Product Group

Structured Interest Rate Products

In this information sheet, Commerzbank provides information on the underlying characteristics as well as the opportunities and risks of the Structured Interest Rate Products product group.

General characteristics and opportunities
Structured Interest Rate Products are contractual agreements between Commerzbank AG and customer. They are referred to as OTC derivatives because they are derived from a so-called underlying instrument (in this case reference interest rates). The valuation of these derivatives is determined by the trend of the relevant reference interest rate. OTC (**O**ver-**T**he-**C**ounter) relates to over-the-counter derivatives that are individually tailored to customer needs.

The motivation for using these instruments can vary widely. Users may want to hedge an existing position with a derivative as an offsetting position (hedging). In this case, the purpose of the derivative is to reduce risks from an underlying transaction.

If derivatives are used to bet on a specific market trend or interest rate change without reference to an underlying transaction, this constitutes a speculative transaction. In this case, investors cannot offset losses incurred against gains in an underlying transaction. Commerzbank AG only offers derivatives transactions to customers relating to underlying transactions.

Structured Interest Rate Products comprise several linked swap and/or option components. The interest rate hedges in this product group provide a hedge for one or more dates, allowing for reliable calculations and better planning of interest rate positions. Some products offer the opportunity for the customer to benefit from a favourable trend in the reference interest rate. In these cases, however, the hedged interest rate is less favourable than that of a comparable conventional interest rate swap. The interest rate applicable on a particular date is determined by the individual product terms.

If the customer pays a premium upon conclusion, the customer can improve the hedged interest rate and/or the product terms. Conversely, the terms become less favourable if the customer receives a premium payment.

In the following we describe selected products of the product group.

Collar
In a Collar, a compensation payment is made, if the reference interest rate on the fixing date trades outside a specified range. In this way, the customer secures a guaranteed minimum or maximum interest rate while also having a limited chance of achieving a more favourable interest rate.

Interest Rate Swap with Floor or Cap
In an Interest Rate Swap with Floor or an Interest Rate Swap with Cap, the customer and the Bank exchange fixed and variable interest payments over a defined period, for example on a quarterly basis. The amount of the variable payment primarily depends on the development of a reference interest rate and the underlying nominal amount. An Interest Rate Cap (Call Option) sets an upper barrier on the variable rate, while an Interest Rate Floor (Put Option) sets a lower barrier. A purchased Interest Rate Cap protects against rising interest rates, while an Interest Rate Floor guarantees a minimum interest rate.

Cap-Swap-Combination
The product is suitable for customers who, e.g., are paying a variable interest rate in a financing arrangement and are concerned that interest rates might rise during the term. It consists of two phases. In the “Cap phase”, customers benefit from a low reference interest rate and receive a compensatory payment if the reference interest rate on the determination date exceeds the Cap. In the “Swap phase”, the customer pays a fixed amount, while in return receiving a variable amount that depends on the reference interest rate.
In addition, a compensation payment can be agreed for the Swap phase, specifically if the reference interest rate is determined to have a negative value (Floor). This allows customers to avoid having to pay a variable amount in addition to the fixed amount.

Double Swap
The Double Swap also consists of two phases. The Bank pays a fixed amount on the respective payment date of an interest period during the first phase. In the second phase, the Bank pays a variable amount, depending on the reference interest rate, if it is positive. If the reference interest rate is negative, the customer must pay the absolute value of the variable amount to the Bank. In return, the customer pays a fixed amount to the Bank on the

respective payment dates of an interest period over the entire term. The counterparties can agree on a Floor in a Double Swap as well.

Interest Rate Swap with Opportunity
In an Interest Rate Swap with Opportunity, the customer pays a fixed interest rate if the reference interest rate on the determination date is above an interest rate barrier. Otherwise, the cash flows associated with this product offset each other. This allows the customer to benefit in his underlying transaction from a decline in the reference interest rate below the interest rate barrier.

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

If the amount payable exceeds the amount receivable, the customer incurs a financial loss. The loss is greater the more the reference interest rate deviates from the agreed fixed interest rate. If the reference interest rate drops to zero, regularly only the fixed interest rate is paid, and the variable interest payment is omitted. If the reference interest rate drops into negative territory, the variable interest payment may have to be made in addition to the fixed interest payment. This payment obligation may not be matched by a corresponding income stream from the underlying transaction.

Fair value risk: The fair value of a transaction is mainly influenced by the actual and expected change in the reference interest rate (volatility), the interest rate level, forward interest rates and the remaining term. If the transaction is terminated early, the customer will have to recognise a loss on termination in case the fair value is negative.

Liquidity and trading risk: In special market situations, it may not be possible to liquidate a financial instrument at all or at a fair market price.

Default risk: In the event of insolvency of Commerzbank AG as your counterparty, Commerzbank AG may default on some or all of your existing claims. Moreover, if Commerzbank's going concern as a financial institution is jeopardised due to bank supervisory regulations, customers are exposed to a default risk in the form of a bail-in even before insolvency, i.e. in the event of a resolution procedure, the relevant resolution authority may order the transaction to be terminated early. If the termination results in a right to payment for the counterparty, the resolution authority might order this to be partially or fully written down or converted into equity (shares or other partnership interests). If Commerzbank AG does not fulfil its obligations under the financial instrument, does not pay or is unable to pay, the customer loses part of the investment or suffers an unlimited financial loss.

The financial instrument and the underlying transaction are legally separate transactions and can be entered into or terminated separately. The financial instrument can only be terminated early by mutual agreement. The financial instrument may have a negative fair value at the time of the transaction due to structured costs and differing buying and selling prices (bid/ask spread). The cancellation or non-fulfilment of the customer's underlying transaction does not result in automatic termination of the financial instrument. In such case, the economic objective pursued at the time of the transaction by the customer may have to be reassessed.
If the payments from the financial instrument and the underlying transaction differ, e.g. due to different investment horizons, the customer might experience a financial loss.

Further information and costs:
For further details on these aspects and the products, please refer to the relevant key information document. When acquiring, holding and eventually selling derivatives, costs will impact their fair value. For further details, please refer to the respective cost information sheet before entering into a derivatives transaction.

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