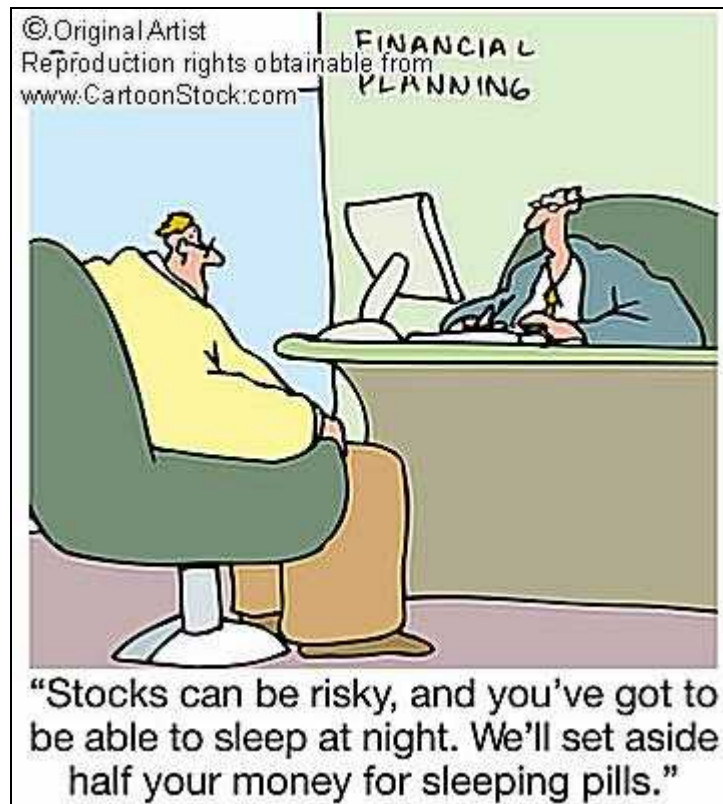


“Structure Your Investments with Structured Products”



BY GIA SINGH

The recent recession fears in the US have left many investors both foreign and local in a state of worry. Stock markets around the world have felt the brunt of the housing crisis and subsequent credit crunch and while the local market has not shown much reaction, it still remains a real possibility. Investors have once again lost confidence in the equity markets and seek safe havens for their hard earned money. While this behavior is mainly driven on emotion, it is quite common, as the investor ignores all the principles of long term equity investing in the noise and confusion. Nevertheless, one thing is for sure, there is no need to resort to hiding your money under your mattress!!!

The natural and most common strategy that investors would take when they become less risk tolerant is to restructure their portfolios accordingly. So for instance, an investor who may have been in an Aggressive Portfolio (**90 per cent Equity; 10 per cent Fixed Income**) may restructure assets so that the Portfolio may become Balanced (**60 per cent Equity; 40 per cent Fixed Income**) or he may have become so risk adverse that he may seek to hold a Conservative Portfolio (**32 per cent Equity; 68 per cent Fixed Income**). While the above example would have the desired effect of mitigating risk, one must be reminded that the lesser the risk the lesser the return!

However, the above example is not the only investment solution to dealing with low risk tolerance. Thus, I would like to use this article to introduce you, if you have not been already, to a sophisticated investment vehicle known as Structured Products. These products are prepackaged investment vehicles designed to meet specified risk-return needs which cannot be met from standardized financial instruments in the markets. Returns are generally linked to the

performance of a benchmark or underlying asset such as interest rates, equity markets, commodities or even foreign exchange markets. However, one of the main benefits or attractive features of structured products is their ability to offer the investor either full or partial principal protection. Also, it is important to note that Structured Products can be designed for any risk profile, that is, products can also be structured for the Aggressive Investor who is very risk tolerant. Thus, these products can be incorporated into your asset allocation mix to ensure portfolio diversification.

Indeed, as the name implies, Structured Products are designed to specifically target the needs of investors in terms of their individual risk profiles, return requirements and market expectations. Generally, they are created through the use of derivatives and other financial instruments which have significant risk/return and or cost saving structures that may not be achievable with other standardized investments in the marketplace.

These products were originally popular in Europe but have become quite the trend in the US. Various products are offered by well established Investment Banks worldwide, such as Morgan Stanley, UBS Investment Bank and JP Morgan Chase to name a few. An example of a Structured Product offered by UBS Investment Bank which provides long term equity exposure with principal protection is the UBS Principal Protected Note which is tied to the S&P 500 Index. This is suitable for an investor who seeks long-term exposure to the U.S. equity market with limited downside risk. Such an investment provides for a degree of S&P 500 exposure over the term (typically four to seven years), while offering full principal protection at maturity. It may be used in planning to meet future obligations (such as retirement or college), or to lock in gains from the sale of equities and maintain some market exposure.

Example:
UBS Principal Protected Notes
For longer-term equity exposure with principal protection

Term	5 years	Outcomes at Maturity		
Index	S&P 500 Index	S&P 500 Return		Note Return
Payment at Maturity	Full principal investment plus 75% of any S&P 500 appreciation	60%	60% Return x 75% Participation Rate	45%
Market Participation		20%	20% Return x 75% Participation Rate	15%
Principal Protection	100%	-60%	Full principal protection for any Index decline	0%

The options available with Structured Products are endless and can become very complex in nature, which is beyond the scope of this article. However, as with any other financial decision one must always be aware of the risks or disadvantages involved. The most common risk with this type of investment vehicle is the fact that there is a lack of liquidity since products can be highly customized to suit individual needs. Notwithstanding, investments in structured products are more of a buy and hold investment decision since returns are mostly realized at maturity, thus liquidity should not really be an issue.

Also, holders of Structured Products should ensure that they carry out proper due diligence on the issuer of the product to ensure credit quality. This is because products are the legal liability of the issuing financial institution and not the underlying benchmark or asset. This should not really be a major problem since as mentioned previously, some of the world's leading financial institutions issue these products.

Also, consideration should be given to pricing transparency as there is no standard for pricing. Thus it is harder to compare the net-of-pricing attractiveness of alternative structured products offerings than it is, for instance, to compare the net expense ratios of different mutual funds or commissions among broker-dealers. Many structured products issuers work the pricing into their option models so that there is no explicit fee or other expense to the investor. This may also be seen negatively since the investor is unaware of the implicit costs.

It is without a doubt, that Structured Products can now offer the individual investor the opportunity to invest in what was once primarily institutional ground. These products can be an attractive addition to portfolios as they have the unique flexibility to meet specific objectives. Additionally, Structured Products allow investors to protect their principal in highly volatile markets or allow them to profit in the flattest of markets.

So forget the sleeping pills!!! Instead, contact your investment advisor today and find a Structured Product that is tailored to meet your financial goals.

Information sourced from:
The Structured Products Association
UBS Investment Bank
Investopedia & Wikipedia

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