

Index	September EOM levels
ITRXPFL Index	212.0867
ITRX EUR CDSI GEN 5Y Corp	68.777
ITRX XOVER CDSI GEN 5Y Corp	274.973
CDX IG CDSI GEN 5Y Corp	59.18
CDX HY CDSI GEN 5Y SPRD Corp	331.007

September was dominated by headlines around Italian government bonds, but corporate credit nonetheless ended the month relatively calmly. Credit risk premia in Europe, expressed by the levels in iTraxx Main for Investment Grade and iTraxx Crossover for High Yield, tightened slightly with Crossover coming in by 9bps to 335bps than Main with 5 bps to 96bps.

European Performance Credit

The performance of the iTraxx European Performance Credit Index, the reference index for the Tabula European Performance Credit UCITS ETF (TCEP), reflected the positive performance of the constituent indices by rising 1.6% on the month. Since launch of the TCEP in August, the strategy was up 1.5% as of 28th September.

Part of the performance comes from the roll, meaning exiting a currently held CDS contract and simultaneously entering a new, slightly longer dated (on-the-run) contract. As credit curves typically have a positive slope due to greater uncertainty over longer time horizons and investors' preference for shorter-dated debt, a protection seller generates a positive return from rolling contracts (more information on the roll in the education section of the website www.tabulaim.com).

The September index roll, as one of two per year, was particularly relevant as IHS MarkIT amended the technical selection criteria for inclusion of names in the iTraxx indices to increase liquidity and align it more closely to the iBoxx cash bond indices. The result was seven name changes in the iTraxx Main and nine in the iTraxx Crossover. Due to the new credit composition, with many names trading at tighter spreads, the average spread on Main and Crossover declined. This also reduced the expected roll yield going forward as the roll yield moves with the absolute level of spreads assuming an unchanged shape of the curve.

Monthly Yields¹

September 2018

Spread	3.15%
Roll	1.99%
Cash	-0.54%
Transaction Costs	-0.10%
Total 1Y est. Yield	4.50%

August 2018

Spread	3.47%
Roll	2.22%
Cash	-0.54%
Transaction Costs	-0.11%
Total 1Y est. Yield	5.04%

Compared to the previous month and before the roll, absolute yield estimates for constant spread levels declined slightly to 4.50% p.a end of month.

Astaldi default

Another important event at the end of the month was the Astaldi S.P.A.'s credit event following the company's press release on 28th September, which was then classified as default by the Credit Determination Committee in early October. The default is the first in an on-the-run series and the second credit event since the restructuring of the French media firm Thomson in 2009.

The ultimate effect on the iTraxx Crossover Index depends on a number of factors. Generally, the default means that 1 of 75 equally weighted names defaulting triggers a payment for the protection seller of 1.333% less the recovery value of the name as well as a loss of the quarterly premium payments until the next roll. The recovery value is set by a bond auction. After the default a new version of the index will be issued with the defaulted entity removed and with a reduced notional.

As the default did not come without warning, the outstanding cash bonds traded around 80% in July and dropped to 60% at the end of August and further deteriorated in September to trade around 30-35% in the second week of October. As a result, a considerable portion of credit deterioration was already priced into the index prior the credit event. The generic recovery assumption is set to 40% and will finally be set by the auction. Therefore, the actual impact on the price of the index is therefore expected to be a fraction of the 1.333% allocated to the credit in the index.

A further factor mitigating the impact on the iTraxx European Performance credit index, tracked by the Tabula European Performance Credit ETF, is that the Crossover Index is typically only 20% of the exposure compared to 80% from the iTraxx Main (even though the notional exposure to the iTraxx Crossover is around 60% due to the three times market exposure).

¹ The estimated yield calculation involves ageing and repricing the fund portfolio and assuming the spread curves remain constant. The calculation involves a number of assumptions and approximations including around the fund composition remaining constant, rebalancing/rolls and interpolation. The estimated yield is not a guarantee of future returns, which will vary based on market price changes.