Danske Bank

Information about risks associated with trading in foreign currency and derivatives

Effective from 18 March 2021

Introduction

This information sheet is provided to clients who enter into foreign currency and derivative transactions. The purpose is to give you a clear understanding of the risks associated with these specific types of products.

Derivatives are financial instruments that typically derive their value from an underlying asset. The underlying asset may be market assets such as interest rates, foreign exchange rates, equities, commodities, or other financial or economic interests or property of any kind.

For the purpose of this information sheet, derivatives are defined as over-the-counter (OTC) products traded directly with us as principal, including swaps, options, forwards and futures on any type of underlying asset.

This information sheet aims to give you a clear understanding of the risks involved, but may not necessarily describe all of the risks and other significant aspects of trading in OTC derivatives. In light of the risks, you should enter into such transactions only if you understand the nature of the financial instruments you are trading and the extent of your exposure to risk.

Please also refer to product-specific fact sheets, which set out in more detail the features of the derivative products that we offer. Fact sheets are provided to you before you begin trading and further copies are available from us on request.

Before trading

Trading in derivatives may entail significant risks, including the potential for large financial losses. The risks depend on the type of transaction and the nature of the underlying asset.

You need to carefully consider whether entering into a particular trade is right for you, including in relation to your experience, objectives, financial resources and other relevant circumstances.

We will never provide you with investment, tax or legal advice. If you believe you need assistance in this regard or are in any way unsure of the suitability of a particular transaction, you should obtain advice from an independent professional.

In deciding whether to trade an instrument, you should be aware of the following risks:

Market risk

Market risk is the risk of loss arising from adverse changes in the value of a derivative instrument due to changes in the underlying asset. Similarly, adverse changes in the volatility of or correlation or relationship between these factors may contribute to losses occurring.

The market risk of a derivatives transaction may increase if a derivatives transaction includes complex pay-out calculations or a leveraged element. Transactions with such features may be subject to significant changes in value because of relatively small changes in the prices or levels of an underlying asset or other market factor. This risk will be increased where the underlying asset is particularly volatile. Such features include, but are not limited to, leverage, multipliers and option-like pay-outs, transactions with knock-in or knock-out rights, etc.

Leverage

If you enter trades that involve leverage (also known as gearing or margining) and those trades go against you, you can lose more than the amount of your initial investment. This is because leverage multiplies the effects of small movements in price. As a result, you may be required to make further payments to us. You may also be required to make further payments to meet your margin requirements and maintain your positions as a result of market volatility. It is therefore important that you monitor any leveraged trades that you enter very closely.

Credit risk

Credit risk is the risk that a counterparty fails, or delays, in meeting its contractual payment obligations because of a dispute over the terms of the contract (whether or not bona fide) or because of the insolvency, bankruptcy or other

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credit or liquidity problems of the counterparty.

Because of the credit risk, our and your (and your guarantor's, if any) creditworthiness is a material consideration when entering into or determining the terms of a derivatives transaction, and this has an impact on the pricing of the transaction.

Liquidity risk

Liquidity risk is the risk of losses attributable to a lack of liquidity (for example, very few active market participants) in a particular market. This is usually indicated by wide bid/offer spreads and very few transactions being carried out in a particular product or market.

The risk is that changes in the underlying market price may be infrequent but very large, and that it is not possible to unwind or transfer a particular transaction in a timely manner, at near the price you had expected, or at all.

In assessing this risk, you should consider that derivatives transactions may be terminated, modified or transferred pursuant to the terms of the particular transaction or by mutual agreement of the parties only. If our consent is required, we may withhold it for a variety of reasons, which we are not required to disclose to you. Further, even though market-makers and dealers may quote indicative prices or mid-market valuations, there is no assurance that another dealer is willing to accept a transfer of your rights and obligations under a particular transaction between you and us.

Accordingly, it may not be possible for you to modify, terminate or transfer your rights and obligations, or your exposure to the risks associated with a particular transaction, prior to its scheduled termination date.

Pricing risk

For complex derivatives transactions, pricing may be determined using various assumptions and mathematical models. Pricing risk is the risk that these models do not accurately reflect conditions in the market and that mispricing causes a financial loss.

Operational risk

In this context, operational risk covers a wide-ranging number of risks such as losses arising from inadequacies in or failures of procedures, systems or controls in connection with derivatives transactions.

Examples of operational risks include

- recording, monitoring and quantifying risks and contractual rights and obligations
- making payments or deliveries
- exercising rights before they expire, including option rights, in a manner that complies with the terms of the relevant transactions
- meeting regulatory filing, reporting and other requirements
- detecting human errors or computer systems failures

Financial losses from operational risk can be substantial, including the entire value of a transaction, for example where an unexercised and in-the-money option expires.

Legal risk

Legal and documentation risks include the risk that transactions and their contractual arrangements may not be legally enforceable or that the conduct of the parties violates applicable laws and regulations.

In general, there is less government regulation and supervision of transactions in OTC derivatives than in derivatives traded on an exchange. Counterparties to OTC derivatives are not afforded the same protections as may apply to those trading on recognised exchanges, such as a performance guarantee.

Contractual agreements

The contractual agreements relating to transactions in derivatives contain various events of default provisions entitling a non-defaulting party to terminate all or some of the transactions under such an agreement. If you are

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subject to events that may constitute a default under the contractual agreement, we have no obligation to consider your interests in determining whether or when to terminate a transaction.

There are EU-level rules on recovery and resolution for distressed financial institutions such as banks (the BRRD or Bank Recovery and Resolution Directive which has been retained as implemented and amended in UK law following the UK's departure from the European Union) to be applied under certain conditions as an alternative to bankruptcy proceedings. The designated national resolution authority may take a variety of actions of a preventive, early intervention or resolution nature, which may lead to restrictions on your ability to terminate and otherwise exercise your rights under a contractual agreement. Further, under certain conditions, the resolution authority has a number of resolution tools and powers ('harmonised toolkit'), including the right to exercise certain so-called bail-in powers, involving the write-down of certain eligible liabilities of the distressed institution, delay performance and/or convert certain claims against the distressed institution, into other types of claims, such as shares.

A safeguard under the BRRD is that counterparties to a distressed institution cannot incur losses greater than what they would suffer if the institution were to go into bankruptcy.

Taxation

The tax treatment of your trading activities depends on your individual circumstances and may change in the future.

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