THE CASE FOR BNKS

AUGUST 2016

BetaShares Global Banks ETF - Currency Hedged (ASX: BNKS)

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Safe as houses? The case for diversifying banking sector exposure through the BetaShares Global Banks ETF – Currency Hedged (ASX Code: BNKS).

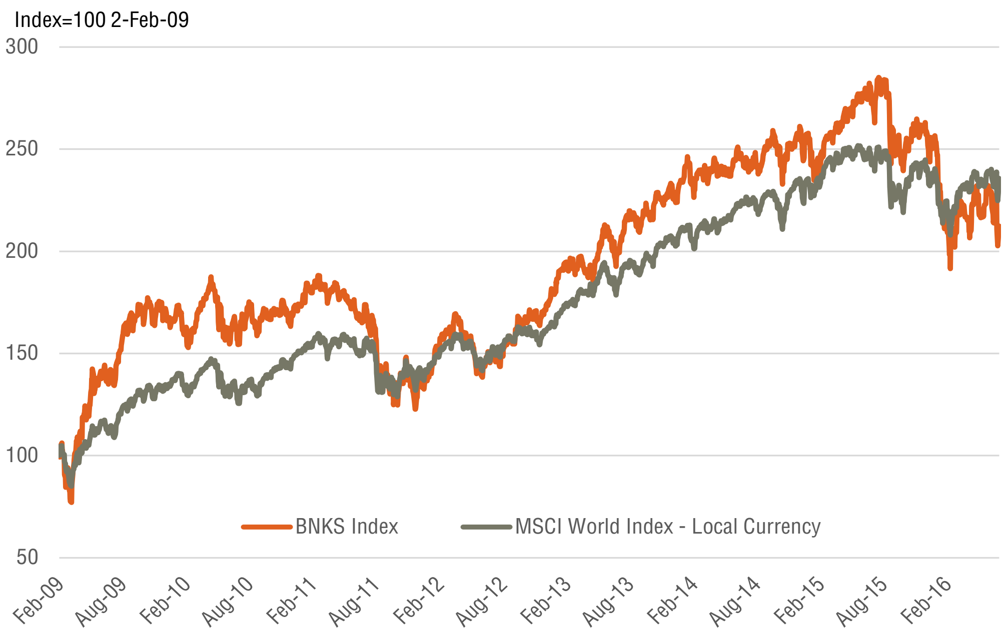
Australian banks have long formed an important part of many Australians' investment portfolios, thanks to their relatively large weight in the Australian stock exchange and attractive dividend returns. That said, by global standards, Australian banks have long appeared relatively expensive on some valuation measures and are significantly exposed to the fortunes of the local housing sector.

With this in mind, investors are now able to achieve more globally diversified banking sector exposure through the BetaShares Global Banks ETF – Currency Hedged (ASX Code: BNKS). Not only can such an investment help spread financial sector risk, but it also offers the potential for good long-run returns to the extent that global banks are able to improve balance sheet performance and profitability as they increasingly shake off the ravages of the 2008 financial crisis.

Why seek global exposure?

As might be expected, the investment performance of global banks is quite sensitive to overall financial market sentiment. As seen in the chart below, global banks have generally rebounded quite well since the global financial crisis, with the Index which BNKS aims to track outperforming the broad global equities market during the major upswings in global equities over this period. As the chart below shows, underperformance tends to take place during bouts of financial market instability as was evident in 2011, and earlier in 2016.

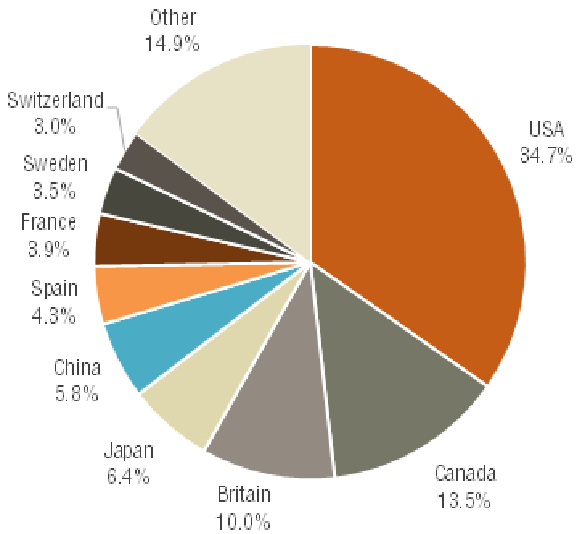
BETASHARES GLOBAL BANKS ETF - CURRENCY HEDGED'S UNDERLYING INDEX - VS. MSCI WORLD INDEX RELATIVE EQUITY PEFORMANCE – FEBRUARY 2009 – JUNE 2016



Source: Bloomberg. The Index which BNKS aims to track is the Nasdaq Global ex-Australia Banks Hedged AUD Index. You cannot invest directly in an index. Performance excludes the impact of ETF fees and expenses. Past performance is not an indication of future performance of the Index or the ETF.

From an Australian investor's perspective, the main advantage of international diversification of banking exposure within an Australian investor's portfolio is to reduce Australian country-specific risk in general, and risks associated with the local housing sector in particular. As seen in the chart below, BNKS offers exposure to 60 major global banks outside of Australia, covering a broad range of geographies across the globe.

COUNTRY ALLOCATION OF BETASHARES GLOBAL BANKS ETF - CURRENCY HEDGED'S UNDERLYING INDEX - 30TH JUNE 2016



Source: Bloomberg. BNKS aims to track the performance of the Nasdaq Global ex-Australia Banks Hedged AUD Index.

More specifically, as seen in the table below, BNKS provides exposure to some of the biggest and best known banks in the world, including JP Morgan, Bank of America and HSBC.

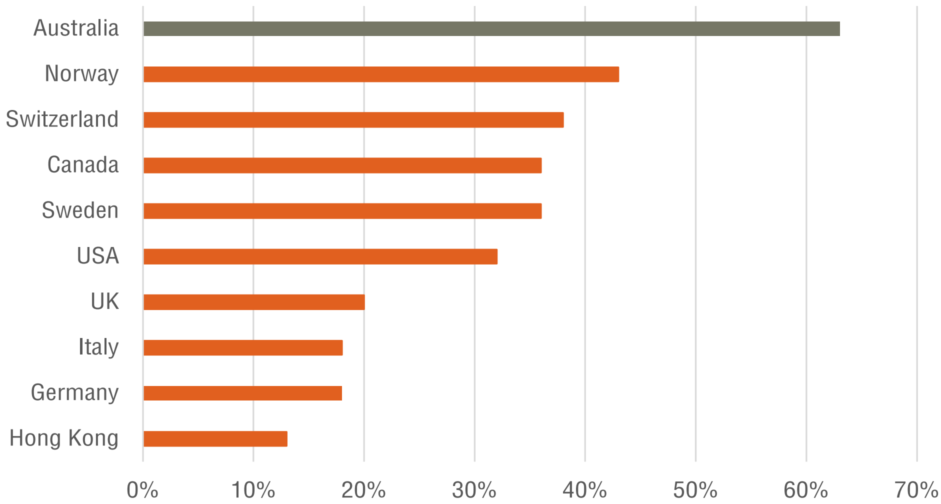
TOP 10 HOLDINGS OF BETASHARES GLOBAL BANKS ETF - CURRENCY HEDGED'S UNDERLYING INDEX - 30TH JUNE 2016

Bank	Country	Weight %
JPMorgan Chase & Co	United States	8.3
Wells Fargo & Co	United States	8.2
Bank of America Corp	United States	5.8
Citigroup Inc	United States	5.3
HSBC Holdings Plc	Britain	5.2
Royal Bank of Canada	Canada	4.0
Toronto-Dominion Bank	Canada	3.6
US Bancorp	United States	2.9
Mitsubishi UFJ Financial Group	Japan	2.9
Bank of Nova Scotia	Canada	2.7

Source: Bloomberg.

Most Australian investors are heavily exposed to the housing sector, either via their own property holdings or via share holdings in the Australian banks. Exposure to international banks helps reduce such exposure. As seen in the chart below, residential mortgages account for a relatively high share of Australian bank lending compared to international peers.

BANKS EXPOSURE TO RESIDENTIAL MORTGAGES BY COUNTRY (% SHARE OF TOTAL BANK LOANS): JUNE 2016



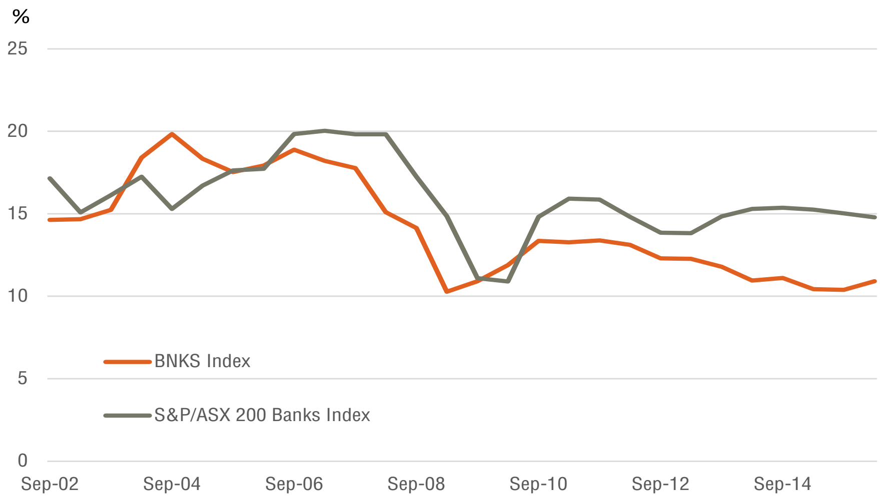
Source: IMF

The Global Banking Recovery

The Australian banking sector has performed relatively well by global standards in recent years, especially compared to global banks in the aftermath of the 2008 financial crisis.

As seen in the chart below, an important reason for this outperformance is that the return-on-equity of Australian banks has held up reasonably well – thanks to ongoing strength in the local property sector, and their lower exposure to the securitised assets that performed poorly in the wake of the financial crisis.

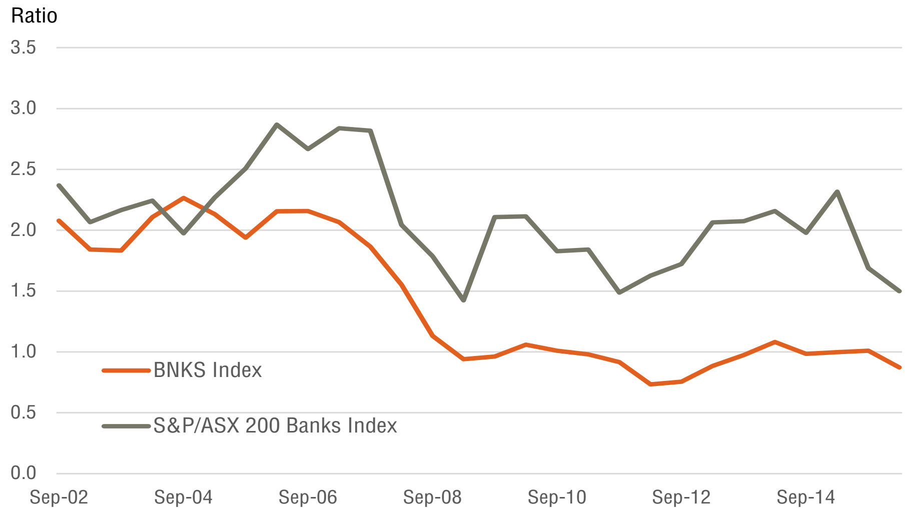
RETURN ON EQUITY: S&P/ASX 200 BANKS INDEX V BNKS' INDEX: MARCH 2002 – MARCH 2016



Source: Bloomberg. The Index which BNKS aims to track is the Nasdaq Global ex-Australia Banks Hedged AUD Index. You cannot invest directly in an index. Performance excludes the impact of ETF fees and expenses. Past performance is not an indication of future performance of the Index or the ETF.

As seen in the chart below, relatively low returns on equity in recent years has been associated with price-to-book valuations for global banks remaining below that of Australian banks. To the extent global banks are able to improve their relative returns on equity - as global economic growth and financial market activity picks up – there is potential for price outperformance vis-à-vis Australian banks though some narrowing in this price-to-book valuation gap.

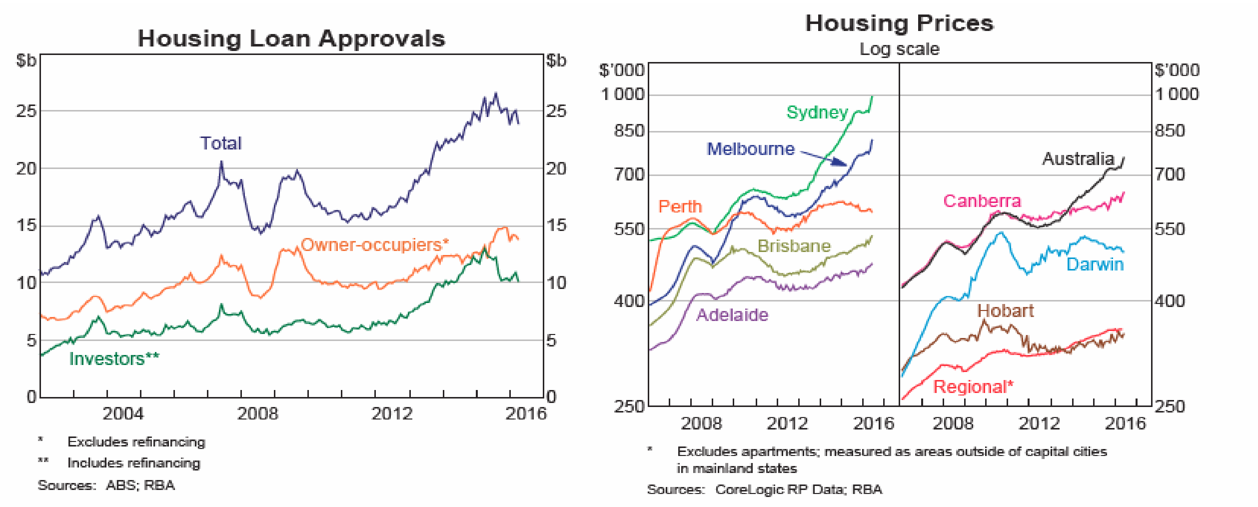
PRICE-TO-BOOK RATIO: S&P/ASX 200 BANKS INDEX V BNKS' INDEX: MARCH 2002 – MARCH 2016



Source: Bloomberg. The Index which BNKS aims to track is the Nasdaq Global ex-Australia Banks Hedged AUD Index. You cannot invest directly in an index. Performance excludes the impact of ETF fees and expenses. Past performance is not an indication of future performance of the Index or the ETF.

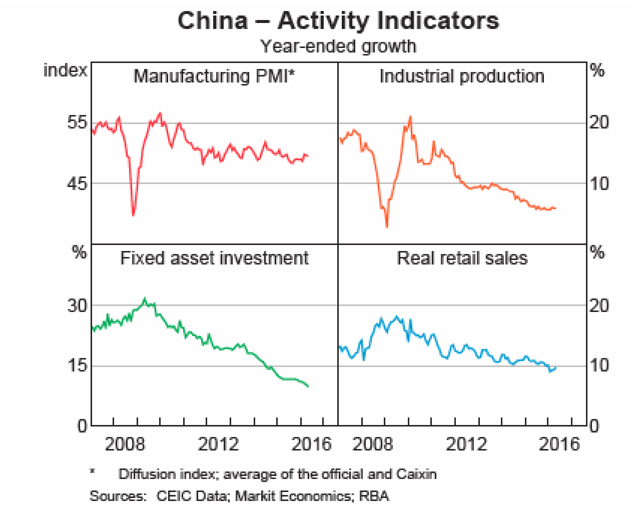
Australian banks, meanwhile, face growing risks of their own. For one, as seen in the charts below, Australia has enjoyed a strong housing upturn in recent years thanks to low interest rates, but house prices in major capital cities such as Sydney and Melbourne are now relatively high, and reduced affordability has started to take its toll on home loan demand.

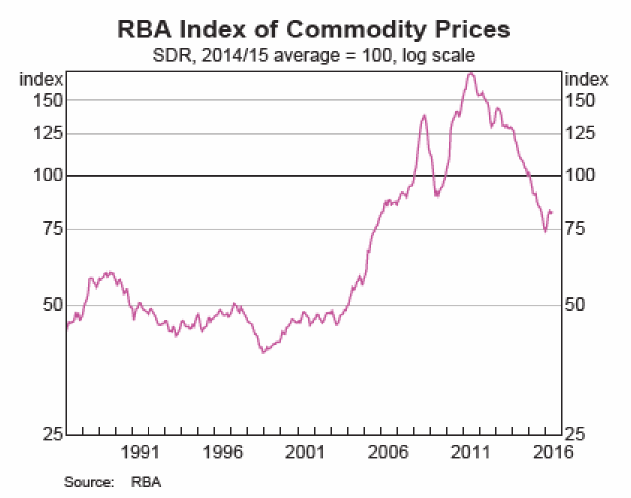
AUSTRALIAN HOUSING AND RESIDENTIAL LOAN INDICATORS



At the same time, as seen in the charts below, the Chinese economy continues to slow, while Australian export commodity prices – despite the solid falls in recent years – still remain high relative to their historic average. Australia remains exposed to a more severe downturn in the Chinese economy, and potential further weakness in national income through ever lower commodity prices.

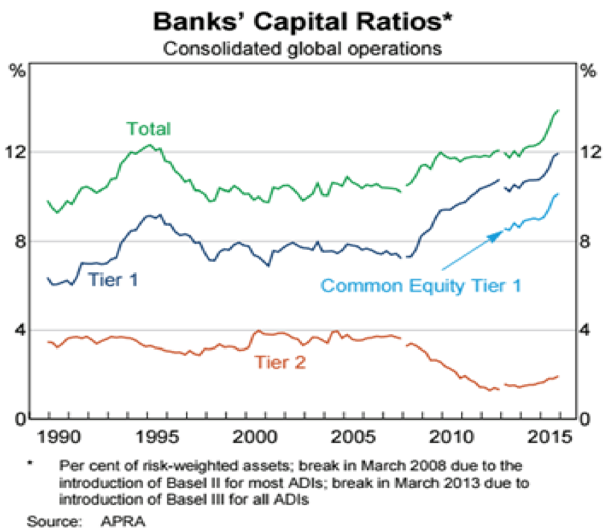
CHINA ACTIVITY INDICATORS AND COMMODITY PRICE INDEX





Arguably, Australian banks are "priced to perfection" with important contributions to earnings in recent years reflecting reduced bad debt write-offs. That leaves banks vulnerable to a potential upsurge in bad debts again as and when the housing sector slows and/or the economy weakens more broadly due to potential economic problems in China.

Another potential challenge to Australian banks' continued relatively high return-on-equity is the global trend toward higher capital ratios. Indeed, due to their exposure to the housing sector and still important reliance on access to international capital markets for funding, the Australian Prudential Regulation Authority (APRA) wants Australian banks to be "unquestionably strong" by global standards. This has meant a significant increase in bank capital raising in recent years to lift their capital ratios.



Note that APRA continues to assess whether Australian bank capital ratios need to rise further compared to international peers. In its latest assessment, APRA argued "Australian banks need to continue to improve their capital ratios in order to at least maintain, if not improve, their relative positioning".[1]

[1] International Comparison Update, APRA Insight Issue 2, 2016.

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Why use the BetaShares Global Banks ETF – Currency Hedged (ASX Code: BNKS)

Thanks to the advent of exchange traded products, it has never been easier for Australian investors to gain exposure to the global banking sector.

The BetaShares Global Banks ETF – Currency Hedged (ASX Code: BNKS) provides exposure to a diversified range of large-cap global banks. From the perspective of an Australian investor seeking financial sector exposure, BNKS offers a number of important advantages.

For starters, there's the obvious benefit of broad global diversification through the convenience of a single fund that can be purchased on the stock exchange just as easily as an Australian listed bank.

In addition, based on the historical trend, investors in BNKS can be expected to receive relatively higher income returns compared to the broad global equities market, due to the dividends paid by the underlying banks that BNKS invests in.

Another important feature of BNKS, moreover, is that it provides currency hedged exposure to global banks. That enables investors to largely disregard the potential impact on investment performance of often volatile movements in international currencies against the Australian dollar.

Like all BetaShares Funds, BNKS is also an Australian domiciled fund. Therefore, investors in BNKS do not need to fill out W-8 BEN forms, or risk any potential U.S. estate tax issues, unlike investors in "cross listed" alternative exposures.

Conclusion

Australian banks have performed relatively well in recent years and have been a popular choice for Australian investors due to their attractive dividend yields. That said, Australian banks are highly exposed to the local housing sector, and the Australian economy more generally is exposed to potential further weakness in commodity prices and the Chinese economy.

Australian banks also face potentially more onerous capital requirements in coming years due to the desire of prudential authorities to lift their capital adequacy ratios from around the median to the top quartile of global peers.

These challenges suggest those seeking banking exposure within their portfolio might do well to consider some international diversification.

Global banks themselves also have scope to improve as they continue to shake off the ravages of the financial crisis. As the global economy continues to grow and financial activity picks up, there appears scope for global banks to improve returns on equity which, in turn, could be reflected in an improvement in relative price-to-book value vis-à-vis Australian banks.

There are risks associated with an investment in the Fund, including market risk, bank sector risk and concentration risk. For more information on risks and other features of the Fund please see the Product Disclosure Statement.

Trading Information

BetaShares ETFs can be bought or sold during the trading day on the ASX, and trade like shares.

EXCHANGE	ASX
ASX CODE	BNKS
CURRENCY	AUD
TRADING	10:00-16:00 (AEST)
BLOOMBERG CODE	BNKS AU
IRESS CODE	BNKS.AXW

Index Information

INDEX	Nasdaq Global ex-Australia Banks Hedged AUD Index
BLOOMBERG INDEX CODE	NQXAUHBN INDEX

Fund Information

ISSUER	BetaShares Capital Ltd
ADMINISTRATOR	RBC Investor Services
CUSTODIAN	RBC Investor Services
REGISTRAR	Link Market Services
AUDITOR	KPMG
DISTRIBUTIONS	Semi-Annual
MANAGEMENT FEE	0.47% p.a
EXPENSES	estimated at 0.10% p.a
FUND INCEPTION	28 July 2016

Available at betashares.com.au

- Net asset value
- Product disclosure statement
- Portfolio holdings
- Distribution details

Contacts for Institutional Clients

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