

# Structured Products: Build in Downside Protection



Our GraySwan investment team has continuously been researching various structured product options to complement our clients' traditional offshore equity and commodity investment portfolio holdings.

We have a dynamic menu of such products which our team has already approved via their robust research process and which is updated every month. In addition, we now have the capability to tailor-make structured products for our clients which have very specific needs.

Structured products are pre-packaged fixed-term investments that provide private investors with easy access to offshore equity and commodity markets, with a pre-defined risk and return profile over a pre-defined investment period. We believe these products should be considered by most investors as they provide downside protection with adequate upside participation.

In the past, it was necessary to rely on third-party providers which offer these products on an ad-hoc basis. We found that most of the products were not suited for our clients and the infrequency of access to those products which was fit for purpose was also not ideal.

*Our investment team found a solution to pro-actively and continuously offer structured products for our clients. Via a world-class offshore trading platform, we now provide access to bespoke structured products tailored to our clients' specific needs. But more on that later...*

Market uncertainty remains high after the unpredictable year of 2022 followed by a very strong equity market recovery over the past month. Timing equity market exposure is challenging, and political and economic uncertainty only adds to the difficulty. We believe, optimally constructed offshore structured products are an appealing investment option as they reduce the risk of market timing and can provide partial or full capital protection, allowing investors to obtain exposure to equities and commodities in a risk-controlled manner.

## MORE ABOUT STRUCTURED PRODUCTS

Structured products typically have a term ranging from three to five years, although shorter or longer terms are also possible. Tax implications will vary depending on the term of the investment, with capital gains tax applying unless the investor surrenders early, in which case it may be taxed as income.

The issuer of structured products uses asset classes such as equities, bonds, and derivatives to structure the performance and risk profile for the investor, also known as the risk return payoff profile. This risk return payoff profile refers to the balance between downside protection and upside participation. Structured products are offered in both offshore and local currencies, linked to offshore assets.

For conservative investors, a higher level of capital protection with a corresponding lower participation in the upside of the markets may be most suitable, while more aggressive investors may prefer less capital protection and a higher level of growth participation, with the possibility of leveraged returns.



## WRAPPERS

Structured products can be invested through vehicles such as sinking funds or endowments, which provide tax and estate duty benefits, including:

- Investment income and capital gains tax paid within the investment, on behalf of the investor, at a capped, effective Income Tax rate of 30% and Capital Gains Tax (CGT) rate of 12% respectively.
- Beneficiary nominations avoid the complications of potential offshore inheritance tax and executors' fees, although the value will still form part of the investor's South African estate for estate duty purposes.
- In a life wrapper, the value is protected from creditors after the investment's first three years have passed.

## POTENTIAL RISKS

Investing in structured products comes with the following risks:

- Counterparty / Credit risk, which refers to the financial institution's ability to keep its promise of guarantee, capital protection, or enhanced return at the maturity of the structured product. Such risk can however be managed via a collateralised product option if the investor do not wish to be exposed to counterparty / credit risk.
- Liquidity risk, as most structured products are designed for a specific period, and full benefits can only be realized if the investor stays invested until maturity.
- Structured products do not pay dividends.

## AVAILABLE OPTIONS THROUGH GRAYSWAN

As previously noted, we have traditionally relied on various investment platforms and structured product providers to offer structured products throughout the year. Our investment team would then conduct analyses of these products before determining which of these products meet our due diligence and investment criteria after which our financial advisors will discuss such with our clients if and where they meet the performance objectives and risk budget of each client.

While we will continue to utilize these external products in the future, we now also have the capability to pro-actively construct tailor-made structured products for our clients. In this regard, we have established a partnership with a Swiss-based platform with an investment grade credit rating which is three levels higher than South Africa's top-rated banks.

We have the flexibility to select any level of capital protection, along with a guaranteed or non-guaranteed investment return, linked to a specific underlying offshore asset. The range of options available is extensive and includes various indices, instruments (i.e. Exchange Traded Funds and Actively Managed Funds), single stocks, or a combination thereof.



We have recently also started utilizing these structured products within our GraySwan \$ Megatrend Global Equity Exchange Traded Note (ETN) and our GraySwan \$ Megatrend Commodities for Change ETN, enhancing our diversification and providing a level of capital protection within these ETN's.

For illustration purposes, examples of these products include outperformance certificates, bonus certificates, and capital protection certificates. The tables below display the final value of the underlying offshore asset on the left, at the end of the investment period (which is three years for all of these examples), versus the final redemption value for the investor:

### Example 1: Outperformance Certificates

This certificate offers a 200% participation in the positive performance of the underlying offshore asset. The performance is capped at 125.11% of the initial level. This means that even if the underlying offshore asset returns more than 25.11% during the investment term, the investor's maximum return would be 50.22% (25.11% return x 200% participation).

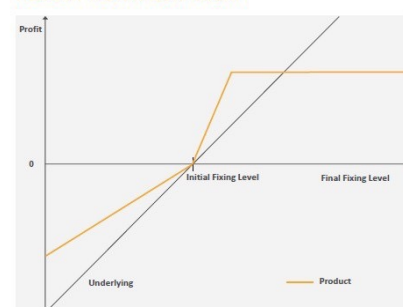
On the downside there is only a 50% participation, meaning that if the underlying offshore asset loses 10%, the investor only loses 5%, etc.

#### REDEMPTION AT MATURITY

FINAL LEVEL OF THE UNDERLYING	FINAL REDEMPTION
140%	150.22%
130%	150.22%
120%	140.00%
110%	120.00%
100%	100.00%
90%	95.00%
80%	90.00%
70%	85.00%
60%	80.00%
50%	75.00%
40%	70.00%
30%	65.00%
20%	60.00%
10%	55.00%
0%	50.00%

Source: LEONTEQ 2023

#### REDEMPTION MECHANISM



Source: LEONTEQ 2023  
This generic chart is for illustration purposes only - the actual payoff profile of the Product may differ.

\*Please note that these examples are based on a very specific set of underlying offshore assets and other factors to create these specific pay-off profiles.



## Example 2: Bonus Certificates

This bonus certificate offers a bonus level of 120% if the underlying offshore asset closes above the barrier level of 54% at maturity. Thus, at the end of the investment term, the underlying offshore asset could have lost up to 46% in value, and the investor will still earn a cumulative 20% investment growth. Also, on the flip side, if the underlying offshore asset grows by 20% or more, the investor's maximum possible return is capped at 20%.

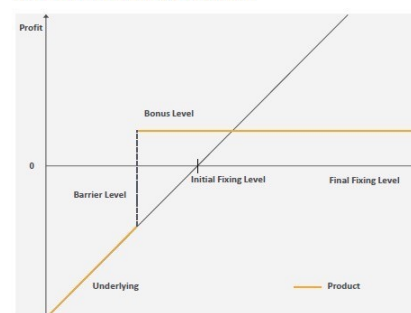
If the asset loses more than 46% (thus crossing the barrier level of 54% of the initial value), the investor will partake in the full loss.

### REDEMPTION AT MATURITY

FINAL LEVEL OF THE UNDERLYING	FINAL REDEMPTION
160%	120%
150%	120%
140%	120%
130%	120%
120%	120%
110%	120%
100%	120%
90%	120%
80%	120%
70%	120%
60%	120%
50%	50%
40%	40%

Source: LEONTEQ 2023

### REDEMPTION MECHANISM



Source: LEONTEQ 2023

This generic chart is for illustration purposes only - the actual payoff profile of the Product may differ.

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### Example 3: Capital Protected Certificates

The capital protected certificate offers a 122.89% participation in the positive performance of the underlying offshore asset, where the performance is capped at 130% of the initial level. This means that should the underlying offshore asset return, for example, 20% at maturity, the investor will earn 24.58% (20% x 122.89% participation).

The return is however, capped at 30%, meaning that if the underlying offshore asset returns 30% or more, the investor's maximum possible return is capped at 36.87% (30% return x 122.89% participation).

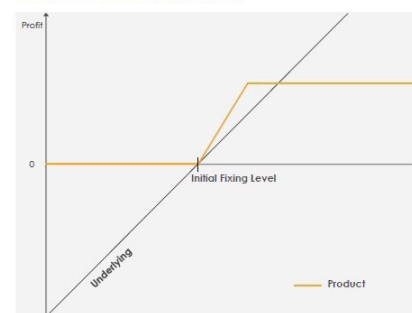
The capital is also fully protected, no matter how much value the underlying asset loses over the investment term.

#### REDEMPTION AT MATURITY

FINAL LEVEL OF THE UNDERLYING	FINAL REDEMPTION
180%	136.87%
170%	136.87%
160%	136.87%
150%	136.87%
140%	136.87%
130%	136.87%
120%	124.58%
110%	112.29%
100%	100.00%
90%	100.00%
80%	100.00%
70%	100.00%
60%	100.00%
50%	100.00%

Source: LEONTEQ 2023

#### REDEMPTION MECHANISM



Source: LEONTEQ 2023  
This generic chart is for illustration purposes only - the actual payoff profile of the Product may differ.

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### COST & FEES

Costs and fees are fully priced into each structured product. The issuer of the product embeds their cost within the pay-off profile. Therefore, the promise made by the issuer is already net of their cost. Other costs such as the implementation and monitoring fee is disclosed upfront to the investor.

As with any investment product, we will ensure that all fees payable will always be disclosed upfront to any investor.



## MINIMUM INVESTMENT

The minimum investment to invest in any of our tailor-made offshore structured products is \$25 000. Such minimum has been set as we typically recommend clients to invest offshore via tax efficient life wrappers and such minimum is also \$25 000.

If and where clients' monies are not yet in foreign currency can we assist with the foreign exchange conversion at low institutional rather than retail rates.

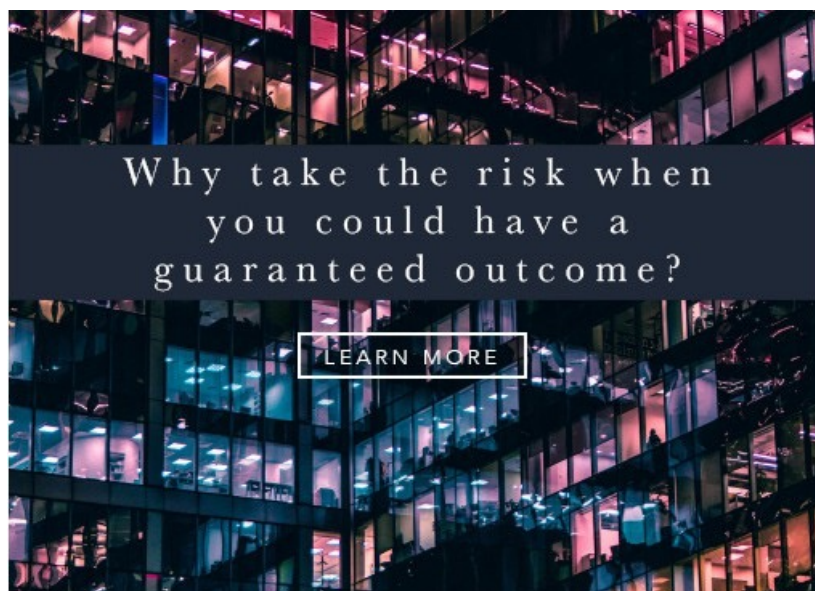
## CONCLUSION

Structured products can be designed to form part of any well-balanced and diversified investment portfolio.

During uncertain times capital protection of any kind is a sought-after benefit. This, coupled with the possibility of an enhanced investment return, is an attractive combination.

Our investment team not only continuously analyses the various structured products available in the market but we now also structure such products ourselves via an offshore investment platform. Our investment team has constructed a menu of various offshore structured products which are fit for most investors. Our financial advisors then pro-actively advises our clients to consider such if they find any option on the menu suitable to their risk profile and performance objectives.

Our ability to analyse and research the various structured products as offered by the market as well as our own ability to tailor-make such product options, provides our clients with the freedom of choice.



## The GraySwan Structured Product Range

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# Sleep Well At Night



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