An Overview of Structured Products

KEY TAKEAWAYS

- Structured notes and CDs enable investors to pursue a defined investment outcome, gain exposure to an asset class, or hedge existing positions.

Structured products are financial instruments that enable investors to pursue a specific objective or express a market view. These instruments have been a key feature of the international finance markets for many years and are gaining ground with U.S. investors seeking a flexible alternative to the essential components of a diversified financial portfolio.

Structured products combine a debt instrument, such as a bond or certificate of deposit, with one or more derivative instruments linked to an underlying asset class or "reference asset," such as equities, commodities, currencies, or interest rates. The returns are based on a specific formula that can be tailored to a particular market outlook or view. Key features such as capital protection, enhanced upside participation, and yield enhancement make structured products a valuable tool for reducing risk and increasing returns for all types of investors.

DIFFERENT OUTCOME-FOCUSED STRATEGIES

Thanks to the growing number of reference assets (indices, exchange traded funds, etc.), and the variety of derivative strategies available, structured products can be adapted to any market situation. Structured products typically fall into one of four categories along the risk-return spectrum, from capital protection to enhanced participation (See Exhibit 1).

Exhibit 1: Risk-Return Spectrum of Structured Product Opportunities

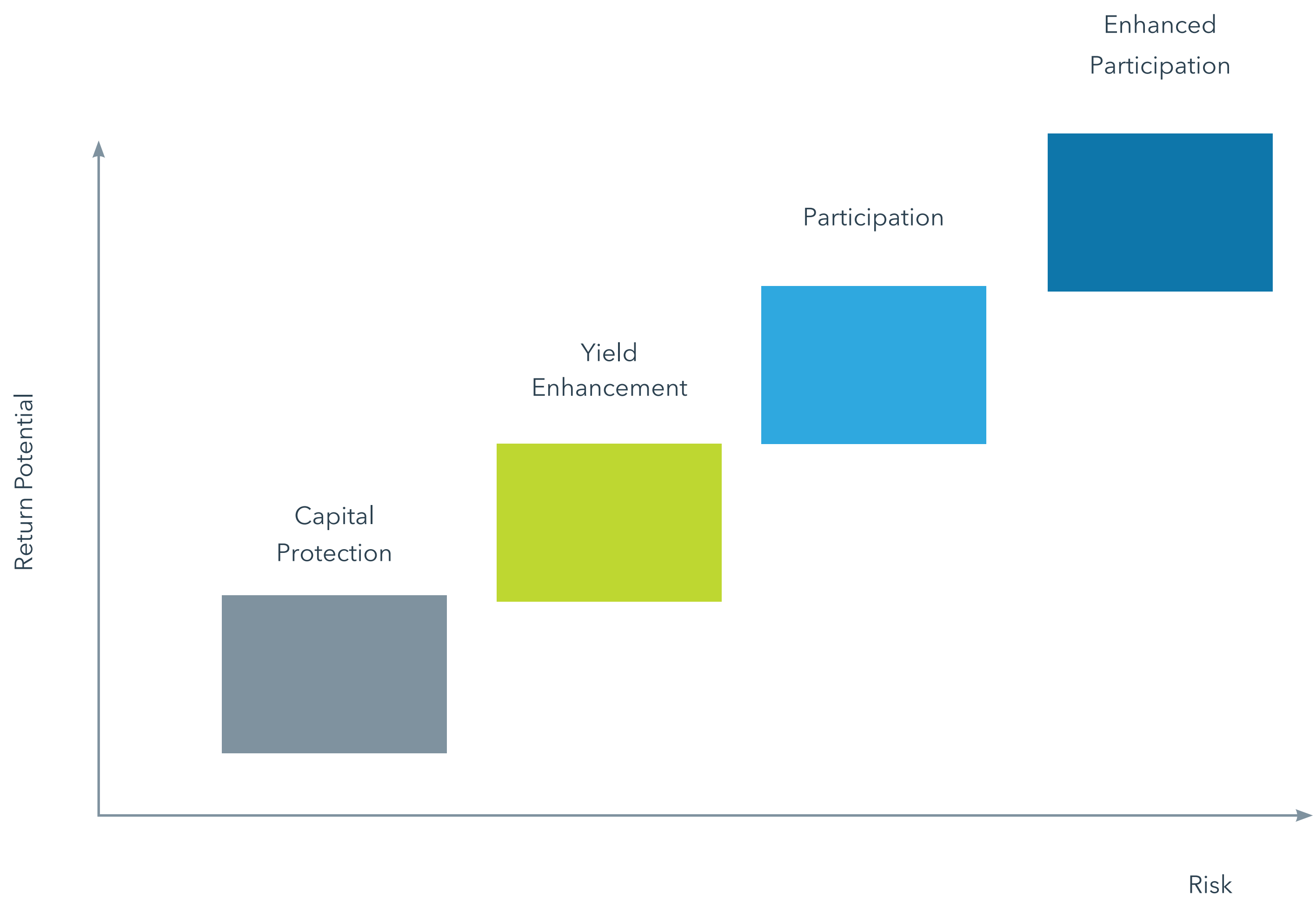
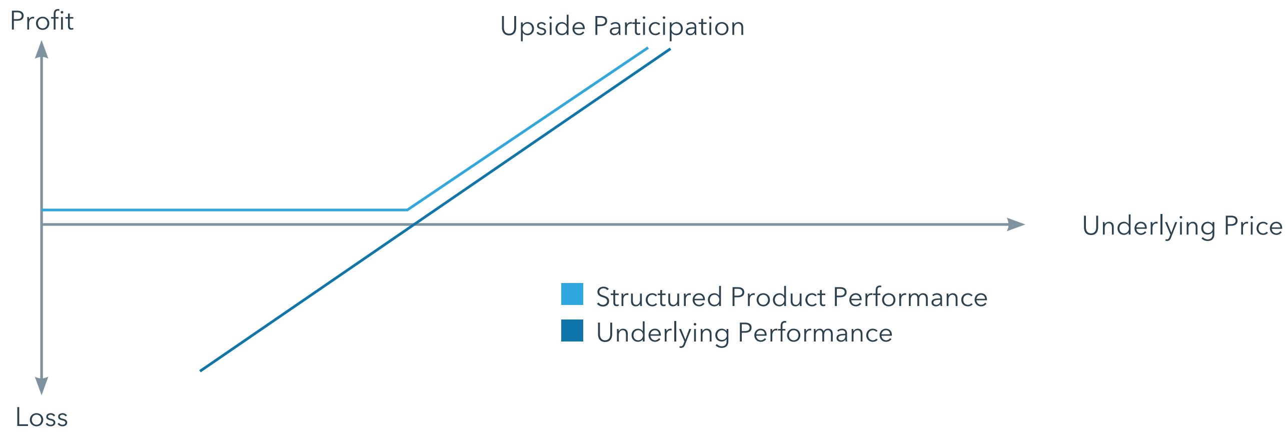


Diagram is for illustrative purposes only.

Exhibit 2: Capital Protection



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CAPITAL PROTECTION: UPSIDE PARTICIPATION WITH DOWNSIDE PROTECTION

Capital protected instruments come in two forms: market-linked notes, which are a type of bond with a senior unsecured credit profile, or FDIC-insured certificates of deposit (CDs). In both instances, protection instruments provide investors with the opportunity to benefit from the performance of the reference asset while protecting their invested capital at maturity (See Exhibit 2).

The return of principal is subject to the credit risk of the issuer and FDIC insurance limits, if applicable.

YIELD ENHANCEMENT: FIXED COUPON WITH SOME DOWNSIDE PROTECTION

Yield enhancement instruments allow investors to benefit from rangebound markets by combining conditional downside protection to a barrier level with partial upside participation via a fixed coupon that typically yields more than the standard interest rate market. If the reference asset declines beyond the established barrier level, the investor is fully exposed to the negative performance of the underlying asset, just as they would be with a direct investment (See Exhibit 3). Yield enhancement products can use multiple reference assets to optimize the coupon rate and barrier level of protection.

Exhibit 3: Enhanced Yield (Barrier)

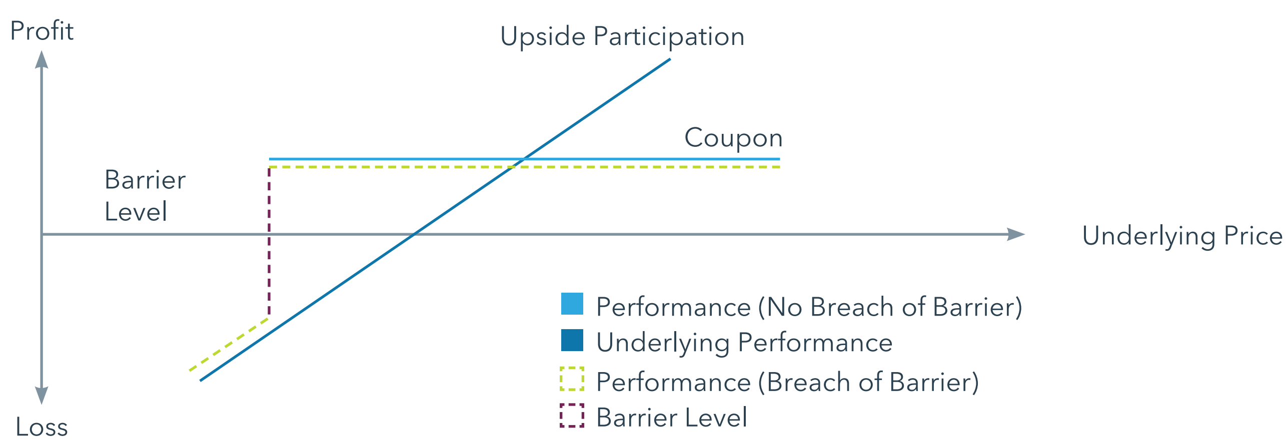

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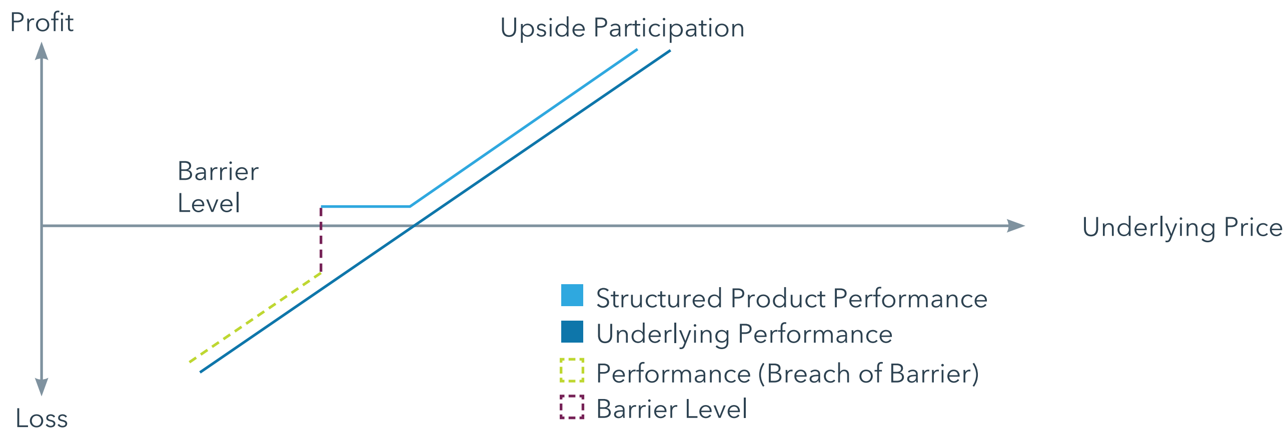
Exhibit 4: Barrier Participation



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PARTICIPATION: ACCESS TO AN ASSET'S RETURNS WITHOUT DIRECT EXPOSURE

Participation strategies provide access to the returns of a sector, assets class, or investment strategy that may be difficult to gain exposure to, or that is deemed too volatile to include in the portfolio as a direct investment. The payoff attempts to mirror the performance of the underlying asset(s) while providing investors a predetermined level of protection against declines. The downside protection is offered through either a barrier level (See Exhibit 4), similar to yield enhancement notes, or a buffer, which is also known as first-loss protection (See Exhibit 5). In the case of a 10% buffer, for example, the investor is protected from the first 10% of losses. Investments may be classified as long-term capital gains or losses for tax purposes if held for more than one year.

ENHANCED PARTICIPATION: AMPLIFIED UPSIDE PARTICIPATION WITH SOME DOWNSIDE PROTECTION

Enhanced participation notes amplify an investor's participation in the price appreciation of a reference asset without incurring leverage to the downside. Typically, the performance of these instruments is subject to a predefined maximum return level and incorporates a degree of protection at maturity against market declines through the use a buffer or a barrier (See Exhibits 6 and 7). Investments may be classified as long-term capital gains or losses for tax purposes if held for more than one year.

Exhibit 5: Buffered Participation

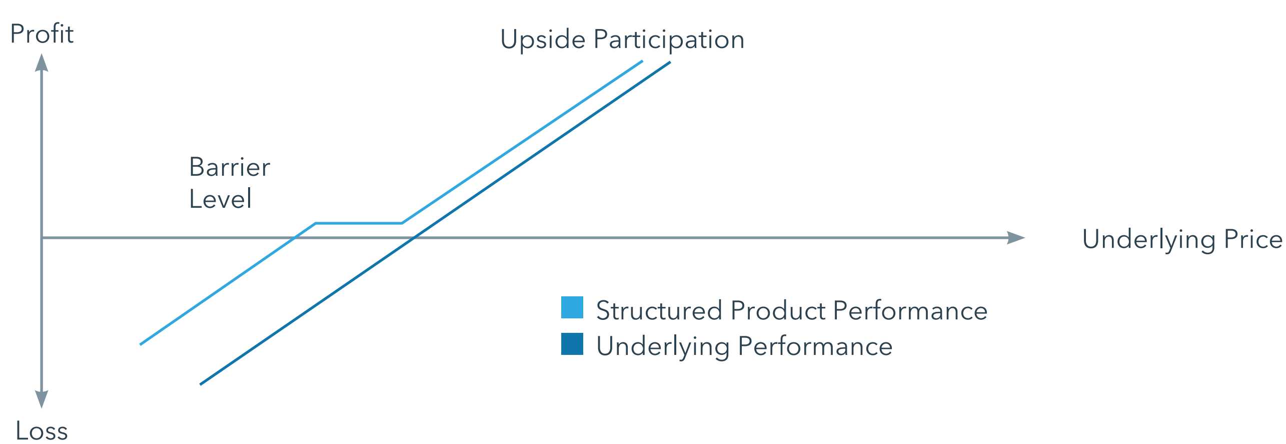

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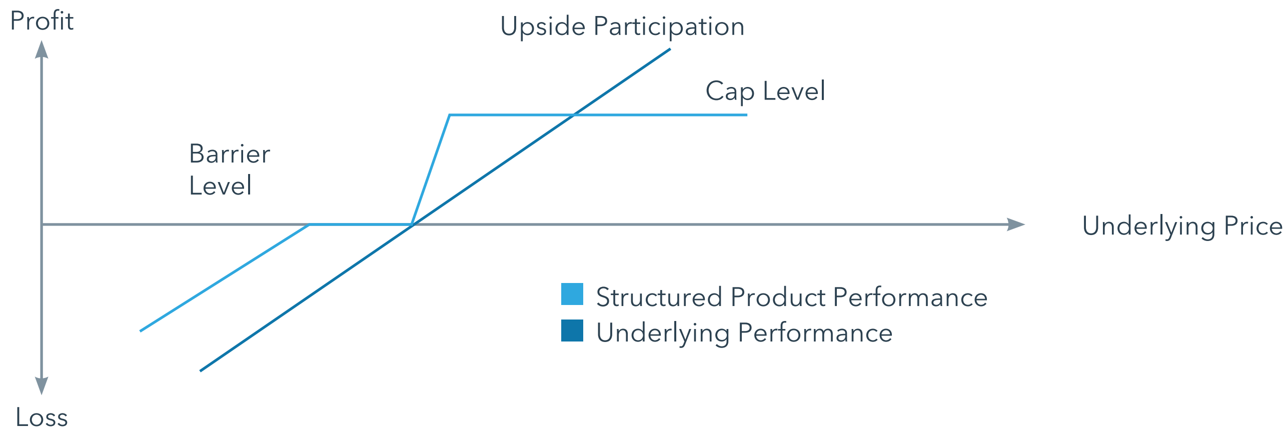
Exhibit 6: Enhanced Participation (Buffered)



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HOW STRUCTURED NOTES FIT INTO AN INVESTOR PORTFOLIO

Selectively incorporating structured products into portfolios can help investors meet their financial goals, whether they seek to pursue a defined investment outcome, gain exposure to an asset class, or hedge existing positions.

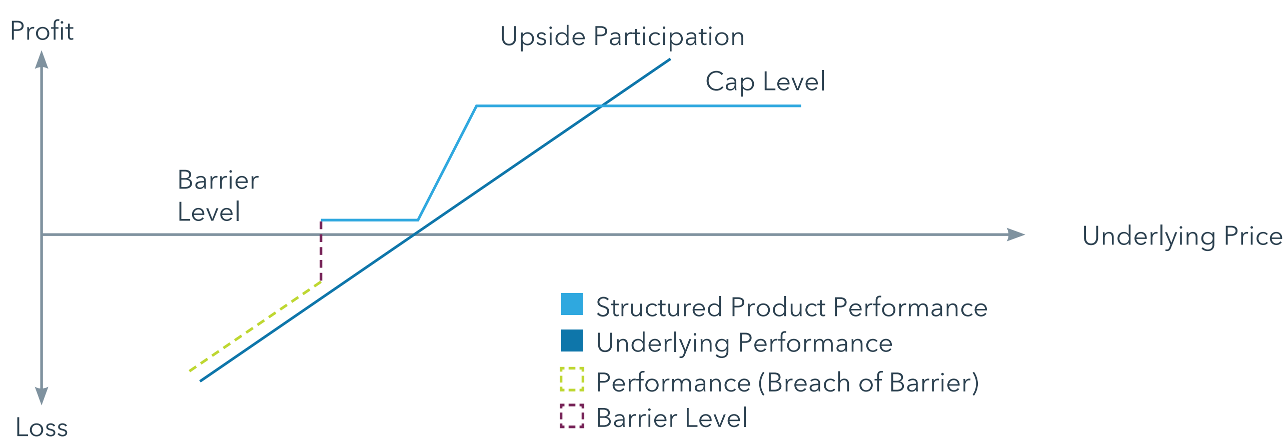
Structured products should be considered an extension of an investor's existing investment strategy, complementing the asset mix and providing greater portfolio diversification. For example, enhanced yield and enhanced return products may work well within the fixed income and equity buckets, respectively.

The vetting process to decide whether to include a structured product in a portfolio is similar to the decision to add a new bond, stock, or other investment position. The selection depends on an investor's objectives and risk tolerance.

A key characteristic of structured products is the formulaic nature of their returns in relation to the reference asset's price appreciation over a specific timeframe. This provides investors with an opportunity to customize a strategy that best suits their individual portfolio needs and targeted outcome.

There are a number of ways that investors can use structured products, including:

Exhibit 7: Enhanced Participation (Barrier)



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STRATEGIC: Structured products may be an effective tool for shifting the risk/return profile of a portfolio. In most cases, they are designed to offer the potential for slightly enhanced returns while providing some degree of downside protection, potentially improving a portfolio's efficiency.

TACTICAL: An investor can use structured products to express a market view on an asset without bearing the full risk associated with being exposed to it directly. If an investor considers an asset to be undervalued (or overvalued), a structured product can be used to express that view while potentially protecting some, or all, of the principal.

MANAGE RISK: Structured products may offer a way to reduce risk by increasing downside protection in a portfolio over a specified time frame. Depending on the chosen product, investors can protect some, or all, of their principal, subject to an issuer's credit risk.

YIELD ENHANCEMENT: Structured products can also monetize volatility. In the pursuit of yield, an investor can focus on employing volatility as the underlying driving factor for a specific asset class.

MARKET ACCESS: Structured products can provide investors access to markets, securities, and other investment vehicles in which they could not previously invest.

RISKS OF STRUCTURED PRODUCTS

There are a number of potential risks associated with investments in structured products. Some of these risks exist across structured products while others are unique to an individual security. As a result, it is essential for advisors and investors to understand the upside and downside potential of each security before investing.

ISSUER CREDIT RISK: Structured notes are considered senior unsecured debt and are exposed to the credit risk of the issuer. Changes to the institution's credit rating or the market's view of the credit risk of the issuer could potentially affect the value of the security, and an issuer default would result in a loss. Diversifying across issuers can help reduce this risk.

LIQUIDITY RISK: There is typically a limited secondary market for structured products, but the issuer is not obligated to repurchase the position. An investor wishing to liquidate an investment must be prepared to receive a price that could represent a significant discount to the initial offering price.

RETURN RISK: A structured product's return potential is defined by the terms of the security. Both downside and upside participation may be either levered or limited. As a result, investors may receive a lower return from the structured product than if they had invested directly in the reference asset. Fees are also built into the contracts and should be factored into return expectations.

LEGAL AND TAX CONSIDERATIONS: There are legal and tax considerations involved with structured products. Regulations governing the securities may change. Investors should consult a tax advisor before investing.

CONCLUSION

Structured products encompass a variety of vehicles that can be used to pursue a defined investment outcome, express a market view on a specific asset class, or hedge an existing exposure. Once the exclusive province of large institutional investors, structured products are now available to individuals and are an additional investing tool that can help them realize their financial goals. As such, structured products are increasingly essential components of high-net-worth investors' portfolios.

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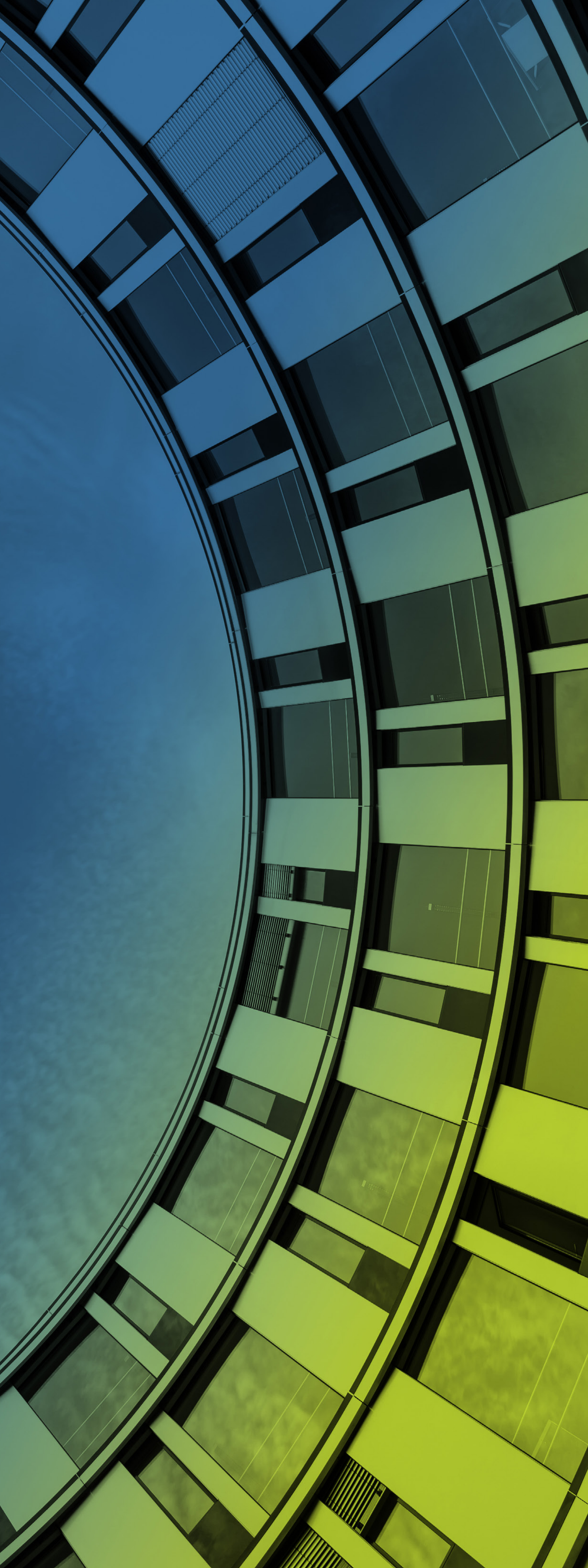
IMPORTANT INFORMATION – DISCLAIMER



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