Product Group

Warrants, Factor Warrants / Leveraged ETPs, Knock-Out Products

In this information sheet, Commerzbank provides information on the underlying characteristics as well as the opportunities and risks of the warrants, factor warrants / leveraged ETPs, knock-out products product group.

General characteristics and investment opportunities
These products are "debt securities with special repayment terms" denominated in euro or another currency and linked to an underlying, e.g., an equity or an equity index. By investing in these products, investors can benefit disproportionately from an expected performance of the underlying; however, investors will not receive a regular income. Depending on their individual design, these products are generally suitable for speculating on rising or falling prices of the underlying or for hedging a securities portfolio in whole or in part. Investors also need to consider the respective subscription ratio, which generally results in a lower capital investment compared to a direct investment.

Typical product characteristics
Warrants securitise the right, but not the obligation, to buy (call) or sell (put) a certain quantity of an underlying. The most important product parameter is the strike price set at the time of issue; this indicates the price the underlying must exceed (call) or fall below (put) in order for the warrant to have an intrinsic value. On the valuation date, the intrinsic value determines whether a warrant expires worthless, or the respective positive difference is paid as cash settlement. Instead of a cash settlement, investors may also be entitled to delivery of the underlying. In addition to the intrinsic value, the price of a warrant is determined by the time value during the term. The time value is essentially determined by the remaining term and the expected price volatility of the underlying. At maturity of a warrant, the time value is always zero; the other leveraged products in this product group are not exposed to a decline in time value.
Warrants come in a wide variety of forms with very different rights, such as barrier warrants, digital warrants, range or inline warrants as well as discount warrants. Depending on the issuer, these may carry very different product names despite having a similar design. It is also possible that differently designed warrants have the same or similar product names.

Factor warrants (previously factor certificates) and leveraged ETPs (exchange-traded products, e.g., on commodity prices and exchange rates) are designed to track a leveraged change in the price of the underlying on the previous day, either positively (long) or negatively (short). This is designed to potentially result in a disproportionate participation with a constant leverage in the respective performance on a daily basis. Products with a factor of 1 or -1 are also included in this category. Since the previous day's closing price of the underlying is always used to determine the percentage change in value, a so-called path dependency arises with these products. Because of this type of daily recalculation, it is possible that the product price declined after several days despite the price of the underlying having remained unchanged. These price deviations become larger the longer the holding period, the greater the price volatility of the underlying and the higher leverage. While these products usually do not have a fixed maturity, investors should not hold them for a long time. The issuer has the right to terminate these products with a standard notice period of only one day, with termination potentially occurring at an unfavourable time for the investor.

The price of knock-out products, which are often also referred to as turbo warrants, is usually determined by the difference between the price of the underlying and the current strike price. Unlike traditional warrants, these products come with a knock-out barrier; if the price of the underlying touches this threshold, the product will become due (knock-out event). The various designs of these leveraged products differ in the following product parameters:

- Term,
- Difference between knock-out barrier and strike price,

- Adjustment of the barrier level and strike price,
- Time period or date of the barrier observation,
- Premium,
- Redemption amount following knock-out event.

The occurrence of the knock-out event results in a de facto total loss of the capital invested.

In contrast to traditional warrants, the level of volatility is only a minor or no factor at all in determining the price of these products.

Investors are advised to obtain information from the issuer on the individual design and the exact functioning of the respective product before acquiring it.

Material risks of the product group

By investing in these leveraged products, investors benefit from return opportunities, but are also exposed to additional material risks. These include the following:

Issuer risk - also referred to as default risk - when the issuer fails to meet its obligations or can only meet them in part, for example as a result of insolvency. The issuer is usually a bank. If the bank runs into financial difficulties, a regulatory intervention may result in a bailout of the bank, partial or total loss of the investment, or a compulsory conversion into equity, such as shares. Generally: The worse the credit rating of an issuer, the higher the default risk, but also the risk premium.

Risk of loss - investors may receive a lower sales price due to a fall in the price of the underlying or other parameters that have a negative impact on the product price. This may even result in a total loss of capital, e.g., if the underlying becomes worthless, a warrant has no intrinsic value at maturity or a knock-out event has occurred.

Sustainability-related decisions relating to the environment, social aspects and corporate governance also impact on the performance of the underlying and the issuer.

Liquidity risk - during the term, investors may not be able to sell the security or may only be able to sell it at a possibly much lower price.

Foreign currency risk - Investors are exposed to currency risk when investing in a foreign currency denominated security as performance could be adversely affected by exchange rate movements.

Early redemption and reinvestment risk - investors are exposed to the risk that the issuer may exercise an ordinary or extraordinary option to call the fixed income security at a time or in a financial market environment that is unfavourable for the investor, as the investor can reinvest the redemption amount only on less favourable terms.

Further information and costs

For further details on these aspects and the product, please refer to the relevant sales prospectus and basic information sheet. In principle, inflation trends impact your investment performance. A resulting loss of purchasing power affects both the income generated and your capital invested. When acquiring, holding and eventually selling securities and derivatives, costs will impact returns. For further details, please refer to the respective cost information before entering into a securities transaction.

For further details on the characteristics and risks of the products, please refer to the brochure “Basic Information on Securities and Other Investments”.