An overview of the features and benefits, and risks and limitations, of structured deposits

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We are now living in a world of higher interest rates on deposits, with *'higher for longer'* rates a possibility. However, everybody is also aware that inflation is currently (and potentially stubbornly) high and eroding the value of money on deposit, in real terms.

Clearly, optimising the level of interest that money on deposit can generate is important… and, importantly, possible.

Structured deposits are very similar to bank and building society fixed term deposits, with a key difference that the level of interest a structured deposit pays may be linked, either fully or partly, to a stock market index, such as the FTSE 100, with the aim of generating higher levels of interest than plain vanilla bank and building society deposits for savers.

Some structured deposits may offer non-conditional, fixed interest; some may offer conditional interest that is linked to the level of a stock market index; and some may offer a combination of non-conditional, fixed interest and conditional, stock market linked interest.

While some conditional, stock market linked structured deposits may require the stock market index to rise in order to generate some or all of their potential interest, many structured deposits are designed so they do not require the stock market index to rise in order to pay interest and some may even allow the index to fall moderately.

Recognising the features and benefits of structured deposits…

- Structured deposits offer the potential for higher levels of interest than other types of deposit, such as bank or building society deposits, including fixed term deposits.
- Notably, even if interest is conditional and linked to the level of a stock market index, the repayment of money in a structured deposit is not subject to stock market risk at the end of the deposit term.
- Importantly, structured deposits are covered by the Financial Services Compensation Scheme *('FSCS')*, if the deposit taker bank is licensed in the UK and if deposit holders are eligible claimants, within FSCS claim limits.

Structured deposits therefore present unique options for saver and investors, offering the potential for stock market linked returns without stock market risk at maturity.

- Savers may consider structured deposits as an alternative and / or complement to high street bank or building society deposits, including fixed term, fixed rate deposits.
- Investors may consider structured deposits as an alternative and / or complement to other investment options, including active and passive mutual funds.

Six reasons for savers and investors to consider structured deposits…

Maximising interest on long term savings is, of course, something that most savers are always likely to be interested in - but it is particularly important at times when inflation is high and eroding the real value of savings over time.

1. The primary reason for savers / investors to choose a structured deposit is their potential to generate higher levels of interest than other types of deposit and / or to access stock market linked returns without stock market risk at maturity, with FSCS protection.

There are also a number of other reasons to consider structured deposits, including:

2. The potential to place deposits with large banks that are recognised as major, global, systemically important banks *('GSIBs')*, instead of smaller, challenger banks and to diversify savings across different deposit taker banks and FSCS licenses;
3. The potential to use annual ISA allowances (without suffering lower rates of interest), which is important when interest rates and the amount of interest being paid is higher;
4. The potential for annual interest payments, which can be offset against annual personal savings allowances (outside of tax wrappers);

5. The potential to opt for longer fixed terms, which many large high street retail banks and building societies do not offer, which may appeal to savers / investors who think that interest rates may be lower than they are now at some point in the future;
6. The potential to access money in a structured deposit during the deposit term, partially or fully (albeit with the need to understand important points about accessing structured deposits and their value during the deposit term), as opposed to bank or building society fixed term, fixed rate deposits, which often offer no access whatsoever.

Understanding the risks and limitations of structured deposits...

As with all forms of saving and investment, it is important for savers / investors to understand the risks and limitations of structured deposits, as well as their features and benefits. Most specifically, savers / investors should carefully consider:

- How the level of interest that a structured deposit may pay is calculated; and
- How the level of interest may compare to bank and building society deposits.

Perhaps the most important point for savers / investors to recognise and understand is that while structured deposits may offer the potential to generate a higher level of interest than other types of deposit, such as bank or building society deposits, including fixed term deposits, there is a risk that conditional, stock market linked interest may not be generated and that the level of interest actually paid may be less than the level of risk free interest that could be paid by a bank or building society deposit, including fixed term deposits.

Savers / investors should always carefully consider the outlook for the relevant stock market index for any structured deposit plan. While many structured deposits are designed so that they do not require the stock market index to rise in order to pay interest, and some may even allow the index to fall moderately, plan managers' target markets for structured deposit plans are typically savers / investors who have a neutral or positive view of the future level of the index, over the deposit term.

> Structured deposits provide important options for savers and investors, offering the potential for higher levels of interest than bank or building society deposits, through stock market links, without stock market risk at maturity, with FSCS protection.

It should also be remembered that as bank deposits, structured deposit plans present deposit taker bank risk. Notwithstanding FSCS protection for eligible claimants, the potential interest and repayment of money depend on the financial stability of the deposit taker bank throughout the deposit term.

Lastly, while accessing a structured deposit plan during the deposit term is usually possible, during normal market conditions (unlike most bank and building society fixed term, fixed rate deposit accounts), it should be understood that this is not guaranteed and the value of structured deposits during the deposit term may be affected by various factors, which can result in values that are below the amount placed on deposit.

Important options for savers and investors: some final points to look for...

Savers / investors should expect to see good use of plain English, with clear explanations of both the features and benefits and risks and limitations of any structured deposit plan, that they can understand.

Savers should look for details of annual equivalent rates *('AERs')*, both minimum AERs and potential maximum AERs, to help compare the potential levels of interest that a structured deposit plan may pay with the level of risk free interest that bank or building society deposits, including fixed term deposits, will pay.

Structured deposits provide important options for savers and investors, offering the potential for higher levels of interest than bank or building society deposits, through stock market links, without stock market risk at maturity, with FSCS protection, for eligible claimants, within FSCS claim limits.

However, structured deposits are not suitable for everyone.

Savers should consider their own circumstances and personal interests / requirements, including their own time horizons and views of and attitude to the stock market and risk - and take advice from a professional adviser, who is part of an authorised and regulated investment firm, who can assess the suitability or appropriateness, for individual, personal circumstances.

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>
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Redefining structured products for professional advisers and their clients

Our aim at Tempo is to *'redefine structured products and structured deposits'* for professional advisers and their clients, focusing on *'doing the right things - and doing simple well'*. This includes: a client-centric, best practice approach to governance and compliance, putting savers and investors first; a bar-raising level and calibre of materials, input and support for professional advisers; and a commitment to *'deliberately defensive'* products.

Our entire emphasis is on working closely with professional advisers to advance and enhance the value that can be gained from best practice use of structured products and structured deposits, for the benefit of their clients.