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The 2025 ETF Investor's Guide

Trends, insights and opportunities to shape your investing

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Introduction

As we move into 2025, investors face concentrated equity markets at all-time highs, elevated government bond yields and political uncertainty.

Investing success this year will require careful navigation across three core investment areas: core equities, fixed income and satellite opportunities.

In this guide, we discuss key market themes for the year and consider **10 investment opportunities** to help investors navigate them, from broadening equity exposure and enhancing yield potential to structural growth themes and defensive opportunities.

Whether seeking growth, income or diversification, these 10 opportunities offer multiple paths forward in an evolving market environment.

Off to a stellar year... where next?

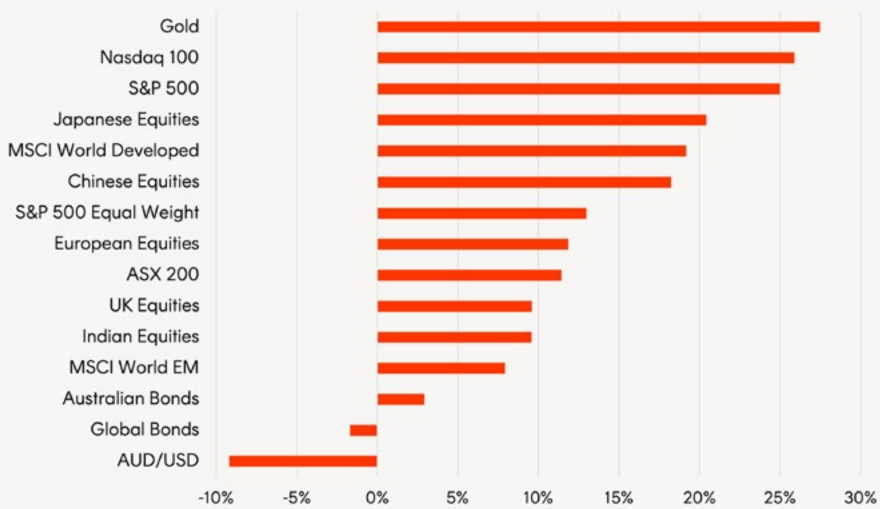
For many investors– particularly those holding equities – 2024 was a great year.

The US S&P 500 and the S&P/ASX 200 indices both performed strongly, with total returns of 25% and 11.4% respectively. Much of these high returns were driven by continued momentum in a narrow band of winners, particularly the 'Magnificent 7' in the US and the banks in Australia.

Credit and the USD also performed well, with the USD providing even greater returns for those Australian investors holding unhedged global assets. While government bond returns were muted and many commodities were soft, gold beat even US equities. As for bitcoin, it was off the charts.

Growth assets responded positively as a 'Goldilocks' scenario – of falling inflation and resilient economic growth – played out, particularly in the US. While diversified portfolios did well in 2024, that was a result of the strong contribution of equities. On the other hand, bonds provided little in terms of returns or diversification.

2024 major asset class returns in local currency terms



Source: Bloomberg. Returns from 31 December 2023 to 31 December 2024 in local currencies. Gold = XAU BGN Currency Index, Chinese equities = CSI 300 Index, UK Equities = FTSE 100, Japanese Equities = Topix Index, Indian Equities = Sensex Index, European Equities = Eurostoxx Index, Australian Bonds = BACM0 Index, Global Bonds = LEGATRUU Index, AUD/USD = Australian and US Dollar exchange rate. You cannot invest directly in an index. Past performance is not an indicator of future performance.

So what's ahead in 2025? This year the starting point is quite different: equity markets are more concentrated and, at a headline level, indices look more expensive and government bond yields are higher.

Nevertheless, an improved economic outlook bodes well for those investors who know where to look.

The 10 trends to guide your ETF investments in 2025

Core equities

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Core equities

The core of your investment portfolio is the group of investments that serve as the foundation of your portfolio, able to help you build wealth over the long term.

Your core investments should give you exposure to a range of asset classes, both Australian and international as well as growth and defensive. They should offer broad-based, diversified exposure, and be cost-effective.

1

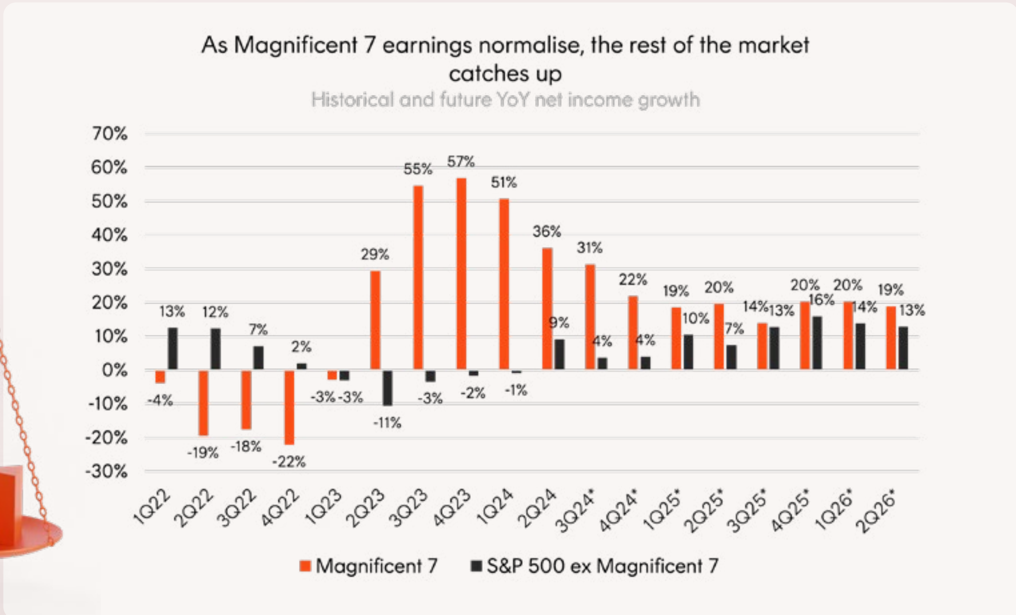
A broadening out of US equity market performance

The narrative that has dominated global equity markets over the last few years has been the rise of artificial intelligence and the 'Magnificent 7' – namely Amazon, Meta, Apple, Alphabet, Microsoft, Tesla and Nvidia – while locally the story has been the tear that Westpac, CBA and the other banks enjoyed over 2024.

The dominance of these small groups of stocks over their respective indices has important implications for investment portfolios. For investors, it raises the question of where to from here in 2025, given the risks from the growing concentration in markets.

ASX: QUS

The Betashares S&P 500 Equal Weight ETF (ASX: QUS) offers a cost-effective exposure to 500 leading US companies using an equal weight approach. The S&P 500 Equal Weight index arguably presents a "cheaper" entry point for US equities[1] and is forecast to see strong earnings momentum in 2025[2].



Source: Bloomberg intelligence. As at 11 January 2024. Magnificent 7 includes AAPL, AMZN, GOOG, GOOGL, META, MSFT, NVDA and TSLA. Figures for 4Q 2024 onwards are analyst consensus forecasts. Actual results may differ materially from forecasts.

[1] Compared to the market cap weighted S&P 500 index and based on current valuations.
[2] Source: Bloomberg intelligence. Based on consensus analyst forecasts. Actual results may differ materially from forecasts.

It's also an exposure which is arguably more favoured by Trump's proposed policy changes:

- The largest two sector weights, US Financials and Industrials, are likely to enjoy increased profitability due to deregulation for financials, and possible increased tariffs on overseas competitors and support for US manufacturing for industrials.
- The proportion of total revenues sourced from the US is about 70% for the Equal Weight index, much higher than the market cap weighted S&P 500. Large offshore earners like Apple are most exposed to a stronger USD eroding earnings or potential blow back from Trump's possible tariffs. Goldman Sachs research recently highlighted the negative correlation between broad dollar strength and S&P 500 earnings surprise.
- Domestically oriented US companies, which have a greater representation in the Equal Weight index, also generally tend to pay more tax,[3] making them bigger beneficiaries of Trump's proposed corporate tax cuts.

ASX: HQUS

HQUS is currency-hedged to the Australian dollar, which seeks to minimise the effect of currency fluctuations on returns. The fund currently obtains its investment exposure by investing in the **Betashares S&P 500 Equal Weight ETF**, with the foreign currency exposure hedged back to the Australian dollar.

2

Australian quality – earning the title

While concern remains for the earnings outlook of Australia's large caps and the broader index, investors can still find growth opportunities in our market.

Financials and Materials are two inherently cyclical sectors which, fortunately for investors, have tended to find themselves at opposite ends of their respective cycles. However, with the prospect of synchronised underwhelming returns from both banks and miners, investors should consider how they can reduce cyclicality in their portfolios. To that end, investing in a diversified exposure to high quality Australian large and mid-cap companies that have strong profitability, more consistent earnings and lower financial leverage may be additive to portfolios.

Last financial year, the companies in the Solactive Australia Quality Select Index, which the **Betashares Australian Quality ETF (ASX: AQLT)** aims to track, experienced earnings growth of 20% compared to a fall of 4.6% for the S&P/ASX 200. AQLT returned 23% last year net of fees, more than doubling the return of the broader S&P/ASX 200 index.[4]

ASX: AQLT

ASX: AQLT provides a transparent and cost-effective way for investors to gain exposure to a diversified portfolio of 40 quality Australian companies that have the potential to sustain high returns on equity over the long-term.

As earnings yields have fallen in Australia, so too have dividends

Source: Bloomberg. May 2000 to December 2024. As at 31 December 2024.
Past performance is not indicative of future performance.

[3] Source: OECD, Base Erosions and Profit Shifting, OECD Policy Issues website.
[4] Past performance is not indicative of future performance.

3

Making up for falling dividends

For many years Australian equities had provided consistently strong and growing dividend income. Recently that has changed, leaving investors reliant on dividend income in the lurch.

For those seeking to make up for lost equity income, **Betashares Australian Top 20 Equity Yield Maximiser Fund (managed fund) (ASX: YMAX)** had a distribution yield of 7.0% last year, or 8.4% grossed up for franking credits, versus the S&P/ASX200 gross yield of only 4.5% (3.5% net). [5]

YMAX uses a covered call strategy to generate additional income from option premiums on top of the underlying dividends received. Such a strategy is best suited to neutral (or sideways trading) markets to gradually rising markets, as it does provide some upside participation to capital growth and growing dividends. However, it would usually be expected to underperform an equivalent portfolio without a covered call strategy during a strongly rising market.

For more information on how covered call strategies work and how they are employed in our Yield Maximiser funds, please read this brochure.

ASX: YMAX

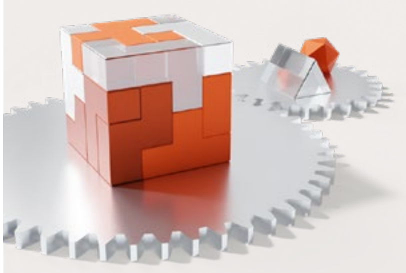
ASX: YMAX aims to generate attractive quarterly income and reduce the volatility of portfolio returns by implementing an equity income investment strategy over a portfolio of the 20 largest blue-chip shares listed on the ASX. YMAX does not aim to track an index.

4

Making the most of invested capital

A concern for many investors is the risk of not building up enough capital to buy a house or retire comfortably.

Gearing can be an effective wealth creation tool by enabling you to make a larger investment in the share market than your available capital would otherwise allow and, in doing so, take advantage of compounding from an earlier point in time.



ASX: GHHF

Betashares Wealth Builder Diversified All Growth Geared (30-40% LVR) Complex ETF (ASX: GHHF) provides investors a simple all-in-one access point to a 'moderately' geared portfolio of more than 4,000 Australian, global developed and emerging market equities. GHHF can be a powerful tool for investors seeking to build long term wealth through a greater exposure to diversified global equities than one's available level of capital would allow for.

Other ETFs in the Betashares Wealth Builder range include:

ASX: G200

Betashares Wealth Builder Australia 200 Geared (30-40% LVR) Complex ETF (ASX: G200)

ASX: GNDQ

Betashares Wealth Builder Nasdaq 100 Geared (30-40% LVR) Complex ETF (ASX: GNDQ)

With one easy trade on the ASX, investors can unlock the power of gearing with exposure to a portfolio of Australian and global stocks without the hassle of complicated loan applications.

> Gearing magnifies gains and losses and may not be a suitable strategy for all investors. Geared investments involve significantly higher risk than non-geared investments. Investors in geared strategies should be willing to accept higher levels of investment volatility and potentially large moves (both up and down) in the value of their investment.

[5] Yield is calculated by summing the prior 12-month per unit distributions divided by the closing NAV per unit at the end of the relevant period. Yield will vary and may be lower at time of investment. Past performance is not indicative of future performance.

Fixed income

With global equity markets coming off strong consecutive years and valuations still appearing stretched, the case for adding bonds as portfolio insurance has strengthened.

The high bond yields to start 2025 suggest that long-term bonds are poised to rally in response to any negative surprises in US or global growth. Furthermore, the improved value of duration now offers investors an opportunity to be rewarded for holding traditional safe havens.

5

Credit where it's due

Longer maturity Australian corporate bonds can offer investors defensive properties through their higher duration, or sensitivity to changes in interest rate expectations, while also providing investors with higher income than government bond equivalents.

With the expected dividend yield of the S&P/ASX 200 falling to 3.5% for the next 12 months, investors looking for alternative sources of income could look to corporate bonds which typically offer higher income than the equity market and lower volatility.

Betashares Australian Investment Grade Corporate Bond ETF (ASX: CRED) holds a diversified portfolio of Australian investment grade corporate bonds offering investors the potential for both equity market diversification and high income. CRED pays monthly distributions to investors and has a yield to maturity of 5.69% (as at 17 January 2025).[6]

ASX: CRED

ASX: CRED provides intelligent exposure to a portfolio of senior, fixed-rate, investment grade Australian corporate bonds.

6

Cash ain't trash

Notwithstanding the promising outlook for bonds, in an era of growing policy and economic uncertainty, complete with both left and right-tail risks (i.e. growth and inflation respectively), cash can provide optionality and tactical flexibility not found elsewhere, and if cash rates remain around 3-4%, can also remain a viable, stable source of income.

Betashares Australian Cash Plus Fund (managed fund) (ASX: MMKT) has been designed to be a core cash allocation in investment portfolios, providing enhanced yield from cash and money market securities, paid monthly, together with a high degree of capital stability. In 2024, MMKT returned 4.87% net of fees for investors.

ASX: MMKT

ASX: MMKT provides exposure to a portfolio of Australian dollar cash and short-term money market securities issued by investment grade entities.

[6] Yield will vary and may be lower at time of investment. Yield to maturity refers to the annualised total expected return of a bond if it is held to maturity, the bond does not default, and the coupons are reinvested at the yield to maturity (YTM). CRED's YTM is the weighted average of its underlying bonds' YTMs.

Beyond the core: growth opportunities

While core allocations serve as the bulk of investor portfolios, the value add from satellite positions, often smaller tactical positions in areas with structural growth opportunities, should not be overlooked.

Satellites positions can be used by investors to leverage opportunities for outperformance over broader market exposures, access tactical and long-term structural growth themes or sectors, provide diversification benefits to portfolios, and hedge against possible tail risk events.

7

Navigating an evolving threat landscape

Cybersecurity remains a critical need in today's society as advanced technologies such as AI expand the attack surface area for adversaries to act upon. As a result, organisations globally have recognised the importance of developing strong security software systems in a geopolitically fragmented world that has only intensified the threat environment.

We see evidence of this with double digit spending growth on security software, which is expected to exceed US$260b[7] in 2025. This backdrop will likely support earnings for established cybersecurity companies with leading-edge product offerings such as CrowdStrike and Palo Alto which are both key holdings in **Betashares Global Cybersecurity ETF (ASX:HACK).**

ASX: HACK In one trade, get diversified, cost-effective exposure to global cybersecurity companies.

[7]Source: https://www.wsj.com/tech/cybersecurity/typhoon-china-hackers-military-weapons-97d4ef95

8

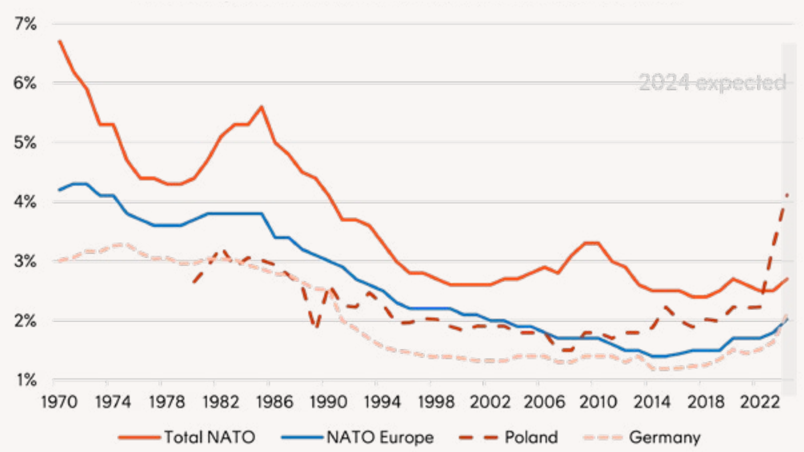
Geopolitical risk and defence

Defence spending has been accelerating globally since Russia's occupation of Crimea in 2014, and the full-scale invasion of Ukraine only furthered this trend.

2024 is expected to be the 10th consecutive year that defence spending increased, reaching a new record of over $US2.5t. The trend towards deglobalisation is spurring a wave of self-sufficiency across essential industries of which defence is a key part.

Defence expenditure is expected to continue to accelerate as European NATO members come under pressure

Defence expenditure as a % of GDP for NATO and select members



Source: NATO. 1970 to 2024. 2024 numbers are NATO estimates.

Further, Trump will likely look to broker major contracts for defence exports to balance trade with allies while promoting 'America first' through the US' world leading defence industry. Talks have already begun with Taiwan for a US$15bn deal for US military hardware. For context, during the Biden administration a total of $US7bn of deals were approved with Taiwan.

Betashares Global Defence ETF (ASX: ARMR) offers investors exposure to leading companies involved in the global defence sector. With strong fundamentals momentum and record levels of order books for the largest defence companies, they remain well placed for future growth.

ASX: ARMR

ASX: ARMR provides exposure to up to 60 leading companies which derive more than 50% of their revenues from the development and manufacturing of military and defence equipment, as well as defence technology.

9

Emerging giant

We see India's recent economic slowdown as temporary and expect it to be corrected through the course of 2025. Government spending is expected to pick back up after a typical election year slowdown and already healthy domestic demand from consumers and the private sector should receive a further boost as inflation continues to normalise. The recent selloff could be a compelling opportunity for investors to add to long-term strategic positions in the region.

Within India, taking a quality investment approach can resolve common shortcomings of investing in the region, like avoiding top-heavy Indian broad market index exposures concentrated in large banks, avoiding speculative or unprofitable companies with high levels of risk, and failing to capture companies with strong fundamental growth prospects.

ASX: IIND

Investors can gain exposure to a portfolio of high-quality Indian companies through **Betashares India Quality ETF (ASX: IIND).**

10

Go for gold

In a period of escalating geopolitical tension, gold provides some unique characteristics to diversify risk embedded in other asset classes. As a reliable store of value, holding gold is important for central banks to diversify their reserves beyond foreign currencies like the USD and US Treasuries.

In the wake of the Ukraine invasion, the US showed they were not afraid to 'weaponise' the dollar-centric global financial system by imposing crippling sanctions on another nation state. As the world's reserve currency, the USD gives the United States enormous leverage on the world stage.

In response to this threat, the central banks of countries that wish to remain non-aligned or independent of the US have become huge buyers of gold in recent years. Since 2022, total reported central bank buying has jumped significantly thanks to Emerging Market and Eastern European countries like China, India, Poland, Turkey and Egypt.

If the deficit widens further under the new US administration, concerns around the serviceability of US government debt may blow out Treasury yields and weaken the US dollar. Historically, there has been a strong correlation between rising US budget deficits and gold prices. Alternatively, a growth scare or pick-up in inflation is also an environment where gold can act as a defensive ballast.

As the only currency hedged gold ETF available on the ASX, **Betashares Gold Bullion ETF – Currency Hedged (ASX: QAU)** offers a truer exposure to the USD gold price.

ASX: QAU

ASX: QAU is backed by physical gold bullion and aims to track the performance of the price of gold, hedged for currency movements in the AUD/USD exchange rate (before fees and expenses).

Takeaways

As markets continue to evolve, the key to success lies in maintaining a balanced approach while staying alert to new opportunities. The 10 investment themes we've highlighted offer various ways to enhance portfolios, whether seeking growth, income or defensive characteristics.

By carefully considering these opportunities within the context of the current market environment and their investment goals, investors can build portfolios designed to weather various market conditions while positioning for long-term success.

The evolution of ETFs has made these opportunities more accessible than ever before, allowing investors to implement sophisticated strategies that were once the domain of institutional investors.

Whether it's gaining exposure to a broader set of US companies, gaining exposure to moderate gearing through our Wealth Builder range, or capturing emerging themes in cybersecurity and defence, investors have a wide range of tools to build diversified portfolios aligned with their objectives.

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This report was prepared with the input and oversight of the Betashares Investment Strategy and Research Group.

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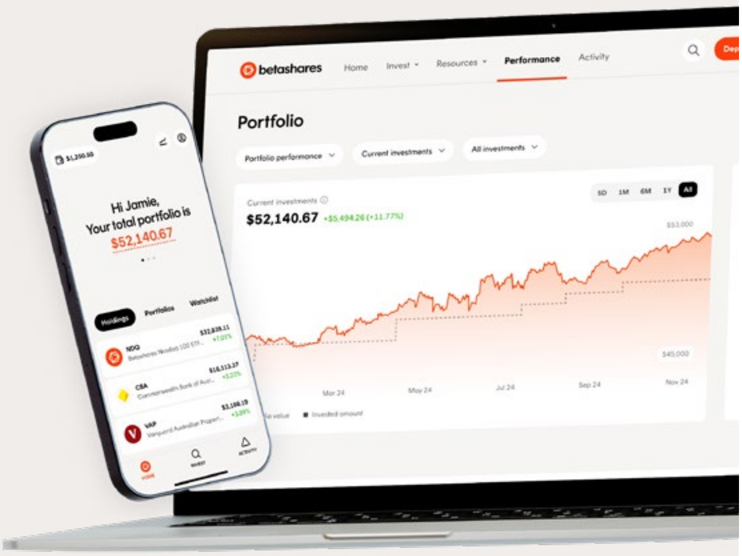

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