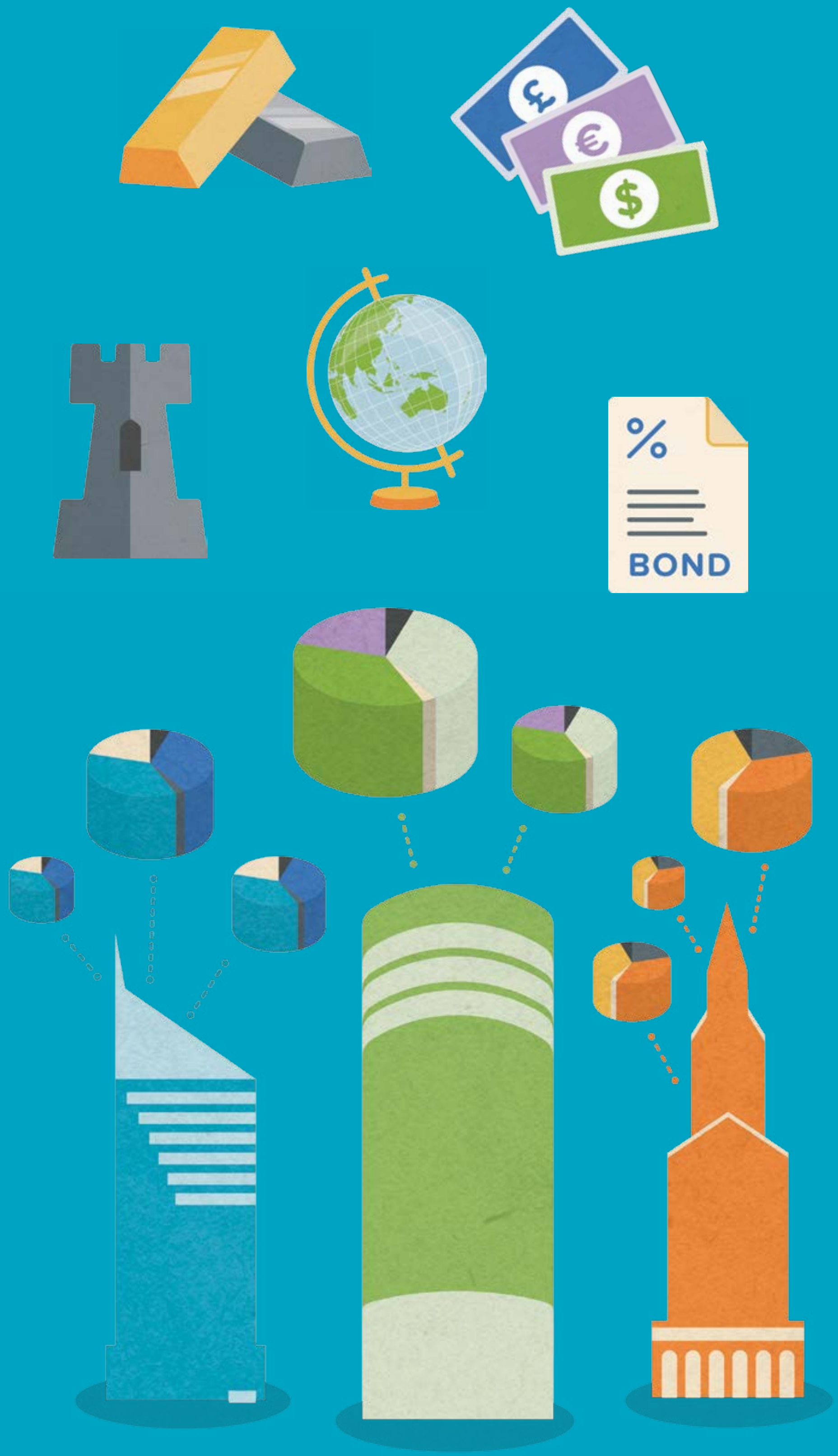
Australian ETF Report

2017

stockspot


£
€
$
%
BOND

Contents

About this report

Welcome to our third Australian ETF report which aims to help investors understand and compare ASX listed ETFs. We want to provide consumers with an objective, independent view of the ETF landscape.

The ETF market in Australia grew from $21.3 billion the past year to $27.2 billion. This represents increase of funds under management (FUM) 28% in the year since April 2016. The size of the ETF market has more than doubled in Australia since 2014. ETFs have become increasingly popular with individual investors, advisers and Self Managed Super Fund (SMSF) trustees due to their low-cost, transparency and diversification benefits, as well as being available on the ASX.

We've analysed over 150 ETFs and given them a rating out of 5 which takes into account factors including **fees, performance, size** and **activity.**

We also look at recent ETF market trends including the continued growth in **global ETFs,** the wide gap between the **performance of different sector and styles,** the **demand for bond and cash ETFs,** and the mixed performance of **alternative index ETFs.**

We hope you find the report useful and please let us know your feedback.

Chris Brycki
Founder & CEO, Stockspot

About Stockspot

Stockspot is Australia's largest digital investment adviser. Our aim is to make professional wealth management accessible to more Australians.

We want to do away with the high fees, confusing jargon, and lack of transparency that gives the wealth management industry a bad reputation.

We can see that:

- The high fees charged by many traditional wealth managers are completely unnecessary and are eating away at investment returns.
- Many Australians are unable to access a professionally managed portfolio due to the significant minimum balances.
- Those who are trying to invest themselves are usually missing out on the returns and diversification benefits of other assets like bonds and international shares.

That's why we created Stockspot.

We're helping Australians manage their money smarter with our simple, low-fee, online investment service.

Find out more:
www.stockspot.com.au

What are ETFs?

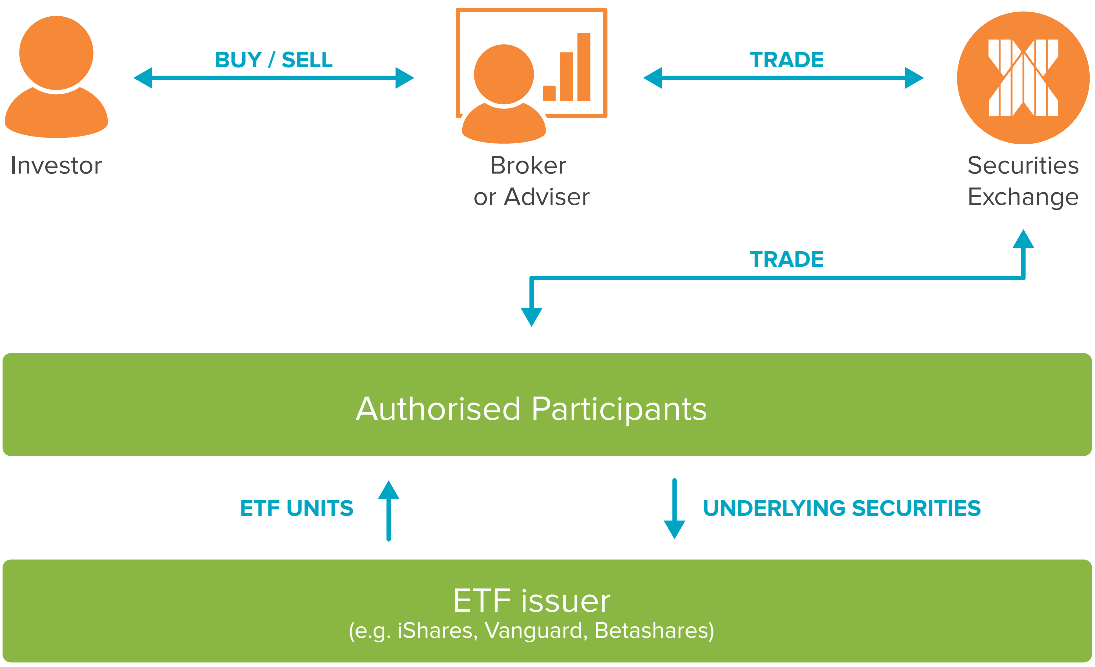
An exchange traded fund (ETF) is an open-ended investment fund that is traded on a stock-exchange. ETFs first emerged in the USA in the early 1990s and their recent explosive growth has led to more options being available across the world, including Australia since their introduction in 2001.

COMMON TYPES OF ETFS

Australian Index | Australian sector | International index | International sector | Fixed Income | Commodities

ETFs can be traded on the ASX in the same way as shares in a company. Rather than owning shares in a business, an ETF tracks an asset class, such as Australian shares or global shares, and provides direct exposure to a wide range of investments within that asset class.

HOW IT WORKS



Types of ETF

INCLUDED IN THIS REPORT

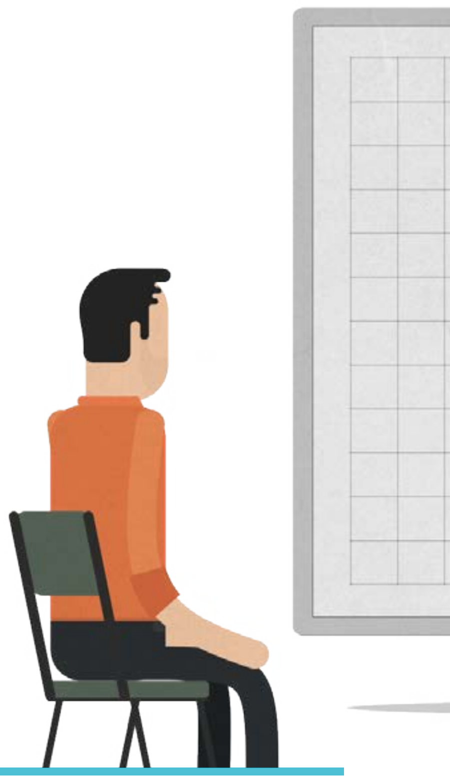
We have covered several types of exchange traded products (ETPs) in this report. Broadly they are all described as exchange traded funds (ETFs), however the ASX has more specific naming conventions to capture some of the subtle differences between exchange traded products:

Exchange traded fund (ETF) — Under ASX naming conventions, ETF technically refers only to funds that passively track an index. These are usually structured as a managed investment scheme, where investors hold units in a trust. The majority of ETPs are indeed ETFs and the remaining ETPs are types of actively managed funds with additional identifying characteristics.

Exchange traded structured products (SP) — These exchange traded products do not typically invest in the underlying asset, but instead aim to mimic the performance of an index synthetically via a structured agreement or derivative over futures contracts. This structure is most commonly used by issuers creating commodity indices as it is not feasible to hold most physical commodities. Where investors are exposed to counterparty risk of more than 10% of the fund's net asset value structured products must have the word 'synthetic' as part of their name for easy identification.

Exchange traded managed fund (ETMF) — These are also admitted to trading status on the ASX like ETFs, but are actively managed funds. Similarly to ETFs they are typically structured as managed investment schemes.

Exchange traded hedge fund (ETHF) — These are a specific type of exchange traded managed fund that fits within the regulations set out by ASIC criteria and class orders. These are funds that use complex instruments such as borrowing, options and short selling and are required to have the words 'hedge fund' in their title for identification. The 'hedge fund' title is a little confusing since these funds are not actually hedge funds as most people know them to be, but rather funds that offer leverage like the Geared Australian Equity Fund (GEAR) - or an inverse pay-off to the market like BetaShares Australian Equities Bear Fund (BEAR).



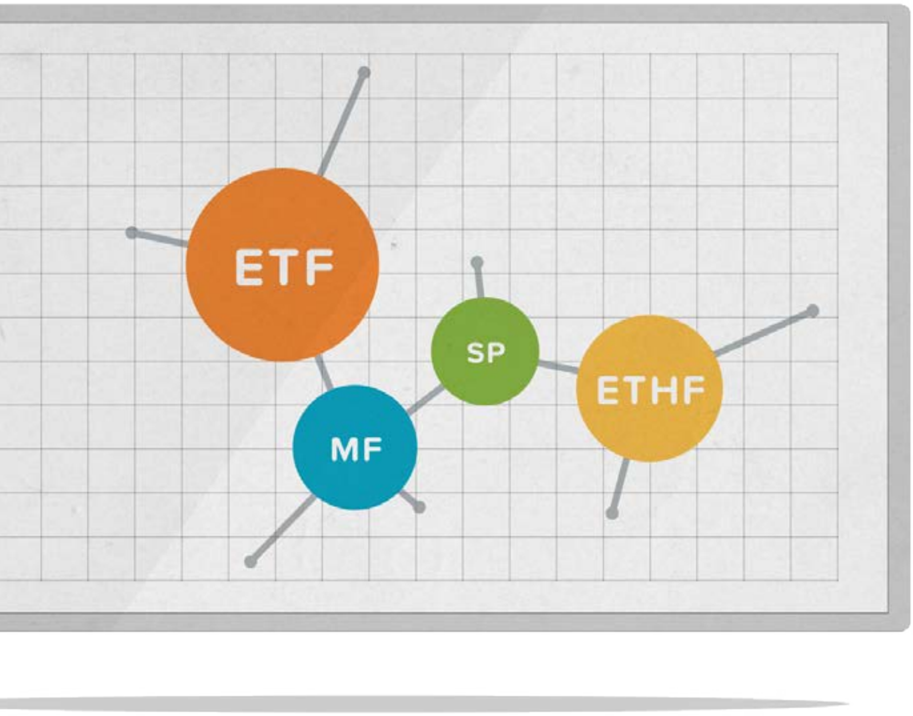
NOT INCLUDED IN THIS REPORT

There are also other investment fund options available on the ASX, which this report does not cover:

mFunds — This is an ASX-linked platform which enables investment in a range of unlisted managed funds via the ASX CHESS system. However there is no standard settlement timeframe across issuers and products. In addition there is no live pricing so investors must wait until after the close of trading each day to know the price of units that have been bought or sold.

Listed Investment Companies (LICs) — These are usually managed funds which are actively managed in a closed ended structure, which means that there is no unit creation/redemption process. Investors in LICs own shares in a company, which may trade at premium or discount to net asset value so there is no guarantee that the prices of LICs will resemble the value of underlying investments. As a result LICs often vary considerably from their Net Asset Value (NAV).

Infrastructure funds and Real Estate Investment Trusts (REITs) — These give investors exposure to portfolios of infrastructure or property assets. Similar to LICs, they can trade at a premium or discount to their Net Asset Value (NAV).



ETF Market Summary

+28% ››› $27.2B
ETF FUNDS UNDER MANAGEMENT

ETF funds under management grew 28% over the past year to to $27.2 billion.

NEW

11
NEW INTERNATIONAL SECTOR ETFS

11 out of 27 new ETFs were global sector ETFs.

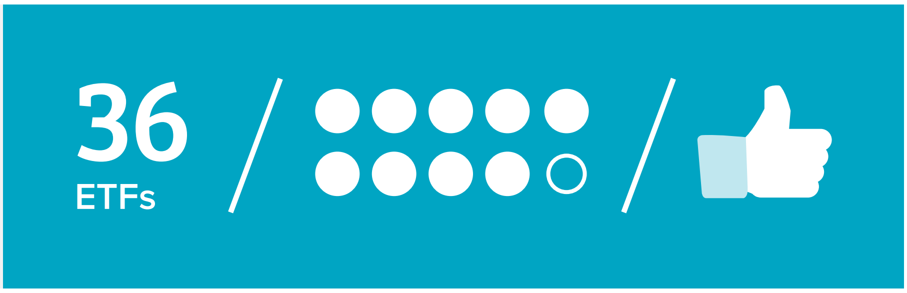
+43%
BEST PERFORMER

Best performing ETF was BetaShares' Geared Australian Equity Fund

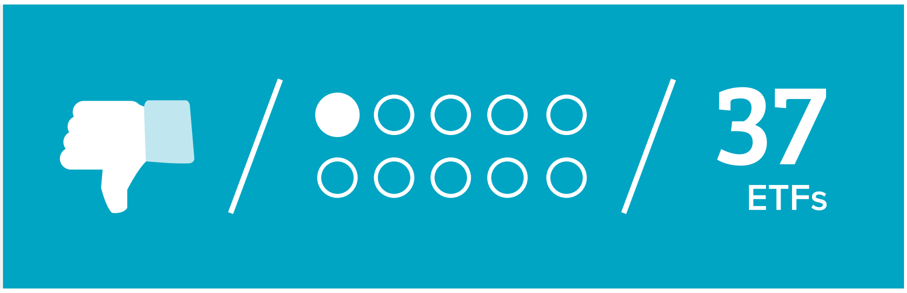
-37%
WORST PERFORMER

Worst performing ETF was BetaShares' Australian Strong Bear (Hedge Fund)

36 ETFs earned our highest ratings of 4 or 5 spots.
(14 with 5 spots)

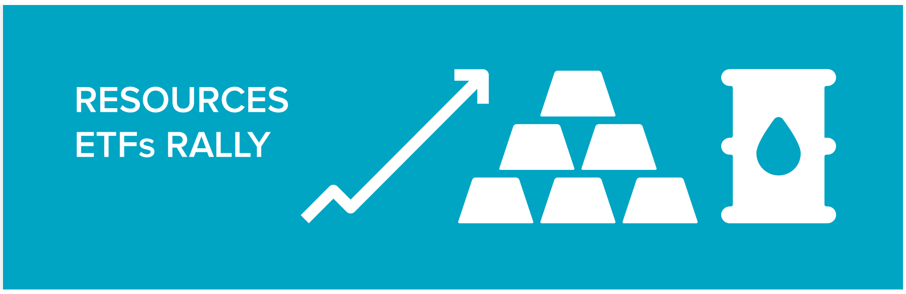


37 ETFs earned our lowest ratings of 0 or 1 spots.
(2 with 0 spots)



Vanguard continued its dominance with $2 billion of ETF growth (+42%)

Resources ETFs rallied 40% after 5 years of underperformance



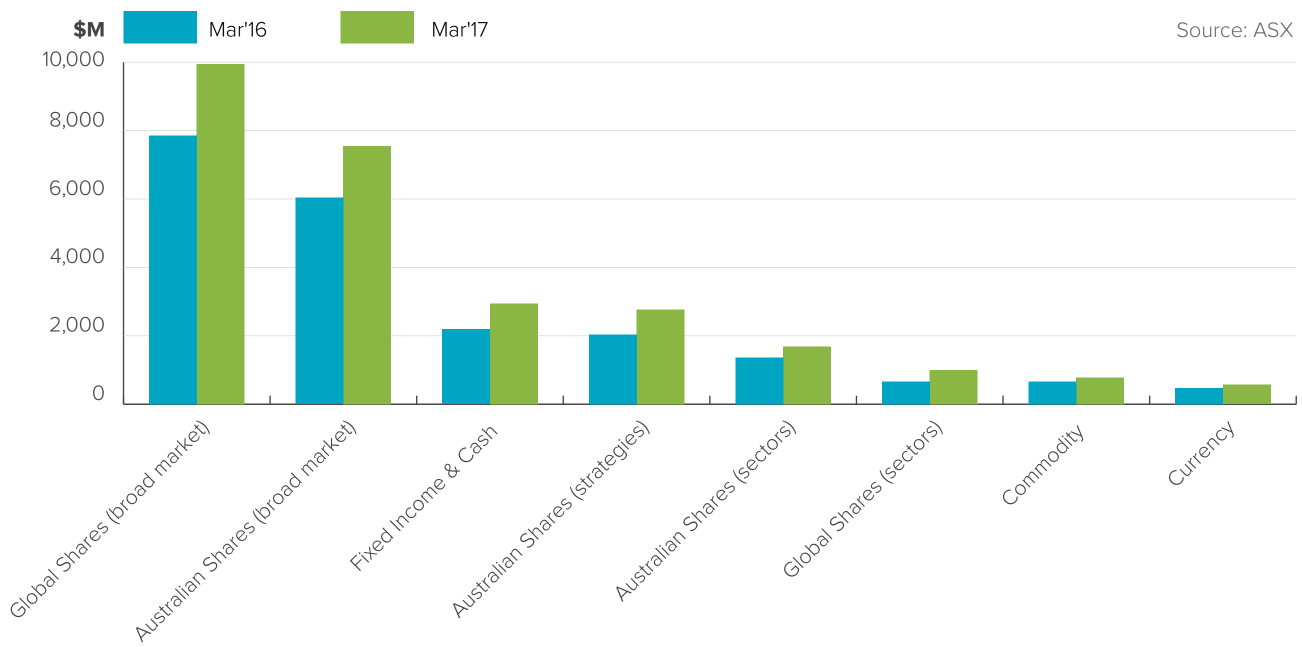
ETF Market Summary

By Sector Group

Sector	Number of Products	FUM ($M) Mar'16	FUM ($M) Mar'17	Annual change in FUM ($M)	Annual change in FUM (%)
Global Shares (broad market)	58	7,855	9,943	2,088	27%
Australian Shares (broad market)	16	6,036	7,550	1,514	25%
Fixed Income & Cash	17	2,191	2,946	754	34%
Australian Shares (strategies)	21	2,042	2,767	725	35%
Australian Shares (sectors)	9	1,370	1,687	317	23%
Global Shares (sectors)	16	665	1,005	341	51%
Commodity	11	664	780	116	17%
Currency	7	473	569	96	20%
Totals	155	21,297	27,248	5,951	28%

Source: ASX

ETF GROWTH BY SECTOR



ETF Market Summary

By Sector Group

WE HAVE DIVIDED THE AUSTRALIAN ETF UNIVERSE INTO 8 BROAD SECTOR GROUPINGS:

Sector	Types of ETFs
Australian shares - broad market	ETFs which track the broad Australian market
Australian shares - sectors	ETFs which track sectors within the Australian market (e.g. Property, Financials or Resources)
Australian shares - strategies	ETFs which only include some Australian stocks rather than the entire index. Stocks are selected according to certain rules-based factors (e.g. dividend yield, or research rating)
Global shares - broad market	ETFs which track the broad international markets
Global shares - sectors	ETFs which track sectors across multiple countries in stock markets (e.g. Healthcare, Banks, Telecommunications)
Fixed income & cash	ETFs which track fixed interest (bonds) and cash
Currency	ETFs which track currencies
Commodity	ETFs which track commodities (e.g. gold, oil)

Each ETF sector saw double digit percentage growth in FUM over the last year, with the largest inflows coming into global sector ETFs, fixed income and cash ETFs, and strategy based Australian share ETFs.

Over five years the average broad market global share ETF returned 13%, compared to a 8% return from the average Australian share ETF. The underperformance of the local market since 2010 has led many Australian investors to look at adding global ETFs into their portfolios. Australian ETFs have seen a shift of funds into strategy based ETFs to chase higher returns. The global sector ETFs have had a great year of new product growth as several new ETFs provided investors with increased options and more unique opportunities.

Investors also continued to diversify their portfolios into fixed income ETFs, as worldwide volatility in share markets remained a theme with multiple unexpected political events occurring in 2016 including Brexit and the US Presidential Election. Notwithstanding, most bond ETFs had a lacklustre year of performance compared to the recent past, returning 1% to 3% over the year compared to much larger share market returns.

Large Australian shares had a very strong year with many ETFs rising over 20% over the 12 months.

The global sector ETFs had the highest number of new ETFs, accounting for 11 out of 27 new ETFs to increase the total available from 5 to 16. Together with global broad market shares gaining 9 new ETFs, these two categories offer a great range of overseas markets. Global sectors grew to over $1 billion in ETF assets.

The Australian Dollar moved within a small band over the last year, leading to the difference between hedged and unhedged versions of ETFs to be relatively minor. Unhedged gold ETF (GOLD)'s return of 0.9% compared to the 'Australian dollar hedged' gold ETF (QAU)'s annual return of 0.3% illustrates that the Australian dollar had limited movement against the US dollar this year. Currency exposure embedded in ETFs remains important to understand as 'hedged' ETFs typically benefit from a rising Australian dollar whereas 'unhedged' ETFs have better relative performance when the Australian dollar falls. All of the Stockspot model portfolio ETFs are currently unhedged ETFs, which has helped our portfolio performance over the past 3 years as the Australian dollar has fallen.

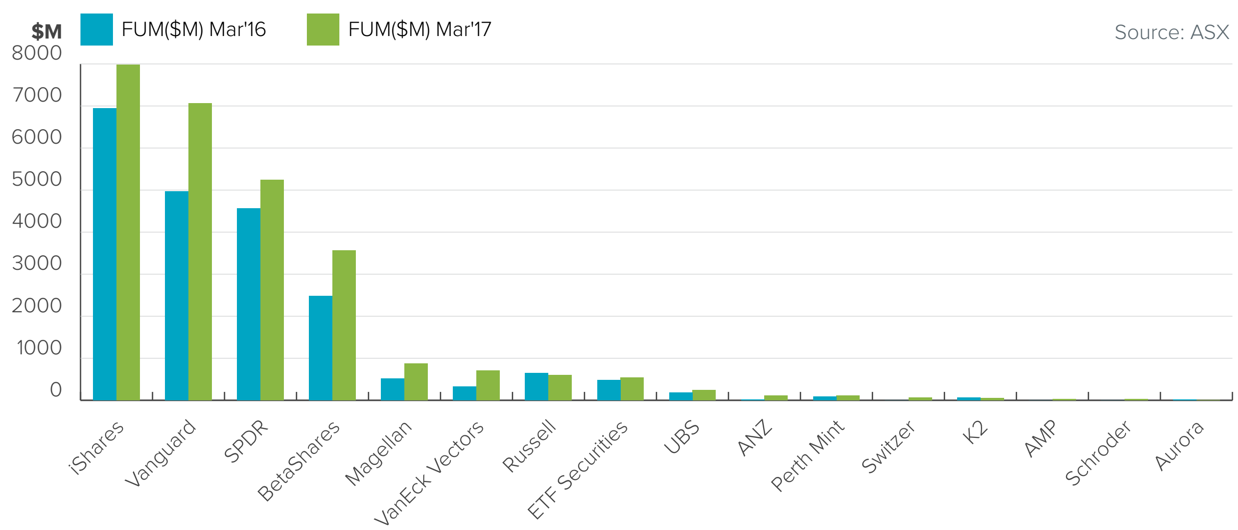
ETFs now cover all major assets classes with the launch of three ETFs tracking infrastructure in 2016. The trend towards existing fund managers launching new 'active' ETFs has also continued with AMP and others launching new actively managed products in 2016.

ETF Market Summary

Issuer	FUM($M) Mar'16	FUM($M) Mar'17	Annual change in FUM ($M)	Annual change in FUM%
iShares	6,942	7,976	1,034	15%
Vanguard	4,973	7,067	2,094	42%
SPDR	4,565	5,247	683	15%
BetaShares	2,477	3,560	1,084	44%
Magellan	512	873	361	71%
VanEck Vectors	325	708	383	118%
Russell	652	603	-49	-7%
ETF Securities	478	546	68	14%
UBS	186	244	59	32%
ANZ	23	118	95	407%
Perth Mint	88	116	28	32%
Switzer	-	60	60	n/a
K2	63	54	-9	-14%
AMP	-	35	35	n/a
Schroders	-	28	28	n/a
Aurora	14	11	-3	-21%
Totals	21,297	27,248	5,951	28%

Source: ASX

ETF GROWTH BY ISSUER



ETF Market Summary

By ETF Issuer

The majority of ETF funds under management are managed by the largest four competitors; with iShares, Vanguard, SPDR and BetaShares accounting for 88% of funds in order of size. These issuers are the businesses that build and 'issue' the ETFs to the public. Several smaller issuers have continued rapid growth, leading to the dominance of the three largest issuers declining 3% to 74% of the total FUM.

iShares (owned by BlackRock) is still the leading issuer in Australia with $1,034 million in new FUM coming into their globally focused ETFs in the last year. It launched six new ETFs, providing an global and Australian focused or Australian Dollar hedged version for three market segments. They track the iShares Core MSCI World All Cap (IWLD and IHWL), a Multifactor index (AUMF and WDMF) and the others have a minimum volatility focus (MVOL and WVOL).

Five iShares ETFs also saw fee reductions, largely for those related to the US share market. This was likely in response to increased competition and Vanguard's dominance. The iShares Core S&P 500 (IVV) now has the lowest fees available after a 0.03% reduction to 0.04% and remains the second largest ETF overall with just over a quarter of iShares' FUM. The hedged version (IHVV) also reduced fees by 0.03% to 0.10% and the same reduction for iShares Global 100 AUD Hedged (IHOO) occurred to 0.43%. The US small-cap (IJR) and mid-cap (IJH) ETFs both reduced fees by 0.05% to 0.07%.

Vanguard had another standout year, increasing FUM by 42% and with a dollar growth of almost double iShares at $2,094 million to now account for over a quarter of the market. It maintained the lowest average fees at 0.24% across its broad market exposure ETFs. In particular its Australian ETFs focused on the broad market, property, high dividends and fixed interest grew rapidly.

Fees were reduced for one ETF, the All-World ex US Shares (VEU) by 0.01% to 0.13% and one new ETF was launched to expand its local fixed income offerings, the Australian Corporate Fixed Interest Index ETF (VACF).

SPDR again saw more subdued growth in a repeat of last year, seeing a total of $683 million new FUM, a 15% increase. A large inflow of funds into its stalwart SPDR S&P/ASX 200 ETF (STW) in March 2017 had a major impact of the annual AUM growth.

SPDR didn't launch any new ETFs or have any fee changes. Its ETFs showed inflows across the fixed income, Australian shares and global sectors.

BetaShares had another year of high growth and again added the second largest amount in new FUM with $1,084 million. BetaShares have successfully focused on niche offerings, which typically have a structured element, such as gearing, and have launched the highest number of new ETFs this year. The majority of new funds again flowed into their cash ETF (AAA), US dollar ETF (USD) and their dividend focused managed fund (HVST).

Their offerings in the Global sectors group have been extended with seven new ETFs. It also launched two ETFs in collaboration with US based WisdomTree (HEUR and HJPN) and three in alliance with AMP (RENT, GLIN and DKMT), for which BetaShares provided the infrastructure to list existing managed funds on the ASX.

Magellan has become the fifth largest issuer by FUM with a 71% increase to $873 million to continue its success. Its original managed fund (MGE) has again attracted high inflows and its new ETP, an infrastructure managed fund (MICH) has also grown quickly.

Van Eck Vectors, previously known as Market Vectors, rebranded under its international name in May 2016. It had rapid growth in FUM from a low base, overtaking Russell and ETF Securities over the year. It launched two new ETFs, one focusing on dividends (FDIV) and one of the infrastructure ETFs. (IFRA)

Russell had a fall of $49 million in FUM this year to fall behind Magellan and Russell, with large outflows from its government bond (RGB) and semi-government bond (RSM) ETFs. Its corporate bond and two of its Australian strategy based ETFs gained funds under management.

EFT Securities gained FUM this year as its large GOLD ETF has remained popular despite gold trading sideways.

UBS continued steady growth with an increase of $59 million across its strategy and ethically focused ETFs. The fees for Australian 'Quality' (ETF) and dividend yield strategy (DIV) were reduced from 0.70% to 0.30% after the fund changed its tracking index to the MorningStar Australa Moat Focus Index.

ANZ showed very rapid growth from a low base by gaining four times the amount of its initial FUM over the year. It reduced for its US dollar ETF (ZUSD) from 0.45% to 0.30% and it also reduced fees for its Reminbi (ZCNH) ETF from 0.57% to 0.30%. Its large cap Australian shares ETF (ZOZI) also proved popular and a new ETF covering European Shares was launched (ESTX).

Perth Mint and **Aurora** only have one ETF each, with a focus on gold and a mining managed fund respectively.

Switzer listed its first managed fund ETF (SWTZ) focusing on dividend shares in February 2017 with a starting asset value of $52 million.

K2 had another decline in its FUM for its two managed funds.

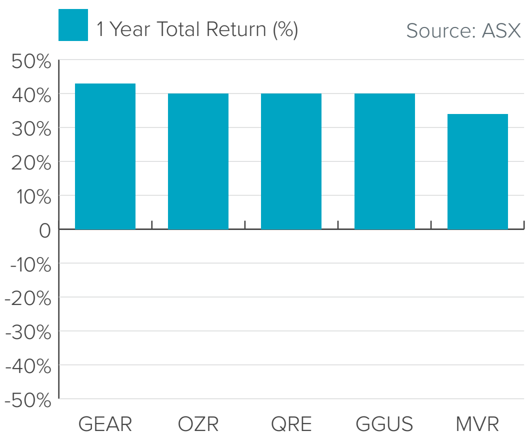
AMP issued its first managed fund ETPs together with BetaShares focusing on global infrastructure (GLIN) and property securities (RENT). It also launched an active ETF (DMKT) global hedge fund product.

Schroders listed its first managed fund ETF (GROW) in 2016.

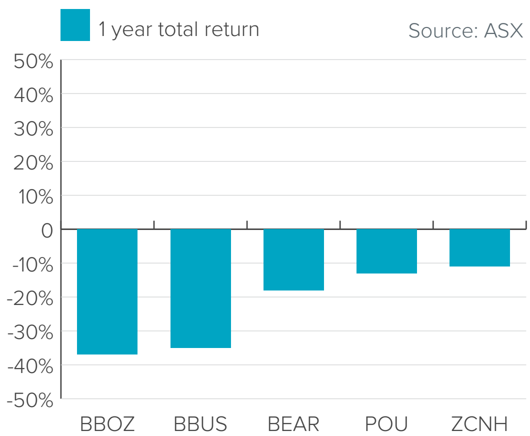
ETF Market Summary

ASX Code	ETF Name	Issuer	FUM($M) Mar'17	1 Year Total Return
Positive performance				
GEAR	BetaShares Geared Australian Equity Fund (Hedge Fund)	BetaShares	57	43%
OZR	SPDR S&P/ASX 200 Resource Fund	SPDR	31	40%
GGUS	BetaShares Geared US Equity Fund Currency Hedged (Hedge Fund)	BetaShares	7	40%
QRE	BetaShares S&P/ASX 200 Resources Sector ETF	BetaShares	16	40%
MVR	VanEck Vectors Australian Resources ETF	VanEck Vectors	25	34%
Negative performance				
BBOZ	BetaShares Australian Strong Bear (Hedge Fund)	BetaShares	86	-37%
BBUS	BetaShares US Equities Strong Bear Currency Hedged (Hedge Fund)	BetaShares	53	-35%
BEAR	BetaShares Australian Equities Bear (Hedge Fund)	BetaShares	57	-18%
POU	BetaShares British Pound ETF	BetaShares	38	-13%
ZCNH	ANZ / ETFS Physical Renminbi ETF	ANZ	0	-11%

Source: ASX



Top 5 ETFs by returns



Worst 5 ETFs by returns

ETF Market Summary

POSITIVE PERFORMANCE

The stock market's recent strength is evidenced by the geared version of ETFs dominating the top and bottom performers this year. Geared ETFs are structured to magnify returns above regular index tracking ETFs. Both GGUS and GEAR actually lost FUM despite strong performances.

The resources sector in Australia enjoyed a resurgence over the last year with three of the top five performers being resource sector focused.

The top performing funds this year highlights that markets tend to revert to their averages. GEAR, OZR and QRE which were top funds this year were amongst the five worst performers in last year's report, highlighting how being contrarian can be helpful when investing in broad asset classes.

NEGATIVE PERFORMANCE

The positive performance from Australian and US share markets have seen negative results of 'bear' hedge funds. These type of funds provide an inverse payoff to the markets and have taken three of the bottom five places in terms of performance.

BEAR also increased its fee from 1.19% to 1.38% in March 2017

The Pound has been negatively affected by the Brexit vote outcome and its ongoing political processes. The Chinese currency also experienced a negative year as its economy grew relatively slower than previous years and high capital outflows from the country continued. There were fears of a 'trade war' being realised after the election of Donald Trump.

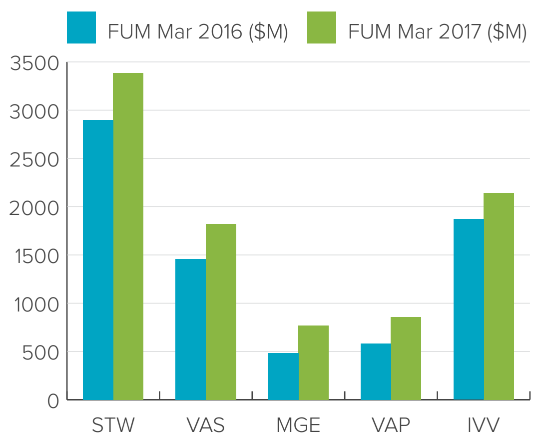
ETF Market Summary

By Funds Under Management (FUM)

ASX Code	ETF Name	Issuer	FUM($M) Mar'16	FUM($M) Mar'17	Annual change in FUM ($M)	1 Year Total Return
Increases in FUM						
STW	SPDR S&P/ASX 200	SPDR	2,900	3,385	485	20%
VAS	Vanguard Australian Shares Index ETF	Vanguard	1,456	1,819	363	20%
MGE	Magellan Global Equities Fund (Managed Fund)	Magellan	485	768	284	10%
VAP	Vanguard Australian Property Securities Index ETF	Vanguard	582	858	276	7%
IVV	iShares S&P 500 ETF	iShares	1,870	2,143	273	17%
Decreases in FUM						
RGB	Russell Australian Government Bond ETF	Russell	138	58	-80	2%
IEU	iShares S&P Europe ETF	iShares	591	522	-69	9%
RSM	Russell Australian Semi-Government Bond ETF	Russell	122	61	-61	3%
IHOO	iShares Global 100 AUD Hedged ETF	iShares	81	28	-53	21%
SLF	SPDR S&P/ASX 200 Listed Property Fund	SPDR	623	586	-37	6%

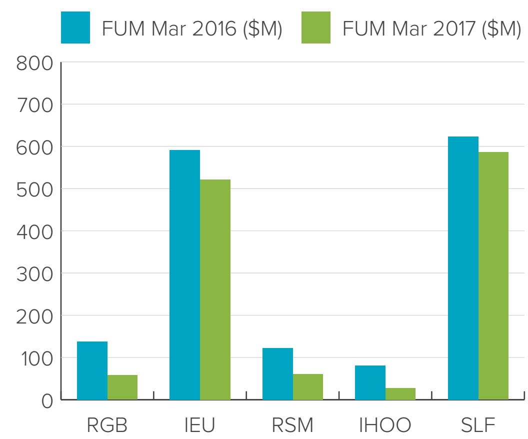
Source: ASX

ETF GROWTH BY FUM



Source: ASX

Top 5 by FUM growth



Source: ASX

Worst 5 by FUM growth

ETF Market Summary

By Funds Under Management (FUM)

INCREASES IN FUM

The highest fund inflows tended to remain with large, broad market ETFs.

This year STW forged ahead of VAS with a large inflow of funds in March 2017. This ETF has attracted institutional investors which can rapidly cause large inflows and outflows of funds.

Magellan's managed fund also continued its success and has set a benchmark for the number of other more traditional fund managers also offering exchange traded managed funds. VAP is another repeat in this category as the Australian property sector remains popular.

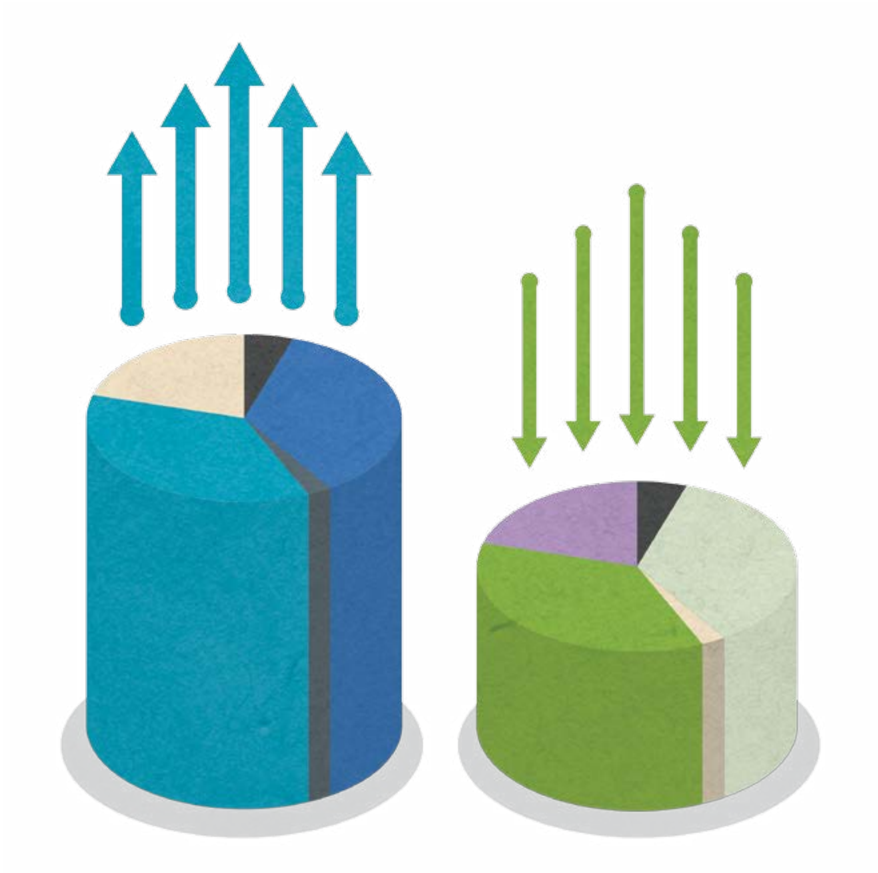
DECREASES IN FUM

The highest ETF outflows were comparatively small.

Whilst the returns for Australian government bonds were still positive, we saw a fall in demand for bonds and a rally in share ETFs as investors moved away from defensive asset classes.

The Europe focused IEU was negatively affected by falls in the Euro and ongoing fears of deflation, whilst other regions of the world performed better in the past year. It's also less attractive than its Vanguard competitor VEQ which has a 0.35% fee compared 0.60% for IEU. Relative fees is likely to have also influenced investors in SLF. As the Australian property ETF's fall in assets is in stark contrast to VAP's large inflow of funds. VAS charges 0.25% per year compared to SLF at 0.40%.

IHOO lost funds to its unhedged version IOO. Australians investing in global ETFs continue to prefer their unhedged versions in order to diversify their currency exposure. Currently all Stockspot model portfolio ETFs are unhedged.



ETF Sectors

SPOTS EVALUATION

Spots are a measure we have to developed to compare ETFs across 5 common characteristics: Fees, Slippage, Liquidity, Size and Counterparty risk. Spots are a quantitative measure and do not constitute a recommendation.

ETFs can qualify for up to 5 spots based on the following criteria:

Measure	Criteria
Fees: Total fund management fees and expenses as a percentage of average net assets, and is equivalent in calculation to the indirect cost ratio (ICR) and the management expense ratio (MER).	Less than 0.25% per annum
Slippage: Average percentage bid/ask spread during the ASX trading hours.	Less than 0.25%
Liquidity: Average daily volume on the ASX over the past calendar quarter. Volume is a measure of market making activity and the trading environment. It may not reflect liquidity in the underlying securities.	More than AU$500,000
Size: Funds Under Management (FUM)	More than AU$25M
Counterparty risk: Synthetic ETFs and Structured Products use derivatives to achieve their investment objective. If you invest in these you are subject to the risk that the counterparty to the derivative may fail to meet some or all of their obligations. Some ETFs can also 'lend out' the underlying securities to earn a fee. It is also known as custody risk. This is the risk that of losing money because the business holding the investments is troubled, rather than investments falling in value. Securities lending can boost investor returns but also increases counterparty risk. We prefer ETFs that are exposed to very low or zero counterparty risk.	Investors are exposed to counterparty risk of less than 10% of the fund's net asset value


%
BOND

ASX code	ETF Name	Issuer	MER (p.a) 2017	FUM ($M) Mar'16	FUM ($M) Mar'17	Change in FUM ($M)	Traded value in Mar'17	% Spread	Historical Distribution Yield	1 Year Total Return	Stockspot Rating
Australian Broad Based											
IOZ	iShares Core S&P/ASX 200 ETF	iShares	0.15%	405	608	203	72,346,270	0.08%	6%	21%	●●●●●
ILC	iShares S&P/ASX 20 ETF	iShares	0.24%	299	339	40	18,020,499	0.08%	6%	22%	●●●●●
ISO	iShares S&P/ASX Small Ordinaries ETF	iShares	0.55%	33	64	31	13,733,513	0.33%	2%	13%	●●○○○
KSM	K2 Australian Small Cap Fund (Hedge Fund)	K2	2.00%	23	20	-2	147,960	2.34%	0%	10%	●○○○○
MVE	VanEck Vectors S&P/ASX MidCap 50 ETF	VanEck Vectors	0.49%	-	28	28	4,201,850	0.21%	1%	N/A	●●●○○
MVS	VanEck Vectors Small Companies Masters ETF	VanEck Vectors	0.49%	38	55	18	7,538,179	0.28%	3%	15%	●●○○○
MVW	VanEck Vectors Australian Equal Weight ETF	VanEck Vectors	0.35%	97	211	114	21,351,885	0.09%	2%	19%	●●●●○
QOZ	BetaShares FTSE RAFI Australia 200 ETF	BetaShares	0.30%	84	201	116	19,177,381	0.12%	5%	27%	●●●●○
SFY	SPDR S&P/ASX 50	SPDR	0.29%	435	456	20	21,087,556	0.06%	5%	21%	●●●●○
SSO	SPDR S&P/ASX Small Ordinaries Fund	SPDR	0.50%	8	12	4	390,268	0.19%	3%	14%	●●○○○
STW	SPDR S&P/ASX 200	SPDR	0.19%	2,900	3,385	485	837,441,572	0.05%	4%	20%	●●●●●
UBA	UBS IQ MSCI Australian Ethical ETF	UBS	0.17%	131	162	31	193,761	0.16%	4%	22%	●●●●○
VAS	Vanguard Australian Shares Index ETF	Vanguard	0.14%	1,456	1,819	363	116,363,679	0.06%	4%	20%	●●●●●
VLC	Vanguard MSCI Australian Large Companies Index ETF	Vanguard	0.20%	58	73	15	3,076,842	0.07%	4%	22%	●●●●○

ASX code	ETF Name	Issuer	MER (p.a) 2017	FUM ($M) Mar'16	FUM ($M) Mar'17	Change in FUM ($M)	Traded value in Mar'17	% Spread	Historical Distribution Yield	1 Year Total Return	Stockspot Rating
VSO	Vanguard MSCI Australian Small Companies Index ETF	Vanguard	0.30%	67	85	18	6,181,106	0.16%	3%	15%	●●●○○
ZOZI	ANZ / ETFS S&P/ ASX 100 ETF	ANZ	0.24%	3	32	29	3,760,103	0.20%	3%	23%	●●●●○
Averages			0.41%					0.28%	3%	19%	●●●●○
Totals				6,036	7,550	1,514	1,145,012,424				

Source: ASX

This group of ETFs track broad Australian share market indices such as the S&P/ASX300, including small or mid-cap indices.

The average 1 year return was 19% after fees, a major increase from last year, and the included distribution yield rate of 3.4% remained relatively similar. All ETF returns were double digits and only the hedge fund KSM provided no yield. Many of these ETFs also distribute franking credits to investors, which can be an additional benefit to Australian taxpayers.

Australian shares ETFs added $1,514M of FUM for the year with 31% of that money finding its way into either SPDR's STW and 24% into Vanguard's VAS. Together with iShares' IOZ they accounted for 69% of all inflows, as investors continued to gravitate towards the largest ETFs with high trading volumes and low fees.

The top heavy nature of Australian equity market can be seen through the small differences in returns between STW tracking the S&P/ASX200 and VAS tracking the S&P/ASX300. Despite including another hundred companies by market capitalisation, VAS' monthly returns tend to be within 0.5% of STW's.

Investors are exposed to significant industry and single-stock tilts when investing in broad Australian equity market; with the market concentrated in financials (~39%) and materials (~16%). Information technology accounts for only 1%, which is very low compared to 22% in the USA iShares Core S&P 500 (IVV). This reveals that even an index funds can have concentration in a few sectors.

MVE has now been reallocated this to sector after changing its tracking index from the MVIS Australia Junior Energy & Mining Index to the S&P/ASX Midcap 50 Index in July 2016 so has not been considered as a new ETF. Given that sectors tend to come in and out of fashion, it is unfortunate that VanEck Vectors abandoned the Midcap Mining ETF close to the low in resource shares and before their large recovery over the past 12 months.

We give four ETFs the full 5 spots (IOZ, ILC, STW, VAS) with the majority receiving 3 or 4 spots.

VAS is our current Stockspot portfolio inclusion from this asset group.

Stockspot themes also include the option of SFY for those after a large-cap focus and VSO for those who prefer to tilt their portfolios towards small-cap shares.

In an interesting development, STW is now being used by some institutions as part of an asset allocation strategy or as a large, liquid way to quickly access market exposure. This is much more common in the US and if the trend continues in Australia we could see ETF growth accelerate generally.

ASX code	ETF Name	Issuer	MER (p.a) 2017	FUM ($M) Mar'16	FUM ($M) Mar'17	Change in FUM ($M)	Traded value in Mar'17	% Spread	Historical Distribution Yield	1 Year Total Return	Stockspot Rating
Australian Sector											
MVA	VanEck Vectors Australian Property ETF	VanEck Vectors	0.35%	52	58	6	4,153,380	0.16%	5%	9%	●●●○○
MVB	VanEck Vectors Australian Bank ETF	VanEck Vectors	0.28%	18	28	10	2,299,232	0.07%	5%	33%	●●●○○
MVR	VanEck Vectors Australian Resources ETF	VanEck Vectors	0.35%	3	25	22	2,239,677	0.11%	2%	34%	●●●○○
OZF	SPDR S&P/ASX 200 Financials ex A-REITs Fund	SPDR	0.40%	48	66	18	4,467,182	0.09%	5%	28%	●●●○○
OZR	SPDR S&P/ASX 200 Resource Fund	SPDR	0.40%	19	31	12	4,658,292	0.18%	2%	40%	●●●○○
QFN	BetaShares S&P/ASX 200 Financials Sector ETF	BetaShares	0.39%	20	18	-2	3,083,028	0.13%	5%	26%	●●○○○
QRE	BetaShares S&P/ASX 200 Resources Sector ETF	BetaShares	0.39%	5	16	11	2,516,291	0.28%	1%	40%	●○○○○
SLF	SPDR S&P/ ASX 200 Listed Property Fund	SPDR	0.40%	623	586	-37	23,342,897	0.20%	4%	6%	●●●●○
VAP	Vanguard Australian Property Securities Index ETF	Vanguard	0.23%	582	858	276	43,654,271	0.13%	5%	7%	●●●●●
Averages			0.35%					0.15%	4%	25%	●●●○○
Totals				1,370	1,687	317	90,414,250				

Source: ASX

ETF Sectors

This group of ETFs track the movements of various sectors of the Australian share market. At this stage there are sector ETFs covering the resources, financials and property sectors.

Performance between sector ETFs varied greatly over the year with property ETFs maintaining their returns (6% to 9%) while financials, resources and mining ETFs had exceptional returns with 26% to 40%. The average total return of 25% is the highest amongst all sectors and dividend yields of 4% is also high. The resource sector has gradually been recovering after a period of slowdown as the mining boom has faded and it has relatively low dividends compared to its returns.

Australian sector ETFs added $317M of FUM for the year with 87% of that money finding its way into the Vanguard property ETFs (VAP). The trend of the SPDR property ETF (SLF) losing market share to Vanguard with its lower-fee option (VAP), 0.40% compared to 0.25% also continued. This sector received the majority of fund inflows, despite having the lowest returns of the group.

Financials had an excellent year with all returns over 26% and dividends of at least 5%. Despite this the inflows of funds was relatively slow compared to property and resources ETFs.

All three of these sectors already account for a significant portion of the Australian index generally. They are also relatively concentrated themselves, with the largest few stocks accounting for over half the index.

- Financials: The ‘big four’ banks typically represent around 73% of the S&P/ASX 200 Financials ex A-REIT Index.
- Property: The largest 5 REITs make up nearly 62% of the S&P/ASX200 Property Index, with Scentre Group, Westfield Corp, Goodman Group, Stockland and Dexus dominating this index.
- Resources: BHP, Rio Tinto, Woodside Petroleum make up approximately 50% of the S&P/ASX200 Resources Index, with BHP alone still contributing around 30% of this index.

Stockspot themes also includes the option of VAP which enjoyed the fastest FUM growth this year and has earned five spots.

ASX code	ETF Name	Issuer	MER (p.a) 2017	FUM ($M) Mar'16	FUM ($M) Mar'17	Change in FUM ($M)	Traded value in Mar'17	% Spread	Historical Distribution Yield	1 Year Total Return	Stockspot Rating
Australian Strategy											
AOD	Aurora Dividend Income Trust	Aurora	0.97%	14	11	-3	137,091	1.31%	6%	2%	●○○○○
AUMF	iShares Edge MSCI Australia Multifactor ETF	iShares	0.30%	-	6	6	177,862	0.17%	0%	N/A	●●○○○
AUST	BetaShares Managed Risk Australian Share Fund (Managed Fund)	BetaShares	0.39%	7	32	25	2,108,886	0.13%	3%	12%	●●●○○
BBOZ	BetaShares Australian Strong Bear (Hedge Fund)	BetaShares	1.19%	77	86	10	50,406,690	0.12%	0%	-37%	●●●●○
BEAR	BetaShares Australian Equities Bear (Hedge Fund)	BetaShares	1.38%	62	57	-5	16,017,317	0.11%	1%	-18%	●●●●○
DIV	UBS IQ Morningstar Australia Dividend Yield ETF	UBS	0.30%	23	27	4	225,935	0.26%	4%	14%	●●○○○
ETF	UBS IQ Morningstar Australia Quality ETF	UBS	0.30%	7	19	12	7,406,441	0.24%	5%	8%	●●○○○
EX20	BetaShares Australian Ex-20 Portfolio Diversifier ETF	BetaShares	0.20%	-	8	8	1,811,600	0.13%	0%	N/A	●●●○○
FDIV	VanEck Vectors S&P/ ASX Franked Dividend ETF	VanEck Vectors	0.35%	-	4	4	151,233	0.17%	3%	N/A	●●○○○
GEAR	BetaShares Geared Australian Equity Fund (Hedge Fund)	BetaShares	0.80%	71	57	-14	29,200,654	0.13%	6%	43%	●●●○○
HVST	BetaShares Australian Dividend Harvester Fund (Managed Fund)	BetaShares	0.65%	157	427	270	51,218,446	0.08%	9%	9%	●●●●○
IHD	iShares S&P/ASX High Dividend Yield ETF	iShares	0.30%	231	257	26	10,566,787	0.11%	5%	20%	●●●○○

ASX code	ETF Name	Issuer	MER (p.a) 2017	FUM ($M) Mar'16	FUM ($M) Mar'17	Change in FUM ($M)	Traded value in Mar'17	% Spread	Historical Distribution Yield	1 Year Total Return	Stockspot Rating
MVOL	iShares Edge MSCI Australia Minimum Volatility ETF	iShares	0.30%	-	6	6	38,229	0.17%	0%	N/A	●●○○○
RARI	Russell Australian Responsible Investment ETF	Russell	0.45%	18	61	42	1,167,177	0.38%	5%	19%	●●○○○
RDV	Russell High Dividend Australian Shares ETF	Russell	0.34%	271	287	16	7,997,789	0.07%	4%	22%	●●●○○
RVL	Russell Australian Value ETF	Russell	0.34%	22	14	-8	90,500	0.08%	4%	25%	●●○○○
SWTZ	Switzer Dividend Growth Fund (Managed Fund)	Switzer	0.89%	-	60	60	6,113,311	0.45%	0%	N/A	●●○○○
SYI	SPDR MSCI Australia Select High Dividend Yield Fund	SPDR	0.35%	142	175	33	17,541,137	0.07%	5%	24%	●●●●○
VHY	Vanguard Australian Shares High Yield ETF	Vanguard	0.25%	620	780	160	44,552,052	0.06%	6%	22%	●●●●○
YMAX	BetaShares Australia Top20 Equity Yield Max Fund	BetaShares	0.59%	317	377	61	20,974,247	0.19%	9%	17%	●●●●○
ZYAU	ANZ / ETFS S&P/ ASX 300 High Yield Plus ETF	ANZ	0.35%	4	16	12	1,627,091	0.23%	3%	25%	●●○○○
Averages			0.52%					0.22%	4%	13%	●●●○○
Totals				2,042	2,767	725	269,530,475				

Source: ASX

These ETFs only include some Australian stocks rather than the entire index. In Strategy based ETFs, stocks are selected according to certain rules-based factors like dividend yield or research rating. This group also includes Hedge Funds - which have gearing and Managed Funds - which include 'active' funds management and typically have higher fees. Some of the strategy ETFs also seek to address concentration issues within the broad market indices by limiting sector and stock exposure limits. For instance Vanguard's VHY ETF restricts any one industry to 40% and one company to 10% of the index.

High yield and dividend themed ETFs captured most of the new flows into this group again as the theme remains very popular in Australia. BetaShares' HVST managed fund more than doubled its FUM by receiving almost $270 million in new funds. The Vanguard (VHY) is still the largest ETF by far with around 28% of the FUM, a slight decrease from 30% last year as investor preferences diverge.

The market rally saw a reverse of last year's returns for several ETF products due to their structures. BetaShares Australian Equities Bear (Hedge Fund) and Geared Australian Equity Fund (Hedge Fund) swapped places for the best and worst performances. A bear hedge fund is designed to provide higher returns as the market falls.

Distributions were generally on par with the other Australian ETFs this year, with an average of 3.7%. The group had both the highest distributions of over 8% due to dividend focused ETFs and synthetic yield products like HVST and YMAX, as well as zero distributions from multiple products such as the hedge fund ETFs. This group provided generally equivalent returns to Australian broad based and sector ETFs this year, but tended to have higher fees.

iShares launched two new ETFs, with AUMF focusing on 'growth factors', including taking measures for quality, value, size and momentum in account when selecting stocks and MVOL that aims to reduce exposure to market volatility for lower losses during downturns. BetaShares launched one new ETF (EX20) that excludes the twenty largest companies in Australia. Switzer issued their first managed fund on the ASX targeting 30 to 50 high dividend stocks.

Stockspot continues to offer RARI, a socially responsible ETF as a theme option for clients. We generally avoid smart beta and strategy based ETFs because their fees tend to be higher and we do not believe they will improve on results from strategic asset allocation using more vanilla ETFs over the long run.

ASX code	ETF Name	Issuer	MER (%p.a)	FUM ($M) Mar'16	FUM ($M) Mar'17	Change in FUM ($M)	Traded value in Mar'16	% Spread	Historical Distribution Yield	1 Year Total Return	Stockspot Rating
Currency											
AUDS	BetaShares Strong Australian Dollar Fund (Hedge Fund)	BetaShares	1.19%	-	2	2	74,195	0.25%	0%	N/A	●○○○○
EEU	BetaShares Euro ETF	BetaShares	0.45%	3	4	1	146,659	0.17%	0%	-6%	●●○○○
POU	BetaShares British Pound ETF	BetaShares	0.45%	7	38	31	5,365,408	0.11%	0%	-13%	●●●○○
USD	BetaShares U.S Dollar ETF	BetaShares	0.45%	459	512	54	47,914,414	0.09%	0%	0%	●●●●○
YANK	BetaShares Strong US Dollar Fund (Hedge Fund)	BetaShares	1.38%	-	1	1	2,396,670	0.25%	0%	N/A	●●○○○
ZCNH	ANZ / ETFS Physical Renminbi ETF	ANZ	0.30%	1	0.4	-0.5	24,911	0.24%	0%	-11%	●●○○○
ZUSD	ANZ / ETFS Physical US Dollar ETF	ANZ	0.30%	3	10	7	2,013,267	0.18%	0%	-2%	●●○○○
Averages			0.65%					0.18%	0%	-6%	●●○○○
Totals				473	569	96	57,935,523				

Source: ASX

These ETFs track the performance of Australian Dollar relative to selected currencies for investors who want direct access to currency performance without holding physical currency.

BetaShares' USD ETF still holds the vast majority of FUM (90%) in the sector. This was the only sector to provide all negative returns, with the impact of Brexit on the Pound and Euro being clearly visible, as well as China's devaluation of its currency.

BetaShares also issued two new hedge fund products for the Australian Dollar (AUDS) and US Dollar (YANK) which involve gearing.

Global Shares (Broad Market)

ASX code	ETF Name	Issuer	MER (%p.a)	FUM ($M) Mar'16	FUM ($M) Mar'17	Change in FUM ($M)	Traded value in Mar'16	% Spread	Historical Distribution Yield	1 Year Total Return	Stockspot Rating
International Broad Based											
ESTX	ANZ ETFS EURO STOXX 50 ETF	ANZ	0.35%	-	3	3	441,408	0.25%	0%	N/A	●○○○○
HEUR	BetaShares WisdomTree Europe ETF - Currency Hedged	BetaShares	0.51%	-	18	18	9,543,712	0.21%	1%	N/A	●●○○○
IEU	iShares S&P Europe ETF	iShares	0.60%	591	522	-69	23,381,642	0.20%	2%	9%	●●●●○
IHOO	iShares Global 100 AUD Hedged ETF	iShares	0.43%	81	28	-53	2,682,647	0.79%	0%	21%	●●○○○
IHVV	iShares S&P 500 AUD Hedged ETF	iShares	0.10%	42	108	65	8,737,129	0.35%	1%	18%	●●●○○
IHWL	iShares Core MSCI World All Cap AUD Hedged ETF	iShares	0.19%	-	4	4	499,978	0.59%	0%	N/A	●●○○○
IJH	iShares S&P Midcap ETF	iShares	0.07%	82	115	33	11,614,085	0.29%	1%	21%	●●●○○
IJP	iShares MSCI Japan ETF	iShares	0.48%	204	169	-35	35,242,377	0.31%	2%	14%	●●●○○
IJR	iShares S&P Small-Cap ETF	iShares	0.07%	44	77	33	4,161,063	0.58%	1%	25%	●●●○○
IOO	iShares S&P Global 100 ETF	iShares	0.40%	1,000	1,121	121	34,870,033	0.17%	2%	16%	●●●●○
IRU	iShares Russell 2000 ETF	iShares	0.20%	47	60	13	4,834,553	0.24%	1%	26%	●●●●○
IVE	iShares MSCI EAFE ETF	iShares	0.33%	261	247	-15	10,010,580	0.26%	2%	11%	●●○○○
IVV	iShares S&P 500 ETF	iShares	0.04%	1,870	2,143	273	93,233,833	0.06%	2%	17%	●●●●●
IWLD	iShares Core MSCI World All Cap ETF	iShares	0.16%	-	6	6	523,749	0.57%	1%	N/A	●●○○○
KII	K2 Global Equities Fund (Hedge Fund)	K2	2.05%	40	33	-7	2,064,946	0.97%	0%	9%	●●○○○
MGE	Magellan Global Equities Fund (Managed Fund)	Magellan	1.35%	485	768	284	46,119,956	0.41%	2%	10%	●●●○○
MHG	Magellan Global Equities Fund Currency Hedged (Managed Fund)	Magellan	1.35%	27	46	19	3,182,864	0.55%	2%	12%	●●○○○
MOAT	VanEck Vectors Morningstar Wide Moat ETF	VanEck Vectors	0.49%	3	34	31	8,468,447	0.21%	1%	24%	●●●○○

Global Shares (Broad Market)

ASX code	ETF Name	Issuer	MER (%p.a)	FUM ($M) Mar'16	FUM ($M) Mar'17	Change in FUM ($M)	Traded value in Mar'16	% Spread	Historical Distribution Yield	1 Year Total Return	Stockspot Rating
NDQ	BetaShares NASDAQ 100 ETF	BetaShares	0.38%	46	88	42	16,797,325	0.16%	1%	22%	●●●●○
QMIX	SPDR MSCI World Quality Mix Fund	SPDR	0.40%	4	6	2	138,419	0.31%	3%	12%	●○○○○
QUAL	VanEck Vectors MSCI World Ex-Australia Quality ETF	VanEck Vectors	0.40%	91	184	93	9,920,366	0.28%	2%	12%	●●○○○
QUS	BetaShares FTSE RAFI US 1000 ETF	BetaShares	0.40%	16	24	8	2,402,871	0.26%	3%	17%	●○○○○
SPY	SPDR S&P 500 ETF Trust	SPDR	0.09%	15	19	4	2,445,358	0.29%	2%	15%	●●○○○
UBE	UBS IQ MSCI Europe Ethical ETF	UBS	0.40%	7	7	0	133,115	0.36%	3%	10%	●○○○○
UBJ	UBS IQ MSCI Japan Ethical ETF	UBS	0.40%	3	3	0	294,735	0.30%	2%	17%	●○○○○
UBU	UBS IQ MSCI USA Ethical ETF	UBS	0.20%	3	6	3	270,893	0.25%	1%	17%	●●○○○
UBW	UBS IQ MSCI World ex Australia Ethical ETF	UBS	0.35%	12	19	7	2,307,077	0.29%	2%	14%	●○○○○
VEQ	Vanguard FTSE Europe Shares ETF	Vanguard	0.35%	6	64	59	3,410,071	0.71%	3%	8%	●●○○○
VEU	Vanguard All-World ex US Shares Index ETF	Vanguard	0.13%	602	771	168	34,385,216	0.22%	2%	13%	●●●●●
VGAD	Vanguard MSCI Index International Shares (Hedged) ETF	Vanguard	0.21%	87	203	116	17,745,378	0.12%	1%	19%	●●●●●
VGS	Vanguard MSCI Index International Shares ETF	Vanguard	0.18%	190	414	224	35,007,937	0.14%	4%	15%	●●●●●
VTS	Vanguard US Total Market Shares Index ETF	Vanguard	0.05%	781	958	177	43,474,763	0.11%	2%	18%	●●●●●
WRLD	BetaShares Managed Risk Global Share Fund (Managed Fund)	BetaShares	0.39%	2	27	25	3,011,345	0.25%	1%	10%	●●●○○

Global Shares (Broad Market)

ASX code	ETF Name	Issuer	MER (%p.a)	FUM ($M) Mar'16	FUM ($M) Mar'17	Change in FUM ($M)	Traded value in Mar'16	% Spread	Historical Distribution Yield	1 Year Total Return	Stockspot Rating
WXHG	SPDR S&P World ex Australian (Hedged) Fund	SPDR	0.35%	57	74	17	3,461,456	0.19%	3%	18%	●●●○○
WXOZ	SPDR S&P World ex Australian Fund	SPDR	0.30%	120	147	27	4,597,239	0.20%	3%	15%	●●●○○
CETF	VanEck Vectors ChinaAMC A-Share ETF	VanEck Vectors	0.72%	2	2	0	143,725	0.53%	1%	3%	●○○○○
HJPN	BetaShares WisdomTree Japan ETF - Currency Hedged	BetaShares	0.51%	-	25	25	6,593,161	0.22%	1%	N/A	●●○○○
IAA	iShares S&P Asia 50 ETF	iShares	0.50%	253	258	5	10,431,440	0.31%	2%	24%	●●○○○
IHK	iShares MSCI Hong Kong ETF	iShares	0.48%	16	13	-2	623,819	0.51%	2%	17%	●○○○○
IKO	iShares MSCI South Korea Capped Index ETF	iShares	0.62%	16	36	20	5,043,577	0.41%	1%	19%	●●○○○
ISG	iShares MSCI Singapore ETF	iShares	0.48%	7	8	1	1,289,437	0.54%	3%	9%	●○○○○
ITW	iShares MSCI Taiwan ETF	iShares	0.62%	41	63	22	2,984,614	0.43%	2%	23%	●●○○○
IZZ	iShares FTSE China Large-Cap ETF	iShares	0.74%	75	67	-8	7,735,760	0.46%	2%	17%	●●○○○
UBP	UBS IQ MSCI Asia APEX 50 Ethical ETF	UBS	0.45%	1	1	0	66,240	0.29%	2%	27%	●○○○○
VAE	Vanguard FTSE Asia Ex-Japan Shares Index ETF	Vanguard	0.40%	22	26	4	3,818,031	0.67%	2%	18%	●●○○○
IBK	iShares MSCI BRIC ETF	iShares	0.68%	33	26	-7	683,448	0.64%	1%	24%	●●○○○
IEM	iShares MSCI Emerging Markets ETF	iShares	0.68%	339	435	95	20,793,130	0.22%	1%	17%	●●●●○
VGE	Vanguard FTSE Emerging Markets Shares ETF	Vanguard	0.48%	47	80	32	5,595,797	0.42%	2%	17%	●●○○○
WEMG	SPDR S&P Emerging Markets Fund	SPDR	0.65%	6	13	6	517,107	0.27%	2%	17%	●○○○○

ASX code	ETF Name	Issuer	MER (%p.a)	FUM ($M) Mar'16	FUM ($M) Mar'17	Change in FUM ($M)	Traded value in Mar'16	% Spread	Historical Distribution Yield	1 Year Total Return	Stockspot Rating
BBUS	BetaShares US Equities Strong Bear Currency Hedged (Hedge Fund)	BetaShares	1.19%	24	53	29	15,302,766	0.21%	0%	-35%	●●●○○
DMKT	AMP Capital Dynamic Markets Fund (Hedge Fund)	AMP	0.48%	-	15	15	875,588	0.63%	2%	N/A	●○○○○
GGUS	BetaShares Geared US Equity Fund Currency Hedged (Hedge Fund)	BetaShares	0.74%	8	7	-1	6,450,995	0.16%	1%	40%	●○○○○
GROW	Schroder Real Return Fund (Managed Fund)	Schroder	0.90%	-	28	28	1,706,838	0.55%	1%	N/A	●●○○○
UMAX	BetaShares S&P 500 Yield Maximiser Fund (Managed Fund)	BetaShares	0.59%	61	87	25	4,711,074	0.20%	5%	13%	●●●○○
WDIV	SPDR S&P Global Dividend Fund	SPDR	0.50%	73	115	42	10,125,687	0.18%	4%	11%	●●●○○
WDMF	iShares Edge MSCI World Multifactor ETF	iShares	0.35%	-	12	12	700,248	0.50%	0%	N/A	●○○○○
WVOL	iShares Edge MSCI World Minimum Volatility ETF	iShares	0.30%	-	12	12	3,795	0.50%	0%	N/A	●○○○○
ZYUS	ANZ / ETFS S&P 500 High Yield Low Volatility ETF	ANZ	0.35%	11	43	32	4,687,910	0.22%	4%	13%	●●●○○
Averages			0.48%					0.35%	2%	15%	●●○○○
Totals				7,855	9,943	2,088	590,300,752				

Source: ASX

This group of ETFs track global markets and share indices including the S&P500 and various region and country markets including Europe, Asia, Japan, Hong Kong, China, Taiwan and South Korea. It maintained its position as the largest sector and saw nine new ETFs created during the year. This group had slightly lower returns compared to Australian shares for the first time in many years.

The majority of new inflows were captured by broad US shares and global funds as investors chased the large, highly-liquid global indices with well-known constituent businesses. Global dividend yields still remain lower on average (2%) compared to Australian shares (4%).

Global Shares (Broad Market)

Single market exposure is still restricted to the USA and several Asian countries, although several new global funds and two Europe focused ETFs were launched. ANZ launched a European ETF (ESTX) focusing on the fifty largest companies in the Eurozone. BetaShares launched two new ETFs in a collaboration with New York based issuer WisdomTree, that are based on its popular products in the USA. They are the first currency hedged ETFs that focus on Europe (HEUR) and Japan (HJPN) that provide investors with more choice for exposure in those regions. Despite sluggish growth in these areas in the past few years, they are sensible opportunities for global diversification.

Over the past year, growth in Europe was comparatively slow and affected by the Euro's decline versus the Australian Dollar. There large loss of funds from iShares' Europe ETF (IEU), whilst UBS' (UBE) had a small inflow and Vanguard's (VEQ) gained FUM rapidly with the lowest fees at 0.30%.

In Asia regional ETFs, such as IAA and UBP for large-cap shares, provided better returns than any specific national market. The iShares Hong Kong (IHK), China (IZZ) and Japan (IJP) ETFs all actually lost funds despite large positive returns.

iShares Core MSCI World All Cap ETF (IWLD) provides exposure to large, medium and small companies in developed countries. It is constructed from four existing iShares ETFs - IVV for large US companies, IJR for small US companies and two of its overseas products, which include large Canadian companies and companies from developed markets excluding the USA and Canada, similar to its IVE ETF. A hedged version was launched as IHWL.

Emerging market ETFs all had returns over 16% as the past year saw greater stability, with the most unexpected political events occurring in developed economies. Several major developing countries, such as Russia and Brazil were helped by recovering commodity prices Although the BRIC (Brazil, Russia, India, China) ETF (IBK) lost funds, there was growth in others tracking emerging markets indices.

The US had another year of great growth, which continued after the presidential election results in November 2016 with the expectation of more growth orientated policies to be implemented. In general small cap stocks performed better than large stocks over the past year, with iShares's IRU focusing on 2000 small companies having the highest returns with 26% and IJR coming second with 25%. The mid-cap (IJH) also had better returns than the popular large-cap ETF (IVV). In Australia, small cap shares did the opposite - underperforming large companies this year.

The currency hedged versions of global ETFs also had slightly higher returns, indicating that the Australian Dollar gained slightly against several currencies over the year. Global shares can include Australian stocks as part of its overall holdings or exclude them to provide an extra degree of diversification and often have 'ex-Australia' in the name.

Managed funds grew from 9% to 10% of the sector, largely due to the continuing popularity of Magellan's global equities product (MGE) which has continued to gain funds despite underperforming global benchmarks. This managed fund sector also saw the entry of other established players in the industry - Schroders and AMP with their managed and hedge funds respectively. Two active ETFs were launched by iShares for investors aiming to gain from multiple factors (WDMF) and be secured against volatility (WVOL), alongside the Australian versions.

There is still a wide disparity in fees between global ETFs as the sector with the greatest number of options for investors. It has both the highest fees with K2 Global Equities Fund (Hedge Fund) (KII) at 2.05% and the lowest with the iShares Core S&P 500 (IVV) now at 0.04% per annum after a further fee reduction. It remains the second largest ETF overall with just over a quarter of iShares' FUM.

Several options for the US market now have fees below 0.10% after iShares reduced them for four more of its ETFs, following the trend of intense downward fee pressure in the US ETF market. These include the hedged version of IVV (IHVV), the Core S&P for ETFs for small-cap (IJR) and mid-cap (IJH), as well as a decline for global ETF (IHOO) to 0.43%.

NEW LISTINGS

The global sector shares had the highest number of new ETFs, with 11 out of 27 new ETFs in total to expand its offerings from 5 to 16. Together with global broad market shares gaining 9 new ETFs, they represent the growing demand for affordable access to overseas markets with 74 of 155 ETFs products available.

The offerings also focused on more niche products, as the most popular indices and most major sectors are now covered, including infrastructure in the past year. This follows international trends, as index investing is becoming more mainstream and its distinction from traditional stock picking methods becoming less clear as investors are still seeking to emulate certain active strategies.

The trend of managed funds constructing their own portfolios to list on the ASX as active ETPs has also continued with Switzer and AMP entering the market, as well as a new offering from Magellan.

The ETF issuers are partnering with other managers - BetaShares worked in partnership with AMP to create its ETPs and with American issuer WisdomTree to list two of its ETFs on the ASX.

	iShares	Vanguard	SPDR	Other Issuers
US shares	• IVV Large cap (0.04%) • IHVV Large cap hedged (0.10%) • IJH Mid-cap (0.07%) • IJR Small-cap (0.07%) • IRU (0.20%)	• VTS (0.05%)	• SPY (0.09%)	• MOAT Strategy (0.49%) • NDQ Technology (0.39%) • QUS - Large cap (0.40%) • UBU - Large/mid ethical (0.20%) • UMAX Yield max (0.59%) • ZYUS Large cap, volatility (0.35%) • BBUS Bear fund, hedged (1.19%) • GGUS Hedged, geared (0.74%)
Regional market	• IEU Europe (0.60%) • IAA Asia (0.50%)	• VEQ Europe (0.35%) • VAE Asia ex-Japan (0.40%)		• ESTX Europe (0.35%) • HEUR Europe • (0.51%) • UBE Europe (0.40%) • UBP Asia ex- Japan (0.45%)
Developed markets	• IOO (0.40%) • IHOO Hedged (0.43%) • IVE ex-US (0.33%) • IHWL Hedged (0.19%) • IWLD (0.16%) • WDMF Multifactor (0.35%) • WVOL Volatility (0.35%)	• VEU ex-US (0.13%) • VGS (0.18%) • VGAD - hedged (0.21%)	• WXHG ex- Australia (0.35%) • WXOZ hedged, ex-Australia (0.30%) • WDIV (0.50%) • QMIX (0.40%)	• QUAL ex-Australia (0.40%) • UBW ex-Australia (0.35%) • WRLD Risk (0.39%) • KII (2.05%) • MGE (1.35%) • MHG Hedged (1.35%)
Emerging markets	• IEM (0.68%) • IBK BRIC countries • (0.68%)	• VGE (0.48%)	• WEMG (0.65%)	• CETF China (0.72%) • HJPN Japan (0.51%) • UBJ Japan (0.40%)
Individual market (non US)	• IJP Japan (0.48%) • IHK Hong Kong (0.48%) • ISG Singapore (0.48%) • ITW Taiwan (0.62%) • IKO South Korea (0.62%) • IZZ China (0.72%)			

Source: ASX

We give five ETFs the full 5 spots (IVV, VEU, VGAD, VGS and VTS).

IOO and IEM are our current Stockspot portfolio from this asset group.

Stockspot themes also include the options of IVV, IEU, IAA, IZZ, IJP and VEU.

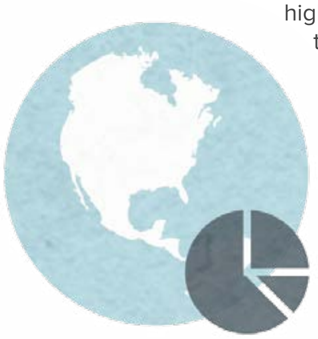
ASX code	ETF Name	Issuer	MER (%p.a)	FUM ($M) Mar'15	FUM ($M) Mar'16	Change in FUM ($M)	Traded value in Mar'16	% Spread	Historical Distribution Yield	1 Year Total Return	Stockspot Rating
International Sector											
BNKS	BetaShares Global Banks ETF - Currency Hedged	BetaShares	0.47%	-	31	31	10,541,482	0.39%	0%	N/A	●●○○○
DRUG	BetaShares Global Healthcare ETF - Currency Hedged	BetaShares	0.47%	-	15	15	3,007,881	0.50%	0%	N/A	●○○○○
ETHI	BetaShares Global Sustainability Leaders ETF	BetaShares	0.59%	-	41	41	7,271,477	0.34%	0%	N/A	●●○○○
FOOD	BetaShares Global Agriculture Companies ETF	BetaShares	0.47%	-	5	5	931,829	0.49%	0%	N/A	●○○○○
FUEL	BetaShares Global Energy Companies ETF - Currency Hedged	BetaShares	0.47%	-	6	6	809,388	0.47%	1%	N/A	●○○○○
GDX	VanEck Vectors Gold Miners ETF	VanEck Vectors	0.53%	22	55	33	4,209,203	0.42%	0%	12%	●●○○○
HACK	BetaShares Global Cybersecurity ETF	BetaShares	0.47%	-	12	12	5,235,377	0.40%	0%	N/A	●○○○○
IXI	iShares S&P Global Consumer Staples ETF	iShares	0.47%	149	146	-4	5,328,889	0.27%	2%	4%	●●○○○
IXJ	iShares S&P Global Healthcare ETF	iShares	0.47%	390	433	43	41,393,600	0.25%	1%	8%	●●●○○
IXP	iShares S&P Global Telecom-munications ETF	iShares	0.47%	23	19	-4	1,139,221	0.40%	3%	-2%	●○○○○
MNRS	BetaShares Global Gold Miners ETF - Currency Hedged	BetaShares	0.47%	-	8	8	3,304,613	0.64%	0%	N/A	●○○○○
GLIN	AMP Capital Global Infrastructure Securities Fund (Unhedged) (Managed Fund)	AMP	0.80%	-	20	20	665,965	0.77%	1%	N/A	●○○○○

ASX code	ETF Name	Issuer	MER (%p.a)	FUM ($M) Mar'15	FUM ($M) Mar'16	Change in FUM ($M)	Traded value in Mar'16	% Spread	Historical Distribution Yield	1 Year Total Return	Stockspot Rating
IFRA	VanEck Vectors FTSE Global Infrastructure (Hedged) ETF	VanEck Vectors	0.52%	-	23	23	1,676,780	0.26%	2%	N/A	●○○○○
MICH	Magellan Infrastructure Fund (Currency Hedged) (Managed Fund)	Magellan	1.05%	-	59	59	6,780,620	0.69%	0%	N/A	●●○○○
DJRE	SPDR Dow Jones Global Select Real Estate Fund	SPDR	0.50%	81	119	38	6,789,160	0.19%	3%	-1%	●●●○○
RENT	AMP Capital Global Property Securities Fund (Unhedged) (Managed Fund)	AMP	0.98%	-	14	14	242,382	0.85%	1%	N/A	●○○○○
Averages			0.58%					0.46%	1%	4%	●●○○○
Totals				665	1,005	341	99,327,866				

Source: ASX

This small group includes ETFs captures the performance of global stocks in specific market sectors. FUM grew by 51% over the year and it had the highest number of new ETFs. There are eleven new unique options for Australian investors to gain access to specific global market sectors, particularly those that are underrepresented within the Australian indices. The new entrants decreased iShares' proportion of the FUM from 85% to just below 60% in under one year as two of their three ETFs lost funds.

VanEck Vector's gold miner ETF was the top performer, benefitting from the recovery of the resources sector and iShares' healthcare ETF (IXJ) continued to provide steady returns. Global ETFs also tend to provide low distributions compared to Australia based ETFs. This sector has relatively high fees with niche exposures that are less accessible to the average Australian investor.



BetaShares launched seven new ETFs to provide new options for banking, sustainability, agriculture, cybersecurity and energy on a global scale. It also added another gold ETF (MNRS) and a healthcare (DRUG) ETF to compete with the largest ETF in this group - iShares' IXJ. AMP launched a global property managed fund (RENT) focusing on Europe, USA and Asia-Pacific, as an active alternative to SPDR's DJRE tracking the Dow Jones Global Select Real Estate Securities Index. Along with several new ETFs they have currency hedges, which will impact future returns versus the unhedged ETFs.

There are now three ETF products focusing on global infrastructure. They include VanEck Vector's IFRA tracking the FTSE index and managed funds by Magellan (MICH) and AMP (GLIN) that are unhedged.

Stockspot themes includes the option of DJRE.

ASX code	ETF Name	Issuer	MER (%p.a)	FUM ($M) Mar'16	FUM ($M) Mar'17	Change in FUM ($M)	Traded value in Mar'16	% Spread	Historical Distribution Yield	1 Year Total Return	Stockspot Rating
Fixed Income & Cash											
AAA	Betashares Australian High Interest Cash ETF	BetaShares	0.18%	954	1,156	202	165,687,612	0.02%	2%	2%	●●●●●
BOND	SPDR S&P/ASX Australian Bond Fund	SPDR	0.24%	24	28	5	1,937,682	0.09%	4%	1%	●●●●○
GOVT	SPDR S&P/ASX Australian Government Bond Fund	SPDR	0.22%	8	15	8	623,479	0.09%	3%	1%	●●●○○
IAF	iShares Core Composite Bond ETF	iShares	0.20%	324	386	62	38,969,696	0.12%	3%	2%	●●●●●
IGB	iShares Treasury ETF	iShares	0.26%	23	30	7	4,380,735	0.33%	2%	1%	●●○○○
ILB	iShares Government Inflation ETF	iShares	0.26%	58	86	27	16,342,624	0.37%	1%	0%	●●●○○
RGB	Russell Australian Government Bond ETF	Russell	0.24%	138	58	-80	1,577,675	0.30%	4%	2%	●●●○○
RCB	Russell Australian Select Corporate Bond ETF	Russell	0.28%	80	122	42	6,801,590	0.31%	4%	3%	●●○○○
RSM	Russell Australian Semi-Government Bond ETF	Russell	0.26%	122	61	-61	3,076,271	0.27%	2%	3%	●●○○○
VACF	Vanguard Australian Corporate Fixed Interest Index ETF	Vanguard	0.26%	-	29	29	7,498,406	0.44%	3%	N/A	●●○○○
VAF	Vanguard Australian Fixed Interest Index ETF	Vanguard	0.20%	361	611	250	42,534,655	0.07%	4%	2%	●●●●●
VGB	Vanguard Australian Government Bond Index ETF	Vanguard	0.20%	79	135	55	17,832,770	0.12%	3%	1%	●●●●●
IHCB	iShares Core Global Corporate Bond (AUD Hedged) ETF	iShares	0.26%	2	47	45	3,154,222	0.44%	3%	4%	●●○○○

ASX code	ETF Name	Issuer	MER (%p.a)	FUM ($M) Mar'16	FUM ($M) Mar'17	Change in FUM ($M)	Traded value in Mar'16	% Spread	Historical Distribution Yield	1 Year Total Return	Stockspot Rating
IHHY	iShares Global High Yield Bond (AUD Hedged) ETF	iShares	0.56%	2	16	14	1,244,103	0.40%	6%	12%	●○○○○
IHEB	iShares J.P.Morgan USD Emerging Markets Bond (AUD Hedged) ETF	iShares	0.51%	1	4	3	271,369	0.47%	7%	11%	●○○○○
VCF	Vanguard International Credit Securities Index (Hedged) ETF	Vanguard	0.30%	4	82	79	7,150,057	0.27%	8%	4%	●●○○○
VIF	Vanguard International Fixed Interest Index (Hedged) ETF	Vanguard	0.20%	12	80	68	13,716,200	0.18%	8%	1%	●●●●○
Averages			0.27%					0.25%	4%	3%	●●●○○
Totals				2,191	2,946	754	332,799,144				

Source: ASX

These ETFs offer exposure to fixed income and cash from Australia and overseas to investors.

An upturn in the stock market has resulted in last year's rapid growth of the sector slowing as investors confidence returned to less defensive ETFs. However, fixed income still remained popular as it provides an important portfolio diversifier, especially for self managed super funds, and retained its place as the third largest sector by FUM.

The sector is still dominated by the BetaShares Australian High Interest Cash ETF (AAA), the only cash ETF, which invests in short-term deposits and returned 2% for the year. Vanguard's fixed interest ETF (VAF) grew by $250 million. Its FUM grew to just over 30% of the group total, whilst BetaShares' AAA has slipped to just under 40% in the past year. Vanguard also launched one new ETF tracking an Australian corporate fixed interest index (VACF).

Investors should be aware of the impact that interest rates and inflation can have on bond returns before choosing a fixed income ETF investment. Bonds generally benefit from falling interest rates and dropping future rate expectations in Australia. Bonds with a longer average term to maturity are more sensitive to interest rate changes than shorter-term bonds.

Whilst Australia's interest rate has declined from 2% to 1.5% since March 2016 and remained steady since September 2016, falling corporate bond spreads have helped corporate bond ETFs outperform government bond ETFs. Russell's government (RGB) and semi-government bonds (RSM) ETFs have lost funds, whereas its corporate bond ETF (RCB) gained $40 million in the past year.

Government bonds from emerging markets tend to have higher yields, but are generally considered to be more risky. These returns can be very attractive to fixed income investors in a period of record low interest rates and potential deflation in advanced economies.

Four ETFs - AAA, IAF, VGB and VAF earned 5 spots.

IAF is our current Stockspot portfolio inclusion from this asset group. We feel it provides a good mix of government, semi-government and corporate bonds with a relatively short average duration. This reduces the sensitivity of IAF to short-term changes in rate expectations.

Stockspot themes also include the option of VIF and AAA.

ASX code	ETF Name	Issuer	MER (%p.a)	FUM ($M) Mar'16	FUM ($M) Mar'17	Change in FUM ($M)	Traded value in Mar'16	% Spread	Historical Distribution Yield	1 Year Total Return	Stockspot Rating
Commodity											
ETPMAG	ETFS Physical Silver	ETF Securities	0.49%	43	62	18	3,154,993	1.20%	0%	18%	●●○○○
ETPMPD	ETFS Physical Palladium	ETF Securities	0.49%	1	2	1	1,067,513	0.68%	0%	37%	●○○○○
ETPMPM	ETFS Precious Metals Basket	ETF Securities	0.43%	4	5	1	1,798,522	0.38%	0%	10%	●○○○○
ETPMPT	ETFS Physical Platinum	ETF Securities	0.49%	3	3	0	2,096,940	0.47%	0%	-5%	●○○○○
GOLD	ETFS Physical Gold	ETF Securities	0.40%	426	475	49	15,817,605	0.20%	0%	1%	●●●●○
OOO	BetaShares Crude Oil Index ETF-Currency Hedged (Synthetic)	BetaShares	0.69%	47	40	-7	8,547,583	0.29%	0%	9%	●○○○○
PMGOLD	Perth Mint Gold	Perth Mint	0.15%	88	116	28	7,427,374	0.51%	0%	1%	●●●○○
QAG	BetaShares Agriculture ETF-Currency Hedged (Synthetic)	BetaShares	0.69%	3	3	0	1,715,940	0.76%	1%	-6%	○○○○○
QAU	BetaShares Gold Bullion ETF (AU$ Hedged)	BetaShares	0.39%	40	53	13	10,494,549	0.37%	0%	0%	●●○○○
QCB	BetaShares Commodities Basket ETF-Currency Hedged (Synthetic)	BetaShares	0.69%	8	9	2	441,881	1.51%	1%	2%	○○○○○
ZGOL	ANZ / ETFS Physical Gold ETF	ANZ	0.40%	2	13	11	2,032,536	0.66%	0%	0%	●○○○○
Averages			0.48%					0.64%	0%	6%	●○○○○
Totals				664	780	116	54,595,438				

Source: ASX

Commodity

This group's ETFs are all focused on the natural resources and commodity sectors. The sector has experienced a significant recovery after a period of negative performance. ETF Securities held its dominant position with 70% of FUM and the rest being almost equally spread between Perth Mint Gold and BetaShares.

The palladium ETF (EPTMPD) had a great performance of almost 37% and unlike other precious metals its demand is almost entirely related to industry, particularly for its use in car engines. The BetaShares Oil ETF (OOO) recovered from the negative returns of last year, but investors still appear wary after the volatility of the past few years with a fall in funds.

The four gold ETFs' returns were minimal from around 0.9% to -0.1%, but still hold around 84% of the sector's FUM. The minor changes in the Australian Dollar resulted in little difference between hedged and unhedged ETFs. Gold's reputation for safety during times of market downturn has shown through, with demand for these ETFs slowing as the share market has provided better returns.

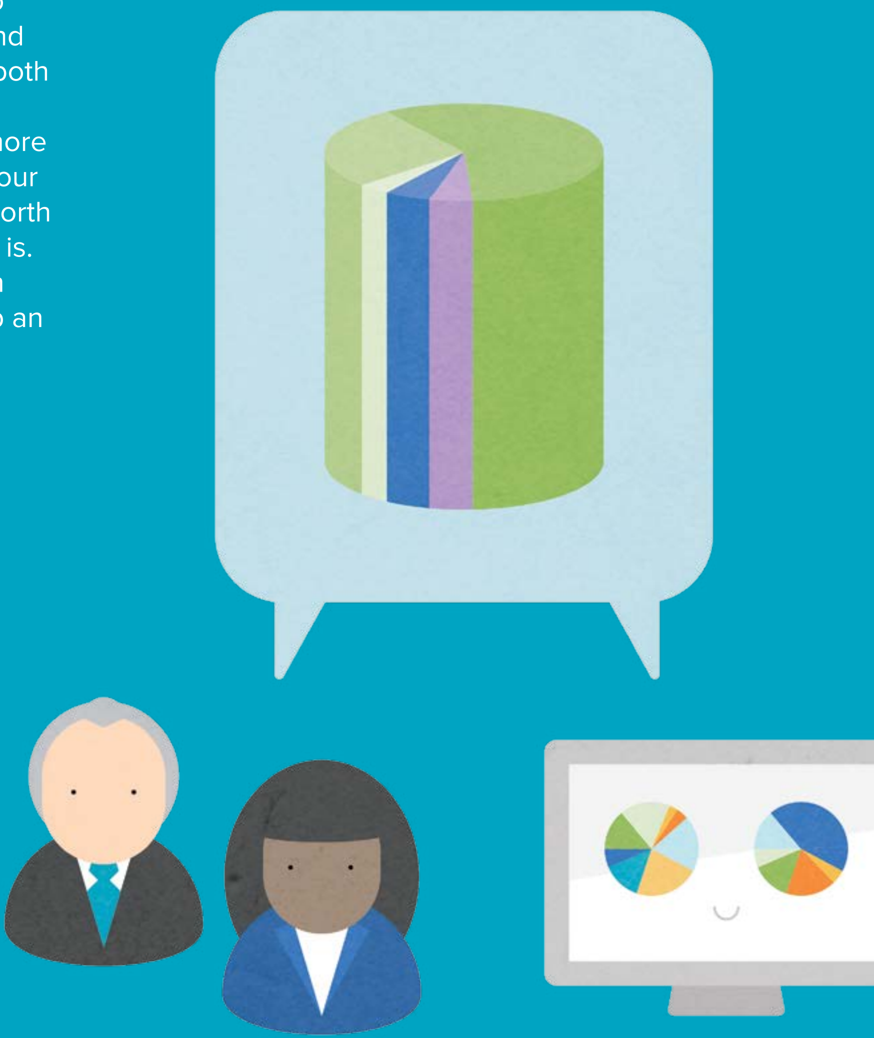
Several products in this category are either Structured Products, or synthetic ETFs - indicating that they hold financial contracts rather than owning the physical underlying assets. Physically backed ETFs offer the most direct approach, but incur the cost of storage and insurance.

GOLD is our current Stockspot portfolio inclusion from this asset group. We prefer unhedged gold compared to the hedged version as a diversifier in our portfolios since it provides better protection against domestic currency debasement and a weak Australian economy.

Alternative Indexing & Active ETMFs

Smart beta is latest investment trend, marketed as a new way to diversify and reduce risk. In this section we look at smart beta ETFs in Australia – what they are, how they are built and how they've performed.

It's nearly impossible to read the financial news or an investment newsletter these days without coming across the term "smart beta". Smart beta – also known as strategic beta, alternative beta, fundamental beta, advanced beta, enhanced beta, and probably a few other names – aims to combine elements of passive index investing and active fund management to deliver the best of both worlds: transparency, broad diversification, and market-beating returns – all at low cost. What more could you ask for? But before you throw all of your savings into the latest smart beta product, it's worth digging a bit deeper into what smart beta really is. Smart beta is all about index construction which refers to which stocks (or other assets) make up an index and their relative size within that index.



EMERGENCE OF SMART BETA

All index funds, by definition, are passive investments. This includes smart beta. There is no fund manager making trading decisions and all buying and selling is done according to a strict set of rules.

However, smart beta indices aim to fix some of the believed shortcomings of weighting investments by market size when building an index. One example is that during a bubble, some shares can make up a larger and larger share of the index, like technology stocks did during the 'tech boom' in the late 1990s, or mining stocks when commodity prices rocketed in 2006-2011. This can cause traditional size-weighted indices to 'overshoot' during booms and busts.

To address this and other similar observations about size-weighted indices, new ways of constructing indices have emerged – with weights determined by different approaches such as dividends, research ratings, simple averages, or consistency of cash flows. This is what's meant by smart beta.

COMMON SMART BETA STRATEGIES

There are 4 common smart beta approaches to building indices:

- High dividend strategies that aim to pick stocks with higher dividend yields to boost investor income.
  e.g. Vanguard Australian Shares High Yield ETF (VHY)
- Other fundamental indices that focus on measures like sales revenue or free cash flow as a more accurate measure of economic contribution rather than using market capitalisation.
  e.g. Russell Australian Value ETF (RVL) or
  BetaShares FTSE RAFI Australia 200 ETF (QOZ)
- Equal weighting – the simplest form of index construction that just averages an entire universe of stocks, thus giving each stock the same importance.
  e.g. VanEck Vectors Australian Equal Weight ETF (MVW)
- Low volatility strategies which target a smoother ride by carefully selecting less risky stocks.
  e.g. ANZ/ETFS S&P 500 High Yield Low Volatility Fund (ZYU)

While some of these funds may advertise a new paradigm of investment thinking, they all use fairly transparent, rules-based approaches to prioritise exposure to certain market factors. These factors include style (growth and value), size (large, mid, small), or momentum (consistency). The challenge for investors is in deciding which factors to want exposure to (if any).

SMART BETA BETS ON MARKET FACTORS

At their core, all smart beta ETFs are taking a bet on certain market factors being more important than others:

- Low volatility and high dividend stocks tend to have a bias towards value stocks that have lower growth and more stable earnings since they tend to be less volatile than companies with less predictable profits like mining businesses or biotechnology. However, when investors crowd into low-volatility or high dividend stocks, as they've been doing over the past few years, it can push valuations in some sectors (e.g. telecommunications, utilities, and property) to the point that they actually become more risky. This can, perhaps counterintuitively, make low volatility or high dividend strategies dangerous after a period of good returns.
- Fundamental indices may use operating cash flow as a better indication of economic size. Analysis shows these approaches have a strong value stock bias as well.
- An equal weighting methodology introduces a significant bias towards small companies because the stocks that have a lower market size have the same weight in the index as bigger businesses like Commonwealth Bank (CBA). The portfolio will likely also have a value bias because equal weighting will expand the weight of value stocks, which tend to trade at lower price compared to their profit.

Shortcomings of smart beta

FACTORS USED TO ESTIMATE A COMPANY'S VALUE

- Profits
- Regulatory environment
- Competitive landscape
- Management effectiveness
- Expected growth
- New products / business
- Counterparty exposure
- Supply chains
- Corporate governance controls
- Liquidity
- International operations
- Hedging activity
- Input Prices
- Natural disasters
- Market Share
- Business Model
- Industry outlook
- Expectations
- Off-balance sheet items
- Share re-purchases
- Accounting irregularities

Factors that smart beta focus on:

- Dividends
- Assets
- Cash flow
- Book value
- Sales
- Volatility

Source: Vanguard

HOW SMART IS IT REALLY?

By offering enhanced exposure to some factors, like value and size, smart beta strategies must also be de-prioritising other factors. Because current price reflects every factor used by any investor to estimate a company's value, a market-size-weighted index also represents an all-factor approach to investing. On the other hand, smart-beta is essentially taking a bet that a few select factors are more important than an all factor (market value) approach.

BACKTESTING CAN GIVE FALSE CONFIDENCE

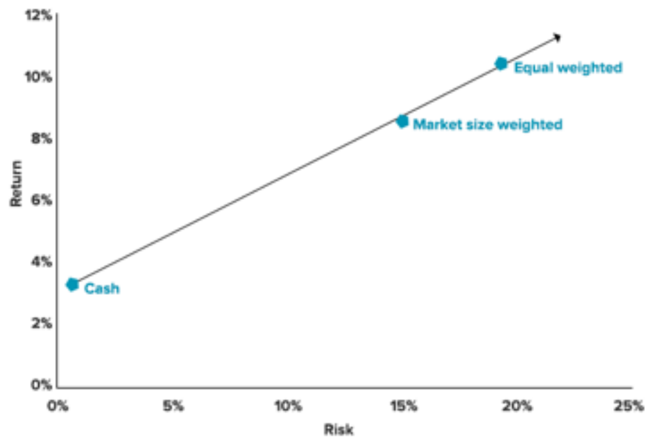
Smart beta strategies are often marketed as being able to 'beat the market'. However the truth is often a lot more murky. Many have only outperformed from backtesting over a select, historical time period which introduces a few significant issues.

Think of an index like a deck of cards. Backtesting lets you shuffle a deck of cards thousands of times until a favourable "shuffle" emerges to match the order you want to show. In essence, backtesting lets the smart beta strategies and ETFs 'stack a deck' of stocks in a way that outperformed the index in the past. But there's no guarantee that the same strategy will work going forward. As a result, many smart beta strategies could have simply worked in the past by chance.

Let's say you rebuilt S&P/ASX200, but weighted the companies according to the birthday of their CEOs and found that this new index outperformed a size weighted index by 20% over 15 years. This would not be because January-born CEOs are better at managing businesses than December ones. This would just be an example of how you can use a random set of data to prove any hypothesis when backtesting.

WHAT ABOUT RISK?

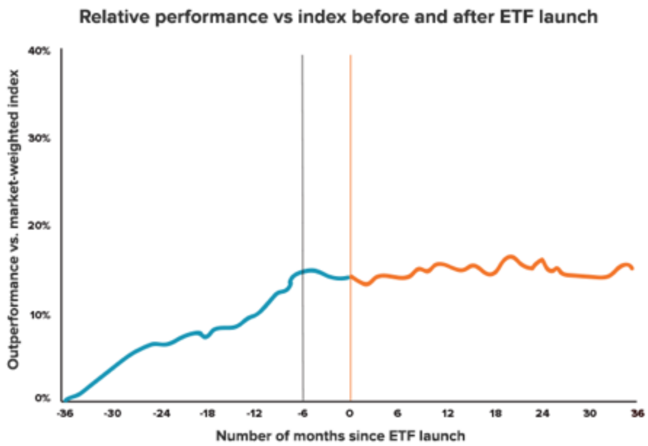
Some smart beta strategies have been able to outperform the index over the long-term, but the differences in return can usually be explained simply by risk. For example, equal-weight indices of stocks do tend to outperform market-size weighted indices over the long-term. However this can be explained entirely due to equal weight taking more risk (due to having more small stocks). On a risk versus returns basis, you're no better off owning the equal weight index even though it generated higher returns. Also, there are sometimes lower-cost ways to get the same factor exposure (small companies) and return profile.



Sources: CRSP US Stock and Index Database, S&P Dow Jones Indexes, Federal Reserve

SMART BETA FOLLOWS IN-VOGUE STYLE TRENDS

It's no coincidence that many of the smart beta funds launched over the past couple of years in Australia have been dividend focused. This is because dividend investment strategies had a great run of performance between 2011 and 2014. ETF issuers know that it's much easier selling strategies that have done well recently than those that haven't since people tend to chase returns.



In fact research has shown that on average, new funds launch about six months after the peak in their particular strategy compared to the broad index. This is not a coincidence – the product teams launching new funds usually take about six months to get them launched so when they decide to launch a fund it is usually at exactly the point that the particular strategy is showing its best results compared to benchmarks. Unfortunately, outperformance tends to end soon after smart beta ETFs are launched.

Source: Research Affiliates

CONCLUSION

Smart beta ETFs give investors the ability to tilt their portfolios towards certain factors that active fund managers have used for years. But if you are considering investing in an smart beta ETF, it is important to understand that you are actually taking bets on certain market factors beating others. You should be comfortable with what those factor bets are, and why you are taking them. If you don't understand the bets you are taking and the only reason you are investing in smart beta is backtesting or recent performance, then what you're buying into isn't smart beta as much as it is smart marketing, and that is not smart investing.

ASX Code	Fund Type	ETF Name	MER	1 Year Total Return	Historical Dividend Yield
Australian ‘Smart Beta’ ETFs					
AUMF	ETF	iShares Edge MSCI Australia Multifactor ETF	0.30%	N/A	0%
DIV	ETF	UBS IQ Morningstar Australia Dividend Yield ETF	0.30%	14%	4%
ETF	ETF	UBS IQ Morningstar Australia Quality ETF	0.30%	8%	5%
EX20	ETF	BetaShares Australian Ex-20 Portfolio Diversifier ETF	0.20%	N/A	0%
FDIV	ETF	VanEck Vectors S&P/ASX Franked Dividend ETF	0.35%	N/A	3%
IHD	ETF	iShares S&P/ASX High Dividend Yield ETF	0.30%	20%	5%
MVOL	ETF	iShares Edge MSCI Australia Minimum Volatility ETF	0.30%	N/A	0%
MVW	ETF	VanEck Vectors Australian Equal Weight ETF	0.35%	19%	2%
QOZ	ETF	BetaShares FTSE RAFI Australia 200 ETF	0.30%	27%	5%
RARI	ETF	Russell Australian Responsible Investment ETF	0.45%	19%	5%
RDV	ETF	Russell High Dividend Australian Shares ETF	0.34%	22%	4%
RVL	ETF	Russell Australian Value ETF	0.34%	25%	4%
SYI	ETF	SPDR MSCI Australia Select High Dividend Yield Fund	0.35%	24%	5%
VAS	**ETF**	**Vanguard Australian Shares Index ETF (for comparison)**	**0.14%**	**20%**	**4%**
VHY	ETF	Vanguard Australian Shares High Yield ETF	0.25%	22%	6%
ZYAU	ETF	ANZ / ETFS S&P/ASX 300 High Yield Plus ETF	0.35%	25%	3%

Source: ASX

High yields and dividends is the most popular theme in this category as the focus on half the smart beta ETFs. Australian investors have become used to comparatively large dividend payouts from companies on a world scale. There are also benefits from franked dividends for Australian investors.

Smart beta ETFs had mixed performances compared to the traditional market cap weighted ETF (VAS provided as an example), with some dividend ETFs performing well this year, but the UBS ETF that focused on the ‘quality’ fundamental factor underperformed.

This years top performer, BetaShares’ QOZ uses its own ‘fundamental’ measurements for weightings of the top two hundred companies, rather than market capitalisation weightings like a traditional index fund.

iShares launched two new products; AUMF focuses on four ‘growth factors’, including taking measures for quality, value, size and momentum in account when selecting stocks and MVOL aims to reduce exposure to market volatility for lower losses during downturns. BetaShares and VanEck Vectors also launched new smart beta products this year.

ASX Code	Fund Type	ETF Name	MER	1 Year Total Return	Historical Dividend Yield
Global ‘Smart Beta’ ETFs					
MOAT	ETF	VanEck Vectors Morningstar Wide Moat ETF	0.49%	24%	1%
QUAL	ETF	VanEck Vectors MSCI World Ex-Australia Quality ETF	0.40%	12%	2%
WDIV	ETF	SPDR S&P Global Dividend Fund	0.50%	11%	4%
WDMF	ETF	iShares Edge MSCI World Multifactor ETF	0.35%	N/A	0%
WVOL	ETF	iShares Edge MSCI World Minimum Volatility ETF	0.30%	N/A	0%
VGS	**ETF**	**Vanguard MSCI Index International Shares ETF (for comparison)**	**0.18%**	**15%**	**4%**
VTS	**ETF**	**Vanguard US Total Market Shares Index ETF (for comparison)**	**0.05%**	**18%**	**2%**
ZYUS	ETF	ANZ / ETFS S&P 500 High Yield Low Volatility ETF	0.35%	13%	4%

Source: ASX

The trend for high yield has been less of a feature for global smart beta ETFs listed in Australia, with only WDIV focusing on global dividend returns and ZYUS for the US stockmarket. This may be because global shares, especially from the US, tend to provide lower yields on average than Australian shares which makes this strategy is less attractive.

iShares’ two new global smart beta ETFs are based on the World MSCI Indices, replicating strategies that they have also launched for Australian shares. WDMF also focuses on the same four factors, including financially healthy firms, inexpensive stocks, smaller companies and trending stocks. WVOL that aims to reduce exposure to market volatility for lower losses during downturns on a global scale. Similarly, ANZ’s ZYUS focuses on fifty high yielding companies from its low volatility US index and is comparable to ZYAU for the Australian market.

SPDR’s WDIV is the only yield focused product with stocks from around the world, with the rule for the hundred companies requiring a ‘managed-dividends policy of increasing or stable dividends for at least ten consecutive years.’

The MOAT product by VanEck Vectors follows an index created by Morningstar’s equity research team for well priced companies that have sustainable competitive advantages. Similar to UBS’ ETF also following a Morningstar research index, issuers can actually outsource this aspect of creating the smart beta fund. MOAT has at least forty stocks selected through criteria, compared to Vanguard’s VTS having around 3,600 holdings from the total US stock market.

Australian Exchange Traded Managed Funds

ASX Code	Fund Type	ETF Name	MER	1 Year Total Return	Historical Dividend Yield
Australian Exchange Traded Managed Funds					
AOD	MF	Aurora Dividend Income Trust	0.97%	2%	6%
AUST	MF	BetaShares Managed Risk Australian Share Fund (Managed Fund)	0.39%	12%	3%
HVST	MF	BetaShares Australian Dividend Harvester Fund (Managed Fund)	0.65%	9%	9%
SWTZ	MF	Switzer Dividend Growth Fund (Managed Fund)	0.89%	N/A	0%
YMAX	MF	BetaShares Australia Top20 Equity Yield Max Fund	0.59%	17%	9%
STW	**ETF**	**SPDR S&P/ASX 200 (for comparison)**	**0.19%**	**20%**	**4%**

Source: ASX

Several managed funds construct their own portfolios to list on the ASX as active ETPs. In this case there is a fund manager making trading decisions and the choice of holdings is generally dependent on similar methods to traditional active investment portfolios. There are many potential outcomes, for it may not be related to a specific index or only employ its strategy to only select stocks from one index. There can be a level of overlap in these processes when related to smart beta ETFs.

High yields and lower volatility are again a popular themes with investors, as they remain wary of risk whilst searching for returns in a low interest rate environment since the Global Financial Crisis. Asset manager Switzer has listed its first product (SWTZ) that provides quarterly dividends from thirty to fifty selected stocks as ETPs become a more common part of existing investors' portfolios.

BetaShares employs a limited amount 'futures' buying and selling in its managed funds to help lessen the impact of stockmarket movements and protect investors against losses.

Dividend harvesting strategies like HVST involve borrowing from future capital returns in order to increase dividends. It invests in large ASX shares that are about to pay dividends while also selling futures contracts which is a form of hedging to reduce risk. YMAX sells 'call options' while investing in the twenty largest stocks by market capitalisation in Australia. This helps it lower volatility due to predictable income from selling calls, but means it is likely to underperform in growing markets, as shown by its higher income but lower total return when compared to STW.

An investor just focused on yield may have a negative total return despite a positive yield because of a capital loss. There is a risk that companies may payout a higher ratio of their profits to attract investors, rather than reinvesting in themselves for sustainable future growth.

Global Exchange Traded Managed Funds

ASX Code	Fund Type	ETF Name	MER	1 Year Total Return	Historical Dividend Yield
Global Exchange Traded Managed Funds					
GLIN	MF	AMP Capital Global Infrastructure Securities Fund (Unhedged) (Managed Fund)	0.80%	N/A	1%
GROW	MF	Schroders Real Return Fund (Managed Fund)	0.90%	N/A	1%
MGE	MF	Magellan Global Equities Fund (Managed Fund)	1.35%	10%	2%
MHG	MF	Magellan Global Equities Fund Currency Hedged (Managed Fund)	1.35%	12%	2%
MICH	MF	Magellan Infrastructure Fund (Currency Hedged) (Managed Fund)	1.05%	N/A	0%
RENT	MF	AMP Capital Global Property Securities Fund (Unhedged) (Managed Fund)	0.98%	N/A	1%
QMIX	MF	SPDR MSCI World Quality Mix Fund	0.40%	12%	3%
VGS	**ETF**	**Vanguard MSCI Index International Shares ETF (for comparison)**	**0.18%**	**15%**	**4%**
WRLD	MF	BetaShares Managed Risk Global Share Fund (Managed Fund)	0.39%	10%	1%
WXOZ	**ETF**	**SPDR S&P World ex Australian Fund (for comparison)**	**0.30%**	**15%**	**3%**
UMAX	MF	BetaShares S&P 500 Yield Maximiser Fund (Managed Fund)	0.59%	13%	5%

Source: ASX

Global managed funds focus on exposure to worldwide indices and currently tend to favour exposure to broad developed markets, with just one country specific product being UMAX for the US. It includes products from asset managers such as Magellan providing both currency hedged and unhedged versions of its popular global equities fund that selects between twenty to forty stocks. (MHG and MGE respectively) ETF issuers also have tendencies to 'repackage' products in this category, for example SPDR's QMIX is composed from three indices capturing factors for value, low volatility and quality for companies in twenty-four developed countries.

UMAX has a similar strategy for the US large companies that YMAX follows for Australian stocks. BetaShares' WRLD focuses on reducing risk in a fund with approximately 1,500 companies from developed countries by selling futures, which is comparable to AUST's strategy for the largest 200 companies in the Australian stockmarket.

Another asset manager, Schroders has listed a managed fund (GROW) targeting returns around 5% above Australia's inflation over three year periods from Australian and global shares.

This group includes new global sector products from AMP in partnership with BetaShares. RENT focuses on global property securities and REITs (real estate investment trusts) and GLIN for a selection of thirty-five to forty-five infrastructure stocks, generally from the energy, transportation, communications and water sectors. Magellan also created a listed version of its infrastructure fund with twenty to forty stocks and provides an unhedged alternative with MICH.

It will be interesting to follow the performance of the actively managed real estate (RENT) and infrastructure funds (GLIN) and compare them to their index equivalent products IFRA and DJRE which charge approximately half the fees.

Alternative Indices

Exchange Traded Hedge Funds

ASX Code	Fund Type	ETF Name	MER	1 Year Total Return	Historical Dividend Yield
Exchange Traded Hedge Funds					
AUDS	MF	BetaShares Strong Australian Dollar Fund (Hedge Fund)	1.19%	N/A	0%
BBOZ	MF	BetaShares Australian Strong Bear (Hedge Fund)	1.19%	-37%	0%
BEAR	MF	BetaShares Australian Equities Bear (Hedge Fund)	1.38%	-18%	1%
BBUS	MF	BetaShares US Equities Strong Bear Currency Hedged (Hedge Fund)	1.19%	-35%	0%
DMKT	MF	AMP Capital Dynamic Markets Fund (Hedge Fund)	0.48%	N/A	2%
GEAR	MF	BetaShares Geared Australian Equity Fund (Hedge Fund)	0.80%	43%	6%
GGUS	MF	BetaShares Geared US Equity Fund Currency Hedged (Hedge Fund)	0.74%	40%	1%
KII	MF	K2 Global Equities Fund (Hedge Fund)	2.05%	9%	0%
KSM	MF	K2 Australian Small Cap Fund (Hedge Fund)	2.00%	10%	0%
STW	**ETF**	**SPDR S&P/ASX 200 (for comparison)**	**0.19%**	**20%**	**4%**
VTS	**ETF**	**Vanguard US Total Market Shares Index ETF (for comparison)**	**0.05%**	**18%**	**2%**
YANK	MF	BetaShares Strong US Dollar Fund (Hedge Fund)	1.38%	N/A	0%

Source: ASX

In the case of hedge funds, ETPs may be 'geared' to magnify returns, which is evidenced by producing some of the best and worst performers this year. For example, a 1% daily increase in an index can become a 2.5% increase in the ETP's returns if it is geared at 250%. These funds also include a level of active human involvement, rather than strictly tracking indices following certain rules. When compared to STW to represent Australian returns and VTS for the US stock market, hedge funds tend to either over or undershoot the average market returns.

Exchange traded hedge funds are generally riskier than regular index ETFs due to both the risks associated with leverage, and those associated with compounding returns on a daily basis. Volatile markets can lead to big losses for leveraged ETFs due to the fact that compounding works in both directions. Leveraged ETF also tend to be more expensive than traditional ETFs.

This category is dominated by BetaShares, including the collaboration with AMP's new hedge fund (DKMT). Although, BetaShares' products do not borrow funds for leverage, 'futures' are used to magnify returns which still adds several layers of risk.

Bear hedge funds are actively managed to provide returns close the opposite of the index that they are tracking and aim to protect investors against market downturns. As the stock market provided high returns over the past year, funds such as BBUS tracking the US and BEAR tracking Australian shares both underperformed. A 'strong' bear fund, such as BBOZ has a higher level of gearing, of between 200% to 275%, rather than the around 100% used for BEAR. This has a greater effect on its returns. As a result, the 'Strong Bear' hedge funds tracking Australian and US shares fell 37% and 35% respectively this year.

Conclusion

The ETF market has continued to grow in popularity in Australia, doubling in size over 4 years. This year's ETF growth was helped by strong performances in Australian and global shares as well as continued diversification into overseas markets and defensive investments like bonds, high interest cash and infrastructure.

The ETF products available keep evolving beyond ETFs tracking broad market indices into sector and strategy specific ETFs, smart beta ETFs, geared ETFs and actively managed exchange traded managed funds. Each group has its own set of unique risks and opportunities for investors.

With greater choice comes the need for investors to be more discerning when selecting ETFs for their portfolio. Many of the new products that have been launched recently make it tempting for investors to 'chase' returns in sectors, markets or strategies that have performed well in the recent past. Be very careful when reading marketing materials that show that a product has 'outperformed' over a period of time. Not only are time periods carefully selected by product issuers to paint a product in the best light, but performance also tends to 'mean revert' over the long run so outperformance is almost always only temporary.

Over longer periods all strategies are likely to return to long term averages which is why we prefer to give our clients broad market diversification and steer clear of the hype surrounding short term market trends. There is no 'free lunch' when investing, strategies that sound too good to be true are always proven to be so.

Even over the past year, several of the ETFs that were heavily out of favour like Asian shares (+24%) and Resources shares (+40%) have been some of the best performers, well outpacing returns in on-trend markets like US shares (+17%) and Australian property shares (+7%). Disciplined portfolio rebalancing can help achieve a balance between being invested in popular strategies while not getting carried away when they overshoot.

Our advice to clients is simple; invest in a broad mix of assets using ETFs, don't pick individual stocks, keep your costs low, rebalance occasionally and don't pay attention to what happens in the short term because it is all just market noise.

Glossary

Asset class:
A type of investment such as shares or property, which have similar financial characteristics.

ASX:
Australian Securities Exchange

Bear hedge fund:
A hedge fund designed to provide higher returns as the market falls, it may track the inverse of an index as an ETF.

Broad market ETFs:
Track the widest range of securities in the market that has been selected.

Bid/Ask spread:
The difference between the highest price offered by a bidder and lowest price offered by a seller for the asset.

Call option:
An agreement that gives the investor the option to buy assets at an agreed price on or before a particular date.

Derivative:
A security that is dependent on one or more underlying assets.

Distribution yield:
A financial ratio that shows how much an ETF pays out in distributions each year relative to its unit price.

FUM:
Funds Under Management.

Hedged ETF:
Funds where strategies are used to neutralise changes in currency movements.

Historical Distribution Yield:
Actual distribution return over the prior 12 months as a percentage of the unit price.

ICR:
Indirect Costs Ratio.

Index:
A section of the stock market with a number of holdings based on their market capitalisation.

LIC:
Listed Investment Company. A managed fund which is actively managed in a closed ended structure and listed on a stock exchange. Unlike ETFs, LICs can trade at significant premium or discount to their net asset value.

MER:
Managed Expenses Ratio. The fees shown as a percentage that will be deducted from the total returns every year.

NAV:
Net Asset Value. The value of a fund's asset less the value of its liabilities per unit.

Sector:
Specific sections of the market.

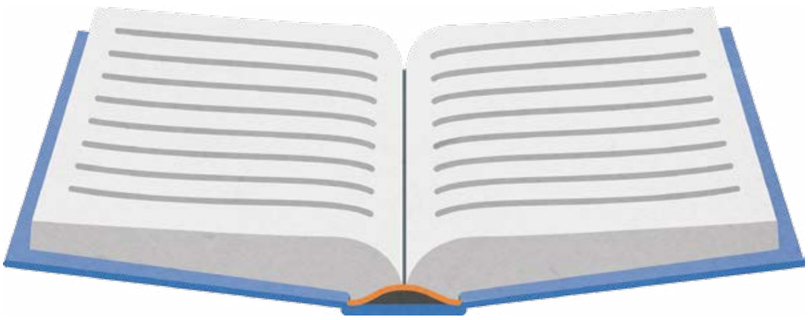
Sector ETFs:
Track sectors within a market. (e.g. property, financials or resources)

Securities:
A financial instrument with proof of ownership that can be traded.

Strategy ETFs:
Only include some securities in the market. Securities are selected according to certain rule-based factors (e.g. dividend yield or research rating)

Synthetic Returns:
Returns from a financial instrument that is created artificially by combining features of different assets.

Unhedged ETF:
Funds which are also impacted by changes in currency movements in addition to movements in the underlying investments.



Notes

Grow your savings the smart way

Stockspot is Australia's first digital investment adviser. We were founded in 2013 with a mission to help more Australians access expert investment advice and portfolio management.

We want to do away with the high fees, confusing jargon, endless paperwork and lack of transparency that gives the wealth management industry a bad reputation.

Today, we're the largest and fastest growing automated investment service in Australia. We're helping thousands of Australians manage their money smarter with our low-fee transparent investment service.

Find out more: www.stockspot.com.au

stockspot