COMMERZBANK

Product Group

Fixed Income, Fixed Income Funds, Fixed Income ETFs

In this information sheet, Commerzbank provides information on the underlying characteristics as well as the opportunities and risks of fixed income, fixed income funds and fixed income ETFs product groups.

General characteristics and investment opportunities
Fixed income securities are interest-bearing securities, often also called bonds, debt obligations or debentures. The investor lends a certain amount of money to the issuer, e.g. a non-financial or a financial company, and in return receives a bond denominated in euro or a foreign currency. Fixed income securities represent a claim to capital repayment and, typically, to fixed or variable interest payments as compensation for the provision of capital. Their yield is determined by the nominal interest rate, the issue or purchase price, the redemption price and the term of the security. Individual characteristics, such as interest rate or maturity, are specified in the terms and conditions of the bond issue.

Typical product characteristics
Fixed income securities from public and private issuers are typically not collateralised. Hence, it is solely the financial strength or creditworthiness of the issuer that determines whether interest and redemption payments associated with the issued bonds will be met on time and in full. Credit ratings from corresponding agencies that assess the probability of default are an established tool for making investment decisions. Bonds with a high rating typically offer a lower yield than bonds with a lower rating.
Asset-backed bonds, e.g. Pfandbriefe (German covered bonds), are a special type of bond. Mortgage Pfandbriefe are bank bonds backed by senior mortgages, while public-sector Pfandbriefe are bank bonds backed by public-sector claims. Both are issued in accordance with the provisions of the German Pfandbrief Act (Pfandbriefgesetz).
The collateralisation greatly reduces the investor's exposure in the event of insolvency. However, despite legally required excess coverage, the collateralisation may not be sufficient to fully service the debt securities.

In a fixed income fund, a capital management company pools funds from many investors. The company invests these funds in different individual fixed income securities from different issuers according to a defined investment strategy, therefore, following the principle of risk diversification and managing them professionally. The price of a fund unit depends on the price performance and the income generated by financial instruments held by the fund, such as securities and derivatives, and may therefore be subject to considerable fluctuations. However, a broad risk diversification reduces the reliance on the performance of individual financial instruments. This diversification effect decreases, though, if the investment fund is dedicated to specific investment themes, such as specific countries, currencies or maturity segments.

Fixed income exchange traded funds (ETFs) are a special type of fixed income fund. They aim to track the performance of a particular index as closely as possible. This is achieved either by direct investment in securities or by replication in the fund assets, for example by using so-called swaps. A swap-based ETF usually tracks the performance of the underlying index more accurately because, for example, corporate actions of index constituents do not trigger transactions in the fund portfolio. A swap-based replication adds the particular risk that the swap partner may no longer be able to meet its payment obligations under the swap transaction (counterparty risk). To minimise the default risk of the swap counterparty, it provides e.g. cash or securities in sufficient amounts as collateral. The fund investor is exposed to the risk that, in the event of insolvency, this collateral may not be sufficient to fully satisfy the claims.

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

Issuer risk - also referred to as default risk - when the issuer fails to meet its obligations or can only meet them partially, for example because of insolvency. Bonds issued by banks are subject to special regulations. If the issuing bank runs into financial difficulties, a regulatory intervention may result in a bailout of the bank, partial or total loss of the investment, or a compulsory conversion into equity, such as shares. As a rule: The worse the credit rating of an issuer, the higher the default risk, but also the higher the risk premium and the resulting yield. Bonds are generally not covered by deposit insurance. Sustainability-related decisions relating to the environment, social aspects and corporate governance also impact on the issuer.
Interest rate and price risk - when interest rates rise, bond prices generally fall. A downgrade in the issuer's credit rating reduces the value of a bond during its term.
Liquidity risk - during the term, investors may not be able to sell the security or may only be able to sell it at a possibly much lower price.
Foreign currency risk - Investors are exposed to currency risk when investing in a foreign currency denominated security as performance could be adversely affected by exchange rate movements.
Early redemption and reinvestment risk - investors are exposed to the risk that the issuer may exercise an ordinary or extraordinary option to call the fixed income security at a time or in a financial market environment that is unfavourable for the investor, as the investor can reinvest the redemption amount only on less favourable terms.

Some bonds of foreign issuers have features not typically applied in Germany, which are specified in the terms and conditions of the fixed income security. This may result in additional risks.

Special characteristics of investment funds
Holders of investment fund units are subject to special risks, for example if unit redemption may temporarily be suspended due to insufficient fund liquidity. That could occur if many investors wish to redeem their units at the same time, or that a fund may be liquidated in an orderly manner.

When funds experience liquidity shortages, fund management companies have certain options to address them. They may, for example, introduce redemption notice periods. This means investors would have to notify the fund company of their intention to redeem their fund units some time in advance.

The fund company may also impose redemption restrictions. For example, fund companies may choose not to meet redemption requests for a certain period of time, or only partially, if the number of redemption requests exceeds a certain threshold.

Furthermore, a fund company may allocate transaction costs arising from unit redemptions or unit issues based on the cost originators. These transaction costs may be included in the calculation of the net asset value of a fund, up to a predefined rate.

These options are intended to prevent fund companies from having to completely suspend unit redemptions, which would be even more detrimental to investors.

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

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