

# PARTICIPATING SWAP

A participating swap may suit a business that:

- Wants to be fully protected against the risk of higher rates
- Wants to be able to gain some benefit if rates fall and hence does not want to lock fully into fixed rates
- Wants to reduce or eliminate the requirement to pay a premium

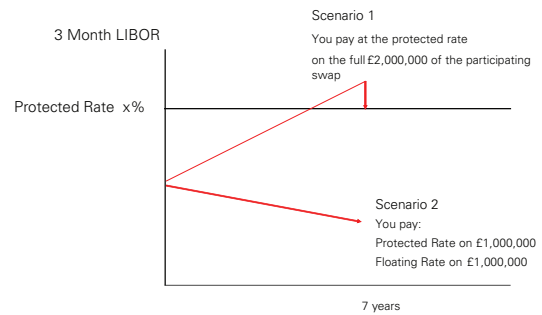
The Participating Swap allows you to protect against the risk of rising interest rates by capping your full exposure so that you will never pay above a pre-agreed level, called the 'protected rate'. It also allows you to participate and receive some benefit on a pre-agreed proportion, if rates fall or stay below the protected rate.

If the LIBOR rate is below the protected rate, you must pay the protected rate on a pre-agreed proportion of the participating swap but you will pay the lower floating rate of interest on the remainder.

To enter into a Participating Swap, you need to specify to us the amount and currency involved, the protection rate you require and the amount, if any, of premium you are prepared to pay. We will then advise you of the proportion of the Participating Swap that we will allow you to pay floating rate on, during periods when LIBOR fixes below your protected rate.

## Scenario

You wish to protect an amount of GBP2 million. In the following example, the 'protected rate' is set at 5.3 per cent allowing you to 'participate' on 50 per cent of the GBP2 million if Libor fixes below 5.3 per cent. If you chose to set your 'protected rate' at a higher level, your degree of participation would increase and vice versa.



**Scenario 1:** LIBOR is above your protected rate of 5.3 per cent. You will pay the agreed protected rate on the full GBP2 million of the Participating Swap.

**Scenario 2:** LIBOR fixes below the protected rate of 5.3 per cent. You pay 5.3 per cent on 50 per cent of your exposure (GBP1 million) and pay the lower, floating LIBOR rate on the other 50 per cent (GBP1 million). For example, if the LIBOR rate was at 4.3 per cent you would pay an average of 4.8 per cent on the GBP2 million notional amount of the Participating Swap.

## Features

- The Participating Swap stands apart from the underlying loan – for example it is possible to enter into one with HSBC to protect debt with another financial institution
- A Participating Swap can be arranged in any major currency, as well as LIBOR



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### Advantages

- Greater flexibility than an Interest Rate Swap
- You can select your own protection level and will be fully protected should rates rise above this level
- You will benefit when LIBOR falls below your protected level on a proportion of the amount of the Participating Swap. This proportion is dependent on where you set your protection level
- A participating Swap can be structured to remove the requirement for a premium

### Disadvantages

- Your protected rate will be at a higher level than could be obtained for a normal Interest Rate Swap
- The benefit you get when interest rates are below the protected rate is only available on a proportion of the amount covered by the Participating Swap
- If you wish to cancel the swap during its lifetime, there may be a cost depending on prevailing market rates at the time

### Important: Please read carefully

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Spot and forward foreign exchange transactions generally are not 'designated investments' as defined in the United Kingdom Financial Services and Markets Act 2000 (the Act) and therefore do not benefit from the protections of the Act and in the Rules of the Financial Services Authority. Any other product described in this document (including a forward extra, forward extra plus, fading forward extra, participating forward or walk away forward contract) is a 'designated investment' as defined in the Act, even when used to cover a commercial trade position.

Hedging instruments, such as caps or options, even when used to cover a commercial position, are investments under the UK's Financial Services and

Markets Act 2000. We are therefore obliged to warn you that these instruments are not readily realisable investments; it may also be difficult to obtain reliable information about their value or the extent to which they are exposed. Their value may also fluctuate.

Investments can fluctuate in price or value and prices, values or income may fall against an investor's interests.

Changes in rates of exchange and rates of interest may have an adverse effect on the value, price or income of these investments. Past performance is not necessarily a guide to future performance. The levels and bases of taxation can change.

Derivatives can be utilised for the management of investment risk. However, derivative instruments may not be suitable for all investors, as they may be contingent liability transactions such as swaps, so therefore please seek advice. This means that the investor may not only lose all the amount invested, but may also have to pay an additional sum at a later date.

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### Settlement

The Bank will compensate you with the difference between the 'protected rate' and the LIBOR rate you pay on the loan.

Settlement under the Participating Swap is made at the end of the LIBOR interest rate period.

The LIBOR rate is an independently calculated rate gathered from a number of leading City banks.

### Contact points

For further information on Participating Swaps, please talk to your HSBC Manager or your local Regional Treasury Manager.