



Structured Products Gain Traction in Eastern European Markets

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The Eastern European financial markets are increasingly looking beyond equities and other “plain vanilla” investment products. As markets mature, a move to more sophisticated investment products follows quite naturally. The current economic unrest has accelerated this trend. Trading in warrants, certificates and other structured products is now growing rapidly across Continental and Eastern Europe. From this follows an increasing need for technology to support ‘financial engineering’.



In Russia, Poland, the Czech Republic and other formerly emerging markets, more than a decade of uninterrupted growth for almost every index, has come to an abrupt end. For investors who had little experience with flat or bearish markets, these circumstances have quickly made it necessary to apply new investment strategies based on more complex products.

Now the search for returns must be conducted outside the main stock indexes, and this in turn requires new investment tools. For investment banks, warrants and other kinds of structured products have become attractive for several reasons. One obvious reason is the need to respond to competitive pressure on maturing markets, where structured products provides a vehicle for differentiation.

Compared to funds, structured products are also easily created at low cost, and they allow banks to create and issue their own product portfolios without the need to share trading commissions with other parties. For banks with a large retail customer base, complex structured products are a particularly attractive offering, as they typically carry the highest margins.

Several firms based in Continental Europe addressing the Eastern European markets, including ABN Amro, BNP Paribas, Erste Bank, and Raiffeisen Bank, have become successful in targeting investors using this approach.

“Structured products are just the kind of investment tools that our clients with a special demand for risk protection are looking for in today’s investment climate,” says Heike Arbter, Deputy Director with Raiffeisen CENTROBANK. “This is particularly evident in Eastern Europe, where there is virtually no experience from a bear market.”

For investors looking for returns during the current unpredictable and volatile market conditions, structured products and equity derivatives such as warrants provide

practical solutions, or form part of investment strategies that balance risks and returns.

To some extent, trading of structured products in Eastern Europe is restricted by local legislation and securities regulations. Structured certificates and warrants based on Russian securities can therefore only be accessed using offshore listings. This development was initially not welcomed by those parties involved, however altered market conditions, together with some clearly visible success stories, is winning over any remaining doubters.

Advanced trading technology serves as the key enabling factor for efficient trading of structured products. For complex securities, calculating theoretical pricing, risk analysis and hedging strategies are also inherently complex tasks that require powerful application support for traders and investors. Key to achieving success with such products is getting the trading technology platform right.

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The new market conditions place added emphasis on high-performance and automated trading solutions. Managing warrants trading requires increased efficiency, based on key parameters such as low latency and high throughput.

Orc Software is a proven solutions provider for building a successful warrants & certificates business. Orc’s projects have ranged from banks launching a few hundred



products on one trading platform to launching several thousand products on multiple trading platforms, with the added capability for new product launches on an ongoing basis.

In addition, Orc can facilitate internal matching to avoid matching own issued products on an external platform with additional in-house order-flow. Products varying in complexity need to be considered, from plain vanilla warrants to highly structured products that may contain basket options, fixed income legs, and are denominated in multiple currencies.

“We looked for a solution that met our requirements for creating a large number of structured products, and to manage trading of these in an efficient manner”, says Ronald Nemeč, Head of Equity Trading and Certificates at Erste Group Bank AG. “We chose Orc as our key technology supplier. Initially, our decision was based mainly on technology factors, but based on experience, today we are equally impressed by Orc’s commitment to service and their understanding of our business and needs.”

The right technology platform for structured products not only covers connectivity to the various platforms, with highly advanced contribution and trading capabilities,

but importantly also generates theoretical prices for the products issued and supplies critical risk and volatility management capabilities. The issuers of warrants & certificates need to launch new products on a continuous basis in order to meet market demand.

It is unlikely that the issuer will find a system on the market that will cover all product requirements. This is why an appropriate system needs to contain financial engineering capabilities, in addition to offering a wide range of pre-defined templates for plain vanilla products. Such financial engineering capabilities should also offer possibilities to interface with external pricing libraries and systems. In this way, existing financial models of the issuer can also be used transparently on the trading platform.

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In the past, a number of issuers have made large investments only to achieve mixed results with building in-house systems. Maintenance costs tend to be very high and banks are forced to keep rather large development teams for the sole purpose of maintaining such systems. Why then build to achieve less functionality when you can buy a leading system such as Orc Software provides with all the proven and fully supported trading capabilities you require? ■