Risk Disclosure for Interest Rate Option (IRO)

PRODUCT DESCRIPTION

Interest Rate Option (IRO) is a derivative financial instrument that gives the buyer the right, but not the obligation, to demand payoff at the end of interest rate period, based on the notional principal amount and the pre-agreed interest rate as a Cap rate and Floor rate (Strike rate). All cash flows and payments are denominated in the same currency as the notional principal amount.

There are two types of options as follows.

- **Cap**

A Cap gives the buyer the right to exercise the periods of caplets (single call IRO) and receive the amount of cash settlement at the end of each periods, in case the reference rate is higher than the cap rate (Strike rate).

- **Floor**

A Floor gives the buyer the right to exercise the periods of floorlets (single put IRO) and receive the amount of cash settlement at the end of each periods, in case the reference rate is lower than the floor rate (Strike rate).

Clients may combine each type of IRO strategies to create option combinations with the derivative products such as IRO strategies with IRS transactions called Custom IRS transactions, and IRO strategies with CCS transactions called Custom CCS transactions.

For example, borrowers may use IRO to estimate the maximum of interest rate, i.e. to buy the cap in order to estimate the maximum interest rate. The option buyer will take an advantage when the interest is expected to rise, and receive the amount of cash settlement in case the reference rate is higher than the cap rate. Also, the Floor option can be used to estimate the minimum interest rate. The option buyer will take an advantage when the interest is expected to fall, and receive the amount of cash settlement in case the reference rate is lower than the strike rate.

Potential Client

Option Types	Client Buying Option
Cap	Clients with floating rate liabilities For example, a client has an obligation to pay the floating rate with loan underlying. The option will provide the right for the clients to estimate the maximum interest rate. If the reference rate is higher than the cap rate, the client will have a positive payoff. The cost of the protection is an option premium.
Floor	Clients with floating rate assets. For example, a client has a receivable from floating rate assets with loan underlying. The option will provide the right for the clients to estimate the minimum interest rate. If the reference rate is lower than the floor rate, the client will have a positive payoff. The cost of the protection is an option premium.

Profit and Loss Analysis
Strategy : Client Buy Cap with floating-rate liabilities

Example : A client with 100 MTHB 3-year loan has annual interest payment of Compounded THOR + 2.00% to a lender. The client expects that the Compounded THOR will rise over 2.50% and wishes to reduce the loan interest payment by buying Compounded THOR Cap with 100 MTHB notional at Cap rate 2.50%, 3-year tenor, annual payment. The payoffs to the client are summarized below.

Summary

- **Loan**: Notional 100 MTHB 3-year Loan with Compounded THOR + 2.00%.
- **Expectation**: Client expects the Compounded THOR to rise over 2.50%.
- **Client buys Cap at Cap rate 2.50%**: The client receives an interest payoff if the Compounded THOR is higher than the Cap rate. However, the client receives nothing if the Compounded THOR is lower than or equal to the Cap rate.
- **Client pays premium at 0.14% of notional 100 MTHB** (Est: 140,000 THB per period)

The maximum loss to the client is limited to the premium paid.

The maximum gain to the client is unlimited depending on how much the Compounded THOR rises over the Cap rate.

Profit and Loss of Buying Cap at each settlement period (Compounded THOR falls)

period	Notional	Compounded THOR	Loan spread	(1) Interest amount	Cap rate	(2) Option payoff	Option Premium percent	(3) Option premium	(1)+(2)+(3) Net Cashflow
1	100 MTHB	1.75%	2.00%	-3.75 MTHB	2.50%	0	0.14%	-0.14 MTHB	-3.89 MTHB
2	100 MTHB	2.00%	2.00%	-4.00 MTHB	2.50%	0	0.14%	-0.14 MTHB	-4.14 MTHB
3	100 MTHB	2.25%	2.00%	-4.25 MTHB	2.50%	0	0.14%	-0.14 MTHB	-4.39 MTHB

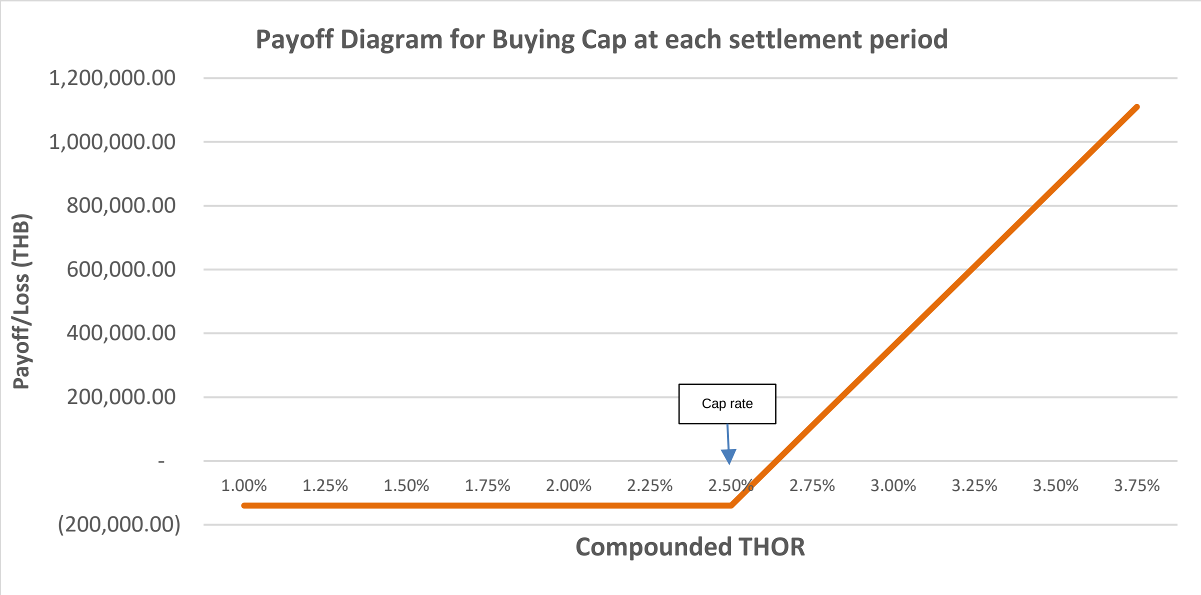
"-" Client pays, "+" Client receives

Profit and Loss of Buying Cap at each settlement period (Compounded THOR rises)

period	Notional	Compounded THOR	Loan spread	(1) Interest amount	Cap rate	(2) Option payoff	Option Premium percent	(3) Option premium	(1)+(2)+(3) Net Cashflow
1	100 MTHB	2.25%	2.00%	-4.25 MTHB	2.50%	0	0.14%	-0.14 MTHB	-4.39 MTHB
2	100 MTHB	2.50%	2.00%	-4.50 MTHB	2.50%	0	0.14%	-0.14 MTHB	-4.64 MTHB
3	100 MTHB	2.75%	2.00%	-4.75 MTHB	2.50%	+0.25 MTHB	0.14%	-0.14 MTHB	-4.64 MTHB

"-" Client pays, "+" Client receives

Payoff Diagram of Buying Cap at each settlement period



Transaction process

If the client would like to enter into Interest Rate Option (IRO) with the Bank, the client is required to follow the steps below:

1. The client contacts the Relationship Manager (RM) for credit line set-up, and signs the product risk disclosure.
2. The bank sends the indicative IRO rate and other related indicative rate to the client.
3. After the client agrees with the IRO rate, the client will receive initial confirmation via email and the client will need to sign such confirmation or reply the email to confirm the transaction.
4. The client will then receive a formal long-form confirmation or short-form confirmation, and will need to sign and return the confirmation back to the bank with authorized signatures.

Required documents for transaction

- Know your customer form (KYC) and Client Suitability form
- Product risk disclosure with authorized signature from the clients
- Underlying documents (if required by related regulations)
- Initial confirmation
- Long form/ Short form confirmation with authorized signature from the client

Termination Process, Cost and associated Risk(s)

In case the client informs the bank of its intention to terminate the contract, the Bank will thoroughly consider the justification provided by the client and related regulations. In the event such termination is agreed upon by the Bank, the client will bear the risk that there may be gain or loss based on the market value on the termination date and associated costs. The changes in market conditions may adversely impact the termination cost paid by the client.

RISK DISCLOSURE STATEMENT

IMPORTANT NOTICE

THIS NOTICE DOES NOT PURPORT TO DISCLOSE OR DISCUSS ALL OF THE RISKS AND OTHER SIGNIFICANT ASPECTS OF ANY TRANSACTION. IT IS THE CLIENT'S SOLE RESPONSIBILITY TO DETERMINE WHETHER ANY TRANSACTION IS SUITABLE FOR ITSELF AND TO SEEK RECOMMENDATION FROM THE CLIENT'S OWN INDEPENDENT ADVISORS TO REACH SUCH CONCLUSION IF NECESSARY.

1. CONTRACTUAL TERMS

The client has the responsibility to fully understand the terms and conditions of the Transactions to be undertaken including, without limitation, (a) the terms as to Rate, Term, Settlement Dates, Business Days, and other terms material to the Transaction; (b) the circumstances under which the client may become obliged to make or take delivery of the underlying interest of a Transaction; and (c) the legal risks surrounding the Transaction including, but not limited to, the circumstances under which the Transaction may be illegal, resulting in it being void and unenforceable.

2. SEVERAL INSTRUMENT TRANSACTIONS

Where a Transaction is made up of several instruments, the client should be aware that there is a risk associated with each instrument evaluated separately and a risk of the Transaction evaluated as a whole. As such Transaction is usually executed over-the-counter, the client should be aware that it may be difficult to liquidate an existing position of, determine a fair price for, or assess your exposure to risks under, such Transaction. This uncertainty should be factored in by the client in the overall consideration of the potential impact on the client's investment in the Transaction.

3. MARKET RISKS

The client's payments or receipts under a Transaction will be linked to changes in the particular financial market or markets to which the Transaction is linked, and the client will be exposed to price, currency exchange, interest rate or other volatility in that market or markets. The client may sustain substantial losses on the contract, trade, product or financial investment if the market conditions move against the client's positions.

It is in the client's interest to fully understand the profit/loss impact of market movements and the extent of loss if the client has to liquidate a position if market conditions move against the client. The lack of market transparency, liquidity and efficiency may subject the Transaction and the parties involved to high volatility and large price differences.

4. LIQUIDITY RISKS

Under certain market conditions the client may find it difficult or impossible to liquidate a position, assess a fair price or assess risk exposure. This can happen, for example, where the market for a Transaction is illiquid or where there is a failure in electronic or telecommunications systems, or where there is the occurrence of an event commonly known as "force majeure" (which shall include, without limitation, any form of restriction, moratorium or suspension on trading imposed by an exchange, market or other authority regulating trading in the Transaction).

5. RISKS ON OPTIONS TRADING

5.1 Options Transactions involve a high degree of risk. Such Transactions should be entered into only by persons who have read, understood and familiarised themselves with the type of options, style of exercise, the nature and extent of rights and obligations and the associated risks. The Bank would like to highlight to the client that exercising any option would result either in a cash settlement, or in the acquisition or delivery of the underlying contract.

5.2 The client should not purchase any option unless the client is able to sustain a total loss of the premium and transaction costs of purchasing the option. Under certain adverse market conditions when the market moves against an option position, the purchased option can worthlessly expire. In such circumstances, the client would suffer a total loss of the investment which would consist of the option premium and the transaction costs.

The client who purchases an option should be aware that in order to realise any value from the option, it will be necessary either to offset the option position or to exercise the option. The purchaser of an option should be aware that some option contracts may provide only a limited period of time for exercise of the option, and some option contracts may provide for the exercise of the option on a specified or stipulated date.

5.3 The risks associated with selling ("writing" or "granting") an option may be generally greater than purchasing an option. It is important for the client to understand the risks that the client, as an options seller, would be exposed to if the purchaser exercises the option, and the client's obligations to either settle the option in cash, or acquire or deliver the underlying contract. If the option is "covered" by a corresponding position in the underlying contract or another option, the risk may be reduced. Conversely, if the option is not covered, the possible loss could be unlimited.

6. TAX RISKS

Before entering into any Transaction, the client should understand the tax implications of doing so, e.g. income tax. Different derivatives transactions may have different tax implications. The tax implications of Transaction are dependent upon the nature of the client's business activities and the Transaction in question. The client should, therefore, consult a tax adviser to understand the relevant tax considerations.

7. COUNTERPARTY RISKS AND CONFLICT OF INTEREST

The client must note that the Bank deals with the client at arms-length as a counterparty. The Bank is not the client's fiduciary. Any dealing, trading or engagement or Transaction with the Bank by the client could result in a loss to the client and a gain to the Bank.

8. NON-TRANSFERABILITY AND NON-MARKETABILITY

A Transaction generally cannot be assigned or transferred without the consent of the other party. The Bank is not obliged to repurchase a Transaction from you. Because the Transactions are customised and not fungible, engaging in a Transaction with another dealer to offset a Transaction you have entered into with the Bank will not automatically close out those positions (as would be true in the case of equivalent exchange-traded futures and options) and will not necessarily function as a perfect hedge.

9. RISKS NOT COVERED IN THIS DOCUMENT

The following risks which are not strictly related to the Transactions are not covered in this document:

Country risks. A country risk can arise if a country hinders currency trading by imposing economic sanctions or currency restrictions; and

Economic risk. In particular, the impact of the global economy and the bigger nations on the world economic market which impact on interest and inflation rates.

This document also does not deal with the issues of taxation or any other legal consequences pertaining to the Transactions (e.g. duties of disclosure), as these issues are very often dependent on the client's individual situation. The Bank recommends that the clients contact their tax specialist or lawyer.