Raiffeisen BANK
Client inspired banking

Information on Investment Instruments, Risks and Client Categories

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1 General information

Transactions with investment instruments are associated with various risk factors that may influence the profitability or loss of any investment. Price or the results of the investment services depend on fluctuations in the financial markets outside the Bank's control and historical performances are no indicators for future performances. Investment risk can be described as the risk that the investor will fail to attain the expected return. A more detailed and extended notice of risks related to transactions with Investment Instruments and their mitigation methods is published at www.rb.cz.

2 General investment risks

- Every form of an investment is closely associated with risk. The higher the expected return, the higher the potential risk is.
- Term of the investment (investment horizon) influences the level of risk.
- Returns on Investment Instruments attained in past periods do not guarantee future returns.
- Overall risk of the portfolio can be mitigated by investing in different types of Investment Instruments.
- Trading with investment instruments using a credit, so-called margin trading, means increased risk. Interest fees for the credit reduce the total profit while use of the credit multiplies the yield, which may, in case of declining investment instruments, result in a major loss.
- The Client is fully responsible for proper taxation of revenue from Investment Instruments.

The Bank informs the Client about the basic types of risk associated with investments in Investment Instruments:

2.1 Market risk

Market risk is affected by fluctuating yield rates as a result of market fluctuations. Market prices of Investment Instruments may rise or decline in response to, for example, changed economic conditions, consumer preferences, interest rates. All Investment Instruments are exposed to market risk. Currency and interest rate risks are types of market risk.

2.2 Exchange rate risk

When investing in assets denominated in a foreign currency, the risk and possible return depend on overall development of the asset price and the exchange rate. Adverse development of the currency rate may have a negative impact on overall development of the investment despite positive development of the price of the Investment Instrument.

2.3 Interest rate risk

Interest rate risk affects fluctuations of the yield rate of Investment Instruments through a changing level of interest rates. These changes have an inverse effect on Investment Instruments, i.e. stocks and bonds respond to increased interest rates by declining prices (bonds also by increasing yield), while the stock and bond market responds to declining interest rates by growing prices.

2.4 Liquidity risk

In the case of investments in Investment Instruments (particularly instruments not traded on regulated markets or other market-unstable Investment Instruments), it must be taken into consideration that there is risk that the price will be adversely influenced by low liquidity or that the Client will be unable to sell or buy the given investment instrument at the desired moment.

2.5 Inflation risk

Inflation risk affects the real yield of Investment Instruments. High inflation may cause that the investor reaches a negative yield level.

2.6 Financial risk

Financial risk is associated with the use of debt capital in corporate financing. The bigger portion of assets financed by debt capital of the company, the bigger the company's financial risk is. Clients may hedge against risks when investing in Investment Instruments. The Client must be aware that the assumed risk should comply with the pre-selected strategy and defined financial objectives.

2.7 Issuer risk

Issuer risk stands for the risk that the issuer will be unable to fulfil its liabilities and make payments. In extreme cases, clients are exposed to the risk of losing the entire investment.

2.8 Industry risk

Industry risk means the risk of changing prices of Investment Instruments as part of an overall decline of the relevant industry.

2.9 Global risk

Global risk means the risk of changing prices of Investment Instruments as part of a global decline of state economies and capital markets.

2.10 Political risk

Political risk means the risk of changes in respect of the Investment Instruments as part of a changing political situation. Political changes may particular affect the price and transferability of securities and the issuer's standing.

2.11 Risk associated with margin trading

The client may lose more funds than originally deposited to the margin account. Declining prices of securities purchased on credit may require additional funds to be deposited with the trader in order to avoid forced sale of securities from the client's account. The trader may sell securities from the client's account without his or her consent. If own resources on the margin account fall below the liquidation margin level, the trader may sell securities from the margin account to cover the difference. The trader may sell securities from the client's account without being obliged to inform the client thereof in advance. Some investors think that they have to receive a margin call from the trader for it to be valid and that the trader cannot sell securities from their account to top up the maintenance cover without contacting them first. The trader usually tries to send the margin call, but is not obliged to send it.

The client is not entitled to postponement of the deadline for topping up the maintenance margin. The term during which the customer must comply with the maintenance margin requirements may be extended under certain conditions; however, the customer is not automatically entitled to such extension.

3 Investment instrument types

3.1 Mutual funds (units)

3.1.1 Description

Fund units are investment instruments representing the subscriber's share in the assets of a mutual fund. Other rights arising out of the law or the fund's statute are associated with the unit. The sum of values of units is the net worth of assets in the mutual fund. Mutual funds can be particularly created as open-end or closed-end funds. Subscribers in an open-end mutual fund have the right for redemption of the unit by the fund-creating investment management company. Mutual funds are broken down by the assets they invest in or by the risk of the market in focus of their investment policy:

i) money market funds
ii) bond funds
iii) mixed mutual funds
iv) equity funds
v) funds of funds, etc.

Mutual funds are managed by investment management companies. Please note that foreign mutual funds may have a legal structure that is different from local mutual funds.
Mutual funds also employ derivative instruments as part of their strategies; the extent of their use is stated in documents issued by the mutual fund, such as the statute.

3.1.2 Returns

Development of the value of a fund unit depends on the investment strategy laid down in the fund's statute and on the market development of the particular investment instruments held by the fund. Yield from units may be disbursed to the subscribers or reinvested in the fund. If a unit is issued by a closed-end mutual fund, it can only be traded on the capital market or sold to other persons interested in the investment. No legal guarantee applies to amounts invested in units or returns on such amounts.

3.1.3 Benefits

It is an investment instrument that is comprehensible for investors; however, investments must take into account the particular fund parameters stated in statutes and other documents issued by funds.

3.1.4 Selected types of mutual funds

3.1.4.1 Real estate mutual funds

Real estate funds are special funds owned by the investment firm that maintains and manages the special fund for the shareholders. Fund units stand for a contractual right to share in profits of the special fund. Real estate funds invest funds acquired from shareholders in line with the principle of diversification of risk, particularly in lands, real property, shares in companies engaged in real estates and similar holdings, and in own construction projects; also, they hold liquid financial investments (investments in liquid assets), such as securities and bank deposits. Liquid investments serve for settlement of payment obligations of the fund (such as under purchases of real property) and for redemption of fund units.

Returns

Total returns of real estate funds from the shareholder’s perspective consist of annual payment of dividends (if the fund distributes dividends instead of reinvesting) and the overall trend of calculated value of the fund. The returns cannot be determined in advance. Performance of a real estate fund

depends on the investment policy specified in the fund rules, market trends, particular real estates held by the fund and on other components of the fund (securities, cash at banks). Past performance of a real estate fund does not indicate its future performance.
Real estate funds are exposed to the risk of reduced returns also due to low occupancy of buildings. Particularly in the case of own construction projects of the funds there may be problems with the first lease. Low occupancy adversely affects the value of the real estate fund and leads to reduced payments of dividends. Investments in real estate funds may also lead to partial loss of the invested capital.
Further, real estate funds invest funds and cash on accounts in other forms of investments, particularly interest-bearing securities. Thus, this part of the fund's assets is exposed to specific risk affecting the selected form of the investment. Where real estate funds invest in foreign projects outside the Czech Republic, the shareholder is also exposed to the exchange rate risk as the market value and return on such foreign investments are converted to the Czech crowns when calculating the unit issue or redemption price.

Price risk
Units may be usually returned for the redemption value at any time. In the case of real estate funds, redemption of units may be subject to limitations. In exceptional cases, redemption may be temporarily suspended until the real estate fund's assets are sold and proceeds from such sale are acquired. Fund rules may stipulate that redemption may be suspended for up to two years in the event of a high number of returned units. In such case, the fund cannot pay out the redemption price during the term. Real estate funds are usually classified as long-term investment projects.

Benefits
Open-end real estate funds represent the simplest and most secure method of investments in real estates.

3.1.4.2 Exchange-traded mutual funds (ETF)
Exchange-traded funds (ETF) stand for shares in funds traded on the exchange market like stocks. ETFs are usually formed by a basket of securities (e.g. stocks) reflecting the composition of an index, i.e. it copies the unit index through securities forming the index and their current weight. ETFs are often called "index stock". ETF returns depend on prices of securities placed in the basket of securities. Thus, ETF risk depends on the risk of securities placed in the basket of securities.

Benefits
A simple and flexible way of investing in a diversified basket of stocks or other underlying assets.

3.1.5 Risk associated with investments in mutual funds

Price risk	Fund units can be usually sold at any time for the current redemption price to the investment firm issuing the units. In exceptional cases, redemption of units may be temporarily suspended. Some types of units can be traded on an exchange. Attainable selling prices of units may differ from prices attainable by means of redemption by the investment firm.
Exchange rate risk	There is no exchange rate risk only if the securities in the fund are denominated in the Czech crowns. If the securities are denominated in a foreign currency, there is low, average or high risk, however depending on movements of the securities' exchange rate vis-a-vis the Czech crown.
Liquidity risk	Liquidity risk is low given the opportunity to sell units back to the investment firm. However, there are certain exceptions, such as in the case of special funds.
Credit risk	Low. However, there is a risk of non-compliance with obligations under securities of

issuers forming the mutual funds.

3.2 Bonds (Debenture notes/Secured obligations)

3.2.1 Description

Bonds are investment instruments expressing the issuer's debtor obligation to the authorized bond holder. Thus, the bond holder is entitled to claim repayment of the nominal value by the issuer at maturity of the bond and payment of determined yield (interest) in given times. The rights and obligations of the bond issuer and bond holder (investor) are usually stipulated in the bond issue terms. The bond holder does not guarantee the company's obligations.

3.2.2 Returns

Returns on bonds may be set by means of a) fixed interest rate, b) variable interest rate, c) zero interest rate, where the return for the bond holder arises from the difference between a lower purchase price upon bond issue and higher selling nominal price paid at maturity, d) otherwise. Payment of the nominal value and returns on bonds is not legally guaranteed. By virtue of the law, banks and securities traders issuing bonds participate in a guarantee system that partially satisfies investments of bond holders when the issuers experience financial difficulties.

3.2.3 Benefits

Clear returns that are known in advance, particularly in the case of corporate bonds, where the returns are usually higher than returns on government bonds and money market instruments (usually due to compensation for existing corporate risk).

3.2.4 Certain special types of bonds

3.2.4.1 Mortgage bonds

Mortgage bonds are bonds issued by mortgage banks in order to raise funds to provide mortgage loans. The nominal value and the value of relative yield of mortgage bonds are fully covered by debts under mortgage loans. Receivables under mortgage loans not exceeding 70% of the price of pledged real estates may be used as proper cover of the nominal value of mortgage bonds. Only banks can issue mortgage bonds. The issuer of mortgage bonds ensures sufficient current cover of liabilities under mortgage bonds in a manner that the sum of liabilities under mortgage loans and total additional cover does not fall below the total amount of liabilities under all its issued mortgage bonds on the market.

3.2.4.2 Subordinated bonds

Subordinated bonds are bonds where it holds that if a) the issuer enters liquidation, b) resolution on the issuer's bankruptcy is issued, c) the foreign issuer is subject to another similar measure, the receivable under the bond will be only satisfied after satisfying all other receivables (except for similarly subordinated receivables).

3.2.5 Risk associated with investments in bonds

Credit risk There is always a risk that the debtor will be unable to fulfil its obligations in their entirety or in part. Thus, the investment decision must always consider the credibility and creditworthiness of the debtor. Certain issuers are given issuer or bond ratings by independent rating agencies, which serves as guidance for the investors.

Price risk The investor as the bond holder receives the redemption price stated in the bond terms at maturity of the bond. However, the issue terms and conditions may stipulate for possible early repayment of the bond by the issuer.

If the bond is sold before maturity, the investor obtains the current market value where the bond price is given by offer and demand for the bond and the current interest rate. For example, prices of securities subject to a fixed interest rate will decline with rising interest on bonds with a comparable maturity term. On the contrary, bonds gain value where the interest on bonds with a similar maturity term declines. Also, change in the issuer's credibility may affect the market price of the bond.

In the case of bonds subject to a variable interest rate, where the interest rate is indexed according to rates on the capital market, the risk of stagnant interest is much higher than in the case of bonds with an interest rate depending on money market rates.

The duration indicator describes the level of changes to the bond price in response to changing interest rates. Duration particularly depends on the time remaining to maturity of the bond. The longer the time to maturity, the higher the influence of changing general interest rates on the price is.

Liquidity risk Tradability of bonds depends on many aspects, such as the issue volume, bond nominal value, remaining time to maturity or conditions on the particular market. If the bonds cannot be sold, the bond holder is required to hold them to maturity.

Bond trading Bonds can be traded on regulated (such as exchange) or other markets. Where bonds are not admitted on a regulated or another market, the issuer must state in the issue terms and conditions whether the issuer is entitled or obliged to redeem bonds from the bond holder before their maturity and under what conditions the bonds may be transferred to a third party. If the bonds are traded on various markets, prices attained on the specific markets may differ.

3.3 Stocks

3.3.1 Description

Stocks are investment instruments associated with rights of the shareholder as a member to participate in the company's management, profits and liquidation proceeds upon dissolution of the company, all in accordance with the law and the company's articles of association. Shareholders are not entitled to require the company to redeem his or her shares. The shareholder does not guarantee the company's obligations. Stocks may be traded on non-regulated markets or on regulated markets (such as exchanges).

3.3.2 Returns

The yield from holding stock is the dividend and capital gain or loss from sale of the stock. The amount of dividends depends on a decision of the general meeting to distribute profits among shareholders. The amount of dividends is either expressed as an absolute amount per share or as percentage of the nominal value of shares. The yield obtained from dividends in relation to the share price is called dividend yield.

3.3.3 Risk associated with investments in stocks

Price risk Stocks can be traded on regulated markets (such as exchange) or other markets. Prices are usually determined every day based on offer and demand. If the investor acquires a share that cannot be traded on public markets, the investor must learn about transferability of the share to a third party from the statutory documents. On regulated markets, the stock price depends on economic development of the particular company, economic and political environment and many other rational or irrational aspects. In the case of bankruptcy of the issuer the investor suffers loss of

the invested capital, amounting up to 100% of the investment. If the stock is listed on multiple markets in different currencies, the investor must consider the exchange rate risk.

Credit risk The owner of the share is the company's shareholder and may suffer up to 100% loss of the investment in the case of the issuer's bankruptcy.

Liquidity risk In the case of stocks accepted for trading on multiple regulated markets or stocks with a narrow market, it may be difficult to transfer the stocks.

Exchange rate risk The risk does not exist where the stock is denominated in the Czech crowns. If the stock is denominated in a foreign currency, there is low, average or high risk, however depending on movements of the exchange rate vis-a-vis the Czech crown.

Stock trading in regulated markets In the case of trades on regulated markets, the shareholder must comply with the trading rules of the particular market (such as trading volumes, trading times, instruction types).

3.3.4 Benefits

Advantages of investments in stocks traded on regulated markets include potential high returns; however, there are significant risks that the high returns will be not attained.

3.4 Options

3.4.1 Description

The option buyer (holder) is entitled to buy (call option) or sell (put option) a certain underlying asset for a previously fixed price at any time during a given period (American option) or on the maturity date (European option). If the option buyer exercises his or her right, the seller (issuer) is obliged to buy or sell the underlying asset.

The price of the option is the option premium paid by the buyer to the seller as compensation for risk associated with issuing the option. The option premium amount is derived from the difference between the current market price of the underlying asset and the agreed price (intrinsic value). On exchange markets, the option premiums is created on the basis of offer and demand. The difference between the option premium and intrinsic value determines the time value of the option. The longer the time to maturity, the higher the time value of the option is. Acquisition of an option is also associated with transaction cost.

3.4.2 Returns

The exercise or strike price of the underlying asset is determined in advance when concluding the option. Thus, the option holder secures the future price of the asset. In the case of a call option, the holder attains yield if the agreed price of the underlying asset is higher than its price on the day of exercising the option. In the case of a put option, the price of the underlying asset on the exercise day must be lower than the agreed price in order to attain yield. If the difference between the previously agreed price and the current price is not favourable for the option holder, he or she may not exercise it. The option holder suffers loss up to the amount of the invested capital. Yield can be also attained through sale of the option itself. Where the price of the underlying asset on the market rises, the value of a call option rises too. In the case of a put option, its price increases with declining prices of the underlying asset.

3.4.3 Risk associated with investments in options

Price risk The amount of the option premium and consequent market value of the option are influenced by development of the price of the underlying asset. Increasing volatility of the price of the underlying asset increases the value of the option premium. Increased price volatility increases the likelihood of exercising the option and hence means a higher price of the same. On the other hand, the price of an option declines with shorter time to maturity. The option value changes every day. In the event of a change of the price of the underlying asset, options often respond by inadequately high fluctuation. This results in a leverage effect which, however, works both ways. The investment risk increases with the size of the leverage effect.

Exchange rate risk There is no risk if the option is in CZK. If investing in a currency option, the buyer is exposed to foreign exchange risk resulting from fluctuating exchange rates.

Interest rate risk The amount of interest rate risk of an option depends on maturity and structure of the option. Rising market interest rates have a positive effect on the value of the option premium of a call option. For put options, the effect is the opposite.

Liquidity risk Liquidity of an option increases with the issue size. The amount of risk is average to high for transactions on an exchange market subject to regulation. For over-the-counter transactions, the risk is average.

3.4.4 Benefits

The investment instrument's benefit is the opportunity for the holder to hedge against changing prices of the underlying asset. Also, the holder has an opportunity to realize a leverage effect upon successful sale. The seller realizes immediate revenue upon issue; however, this position generally brings increased risk. The amount of total loss for the seller is not limited and may exceed the value of the option premium.

Investments in options are recommended to experienced investors having sufficient knowledge of the instrument and having opportunities to monitor current market developments. The option buyer should be able to calculate how the price of the underlying asset may change so that the investment remains profitable after taking into account the amount of the premium and related transaction cost.

3.5 Warrants

3.5.1 Description

Warrants are close to options in terms of the valuation method and trading. Much alike with options, the warrant holder is entitled to buy or sell the underlying asset (stock, stock index, currency, commodity) for a pre-arranged strike price during the valid term of the warrant or at its maturity. The seller is obliged to sell or buy the underlying asset. In the case of warrants, real performance, i.e. purchase or sale of the underlying asset, does not take place. The seller only pays the difference between the strike price and the current price to the buyer. Compared to options, warrants are subject to certain limitations, particularly relating to the issuing opportunities. The price of a warrant is given by the size of the difference between the strike and current price (intrinsic value) and time to maturity of the warrant (time value). The time value of a warrant declines with shortening time to maturity. Warrants are traded on exchanges or on over-the-counter markets. Hence, their prices are also affected by investor offer and demand, movements of prices of the underlying assets and interest rate.

3.5.2 Returns

Yield from a warrant is given by the difference between the strike and current prices of the underlying asset. When evaluating the investment, it is also necessary to deduct the purchase price of the warrant and transaction cost. The buyer's loss may reach the amount of the invested capital, at maximum. The amount of loss for the seller is not limited in any manner. Investor's failure to exercise the right associated with the holding of a warrant leads to total loss of the investment. Warrants are attractive to investors due to the opportunity to realize a leverage effect. Even minor changes of the price of the underlying asset may cause a major change of the price of the warrant. As the leverage works both ways, it may lead to high yield as well as to loss of the invested capital in certain cases.

3.5.3 Risk associated with investments in warrants

Credit Risk Credit risk is given by credibility of the seller. If the seller of a warrant becomes insolvent and unable to fulfil its obligations, the investor is exposed to the risk of losing the entire capital invested.

Liquidity risk Warrants are usually issued in smaller issues which increases their liquidity risks. Liquidity is particularly given by the buying and selling listing of the company issuing the warrant.

Interest rate risk The amount of interest rate risk of a warrant depends on maturity and structure of the warrant. Rising market interest rates have a positive effect on the value of a call warrant. In the case of a put warrant, the effect on the value is the opposite. Fluctuating interest rates also have an indirect impact on the underlying asset.

Price risk Price risk is given by price volatility of the underlying asset. Movements of the price of the underlying asset is reflected in the value of the warrant by means of high fluctuations due to leverage. This may lead to high gains as well as high losses.

Exchange rate risk Exchange rate risk applies to investments in currency warrants. The warrant value depends on the exchange rate of the underlying asset's currency.

3.5.4 Benefits

Warrants are considered high-risk securities. With regard to decreasing time value of a warrant with approaching maturity, purchase of a warrant right before expiration is not recommended. Investments in warrants should be only made by investors who are able to identify and evaluate all their risks. The investor must realize that the higher the leverage of a warrant, the riskier the investment is. Similarly to options, the buyer knows his or her maximum loss. The amount of loss is not limited for the seller. Limited secondary market liquidity may cause fluctuating prices or issues with full realization of the order.

3.6 Structured products

3.6.1 Description

Structured products are investment instruments combining several financial products, of which at least one is usually a derivative. Generally speaking, derivatives are financial instruments of value derived from the value of the underlying asset (e.g. currency, commodity, stock, index). The value of derivatives is further affected by other factors, such as interest rates, maturity, and the volatility of the underlying asset.

Guaranteed funds combining a term deposit and an option may serve an example of a simple structured product. The deposit usually forms the guaranteed item and the option stands for the yield item. Guaranteed investment certificates consisting of a low-risk bond and an option may serve another example.

The bond "guarantees" return on the capital at maturity, while the option creates possible yield, i.e. participation in the underlying asset. In the event of a declining underlying asset, the option is not exercised and the investor thus obtains at least the guaranteed amount of the invested capital. Structured products may also be terminated prematurely or automatically if an agreed parameter occurs earlier. There are various Structured products on the market, differing in their structure or payout schemes as well as in the terminology used; thus, investors should thoroughly read the product terms and conditions of the particular securities before buying.

3.6.2 Risks

Generally speaking, structured products assume risks of the instruments they are composed of. Hence, structured products are designed for experienced investors. Prior to the acquisition of such an instrument, the investor should thoroughly read all the terms and conditions and learn about the scope of potential loss. Structured products involve virtually all types of risks associated with investments in investment instruments, although in some structured products, a portion of the risks is significantly reduced through a combination of multiple instruments.

Exchange rate risk If the investment instrument or its part is denominated in a foreign currency, return on the investment may be significantly affected in the case of a changing exchange rate, despite the development of the underlying asset is “as expected”, where the investor may realize gains as well as losses in relation to the exchange rate.

Interest rate risk Similarly to the currency risk, another variable affects returns on investment instruments depending on the developments on the investment market – the level of interest rates develops over time, and interest rate changes have an inverse effect - growing interest rates lead to declining stock and bond prices (and growing yield for bonds), while declining interest rates result in growing stocks and bonds.

Liquidity risk For the investor, liquidity risk means that the price of the investment instrument may be influenced by low liquidity and the client will be unable to buy or sell it at the desired moment. This risk particularly applies to low-volume investment instruments and trading outside a regulated market (OTC).

Issuer risk (credit risk) Securities are issued by the issuer. It may happen that for any reason the issuer will be unable to meet its obligations and pay out the yield or value of the securities. In extreme cases, investors are exposed to the risk of losing the entire investment. The risk can be significantly mitigated by choosing a trusted issuer with a higher rating and by trading on a regulated market.

Volatility risk Volatility risk depends on the derivative's underlying assets in a structured product; some types of derivatives, typically options, may completely lose their value, or lose their value in time (warrants). In addition, the value develops according to the market, typically on a daily basis.

Risk of the underlying asset If the payment of interest, dividends or principal is conditional on future development of the underlying asset or specific events (stock price, value of commodities, underlying indexes, etc.), payout may be reduced or suspended based on such development. In the context of the underlying asset, all associated risks must be taken into account, including interest rate risk, currency risk, issuer risk, industry, global or credit risk. These factors may affect the price of the instrument in the course of its valid term. In extreme cases, issuer risk, industry risk, global or credit risk may result in total loss due to limitations to the rights of secured creditors and the inability to separate and acquire the assets that are not part of the bankrupt's estate in the event of bankruptcy.

In addition, the investor must be aware of the tax risk.

Leverage risk If the structured product includes a derivative with leverage, both the potential yield and loss increase with this parameter and also change in time; for example, in the case of warrants, leverage increases with approaching maturity.

3.6.3 Selected types of structured products

3.6.3.1 Reverse convertible bonds

The principal difference of reverse convertible bonds from traditional ones is the issuer's opportunity to choose at maturity to repay the nominal value in cash or by a previously defined number of shares for an agreed price. The bond contains an option premium; thus, the instrument has higher potential yield over a relatively short period of time.

Risks

In the case of reverse convertible bonds there is a risk of loss of the value of the underlying stock or index as well as liquidity risk because of limited availability on the secondary market. In addition, the investor must consider market risk (exchange and interest rate risk) and issuer risk. The underlying asset is then associated with volatility risk.

3.6.3.2 Guaranteed and structured bond funds

3.6.3.3 Description

Guaranteed funds usually have a fixed maturity date and focus on attaining maximum returns specified in the fund prospectus. As at the maturity date, they guarantee the input capital or its part and additional interest in certain cases. Thus, the actual returns may be higher. On the other hand, the guarantee involves cost that is usually reflected in fees.

3.6.3.4 Risks

Guaranteed funds are associated with liquidity risk, exchange rate risk (despite the fact that guaranteed funds may be hedged against exchange rate risk to a certain level) and interest rate risk (increasing with time to maturity).

3.6.3.5 Investment certificates without leverage

Investment certificates are popular structured products as they represent an alternative to the purchase of bonds and stocks; the investor can choose from a wide range according to the underlying asset and risk profile. Investment certificates are usually linked to the development of particular stocks, stock baskets, stock indices, exchange rates and commodities and can deliver additional yield at times of growing, stagnating or declining markets. Settings of the particular product always matter - the terms and conditions are described in the prospectus of the particular certificate. From the legal perspective, certificates are debentures, where the certificate issuer undertakes to make a certain payment to the investor for the borrowed funds. In respect of stock certificates, the investor does not own the stock, but in some cases has the right to receive the dividend. Investment certificates are largely issued by renowned financial institutions and are traded with the issuer directly (primary market) or on the exchange (secondary market).

Basic categories of certificates

The basic types of investment certificates without leverage, according to risk, are **guaranteed certificates with capital protection** and **discount, express, index** and **participation certificates without capital protection, outperformance certificates** and **bonus certificates**.

Risks

Purchase of investment certificates involves issuer risk, resulting in total loss in extreme cases. Risk can be eliminated by choosing products on a regulated market from renowned issuers (with a high rating). Liquidity risk is closely associated with the issuer and valuation of the certificate, which is only limited by market regulation. Every certificate in a foreign currency is subject to variable currency risk. Also, the investor should pay attention to the risk of the underlying asset - in the event of extremely adverse development, the investor is fully exposed to market risk. In the case of investment certificates linked to commodities, the underlying assets are futures contracts; upon adverse development, the issuer may terminate the certificate early and pay out the market value.

3.6.3.6 Leverage investment certificates

Leverage investment certificates are high-risk investment products also known as turbo or knock-out certificates. The investor buys the certificate for a part of its value and finances the rest by a credit (margin trading). This creates leverage – for a smaller amount, the investor may multiply the profit or loss. In extreme cases, the investor loses the invested capital and also has to repay the credit. When choosing turbo certificates, the investor should focus, in addition to the basic parameters, to the following characteristics.

Basic parameters of leverage certificates

Subscription rate - how many certificates are required to acquire a unit of the underlying asset

Strike – price of the underlying asset; for growth certificates, the price is defined as the difference between the current price and strike; for certificates aimed at decline the current price is deducted from the strike.

Knock-out – price of the underlying asset where the certificate loses value. A growth turbo certificate becomes worthless at the moment when the underlying asset breaks the bottom barrier - i.e. the value reaches or falls below a defined level. For decline certificates it is the other way around - it loses value when the value of the underlying asset exceeds the upper barrier and market trend is against expectations.

Cap – maximum participation of the investor's yield in the underlying asset defined by the issuer; if the price exceeds the cap, the investor no longer participates in the growth in terms of yield. A cap is also related to a discount, which is the level of discount under a discounted certificate compared to direct investment in the underlying asset.

Gear – for certificates, it defines the level by which the certificate value rises/declines if the value of the underlying assets changes by 1%.

Risks

The risk associated with leverage certificates are the same as for certificates with no leverage. In addition, they bear the risk of leverage, as explained above - gain/loss does not grow linearly according the underlying asset, but exponentially. The investor should be prepared for potential high losses. Risk of breaking the knock-out barrier – if the underlying asset reaches a knock-out barrier before maturity, the certificate expires and loses value, or a previously defined residual value is paid out. The knock-out barrier can be also reached by mere one transaction realized for a price defined in the knock-out criteria.

3.7 Swaps

3.7.1 Description

Swap is a contract of two or more parties to exchange future periodical payments from a underlying asset over a defined period. Most swaps are characteristic of being over-the-counter derivatives as they are customized for both parties. The most frequent swaps are interest rate swaps, currency swaps and cross currency swaps (contract to exchange the principal of two currencies and the associated interest cost).

3.7.2 Returns

Returns are given by the difference between the fixed and current value of the underlying asset/exchange rate/interest rate etc. For example, in an interest rate swap, the buyer (payer of fixed interest) profits from rising interest rates. On the contrary, the seller of an interest rate swap (recipient of fixed interest) profits from the contract with declining interest rates. The yield cannot be determined in advance.

3.7.3 Risks

Credit Risk Credit risk of a swap consists of the risk of the partner's insolvency, i.e. possible temporary or permanent incapacity to perform obligations under the swap and the resulting necessity to cover the transaction on the market. This may be unfavourable in some cases.

Interest rate risk In the case of interest rate swaps (IRS), interest rate risk consists of uncertainty of future changes to market interest rates.

Exchange rate risk In the case of currency swaps, exchange rate risk consists of uncertainty of future changes to foreign exchange rates.

Transfer risk Opportunities for transfers of the particular currencies may be restricted as a result of foreign exchange control of the state issuing the currency in question, which may jeopardize realization of the transaction.

3.7.4 Benefits

Swaps serve investors to manage risk as well as to speculate or reduce transactions cost. The counterparties provide each other with better terms given the conditions of their local markets. The investor must consider the amount of possible loss that cannot be specified in advance and is not limited in any manner.

3.8 Forward contracts

3.8.1 Description

A forward contract is an over-the-counter contract of two or more parties, under which they undertake to buy or sell an underlying asset on predefined terms at a given time in the future.

3.8.2 Returns

The yield is given by the difference of the price agreed in the contract and the spot price of the underlying asset. The buyer profits where the spot price is less favourable than the strike price. Potential loss is not limited.

3.8.3 Risks

Price risk Price risk of a forward contract consists of the risk that the underlying asset will be available for purchase at the forward contract realization date for a better price than agreed in the contract. The risk size depends on volatility of the underlying asset price.

Credit Risk Credit risk of a forward contract consists of the risk of the partner's insolvency, i.e. possible temporary or permanent incapacity to perform obligations under the forward contract and the resulting necessity to cover the transaction on the market, which may be unfavourable at the given moment.

Interest rate risk In the case of interest rate forward contracts, interest rate risk consists of uncertainty of future changes to market interest rates.

Exchange rate risk In the case of currency forward contracts, exchange rate risk consists of uncertainty of future changes to foreign exchange rates.

Liquidity risk Liquidity risk is given by the degree of individualization of the contract terms. The more the contract is customized for a counterparty, the lower liquidity of the instrument is.

3.8.4 Benefits

Forward contracts serve investors to manage risk as well as to speculate or reduce transactions cost. The investor must realize that the yield cannot be specified in advance and that the potential loss may be unlimited. As it is an over-the-counter transaction, the contracting parties may agree on specific transaction terms. Also, it is necessary to keep in mind that liquidity of the instrument is limited.

3.9 Money market instruments

3.9.1 Description

Investment instruments of the money market include, for example, **deposit certificates, bonds, short-term securities issued by corporations**, etc. Their common characteristic is the short-term investment horizon. The investment can be carried out either directly or through money market funds.

Money market funds offer various investment strategies and enable investments of available funds on both local and foreign markets.

3.9.2 Returns

The investment strategy is always defined in the securities prospectus. Investors investing through money market funds may reach for more favourable terms and thus also higher returns as money market funds accumulate large volumes of money. Returns usually exceed the interest rate offered by banks on savings accounts or term deposits.

3.9.3 Risks

Credit Risk Credit risk is given by the fund's investment strategies and its managers. In the case of direct investment in securities it derives from credibility of the issuer.

Liquidity risk For money market instruments there are no organized secondary markets; hence, there is no certainty regarding easy sale of the instrument unless the issuer guarantees to pay the invested capital at any time and is credible enough to comply with its obligation.

In the case of investments through money funds, the investment is a very liquid one.

Exchange rate risk In the case of investment instruments denominated in the local currency, the exchange rate risk is zero. The risk of investment in securities in a foreign currency derives from volatility of the foreign exchange rates.

Interest rate risk Moving interest rates affect the net value of assets.

3.9.4 Benefits

It is a relatively safe form of investments. Investments in these instruments are advisable for conservative investors and investors seeking a shorter investment horizon.
In the case of investments through money funds, we advise to pay attention to the regulations under which the particular money market fund is formed. Money market funds may be established in accordance with Czech or foreign laws. Investments through money market funds also allows individual investors to invest in instruments that are otherwise difficult to access. On the other hand, investments in this manner are usually associated with higher fees.

3.10 Categorisation of clients

3.10.1 Bank's obligation to perform categorisation of clients

In accordance with relevant regulations, the Bank is required to categorize all its clients, to whomit provides investment services, and to inform them about such categorisation. Three categories of clients are recognized pursuant to legislation, namely:

- retail, non-professional client
- professional client and
- eligible counterparty (professional client)

To place a client into a category, the Bank relies on available information about the client.

3.10.2 Legal definition of client categories

Retail clients are clients not identified as professional clients.

Professional client
Clients are placed in this category if they are any of the following entities:

1. entities required to be authorized and/or supervised by the competent regulatory authority to act on the financial market, namely:
a) credit institutions;
b) investment firms;
c) other authorised or regulated financial institutions;
d) insurance companies;
e) collective investment schemes and management companies of such schemes;
f) pension funds and management companies of such funds;
g) pension insurance company;
h) commodity and commodity derivatives dealers;
i) locals;
j) other institutional investors whose core business activity is not covered by subparagraphs a) to h), and who must be authorized or supervised to allow them to participate in the financial market;
2. large undertakings meeting two of the following size requirements on a company basis:
- balance sheet total : EUR 20 000 000;
- net turnover : EUR 40 000 000;
- own funds : EUR 2 000 000;

3. national and regional governments, public bodies that manage public debt at national or regional level, Central Banks, international and supranational institutions such as the World Bank, the IMF, the ECB, the EIB and other similar international organisations;

4. other institutional investors whose main activity is to invest in financial instruments, including entities dedicated to the securitisation of assets or other financing transactions.

Also, a professional client also means a person who requests the Bank to be treated as a professional customer, the Bank agrees with such request on terms stipulated by law, and the person satisfies at least 2 of the following 3 criteria: 1. has carried out an average of 10 transactions of significant volume within each quarter, over the past year, on the relevant market for him/her (the market on which the financial instruments for which the client wishes to obtain professional investor status are traded); 2. the volume of its assets formed by cash and investment instruments corresponds to at least EUR 500,000; 3. the person works or has worked in the financial sector for at least one year in professional jobs that require knowledge of transactions or services for which professional investor status is sought.

An eligible counterparty is

An eligible counterparty is one of the below indicated types of professional clients:
- investment firms,
- credit institutions,
- insurance companies,
- UCITS and their management companies,
- pension funds and their management companies,
- other financial institutions authorised or regulated under Union law or under the national law of a Member State,

- national governments and their corresponding offices including public bodies that deal with public debt at national level,
- central banks and
- supranational organisations

to whom the Bank provides services relating to the reception and transmission of orders in relation to one or more financial instruments, execution of orders on behalf of clients and dealing on own account, as well as any ancillary services directly related to the above services, and towards whom the Bank is not obliged to comply with the conduct of business rules, save for the obligation to provide the eligible counterparties with appropriate information in a timely manner, before providing investment or ancillary services, in a form that is comprehensible and specifically tailored to the client or potential client for whom the information is intended, ensuring that the client or potential client can reasonably understand the nature and risks associated with the investment services and specific types of investment instruments being offered, and thus enable them to make informed investment decisions based on the provided information.

3.10.3 Information about client categorisation and the right to request a different category

Relevant regulations stipulate obligations of investment service providers in relation to clients in accordance with the defined client categories. Different treatment of clients according to statutory categories can be seen particularly in the following:

I. Level of protection of the client. A non-professional (retail) client is afforded maximum protection from the Bank. To a professional client, the Bank is obliged to provide the minimum required level of protection. Eligible counterparties are afforded no protection in the performance of an investment service.

II. Provided statutory disclosures. As opposed to professional clients, non-professional clients have the right to obtain detailed information related to the provision of investment services pursuant to relevant regulations.

III. Detailed tests of appropriateness and suitability of investment instruments. When providinginvestment services to a professional client, the Bank is entitled to presume some of the answers.

3.10.4 Changed client category

Clients receiving investment services from the Bank are entitled to request the Bank to be placed in a different client category. The change of the client category can either apply to i) the provided investment service or ii) transaction(s) with a particular investment instrument. If meeting the quantitative limits stipulated by law, non-professional clients may request to be categorized as a professional client instead of a non-professional (retail) client. Such a change is also associated with the loss of the existing level of protection and the level of treatment. A non-professional client must be aware that in such a case, he or she may be no longer entitled to receive compensation from foreign systems similar to the Investor Compensation Fund and that performance of some of the bank's obligations pursuant to relevant regulations may be limited. A professional client may request to be placed in a category with a higher level of protection (the non-professional client category). The eligible counterparty may request to be treated as professional or a retail client.