SGX

Daily Leverage Certificates

Frequently Asked Questions

DLCs at a Glance

7x

Leverage
Fixed leverage of up to 7 times both long and short.

Pricing Structure
No margins.
No implied volatility impact.
No time decay impact.

Transparency
Transparent pricing due to tradability of the products on exchange.

Long or Short
DLCs offer the flexibility to trade both rising and falling markets.

Risk Management
Low capital outlay and loss limited to invested amount.

Airbag
Mitigates the investor's rate of loss in extreme market conditions.

1. What are DLCs?

Daily Leverage Certificates (DLCs) offer investors fixed leveraged returns of 3 to 7 times of the daily performance of the underlying asset, be it a rising or falling market. The basic principle is simple - if the underlying index moves by 1% from its closing price the previous day, the value of the 3x DLC will move by 3%, and that of a 7x DLC will move by 7%.

DLCs are designed to be traded over short periods of time, predominantly on an intra-day basis. The DLC offers the flexibility to trade both rising and falling markets. For each underlying and leverage level, there is a long and short DLC available.

A bullish investor who thinks that the underlying index is set to rise over the trading day can select a 3x Long DLC, which will rise in value by 3% for each 1% rise in the underlying index (before cost & fees).

A bearish investor who expects the underlying index to fall can instead select the 3x Short DLC, which will rise in value by 3% for every 1% fall in the underlying index (before cost & fees).

At the same time, if the market goes against the investor, the DLC will amplify losses in the same way. The investor's entire invested capital is at risk but not more than the invested capital.

Investors should note that the leveraged 3 to 7 times exposure to the daily performance of the underlying index is on the basis of a one-day holding period. If held over a period longer than one day, actual returns will deviate from the projected leverage exposure. In addition, even with a one-day holding period, there will be tracking errors due to cost and fees.

DLCs are a “Specified Investment Product” (“SIP”). Under MAS’ guidelines to enhance safeguards to retail investors, brokers must assess if investors have the relevant knowledge and experience before they can invest in “Specified Investment Products”. SIPs are products that have structures, features and risks that may be more complex and include DLCs, structured warrants, synthetic ETFs, futures and options. Investors who wish to trade DLCs need to complete a customer account review with their respective broker. Alternatively, investors may assess their qualifications to trade SIPs or enhance their product understanding through the **SGX online education program.**

2. How to buy and sell DLCs?

Similar to shares, investors may buy and sell DLCs on the SGX securities market through your broker or your online trading account. DLCs are also settled on the same basis as share transactions, which is on the third business day after the trade date, or T+3.

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3. What are the obligations of a Designated Market Maker? How do market makers determine the spread and volume of their quotes?

A Designated Market Maker (“DMM”) (i.e. a market-maker registered with SGX-ST) is required under the SGX-ST Trading Rules to provide competitive bid and offer quotations on a continuous basis, within the maximum spread, and for not less than the minimum quantity, set out below:

- Maximum Bid and Offer Spread – 10 ticks or $0.20, whichever is greater
- Minimum Quantity subject to Bid and Offer Spread – 10,000 DLCs

Please refer to Chapter 5 of the SGX-ST Rules on Designated Market-Maker and Directive No. 3 on Obligations of a Designated Market-Maker for more information.

In addition, apart from market-makers, there may be other investors who are actively buying and selling a specific DLC. The forces of supply and demand from both the market makers and the other market participants will determine the prevailing bid and offer prices of a DLC at any one time.

4. Are there circumstances in which the DMM may not provide bid-offer quotes?

DMMs are required to make a market for their DLCs during the normal trading hours. If there is no quotation provided for a DLC on-screen when the underlying market is open, investors can also contact the respective issuer or DMM to request for quotes. See answer to question 24 below for the issuer’s contact details.

However, there are circumstances in which DMMs will/may not be able to provide bid and offer prices which will be specified in the listing documents of the respective DLC. Some examples of the circumstances include

- during the pre-market opening and five minutes following the opening of SGX-ST on any trading day;
- when trading in the underlying is suspended or limited in a material way for any reason;
- when trading in the DLC is suspended or limited in a material way for any reason;
- when the stock market experiences exceptional price movements and volatility;

- when the DLC issuer and/or DMM faces technical problems affecting the ability of the DLC issuer and/or DMM to provide bid and offer prices;
- when the DLC issuer is unable to hedge its exposure or unwind an existing hedge.
- The circumstances may vary for different issuers and DLCs. Investors are advised to refer the listing documents accordingly.

5. How to decipher the counter name of DLCs

The counter name for the DLCs has the following naming convention e.g. "DLC SG3xLongHSI 200714" can be broken down into [DLC] [Issuer][Leverage level][Long or Short][Underlying index] [Expiry date in YYMMDD format i.e. 14 July 2020]

6. There are DLCs on the same underlying index, but with different features. What factors should an investor consider in picking a DLC?

There could be two or more DLCs on the same underlying index but you will notice that the DLCs will have a different feature, for example it may be a different issuer or a different leverage level or a different expiry date. In the first scenario, there could be two different issuers listing the same 3x Long HSI DLC. In the second, there could be the same issuer listing a 3x Long HSI DLC and a 5x Long HSI DLC. In the last scenario, there could be the same issuer listing another 5x Long HSI DLC with a longer dated expiry. You can spot the difference in either the issuer, the leverage level or expiry date by looking at the counter name as described above.

7. Is DLCs a zero-sum game? Are issuers engaged in a zero-sum game with DLC investors?

When issuers issue DLCs, they do not take a view on the future direction of the underlying asset but rather hedge the risk arising from the sale of the DLC to investors. Such hedging may be done through various means including buying or selling futures on exchanges. Any rise or fall in the value of the DLC will be offset by a change in the value of the underlying hedge. Therefore issuers not engaged in a zero-sum game with the DLC investor.

8. Where can I access DLC prices?

You can access prices on SGX website under "Market Information", the issuer's website as well as through your stockbroker.

9. Is my invested capital at risk?

Your entire invested capital is at risk. Before trading you should understand the nature of DLCs and the extent of your exposure to risk. In the event the value of a DLC reaches zero /becomes worthless, the issuer may request that the DLC be suspended and subsequently apply for them to be de-listed. Investors should also refer to other risks listed in the listing documents published by the issuer which can be found under "Company Information" on the SGX website.

10. Is there a knock-out feature similar to knock-out warrants?

Unlike knock-out warrants, DLCs do not have a knock-out barrier. However there is an airbag mechanism, which if reached or exceeded by the underlying, causes the DLC to re-set intraday. This reduce the rate of loss of an extreme market move in the underlying index in one day and prevents an investor from losing more than his invested capital. For more information, please refer to the issuers' product guide or the SGX Products page [www.sgx.com/DLC]

11. What happens at expiry?

DLCs have a limited life with a maximum tenure of 3 years. At expiry the final exercised value of the DLC is calculated and automatically paid to investors.

12. Do I face counterparty risk?

Yes, these products are issued by the issuer and may be guaranteed by a guarantor. Any failure of the issuer or guarantor to perform obligations when due could result in the loss of all or part of an investment. You should also refer to risks listed in the listing documents published by the issuer which can be found under "Company Information" on the SGX website.

13. How will dividend pay-outs affect the price performance of the DLC?

DLC will track the total return index of the specific underlying market where the dividends are reinvested and as such will not have an impact on the price performance of the DLC.

Every index has a few available versions; the key ones are a price return and the total return index. The latter provides an overview of e.g. the performance of the index stocks including dividends, so both the appreciation in the stock prices as well as the dividend payouts. All dividends paid are reinvested in the total index to keep to proper weights. For products tracking an index, they should track the total return index as if a product would only track the price index, the investor would miss out on sizable returns paid as dividends. Suppose index trades at 3,000 points and one company would pay an equivalent of 10 points in dividend payout. The price return index would drop to 2990 as the specific company's share price would be impacted. The total return index would however remain at 3,000 (10 points are reinvested) and is therefore unaffected. DLC investors will not be impacted by this dividend payment.

14. What happens when the underlying market is closed?

The DLCs will be open for trading during SGX Securities market trading hours (9am-12pm and 1pm-5pm). However the designated market maker would not quote in the market if the underlying market of the respective DLCs is closed. For example, in the case of a DLC with a HSI underlying, it would mean that the DMM is only required to provide quotes for the DLC when the HSI (Hong Kong stock market) is open, which is from 9:30am – 12pm and 1pm – 4pm.

15. How does the airbag mechanism help investors?

An airbag mechanism is built into the product to slow the rate of loss in the value of DLCs in extreme market conditions. Each DLC listed will have a pre-set trigger for the airbag mechanism. This trigger is usually activated upon a 10% movement in the underlying index for a 7x DLC and a 5x DLC and a 20% movement in the underlying index for a 3x DLC (based on the closing price of the underlying index in the previous trading day). The airbag mechanism will only be triggered upon movements of the underlying index that go against the direction of the product. For example, if the underlying index falls by 10%, (a) the airbag mechanism for a 7x Long DLC will be triggered as the value of the DLC will decrease by 70% (7 x 10%) with the fall in the underlying index; but (b) the airbag mechanism for a 7x Short DLC will not be triggered because with the fall in the underlying index, this DLC will increase in value by 70% (7 x 10%). For certain DLCs, the airbag mechanism may not be available or triggered in certain circumstances. Investors should read all listing documents provided by the issuer for the specific airbag mechanism for each product.

If the underlying index moves by the pre-determined percentage (e.g. 10%) during the trading day of the DLC, the airbag mechanism triggers an intraday re-set. The re-set takes place over a 30 minute period where trading of the DLC will be suspended. Following the re-set, the performance of the DLC is based on the New Observed Level which is determined as the lowest value of the underlying Index for the Long DLC (respectively the highest value for the Short DLC) during the 15 minutes period after the airbag trigger. Thus if the market continues on a downward trend, the airbag mechanism serves to slow the rate of loss for investors.

Example:

Assume an investor bought a 7x Long DLC on Tuesday and the DLC had previously closed on Monday at a price of S$2.00 and the underlying index closed at 1,000 points. If on Tuesday, by 11.00 am, the underlying index drops 10% (from 1,000 to 900 points), this would translate into a 70% loss on the DLC, leaving it at a price of S$0.60. At this point the airbag mechanism is triggered and the DLC issuer will request SGX to suspend trading in the relevant DLC for 30 minutes from 11.00am to 11.30am.

The performance of the DLC after the suspension will be based on the New Observed Level. Assuming the New Observed Level equals the airbag trigger point (900 points), if the underlying index were to fall another 4% after trading resumes at 11.30am, the loss to the DLC would be 28% (i.e. 7 X 4%) of S$0.60 (instead of the previous close of S$2.00), which will leave the DLC at a value of S$0.43.

Without the airbag mechanism, an additional 4% fall in the underlying index would have left the DLC at a lower value of S$0.04 (total of 14% fall in underlying index multiplied by 7 times leverage would result in a 98% loss on the DLC based on the previous close of S$2.00). In a more extreme case where the underlying index falls by an additional 5%, the DLC would be worthless. This is because the total fall of 15% in the underlying index would result in a 100% loss on the 7x Long DLC if there is no airbag mechanism.

16. Whom are DLCs suited for?

Daily Leverage Certificates (DLCs) are for investors who are willing to accept the risk of substantial losses up to the principal investment amount, possibly within a very short timeframe. Investors should also have sufficient understanding of the product and should possess either a high level of knowledge or sufficient trading experience to properly evaluate and assess the product structure, associated risks, valuation, costs and expected returns.

All investors need to be **Specified Investment Products (SIP)** qualified to invest in DLCs. DLCs seek to achieve short-term investment results that correspond to the daily magnified performance of the underlying benchmarks.

17. How might I use DLCs?

DLCs can complement a portfolio by offering enhanced returns over a shorter time frame. You can take advantage of daily market news or when expecting economic events. Provided that the markets go the right way for you, these amplified returns can be an effective way to boost the overall return of your portfolio.

18. Where can I find more information on the leveraged indices?

The long and short leveraged indices (if available) for the products will be calculated and disseminated by the respective calculating agents. For some DLCs there is no separate leveraged underlying index but instead the DLCs have the leverage formula incorporated in their payoff. Although the availability of a leveraged index makes it more convenient for an investor to track the corresponding value of the DLC, it should be noted that an investor can expect the same payoff with or without the leveraged index, i.e. a 1% move in the MSCI Singapore will correspond to a 5% move in the 5x DLC.

To identify if the DLC has a leveraged underlying index, please refer to the “Market Information” page on SGX.com where the column labeled ‘leveraged index’ will indicate if there is a leveraged underlying index for the DLC.

19. Where can I find the list of DLCs to trade?

The list of available DLCs can be found under “Market Information” on the SGX website.

20. How are the DLCs different from Leverage and Inverse (L&I) Products?

The setup of L&I Products is different from DLCs despite them have the same payoff scenarios. An L&I Product has a fund structure while the DLC is a structured product issued by a bank. L&I Products are only one to two times leverage while the DLCs are three to seven times leverage.

21. Where can I learn more about DLCs?

SGX Products page www.sgx.com/DLC and issuer’s Website dlc.socgen.com

22. What are the Cost & Fees?

Investors trading in and out of a DLC on the same day have to pay a brokerage commission and SGX trading and clearing fees, and the spread on the bid & ask prices (the difference between the offer price paid when buying the DLC and the bid price received when selling the DLC). Overnight positions will incur additional cost charged by the issuer. For more information on the overnight costs, please refer to the issuers’ product guide and website.

23. How are DLCs different from CFDs and Structured Warrants?

DLCs and Structured Warrants are products traded on SGX-ST whereas CFDs are products traded over the counter (not on an exchange). The leverage level for DLCs is a maximum of 7 times and is fixed while the leverage level for CFDs can be up to 20 times and is margin based. The leverage level for Structured Warrants can vary from 5-50 times depending on the underlying value and other optionality features. You can potentially lose more than your invested capital when trading CFDs whereas losses for DLCs and Structured Warrants are capped at the total invested capital. For a more detailed overview comparing the three products, please refer to the DLC investor guide published on www.sgx.com/DLC.

24. Who can I contact if I have more queries on DLCs?

Investors can write in to asksgx@sgx.com and our customer service personnel will reply within 3 business days. Investors may also call the SGX main line at +65 6236 8888. Alternatively, visit the issuer’s website at dlc.socgen.com or call their Singapore hotline at +65 6226 2828.

25. Would the market price of a DLC deviate from the official intrinsic value of the DLC, and why?
Yes. During the trading day, the DLC market price could deviate from its official intrinsic value due to any one or combination of the following reasons:

- Potential difficulties in the issuer's hedging activities of the Underlying Index as a result of cost, fees, liquidity, volatility, access (e.g. underlying market is closed) etc.
- If any constituent stocks of the Underlying Index is halted or suspended from trading, there could still be a market value of the constituent stock (i.e. the market's forward looking expectation of the constituent stock price which is usually reflected in other derivatives of the Underlying Index such as the Futures market). The market value of the constituent stock is not reflected in the Price Return Index and therefore may cause a difference between the published Price Return Index and the market value of the Underlying Index. Hence, the DLC's bid/ask quotes and market price may be at a discount or premium to the official intrinsic value.

26. What happens when an underlying constituent stock of the Underlying Index is halted or suspended from trading?

- If any constituent stocks of the Underlying Index is halted or suspended from trading, there could still be a market value of the constituent stock (i.e. the market's forward looking expectation of the constituent stock price which is usually reflected in other derivatives of the Underlying Index such as the Futures market). The market value of the constituent stock is not reflected in the Price Return Index and therefore may cause a difference between the published Price Return Index and the market value of the Underlying Index. Hence, the DLC's bid/ask quotes and market price may be at a discount or premium to the official intrinsic value.
- The degree of deviation from the official intrinsic value would depend on the size and weighting of the constituent stock of the Underlying Index, as well as the market value of the constituent stock compared to its last traded value before the suspension.
- The deviation would persist for as long as the constituent stock is halted or suspended but should again reflect the official intrinsic value once the stock resumes trading.