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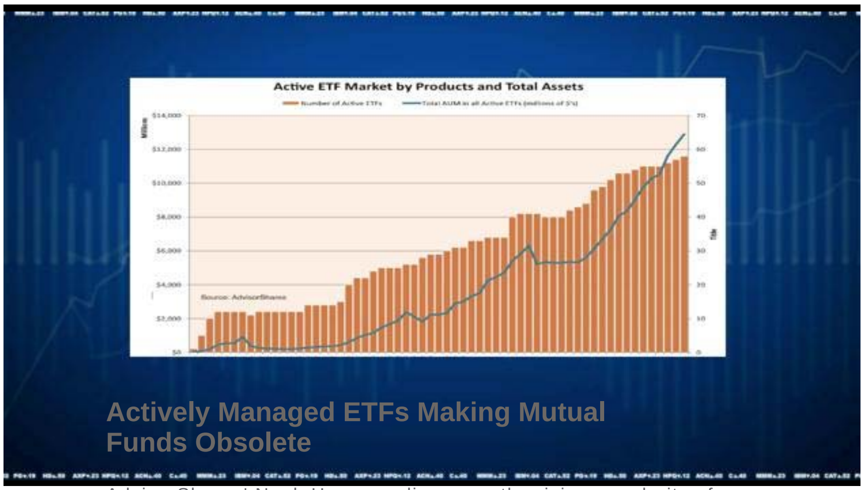
Actively Managed ETFs Are Making Mutual Funds Obsolete

By Jeff Macke | Breakout – Fri, Apr 19, 2013 1:15 PM EDT



AdvisorShares' Noah Hamman discusses the rising popularity of ...Fs

Five years ago actively managed ETFs hit the scene, marking a clear and present danger to the mutual fund industry as we know it. As founder and CEO of AdvisorShares, Noah Hamman was a pioneer in the field. In the attached clip Hamman says his niche of the ETF business is just getting started.

First the basics. An actively managed ETF operates behind the scenes "just like an actively managed mutual fund," according to Hamman. There are fund managers making portfolio decisions within a specific asset class, be it High Yield, Emerging Markets or any other type of exposure an investor is seeking. The main differences for investors are cost savings compared to mutual funds and the ability of investors to trade the assets just as they would a single stock or traditional indexed ETF.

"Simple things that you're used to in the stock market like a limit order, you can't do with a mutual fund," says Hamman. To the degree that onerous mutual fund fees forced investors to buy and hold for the long-term, such flexibility could make it all too easy to start trading ETFs that are in turn being traded by a fund manager.

Of course, we don't live in a buy and hold world anymore. Whatever risk is created by over-trading actively managed funds, it pales in comparison to the risks of some of the ETFs that use derivatives to replicate positions like a triple-levered short of the volatility index. Actively managed or even indexed ETFs will rise and fall based on their underlying assets, not based on whether or not an ETF company has set up a hedge correctly.

Obviously Hamman is selling a product as opposed to doing charity work. AdvisorShares is selling a product similar to mutual funds but targeted to fee-based advisers rather than those collecting the huge commissions associated with traditional mutual funds.

Actively managed ETFs are simply cheaper for individuals with the same risk profile, at least for investors. For the mutual fund companies themselves, the risk is much, much greater.