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Access the opportunities.

YOUR GUIDE TO

Exchange Traded Funds

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Dear Investor

Welcome to the third edition of our *Guide to Exchange Traded Funds*.

Now more than ever, investors' constitutions are being tested. While we continue to grapple with the new "normal" in a world irrevocably changed by COVID-19, market behaviour, including the market rally in the second quarter of 2020, has been somewhat bewildering and perplexed the most judicious investor.

However, the growth trajectory of Exchange Traded Funds (ETFs) in Australia has only strengthened, growing by more than 12.2% in the first half of 2020 to reach $56.5 billion in assets under management. More and more Australians are choosing to invest in ETFs for their increased transparency, cost effectiveness, targeted outcomes and ease of access via ASX.

Founded in 1955, VanEck is one of the largest issuers of ETFs and globally manages in excess of $60 billion for our investors. ETFs have helped democratise investing, giving one-trade access to a diversified portfolio of stocks or bonds, as well as opening up asset classes and investment strategies previously only accessible to professional and institutional investors. With over 20 ETFs on ASX VanEck's range of ETFs offer a range of asset classes and outcomes to help investors meet their investment objectives.

While the pandemic continues and unprecedented fiscal and monetary intervention impacts markets, many investors are asking how they should position their investment portfolio. We have dedicated this edition to help answer that question.

I hope you enjoy this edition and I hope that you, your family and loved ones are all safe. If you have any questions about investing or your portfolio, we recommend you to speak to your financial adviser or stock broker in assessing which ETFs are right for you.

If you would like a copy of our first or second *Guide to Exchange Traded Funds*, please contact us on 02 8038 3300 or email us at info@vaneck.com.au

Keep safe,

Arian Neiron
Managing Director & Head of Asia Pacific, VanEck

Exchange Traded Funds allow you to invest in a diversified portfolio of stocks, bonds or other assets that track an index in one trade on ASX.

ETF

$57 billion
invested in ETFs in Australia.[1]

$8 trillion
invested in ETFs globally.[2]

Environmental, Social & Governance
ESG investing seeks to identify companies that are doing "good" and can deliver shareholder value.

Smart beta
An investment strategy that takes a considered approach to the way it selects and weights stocks or bonds.

Performance
The #1 motivation for financial advisers and stock brokers using smart beta ETFs.[3]

All figures are in AUD. 1. Source: ASX, as at 30 June 2020. 2. Worldwide ETF assets under management 2003-2019, M. Szmigiera, 2020. 3. Source: VanEck 2019 Australian Smart Beta Survey.

The world's leading gold miners ETF

ASX code: GDX

With a deep heritage investing in gold companies,
VanEck has one of the longest track records among investment managers in this sector.

With one trade on ASX, GDX gives you instant exposure to a global portfolio of 53 gold miners.

Learn more at vaneck.com.au. Speak to your financial adviser or stock broker today.

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POSITIONING FOR THE RECOVERY

There are compelling options that could help investors navigate the current environment and the recovery down the road. And they are available on ASX.

As we entered 2020, investors were faced with tricky choices. Share markets were trading near all-time highs while measures of volatility were near all-time lows.

There seemed to be little compensation for risks, and even less for sitting on the sidelines as bond rates lingered near zero. Then the COVID-19 pandemic struck and those that had resisted the urge to own risky assets were justified.

With the exception of cash, there was no place to hide from one of the most severe sell-offs in history.

However, as central banks and governments came to the rescue, financial markets staged an equally spectacular recovery.

The opportunity to take advantage of the sell-off proved fleeting and what now remains is more volatility and uncertainty.

Equity valuations in some sectors are now materially higher than before the crisis even though household and corporate confidence is low.

Meanwhile economic and market uncertainty has increased as policy responses have further lowered yields on safe assets, increasing the cost of being cautious.

There are, however, compelling options that could help investors navigate the current environment and the recovery down the road. And they are available on ASX.

The first is China's equity market. While China was the epicentre of the COVID-19 pandemic, ironically it is now among the best-placed economies to prosper in the post COVID-19 world.

China's share market has previously been overlooked by international investors as it has been hard to access and over-exposed to state owned enterprises.

But there is now a way to gain access to the sectors that have direct exposure to the Chinese economy's dynamism.

Gold too is set to glitter in the post-COVID-19 world, or at the very least provide a hedge against

unprecedented money supply creation and the threat of monetisation.

While investors have been apprehensive to own gold on the basis that it does not generate an income, that's not the case for gold miners. They are well poised to deliver profits to investors, while providing a hedge against a range of outcomes.

Investors too can take a smarter approach to Australian equities, one which provides access to the broader opportunities within the Australian economy as the nation emerges from the aftermath of the economic and health crisis.

While we experience a time in history that has led to a response from governments around the world not seen since World War II, there are investment opportunities that can easily be accessed via ETFs which can help investors of all sizes to position for what lies ahead.

FUTURE PROSPERITY WITH CHINA'S NEW ECONOMY

It's been a wild ride in equity markets since the beginning of the year.

Among the winners have been Chinese stocks and certain sectors there too have shone – such as healthcare, technology and the consumer sectors. It is these sectors which make up the 'New Economy'.

As China manages its cases of COVID-19, and beyond, we expect these sectors will continue to thrive.

Despite the contraction in China's economy during the first quarter of 2020, the IMF still projects the economy to grow by 1.2 percent for the year.

For 2021, the IMF predicts China's economy will grow by 9.2 percent, leading all major economies. This puts the growth rate near the ruling Communist Party's goal of doubling 2010 GDP and per capita income levels by 2021 in celebration of the Party's 100th anniversary.

There is already evidence that China's economic activity is coming back with strong PMI (Purchasing Managers' Index) numbers in May and June. While China has abandoned its growth target this year, if the IMF's 2021 projections are correct, China will be making up for lost time next year.

In line with the Made in China 2025 policy we expect continued stimulus to focus on developing new infrastructure, such as 5G networks, NEV charging stations, energy efficiency programs, and other initiatives that will help build China's economy of the future.

If China's stimulus policies are effective, they will not only stabilise the economy in the short-term but help further transition the country towards a high-tech and service-driven economy to set the stage for the coming decade.

Now may be the time to incorporate China A-shares exposure into portfolios and gain exposure to the New Economy.

The VanEck Vectors China New Economy ETF (ASX code: CNEW) is a portfolio of 120 of the most fundamentally sound companies making up China's New Economy. Only VanEck offers a specific China A-shares ETF that allows investors to participate in what may be the next growth phase for domestic China investments.

HEDGING AGAINST UNCERTAINTY WITH GOLD MINERS

In times of real crisis, there are few better investments than gold. The precious metal has been a reliable store of wealth for centuries and a buffer against some of the worst crises in financial history.

While gold has proved its defensive qualities time and time again, professional investors have shied away from it because it generates no income and can therefore be difficult to value.

That is not the case for gold miners that benefit from higher gold prices and lower production costs.

In fact, an exposure to gold miners rather than gold itself has been a preferred way for institutional investors to get exposure to the precious metal's unique qualities.

The response to the COVID-19 pandemic has convinced more investors about the merits of having an exposure to gold.

This is because most of the extreme risk scenarios would, all things being equal, suggest a higher price for gold.

Gold is a proven hedge for both a deflationary – where asset values are falling sharply – and an inflationary environment when purchasing power is being rapidly eroded by rising prices and devalued currencies.

The risks are rising for both outcomes but perhaps the most analogous historic examples are the World War periods when governments increased spending and lowered interest rates. The periods that followed were characterised by high inflation and an erosion in paper wealth, that is, asset values.

Gold is also the investment of choice for those that hold the starkest fear that there may be a loss of confidence in our monetary system. The lessons of history are that financial systems oscillate between trust based paper systems and those backed by gold.

There is a risk that governments and policymakers reach a point of no return and finance spending by printing money, undermines faith in the fiat money system.

The only protection against that is gold and an efficient hedge is to own the world's largest miners of this asset. VanEck Vectors Gold Miners ETF (ASX code: GDX) tracks an index of the world's largest gold miners whose cash flows and valuations rise in line with the gold price and the sentiment that influences it.

TAKING A MEASURED APPROACH TO AUSTRALIAN EQUITIES

Australia's equity market has been one of the top performing share markets this century as the 'lucky country' successfully managed economic tests and enjoyed periods of prosperity.

The COVID-19 pandemic has presented another stern test and while Australia's economy has been challenged, on a relative basis, the nation has managed the crisis well.

Australia has always been cursed with the tyranny of distance but it has proved to be an advantage in fighting and managing pandemics.

Australia is also well placed to respond to the economic crisis. The Commonwealth's relatively low level of government debt means it has more capacity than most to spend money to support the economy.

This resilience lends weight to the argument that an exposure to Australian equities is a sensible long term allocation.

But the companies that have dominated the S&P/ASX 200, specifically the banking sector which equates to roughly 20% of the index, will undoubtedly battle through a period of rising bad debts, weaker profitability and reduced dividends.

A more diverse exposure to Australia's largest companies could therefore benefit investors. A way to do this is through "equal weighting" your Australian equities portfolio. The result is a more diversified portfolio with greater exposure to smaller stocks and less exposure to mega-cap stocks and sectors that dominate the S&P/ASX 200. That is, you reduce your concentration risk.

Given the current market volatility, ensuring you are truly diversified across sectors is more important than ever. As an example, Australia's share market is changing – demonstrated by the increasing number of companies in the information technology sector. In Australia's only equal weight ETF, the VanEck Vectors Australia Equal Weight ETF (ASX code: MVW) tech stocks now represent over 8% of the fund, up from 1.3% five years ago. However an ETF tracking the S&P/ASX 200, despite owning the same names, only has around 3.5% exposure to this emerging sector.

Since its inception in March 2014, MVW has consistently delivered better returns than the market capitalisation approach (i.e. an ETF tracking the S&P/ASX 200 index) and is well positioned to outperform in a recovery. This is because, as academic research has confirmed, 'smaller' stocks have a wider outcome of returns relative to mega-cap stocks. By increasing exposure away from mega-caps through an equal weight strategy, in aggregate, higher returns are captured when markets rise.

If you would like a copy of the aforementioned research, please email info@vaneck.com.au

Beyond the banks

The quest for income in the post COVID-19 world

For decades, Australian banks have been a staple of investors' portfolios. However, the golden era of bank dividends now appears to be behind us. Savvy investors are now finding their income elsewhere.

After three decades of uninterrupted economic prosperity, Australia has well and truly lived up to its billing as the lucky country.

The good fortune has also rewarded savers and investors with the nation's largest banks offering generous interest rates and distributions.

As the banks have fed demand for credit to buy homes and run businesses, the banks have been willing to pay savers a premium to attract their deposit.

Meanwhile a favourable market structure and economic environment has allowed the banks to generate high profits while the dividend imputation regime has encouraged them to distribute a large share of those profits to shareholders.

Australia was well and truly a land of abundant income and investors had little reason to venture overseas for yield.

However, the golden era of Australian banking had well and truly lost its lustre as we headed into 2020.

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In response to weaker growth, the Reserve Bank cut the cash rate to below 1%, squeezing savers. In addition, as has been the experience for global banks, near zero interest rates has had a detrimental impact on bank profits.

Then the COVID-19 crisis hit. The RBA slashed the cash rate and pledged to keep it low well into the future. Australia's banks also stepped up allowing households to defer loan repayments while they braced for rising bad debts from the pending recession.

In times of economic crisis, the first casualty is often those beloved bank dividends. That capital was once set aside to reward shareholders has been called upon to absorb losses and support new lending into the economy during this crisis.

The result is that billions of dollars of income paid by banks to investors, has vanished. When it will return is uncertain at best. Interest rates are destined to remain low while more bank-generated profits may need to be conserved in the years ahead.

However, the desire for income has only increased among the cohort of investors which relied on the banks.

The time is right for investors to explore alternative sources of income. ETFs can provide income solutions that pay more attractive returns than cash or term deposits with different levels of risk, including some that are generating higher returns than bank shares, but with lower risk than equities.

There are several income options available on the ASX that investors may not have considered in the past.

Expanding beyond our borders

Under promise, over-deliver

In the search for yield, many investors have overlooked an important asset class. Yet the data shows it warrants a closer look.

Emerging markets bonds is both a well-established sector within fixed income, and one that has delivered the most reliable returns relative to risk than almost any investment option, including equities.

So why have investors previously shunned emerging markets bonds? There are a number of possible explanations such as a lack of awareness, understanding or simply an inability to access these particular bonds.

There are two compelling reasons why investors should consider allocating to emerging markets bonds.

The first is the returns which have been consistently higher compared to developed market bonds and commensurate with returns from high yield corporate bonds, and even equities, with lower historic risk.

The second reason is that bonds issued by emerging market nations have, in aggregate, become a less risky proposition.

The emerging markets crises of the late 1990s and 2000s forced these nations to take the steps necessary to protect their economies from capital flight.

They have reformed their economies, accumulated a stockpile of foreign currency reserves and reduced overall debt.

In contrast, developed nations have tended to borrow more funds and have shunned structural reform, leaving central banks to drive growth through lower interest rates and returns for bond investors.

The COVID-19 crisis has arguably reduced the economic gap between developed and emerging nations, without reducing the investment return premium.

Emerging market economies are forecast to suffer less of a growth hit from the crisis than developed market economies. This is in keeping with the period after the GFC (Global Financial Crisis) where some emerging markets barely registered a recession.

The compelling investment case for emerging markets bonds, in an environment of low interest rates, is why VanEck launched the world's first actively managed emerging markets bonds exchange traded fund.

The VanEck Emerging Income Opportunities Active ETF (Managed Fund) (ASX code: EBND), targets a yield of 5% per annum paid monthly. Active management is important to help identify and avoid emerging markets that are too risky.

The COVID-19 crisis has not only demonstrated, but also enhanced the relative attractiveness of actively managed emerging markets bonds as a source of income.

Infrastructure and property

Real and durable

In this environment of persistently low interest rates, more and more investors of all sizes have turned to alternative investments in search of reliable sources of income.

The two most established sectors that fit this description and therefore have become asset classes in their own right are international property and global infrastructure.

Rents, tolls and levies tend to be more predictable than corporate earnings, which has made these assets more attractive to cautious income seeking investors in a low rate environment.

However, these sectors found themselves in the eye of the storm when the COVID-19 lockdowns hit as investors questioned the sustainability of rental payments and the decline in usage of seemingly entrenched infrastructure assets.

Market valuations reflected the hit these sectors took, as seen in the benchmark indices FTSE EPRA Nareit Developed ex Australia Rental Index AUD Hedged, which declined by -28.49%, and the FTSE Developed Core Infrastructure 50/50 Hedged into Australian Dollars Index which declined by -20.27% in the March quarter.

What has since emerged is that while some infrastructure and property assets, such as shopping centres and airports, continue to be severely affected by the lockdowns, other assets such as logistics centres and toll-roads have assumed greater economic importance, and therefore value.

The COVID-19 crisis has highlighted the importance of diverse holdings in these key asset classes by region and type – both to protect investor capital and ensure incomes remain reliable.

The volatility has also created an opportunity for investors to gain exposure to the same diverse and reliable cash flows at a lower entry point.

The thesis for investing in global infrastructure assets remains intact. That is, infrastructure offers stable income due to steady cash flows that are often tied to inflation and protected by government regulations. Those returns tend to be un-correlated to mainstream asset classes.

In international property, the large listed REITs (Real Estate Investment Trusts) tend to operate high-quality assets with tenants whose businesses have continued to operate.

ETFs such as the VanEck Vectors FTSE Global Infrastructure (Hedged) ETF (ASX code: IFRA) and the VanEck Vectors FTSE International Property (Hedged) ETF (ASX code: REIT) allow investors to access diversified global portfolios of the largest companies in these asset classes.

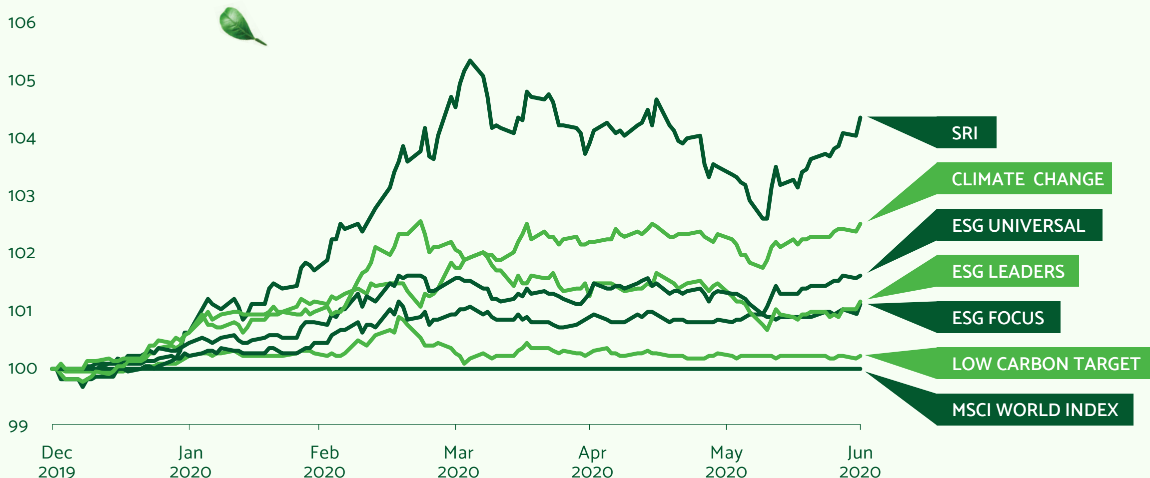
SUSTAINABLE INVESTING MAKES MORE SENSE THAN EVER

During the darkest days of the COVID-19 global lockdown, images and reports of clear skies above oft polluted cities and flourishing wildlife led us to believe that the planet may have finally been given a chance to heal.

Time will tell if the pandemic crisis will have a lasting positive effect on the environment, but it has certainly forced a rethink about the role and responsibilities of large corporations in society.

And one couldn't help but wonder if the markets were sending a message themselves, as Environmental, Social and Governance (ESG) and Socially Responsible Investment (SRI) strategies came into their own during the COVID-19 pandemic.

In the first half of 2020 ESG focused indices materially outperformed the broader MSCI World Index.



Source: MSCI. Rebased to 100. Past performance is not a reliable indicator of future performance.

There is an acute awareness that the rewards for being a good corporate citizen are greater than ever, while the costs for failing to do so are more severe.

There are specific reasons that have contributed to the strong performance of ESG focused funds and indices, other than an 'invisible hand' of altruism.

For instance ESG indices tend to have a larger weighting to technology stocks – that naturally have low carbon emissions – which are set to become more entrenched in the post lock-down environment.

Meanwhile the plunge in the oil price also aided ESG funds on a relative basis. While falling energy prices were related to the pandemic, rising geopolitical tensions between major oil producers further exacerbated the fall.

These short term factors have been supportive for ESG and SRI thematic approaches through the COVID-19 crisis.

But there are also structural forces that will accelerate and could enhance the benefits of incorporating ESG and SRI in selecting stocks well into the future.

The COVID-19 crisis has required a closer collaboration between the private and the public sector, which has done much in its power to support large corporations through wage subsidies and central bank corporate debt purchases.

In turn, many companies have joined the response by ramping up the manufacturing of key supplies. The healthcare sector is racing to meet supply demands for equipment and treatments, while searching for a vaccine.

Across industries, many market-leading companies have prioritised the safety of their employees, the needs of their customers and looked to help the broader community navigate the crisis.

So, as expectations change and the public and private sector becomes more intertwined, the importance of ESG will increase.

The strong showing of ESG indices has all but put an end to the debate that there is a cost involved in investing in an ethically minded way.

If anything, there is a benefit in avoiding companies that have a higher chance of becoming the subject of a value-destructive scandal.

ESG and SRI funds have well and truly entered the mainstream. The question is, what is the most efficient and cost effective way to achieve the dual goals of investing responsibly while creating wealth?

The rise of ESG has been touted as the saviour of active management. That is, so the argument goes, because the extensive analysis in assessing ESG strengths and weaknesses cannot be systematised at low cost. ESG and SRI investing reflects societal values that are ever shifting and cannot be captured in numbers.

However, that's where index innovation comes to the fore. VanEck has partnered with index provider MSCI to create state-of-the-art indices that utilise MSCI's ESG capability. MSCI has a team of over 200 analysts worldwide assessing all of the stocks in its global universe on a 'AAA' to 'CCC' scale according to their exposure to industry specific ESG risks and their ability to manage those risks relative to their peers.

This has resulted in low-cost passive ETFs that allow investors to incorporate both values-based and ESG considerations, backed by deep ESG research, into their investment portfolio.

Screening out poorly governed companies with little regard for the environment and society, while allocating towards well governed responsible companies, has shown to be an effective risk management strategy.

An example of the process in action is the VanEck Vectors MSCI International Sustainable Equity ETF (ASX code: ESGI). ESGI's largest holding is Microsoft, which has a high AAA MSCI ESG rating. That compares to a BBB rating for Facebook, which has never been in ESGI, and has recently again been embroiled in controversy for its failure to prevent hate-groups from using the social media platform. While an increasing number of advertisers boycott Facebook, Microsoft has stayed out of the headlines and returned over 32 per cent for investors so far this year[1].

Incorporate MSCI's world-leading ESG research in your portfolio via the VanEck Vectors MSCI International Sustainable Equity ETF (ASX code: ESGI) or the VanEck Vectors MSCI Australian Sustainable Equity ETF (ASX code: GRNV).

1. As at 30 June 2020.

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A world of QUALity is within your reach

VanEck Vectors MSCI World ex Australia Quality ETF

Now you can gain exposure to 300 quality international stocks in a single trade on ASX.
Holdings are selected for their quality fundamentals and include Apple, Johnson & Johnson and Google.

Performance of QUAL to 30 June 2020

	1 Year (%)	3 Years (% p.a.)	5 Years (% p.a.)	Since inception* (% p.a.)
VanEck Vectors MSCI World ex Australia Quality ETF (QUAL)	16.81	17.18	13.97	16.11
MSCI World ex Australia Index	5.18	10.75	9.36	11.98
Difference	**+11.63**	**+6.43**	**+4.61**	**+4.13**

Learn more at vaneck.com.au or speak to your financial adviser or stock broker today.

Indexed to

ASX CODE:
QUAL

A$ hedged
ASX CODE:
QHAL

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The table above shows past performance of QUAL and the MSCI World ex Australia Index. *'Since inception' date is 29 October 2014. Source: VanEck, Morningstar Direct. Results are calculated daily to the last business day of the stated period and assume immediate reinvestment of distributions. QUAL results are net of fees and other costs incurred in the fund but before brokerage fees or bid/ask spreads incurred when investors buy/sell on the ASX. Past performance is not a reliable indicator of future performance. VanEck Investments Limited. ABN 22 146 596 116 AFSL 416755 is the responsible entity and issuer of QUAL and QHAL. This is general advice only about financial products and is not personal financial advice. You need to consider your own financial circumstances, needs and objectives before making an investment decision. All investments carry some level of risk. Speak to a financial adviser and read the PDS which details the key benefits and risks and is available at vaneck.com.au or by calling 1300 68 38 37. QUAL and QHAL are not sponsored, endorsed or promoted by MSCI. The PDS contains more details about the risks and the limited relationship between MSCI and VanEck.