

**Information about
the characteristics of, and risks
associated with, financial instruments**

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As a client, it is essential for you to be aware that:

- trading in financial instruments takes place at your own risk
- prior to the commencement of trading in financial instruments, you must carefully study the undertaking's general business terms and conditions and other relevant information about the financial instrument in question and its characteristics and risks
- you must immediately check the contract note and give immediate notice of any error
- it is your responsibility to monitor fluctuations in the value of the financial instruments in which you hold positions
- it is your responsibility to monitor, on a continuous basis, the performance of your investments and to take such measures as are necessary to adapt them to suit your investment strategy and risk profile.
- it is your responsibility to familiarise yourself with relevant KID ((Key Information Document) for derivatives and investment products, see <https://sebgroupp.com/priips>

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1. Definitions

Financial instruments. This is a general term used to refer to the assets and liabilities traded in the securities market, derivatives market and to some extent in the currency market, and that are defined in more detail in section 2-2 of the Securities Trading Act.

Regulated market. A regulated market is a marketplace where financial instruments are traded. A regulated market operates under a licence and is subject to a number of rules and obligations. There is a specific statute that governs regulated markets.

Stock exchange. A stock exchange is a regulated market that is licensed specifically to operate as a stock exchange, and that has the right to use the term "stock exchange" in or as an addition to its name.

Multilateral trading facility (MTF) An MTF is not a regulated market but a trading venue for trading in financial instruments. All investment firms that satisfy the objective requirements established by the MTF in question may participate in trading in this venue. In Norway, the Securities Trading Act requires MTFs to operate under a licence.

Systematic Internaliser (SI). An investment firm that deals extensively on own account by executing client orders must seek registration as an SI in the relevant financial instrument. An SI has an obligation to set binding bid and offer prices and to publish these to its clients.

Dark pool. A marketplace where participants can submit orders that are not displayed in the order book, but that will be matched automatically if another participant submits a corresponding order. Often such orders are subject to minimum size requirements and matching must take place at the mid-market rate, i.e. the midpoint of the best bid and offer prices on the open order book. Some dark pools also allow investors to submit orders to the pool personally.

Underlying assets / Underlying financial instrument(s). These are the asset(s) or financial instrument(s) that a derivative gives the parties rights and obligations to buy or sell, or that the parties have agreed to use as the basis for settlement in cash.

Option. A contract that that gives one party (the Holder) a time-limited right, but no obligation, to buy (Call Option) or sell (Put Option) an agreed quantity of financial instruments at a pre-agreed price from/to the other party (the Issuer/Writer).

Futures/forwards. A contract whereby both the buyer and the seller enter into a binding agreement to the effect that an agreed quantity of financial instruments will be transferred from the seller to the buyer at an agreed price on an agreed date after the normal deadline for settlement in the underlying financial instruments covered by the contract.

Price swap. A contract linked to an agreed quantity of financial instruments, a settlement rate (swap rate), and a settlement date, which rather than involving the delivery of the underlying financial instruments involves a cash settlement based on the difference between the swap rate and the market rate on the expiry date.

Contract for difference (CFD). A contract whereby both the buyer and seller are bound to settle in cash the difference between the opening price and closing price of a single financial instrument, index, currency or similar asset or a group of financial instruments, indices, currencies or similar assets. The buyer of a CFD will make a gain if the price rises and a loss if it falls. A CFD does not have a pre-agreed expiry date, but the buyer may close his position at any time.

Credit Default Swap (CDS). A contract that secures the buyer against the risk that the issuer of a debt obligation will be wholly or partially unable to settle the debt on the settlement date.

Index option/Index future. A contract where the underlying value is not a security, but an index value. Such a contract is not settled through the delivery of financial instruments, but by calculating the cash value of the contract.

Short sale. The sale of financial instruments that the investor does not own, but has borrowed in order to perform timely settlement. The financial instruments will be purchased at a later date and redelivered to the lender. Short selling when the investor has not borrowed the underlying financial instruments is referred to as naked short selling. Naked short selling is illegal in Norway.

Securities swap. A combination of short and long positions in (at least) two financial instruments, where one sets off the price change in one instrument (the long position) against the price change in the other (the short position).

Exercising an option. Exercising an option means to demand trading of the underlying financial instrument in accordance with the option agreement. Ordinarily the Holder will be entitled to demand partial exercise of the option.

Expiry Date. The day upon which an option must be exercised to prevent it lapsing without value. The expiry date for a futures/forward contract is the date upon which the contract converts to a transaction with an ordinary settlement date for the delivery of the underlying financial instruments in return for the payment of the purchase price.

Settlement date. The day upon which a futures/forward contract, option or price swap is finally concluded through the delivery of the underlying financial instruments against the payment of the agreed purchase price, or the cash settlement becomes due for payment. The settlement date is generally three stock-exchange trading days after the expiry date.

American option. An option that the Holder can exercise either wholly or partially at any time until the agreed time on the expiry date.

European option. An option that can be exercised only on the expiry date.

Spot price/Spot rate. The price a security is traded at for delivery on the second stock-exchange trading day following the trade date.

Strike price/Strike rate. The agreed price for the exercise of an option.

Forward price/Forward rate. The agreed price for the exercise of futures/forward transaction.

Swap price/Swap rate. The agreed price(s) to be applied when setting off the individual elements in a swap.

Option premium. The amount the Holder has paid to the Issuer/Writer when buying the option.

Hedge. If a seller of an option/future/forward/swap wants to avoid the risk of price fluctuations, he can buy/short sell a quantity of the underlying

securities, such that any increase in the value of the sold derivatives will be counterbalanced by a corresponding increase in the value of the underlying securities. Securities that provide the issuer with this kind of protection against the risk of price fluctuations are often referred to as a hedge.

NIBOR rate. An interest rate calculated by the Oslo Stock Exchange in accordance with rules established by Finance Norway, which specifies the market interest rate for unsecured loans in NOK. The rate is fixed daily for various maturities.

Interest rate risk. The risk of a decrease in the value of a financial instrument in which the client has invested due to changes in the market rate.

Credit risk. Risk that an issuer or counterparty will become unable to pay.

Clearing. Function as counterparty between the parties to derivatives contracts or trading in shares and guarantees that the parties will receive settlement for the transaction.

2. Trading in financial instruments

Trading in financial instruments, such as shares, equity certificates, bonds, commercial paper, derivatives or other rights and obligations intended for trading in the securities market, normally takes place in an organised form in a trading system.

Trading takes place through the investment firms using the trading system. As a client you normally have to contact such an investment firm in order to buy or sell financial instruments. There are also investment firms that transmit orders to another investment firm that in turn makes use of the trading system. Trading may also take place internally within an investment firm, for example by the firm assuming the position of counterparty to the trade, or by trading with another client of the firm (internal trading).

Financial instruments may qualify for **listing** on a **regulated market**. This means that the instruments are approved for trading and that the market authorities are monitoring whether the company that has issued the financial instruments fulfils the listing criteria. The financial instruments listed on the Oslo Stock Exchange comprise shares, equity certificates, bonds, commercial paper, certain fund

units, and financial derivative instruments linked to financial instruments.

Trading in listed financial instruments may take place on regulated markets, on an MTF, in a dark pool, or through an SI.

Price information relating to financial instruments that are traded on a regulated market is published regularly on the market's website, in newspapers and/or in other media.

2.1. Share trading

Shares in a limited company give the holder a right to a portion of the company's share capital. Shares give the holder a right to a portion of the dividends or other distributions by the company. Shares also give the holder a voting right at the general meeting, which is the highest-ranking decision-making body in the company. The more shares the holder owns, the greater the portion of capital, dividends and votes he will normally be entitled to. Voting rights may vary according to the class of shares in question. There are two types of limited companies in Norway, **public limited companies** (ASA) and **private limited companies** (AS).

Only shares issued by public limited companies (ASA) or corresponding foreign companies can be listed on a stock exchange in Norway. In addition, there are requirements with regard to the size, history and ownership of the company, as well as the disclosure of information relating to the company's financial position and activities in general.

Less stringent rules will often apply for listing on regulated markets that are not stock exchanges.

Norway currently has two **regulated markets** for trading in shares: Oslo Stock Exchange and Oslo Axess. Only Oslo Stock Exchange is licensed to operate as a **stock exchange** (www.oslobors.no). Oslo Axess (www.osloaxess.no) is to all intents and purposes subject to the same rules as the Oslo Stock Exchange with regard to follow-up and monitoring and the application of sanctions for breaches of the regulatory regime

Shares may be listed on several regulated markets ("secondary listing"). Several Norwegian companies have secondary listings on foreign regulated markets.

Trading in Norwegian securities also takes place on a number of MTFs.

Trading in shares that are not listed on a regulated market takes place on the so-called OTC market. Trading in this market is based largely on information about prices and interests that the brokerage houses supply to each other. In Norway, brokerage houses may enter interests to purchase or sell into a trading support system operated by NOTC AS, a company owned by the Norwegian Securities Dealers Association and Oslo Stock Exchange. Thereafter purchase and sale contracts are entered into between brokerage houses by telephone. Companies that are registered on NOTC are required to publish relevant price information that is of material significance on NOTC's trading support system. For more information about the NOTC list, please refer to www.vpff.no.

If a share is neither listed on a regulated market, traded on an MTF, nor subject to the publication of purchase and sale interests on a trading support system, trading will normally take place through brokerage houses seeking to assist the client by contacting other potential clients that may be interested in assuming the position of counterparties. Investment in these types of shares is associated with significant liquidity risk and significant uncertainty relating to the determination of the price.

Trading in a regulated market or other trading system constitutes the **secondary market** in shares and equity certificates that have previously been issued by a company. In addition, the NOTC list also functions as a secondary market for shares. If the secondary market works well, i.e. it is easy to find buyers and sellers, and bid prices from buyers and sellers and offer prices from sellers are quoted on a continuous basis, together with closing prices for executed trades, then companies will benefit as it will become easier to issue new shares, thereby raising more capital to fund a company's activities. The **primary market** is the market for trading in/subscription to newly issued shares, equity certificates or bonds.

Shares listed on a regulated market or other trading systems are normally divided into different segments depending on the company's market value and liquidity. These segments are typically published on the website of the relevant trading

system, in newspapers and through other media. The companies listed on the Oslo Stock Exchange are divided into three different segments depending on the company's liquidity, **OBX**, **OB Match**, and **OB Standard**, respectively.

Daily key figures for the prices at which the shares are traded, such as "day high", "day low" and "closing", as well as information about trading volumes, are published by means including the financial press and various websites operated by the markets, investment firms and suppliers of information to the financial sector. The extent to which such price information is up to date may vary depending on the means of publication.

Shares may be issued in different **classes**, usually A and B shares. Such classification is generally significant in relation to the exercise of voting rights at the company's general meeting. Only a small number of Norwegian listed companies have more than one class of shares. Each A share will generally carry one vote, while B shares will generally carry only limited or no voting rights. The difference in voting rights may reflect, for example, a desire to protect the original founders' and owners' influence over the company by giving them stronger voting rights.

The **nominal value (par value)** of a share is the amount of the share capital of a company that the share represents. The share capital of a company can be calculated by multiplying the total number of shares by the nominal value of each share. Sometimes a company will wish to change the nominal value of its shares, for example, because the market price of its shares has increased significantly. By dividing each share into two or more shares, a so-called **split**, the nominal value of each share and the price of each share will be reduced accordingly. The amount of capital owned by the shareholder remains unchanged after a split, but it will be divided into a larger number of shares, each with a lower nominal value and a lower price.

Conversely, a **reverse split** may be effected if, for example, there has been a significant reduction in the share price. This involves combining two or more shares into one share. The amount of capital owned by the shareholder remains unchanged after a reverse split, but it will be divided into fewer shares, each with a higher nominal value and a higher price.

The term **initial public offering** refers to the process whereby the shares of a limited company become listed on a regulated market and made available for trading. In this connection, the general public may be offered the opportunity to subscribe for (purchase) shares in the company on the occasion of such listing. Usually the company in question will be an existing company whose owners have decided to improve the company's access to the capital markets and also facilitate trading in the company's shares.

A **takeover** will normally be effected by one or more investors offering the shareholders of a company the opportunity to sell their shares on certain terms. If the purchaser obtains more than 90% of the share capital and the voting rights of the company, the purchaser may effect a **forced merger or squeeze-out** whereby the remaining shareholders are forced to sell their shares.

A **mandatory bid** refers to the situation where a single shareholder acquires a potentially controlling shareholding and as a result is required to make an offer to the other shareholders to purchase their shares. Under the Securities Trading Act, this threshold is reached when a single shareholder becomes the owner of, or otherwise controls, more than a third of the company's shares. The offer must be repeated if the dominant owner comes to control more than 40% or 50% of the shares. A shareholder whose holding exceeds one of these thresholds will be obliged, unless he takes immediate steps to reduce his holding below the threshold, to make an unqualified offer to all the shareholders in the company to purchase their shares at the highest price that the offeror has paid within a specific period.

A **company that needs additional capital may mount a rights issue**. A limited company that wants to expand its activities will often need additional capital. One way in which the company can generate this additional capital by issuing new shares is through a rights issue. The general rule under the Companies Act is for the company's existing shareholders to have pre-emptive rights to subscribe to the shares being issued. The number of shares a shareholder may subscribe to will depend on the number of shares already held by the relevant shareholder, and the company will issue subscription rights to its existing shareholders. The

subscriber will have to pay a subscription price for the newly issued shares. Generally this will be lower than the market price. Accordingly these subscription rights have a certain market value, and the share price will generally fall after these rights have been uncoupled from the shares. Those shareholders who hold pre-emptive rights, but who do not subscribe for new shares, may during the subscription period (which must last for at least two weeks in a rights issue) sell their subscription rights in the market on which such rights are listed. The pre-emptive rights will lapse upon the expiry of the subscription period and the allotment of shares, thus having no further utility or value.

A limited company may also implement a so-called **private placement**, which is similar to a rights issue, but targeted only at a limited group of investors. Before a company can implement a private placement, a general meeting of shareholders must have resolved to waive the pre-emptive rights that would otherwise be attached to the shares issued in a rights issue. Private placements are often implemented on the basis of authority given by the general meeting to the company's board of directors. A private placement involves a so-called **dilution** of the existing shareholders' voting rights and of the share capital of the company.

2.2. Other equity-related instruments

Equity certificates, convertible bonds and depository receipts may all have characteristics similar to shares. Ordinarily, trading in such instruments takes place in a regulated market (hereunder a stock exchange), but these types of financial instruments may also be the subject of OTC trading.

Equity certificates (formerly known as "primary capital certificates") have some clear similarities with shares. The main differences concern rights of ownership over the company's assets and influence over the decision-making bodies of the issuer. In addition, certain restrictions are imposed with regard to the distribution of dividends. In Norway, listed equity certificates are issued by savings banks. More information about equity certificates is available at www.egenkapitalbevis.no.

Convertible bonds are interest-bearing securities that may, during a specific period, be converted

into newly issued shares at a pre-determined price. A convertible bond is both an interest-rate instrument and an option to purchase. If the conversion price is significantly higher than the market price of the shares, a convertible bond will normally be priced as any other interest-rate instrument. If the opposite is the case, the price of the convertible bond will reflect both the value of the option and the interest element. In both cases, the price is expressed as a percentage of the nominal value of the convertible bond.

A depository receipt is a financial instrument that entitles the holder to all of the ownership rights to an underlying financial instrument that is registered with a depository (custodian trustee). Depository receipts are normally traded in the same manner as the underlying financial instrument.

2.3. Interest-bearing financial instruments

An interest-bearing financial instrument is a right to claim against the issuer of a loan. The return is normally provided in the form of **interest (coupon)**. There are various types of interest-bearing instruments depending on the nature of the issue, the security provided for the loan by the issuer, the term until the maturity date, and how interest is paid.

Instruments with a term to maturity of one year or less are often known as commercial paper, while instruments with longer terms to maturity are known as bonds.

Many interest-bearing financial instruments are assessed by independent organizations known as credit rating agencies. Such an assessment, known as a **rating**, expresses the risk that the issuer may default on the debt.

In addition to the rating provided by credit rating agencies, several Norwegian brokerage houses have started to provide so-called "shadow" ratings. This means that the brokerage house makes its own assessment of the creditworthiness of the issuer and assigns a rating to the security. The methods they use are similar to those employed by credit rating agencies.

Usually interest (coupons) is paid at either a fixed or floating rate. In the case of a fixed-interest loan, the same interest rate applies for the entire lifetime of the loan. In the case of loans with a floating

interest rate, the rate is normally fixed each quarter based on NIBOR and an agreed mark-up (spread). The spread is fixed for the entire lifetime of the loan in the absence of agreement that certain events will trigger a change. In the case of non-rated loans, it is not unusual for there to be agreement that the spread will change if the loan achieves a specific credit rating.

On certain types of loans, no interest is payable and only the nominal amount is repaid on the loan's maturity date (zero-coupon bonds). The purchase of zero-coupon bonds takes place at a significant discount, which means that the effective interest rate is the same as for bonds on which regular coupon interest is paid. For example, all the debt that the Norwegian state issues in treasury bills is issued in the form of zero-coupon bonds.

The interest rate that the issuer must pay corresponds to the market's view of the risk of default. Interest-rate securities are usually classified in one of two categories: High Yield and Investment Grade. Interest-rate securities that are rated **bbb** or lower by credit rating agencies are considered to carry a significant risk of default, and accordingly are classified as High Yield securities.

A number of bonds are stock-exchange listed, which means that trading in these bonds is reported in the same way as trading in listed shares on a regulated market. In addition, Oslo Stock Exchange offers an alternative market for trading in non-listed bonds and commercial paper - **the Alternative Bond Market (ABM)**. The ABM is a separate marketplace that is not regulated by, or licensed pursuant to, the Norwegian Stock Exchange Act, but is administered and organized by the Oslo Stock Exchange.

In general, trading in bonds is conducted differently than trading in shares. In practice, the interest and currency market is regarded as a **quoting or price-driven market**, in contrast to the stock market, which is an order-driven market.

2.4. Derivative Instruments

Share options give the holder the right to buy or sell shares. Acquired (bought) call options give the owner the right to purchase already issued shares within a specific period of time at a predetermined

(strike) price. Acquired (bought) put options give the holder the right to sell shares at a predetermined (strike) price within a specific period of time. Every call or put option has a corresponding **sold option**.

Index options produce a gain or loss linked to movements in the underlying index. These gains and losses are settled in cash reflecting the difference between the strike and market prices when this difference is in the purchaser's favour.

The price of an option normally follows the price movements of the option's underlying asset or index.

Call options with a longer term to maturity than the standardised call options are known as warrants. Warrants may be used to buy underlying shares or to provide a cash settlement if a gain has been achieved as a result of the price of the underlying share being higher than the agreed future purchase price/selling price. Many stock-exchange traded warrants are issued by investment firms or banks as a part of their derivatives-based activities. Warrants can also be issued by a company on its own behalf. Such warrants are redeemed by the company issuing new shares or selling treasury shares.

A derivative instrument is a form of agreement (contract) where the actual agreement may be negotiable on the capital markets in financial instruments. A derivative instrument is tied to an underlying financial instrument or to an underlying value indicator, such as an index.

Derivatives can also have other types of underlying values, such as, for example, currencies or commodities, or currency- or commodity-related indices. These types of derivatives are known, respectively, as foreign-exchange derivatives and commodities derivatives, and have similar characteristics to derivatives tied to underlying financial instruments. The information below focuses mainly on derivatives tied to underlying financial instruments.

Derivative instruments may be used for many different purposes:

- to counter an unfavourable price development in financial instruments one owns;

- to achieve a profit by taking advantage of changes in market prices without actually owning or short selling the underlying financial instrument;
- to achieve a profit or return using less capital than would be required to carry out an equivalent trade directly in the underlying financial instrument; or
- to agree a securities trade with settlement at a future date.

In general, the price of a derivative will swing in the same direction as that of the underlying financial instrument. Accordingly, investment in derivatives is to a large extent based on the same considerations as apply to investment in the underlying financial instrument. However, investment in derivatives is subject to a different risk profile than direct investing.

Investors in the derivatives market may also speculate on changes in secondary parameters that influence the prices of derivatives, such as changes in interest rates and market volatility.

In Norway, standardised derivatives are traded on the Oslo Stock Exchange. Derivatives tied to Norwegian shares and indices are also traded in other markets, including NASDAQ OMX.

Trading in unlisted derivatives takes place on the so-called OTC market. Trading in this market is based largely on information about prices and interests that the brokerage houses supply to each other. Brokerage houses often trade for their own account in OTC derivatives, and fix prices and act as counterparty to their clients.

3. Risk associated with trading in financial instruments

3.1. General information about risk

Financial instruments normally provide a **return** in the form of **dividends** (shares and mutual fund units) or **interest** (interest-bearing instruments). In addition, one may make a profit or loss due to an increase or decrease in the price of the instrument. The total return is the sum of the dividend/interest and the change in the price of the instrument.

Naturally, the investor is seeking a total return that is positive, i.e. a **profit**. However, there is also a **risk**

that the total return will be negative, i.e. that the investor will make a **loss** on the investment. The risk of loss varies between different instruments. In an investment context, the word risk is often used to express both the risk of loss and the chance of making a profit. In the description below, however, the word risk is used solely to refer to the risk of loss.

There are various ways of investing in financial instruments in order to reduce the level of risk. Generally it is better from a risk perspective to invest in several different financial instruments rather than in just one or only a few financial instruments. These instruments should have characteristics that result in the **risk being spread** (often referred to as **diversification**) and should not concentrate risks that may be triggered simultaneously. One can also invest in negative positions in financial instruments (short positions). Such investments will increase in value when the share price falls.

The client bears the risk that the value of an investment may fall, and accordingly must familiarise himself with the terms and conditions, prospectuses etc. prepared in relation to transactions in such instruments and the specific risks and characteristics of the instruments in question. The client must also continuously monitor his investments in such instruments. This applies regardless of whether the client received individual advice in connection with the investment. The information required for monitoring prices, and accordingly changes in the value of investments, is available in the market listings published in the mass media outlets, such as newspapers, websites and, in some cases, by investment firms themselves.

The client must continuously assess the risk attached to his investments. There are many different factors that may affect the prices of financial instruments. Accordingly the client should familiarise himself with the factors that may affect different kinds of instruments and take an active interest in the factors that may affect his own investments. The client should keep his investment portfolio under continual review, and if necessary should make such changes as are necessary to adapt it to his investment strategy and risk profile.

3.2. Shares and share-related instruments

The **price** of a share is affected to a great extent by the **company's prospects**. A share price may rise or fall depending on investors' analyses and assessments of the company's opportunities to make **future profits**. Future external developments in the economy, technology, legislation, competition, etc, determine the likely level of future demand for the company's products or services and, consequently, are also fundamental to changes in the price of the company's shares.

The price may also be affected by general **market risk** – the risk of a decline in the entire market, or certain parts of the market, in which the client has invested. In addition, movements in the prices of financial instruments that are listed on **foreign** regulated markets may affect prices in Norway.

The price will also be affected by trends in the sector to which the company belongs, **sector-specific risk** – the risk that a specific sector performs worse than expected or is affected by a negative event such that financial instruments linked to companies in the relevant sector may fall in value. The prices of shares in companies that fall within the same industry/sector are often affected by changes in the prices of shares in other companies in the same industry/sector, regardless of the companies' respective home countries.

In addition, **other factors relating directly to the company**, e.g. changes in the company's senior management and structure, or business interruption, may affect the company's future ability to generate profits, in both the short- and long-term. This is known as **company-specific risk** – the risk that a specific company may perform worse than anticipated or may be affected by a negative event such that financial instruments linked to that company may fall in value.

The **framework conditions** for business activity, both nationally and internationally, may also affect share prices. Changes in tax and duty levels nationally and in other countries will affect companies' operating costs and thus their competitive situation. International agreements between countries regarding customs charges and duties on the import and export of goods and services will affect the companies' competitiveness and thus also share prices. Events such as natural

disasters, terrorist attacks and wars may also have a major impact on share prices in stock exchanges worldwide.

Prevailing market interest rates also have a crucial effect on the price of a company's shares. If market interest rates are rising, investors may become more interested in investing in interest-bearing financial instruments. As a result, investors will move some of their investments from shares to interest-bearing securities, putting shares in less demand. Generally share prices will decline when demand falls. An increase in the rate of interest payable on a company's debt will also have a negative effect on its share price, because the increased payments of interest will have a negative impact on the company's financial results.

Foreign-exchange fluctuations may also affect a company's share price. Companies whose revenues and operating costs are determined in different currencies will be particularly vulnerable to such fluctuations. This applies to several Norwegian exporters. When investing in foreign markets, foreign-exchange fluctuations will also affect the company's results once the purchase and sale price have been converted to NOK.

The worst case scenario is that the company performs so badly that it has to be declared **bankrupt**. The shareholders rank lowest in priority for repayments from the estate in bankruptcy. The company's other obligations must first be repaid in their entirety. Only in exceptional cases are there assets left in a bankrupt company after its debts have been paid, meaning that the shares in the company are worthless.

Players in the financial markets often have different opinions as to how share prices will develop, often because they differ in the importance they attach to factors that will affect the share price, or have different views as to how these factors will develop in the future. As a result, there are both buyers and sellers. When many investors share the same opinion regarding price trends, they will either buy, thereby creating buying pressure, or sell, thereby creating selling pressure. Pressure to buy a share will cause its price to increase, while pressure to sell a share will cause it to fall.

The turnover, i.e. the quantity of a particular share that is bought or sold, affects the share price. In the event of a high turnover, the difference, also called the **spread**, between the price the buyers are prepared to pay (bid price) and the price asked by the sellers (ask price) is reduced. A share with a high turnover, where large quantities can be traded without any major effect on the price, enjoys good **liquidity** and is thus easy to buy or sell. Companies quoted on regulated market indices normally enjoy good liquidity.

3.3. Interest-bearing instruments

The risk associated with an interest-bearing instrument consists partially of the price changes that may occur during the term of the instrument due to changes in market interest rates, and partially of the market's assessment of the risk that the issuer may be unable to repay the loan. Loans for which satisfactory security has been provided for repayment are thus less risky than unsecured loans.

Loans considered to carry a particularly high risk of default are characterised by the issuer being required to pay a particularly high rate of interest. Such interest-bearing securities are often known as **high-yield** bonds.

If a company goes bankrupt or enters into debt settlement proceedings, the holder of an interest-bearing instrument may lose all or part of his investment. In the event of a bankruptcy, all debt must be repaid before anything can be paid to the shareholders. So in general it is possible to say that the risk of loss in the case of interest-bearing instruments is lower than for shares.

Market interest rates are established each day, both for instruments with short terms to maturity (less than a year), e.g. **commercial paper**, and for instruments with longer terms to maturity, e.g. **bonds**. This takes place on the money market and bond market. Market interest rates are affected by analyses and assessments conducted by the Central Bank of Norway and other major institutional market players with regard to a range of economic factors, such as inflation, the state of the economy, and interest rate trends in other countries both in the short- and long-term.

If the market interest rate increases, the price of fixed-rate interest-bearing financial instruments will fall, since the return on the instrument will become less favourable in comparison with current market interest rates. Conversely, the price of interest-bearing instruments increases when the market interest rate declines.

Bonds issued by the Norwegian state, county councils and municipalities (or guaranteed by such bodies) are considered to be virtually risk-free with respect to redemption at the predetermined value on maturity.

3.4. General information about risks associated with trading in derivative instruments

Trading in derivative instruments is associated with particular risks in addition to the risks associated with the underlying financial instruments. The client is personally responsible for this risk and must carefully study the characteristics of such instruments, together with the general terms and conditions, prospectuses and similar documents that apply to trades in such instruments. The client must also continuously monitor his investments (positions) in such instruments. The information required for such monitoring may be found in listings published online, in the mass media, and by the client's investment firm.

Trading in derivative instruments can be described as trading in, or the transfer of, risk. For example, someone who expects prices to fall in the market can buy put options which will increase in value if the market falls. In order to reduce or avoid the risk involved in a fall in price, the buyer pays a premium, i.e. the cost of the option. In most cases, trading in derivatives cannot be recommended for clients with little or limited experience of trading in financial instruments, as derivatives trading often requires specialised knowledge. The structure of derivative instruments is such that price changes in the underlying asset are reflected in the price of the derivative instrument. The change in the price of the derivative instrument is often greater in relation to the amount invested than the change in the value of the underlying asset. The change in the price of the derivative instrument is therefore referred to as a leverage/gearing effect, and can lead to a larger profit on the invested capital than if

the investment had been made directly in the underlying asset. On the other hand, the leverage effect may result in a greater loss on the derivative instrument compared to the change in value of the underlying asset if the price of the underlying asset falls. As a result, it is extremely important to monitor the prices of both the derivative instrument and the underlying asset. The client should, in his own interests, be prepared to act swiftly, often within the same day, should the derivative instrument take a negative turn.

A party that assumes an obligation by issuing an option or entering into a futures/forward contract is required to provide collateral for his position from the outset. The collateral requirements vary in step with upward or downward movements in the price of the underlying asset that in turn cause the value of the derivative instrument to increase or decrease. Accordingly, further security in the form of supplementary collateral may also be required. Thus the leverage effect also has an impact on the collateral requirement, which may change quickly and radically. If the client fails to provide adequate collateral, the clearing institution organisation or investment firm is entitled to terminate the investment (close out the position), without the client's consent, in order to reduce the loss. This means that the client should carefully monitor price developments and collateral requirements in order to prevent an unwanted closing out of his positions.

The term to maturity for derivative instruments may be anything from a very short period to several years. The relative price changes are often greatest for instruments with a short (remaining) term to maturity. For example, the price of an option generally decreases more and more rapidly towards the end of the term to maturity due to the fact that the time value decreases. Clients should therefore also carefully monitor the maturity periods of their derivative instruments.

Certain derivative trades may require the client to provide separate security (**margin requirement**), for example, when selling options, buying or selling forward/futures contracts, or entering into swap agreements. The margin requirement will vary depending on factors such as the underlying security, the type of instrument, the instrument's term to maturity and volatility. The margin requirement may also vary considerably from day

to day. The client should, in his own interests, be prepared to take immediate action, for example by providing further security (to meet margin requirements that may arise) or by terminating his investments in derivative contracts (closing out his positions) through the purchase or sale of (offsetting) contracts.

3.5. Risks associated with various types of derivative instruments

The main types of derivative instruments are options, futures/forwards and swap agreements.

3.5.1. Options

An option is a contract which involves one party (the writer of the option contract) undertaking to buy (a put option) or sell (a call option) the underlying financial instrument to the other party (the holder of the contract) at a predetermined (strike) price if the holder exercises his option right. The date when the holder can exercise this right may depend on the type of option concerned. An **American option** may be exercised at any time during the term to maturity. A **European option** may only be exercised on the expiry date. The holder pays a price (premium) to the writer for the rights conferred by the contract. The price of the option normally reflects the price of the underlying asset. The main factors determining the price of an option are the difference between the market value of the underlying financial instrument and the agreed strike price, together with a time value, which is an expression of possible future fluctuations in the value of the underlying financial instrument. The time value gradually declines as the remaining term to maturity is reduced, with the result that the price of a call option may fall even though the value of the underlying financial instrument has risen.

The investor must take all these price-related factors into account when deciding whether to close a derivative position or keep it open.

3.5.2. Call options

When **buying** a call option, the investor gains the right to buy the underlying financial instrument at a future date at a predetermined price. The investor pays an option premium, together with costs

relating to selling and administering the option contract.

The maximum amount the holder of a call option can lose is limited to the option premium and the costs paid. The maximum loss arises when the price of the underlying financial instrument remains lower than or equal to the agreed strike price.

The potential gain is in theory unlimited. When the option is exercised, the gain is the value of the underlying financial instrument on the exercise date less the strike price and the option premium, including costs.

The **writer/seller** of a call option has an obligation to sell (if the option holder exercises his option to buy) the underlying assets at a future date at a predetermined price. The writer of a call option receives the option premium, less costs incurred in relation to selling and administering the option contract.

The writer's potential gain from the call option is limited to the net option premium. If the strike price remains higher than or equal to the market price of the underlying financial instrument until the expiry date, the option holder will generally not insist on buying the securities, and the writer can record the entire option premium as income.

The writer of a call option risks unlimited losses if the price rises. If the holder exercises his option, the writer will have to buy the financial instruments in the market at the market price. The loss will be equal to the market value of the underlying financial instruments, less the strike price and option premium.

If the writer has hedged his position by owning the underlying financial instruments (a covered call), a price rise will not result in any loss having to be paid out, but the writer will miss out on the possible gain from the rise in value in excess of the strike price plus the net option premium. By holding the underlying financial instruments, the writer exposes himself to the risk of a loss in the event that the price falls, and a loss will arise when the fall in value exceeds the option premium. If the writer sells the underlying assets, he will be exposed to the risk of their price rising again. Writers of covered calls often attempt to manage

the risk of a falling price by selling some of the underlying assets.

3.5.3. Put options

The **buyer** of a put option gains the **right** to sell the underlying financial instrument at a future date at a predetermined price. The buyer of a put option pays an option premium, together with costs relating to selling and administering the option contract.

The maximum amount the holder of a put option can lose is limited to the option premium and the costs paid. The maximum loss arises when the market value of the underlying financial instrument remains higher than or equal to the strike price.

The potential gain is limited to the strike price less the option premium, including costs. The gain is the strike price less the value of the underlying financial instrument on the exercise date and the option premium, including costs.

The **writer/seller** of a put option has a **duty** to buy (if the option holder exercises his option to sell) the underlying assets at a future date at a predetermined price. The writer of a put option receives the option premium, less costs incurred in relation to selling and administering the option contract.

The potential for gain on writing a put option is limited to the net option premium. If the value of the underlying financial instrument remains higher than, or equal to, the strike price, the holder will normally not insist on selling the securities, and the writer can record the entire net option premium as income.

If the price falls, a loss will arise when the value of the underlying financial instruments is lower than the strike price less the net option premium. The maximum loss is limited to the strike price less the net option premium.

3.5.4. Futures/forwards

Futures contracts and forward contracts involve the parties entering into a mutually enforceable agreement to buy and sell the underlying financial instrument at a predetermined price, with delivery of the asset or other contractual performance to take place on a specified date.

No premiums are paid for futures/forwards, but the agreed forward price will normally be fixed at the spot price (the current market price) of the underlying financial instrument, plus interest costs until the settlement date. In addition, the investor has to pay costs relating to trading and administering the contract.

In futures/forward transactions, the **purchaser** assumes the entire price risk associated with the underlying financial instrument. If the price falls, the purchaser will incur a loss equal to the difference between the value of the underlying financial instrument and the forward price. Similarly, if the price rises there will be a gain equal to the difference between the value of the underlying financial instrument and the forward price. In addition to the price risk, the purchaser assumes a credit risk with regard to the seller's ability to deliver the relevant financial instruments on the settlement date.

A **seller who owns** the underlying financial instruments assumes no risk in connection with changes in their price, but will not make any gain if their value rises above the agreed forward price. The seller assumes a credit risk regarding the buyer's ability to pay the agreed amount on the settlement date.

If the seller does not own the underlying financial instruments, his potential loss is, in theory, unlimited in the event of a price increase. The loss will be equal to the value of the underlying financial instruments, less the agreed forward price. Correspondingly, if the price falls, the seller has the potential to make a gain equal to the forward price less the value of the underlying financial instruments. The seller also assumes a credit risk regarding the buyer's ability to pay the agreed amount on the settlement date.

Futures/forwards are general terms covering instruments with various delivery and settlement mechanisms, but with the same risk profiles. Contracts that are settled by the physical delivery of the underlying financial instrument are often called forwards, while contracts that are settled in cash on the settlement day are known as futures.

Collateral provided in the case of futures/forward transactions is intended to protect against future price changes. Traditionally, the intermediary or

settlement agent in a futures/forward transaction has not been required to furnish collateral, but requirements concerning the reciprocal furnishing of collateral are becoming increasingly stringent.

In the case of futures, in addition to the collateral provided to protect against future price changes, it is also usual for collateral requirements to be monitored on a daily basis based on prices from the previous stock-exchange trading day.

3.5.5. Contracts For Difference (CFDs)

Standardised futures where the underlying instrument consists of specific shares or indices are often sold nowadays as Contracts For Difference (CFDs). Providers of CFDs often require only a low margin requirement, with the result that investors can achieve a high level of market exposure with only a small initial deposit.

A CFD entails a high level of risk. It is possible to lose more than the original amount invested. Prices may move very rapidly in an unexpected direction, and losses may mean that the investor has to increase his margin. In certain market conditions, it may be difficult or even impossible to close out a position. This may happen, for example, if the price of an underlying instrument rises or falls so fast that trading in the instrument is restricted or suspended.

Low margins also raise the risk that the CFD provider may close out the position at any time, even in the course of the day, if the value of the collateral falls below the margin requirement. The client will often have to furnish more collateral within very short deadlines, and rapid price fluctuations may cause the CFD provider (in accordance with the contract) to close out the position contrary to the client's wishes.

The value of investments in CFDs with underlying instruments quoted in foreign currencies may also vary due to exchange-rate fluctuations.

CFDs are not suitable for all clients. The client must ensure that he is fully aware of the risks involved and must seek independent advice if necessary.

3.5.6. Swap agreements

A **swap agreement** involves the parties agreeing to make payments to each other on an ongoing basis,

for example calculated on the basis of a fixed or a floating interest rate (an interest-rate swap), or to swap, at a specific point of time, certain assets with each other, for example different currencies (a currency swap).

3.6. Standardised and non-standardised derivative instruments

Derivative instruments are traded in standardised and non-standardised forms.

Trading in standardised derivative instruments takes place on regulated markets and in accordance with agreements and terms that are standardised by a stock exchange or a clearing institution. In the Norwegian derivatives market, for example, the Oslo Stock Exchange offers trading in standardised options and futures. The following regulated markets in Norway offer trading in standardised derivative instruments:

- **Oslo Børs ASA** – trading in standardised options and futures
Transactions on Oslo Stock Exchange are cleared by SIX x-clear and London Clearing House (LCH).
- **NASDAQ OMX OSLO ASA** - trading in, and clearing of, commodity derivatives, including financial energy contracts, and freight derivatives.
- **Fish Pool ASA** – trading in salmon contracts.
Transactions on Fish Pool ASA are cleared by NASDAQ OMX.

Trading in foreign standardised derivative instruments will normally be governed by the rules and terms and conditions applicable in the country in which the stock exchange transaction and clearing take place. It is important to note that such foreign rules and terms and conditions may differ from those applicable in Norway.

Some investment firms offer their own forms of derivative instruments that are not traded on regulated market. Such instruments are known as **non-standardised** derivative instruments (OTC derivatives). Clients wishing to trade in these types of derivative instruments should study the agreements and terms and conditions applying to these instruments with particular care.

3.7. Clearing

The clearing of derivatives involves clearing institutions assuming the role of counterparty between the investment firms respectively representing the buyer and the seller of derivatives contracts, and guaranteeing that the investment firm receives the settlement of the contract. The clearing institution acts as seller in relation to the buyer and as buyer in relation to the investment firm on the selling side. In the standardised derivatives market, derivatives contracts are usually cleared by a licensed central counterparty (CCP). In the OTC market the investment firm will typically assume this role.

As CCPs operate currently, they provide no direct protection to the end-investor. In the case of both CCP-cleared and OTC transactions the investor bears the risk that his investment firm may not settle the contract.

Investors who do not wish to bear this risk may enter into a contract to open a segregated account at the clearing institution. This arrangement requires a separate set of contracts and will increase costs. Accordingly it is most suitable for large institutional investors.

4. SECURITIES FUNDS

A securities fund (mutual fund) is a "portfolio" of different financial instruments, such as, for example, equities and/or bonds. The fund is owned by all the investors (**UNIT HOLDERS**) in the fund, and is managed by a **MANAGEMENT COMPANY**. There are different types of securities funds with different investment strategies and risk profiles.

When an investor invests in a fund, he receives a number of units in the fund that represents his percentage of the fund's total assets under management.

The units may be bought from and redeemed by (sold to) the management company. The units' actual value is calculated daily by the management company and reflects the current prices of the financial instruments in which the fund has invested. Units in some funds can be traded on a regulated market (Exchange Traded Funds ("ETF")), see paragraph 5 below.

One of the purposes of a securities fund is to invest in several different shares and other financial instruments. This means that unit holders bear less risk than shareholders who only invest in one security or a small number of securities. Unit holders do not have to select, buy, sell or monitor the shares or perform other related management tasks.

Securities funds are subject to various statutory and regulatory requirements.

UCITS funds are funds established in accordance with the European UCITS Directive, and that accordingly are approved for marketing throughout the EEA. Most new funds are UCITS funds.

National funds are funds that are regulated under the Norwegian Securities Funds Act.

Alternative Investment Funds are not funds, but are investment entities that are similar to funds and that may be structured as a limited company or other form of corporation. These entities are governed by a separate statute, the Alternative Investment Funds Act.

For further information about securities funds, please refer to www.vff.no

Securities funds are also categorised according to the fund's investment policy. The following is a brief description of the most common types of securities funds:

Unit trust/equity fund – a securities fund that must normally invest at least 80 per cent of its total assets in company shares (or other equity instruments) and which must not, as a general rule, invest in interest-bearing securities.

Fixed-income fund – a securities fund that is to invest in interest-bearing financial instruments. These funds are divided into bond funds and money market funds.

Balanced fund – a securities fund that is not defined purely as a unit trust or a fixed-income fund. The weighting between shares and interest-bearing securities may be more-or-less fixed, but the proportions of various securities may also change during the fund's lifetime.

Index fund – a securities fund that is managed relatively passively in relation to the market index that the fund tracks.

Fund of funds – a securities fund that invests in one (or possibly more) underlying securities funds.

Specialised fund - includes national funds that are often known as hedge funds. Specialised funds are managed more flexibly than ordinary securities funds. Specialised funds may vary considerably with regard to their risk profile and the amount of protection offered to investors. Investment in a specialised fund may involve a high level of risk. Specialised funds/hedge funds often make use of investment techniques such as the extensive use of derivatives, short-selling, leveraged trading, and open currency positions. Holdings in specialised funds may be offered only to professional clients. This means that investments in specialised funds may be neither marketed nor sold to retail clients. This rule applies regardless of whether the idea is initiated by the client or the bank. Specialised funds operate under the supervision of the Financial Supervisory Authority of Norway, and are also regulated separately under the Securities Funds Act. Subject to the approval of the Financial Supervisory Authority of Norway, foreign hedge funds may be marketed in Norway to professional clients.

5. Listed funds and similar products

ETP (Exchange Traded Products) is an umbrella term for ETF (Exchange Traded Funds) and ETN (Exchange Traded Notes). These products are traded on various trading systems, such as, for example, the Oslo Stock Exchange. These products make it possible to gain exposure to shares, indices, currencies, commodities etc. Some of these products are structured with a gearing element. The exposure can either be to a falling market (short) or a rising market (long). There may be significant variations in how these products are structured, and it is essential that the investor studies the product in question carefully.

An ETN is usually issued by a financial institution (bank/brokerage house) and will be traded in the secondary market in the same way as a share. Investment in this type of product involves taking on a **credit risk** in respect of the issuer. Credit risk is the risk that an issuer or counterparty will become unable to pay. This means that if the issuer is unable to meet its obligations, the securities may become worthless.

ETFs are fund units issued by a mutual/securities fund. This means that, through ownership of the fund units, the investor directly owns underlying assets and thus has no credit risk in relation to the issuer.

Some ETPs include derivative elements and/or are geared in a way that means the product carries a high level of market **risk**. This means that the prices of these products may fluctuate more than the prices of the underlying assets, and thus investment in these products is normally more risky than investment in the underlying assets, e.g. shares. In addition, these geared products are rebalanced daily. In the longer term, this means that the return will deviate from price trends in the market due to the gearing factor. The return may be negative, even though the value of the underlying assets is the same at both the buying and selling dates. As a result of these characteristics, these geared products are less suitable choices for long-term investment.

The facts that the underlying assets are often traded in foreign markets and in currencies other than NOK mean that the investor should also be aware of the potential **foreign-exchange risk**. This may mean that even though price trends regarding the underlying asset would indicate that the security should yield a positive return, the return may in fact be reduced, eliminated or become negative due to foreign-exchange fluctuations.

An ETP normally has one or more liquidity guarantors, or market makers, who have undertaken to provide binding buy and sell prices for the security. Nevertheless, it may sometimes be difficult to trade in a particular ETP. For example, there may be little liquidity or the relevant market may be closed for trading.

6. Short trading

Short trading means selling financial instruments that the investor does not own. "Naked" short trading is illegal in Norway. Accordingly an investor who wishes to sell short must borrow shares from the investment firm or obtain them in some other way on the settlement date. At the same time, the borrower undertakes to return instruments of the same type to the lender on a predetermined later date.

Short trading is often used as an investment strategy when the financial instrument is expected to fall in value. On the sale date, the borrower anticipates being able to buy the borrowed instruments in the market on the date when the instruments are to be returned at a lower price than the price at which they were sold. If instead the price rises, the borrower will incur a loss which, in the case of a sharp price increase, may be significant.

Contracts concerning the lending of financial instruments often contain terms to the effect that the lender may at any time demand, subject to two or three days' notice the return of the instruments. This increases the risks associated with short selling.

7. Trading frequency and costs

The more frequent the trading, the greater the commission costs, since normally these costs are incurred on every individual trade (purchase or sale). If the commission costs incurred over a period of time are greater than the return, the client will incur a loss. For the purposes of clarification, commission costs also apply to leveraged trading.

In the case of securities trading, commission costs ordinarily increase pro rata according to the quantity being traded. For example, if the client sells shares at a value of NOK 50 000 and the commission is charged at 0.2 %, the sale will cost NOK 100. If however the client sells shares at a value of NOK 500 000, the commission cost will be NOK 1000. In addition, the bank applies minimum rates of commission, such that sales or purchases of securities for small amounts of money may be disproportionately expensive.

8. Leveraged trading

In many cases, financial instruments may be purchased with partially borrowed capital. Since both the client's own capital and the borrowed capital affect the rate of return, the client may achieve a greater gain by borrowing, if the investment develops favourably, than would have been the case if the client had only invested his own capital. The debt associated with the borrowed capital is not affected by positive or negative changes in the prices of the purchased instruments, which is an advantage as long as the

price develops positively. If the price of the purchased instruments changes negatively, there will be a corresponding disadvantage, as the debt will remain unchanged. Consequently, in the case of a price fall the client may lose part or all of his own invested capital, and at the same time the debt will also have to be repaid in whole or in part from the revenues from the sale of the financial instruments that have fallen in value. The debt will have to be repaid even if the revenue from selling the financial instruments does not cover the entire debt.

The risks of leveraging share purchases increase with the level of borrowing. For example, an investor whose portfolio is 80% leveraged, will

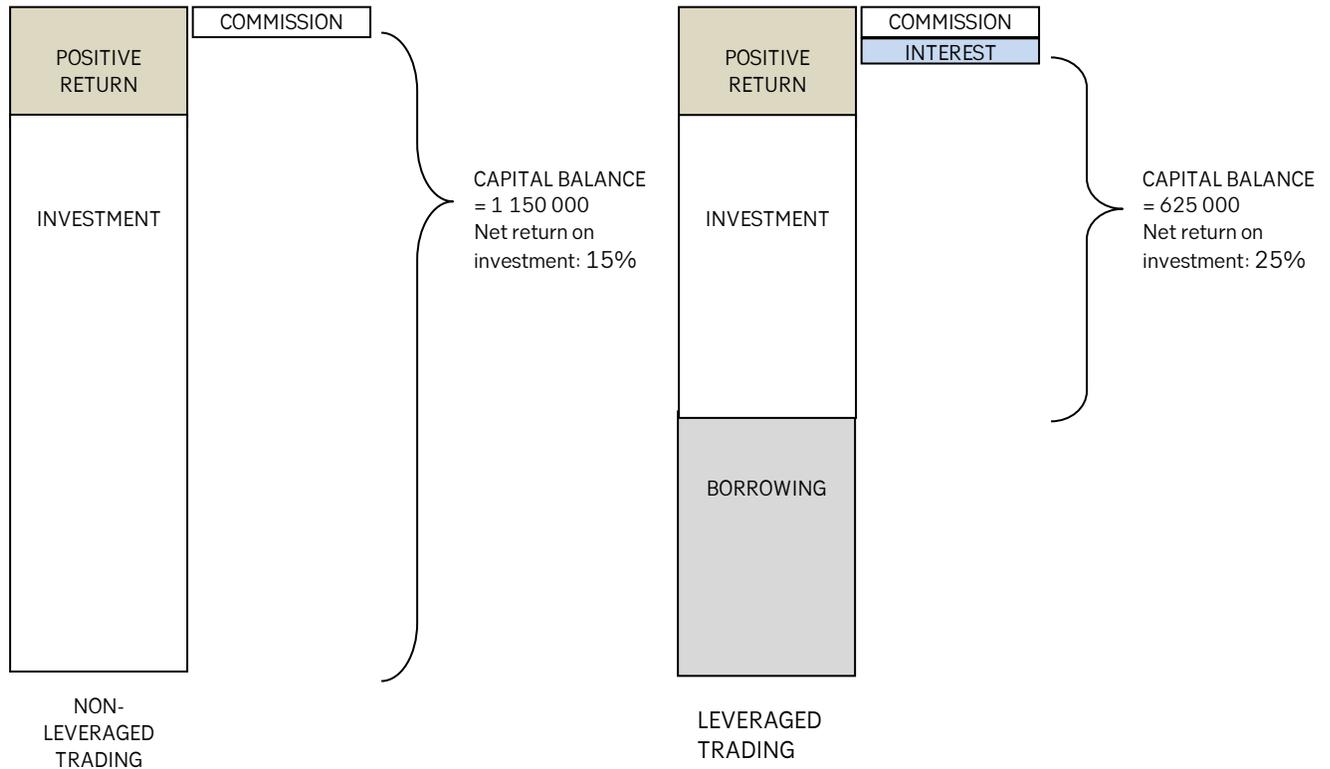
lose all his own capital if prices fall by 20%. If the portfolio is 60% leveraged, he will lose his own capital if prices fall by 40%.

The return on the client's own capital in a partially leveraged portfolio will fluctuate more than in a corresponding non-leveraged portfolio, and the leverage will result in an increased rate of return only when the return on the underlying investments exceeds the interest rate on the loan.

Please see below for an example of a positive return on a partially leveraged portfolio.

Assumptions:

- 20% positive return
- NOK 1,000,000 invested in the market
- 5% commission (20 transactions at 0.25% commission)
- 5% interest rate
- 50% leverage



Please see below for an example of a negative return on a partially leveraged portfolio. Assumptions:

- As above, but with a negative return of 20%.

