Prospects Improve For European Equity ETFs

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Summary of Q2 2017 ETF Flows and Trends

- Estimated net inflows for US-listed exchange-traded funds (ETFs) totaled $111 billion in Q2 2017, marking the third straight quarter in which asset net inflows were greater than $100 billion.
- Estimated net inflows for US Equity ETFs slowed from $43.6 billion in Q1 to $16 billion in Q2, while sector equity ETFs faced $92 million in estimated net outflows in Q2, compared to $19 billion in estimated net inflows in Q1.
- International Equity ETFs received the greatest level of estimated net inflows in Q2, with $57 billion. This was a further acceleration from Q1, in which the International Equity ETFs received $33.5 billion.
- Taxable Bond ETFs received $33.7 billion in estimated net inflows in Q2, nearly the same level of estimated net inflows as in Q1. Estimated net inflows for Municipal Bond ETFs totaled $1.4 billion in Q2, more than double the level of estimated net inflows from Q1.
- Both Commodities ETFs and Alternatives ETFs received estimated net inflows for the second straight quarter in Q2, totaling $0.9 billion and $1.7 billion, respectively.

Table 1

US Category Group	Total US-Listed ETF Assets (6/30/17)	Q2 2017 Estimated Net Asset Flows	Previous Quarter Estimated Net Asset Flows (Q1 2017)
Allocation	$11,250,536,286	$623,688,982	$165,280,960
Alternative	$45,183,119,219	$1,747,071,912	$1,624,987,969
Commodities	$63,959,440,166	$865,589,225	$1,050,371,016
International Equity	$608,627,369,363	$57,010,192,722	$33,509,548,672
Municipal Bond	$26,542,133,630	$1,456,905,230	$718,131,483
Sector Equity	$432,155,455,936	($91,513,225)	$19,231,078,207
Taxable Bond	$497,459,301,983	$33,702,529,281	$33,856,537,694
US Equity	$1,294,175,174,619	$16,128,721,138	$43,547,266,704
Total	$2,979,352,531,202	$111,443,185,265	$133,703,202,705

Source: Morningstar, as of 6/30/17. Includes all US-listed exchange-traded funds, exchange-traded notes and other exchange-traded products. All net inflow and outflow numbers are estimates based on information provided by Morningstar.

European equity ETFs received net inflows for the second straight quarter in 2017, totaling $12.6 billion in Q2.[1] In contrast, these funds faced four quarters of net outflows in 2016, totaling $27.8 billion.

We believe the prospects for European equities remain attractive, and may strengthen in the coming months, fueled by decreased concerns about political instability within the European Union, potential increases in consumer spending and business investment, and relatively attractive valuations.

Anti-European Union Anxieties Assuaged

For those concerned about a potential erosion of the political and monetary unity of the European Union (EU) in the wake of Brexit (UK citizens voted to leave the EU on June 23, 2016), the election of French President Emmanuel Macron likely alleviated some distress. In May, the centrist Macron defeated his opponent, Marine Le Pen, who had pledged to renegotiate France's relationship to the European Union if elected.[2] In June, Macron's position was further strengthened as his centrist coalition won a majority in the parliamentary elections. As one of Europe's largest economies, we believe political stability in France may help foster economic growth in the region.

Consumers in Position to Potentially Increase Spending

We believe consumers in Europe may be poised to increase spending in the coming months, as consumer confidence approaches new highs, unemployment trends lower, and inflation returns to normal levels.

In June, the European Commission (EC) Consumer Confidence Indicator for the European Union reached its second highest level since the summer of 2007. Within this survey, participants assessed the current financial situation of their households more positively than any time in the survey's 32-year history (See Chart 1). Moreover, since peaking at 11% in early 2013, the EU unemployment rate has gradually improved, reaching 7.8% in May. For context, the average EU unemployment rate since January of 2000 has been approximately 9% (See Chart 2). Finally, while year-over-year inflation has accelerated in 2017 from the anemic 0.3% average from 2014-2016, we do not believe inflationary pressures are strong enough to dampen consumer spending, as inflation is in line with the 1.8% average over the past 20 years (See Chart 3 on the next page).

Chart 1*
■ EC Consumer Confidence Indicator (Left Axis)
■ EC Consumer Confidence Current Financial Situation of Households (Right Axis)
(European Union) (3/00 - 6/17)

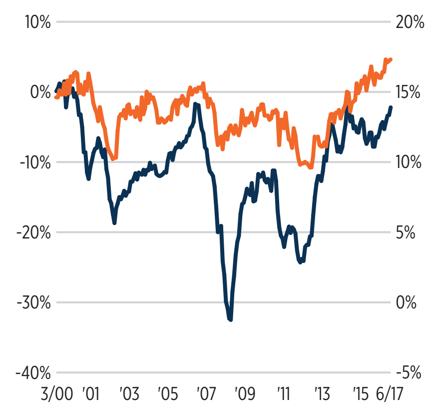
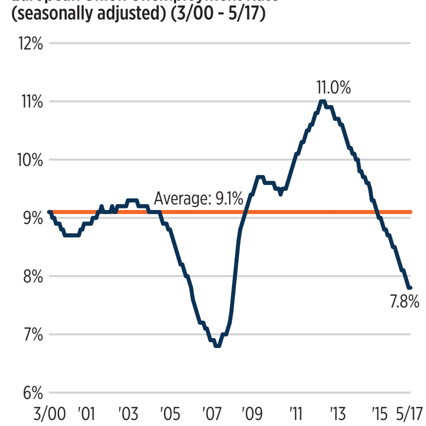


Chart 2*
European Union Unemployment Rate
(seasonally adjusted) (3/00 - 5/17)



Business Investment May Fuel Growth

In our opinion, high levels of business confidence, above average capacity utilization, and low interest rates may fuel increased investment on the part of businesses in Europe.

In June, the EC Industrial Confidence Indicator reached its highest level in over six years, while the EC Construction Confidence Indicator reached its highest level since January of 2008 (Chart 4). Meanwhile, Capacity Utilization reached 82.4% in Q2, the highest level measured since Q3 of 2008 (Chart 5). Together, we believe these data points signal both the need for businesses to invest, as well as the confidence to do so. Lastly, interest rates remain near historic lows for European corporations needing to invest. Per the European Central Bank (ECB), the average interest rate for loans greater than €1 million to non-financial corporations was 1.67% in May (Chart 6).

Relatively Attractive Valuations for European Equities

In addition to the favorable macroeconomic conditions discussed above, we believe valuations for European equities relative to other developed markets may provide an attractive opportunity for investors. As of 6/30/17, the price/earnings ratio (based on 2017 earnings) for the MSCI Europe Index was 15.5, compared to 17.4 for the Nikkei 225, and 18.6 for the S&P 500 Index. The price/book ratio for the MSCI Europe Index was 1.8, compared to 1.8 for the Nikkei 225, and 3.1 for the S&P 500 Index.

Considerations for Selecting a European Equity ETF

As ETF investors assess various options to gain exposure to European equities, we believe that two of the most important considerations should be:

1. How stocks are selected, and
2. Whether currency exposure is hedged.

To Hedge or Not to Hedge?

Over the past few years, investors have become acutely aware of the impact that fluctuations in currency exchange rates can have on the returns of international equities. For example, as the value of the Euro fell relative to the US Dollar (USD) in 2014-2015, the MSCI Europe Index produced a 16.9% cumulative total return in Euros, but a -7.9% cumulative total return in US Dollars. On the other hand, during the first half of 2017, as the Euro strengthened versus the USD, the MSCI Europe Index produced a 7.1% total return in Euros, but a 15.9% total return in US Dollars.

To mitigate the impact of fluctuating currency exchange rates, several ETF providers have launched currency-hedged ETFs over the past few years. While these ETFs have often outperformed when foreign currencies have depreciated relative to the USD, hedges on currency may also have a negative impact on returns for US investors when foreign currencies are appreciating. The choice between hedging, or not hedging, currency exposure is significant.

The First Trust Riverfront Dynamic International ETFs provide an alternative to both currency-hedged and unhedged international ETFs, which either do not protect against currency risk or are statically hedged. These professionally managed funds apply an active, dynamic approach to currency exposure, which can range from fully hedged to fully unhedged as conditions warrant. For example, while the First Trust Riverfront Dynamic Europe ETF (RFEU) was fully unhedged as of 6/30/17 maximizing foreign currency exposure, the fund's selective use of currency hedging has contributed to its outperformance relative to the MSCI Europe Index, in terms of both Euros and US Dollars, since its inception on April 13, 2016.

A dynamic approach to currency hedging within an ETF may also be more tax-efficient than trading between multiple currency-hedged and unhedged international ETFs. While the former approach realizes gains or losses from currency hedges as they are applied or removed within an ETF, the latter entails selling shares of one ETF and then buying shares of another ETF, realizing potential gains or losses generated by both currency hedges as well as underlying equities, even though both ETFs may have similar, if not identical, equity portfolios.

The Importance of Portfolio Construction

In our opinion, the methodology by which an ETF's portfolio is constructed may be the single most important consideration for investors. While most Europe ETF assets are invested in funds that track market-cap weighted benchmark indexes, others utilize different factors to construct portfolios. For example, the First Trust Europe AlphaDEX® Fund (FEP) employs the AlphaDEX® methodology to select a portfolio of 200 stocks, seeking a combination of attractive valuations and strong momentum, factors we believe may enhance risk-adjusted returns.

Chart 3*
■ European Union HICP Index (year-over-year)
■ Average 1997-6/17: 1.8%
■ Average 2014-2016: 0.3%
(1/97 - 6/17)

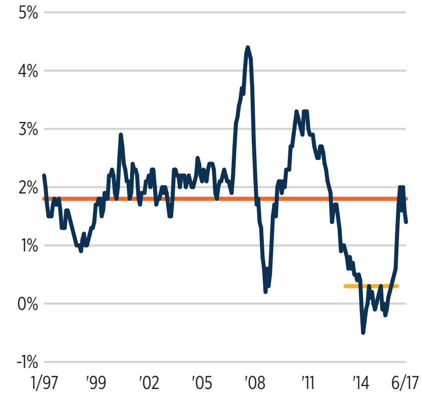


Chart 4*
■ EC Industrial Confidence Indicator
■ EC Construction Confidence Indicator
(European Union) (9/00-6/17)

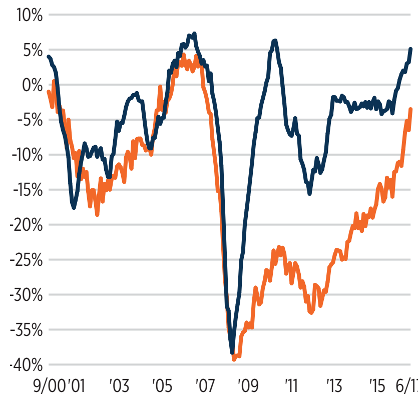
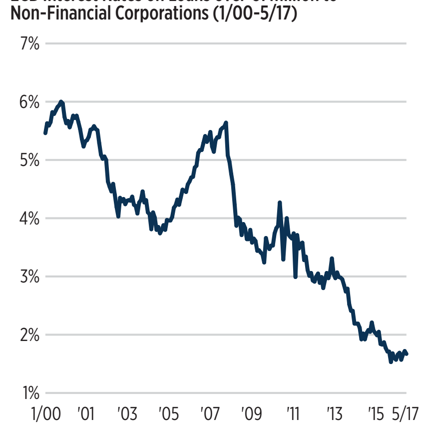


Chart 5*
EC Capacity Utilization (European Union) (3/00-6/17)

Chart 6*
ECB Interest Rates on Loans over €1 million to Non-Financial Corporations (1/00-5/17)



Past performance is not a guarantee of future results and there is no assurance the events or improvements mentioned herein will continue.

In the current environment, another important benefit of FEP is that it tends to underweight European exporters relative to market cap weighted benchmarks. In 2016, FEP's underlying portfolio generated approximately 35% of revenue outside of Europe, compared to 45% for the MSCI Europe Index.[3] This may be significant if the Euro continues to trend higher, as revenues generated overseas could be weaker when converted back to Euros from a foreign currency. However, if the Euro weakens, the opposite could also be true.

European equities had a relatively strong start to 2017, following a lackluster 2016. We believe the region remains attractive going forward, given the political and macroeconomic trends discussed above (calming of geopolitical concerns about the European Union, historically low interest rates, and growing confidence on the part of consumers and businesses), combined with relatively cheap valuations.

In our opinion, ETF investors may benefit from broad exposure to European stocks, however, we believe that some of the best opportunities may be found outside of the largest weightings of market-cap weighted benchmark indexes. Many of these stocks are more prominent in both FEP and RFEU. For investors desiring a long-term strategy to manage currency risk, we believe RFEU is a more efficient option than trading between currency hedged, and unhedged Europe ETFs.

In addition to the ETFs mentioned above, investment advisors seeking narrower exposure to Europe may consider the First Trust Eurozone AlphaDEX® ETF (FEUZ), which excludes countries outside of the Euro currency block, as well as single country funds including: the First Trust Germany AlphaDEX® Fund (FGM), the First Trust Switzerland AlphaDEX® Fund (FSZ), and the First Trust United Kingdom AlphaDEX® Fund (FKU).

[1]Morningstar is the data source for all ETF flows data discussed in this report.

[2]Cabrera, Michael. "France's Le Pen says the EU 'will die', globalists to be defeated." Reuters, March 26, 2017.

[3]Factset.

*Source for Charts 1-6: Bloomberg.

You should consider a fund's investment objectives, risks, and charges and expenses carefully before investing. Contact First Trust Portfolios L.P. at 1-800-621-1675 or visit www.ftportfolios.com to obtain a prospectus or summary prospectus which contains this and other information about a fund. The prospectus or summary prospectus should be read carefully before investing.

ETF Characteristics

An index fund's return may not match the return of the applicable index. Securities held by a fund will generally not be bought or sold in response to market fluctuations.

Investors buying or selling fund shares on the secondary market may incur customary brokerage commissions. Market prices may differ to some degree from the net asset value of the shares. Investors who sell fund shares may receive less than the share's net asset value. Shares may be sold throughout the day on the exchange through any brokerage account. However, unlike mutual funds, shares may only be redeemed directly from a fund by authorized participants, in very large creation/redemption units. If the fund's authorized participants are unable to proceed with creation/redemption orders and no other authorized participant is able to step forward to create or redeem, fund shares may trade at a discount to the fund's net asset value and possibly face delisting.

Risk Considerations

A fund's shares will change in value, and you could lose money by investing in a fund. One of the principal risks of investing in a fund is market risk. Market risk is the risk that a particular security owned by a fund, fund shares or securities in general may fall in value. Actively managed funds are subject to management risk. In managing a fund's investment portfolio, the advisor or sub-advisor will apply investment techniques and risk analyses that may not have the desired result. There can be no guarantee that a fund will meet its investment objective.

A fund may invest in securities issued by companies concentrated in a particular industry or country. A fund may invest in small capitalization and mid capitalization companies. Such companies may experience greater price volatility than larger, more established companies. An investment in a fund concentrated in a single country or region may be subject to greater risks of adverse events and may experience greater volatility than a fund that is more broadly diversified geographically.

An investment in a fund containing securities of non-U.S. issuers is subject to additional risks, including currency fluctuations, political risks, withholding, the lack of adequate financial information, and exchange control restrictions impacting non-U.S. issuers. These risks may be heightened for securities of companies located in, or with significant operations in, emerging market countries.

A significant number of countries in Europe are member states in the European Union, and the member states no longer control their own monetary policies. In these member states, the authority to direct monetary policies, including money supply and official interest rates for the Euro, is exercised by the European Central Bank. Furthermore, the European sovereign debt crisis has had, and continues to have, a significant negative impact on the economies of certain European countries and their future economic outlooks.

A fund may invest in depositary receipts which may be less liquid than the underlying shares in their primary trading market. A fund may effect a portion of creations and redemptions for cash, rather than in-kind securities. As a result, a fund may be less tax-efficient.

Large inflows and outflows may impact a fund's market exposure for limited periods of time.

RFEU may invest in Business Development Companies (BDCs) which may carry risks similar to those of a private equity or venture capital fund. BDCs are not redeemable at the option of the shareholder and they may trade in the market at a discount to their net asset value. The BDCs held by the fund may employ the use of leverage through borrowings or the issuance of preferred stock. While leverage often serves to increase the yield of a BDC, this leverage also subjects a BDC to increased risks, including the likelihood of increased volatility and the possibility that a BDC's common share income will fall if the dividend rate of the preferred shares or the interest rate on any borrowings rises.

Illiquid securities involve the risk that the securities will not be able to be sold at the time desired by RFEU or at prices approximately the value at which RFEU is carrying the securities on its books.

RFEU may employ in part a "momentum" or "value" style methodology that emphasizes selecting securities that have had higher recent price performance compared to other securities or that the sub-advisor considers to be undervalued or inexpensive, respectively. Momentum can turn quickly and cause significant variation from other types of investments. And disciplined adherence to a "value" investment mandate can result in significant underperformance relative to overall market indices and other managed investment vehicles that pursue growth or flexible style mandates.

Forward foreign currency exchange contracts involve certain risks, including the risk of failure of the counterparty to perform its obligations under the contract and the risk that the use of forward contracts may not serve as a complete hedge because of an imperfect correlation between movements in the prices of the contracts and the prices of the currencies hedged. Hedging against a decline in the value of a currency does not eliminate fluctuations in the value of a portfolio security traded in that currency or prevent a loss if the value of the security declines.

Because of RFEU's utilization of the dynamic currency hedging strategy, RFEU may have lower returns than an equivalent non-currency hedged investment when the component currencies are rising relative to the U.S. dollar. Although RFEU seeks to minimize the impact of currency fluctuations on returns, the use of currency hedging will not necessarily eliminate exposure to all currency fluctuations.

Real estate investment trusts (REITs) are subject to certain risks, including changes in the real estate market, vacancy rates and competition, volatile interest rates and economic recession.

Preferred securities combine some of the characteristics of both common stocks and bonds. Preferred securities are typically subordinated to bonds and other debt instruments in a company's capital structure, in terms of priority to corporate income, and therefore will be subject to greater credit risk than those debt instruments.

Certain securities held by RFEU are subject to credit risk, interest rate risk and income risk. Credit risk is the risk that an issuer of a security will be unable or unwilling to make dividend, interest and/or principal payments when due and that the value of a security may decline as a result. Interest rate risk is the risk that the value of fixed-income securities in RFEU will decline because of rising market interest rates. Income risk is the risk that income from RFEU's portfolio could decline if interest rates fall.

A fund pays transaction costs, such as commissions, when it buys and sells securities (or "turns over" its portfolio). A higher portfolio turnover rate may indicate higher transaction costs and may result in higher taxes when fund shares are held in a taxable account.

The use of derivatives can lead to losses because of adverse movements in the price or value of the underlying asset, index or rate, which may be magnified by certain features of the derivatives. These risks are heightened when RFEU's portfolio managers use derivatives to enhance RFEU's returns or as a substitute for a position or security, rather than solely to hedge (or offset) the risk of a position or security held by RFEU.

The funds are classified as "non-diversified" and may invest a relatively high percentage of its assets in a limited number of issuers. As a result, a fund may be more susceptible to a single adverse economic or regulatory occurrence affecting one or more of these issuers, experience increased volatility and be highly concentrated in certain issuers.

Please visit www.ftportfolios.com for the holdings of each fund and to read a full description of each fund's specific risks before investing.

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The **MSCI Europe Index** is a free float-adjusted market capitalization weighted index that is designed to measure the equity market performance of the developed markets in Europe. The **Nikkei 225** is a price-weighted equity index, which consists of 225 stocks in the 1st section of the Tokyo Stock Exchange. The **S&P 500 Index** is an unmanaged index of 500 stocks used to measure large-cap U.S. stock market performance.

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