

How to take full advantage of ETFs in a bond portfolio



Investment Risks

For complete information on risks, refer to the legal documents.

Applies to all

Value fluctuation: The value of investments, and any income from them, will fluctuate. This may partly be the result of changes in exchange rates. Investors may not get back the full amount invested.

Applies to all except for ESG ETFs

Securities lending: The Fund may be exposed to the risk of the borrower defaulting on its obligation to return the securities at the end of the loan period and of being unable to sell the collateral provided to it if the borrower defaults.

Applies to all except Invesco Preferred Shares UCITS ETF

Credit risk: The creditworthiness of the debt the Fund is exposed to may weaken and result in fluctuations in the value of the Fund. There is no guarantee the issuers of debt will repay the interest and capital on the redemption date. The risk is higher when the Fund is exposed to high yield debt securities.

Interest rates: Changes in interest rates will result in fluctuations in the value of the fund.

Applies to all currency-hedged versions:

Currency hedging Risk: Currency hedging between the base currency of the Fund and the currency of the share class may not completely eliminate the currency risk between those two currencies and may affect the performance of the share class.

Invesco Emerging Markets USD Bond UCITS ETF

Emerging markets: As a large portion of this fund is invested in less developed countries, investors should be prepared to accept a higher degree of risk than for an ETF that invests only in developed markets.

Invesco USD High Yield Corporate Bond ESG UCITS ETF, Invesco Global High Yield Corporate Bond UCITS ETF & Invesco US High Yield Fallen Angels UCITS ETF

High yield debt instruments: This fund may hold a significant amount of debt instruments which are of lower credit quality. This may result in large fluctuations of the value of the ETF as well as impacting its liquidity under certain circumstances.

All Invesco Corporate Bond ESG UCITS ETFs, Invesco USD High Yield Corporate Bond ESG UCITS ETF, Invesco Global High Yield Corporate Bond UCITS ETF, Invesco EUR Government & Related Green Transition UCITS ETF

Environmental, social and governance: The fund invests in securities based on their ESG exposures. This may affect the Fund's exposure, limit investment opportunities and cause the fund to underperform funds not seeking investments based on ESG ratings.

Invesco AT1 Capital Bond UCITS ETF

Contingent Convertible Bonds: This fund invests in contingent convertible bonds, a type of corporate debt security that may be converted into equity or forced to suffer a write down of principal upon the occurrence of a pre-determined event. If this occurs, the Fund could suffer losses. Other notable risks of these bonds include liquidity and default risk.

Invesco Global High Yield Corporate Bond ESG UCITS ETF

Liquidity Risk: It may be difficult for the Fund to buy or sell certain instruments in stressed market conditions. Consequently, the price obtained when selling such instruments may be lower than under normal market conditions.

Invesco Euro Corporate Hybrid Bond UCITS ETF, Invesco Preferred Shares UCITS ETF, Invesco Variable Rate Preferred Shares UCITS ETF

Equity Risk: The value of equities and equity-related securities can be affected by a number of factors including the activities and results of the issuer and general and regional economic and market conditions. This may result in fluctuations in the value of the Fund.

Invesco US Municipal Bond UCITS ETF, Invesco Preferred Shares UCITS ETF, Invesco US High Yield Fallen Angels UCITS ETF, Invesco Corporate Bond ESG UCITS ETFs

Concentration Risk: The Fund might be concentrated in a specific region or sector or be exposed to a limited number of positions, which might result in greater fluctuations in the value of the Fund than for a fund that is more diversified.

Invesco EUR Government & Related Green Transition UCITS ETF, Invesco EUR Corporate Bond ESG Multi-Factor UCITS ETF & Invesco EUR Corporate Bond ESG Short Duration Multi-Factor UCITS ETF

Use of derivatives for investment purposes: This fund may use derivatives for investment purposes. The use of such complex instruments may impact the magnitude and frequency of the fluctuations in the value of the fund.

Green Bond Risk: The Fund invests in Green Bonds which means the Fund will be more affected by the performance of Green Bonds than a fund that is more diversified across the bond market. The market for Green Bonds and related regulation is evolving. The current accepted market standard definitions of "green" may change over time and in such event, the Fund may change the definition of Green Bonds that is applied by the Fund.

Contents

Overview

Benefits of the ETF structure

The basic structure and the way ETFs trade could provide advantages compared to other investment vehicles.



ETFs vs. individual bonds

There are several advantages of gaining exposure to fixed income via ETFs rather than directly investing in underlying bonds.

Use cases

While structural advantages make ETFs inherently useful tools, some fixed income ETFs could be ideally suited to meet specific portfolio objectives.

Summary



Improve portfolio outcomes with Invesco Fixed Income ETFs



Overview

The ETF market in Europe has been growing strongly over the past decade and this growth has accelerated in the most recent years as a broader range of investors discover the potential benefits ETFs offer to their portfolios. This trend is arguably most noticeable in fixed income, where ETF flows appear to be gaining momentum, including among pension and insurance funds as well as other traditional bond buyers who are using ETFs for both strategic and tactical allocation requirements.

After decades of falling yields, fixed income markets rapidly reversed course in 2022 as central banks acted to combat inflation. This has driven yields in many fixed income asset classes to levels that haven't been seen since before the global financial crisis, well over a decade ago. Crucially, this means that fixed income once again warrants a material allocation in a multi-asset portfolio as income will once again be an important part of returns, without relying solely on central bank policy driving yields even lower to produce capital gains. It should also help fixed income to act a diversifier to riskier asset classes once again. Following the repricing of yields and spreads across the entire fixed income asset class, now may be a good time to review your portfolios and ensure you're making the most of opportunities available.

Choosing between ETFs, index trackers, segregated mandates, derivatives and direct investment will often be influenced by a host of factors, including individual circumstances, objectives, timeframe, costs, size of portfolio, frequency of trading and level of expertise in the asset class. Here, we will look at different areas of fixed income and highlight where and how ETFs may be worth considering.



ETF growth has accelerated... as more investors discover the potential benefits ETFs offer.

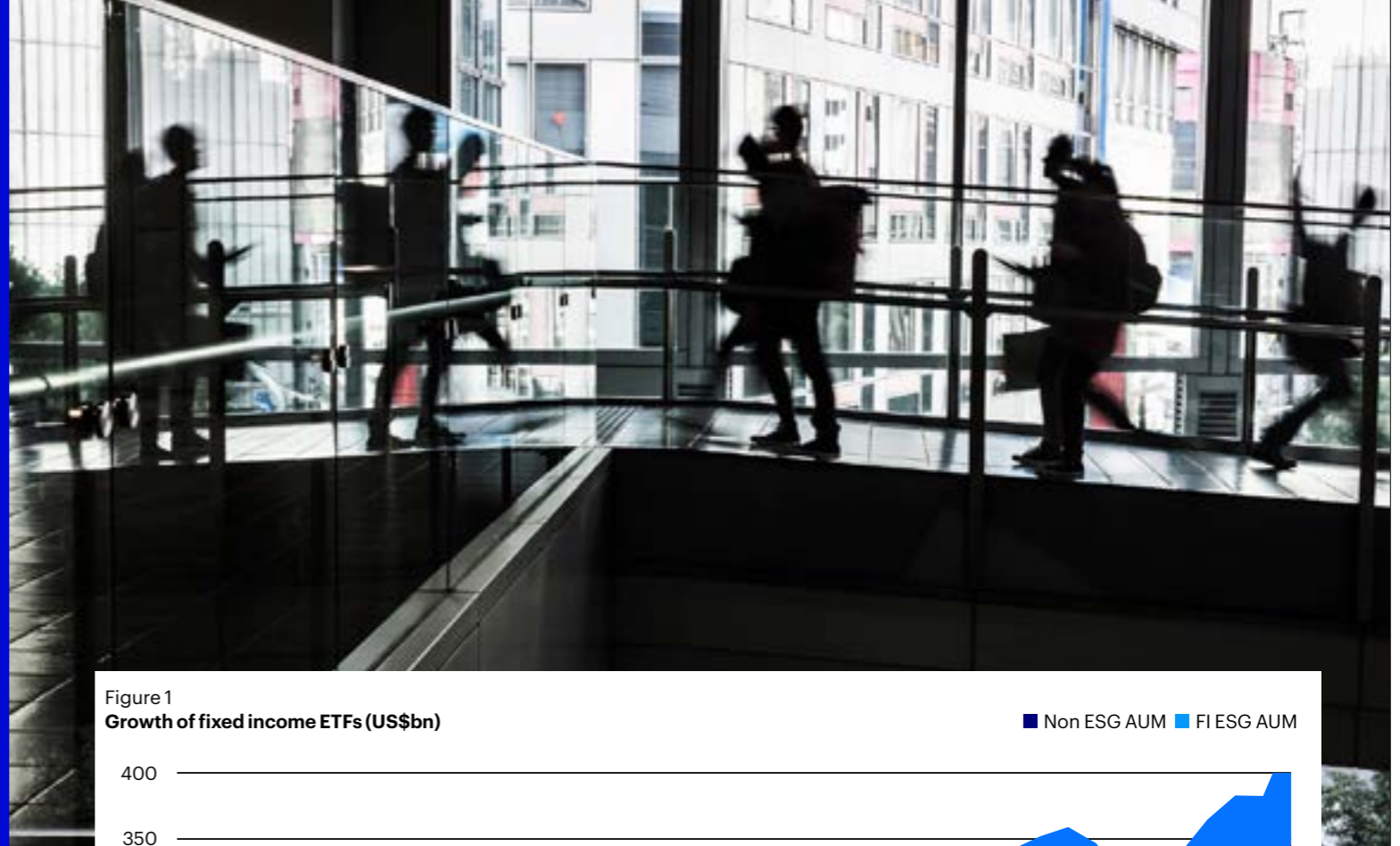
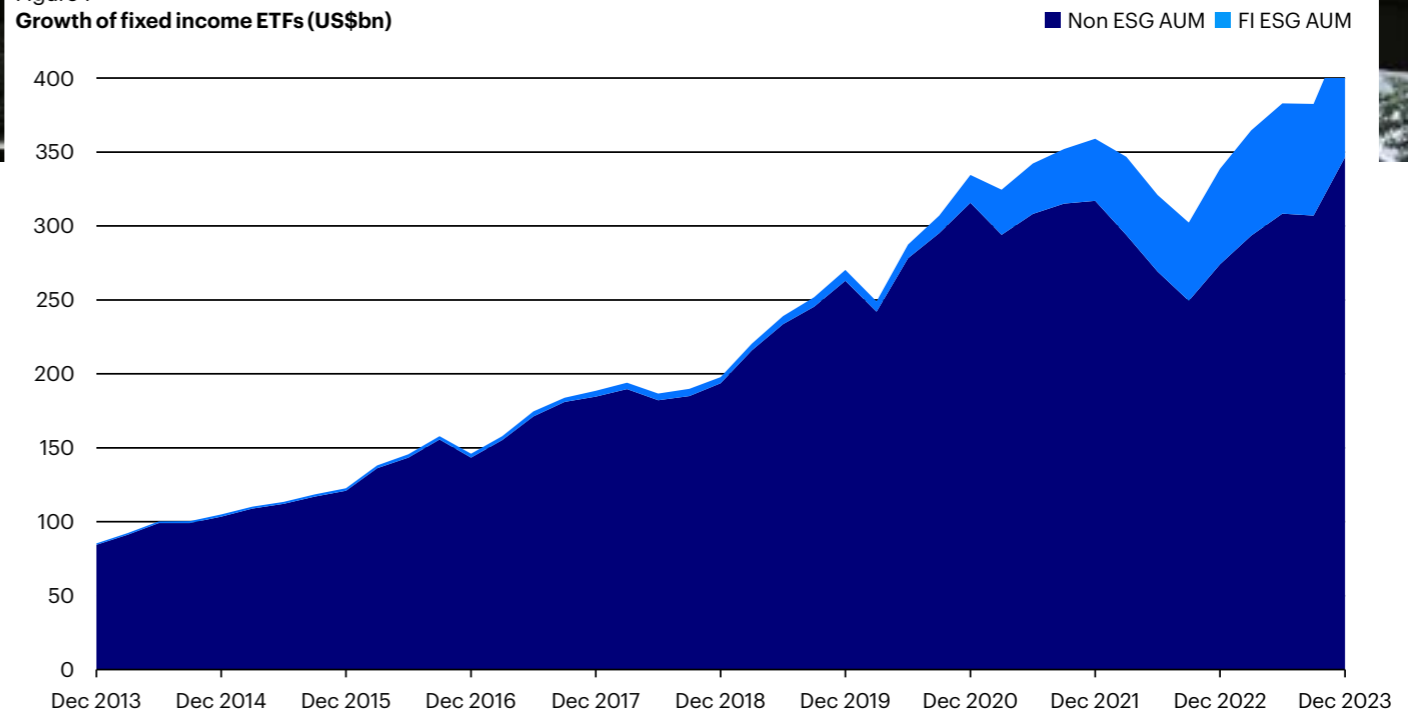


Figure 1
Growth of fixed income ETFs (US\$bn)



Data: Invesco, Bloomberg as at 29 December 2023.

Benefits of the ETF structure

The basic structure and the way ETFs trade could provide advantages compared to other investment vehicles.



Low cost of ownership

ETFs generally have low cost of ownership, particularly in fixed income. Headline fees only tell part of the story, however, so you need to compare other less obvious costs to determine which vehicle available to you offers the lowest overall cost of ownership. Variable costs are incurred from transactions and rebalancing, for instance, but you should also consider any revenues earned from securities lending as they will effectively reduce costs. You can compare the total costs of different vehicles tracking the same index by measuring their tracking difference.



Quick and easy access

Unlike some of the other investment alternatives, ETFs can be bought and sold throughout the trading day at continually updated bid and offer prices. Investing in an ETF is as simple as it is with ordinary stocks and shares. You may also be able to place different order types, which can give you more control over the price paid or received.



Transparency

The nature of the ETF structure requires transparency, as they are traded throughout the day rather than having a single valuation point. For this to be workable, investors, market makers and authorised participants (AP) all need to be able to agree on the value of the ETF's assets at any point in time. Therefore, every ETF disseminates to the market a detailed daily statement of its exact holdings. In combination with publicly available index rules, this level of transparency allows an investor to see exactly what they are getting when they buy an ETF, allowing them to anticipate how it should perform in a variety of market conditions.



Portfolio management

Passive portfolio management requires precision and accuracy to efficiently track fixed income indices. Having a dedicated ETF fixed income portfolio management team can offer further potential benefits through the use of sampling techniques, rebalancing procedures, and even through the creation / redemption process.

With an average of over 10 years' experience, our ETF portfolio management team has the experience and expertise to deliver accurate and consistent index performance. We have developed proprietary tools to assess key performance drivers and risks parameters across the entire investment horizon. As an independent US\$1.58 trillion¹ global asset manager, we also have the resources and trading relationships to find additional ways to improve costs and, in turn, performance.

¹ Source: Invesco, as at 31 December 2023.



Liquidity

One of the biggest advantages of an ETF is the enhanced liquidity compared to other types of investment. The vast majority of an ETF's trading activity is executed between buyers and sellers on the secondary market (the stock exchange) and with market-makers providing their own bid and offer prices. These matching trades do not involve the buying or selling of the underlying securities. Where orders cannot be filled in this way, shares in the ETF can be either created or redeemed on the primary market, offering an additional source of liquidity for investors.

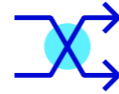
A further factor is that, due to the requirement for intraday liquidity, indices used for fixed income ETFs are often more liquid versions of broad benchmarks. Fixed income benchmarks are often complex with a high number of constituents. To make them more replicable and therefore suitable for an ETF, the number of constituents may be reduced, often by adding liquidity screens such as minimum issue size or seasoning (limiting the time since issue). As long as this is done intelligently, it should not detract from overall performance and can potentially enhance returns relative to a broad index, thus providing investors with a more liquid exposure to a fixed income asset class.



ETFs can provide investors with a more liquid exposure to a fixed income asset class.

ETFs vs. individual bonds

There are several possible advantages of gaining exposure to fixed income via ETFs rather than directly investing in underlying bonds.



Diversification

The first, and potentially most obvious, advantage is diversification. Buying a single ETF by trading just one line of stock can provide exposure to the broadest of fixed income asset classes. Fixed income indices are complex, making them difficult to replicate. For example, the Bloomberg Euro Aggregate Corporates Index has over 3,607 constituents from more than 690 issuers¹. Additionally, while some bonds have minimum trading lot sizes as low as €1,000, most fixed income securities have minimum lot sizes of €100,000, making it impossible for smaller investors to create a truly diversified portfolio through direct investment. Not only that, but the speed and ease of executing a single trade to gain broad asset class exposure relative to calculating a long list of trades, finding counterparties with the right inventory, executing, booking, and settling those trades will be far more time efficient.



Rebalancing

Adding to the efficiency of an ETF relative to direct holdings is the fact that cash flows are automatically reinvested (or paid out on a fixed schedule for distributing asset classes). There's also no need to monitor new issuance or bonds exiting the index as the portfolio is regularly rebalanced in line with index rules.



Transaction Costs

Another, but potentially less obvious advantage, concerns trading costs. The cost of investing in fixed income is not just about the fee being paid to access the asset class via a pooled vehicle, but rather the investor's "total cost of ownership", which also includes the cost of trading the underlying bonds. Bonds are traded over the counter (OTC), making pricing less transparent than securities that trade on exchange. Many corporate bonds do not have two-way (bid and offer) prices being quoted on a daily basis, which could make direct investment in underlying bonds *more costly* than investing in them via an ETF and accessing Invesco's top tier status as a \$1.58 trillion² asset manager.



Liquidity, efficiency, and currency hedging

The breadth of interest in an asset class is generally broader than it is for any individual security within that asset class. That means when it comes to secondary market trading, the ETF capitalises on demands of asset allocators or other "macro-level" investors. The diversified portfolio mitigates idiosyncratic risk and facilitates use of broad-market hedges, which means bid-offer spreads on the ETF can be tighter than the average spreads across its underlying securities. Additionally, the availability of currency hedged share classes can save time for portfolio managers who would otherwise have to value their direct holdings and execute appropriate forward FX trades to hedge currency exposure.

¹ Source: Bloomberg, as at 29 December 2023.

² Source: Invesco, as at 31 December 2023.

Use Cases

While structural advantages make ETFs inherently useful tools, some fixed income ETFs could be ideally suited to meet specific portfolio objectives.



Core Allocation

ETFs could be particularly attractive to investors looking for low-cost targeted exposure to specific segments of an asset class. Investors can construct the core, long-term, strategic elements of their diversified portfolios with a choice of government, agency and corporate debt exposures, with maturity buckets and currencies to match their requirements and objectives.

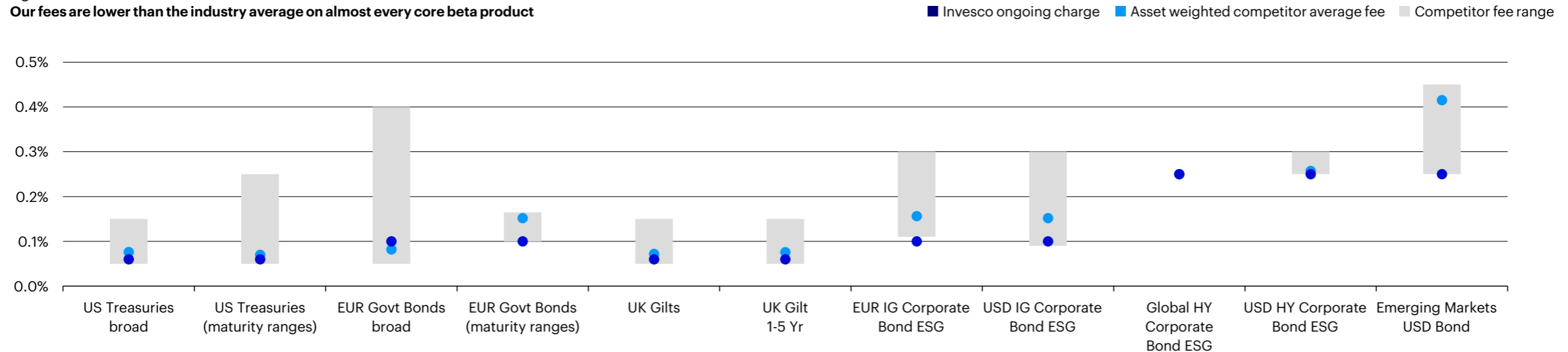
Taking a simplistic example of a 50/50 allocation between US Treasuries and US Investment Grade Credit, with no specific maturity target, an investor

could gain total exposure in two trades for an average OCF of just eight basis points (Invesco US Treasury Bond UCITS ETF at 6bps and Invesco USD Corporate Bond UCITS ETF at 10bps). Most investors will have more diverse and targeted strategic allocations than this, but the precision and variety of ETFs and their generally low cost compared to most other competing vehicles enables investors to construct well-diversified portfolios where each of the components follows a predictable, rules-based methodology.



Figure 2

Our fees are lower than the industry average on almost every core beta product



Source: Invesco, Bloomberg, 29 December 2023. Fee range is for ongoing charges, excluding Invesco products. Average is weighted by AUM. Competitor range is defined by all ETFs listed on a European exchange tracking the same or similar index.



Tactical allocation

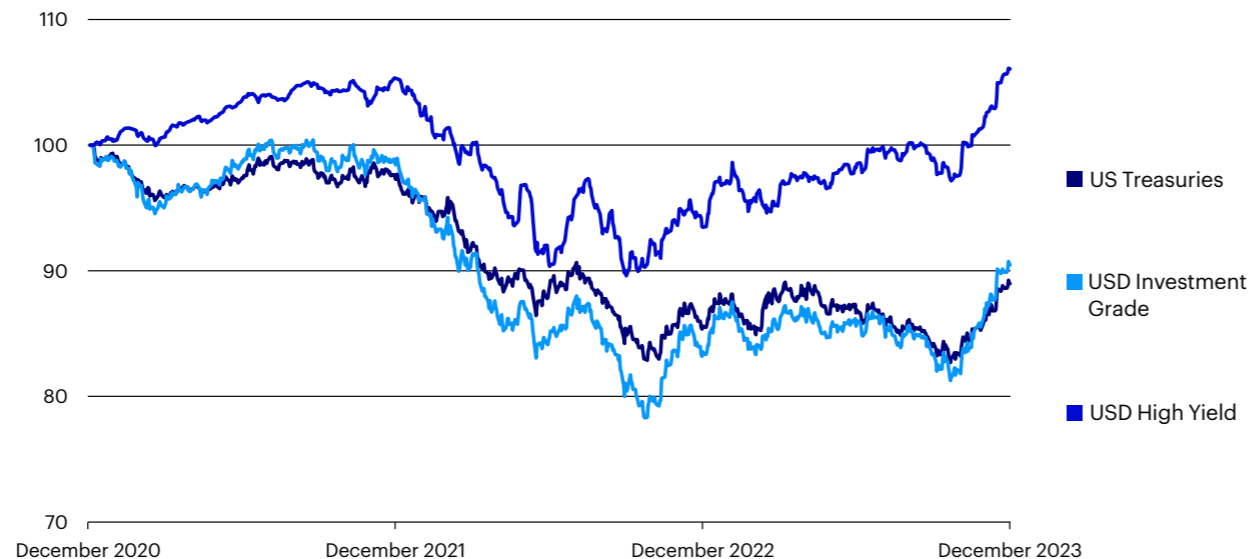
Given the targeted nature of ETFs, they provide an ideal vehicle to implement tactical asset allocation decisions compared to traditional actively managed mutual funds. Take, for example, an actively managed strategic bond fund. It would likely include allocations to sovereign, investment grade credit and potentially some high yield debt with the portfolio manager allocating to each asset class based on their views while remaining within their risk limits. The investor in that fund is relying on the portfolio manager to identify opportunities and to implement relevant allocations in the fund. However, an ETF can provide an end investor with the tools to be able to implement an asset allocation decision based on their own market views and risk appetite.

As an example, the COVID pandemic caused financial market volatility to increase substantially in February-March 2020, when government bonds rallied while credit spreads widened dramatically. However, central banks acted swiftly and aggressively to both support the global economy and

to stabilise financial markets. This provided a perfect opportunity to take on more credit risk, switching from government debt to investment grade credit and, for those with a higher risk tolerance, to allocate to riskier areas such as high yield, including fallen angels and subordinated debt. As the timing of the asset allocation decision (rather than the individual stock selection) would be the main driver of future returns, the ability to switch between asset classes with one sell and one buy trade is key. Trades being executed on same day allowed the end investor to quickly react to breaking news. There would have been no delay from deciding which holdings to sell, which to buy and having to seek liquidity and axed counterparties for potentially hundreds of lines of stock. ETFs would also ensure the investor gained broad asset class exposure, avoiding unwanted idiosyncratic risk. Over time, once the asset allocation had been changed, then some or all the new allocation could be unwound into an active fund or into individual bonds, depending on the investor's view.

Figure 3
Index performance

Past performance does not predict future returns.



Source: Bloomberg, Invesco, as at 29 December 2023. Indices shown are Bloomberg US Treasury Index, Bloomberg US Corporate Bond Index, and Bloomberg US Corporate High Yield Bond Index. Returns may increase or decrease as a result of currency fluctuations.



Core-satellite approach

ETFs can also be employed in a core-satellite approach, enhancing returns by adding higher performing asset classes in which the investor may lack expertise to be able to select individual holdings. An example could be adding the Invesco US High Yield Fallen Angels UCITS ETF to a broad high yield portfolio.

Over the long term, fallen angels have outperformed the broad high yield market, but they tend to be more volatile, particularly during economic downturns when there are a higher number of downgrades. A high yield investor is unlikely to fully switch their high yield exposure to a fallen angel strategy because they have different characteristics, but they may wish to boost exposure to that sector, particularly at certain points in the economic cycle, in which case an ETF using a systematic approach to investing in fallen angels would be the ideal vehicle. It avoids the need for the investor to monitor downgrades and source bonds, which can be time-consuming, as that is taken care of by the index methodology and the ETF manager.

This core-satellite approach can be applied to EUR-denominated investment grade credit with an addition of Invesco Euro Corporate Hybrid Bond UCITS ETF, or USD-denominated credit with the addition of Invesco AT1 Capital Bond UCITS ETF or Invesco US Municipal Bond UCITS ETF to either diversify risk, enhance returns, or in some cases, do both.

Either way, the principle is that fixed income ETFs give the end investor the ability to make the asset allocation decision themselves, based on their views and risk tolerance without having to rely on an active manager to identify opportunities and implement new allocations whilst remaining within their own risk limits.



ETFs provide an ideal vehicle in which to implement tactical asset allocation decisions



“
ETFs can provide investors with the ability to choose the right balance between improvement in ESG score and similarity to a broad non-ESG index.



Liquidity sleeve

Fixed income ETFs can be used as a liquidity sleeve in the strategic asset allocation of a multi-asset portfolio. Holding a small percentage of each asset class in an ETF could enable creations and redemptions to be handled efficiently, requiring only a single order per asset class rather than trading several lines of underlying bonds and seeking appropriate secondary market liquidity to execute the required orders.

An ETF could also be an efficient means for an active manager to remain fully invested with broad market exposure while waiting on primary market issuance to enter more concentrated positions and pick up some new issue premium. They also allow a higher level of precision for multi-asset portfolio rebalancing as trades will be executed on the same day as orders are placed.



ESG implementation

As ESG reporting becomes increasingly important, the ability to identify transparent methodologies and characteristics for those who do not have internal capabilities is vital. A passive and systematic approach where the same rules are applied across a broad investment universe can ensure high data quality where there is no scope for subjective interpretation. ETFs can provide investors with the ability to choose the right balance between improvement in ESG score and similarity to a broad non-ESG index.



Cash management

The granularity of ETF offerings can provide a solution for longer-term cash holdings by providing exposure that fits somewhere between money market and short-dated bond funds. This “ultra-short” sector is the first step out of cash along the yield curve and may offer higher returns than money market funds and lower volatility than short-term bond portfolios. They are not true substitutes for money market funds and are only suitable for longer-term cash holdings but can help in reducing cash drag in a multi-asset portfolio and may be used as a cash buffer to help absorb regular cash flows.



Transition management

ETFs provide targeted exposure to many different sectors of the fixed income market, enabling investors to remain fully invested in the asset class of their choice, with the appropriate characteristics such as duration, and at low cost, while they are going through the due diligence process of selecting a new active manager.

For example, if an active investment grade credit manager has been underperforming or has moved firms, the decision to move assets out of the active fund may occur before a new manager has been selected. In this case, it's most important to move the allocation away from the incumbent quickly but without changing the overall asset allocation. ETFs can provide the vehicle to remain fully invested in line with the desired asset allocation until the new manager has been chosen and avoiding the consequences of the portfolio being mismatched to that allocation until the new manager has been selected.



When an asset class is better as beta

One of the determining factors when deciding between an actively managed or passive approach is the potential to outperform the broad benchmark through security selection. This case is often illustrated by the US large-cap equity market, which has been notoriously difficult for most active managers to beat with any consistency.

The same can be observed in fixed income, with some segments more suitable for an active approach and others for passive exposure. The AT1 Capital Bond market is an example of the latter. When these instruments were first introduced, after the global financial crisis, active managers could use the newness and relatively small number of participants to their advantage. However, as the market has grown and investors have gained confidence and understanding, the AT1 market has become quite homogenous, with less distinction between issues. As a result, returns from actively managed AT1 funds and (lower cost) passive AT1 ETFs are now highly correlated. If you want exposure to the AT1 asset class, beta exposure makes the most sense.

Summary

Using ETFs to gain exposure to fixed income may have several advantages over other investment vehicles and offer effective use cases in your portfolio.

There are numerous ways that ETFs can be employed within a fixed income portfolio. From acting as a low cost core holding, to efficient means of implementing tactical asset allocations, and to simply avoid paying for active management in areas where opportunities for alpha generation are limited.

Fixed income ETFs have seen rapid growth in recent years – both in total assets under management and also in the number of products available with the market now offering a solution for (almost) every need of a fixed income investor.



Improve portfolio outcomes with Invesco's fixed income ETFs



Efficiency
Our ETFs are designed to track accurately.



Competitive fees
We aim to keep fees below the industry average across our core range and are continuously looking for ways to reduce costs.



High quality benchmarks
We work closely with index providers to offer intelligent choice of benchmarks, considering market representation, robustness, liquidity and value for money.



ESG options
We are committed to launching ESG versions of our core ETFs, with fees typically the same or lower than the equivalent non-ESG ETFs.

■ Core ■ ESG ■ Innovative income

Invesco Fixed Income ETFs	ISIN	Bloomberg ticker	Ongoing charge (p.a.)
Invesco US Treasury Bond 0-1 Year UCITS ETF	IE00BKWD3C98	TREI LN	0.06%
Invesco US Treasury Bond 1-3 Year UCITS ETF	IE00BF2FNG46	TRE3 LN	0.06%
Invesco US Treasury Bond 3-7 Year UCITS ETF	IE00BF2FNQ44	TRE7 LN	0.06%
Invesco US Treasury Bond 7-10 Year UCITS ETF	IE00BF2FN646	TREX LN	0.06%
Invesco US Treasury Bond 10+ Year UCITS ETF	IE00BKWD3743	TREL LN	0.06%
Invesco US Treasury Bond UCITS ETF	IE00BF2GFH28	TRES LN	0.06%
Invesco UK Gilt 1-5 Year UCITS ETF	IE00BGOTQ445	GLT5 LN	0.06%
Invesco UK Gilts UCITS ETF	IE00BGOTQC25	GLTP LN	0.06%
Invesco Euro Government Bond UCITS ETF	IE00BGJWWX56	EIBB GY	0.10%
Invesco Euro Government Bond 1-3 Year UCITS ETF	IE00BGJWWY63	EIB3 GY	0.10%
Invesco Euro Government Bond 3-5 Year UCITS ETF	IE00BGJWWV33	EIB5 GY	0.10%
Invesco Euro Government Bond 5-7 Year UCITS ETF	IE00BGJWWT11	EIB7 GY	0.10%
Invesco Euro Government Bond 7-10 Year UCITS ETF	IE00BGJWWW40	EIBX GY	0.10%
Invesco GBP Corporate Bond UCITS ETF	IE00BKW9SW28	IGCB LN	0.10%
Invesco Emerging Markets USD Bond UCITS ETF	IE00BF51K132	PEMD LN	0.25%
Invesco USD IG Corporate Bond ESG UCITS ETF	IE00BF51K025	PUIG LN	0.10%
Invesco EUR IG Corporate Bond ESG UCITS ETF	IE00BF51K249	PSFE GY	0.10%
Invesco EUR Corporate Bond ESG Multi-Factor UCITS ETF	IE0006LBEDV2	ECMF GY	0.19%
Invesco EUR Corporate Bond ESG Short Duration Multi-Factor UCITS ETF	IE000PA766T7	ECMS GY	0.15%
Invesco EUR Government & Related Green Transition UCITS ETF	IE0008SEV3B2	EGVD GY	0.15%
Invesco GBP Corporate Bond ESG UCITS ETF	IE00BKW9SV11	IGBE LN	0.10%
Invesco Global High Yield Corporate Bond ESG UCITS ETF	IE0001VDDL68	GBHA SW	0.25%
Invesco USD High Yield Corporate Bond ESG UCITS ETF	IE00BJP5NL42	UHYD LN	0.25%
Invesco US High Yield Fallen Angels UCITS ETF	IE00BDOQ9673	HYFA LN	0.45%
Invesco AT1 Capital Bond UCITS ETF	IE00BFZPF322	AT1 LN	0.39%
Invesco Euro Corporate Hybrid Bond UCITS ETF	IE00BKWD3966	EHBD GR	0.39%
Invesco Preferred Shares UCITS ETF	IE00BDVJF675	PRFD LN	0.50%
Invesco US Municipal Bond UCITS ETF	IE00BNG70R26	MUNI LN	0.28%
Invesco Variable Rate Preferred Shares UCITS ETF	IE00BG21M733	VRPS LN	0.50%

Source: Invesco, as at 29 December 2023. Bloomberg ticker shown is for primary exchange listing. Distributing, accumulating, and currency-hedged share class available for select ETFs. Any investment decision should take into account all the characteristics of the fund as described in the legal documents. For sustainability related aspects, please refer to [invesco.com/managementcompany.ie/dub-manco](https://www.invesco.com/managementcompany.ie/dub-manco). The investment concerns the acquisition of units in a fund and not in a given underlying asset.

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