



Swaption

Product Overview



**Bank of
Ireland**

Swaption

The Governor and Company of the Bank of Ireland acting through its business unit Global Markets (hereafter "Bank of Ireland") provides Swaptions as a tool for managing interest rate exposure which provides protection against adverse interest rate movements.

In exchange for an upfront premium, the buyer of a Swaption gains the right, but not the obligation, to enter into a pre-defined interest rate swap at a future exercise date, i.e. the buyer can 'exercise' their option. Swaptions can be European - exercisable only on one date, American- exercisable at any date over an exercise period, or Bermudan - exercisable on a number of pre-agreed dates over the exercise period. Physical settlement is where the buyer and seller enter into the underlying swap on exercise. Cash settlement means that a cash payment is made by the Swaption seller on expiry to compensate the Swaption buyer for any adverse movements in the underlying swap rate i.e. the value of the underlying swap is paid to the Swaption purchaser.

An interest rate swap is an agreement between a Bank and a customer to swap Floating Interest Rate Payments, linked typically to a Reference Rate, (e.g. Euribor/Libor), for Fixed Interest Rate Payments over a specified Term for an agreed Notional Amount. The Notional amounts are not exchanged and, on each interest Payment Date, the cash flows are netted. For more information on interest rate swaps please see our Guide to Interest Rate Management.

Please note this booklet has been prepared by Bank of Ireland as an information/marketing communication. Terminology used in this document is defined within the glossary, in our Guide to Interest Rate Management and Guide to Foreign Exchange Management which can be found at <https://corporate.bankofireland.com/library/>.

Bank of Ireland doesn't provide products for speculative purposes. Products are provided by Bank of Ireland in order to manage a known exposure e.g. where you have a loan in one currency that you wish to service with cashflows you are in receipt of in another currency and you require protection from this risk.

Other mechanisms / products are available to manage interest rate risk including, but not exclusively, IR options and Interest Rate Swaps. Please contact your Bank of Ireland Relationship Manager for further details. We may be in a position to provide a solution tailored to your particular requirements dependent on your experience.

PLEASE NOTE:

Bank of Ireland Global Markets does not provide investment advice and provides risk management solutions on a strictly non-advised basis only.

You should consider seeking your own independent advice on the financial and legal aspects before entering into any derivative transaction

The product outlined is intended for both retail and professional clients taking account of the identified target market in accordance with Appendix 1 of our Guide to Interest Rate Management <https://corporate.bankofireland.com/library/>.

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Key Benefits

Certainty

- A Swaption enables you to align your future known or expected cash flows and your view of the market, by considering the following parameters:
 - Notional Amount (this Notional Amount can remain constant over the Term or can vary)
 - Currency of your Notional Amount
 - Exercise Date
 - Effective Date / Start Date
 - Term / Maturity Date
 - Interest Payment frequency (monthly, quarterly or semi-annually)
 - Floating Reference Rate
 - Interest Payment Dates
 - Reset Dates
 - Strike Rate
- Your Swaption can provide certainty by securing a maximum interest rate for the life of the underlying swap. This can allow for more accurate cash flow management and budgeting.

Portability

It may be possible to novate i.e. transfer a Swaption to another entity or another bank, subject to credit approval.

Early Termination

It may be possible to terminate the product during the life of the swap, at prevailing market rates. This may incur costs. Please refer to Early Termination section for further information.

Key Risks

Interest Rate Risk

Interest rate markets can be unpredictable and can move in either direction. As a result, the value of this Swaption will change and the strike rate on the underlying swap may be higher or lower than the prevailing rates in the market on exercise.

Early Termination / Changes to the terms of the Swaption

It is sometimes possible to terminate your Swaption early or alter other pre-agreed terms during the life of the Swaption. However, depending on prevailing interest rates at the time, there may be a cost to you or you may realise a gain. Given these risks it is important that you consider carefully the terms and duration of your Swaption at the time of trading. Please refer to the Early Termination section for further information.

Counterparty Risk

- By entering into a derivative contract with Bank of Ireland you have an exposure to Bank of Ireland in the event of insolvency or related events such as bail in.

Key Risks

There are two types of Swaption available:

- A Payer Swaption is where the buyer has the right to pay a fixed rate and receive a floating rate
- A Receiver Swaption is where the buyer has the right to receive a fixed rate and pay a floating rate.

At expiry of the Swaption, the following outcomes may occur:

- If the market swap rate on the exercise date is greater than the strike rate on a Swaption, then payer's Swaption will have a positive market value while a receiver's Swaption will expire worthless.
- If the market swap rate on the exercise date is less than the strike rate on the Swaption, the payer's Swaption will expire worthless and the receiver's Swaption will expire with a positive market value.

If the Swaption has a positive market value it can be either cash settled or physically settled. If the swaption is physically settled, you will enter into the Interest Rate Swap on expiry of the option.

Please see our guide to Interest Rate management for further details on Interest Rate Swaps.

Example

The examples below are indicative only. In order to assess the merits of any particular Swaption, you would need to use the actual rates and figures quoted to you at the time.

A Company expects to draw down €10m of 3 year debt in 6 months time, however, there is uncertainty around whether the underlying project requiring the debt will proceed. In order to hedge this potential interest rate exposure the customer purchases a European Payer Swaption which expires in 6 months time with physical settlement. The cost of this Swaption is 1.25% of the principal amount or €125,000, and is paid by the Company upfront.

The underlying swap is for a 3 year term and matches the debt profile of the loan in question. The strike rate on the swap is the prevailing market rate for a 3 year swap starting in 6 months time, in this example, 3%. The below tables outlines the possible scenarios at expiry.

Scenario	Prevailing 3 year market swap rate on expiry	Has the loan drawn down?	Does the Swaption have value i.e. is the 3 year swap rate >3%?	Will the Swaption be exercised, i.e. should the Company enter into the underlying swap?
A	2.75%	Yes	No	No
B	3.50%	Yes	Yes	Yes
C	3.50%	No	Yes	Yes

Warning: These figures are estimates only. They are not a reliable guide to the future performance of your investment

Scenario A: The Company can enter into an interest rate swap in the market at 2.75%.

Scenario B: The Company will exercise and enter into a swap to hedge the loan, at a 0.5% discount to the current available rate.

Scenario C: The Company does not need the swap but rates have risen and so the swap has value. After exercising the treasury manager can then cancel this swap, locking in a profit as they do so.

Generic Example of an Early Termination

If you wish to terminate early or partially terminate a transaction before its Maturity Date, we will consider such request as soon as reasonably practicable. Should we agree to such a request, the termination may result in a breakage cost payable by either you (to the Bank) or the Bank (to you) (the "Breakage Cost"). This cost will be dependent on the time remaining on the transaction and the relevant market rate available to the Bank on the day on which such Early Termination takes effect. The market rate available is not controlled by the Bank and is impacted by external factors such as volatility, liquidity or lack of thereof and economic or political turbulence. All of these factors will impact the breakage cost. You are strongly advised to discuss potential Early Termination cost with us in advance of requesting an Early Termination of a transaction.

Example of Early Termination cost calculation for a Swaption

If you purchase a payer Swaption, the Early Termination cost would be determined by:

- The value of the underlying swap, which will be higher if rates are higher
- The time remaining until exercise; the value of the Swaption is correlated with the time to expiry
- The volatility of rates in the market; an increase in volatility increases the value of the Swaption

Should you wish to transact an Interest Rate Swaption

Please follow the steps below to enter into a Swaption:

- talk to your Bank of Ireland Relationship Manager who will refer you to the relevant interest rate derivative contact in our Global Markets unit.
- ensure you have read and understood this document.
- you will be required to sign an ISDA Master Agreement.
- talk to your Bank of Ireland Global Markets contact about the particular parameters of the Interest Rate Swaption you require.

In accordance with the rules and requirements set out by the European Union (Markets in Financial Instruments) Regulations 2017 and the Financial Conduct Authority the Bank of Ireland is required to categorise each client either as eligible counterparty, professional client or retail client. Bank of Ireland also has to assess the appropriateness of the product for each customer. Therefore, you may be required to supply supporting documents in order to establish the client category and the appropriateness of the transaction. Before your first transaction, you should receive a categorisation letter and associated Terms of Business. If you do not receive these before the proposed transaction, please contact your Bank of Ireland Global Markets contact.

Your Bank of Ireland Global Markets contact will give you an indicative quote based on the details of your Swaption. Once you have decided you would like to enter into a Swaption, you will be required to provide the necessary documentation, such as:

- Mandate and other account opening requirements
- Credit approval will be required before entering into a physically settled Swaption
- Confirmation of capacity as detailed in your Memorandum and Articles of Association
- Execution of an ISDA Master Agreement
- Any other relevant documents

All conversations such as telephone conversations and electronic communications will be recorded (even where they do not lead to the conclusion of an agreement). Transactions are also executed on recorded lines.

As the prevailing market rates are constantly changing, the rate quoted is only valid for immediate acceptance. This rate may differ from the indicative quote given previously.

Any person authorised in your mandate to trade the relevant product may engage and conclude transactions with Bank of Ireland.

Confirmations

Post transaction Bank of Ireland will send you a Confirmation outlining the relevant commercial terms of the transaction.

It is important you check the Confirmation to make sure that it matches your understanding of the Trade. If so, please sign and return the Confirmation as directed. In the case of a discrepancy, you will need to raise the matter with your Bank of Ireland Global Markets contact as a matter of urgency

What are the Fees and Charges?

Typically there are no upfront fees. However, the Fixed Rate agreed will incorporate Bank of Ireland's risk, execution, administration costs and revenue margin.

A disclosure of expected Aggregated Costs and Charges and expected Total Consideration is available on our website at <https://corporate.bankofireland.com/library/>. We will also provide this information on a post trade term sheet confirming actual Aggregated Costs and Charges and actual Total Consideration following execution of any Derivative trade. An itemised break down of costs will be provided on request.

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In the UK, Bank of Ireland is authorised by the Central Bank of Ireland and the Prudential Regulation Authority, and is subject to limited regulation by the Financial Conduct Authority and the Prudential Regulation Authority. Details about the extent of our authorisation and regulation by the Prudential Regulation Authority and our regulation by the Financial Conduct Authority are available from us on request.

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