of a core bond portfolio, while continuing to benefit from the diversification of a multisector portfolio.

Quick Facts

Ticker: CAGS

Class: Non-Hedged

Exchange: TSX

Management Fee: 0.18%

Management Expense Ratio: 0.20%

Structure: ETF

Objective: The Fund seeks to track the price and yield performance, before fees and expenses, of the Bloomberg Barclays Canadian Short Aggregate Enhanced Yield Index.

Primary Exposure: Canadian dollar-denominated, investment-grade, short-term fixed income.

At WisdomTree, we do things differently. We build our ETFs with proprietary methodologies, smart structures and uncommon access to provide investors with the potential for income, performance, diversification and more.

Management Expense Ratio (MER) - As reported on the Fund's most recent Management Report of Fund Performance. MER is the total of the Fund's management fee and operating expenses, including all waivers and absorptions, and is expressed as an annualized percentage of the average daily net asset value.

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Bloomberg Barclays Canadian Aggregate Index: a broad-based benchmark that measures the investment grade, Canadian dollar-denominated, and fixed-rate bond market. The index includes treasuries, government-related, corporate issues from developed and emerging markets issuers. *Bloomberg Barclays Canadian Short Aggregate Enhanced Yield Index*: a constrained, rules-based approach that reweights the sector, maturity and credit quality of the Bloomberg Barclays Canadian Aggregate Index across various subcomponents in order to enhance yield maturing in one to five years.

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