

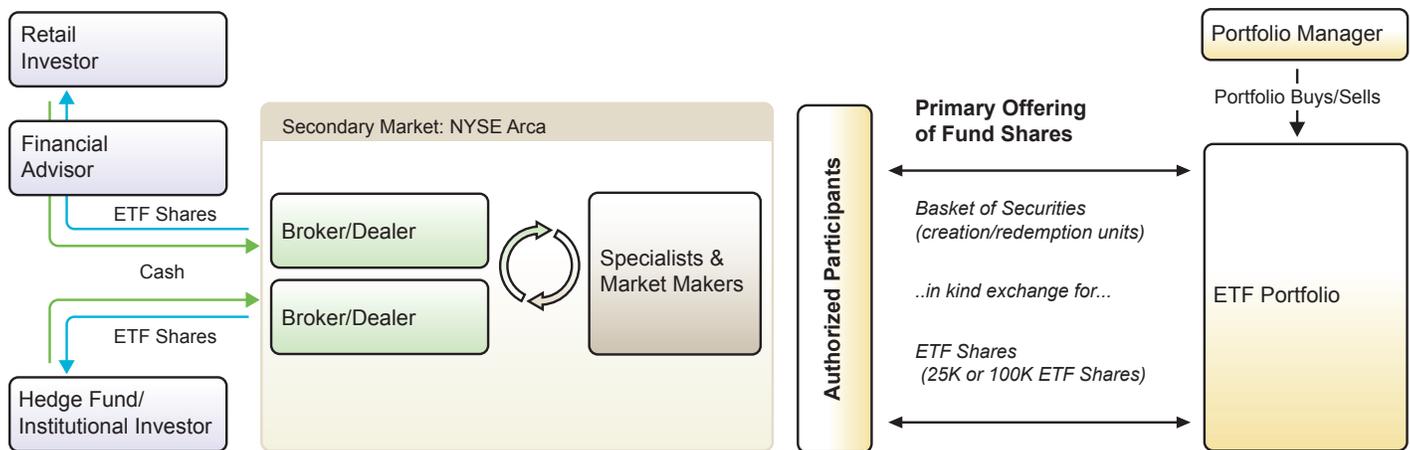


## What is an ETF?

An ETF is a unique investment vehicle that combines some of the features of mutual funds, with some of the features of individual stocks. Like a mutual fund, an ETF gives investors exposure to a group of securities (“index basket” or “alpha basket”) in a single transaction. Like a stock, ETFs are traded on an exchange, which allows investors the ability to set limit orders and stop orders to better control their purchase or sales price.



## How an ETF Operates



ETF Shareholders	Secondary Market Participants	ETF Share Creation/Redemption
<ul style="list-style-type: none"> <li>Retail investors working with Financial Advisors to buy or sell (or sell short) ETF Shares</li> <li>Hedge Funds or Institutional Investors buy or sell (or sell short) ETF shares. Institutional investors may assist in the efficient pricing of ETFs by arbitraging any premiums or discounts in the ETF price during the day</li> </ul>	<ul style="list-style-type: none"> <li>Broker-Dealers, Specialists, Market Makers, and Authorized Participants (APs) work together to ensure liquidity and efficient pricing by creating or redeeming ETF shares</li> <li>APs may assist in the efficient pricing process by arbitraging any premiums or discounts in the ETF price during the day</li> </ul>	<ul style="list-style-type: none"> <li>Process between ETF and AP to create and redeem ETF shares</li> <li>“In kind transfer” not considered a taxable event to the shareholders</li> </ul>



## ETFs and Stocks

While price for both individual stocks and ETFs are market driven, the factors that weigh into the price changes are different. The table below discusses the main differences in pricing and liquidity of stocks and ETFs, although other differences exist.

	Pricing	Liquidity
Common Stocks	Shares of individual stocks are purchased and sold through major exchanges or over-the-counter. The level of demand and the corresponding availability of a stock is the primary factor behind a stock's price. The number of shares available is fixed and prices fluctuate based on investor demand.	For individual stocks, liquidity and price are based on demand. With a limited number of shares available, buyers and sellers of a stock control the price. If a shareholder wishes to sell their shares, he/she attempts to find a buyer willing to pay. If no buyer exists the seller reduces the price to find a buyer. Conversely, higher demand for the stock would push the share price higher.
ETFs	Shares of ETFs are created in large quantities by the ETF and authorized participant (AP). The AP will create as many shares as the market demands. The creation units usually mirror the holdings in the ETF, whose underlying stocks are priced every 15 seconds. The value of these stocks is totaled to provide the intraday indicative value. Due to the arbitrage process for APs, the trading price of an ETF is normally close to the indicative value.	The AP facilitates how many shares of the ETF are available. This allows the AP to support the supply and demand process. If an ETF seller does not have a buyer, the price will not necessarily go lower. In a situation where more sellers exist than buyers, the AP can redeem shares removing them from the market and balancing the supply with the demand. The opposite would occur in a situation where more buyers are present. Rather than driving the ETF price higher, the AP will create more ETF shares to accommodate the demand.

## The Arbitrage Process

While the price difference between the ETF and the underlying stocks indicative value is often small, some APs attempt to profit from the difference by offering shares of the ETF at a discount or premium to the intraday NAV. For example: if one AP sets an asking price of an ETF at \$20 a share and the underlying stocks value is \$21, another AP could purchase and redeem the shares while turning a \$1 per share profit. Since this would result in a \$1 per share loss for the first AP, it is beneficial for ETFs to trade at or very near the intraday indicative value as it prevents the APs from creating an unfair market for the ETF shares.



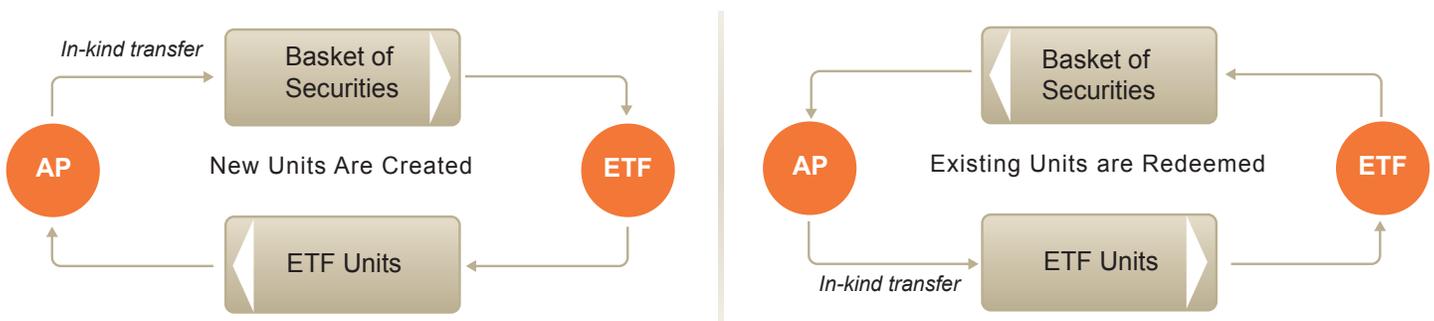
## Creating and Redeeming ETF Shares

In order to create new shares or redeem existing shares an ETF requires an Authorized Participant (AP). The AP establishes a contractual agreement with the ETF to create or redeem large quantities of ETF shares. The AP is the only entity who trades directly with the ETF.

In order to create new ETF shares the AP transfers a basket of securities to the ETF. The basket of securities represents the same securities being tracked by the ETF's corresponding index. The basket of securities being transferred to the ETF is referred to as a creation unit. In return, the ETF will transfer ETF units to the AP. The transaction is considered an "in-kind transfer" and therefore has no cost and is not considered a taxable event to the ETF shareholder.

Creation/redemption units range from approximately 50,000 to 100,000 ETF shares, however AdvisorShares has obtained exemptive relief to have 25,000 share creation units on some Funds, which would allow an AP to hold a smaller amount of shares in inventory (reducing the AP's holding risk).

The process is reversed when an AP is redeeming existing shares of an ETF. The AP transfers the ETF units back to the ETF, called a redemption unit. In return the ETF transfers the corresponding specific basket of securities back to the AP.





## Fund Shareholders

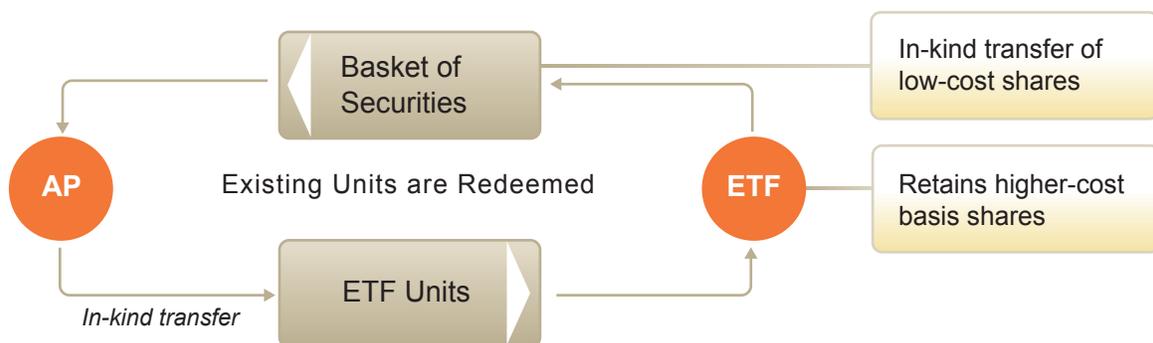
Any investor with a brokerage account can purchase shares of an ETF. It is this type of availability that makes ETFs attractive for some investors, although commission costs exist with each buy and sell. Additional shareholder benefits include:

- Increased Liquidity - Investors can buy or sell ETFs any second of the trading day; however ETFs are only as liquid as their underlying securities
- Transparency - Allows investors to make more educated investment decisions
- Trading Flexibility - Shareholders can hedge, buy on margin, purchase options (if available), and sell short

## Tax Efficiency

Unlike mutual funds, where investors are responsible for taxes on capital gains, many ETF do not make taxable capital gain distributions. Transactions between the AP and the ETF are transferred in-kind and therefore do not generate a taxable gain or loss for the shareholder.

Since the transactions will not be taxed it is beneficial to transfer the lower basis securities. However, at times it is advantages to sell high-basis securities at a loss in order to harvest losses to offset the taxable gains from that year. By balancing the cost basis, the ETF may be a tax efficient investment strategy.



**Before investing you should carefully consider the Funds' investment objectives, risks, charges and expenses. This and other information is in the prospectus, a copy of which may be obtained by visiting the Funds' website at [www.AdvisorShares.com](http://www.AdvisorShares.com). Please read the prospectus carefully before you invest.** Foreside Fund Services, LLC, Distributor.

An investment in the Funds is subject to risk, including the possible loss of principal amount invested. The risks associated with each Fund include the risks associated with the underlying ETFs, which can result in higher volatility, and are detailed in each Fund's prospectus and on each Fund's webpage.

Alpha measures the difference between a fund's actual returns and its expected performance, given its level of risk (as measured by beta).