



## Mythbusted: Proof that active exchange-traded funds (ETFs) can be as tax efficient as passive ETFs

### Key takeaways

**45%**

of mutual funds still paid capital gain distributions\* in 2022, despite poor market returns

**4%**

of ETFs paid capital gain distributions

**0**

Capital Group ETFs paid capital gain distributions

Source: Morningstar based on data for the year ending December 31, 2022 and accessed on January 20, 2023.

\*See key terms section on page three for definition.

Investments are not FDIC-insured, nor are they deposits of or guaranteed by a bank or any other entity, so they may lose value.

For tax-sensitive investors, a major potential benefit of ETFs\* has always been fewer or no capital gain distributions. However, a once-common myth was that ETFs are more tax efficient than mutual funds\* because ETFs are predominantly passively managed. In 2022, Capital Group's actively managed ETFs reinforced that ETFs can be more tax efficient than mutual funds due to the vehicle structure, not because of passive management or active management.\*

## Mutual funds paid capital gains at a much higher rate than ETFs in 2022

There were few places for investors to hide in 2022, with equity and fixed income markets broadly producing double-digit negative returns. Despite weak markets, 45% of all mutual funds paid capital gains in 2022 according to Morningstar. Meanwhile, 4% of all ETFs paid capital gains during the same period.

	Mutual funds	ETFs
<b>All</b>	<b>45%</b>	<b>4%</b>
Actively managed	46%	6%
Passively managed	32%	2%
Equity	60%	4%
Fixed income	13%	3%

Source: Morningstar based on data for the year ending December 31, 2022 and accessed on January 20, 2023.

### % of funds that distributed capital gains in 2022

When comparing the management styles, just 6% of actively managed ETFs and 2% of passively managed ETFs distributed capital gains in 2022. The narrow difference emphasizes that the ETF vehicle structure\* is what brought greater tax efficiency, not the investment approach itself.

## Capital Group ETFs distributed no capital gains in 2022

Capital Group ETFs' short history, a volatile market environment and the features of the vehicle helped our ETFs distribute no capital gains in 2022. While there's no guarantee Capital Group ETFs will continue to pay no capital gain distributions in the future, we continue to leverage an extensive array of resources to help identify opportunities to reduce capital gains distributed to fund shareholders.

\*See key terms section on page three for definition.

Ticker	Fund name	Morningstar category	Expense ratio <sup>†</sup>
<b>CGGR</b>	Capital Group Growth ETF	Large Growth	0.39%
<b>CGXU</b>	Capital Group International Focus Equity ETF	Foreign Large Growth	0.53%
<b>CGGO</b>	Capital Group Global Growth Equity ETF	Global Large-Stock Growth	0.47%
<b>CGDV</b>	Capital Group Dividend Value ETF	Large Value	0.33%
<b>CGUS</b>	Capital Group Core Equity ETF	Large Blend	0.33%
<b>CGCP</b>	Capital Group Core Plus Income ETF	Intermediate-Term Core Plus Bond	0.34%
<b>CGSD</b>	Capital Group Short Duration Income ETF	Short-Term Bond	0.25%
<b>CGMS</b>	Capital Group U.S. Multi-Sector Income ETF	Multisector Bond	0.39%
<b>CGMU</b>	Capital Group Municipal Income ETF	Muni National Intermediate	0.27%

**Category:** ● Growth ● Growth and income ● Taxable ● Tax-exempt

<sup>†</sup>The expense ratio is as of the fund's prospectus available at the time of publication. The expense ratio is estimated.

## Key terms

**Capital gain distribution:** A capital gain distribution is a payment made by a mutual fund or an exchange-traded fund (ETF) that is a portion of the proceeds from the fund's sales of stocks and other assets from within its portfolio. The amount paid corresponds to a pro-rated share of an investor's proceeds from the fund's transaction.

**Passive management:** Passive refers to an investment fund that is managed based on the holdings of a market index or an established set of criteria/rules to select investments from a predetermined list of public companies.

**Active management:** Active refers to a fund that is managed by a portfolio manager or managers that make decisions to buy, hold or sell investments in a portfolio.

**Mutual fund:** A mutual fund is a company that pools money from many investors and invests the money in securities such as stocks, bonds and short-term debt. The combined holdings of the mutual fund are known as its portfolio. Investors buy shares in mutual funds. Each share represents an investor's part ownership in the fund and the income it generates. A mutual fund is purchased/sold directly by the fund or through a financial intermediary, such as a broker-dealer. Investors may pay a sales charge or an asset-based fee, depending on the service relationship with the intermediary. Investors may also purchase on brokerage platforms after paying a ticket charge. Mutual funds are priced at the net asset value of the fund's portfolio determined at the end of each trading day. Mutual funds typically distribute proceeds from the fund's selling activity annually in the form of a capital gain distribution. Investors may be taxed on capital gains realized on the sale of their fund shares.

**Exchange-traded funds (ETFs):** An ETF is a professionally managed fund that combines diversification benefits of a mutual fund with the trading flexibility of a stock. An ETF is purchased/sold like a stock, on an exchange through a brokerage account. Investors may pay a brokerage commission or an asset-based fee, depending on the servicing arrangement with the intermediary. Investors pay the market price on a national exchange based on the bid/ask spread around the intraday net asset value of the ETF. ETFs typically have minimal to no capital gain distributions due to the vehicle structure. Investors may be taxed on capital gains realized on the sale of their fund shares.

**ETF tax efficiency:** ETFs' tax advantages stem from the unique way that they're structured, which allows for two main sources of tax efficiency:

1) Externalization: ETFs trade in the secondary market, like a stock exchange, which largely insulates the fund from individual investors' trading activity. In other words, if an ETF investor decides to sell shares of an ETF, a majority of the time, the transaction will occur in the secondary market, which does not involve any interaction with (or impact to) the fund. The secondary market is where most retail investors buy and sell securities. The most common examples are stock exchanges like the NYSE and NASDAQ but trading in this market can occur across several exchanges, dark pools, direct broker and market maker trades.

2) In-kind redemptions: When selling activity on an exchange does result in a redemption from the fund, it is usually tax-free to remaining investors. ETFs generally satisfy redemption requests in the primary market through an in-kind delivery of securities to an intermediary (rather than cash), which means client redemptions from the fund do not generally create taxable events for remaining shareholders. The primary market is the section of the capital market where new securities are issued. It's also where authorized participants (AP) work with ETF issuers to adjust the supply of ETF shares in the market, either creating new shares or redeeming excess shares. An authorized participant is broker-dealer that has a contracted opportunity with the ETF issuer to create and redeem shares in the primary market to meet market demand. An ETF issuer is a firm that creates, manages and operates an ETF, establishing its strategy and working with regulators and exchanges to obtain permission to offer the fund.

**Investors should carefully consider investment objectives, risks, charges and expenses. This and other important information is contained in the fund prospectuses and summary prospectuses, which can be obtained from a financial professional and should be read carefully before investing.**

Capital Group exchange-traded funds (ETFs) are actively managed and do not seek to replicate a specific index. ETFs are bought and sold through an exchange at the then current market price, not net asset value (NAV), and are not individually redeemed from the fund. Shares may trade at a premium or discount to their NAV when traded on an exchange. Brokerage commissions will reduce returns. There can be no guarantee that an active market for ETFs will develop or be maintained, or that the ETF's listing will continue or remain unchanged.

For CGCP, CGSD and CGMS, the use of derivatives involves a variety of risks, which may be different from, or greater than, the risks associated with investing in traditional securities, such as stocks and bonds.

For CGCP, CGMS and CGMU, lower rated bonds are subject to greater fluctuations in value and risk of loss of income and principal than higher rated bonds.

For CGCP, CGSD, CGMS and CGMU, the return of principal for bond funds and for funds with significant underlying bond holdings is not guaranteed. Fund shares are subject to the same interest rate, inflation and credit risks associated with the underlying bond holdings.

For CGMU, income from municipal bonds may be subject to state or local income taxes and/or the federal alternative minimum tax. Certain other income, as well as capital gain distributions, may be taxable.

For CGGR, CGXU, CGGO, CGUS, CGCP and CGMS, investing outside the United States involves risks, such as currency fluctuations, periods of illiquidity and price volatility. These risks may be heightened in connection with investments in developing countries.

As nondiversified funds, Capital Group ETFs have the ability to invest a larger percentage of assets in securities of individual issuers than a diversified fund. As a result, a single issuer could adversely affect a fund's results more than if the fund invested a smaller percentage of assets in securities of that issuer. See the applicable prospectus for details.

All Capital Group trademarks mentioned are owned by The Capital Group Companies, Inc., an affiliated company or fund. All other company and product names mentioned are the property of their respective companies.

American Funds Distributors, Inc., member FINRA.

This content, developed by Capital Group, home of American Funds, should not be used as a primary basis for investment decisions and is not intended to serve as impartial investment or fiduciary advice.

©2023 Morningstar, Inc. All Rights Reserved. Except for Lipper rating information, the information contained herein: (1) is proprietary to Morningstar and/or its content providers; (2) may not be copied or distributed; and (3) is not warranted to be accurate, complete or timely. Neither Morningstar, its content providers nor Capital Group are responsible for any damages or losses arising from any use of this information. Past performance is no guarantee of future results. Information is calculated by Morningstar. Due to differing calculation methods, the figures shown here may differ from those calculated by Capital Group.