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European Leveraged Finance, Third Quarter 2014

Highlights and Market Environment

Highlights

European leveraged finance issuance (leveraged loans and high yield bonds) decreased in 3Q’14 to €38.8 billion, a 58.5% decrease quarter-over-quarter (q-o-q), a 28.9% decrease year-over-year (y-o-y), and the smallest quarterly issuance since 3Q’12. The decrease q-o-q stems from the large decline in high yield bond issuance, which experienced a 69.6% drop during the third quarter of 2014; the high yield share of the leveraged finance market declined to 45.6%, down from 62.2% in 2Q’14.

Market and Economic Environment

According to the October 2014 European Central Bank lending survey, credit standards for all loan categories eased in net terms in the third quarter of 2014. More notably, for the second consecutive quarter euro area banks reported a net easing of credit standards on loans to enterprises in the third quarter of 2014. Across firm size, credit standards were eased on loans to large firms while remaining unchanged for loans to small and medium-sized enterprises (SMEs). Overall, developments across countries continued to become less diverse. Among the largest euro area countries, credit standards on loans to enterprises were eased in net terms in France and Germany, while remaining unchanged in Italy and Spain and increasing in the Netherlands. 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 third quarter. Net demand for loans to enterprises continue to be positive and recovered further in the third quarter of 2014 to 6%, from 4% in the previous quarter.

Issuance

Issuance: Leveraged Loans

Leveraged loan issuance, including first lien, second lien, and mezzanine financing, declined in the third quarter to €21.1 billion, down 40.4% q-o-q (€35.4 billion) and 39.1% y-o-y. Amend and extend (“A&E”) transactions continue to take place, with slightly more than a tenth of deals in the third quarter structured as such (11.3% by euro amount), a decrease from the second quarter (21.4%).

In the third quarter, no mezzanine loans and €1.8 billion in second liens were financed. Spreads at pricing for institutional loans widened by 4.8 basis points (bps) while spreads for pro rata loans widened by 6.8 bps. Mezzanine loan spreads widened to 766.4 bps from 668.7 bps in the second quarter.

According to Dealogic, the leading sector in leveraged loan issuance for the third quarter of 2014 was healthcare (€4.18 billion), followed by construction and building (€2.47 billion) and aerospace (€2.20 billion).
Issuance: High Yield Bonds

Primary issuance in 3Q’14 totalled €17.72 billion on 45 deals, a decrease of 69.6% and 11.3%, respectively, q-o-q and y-o-y. Issuance from developed market Europe fell in the third quarter as did issuance from emerging market Europe.

Primary issuance in developed market Europe in the third quarter was €16.95 billion on 41 deals, a decline of 70.4% and 5.5% by euro amount, respectively, q-o-q (€57.2 billion on 102 deals) and y-o-y (€17.9 billion on 42 deals). In emerging market Europe primary issuance in 3Q’14 was €0.77 billion on 4 deals, a decline of 24.1% and 62.2% by euro amount, respectively, q-o-q (€1.0 billion on 5 deals) and y-o-y (€2.0 billion on 6 deals).

In third quarter 2014, average deal sizes from developed market Europe fell from second quarter, with an average of €413.4 million per deal in 3Q’14 (€560.7 million for 2Q’14). Average deal sizes for emerging market Europe also fell to €192.5 million in 3Q’14 from €203.0 million in 2Q’14.

High yield issuance for refinancing and/or repayment of debt in developed market Europe decreased q-o-q and y-o-y, representing 23.9% of all issuance by euro amount in 3Q’14, compared to 54.6% in 2Q’14 and 43.1% in 3Q’13. In emerging market Europe, no debt was issued for refinancing and/or repayment of debt purposes in the third quarter.

The proportion of USD-denominated issuance decreased in 3Q’14, representing 12.5% of all issuance by euro amount, compared to 33.8% in 2Q’14 and 34.8% in 3Q’13. USD-denominated issuance in emerging market Europe rose to represent 48.0% by euro amount, compared to 41.1% in the previous quarter, while USD-denominated issuance in developed market Europe decreased to 10.9% of all issuance by euro amount from 33.7% in the prior quarter.

Returns & Credit Quality

Covered bonds led returns in the third quarter (2.04%) followed by US municipal debt (1.64%) and emerging market European financial corporates (1.59%). US distressed high yield, however, performed poorly, returning negative 12.9% as the worst performing asset class.

High-yield bond default rates increased in the third quarter, with S&P reporting 2.0% (up from 1.5% end-June). Four bond-related defaults were reported in the third quarter: Espirito Santo Financial Group S A., New World Resources N.V., Mriya Argo Holding PLC, and Phones4u Finance PLC.

According to S&P, downgrades exceeded upgrades in developed market Europe, with 25 downgrades and 24 upgrades. Upgrades were distributed across the sector spectrum. Downgrades were concentrated among media and entertainment (4 downgrades), while the remainder distributed across sectors.

Conversely, upgrades exceeded downgrades in emerging market Europe, with four upgrades and no downgrades. Two telecommunications firms, one bank, and one financial institution were upgraded in the third 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

A positive net percentage signifies a factor that contributed to higher demand; a negative net percentage signifies a factor that contributed to lower demand.

1.8. Global Comparison – High Yield Issuance

<table>
<thead>
<tr>
<th>€ Billions</th>
<th>2014</th>
<th>2013</th>
<th>Prior</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Q1</td>
<td>Q2</td>
<td>Q3</td>
</tr>
<tr>
<td>United States</td>
<td>44.7</td>
<td>50.9</td>
<td>46.9</td>
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<td>Asia Pacific</td>
<td>8.4</td>
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<tr>
<td>Europe</td>
<td>28.5</td>
<td>62.1</td>
<td>20.5</td>
</tr>
</tbody>
</table>

AFME High Yield Division
Third Quarter 2014
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

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3.3. European Corporate Bonds Outstanding

3.4. European Corporate Bonds 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, Bloomberg, AFME, SIFMA
3.7. European Corporate Bond Issuance by Rating

3.8. European Corporate Bond Issuance by Tenor

3.9. European HY Use of Proceeds

4. Issuance – European Developed Market High Yield Bonds

4.1. European Developed Market HY Bond Issuance

4.2. European Developed Market HY Issuance by Currency
4.3. European Developed Market HY Issuance by Industry

![European Developed Market HY Issuance by Industry 2014:Q3](image)

**Source:** Dealogic

4.4. European Developed Market HY Issuance by Country of Risk

![European Developed Market HY Issuance by Country of Risk 2014:Q3](image)

**Source:** Dealogic

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

![European Developed Market HY Bond Issuance, Fixed vs Floating 2006 - 2014:Q3](image)

**Source:** Dealogic

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

![European Developed Market HY Issuance, Sponsored vs Corporate 2006 - 2014:Q3](image)

**Source:** Dealogic

4.7. European Developed Market HY Rating Distribution at Issuance

![European Developed Market HY Rating Distribution at Issuance 2011:Q3 - 2014:Q3](image)

**Source:** Dealogic, AFME/SIFMA

4.8. European Developed Market Corporate Bonds Outstanding

![European Corporate Bonds Outstanding, Developed Europe 2014:Q3](image)

**Sources:** Bloomberg, AFME, SIFMA

AFME High Yield Division
Third Quarter 2014
## 4.9. European Developed Market HY Bond Issuance

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<tr>
<th>Issuer</th>
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<th>Date</th>
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<th>Coupon</th>
<th>Moodys</th>
<th>S&amp;P</th>
<th>Fitch</th>
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<td>B+</td>
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<td>BB-</td>
<td>NA</td>
<td>NA</td>
</tr>
</tbody>
</table>

†PK (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

<table>
<thead>
<tr>
<th>Issuer</th>
<th>Industry Group</th>
<th>Date</th>
<th>Currency</th>
<th>Amount (Millions)</th>
<th>Coupon</th>
<th>Moody's</th>
<th>S&amp;P</th>
<th>Fitch</th>
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<td>Promsvyazbank OAO</td>
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<td>10.500</td>
<td>NA</td>
<td>NA</td>
<td>B</td>
</tr>
<tr>
<td>Agrokor d.d.</td>
<td>Food &amp; Beverage</td>
<td>04/08/2014</td>
<td>EUR</td>
<td>50</td>
<td>3M EURIBOR + 525</td>
<td>NA</td>
<td>NA</td>
<td>NA</td>
</tr>
<tr>
<td>4Finance SA</td>
<td>Finance</td>
<td>08/08/2014</td>
<td>USD</td>
<td>200</td>
<td>11.750</td>
<td>B3</td>
<td>B</td>
<td>NA</td>
</tr>
</tbody>
</table>

1Pik (Payment in Kind); 2Debut issue

Source: Bloomberg, Dealogic
6. Credit Quality

6.1. European HY Default Rate

European HY Default Rate (LTM) Sept. 2012 - Sept. 2014

- Source: Standard & Poor’s, Moody’s
- Note: Moody’s data is on a monthly lag.

6.2. Developed Europe Issuer Rating Actions

S&P Developed Europe Issuer Rating Actions 2008 - 2014:Q3

- Source: Standard & Poor’s

6.3. Emerging Europe Issuer Rating Actions


- Source: Standard & Poor’s

6.4. Developed European Industry Rating Actions by # of Ratings

- Source: Standard & Poor’s

6.5. Emerging European Industry Rating Actions by # of Ratings

- Source: Standard & Poor’s

---

1 Numbers include both corporate and sovereigns.
2 Numbers include both corporate and sovereigns.
6.6. European Defaults

<table>
<thead>
<tr>
<th>Issuer</th>
<th>Industry Group</th>
<th>Country</th>
<th>Date</th>
<th>Reported By</th>
<th>Reason</th>
</tr>
</thead>
<tbody>
<tr>
<td>New World Resources N.V.</td>
<td>Metals, Mining and Steel</td>
<td>Netherlands</td>
<td>August 2014</td>
<td>S&amp;P</td>
<td>Missed Interest Payment</td>
</tr>
<tr>
<td>Mriya Argo Holding PLC</td>
<td>Consumer Products</td>
<td>Cyprus</td>
<td>August 2014</td>
<td>S&amp;P</td>
<td>Missed Interest Payment</td>
</tr>
<tr>
<td>Phones4u Finance PLC</td>
<td>Retail</td>
<td>UK</td>
<td>September 2014</td>
<td>S&amp;P</td>
<td>Foreign Bankruptcy</td>
</tr>
</tbody>
</table>

Source: Moody's, Standard & Poor's

7. Relative Value

7.1. European HY Bonds, Cash vs. Synthetic

![Graph showing Basis Points for HY Spread (iTraxx + 5Y - iBoxx EUR HY)]

Sources: Markit

7.2. European Leveraged Loans, Cash vs. Synthetic

![Graph showing Price/Bid for LevX Senior and Euro Lev Top 40] (Basis Points)

Sources: Thomson Reuters LPC, Markit

8. Total Return

8.1. European HY Bond Total Return

![Graph showing Percentage of European High Yield Total Return 2008 - 2014:Q3] (Percentage)

Source: Bank of America-Merrill Lynch

8.2. European Leveraged Loan Total Return

![Graph showing Percentage of European Leveraged Loan Total Return 2008 - 2014:Q3] (Percentage)

Source: Standard and Poor's LCD

ELLI EUR-denominated only unavailable for 2003 and 2004.

8.3. Asset Class Total Return, Quarter

![Graph showing Asset Class Total Returns 2014:Q3] (Percentage)

Source: BofAML, Bloomberg

AFME High Yield Division
Third 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 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 and developed market European issuance are 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 bonds 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 perpetuals.

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 inclusion.

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, Ireland, Iceland, 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 countries 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 developing 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 loan synthetic prices from Market.

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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