

2. Risk Disclosure Statement

There is no investment without risk. Before engaging in any financial transaction, it is essential to understand the nature of risk involved, in order to avoid unpleasant surprises and to be able to realistically assess investment return expectations. This section presents the most common risks, both general and instrument-specific, that various types of investments are vulnerable to.

In this chapter, Nordea Bank S.A., Singapore Branch (the “Bank”) does not intend to describe all risks inherent in investments in financial instruments. Its objective is rather to give basic information and to caution Clients concerning the risks inherent in all investments in financial instruments. The Client should not enter into any investment transaction before being assured of his/her understanding of all the risks and having adapted his/her investments to his/her assets and needs.

Should Clients have any specific queries, or be interested in particular financial instruments, we recommend that they contact the Bank for further information.

This document does not deal with the tax or legal consequences pertaining to transactions in financial instruments. Therefore, the Bank recommends that Clients request tailor-made advice on these issues from specialists before making any investment.

2.1 Basic risks

These risks apply to any type of investment. However, depending on the relevant financial instrument, one or several of the risks described hereinbelow may apply cumulatively, thereby entailing an overall increase in the level of risk incurred by the investor.

2.1.1 Economic risk

Changes in the activity of a market economy always influence the prices of financial instruments. Prices fluctuate according to the rhythm of economic activity. The duration and scope of economic advances and declines are variable, as are their repercussions on the different sectors of the economy. In addition, economic cycles may vary depending on the countries concerned.

Failure to take these factors into account, as well as a mistaken analysis of the development of the economy when taking an investment decision, may lead to losses. The repercussions of the economic cycle on the evolution of the prices of investments should particularly be taken into account.

Depending, inter alia, on economic trends, the past performance of a financial instrument is no guarantee of the future performance of the same investment.

Therefore, investors must at all times ensure that their investments are appropriate in view of the economic situation and, if necessary, make the appropriate changes in their portfolio.

2.1.2 Risk of inflation

Inflation means that the purchasing power of money diminishes over time. Loss of purchasing power of money (i.e. the relative value of money in a certain currency compared with another currency) may have an influence on the actual value of the existing portfolio of the investor, as well as the actual yield that is realised through this portfolio. One should therefore take into account ac-

tual yields (e.g. real interest rates), i.e. the difference between the nominal interest rate and the inflation rate for fixed-rate investments, since, when the inflation rate exceeds the yield generated by the financial instruments (gains in capital and interest), this will lead to a loss in the value of the capital actually invested.

2.1.3 Government risk (country risk)

It may happen that an investor, although solvent, is unable to repay his/her loan and interest at expiration, or may even completely default on the loan, due to e.g. the unavailability of the foreign currency in question or to currency exchange controls triggered, for instance, by economic, political or social instability in the relevant country.

The ensuing unavailability of the foreign currency, or the imposition of currency exchange controls, may indeed lead to defaults on payments by investors. Concerning financial instruments issued in a foreign currency, the investor risks having to make loan repayments in a currency which turns out to be no longer convertible because of exchange controls. In principle, there are no means to shield oneself against such risks.

Moreover, even in the absence of any crisis, state intervention in some economic sectors (e.g. nationalisation) may have an influence on the value of investors' assets. In certain extreme cases, investors' assets can even be confiscated or frozen by local authorities, or their rights to these assets may be restricted in some way. As a matter of principle, there are no means to hedge against such risks. However, country ratings published in the financial press can be a useful guide for investors in this regard.

Finally, and more generally, instability in the political and/or economic and/or social situation of certain countries may lead to volatile price fluctuations.

2.1.4 Exchange rate risk

Exchange rates between currencies can change over time – sometimes rapidly – due to a wide range of economic, political and other factors, which will expose the Client to currency exchange risk and potential permanent loss whenever financial instruments are held in a foreign currency. Depending on prevailing exchange rates, the same investment may therefore generate profits or losses.

Hence, when the Client holds investments in a foreign currency, like the US Dollar, a devaluation or revaluation of the Singapore Dollar against the US Dollar exposes the Client to potential losses or gains.

Moreover, since the activities of companies are, to a greater or lesser extent, related to exchange rates, fluctuations in these rates are likely to have an impact on the price of the financial instruments issued by those companies.

Material elements affecting the exchange rate of a country's currency include the inflation rate of the country, the differential between domestic interest rates and foreign interest rates as well as between domestic and foreign productivity levels, the general assessment of the evolution of economic activity, the political situation in the world and the perceived relative safety of the investments.

Additionally, psychological events, such as internal political crises, may weaken the exchange rate of the domestic currency.

Loan or credit facilities offered to the Client by the Bank may also be exposed to exchange rate risks in case they are denominated (and therefore payable) in an alternate currency to that of the source(s) of repayment, i.e. of the Client's income and/or assets. Among the key risks facing the Client in such case is the possible devaluation of the currency used for repayment of the loan or credit facility.

In case the Client with income/assets in Singapore Dollars borrows certain amounts in US Dollars at a certain SGD/USD exchange rate and if on the repayment date the US Dollar has considerably appreciated against the Singapore Dollar, then the Singapore Dollar equivalent required to repay the loan or credit facility will no longer be the same as on the date of drawdown, but will have increased.

Furthermore, if the Client borrows in one currency and invests in assets denominated in a different currency, changes in exchange rate between the two currencies may result in a fall in the value of the assets. If the assets were used as collateral for the loan or credit facility, their collateral value may no longer be sufficient to cover the liabilities of the Client under the loan or credit facility and this might result in a demand from the Bank for the Client to provide additional assets as collateral.

Finally, the interest rate of the loan or credit facility will be based on the Bank's cost of funding in the interbank market for the relevant currency, which may fluctuate differently than the rate for the currency of the Client's income and/or assets and cause the relative interest cost of the loan or credit facility to rise.

Therefore, whilst all loan or credit facilities are subject to risk in the form of future interest rate developments, in the case of a foreign currency loan or credit facility, there is an additional risk associated with the development in the exchange rate of the chosen currency.

2.1.5 Liquidity risk

The possibility for an investor to sell financial instruments at any time at market prices is described as liquidity.

Insufficient liquidity in the market may prevent investors from selling their financial instruments at market prices. Fundamentally, a distinction has to be made between a lack of liquidity caused by market supply and demand, and a lack of liquidity due to the characteristics of financial instruments or market practices.

A lack of liquidity due to market supply and demand arises when the supply or the demand for one financial instrument at a certain price is non-existent or extremely low. Under those circumstances, purchase or sell orders may either not be carried out immediately, or not fully, or only under unfavour-

able conditions. In addition, higher transaction costs may apply.

A lack of liquidity due to the inherent characteristics of financial instruments or to market practices may occur, for example, because of: a lengthy transcription procedure for a transaction involving registered shares; long performance delays because of market practices or other limitations of commerce; a short-term liquidity need that cannot be covered quickly enough by the sale of the financial instruments; long lock-in periods that must expire before a transaction can be executed, in particular for alternative investment funds.

2.1.6 Psychological risk

Irrational factors (e.g. trends, opinions or rumours) may affect the overall performance of financial instruments on stock exchanges. They may cause important falls in prices even if the prospects of the companies are favourable.

Moreover, psychological events, such as a lack of trust in political leaders, could weaken the currency of a country, or the domestic securities traded there.

2.1.7 Credit risk

An investor who lends funds by purchasing a bond issue is exposed to credit risk. There are three types of credit risk: default risk; credit spread risk; downgrade risk.

Default risk is the risk that the issuer of a bond will fail to satisfy the terms of the obligation with respect to the timely payment of interest and principal. If a default occurs, this does not necessarily mean that the investor loses the entire amount invested. Normally, an investor can expect to recover a certain percentage of the investment.

Even in the absence of default, an investor experiences a loss on his/her securities if the market value of a bond declines, even though the market value of other bonds increases. This is called the credit spread risk and happens if the bond issuer's credit outlook worsens, or is perceived to worsen, compared with similar bonds.

Finally, credit-rating agencies (e.g. Moody's or Standard & Poor's) can lower the credit rating on the bond, which normally leads to an increase in the credit spread (see above). A credit rating is an indicator of the potential default risk associated with a particular bond issue or issuer. It is important to realise that the credit-rating agencies' evaluation of the debtor's creditworthiness need not concur with other parties' judgement of the debtor's creditworthiness.

2.1.8 Interest rate risk

Generally speaking, fluctuations in interest rates, whether short-term or long-term, may have substantial, adverse consequences on the prices of financial instruments.

2.1.9 Risk of insolvency of the issuer or of the clearing and settlement system

In case of the insolvency of the issuer of financial instruments, or of the clearing and settlement system on which those instruments are negotiated, an investor may lose part or all of the monies invested.

2.1.10 Additional risks in emerging markets

Emerging markets are the financial markets of those countries in which the percentage share of income per inhabitant is considered as average or low by the World Bank. More practically,

this concept encompasses markets established in countries that are characterised by a certain degree of political instability, or by relatively unpredictable financial markets and economic growth patterns, or by a financial market which is still at the development stage and represents a weak economy. This concept of emerging markets encompasses a large number of markets established in South America, Africa, Eastern Europe and certain Asian countries.

Generally speaking, in these markets, the risks identified above are enhanced. Indeed, political or economic changes (e.g. inflation, exchange rates) will have more influence on investment prices in emerging markets than in other countries. Likewise, emerging markets usually react more deeply and durably to natural disasters or wars.

Moreover, emerging markets often have less elaborate rules for the clearance and settlement of transactions than more developed markets, with the consequence that processing errors or a default in the delivery of instruments are more likely to occur. Finally, regulatory supervision of these markets, and investor protection rules, are often weak.

2.1.11 Additional risks related to credit-financed investments (“leverage”)

Credit-financed purchases of financial instruments contain additional risks. On the one hand, supplementary collateral may be required in case the evolution of prices leads to insufficient collateral for the credit. If the investor, as borrower, turns out to be unable to provide such collateral, the lender may be forced to sell deposited financial instruments at an unfavourable moment. On the other hand, the loss incurred due to an unfavourable evolution of the price of a financial instrument may exceed the initial investment amount. Fluctuations of prices of pledged financial instruments may influence the capacity to repay loans in a negative way.

The use of borrowed monies to finance the purchase of financial instruments is referred to as leverage and aims at increasing the potential return of an investment. The proceeds of a loan or other borrowings are reinvested with the intent of earning a greater rate of return than the cost of interest. Leverage involves the assumption of greater risk: if an investor uses leverage to make an investment and the investment moves against the investor, his/her loss is much greater than it would have been had the investment not been leveraged, as leverage can magnify gains or losses. Leverage can also be created through derivatives such as options, futures, margin and other financial instruments.

The investor needs to be aware that, as a consequence of the leverage factor accompanying the purchase of credit-financed financial instruments or derivatives, the sensitivity to price fluctuations of those investments will be proportionally more significant. As a consequence, the potential for gains increases, as does the risk of losses. Therefore, the risks of such purchases rise according to the importance of the leverage.

2.1.12 Other basic risks

2.1.12.1 Information risk

Information risk is the risk of poor investment decisions that arise from a lack of information, incomplete information or inaccurate information. This may be due, in turn, to the use by the investor of unreliable sources, the misinterpretation of originally accurate information by the latter, or communication errors.

2.1.12.2 Transmission risk

When placing an order, the investor must provide certain details necessary for its execution (financial instrument, type of order, volume, execution date, etc.). The more precise the order placed, the smaller the risk of transmission error.

2.1.12.3 Risks pertaining to transaction costs

The Bank, as well as other domestic or foreign parties (e.g. brokers), may be involved in the execution of an order, in which case the fees and commissions of these parties will be passed on to the investor.

An investment becomes profitable only when all these costs have been covered.

2.2 Specific investment risks for the investor’s consideration

2.2.1 Bonds

A bond is a certificate or evidence of a debt for which the issuer promises to pay the holders a specified amount of interest for a specified length of time, and to repay the loan at the maturity date. A bond may be in bearer or registered form. A bearer bond belongs simply to the holder of the relevant certificate; a registered bond is the property of an owner registered as such on the books of the issuer’s agent. The interest payments on bonds may be either fixed or variable. The duration of the loan, as well as the terms and conditions of its repayment, are determined in advance. The purchaser of a bond (the creditor) has a claim against the issuer (the debtor).

Certain structured products may take the form of a bond; these products will be described under the section “Specific risks associated with structured products”.

2.2.1.1 Characteristics

- **Yield:** the investment return, expressed in percentage terms, which is typically composed of periodic interest payments, if any, and possible increases in value (the difference between the purchase/issuance price and the sale/redemption price).
- **Maturity:** short-term (up to 5 years), medium-term (5-10 years) or long-term (more than 10 years).
- **Currency:** national currency of the investor or foreign currency; where repayment of capital and interest payments can be made in different currencies, an option can be acquired in order to limit the exchange rate risk.
- **Form:** individual documents with specific nominal values (which can be delivered to the investor) or collectively represented by a global certificate deposited with a custodian bank.
- **Issue price:** at par (100% of the nominal value); below par (the issue price is lower than the nominal value); above par (the issue price is higher than the nominal value).
- **Place of issuance:** the domestic market of the issuer or a foreign market.
- **Repayment:**
 - scheduled repayment - unless otherwise provided for, or unless the issuer becomes insolvent, the loans are repaid either at the maturity date, or through annual payments (generally after a lock-in period), or at different dates determined by drawing lots (generally after a lock-in period);
 - unscheduled repayment - the issuer may reserve the right to repay at a date it will determine, at its own discretion, at a later stage.

- Interest: depends on the terms and conditions of the loan; e.g. fixed interest (coupon) for the entire duration, or variable interest determined by reference to the Interbank rates of the appropriate financial market (e.g. LIBOR or EURIBOR); in this latter case, a minimum and/or maximum rate can be provided.
- Particular features (e.g. relations between the issuer and the investor): set out in the terms and conditions of the issue of the relevant bond.

2.2.1.2 Advantages

Depending on market conditions, these products may provide a higher return than other fixed-income products, such as time deposits.

2.2.1.3 Risks

2.2.1.3.1 Insolvency risk

The issuer risks becoming temporarily or permanently insolvent, resulting in its incapacity to pay interest or repay the loan. The solvency of an issuer may change depending on the general evolution of the economy, and/or in consequence of changes related to the issuer and/or the economic sector of the issuer, and/or political developments with economic consequences. This may be due in particular to the general evolution of the issuer, changes related to the issuer, the economic sector of the issuer and/or the relevant country, as well as political changes that engender substantial economic consequences.

This risk may be more (or less) significant, depending on whether the bonds are issued by a governmental body or a private institution, and is also related to the domicile of the issuing governmental body or the type or sector of activity of the private institution which has issued the bonds (credit institution, industrial company, etc.) as well as, more generally, the creditworthiness of the latter.

This risk is more limited if the bonds are collateralised. However, in such cases, the additional protection granted to the investor will have to be assessed on the basis of the status and creditworthiness of the guarantor.

From that point of view, it should be noted that, as a matter of principle, bonds issued by entities that are considered to be safe generally offer lower returns. However, the risk of total loss of the investment is correspondingly lower.

The deterioration of the issuer's cash flow logically influences the price of the relevant financial instruments.

2.2.1.3.2 Interest rate risk

Bond prices have an inverse relationship to bond yields: when bond yields rise, e.g. because of a general rise in market interest rates, bond prices will fall. The uncertainty concerning the evolution of market interest rates means that the purchaser of a fixed-rate financial instrument carries the risk of a decrease of the price of such financial instrument in case market interest rates rise. The longer the maturity of the loan, and the lower the interest rate, the higher the sensitivity of the bonds to a rise in market interest rates.

2.2.1.3.3 Early reimbursement risk

The issuer of a bond may include a provision allowing the premature reimbursement to the bondholder in case of a decrease in market rates. Thus, premature reimbursement may trigger modifications to the yields expected at the time of the issue or the purchase.

2.2.1.3.4 Risks specific to bonds redeemable by drawing lots

Loans that are redeemable by lot, and whose expiration is difficult to determine, may create unexpected changes to the yield of the bonds.

2.2.1.3.5 Risks related to the country of issue

If the bond is issued on a foreign market, it will in principle be governed by the law of the country of issue. The investor must thus inquire about the possible impact of the applicability of such foreign laws on his/her rights.

2.2.1.3.6 Risks to specific kinds of bonds

Some kinds of bonds (e.g. floating rate notes, reverse floating rate notes, zero-coupon bonds, foreign bonds, convertible bonds, indexed bonds, option bonds, subordinated bonds, etc.) are vulnerable to additional risks.

For these types of bonds, the investor should make inquiries about their risks by reference to the issuance prospectus and not purchase such financial instruments before understanding all the risks involved.

In the case of subordinated bonds, investors ought to enquire about the ranking of the bond compared with other bonds of the issuer. Indeed, in the case of an issuer's bankruptcy, these bonds will only be reimbursed after repayment of all higher-ranked creditors.

In the case of reverse convertible bonds, there is the risk that the investor will not be entirely reimbursed, but will receive only an amount equivalent to the underlying financial instruments at maturity.

2.2.1.3.7 Floating rate bonds

Floating rate bonds can take several forms, such as:

- floor floater bonds, which are variable-interest bonds that pay a minimum level of interest; in the event that the sum of the reference rate and the spread falls below this level, the investor will receive interest at least at the minimum rate determined in advance; conversely, for cap floater bonds, the rate of interest paid to the investor is limited to a maximum amount determined in advance; for these bonds, it is not possible to anticipate, as the time of issue, the actual yield of the investment, since the latter will vary according to the fluctuations of market rates;
- certain variable-interest bonds, for which it can be provided that the interest rate moves in the opposite direction to market rates (i.e. reverse floating rate bonds); for these medium- or long-term bonds, the interest rate payable to the investor is calculated according to the difference between a fixed rate of interest and a reference rate (e.g. 16% minus LIBOR); this means that the investor's interest income rises when the reference rate falls; the price of these bonds is usually subject to higher market fluctuations than fixed-rate bonds having the same maturity;
- convertible floating rate bonds, which give the investor or the issuer (depending on the terms and conditions of the bonds) the right to convert the note into a normal fixed-interest bond; if the issuer reserves this right, the actual yield of the bond may be lower than that contemplated by the investor.

2.2.1.3.8 Zero-coupon bonds

Zero-coupon bonds do not have interest coupons attached. Instead of periodic interest payments, the investor receives the difference between the redemption price and the issue price (in addition to the repayment of the principal amount).

Such bonds are usually issued at a discount to their nominal value, and redeemed on maturity at par. The size of the discount granted to the investor depends on the maturity of the bond, the issuer's creditworthiness and prevailing market interest rates.

Hence, such bonds offer investors a fixed lump-sum payment at a future date if the bond is held until maturity (which may have various tax implications depending on the countries concerned). However, if the bond is sold before maturity, the investor will only receive payment of the sale price of the bonds.

Therefore, if market interest rates decrease, the prices of these bonds fall more sharply than for other bonds with the same maturity and credit rating. Moreover, in case of foreign currency-denominated zero-coupon bonds, there is also an increased exchange rate risk because interest payments are not made on a regular basis over the life of the bond and there is only payment of a lump sum at a future date determined in advance.

2.2.1.3.9 Combined-interest bonds/step-up bonds

For combined-interest bonds, or step-up bonds, the investor does not receive interest payments at a single, fixed rate over the entire life of the bond. However, such bonds are similar to fixed-rate bonds in so far as the interest rate is determined in advance and does not depend on fluctuations in market rates. Instead, the rate of interest only changes during the term of the bond, following a pattern agreed at the time of issue.

Indeed, with combined-interest bonds, it is agreed that there will be no coupon for the first few years of the life of the bond; rather, an above-average coupon will be paid to the investor for the remaining years. These bonds are usually issued and redeemed at par.

With step-up bonds, a relatively low coupon is paid initially, and a very high one is paid to the investor during the following years. These bonds are usually issued and redeemed at par.

2.2.1.3.10 Phased interest rate bonds

These bonds are actually a hybrid of fixed- and variable-interest notes. They usually have a maturity of 10 years, and pay a fixed coupon for the first few years after issuance. Thereafter, over a period of several years, the investor will receive interest calculated on the basis of a variable interest rate that is in line with market rates. For the last years of the life of the bond, the bond reverts to paying a fixed rate of interest to the investor.

2.2.1.3.11 Index-linked bonds

For these bonds, the redemption amount and/or interest payments are determined on the basis of the level of an index, or of a managed account determined in advance - at redemption, or on the interest payment date - and are thus not fixed. These bonds are often zero-coupon bonds.

Such bonds are usually issued in two "tranches": bull bonds (bonds which appreciate in value if the index rises) and bear bonds (bonds which appreciate in value if the index falls). The investor runs the risk of price losses if the value of the index falls (bull bonds) or if the value of the index rises (bear bonds).

2.2.1.3.12 Subordinated bonds

For these bonds, investors should inquire about the ranking of such bonds compared with other bonds of the issuer, since, in the case of the issuer's bankruptcy, those bonds will only be reimbursed after repayment of all higher-ranked creditors (preferential and *pari passu* bonds).

However, in general, the better the position of the creditor in case of insolvency, the lower the return of the bond.

2.2.1.3.13 Convertible/warrant bonds

In this case, the investor is granted the right to exchange the bonds, at a specific time or within a specific period, for shares in the issuer at a ratio determined in advance. There is usually a minimum lock-in period, during which an investor cannot exercise his/her right of conversion. In case the right of conversion is not exercised, the bonds remain fixed-interest notes, repayable at par on maturity.

Because they offer a conversion right, such bonds usually offer a lower interest rate than ordinary bonds. The price of these bonds is essentially determined by the price of the underlying shares. Indeed, if the price of the shares drops, the price of the bonds falls as well, all other things being equal. Therefore, the risk of price losses is higher than for bonds without conversion rights (but usually lower than the risk of price losses associated with a direct investment in the relevant shares).

There are also bonds that give the investor the right to subscribe for shares, in addition to the bond and not as an alternative. This subscription right is certificated by a warrant that is detachable from the bond and can be traded separately. The shares in the issuer can be purchased by the investor on surrender of the warrant, on terms agreed in advance. The investor continues, in addition hereto, to hold the bond until maturity. As for bonds with conversion rights, the periodic interest payments are usually relatively low. Moreover, the price of such bonds, with the warrant attached, will equally track the price of the underlying shares. If the bonds are without the warrant attached, they amount to traditional bonds and, therefore, their price is mainly determined by market rates.

Certain special forms of the bonds described in the preceding paragraph give the holder of the warrant the right to buy or sell another bond determined in advance at a fixed price.

2.2.2 Bonus certificates

Bonus certificates represent certain rights as described in the terms and conditions of those bonds. In general, they come in the form of par-value debt instruments that entitle the holder to a part of the profit of the issuer.

In principle, a distinction should be made between bonus certificates with fixed or variable distribution and bonus certificates with option or conversion rights.

2.2.2.1 Absence of distribution or reduction of reimbursement risk

In case of losses by the issuer, interest payments may be halted if no minimal interest payment has been provided for. In addition, the repayment of the principal may be reduced.

2.2.2.1.1 Issuer risk

The bankruptcy of the issuer will consequently result in the complete loss of the invested funds.

2.3 Stock (shares)

A stock certificate represents the rights of the stockholder in a company. Stock may take bearer or registered form. One share of stock represents a fraction of the legal capital of a corporation.

2.3.1 Characteristics

- Yield: dividend payments and increase in value of the financial instrument are possible.
- Stockholder's rights: financial and ownership rights, as determined by the law and the articles of incorporation of the issuing company.
- Transferability: unless otherwise provided, the transfer of bearer shares does not require any formalities, as opposed to the transfer of registered shares, which is often subject to limitations.

2.3.2 Advantages

In principle, the investor has voting rights and shares in the profits of the company, and may equally obtain higher returns than for investments in term deposits or bonds.

2.3.3 Risk

2.3.3.1 Entrepreneurial risk

A share purchaser does not lend funds to the company, but makes a capital contribution and, as such, becomes a co-owner of the company. He/she participates in the development of the company as well as in the opportunities and risks related thereto, which may entail unexpected fluctuations in the value of such investment. Therefore, the precise yield of such investment cannot be easily forecast. An extreme situation would consist in the bankruptcy of the issuing company, which could result in the complete loss of the invested amount.

2.3.3.2 Price fluctuation risk

Stock prices may undergo unforeseeable price fluctuations that cause risks of losses. Increases and decreases of prices in the short, medium and long term alternate without it being possible to determine the duration of those cycles.

The general market risk must be distinguished from the specific risk attached to the company itself. Both risks, together or separately, influence the evolution of share prices.

2.3.3.3 Dividend risk

The dividend of a share mainly depends on the profit realised by the issuing company. Therefore, in case of low profits or even losses, it may happen that dividend payments are reduced or that no payments are made.

2.4 Investment funds

An investment fund is a company or an organised joint ownership that collects funds from a certain number of investors, and is engaged in reinvesting those funds according to the principle of risk spreading and to enable its shareholders or unitholders to benefit from the results of its asset management.

2.4.1 Characteristics

2.4.1.1 Open-ended funds

Capitalisation is not fixed, which means that the number of shares/units and participants is not determined; such funds may issue new shares/units or may redeem already issued shares/units; they are obliged to redeem shares/units at any time, at the prevailing redemption price and according to contractual provisions.

2.4.1.2 Closed-ended funds

The issue of shares/units is limited to a number determined in advance; as opposed to open-ended funds, redemption of shares/units is not mandatory; shares/units may only be traded to third parties or, as the case may be, on a stock exchange; the final price is determined in relation to the law of supply and demand, as for a traditional share; the price of shares/units depends on market supply and demand.

2.4.2 Advantages

The holder of shares/units receives part of the income of the fund. Theoretically, as a result of the diversification of the underlying investments made by the fund, the potential for profits increases and the risks of losses are limited. For the investments made by the fund, the latter usually benefits from better market conditions (in particular for costs) than the conditions which would apply to the investor should he/she have invested directly in the same investments.

2.4.3 Risks

2.4.3.1 Management risk

Since the yield of investment fund shares/units depends, among other factors, on the capacities of the managers and on the quality of their decisions, errors in the management of the fund may lead to losses or loss of profits.

2.4.3.2 Risk of a drop in share prices

Investment fund shares/units are exposed to the risk of a drop in their prices, reflecting the decrease in value of the financial instruments or currencies that compose the asset portfolio of the fund, all other things being equal. The higher the diversification of the fund, the lower the risk of losses. Conversely, risks are more important for more specialised and less diversified investments. It is therefore important to pay attention to the general and specific risks attached to financial instruments and currencies contained in the fund. The investor may usually obtain information about a fund by consulting the issue prospectus.

2.5 Derivatives

Derivatives are financial instruments, the values of which vary according to the value of an underlying asset, or assets; the underlying asset(s) may be a market index, an interest rate, a currency, the price of commodities or even another derivative. Concerning derivatives, a distinction must be made between:

- a) option transactions, which give the holder the right, but not the obligation, to enter into a transaction, whereby one party (the seller of the option) is irrevocably bound to honour his/her side of the bargain, if called upon to do so, while the other party (the purchaser of the option) is free to exercise the option or not;
- b) forward transactions, where the parties enter into a transaction which is to be settled at a specified date, and at a predetermined price, in the future; in a forward transaction, parties bind themselves irrevocably to settle the transaction as provided for at the specified date.

Transactions on such products trigger higher risks of losses and can even lead to the total loss of the funds invested. Since such transactions can lead to margin calls (account liquidation maintenance) over the life of the product, investors must ensure that they have sufficient liquid assets before entering into such transactions.

2.5.1 Option transactions

Options are derivative instruments whose value evolves proportionally to the evolution of the value of their underlying assets. The purchaser of an option receives, after having paid

a premium to the counterparty i.e. the seller of the option, the right to purchase (call) or to sell (put) the underlying asset at maturity, or during a certain period at a pre-determined price.

The characteristics of the option can be standardised or defined on a case-by-case basis between the purchaser and the seller.

2.5.1.1 Characteristics

2.5.1.1.1 Duration

The duration of the option starts from the day of the purchase until the day of the maturity of the option right.

2.5.1.1.2 Link between the option and the underlying asset

The link between the option and the underlying asset establishes the number of units of the underlying asset that the holder of the option has the right to purchase (call) or to sell (put) by exercising his/her option right.

2.5.1.1.3 Strike price

The strike price equals the price, agreed to earlier, at which the holder of the option may purchase or sell the underlying asset when he/she exercises his/her option.

2.5.1.1.4 Strike date

Options which can be exercised on any trading day up until the maturity date are called "American-style" options; options which can be exercised only on their maturity date are called "European-style" options; the latter can nonetheless be traded on the secondary market before their maturity, if the market is sufficiently liquid.

2.5.1.1.5 Conditions of exercise

The option can be settled physically, in which case the buyer of a call option can demand physical delivery of the underlying asset against payment of the strike price, or the buyer of a put option can deliver to the seller of the option the underlying asset against payment of the strike price by the seller; the option can also be settled "cash", in which case the difference between the strike price and the market value of the underlying asset is due, provided that the option is "in-the-money" (see below).

- Options "in-the-money", "out-of-the-money", "at-the-money": A call option is "in-the-money" if the market value of the underlying asset is higher than the strike price, and is "out-of-the-money" if the current market value of the underlying asset is lower than the strike price; a put option is "in-the-money" if the market value of the underlying asset is lower than the strike price, and is "out-of-the-money" if the current market value of the underlying asset is higher than the strike price; when the market value and the strike price are the same, the option is "at-the-money".

2.5.1.1.6 Price of the option

The price of an option depends on its intrinsic value and a variety of other factors such as the remaining life of the option (time value) and the volatility of the underlying asset; time value reflects the chance that the option will be "in-the-money" at some point before the expiration of the option and is therefore higher for long-duration options with a very volatile underlying asset.

2.5.1.1.7 Margin

Over the lifetime of an option, the seller must provide, as collateral, either the corresponding amount of the underlying asset or another form of collateral; the margin is determined by the Bank. Stock exchanges stipulate a minimum margin for listed options. If the margin cover provided by the investor proves to be insufficient, the Bank is entitled to request ad-

ditional collateral, sometimes at very short notice.

2.5.1.1.8 Form

- option certificates (warrants, listed options): the rights and obligations associated with the relevant option are securitised; they are sometimes listed on the stock exchange;
- traded options: these are standardised options for which the rights and obligations are not securitised and which are traded on certain specific stock exchanges;
- over-the-counter (OTC) options: these are options traded outside a stock exchange or agreed directly between the parties; their level of standardisation depends on market practices; they can also be tailor-made to meet investors' needs; this type of option is not listed and rarely takes the form of a certificate.

2.5.1.1.9 Leverage

Every change in the price of the underlying asset entails a change in the price of the option premium.

2.5.1.1.10 Purchase of a call or a put

The buyer of a call option speculates on a rise of the price of the underlying asset, which causes an increase of the option premium, whereas the buyer of a put option profits from a price drop of the underlying assets.

2.5.1.1.11 Sale of a call or a put

The seller of a call option anticipates price drops of the underlying asset, whereas the seller of a put profits from a rise of the value of the underlying asset.

2.5.1.2 Advantages

Over the lifetime of the option, the beneficiary of the option is granted the right to purchase or sell certain assets. The potential for profits is important due to the leverage effect linked to the use of an underlying asset. For the counterparty, such a transaction mainly permits an increase in the return on an existing position.

2.5.1.3 Risks

2.5.1.3.1 Price risk

Options may be traded at stock exchanges or over-the-counter. They follow the law of supply and demand. An important point for the determination of the price of an option consists, on the one hand, of the liquidity of the option's market and, on the other hand, of the real or expected evolution of the price of the underlying asset. A call option may lose value when the price of the underlying asset decreases, whereas the opposite is true for put options. The price of an option does not solely depend on the price variations of the underlying asset; other factors may come into play, such as the duration of the option, or the frequency and intensity of the changes of the value of the underlying asset. Consequently, falls in the option premium may occur even though the price of the underlying asset remains unchanged.

2.5.1.3.2 Leverage risk

Due to the leverage effect, price variations in the option premium are generally higher than the changes in the price of the underlying asset. Thus, the holder of an option may benefit from large gains but may also incur large losses. The risk attached to the purchase of an option increases with the degree of leverage.

2.5.1.3.3 Purchase of options risk

The purchase of an option represents a highly volatile investment.

The likelihood that an option reaches maturity without any value is relatively high. In this case, the investor loses the option premium as well as commissions paid for the purchase of the option. The investor has three choices: maintain the position until maturity, try to sell the option before maturity, or, for American-style options only, exercise the option before maturity.

The exercise of the option may either entail the payment in cash of the difference between the strike price and the market price, or the purchase or the delivery of the underlying asset. In case the option concerns a futures contract, its exercise causes the taking of a position in futures, which supposes the acceptance of certain obligations concerning financial instrument margins and the conclusion of futures contracts.

2.5.1.3.4 Sale of options risk

The sale of an option triggers, generally speaking, higher risk-taking than its purchase. Indeed, even if the price obtained for an option is fixed, the losses that the vendor incurs may be potentially unlimited.

If the market price of the underlying asset develops in an unfavourable way, the seller of the option will have to adapt his/her financial instrument margins in order to maintain his/her position.

If the sold option is American-style, settlement in cash, or the buying or delivering of the underlying assets, may be required from the seller at any moment until expiration. If the subject of the option is a futures contract, the seller will take a position in futures and will have to respect his/her obligations concerning financial instrument margins and the conclusion of futures contracts.

The seller's risk exposure may be reduced by holding a position in the underlying asset (financial instruments, index or other) corresponding to the sold option.

2.5.1.3.5 Purchase of the underlying asset in case of short sales

The seller of an "uncovered" call option does not have a corresponding quantity of the underlying asset at his/her disposal upon the conclusion of the contract (short sale).

In the case of options with physical settlement, the potential loss for the investor amounts to the difference between the strike price paid for the delivery of the underlying assets (in case the option right is exercised) and the price he/she will have to pay to acquire the relevant underlying asset. For options with cash settlement, the risk of loss for the investor amounts to the difference between the strike price and the market value of the underlying asset. Since the market value of the underlying asset can move well above the strike price when exercising the option, the risk of loss for the investor cannot be determined in advance and is, theoretically at least, unlimited.

This risk is more important for American-style options, which may be exercised at any time and thus at a highly unfavourable time for the seller of the option.

Another risk for the option seller is the potential inability of obtaining the requested underlying asset when the option is exercised, or the possibility of obtaining it only at very unfavourable conditions (in particular where costs are concerned) due to the situation prevailing in the markets.

In this context, it must be remembered that the potential loss can also be greater than the value of the margin cover provided by the investor.

2.5.1.3.6 Specific risks associated with options traded over-the-counter (OTC)

A position arising from the purchase or the sale of an OTC option can only be closed with the approval of the counterparty.

2.5.1.3.7 Specific risks associated with combined options

A combination consists of the conclusion of two or more option contracts based on the same underlying asset that differ in the option type or the characteristics of the option.

The number of possible combinations is significant. Therefore, the risks involved in any particular combination cannot be described in this document. Consequently, the investor must inquire about the specific risks associated with the intended combination.

It can nonetheless be noted that, for any combination, the cancellation, at a certain point, of one or more options, may result in substantial changes to the investor's risk position.

2.5.1.3.8 Specific risks associated with "exotic" options

These options are subject to additional conditions or agreements. Their payment structures cannot be obtained by using a combination of transactions. They can take the form of tailor-made OTC options or warrants. The range of exotic options is unlimited, so that it is impossible to describe the risks entailed by each "exotic" option in this document. However, the most common "exotic" options entail the following additional risks compared with normal options.

2.5.2 Options depending on the overall evolution of the underlying asset

It is not just on expiration or exercise date of the option that the market value of the underlying asset is important. The investor needs to take into account potential fluctuations in the market value of the underlying asset during the entire life of the option in order to assess potential gains or risks of losses.

2.5.2.1 Barrier options

The rights attached to such options arise (knock-in options) or expire (knock-out options) fully and irrevocably only when, during a period determined in advance, the market value of the underlying asset reaches a fixed threshold.

2.5.2.2 Payout options

Payout options grant a right to payment of a fixed amount, agreed in advance.

2.5.2.3 Digital option

Payment occurs only if, upon maturity, the market value of the underlying asset is above (digital call) or below (digital put) the strike price. In this case, if the option is "in-the-money", the seller of the option must pay the amount initially agreed upon.

2.5.2.4 Lock-in option

Payment occurs only if, during the life of the option or at a specified time period during its lifetime, the market value of the underlying asset reaches a threshold determined in advance. Indeed, when the fixed threshold is reached, the seller of the option must pay the amount initially agreed upon, irrespective of the subsequent evolution of the price of the underlying asset.

2.5.2.5 Lock-out options

The fixed payment only occurs if, during the entire life of the option or within a specified time period during its lifetime, the market value of the underlying asset never reaches a threshold or certain thresholds determined in advance. In such a case, whenever the fixed threshold or thresholds are reached, the option becomes invalid and thus loses its value, irrespective of the subsequent evolution of the price of the underlying asset.

2.5.2.6 Asian options

For these options, an average value is derived from the market value of the underlying asset over a specified time period. This average is used to fix the underlying asset's value which must be delivered (average-rate option), or the strike price which must be paid (average-strike option). The calculation of an average value for the underlying asset can result in:

- average-rate option - the value of the option on its maturity date being lower for the buyer and considerably higher for the seller than the difference between the strike price and the market value of the underlying asset at maturity;
- average-strike option - the strike price of a call option being higher than the price originally agreed upon, or the strike price of a put option being lower than the price originally agreed upon.

2.5.2.7 Lookback options

The market value of the underlying asset is recorded periodically over a specified time period.

For a strike lookback option, the lowest value (call option), or the highest value (put option), of the underlying asset becomes the strike price.

For a price lookback option, the strike price remains unchanged, but the highest value (call option), or the lowest value (put option) is used in calculating the value of the underlying asset.

Therefore, the risk is that the calculated strike price or calculated value of the underlying asset varies considerably from the prevailing market prices on the maturity date. Consequently, in the above-mentioned cases, the seller must be aware that, upon calculation or exercise of the right, the most unfavourable strike price or market value will be applied.

2.5.2.8 Contingent options

Buyers of such options must only pay the premium if the market value of the underlying asset reaches or exceeds the strike price during the life of the option (American-style option) or on the maturity date (European-style option).

The risk is thus to be compelled to pay the entire premium, even if the option is only just "in-the-money" or "at-the-money".

2.5.2.9 Cliquet and ladder options

2.5.2.9.1 Cliquet options

The strike price is periodically modified for a subsequent period - in general, at regular intervals - to bring it into line with the market value of the underlying asset; an intrinsic value, if applicable, is then calculated and accumulated over the lifetime of the option. In this case, the modifications take place periodically only when the underlying asset reaches specified market prices; normally, only the higher market value is taken into account.

On the maturity date, the seller of a cliquet option is required to pay all the accumulated lock-in market values, in addition to any intrinsic value of the option, and the seller of a ladder option must pay the highest lock-in market value. For the seller, the amount to be paid can thus be considerably higher than the option's intrinsic value on the maturity date.

2.5.3 Options on several underlying assets

2.5.3.1 Spread and outperformance options

Both types of options are based on two underlying assets.

With a spread option, the absolute difference in movement between the values of the two underlying assets forms the basis for calculating the option's value.

With an outperformance option, the relative difference, i.e. the percentage improvement of the value of one underlying asset over the other, is taken into account.

The risk is that, despite a positive performance of the market value of both underlying assets, the performance difference between the underlying assets may be equal or even lower, thus having an impact on the value of the option.

2.5.3.2 Compound options

The underlying assets of such options are themselves options. Such options can consequently be impacted by leverage, which may trigger important financial obligations.

2.5.4 Other forward transactions

Futures are contracts traded on a stock exchange. They are standardised as regards the quantity of the underlying asset and the expiration date of the transaction. Over-the-counter (OTC) or forward contracts are contracts that are not traded on a stock exchange and which may be standardised or individually negotiated between purchaser and seller.

2.5.4.1 Characteristics

2.5.4.1.1 Deposit of initial margin

Be it a future purchase or sale of an underlying asset, the initial margin is fixed at the moment the contract is concluded; this margin is generally determined with regard to each contract.

2.5.4.1.2 Variation margin

During the entire contract, a complementary variation margin is periodically determined and required from the investor. It represents the accounting benefit or loss, derived from the changes in the contractual price or the price of the underlying asset. The variation margin may far exceed the initial required margin. The computation method for the variation margin, be it for the duration of the contract or at liquidation, depends on the relevant stock exchange rules and on the specific contractual provisions, and the investor must immediately provide the Bank with variation margin upon request from the latter.

2.5.4.1.3 Liquidation

In general, the investor may, at any time for the duration of the contract, liquidate or undo his/her position before maturity of the agreement, either by selling the contract or by entering into an opposite contract. In this latter case, the provisions of the opposite contract will be such that the delivery and reception obligations arising from both contracts cancel one another out; the liquidation ends the positions incurred, and gains and losses accumulated until liquidation are realised.

2.5.4.1.4 Settlement

Contracts that have not been undone until settlement must

be honoured by the parties to them. Contracts having as an underlying asset a tangible property asset may be settled by the effective delivery of the asset. In specific cases, contracts can be honoured by delivery of cash compensation. Contracts where the underlying asset refers to base rates (except currencies) can not be settled by effective delivery of the underlying asset, but only by cash delivery. In case of an effective delivery of the asset, the contractual provisions need to be performed in full, whereas for cash settlement contracts, only the difference between the contract price and the market price at the time of delivery is payable. Therefore, investors need more available funds for contracts providing for the delivery of the underlying asset than for contracts providing for cash settlement.

2.5.4.2 Advantages

Potential gains are importantly dependant on the market value of the underlying asset upon maturity, especially because the principal amount originally invested is low. Such contracts may also be used to secure existing positions.

2.5.4.3 Risks

2.5.4.3.1 Changes in the value of the contract or the underlying asset

The investor incurs a risk if the evolution of the actual value of the contract, or of the underlying asset, is not in line with the evolution expected by the investor when concluding the contract.

Despite a rise in the price of the contract or the underlying asset, the forward seller will have to deliver the underlying asset at the initially agreed-upon price, which may be much lower than the current price. For the seller, the risk is equal to the difference between the price agreed upon in the contract and the market value at settlement date. As the market value may theoretically rise in an unlimited manner, the potential loss for the seller is unlimited, and may considerably exceed the required margins.

In case the value of the contract or the underlying asset decreases, the forward purchaser will still have to accept the asset at the price agreed upon in the contract, which can be potentially very much higher than the current market value. Therefore, the seller's risk consists in the difference between the price agreed upon in the contract and the market value at delivery. Thus, the maximum the purchaser may lose is the initially agreed-upon price. This loss may, however, by far exceed the required margins.

Transactions are regularly evaluated (mark-to-market). The investor will need to have sufficient margin cover constantly at his/her disposal. In case the margin becomes insufficient during the forward transaction, a variation margin will be required from the investor at very short notice. If the investor defaults, the transaction will be liquidated before due term and generally at a loss.

2.5.4.3.2 Difficult or impossible sales

In order to limit excessive price fluctuations, a stock exchange may fix limits for certain contracts. The investor has to keep in mind that it may be very difficult, if not momentarily impossible, in such cases to sell the contract. Thus, every investor should, before entering into a forward contract, make an inquiry concerning the existence of such limits. It will not always be possible (depending on the market and the terms and conditions of the transaction) to sell contracts at any moment in order to avoid, or to reduce, the risks of a current transaction. Stop-loss transactions, if they are possible, may only be performed during office hours.

They do not allow the limiting of losses to the indicated amount, but they will be executed once the limited amount is reached and they then become a "market order" (an order to perform such a transaction at the then current market price).

2.5.4.3.3 Acquisition of underlying assets in short sales

To sell an underlying asset without owning it at the conclusion of the contract (short sale), entails the risk that the seller will have to buy the underlying asset in an extremely unfavourable market, in order to be able, at settlement, to settle and to effectively deliver the underlying asset.

2.5.4.3.4 Specific risks for over-the-counter transactions

The market for standardised OTC transactions is, in general, liquid and transparent. Therefore, the selling of contracts can normally be effected. However, no market exists for non-standardised OTC transactions, and that is why liquidation is only possible with the agreement of the counterparty.

2.5.4.3.5 Specific risks associated with forward exchange products

A forward exchange transaction allows the selling or the purchase of a currency at a future date and at a price fixed when the contract is concluded. This type of investment eliminates exchange risk. Moreover, no premium has to be paid upon conclusion of the contract. The main risk for the investor is the loss of profit in the event that the evolution of market rates is more favourable than the evolution of exchange rates anticipated when concluding the contract.

2.5.4.3.6 Specific risks associated with combined transactions

The number of possible combinations is significant. Therefore, the risks involved by any particular combination cannot be described in this document. Consequently, the investor must inquire about the specific risks associated with the intended combination. It can nonetheless be noted that, generally speaking, the risks associated with such combined transactions may vary when elements of the combination are sold.

2.5.4.3.7 Specific risks associated with structured products

Structured products are synthetic investment instruments that have been specially created to meet specific needs that cannot be met by the standard financial instruments available in the markets. Structured products can be used as alternatives to direct investments, as part of the asset allocation process to reduce risk exposure of a portfolio or to utilise the current market trend. The investment in a structured product is linked to the performance of one or more market prices, rates, indices, securities and other financial instruments that introduce significant risk that will affect the performance of the investment.

A structured product is generally a pre-packaged investment strategy which is based on derivatives (e.g. options) but which typically features protection of principal if held to maturity. For example, a structured product can consist of a bond and an option: an investor invests EUR 100; the issuer simply invests EUR 80 in a risk-free bond which has sufficient interest to grow to 100 after the five-year period. With the remaining funds, the issuer purchases the option needed to perform whatever the investment strategy is.

In general, the aim of structured products is to reduce the risk that otherwise would exist for each individual component of the structured product. However, the risks involved by any particular combination of the elements of the structured product cannot be described in this document. Consequently, the investor must inquire about the specific risks associated with the intended combination.

2.6 “Alternative” investments and offshore funds

An “alternative investment” consists of an investment in domestic or foreign investment funds, the style of which is completely different from traditional investments in stocks and bonds, due to the type of investments made by the relevant fund. Hedge funds are the most usual form of alternative investments. Their investment style often includes short sales, leverage and derivatives. Hedge funds can freely choose the products and markets (including emerging markets) in which they invest, and their trading methods. Such funds usually set high minimum investment requirements for investors. The remuneration of the managers of these funds is often linked to the performance of said funds. Investments in private equity funds (venture capital, financing of acquisitions of companies) are also included in this category. The term “offshore” refers to investment funds located in offshore jurisdictions, e.g. the Bahamas, the Bermudas, the Cayman Islands, Panama or the Netherlands Antilles.

Each fund has its own risks and it is therefore not possible to describe in detail the risks associated with investments in such products in this document, but only to provide summary information. Consequently, the investor must inquire, on a case-by-case basis, before investing in such products, for instance by consulting the prospectus of the fund in question.

2.6.1 Advantages

The prospects of gains are usually attractive for the level of risk incurred (volatility risk).

2.6.2 Risks

2.6.2.1 Leverage risk

In this area, investment strategies may lead to high risks. For example, by using leverage, a slight change in the market may lead to meaningful gains or losses. In some situations, the entire investment may be lost.

2.6.2.2 Lack of information

The net asset value of such investment instruments is usually unknown at the time when the investor decides to invest or redeem his/her investment. This is due to the fact that, in principle, a notice period is necessary before such a transaction can be executed. Consequently, the net asset value can only be calculated once the investment has been made or redeemed. Very often, investors in alternative investments have little information at their disposal. The sometimes very complex strategies of these investment funds frequently lack transparency. Strategic changes that may lead to a significant increase of the risks often remain unclear or even completely underestimated by investors.

2.6.2.3 Potential lack of liquidity

Alternative investments may be more or less liquid. Sometimes, liquidity is very poor. Most of these investments are subject either to lock-in periods, or redemption penalties if investments are redeemable within a certain period of time. This is due to the relatively illiquid nature of the investments held by such vehicles, which tend to be constructed with a long-term investment view. Moreover, many of the investment techniques used in the alternative investment industry involve investments either in illiquid financial instruments, or in instruments that are subject to legal or other restrictions on transfer. Therefore, selling an alternative investment position may only be possible periodically, or on certain dates after a notice period of several weeks, or, for example, four times a

year on specific dates. Due to bid/ask spreads, the payment of sales proceeds may not amount to the net asset value of the instrument.

Thus, share redemptions for hedge funds will probably only be possible monthly, quarterly or annually. Concerning private equity funds, the lock-up period may last up to 10 years or more. Lastly, due to the complexity of the underlying investments made by these funds, adjustments in the net asset value may be necessary after receipt of the revised annual accounts. As a consequence, certain alternative investment funds block part of the shares of the investor, should the latter wish to sell 100% of his/her shares, until receipt of the revised annual accounts.

2.6.2.4 Minimal regulation

An important number of funds in this sector are located in offshore centres (offshore funds). Frequently, those offshore centres only impose minimal regulations on the funds. As a consequence, numerous problems or delays may appear during the carrying out of buy or sell orders for which the Bank cannot be held liable. The non-violation of the investor’s rights is not systematically guaranteed. The investor interested in alternative investments, notably offshore funds, needs to be conscious of such risks. Before proceeding, the actual investment products should be carefully examined.

2.6.2.5 Additional risks associated with private equity funds

Private equity investments typically carry the following additional risks.

2.6.2.5.1 No assurance of investor return

The risk for the investor is that he/she may not recoup the full invested amount, and may even lose it entirely. The past investment performance of these instruments is no guarantee of future investment performance, particularly as the nature of the investment environment is constantly changing (new geographic areas, new specialised areas, etc.). In particular, there is often strong competition to acquire portfolio companies during a cyclical upturn, whilst it may be difficult to withdraw from such investments during a cyclical downturn.

2.6.2.5.2 Low liquidity

These funds usually have a term of 7-15 years; there is no recognised secondary market in such private equity investments. As a result, the penalty of withdrawing from a private equity fund (which will usually require payments over a number of years) can be extreme, up to and including complete forfeiture of any rights to monies already invested in such an investment. As regards the monies that an investor commits to pay to the fund, the investor must pay particular attention to the notice periods, which are usually very short (possibly as short as seven days), and should make sure that he/she has sufficient liquid assets set aside to meet these calls for payments at short notice.