

THE CASE FOR EUROPE

BetaShares WisdomTree Europe ETF - Currency Hedged (ASX: HEUR)



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While most Australians think of Europe as a great holiday destination, it probably remains under-appreciated as an investment opportunity by many investors. After all, Europe comprises a wide range of countries with differing cultures and business climates. The region's economy has also struggled in recent years with relatively low growth and stubborn price deflation, not to mention the debt problems in some countries such as Italy and Greece.

As this note will demonstrate, Europe offers a potentially good investment destination and diversifier for Australians.

Thanks to the continued growth in the Australian exchange traded fund industry, moreover, it has now never been easier for Australians to get exposure to the performance of European companies, particularly through the **Betashares WisdomTree Europe ETF – Currency Hedged (ASX: HEUR)**.

Europe's equity performance has been surprisingly good over the medium/long-term

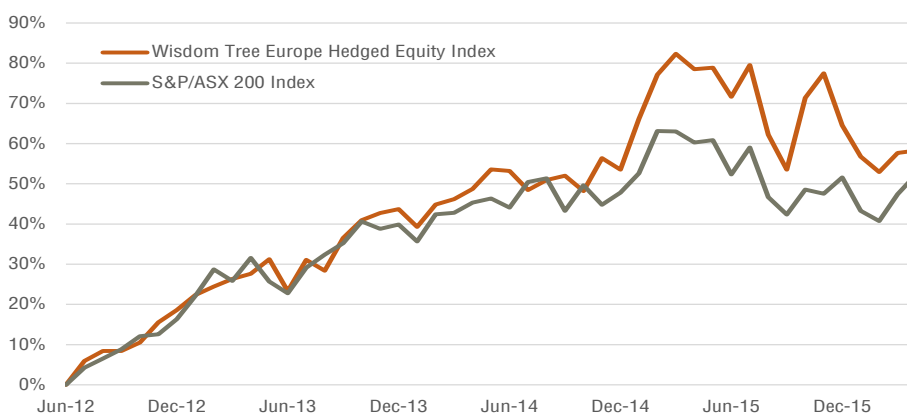
Although its economy has continued to struggle of late, and the European equity market has pulled back over the past year, it has performed relatively well in recent years and its medium-term prospects remain favourable. As seen in the table and chart below, the Index which HEUR aims to track, the Wisdom Tree Europe Hedged Equity Index (in local currency terms) has produced annual compound returns of 7.4% p.a. over the three years to April 2016, compared to only 5.0% p.a. for the Australian S&P/ASX 200 Index.

TOTAL RETURN EQUITY PERFORMANCE - TO 29 APRIL 2016, LOCAL CURRENCY

	1-yr	3-yr	Since Inception*
Wisdom Tree Europe Hedged Equity Index	-11.3%	7.4%	12.7%
S&P/ASX 200 Index-	-4.9%	5.0%	9.4%

Source: Bloomberg. Table shows performance of underlying index relative to S&P/ASX 200 Index, not ETF performance and does not take into account ETF management costs. You cannot invest directly in an index. Returns for periods longer than one year are annualised. Past performance is not an indicator of future performance of index or ETF. Inception date of WisdomTree Index 29 June 2012

EUROPEAN EQUITY PERFORMANCE V S&P/ASX 200 INDEX – CUMULATIVE RETURN 29 JUNE 2012 TO 29 APRIL 2016



Source: Bloomberg

Graph shows performance of underlying index relative to S&P/ASX 200 Index, not ETF performance and does not take into account ETF management costs. You cannot invest directly in an index. Past performance is not an indicator of future performance of index or ETF.

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Unlike Australia, Europe is a net-commodity importer, meaning it has benefited from the decline in commodity prices in recent years. What's more, due to low inflation and relatively more spare capacity, the European Central Bank is likely to remain more accommodative than that of the United States Federal Reserve for the foreseeable future, meaning European stocks could benefit from ongoing monetary stimulus and a cheaper and more competitive currency.

Relative valuations for Europe are attractive

Relative to underlying growth in their respective economies, the European equity market appears to offer comparably good value to that of the United States. As the chart below suggests, although both markets have broadly posted similar performance over past cycles, the US equity market has outperformed that of Europe in recent years - suggesting scope for catch up potential in Europe should the historical performance similarities return in the future.

CYCLICALLY ADJUSTED PRICE-EARNINGS RATIO: DECEMBER 1995 TO APRIL 2016

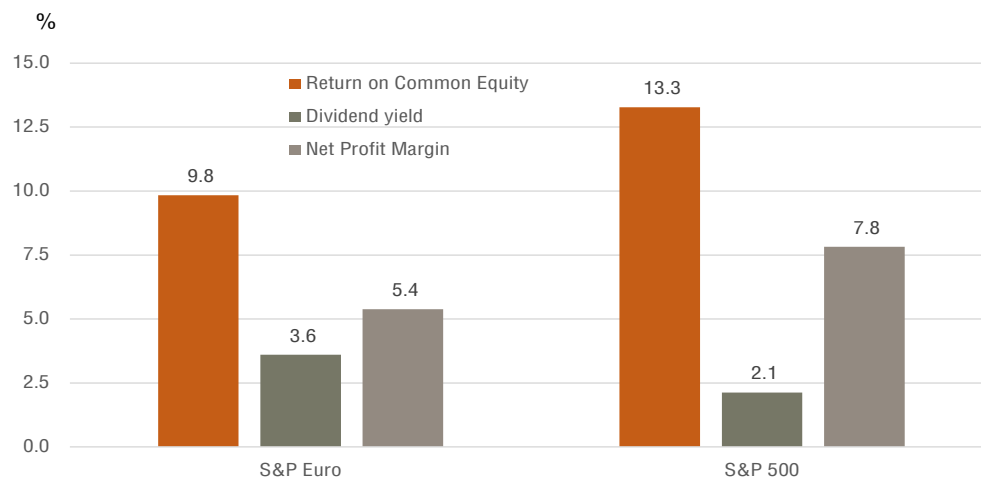


*Price to trend forward earnings Dec-94

Source: Bloomberg. Past performance is not an indicator of future performance

Good dividends and scope for even better profitability in European companies

Another feature of European equities is that companies in the region tend to pay out higher dividends than their US counterparts – meaning they offer one of the better sources of income potential for Australian investors seeking international equity exposure. What's more, on some profitability measures – such as return on equity and profit margins - European companies still tend to lag US companies, so there's scope to improve earnings further as companies strive to improve shareholder value.



Source: Bloomberg. Past performance is not an indicator of future performance

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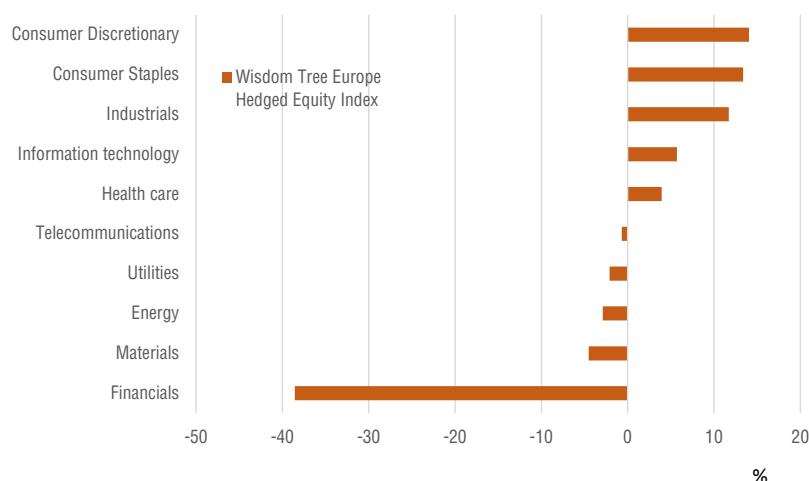


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Europe: A good source of diversity

As most investors would appreciate, there is value in having a diversified portfolio. In this regard, Europe offers quite distinct sector exposures from those found in Australia. Compared to the Australian S&P/ASX 200 Index, the Wisdom Tree Europe Hedged Equity Index has notably less exposure to financials, offset by more exposure to the consumer, industrial and technology sectors.

SECTOR WEIGHT DIFFERENCES WITH S&P/ASX 200 INDEX*



Source: Bloomberg. *As at December 2015

The Betashares WisdomTree Europe ETF – Currency Hedged (ASX: HEUR)

As an ASX traded product, HEUR is designed to provide Australian investors relatively easy and diversified exposure to the European equity market through a single, transparent fund, with competitive management costs. But while HEUR allows investors to gain exposure to European equities just as easily as they can to listed Australian company shares, it is also structured to focus on globally competitive dividend-paying companies, and to minimise the currency risks. In addition, as a locally domiciled fund, it reduces the administrative obligations that can be associated with some other ASX-traded ETFs providing exposure to international equities.

> **Getting paid to reduce downside Euro currency risk**

When investing internationally, investors have a choice to either hedge or not to hedge currency risk. Not hedging currency risk effectively means investment performance will reflect two often disparate factors: the performance of the international equity market in question, and the performance of that market's relevant currency. In the case of an unhedged investment in Europe by Australian investors, for example, any returns from the equity market would be offset to the extent the Euro also fell against the Australian dollar – though, of course, returns would also be boosted if the Euro rose in value.

So as to provide a “purer” exposure to the European equity market – without having to worry about the currency – HEUR is currency hedged for Australian investors. While picking currency trends is notoriously difficult, in the current global climate hedging also has the advantage of guarding against potential future substantial weakness in the Euro given the determination of European Central Bank President Mario Draghi to do “whatever it takes” to ward off deflation across the Euro-zone.

Indeed, the ECB has already pushed official interest rates into negative territory and has embarked on an extensive quantitative easing program which has already pushed central bank assets to around 30% of Eurozone GDP. Due to a reliance on exports as a source of economic growth, European policy makers remain very keen to encourage a competitively cheap Euro.

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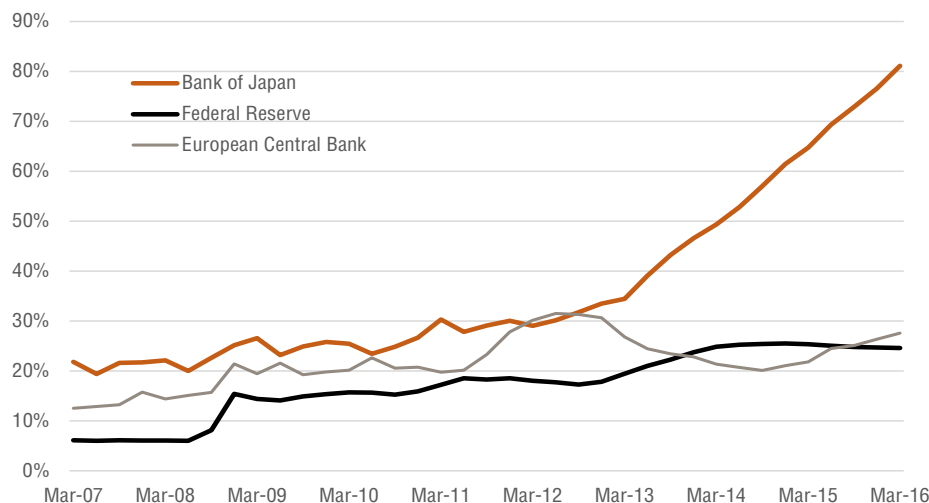


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CENTRAL BANK ASSETS - % OF NOMINAL GDP: MARCH 2007 - MARCH 2016



Indeed, to the extent Europe's equity market in coming years is benefited by currency weakness, it suggests tactical allocations to the market by foreign investors on a hedged basis may bear fruit. As such, investors exposed to the Euro as well as European equities may not be able to fully realise the equity market's potential gains. By hedging exposure to the Euro, HEUR offers investors a way to more fully access the return potential of European equities in a weakening Euro environment.

Another advantage of currency hedging in the case of a region such as Europe with very low (in fact currently negative) overnight interest rates is that it provides Australian investors access to the 'carry trade' (i.e. the relative difference between European interest rates and those of Australia). This interest rate differential is essentially passed on to investors which boosts returns over time (so long as the interest rate differential remains positive). That's because the process of hedging currency risk is akin to borrowing Euros (at very low rates) – to offset the currency exposure from the investment in European equities – and then using these borrowings to buy Australian dollars which earn a higher interest rate return.

In other words, Australian investors are paid to reduce their currency risk by hedging exposure to fluctuations in the Euro.

> **Focus on globally competitive dividend paying companies**

The index which HEUR aims to track adopts transparent "rules based" criteria for stocks to be included in the index that focus on the largest dividend paying stocks on European markets that trade in Euros and which also generate a portion of their revenues offshore (no more than 50% of the company's revenues can be generated from inside Europe). This allows HEUR to provide exposure to a selection of globally competitive European companies. These companies are well placed to benefit from growth in international trade and the potential ongoing reliance by European economies on exports and currency weakness to sustain economic growth. By weighting stocks according to dividends, moreover, the Fund's index tilts exposure toward those companies with the potential to produce sustainable profits and which are focused on shareholder value.

> **Reduced administrative and international tax obligations**

Like all BetaShares Funds, HEUR is an Australian domiciled fund. Therefore, investors in HEUR 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.

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Benefits of BetaShares WisdomTree Europe ETF – Currency Hedged

- Access - simple and cost-effective way to access a diversified portfolio of European equities
- Reduce currency risk – Euro exposure is hedged substantially back to the Australian dollar to reduce currency risk for Australian investors
- Diversification - diversify global equities allocation to Europe, which includes a number of sectors which are under-represented in the Australian equities market
- Low cost – cost of ETF is lower than traditional active managers focusing on European equities
- Reduced administrative burden – as an Australian domiciled fund, investors do not need to fill out W-8 BEN forms, or risk any potential U.S. estate tax issues
- ASX-traded – the ETF can be bought or sold like any share, and is not platform dependent
- Liquidity – trades on ASX during the day
- Transparent – portfolio holdings, value of ETF's assets and net asset value per unit available daily on BetaShares' website

Uses of BetaShares WisdomTree Europe ETF – Currency Hedged

The ETF may be suitable for a variety of investors and uses including:

- Gain broad exposure to dividend paying, globally competitive European companies
- A core component of a global equities allocation providing transparency and diversification benefits
- Tactical exposure to European equities

Trading Information

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

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

Index Information

INDEX	WisdomTree Europe Hedged Equity Index
BLOOMBERG INDEX CODE	WTEHIT 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 FEES	0.51% p.a
EXPENSES	estimated 0.07% p.a
FUND INCEPTION	10 May 2016

Available at betashares.com.au

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

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