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European Leveraged Finance, Second Quarter 2014

Highlights and Market Environment

Highlights
European leveraged finance issuance (leveraged loans and high yield bonds) rose in 2Q’14, with €93.6 billion issued, a 103.1% increase quarter-over-quarter (q-o-q) and an 88.3% increase year-over-year (y-o-y). The increase q-o-q stems from the increase in high yield bond issuance, which experienced a surge during the second quarter of 2014, despite continued turmoil in eastern Europe; the high yield share of the leveraged finance market rose to 62.2%, up from 56.1% in 1Q’14.

Market and Economic Environment
According to the July 2014 European Central Bank lending survey, credit standards for all loan categories eased in net terms in the second quarter of 2014. More notably, for the first time since the second quarter of 2007, euro area banks reported a net easing of credit standards on loans to enterprises in the second quarter of 2014. Across firm size, credit standards were eased both for loans to large enterprises and for loans to small and medium-sized enterprises (SMEs). Regarding loan maturity, credit standards for both short-term and long-term loans were eased. Despite the easing during the quarter the European Central Bank stated that the level of credit standards is still relatively high.

The net demand for loans increased in the second quarter. For the first time since the second quarter of 2011, financing needs related to fixed investment contributed, albeit on a marginal basis, positively to the demand for loans to enterprises.

Issuance

Issuance: Leveraged Loans
Leveraged loan issuance, including first lien, second lien, and mezzanine financing, rose in the second quarter to €35.4 billion, up 75.2% q-o-q ($20.2 billion) and 80.2% y-o-y. Amend-and-extend (“A&E”) transactions continue to take place, with slightly less than a quarter of deals in the second quarter structured as such (21.4% by euro amount), a decrease from the first quarter (30.9%).

In the second quarter, no mezzanine loans and €1.3 billion in second liens were financed. Spreads at pricing for institutional loans widened by 3.4 basis points (bps) while spreads for pro rata loans tightened by 10.8 bps. Mezzanine loan spreads remained unchanged at 668.7 bps.

According to Dealogic, the leading sector in leveraged loan issuance for the second quarter of 2014 was food and beverage (€9.68 billion), followed by telecommunications (€4.64 billion) and construction and building (€2.71 billion). The largest deal was a €3.00 billion deal by Numericable Group for repayment of debt and new acquisitions.

The share of deals aimed to refinance and/or repay debt fell q-o-q and y-o-y, falling to 40.0% of all deals by euro amount in the second quarter, compared to 62.0% in 1Q’14 and 65.7% in 2Q’13.

European CLO outstandings, including SME deals, declined by 22.9% on an annualized basis in the second quarter, ending June 2014 at €186.1 billion. Non-SME CLOs shrank at an annualized rate of 27.4% in 2Q’14 while SME CLOs decreased only by an annualized 0.2%.
Issuance: High Yield Bonds

Primary issuance in 2Q’14 totalled €58.21 billion on 107 deals, an increase of 125.0% and 93.7%, respectively, q-o-q and y-o-y. Issuance from developed market Europe rose in the second quarter but, given the lingering turmoil in eastern Europe, issuance from emerging market Europe fell.

According to Standard and Poor’s, some $4.2 trillion of European corporate debt (44% of global debt) is expected to mature between 2014 and 2019.¹ The rating agency noted that “some recent signs that the economy is moving in the right direction are encouraging, but the uncertainty caused by geopolitical instability, both within and outside of Europe, could give investors pause. For example, the current situation in Ukraine is very delicate, and investor concerns over this conflict could impede some European companies’ financing and refinancing prospects.”

Primary issuance in developed market Europe in the second quarter was €57.19 billion on 102 deals, while in emerging market Europe primary issuance was €1.01 billion on 5 deals.

In second quarter 2014, average deal sizes from developed market Europe rose from first quarter, with an average of €932.0 million per deal in 2Q’14 (€655.9 million for 1Q’14). Average deal sizes for emerging market Europe also rose to €560.7 million in 2Q’14 from €406.4 million in 1Q’14.

High yield issuance for refinancing and/or repayment of debt in developed market Europe increased q-o-q but decreased y-o-y, representing 54.6% of all issuance by euro amount in 2Q’14, compared to 27.7% in 1Q’14 and 54.8%, in 2Q’13. In emerging market Europe, refinancing and/or repayment of debt deals increased q-o-q and y-o-y, representing 39.3% of issuance by euro amount in 2Q’14, up from 0% in 1Q’14 and from 13.7% in 2Q’13.

There was no issuance of senior secured structures in the second quarter 2014 in developed market Europe, although secured structures remain prevalent, representing 21.8% of deals by euro amount in 2Q’14. Secured structures were absent in emerging market Europe in 2Q’14.

The proportion of USD-denominated issuance increased in 2Q’14, representing 33.8% of all issuance by euro amount, compared to 17.2% in 1Q’14 and 43.2% in 2Q’13. USD-denominated issuance in emerging market Europe rose to represent 41.1% by euro amount, compared to 27.4% in the previous quarter, while USD-denominated issuance in developed market Europe also increased to 33.7% of all issuance by euro amount from 16.7% in the prior quarter.

Returns & Credit Quality

Emerging markets equities led returns in the second quarter (5.64%) followed by US distressed high yield (5.54%) and US equities (4.69%). European leveraged loans, however, performed poorly, returning 0.52% as the worst performing asset class.

High-yield bond default rates fell in the second quarter, with S&P reporting 1.5% (down from 1.8% end-March). One bond-related default was reported in the second quarter: Baghlan Group FZCO.

According to S&P, upgrades exceeded downgrades in developed market Europe, with 43 upgrades and 17 downgrades. Upgrades were concentrated largely in financial institutions (12 upgrades), with the balance distributed across the sector spectrum. Downgrades were concentrated among metals, mining & steel (3 downgrades), while the remainder also distributed across sectors.

Conversely, downgrades exceeded upgrades in emerging market Europe, with four upgrades and 14 downgrades. Five financial institutions, three oil and gas producers, two sovereigns, two transportation firms and two utility companies were downgraded in the second quarter.

1. Leveraged Finance Overview

1.1. European Leveraged Issuance by Type

1.2. European Leveraged Issuance by Percentage

1.3. European Leveraged Issuance Average Deal Size

1.4. Bank Credit Standards

1.5. Factors Affecting Bank Credit Standards

1.6. Loan Demand

1 A positive net percentage number signifies tightening bank credit; a negative net percentage number signifies easing credit.
2 A positive net percentage signifies the factor contributed to tightening credit standards; a negative net percentage signifies the factor contributed to easing credit standards.
3 A positive net percentage signifies increased demand; a negative net percentage signifies decreased demand.
1.7. Factors Affecting Loan Demand

Factors Affecting Loan Demand
Jul. 2014

<table>
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<tr>
<th>Factor</th>
<th>Net Percentage</th>
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<tbody>
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<td>Inventories, Working Capital</td>
<td>-3.7%</td>
</tr>
<tr>
<td>Debt Restructuring</td>
<td>0.1%</td>
</tr>
<tr>
<td>M&amp;A, Restructuring</td>
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<tr>
<td>Equity Issuance</td>
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<td>Loans from Non-Banks</td>
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<td>Loans from Other Banks</td>
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<tr>
<td>Fixed Investment</td>
<td>0.7%</td>
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<tr>
<td>Debt Issuance</td>
<td>0.8%</td>
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<tr>
<td>Internal Financing</td>
<td>0.9%</td>
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Source: ECB

1.8. Global Comparison – High Yield Issuance

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<th>2014</th>
<th>2013</th>
<th>2012</th>
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<tr>
<td></td>
<td>Q1</td>
<td>Q2</td>
<td>Q3</td>
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<tr>
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<tr>
<td>Europe</td>
<td>28.5</td>
<td>62.1</td>
<td>90.6</td>
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</table>

\[4\] A positive net percentage signifies a factor that contributed to higher demand; a negative net percentage signifies a factor that contributed to lower demand.
2. Issuance – Leveraged Loans

2.1. European Leveraged Loan Issuance By Loan Type

2.2. European Leveraged Loan Issuance by Industry Sector

2.3. Forward Pipeline of Leveraged Loan Market

2.4. S&P ELLI Total Institutional Loans Outstanding

2.5. S&P ELLI Ratings Diversification

2.6. Distribution of Leveraged Loan Secondary Market Bids
2.7. Institutional and Pro Rata Spreads

2.8. Mezzanine Spread
3. Issuance – High Yield Bonds Overview

3.1. European HY Bond Issuance, Developed and Emerging Market

3.2. European HY Bond Issuance, Sponsored vs Corporate

3.3. European Corporate Bonds Outstanding

3.4. European Corporate Maturity Wall

3.5. European Corporate HY Bonds Outstanding By Sector

3.6. European Corporate HY Bonds Outstanding by Current Rating

Sources: Dealogic, Thomson Reuters LPC

Sources: Bloomberg, AFME, SIFMA

AFME High Yield Division
Second Quarter 2014
3.7. European Corporate Bond Issuance by Rating

**European HY Issuance by Rating**

2014:Q2

Developed vs. Emerging Markets

Sources: Bloomberg, Dealogic, Moody’s, Standard and Poor’s, Fitch Ratings

3.8. European Corporate Bond Issuance by Tenor

**European HY Issuance by Tenor**

2014:Q2

0.0 - 5.0 - 10.0 - 15.0 - 20.0 - 25.0 - 30.0 - 35.0 - 40.0

< 5 Years - 5 - 7 Years - 8 - 10 Years - 10+ Years - Other

Sources: Bloomberg, Dealogic, Moody’s, Standard and Poor’s, Fitch Ratings

3.9. European HY Use of Proceeds

**European HY Issuance By Use of Proceeds**

2006 - 2014:Q2

Other - Restructuring - Repay Debt/Refinancing - LBO/MBO - General Corporate Purposes - Acquisitions

YTD 2013 - 2014

Sources: Dealogic, AFME/SIFMA

3.10. European HY Issuance, Secured Share

**European HY Issuance, Senior Secured, Secured, and Senior Unsecured**

2010 - 2014:Q2

Other - Secured - Senior Secured - Senior Unsecured

% Secured (right)

Sources: Bloomberg, Dealogic

4. Issuance – European Developed Market High Yield Bonds

4.1. European Developed Market HY Bond Issuance

**European Developed Market HY Bond Issuance**

2006 - 2014:Q2

YTD 2013 - 2014

Sources: Dealogic

4.2. European Developed Market HY Issuance by Currency

**European Developed Market HY Issuance by Currency**

2006 - 2014:Q2

YTD 2013 - 2014

Sources: Dealogic
4.3. European Developed Market HY Issuance by Industry

4.4. European Developed Market HY Issuance by Country of Risk

4.5. European Developed Market HY Issuance, Fixed vs. Floating

4.6. European Developed Market HY Issuance, Sponsored vs. Corporate

4.7. European Developed Market HY Rating Distribution at Issuance

4.8. European Developed Market Corporate Bonds Outstanding
## 4.9. European Developed Market HY Bond Issuance

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<th>Issuer</th>
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<th>S&amp;P</th>
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†PIK (Payment in Kind); ‡Debut issue

Source: Bloomberg, Dealogic

AFME High Yield Division
Second Quarter 2014
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<th>Issuer</th>
<th>Industry Group</th>
<th>Date</th>
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<th>Moodys</th>
<th>S&amp;P</th>
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†PIK (Payment in Kind); ‡Debut issue

Source: Bloomberg, Dealogic

AFME High Yield Division
Second Quarter 2014
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<thead>
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<th>Issuer</th>
<th>Industry Group</th>
<th>Date</th>
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<th>S&amp;P</th>
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*PIK (Payment in Kind); ‡Debut issue

Source: Bloomberg, Dealogic
5. Issuance – European Emerging Market High Yield Bonds

5.1. European Emerging Market HY Bond Issuance

5.2. European Emerging Market HY Bond Issuance by Currency

5.3. European Emerging Market HY Issuance by Industry

5.4. European Emerging Market HY Issuance by Country of Risk

5.5. European Emerging Market HY Issuance, Fixed vs. Floating

5.6. European Emerging Market HY Issuance, Sponsored vs. Corporate

Source: Dealogic
5.7. European Emerging Market HY Rating Distribution at Issuance

5.8. European Emerging Market Corporate Bonds Outstanding

5.9. Emerging Market HY Bond Issuance

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<th>Issuer</th>
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<th>Coupon</th>
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<th>S&amp;P</th>
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†PIK (Payment in Kind); ‡Debut issue

Source: Bloomberg, Dealogic
6. Credit Quality

6.1. European HY Default Rate

6.2. Developed Europe Issuer Rating Actions

6.3. Emerging Europe Issuer Rating Actions

6.4. Developed European Industry Rating Actions by # of Ratings

6.5. Emerging European Industry Rating Actions by # of Ratings

6.6. European Defaults

1 Numbers include both corporate and sovereigns.
2 Numbers include both corporate and sovereigns.
7. Relative Value

7.1. European HY Bonds, Cash vs. Synthetic

7.2. European Leveraged Loans, Cash vs. Synthetic

8. Total Return

8.1. European HY Bond Total Return

8.2. European Leveraged Loan Total Return

8.3. Asset Class Total Return, Quarter

AFME High Yield Division
Second Quarter 2014
Summary of the Methodologies
Adopted for this Report

1. Leveraged Issuance – Overview
1.1. – 1.3. Leveraged Loans and High Yield Bonds
Leveraged loan data are sourced from Thomson Reuters LPC and Dealogic.

Leveraged loan data from Thomson Reuters LPC are defined primarily as having sub-investment grade ratings and/or a margin spread minimum of 200 basis points (spread minimums will vary from year to year to make Thomson LPC’s cutoff). Leveraged loan aggregates will include first lien, second lien, and mezzanine financing. Discrepancies in Thomson Reuters LPC data are due to rounding and/or currency rate of exchange.

Leveraged loan data from Dealogic are defined primarily as coming from a leveraged or highly leveraged European deal; loan tranches must have sub-investment grade ratings, or, if unrated, a margin spread minimum of 125 basis points over a benchmark (e.g., Euribor, LIBOR). Under these guidelines, sub-investment grade-rated loans with a margin spread of less than 125 basis points are included. Deals must be European and are inclusive of both developed and emerging market Europe as defined in high yield criteria in Section 3. Deals must also be marketed either in Europe or in the United States. Loans not EUR-denominated are converted to EUR as of credit date for purposes of aggregation. Aggregates include new money as well as non-new money deals.

Criteria for high yield bond transactions can be found in Section 3, 4, and 5.

1.4. – 1.7. Bank Lending Surveys
Data for loan demand and credit standards are sourced from the ECB’s bank lending survey. Graph numbers are net percentages of reporting banks.

1.8. Global Comparison – High Yield Issuance
Data for global high yield issuance are sourced from Dealogic. Asian deals are inclusive of Japan and Australia.

2. Issuance – Leveraged Loans
2.1. – 2.2.
Leveraged loan issuance data are sourced primarily from Dealogic and Thomson Reuters LPC. For more details on qualifying criteria, please refer to section 1.

2.3. Forward Pipeline of Leveraged Loan Market
Forward leveraged loan pipeline data are sourced from S&P LCD.

2.4. S&P ELLI Total Institutional Loans Outstanding
Total institutional loan outstanding data are sourced from S&P LCD and are outstanding loans in the S&P ELLI index.

2.5. S&P ELLI Ratings Diversification
S&P ELLI ratings diversification are the percentages of currently outstanding loans in S&P’s ELLI index that are rated accordingly. Data are provided by S&P LCD.

2.6. Leveraged Loan Secondary Market Bids
European leveraged trading volumes are sourced from Thomson Reuters LPC and are percentage of volume by bid price.

2.7. – 2.8. Loan Spreads
Loan spread data are sourced from Dealogic under our criteria for leveraged loans (see Section 1). For purposes of loan spread calculations, deals marketed in the US are excluded. Spreads are a weighted average of spread margin on new leveraged issuance on a rolling twelve months basis, and are typically benchmarked to LIBOR or EURIBOR. Institutional loan spread data are inclusive of 2nd lien; pro rata spreads include all revolvers and term loan A (Tla).

3. Issuance – High Yield Bonds Overview
High yield bond transactions are sourced primarily from Dealogic, with supplemental information sourced from Bloomberg. High yield transactions are defined as transactions with a Dealogic “effective” rating of equal or less than BB+, and may include unrated transactions based on issuer and desk notes. Split-junk rated transactions are generally excluded.

European issuance, inclusive of both emerging market Europe and developed market Europe, are defined as an issue having a Dealogic “deal nationality” as well as “nationality of risk” within Europe issued in the euro, foreign, and global markets; deals marketed locally are excluded. Sovereign, sub-sovereign, and supranational parent issuers are excluded from issuance, as well as ABS/MBS issuers.

Emerging market Europe is defined by nationality of risk, rather than nationality of deal, and although primarily sourced from Dealogic, are ultimately subject to AFME’s discretion. Emerging and developed market issuance are mutually exclusive and will contain no overlap unless otherwise mentioned.

European emerging market bonds are further defined with having a minimum deal size of €75.0 million; deals on the same day from the same issuer are aggregated for the purpose of meeting this minimum. Russian ruble (RUB)-denominated issuance are excluded due to differences in
3.2. European HY Issuance by Sponsor
Data for high yield issuance by sponsor are sourced from Dealogic. LBO deals are defined as all high yield transactions whose issuer parent is a public or private finance entity (i.e., a financial sponsor), regardless of use of proceeds.

3.3. – 3.6. European Corporate Bonds Outstanding
Data for European corporate outstanding are sourced from Bloomberg and AFME/SIFMA estimates. Criteria for European corporate bonds are: bonds must be placed in the domestic, euro, foreign, and global markets with nationality of incorporation from a European developed or emerging market country as defined by AFME. Corporate bonds exclude all structured notes, covered bonds, warrants, deposit notes, receipts, and certificates of deposit. All currencies are included and have been converted to EUR at time of pricing and/or issue.

High-yield ratings are sourced from Bloomberg’s composite rating, which is an average of all available ratings from four rating agencies: Moody’s, Standard and Poor’s, Fitch Ratings, or DBRS. Split-rated securities may be included in high yield numbers due to this.

Corporate bonds outstanding include certain securities that may be considered corporate securitisations or structured finance securities; while all effort is made to exclude the latter, the former will be counted toward the corporate bonds outstanding total, and will subsequently overlap to some extent to AFME structured finance outstanding numbers.

3.7. European Corporate Bond Issuance by Rating
Data for HY issuance by rating are sourced from Dealogic, Bloomberg, and the three rating agencies. The composite rating is determined by the lowest rating assigned by either Moody’s, Standard and Poor’s, or Fitch Ratings.

3.8. European Corporate Bond Issuance by Tenor
Data for HY issuance by tenor are sourced from Dealogic. “Other” includes perpuals.

3.9. European HY Issuance By Use of Proceeds
Data for HY issuance by use of proceeds are sourced from Dealogic and aggregated for the purposes of this calculation. Please refer to Section 3 for criteria on high yield issuance.

3.10. European HY Issuance, Senior Secured Share
Data for HY issuance by seniority are sourced from Dealogic and Bloomberg. “Senior Unsecured” totals include all bonds that are senior but not senior secured.

4. Issuance – European Developed Market High Yield Bonds
4.1. – 4.7., 4.9
High yield bond issuance data are sourced from Dealogic. For further criteria on how high yield issuance are defined, please refer to section 3.

Developed European issuance are deals predominantly from western Europe and includes deals from Andorra, Austria, Belgium, Bulgaria, Cyprus, Switzerland, Germany, Denmark, Spain, Estonia, Finland, France, Faroe Islands, United Kingdom, Guernsey, Gibraltar, Greenland, Greece, Isle of Man, Iceland, Ireland, Italy, Jersey, Liechtenstein, Luxembourg, Monaco, Malta, Montenegro, Netherlands, Norway, Portugal, San Marino, and Sweden.

4.8. European Developed Market Corporate Bonds Outstanding
Data for corporate bonds outstanding are sourced from Bloomberg. Please refer to Section 3 for criteria and methodology.

5. Issuance – European Emerging Market High Yield Bonds
5.1. – 5.7., 5.9.
High yield bond issuance data are sourced from Dealogic. Criteria for all high yield issuance are found in section 3.

Emerging market European issuance deals are predominantly from eastern Europe but will also additionally include Turkey, the Russian Federation, Kazakhstan, Turkmenistan, Uzbekistan, Tajikistan, Azerbaijan, and Kyrgyzstan. Certain sub-investment grade counties are not included in the emerging market total, including, among others, Iceland and Greece.

5.8. European Emerging Market Corporate Bonds Outstanding
Data for corporate bonds outstanding are sourced from Bloomberg. Please refer to Section 3 for criteria and methodology.

6. Credit Quality
6.1. European HY Default Rate
European HY bond default rates are sourced from S&P and are on a trailing 12 month basis.

“Europe” for the S&P default rate is defined to include Austria, Belgium, Bulgaria, Channel Islands, Cyprus, Czech Republic, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, Iceland, Ireland, Italy, Latvia, Lithuania, Luxembourg, Malta, Netherlands, Norway, Poland, Portugal, Slovak Republic, Slovenia, Spain, Sweden, Switzerland and the United Kingdom. Countries are subject to revision.

6.2. – 6.3. European Issuer Rating Actions
European issuer upgrades and downgrades are sourced from S&P. The breakdown by emerging market and developed Europe are from AFME’s definition of developed and emerging markets and would be, under S&P’s guide-
lines, a combination of both European and EMEA rating actions. Multiple downgrades of a single issuer are counted separately. Rating actions are inclusive of both corporate (both credit and merger-related) as well as sovereign ratings.

6.4. – 6.5. European Issuer Rating Actions by # of Rating Actions
Rating actions are sourced from S&P. Breakdown by emerging market and developed Europe are from AFME’s definition of developed and emerging markets and would be, under S&P’s guidelines, a combination of both European and EMEA rating actions.

6.6. European Defaults
Defaults reported by either Moody’s or Standard and Poor’s in the European bond markets and loan markets, when available.

7. Cash and Synthetic
7.1. – 7.2. Loans and Bonds, Cash and Synthetic
Data are sourced from Markit and Thomson Reuters LPC. High yield bond cash and synthetic spreads from Markit; European leveraged loan cash bid prices from Thomson Reuters LPC, and European leveraged loans synthetic prices from Markit.

8. Total Return
8.1. European HY Bond Total Return
European HY bond total return data are sourced from the Bank of America-Merrill Lynch’s Euro High Yield Index (HE00). The index tracks the performance of EUR-denominated below-investment-grade corporate debt publicly issued in the euro domestic or Eurobond markets. Qualifying securities must have a below-investment-grade rating and an investment-grade rated country of risk. Qualifying securities must have at least one year remaining term to maturity, fixed coupon schedule and minimum amount outstanding of €100 million. Original issue zero coupon bonds, “global securities” (debt issued simultaneously in the Eurobond and euro domestic markets), 144a securities and pay-in-kind securities, including toggle notes, qualify for inclusion in the index. Callable perpetual securities qualify provided they are at least one year from the first call date. Fixed-to-floating rate securities also qualify provided they are callable within the fixed rate period and are at least one year from the last call prior to the date the bond transitions from a fixed to a floating rate security. Defaulted, warrant-bearing and euro legacy currency securities are excluded from the index.

8.2. European Leveraged Loan Total Return
Total return data are provided by S&P LCD and are total returns from S&P’s ELLI index, both ELLI and EUR-denominated ELLI. Total returns for ELLI EUR-denominated data are unavailable for 2003 and 2004.

8.3. Asset Class Total Return (Cash Basis)
Total returns are sourced from respective index owners and Bank of America-Merrill Lynch’s indices.
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