



# Overview of the key characteristics and risks of financial instruments

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## ★ Introduction

Risks are inherent in investment in financial instruments.

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

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

This overview of the most important characteristics and risks of financial instruments is, however, not exhaustive. Investing always requires a dose of common sense. You must set realistic expectations and well-defined investment goals, knowing how much money you can afford to lose and for how long, and never taking more risks than appropriate to your knowledge and experience.

Furthermore, you need be aware that past performance of a financial instrument is not a reliable indicator of future performance. By adhering to these principles, you will avoid disappointments and unpleasant financial surprises.

## ★ 1. General investment risks

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

### PRICE RISK

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

### EXCHANGE RATE RISK

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

### CREDIT RISK

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

### LIQUIDITY RISK

Liquidity risk occurs when a given investment is difficult to trade. A distinction needs to be made between:

- illiquidity caused by the relationship between supply and demand: if there is (almost) only a supply (sellers) of a financial instrument at a given price. This is also the case if there is (almost) only demand (buyers) for a financial instrument for a given price. The result of this is that buy and sell orders cannot be executed immediately, or only in part and on unfavourable terms.
- Illiquidity linked to the nature of the specific financial instrument or market practices: when there are lengthy execution deadlines, among other reasons, due to market practices or other restrictions on trading, or a need for short-term liquidity that cannot be met by the sale of financial instruments. For example, in some mutual funds, the investor may not divest and liquidate their units before the fund is closed; this type of information is generally included in the prospectus or in the Key Investor Document (KID) for the fund.

Therefore, when an investor is considering making an investment or purchasing a financial instrument, they must consider whether they would be able to liquidate their position, i.e. convert their units or their investment into liquidities/currencies. Further information about the divestment requirements is generally included in the key information documents for each product.

### INTEREST RATE RISK

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

### REINVESTMENT RISK

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

### FISCAL RISK

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

### CYCLICAL RISK

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

### MARKET RISK (also known as SYSTEMATIC RISK)

The market risk is the risk that the entire financial market or one category of assets will decline, meaning that the value of the assets in your portfolio may be affected. This kind of fluctuation can occur for a variety of reasons including currency movements or sharp rises or falls in interest rates and/or stock-exchange prices generally. This risk, which affects how the entire market works, cannot be covered by portfolio diversification because the danger goes beyond a single industry or a single sector of activity.

### BANKRUPTCY RISK

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

### INFLATION RISK

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

### GEOGRAPHICAL RISKS

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

### COMPLEXITY RISK

Following the implementation of the European Directive on Markets in Financial Instruments (MiFID) into Belgian law, Keytrade Bank differentiates between complex and non-complex financial instruments. Information about the complexity of the financial instrument is provided below under «General Risks» for each financial instrument.

Please note that, in connection with orders placed on your own initiative, Keytrade Bank is not required to assess on beforehand whether the product is appropriate or suitable for you. Valuation is only required for complex financial instruments.

### PSYCHOLOGICAL RISKS

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

### RISKS FROM USING IT SYSTEMS

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

## SYSTEMIC RISK

This refers to the risk triggered by an economic shock (such as the failure of a company, sector, industry or financial institution) in a given sector, and which could, through a knock-on effect, spread throughout the entire system and lead to a given economy collapsing (for example: the collapse of Lehmann Brothers Holdings Inc. in 2008).

## ★ 2. Characteristics and risks of each financial instrument

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

### 2.1. Shares and share certificates

#### 2.1.1. Description

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

If the company is in good health and its operations generate profits, then you share in the price rise and possibly in dividend payments. However, if the company runs into financial difficulties and market participants believe that the company will struggle to generate a profit in the future, then the price will fall and you may receive reduced dividends or none. In the event of bankruptcy, the value of the shares may fall to zero.

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

- internal factors: actual or expected company profits, news about the company and/or sector, the dividend policy and more;
- external factors: political events, macroeconomic developments and irrational factors that may exacerbate stock market fluctuations.

As a shareholder, you are entitled, among other things, to vote at the annual general meeting (except if you hold No-voting shares) and to a part of the company's liquidation value if it is dissolved (as long as there is a liquidation balance). Shares may be registered by name, or dematerialised.

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

Dematerialised shares are represented by an entry in a share account in the name of the shareholder at an institution authorised for this purpose. You can generally sell these easily at any time, on any day. This is even easier for shares in exchange-listed companies.

Shares may be listed on regulated markets (outside the EU) but also on OTC Markets (previously known as OTCBB and Pink Sheets, with OTC<sup>1</sup> standing for "Over The Counter"), which is a decentralised American broker/dealer network providing prices and liquidity information for thousands of securities traded over-the-counter.

**Share certificates** are securities which represent original shares and are managed by a trust company. They track a share's value (price) and yield the same income as the underlying share (dividend). The major difference between this and a share is that a certificate does not give the right to participate in the vote at a shareholders' meeting. The risks are basically the same as the risks linked to the normal shares.

Share certificates can be found in the shares section of the Transaction Website and the mobile app.

**Listed rights** are issued by listed companies and attributed to existing shareholders to allow them to subscribe to new shares in the context of a capital increase. As the rights are listed, shareholders can sell their rights if they don't want to participate in the capital increase, if there's a counterparty willing to buy their rights. Additional rights can also be acquired. These rights expire, possibly worthless, towards the end of the capital increase. Please note that a capital increase can have many forms. Listed rights will not always be attributed to shareholders. Rights may also be unlisted. However, companies may proceed with a capital increase without granting shareholder rights (or even without existing shareholders being able to participate, as part of a private investment, for example).

Shareholders might also be attributed **contingent value rights** (CVR), typically in the context of a merger or acquisition. If and when certain milestones are met by the company, shareholders are entitled to additional compensation. A CVR can be sold on the market (if and when there is a counterparty willing to trade) and has an expiration date. It may expire worthless if the milestone(s) are not reached.

An **American Deposit Receipt** (ADR) is a certificate of a foreign company, and is traded in USD on an American exchange. The ratio between the ADR and the original share is not necessarily 1:1. An ADR might represent a bundle (example 1 ADR = 5 shares) or a fraction (example 1/10th) of an underlying shares of the foreign company.

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<sup>1</sup>- For more information, please refer to the document "Trading on OTC Markets"

Depending on the ADR, a holder of the ADR can or cannot be entitled to a dividend, voting rights and more.

## 2.1.2. Risks

### GENERAL RISKS

PRICE RISK	Yes. This is determined by both the company policy and the macro-economic, micro-economic and financial context. Favourable or unfavourable market conditions may affect the instrument.
EXCHANGE RATE RISK	Yes, if the share price is not listed in euros, or if the company does its business outside of the Eurozone.
CREDIT RISK	No, shares are risk-bearing capital, and not debts. Of course, shares can lose some or all of their value should the company go bankrupt.
LIQUIDITY RISK	Yes, depending on the volume of transactions in the share and the free float. The larger the company's market capitalisation, the more liquid the market for its shares will be.
INTEREST RATE RISK	Yes, depending on the shares and the investment climate. Generally, a rise in interest rates negatively affects share prices.
REINVESTMENT RISK	Yes
FISCAL RISK	Yes
MARKET RISK	Yes
INFLATION RISK	Yes
GEOGRAPHICAL RISK	Yes
COMPLEXITY RISK (MiFID)	Yes, if listed on OTC Markets

### SPECIFIC RISKS

#### Entrepreneurial risk

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

#### Dividend risk

When there are low profits or even losses, you may receive reduced dividends or none. However, some companies do not have policy of paying out dividends. When times are bad, you share in the losses. That can reach 100% of your investment in the event of bankruptcy.

## 2.2. Real estate certificates and public regulated real estate company

### 2.2.1. Real estate certificates (Belgian)

#### 2.2.1.1. DESCRIPTION

Real estate certificates are financial instruments issued by a company in order to finance the purchase or construction of real estate. The certificates may or may not be listed on a stock exchange. As the holder of a certificate, you hold a claim against the income from a real estate investment (income from rent for the building and potential capital gains on its sale).

The investor is not the co-owner of a real estate certificate. Instead, the co-owner is the creditor of the real estate company that issued the certificate.

As they are debt instruments, real estate certificates have a variable maturity. However, as real-estate investments are typically long-term, they generally have a maturity of between 15 and 20 years.

Real estate certificates can be found in the shares section of the Transaction Website and the mobile app.

#### 2.2.1.2. Risks

### GENERAL RISKS

PRICE RISK	Yes, depending on developments in the real estate sector, which may be positive or negative, and the intrinsic aspects of the building (location, age and quality of tenants). The price may also be influenced by the profitability of the company that issued the certificates.
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EXCHANGE RATE RISK	No, given that real estate certificates are denominated in euros
CREDIT RISK	Yes, un certificat immobilier est un titre de créance. Si la société émettrice du certificat immobilier rencontre des difficultés financières ou fait faillite, vous risquez de perdre (une partie de) votre capital investi.
LIQUIDITY RISK	Yes, depending on the issue volume. Liquidity is generally limited due to the small market capitalisation.
INTEREST RATE RISK	Yes, real estate certificates are sensitive to interest rate movements. An increase in interest rates normally results in a reduction in the value of the certificate.
REINVESTMENT RISK	Yes
FISCAL RISK	Yes
MARKET RISK	Yes
INFLATION RISK	Yes
GEOGRAPHICAL RISK	No
COMPLEXITY RISK (MiFID)	No

### SPECIFIC RISKS

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

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

#### Diversification risk

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

### HYPOTHETICAL SCENARIOS

This section describes a number of hypothetical positive/negative performance scenarios for an investor holding real estate certificates. These scenarios are purely notional for the purposes of illustrating the mechanics of the investment; these scenarios will not necessarily occur for any investments that the investor decides to make.

#### • Positive Scenario #1

When they are issued, the investor buys a real estate certificate for a commercial building (offices) in the centre of Brussels, with the intention of holding the certificate until its maturity (15 years). During this period, the real estate and rental market category is healthy; and the building is occupied at maximum capacity.

During the entire investment period, the investor receives the contractual return (i.e. the income from the tenants minus the building costs) established by the certificate. Upon maturity, the building is sold with a capital gain and the investor receives a share of the profit, as established by the certificate.

#### • Negative Scenario #1

When they are issued, the investor buys a real estate certificate for a commercial-office building in the centre of Brussels, with the intention of holding the certificate until its maturity (15 years). During this period, the real estate and rental markets are healthy, but the real estate company is struggling to rent the property and the offices are occupied at half capacity, generating little in the way of returns.

The investor does not receive coupons during the investment period. When the property is sold, it is sold at «break-even», and does not generate any capital gains. The investor will not receive any return or capital gains from this investment.

#### • Negative Scenario #2

When they are issued, the investor buys a real estate certificate for a commercial-office building in the centre of Brussels, with the intention of holding the certificate until its maturity (15 years). During this period, there is a real estate crisis in Belgium and real estate prices fall sharply. In addition to this, the company is struggling to rent out its premises and is generating little revenue from them.

Upon maturity, the building is sold on with a capital loss; and the investor makes a capital loss on their investment.

## 2.2.2. Public regulated real estate company

### 2.2.2.1. DESCRIPTION

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

The REC is not a fund. However, RECs must satisfy most of the same obligations, such as the distribution obligation, limitation of the debt ratio, real estate diversification and more.

RECs can be found in the shares section of the Transaction Website and the mobile app.

REC is a potential legal status for a real estate company in Belgium. A similar status also exists in several other countries, like France (SIIC, or Société d'Investissement Immobilier Cotée) and Spain (SOCIMI). Globally, real estate companies with such a legal status are called REITs (Real Estate Investment Trusts). Rules and obligations with regard to REITs differ from country to country.

### 2.2.2.2. RISKS

#### GENERAL RISKS

PRICE RISK	Yes, depending on developments in the real estate sector and the intrinsic quality of the portfolio.
EXCHANGE RATE RISK	Yes, if the asset portfolio is made up of real estate in non-Eurozone countries
CREDIT RISK	It may be high, based on the financial leverage applied and interest rate movements.
LIQUIDITY RISK	Yes, RECs are listed on the stock exchange. Therefore, their liquidity is dependent upon the secondary market, where liquidity varies from REC to REC.
INTEREST RATE RISK	A significant prolonged interest rate movement (either upwards or downwards) can significantly affect the portfolio's value, as well as the REC's price.
INTEREST RATE RISK	A significant prolonged interest rate movement (either upwards or downwards)
REINVESTMENT RISK	Yes
FISCAL RISK	Yes
MARKET RISK	Yes
INFLATION RISK	Yes
GEOGRAPHICAL RISK	Yes, depending on the composition of the asset portfolio.
COMPLEXITY RISK (MiFID)	Yes, if listed on OTC Markets (Over The Counter).

#### SPECIFIC RISKS

##### Risk of inadequate income

Dividend payments may be suspended due to major renovation costs or real estate vacancies.

#### HYPOTHETICAL SCENARIOS

This section describes a number of hypothetical positive/negative performance scenarios for an investor holding shares in an REC. These scenarios are purely notional for the purposes of illustrating the mechanics of the investment; these scenarios will not necessarily occur for any investments that the investor decides to make.

##### • Positive Scenario #1

The investor purchases a stake in an REC, which invests in Belgian real estate. The investor has a 10-year investment horizon and intends to sell their shares at that point in time.

While holding these shares, the real estate market in Belgium is healthy, the REC's investment portfolio produces a stable annual return and the company pays out a 2% annual dividend.

After 10 years, the investor sells their stake. Thanks to the real estate sector's healthy position and the quality of the investments chosen by the REC, this sale generates a capital gain for the investor.

##### • Negative Scenario #1

The investor purchases a stake in an REC, which invests in Belgian real estate. The investor has a 10-year investment horizon and intends to sell their shares at that point in time.

While holding these shares, the real estate market in Belgium is healthy, but the REC's investment portfolio is not generating a return and some properties are losing value. The company does not distribute dividends during the period when the investor holds their stake.

##### • Negative Scenario #2

The investor buys shares of a SIR that has invested in Belgian real estate. The investor has a 10-year investment horizon and intends to sell their shares at the end of this period. During this period, interest rates increase significantly, and suddenly. In general, this puts the value of real estate under pressure. This decreasing value of buildings puts the LTV (Loan To Value) ratio under pressure, which is a problem for RECs: they must respect rules with regard to the

debt levels. The REC sees itself obliged to do a capital increase to lower the debt. Because of the negative market conditions, the capital increase is done at a significant discount on the NAV (net asset value). An investor who does not want to be diluted is required to invest a significant additional amount. After the 10 year holding period, the investor sells their investment with a significant loss on their initial investment.

## 2.3. Fund

### 2.3.1. General

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

#### LEGAL CLASSIFICATION

From a legal standpoint, UCIs/funds may be set up through a legal agreement, which in this case are referred to as **mutual funds** (see 2.3.2), or through articles of association, which in this case are referred to as **investment companies** (see 2.3.3).

The units held in a mutual fund are referred to as «equity securities». Those held in an investment company are referred to as «shares».

#### ADDITIONAL CLASSIFICATIONS

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

- they either have a **variable** number of units (which are referred to as open-ended UCIs). This type of UCI can increase its capital by issuing new units and can reduce its capital by redeeming existing units. These UCIs/funds may be **listed** on stock exchanges (and can then be traded in the same way as shares – see also the Trackers under 2.4) or **unlisted** (and have a net asset value that is calculated periodically, usually daily). This includes the Belgian and Luxemburg SICAVs.
- or they have a **fixed** number of units (which are referred to as closed-ended UCIs). These UCIs are always listed on stock exchanges (the price of the units or shares is determined by supply and demand). This includes the Belgian and Luxemburg SICAF.

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

### 2.3.2. Mutual fund

A mutual fund is not a legal entity, but is established through a joint ownership agreement. The fund is managed on investors' behalf by a management company. This means that the mutual fund is fiscally transparent, as dividends and interest received by the mutual fund are deemed to have been received directly by the end investor. You, as an investor, rather the mutual fund must pay tax on this income. Therefore, you must declare this income in your tax return.

Mutual funds can be found in the fund section of the Transaction Website and the mobile app.

**Pension savings funds** are funds specifically created under Belgian tax legislation on savings. This type of fund invests in shares and bonds, meaning that a minimum return is not guaranteed. The pension savings fund does not have a maturity date. For more information, please take a look at the website.

Mutual funds can be found in the fund section of the Transaction Website and the mobile app, and pension savings funds can only be found in the mobile app.

### 2.3.3. Investment profile

#### 2.3.1.1. SICAV

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

Each unit is valued in relation to the SICAV's income. If these are distribution units, you receive the income. In the case of capitalisation units, the income is reinvested in the company.

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

SICAVs can be found in the fund section of the Transaction Website and the mobile app.

### 2.3.1.2. SICAF

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

SICAFs invest either in shares or in real estate. When a SICAF invests in real estate, they are referred to as real estate SICAFs or SICAFIs (see 2.2.2.). SICAFs are not available on the Keytrade Bank platform.

### 2.3.4. Risks

#### GENERAL RISKS

PRICE RISKS	Yes, depending on the fund's underlying investments and diversification, as well as on favourable or unfavourable market conditions.
EXCHANGE RATE RISK	Yes, if the underlying investments or the fund is/are not listed in euros.
CREDIT RISK	Yes, particularly for bond funds.
LIQUIDITY RISK	Yes, particularly for SICAFs that are dependent upon the secondary market, where liquidity varies from fund to fund (for example, real estate SICAFs).
INTEREST RATE RISK	Yes, especially for funds that invest in fixed income assets. However, a rise in interest rates will also have a negative impact on the share prices and, therefore, indirectly on funds that invest in shares.
REINVESTMENT RISK	Yes
FISCAL RISK	Yes
MARKET RISK	Yes
INFLATION RISK	Yes
GEOGRAPHICAL RISK	Yes, depending on the fund/UCI.
COMPLEXITY RISK (MiFID)	<p>(1) Unlisted funds/UCIs: Keytrade Bank regards UCITS funds as non-complex financial instruments. However, non-UCITS funds are regarded as complex financial instruments.</p> <p>UCITS stands for "Undertakings for Collective Investment in Transferable Securities". This term refers to a European Union Directive that defines which criteria a fund based in the EU must meet to be able to be sold in all the EU countries (the so-called European passport). The aim of the directive is to simplify investment guidelines in Europe and to offer investors more protection.</p> <p>(2) Listed funds/UCIs: The rule is the same as the share rule. Complex.</p>

#### SPECIFIC RISKS

##### Management risk

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

##### Dividend risk

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

##### Price risk for open-ended and closed-ended funds/UCIs

The price risk for open-ended funds/UCIs is quite different to the price risk for closed-ended funds/UCIs. In normal market conditions, open-ended funds/UCIs are traded at or near the real value of the underlying investments, depending on the market liquidity of the fund's units.

Investors can subscribe to units or shares of open-ended funds/UCIs at any time during their existence (depending on the fund's liquidity). Therefore, the unit or share value is influenced by market supply and demand.

Closed-ended fund/UCI units are marketed during specific predefined periods only. The investor/unitholder may only liquidate their units on the liquidation dates initially set out in the fund prospectus.

## Specific fund risks

Before investing in a fund, you must first read the prospectus and the Key Investor Information Document (KIID). The prospectus and KIID contain a description of the key characteristics and risks, as well as the fees connected with the fund management. These fees will of course affect the return on your investment.

### HYPOTHETICAL SCENARIOS

This section describes a number of hypothetical positive/negative performance scenarios for an investor holding units in a fund. These scenarios are purely notional for the purposes of illustrating the mechanics of the investment; these scenarios will not necessarily occur for any investments that the investor decides to make.

#### • Positive Scenario #1

On 31 December 2020, the investor purchases a unit in a SICAV fund that sets out an aim in its prospectus to invest in a diversified manner in EU countries, as well as in various sectors. The fund does not use leveraging, and can only buy shares and bonds. The investor has a five-year investment horizon. During this period, the EU economy is healthy, the price of the shares selected by the fund manager is rising and the bonds are generating returns.

Thanks to this positive performance, the fund's unit price goes up and the investor sells their unit with a capital gain after five years.

#### • Negative Scenario #1

On 31 December 2020, the investor purchases a unit in a SICAV fund that sets out an aim in its prospectus to invest in a diversified manner in EU countries, as well as in various sectors. The fund does not use leveraging, and can only buy shares and bonds. The investor has a five-year investment horizon. During this period, the EU is hit by a major crisis and many companies go bankrupt. The price of the shares selected by the fund manager go down and some bonds default.

As a result of this negative performance, the fund's unit price plummets and the investor sells their unit after five years at a lower price than the purchase price; therefore, the investor makes a capital loss.

## 2.4. Trackers

### 2.4.1. Description

A tracker is a product listed on an exchange (Exchange Traded Product - ETP) that tracks the performance of a stock market index or a basket of assets. There are different types of trackers, such as stock-exchange index trackers and sector, commodity and bond-index trackers. They can be traded on any trading day, just like shares.

A tracker can take the following legal forms:

- Trackers are usually structured like a fund. When this occurs, they are referred to as «**Exchange Traded Funds**» (ETFs). They are open-ended funds that replicate an index as closely as possible (also known as «passive ETFs»). ETFs are usually UCITS compliant. Like funds, ETFs can be set up in the form of an investment company or a mutual fund. For the general characteristics and risks of these funds, see chapter «2.3 Funds».
- A tracker can also be offered in the form of a debt claim. This is normally used for commodity trackers (such as energy, oil and metals). They are generally referred to as either «**Exchange Traded Notes**» (ETNs) or «**Exchange Traded Commodities**» (ETCs). ETCs track the price of either an individual commodity or broader commodities indices, without owning the assets. They are issued by banks or specialty issuers. If you buy an ETC, you will receive a debt claim that is similar to a bond. ETCs are backed by institutions with high credit ratings, but are not completely free of credit risk.

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

By choosing a Tracker, you are investing in a basket of assets. Therefore, there is less risk than investing in individual financial instruments. A Tracker is the opposite of an actively managed fund, where the manager is constantly trying to select the best shares to get the highest possible return. This type of investment management is very cost- and time-intensive. Therefore, the management costs are generally lower for a Tracker than for a traditional fund.

For some Trackers, you can multiply the performance of the index (leveraging) or track the reverse of the index movements (an inverse tracker), with or without leverage. This obviously involves more risks.

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

In order to achieve their investment goals, Tracker issuers seek to **physically** or **synthetically replicate** the index in question. **Physical replication** can be achieved by fully replicating the underlying index (the Tracker invests in all the index components) or by using a process known as «optimisation». This is done when the underlying index consists of a very large number of constituents, or includes securities that are difficult to trade, or if multiple indices are being tracked. In this case, the Tracker issuer will invest only in a basket of constituents that provides a representative sample in terms of risk and performance. Therefore, the Tracker does not always include exactly the same financial instruments as the index that is being tracked.

A Tracker may also **synthetically** reproduce the returns on its underlying index. When this occurs, the Tracker issuer agrees one or more swap(s)<sup>2</sup> with one or more counterparties. The Tracker issuer agrees to pay the swap issuer the returns on a pre-defined basket of securities, in exchange for the return on the index. You then are paid out the return on the whole underlying index, but the actual investment might be made in quite different securities. This technique is called **synthetic replication**. This type of replication generally reduces the costs and the tracking error (deviation from the index), but increases the counterparty risk. For markets that are not easily accessible, swap structures are preferable to physical replication.

A Tracker can distribute its own income from dividends or interest (**distribution** method) or automatically reinvest it (**accumulation** method). For a Tracker of the accumulation method, the fund manager will reinvest all received income like dividends and interests. For a distribution Tracker, income from dividends and interest will be distributed to the holders of the Tracker and not reinvested in the Tracker.

**Leveraged trackers** are designed for a specific purpose: to amplify the daily price movements of a benchmark index. Because of this amplification, the impact of market movements is doubled or tripled (depending on the leverage factor). In the event of an unfavourable market, the consequences are severe: losses will be amplified and will significantly exceed those of the underlying benchmark index. To achieve their objectives, these trackers do not simply hold the underlying shares. Instead, they primarily utilise derivative products, such as futures or options, to create the necessary exposure. To maintain the target leverage ratio, the fund manager must rebalance the positions on a daily basis. This daily reset is a critical feature, as it ensures that the leverage remains constant relative to the index's closing price each day. Because of the daily rebalancing, these instruments can lose value even if the index remains flat over a long period. Such a daily rebalance is also applicable to **Crypto ETNs**.

**The Crypto ETNs** are a debt security that provides exposure to the performance of an underlying crypto asset and are regarded as complex. The issuer of the debt security acts as the counterparty. Should the Issuer default, some or all of the capital may be lost. Some ETNs may include a collateralisation mechanism. **Crypto ETNs**, due to their product characteristics, accumulate and do not distribute income, dividends or coupons to the holders of these debt securities.

However, the Crypto ETN performance is made up of:

- the performance of the underlying asset.
- a potential share of the issuer's income from holding specific crypto assets (or staking).

Staking involves locking up a specific amount of crypto assets in a portfolio in order to support the operations of a consensus-based Proof of Stake (PoS) blockchain or its derivatives. In return, participants (referred to as «stakers») receive rewards, usually in the form of new units of the staked crypto assets.

Finally, management fees associated with **Crypto ETNs** apply, which may affect the net performance of the product compared to holding crypto assets directly.

An investor may prefer a **Crypto ETN** to a direct investment in cryptocurrencies in order to enjoy a stricter regulatory framework and better protection. A crypto Tracker does not meet the requirements of the UCITS Directive. The main consequence is: less stringent diversification constraints, which allows for less concentrated exposure.

**Active trackers:** while passive trackers have as a goal to replicate the performance of an underlying index, active trackers however have a divergent objective. The goal can be to beat an underlying index, or to obtain a specific investment result that passive trackers cannot obtain. For example by adapting the portfolio in times of high volatility or downwards markets, and thus having divergent positions and order position weights as compared to a benchmark index. Outperformance is not guaranteed, while the Total Expense Ratio tends to be higher because of the active management of the Tracker.

## 2.4.2. Risks

### GENERAL RISKS

PRICE RISKS	Yes, mainly depending on general positive or negative movements on stock exchanges and underlying investments.
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<sup>2</sup>- A swap is an agreement between two parties where one party makes a payment based on a defined percentage that may be fixed or variable, while the other party makes a payment based on the total return from an underlying asset.

EXCHANGE RATE RISK	Yes, if the underlying investments or the tracker are not listed in euros.
CREDIT RISK	Yes, especially for bond-index trackers.
LIQUIDITY RISK	Yes, depending on the tracker's trading volume and the liquidity of the underlying investments.
INTEREST RATE RISK	Yes, for bond-index trackers, and indirectly for share-index trackers.
REINVESTMENT RISK	Yes
FISCAL RISK	Yes
MARKET RISK	Yes
INFLATION RISK	Yes
GEOGRAPHICAL RISK	Yes, depending on the tracker
COMPLEXITY RISK (MiFID)	Yes. The following are regarded as complex: 1. Non-UCITS trackers. - 2. Leveraged UCITS trackers. - 3. ETNs and ETCs; 4. Inverse trackers

#### SPECIFIC TRACKER-RELATED RISKS

##### Deviation from the index («tracking error»)

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

##### Counterparty risk

If the Tracker can also buy derivatives or make agreements with other parties (swaps), then counterparty risk is created (especially for Trackers that use synthetic replication of an index). That is the risk that another party will not be able to meet their commitments (failure to return securities on loan, for example). For synthetic Trackers that comply with the UCITS Directive, the counterparty risk can be a maximum of 10% of the net asset value of the total assets.

##### Liquidation risk

A tracker is only profitable for a fund manager if it reaches a certain scale. If the assets under management (AUM) drop to and stay at a too low level, the operational costs for the fund manager outweigh income from management fees. In such an event, the manager halts the Tracker, and investors are forced to exit their position and are paid out their units at the Net Asset Value (NAV) of that moment. This might be an unfavourable value for the investor.

##### Liquidity risk

In normal market conditions and for Trackers with a large enough size (AUM), liquidity offered by the market makers is sufficient for retail investors. It can occur that market makers withdraw from the orderbook, or increase the bid-ask spread, for example in times of high volatility. This makes it hard or impossible for the investor to exit at a fair price.

#### SPECIFIC ETN-RELATED RISKS

##### Credit risk and counterparty risk

Given that ETNs are debt instruments, there is the risk that the issuer does not meet their commitments as a counterparty. For Crypto ETNs, this risk is considerably increased when they are synthetically replicated.

That is why it is important to know the credit rating of the issuing institution. In addition, issuers are more and more offering ETNs with collateral to reduce the counterparty risk.

##### Liquidity risk

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

##### Risk relating to a single underlying

When a product is exposed to the performance of a single underlying, this poses a concentration risk due to the lack of diversification. For a product providing exposure to an underlying crypto asset (for Crypto ETNs), this may lead to increased product volatility.

#### SPECIFIC ETC-RELATED RISKS

##### Risk relating to usage of futures

Some ETCs are physically backed by gold or silver, for example. However, ETCs tracking commodities that are difficult or expensive to store – such as energy or agricultural products - rely on futures contracts. Since futures are instruments with a fixed expiry date, futures contracts must be rolled into the next period. The investor can be significantly impacted by a negative rollover yield: this occurs when the fund manager is forced to buy a new more expensive future than the expiring one (a market condition known as Contango). This can have a massive impact

on the investor's return, sometimes even outweighing the price movement of the underlying commodity itself. In a more favourable scenario, the new, replacement future might be cheaper than the expiring one (market condition known as Backwardation). Such a positive rollover yield influences the investor's return positively.

### Credit risk and counterparty risk

ETCs that are not physically backed but use futures or swaps are almost always debt instruments, which comes with a counterparty risk.

### Liquidation and liquidity risk

A significant number of ETCs have a relatively small size (AUM). The result is that there is an increased liquidation risk, and potentially an increased liquidity risk.

## HYPOTHETICAL SCENARIOS

This section describes a number of hypothetical positive/negative performance scenarios for an investor holding units in a Tracker. These scenarios are purely notional for the purposes of illustrating the mechanics of the investment; these scenarios will not necessarily occur for any investments that the investor decides to make.

- Positive Scenario #1

The investor purchases a unit of a Tracker that replicates the performance of the BEL20, aiming to hold the investment for five years.

During this period, the Belgian shares perform well and the benchmark index goes up 50%.

On the sale date, the investor sells their unit with a capital gain.

- Negative Scenario #1

The investor purchases a unit of a Tracker that replicates the performance of the BEL20, aiming to hold the investment for five years. During this period, there is a financial crisis and the BEL20 loses one third of its value.

On the sale date, the investor sells their unit with a capital loss.

- Negative Scenario #2

The investor has bought units of a Tracker that tracks the performance of a specific theme index that has been popular in the past. During the five-year holding period, this theme becomes very unpopular and the fund size shrinks significantly. The fund manager is no longer able to cover the costs and decides to halt the Tracker. All holders of units in this Tracker are paid out at the market value of their units at that moment. This value might be significantly lower than the initial acquisition price.

- Negative Scenario #3

The investor purchases a unit of a triple-leveraged Tracker that replicates the performance of the Brent Barrel price. In the days following the transaction, OPEC announces that it will double its production for the year. The Brent Barrel price loses more than two thirds of its value and the managing company liquidates the Tracker.

The investor loses their entire investment.

## 2.5. Bonds

### 2.5.1. General

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

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

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

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

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

### 2.5.2. Ordinary (non-complex) bonds

The following bonds are regarded as non-complex: government bonds (treasury bonds and OLOs), supranational bonds, domestic corporate bonds in euros, and fixed-rate Eurobonds with a fixed redemption price.

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

Public authorities guarantee government bonds. The credit risk for bonds issued by OECD<sup>3</sup> member states is generally very low (see the credit ratings for these countries). On the secondary market, government bonds are very liquid.

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

**Domestic corporate bonds in euros** are fixed-interest bonds issued by private companies. The quality of the issuer is determined by the rating that they are given by specialised rating agencies. These agencies use a scale from AAA (top quality) to C (very weak)<sup>4</sup>.

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

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

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

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

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

#### GENERAL RISKS

PRICE RISKS	Yes, should the bond be sold before maturity or if the issuer's financial situation worsens.
EXCHANGE RATE RISK	Yes, if not denominated in euros.
CREDIT RISK	Yes, depending on the quality (rating) of the issuer. Subordinated loans involve higher risk.
LIQUIDITY RISK	Yes, depending on the issue size, the transaction volume, the issuer type and the currency.
INTEREST RATE RISK	Yes, depending on the time remaining until maturity. The longer the time remaining until maturity, the greater the risk that interest rates will rise and the bond's value will fall.
REINVESTMENT RISK	Yes
FISCAL RISK	Yes
MARKET RISK	Yes
INFLATION RISK	Yes
GEOGRAPHICAL RISK	Yes
COMPLEXITY RISK (MiFID)	No

<sup>3</sup>- OECD stands for «Organisation for Economic Cooperation and Development». The organisation contains approximately thirty developed countries.

<sup>4</sup>- AAA and AA (high credit rating) rated bonds and A and BBB (average credit rating) rated bonds are referred to as «investment grade» bonds. Bonds with lower ratings (such as BB, B and CCC) are regarded as less creditworthy and are referred to as «speculative bonds» or «junk bonds».

## SPECIFIC RISKS

### Insolvency risk

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

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

### Early redemption risk

In certain cases, the issuer can move to early redemption of a loan. For example, if interest rates fall.

This can have an adverse effect on returns.

## HYPOTHETICAL SCENARIOS

This section describes a number of hypothetical positive/negative performance scenarios for an investor holding a normal bond. These scenarios are purely notional for the purposes of illustrating the mechanics of the investment; these scenarios will not necessarily occur for any investments that the investor decides to make.

### • Positive Scenario # 1

On 31 December 2020, the investor buys a Belgian government bond which pays out a 1% annual coupon and which has a maturity date of 31 December 2025. The investor holds the bond up to the maturity date.

While holding the bond, the investor receives the coupons due and, upon maturity, the nominal value of the bond is repaid.

The investor retains their capital and receives a 1% coupon during the five years that they hold the bond.

### • Negative Scenario #1

On 31 December 2020, the investor buys a Belgian corporate bond which pays out a 3% annual coupon and which has a maturity date of 31 December 2025. The investor holds the bond up to the maturity date.

On 31 December 2022, the bond issuer defaults and is unable to pay out the coupon. After the company is liquidated, the investor recoups 50% of the value of their investment

### • Negative Scenario #2

On 31 December 2020, the investor buys a Belgian corporate bond which pays out a 3% annual coupon and which has a maturity date of 31 December 2025. The investor intends to hold the bond up to the maturity date.

By 31 December 2022, the bond has lost 20% of its value due to poor results and a deterioration in the financial health of the company. As the investor is worried that the company may default, they decide to sell their bond at market price. As the sale price is lower than the purchase price, the investor makes a capital loss on their investment.

## 2.5.3. Complex bonds

Keytrade Bank regards the following bonds as complex (MiFID): convertible bonds, reverse convertibles, variable-rate Eurobonds, perpetual bonds and bonds with other special characteristics. Keytrade Bank does not currently offer any complex bonds on the Transaction Website or on its mobile app.

**Convertible bonds** are corporate bonds that you can swap, under specific conditions, for a predetermined number of shares in the company in question. You receive less interest in return for this option. Depending on the price evolution of the underlying security, this conversion might result in a higher total return for the investor than simply holding the bond until maturity, without conversion.

**Reverse convertibles** differ from normal convertible bonds in that only the issuing (financial) institution can make the decision to convert the security into shares. In exchange, you, as the bondholder, will receive a higher coupon rate.

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

**Perpetual bonds** are bonds with no maturity date (and therefore, no capital redemption dates) and fixed coupons. Investors can sell/buy bonds with a put or call option on the bond's maturity date.

## GENERAL RISKS

PRICE RISKS	Yes, for <b>convertible bonds</b> and <b>reverse convertibles</b> : particularly when sold before maturity and after conversion. The price of <b>perpetual bonds</b> is sensitive to positive or negative movements in the bond market, due to the lack of a maturity date.
EXCHANGE RATE RISK	Yes, if not denominated in euros.
CREDIT RISK	Yes, depending on the issuer
LIQUIDITY RISK	Yes, complex bonds are generally more difficult to trade.
INTEREST RATE RISK	Yes, the interest rate risk for <b>convertible bonds</b> , is limited, due to the lower coupon rate. However, this risk is high for <b>reverse convertibles</b> , <b>variable rate bonds</b> and <b>perpetual bonds</b> .
REINVESTMENT RISK	Yes
FISCAL RISK	Yes
MARKET RISK	Yes
INFLATION RISK	Yes
GEOGRAPHICAL RISK	Yes
COMPLEXITY RISK (MiFID)	Bonds are regarded as complex if they are not regarded as «plain vanilla», i.e. a bond offering a fixed coupon payment on a fixed maturity date and a previously defined maturity.

## SPECIFIC RISKS

## Credit risk

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

## Risk relating to the price of the underlying security

- Convertible bonds: If the price of the underlying security (the company) is no higher than the price that, under the terms of the convertible bond, you have to pay for new shares, then you do not have to purchase the new shares being issued and, in principle, will recoup the principal amount that you paid for the bond.
- Normally the (financial) company that issues a reverse convertible exercises its right to exchange if the price is (sharply) lower than the price that you have to pay the company when it is exercised. Theoretically, the underlying security may not even be worth anything on the stock exchange any longer. This risk is factored into the price of the reverse convertible. If you make a major loss on the underlying security, the reverse convertible will therefore be traded well below its face value

## Risks of specific convertible bonds/reverse convertibles

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

## Early redemption risk – reinvestment risk

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

## 2.6. Derivative financial instruments

Derivative financial instruments, or derivatives, are financial products whose value depends on the value of other products such as, for example, an index, shares, gold or currencies. Trading in derivatives can be of interest to experienced investors because of their leveraging a price increase or decrease in the underlying security results in a much greater increase or decrease in the derivative's value. In addition, you can use derivatives to reduce risks and so protect your portfolio. The most well-known derivatives are options, warrants and Turbos.

Derivative financial instruments are considered complex (MiFID).

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

## 2.6.1. Derivative financial instruments with options to limit the risk of loss of the capital invested

### 2.6.1.1. LONG OPTIONS

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

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

For each buyer of an option, there is also a seller, the so-called writer. The buyer pays them the premium.

As a writer, you have an obligation (and not, like the buyer, a right) to buy the underlying security (for a put option) or to sell it (for a call option).

For options issues, see 2.6.2.1. Short options.

You cannot exercise long options with Keytrade Bank. Either you sell the option contract before the expiry date, or the contract is automatically exercised on the expiry date if the option is “in the money”<sup>5</sup>, or the contract expires worthless and the loss is limited to the premium amount paid. For more details, please refer to the relevant transaction rules at [www.keytradebank.be](http://www.keytradebank.be).

#### GENERAL RISKS

PRICE RISKS	Yes, a «long» option may lose its entire value depending on movements in the underlying security, which may be influenced by favourable or unfavourable market conditions.
EXCHANGE RATE RISK	Yes, if not denominated in euros.
CREDIT RISK	None for transactions on a regulated market or equivalent to a regulated market.
LIQUIDITY RISK	Yes, thanks to the often small volumes traded on the secondary market
INTEREST RATE RISK	Yes, depending on the option’s term and structure
REINVESTMENT RISK	Yes
FISCAL RISK	Limited
MARKET RISK	Yes
INFLATION RISK	Limited
GEOGRAPHICAL RISK	Yes
COMPLEXITY RISK (MiFID)	Yes

#### SPECIFIC RISKS

##### Leverage risk

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

##### Counterparty risk

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

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

#### HYPOTHETICAL SCENARIOS

This section describes a number of hypothetical positive/negative performance scenarios for an investor holding a long option. These scenarios are purely notional for the purposes of illustrating the mechanics of the investment; these scenarios will not necessarily occur for any investments that the investor decides to make.

##### • Positive Scenario # 1

On 31 December 2020, the investor buys a call option with a premium of €10; the option entitles the investor to buy a share in the company AB InBev at the price of €70 upon maturity (31 December 2022). The investor decides to keep the option until its expiry.

On 31 December 2022, the AB InBev share is listed at €90. The investor had cancelled the auto-sell option and did not close the position. Keytrade Bank exercises its option and the customer immediately sells the share on the market for a capital gain of €20 (excluding the premium). If you include the price that the investor paid for buying the option, the capital gain is €10.

<sup>5</sup> - If the strike price is lower than the underlying security's price for a call (higher than the underlying security's price for a put).

• Negative Scenario #1

On 31 December 2020, the investor buys a call option with a premium of €10; the option entitles the investor to buy a share in the company AB InBev at the price of €70 upon maturity (31 December 2022). The investor decides to keep the option until its expiry.

On 31 December 2022, the AB InBev share is listed at €60. The option expires worthless and the investor loses the €10 premium.

**2.6.1.2. WARRANTS**

A warrant can be compared to an option (see 2.6.1.1). It confers the right to buy (call warrant) or to sell (put warrant) the underlying security during a defined period for a predefined price (strike price).

Such an underlying value can be a share, an index, a currency or a commodity.

While the majority of warrants that you find on the market are covered warrants, there are also non-covered warrants.

A non-covered warrant is issued by a listed company and allows the bearer of the warrant to acquire additional shares at a fixed price, during a certain period. A non-covered warrant expires worthless if no action is taken by the investor to exercise the warrant.

A covered warrant, on the other hand, is issued by a financial institution and exercise is only possible at expiration (European style). Such exercise of a covered warrant at expiry is automatic and always cash settled, and therefore does not obtain the underlying value.

A warrant, both covered and uncovered, is labelled "in the money" if the strike price is inferior to the price of the underlying value in case of a warrant call. A warrant put is "in the money" when the price of the underlying value is inferior to the strike price.

**GENERAL RISKS**

PRICE RISKS	Yes, the warrant may lose its entire value, depending on changes in the underlying security, which may be influenced by favourable or unfavourable market conditions.
EXCHANGE RATE RISK	Yes, if not denominated in euros.
CREDIT RISK	None for transactions on a regulated market (or equivalent). For OTC transactions, the risk will be determined by the counterparty's creditworthiness
LIQUIDITY RISK	Yes, thanks to the often small volumes traded on the secondary market.
INTEREST RATE RISK	Yes, depending on the warrant's term and structure.
REINVESTMENT RISK	Yes
FISCAL RISK	Limited
MARKET RISK	Yes
INFLATION RISK	Limited
GEOGRAPHICAL RISK	Yes
COMPLEXITY RISK (MiFID)	Yes

**SPECIFIC RISKS**

**Leverage risk**

Because of the leveraging, trading warrants is much more risky than direct investment in the underlying security. The specific risks of a warrant are comparable to those of buying options. That means that you can lose the whole of the invested amount (including transaction costs).

**Specific warrant risks**

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

**HYPOTHETICAL SCENARIOS**

See options. The same mechanisms apply, but securities are not supplied for warrants. Warrants are always cleared in cash.

### 2.6.1.3. TURBOS®

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

With **Turbos**, thanks to leveraging, you can make quick profits from increases (e.g. long Turbos) or falls (e.g. short Turbos) in the value of underlying securities, such as indices, shares, commodities and bonds, with a multiplier effect. Only a fraction of the underlying value is included in the price of these products: the rest is financed by the issuer (this component is referred to as the «financing level»). The differences between these products are so minor that we will restrict ourselves to describing the Turbo.

Unlike options (see point 2.6.1.1.), Turbos have no maturity date and a «stop loss» level<sup>6</sup>.

If the underlying security reaches or passes that level, the Turbo is automatically settled and any remaining value is paid out to the investor. The stop loss level is a mechanism that ensures that you can never lose more than the amount that you invested. A Turbo long is closed out if the underlying security falls below the stop loss level. A Turbo short is closed out if the underlying security rises above the stop loss level.

• Example 1: Leveraging

Underlying security = €100; financing level = €75;

your own contribution to the Turbo's value in this case is €25. The leveraging of the Turbo is 4; or  $100 / (100 - 75) = 4$ .

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

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

• Example 2: Residual value

Underlying security = €100; Financing level = €75.

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

#### GENERAL RISKS

PRICE RISKS	Yes, depending on the value of the underlying assets, which may change as a result of favourable or unfavourable market conditions.
EXCHANGE RATE RISK	Yes, if the underlying security is not denominated in euros.
CREDIT RISK	Limited
LIQUIDITY RISK	Yes
INTEREST RATE RISK	Yes, depending on the Turbo's structure
REINVESTMENT RISK	Yes
FISCAL RISK	Limited
MARKET RISK	Yes
INFLATION RISK	Limited
GEOGRAPHICAL RISK	Yes
COMPLEXITY RISK (MiFID)	Yes

#### SPECIFIC TURBO-RELATED RISKS

##### Liquidation risk

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

<sup>6</sup>- There are also closed-ended Turbos with a fixed maturity date. They have much greater leveraging.

### Specific risks related to Turbos and similar products

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

#### HYPOTHETICAL SCENARIOS

See examples above

### 2.6.1.4. STRUCTURED PRODUCTS

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

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

#### GENERAL RISKS

PRICE RISKS	Yes, particularly if the investor sells before maturity, and depending on the value of the underlying assets, which may change as a result of favourable or unfavourable market conditions.
EXCHANGE RATE RISK	Yes, if not denominated in euros.
CREDIT RISK	Yes, depending on the issuer
LIQUIDITY RISK	Yes, given that a secondary market is generally not structured to trade in these products.
INTEREST RATE RISK	Yes, depending on the structure's composition (higher for structures with fixed-interest-rate assets).
REINVESTMENT RISK	Yes
FISCAL RISK	Yes
MARKET RISK	Yes
INFLATION RISK	Yes
GEOGRAPHICAL RISK	Yes
COMPLEXITY RISK (MIFID)	Yes

#### SPECIFIC RISKS

##### Early redemption risk

Under certain circumstances, the issuer may decide to redeem the product early, particularly should there be a fall in interest rates on the market.

This can have an adverse effect on returns.

##### Insolvency risk

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

##### Risks of specific structured products

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

## 2.6.2. Derivative financial instruments with the risk of losses greater than the capital invested

### 2.6.2.1 SHORT OPTIONS

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

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

For the purchase of options, see 2.6.1.1. Long options.

As the writer, you may be required at any time to supply or to buy the underlying security. In principle, you will also be instructed by the counterparty if the option that you have issued is «in the money»<sup>7</sup> on the maturity date. This obligation expires if the counterparty does not exercise their right. You may be able to avoid the security allocation and the costs associated with it arising from your short position by buying back (closing purchase) the short option. However, you should bear in mind that you might still be instructed by the counterparty on the closing-purchase date. For more details, please refer to the relevant transaction rules at [www.keytradebank.be](http://www.keytradebank.be).

#### GENERAL RISKS

PRICE RISKS	Yes, should a put option be issued, the maximum risk is the strike price for the option. Should a call option be issued, there is, in theory, unlimited risk.
EXCHANGE RATE RISK	Yes, if not denominated in euros.
CREDIT RISK	None for transactions on a regulated market or equivalent to a regulated market.
LIQUIDITY RISK	Yes
INTEREST RATE RISK	Yes, depending on the option's term and structure.
REINVESTMENT RISK	Limitéed
FISCAL RISK	Limited
MARKET RISK	Yes
INFLATION RISK	Limited
GEOGRAPHICAL RISK	Yes
COMPLEXITY RISK (MIFID)	Yes

#### SPECIFIC RISKS

##### Leverage risk

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

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

As the writer of a put option, your maximum risk is the strike price of the option, plus the transaction costs. The underlying securities may have become worthless while you may be required to buy them at a higher price.

As for the call options, you can limit your losses by closing your option position before you have to buy the underlying shares. Of course, to close your position you need to pay a premium and transaction costs.

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

##### Margin obligations.

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

##### Shortfall procedure

If at any time, the commitments entered into by you are greater than the balance of your trading account, the shortfall procedure will be initiated (higher than the price of the underlying in the case of a put). You are obliged to fulfil your margin obligation within five (5) Euronext trading days by transferring funds into your trading account, by selling investments (through a telephone order) or by closing option positions until the margin shortfall is cleared. If after five Euronext Brussels trading days your trading account still shows a shortfall, Keytrade Bank may close some

<sup>7</sup>- If the strike price is lower than the underlying security's price for a call (higher than the underlying security's price for a put).

or all of your open positions or arbitrarily sell some of the assets on your account to settle the shortfall. Keytrade Bank is also entitled to raise the level of the margin obligation.

### HYPOTHETICAL SCENARIOS

This section describes a number of hypothetical positive/negative performance scenarios for an investor holding a long option. These scenarios are purely notional for the purposes of illustrating the mechanics of the investment; these scenarios will not necessarily occur for any investments that the investor decides to make.

- Positive Scenario #1

On 31 December 2025, the investor sells a call option with a premium of €10; the option entitles the investor to buy a share in the company AB InBev at a price of €70 upon maturity (31 December 2027).

On 31 December 2025, the AB InBev share is listed at €60. The option expires worthless and the investor retains the €10 premium.

- Negative Scenario #1

On 31 December 2025, the investor sells a call option with a premium of €10; the option entitles the investor to buy a share in the company AB InBev at a price of €70 upon maturity (31 December 2027).

On 31 December 2027, the AB InBev share is listed at €90 and the option buyer exercises their right. The investor is instructed and must supply the asset. They supply it at a price of €90. The investor loses €10 on the transaction (premium included).

- Negative Scenario #2

On 31 December 2025, the investor sells a call option with a premium of €10; the option entitles the investor to buy a share in the company AB InBev at a price of €70 upon maturity (31 December 2027).

A few weeks later, the company announces better-than-expected results and the share price rises to €90; the investor receives a margin call from the bank to hedge their short position.

The investor is unable to provide liquidity within the statutory timeframe and the bank closes the position automatically and sells the investor's assets in the portfolio in order to fulfil the margin call.

The investor's final loss is larger than the premium that they invested in the option.