FEATURE-Banks pitch structured equity at Asia retail market

By Saeed Azhar
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SINGAPORE, Nov 22 (Reuters) - Office secretary Jessie Tan plunked down S$5000 in May to buy a "Triple Happiness" structured fund that pays a fixed interest rate and guarantees her capital.

"I only want my capital to be protected," 52-year-old Tan told Reuters. "I didn't even ask how much I would lose or win."

The fund charges a 3 percent upfront fee, and some critics warn investors should think twice before putting money into such funds. Many of these products come at a cost, such as high fees, expensive hedging techniques and reduced overall returns.

"As always in finance, there is no such thing as a free lunch, and capital protection does come at a price," said Claudia Zeisberger, a finance professor at the INSEAD business school in Singapore.

"As long as investors understand it and accept it, it's fine." The market for these so-called structured products is flourishing in Asia, with estimates starting at about US$40 billion.

Dominated in Asia by Societe Generale , UBS , Citigroup and Merrill Lynch , the business took off after global short-term interest rates started falling in 2001.

This prompted greater interest from retail investors, and bankers say growth in Asia -- at 20 to 25 percent a year -- has been faster than in Europe and the United States.

"Consumer banks have a huge number of clients who are hungry for yields and investment banks have the capability to deliver that," said Christopher Lee, a managing director for equity risk management at Swiss bank UBS in Hong Kong.

UBS sold $12 billion worth of equity structured products in Asia, excluding Japan in 2005, and its Asian business has doubled since 2003, Lee said.

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Merrill Lynch recently launched a U.S. dollar fund that shows the benefits and pitfalls of structured products. The U.S. dollar notes, which mature after a period of three years and 11 months, provide investors with a fixed 6 percent coupon for the first six months and a variable coupon depending on the price of a basket of eight global blue-chip shares.

If the share basket trades above 90 percent of its initial price every day of the year, an investor could earn a total return of up to 12 percent, including the 6 percent coupon, said Gary Hung, who heads the Hong Kong and Singapore retail equity structured business for Merrill, said that

But if the shares traded below that threshold, investors would see no return, although their capital would be protected.

Few banks disclose how much money they make from these products. One reason is that they can't be sure.

Nicolas Reille, who heads Asian equity structured products for Societe Generale in Asia-Pacific excluding Japan, said banks can only evaluate profitability when the position is closed.

"We are taking views on volatility, correlation and dividend and are managing the risk. We would know whether the operation has been profitable or not only on the maturity, once the position is closed," he said.

RISKS

For investors, it's hard to know the embedded charges.

"Most of these transactions are structured in a complex way so it is not easy to know the fees because they are very tailor made," said Marjan van der Weijden, senior director for global structured finance at Fitch Ratings agency.

She said the profit could come from the bid and ask spread in the case of a simple derivative product, or a distribution fee in the case of a note, or from the inclusion of options and hedging.

Banks need to give more information about the fees involved, she said, adding that might happen as the market evolves and the products become more mainstream.

If investors cannot evaluate the risk behind structured products, they should not buy them, said David Webb, a Hong Kong-based corporate governance advocate and former investment banker,

Investors also need to realise that an economic downturn or spike in interest rates would probably hit structured products, said INSEAD's Zeisberger.

"I am convinced that investors will be quite surprised to see the non-performance of their products, once market volatility starts to increase, interest rates start to rise and credit risk starts to become more expensive," she said.

But as far as investors like Jessie Tan are concerned, guaranteeing capital is paramount.

Her fund, sold by Singapore's DBS Bank , matures after four years and 11 months. It offers a fixed coupon of around 6.5 percent for the first six months, and after that returns linked to the performance of eight underlying stock indices.

"I want my money to be safe," she said.

($1=7.786 Hong Kong Dollar)

($1=1.584 Singapore Dollar)

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