T. Rowe Price

How to gain the benefits of active management in an exchange-traded fund

From the Field

Key Insights

- Actively managed strategies can adapt to changing market environments.
- T. Rowe Price offers active strategies specifically designed as exchange-traded funds (ETFs) that are based on some of our existing mutual fund strategies.
- Our actively managed ETFs benefit from the same skilled portfolio expertise as our active funds as well as the advantages of an ETF structure.

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For most of the three decades they have existed, exchange-traded funds (ETFs) have largely pursued a passive investment strategy. Today, 91% of the USD 10.7 trillion invested in ETFs is held in passive strategies.[1] Even so, the number of actively managed ETFs is rapidly approaching the number of passively managed ETFs.[2] Indeed, a majority of ETFs that launched in the past few years have offered active strategies.

Much of this surge in active ETFs stems from a 2019 change in the U.S. Securities and Exchange Commission (SEC) rules that streamlined the process of launching new ETFs. Many of the new active funds are being launched by asset managers with long track records in actively managed mutual funds, including T. Rowe Price. As a result, investors are now able to take advantage of the benefits of active management within the advantageous structure of an ETF.

What is an active ETF?

An ETF is very similar to a mutual fund in many ways, particularly in the fact that they both represent a basket of pooled securities, such as stocks or bonds. As with mutual funds, ETFs can be actively or passively managed. With an active ETF,

Actively managed ETFs offer investors the potential to outperform benchmarks within the potentially advantageous ETF structure.

[1] As of January 22, 2025. Source: ETF Action.
[2] As of November 19, 2024. Source: Morningstar.com.

portfolio managers take an active role in managing the pooled assets, typically making decisions about what securities to include and at what relative weighting, based on a predetermined strategy or set of criteria.

By comparison, passive ETFs are generally designed to match the investments in a benchmark index. Changes to the investments held in the ETF are typically made only to keep the fund in line with the holdings of the benchmark index.

How do active ETFs work?

In many ways, active ETFs work in much the same way as an actively managed mutual fund. Investors can invest in a diverse pool of securities that is managed professionally on behalf of all shareholders according to a stated objective or investment strategy. Both active ETFs and active mutual funds allow individual investors to benefit from the expertise offered by professional management through an active strategy that typically seeks to outperform the target benchmark index. There are some important structural similarities and differences to be aware of, however (see Fig. 1).

ETFs are designed to outperform

By their very nature, ETFs are designed to provide investors with a competitive alternative to mutual funds (see Fig. 2, on page 3). The ability to buy and sell shares of ETFs on an exchange throughout the day can make it easier for investors to build diversification into their portfolio, compared with buying or selling mutual funds once a day after the market closes. The relatively low expense ratios of ETFs compared with mutual funds are attractive to cost-conscious investors.

In addition, ETFs are considered to be a more tax-efficient alternative to mutual funds, in part, because of the way capital gains are handled when shareholders sell or redeem their shares.

Comparing active ETFs and active mutual funds

(Fig. 1) Actively managed mutual funds and ETFs share some similarities, along with a few important differences.

	Active mutual funds	Active ETFs
Professionally managed	Yes, on behalf of all shareholders	Yes, on behalf of all shareholders
Trading	Shares are purchased and redeemed once per day at market close	Shares are purchased and sold throughout the day on an exchange, much like a regular stock
Minimum investment	Minimums depend on share class but can be low	No minimums; investors can invest as little as the cost of a single share
Fees	Includes management fees and shareholder servicing costs; fees vary by share class	Expense ratios are typically lower and with fewer layers of fees

For educational purposes only. The table above is not a comprehensive list of investment vehicle features, benefits, or risks. Vehicle structures, portfolio strategies, investment objectives, and risks will vary. Consult your financial advisor or tax professional for more information.

The popular benefits of ETFs

(Fig. 2) ETFs offer investors a competitive alternative to mutual funds.

Convenience
ETFs give investors the flexibility to buy or sell intraday without trading frequency limitations or minimum investment amounts.

Cost-effectiveness
ETF expenses are streamlined, with fewer operational costs.

Tax efficiency
The ETF structure has the potential to reduce capital gain distributions by minimizing the impact of shareholder purchase and redemption activity.

When an investor redeems their shares in a mutual fund, the fund may need to liquidate assets to fund that redemption. This event could lead to capital gains, which would be a tax liability shared by all the fund's shareholders. By comparison, when an ETF investor sells their shares of the ETF, they sell to another investor with no effect on the fund's assets or its other shareholders.

The benefits of active strategies

With passive investment strategies, investors are at the whim of the market. Whether a passive investment is tied to a specific sector or broad market index, by definition, there is no objective to outperform. And in market downturns, passively managed ETFs have no discretion to make adjustments.

On the other hand, actively managed investment strategies can adapt to changing market environments in pursuit of more attractive risk-adjusted returns. Active funds tend to perform best in areas of the market where there is less efficiency, such as in the small-cap space or in emerging markets, for example. In these areas, the expertise and research capabilities of professional managers can provide a competitive edge.

For example, T. Rowe Price Active ETFs seek to outperform benchmark indexes through the added value of our investment management expertise and global research capabilities. Our global team of investment professionals goes beyond the numbers every day to evaluate markets and study opportunities. This depth of understanding helps inform better decision-making and prudent risk management for our clients. Regardless of market conditions, our experienced investment professionals have the flexibility to adjust their actively managed portfolios in pursuit of the most advantageous positions. None of this is possible with the limitations of passively managed ETFs.

We have long believed that we could deliver the benefits of our core investment approach in the form of an ETF. Managed through rigorous fundamental research and a forward-looking strategic perspective, T. Rowe Price Active ETFs are the latest vehicle that enables us to package this expertise for clients who may prefer the ETF structure.

Our commitment

T. Rowe Price active strategies have a compelling long-term track record. Regardless of the market environment, we seek to deliver strong performance through our commitment to fundamental research and in-depth insight. T. Rowe Price Active ETFs offer investors the benefits of ETFs while also offering the potential for outperformance.

For clients seeking returns that go beyond the limitations of an index, T. Rowe Price is committed to offering a different kind of ETF: one that combines the features and benefits of the ETF's structure with the additional edge our strategic investing approach can deliver. We will continue to pursue innovative investment solutions and strategies to help clients feel confident in reaching their investing goals.

Learn how active ETFs can help you reach your goals

T. Rowe Price seeks to offer investors the potential for outperformance.

Visit troweprice.com/exploreetfs

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T. Rowe Price identifies and actively invests in opportunities to help people thrive in an evolving world, bringing our dynamic perspective and meaningful partnership to clients so they can feel more confident.

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