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Three-Year Anniversary for the Largest Actively Managed High Yield ETF

Author:

Ryan O. Issakainen, CFA
Senior Vice President
Exchange Traded Fund Strategist
First Trust Advisors L.P.

Summary of Q1 2016 ETF Flows and Trends[1]

Table 1

US Category Group	Total US-Listed ETF Assets (3/31/16)	Estimated Net Asset Flows Q1 2016	Estimated Net Asset Flows Previous Quarter (Q4 2015)
Allocation	$7,152,397,367	($894,744,715)	$720,765,714
Alternative	$43,793,939,729	$3,281,080,443	($330,390,924)
Commodities	$60,625,420,014	$9,355,558,145	($213,034,671)
International Equity	$431,648,458,668	($5,205,454,228)	$22,254,583,415
Municipal Bond	$20,242,903,890	$1,667,731,259	$1,452,390,686
Sector Equity	$291,949,070,452	($5,556,916,547)	$10,470,553,217
Taxable Bond	$375,949,775,020	$32,258,009,632	$14,221,685,718
US Equity	$952,404,835,615	($2,227,765,391)	$46,899,148,127
Total	2,183,766,800,755	32,677,498,598	95,475,701,282

Source: Morningstar.

- US listed ETF net inflows totaled an estimated $32.7 billion in Q1, a significant drop from the $95.5 billion in net inflows in the previous quarter.
- Taxable Bond ETFs had the strongest net inflows, totaling $32.3 billion, more than double the net inflows for the category in the previous quarter.
- Commodity ETFs—one of two categories with net outflows in Q4 2015—had the second strongest net inflows in Q1 with $9.4 billion, as investors piled into precious metals ETFs.
- Equity ETF categories had the greatest net outflows in Q1, led by Sector Equity ETFs (-$5.5 billion), International Equity ETFs (-$5.2 billion), and US Equity ETFs (-$2.2 billion). This was a reversal from Q4 2015, in which all three had relatively strong net inflows.

HYLS and the Case for Active Management

While equity ETF categories were beset with net outflows in Q1, this pattern did not carry through to all "risky" asset categories, as high yield bond ETFs had $5.4 billion in net inflows, according to Morningstar data. Notably, the largest actively managed high yield bond ETF[1], the First Trust Tactical High Yield ETF (HYLS), grew by 45% in Q1 to $808 million, while also reaching its third anniversary on 2/25/16.

In contrast to passive index funds, the actively managed strategy employed by HYLS enables the fund's portfolio management team to address important risks faced by high yield investors, including credit risk, sector risk, and interest rate risk (among others). We believe that navigating these risks is critical for investors pursuing superior risk-adjusted total returns from high yield bonds. The following highlights some of the techniques utilized by HYLS to manage risk, while drawing comparisons with passive high yield bond index funds.

Credit Risk

High yield bond indices are comprised of debt securities issued by below-investment grade borrowers. In most cases, portfolio weightings are determined by the relative market values of constituent bond issues. Put another way, these indices tend to allocate proportionately higher weights to the most indebted issuers. While such indices may be suitable benchmarks for measuring the performance of the high yield asset class, we believe this approach fails to explicitly consider one of the simplest criteria for determining whether or not to lend money to any borrower: namely, their ability to pay the interest and principal on their debts.

As an actively managed ETF, HYLS does not seek to replicate the performance of a benchmark. This provides the ETF's portfolio management team more flexibility to be selective in determining portfolio holdings and allocations. Decisions about which bonds to invest in are made after assessing macro-economic and industry trends, and evaluating the consistency of issuers' cash flows, asset values, and management quality. In contrast to passive index funds, bonds that are deemed too risky, or believed to not offer adequate compensation for the assessed level of risk, may be avoided by the fund's portfolio managers.

Sector Risk

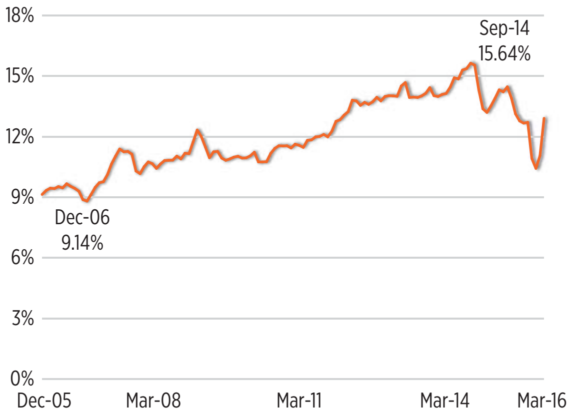
Another consequence of the market cap weighting scheme utilized by most high yield bond indices is that allocations tend to favor sectors in which the greatest amount of borrowing has occurred. For many cyclical sectors and industries, the greatest amount of leverage—and bond issuance—tends to occur toward the end of expansionary cycles. As revenue growth slows, these issuers may have a more difficult time servicing their debts, and default rates may increase.

[1]Based on Morningstar data, as of 3/31/16.
Past performance is not a guarantee of future results and there is no assurance that the events or improvements mentioned herein will continue.

The energy sector provides one recent example to illustrate this point. At the start of 2007, the energy sector represented 9.1% of the Bank of America Merrill Lynch US High-Yield Constrained Index (See Chart 1). As energy companies began to develop and employ new exploration and production techniques, such as hydraulic fracturing and horizontal drilling, and as crude oil prices trended higher, they began to increase leverage by issuing more bonds. As a result, the index's allocation to the energy sector steadily increased to 15.6% by 9/30/14, when the spot price of WTI Crude Oil closed at $91.16 (See Chart 2). As crude oil prices collapsed in the subsequent months, concerns about potential defaults resulted in significant underperformance for most energy bonds.

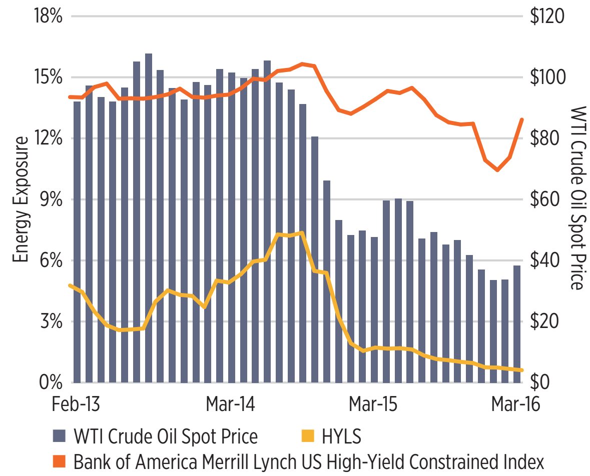
Since HYLS is an actively managed ETF, its portfolio management team may choose to over- and underweight certain sectors, based on perceived opportunities and risks. Accordingly, HYLS had a significantly underweight allocation to the energy sector, at 7.4%, on 9/30/14. Moreover, during the next four months, as the spot price of WTI crude oil dropped below $50/barrel, the energy allocation within HYLS was further reduced to below 2%. As a result, HYLS avoided much of the negative impact that falling oil prices had on energy bonds, as compared to passive high yield bond index funds.

Chart 1
Bank of America Merrill Lynch US High-Yield Constrained Index: Energy Exposure (12/31/05-3/31/16)



Source: Bloomberg.

Chart 2
High Yield Energy Exposure and WTI Crude Oil Spot Price (2/28/13-3/31/16)



Source: Bloomberg.

Interest Rate Risk

High yield bonds have often been less sensitive to rising interest rates than investment grade bonds during periods in which a strengthening economy has led to lower default rate expectations and narrowing credit spreads. However, during periods in which credits spreads are already narrower than average, high yield bonds may exhibit a greater degree of interest rate sensitivity.

While interest rate risk is not generally addressed by passive high yield bond index ETFs, HYLS may employ several measures to manage duration. For example, while the duration of passive indices is generally determined by historical bond issuance, HYLS may tailor its duration exposure at certain key rates. Additionally, in order to shorten its effective duration, the fund may invest in floating-rate debt securities, with ultra-short durations. The fund also has the ability to take short positions in US Treasury securities in order to reduce its effective duration. Each of these measures may be tactically employed, or removed, in order to manage interest rate risk.

In the context of a diversified investment portfolio, we believe that high yield bond ETFs may enhance portfolio diversification, while providing an attractive level of income for investors. However, passively managed high yield bond index ETFs fail to address many of the risks that can be mitigated by active management, in our opinion.

HYLS has received an Overall Morningstar Rating™ of five stars, as of 3/31/16, among 646 funds in the High Yield Bond category. This fund was rated 5 stars/646 funds (3 years).[2] The fund was the top performing ETF tracked by Morningstar in the high yield category for 2014 and 2015 (out of 17 and 21 funds, respectively).

You should consider a fund's investment objectives, risks, and charges and expenses carefully before investing. Contact First Trust Portfolios L.P. at 1-800-621-1675 or visit www.ftportfolios.com to obtain a prospectus or summary prospectus which contains this and other information about a fund. The prospectus or summary prospectus should be read carefully before investing.

[2]The Morningstar Rating™ is provided for those exchange-traded funds ("ETFs") with at least a three-year history. Ratings are based on the ETF's Morningstar Risk-Adjusted Return measure which accounts for variation in monthly performance, placing more emphasis on downward variations and rewarding consistent performance. An ETF's risk-adjusted return includes a brokerage commission estimate. This estimate is intended to reflect what an average investor would pay when buying or selling an ETF. PLEASE NOTE, this estimate is subject to change and the actual brokerage commission an investor pays may be higher or lower than this estimate. Morningstar compares each ETF's risk-adjusted return to the open-end mutual fund rating breakpoints for that category. Consistent with the open-end mutual fund ratings, the top 10% of ETFs in each category receive 5 stars, the next 22.5% receive 4 stars, the next 35% receive 3 stars, the next 22.5% receive 2 stars and the bottom 10% receive 1 star. The overall rating for an ETF is based on a weighted average of the time-period ratings (e.g., the ETF's 3, 5, and 10 year rating). The determination of an ETF's rating does not affect the retail open end mutual fund data published by Morningstar. ©2016 Morningstar, Inc. All Rights Reserved. The Morningstar Rating™ information contained herein: (1) is proprietary to Morningstar; (2) may not be copied or distributed; and (3) is not warranted to be accurate, complete or timely. Neither Morningstar nor its content providers are responsible for any damages or losses arising from any use of this information. Past performance is no guarantee of future results.

ETF Characteristics

The fund lists and principally trades its shares on The Nasdaq Stock Market LLC.

Investors buying or selling fund shares on the secondary market may incur customary brokerage commissions. Market prices may differ to some degree from the net asset value of the shares. Investors who sell fund shares may receive less than the share's net asset value. Shares may be sold throughout the day on the exchange through any brokerage account. However, unlike mutual funds, shares may only be redeemed directly from the fund by authorized participants, in very large creation/redemption units.

Risk Considerations

The fund's shares will change in value and you could lose money by investing in the fund. The fund is subject to management risk because it is an actively managed portfolio. In managing the fund's investment portfolio, the advisor will apply investment techniques and risk analyses that may not have the desired result. There can be no assurance that the fund's investment objectives will be achieved.

The fund is subject to market risk. Market risk is the risk that a particular security owned by the fund or shares of the fund in general may fall in value.

High-yield securities, or "junk" bonds, are subject to greater market fluctuations and risk of loss than securities with higher ratings, and therefore, may be highly speculative. These securities are issued by companies that may have limited operating history, narrowly focused operations, and/or other impediments to the timely payment of periodic interest and principal at maturity. The market for high-yield securities is smaller and less liquid than that for investment grade securities.

High-yield securities are subject to credit risk, interest rate risk, and income risk. Credit risk is the risk that an issuer of a security will be unable or unwilling to make dividend, interest and/or principal payments when due and that the value of a security may decline as a result. Interest rate risk is the risk that if interest rates rise, the prices of the fixed-rate instruments held by the fund may fall. Income risk is the risk that if interest rates fall, the income from the fund's portfolio will decline as the fund intends to hold floating-rate debt that will adjust lower with falling interest rates.

Companies that issue loans tend to be highly leveraged and thus are more susceptible to the risks of interest deferral, default and/or bankruptcy. Senior floating rate loans, in which the fund may invest, are usually rated below investment grade but may also be unrated. As a result, the risks associated with these loans are similar to the risks of high-yield fixed income instruments. Loans are subject to prepayment risk. The degree to which borrowers prepay loans may be affected by general business conditions, the financial condition of the borrower and competitive conditions among loan investors, among others. The fund may not be able to reinvest the proceeds received on terms as favorable as the prepaid loan.

The market values of convertible bonds tend to decline as interest rates increase and, conversely, to increase as interest rates decline. A convertible bond's market value also tends to reflect the market price of the common stock of the issuing company.

The fund may invest in distressed securities and many distressed securities are illiquid or trade in low volumes and thus may be more difficult to value.

In times of unusual or adverse market, economic, regulatory or political conditions, the fund may not be able, fully or partially, to implement its short selling strategy. Short selling creates special risks which could result in increased volatility of returns and may result in greater gains or greater losses.

The fund invests in securities of non-U.S. issuers which are subject to higher volatility than securities of U.S. issuers. Because the fund's NAV is determined on the basis of U.S. dollars and the fund invests in non-U.S. securities, you may lose money if the local currency of a non-U.S. market depreciates against the U.S. dollar.

The fund currently intends to effect a portion of creations and redemptions for cash, rather than in-kind securities. As a result, the fund may be less tax-efficient.

First Trust Advisors L.P. is the adviser to the fund. First Trust Advisors L.P. is an affiliate of First Trust Portfolios L.P., the fund's distributor.

» Performance Summary (%)	Inception Date	Quarter	YTD	1 Year	3 Year	Since Inception
HYLS Performance as of 3/31/16*	2/25/13					
Net Asset Value (NAV)		2.11	2.11	-0.57	3.74	4.07
After Tax Held		1.46	1.46	-3.06	1.15	1.48
After Tax Sold		1.19	1.19	-0.32	1.69	1.94
Market Price		2.22	2.22	-0.60	3.83	4.13

Performance data quoted represents past performance. Past performance is not a guarantee of future results and current performance may be higher or lower than performance quoted. Investment returns and principal value will fluctuate and shares when sold or redeemed, may be worth more or less than their original cost. You can obtain performance information which is current through the most recent month-end by visiting www.ftportfolios.com.

Total Annual Expenses are 1.23%. Management fees are 0.95% and borrow costs are 0.28%. Borrow costs include expenses associated with short sales transactions. Please refer to a fund's current prospectus for a complete description of fees and expenses.

*__After Tax Held__ returns represent return after taxes on distributions. Assumes shares have not been sold. **After Tax Sold** returns represent the return after taxes on distributions and the sale of fund shares. Returns do not represent the returns you would receive if you traded shares at other times. **Market Price** returns are based on the midpoint of the bid/ask spread. Returns are average annualized total returns, except those for periods of less than one year, which are cumulative. After-tax returns are calculated using the historical highest individual federal marginal income tax rates and do not reflect the impact of state and local taxes. Actual after-tax returns depend on the investor's tax situation and may differ from those shown. The after-tax returns shown are not relevant to investors who hold their fund shares through tax-deferred arrangements such as 401(k) plans or individual retirement accounts.

30-Day SEC Yield as of 3/31/16 is 5.32%. The 30-day SEC yield is calculated by dividing the net investment income per share earned during the most recent 30-day period by the maximum offering price per share on the last day of the period and includes the effects of fee waivers and expense reimbursements.

The **BofA Merrill Lynch US High Yield Constrained Index** tracks the performance of U.S. dollar denominated below investment grade corporate debt publicly issued in the U.S. domestic market but caps issuer exposure at 2%.