



ACTIVE ETFs

What you need to know



INSIGHTS
IDEAS
RESULTS

ACTIVE ETFS – WHAT YOU NEED TO KNOW



PAUL GAMBALE
Senior Product Owner,
Innovation & New Ventures

ABOUT THE AUTHOR

Paul Gambale is the Senior Product Owner – Innovation and New Ventures at AMP Capital. He is responsible for SMSF and Self-Directed Wealth product development, including management of AMP Capital’s mFund and Active ETF initiatives.

An Active Exchange Traded Fund (Active ETF) is, most simply, a managed fund that is traded on a stock exchange such as the ASX. They are built like managed funds, but trade like shares, meaning that pricing is transparent and they can be bought and sold during any trading day just like ordinary shares.

Active ETFs, also known as Exchange Traded Managed Funds, share many similarities with exchange traded funds (ETFs) but have one key difference: ETFs are “passively managed” and aim to track a particular benchmark or index, whereas Active ETFs are “actively” managed by fund managers with the aim of outperforming a relevant benchmark.

THE GLOBAL MARKET

Exchange Traded Products (ETPs), which include ETFs and other exchange tradeable funds, are one of the fastest growing categories of investment products in the world, with over US\$3.8 trillion of assets held in over 6,700 products globally¹. A key reason for their popularity is that they exhibit all the advantages of stocks, such as being easy to trade and liquidity, coupled with the benefits of managed funds, such as diversification.

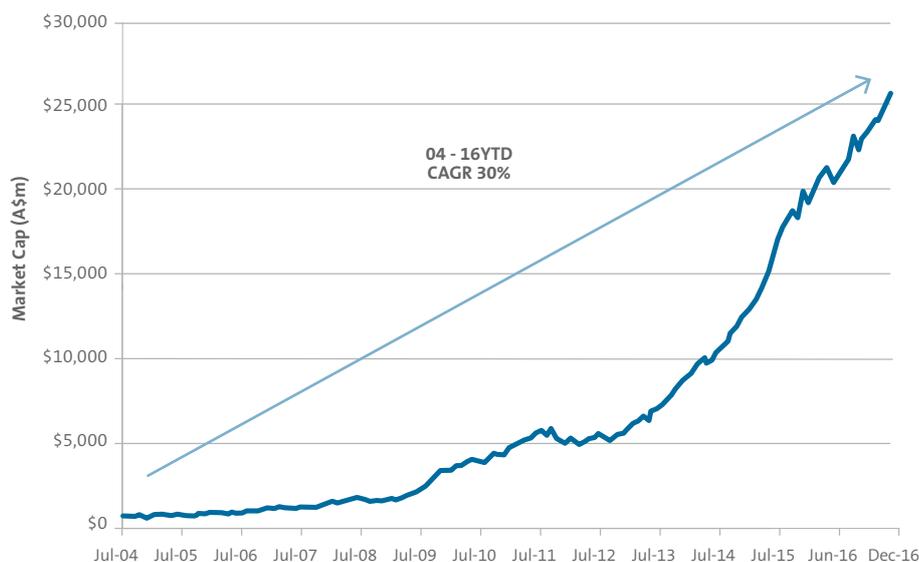
THE AUSTRALIAN EXPERIENCE

The Australian ETP industry, while comparatively small on a global scale, has grown dramatically over the last few years. As the chart below shows, the total market capitalisation of all ETP assets has grown from around AU\$6 billion in December 2012 to over AU\$25 billion in December 2016.

This growth is expected to continue as Australian investor awareness of ETPs increases and as continued product innovation takes place. Active ETFs are at the forefront of this innovation.

MARKET SIZE AND GROWTH: DECEMBER 2016

Australian ETP Market Cap: July 2004 - December 2016 (A\$m)



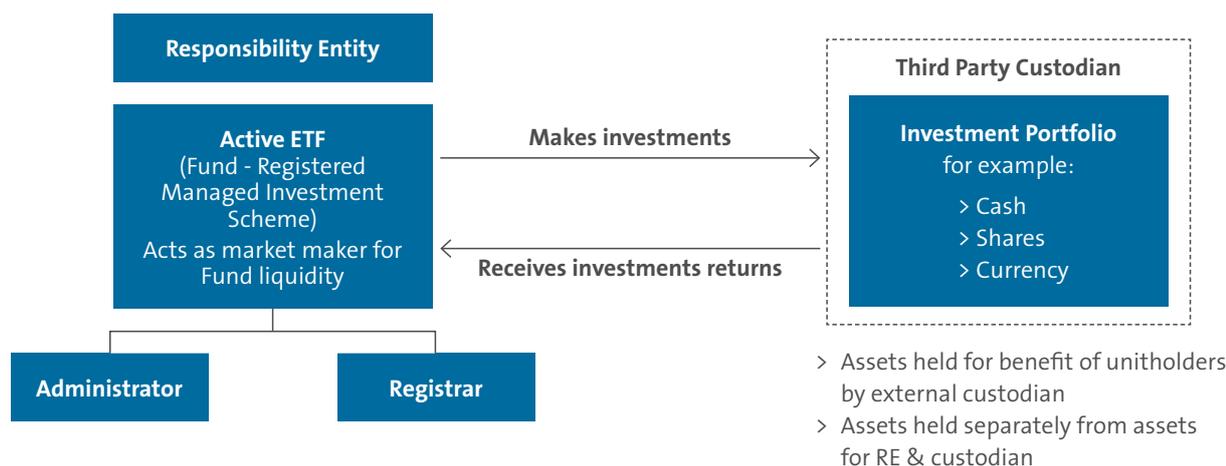
Source: BetaShares Australian ETF Review December 2016. CAGR = Compound Annual Growth Rate

¹ Source: ETFGI.com, as at end January 2017.

HOW ACTIVE ETFS ARE STRUCTURED

Safe-keeping of investments is a high priority, and Active ETFs are governed by a strong set of legal arrangements regarding the ownership of assets. They have the same legal structure as traditional managed funds, and are therefore subject to a high degree of investor protection regulation.

The assets underlying the funds do not form part of the assets of the Responsible Entity (RE) or Investment Manager. Rather, they are held on trust for the benefit of unitholders. The RE normally appoints an independent, third party custodian to hold the assets of an Active ETF. They are completely segregated from the assets of the RE, Investment Manager and the Custodian.



HOW ACTIVE ETFS COMPARE TO OTHER PRODUCT STRUCTURES

With so many investment structures, it can be hard to understand the differences between options and the opportunity each presents. The table below highlights the key differences between Active ETFs and other popular investment product structures.

| | ACTIVE EXCHANGE TRADED FUNDS (ACTIVE ETFS) | EXCHANGE TRADED FUNDS (ETFs) | LISTED INVESTMENT COMPANIES (LICs) | TRADITIONAL MANAGED FUNDS | ASX MFUNDS |
|-----------------------------------|--|--|--|--|--|
| Structure | Trust | Trust | Company | Trust | Trust |
| Management Style | Actively managed | Passive management/ index tracking | Actively managed | Actively managed | Actively managed |
| Investment/ withdrawal process | On market via ASX | On market via ASX | On market via ASX | With manager via platform or direct | Direct with manager via ASX |
| Disclosure | <ul style="list-style-type: none"> > Daily Net Asset Value (NAV) > Intraday indicative NAV (iNAV) > Full portfolio disclosure quarterly, within two months of end of quarter | <ul style="list-style-type: none"> > Daily Net Asset Value > Full portfolio disclosure daily or an iNAV | <ul style="list-style-type: none"> > Only required to disclose NAV monthly > Not required to provide portfolio information | <ul style="list-style-type: none"> > Daily unit prices > Usually only top 10 portfolio holdings (lagged) | <ul style="list-style-type: none"> > Daily unit prices > Usually only top 10 portfolio holdings (lagged) |
| Liquidity | <ul style="list-style-type: none"> > Fund is open-ended and issues/redeems units daily > Fund acts as a market maker to provide on-market liquidity | <ul style="list-style-type: none"> > Open-ended and regularly issues/redeems units > Use of third party market makers to provide on-market liquidity | <ul style="list-style-type: none"> > Closed-ended. Can only grow through placements, rights issues and Distribution Reinvestment Plans | <ul style="list-style-type: none"> > Open-ended and regularly issues/cancels units > Does not trade on ASX | <ul style="list-style-type: none"> > Open-ended and regularly issues/cancels units |
| Pricing | Generally expected to trade at tight spread around NAV as open ended | Generally expected to trade at a tight spread around NAV as open ended | Can trade at Discount/Premium to NAV as closed-ended. | Entry/exit price not known until T+1 | Entry/exit price not known until T+1 |

HOW ACTIVE ETFS WORK

Like ETFs, Active ETFs are open-ended. This means that, unlike a typical company that lists its shares on the market (including LICs), should investor demand exceed supply, the Active ETF has the ability to simply create more units to meet the demand. Similarly, units can also be redeemed should supply exceed demand.

Active ETFs differ from ETFs, however, in that the fund itself acts as market maker, rather than relying on third party market makers. This means that each Active ETF, rather than third parties, will set bids/offers for investors in the market during the trading day.

Third party market makers facilitate pricing and trading on the market for ETFs because ETFs, being index tracking funds, disclose their full portfolio on a daily basis. As such, third party market makers can accurately calculate the true value of the ETF (or net asset value (NAV)) and set bids/offers accordingly. For active fund managers, however, the composition of their portfolio is their key intellectual property with proprietary knowledge and can't be continuously revealed to the market; otherwise other parties could replicate their portfolios. Hence, the Active ETF itself acts as market maker, with the full portfolio only disclosed to the market quarterly, with a lag of up to two months. This protects active fund managers and the Active ETF's unitholders from conduct such as "front-running" and prevents replication.

As self-market maker, Active ETFs provide available bids/offers on market that reflect the fund's view of "fair value", as referenced by the indicative net asset value (iNAV), market conditions and the supply and demand for units during the trading day. At the end of each trading day, the fund will then issue or redeem units according to its net position in units bought or sold on the ASX on that day, and any gains or losses from the market making process will accrue to the fund.

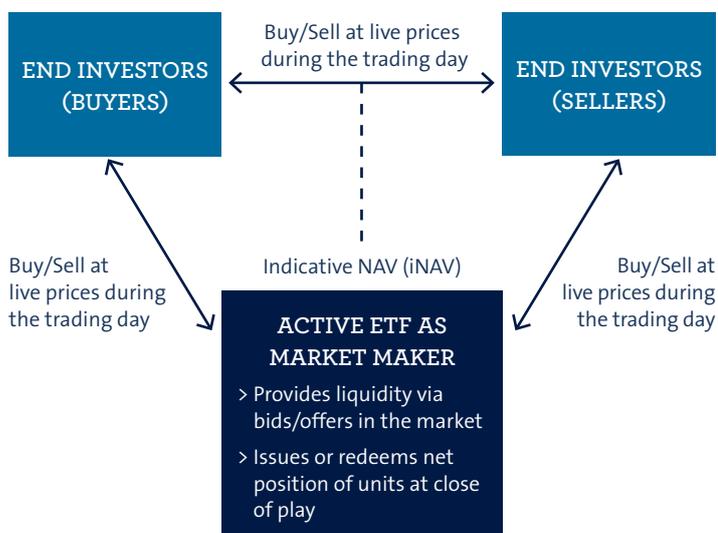
For investors looking to trade, the Active ETF acting as market maker will be available on the other side of the trade to buy/sell units. This is different from shares in listed companies and LICs, which are traded between "Investor A" and "Investor B" only. With an Active ETF, units can be traded between Investor A and Investor B, or in cases when there is no Investor B, the fund as market maker can be expected to be "on screen" to buy/sell directly to Investor A.

HOW ACTIVE ETFS BENEFIT INVESTORS

Active ETFs offer easy access to managed funds and therefore to active investment management capabilities which offer the potential to outperform an index or benchmark, unlike passive ETFs.

They can be bought or sold via an exchange (such as the ASX) in exactly same way as buying a share or an ETF. This means they can be easily managed alongside all other broker holdings, making administration and tax reporting easy for investors. They can also offer diversification benefits as they generally invest in a diversified portfolio which can be difficult for retail investors to access or replicate.

From an administration perspective, they don't require any forms to complete - or additional paperwork, and have no minimum investment requirement. Active ETFs can also be considered more transparent than traditional managed funds as they provide intra-day pricing via the exchange whereas traditional managed fund prices are only set once per day or less frequently.



WHAT ARE THE RISKS TO CONSIDER?

A risk applicable to all Active ETFs that should be considered is that the trading price of units on the ASX may differ from the underlying Net Asset Value. However, as the Funds' are open ended and act as their own market maker, each Fund will aim to provide bids and offers in the market at a tight spread. Other risks associated with Active ETFs are liquidity (as there can be no assurance that there will be a liquid market for units), ASX trading and market making. Please also consider the relevant Product Disclosure Statement (PDS) for specific risks which may relate to each AMP Capital Active ETF.

HOW ACTIVE ETFS ARE BOUGHT AND SOLD

Transacting to buy or sell units in an Active ETF is done through any full service or online broker, just like buying or selling a share or an ETF. All settlement is via CHESS. Please remember to read the PDS of each Active ETF prior to investing.

WANT TO LEARN MORE ABOUT ACTIVE ETFS?

- > [Top tips for trading](#)
- > [Understanding buy and sell spreads](#)
- > [Understanding liquidity](#)

WANT TO KNOW MORE ABOUT AMP CAPITAL'S ACTIVE ETFS?

- > [FAQs](#)
- > [Active ETFs homepage](#)
- > [Find out how you can access Global Listed Infrastructure, Global Listed Property and a Multi-Asset portfolio solution](#)



WANT TO LEARN MORE ABOUT ACTIVE ETFS?

- > [Top tips for trading](#)
- > [Understanding buy and sell spreads](#)
- > [Understanding liquidity](#)

WANT TO KNOW MORE ABOUT AMP CAPITAL'S ACTIVE ETFS?

- > [FAQs](#)
- > [Active ETFs homepage](#)
- > [Find out how you can access Global Listed Infrastructure, Global Listed Property and a Multi-Asset portfolio solution](#)

CONTACT US

If you would like to know more about how AMP Capital can help you, please visit www.ampcapital.com.au/smsf-suite

Important notice: While every care has been taken in the preparation of this information contained in this paper, neither AMP Capital Investors Limited (ABN 59 001 777 591) (AFSL 232497) nor any member of the AMP Group make any representation or warranty as to the accuracy or completeness of any statement in it including without limitation, any forecasts. This content has been prepared for the purpose of providing general information only, without taking account of any particular investor's objectives, financial situation or needs. Investors should, before making any investment decisions, consider the appropriateness of the information on this website, and seek professional advice, having regard to their objectives, financial situation and needs.