



OVERVIEW OF THE PRINCIPAL CHARACTERISTICS  
AND RISKS OF FINANCIAL INSTRUMENTS

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# INTRODUCTION

Risks are inherent in investment in financial instruments. They are not identical nor at the same level for all financial instruments. There are, for example, more risks related to investing in turbos than investing in funds. This kind of product is therefore not suitable for less experienced investors.

It is important that you are aware of the risks before you invest with Keytrade Bank. That is the purpose of this document. First, we will describe some general risks that may apply to any financial instruments. We describe below the characteristics and risks of each financial instrument.

This overview of the most important characteristics and risks of financial instruments is, however, not exhaustive nor very detailed. Investing always also Nods a dose of common sense. Realistic expectations and pre-defined investment goals. Knowing how much money you can afford to lose, and never taking more risks than appropriate to your knowledge, experience and character. By adhering to these rules you will avoid disappointments and unpleasant financial surprises.

For more information about investment risks you can always contact Keytrade Bank. Our Helpdesk staff will be happy to help you on + 32(0)2 / 679 90 00 (business days from 9.00 am until 10.00 pm), or by email at [info@keytradebank.com](mailto:info@keytradebank.com).

Keytrade Bank organises regular information sessions relating to the products and services that we offer. See our website at [www.keytradebank.be](http://www.keytradebank.be) for the dates and topics of these info-sessions.

## 1 GENERAL INVESTMENT RISKS

The following general risks may exist to a greater or lesser extent for any financial instruments.

### Price risk

An unexpected fall in the price of the financial instruments is almost inevitable when investing. You can limit price risk as far as possible, of course. Spreading your investments across different types of financial instruments and, within the same category, across different instruments, is one of the best ways of doing this.

### Exchange rate risk

If you invest in a currency other than the euro then the rate for that currency when you sell securities may be different to the rate when you bought it. This can have either a positive or a negative effect on your investments. This risk is greatest with weaker currencies or the currencies of countries that are having problems.

### Credit risk

This is the possibility that the body issuing a financial instrument (such as a bond) – the debtor – will not meet its obligation to repay the principal, or fails to make the (annual or interim) interest payments, in part or in full. The most common cause of this is the poor financial position or bankruptcy of the issuing body.

### Liquidity risk

Liquidity risk occurs when a given investment is difficult to sell. A distinction Nods to be made between illiquidity caused by the interaction of supply and demand and illiquidity due to the nature of the specific financial instrument or market practices. Illiquidity is caused by supply and demand if there is (almost) only a supply (sellers) of a financial instrument at a given price. This is also the case if there is (almost) only demand (buyers) for a financial instrument for a given price. The result of this is that buy and sell orders cannot be executed immediately, or only in part and on unfavourable terms. Illiquidity due to the innate characteristics of a financial instrument or because of market practices occurs when there are lengthy execution deadlines, among other reasons, due to market practices or other restrictions on trading, or a Nod for short term liquidity that cannot be met by the sale of financial instruments.

### Interest rate risk

If the market interest rate rises, the value of certain investments will fall. This is especially the case for bonds. A rising interest rate can have a negative impact on shares because it increases the cost of investing. For bonds, an increase in interest rates causes a fall in the price of bonds. This is caused by investors demanding compensation for the higher interest rate. Given that the interest payments made on a bond are fixed for its lifetime when the bond is issued, this compensation can only be provided by lowering the price. The fixed interest payment provides a higher yield for the buyer of the bond when the purchase price is lower. Falling interest rates have the opposite effect: the price of your bonds will rise - assuming all other factors affecting the bond are equal.

### Reinvestment risk

This refers to the risk that you will not be able to reinvest the interest paid, the dividend issued, investments you have sold or other investment income on the same terms as the original investment.

### Fiscal risk

Fiscal risk appears where legislation is ambiguous or likely to change in respect of the fiscal aspects or tax treatment of financial instruments. For overseas financial products, fiscal agreements between governments can affect returns. And changes in your personal situation, such as a divorce or death can also mean a different tax treatment applies to your investments. Moreover, if you make profits outside of your professional activities from transactions or speculation outside the scope of normal management of private wealth, the increase in value in your portfolio may be subject to tax.

### Cyclical risk

This risk is linked to changes in the economic situation. Think of times of economic recession, of largescale social changes, or of dwindling worldwide commodity reserves. These changes have an impact on the price levels of financial instruments.

### Market risk

The market risk is the risk that the entire financial market or one category of assets will decline, meaning that the value of the assets in your portfolio may be affected. This kind of fluctuation can occur for a variety of reasons including currency movements or sharp rises or falls in interest rates and/or stock Exchange prices generally.

### Risk of bankruptcy

When you buy shares in a business, you as a shareholder are an owner of a part of that business. As a shareholder you need to be prepared to take risks. You can enjoy a share of the company's profits when things go well, but equally you will share in potential losses the company suffers if things go less well. You can lose the whole of your investment should the company fail.

### Risk of inflation

Inflation means an increase in the general level of prices, with the result that the (innate) value of money falls, the purchasing power of the money. Inflation brings with it the chance of a fall in the real value of your investment portfolio even if the (nominal) return continues to look respectable. To calculate the real situation, you need to adjust the value of your investments by a percentage for inflation.

### Geographic risks

A country or region can be economically or politically unstable, to the point where no currency is available or the entire payment system comes to a halt. In that case, an otherwise solvent overseas debtor, through no fault of his own, may be unable to meet his commitments. If financial products are issued in foreign currency, then as an investor you are also running the risk of receiving payments in currencies that are not convertible because of Exchange restrictions.

### Complexity risk

Under the implementation of the European Directive on Markets in Financial Instruments (MiFID) into Belgian law, Keytrade Bank differentiates between complex and non-complex financial instruments.

Shares and Funds listed on a regulated market<sup>1</sup> or on a market considered as equivalent to a regulated market<sup>2</sup>, ETFs listed on a regulated segment of Euronext, normal bonds, unlisted Funds with a European passport (UCITS funds) are regarded by Keytrade Bank as non-complex financial instruments.

Shares and Funds listed on an unregulated market, on a market considered as equivalent to an unregulated market (such as the OTCBB market) or on an MTF<sup>3</sup>, ETFs listed on MTF segments of Euronext and on markets other than Euronext, ETNs, ETCs, complex bonds, unlisted Funds without a European passport (non-UCITS funds), Turbos, Spinters, warrants, options, forex, futures, CFDs and structured products are regarded by Keytrade Bank as complex financial instruments.

Please note that Keytrade Bank is not required to assess on beforehand whether the non complex product is appropriate or suitable for you.

### Psychological risks

Although the outlook for a company may objectively appear to be good, rumours, opinions, trends or other feeling-driven factors can have a major influence on the share price. Due to irrational actions by other investors, but also your own actions.

### Risks from using IT systems

Every IT system has its own user interface, with specific terminology and methodology for executing financial transactions. So a certain term in a certain language in a certain system may mean something different to what it means in another language or system. If this results in incorrect orders being placed, that is especially annoying. You can reduce this risk by learning all about our user interface.

## 2 CHARACTERISTICS AND RISKS OF EACH FINANCIAL INSTRUMENT

In this chapter we describe the characteristics and risks of the most common financial instruments. General risks are shown in tables, specific risks are explained briefly.

### 2.1. SHARES AND SHARE CERTIFICATES

#### 2.1.1. DESCRIPTION

A **share** is a title of ownership that represents a part of the subscribed capital of a company. By purchasing a share you become an owner of a piece of the company. This means that the return on your investment will depend on the success (or failure) of the company.

If things go well, then you share in the rise in price and possibly in dividend payments. But if things go badly with the company, then the price will fall and you may receive less or no dividends. In the event of bankruptcy, the value of the shares may fall to zero.

*1 A regulated market is understood as a multilateral system, operated and/or managed by a market operator in the EEA, which handles or facilitates bringing together - on that market itself and according to its non-discretionary rules - multiple buyer and seller interests expressed by third parties for financial instruments, in a way that results in the conclusion of contracts concerning financial instruments accepted for trading in the context of its rules and/or its systems, and which is authorized and functions in due and proper form. Examples : regulated segments of Euronext, Equiduct.*

*2 A market located outside the EEA and for which there are frequent opportunities to dispose of, redeem, or otherwise realise financial instruments at prices that are publicly available to market participants and that are either market prices or prices made available, or validated, by valuation systems independent of the issuer are considered by Keytrade Bank as equivalent to a regulated market for the determination of the complex character of financial instruments. Examples : NASDAQ, NYSE.*

*3 A multilateral trading facility governed by the law of a member state of the European Economic Area, which brings together - within its own system and under non-discretionary rules - multiple third-party buying and selling interests for financial instruments and applies procedures that result in the conclusion of contracts. Examples : Alternext of Free Market segments of Euronext.*



The price of the shares depends on both internal and external factors:

- Internal factors: actual or expected company profits, news about the company and/or sector and the dividend policy, ...;

-External factors: include political events, macro-economic developments and irrational elements that can cause exaggerated stock Exchange swings.

As a shareholder you have the right, among other things, to vote at the annual general meeting (except in the case of non-voting shares) and to a part of the liquidation value of the business if the company is dissolved.

Shares may be registered by name, or dematerialised.

Registered shares are characterised by being included in the register of shareholders of a company, in the name of the shareholder. Transfer to third parties is carried out by an entry in the register recording the transfer of ownership. This type of transfer is relatively unusual.

Dematerialised shares are represented by an entry in a share account in the name of the shareholder at an institution recognised for this purpose.

You can easily sell electronic shares at any time any day. This is simpler for shares in exchange-listed companies.

**Share certificates** are securities which represent original shares and are managed by an administrative office. They track a share's value (price) and yield the same income as the underlying share (dividend).

The major difference between this and a share is that a certificate does not give the right to participate in the vote at a shareholders' meeting.

The risks are basically the same as the risks linked to the normal shares.

You can find share certificates in the shares section of the Transaction Site.

## 2.1.2. RISKS

### GENERAL RISKS

<b>Price risk</b>	Yes, depending on the volatility of the share. This is determined by both the company policy and the macro-economic, micro-economic and financial context.
<b>Exchange rate risk</b>	Yes, if the price of the share is not listed in Euro, or if the company's activities occur outside the euro zone.
<b>Credit risk</b>	No, shares are risk-bearing capital, and not debt claims. Naturally shares can lose some or all of their value in the event of bankruptcy.
<b>Liquidity risk</b>	Yes, depending on the volume of transactions in the share and of the free float <sup>4</sup> . The larger the market capitalisation of the company, the larger and more liquid the market for its shares will be.
<b>Interest rate risk</b>	Yes, depending on the shares and the investment climate. Usually an increase in interest rates has a negative impact on share prices.
<b>Reinvestment risk</b>	Yes
<b>Fiscal risk</b>	Yes
<b>Market risk</b>	Yes
<b>Risk of inflation</b>	Yes
<b>Geographic risks</b>	Yes
<b>Complexity risk (MiFID)</b>	Yes, if traded on an unregulated market or equivalent to an unregulated market or an MTF.

### SPECIFIC RISKS

#### Entrepreneurial risk

As you are a co-owner of a company, you run the same risks as any other entrepreneur: when times are bad you share in the losses; that can reach 100% in the event of bankruptcy.

#### Dividend risk

The dividend can be low or not be paid out at all if there is little profit or a loss. There are also companies whose policy is never to pay a dividend.

<sup>4</sup> The part (or percentage) of the share capital that is not in the hands of strategic investors, and therefore is traded freely is on the financial markets.

## 2.2. REAL ESTATE

### 2.2.1. REAL ESTATE CERTIFICATES

#### 2.2.1.1. Description

Real estate certificates are financial instruments that are issued by a company in order to finance the purchase or construction of commercial buildings or office buildings. The certificates may or may not be listed on an Exchange. As the holder of a certificate you hold a claim against the income from a real estate investment (income from rent for the building and potential capital gains on its sale). Without technically being the legal co-owner of the property, as the holder of a real estate certificate you are economically the co-owner.

When issued, real estate certificates normally have a lifetime of between 15 to 25 years. At the end of this term, the certificate is settled, not extended.

You can find real estate certificates under the stocks section of the Transaction Site.

#### 2.2.1.2. Risks

##### GENERAL RISKS

<b>Price risk</b>	Yes, depending on the trends in the property sector and the intrinsic aspects of the building (location, age, quality of tenants).
<b>Exchange rate risk</b>	No, given that property certificates are denominated in Euro.
<b>Credit risk</b>	Low, given that certificates are normally backed by a financial institution.
<b>Liquidity risk</b>	Yes, depending on the volume of the issue. Liquidity is normally restricted, due to the low market capitalisation.
<b>Interest rate risk</b>	Yes, property certificates are sensitive to interest rate movements. An increase in rates normally leads to a reduction in value of the certificate.
<b>Reinvestment risk</b>	Yes
<b>Fiscal risk</b>	Yes
<b>Market risk</b>	Yes
<b>Risk of inflation</b>	Yes
<b>Geographic risks</b>	No
<b>Complexity risk (MIFID)</b>	Yes, if listed on an unregulated market or equivalent to an unregulated market or an MTF.

##### SPECIFIC RISKS

###### **Risk of inadequate income and capital growth on the due date**

The income that is paid out is variable and depends, among other things, on the extent to which the building was rented and from rent indexation. Capital growth is uncertain and only known on the due date, when the building and/or land represented by the certificate is sold.

###### **Diversification risk**

Given that a property certificate relates to a specific property or a specific complex there is no spreading of risk.

### 2.2.2. SICAFI

From a legal point of view, the SICAFI is a fund or undertaking for collective investment (see 2.3). For a general description on SICAFs: see 2.3.3.2..

#### 2.2.2.1. Description

A SICAFI (standing for "Société d'Investissement à Capital Fixe") is an investment company with fixed capital whose objective is to invest in real estate. It is listed on the stock Exchange. The legislator has provided very strict rules that the SICAFI must follow with regard to diversification, limitation of debt ratio, distribution of income, etc.

By the end of 2014, the SICAFI will obtain the AIFM status (stands for «Alternative Investment Fund Managers»), driven by a EU Directive (called the «AIFM Directive») transposed into Belgian law by the Act of April 19, 2014 relating to the alternative collective investment undertakings and their managers. This statute imposes additional obligations on SICAFIs, such as the appointment of a custodian, performing regular stress tests with respect to risk management and liquidity...

Given these additional obligations, Belgian SICAFIs have decided to transform themselves into a public Regulated Real Estate Company. This new form of company was established by the Act of May 12, 2014 (see 2.2.3 Public Regulated Real Estate Company).

You can find SICAFIs under the stocks section of the Transaction Site.



## 2.2.2.2. Risks

### GENERAL RISKS

<b>Price risk</b>	Yes, depending on the trends in the property sector and the intrinsic quality of the portfolio.
<b>Exchange rate risk</b>	No, given that SICAFIs invest in Belgian and Luxembourg real estate.
<b>Credit risk</b>	Low
<b>Liquidity risk</b>	Yes, SICAFIs are listed. Therefore their liquidity depends from the secondary market where liquidity varies following the SICAFI.
<b>Interest rate risk</b>	Moderate. In principle, an increase in rates normally leads to a reduction in value of the SICAFI.
<b>Reinvestment risk</b>	Yes
<b>Fiscal risk</b>	Yes
<b>Market risk</b>	Yes
<b>Risk of inflation</b>	Yes
<b>Geographic risks</b>	No
<b>Complexity risk (MiFID)</b>	Yes, if listed on an unregulated market or equivalent to an unregulated market or an MTF.

### SPECIFIC RISKS

#### **Risk of inadequate income**

The payment of dividends may be interrupted due to major renovation costs or vacancy.

## 2.2.3. PUBLIC REGULATED REAL ESTATE COMPANY

### 2.2.3.1. Description

A public Regulated Real Estate Company (hereafter 'REC') is a listed company that conducts an activity that consists in holding on a long term real estate to make it available to users. The activity of the company is focused on the development and the daily management of real estate.

Its activity is therefore broader than the activity of a SICAFI that only invests in real estate (see 2.2.2). Contrary to the SICAFI, the REC is not a fund. The REC must nevertheless satisfy to most of the same obligations as the SICAFI (distribution obligation, limitation of the debt ratio, diversification of the real estate, ...).

You can find RECs under the stocks section of the Transaction Site.

### 2.2.3.2. Risks

The risks are the same as for investments in SICAFI (see 2.2.2).

## 2.3. FUNDS

### 2.3.1. GENERAL

**A fund or Undertaking for Collective Investment (UCI)**, is an investment undertaking that invests money from a number of different investors and places the total capital in a number of diversified financial instruments (such as shares, bonds, holdings in other UCIs or real estate), applying the risk diversification principle. UCIs are therefore a form of collective portfolio management.

#### **Legal classification**

From a legal point of view, the UCI may be set up by agreement - in which case we call it a **mutual fund** (see 2.3.2) - or by articles of association - in which case we speak of an **investment company** (see 2.3.3).

The shares held in a mutual fund are referred to as 'units'. Those held in an investment company are referred to as 'shares'.

#### **Additional classifications**

A UCI (both the mutual funds and the investment companies) always belong to one of the following categories:

Either they have a **variable** number of units (so called open UCIs or open-end funds). This type of UCI can increase its capital by issuing new units or shares and can reduce its capital by buying back existing ones. These UCIs may be Exchange **listed** (and are tradable in the same way as shares – see also the ETFs under 2.4) or **unlisted** (and have a net asset value that is calculated periodically, usually daily). This includes the Belgian and Luxembourg SICAV.

Or they have a **fixed** number of units (a so-called closed UCI or closed-end fund). These UCIs are always Exchange listed (the price of the units is determined by demand and supply). This includes the Belgian and Luxembourg SICAF.

Depending on the dividend policy, UCI units may be **income/distribution** shares or units (dividends are paid out to the owners of the holdings) or **accumulation/capitalisation** shares or units (dividends are capitalised).



### MiFID classification: «UCITS funds» vs “non-UCITS funds»

The bank regards UCITS funds as being non-complex financial instruments. Non-UCITS funds are treated as complex financial instruments.

UCITS stands for “Undertakings for Collective Investment in Transferable Securities”. This term refers to a European Union Directive that defines what criteria a fund based in the EU must meet to be able to be sold in all the EU countries (the so-called European passport). The aim of the directive is to simplify investment guidelines in Europe and to offer investors more protection.

## 2.3.2. MUTUAL FUND

A mutual fund is not a separate legal entity, but is set up by means of an agreement with joint ownership and is managed by a management company on behalf of the participants. This means that the mutual fund is fiscally transparent: the dividends and interest income received by the mutual fund is treated as if it were received directly by the final investor. It is not the mutual fund, but you the investor that owes tax on this income. Therefore you need to include this income in your tax return.

Mutual funds can be found under the funds section of the Transaction Site.

## 2.3.3. INVESTMENT COMPANY

### 2.3.3.1. SICAV

A SICAV is an investment company with variable capital and is a legal entity. As an investor, you become a shareholder in the SICAV and you receive a number of shares that reflect your relative investment. You can also join or leave a SICAV at any time: a SICAV can easily increase its capital at any time by issuing new shares (this happens when you want to invest or buy shares in a SICAV) or equally can reduce its capital by buying back existing shares (this happens when an investor sells his shares).

Each share is valued in relation to the SICAV's income. If these are income shares you receive the income, in the case of growth shares the income is reinvested in the company.

The SICAV can be divided into sub-funds that invest in different assets. From an economic point of view, each sub-fund is like a separate fund.

You can find SICAVs under the funds section of the Transaction Site.

### 2.3.3.2. SICAF

A SICAF is an investment company with fixed capital and, like a SICAV, is a legal entity. A SICAF differs from a SICAV in that its capital is basically fixed: it can only be increased or reduced under the same rules that apply to a normal company. The shares in a SICAF must be listed on a stock Exchange. Unlike SICAVs, the listed price for a SICAF may differ substantially from its intrinsic value. The price is determined only by the supply and demand on the stock Exchange.

SICAFs invest either in shares or in real estate. The latter are known as immovable SICAFs or SICAFIs (see 2.2.2).

You can find SICAFs under the stocks section of the Transaction Site.

## 2.3.4. RISKS

### GENERAL RISKS

<b>Price risk</b>	Yes, depending on the underlying investments and the diversification of the fund.
<b>Exchange rate risk</b>	Yes, if the underlying investments or the prices for the fund are not quoted in Euro.
<b>Credit risk</b>	Yes, particularly for bond funds.
<b>Liquidity risk</b>	Yes, particularly for SICAFIs that depend on a secondary market that has variable liquidity depending on the fund (for example property SICAFI).
<b>Interest rate risk</b>	Yes, especially for funds that invest in fixed income assets. But an increase in interest rates will have a negative impact on the share prices and so indirectly on those funds that invest in shares.
<b>Reinvestment risk</b>	Yes
<b>Fiscal risk</b>	Yes
<b>Market risk</b>	Yes
<b>Risk of inflation</b>	Yes
<b>Geographic risks</b>	Yes, depending on the fund
<b>Complexity risk (MiFID)</b>	Yes. (1) Unlisted funds: if no UCITS structure exists. (2) Listed funds: if traded on an unregulated market or equivalent to an unregulated market or an MTF.





## SPECIFIC RISKS

### Management risks

The return on a fund's investments depends among other things on the skill of the manager and the quality of his/her decisions. Poor judgements can lead to a reduction in value.

### Dividend risk

There are many different types of funds. One of the differences relates to whether or not they pay a dividend: growth funds do not pay out income, income funds do so. Whenever the results for an investment fund are poor, the manager of an income fund can decide not to pay out any dividend. And the direct reinvestment of dividends is not always what investors want.

### Price risk open-end and closed-end funds

The price risk with open-end funds is quite different to the price risk for closed-end funds. Open-end funds under normal market conditions are listed at or near the real value of the underlying investments. Because open-end funds can continually issue or buy back shares, you are subject to the price risk of the underlying investments. For closed-end funds this flexibility is not available and the number of shares issued is fixed. The price is therefore (also) determined by demand and supply for the fund. This price can deviate substantially from the underlying value of the fund.

### Risks of specific funds

Lees voor u gaat beleggen in een fonds eerst het prospectus, het document Essentiële Beleggersinformatie (Key Investor Information Document of 'KIID') en de Yesar-/halfYesarverslagen. In het prospectus en de KIID worden alle specifieke kenmerken en Risks beschreven, alsook de kosten verbonden aan het beheer van het fonds. Deze kosten hebben een impact op het rendement van uw belegging.

## 2.4. TRACKERS

### 2.4.1. DESCRIPTION

A tracker is a product listed on an exchange (**Exchange Traded Product** - ETP) that tracks the movements of a basket of assets. There are different types of trackers: Exchange index trackers, trackers of sectors, commodities, property, bond indices, .... They can be traded on any trading day, just like shares.

A tracker can take the following legal forms:

Trackers are usually structured like a fund, in which case they are referred to as **Exchange Traded Funds** (ETFs). These are open-end funds that follow an index as closely as possible (also known as passive ETFs<sup>5</sup>). ETFs are usually UCITS compliant. Like funds, ETFs can be set up in the form of an investment company or a mutual fund. For the general characteristics and risks of these funds, see chapter '2.3 Funds'.

A tracker can also be offered in the form of a debt claim. This is normally used for commodity trackers (such as energy, oil and metals). They are generally referred to as either Exchange **Traded Notes** (ETNs) or **Exchange Traded Commodities** (ETCs). ETCs track the price of either an individual commodity or broader commodities indices, without owning the assets. They are issued by banks or specialist issuers. If you buy an ETC, you will receive a debt claim that is similar to a bond. ETCs are backed by institutions with high credit ratings, but are not completely free of credit risk.

Within the trackers, Keytrade Bank makes a distinction between ETFs listed on a regulated segment of Euronext (considered as non-complex financial instruments), and ETFs listed on MTF segments of Euronext and other markets than Euronext, ETNs and ETCs (considered as complex financial instruments).

In this part we will only look more closely at 'passive' Exchange Traded Funds. Generally the risks for ETFs and ETNs are the same (see 2.4.2 below).

Given that by investing in an ETF you are investing in a basket of assets, this can involve less risk than investing in individual financial instruments. ETFs are the opposite of active managed funds, where the manager is constantly trying to select the best shares to get the highest possible yield. That is very cost and time intensive. Therefore the management costs are generally quite a bit lower for ETFs than for traditional funds.

For some ETFs you can multiply the performance of the index (leveraging) or track the reverse of the index movements (a so-called bear tracker), with or without leverage. This obviously involves more risks.

The price of an ETF is defined principally by the level of the underlying index. If the index rises, then value of the ETF will also rise. The price of the ETF does not have to be the same as the level of the index. This is because the accumulated dividends and the management costs applied are included in the calculation of the ETF's price. In addition, the buy and sell orders on the Exchange also determine the price. The more an ETF is traded, the smaller the spread between the bid and offer prices, and the closer the price will stay to the price of the index.

To achieve their investment goals, ETF issuers may use **physical** or **synthetic** replication of the relevant index.

Physical replication can be achieved by fully replicating the underlying index (the ETF invests in all the index constituents) or by using a process known as 'optimisation'. This is done when the underlying index consists of a very large number of constituents, or includes securities that are difficult to trade, or if multiple indices are being tracked. In this case, the ETF issuer will invest only in a basket of constituents that provides a representative sample in terms of risk and performance. So an ETF does not always include exactly the same financial instruments as the index that is being tracked.

<sup>5</sup> Besides the classic ETFs that follow an index as closely as possible, there are now also 'active' ETFs. These instruments are focused on performing better than the index. That is not a guarantee of a better performance. Some active managed ETFs perform better than the index, others perform worse. Per definition, active ETFs are not trackers.

An ETF can also be created by **synthetically** imitating the returns on the underlying index. The issuer of the ETF agrees one or more swaps<sup>6</sup> with one or more counterparties. The ETF issuer agrees to pay the swap issuer the returns on a pre-defined basket of securities, in Exchange for the return on the index. You then get paid out the return on the whole underlying index, but the actual investment might be made in quite different securities. This is called **synthetic replication**. This type of replication generally reduces the costs and the tracking error (deviation from the index), but increases the counterparty risk. For markets that are not easily accessible, swap structures are preferable to physical replication.

## 2.4.2. RISKS

### GENERAL RISKS

<b>Price risk</b>	Yes, depending mainly on the general trend of the stock Exchange and the underlying investments.
<b>Exchange rate risk</b>	Yes, if the underlying investments or the tracker price are not quoted in Euro.
<b>Credit risk</b>	Yes, especially for bond index trackers.
<b>Liquidity risk</b>	Yes, depending on the trading volume of the tracker and the liquidity of the underlying investments.
<b>Interest rate risk</b>	Yes, for bond index trackers, and indirectly for share index trackers.
<b>Reinvestment risk</b>	Yes
<b>Fiscal risk</b>	Yes
<b>Market risk</b>	Yes
<b>Risk of inflation</b>	Yes
<b>Geographic risks</b>	Yes, depending on the tracker.
<b>Complexity risk (MiFID)</b>	Yes, are complex: ETFs listed on the MTF segments of Euronext and other markets than Euronext, ETNs, ETCs.

### SPECIFIC RISKS LINKED TO ETFs

#### Deviation from the index ('tracking error')

Due to lack of liquidity or, for example, volatility, the price of the ETF can deviate from the index being tracked.

#### Counterparty risk

If the ETF can also buy derivatives or make agreements with other parties (swaps), then counterparty risk is created (especially for ETFs that use synthetic replication of an index). That is the risk that another party will not be able to meet his commitments. Think about the failure to return securities on loan. In the case of UCITS providing synthetic ETFs, the counterparty risk can be a maximum of 10% of the net asset value of the fund.

#### Specific risks related to ETNs

##### Credit risk and counterparty risk

Given that ETNs are debt instruments, there is the risk that the issuer does not meet his commitments as a counterparty. That is why it is important to know the credit rating of the issuing institution. Issuers are more and more offering ETNs with collateral to reduce the counterparty risk.

##### Liquidity risk

Certain ETNs have smaller trading volumes and so may be less liquid than ETFs.

## 2.5. BONDS

### 2.5.1. GENERAL

A bond is a negotiable security that represents a debt, issued by a national authority ('government bonds'), supranational institution ('supranational bonds') or company ('corporate bonds'). As a bondholder you have a certificate of participation in a long-term loan (> 1 year) for which you will normally receive regular interest payments (coupons).

A bond is always issued on the primary market. This is the market where new bonds are issued. You can only subscribe to a new bond issue during the subscription period.

The issue price may be at par (100%), or higher or lower to adjust the return to match market conditions. If you want to buy a bond after this period, then you have to go to the secondary market where these debts are freely traded. Their liquidity depends, among other things, on the size of the issue and on the issuer. The price of transactions depends on interest rate movements (the price is basically below the issue price if interest rates have risen since issue, and above it in the opposite case) and any changes in the solvency of the issuer since the time of issue.

On the final maturity date, the bond is repaid at the price fixed in advance, usual at par (100% of the face value). Some bonds can be redeemed earlier, usually at the issuer's instigation.

Based on the characteristics of bonds, Keytrade Bank differentiates between non-complex bonds (see 2.5.2) and complex bonds (see 2.5.3).

<sup>6</sup> A swap is an agreement between two parties where one party makes a payment on the basis of a defined percentage, that may be fixed or variable, while the other party makes a payment on the basis of the total yield of an underlying asset.

## 2.5.2. NORMAL (NON-COMPLEX) BONDS

The following bonds are considered to be non-complex: government bonds (treasury bonds, OLOs), supranational bonds, domestic corporate bonds in euro, Euro-bonds with a fixed rate and redemption price.

**Government bonds** are issued by the authorities and are used to finance their borrowing or plans. They have different maturities and offer fixed interest rates. In Belgium, government bonds and linear bonds (OLOs) are the best-known types. As a non-professional investor, you can purchase government bonds either on the primary market (when issued) or on the secondary market. But OLOs are intended for institutional investors. Therefore, non-professional investors cannot subscribe to these on the primary market. On the secondary market everyone who wants to can buy and sell OLOs.

Government bonds are guaranteed by the authorities. The credit risk for bonds issued by OECD member states<sup>7</sup> is generally very low (see credit ratings of these countries). On the secondary market, government bonds are totally liquid.

**Supranational bonds** are issued by international institutions such as the European Investment Bank and the World Bank. In terms of risk, they are comparable to the safest government bonds.

**Domestic corporate bonds in Euro** are fixed-interest bonds issued by private companies. The quality of the issuer is determined by the rating that they are given by specialised rating bureaus. These bureaus use a scale from AAA (top quality) to C (very weak)<sup>8</sup>.

Corporate bonds may be **subordinated**. This means that in the hierarchy of debtors they will be repaid only after normal debts and bonds, and just ahead of shareholders.

They usually have a rather higher yield than government bonds, because they incorporate a higher level of risk.

**Euro-bonds**, also called «**Eurobonds**», are bonds that are often issued in several European countries simultaneously. The issuers are often large international institutions, companies or sometimes public authorities. The «euro» prefix simply indicates that place of issue of the bonds (i.e. Europe) and not the nationality of the issuer or the currency of the issue. A Eurobond can therefore perfectly well be issued by a Japanese company in US dollars.

Eurobonds can be **subordinated**. This means that in the hierarchy of debtors they will be repaid only after normal debts and bonds, and just ahead of shareholders.

There are a number of categories of Eurobonds. Among the normal (non-complex) bonds are those with fixed rates and with zero coupons (**zero-coupon bonds**). Eurobonds with zero coupons do not pay any annual interest, instead they capitalise the interest until maturity. The issue price is the same as the face value, updated depending on the issue date and the defined interest.

Eurobonds with variable interest, without a fixed maturity and with other special characteristics are regarded as complex and are discussed in section 2.5.2.

### GENERAL RISKS

<b>Price risk</b>	Yes, when sold before maturity or if the financial situation of the issuer worsens.
<b>Exchange rate risk</b>	Yes, if not denominated in Euro.
<b>Credit risk</b>	Yes, depending on the quality (rating) of the issuer. Subordinated loans involve higher risks.
<b>Liquidity risk</b>	Yes, depending on the size of the issue, the transaction volume, the type of issuer and the currency.
<b>Interest rate risk</b>	Yes, depending on the remaining time to maturity. The longer the remaining time, the greater the chance of a rise in interest rates and a fall in the value of the bond.
<b>Reinvestment risk</b>	Yes
<b>Fiscal risk</b>	Yes
<b>Market risk</b>	Yes
<b>Risk of inflation</b>	Yes
<b>Geographic risks</b>	Yes
<b>Complexity risk (MiFID)</b>	No

### SPECIFIC RISKS

#### Insolvency risk

The issuing body may be temporarily or permanently insolvent and unable to pay the interest or redeem the loan. For example, due to a general downward trend in the economy, or political developments. If bonds are exchange listed, that can also have negative effects on their price movements.

This risk is as good as non-existent for government bonds from OECD countries (state guarantee), for bonds issued by supranational bodies, and normally for issues where the issuer has a quality rating (of at least investment grade, or a credit rating of at least BBB). In the case of non-investment grade bonds, the risk of insolvency by the debtor rises, and with it the risk of non-payment.

<sup>7</sup> OECD stands for the Organisation for Economic Cooperation and Development. This is an alliance of about 30 countries. The member states are mainly rich countries.

<sup>8</sup> Bonds with 'AAA' and 'AA' ratings (high creditworthiness), 'A' and 'BBB' (medium creditworthiness) are regarded as 'investment grade bonds'. Bonds with lower credit ratings ('BB', 'B', 'CCC', etc.) are regarded as bonds with low creditworthiness, also referred to as 'junk bonds'

### Risk of early redemption

In certain cases, the issuing body can move to early redemption of a loan. For example, if interest rates fall. This can have an adverse effect on yields

## 2.5.3. COMPLEX BONDS

Keytrade Bank regards the following bonds as being complex (MiFID): convertible bonds, reverse convertibles, Eurobonds with variable interest rates, perpetual bonds and bonds with other special characteristics. Keytrade Bank does not currently offer any complex bonds on the Transaction Site.

**Convertible bonds** are corporate bonds that you can swap at any time for a predetermined number of shares in the relevant company. You receive less interest in return for this option. On the other hand, price gains can push the yield above that of the original bond.

**Reverse convertibles** differ from normal convertible bonds in that only the issuing (financial) institution controls the conversion to shares. In Exchange for that right, you as the holder of the bond will again get a higher interest rate.

**Eurobonds with variable rates** (FRN – floating rate note) are bonds with variable interest rates. The rate is fixed at regular intervals for the next period (for example, every 6 months for the following 6-month period) using a reference interest rate on the international money market, plus a fixed mark-up (see 2.5.1 for a general description of Eurobonds).

**Perpetual bonds** are bonds with an endless lifetime, fixed coupons, with no redemption of the principal.

## GENERAL RISKS

<b>Price risk</b>	Yes. For convertible and reverse convertible bonds: including when sold before maturity or after conversion. For perpetuals: the price is sensitive to trends in the bond market due to the long maturity.
<b>Exchange rate risk</b>	Yes, if not denominated in Euro.
<b>Credit risk</b>	Yes, depending on the issuing body.
<b>Liquidity risk</b>	Yes, complex bonds are generally difficult to trade.
<b>Interest rate risk</b>	Yes. The interest rate risk for regular convertible bonds is limited because of the lower coupon. This risk is high for reverse convertibles, bonds with variable interest rates and perpetuals.
<b>Reinvestment risk</b>	Yes
<b>Fiscal risk</b>	Yes
<b>Market risk</b>	Yes
<b>Risk of inflation</b>	Yes
<b>Geographic risks</b>	Yes
<b>Complexity risk (MiFID)</b>	Yes

## SPECIFIC RISKS

### Credit risk

- Convertible bonds have a credit risk, just like regular bonds. In addition, convertible bonds are often subordinated to regular bonds which means there is a greater risk for convertible bonds.
- Reverse convertibles are usually issued by (financial) companies. As the holder of a reverse convertible, you have a credit risk relating to this (financial) institution. Because reverse convertibles are often subordinated to regular bonds, the credit risk on reverse convertibles is higher.

### Rate risk on underlying security

- For convertible bonds: if the price of the underlying security (the company) is no higher than the price that, under the terms of the convertible bond, you have to pay for new shares, then you do not have the obligation to purchase the new share issue and normally are repaid the principal of the bond.
- Normally the issuing (financial) company that issues a reverse convertible exercises its right to Exchange if the price is (sharply) lower than the price that you have to pay the company when it is exercised. Theoretically, the underlying security may not even be worth anything on the Exchange any longer. This risk is factored into the price of the reverse convertible. If you make a major loss on the underlying security, the reverse convertible will therefore be traded well below its face value.

### Risks for specific convertible bonds / reverse convertibles

Before buying a convertible bond or reverse convertible read the prospectus and ask for additional information from the issuing institution. The prospectus describes all the specific product characteristics and risks.

### Risk of early redemption - reinvestment risk

Bonds with variable rates or perpetual bonds can come with a call option. This allows the issuing body to carry out early redemption of the bond if they see an opportunity to raise financing at a better price. For example, if interest rates fall. This can have an adverse effect on the yield because the bondholder is then required to reinvest under less favourable market conditions.

## 2.6. DERIVATIVE FINANCIAL INSTRUMENTS

Derived financial instruments, or derivatives, are financial products whose value depends on the value of other products such as for example an index, shares, gold or currencies. Trading in derivatives can be of interest to experienced investors because of its leveraging effect: a price



increase or decrease in the underlying security gives rise to a much greater increase or decrease in value of the derivative. In addition, you can use derivatives to reduce risks and so protect your portfolio. Well-known derivatives are options, warrants, turbos and sprinters.

The derivative financial instruments are considered to be complex (MiFID).

Keytrade Bank distinguishes between derivatives where, in principle, the possible losses are limited to the invested capital (see 2.6.1), and derivatives which allow more than the invested capital to be lost (see 2.6.2).

## 2.6.1. DERIVATIVE FINANCIAL INSTRUMENTS WITH OPTIONS TO LIMIT THE RISK OF LOSS OF THE CAPITAL INVESTED

### 2.6.1.1. Long options

A long option is an Exchange listed financial instrument that gives you as the buyer (or holder) of the option contract the right to buy (call option) or sell (put option) an underlying security (such as a share, bond, currency, exchange index etc.) during a defined time period or at a specific point in time, for a predefined price (strike price).

To acquire this right – either a call or a put option – you pay a premium.

For each buyer of an option there is also a seller, the so-called writer. They are paid the premium by the buyer. As a writer you have an obligation (and not, like the buyer, a right) to buy the underlying security (for a put option) or to sell it (for a call option). For writing options, see 2.6.2.1. Short options.

You cannot exercise long options with Keytrade Bank. Either you sell the option contract before the strike date, or the contract is automatically exercised on the expiry date if the option is «in the money»<sup>9</sup>, or the contract expires with no value and the loss is limited to the amount of the premium paid. For more details you can see the relevant transaction rules at [www.keytradebank.be](http://www.keytradebank.be).

### GENERAL RISKS

<b>Price risk</b>	Yes, depending on the underlying asset, an option can lose its entire value.
<b>Exchange rate risk</b>	Yes, if not denominated in Euro
<b>Credit risk</b>	None, for transactions on a regulated market.
<b>Liquidity risk</b>	Yes,
<b>Interest rate risk</b>	Yes, depending on the term and structure of the option.
<b>Reinvestment risk</b>	Limited
<b>Fiscal risk</b>	Limited
<b>Market risk</b>	Yes
<b>Risk of inflation</b>	Limited
<b>Geographic risks</b>	Yes
<b>Complexity risk (MiFID)</b>	Yes

### SPECIFIC RISKS

#### Leverage risk

Because of the leveraging, trading options is much more risky than direct investment in the underlying security.

As the buyer of a call or put option you run the risk of losing all or part of the invested amount – the premium you paid. Your maximum loss is the option premium plus the transaction costs, unless it is exercised automatically on the expiry date when the losses can be greater than the premium amount.

### 2.6.1.2. Warrants

A warrant can be compared to an option (see 2.6.1.1).

It is an Exchanged listed financial instrument that confers the right to buy (call warrant) or to sell (put warrant) the underlying security (such as a share, bond, currency, Exchange index etc.) during a defined period for a predefined price (strike price).

The major difference to an option is that a warrant is not issued by the Exchange but by a financial institution. This also means that you can never 'write' a warrant.

If you do not take any action before the strike date of a warrant, then the warrant expires with no value.

<sup>9</sup> If the strike price is lower than the price of the underlying in the case of a call (higher than the price of the underlying in the case of a put).

## GENERAL RISKS

<b>Price risk</b>	Yes, depending on the underlying security, the warrant can lose its entire value.
<b>Exchange rate risk</b>	Yes, if not denominated in Euro.
<b>Credit risk</b>	None, for transactions on a regulated market (or equivalent). For OTC transactions, the risk depends on the creditworthiness of the counterparty.
<b>Liquidity risk</b>	Yes, thanks to the often small volumes traded on the secondary market.
<b>Interest rate risk</b>	Yes, depending on the duration and structure of the warrant.
<b>Reinvestment risk</b>	Yes
<b>Fiscal risk</b>	Limited
<b>Market risk</b>	Yes
<b>Risk of inflation</b>	Limited
<b>Geographic risks</b>	Yes
<b>Complexity risk (MiFID)</b>	Yes

## SPECIFIC RISKS

### Leverage risk

Because of the leveraging, trading warrants is much more risky than direct investment in the underlying security.

The specific risks of a warrant are comparable to those of buying options. That means that you can lose the whole of the invested amount (including transaction costs)

### Risks of specific warrants

Because warrants exist in so many different types, you must always study the prospectus carefully and investigate in detail the conditions of the product (for example, the expiry date and the last strike date) and the product risks. Ask for additional information from the issuing institution.

### 2.6.1.3. Turbos® and Sprinters®

Turbos and Sprinters are brand names for speculative Exchange listed investment products that all seek to make rapid profits from stock Exchange movements.

With **Turbo's and Sprinters**, thanks to leveraging, you can make quick profits from increases (e.g. Turbo long) or falls (e.g. Turbo short) in the value of underlying securities such as indices, shares, commodities, currencies and bonds. The purchase price of these products is just a fraction of that of the underlying security: the rest is financed by the issuing institution (this part is known as the financing level). The differences between these products are so minor that we will restrict ourselves to describing the Turbo.

In contrast to options (see 2.6.1.1), Turbos generally do not have an expiry date, but do have a stop loss level<sup>10</sup>. If the underlying security reaches or passes that level, the Turbo is automatically settled and any remaining value is paid out to the holder. The stop loss level is a mechanism that ensures that you can never lose more than the amount you invested. A Turbo long is closed out if the underlying security falls below the stop loss level. A Turbo short is closed out if the underlying security rises above the stop loss level.

#### Example 1 : Leverage effect

Underlying security = EUR 100; Financing level = EUR 75; your own contribution to the value of the Turbo in this case is EUR 25. The leveraging of the Turbo is 4; or  $100/(100-75) = 4$ .

Assume that the underlying security rises by EUR 10 (increases by 10%) to EUR 110. The value of the Turbo is then EUR 35 (that is, the difference between the price of the underlying security and the financing level). This means, therefore, that the value of the Turbo has risen by 40% (so your contribution of EUR 25 is now worth EUR 35).

This leveraging works in both directions. If the price of the underlying security falls by e.g. EUR 10 to EUR 90 (fall of 10%) then the value of the Turbo will also fall: EUR 90 - EUR 75 = EUR 15 (price of underlying security - financing level). In this case, the value of the Turbo falls from EUR 25 to EUR 15 or a fall of 40%. So the Turbo has fallen in value four times faster than the price of the underlying security.

#### Example 2 : Remaining value

Underlying security = EUR 100; Financing level = EUR 75. Assume the stop loss level is EUR 90. If the underlying security falls from EUR 100 to EUR 90 then the stop loss level is reached and the Turbo is closed out. If the settlement price is EUR 89.5 then the Turbo is still worth EUR 14 (EUR 89 - EUR 75). The remaining value that is paid back is EUR 14. If the settlement price is the same as or lower than the financing level, the remaining value is EUR 0 and you are not paid back any remaining value.

<sup>10</sup> There are also Closed-end Turbos with a fixed maturity date. They have a much higher leveraging effect.

## GENERAL RISKS

<b>Price risk</b>	Yes, depending on the underlying asset.
<b>Exchange rate risk</b>	Yes, if the underlying security is not denominated in Euro
<b>Credit risk</b>	Limited
<b>Liquidity risk</b>	Yes
<b>Interest rate risk</b>	Yes, depending on the term and structure of the Turbo.
<b>Reinvestment risk</b>	Yes
<b>Fiscal risk</b>	Limited
<b>Market risk</b>	Yes
<b>Risk of inflation</b>	Limited
<b>Geographic risks</b>	Yes
<b>Complexity risk (MiFID)</b>	Yes

## SPECIFIC RISKS OF TURBOS AND SPRINTERS.

### Settlement risk

Due to the leverage, an investment in turbos, sprinters, etc., incorporates considerably more risk than a direct investment in the underlying security. If the price of the underlying security reaches or passes the stop loss level, the turbo is automatically settled. The remaining value is then paid back to you. This may in fact be zero: in other words, you can lose the whole of your investment.

### Risks of specific turbos, sprinters, etc.

Because turbos, sprinters, etc. exist in so many different forms, you must always read the prospectus carefully and investigate in detail the conditions of the product and the product risks. Ask for additional information from the issuing institution.

### 2.6.1.4 Structured products

A structured product is a financial instrument that consists of one or more financial instruments whose repayment or yield depends, following a defined formula, on the movements of one or more underlying securities. At Keytrade Bank structured products also include the following financial instruments: Leverage & Short Certificates, Bonus and Capped Bonus Certificates, Capped and Floored Certificates, and Factors).

The underlying securities may consist solely of traditional financial instruments such as shares, Exchange indices, currencies, commodities or of a combination of conventional financial instruments and derivatives (such as options). Structured products have a fixed lifetime, and may or not guarantee a final level of capital (for example 90% or 100% of the investment).

## GENERAL RISKS

<b>Price risk</b>	Yes, among other things when selling before the maturity date and depending on the underlying assets.
<b>Exchange rate risk</b>	Yes, if not in euro.
<b>Credit risk</b>	Yes, depending on the issuing body.
<b>Liquidity risk</b>	Yes, given that a secondary market is organised to trade in these products.
<b>Interest rate risk</b>	Yes, depending on the composition of the structure (higher for structures with fixed interest assets).
<b>Reinvestment risk</b>	Yes
<b>Fiscal risk</b>	Yes
<b>Market risk</b>	Yes
<b>Risk of inflation</b>	Yes
<b>Geographic risks</b>	Yes
<b>Complexity risk (MiFID)</b>	Yes

## SPECIFIC RISKS

### Risk of early repayment

Under certain circumstances, the issuing body may decide to redeem the product early. For example, if interest rates fall. This can have an adverse effect on yields.

### Insolvency risk

The issuing institution or the guarantor of a structured product may be temporarily or permanently insolvent. That is also possible with a guarantee product. The risk exists here that the invested capital will not be paid back at all, or only in part.

### Risks of specific structured products

Because structured products exist in so many different forms, you must always read the prospectus carefully and investigate in detail the conditions of the product and the product risks. Ask for additional information from the issuing institution.

## 2.6.2. DERIVATIVE FINANCIAL INSTRUMENTS WITH THE RISK OF LOSSES GREATER THAN THE CAPITAL INVESTED

### 2.6.2.1. Short options

A short option is an Exchange listed financial instrument that commits you as the seller (or writer) of an option contract to supply (call option) or to buy (put option) an underlying security (such as a share, bond, currency, Exchange index etc.) during a defined period or at a specific point in time at a predefined price (strike price).

For each writer of an option there is a buyer or holder. They pay a premium to the writer. As the holder you have the right (and not, like the writer, an obligation) to sell the underlying security (for a put option) or to buy it (for a call option). For the purchase of options, see 2.6.1.1. Long options.

As the writer, you may be required at any time to supply or to buy the underlying security. You will in principle also be instructed by the counterparty if the option you have written is «in the money»<sup>11</sup> on the maturity date. This obligation expires if the counterparty does not exercise his right. You may be able to avoid the security allocation and the costs associated with it arising from your short position by buying back (buy 'closing') the short option. You must take into account that on the day of the closing buy you may still be instructed by the counterparty on the day of the closing buy. For more details, see the relevant transaction rules at [www.keytradebank.be](http://www.keytradebank.be).

### GENERAL RISKS

<b>Price risk</b>	Yes, for a written put option the maximum risk is the strike price of the option. For a written call option the risk is, in theory, unlimited.
<b>Exchange rate risk</b>	Yes, if not denominated in Euro.
<b>Credit risk</b>	None, for transactions on a regulated market or equivalent to a regulated market.
<b>Liquidity risk</b>	Yes
<b>Interest rate risk</b>	Yes, depending on the term and structure of the option.
<b>Reinvestment risk</b>	Limited
<b>Fiscal risk</b>	Limited
<b>Market risk</b>	Yes
<b>Risk of inflation</b>	Limited
<b>Geographic risks</b>	Yes
<b>Complexity risk (MiFID)</b>	Yes

### SPECIFIC RISKS

#### Leverage risk

Because of leveraging, trading options is much more risky than direct investment in the underlying security.

Did you write a call option on shares that you own (covered call)? In the event of a rise in the price of the underlying security you run the risk of an opportunity loss. This means that you will make little or no profit from a further rise in the price of the underlying security: you are still obliged to sell the shares at the strike price of the option, which is then lower than the market price of the underlying security. If the price of the underlying security falls the value of the shares in your portfolio will fall just as much. Your loss is partially offset by the premium you received when writing the call option. The risks are even greater if you have written a naked call option. In that case you do not own the underlying security. You may then be forced to buy the shares on the Exchange at a higher price, in order to supply them to the option holder at a (much) lower price. Your risk here in theory is unlimited, and you may be left with debts. You can limit a potential loss by closing your position in the meantime. Your maximum loss is then the difference between the premium received at the start, and the premium paid when closing, plus all the transaction costs.

As the writer of a put option, your maximum risk is the strike price of the option plus the transaction costs. The underlying securities may have become worthless while you may be required to buy them at a higher price. As for call options you write, you can limit your losses by closing your option position before you have to buy the underlying shares. Of course, to close your position you need to pay a premium and transaction costs.

When writing options there is the possibility that you will lose more than you have received and you may even be left with a debt.

#### Margin obligations

Writing options requires you to maintain a margin in your trading account. The margin serves to cover (some of) the commitments you are entering into (or have entered into). The margin is a certain amount of money or, in the case of writing a call option, possibly the underlying security if it is owned by you. Any price change of the underlying security can change the margin to be maintained.

#### Shortfall procedure

If at any time the commitments entered into by you are greater than the balance of your trading account the shortfall procedure will be

<sup>11</sup> If the strike price is lower than the price of the underlying in the case of a call (higher than the price of the underlying in the case of a put).



initiated. You are obliged to fulfil your margin obligation within five (5) Euronext trading days by transferring funds into your trading account, by selling investments (through a telephone order) or by closing option positions until the margin shortfall is cleared. If after five Euronext Brussels trading days your trading account still shows a shortfall, Keytrade Bank may close some or all of your open positions or arbitrarily sell some of the assets on your account to settle the shortfall. Keytrade Bank is also entitled to raise the level of the margin obligation.

## 2.6.2.2. Futures

A future is a standardised contract, listed on an organised or regulated market, where you sell or buy a commodity or financial product as the underlying security for a predefined price: delivery takes place later at a predefined date.

These contracts have a variety of characteristics: the underlying security can be a commodity (oil, gold, coffee, ...) or a financial product (interest rate, shares, Exchange indices, ...). The contract includes a volume (for commodities) or a quantity (financial products). They are listed in the form of percentages or by value. The value of the contract varies with nominal price fluctuation («tick»). The contract defines the time period and the type of settlement (by delivery of the underlying security or in cash). Keytrade Bank only offers the option of delivery of the underlying security as cash.

You must deposit a guarantee to cover the required initial margin. This margin is used to cover the potential risk that can arise from the transaction. An additional margin can be determined at intervals throughout the period of the contract, which is required from the investor. This additional margin represents the book value of the profit, or the book value of the loss resulting from changes in the value of the contract or of the underlying security. It can be many times the level of the initial margin. The way in which the additional margin is calculated during the lifetime of the contract or on settlement depends on the rules of the Exchange and the contractual details in each case.

Future contracts can be traded on our KeytradePro platform at [www.keytradebank.be/pro](http://www.keytradebank.be/pro). You can read more about this financial instrument on that website.

### GENERAL RISKS

<b>Price risk</b>	Yes, depending on the underlying security the future may lose all its value.
<b>Exchange rate risk</b>	Yes, may be high if currencies are volatile, but does not exist for contracts in euro.
<b>Credit risk</b>	No, on regulated markets a clearer will act as guarantor of correct processing. A clearer is a clearing office that acts as the counterparty for both buyer and seller.
<b>Liquidity risk</b>	Low, futures are easily traded on organised markets.
<b>Interest rate risk</b>	Yes, especially in the case of a bond future.
<b>Reinvestment risk</b>	Yes
<b>Fiscal risk</b>	Limited
<b>Market risk</b>	Yes
<b>Risk of inflation</b>	Yes
<b>Geographic risks</b>	Yes
<b>Complexity risk (MiFID)</b>	Yes

### SPECIFIC RISKS

#### **Risk of leveraging effects**

If the market does not move as you expected it to, the leveraging can work against you. Losses can be very high (in theory, unlimited).

#### **Risk of loss**

For a forward purchase, the loss is limited to the amount of the purchase if the underlying security falls. But, in the case of a naked forward sale, i.e. without having the underlying security in your portfolio, there is theoretically no limit to the potential losses: if the price of the sold naked underlying security rises sharply the losses can be very high because the seller has to buy the underlying security at a very high price in order to meet his commitments.

#### **Counterparty risk**

As the counterparty is unknown, there is always a risk that the counterparty will not meet their commitments.

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