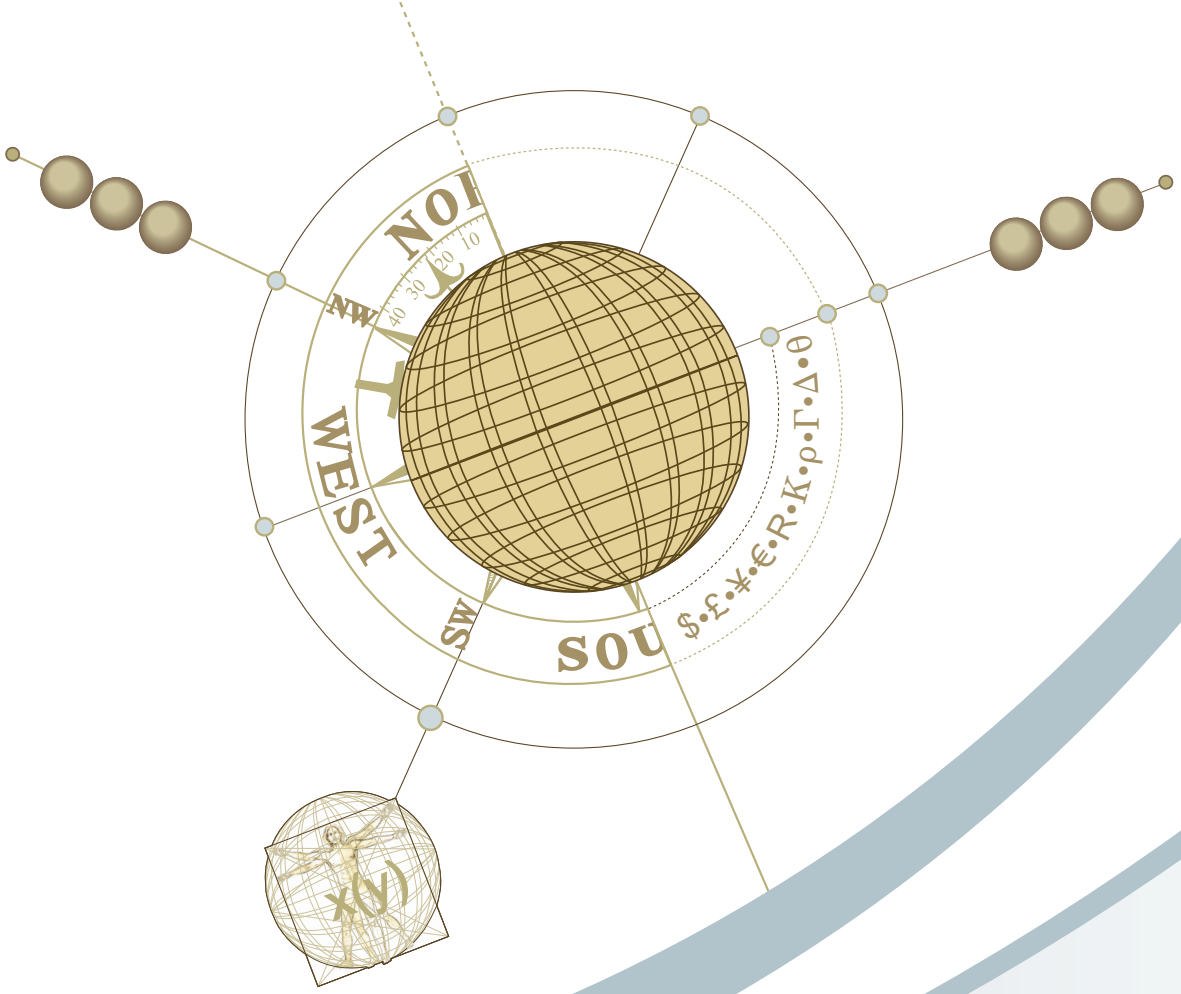


# Global Markets
# Reset Warrants

Standard Bank

# Reset Warrants

The Standard Bank of South Africa Limited ("Standard Bank"), South Africa's leading warrant issuer, is pleased to launch an innovative new product called Reset Warrants. This product is designed to give investors added security when dealing in the warrant market.

## What are Reset Warrants?

A Reset Warrant is a derivative, meaning that its value is derived from another underlying asset. Reset Warrants differ from Vanilla Warrants in that they have a pre-determined reset date on which the strike price of the warrant could change in an investor's favour. Reset Warrants are available as call warrants listed over individual indices or shares traded on the Johannesburg Stock Exchange Limited ("JSE").

The reset date is an observation date on which the strike of a call warrant could decrease to the prevailing market level if the underlying price is below the warrant's initial strike price. This increases the probability of the warrant ending 'in the money', and effectively gives investors a second chance when an anticipated move in the underlying asset does not occur as initially expected. Reset Warrants therefore give investors a degree of insurance against the market moving in the opposite direction to their view.

Prior to the reset date, Reset Warrants will lose their value at a slower rate than Vanilla Warrants when the market moves against investors. Once the reset date has passed, Reset Warrants behave like Vanilla Warrants.

## Reset Call Warrants

Reset Call Warrants allow an investor to take advantage of positive movements in the underlying asset. A Reset Call Warrant's strike will reset if, at the reset date, the closing price of the underlying asset has fallen below the initial strike price.

The performance of a Reset Call Warrant is linked to the value of the underlying asset over which it is listed. As the price of the underlying asset **increases**, all other things being equal, Reset Call Warrants will **increase** in value. As the price of the underlying asset **decreases,** all other things being equal, Reset Call Warrants will **decrease** in value.

## How do Reset Warrants differ from Vanilla Warrants?

Reset Warrants differ from Vanilla Warrants in the following respects:

- Reset strike price
- Gearing or leverage
- Time decay
- Delta

**Reset strike price**

The reset strike price is what differentiates Reset Warrants from Vanilla Warrants. Reset Warrants are issued with an 'at-the-money' strike price; however, unlike Vanilla Warrants, the strike of a Reset Warrant may reset at the pre-determined reset date.

The strike price for a Reset Call Warrant will reset to the closing spot price of the underlying asset on the reset date if the underlying asset price is lower than the initial strike price.

**Example** Consider a Reset Call Warrant issued with a strike price of R100 when the underlying price is R100 ('at-the-money'). If, at the reset date, the underlying price had fallen to R70 ('out-the-money'), then the strike price would be reset to R70. This would result in the warrant moving from being 'out-the-money' to 'at-the-money', resulting in the warrant having an increased probability of expiring 'in-the-money'.

**Gearing or leverage**

Reset Warrants provide investors with leveraged exposure to the underlying asset, but will have less gearing than Vanilla Warrants on a like-for-like basis. In exchange for the possibility of the strike price resetting favourably on the reset date, an investor sacrifices some gearing up to the reset date when compared to Vanilla Warrants.

Gearing improves potential profits when trading a warrant. However, an adverse movement in the underlying asset will also result in a greater percentage loss in the value of the warrant relative to the underlying asset.

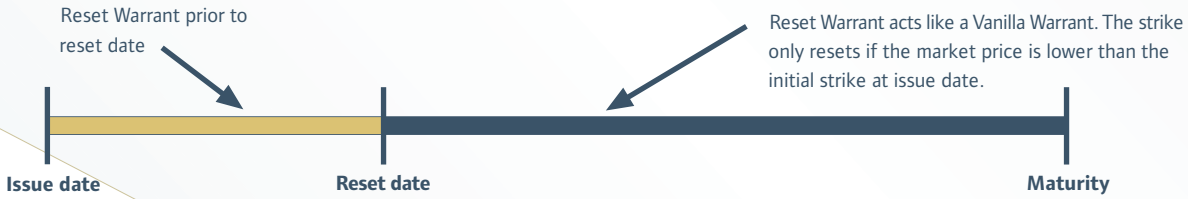
**Time decay**

Reset Warrants have more time value than Vanilla Warrants. The time decay of Reset Warrants is thus greater than the relative time decay of Vanilla Warrants. This is true only up to the reset date. After the reset date, Reset Warrants behave in the same manner as Vanilla Warrants.

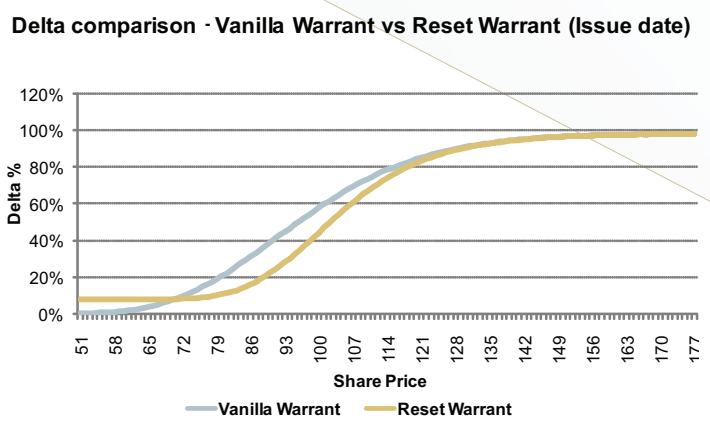
**Delta**

The delta of a warrant is defined as the theoretical change in the price of a warrant for a 1-cent change in the price of the underlying asset. The delta of a warrant is between 0 and 1. For example: A warrant with a delta of 0.5 will move 0.5 cents every time the underlying price moves by 1 cent.

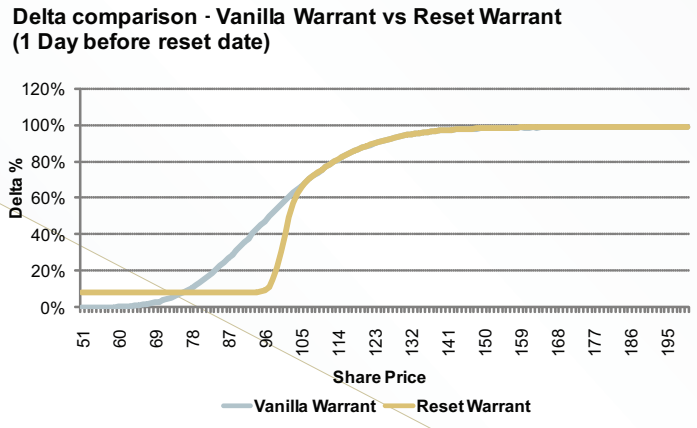
The delta of Reset Call Warrants approaches that of Vanilla Call Warrants as the underlying price moves further above the strike price (i.e. as the probability of the strike resetting decreases). The delta of a Reset Call Warrant decreases faster than that of a Vanilla Call Warrant as the underlying price moves below the reset strike (i.e. as the probability of the strike price resetting increases). After the reset date, Reset Warrants behave the same as Vanilla Warrants.




**a) Delta three months prior to reset date (strike of 100)**




**b) Delta one day prior to reset date (strike of 100)**



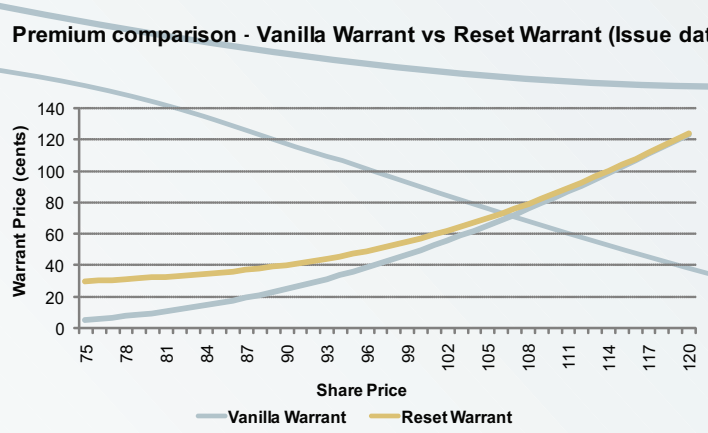

** Please note: "Out–the-money" Reset Warrants have very low deltas, particularly as the warrant approaches the reset date. This can result in the warrants showing very little movement, even if there are large movements in the underlying assets. Clients are urged to exercise caution when trading in Reset Warrants in these circumstances.

## Reset Call Warrants compared to Vanilla Call Warrants

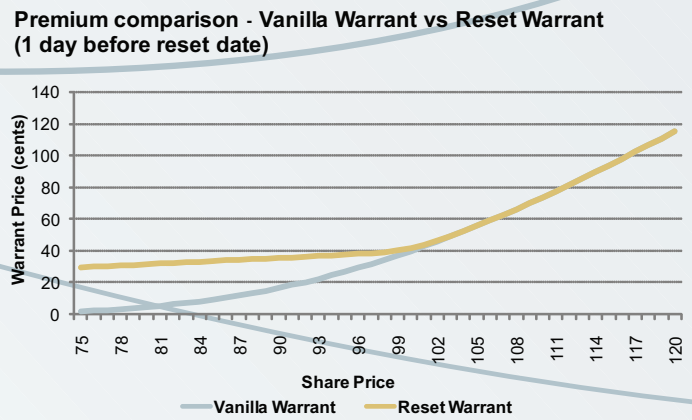
Reset Call Warrants resemble Vanilla Call Warrants in that they allow investors to profit if the underlying price rises. Reset Warrants are ideal for investors who would like a second chance if an anticipated move does not happen as expected and the market moves against their position. Reset Warrants may also assist clients to overcome some of the risks associated with timing their entry into the market.

**Example** Investor A purchases a Reset Call Warrant when the underlying price is 100 (with a strike of 100). The maturity of the warrant is nine months. Assume that the reset date is three months after the Reset Warrant was purchased. Firstly, we investigate how Reset Call Warrants behave near inception (three months before the reset date in this example). Secondly, we investigate how Reset Call Warrants behave a day before the reset date. Finally, we investigate how Reset Warrants and Vanilla Warrants behave in an identical manner after the reset date (with a strike being the lower of the initial strike and the closing level at reset date).

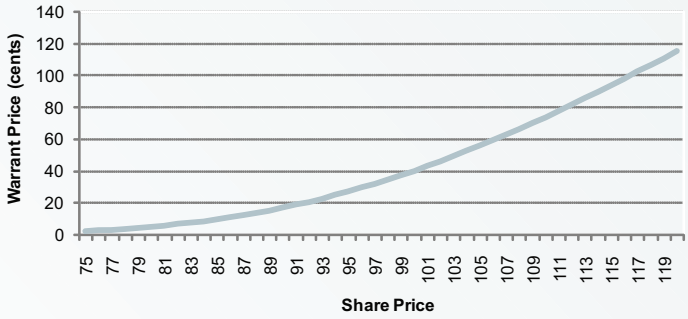
**a) Three months prior to reset date**




**b) One day prior to reset date**




**c) One day after reset date**




## Advantages of trading Reset Warrants

- Reset Warrants give an investor a second chance if the market price is below the initial strike price.
- Before their reset date, Reset Warrants lose value more slowly than Vanilla Warrants when the market moves against them.
- Reset Warrants reduce some of the risks associated with timing an investor's entry to the market.
- Liquidity is provided by Standard Bank, ensuring that investors are able to efficiently enter and exit positions.
- Many of the benefits of trading Vanilla Warrants are inherent in Reset Warrants.
- Reset Warrants are less risky than Vanilla Warrants.

## Risks and disadvantages of Reset Warrants when compared to Vanilla Warrants

- Reset Warrants have a reduced gearing compared to Vanilla Warrants prior to the reset date.
- The time value of Reset Warrants prior to the Reset Date is greater than that of Vanilla Warrants.
- 'Out-the-money' Reset Warrants have very low deltas, particularly as the warrant approaches the reset date.
- Reset Warrants can be considered less risky than Vanilla Warrants before the reset date; however, some of the gearing when compared to that of a Vanilla Warrant is sacrificed for the added security imbedded in Reset Warrants.

## Risks and disadvantages associated with trading in Reset Warrants

- Standard Bank Reset Warrants are primarily exposed to changes in the underlying share price. The value of Standard Bank Reset Call Warrants usually increases as the underlying share price rises and usually decreases as the underlying share price falls.
- In addition to the exposure to changes in the underlying share price, the Reset Warrants are exposed to changes in the expected volatility of the underlying share price; market interest rates; the expected dividends of the underlying share; and the time to expiry.
- Standard Bank Reset Warrants are leveraged investments. Like other leveraged share investments, they provide more exposure to both increases and decreases in the share price when compared with investing directly in the underlying shares. Investors should understand that they may lose their entire investment in Standard Bank Reset Warrants.
- Standard Bank Reset Warrants are not bank deposits. They are unsecured obligations of the Issuer and, in the event of the winding up of the Issuer, would rank equally with other unsecured creditors of the Issuer and ahead of subordinated debt and obligations to shareholders.

## Standard Bank – the issuer and liquidity provider

Standard Bank is acting as a market maker, providing liquidity and ensuring that investors are able to efficiently enter and exit positions throughout the day.

## Choosing your Reset Warrant

- Ensure that you understand the product properly and have experience in trading derivatives.
- With every investment, one needs to have a time horizon. Reset Warrants may be used for longer-term views or for added security when a view is uncertain.

## Glossary

### American style
Means that the warrant can be exercised at any time up to and including the expiry date.

### At the money
A  in which the  of an  is equal to (or nearly equal to) the  of the underlying share or index.

### Conversion ratio
The number of warrants that must be exercised in relation to one share or an underlying parcel of shares.

### Call warrant
A contract giving the holder the right, but not the obligation, to buy a share for the exercise price at a future date. (See also European style and American style.) Taking up this right is known as 'exercising' the warrant.

### Delta
The delta of the warrant represents the change in the value of the warrant relative to changes in the value of the underlying share price.

### European style
Means that the warrant may be exercised only on the expiry date.

### Exercise price
Fixed price at which a warrant holder may buy (in the case of calls) or sell (in the case of puts) a share.

### Expiry date
The expiry date is the last day on which a warrant may be exercised.

### Gearing
Simple gearing is the ratio of the share price to the warrant price. Effective gearing is the simple gearing multiplied by the warrant's delta. Delta is the measure of the change in the warrant price relative to a change in the price of the underlying asset.

### Index warrant
A warrant where the underlying asset is a nominated index instead of an individual asset.

### Intrinsic value
The amount a warrant would be worth if it were to expire today; the difference between the underlying price and the exercise price per share, divided by the conversion ratio.

### In the money
For a call option, when the option's strike price is below the underlying share or index price.

### Out the money
For a call, an option is out the money when an option's strike price is higher than the market price of the underlying asset.

### Premium
The price paid upfront for the purchase of the Reset Warrant.

### Put warrant
A contract giving the holder the right, but not the obligation, to sell a share for the exercise price at a future date. (See also European style and American style.)

### Reset date
Date at which the strike price of the warrant will reset if favourable to do so.

### Reset strike price
Closing level of the underlying share or index on reset date.

### Strike price
The price at which a specific option contract can be exercised. For call options, the strike price is where the security can be bought (up to the expiration date), while for put options the strike price is the price at which shares can be sold.

### Theta or time value
The additional value of a warrant (if any) over intrinsic value due to the remaining term of the warrant.

### Vanilla Option
An option is a contract that gives the investor the right, but not the obligation, to buy or sell a financial instrument at a specific price (strike price) and time. With a Vanilla European option, the contract terms allow the option to be only on the expiration date.

### Volatility
A measure of the variation in a price over time.

### Warrant
An option contract traded on the JSE Limited, issued by an institution such as The Standard Bank of South Africa Limited.

## Disclaimer



### Authorised financial services and registered credit provider (NCRCP15)
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