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# INVESTING IN COMPLEX INVESTMENTS

# RISK WARNING

Under current Financial Conduct Authority rules, the investment you wish to deal in is defined as “complex”. We are required to make sure you understand how dealing in this type of investment differs from trading “non-complex” investments, such as most shares and funds (known as Unit Trusts and OEICs).

Where you have not dealt in a particular complex investment in the past, we are also required to carry out an Appropriateness Assessment. This involves asking you a number of questions about your investment experience in relation to that class of complex investment. If, based on the answers you provide, we believe the investment would not be appropriate for you, we will tell you, and we will not undertake the transaction.

If you have any questions, please call us on 020 3889 1610 for further details.

This notice is provided to you as a Retail Client, in compliance with the rules of the Financial Conduct Authority. Retail Clients are afforded greater protections under these rules than other customers. Please note that this notice cannot disclose all the risks and other significant aspects of complex investments. You should not deal in these products unless you understand the nature and extent of your exposure to them. You need to be satisfied that the product is suitable for you having considered your circumstances and financial position.

Although these products can be used for the management of investment risk, some of these products are unsuitable for many investors.

Different instruments involve different levels of exposure to risk and in deciding whether to trade in such instruments you need to be aware of the following points:

## 1. Warrants

A warrant is a time-limited right to subscribe for shares, debentures, loan stock or government securities and is exercisable against the original issuer of the underlying securities. A relatively small movement in the price of the underlying security results in a disproportionately large movement, unfavourable or favourable, in the price of the warrant. The prices of warrants can therefore be volatile. It is essential for anyone who is considering purchasing warrants to understand that the right to subscribe which a warrant confers is invariably limited in time. This means that if the investor fails to exercise this right within the predetermined time-scale then the investment becomes worthless.

You should not buy a warrant unless you are prepared to sustain a total loss of the money you have invested plus any commission or other transaction charges.

## 2. Subscription Shares

Subscription shares are similar to warrants, in that they offer shareholders the right to purchase shares at specified future dates or during predetermined conversion periods at predetermined prices. However, unlike warrants, subscription shares qualify for the stocks and shares component of an ISA and self invested personal pensions (SIPPs).

As a holder of subscription shares, an investor can decide whether to subscribe for new ordinary shares on these dates. Subscription Shares represent a geared investment, so a relatively small movement in the market price of the Ordinary Shares may result in a disproportionately large movement, either positively or negatively in the market price of the Subscription Shares. In addition, the price may not move in line with that of the ordinary underlying share price for reasons such as supply and demand, and because of the remaining time period for which they are in existence. You could lose your entire investment as the Subscription Shares could expire worthless if their net asset value is below the Final Exercise price.

## 3. Securitised Derivatives

These instruments may give you a time-limited right to acquire or sell one or more types of investment, which are normally exercisable against someone other than the issuer of that investment. Or they may give you rights under a contract for differences, which allow for speculation on fluctuations in the value of the property of any description or an index, such as the FTSE 100 index. In both cases, the investment or property may be referred to as the “underlying instrument”. These instruments often involve a high degree of gearing or leverage, so that a relatively small movement in the price of the underlying investment results in a much larger movement, unfavourable or favourable, in the price of the instrument. The price of these instruments can therefore be volatile.

These instruments have a limited life, and may (unless there is some form of guaranteed return to the amount you are investing in the product) expire worthless if the underlying instrument does not perform as expected. You should only buy this product if you are prepared to sustain a total loss of the money you have invested plus any commission or other transaction charges. You should consider carefully whether or not this product is suitable for you in light of your circumstances and financial position, and if in any doubt please seek professional advice.

## 4. Convertible Bonds

A convertible bond is one which has an equity convertible element contained within it. This allows the investor the option to convert the bond into a given number/ratio of shares in the underlying company at a given price. Throughout the specified life of the bond, holders receive a regular dividend income, albeit generally at levels lower than those associated with the vast majority of bonds. However, at the specified point in time, holders have the right to convert into the said number of shares. The conversion is at the holder's choice and cannot be forced by the issuing company. Having the option to convert to shares, the bonds are often seen as having an embedded ‘call’.

In times when the underlying company is doing well, the share price will rise, however, the bond itself is unlikely to do much and the holder will wish to exercise the option at the earliest possible point. However, in times of a decline and value in the share price, the holder is unlikely to convert, preferring to keep within the bond unconverted. In the extreme event of the company going bust, bondholders rank higher than shareholders in terms of repayment.

The final consideration should be that of the income differential between converting and not converting. The bond will be paying interest, albeit lower than normal due to the convertible element, however, the share will pay a dividend, and is unlikely to exceed the income stream from the bond in the early years of the life of the bond.

## 5. Convertible Preference Shares

The investor has the option at a pre-defined date or dates, to convert the holding of preference shares into the class of underlying ordinary shares. Due to the investor having the option to convert, they are seen to have an embedded ‘call’ option. The risk exposure to which the investor should be aware is that of general market volatility. As with Convertible Bonds, the option to exercise the ‘call’ is entirely at the discretion of the holder subject to the specified conversion dates. Like convertible bonds, the convertible preference shareholder is ranked higher than ordinary shareholders in terms of repayment, although it is outranked by bond holders.

## 6. Exchange Traded Commodities (ETCs)

Exchange Traded Commodities are investments (asset backed bonds) that allow the investor to track the underlying performance of a commodity index, including total return indices. Trading is exactly the same as any normal share, in that prices are available throughout the trading day, with market maker support, thereby stimulating liquidity.

ETCs themselves will either focus solely on a single commodity or on an Index, examples being Gold, Silver or Lean Hogs for individual commodity exposure or energy and livestock for Index exposure.

In terms of risk, due to the very nature of the underlying commodity in which the ETC invests, this asset class is not for the faint hearted as sudden swings and drops in worldwide demand will immediately impact the share price. The commodity investment will be either directly within the physical product, or be priced on the futures market. If the investment is based on the futures market, the risks associated with this form of investment include gearing or leverage (as explained in paragraph 2), which will increase the risk and volatility.

## 7. Nil Paid Rights

Sometimes, companies may decide to raise further funds from its shareholders in return for the issue of further shares. This is known as a ‘rights issue’. Should an entitled shareholder decline to take up the rights allocated to them, they have the opportunity to sell these rights to the new shares ‘nil paid’ (i.e. without paying anything further to the company) or let them lapse (where the company sells the ‘nil paid rights’ on the investors behalf and remits any realising proceeds to the relevant investors). The purchaser in the open market will then have the opportunity to take up the shares at the discounted rights issue price. The new investor has effectively purchased a short dated (maximum 21 days) ‘call’ option, which can only be exercised within this given period. Investors need to be fully aware as to why the rights issue has been made by the company, as there is the potential that take up of the rights issue may not reach the required levels and will introduce an exposure to the risk of failure of any ‘guaranteeing’ party, therefore increasing the risk and volatility.

## 8. Structured Products

Structured products have been created to allow investors to meet needs that are unable to be met through the standard financial instruments available within the markets. They are used as an alternative to direct investment and as part of an asset allocation process to help reduce risk and exposure within a portfolio.

The general concept is based around investment within derivatives (normally options, but with the ability to utilise ‘swaps’ i.e. when one investment is temporarily exchanged for another) but with the added feature of protection if held to maturity. Due to the varying combinations of derivatives and financial instruments within the structures, there are significant risks involved, which should not be underestimated.

## Liquidity

In certain circumstances, a variety of financial instruments may have difficulty in providing readily available liquidity due to the nature of the underlying investment. To this extent, certain investments may carry warnings advising that should the investor wish to liquidate their holding, there may be a given period of time before which the benefits can be realised. An example of this may potentially be an investment containing commercial property, which following a run of people requesting their money, the investment manager may need to sell some of the underlying assets to raise cash.

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## APPROPRIATENESS ASSESSMENT

In order for us to understand a little bit about your investment knowledge and experience, please can you take a moment to complete this assessment.

If based on the answers you provide, we believe the investment would not be appropriate for you, we will tell you, and we will not undertake the transaction.

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Please tick Yes or No in the **Risk section**

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Please tick the statements that you feel apply to you in the **Your Understanding section**

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Please tick the investments that you propose to invest in

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Are you fully aware of the risks these types of investments carry?

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What is the approximate value of your overall investment portfolio?

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What level of your overall portfolio does this investment represent?

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### Section 1: Your details

Title \_\_\_\_\_ Surname \_\_\_\_\_

First names \_\_\_\_\_

Phone \_\_\_\_\_ Email \_\_\_\_\_

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### Section 2: Assessment

Are you comfortable with the level of risk you are taking with these types of investments? Yes  No

Do you understand that there may not be a cooling off, or cancellation period and once the application and monies have been submitted, encashment of the investment may not be possible? Yes  No

Do you understand that higher risk investments can yield higher returns but there is no guarantee and you may get back less than you invested? Yes  No

Do you understand the nature and level of charges payable with these types of investment? Yes  No

I have substantial experience and knowledge of dealing in stock market securities on an execution only basis (i.e. making my own investment decisions).

I have gained adequate knowledge of Complex Financial Instruments in my current profession or a former one.

Neither of the above statements applies to me.

Please detail in the box below any other information which you feel will help explain how you have gained the necessary investment knowledge to deal in Complex Financial Instruments. This might include, for example, brief details of your present or former occupation, or details of particular aspects of your general education or courses you have attended.

- |  |  |  |
|--|--|--|
| <input type="checkbox"/> Contract for Difference     | <input type="checkbox"/> Forex (Spot or Forward)       | <input type="checkbox"/> Futures & Options   |
| <input type="checkbox"/> Warrants                    | <input type="checkbox"/> Securitised Derivatives       | <input type="checkbox"/> Convertible Bonds   |
| <input type="checkbox"/> Exchange Traded Commodities | <input type="checkbox"/> Nil Paid Rights               | <input type="checkbox"/> Structured Products |
| <input type="checkbox"/> Subscription Shares         | <input type="checkbox"/> Convertible Preference Shares |  |

Yes  No  Unsure

Up to £5,000  £5,000 to £15,000  £15,000 to £30,000  
 £30,000 to £75,000  £75,000 to £150,000  £150,000+

Up to 1%  1% to 3%  3% to 7%  
 7% to 10%  10% to 20%  20%+

Have you invested in any of these investments in the past? (tick all that apply)

- Warrants
- Exchange Traded Commodities
- Subscription Shares
- Securitised Derivatives
- Nil Paid Rights
- Convertible Preference Shares
- Convertible Bonds
- Structured Products

Would you be prepared to lose a significant part of your investment?

- Yes
- No

How long have you been dealing in these Complex Investments?

- Up to 1 year
- 5 to 10 years
- 1 to 3 years
- 10+ years
- 3 to 5 years

What is your average total dealing activity per year?

- Up to 5 deals
- 20 to 50 deals
- 5 to 10 deals
- 50+ deals
- 10 to 20 deals

Do you believe your educational background and/or profession or former profession are relevant in understanding the risks involved?

- Yes
- No

I/we are satisfied that the instrument is an appropriate investment product in light of my/our circumstances and financial position. I/we have read and understood the complex investments risk warning and have answered the questions overleaf to the best of my/our knowledge.

**Section 3: Declaration**

Signature \_\_\_\_\_ Date \_\_\_\_\_

Signature \_\_\_\_\_ Date \_\_\_\_\_

**For office use only**

CF30 \_\_\_\_\_ Date \_\_\_\_\_

Outcome \_\_\_\_\_