A GOOD FOUNDATION

Why should you invest in a structured product fund? **Mark Fuller,** Head of Structured Products

The benefits of structured products within a diversified portfolio are easy to explain. Investing in structured products can give the buyer returns that are uncorrelated to the performance of the usual benchmarks, such as the FTSE100 or the S&P 500; they can also provide leverage, so an underlying asset that moves 1% can provide a return of much more than 1% if bought as part of a structured product.

At Mattioli Woods, we have used UK inflation and the movement of house prices to provide returns for our structured products. Return on these underlying assets and many others are difficult for investors to access directly, but can be easily provided via a structured product. The final benefit, the return of the initial investment, can be demonstrated by Mattioli Woods' track record in structured products. Over the last 10 years, 45 of the structured products we have put together for our clients have matured. Of these, 82.23% have paid a positive return, 13.33% have returned the investor's original investment and just 4.44% have returned less than the original investment.

Since 2005, we have arranged our structured product investments via plans. Although the advantages of structured product investing are clear, structured product plans as an investment strategy have a few flaws from a client's perspective that cannot be easily overcome.

For example...

- All structured product plans have a fixed start and end date, so clients cannot control the start level for any index or other underlying asset used for the structured product in which they invest
- When a plan matures, the client will automatically receive their money back whether they want it or not, but without an obvious next investment; structured products are "buy and hold" investments, so holders usually have to keep the plan until maturity to get the full return
- Some structured products can be held without any prospect of a return if the underlying asset moves dramatically in the wrong direction shortly after the start date
- The terms of any structured product, including the pay-off at maturity, are predefined

- Buying a structured product via a plan exposes the customer to the risk of losing some or all of their initial investment if the bank issuing the plan becomes insolvent
- Comparing one structured product with another is impossible as no two structured products are the same

By contrast, investing in funds is straightforward ...

- Fund investment can happen immediately
- Liquidity is constantly available
- An infinite number of funds with a similarly infinite number of objectives exist – and with the ease of liquidity an investor can change their view and their fund holding very quickly
- Funds can be compared and the track record of fund managers can be accessed from many sources
- Funds are open-ended investments – the entry and exit to a fund are determined by the individual investor, not the structured product plan manager
- The risks to initial capital of fund investment are limited to the performance of the fund

A structured product fund eliminates most of the flaws of structured product investing via a plan, maintains all the benefits of structured products, and adds all of the benefits of investing via a fund. We are developing a collateralised structured investment fund with the sole objective of providing returns similar to an absolute returns fund via investments in structured products. The fund itself will be 100% collateralised – eliminating any counterparty risk. Investors can buy or sell units in the fund at any time, and investors immediately receive exposure to a diversified portfolio of structured products. The products are selected by managers with a combined 25 years' experience of structuring and selling structured products. The fund itself will be transparent – all the structured product pay-offs held by the fund will be available on our website, and as it is a fund, it will be open-ended with no fixed maturity date.

Our structured investment fund will have various structured product pay-offs, which could take into account every form of underlying asset – the following list is just for demonstration purposes and is not exhaustive!

- Equities
- Commodities
- Bonds
- Rates
- Foreign exchange
- Mutual funds

These underlying assets will be in a fund with an objective to provide a smooth return in excess of the risk-free rate with a low volatility – regardless of the performance of traditional benchmarks. The returns on the fund will be subject to capital gains tax when investment is not via a SIPP, SSAS or ISA. We will continue to sell structured product plans that pay income, but in time we will have a separate structured investment fund that pays income too.

So, in answer to my initial question, "Why should you invest in a structured product fund?" ... By combining the benefits of fund investing and the unique way a structured product can increase the returns in a portfolio, a structured product fund is without doubt the best way to invest in this asset class for growth-seeking investors.

FIVE THINGS YOU ALWAYS WANTED TO KNOW ABOUT STRUCTURED PRODUCTS*

Mark Fuller,
Head of Structured Products

The return on a structured product can be linked to almost any underlying asset... don't believe me? – then look below...

1) The following have been used to pay a return on retail structured products:
   a. Spain winning the football World Cup in 2010 (they won, and Banco Sabadell paid a bonus coupon).
   b. Snow falling on Christmas Day 2005 at Heathrow Airport (this was part of a Bristol and West Building Society structured deposit – it didn't snow).
2) Some structured products linked to commodities pay a return in the form of a physical delivery of the commodity. That's OK if the underlying asset is gold, but it has always limited the demand for uranium-linked structured products...
3) In November 2005, The Birmingham Midshires Building Society offered a structured product to fans of Wolverhampton Wanderers. Promotion to the Premiership boosted returns by 1% and there were added bonuses ... you could get tickets in the box, or a signed Wolves shirt and a signed football. Mattioli Woods could have offered a similar product linked to the performance of Leicester City this season, but pension schemes and trusts would not have been allowed to receive the signed memorabilia and tickets... I am sure they would be happy to receive the cash bonuses though!
4) Some structured products are given nicknames to promote an understanding with the investing public. For example, a "Commodore" structured product was named after the Commodores song "Once, Twice, Three Times a Lady", because the possible return was "once, twice, three times" the performance of the FTSE100. If you work in structured products, this is a hilarious play on words... apparently.
5) FIFA, the global governing body of football, arranged a structured product named "The 2006 FIFA World Cup Cancellation Bond" for the 2006 World Cup in Germany. This was a catastrophe-linked bond to protect FIFA against financial losses that would result should the 2006 World Cup in Germany be cancelled. History does not record where the FIFA's upfront fee for this bond was paid...

*BUT WERE TOO AFRAID TO ASK