Leonteq Surveys Three Smart Investment Products for The Current Market Conditions

Peter Muehlsiegl, Director, Sales Structured Solutions, Leonteq Securities (Singapore), addressed the delegates at the Hubbis Independent Wealth Management Forum to offer them some trading ideas that the firm considers an ideal fit for the prevailing financial markets environment.

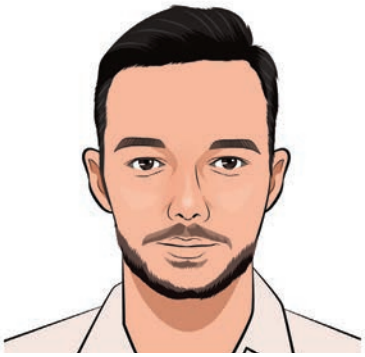
MUEHLSIEGL BEGAN BY EXPLAINING THAT Leonteq had been operating in Singapore for more than seven years, offering a range of bespoke structured investment products. "Leonteq works with many external asset managers, private banks, and family offices," he reported. "The company employs some 50 people here and around 15 in Hong Kong and has 5 headcount in its newly opened office in Tokyo, giving it excellent coverage in the region."

"The current market environment," he told the delegates on March 6 when he gave his presentation, "feels a little bit like early 2018, when the markets were up and some of our clients even thought about closing the books already." But markets can change, and fast, as the world saw during the course of 2018.

Muehlsiegl's first suggestion was a capital protected note that he said basically helps investors to lock in the gains that hopefully they had already made in early 2019 but still to benefit from some upside. This product is named the Shark Fin Note.

Protection, with decent upside

A Shark Fin Note offers up to 100% capital protection at maturity, meaning if the market does not perform, the investor's initial investment would not be at risk. It is suitable for investors who are moderately bullish on the underlying as it offers investors upside participation up to the predefined barrier level. Even if



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the underlying does breach this barrier level a rebate coupon could be paid. Muehlsiegl illustrated this with reference to some excellent slides for the delegates.

"The underlying can be chosen by the investor," he reported, "it can be an ETF, it can be a basket of stocks, can be commodities, anything you like. Additional upside participation, however, comes at a cost, as most of you know, and that is why it is structured the way we did. If markets rally too much from today, you still get back 100% of your capital plus the so-called rebate coupon."

Muehlsiegl then offered an example. He highlighted an example of a Shark Fin Note in US dollars that is 100% capital protected at the 18-month maturity, with the underlying comprising an average basket of two stocks, Apple and Google. The 'strike' level is 100% of the initial fixing so the basket performance will be based according to the strike level.

Looking for the sweet spot

He explained that if the basket moves up by 1% the investor will receive 1% return. And the barrier is set at 117%, which means that if the basket climbs by 17% from the initial level during the lifetime of the products, the barrier level would have been breached. When the barrier has been breached the investor will receive at maturity the 6% coupon, equivalent to 4% per annum return for the 18 months, he noted.

"Here we can work with our clients on a bespoke basis," he added. "They tell us their portfolio construction, their conviction list and then we can come up with a solution tailored to their needs."

Muehlsiegl also focused on what happens if the underlying does not perform and the basket falls, for example, 10%, thereby closing at 90% of the initial investment. Because the product is capital protected, the client will still receive their initial investment back, they are 100% capital protect but of course will not receive any coupon in this scenario.

Should the basket move up 10%, this results in the client getting a 10% in return, in other words in a one to one ratio, or 15% for a 15% rise in the basket. But if, on any single day, the basket breaches the 117% threshold, so for example if it ends up at 120%, at maturity instead of getting the performance

the client will receive only the flat coupon, in this case the 6% flat coupon return.

Accordingly, the sweet spot is actually in the range only up to the 117%, within which the client participates alongside the positive performance of the basket. But if 117% is breached, the client only receives back their capital plus the modest coupon.

Cash replacement ideas

Muehlsiegl then moved on to another capital protected note that can be looked at as cash replacement, in this case citing an example based on three Singapore Blue Chip stocks.

"It is a very simple trade, with a one-year maturity, and 100% capital protected," he reported. "Take for example CapitaLand, Ascent, and DBS stocks. Every quarter if the stocks are up, any amount, the product is early redeemed at 100 plus 10% annualised coupon. Accordingly, if after one year the stocks are mildly up you get 100 plus 10% coupon which obviously is more than you could expect on your bank account here in Singapore."

There is no downside risk, other than the credit risk of the issuer. "If you are happy with the credit risk of the bank that we choose as an issuer for you," he noted, "then this should be good addition to your portfolio."

Recovery products to the rescue

The third product he highlighted involves for example three stocks, a fixed coupon of 12% per year and some downside protection of 25% of the original capital.

If for example, the investor is down 16% at a point in the structure's life, Leonteq can offer to buy back the products that are under water and issue a new product that costs exactly the same amount with the sole purpose of recovering that loss.

"How we do this," he reported, "is that we extend the maturity and we take away the coupon which enables us to issue the note at the same price as your old product had cost. That way the client has no cash flow outgoing and usually is quite happy about these proposals." He then explained in more detail how the recovery works. ■

Leonteq: Building its Name and Product Delivery in Asia

Leonteq is an independent financial services firm, listed on the stock exchange in Switzerland. Leonteq has around 490 employees globally in 11 offices. In Asia, the firm operates through the regional headquarters in Singapore, and has an office and onshore license in Hong Kong and Tokyo.

Switzerland is one of the largest markets globally for Structured products (SPs) in terms of volume, and Leonteq is one of the largest issuers. In 2018 the firm issued roughly 28,000 bespoke products, for a total traded volume globally of around USD29 billion.

The firm is an expert at creating structured investment products for financial institutions, mostly private banks, securities houses, who sell them to their private clients. Leonteq also creates SPs tailored for institutional clients such as the asset managers and insurance companies, for their own investment purposes.

A key feature of SPs is that they can be customised to align directly the risk-return profile of the investors with their investment views. Crucially, they are not created by Leonteq based on any views the firm might have on the direction of any markets.

Leonteq is well known for having an outstanding technology platform, from which it can create these tailored SPs efficiently. The firm aims to be faster to price and issue new products, while proposing competitive pricing even for small trade sizes. Innovation and flexibility are core to Leonteq's abilities to suit local needs.

SPs are usually created through the combination of a bond and a derivative, packaged in a single product. SPs are therefore tailor-made solutions that can be created on various asset classes, such as equities, indices, ETFs, mutual funds, commodities, FX, interest rates, credit and so forth.

SPs can for simplicity be defined in three categories. The first is the capital protection product; this is typically created on low volatile underlying assets, such as fixed income and balanced funds. It allows the investor to participate simply in the fund performance with full capital protection.

The second SP would be classified as yield enhancement product. It is usually used on volatile underlying assets, such as equities, indices and commodities. Investors will receive a fixed guaranteed or conditional coupon/yield (the upside), while combining soft downside protection.

The third category is the participation product. It allows the investor to get more upside with the same downside risk inherent to the underlying asset(s); or the same upside with less downside exposure. These products are usually seen as equity replacement ideas.