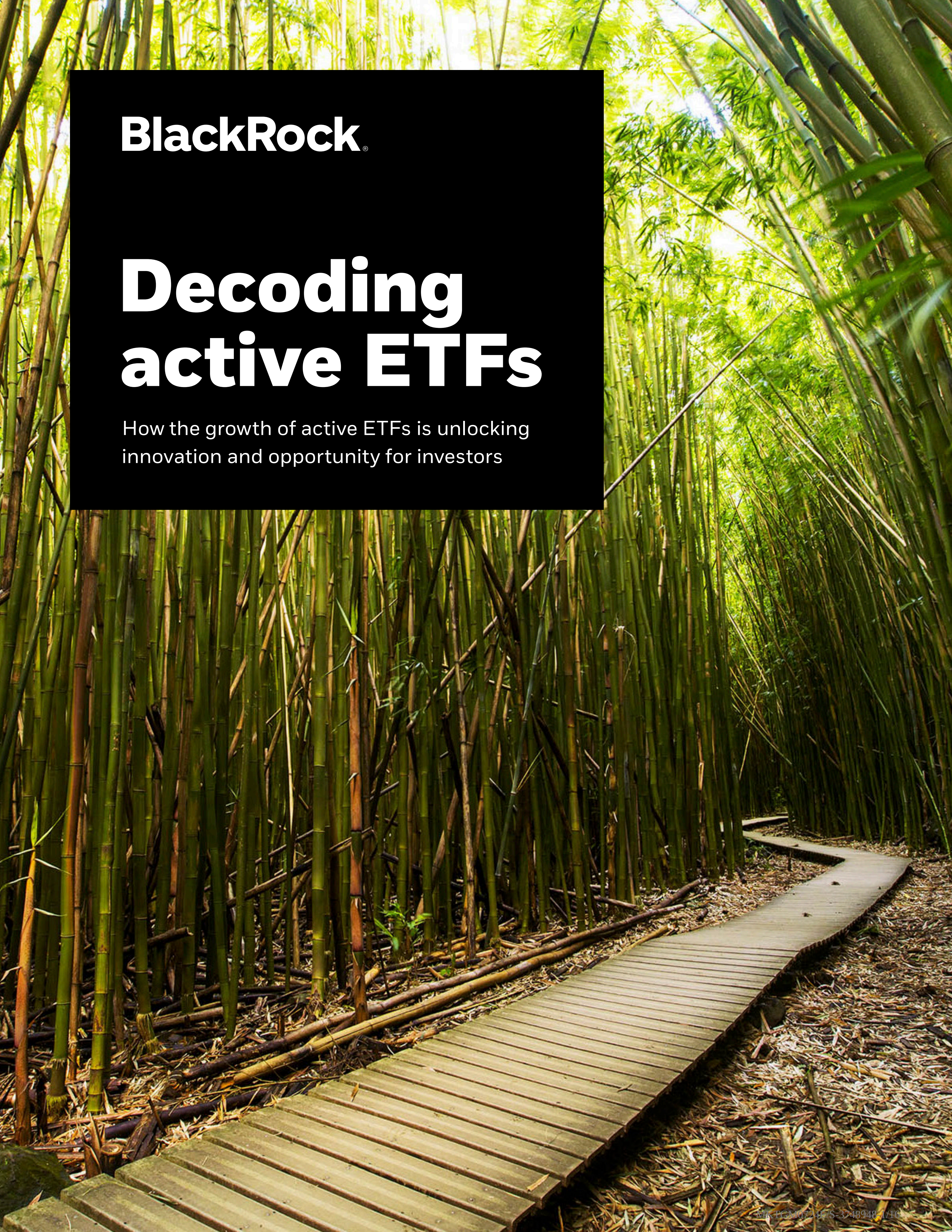
BlackRock

Decoding active ETFs

How the growth of active ETFs is unlocking innovation and opportunity for investors



Foreword

The Exchange-Traded Fund (ETF) industry has been innovating seemingly non-stop since its creation in the 1990s. Starting with just a handful of ETFs, there are now over 13,000 globally, providing access to an ever-widening range of asset classes, sectors, and geographies.[1]

ETFs are now firmly mainstream — and they've moved well beyond their roots in indexing. Investors are choosing ETFs because of the wrapper's key benefits, offering operational efficiencies and liquidity that investors now see can be extended across a range of assets.

Amid a market environment of higher volatility, investors are pivoting to active management and its specialist insights, differentiated strategies, and actively managed risk. While active management has been available in mutual funds for years, investors are increasingly turning to the ETF wrapper to access these strategies.

This dynamic is giving rise to what we see as a new era of active ETF innovation. Across the industry, and within our own firm, the growth of new offerings in active ETFs is accelerating. In 2021, about a quarter of global ETF launches were actively managed; through the first half of 2024, 41% of all ETFs launched were active.[2] Given these trends, we expect global active ETF assets under management to reach $4 trillion by 2030 — more than a four-fold increase in about six years.[3]

We believe the asset management industry is at an inflection point, where active ETFs are becoming an integral part of investor portfolios around the world.

BlackRock launched its first actively managed ETF in 2013.[4] In the past decade, we've expanded what the wrapper could do to help investors, from individuals to financial advisors to institutions. Because of actively managed strategies, ETFs can now be used to seek above-benchmark returns or look to achieve certain outcomes or gain unique exposures. This dynamic coincides with changing investment priorities as a new market regime of higher macro volatility means a potential to benefit from a more active approach.

BlackRock was created on the foundation of risk management, technology, and democratizing access to financial markets for investors. All of this comes together as we innovate around actively managed ETFs to meet this demand. Technology is key as we leverage insights from expert portfolio managers to develop new products and expand existing ones, and research and integrate AI, machine learning, and natural language processing technologies into our investment process — many of which we have been doing for years.

This is an exciting time of growth in the industry. We are committed to expanding the boundaries of what's possible in the ETF wrapper and helping equip investors as they seek to navigate today's markets and those for decades to come.

1 Source: BlackRock Global Business Intelligence. There are 13,200 globally as of 30/06/24. **2** Source: BlackRock Global Business Intelligence as of 30/06/24. Globally in the first half of 2024, there were 324 active ETF launches and 472 index ETF launches; in 2021: 406 active ETF launches, and 1,097 index. **3** Source: BlackRock, as of 30/06/24. Estimates are for global figures and include 2027 and 2030 scenario calculations based on proprietary research by BlackRock Global Product Solutions. Subject to change. The figures are for illustrative purposes only and there is no guarantee the projections will come to pass. **4** The BlackRock Short Duration Bond ETF (ticker: NEAR) launched 25/09/13.

Stephen Cohen
Chief Product Officer,
BlackRock

Rich Kushel
Head of the Portfolio
Management Group,
BlackRock

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Key points

1

Growth to $4 trillion

- **BlackRock projects that global active ETF AUM will more than quadruple to $4 trillion by 2030, from $900 billion as of June 2024.**
- Investors are increasingly seeking actively managed strategies amid today's markets of higher volatility, and they're frequently choosing to access them through ETFs due to the wrapper's benefits, including efficiency and transparency.
- Key changes in the market are driving interest and innovation within active ETFs: the increasing adoption of ETFs overall, the rise of digital wealth platforms — empowering end-investors, and the shift to fee-based investing and models.

2

Active ETFs: Alpha-seeking, outcomes, exposures

- **The active ETF universe is broad, with three distinct categories: alpha-seeking, outcomes, and exposures.**
- We see active ETFs becoming an increasingly important part of investor toolkits, alongside mutual funds, closed-end funds (including private markets), separately managed accounts, and index ETFs. Investor objectives and preferences drive vehicle selection.
- Active ETFs play a significant role in new strategy innovation within the global ETF industry, accounting for 41% of all ETF launches in 2024 through June. In EMEA the market is more nascent, with new launches at 12% active.

3

ETFs: A wrapper of choice

- **We believe active ETFs are poised to earn a place in portfolios by helping investors to access more strategies and differentiated returns through the convenience of the ETF wrapper.**
- We expect active mutual funds to continue to coexist with active ETFs in EMEA, given regional preferences and business model dynamics.

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Introduction

The landscape of actively managed ETFs is rapidly transforming, with a marked expansion in capabilities and offerings to meet investors' rising demand as they navigate a new market regime of greater volatility and uncertainty. As more innovation has been brought to market through the active ETF wrapper, institutional and individual investors, and wealth managers, are increasingly considering ETFs as another vehicle to pursue active management, often to complement other fast-growing categories like alternative investing, direct indexing, or traditional mutual funds or ETFs.

Active ETF assets under management reached $900 billion globally through the first half of 2024.[5] Although active ETFs comprise 7% of total ETF assets, they're rising fast, and far outpacing growth for index ETFs.[6]

Active ETFs are available worldwide, yet the US is by far the biggest market, with 77% of total industry AUM.[7] In EMEA, mutual funds continue to be a wrapper of choice for many client types. Active ETFs remain nascent, accounting for 2% of ETF AUM at about $40 billion.[8] But the market is expanding, with AUM up 25% from year-end 2023 to the first half of 2024.[9]

We expect active ETFs to reach

$4T

in AUM globally by 2030

5 Source: BlackRock Global Business Intelligence. Data as of 30/06/24. **6** Source: BlackRock Global Business Intelligence as of 31/12/23. Active ETF AUM had a 31% three-year compound annual organic growth rate globally through 2023 vs 11% for index. Organic asset growth rate calculated by dividing net new business (NNB) over beginning of period AUM and compounding annual growth rates over the 36-month period of 01/01/21 to 31/12/23. Active ETF growth rates exclude the NNB impact of active mutual fund to active ETF conversions over the three-year period. Organic growth excludes the impact of market movement. **7** Source: BlackRock Global Business Intelligence as of 30/06/24. Through the first half of 2024, active ETFs had $693 billion of AUM in the US. **8** Source: BlackRock Global Business Intelligence as of 30/06/24. Through the first half of 2024, active ETFs had $40 billion of AUM in Europe, Middle East, and Africa. **9** Source: BlackRock Global Business Intelligence as of 30/06/24. In 2024 through June 30, active ETFs had $40 billion of AUM in Europe, Middle East and Africa, up 25% from $32.1 billion at year-end 2023.

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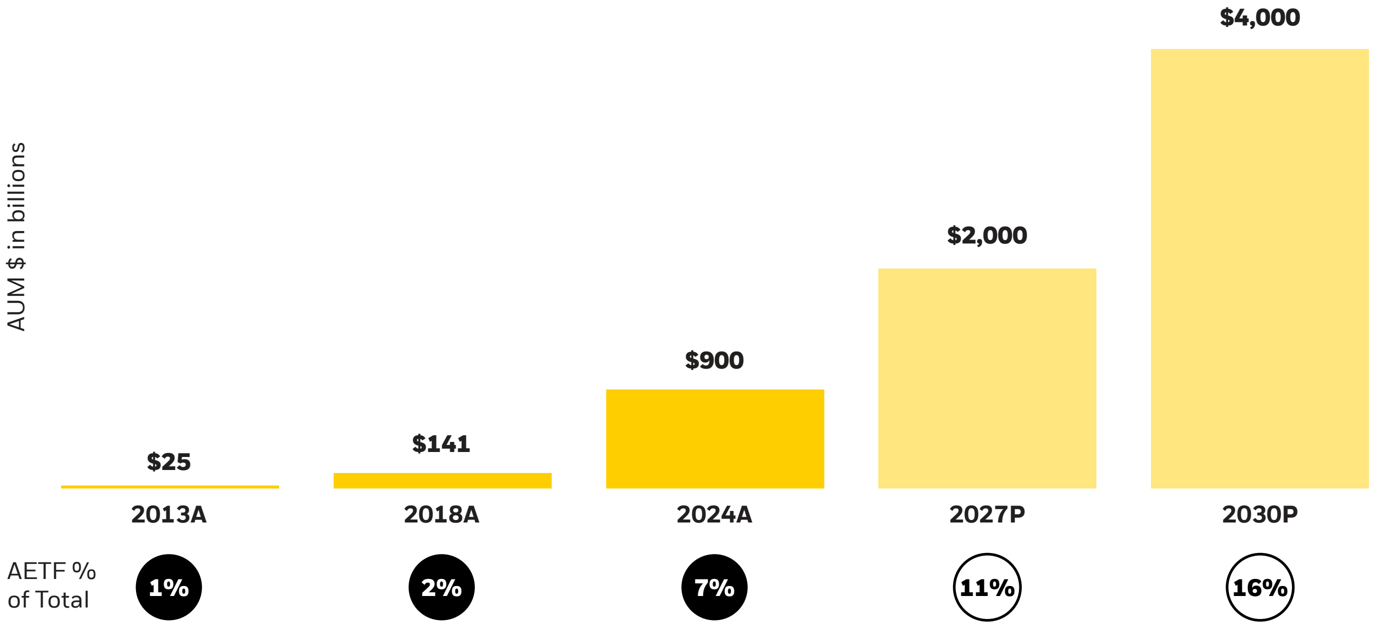
We expect this pace to continue and for global active ETF AUM to more than quadruple to $4 trillion by 2030 (Figure 1). This would constitute 16% of the global ETF industry, which we expect to more than double to $25 trillion by 2030 from $11.5 trillion in 2023.[10] Stronger regulatory tailwinds could drive faster growth in active ETFs. And ETFs themselves are becoming a wrapper of choice, expanding from 15% of total fund assets in 2013 to 31% in 2023.[11]

Figure 1: Actual and projected growth of active ETFs (USD billions)

We expect global active ETF assets to reach $4T by 2030



Source: BlackRock, as of 30/06/24. The 2024 number is actual through the first half of the year. Estimates are for global figures and include 2027 and 2030 scenario calculations based on proprietary research by BlackRock Global Product Solutions. Subject to change. The figures are for illustrative purposes only and there is no guarantee the projections will come to pass.

10 Source: BlackRock, as of 31/12/23. Estimates include 2025 and 2030 scenario calculations based on proprietary research by BlackRock Global Product Solutions. Subject to change. The figures are for illustrative purposes only and there is no guarantee the projections will come to pass. **11** Source: Morningstar Direct as of 31/12/23. Fund AUM includes ETFs and Mutual Funds only.

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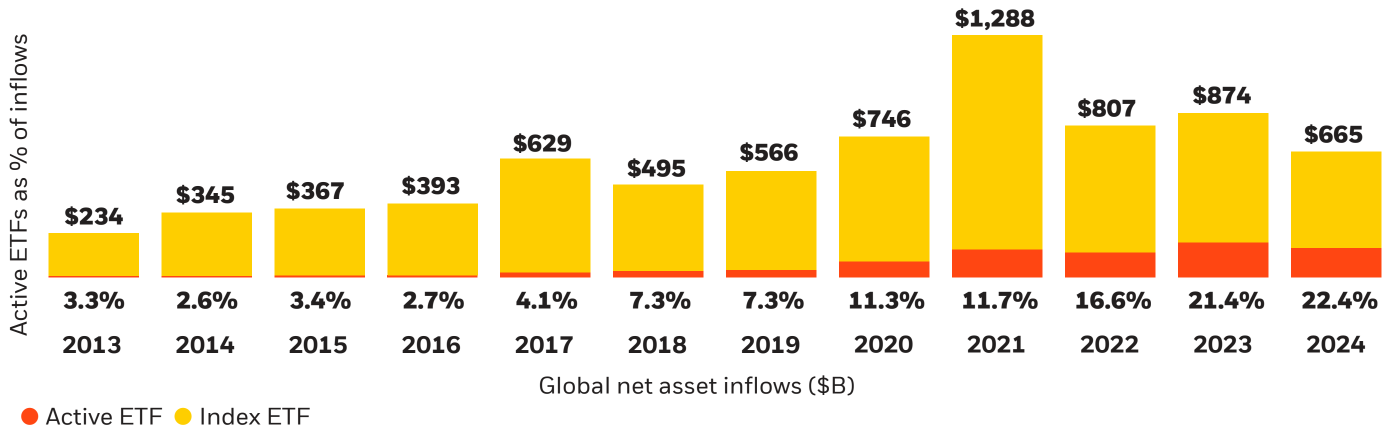
This expected growth trajectory reflects how active ETFs are at the nexus of innovation within the asset management industry, accounting for 41% of global ETF launches through June 2024.[12] In the more nascent EMEA market, active ETFs comprised 12% of launches in 2024, an acceleration from 7% in 2022.[13] Competition among issuers is strong given today's volatile markets, with issuers numbering roughly the same for active and index ETFs globally.[14] As Figure 2 shows, active ETFs are also taking a larger share of global ETF net asset inflows and organic asset growth.

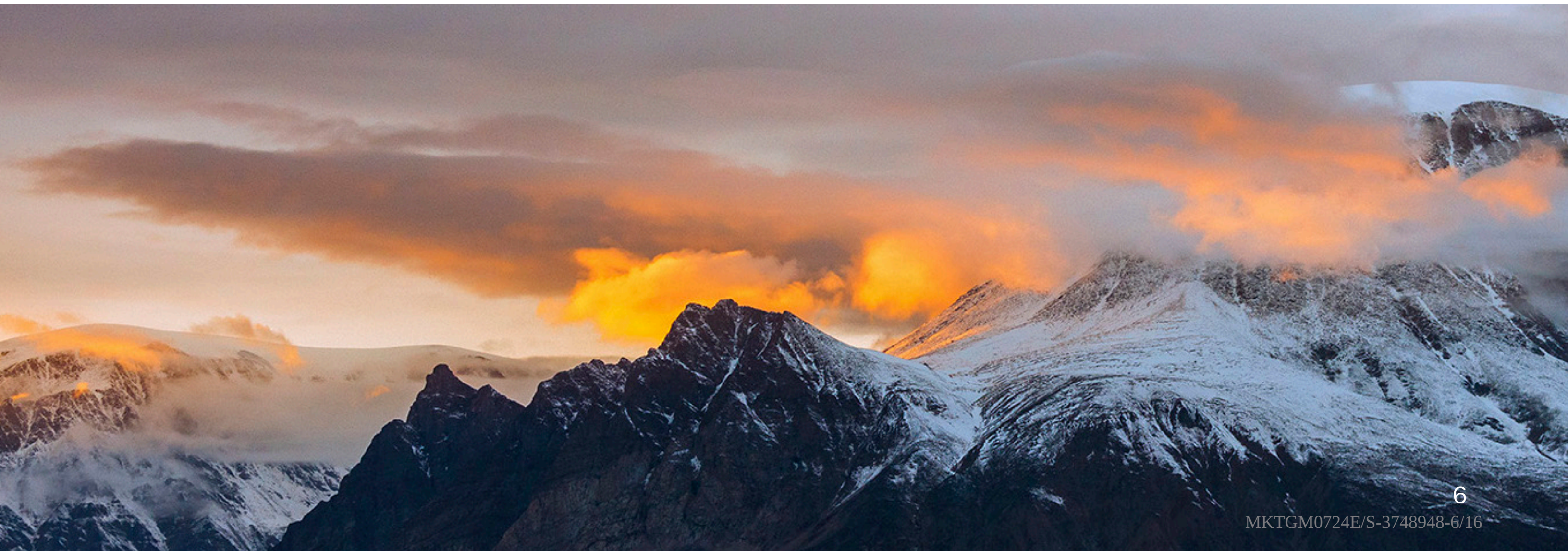
Figure 2: Global active ETF net asset inflows (USD billions, %), 2013-2024

Active ETFs are comprising a larger share of industry net asset inflows



Source: ETF groupings determined by BlackRock Global Business Intelligence as of June 2024. Numbers for 2024 are through June.

12 Source: BlackRock Global Business Intelligence as of 30/06/24. Globally in the first half of 2024, there were 324 active ETF launches and 472 index ETF launches. **13** Source: BlackRock Global Business Intelligence as of 30/06/24. In 2024 through June, there were 26 active and 193 index launches in EMEA. In 2022, there were 38 active launches and 477 index. **14** Source: BlackRock Global Business Intelligence as of 31/12/23. There were 393 issuers for active ETFs globally in 2023, while index ETF issuers numbered 399.



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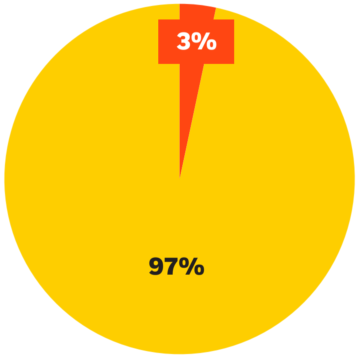
While active ETFs are growing rapidly, they are still far smaller than the actively managed mutual fund universe (Figure 3). Actively managed strategies are a sizable portion of the mutual fund market: with $25.2 trillion AUM worldwide through year-end 2023, or 76% of all mutual fund AUM.[15]

In this paper, we will explore the factors that have propelled the active ETF category, the types of actively managed ETFs, who is using them and how they are doing so.

Figure 3: Global active ETF assets as % of active mutual fund assets

Active ETFs are a small but growing portion of overall active assets

% of total global active industry AUM



● Active ETF ● Active Mutual Fund

Source: All data through 31/05/24. BlackRock Global Business Intelligence for global active ETFs; Simfund for US active mutual funds; Broadridge for non-US active mutual funds. Total figures are as follows: $867.8 billion for global active ETFs and $26.9 trillion for global active mutual funds.

"Active ETFs provide the opportunity to offer specific strategies and active management via transparent, efficient ETF packaging. In the world of fixed income, active strategies can provide more diversified portfolios that take advantage of better relative value opportunities in hard-to-reach asset classes with less interest rate risk and lower volatility."

– Rick Rieder, BlackRock's Chief Investment Officer of Global Fixed Income, Head of Global Allocation Team

15 Source: Investment Company Institute as of 14/03/24.

Understanding the active ETF universe

Active ETFs are investment funds managed by professional portfolio managers who actively select and adjust the fund's holdings in an effort to outperform the market, deliver a specific outcome or gain exposure to hard-to-index markets. This involves ongoing analysis and decision-making based on market conditions. In contrast, index ETFs seek to replicate the performance of a specific index.

Our clients are telling us navigating the active ETF universe can be difficult because it is so broad. **We see three distinct categories within active ETFs that help describe each category's use case: alpha-seeking, outcomes, and exposures.**

1 Alpha-seeking

Alpha strategies seek to outperform a benchmark based on proprietary research and insights. These include both fundamental and systematic strategies, such as:
- Core, thematic and rotation strategies
- Multi-sector, credit, securitized, ultra-short bond and loans
- Liquid alternatives

Active factor strategies that seek to outperform by tilting toward broad, persistent drivers of return

2 Outcomes

Options-based strategies offer targeted investment objectives combining or modifying market exposures via the use of derivatives or portfolio construction, including:
- Income strategies, such as buy-writes, covered calls and risk-managed income strategies
- Protection strategies, such as buffered, convexity and tail risk strategies
- Growth strategies, such as accelerators, stackers and step-ups

Goal-based strategies including target income, target risk, target date

3 Exposures

Non-index strategies feature access to segments of the market that are difficult to index, such as cash or commodities
- **Derivative-based** exposures, including leveraged, inverse and single stock products

Investment comparisons are for illustrative purposes only. To better understand the similarities and differences between investments, including investment objectives, risks, fees and expenses, it is important to read the products' prospectuses.

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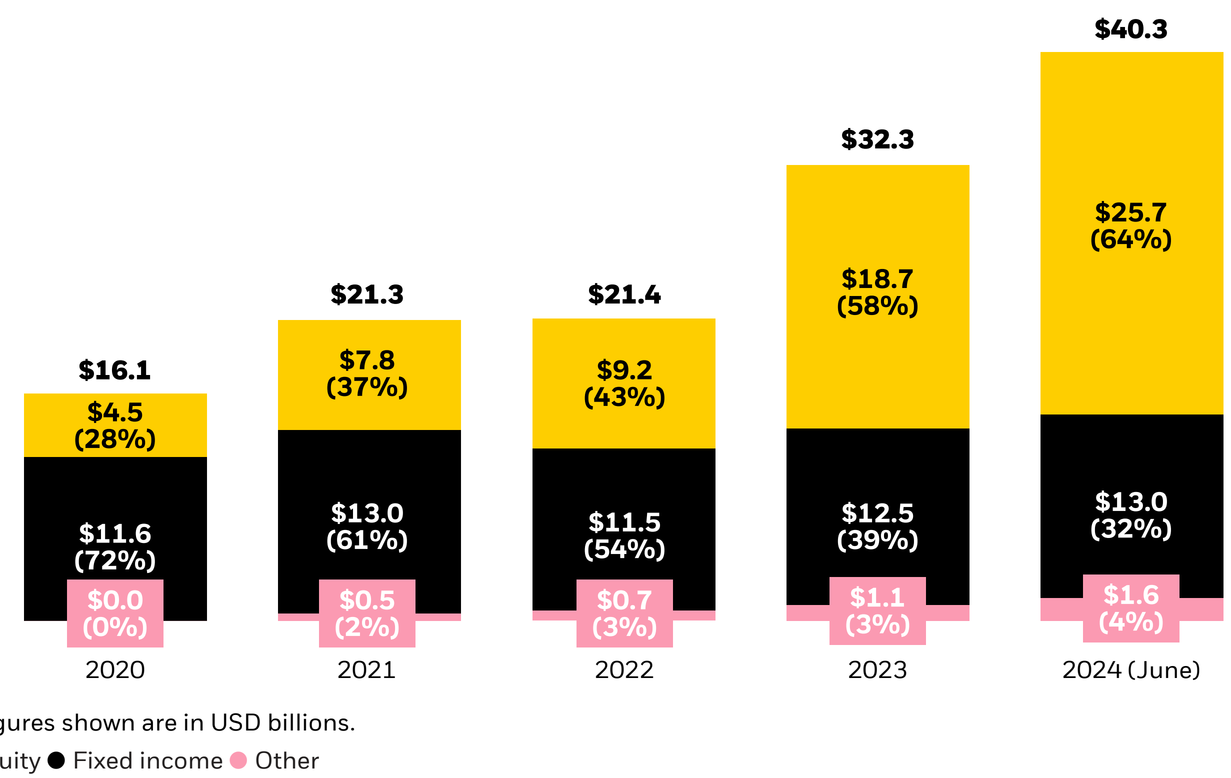
> **"Amid fluctuating market dynamics, outcome-oriented and alpha-seeking active ETFs help address investors' specific investment objectives, whether that's generating income, seeking outperformance or enhancing downside protection."**
>
> **– Raffaele Savi, Global Head of BlackRock Systematic and Co-Head of Systematic Equities**

Any asset class can be managed within alpha-seeking, outcome, and exposure ETFs (Figure 4). Outcomes strategies replicate defined outcomes previously only available in vehicles such as structured notes, which can be opaque, costly, and difficult for individual investors to access. Meanwhile, alpha-seeking strategies are often similar to those previously delivered only in mutual funds. Exposures can offer investors access to markets that are not easily investible via indexing.

Figure 4: EMEA active ETF Industry by asset class (USD billions)

Active ETFs in EMEA cut across asset classes



Source: BlackRock Global Business Intelligence, as of 30/06/24.

Benefits of combining ETFs with an active investment approach

Access to investment expertise: Active ETFs provide access to investment strategies managed by specialist portfolio managers who utilise their expertise to help deliver better performance, specific outcomes (such as downside protection or regular income) or provide exposure to markets which are hard to access.

The proven benefits of an ETF: Delivering investor-designed strategies in a transparent, flexible, and convenient wrapper, provides benefits such as ease of trading, low fees, and no minimum investment amounts. ETFs can also be tax-efficient vehicles for investors for certain exposures.

Transparency, convenience, and efficiency: ETFs are transparent and typically disclose their full portfolio holdings each day, which can help investors look through to see their full risk exposure across their whole portfolio on a daily basis.[16] Additionally, there is a structural convenience for investors to use the same vehicle across portfolios for consistency in custody, settlement, and reporting — and for many, that's ETFs.

"Active management is essential to navigating today's market volatility. By seeking alpha and utilising the ETF wrapper, a broad range of investors can gain access to differentiated sources of returns in a flexible, liquid, transparent vehicle."

– Becci McKinley Rowe, Co-Head of BlackRock Fundamental Equities

In today's market — with increased market volatility and uncertainty leading to greater stock market dispersion — we see even greater opportunities for active ETFs, because portfolio managers can incorporate proprietary research and react in real-time to evolving market conditions to maximise alpha.[17]

Mutual funds will continue to coexist with active ETFs given regional preference and business model dynamics.

16 Source: BlackRock Global Business Intelligence data as of 31/12/23. Transparent active ETFs comprised about 98% of total ETF AUM globally. **17** For more, see the BlackRock Investment Institute paper "A bigger role for active strategies" published in February 2024: https://www.blackrock.com/institutions/en-zz/a-bigger-role-for-active-strategies.

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Decoding growth in active ETFs

In EMEA, initial growth in the active ETF space was led by bond funds not seeking to outperform but rather providing exposures to parts of the market viewed by some as difficult to index. More recently, the new regime of higher macro volatility resulting in greater uncertainty and dispersion of returns, has led to a renewed focus on active strategies, which has driven the launch and growth of equity active ETFs, particularly low-risk, low-fee alpha-seeking strategies. Global and European active managers are tapping into general ETF growth and diversifying into new distribution channels by embedding active strategies into the ETF wrapper.

We believe we are at a tipping point in the EMEA active ETF market and starting to see demand increase. Key evolutions in investor preferences combined with the shifting distribution landscape are positioning active ETFs for growth.

"Actively managed portfolio ETFs democratise access for retail investors seeking to invest in professionally managed whole portfolio solutions, delivered through an innovative and convenient wrapper."

– Rafael Iborra, Portfolio Manager, BlackRock Model Portfolio Solutions

1 More investors are choosing the ETF wrapper

ETFs have been on a steady rise in Europe and their growth now outpaces mutual funds. ETFs saw an 18% annual growth rate over the last five years (exceeding 4% for mutual funds), with total ETF AUM about doubling from $1.1 billion in 2019 to about $2.1 trillion through June 2024.[18] There are now 192 active ETFs in Europe, and although small in size, the assets in these ETFs have been growing at an average of 25% a year since 2020.[19] At the same time, investors are increasingly looking to solve problems or meet a specific need with a product. Because of ongoing innovation within active ETFs, they can offer a wider range of strategies to meet these needs, including outcome strategies, like income.

18 Source: BlackRock Global Business Intelligence, as of 30/06/24. **19** Source: BlackRock Global Business Intelligence/Broadridge, as of 30/06/24, there were 192 active ETFs in Europe. Compound annual growth rate of 25% from 2020 through year-end 2023.

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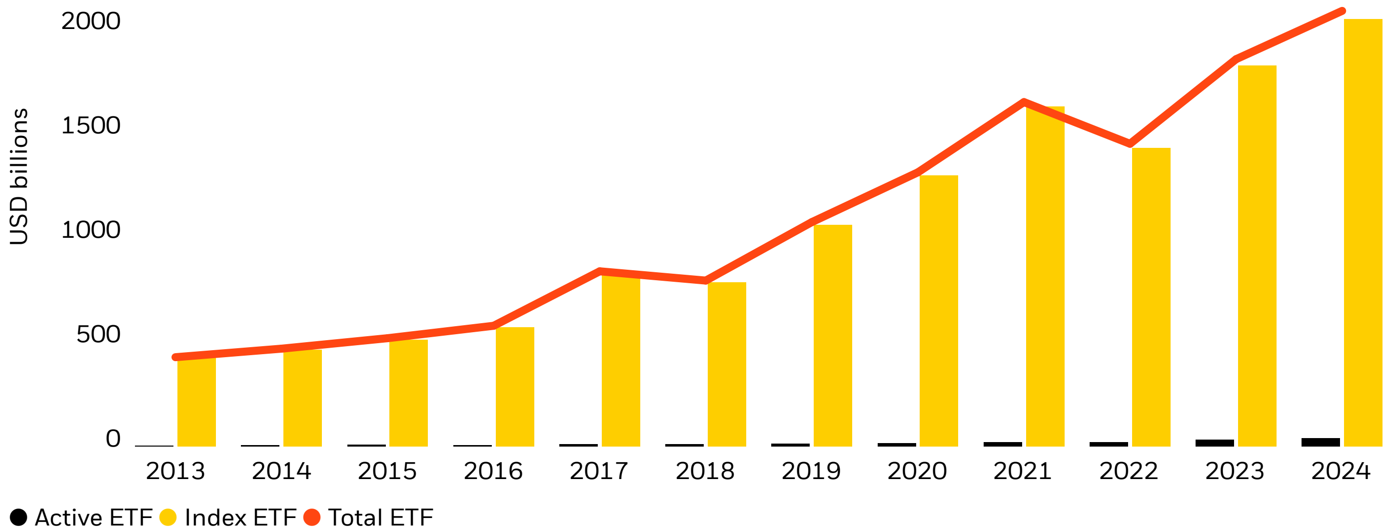
Figure 5: ETF assets under management in EMEA (USD billions) 2013-2024

ETF use has been increasing across EMEA



Source: BlackRock Global Business Intelligence. ETF groupings determined by BlackRock Global Business Intelligence as of June 2024. Numbers for 2024 are as of June.

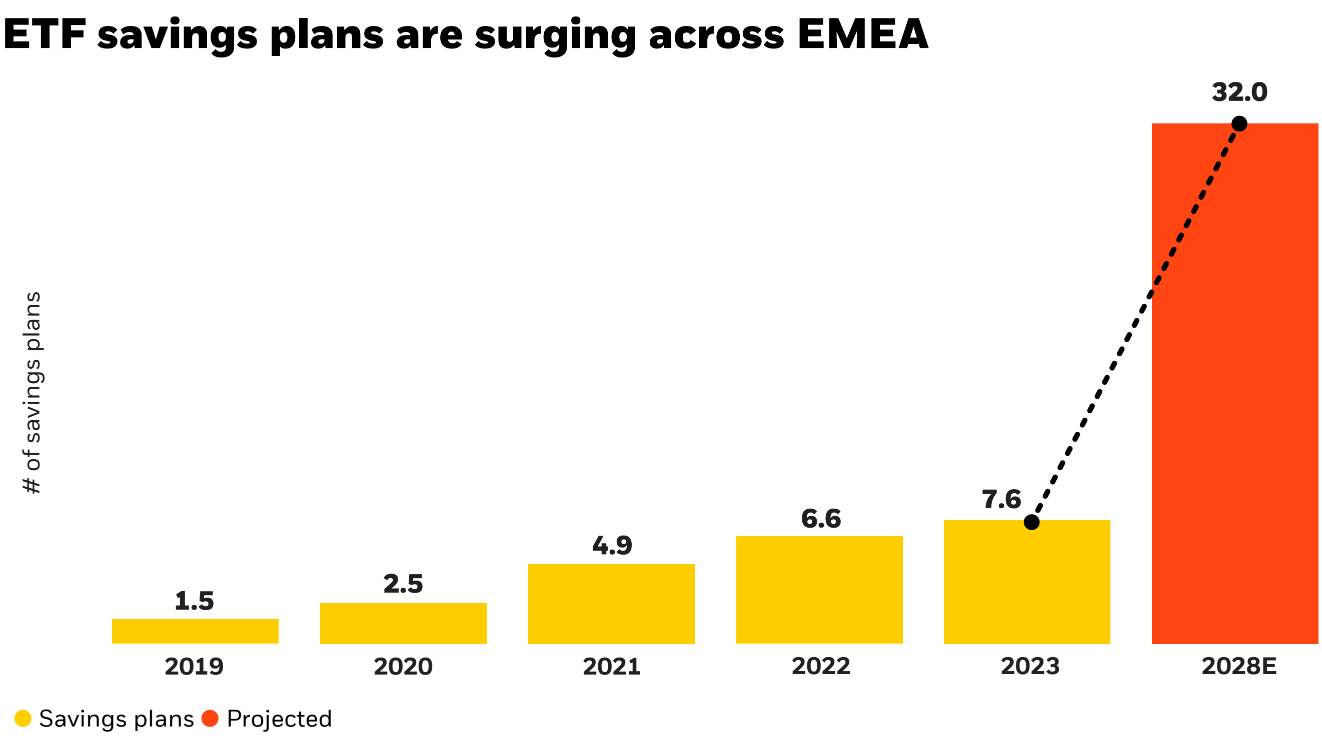
2 Growth of fee-based advisory, financial planning, and models

Centralised and fee-based propositions are expanding across EMEA. In addition, many financial advisors are shifting their business focus towards more holistic wealth planning, combining centralised models with financial planning to strengthen long-term relationships. Access to a broader range of portfolio building blocks will be important to assist this change with increased shares of index at the core, more differentiated alpha, leading investors to active ETFs, in addition to allocations to private markets.

3 The shift from savers to investors

Europe is still largely a savings culture, but digital investing platforms are gaining traction and converting savers to investors. While banking-led distribution continues to dominate the region, growth in digital distribution assets under management is outpacing all other segments — at a 15.5% compound annual growth rate from 2018 to 2023.[20] Digital assets under management in EMEA more than doubled to $1.3 trillion in 2023 from about $620 billion in 2018.[21] This growth in digital has been accelerated by the pandemic, and is combining with socioeconomic shifts that are spurring more needs for investors to take ownership of their retirement funds. Digital banks are now offering monthly investment subscriptions through the ETF wrapper and the number of these plans is expected to surge in coming years. In 2023, there were 7.6 million ETF savings plans across Europe, more than quadrupling from 1.5 million in 2019. (Figure 6). By 2028, this number is expected to reach 32 million. That, combined with the ability to access actively managed strategies through these savings accounts could be a significant driver of active ETF growth.

Figure 6: Actual and projected ETF savings plans in EMEA (millions)



Source: extraETF Research, as at September 2023.

20 Source: BlackRock analysis and bottom up sales input as of 31/12/23. Growth in digital assets under management was 15.5% from 2018 to 2023, compared to 8.2% for both wealth managers and independent financial advisors & platforms and 3.9% for private banks and retail banks. **21** Source: BlackRock analysis as of 31/12/23. Inputs from BlackRock country sales heads, McKinsey Global Growth Cube and Broadridge.

A varied global landscape

In the US, active ETFs are growing fast, with 31% of net asset inflows for ETFs coming from actively managed strategies.[22] Key changes across US regulations, the growth of fee-based advisory and models, and the rise of self-directed investors through online brokerage platforms have combined to increase innovation within active ETFs and drive investor interest.

In Latin America, the landscape for active ETFs is evolving, with varying degrees of engagement across the region. Chilean investors are now able to access certain US-domiciled active ETFs after regulators in 2024 allowed products from other markets to be cross-listed locally for the first time. The offshore market is starting to engage with US-domiciled active ETFs. However, because of more favorable tax treatment, offshore advisors are preferring to engage with versions of active ETFs in UCITS offerings, leveraging the regulatory framework from the EU.

In Asia-Pacific, active ETFs are relatively new. Japan and Singapore implemented rules for active ETFs in 2023, while Australia has the longest history of active ETFs with the first listing in 2015. Locally domiciled active ETFs are also offered in China, Hong Kong, and South Korea. Rulemaking for active ETFs in APAC varies by country and poses challenges to allowing different active ETF structures, such as those using derivatives.

22 Source: BlackRock Global Business Intelligence as of 30/06/24. Through the first half of 2024, active ETFs had $693 billion of AUM in the US.

Conclusion

We believe active ETFs are the next frontier in ETF innovation and are helping to shape the future of the industry, giving investors the potential to unlock value and opportunities by accessing new strategies and markets in the ETF wrapper.

The record growth of active ETFs witnessed in recent years is expected to continue as more investors seek out the wrapper to access active strategies amid a new market regime of greater volatility, uncertainty, and divergence in market performance. Worldwide, active ETFs are taking a larger share of asset inflows, with issuers bringing new ideas and established strategies to the ETF wrapper, though they still have a fraction of the assets held within actively managed mutual funds. In Europe, a surge of growth is expected in coming years powered by the shift to fee-based investing and models, along with the rise of digital wealth and increasing adoption of ETFs overall. Still, we expect active mutual funds will continue to coexist with active ETFs, given regional preferences and business model dynamics.

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