BetaShares
Exchange Traded Funds

Global
Market Review

March Qtr 2015

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SUMMARY

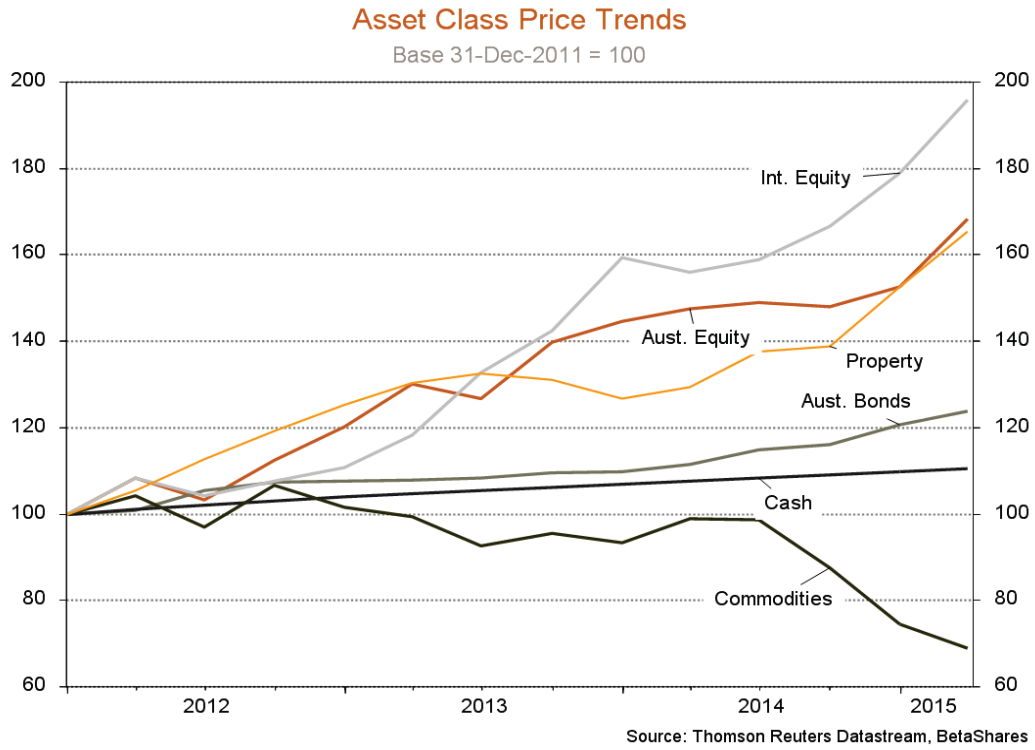
Both local and international equities posted solid gains in the March quarter, reflecting continued confidence that central banks will retain an accommodative policy in the face of low global inflation – with Europe's quantitative easing program a major new feature. In unhedged (i.e. $A) terms, international equities were also boosted by further weakness in the Australian dollar. As in Europe, local equities got a boost as the Reserve Bank switched back to an easing policy bias, after a "surprise" rate cut in February. Commodity prices remained under downward pressure. All up, however, low interest rates continue to push up equity valuations and prices, even though persistent soft economic growth has led to an intensification of corporate earnings downgrades.

Asset Class: Total Return Performance - March Qtr 2015

	3-mth	6-mth	12-mth	3-mth	6-mth	12-mth
Cash	0.7%	1.4%	2.7%	5	5	5
Aust. Bonds	2.7%	6.7%	11.1%	4	4	4
Aust. Property	9.4%	22.0%	34.7%	3	1	1
Aust. Equities	10.3%	13.8%	14.1%	1	3	3
Int. Equities*	10.1%	18.8%	28.8%	2	2	2
Commodities**	-7.6%	-21.2%	-30.2%	6	6	6

*Unhedged **Hedged

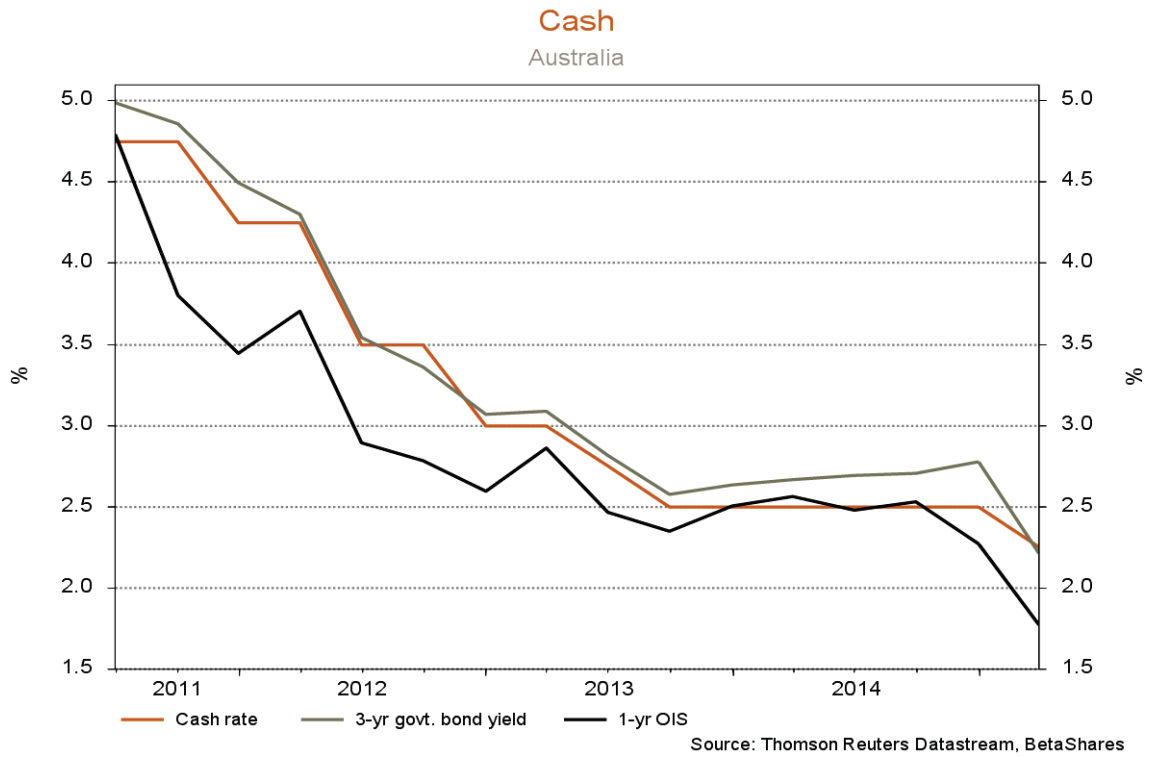
Source: Thomson Reuters DataStream. Past performance is not an indication of future performance.



CASH

Cash rates moved lower over the March quarter following the Reserve Bank's decision to cut the official cash rate from 2.5% to 2.25% p.a. The RBA hinted at further possible rate cuts if needed to support the economy. Although the housing market – particularly in Sydney – remains strong, export commodity prices have dropped notably and business and consumer confidence remain subdued. And although the $A has fallen, the RBA still appears to feel it is overvalued given the weakness in commodity prices.

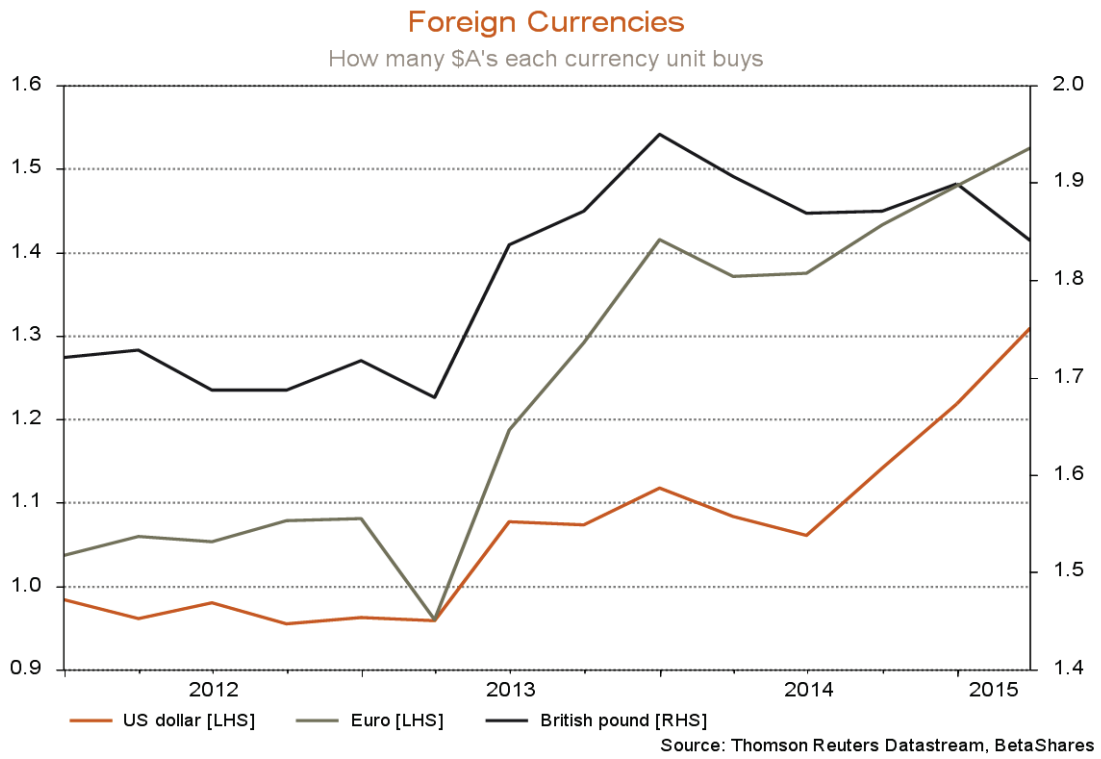
The market ended the quarter expecting the RBA to cut the official cash rate to around 1.75% over the coming year.



Bassanese's Outlook: My core view is that official interest rates will be cut again by mid-year, and end the year at 1.5% p.a.. This reflects my expectation that economic growth will remain sub-trend at least until mid-2016 - longer than the RBA currently expects - due to continued disappointment on the rebound in non-mining investment. There is also a risk that home building approvals – which are already at a high level – could peak within coming months. Cash returns look like being sub-2% over the coming year.

FOREIGN CURRENCIES

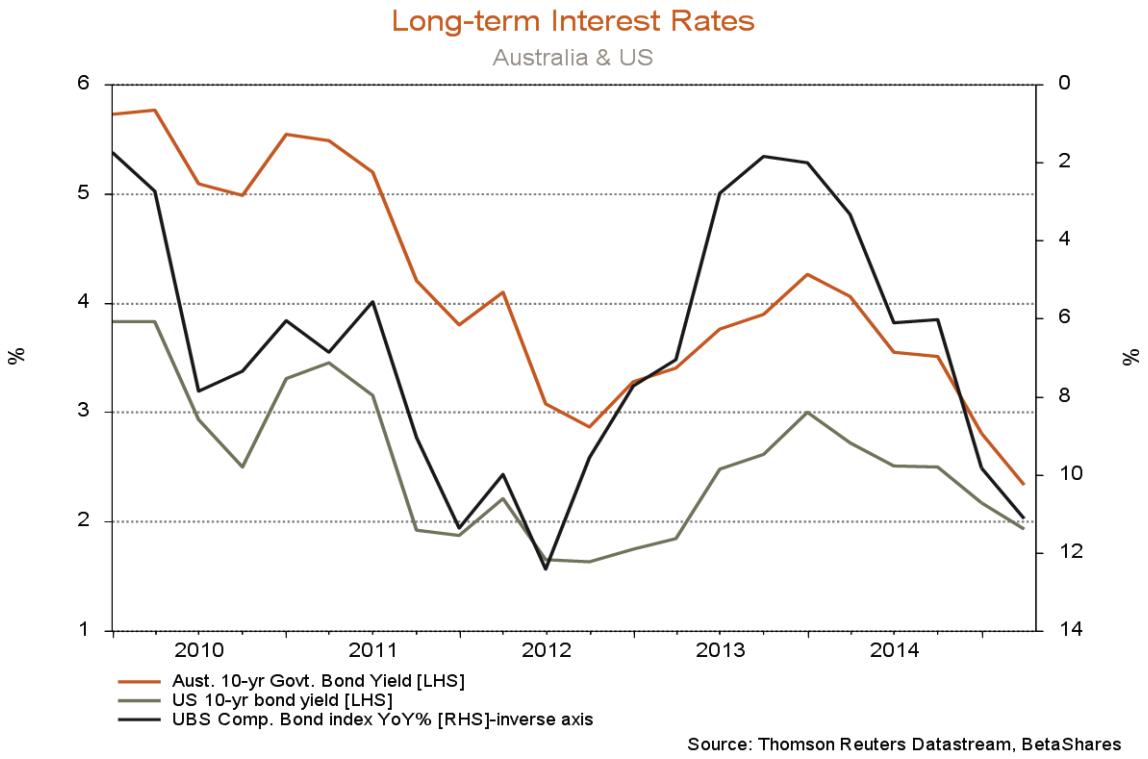
Both the Euro and US dollar rose against the Australian dollar in the March quarter due to both the steep decline in commodity prices and the shift to an easing policy bias by the RBA. Against the Aussie, the US dollar rose by 7.4% in the quarter, to be up 20.8% over the past year. Despite the weaker $A, however, the RBA still maintains it is a little overvalued given the equally steep decline in commodity prices over recent months.



Bassanese's Outlook: My core view remains that the $A will continue to slide this year, reaching around US68c by year-end Lower local interest rates, continued soft commodity prices, and higher interest rates in the United States, should all conspire to push the Aussie lower. Given the soft Australian economy, a weaker $A is one of the key requirements to help re-balance growth following the end of the mining boom.

AUSTRALIAN BONDS

Already low bond yields fell even lower over the past quarter, continuing to confound wide-spread market expectations that yields would eventually rise as tightening by the US Federal Reserve loomed into view. Instead, falling oil prices – which have added to downward pressure on global inflation – together with a continued cautious stance by the US Federal Reserve over when it will begin to raise official US rates, helped push yields lower. **Australian 10-year government bond yields declined from 2.8% to 2.3% over the March quarter. The Bloomberg Australian Composite Bond Total Return Index gained a further 2.7% in the quarter, to be 11.1% higher over the past year.** Long-term Australian bond yields remain low by historic standards, but are still relatively attractive against even lower yields on offer in the United States, Europe and Japan.

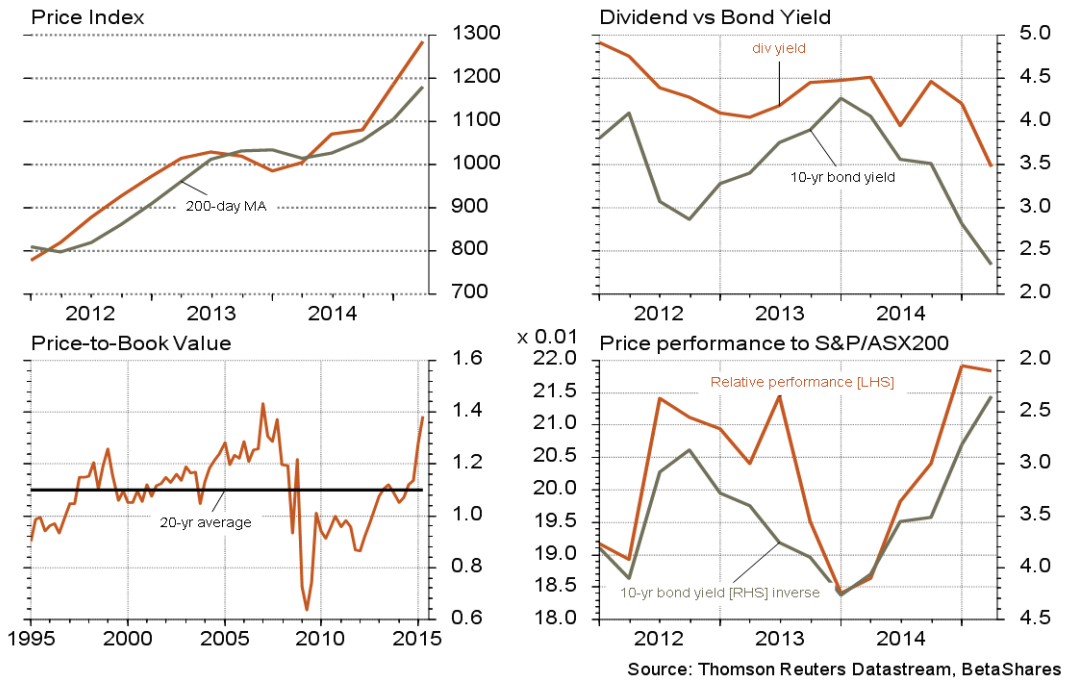


Bassanese's Outlook: Despite the continued rally in bond yields, I remain negative on the medium-term bond market outlook - given my confidence in America's economic recovery and expectation that the Fed will begin tightening in either June or September. That said, as local official interest rates head lower, the spread between Australian and US bond yields should narrow further. Given global bond yields should eventually move higher from today's quite low levels, only muted fixed income returns over the coming year should be expected.

LISTED PROPERTY

The listed property sector posted solid total returns of 9.4% in the March quarter, helped by the further decline in bond yields. That said, the sector underperformed (slightly) the wider market last quarter for the first time since early last year. Reflecting the global "search for yield", foreign investor interest in the commercial property sector remains strong, even as pockets of excess supply are emerging – particularly in the office sector. The RBA has expressed concerned about rising commercial property valuations in the face of rising vacancy rates. More broadly, traditional price-to-book valuations for the sector are now approaching pre-financial crisis levels.

S&P/ASX 200 A-REITs

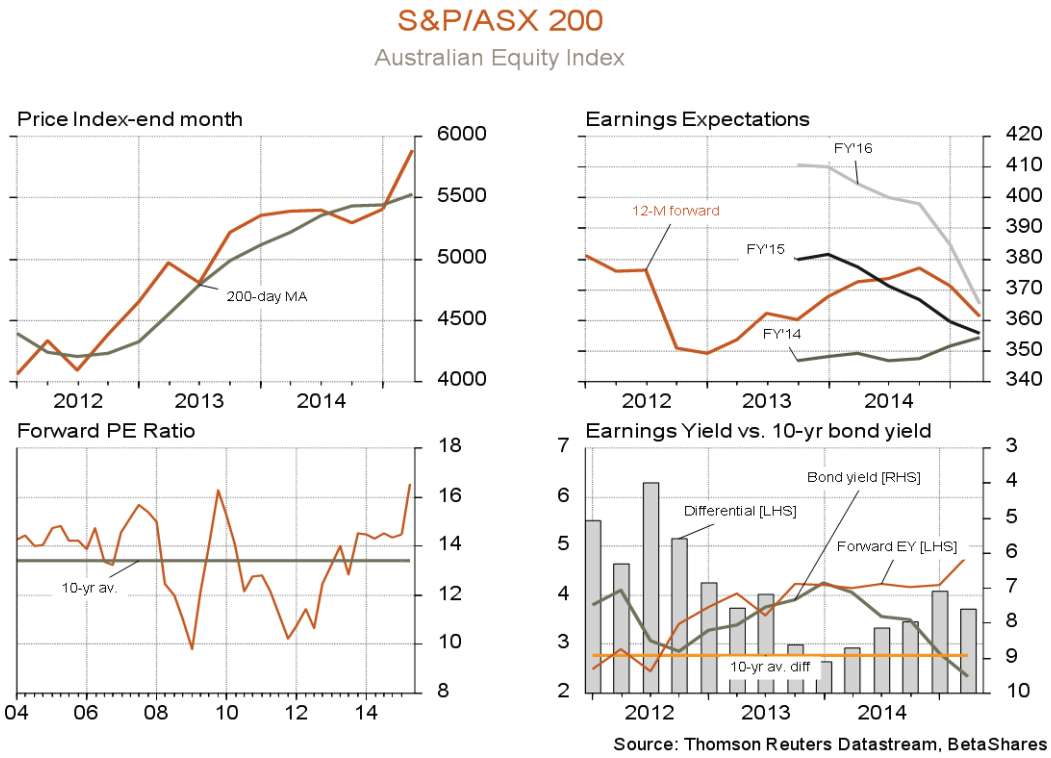


Source: Thomson Reuters Datastream, BetaShares

Bassanese's Outlook: With price to book valuations getting stretched, the sector is vulnerable to a correction as and when bond yields rebound. In the meantime, the "yield chase" is likely to continue to favour outperformance by the sector. In line with my view on bond yields, however, I would adopt a cautious medium-term outlook – with property likely to underperform on a one to three year view.

AUSTRALIAN EQUITIES

After travelling sideways for much of 2014, Australian equity total returns surged by 10.3% in the March quarter - to be up 14.1% over the year. The switch in the local interest rate outlook was a major factor. Indeed, equities rose despite a continued steep decline in corporate earnings expectations and persistent weakness in the economy – highlighting the fact that the market remains very much yield driven. After rising through 2013 and most of 2014, the market's "forward earnings" measure has now declined over the past two quarters – adding further upward pressure to the price-to-earnings ratio. Relative to (very low) bond yields, the market remains cheap, though outright PE valuations are now around their highs over the past decade.

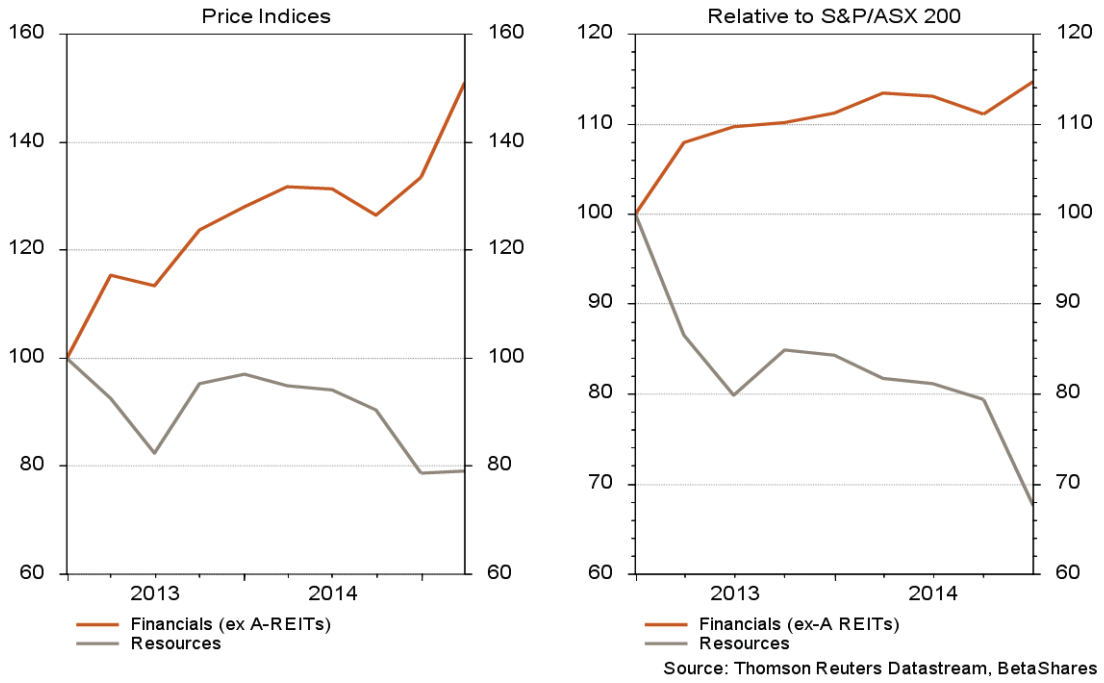


Bassanese's Outlook: While outright market valuations are now expensive and earnings are under downward pressure, the market's dividend yield still remains attractive in a low interest-rate environment. The prospect of lower local interest rates and weaker $A should continue to support market sentiment in coming months - though the market is vulnerable should the economy and earnings not begin to improve by late 2015. High US interest rates and an associated pull back in global equities is another downside risk.

RESOURCES VS. FINANCIALS SECTOR

The **trend favouring financials over resources remained in place in the March quarter, with total returns for the former sector up 14.1% compared with the latter's gain of only 3.1%.** As with listed property, declining bond yields are helping support high yielding sectors like financials, while weakness in commodity prices continues to plague the resources sector.

S&P/ASX 200 Sectors-end month



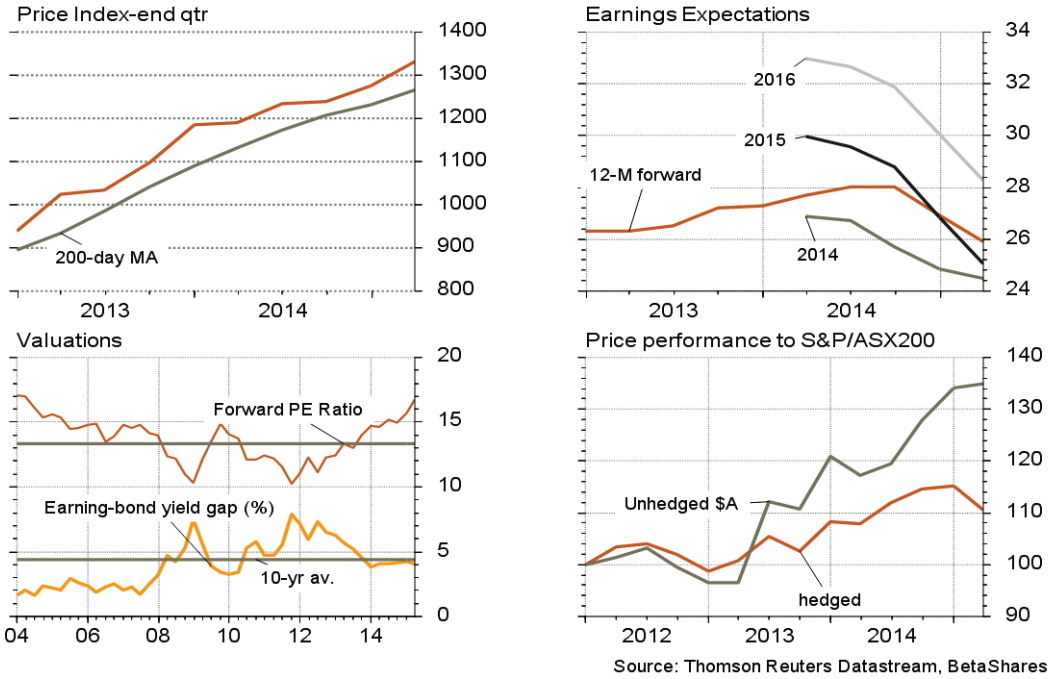
Bassanese's Outlook: Given low interest rates and weak commodity prices, the market environment should continue to favour outperformance by financials over resources. As with listed property, however, an eventual rise in bond yields poses a risk to the financial sector outlook.

INTERNATIONAL EQUITIES

The world (developed markets) **MSCI total return index rose by 5.0% in hedged (local currency) terms over the March quarter,** slightly reversing the trend of outperformance against Australian equities over the past year. Global equities were largely held back by the US market, where prices rose only 1.4% in the quarter, compared with gains of 11.2% and 9.3% in Europe and Japan respectively. As in Australia, however, equity gains came despite continued downgrades to the corporate earnings outlook – and a decline in "forward earnings". **On an unhedged basis, the world MSCI total returns index rose a much stronger 10.1%,** due to weakness in the Australian dollar.

As in Australia, outright global equity price-to-earnings valuations are now around peak levels over the past decade. The earnings-to-bond yield gap, however, remains close to its 10-year average, suggesting that relative to bond yields the market is still fairly valued.

World MSCI

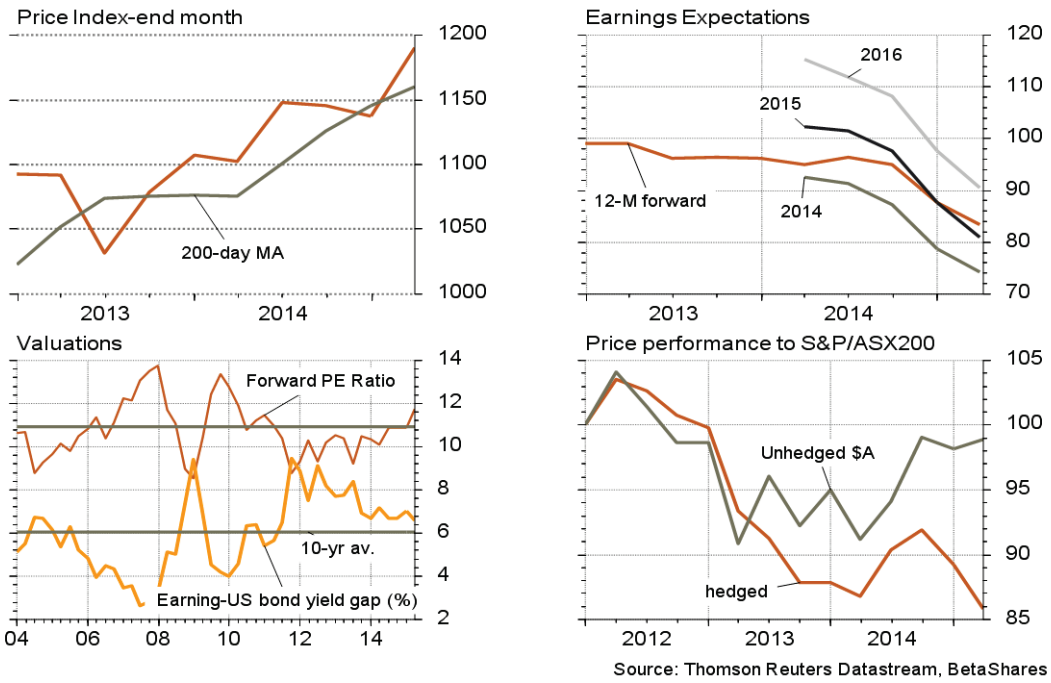


Bassanese's Outlook: I remain positive on global equity markets due to still reasonable valuations against bond yields. Low inflation means central banks will also keep policy expansionary, especially if equity markets correct. That said, global "forward earnings" have started to turn down, and outright valuations are becoming expensive. As a result, the market seems increasingly vulnerable to another decent correction to restore more alluring value for investors. With interest rates set to decline in Australia, I am neutral on relative international performance (against Australia) in hedged terms – but continue to expect outperformance in unhedged terms due to further $A weakness.

EMERGING MARKETS

The **MSCI Emerging Markets total returns index also rose 5.0% in the March quarter in hedged local currency terms, and by 10.1% in unhedged (A$) terms**. Performance across the major emerging economies was mixed, with Chinese and Russian markets up strongly, and more muted gains in India and Brazil. China's market has lifted strongly of late with speculative money switching from property to shares and further central bank policy easing. Russia rebounded after a steep sell-off late last year amid an easing in tensions with Ukraine and hopes of an eventual stabilisation in oil prices. Emerging market outright PE valuations are still only slightly above their decade average, with the earnings-to-bond yield gap a little higher than the decade average – suggesting the market is on the cheaper side of fair value relative to interest rates.

MSCI Emerging Markets



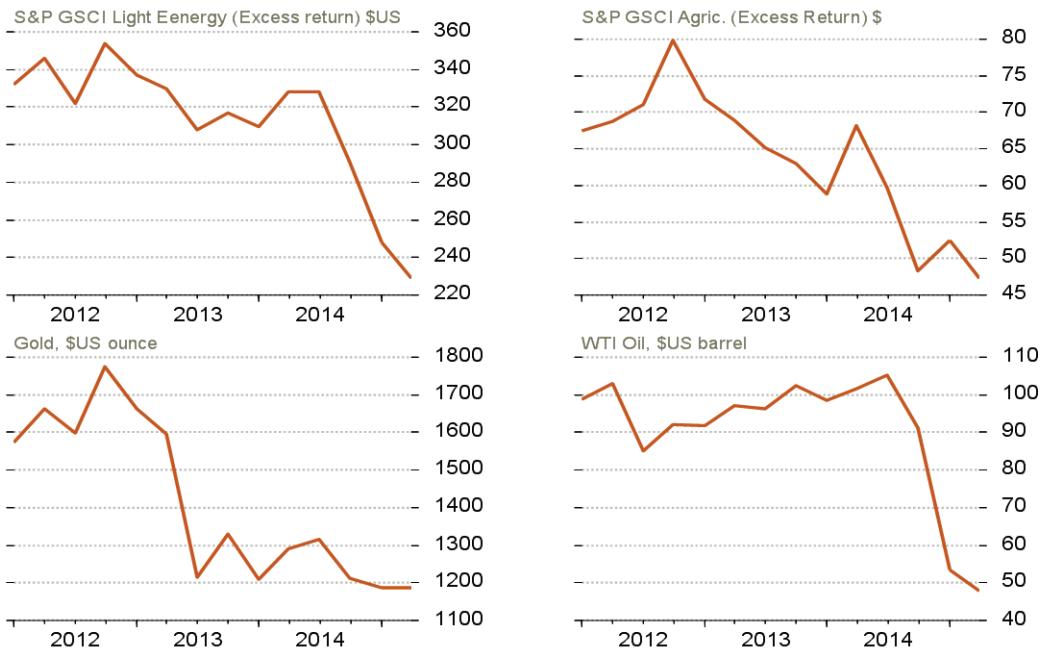
Bassanese's Outlook: My core view is that emerging markets should continue to benefit from the broader global equity market upswing, but due to greater capital flow and commodity-producer exposure the asset class may underperform developed markets if, as expected, the US begins to raise interest rates. I am neutral on the asset class compared to Australia.

China's market, however, appears to be developing a major head of steam as speculative capital switches from the property market to equities. The fact China is a net-commodity importer also helps.

COMMODITIES

The broad **S&P GSCI Light Energy index fell a further 7.6% in the March quarter, with a relapse in agricultural prices and a further decline in oil prices.** That said, gold prices stabilised over the quarter, and the decline in oil prices was less rapid than evident the previous few quarters. Signs of US production cut backs appear to have helped stem the slide in oil prices, while gold benefited from some doubts over how quickly the US Fed would raise interest rates. Agricultural prices fell back, however, given continued good growing conditions in the United States and ample stocks.

Commodities



Source: Thomson Reuters Datastream, BetaShares

Bassanese's Outlook: As I've long maintained, modest global economic growth, low inflation, rising supply and a gradually strengthening US dollar make it hard to be positive on the nearer-term commodity price outlook. That said, the slump in oil in recent months has been so severe that at least a short-run corrective rally now seems possible.

The long-term agricultural price outlook remains positive - due to rising Asian living standards. As has been evident in recent years, moreover, commodities such as oil and gold continue to offer useful hedges should a more severe outbreak of geo-political instability or global inflation arise.

ASSET PERFORMANCE MARCH QTR 2015: DETAILED REVIEW*

	3-mth	6-mth	12-mth
Cash	0.7%	1.4%	2.7%
US Dollar	7.4%	14.6%	20.8%
Aust. Bonds	2.7%	6.7%	11.1%
Aust. Property	9.4%	22.0%	34.7%
Aust. Equities	10.3%	13.8%	14.1%
Financials	14.1%	22.4%	20.7%
Resources	3.1%	-10.3%	-13.1%
Int. Equities	5.0%	8.5%	14.6%
-unhedged	10.1%	18.8%	28.8%
Em. Markets	5.0%	4.7%	10.9%
-unhedged	10.1%	12.0%	21.8%
Commodities	-7.6%	-21.2%	-30.2%
Agric.	-9.7%	-1.8%	-30.5%
Gold	0.1%	-2.1%	-7.9%
Oil	-10.7%	-47.7%	-53.0%

Price returns for latest month, total returns for 3 and 12 months periods.
Source: Thomson Reuters DataStream. Past performance is not an indication of future performance.

*ASSET BENCHMARKS

Cash: UBS Bank Bill Index
US Dollar: spot US dollar exchange rate vs. A$
Australia bonds: UBS Composite Bond Index
Australian property: S&P/ASX 200 A-REITs
Australian equities: S&P/ASX 200 Index
Financials: S&P/ASX 200 Financials (ex A-REITs)
Resources: S&P/ASX 200 Resources
International equities: MSCI World (developed market) Equity Index, local currency & unhedged $A terms
Emerging markets: MSCI Emerging Markets Equity Index, local currency & unhedged $A terms
Commodities: S&P GSCI Light Energy Index, $US terms
Agriculture: S&P GSCI Agricultural (excess return) Index, $US
Gold: spot gold bullion price/ounce, $US
Oil: West Texas Intermediate, price per barrel, $US.

BETASHARES PRODUCT OFFERINGS ACROSS ASSET CLASSES

Asset Class	Investment Exposure	BetaShares Fund	ASX Ticker	MER(%)
Australian Cash	Australian Cash	Australian High Interest Cash ETF	AAA	0.18%
Foreign Currencies	U.S. Dollars	U.S. Dollar ETF	USD	0.45%
	Euro	Euro ETF	EEU	0.45%
	British Pounds	British Pound ETF	POU	0.45%
Australian Equities	Largest 200 Australian companies by fundamental weight	FTSE RAFI Australia 200 ETF	QOZ	0.40%
	Financials Sector excluding A-REITS	S&P/ASX 200 Financials Sector ETF	QFN	0.39%
	Resources Sector	S&P/ASX 200 Resources Sector ETF	QRE	0.39%
	S&P/ASX 20 + Equity Income strategy	Equity Yield Maximiser Fund (managed fund)	YMAX	0.79%
	S&P/ASX 50 + Dividend Income strategy	Australian Dividend Harvester Fund (managed fund)	HVST	0.90%
	Geared exposure to diversified portfolio of Australian Equities	Geared Australian Equity Fund (hedge fund)	GEAR	0.80%
	Short Australian Equities	Australian Equities Bear Hedge Fund	BEAR	1.38%
International Equities	US S&P 500 Index + Equity Income strategy	S&P 500 Yield Maximiser	UMAX	0.79%
	Largest 1000 US Companies by fundamental weight	FTSE RAFI US 1000 ETF	QUS	0.40%
Commodities	Gold Bullion (US$)	Gold Bullion ETF - Currency Hedged	QAU	0.59%
	S&P GSCI Crude Oil Index	Crude Oil Index ETF – Currency Hedged (synthetic)	OOO	0.69%
	S&P GSCI Index (Light Energy)	Commodities Basket ETF – Currency Hedged (synthetic)	QCB	0.69%
	S&P Agriculture Enhanced Select Index	Agriculture ETF – Currency Hedged (synthetic)	QAG	0.69%

Other costs may apply. Please refer to PDS for more information.

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BetaShares Capital Ltd ("BetaShares") is a leading provider of exchange traded products ("ETPs") which are traded on the Australian Securities Exchange. BetaShares offers a range of ETPs which cover Australian and international equities, cash, currencies, commodities and alternative strategies. BetaShares currently has approximately $2.2 billion in assets under management.

BetaShares is a member of the Mirae Asset Global Investments Group, one of Asia's largest asset management firms. Mirae currently manages in excess of US$60B, including over US$8B in ETFs.

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