UBS Education:

Advanced Knowledge of CBBCs and warrants

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We have shared some features of the callable bull/bear contracts (CBBCs) and warrants in the UBS Education before, and now we would like to further discuss about call mechanism and calculation on residual value of CBBCs, as well as calculation method on value of CBBCs and warrants at expiry.

There is call mechanism for CBBCs. If the value of the underlying asset (such as index, stock price) linked to CBBCs hits the call price listed on CBBCs terms, the CBBCs will be ceased, suspended and called immediately. The calculation of residual value of CBBCs being called refers to the relevant observation period. Observation period means the period from the CBBCs being called to the end of the following trading session. If the CBBCs are called in the morning session, the closing price or closing index determined in the closing auction session will naturally be included in the observation period; if the CBBCs are called in the afternoon session, the opening price set in the pre-opening session in the next trading day will be included in the observation period. The settlement price of residual value of a bull contract is the difference between the lowest price of underlying asset during the observation period (two trading sessions) and the exercise price of bull contract and divided by the entitlement ratio. If the lowest price of underlying asset during the observation period hits and / or becomes lower than the exercise price, then there would be no residual value for the bull contract. The settlement price of residual value of a bear contract is the difference between the exercise price of the bear contract and the highest price of underlying asset during the observation period (two trading sessions) and divided by the entitlement ratio. If the highest price of underlying asset during the observation period hits and / or becomes higher than the exercise price, then there would be no residual value for the bear contract.

If the underlying assets linked to CBBCs (such as index and stock price) do not hit the call price listed on CBBCs terms until the expiry date of CBBCs, the calculation of maturity settlement price of bull contract of share represents the closing price of share on the trading day immediately preceding the expiry date minus the exercise price of bull contract of such share and then divided by the entitlement ratio. If the value is negative, then the settlement value would be zero. The maturity settlement price of bear contract of share represents the exercise price of bear contract of such share minus the closing price of share on the trading day immediately preceding the expiry date and then divided by the entitlement ratio. Similarly, if the value is negative, then the settlement value would be zero. The closing price of share on the expiry date would not be counted regardless of bull contract or bear contract.

With regard to CBBCs on Hong Kong indices, the investor would realize that the expiry date of terms must be the settlement date of futures index. The calculation of settlement price is based on the Estimated Average Settlement (EAS) price of indices as announced by Hang Seng Indexes Company Limited after closing of such day, which represents the 5-minute average price on the expiry date of futures index for the current month. For the bull contract of index, it should be calculated by the EAS price minus the exercise price and then divided by entitlement ratio; for the bear contract of index, it should be calculated by the exercise price minus the EAS price and then divided by the entitlement ratio. If the value is negative, then the settlement value would be zero.

The calculation of maturity value of warrants is similar, where the maturity settlement value of warrants represents the average closing price of stock on 5 trading days immediately preceding the expiry date minus the exercise price of such warrant and then divided by entitlement ratio. If the value is negative, then the settlement value would be zero. The maturity settlement value of put warrant represents the exercise price of such put warrant minus the average closing price of share on 5 trading days immediately preceding the expiry date of stock and then divided by the entitlement ratio. Similarly, if the value is negative, then the settlement value would be zero. The closing price of share on the expiry date would not be counted regardless of call warrant or put warrant.

With regard to warrants of Hong Kong indices, the calculation of settlement price is also based on the EAS price of indices as announced by Hang Seng Indexes Company Limited after closing of such day, which represents the 5-minute average price on the expiry date of futures index for the current month. For the call warrant, it should be calculated by the EAS price minus the exercise price and then divided by entitlement ratio; for the put warrant, it should be calculated by the exercise price minus the EAS price and then divided by the entitlement ratio. Similarly, if the value is negative, then the settlement value would be zero.

It should be noted that, if there is residual value on CBBCs or warrants, the amount will be automatically credited into the investor's stock or security accounts within 4-5 trading days in general.

For details on warrants and CBBCs, please refer to UBS website: http://www.ubs.com/hkwarrants

Clip of warrants' tutorial and market highlights
https://www.youtube.com/channel/UCKw86qy4eBAInmd52MND45Q?view_as=subscriber

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