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Structured products with leverage effect

This document contains information about the properties of structured products with leverage effect and informs you about potential benefits and risks of this class of products. These principles can support you in your investment decisions. Please contact your Client Advisor if you would like further information or have any questions.

General Information

Structured products are debt securities with a value comprised of different components. They usually have pre-defined terms. Their underlying assets can be bonds, stocks, indices, currencies, and commodities, as well as derivatives of the named investment categories.

Structured products with leverage effect These are structured products that contain derivatives with a leverage effect. The performance of such products depends disproportionately on their underlying assets. The leverage effect occurs in that the investor participates in the price development of the underlying asset without buying the underlying asset itself. For example, the investor only invests the option premium, which is less than the price of the underlying asset. In this way, with a much lower capital input a similarly high profit can be obtained. The leverage is the percentage price change of the product if the underlying assets change by 1 %. For example, if the price of the product changes by 7 % with a price change of 1 % in the underlying assets, then the leverage is 7.

The price of an option[1] depends on the term, the underlying assets and their volatility, the interest rate, and any dividends on the underlying assets.

Types of leverage products

Warrants (option certificates) are securitized options. Tradable quantities are typically smaller than with exchange-traded option contracts.

Spread warrants are comprised of two options. In this respect, one option is purchased and at the same time another is sold. Both options have the same underlying assets. The profit and loss opportunities are thereby limited. Depending on the combination, the investor may be counting on rising prices (bull spread) or falling prices (bear spread) of the underlying assets.

Knock-out warrants have an additional barrier. If the barrier is exceeded or not reached, the option expires immediately. The prices of these warrants are not, or only slightly, influenced by the volatility of their underlying assets. A rise in volatility increases the likelihood of a knock-out. There is no or only a minimal time value. The leverage effect with knock-out warrants is higher than with other warrants. They are therefore riskier than other types of warrants.

Mini-futures: Investors finance the underlying assets only to a limited extent. The remainder (financing level) is assumed by the issuer of the mini future. The closer the financing level is to the current share price, the greater is the leverage effect, because the investor participates fully in the development of the underlying assets. For this, interest is paid on the financing portion. The issuer charges the interest by adjusting the financing level daily. A stop-loss mark is built in. If the underlying assets reach this mark, the product is liquidated and any remaining amount is paid out. The term of these products is not limited.

Forms of exercise: A distinction is made between American and European types. American-type warrants may be exercised on any trading date up to the date of maturity. European-type warrants may only be exercised on their date of maturity, but may be traded beforehand over the secondary market.

Potential benefits

Investments with low capital input: With a low amount of capital, an investor can participate in the development of the underlying assets.

Representation of all market expectations: An investor who has negative expectations with regard to the price movements of a particular underlying asset can use the leverage effect to focus on it.

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[1] A detailed description of options is included in the derivatives fact sheet. Please contact your Client Advisor for additional information.

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Hedging: Derivates can be used for hedging of certain positions against losses in value or the occurrence of unwanted developments. A transfer of risk takes place.

Potential risks

Risk of loss: Depending on the development of the underlying assets, major losses, including the total loss of the invested capital, may occur.

Risk of leverage effect: The greater the leverage, the riskier and more speculative is the product. The potential for loss in dependence on the development of the underlying assets is strengthened proportionally to the leverage.

Market risk: The investor bears the risk that the value of the structured product may decrease during the term.

Counterparty risks: The issuer risk (counterparty risk) describes the risk regarding the credit rating of the counterparty. In the event of insolvency of the issuer, the repayment at the end of the term may fail to materialize and thus a total loss of the invested capital may occur. If the credit rating of an issuer deteriorates during the term of the product, the secondary market price may decrease. This may also result in a loss in the event of a sale before the end of the period.

Liquidity risk: The investor bears the risk that the investment must be held until the end of the term in an illiquid market or sold before maturity at an unfavourable price.

Foreign currency risk: If the financial instruments or the underlying assets are listed in a different currency from the local currency of the investor, there is a risk that fluctuations in the exchange rate will decrease the value of the investment from the investor's perspective. It is possible that the price gains of an investment result in a total loss for the investor due to exchange rate changes. Exchange rates can fluctuate substantially.

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