

EUROPE HIGH GRADE INDICES

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Euro high grade index posts only second loss of 2019

It was only the second loss for the high grade Euro Broad Market Index so far in 2019. This setback comes after a three month period of sharply lower interest rates, so perhaps a breather was overdue. At any rate, the rising yield curve gave another opportunity for spread tightening to take the spotlight, and this past month the spread return significantly cushioned the blow from higher rates.

Sovereigns, not credit, lead spread rally

As usual, it was the Sovereign sector itself that contributed the lion's share to the Euro Broad Market's excess return. That is not simply because Sovereigns make up 56% of the Euro Broad Market Index, but because that sector outperformed risk-matched German governments by 0.77%. The next-best credit sector, Quasi-Governments, posted a +0.26% excess return.

Italy continues to tighten, but more room to go

Italy (+2.33% excess return) did the best vs risk-matched Bunds as the country appears to be re-stabilizing after ousting the populist La Lega party from government. However, despite Italy's +11.62% excess return over the last 12 months there is still room for further improvement. Italy's OAS differential versus Spain still stands at 53bps, compared to a 20bps historical average.

Sterling index daily return volatility spikes higher

Despite a modest 0.39% total return for September, the Sterling Broad Market Index saw significant gyrations intra-month. As a result, the short-term volatility of daily total return spiked higher to one of its highest readings – about 2x the 10-year historical average. That may be a bit surprising looking at the month's modest ending total return, but considering the global headline risks combined with the UK domestic political turmoil, it certainly makes sense.

Enhanced rebalancing preview information now available

We will now be publishing daily rebalancing previews starting on the 15th of each month. Previously, preview files were only available on the last three days of the month, so this change gives investors significantly more time to monitor anticipated changes in the index constituencies as they evolve.

Euro Broad Market Index

Overview

Euro high grade index sees only its second loss of the year.

It was only the second loss for the high grade Euro Broad Market Index so far in 2019. The rising German yield curve cost the index nearly 1%. This setback comes after a three month period of sharply lower interest rates, so perhaps a breather was overdue. At any rate, the rising yield curve gave another opportunity for spread tightening to take the spotlight, and this past month the spread return significantly cushioned the blow from higher rates (+0.41%, see Chart 1). As usual, it was the Sovereign sector itself that contributed the lion's share to the Euro Broad Market's excess return. That is not simply because Sovereigns make up 56% of the index, but because that sector outperformed risk-matched German governments by 0.77%. The next-best credit sector, Quasi-Governments, posted a +0.26% excess return.

Euro credit lagged sovereign excess return, but swings are not unusual.

The difference in excess return between the Euro Government Index (EG00) and the Euro Non-Sovereign Index (EX00) can be extreme from month to month, but over longer periods of time the average difference is usually only a few basis points (Exhibit A). In fact, the 10-year average excess return gap is +0.05% in favor of EX00, while the more recent 5- and 3-year averages of the monthly difference is exactly zero. The average spread gap between the Non-Sovereign and Sovereign indices is 28bp over the last 10 years (Exhibit B), so you would expect a modest average pick-up over time. It is also worth mentioning that while the excess returns of the two asset classes are relatively consistent – at least over time – the Non-Sovereign monthly series is notably less volatile, and thus has the higher information ratio.

Exhibit A: Non-Sovereign - Sovereign excess return%

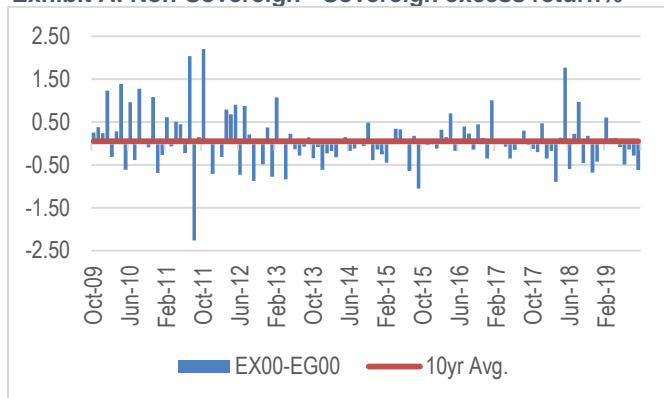


Exhibit B: Non-Sovereign - Sovereign OAS

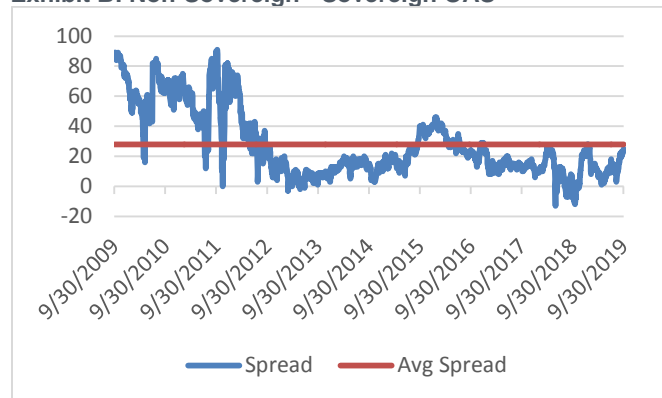


Chart 1: Euro Broad Market Index performance attribution (Sept)

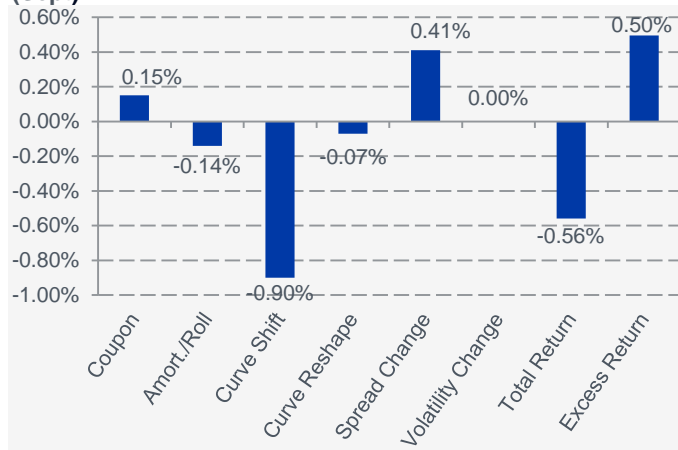


Chart 2: Euro Broad Market Index performance attribution (YTD)

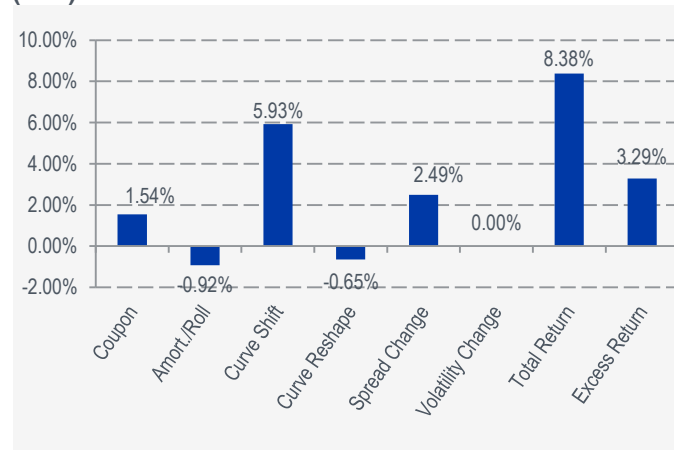


Table 1: Euro Broad Market Index return by sector (EUR terms)

Sector	Total Return		Price Return	
	1-month	YTD	1-month	YTD
Broad Market	-0.559	8.385	-0.706	6.845
Large Cap	-0.558	8.428	-0.705	6.888
Euro Sovereigns	-0.411	10.009	-0.577	8.241
1-3 Years	-0.146	0.693	-0.301	-0.826
3-5 Years	-0.229	2.870	-0.409	1.192
5-7 Years	-0.274	6.150	-0.427	4.578
7-10 Years	-0.459	9.717	-0.609	8.163
10+ Years	-0.690	22.712	-0.869	20.473
Quasi-Governments	-0.807	6.934	-0.911	5.853
1-3 Years	-0.242	0.209	-0.381	-1.098
3-5 Years	-0.500	2.014	-0.591	1.143
5-7 Years	-0.663	4.657	-0.747	3.768
7-10 Years	-0.839	8.532	-0.927	7.639
10+ Years	-1.696	21.978	-1.809	20.562
Securitized/Collateralised	-0.625	4.317	-0.725	3.312
Covered	-0.623	4.304	-0.723	3.299
Asset backed	-1.150	10.815	-1.296	9.378
Corporates	-0.757	6.746	-0.901	5.266
1-3 Years	-0.257	1.384	-0.421	-0.190
3-5 Years	-0.567	4.137	-0.701	2.793
5-7 Years	-0.867	7.989	-1.005	6.542
7-10 Years	-1.098	11.844	-1.233	10.382
10+ Years	-1.699	17.868	-1.848	16.086
Financial	-0.649	5.954	-0.797	4.440
Non- Financial	-0.817	7.179	-0.959	5.718
AAA Rated	-1.401	7.853	-1.522	6.588
AA Rated	-0.885	4.409	-1.010	3.186
A Rated	-0.878	5.937	-1.004	4.626
BBB Rated	-0.628	7.919	-0.790	6.241

The German curve moved higher for the first time in three months, and in a nearly perfect parallel shift. But the move up was not enough to bring the curve out of negative territory.

Chart 3: Monthly change in the German curve

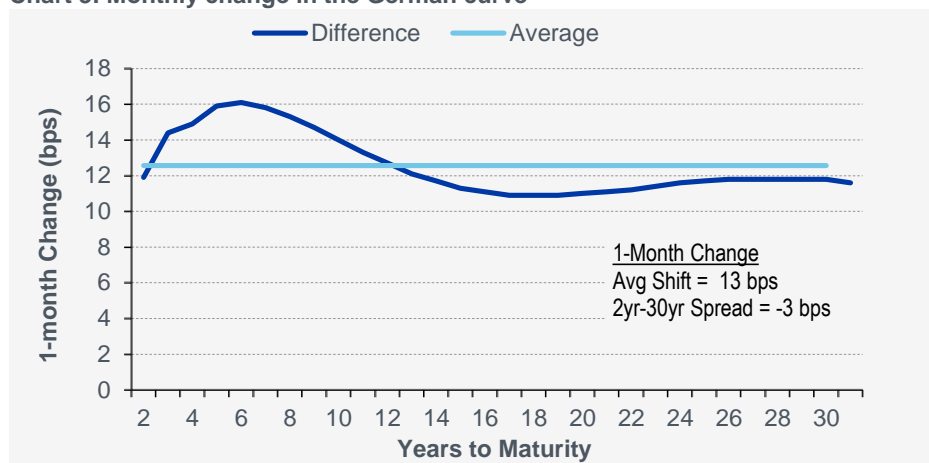


Chart 4: Duration-Adjusted German Government price returns (Aug)

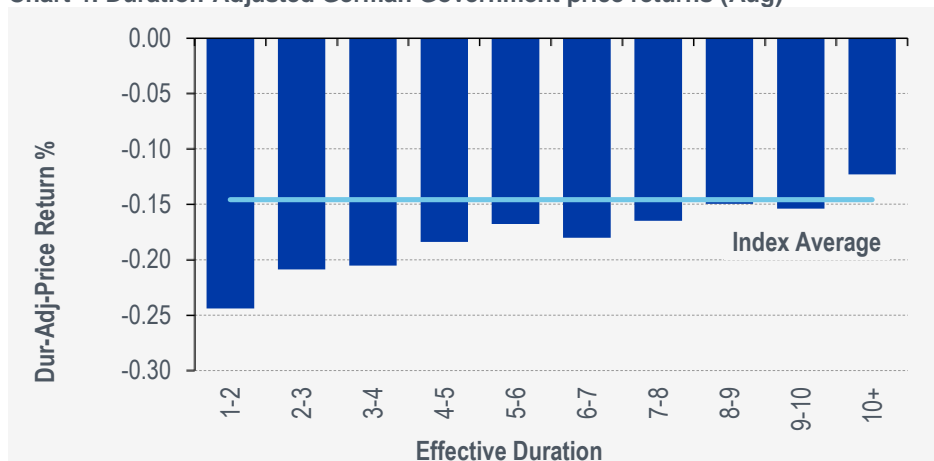


Table 2: Duration-matched combinations vs. German Government Index total return

Eff. Duration	1-2 yr	2-3 yr	3-4 yr	4-5 yr	5-6 yr	6-7 yr	7-8 yr	8-9 yr	9-10 yr	10+
1-2 yr	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	(0.05)	(0.05)	0.08
2-3 yr		n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	(0.05)	(0.06)	0.05
3-4 yr			n.a.	n.a.	n.a.	n.a.	n.a.	(0.05)	(0.07)	0.01
4-5 yr				n.a.	n.a.	n.a.	n.a.	(0.06)	(0.07)	(0.03)
5-6 yr					n.a.	n.a.	n.a.	(0.06)	(0.08)	(0.04)
6-7 yr						n.a.	n.a.	(0.06)	(0.09)	(0.08)
7-8 yr							n.a.	(0.07)	(0.10)	(0.10)
8-9 yr								n.a.	n.a.	n.a.
9-10 yr									n.a.	n.a.
10+										n.a.

Note: Each cell represents a combination of the bonds in each intersecting duration bands of the index weighted to match the average duration of the German Sovereign Index.

Excess Returns

The 13bp average sell-off in the German government yield curve was an easy hurdle for all Eurozone member countries with the exception of Slovakia (-0.03%) and Slovenia (-0.35%). All others managed to beat Bunds on a duration-matched basis. Italy (+2.33%) did better than any other country by a big margin as the Southern European nation appears to be re-stabilizing after ousting the populist La Lega party from government. However, despite Italy's +11.62% excess return over the last 12 months there is still room for further improvement. Italy's OAS differential versus Spain still stands at 53bps, compared to a 20bps historical average.

Table 3: Euro Government Index excess returns by country

		Effective Duration	1-mth Chg OAS (1)	Excess Return		
				1-mo	3-mo	12-mo
Sovereign						
AAA						
Germany	G0D0	8.36	0	0.04	0.02	0.07
Luxembourg	G0LU	4.82	-3	0.15	0.27	0.54
Netherlands	G0N0	9.07	-3	0.19	0.06	0.01
AA						
Austria	G0H0	11.52	-2	0.24	0.38	0.28
Belgium	G0G0	10.57	-6	0.72	0.96	1.38
Finland	G0K0	7.84	-2	0.08	0.11	0.04
France	G0F0	8.93	-1	0.12	0.16	0.55
A						
Ireland	G0R0	8.78	-7	0.78	-0.22	0.82
Latvia	G0LV	13.85	-8	1.02	3.72	1.78
Slovakia	G0SL	8.47	1	-0.03	0.55	0.89
Slovenia	G0SV	9.43	2	-0.35	-0.36	1.13
Spain	G0E0	8.30	-7	0.67	0.07	3.82
Lithuania	G0LT	10.81	-10	1.15	2.84	0.03
BBB						
Italy	G0I0	7.34	-31	2.33	6.72	11.62
Portugal	G0U0	7.05	-8	0.64	0.17	5.59
Sovereign	EG00	8.51	-9	0.77	1.66	3.55

1-mnth Change OAS spread is based on the constituents for the month and excludes the impact of the end of month re-balancing. Spread changes are averaged on the basis of beginning-of-month bond weights.

Euro Corporates (+0.06%) basically managed to keep pace with duration-matched German governments, but six sectors actually recorded negative excess returns. All sectors but two posted excess returns within a +/- 0.20% band. The only two that broke out of that corridor were Energy (+0.41%) and Capital Goods (+0.77%). Energy benefited from bounce in Pemex (+3.45%; 10.1% weight), while Capital Goods was propelled by a strong rebound in General Electric (+4.27%; 19.4% weight). GE's sizable rally followed its big loss in August as an accounting fraud investigation was announced that related to losses at its Baker Hughes subsidiary.

Table 4: Euro Non Sovereign Index excess returns by sector

		Effective Duration	1-mth Chg OAS (1)	Excess Return		
				1-mo	3-mo	12-mo
Non Sovereign						
Quasi-Government	EQ00	7.30	-2	0.27	0.63	0.86
Covered Bonds	ECV0	4.90	-4	0.16	0.49	1.31
Asset Backed	EA00	6.78	4	-0.14	-0.17	0.82
Securitized/Collateralized	EL00	4.90	-3	0.16	0.49	1.31
Banking	EBBA	4.21	-1	0.10	0.60	2.21
Financial Services	EBFS	5.37	1	0.04	0.71	2.19
Insurance	EBIN	5.55	2	-0.02	1.42	4.77
Sub-Total Financial	EB00	4.44	0	0.08	0.71	2.55
Automotive	EJAU	4.65	-1	0.18	0.70	2.09
Basic Industry	EJBS	5.01	1	0.03	0.40	1.82
Capital Goods	EJCP	5.95	-7	0.77	0.21	0.51
Consumer Goods	EJCS	6.05	4	-0.20	0.30	1.39
Energy	EJEN	5.25	-8	0.41	0.74	1.82
Healthcare	EJHC	7.04	3	-0.12	0.24	1.41
Leisure	EJLE	3.68	-4	0.15	0.55	1.34
Media	EJME	5.06	-4	0.11	0.62	2.45
Real Estate	EJRE	5.75	0	0.06	0.60	3.12
Retail	EJRL	5.54	0	0.00	0.45	0.79
Services	EJSE	4.96	1	0.06	0.61	2.03
Technology & Electronics	EJTE	5.52	2	-0.04	0.40	1.54
Telecommunications	EJTC	6.22	3	-0.16	0.37	2.48
Transportation	EJTR	5.96	3	-0.16	0.32	1.90
Sub-Total Industrial	EJ00	5.68	0	0.05	0.45	1.85
Sub-Total Utility	EK00	5.75	0	0.04	0.58	2.63
Corporate	ER00	5.25	1	0.06	0.56	2.18
Non-Sovereign	EX00	5.91	-1	0.15	0.57	1.71

1 Change OAS spread is based on the constituents for the month and excludes the impact of the end of month re-balancing.
Spread changes are averaged on the basis of beginning-of-month bond weights.

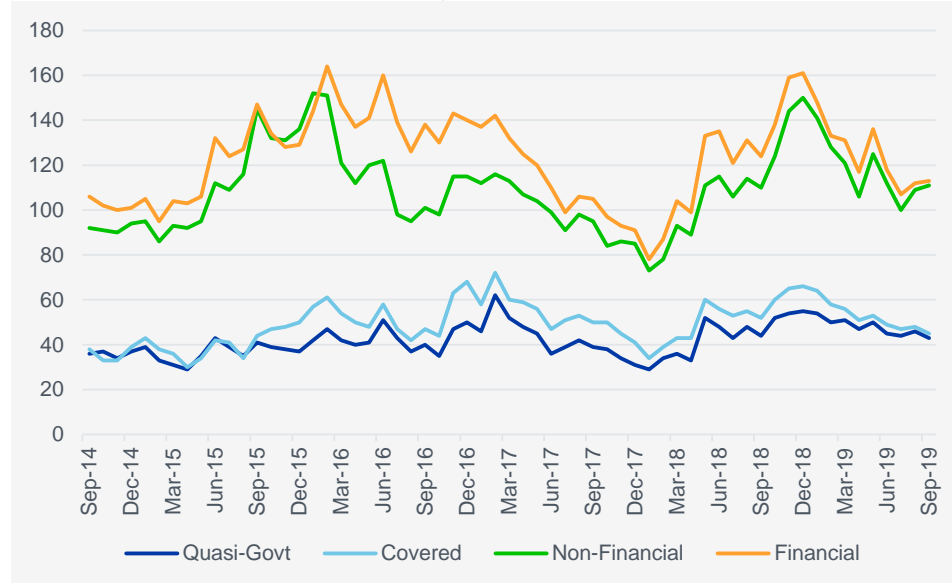
A total of eight Banking issuers were included in the top-twenty performers list, and five of them were British (Barclays, Royal Bank of Scotland, Lloyds, HSBC and Nationwide). However, neither a Banking issuer nor a British company was included in the top three. Those positions went to General Electric (+4.27%), Pemex (+3.45%) and Volkswagen (+0.37%). And in the case of the last one it was mostly due to its sheer weight, which at 2.05% share it is the second-biggest issuer in the Euro Corporate Index. At the other end of the spectrum, EDF (-0.61%) took the bottom position in the table as it announced it will cost an extra £2.9bn to complete the controversial Hinkley Point C nuclear power plant in the south-west of England.

Table 5: Best/Worst performers ranked by weighted excess returns

Rank	Issuer	1-mo Chg OAS ¹	Excess Return	Beginning of Month % Weight	Weighted Excess Return	Sector
Top Twenty Performers:						
1	GE	-54	4.27	0.63	0.0268	Capital Goods
2	PEMEX	-77	3.45	0.53	0.0182	Energy
3	VW	-2	0.37	2.05	0.0077	Automotive
4	ISPIM	-12	0.72	0.55	0.0040	Banking
5	UCGIM	-18	0.76	0.50	0.0038	Banking
6	BACR	-15	0.70	0.53	0.0037	Banking
7	ASSGEN	-11	0.75	0.43	0.0032	Insurance
8	MDT	-4	0.68	0.47	0.0032	Healthcare
9	RBS	-20	0.94	0.34	0.0032	Banking
10	AUCHAN	-33	1.46	0.19	0.0028	Retail
11	LLOYDS	-11	0.77	0.33	0.0025	Banking
12	TOTAL	-3	0.23	1.07	0.0025	Energy
13	GAZPRU	-24	1.16	0.21	0.0024	Energy
14	DAIGR	-2	0.20	1.06	0.0021	Automotive
15	DB	-7	0.37	0.49	0.0018	Banking
16	MRKGR	-2	0.70	0.23	0.0016	Healthcare
17	HSBC	-3	0.24	0.67	0.0016	Banking
18	ENELIM	-1	0.24	0.62	0.0015	Utility
19	NWIDE	-10	0.82	0.17	0.0014	Banking
20	BHP	-9	0.48	0.28	0.0013	Basic Industry
				11.33	0.0952	
Bottom Twenty Performers:						
697	CFRVX	9	-0.78	0.1816	-0.0014	Retail
698	BPLN	5	-0.22	0.7037	-0.0016	Energy
699	NNGRNV	14	-0.56	0.2801	-0.0016	Insurance
700	JNJ	11	-1.06	0.1759	-0.0019	Healthcare
701	ABESM	12	-0.63	0.3047	-0.0019	Transportation
702	DGFP	6	-0.36	0.5956	-0.0021	Transportation
703	ABNANV	11	-0.35	0.6146	-0.0021	Banking
704	ANNGR	6	-0.44	0.5013	-0.0022	Real Estate
705	CMZB	11	-0.43	0.5306	-0.0023	Banking
706	ULFP	6	-0.37	0.6474	-0.0024	Real Estate
707	VZ	6	-0.42	0.5588	-0.0024	Telecommunications
708	SANFP	5	-0.34	0.7522	-0.0026	Healthcare
709	DT	5	-0.29	0.9176	-0.0026	Telecommunications
710	F	31	-0.87	0.3104	-0.0027	Automotive
711	T	8	-0.33	0.8388	-0.0027	Telecommunications
712	TELEFO	6	-0.34	0.8093	-0.0028	Telecommunications
713	MO	34	-2.08	0.1849	-0.0039	Consumer Goods
714	ATLIM	31	-1.33	0.3146	-0.0042	Transportation
715	BATSLN	19	-1.27	0.3390	-0.0043	Consumer Goods
716	EDF	10	-0.61	1.0676	-0.0066	Utility
				10.63	0.7292	

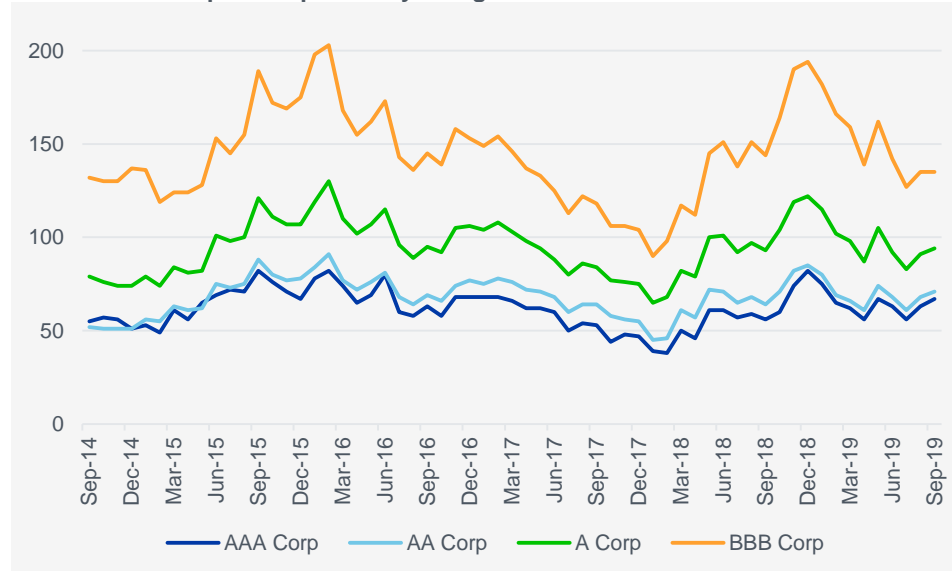
Spread changes were mixed in September, with the Quasi Government and Covered sectors tightening while the Corporate sector widened. All sectors tightened over 3Q-19, with the Covered sector tightening the most – and twice as much as the next sector – at least on a percentage basis (-8%).

Chart 5: Euro credit market spreads by sector



All Corporate rating spreads continued to widen and, for the second consecutive month, the highest-rated segments moved more on a percentage basis.

Chart 6: Euro corporate spreads by rating



Composition

The Euro Government Index saw a 0.11-year rebalancing duration extension that was slightly above the 10-year September average (+0.08yr). However, the index's duration remained practically unchanged MoM (-0.01yrs) as the rebalancing shift was not enough to offset both the monthly duration drift and the impact of the rising yield curve. The Sovereign sector gave up 0.16% share in the Euro Broad Market Index, Corporates gained 0.33% versus a month ago. Now at 21.10%, this is the most Corporates have represented in the Euro Broad Market Index since July 2011.

Table 6: Euro Broad Market Index characteristics

Sector	Effective Mod Dur			% Sector			% of Broad Market		
	30-Sep	31-Aug	Chg	30-Sep	31-Aug	Chg	30-Sep	31-Aug	Chg
Broad Market	7.38	7.39	-0.01	100.00	100.00	0.00	100.00	100.00	0.00
Euro Sovereigns	8.51	8.52	-0.01	100.00	100.00	0.00	56.37	56.52	-0.16
Austria	11.52	11.85	-0.33	3.53	3.54	-0.02	1.99	2.00	-0.02
Belgium	10.57	10.17	0.40	6.05	6.31	-0.27	3.41	3.57	-0.16
Finland	7.84	7.63	0.20	1.39	1.44	-0.05	0.78	0.82	-0.03
France	8.93	9.05	-0.12	25.21	25.06	0.15	14.21	14.17	0.04
Germany	8.36	8.31	0.05	15.97	16.30	-0.33	9.00	9.21	-0.21
Ireland	8.78	8.88	-0.10	1.83	1.81	0.02	1.03	1.02	0.01
Italy	7.34	7.23	0.10	23.54	23.22	0.31	13.27	13.13	0.14
Latvia	13.85	14.01	-0.17	0.07	0.07	0.00	0.04	0.04	0.00
Lithuania	10.81	10.91	-0.11	0.04	0.04	0.00	0.02	0.02	0.00
Luxembourg	4.82	4.91	-0.09	0.08	0.08	0.00	0.04	0.04	0.00
Netherlands	9.07	9.21	-0.15	4.68	4.68	0.00	2.64	2.64	-0.01
Portugal	7.05	7.12	-0.07	2.27	2.24	0.03	1.28	1.27	0.01
Slovakia	8.47	8.56	-0.09	0.56	0.56	0.00	0.32	0.32	0.00
Slovenia	9.43	9.59	-0.16	0.42	0.42	-0.01	0.24	0.24	0.00
Spain	8.30	8.37	-0.08	14.35	14.19	0.16	8.09	8.02	0.07
Cyprus	6.69	6.75	-0.06	0.10	0.10	0.00	0.05	0.05	0.00
Quasi-Governments	7.41	7.47	-0.06	100.00	100.00	0.00	14.67	14.76	-0.09
Foreign Sovereigns	7.41	7.36	0.05	7.42	7.52	-0.10	1.09	1.11	-0.03
Agencies	6.12	6.21	-0.09	17.32	17.32	0.00	2.54	2.57	-0.02
Local Governments	7.66	7.68	-0.02	20.53	20.67	-0.14	3.01	3.06	-0.05
Supranationals	7.95	7.96	-0.01	23.43	23.47	-0.04	3.44	3.48	-0.04
Government Guaranteed	7.55	7.69	-0.14	31.30	31.03	0.27	4.59	4.60	0.00
Securitised/Collateralised	4.90	4.92	-0.01	100.00	100.00	0.00	7.86	7.95	-0.09
Covered Bonds	4.90	4.91	-0.01	99.69	99.69	0.00	7.84	7.92	-0.09
Asset backed	6.78	6.90	-0.12	0.31	0.31	0.00	0.02	0.02	0.00
Corporate	5.25	5.18	0.07	100.00	100.00	0.00	21.10	20.77	0.33
Financials	4.44	4.44	0.00	35.47	35.82	-0.35	7.49	7.44	0.05
Non-Financials	5.69	5.59	0.10	64.53	64.18	0.35	13.62	13.33	0.29
Broad Market	7.38	7.39	-0.01	100.00	100.00	0.00	100.00	100.00	0.00

Sterling Broad Market Index

Overview

After a 5+% two-month run, sterling high grade posts a “modest” return.

It was an almost notably modest return for the Sterling Broad Market Index in September (0.39%). A small Gilt rally gave a positive cast to performance, but after the strong rally over the prior two-month period delivered a 5.26% total return it seems exceedingly modest. But that is an illusion created by the unusually large scale of the June-August rally. In fact, given the 1% starting yield of the Sterling Broad Market Index, this past month's return represents over 4x the amount of pure interest accrual.

Daily return volatility spikes to twice the historical average.

The relatively staid performance of the sterling high grade index in September was the result of a roller-coaster ride over the course of the month. In the first couple of days the MTD return of the Sterling Broad Market Index was as over 1%, then slipped back to a nearly 2.5% loss by midmonth before recovering over the next few weeks. As a result the short-term volatility of daily total return spiked higher to one of its highest readings (1.72, Exhibit C), and about 2x the 10-year historical average. That may be a bit surprising looking at the month's modest ending total return, but considering the global headline risks combined with the UK domestic political turmoil, it certainly makes sense.

Exhibit C: Sterling Broad Market Index 30-day Standard Deviation of Daily Total Return %

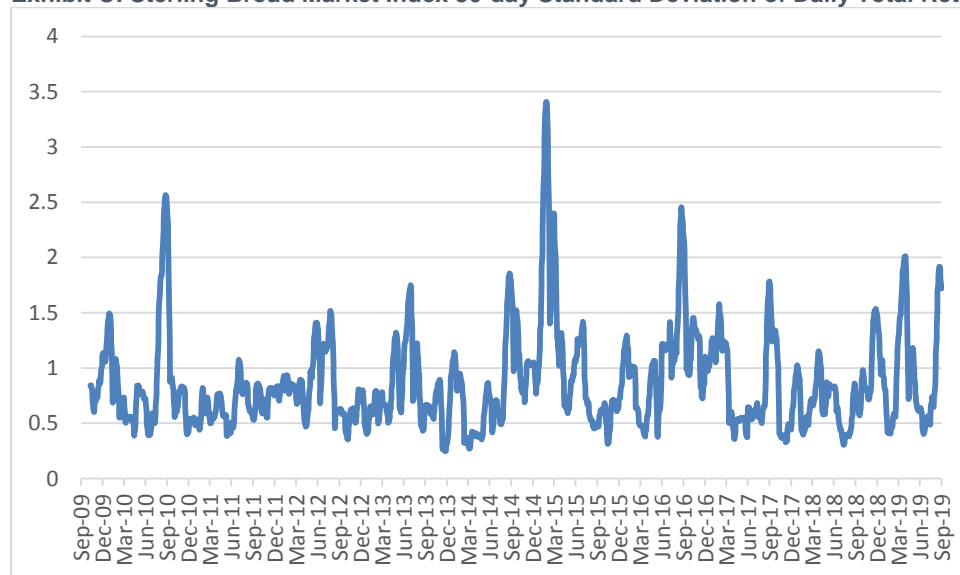


Chart 7: Sterling Broad Market Index performance attribution (Sept)

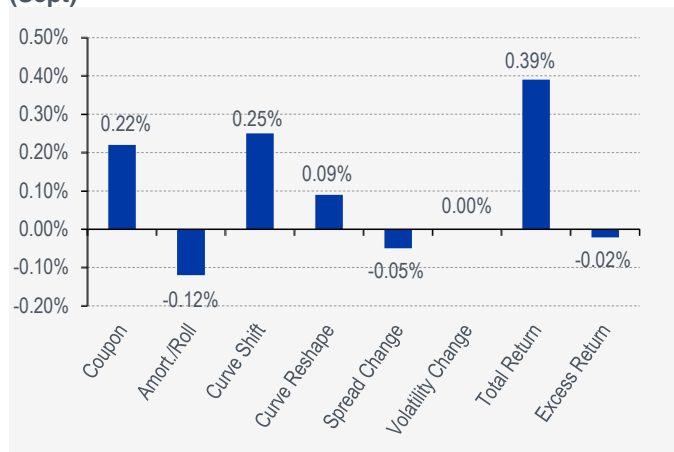


Chart 8: Sterling Broad Market Index performance attribution (YTD)

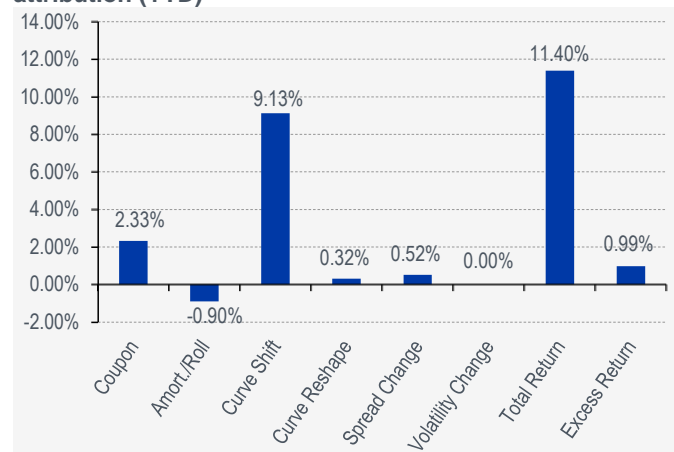


Table 8: Sterling Broad Market Index returns by sector (local)

	Ticker	# Issues	Total Return		Price Return	
			1-month	YTD	1-month	YTD
Broad Market	UK00	1244	0.389	11.398	0.170	9.071
Gilt	G0L0	42	0.530	11.953	0.334	9.846
1-3 Years	G1L0	6	0.085	1.069	-0.181	-1.483
3-5 years	G2L0	4	0.217	2.696	0.104	1.568
5-7 Years	G3L0	4	0.277	4.583	0.072	2.475
7-10 Years	G4L0	4	0.050	7.436	-0.158	5.476
10+ Years	G9L0	24	0.782	18.566	0.594	16.364
All Non-Gilts	UN00	1202	0.080	10.225	-0.191	7.413
1-3 Years	UN01	251	0.116	2.679	-0.124	0.350
3-5 years	UN02	180	0.268	4.820	0.013	2.502
5-7 Years	UN03	168	0.260	7.742	-0.007	4.935
7-10 Years	UN04	170	0.025	9.790	-0.267	6.698
10+ Years	UN09	433	-0.039	16.873	-0.323	13.715
AAA Rated	UN10	167	0.123	6.321	-0.065	4.435
AA Rated	UN20	168	0.096	9.301	-0.112	7.127
A Rated	UN30	376	0.035	12.060	-0.239	9.146
BBB Rated	UN40	491	0.084	11.354	-0.250	7.871
Foreign & Quasi- Governments	UQ00	184	0.156	6.720	-0.026	4.878
1-3 Years	UQ01	69	0.064	1.712	-0.068	0.409
3-5 Years	UQ02	40	0.192	3.476	0.073	2.396
5-7 Years	UQ03	21	0.247	5.545	0.065	3.547
7-10 Years	UQ04	17	0.209	9.686	-0.062	6.797
10+ Years	UQ09	37	0.177	15.439	-0.065	12.761
Corporate & Collateralized	UC00	1018	0.058	11.237	-0.238	8.140
1-3 Years	UC01	182	0.146	3.337	-0.157	0.322
3-5 years	UC02	140	0.304	5.393	-0.016	2.526
5-7 Years	UC03	147	0.262	8.090	-0.020	5.148
7-10 Years	UC04	153	-0.032	9.797	-0.331	6.646
10+ Years	UC09	396	-0.071	17.109	-0.361	13.877
AAA Rated	UC10	45	0.238	9.005	-0.015	6.409
AA Rated	UC20	112	0.017	9.733	-0.205	7.417
A Rated	UC30	374	0.033	12.084	-0.241	9.168
BBB Rated	UC40	487	0.063	11.233	-0.270	7.766

After back-to-back double-digit basis point curve rallies, the Gilt curve fell by only a relatively modest 2bp on average.

Chart 9: 1-Month change in the Gilt curve

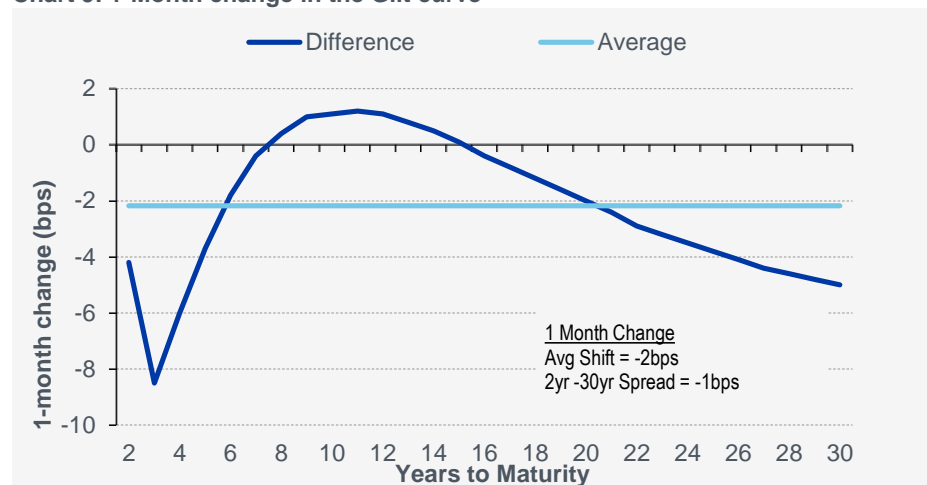
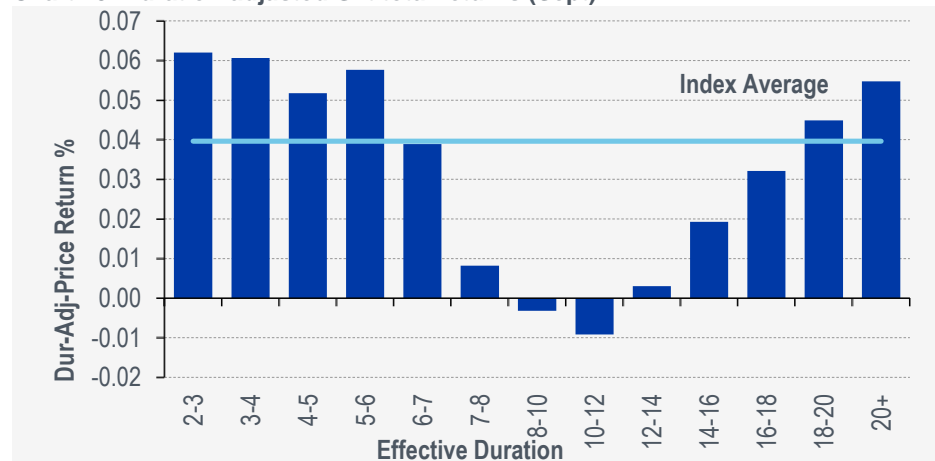


Chart 10: Duration-adjusted Gilt total returns (Sept)



Excess Returns

The Sterling Corporate Index (-0.17%) posted its second consecutive negative excess return, and just the third of 2019. Most sectors ended with a loss vs risk-matched Gilts, with the only exceptions Banking (+0.22%), Insurance (+0.64%) and Capital Goods (+0.89%). Capital Goods benefited from the rebound of General Electric (+1.54%) following August's sizable losses, as that issuer accounts for two thirds of the sector weight. At the other side of the spectrum, the worst-performing sector was Utility (-0.72%), mostly due to French issuer EDF (-1.61%; 16.9% weight), as it announced it will cost an extra £2.9bn to complete the controversial Hinkley Point C nuclear power plant in the south-west of England. Quasi-governments (-0.03%) and Securitized/Collateralized (-0.16%) also ended behind duration-matched Gilts. In the case of Securitized/Collateralized, like Corporates, September's result was a third negative monthly excess return and first negative calendar quarter of the year.

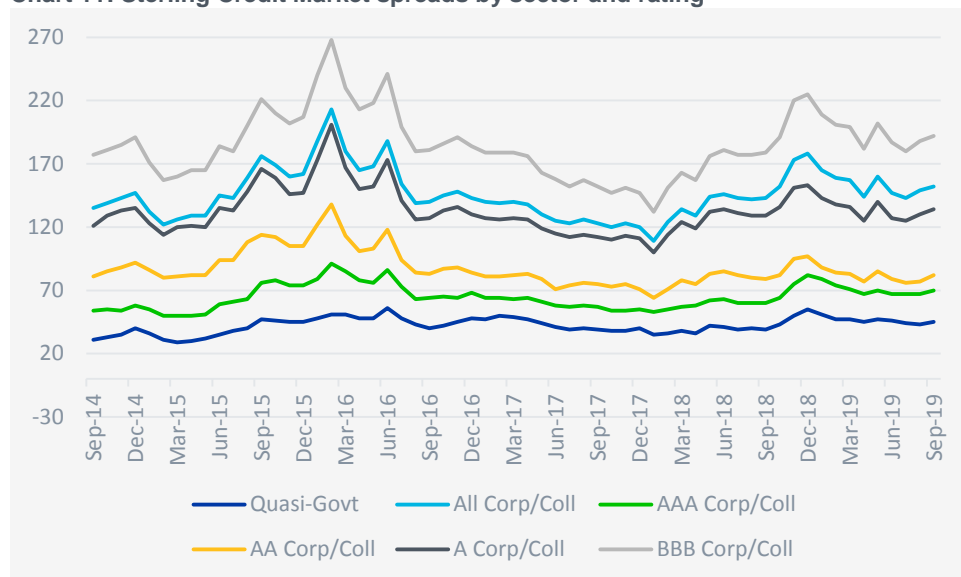
Table 9: Sterling Broad Market excess returns by sector

		Effective Duration	1-mo Chg OAS (1)	Excess Returns		
				1-mo	3-mo	12-mo
Quasi & Foreign Sov	UQ00	6.404	2	-0.03	0.21	0.18
Corporates:						
Banking	UFBA	5.91	-1	0.22	0.10	2.11
Financial Services	UFFS	9.84	3	-0.29	-0.27	1.42
Insurance	UFIN	6.38	-4	0.64	0.10	3.58
Sub-Total Financial	UF00	6.356	-1	0.29	0.07	2.45
Automotive	UIAU	3.19	9	-0.15	0.42	1.53
Basic Industry	UIBS	7.71	4	-0.35	-0.11	1.77
Capital Goods	UICP	8.53	-10	0.89	-1.03	-5.30
Consumer Goods	UICS	6.86	6	-0.40	0.22	-0.23
Energy	UIEN	6.99	4	-0.27	-0.02	1.44
Healthcare	UIHC	12.21	7	-0.70	-0.87	-0.61
Leisure	UILE	4.81	4	-0.07	0.49	1.17
Media	UIME	8.81	6	-0.59	-0.68	1.37
Real Estate	UIRE	12.77	1	-0.10	0.35	1.19
Retail	UIRL	8.30	7	-0.52	-0.31	0.71
Services	UISE	19.92	3	-0.30	0.33	2.30
Technology & Electronics	UITE	7.02	4	-0.19	0.06	0.69
Telecommunications	UITC	10.25	6	-0.54	-0.26	1.44
Transportation	UITR	9.62	2	-0.20	0.29	1.42
Sub-Total Industrial	UI00	9.952	4	-0.27	0.00	0.75
Sub-Total Utility	UU00	9.828	7	-0.72	-0.60	1.97
Total Corporate	UR00	8.728	3	-0.17	-0.09	1.57
Securitized/Collateralized	UL00	7.791	3	-0.16	-0.44	0.31
Grand Total Non- Gilt	UN00	8.089	3	-0.14	-0.07	1.09

(1) Change OAS spread is based on the constituents for the month and excludes the impact of the end of month re-balancing. Spread changes are averaged on the basis of beginning-of-month bond weights.

After previously tightening, all credit segment spreads widened. By the end of the quarter only the Quasi Government sector was able to post a modest Q3 spread rally.

Chart 11: Sterling Credit Market spreads by sector and rating



Composition

UK Gilt duration saw its third consecutive double-digit duration extension MoM to extend the index to another new all-time high of 13.61 years. At the rebalancing the Gilt index saw a 0.25-year extension, and while this might appear unusually large the last five of six October rebalancing extensions have been equal or bigger. This extension was partially the result of taps in the 6-, 10- and 35-year bonds for a total £10bn, but a larger impact came from the removal of a £25bn short bond.

Table 10: Sterling Broad Market Index characteristics

	Effective Mod Dur			% Sector			% of Broad Market		
	30-Sep	31-Aug	Chg	30-Sep	31-Aug	Chg	30-Sep	31-Aug	Chg
Broad	11.87	11.74	0.14	100.00	100.00	0.00	100.00	100.00	0.00
Gilts	13.61	13.38	0.23	100.00	100.00	0.00	68.60	68.77	-0.17
For. & Quasi-Govt	6.40	6.47	-0.06	100.00	100.00	0.00	6.93	6.88	0.06
Agency	7.45	7.50	-0.05	11.55	11.59	-0.03	0.80	0.80	0.00
Government Guaranteed	5.94	5.99	-0.05	41.86	42.13	-0.27	2.90	2.90	0.00
Local-Authority	5.84	5.95	-0.11	5.46	5.31	0.15	0.38	0.36	0.01
Supranational	6.40	6.45	-0.05	37.08	36.94	0.13	2.57	2.54	0.03
Foreign Sovereign	9.11	9.25	-0.14	4.06	4.04	0.02	0.28	0.28	0.00
Corporate & Collateralized	8.57	8.58	-0.01	100.00	100.00	0.00	24.47	24.35	0.11
Asset backed	9.13	9.21	-0.08	9.20	9.49	-0.29	2.25	2.31	-0.06
Automotive	3.19	3.22	-0.03	2.73	2.58	0.15	0.67	0.63	0.04
Banking	5.91	5.92	-0.01	18.11	17.76	0.35	4.43	4.32	0.11
Basic Industry	7.71	7.76	-0.05	1.77	1.79	-0.02	0.43	0.44	0.00
Capital Goods	8.53	8.27	0.26	1.59	1.64	-0.05	0.39	0.40	-0.01
Consumer Goods	6.86	6.92	-0.06	3.76	3.80	-0.04	0.92	0.93	0.00
Energy	6.99	6.69	0.30	2.32	2.36	-0.04	0.57	0.57	-0.01
Financial Services	9.84	9.93	-0.09	2.29	2.30	-0.01	0.56	0.56	0.00
Healthcare	12.21	12.28	-0.07	2.39	2.41	-0.02	0.58	0.59	0.00
Insurance	6.38	6.30	0.08	7.20	6.95	0.25	1.76	1.69	0.07
Leisure	4.81	4.89	-0.08	0.32	0.32	0.00	0.08	0.08	0.00
Media	8.81	8.88	-0.07	0.94	0.95	-0.01	0.23	0.23	0.00
Real Estate	12.77	12.79	-0.02	8.98	8.96	0.02	2.20	2.18	0.01
Retail	8.30	8.37	-0.07	2.04	2.06	-0.02	0.50	0.50	0.00
Services	19.92	19.81	0.11	2.14	2.13	0.00	0.52	0.52	0.00
Technology & Electronics	7.02	7.11	-0.09	1.19	1.19	0.00	0.29	0.29	0.00
Telecommunications	10.25	10.15	0.10	6.18	6.24	-0.06	1.51	1.52	-0.01
Transportation	9.62	9.61	0.01	3.23	3.26	-0.03	0.79	0.79	0.00
Utility	9.83	9.71	0.12	15.49	15.64	-0.16	3.79	3.81	-0.02

Return Attributions

Table 11: Pan-European index return attribution by sector (Sept)

	Index	Coupon	Amort./Roll	Curve Shift	Curve Reshape	Spread Change	Volatility Return	Total Return	Excess Return
Pan-Europe Broad Market	PE00	0.16%	-0.14%	-0.73%	-0.04%	0.33%	0.00%	-0.43%	0.41%
Euro Markets									
Euro Broad Market	EMU0	0.15%	-0.14%	-0.90%	-0.07%	0.41%	0.00%	-0.56%	0.50%
Euro Large Cap	EMUL	0.15%	-0.14%	-0.90%	-0.07%	0.41%	0.00%	-0.56%	0.50%
Euro Governments	EG00	0.17%	-0.16%	-1.04%	-0.05%	0.67%	0.00%	-0.41%	0.77%
Quasi-Governments	EQ00	0.10%	-0.12%	-0.91%	-0.07%	0.19%	0.00%	-0.81%	0.26%
Pfandbriefe	EP00	0.05%	-0.07%	-0.65%	-0.11%	0.09%	0.00%	-0.70%	0.14%
Corporates	ER00	0.14%	-0.11%	-0.63%	-0.10%	-0.05%	0.00%	-0.76%	0.06%
Asset-backed	EA00	0.15%	-0.31%	-0.83%	-0.01%	-0.14%	0.00%	-1.15%	-0.14%
Financial	EB00	0.15%	-0.12%	-0.54%	-0.11%	-0.02%	0.00%	-0.65%	0.08%
Non-Financial	EN00	0.14%	-0.11%	-0.68%	-0.10%	-0.07%	0.00%	-0.82%	0.05%
AAA Corporates	ER10	0.12%	-0.11%	-0.90%	-0.05%	-0.47%	0.01%	-1.40%	-0.35%
AA Corporates	ER20	0.12%	-0.13%	-0.61%	-0.09%	-0.17%	0.00%	-0.89%	-0.10%
A Corporates	ER30	0.13%	-0.11%	-0.66%	-0.10%	-0.13%	0.00%	-0.88%	-0.03%
BBB Corporates	ER40	0.16%	-0.11%	-0.61%	-0.11%	0.04%	0.00%	-0.63%	0.18%
Banking	EBBA	0.13%	-0.12%	-0.52%	-0.11%	0.01%	0.00%	-0.60%	0.10%
Financial Services	EBFS	0.13%	-0.09%	-0.67%	-0.10%	-0.08%	0.00%	-0.82%	0.04%
Insurance	EBIN	0.26%	-0.17%	-0.67%	-0.12%	-0.19%	0.00%	-0.89%	-0.02%
Automotive	EJAU	0.12%	-0.08%	-0.57%	-0.09%	0.04%	0.00%	-0.57%	0.18%
Basic Industry	EJBS	0.14%	-0.11%	-0.60%	-0.10%	-0.09%	0.00%	-0.76%	0.03%
Capital Goods	EJCP	0.12%	-0.08%	-0.72%	-0.10%	0.64%	0.00%	-0.13%	0.77%
Consumer Goods	EJCS	0.12%	-0.09%	-0.75%	-0.09%	-0.32%	0.01%	-1.13%	-0.20%
Energy	EJEN	0.16%	-0.12%	-0.64%	-0.11%	0.29%	0.00%	-0.41%	0.41%
Healthcare	EJHC	0.11%	-0.08%	-0.78%	-0.09%	-0.23%	0.01%	-1.07%	-0.12%
Leisure	EJLE	0.14%	-0.11%	-0.44%	-0.10%	0.05%	0.00%	-0.47%	0.15%
Media	EJME	0.13%	-0.10%	-0.58%	-0.11%	-0.01%	0.00%	-0.66%	0.11%
Real Estate	EJRE	0.14%	-0.10%	-0.68%	-0.11%	-0.08%	0.01%	-0.82%	0.06%
Retail	EJRL	0.14%	-0.11%	-0.69%	-0.11%	-0.11%	0.01%	-0.88%	0.00%
Services	EJSE	0.13%	-0.11%	-0.61%	-0.12%	-0.04%	0.01%	-0.74%	0.06%
Technology & Electronics	EJTE	0.11%	-0.10%	-0.68%	-0.12%	-0.12%	0.01%	-0.91%	-0.04%
Telecommunications	EJTC	0.16%	-0.13%	-0.73%	-0.09%	-0.28%	0.00%	-1.07%	-0.16%
Transportation	EJTR	0.16%	-0.13%	-0.73%	-0.11%	-0.27%	0.01%	-1.08%	-0.16%
Utility	EK00	0.18%	-0.15%	-0.70%	-0.10%	-0.08%	0.01%	-0.85%	0.04%
Sterling Markets									
Sterling Broad Market	UK00	0.22%	-0.12%	0.25%	0.09%	-0.05%	0.00%	0.39%	-0.02%
UK Gilts	G0L0	0.20%	-0.13%	0.29%	0.13%	0.04%	0.00%	0.53%	0.03%
Non-Gilts	UN00	0.27%	-0.11%	0.17%	0.00%	-0.26%	0.00%	0.08%	-0.14%
Quasi-Governments	UQ00	0.18%	-0.10%	0.14%	0.01%	-0.08%	0.00%	0.16%	-0.03%
Corporates & Collateralized	UC00	0.30%	-0.11%	0.18%	0.00%	-0.31%	0.00%	0.06%	-0.17%
AAA Corporates & Collateralized	UC10	0.25%	-0.15%	0.18%	0.09%	-0.14%	0.00%	0.24%	-0.08%
AA Corporates & Collateralized	UC20	0.22%	-0.09%	0.18%	0.03%	-0.33%	0.00%	0.02%	-0.24%
A Corporates & Collateralized	UC30	0.27%	-0.09%	0.21%	-0.01%	-0.35%	0.00%	0.03%	-0.24%
BBB Corporates & Collateralized	UC40	0.33%	-0.12%	0.16%	-0.01%	-0.30%	0.00%	0.06%	-0.12%
Banking	UFBA	0.28%	-0.12%	0.13%	0.00%	0.08%	0.00%	0.37%	0.22%
Finance & Investments	UFFS	0.29%	-0.09%	0.21%	0.00%	-0.43%	0.00%	-0.01%	-0.29%
Insurance	UFIN	0.38%	-0.15%	0.14%	0.08%	0.35%	0.00%	0.81%	0.64%
Automotive	UIAU	0.17%	-0.06%	0.07%	0.08%	-0.29%	0.00%	-0.03%	-0.15%
Basic Industry	UIBS	0.27%	-0.12%	0.17%	-0.03%	-0.46%	0.00%	-0.17%	-0.35%
Capital Goods	UICP	0.34%	-0.12%	0.18%	-0.05%	0.73%	0.00%	1.08%	0.89%
Consumer Goods	UICS	0.28%	-0.13%	0.15%	-0.01%	-0.50%	0.00%	-0.21%	-0.40%
Energy	UIEN	0.27%	-0.12%	0.14%	-0.05%	-0.37%	0.00%	-0.13%	-0.27%
Healthcare	UIHC	0.27%	-0.10%	0.26%	-0.06%	-0.77%	0.00%	-0.39%	-0.70%
Leisure	UILE	0.25%	-0.10%	0.10%	0.03%	-0.20%	0.01%	0.09%	-0.07%
Media	UIME	0.30%	-0.09%	0.19%	-0.09%	-0.72%	0.00%	-0.41%	-0.59%
Real Estate	UIRE	0.26%	-0.05%	0.27%	0.03%	-0.23%	0.00%	0.29%	-0.10%
Retail	UIRL	0.30%	-0.13%	0.18%	-0.09%	-0.61%	0.00%	-0.35%	-0.52%
Services	UISE	0.21%	-0.06%	0.43%	0.35%	-0.34%	0.00%	0.58%	-0.30%
Technology & Electronics	UITE	0.22%	-0.08%	0.15%	-0.06%	-0.29%	0.00%	-0.05%	-0.19%
Telecommunications	UITC	0.32%	-0.11%	0.22%	-0.05%	-0.66%	0.00%	-0.29%	-0.54%
Transportation	UITR	0.28%	-0.11%	0.21%	0.00%	-0.30%	0.00%	0.08%	-0.20%
Utility	UU00	0.32%	-0.14%	0.21%	-0.01%	-0.86%	0.00%	-0.48%	-0.72%
Other European Governments									
Denmark	G0M0	0.13%	-0.18%	-0.90%	-0.07%	0.00%	0.00%	-1.01%	0.02%
Sweden	G0W0	0.19%	-0.21%	-0.57%	-0.06%	0.00%	0.00%	-0.65%	0.01%
Switzerland	G0S0	0.13%	-0.19%	-3.07%	0.04%	0.07%	0.00%	-3.02%	0.19%
European High Yield Markets									
European Currencies	HP00	0.34%	-0.08%	-0.32%	-0.07%	0.02%	0.01%	-0.10%	0.37%
Euro Currencies	HE00	0.32%	-0.09%	-0.37%	-0.08%	-0.01%	0.02%	-0.21%	0.32%

Table 11: Pan-European index return attribution by sector (Sept)

	Index	Coupon	Amort./Roll	Curve Shift	Curve Reshape	Spread Change	Volatility Return	Total Return	Excess Return
Sterling High Yield	HL00	0.48%	-0.02%	0.07%	0.03%	0.31%	0.01%	0.87%	0.77%
European Issuers	HWP0	0.41%	-0.07%	-0.38%	-0.05%	0.51%	0.04%	0.46%	0.90%

Table 12: Pan-European index return attribution by sector (YTD)

	Index	Coupon	Amort./Roll	Curve Shift	Curve Reshape	Spread Change	Volatility Return	Total Return	Excess Return
Pan-Europe Broad Market	PE00	1.66%	-0.92%	6.46%	-0.49%	2.14%	0.00%	8.84%	2.88%
Euro Markets									
Euro Broad Market	EMU0	1.54%	-0.92%	5.93%	-0.65%	2.49%	0.00%	8.38%	3.29%
Euro Large Cap	EMUL	1.54%	-0.92%	5.95%	-0.64%	2.50%	0.00%	8.43%	3.30%
Euro Governments	EG00	1.77%	-1.10%	6.81%	-0.34%	2.87%	0.00%	10.01%	3.66%
Quasi-Governments	EQ00	1.08%	-0.72%	5.86%	-0.67%	1.38%	0.00%	6.93%	1.93%
Pfandbriefe	EP00	0.46%	-0.24%	4.30%	-1.28%	0.83%	0.00%	4.08%	1.29%
Corporates	ER00	1.48%	-0.62%	4.35%	-1.24%	2.78%	0.00%	6.75%	3.90%
Asset-backed	EA00	1.44%	-1.26%	6.40%	-0.73%	4.98%	0.00%	10.82%	5.02%
Financial	EB00	1.51%	-0.69%	3.74%	-1.42%	2.81%	0.00%	5.95%	3.93%
Non-Financial	EN00	1.46%	-0.58%	4.69%	-1.14%	2.76%	0.00%	7.18%	3.88%
AAA Corporates	ER10	1.26%	-0.65%	6.47%	-0.34%	1.12%	-0.01%	7.85%	1.94%
AA Corporates	ER20	1.22%	-0.83%	4.20%	-1.14%	0.95%	0.00%	4.41%	1.62%
A Corporates	ER30	1.31%	-0.64%	4.47%	-1.18%	1.98%	0.00%	5.94%	2.91%
BBB Corporates	ER40	1.68%	-0.56%	4.27%	-1.32%	3.86%	0.00%	7.92%	5.22%
Banking	EBBA	1.34%	-0.67%	3.53%	-1.45%	2.35%	0.00%	5.10%	3.33%
Financial Services	EBFS	1.33%	-0.36%	4.57%	-1.22%	2.70%	0.00%	7.02%	3.91%
Insurance	EBIN	2.67%	-0.95%	4.74%	-1.30%	5.70%	0.00%	10.85%	7.62%
Automotive	EJAU	1.19%	-0.23%	3.94%	-1.37%	3.21%	0.00%	6.74%	4.38%
Basic Industry	EJBS	1.44%	-0.66%	4.14%	-1.25%	2.47%	0.00%	6.12%	3.49%
Capital Goods	EJCP	1.22%	-0.33%	5.00%	-1.04%	2.68%	0.00%	7.52%	3.85%
Consumer Goods	EJCS	1.20%	-0.43%	5.02%	-1.01%	2.17%	0.00%	6.95%	3.19%
Energy	EJEN	1.68%	-0.70%	4.39%	-1.25%	2.87%	0.00%	6.98%	4.11%
Healthcare	EJHC	1.10%	-0.35%	5.21%	-0.88%	1.89%	-0.01%	6.96%	2.88%
Leisure	EJLE	1.33%	-0.58%	3.26%	-1.44%	1.14%	0.00%	3.70%	2.22%
Media	EJME	1.27%	-0.46%	4.15%	-1.42%	2.78%	0.00%	6.31%	3.84%
Real Estate	EJRE	1.47%	-0.33%	4.76%	-1.24%	4.47%	0.00%	9.13%	5.88%
Retail	EJRL	1.36%	-0.53%	4.81%	-1.12%	1.91%	0.00%	6.43%	2.97%
Services	EJSE	1.25%	-0.44%	4.38%	-1.29%	2.39%	0.00%	6.29%	3.48%
Technology & Electronics	EJTE	1.13%	-0.49%	4.80%	-1.15%	2.11%	0.00%	6.41%	2.99%
Telecommunications	EJTC	1.67%	-0.75%	4.97%	-1.02%	3.00%	0.00%	7.87%	4.19%
Transportation	EJTR	1.67%	-0.79%	5.04%	-1.05%	2.45%	0.00%	7.33%	3.58%
Utility	EK00	1.85%	-0.96%	4.80%	-1.14%	2.97%	0.00%	7.52%	4.04%
Sterling Markets									
Sterling Broad Market	UK00	2.33%	-0.90%	9.13%	0.32%	0.52%	0.00%	11.40%	0.99%
UK Gilts	G0L0	2.11%	-0.97%	10.29%	0.49%	0.04%	0.00%	11.95%	0.10%
Non-Gilts	UN00	2.81%	-0.75%	6.55%	-0.04%	1.65%	0.00%	10.23%	2.96%
Quasi-Governments	UQ00	1.84%	-0.63%	5.17%	-0.27%	0.60%	0.00%	6.72%	1.02%
Corporates & Collateralized	UC00	3.10%	-0.78%	6.95%	0.03%	1.94%	0.00%	11.24%	3.52%
AAA Corporates & Collateralized	UC10	2.60%	-1.10%	6.58%	-0.22%	1.15%	0.00%	9.01%	2.01%
AA Corporates & Collateralized	UC20	2.32%	-0.60%	7.08%	0.08%	0.86%	0.00%	9.73%	1.75%
A Corporates & Collateralized	UC30	2.92%	-0.69%	7.95%	0.21%	1.70%	0.00%	12.08%	3.13%
BBB Corporates & Collateralized	UC40	3.47%	-0.84%	6.23%	-0.08%	2.46%	0.00%	11.23%	4.38%
Banking	UFBA	2.88%	-0.78%	4.87%	-0.32%	2.18%	0.00%	8.83%	3.61%
Finance & Investments	UFFS	3.26%	-0.69%	7.07%	0.19%	1.65%	0.00%	11.48%	3.44%
Insurance	UFIN	3.89%	-1.11%	5.44%	-0.50%	3.85%	-0.01%	11.56%	6.00%
Automotive	UIAU	1.58%	-0.05%	2.69%	-0.77%	1.51%	0.00%	4.96%	2.45%
Basic Industry	UIBS	2.93%	-0.93%	6.24%	-0.09%	1.95%	0.00%	10.09%	3.16%
Capital Goods	UICP	3.57%	-0.90%	7.17%	0.13%	3.93%	0.00%	13.90%	6.05%
Consumer Goods	UICS	2.84%	-0.83%	5.66%	-0.21%	1.41%	0.00%	8.88%	2.67%
Energy	UIEN	2.74%	-0.73%	5.55%	-0.19%	1.61%	0.00%	8.97%	2.88%
Healthcare	UIHC	2.95%	-0.68%	10.16%	0.67%	0.72%	0.00%	13.82%	1.96%
Leisure	UILE	2.47%	-0.38%	4.12%	-0.59%	1.59%	0.00%	7.21%	3.08%
Media	UIME	3.14%	-0.58%	7.24%	0.18%	1.05%	0.00%	11.02%	2.74%
Real Estate	UIRE	2.93%	-0.22%	10.43%	0.62%	2.02%	0.00%	15.78%	3.79%
Retail	UIRL	3.06%	-0.90%	7.03%	0.18%	1.11%	0.00%	10.48%	2.43%
Services	UISE	2.47%	-0.35%	16.06%	1.05%	2.92%	0.00%	22.15%	4.75%
Technology & Electronics	UI TE	2.22%	-0.49%	5.67%	-0.21%	1.84%	-0.01%	9.03%	2.77%
Telecommunications	UITC	3.42%	-0.80%	8.26%	0.36%	2.12%	0.00%	13.36%	3.99%
Transportation	UITR	2.94%	-0.71%	7.74%	0.15%	2.09%	0.00%	12.21%	3.54%

Table 12: Pan-European index return attribution by sector (YTD)

	Index	Coupon	Amort./Roll	Curve Shift	Curve Reshape	Spread Change	Volatility Return	Total Return	Excess Return
Utility	UU00	3.42%	-1.00%	8.00%	0.27%	2.79%	0.00%	13.48%	4.50%
Other European Governments									
Denmark	G0M0	1.44%	-1.30%	8.37%	0.01%	0.03%	0.00%	8.54%	0.07%
Sweden	G0W0	1.78%	-1.53%	5.46%	-0.75%	-0.01%	0.00%	4.94%	0.03%
Switzerland	G0S0	1.35%	-1.37%	7.53%	0.66%	-0.07%	0.00%	8.11%	0.12%
European High Yield Markets									
European Currencies	HP00	3.42%	-0.24%	2.84%	-1.21%	4.41%	-0.01%	9.22%	7.76%
Euro Currency	HE00	3.26%	-0.28%	2.85%	-1.30%	4.61%	-0.01%	9.13%	7.85%
Sterling High Yield	HL00	4.68%	0.10%	2.78%	-0.55%	2.90%	-0.02%	9.89%	7.04%
European Issuers	HWP0	4.15%	-0.60%	3.05%	-0.77%	5.39%	-0.07%	11.16%	8.35%

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