



American
Bankers
Association

American Bankers Insurance Association
an ABA subsidiary

Market Linked CDs

New Popularity for a Not-so-New Product





Speakers

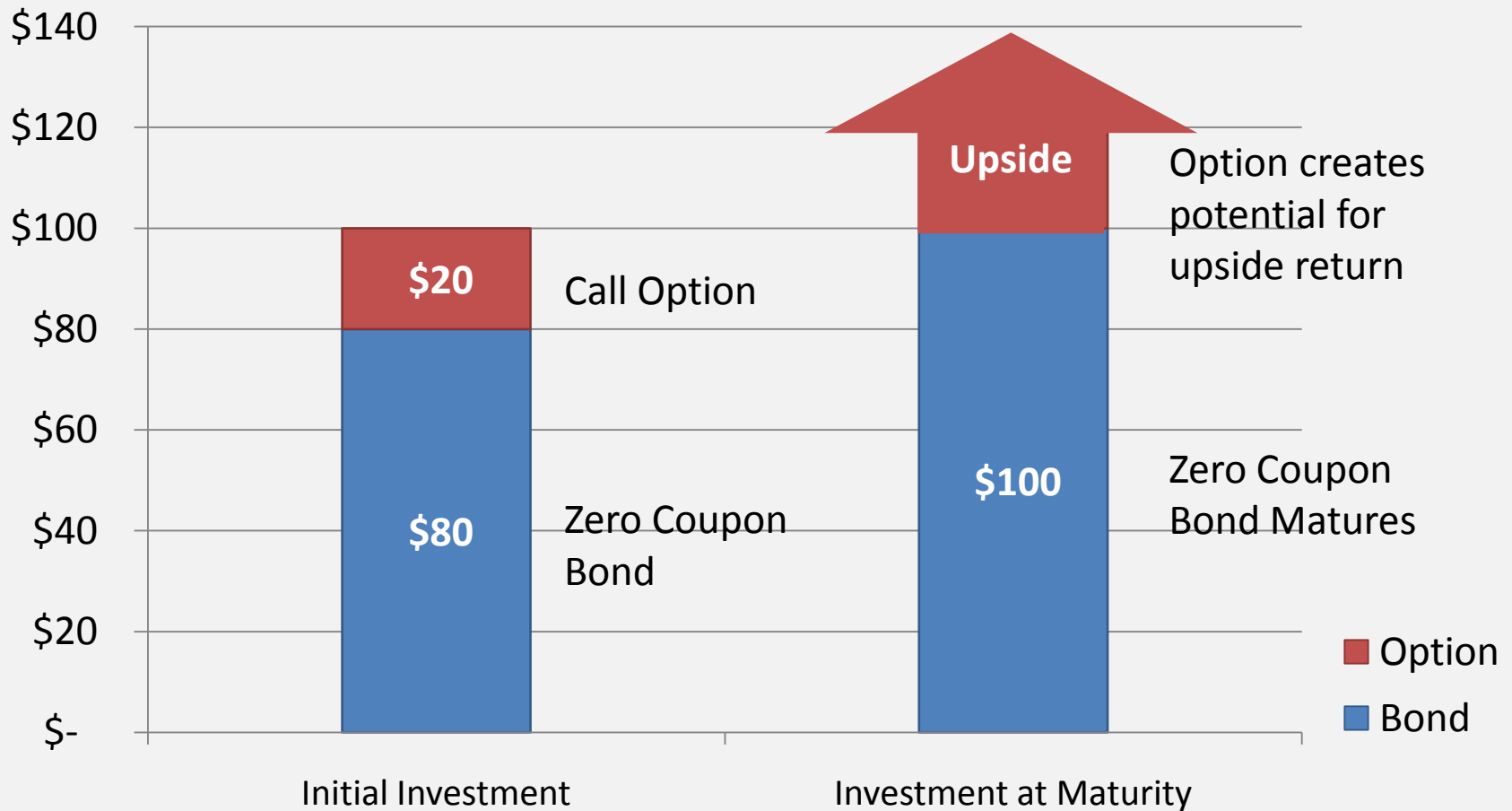
- Steven Saltzman
 - President Saltzman Associates, LLC
- Peter Berneburg
 - Packaged Product Manager, Capital One Investments



Market Linked CDs

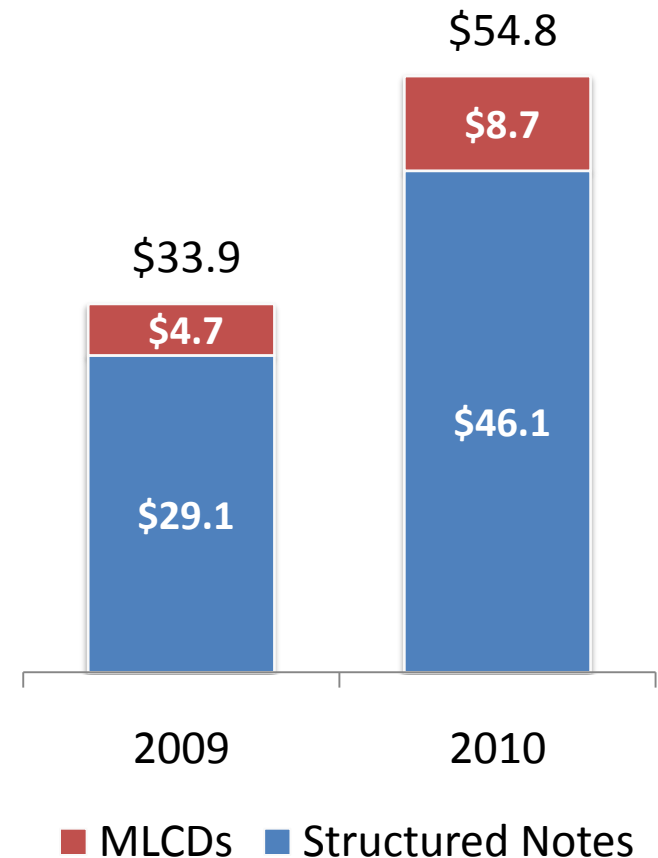
- Market Linked Certificates of Deposits (MLCD) are a particular type of principal-protected structured investment product
- Unlike conventional CDs that offer a fixed coupon, a MLCD typically offers no fixed coupon but provides a return linked to the future performance of an underlying market measure.
- Market measures may include major domestic or international equity indexes, commodity indexes or a basket of commodities, a basket of currencies, an inflation benchmark, or any number of other investment instruments or indexes.
- MLCDs may include FDIC protection

Structure of a Principal Protected Investment



Sales of Structured Products

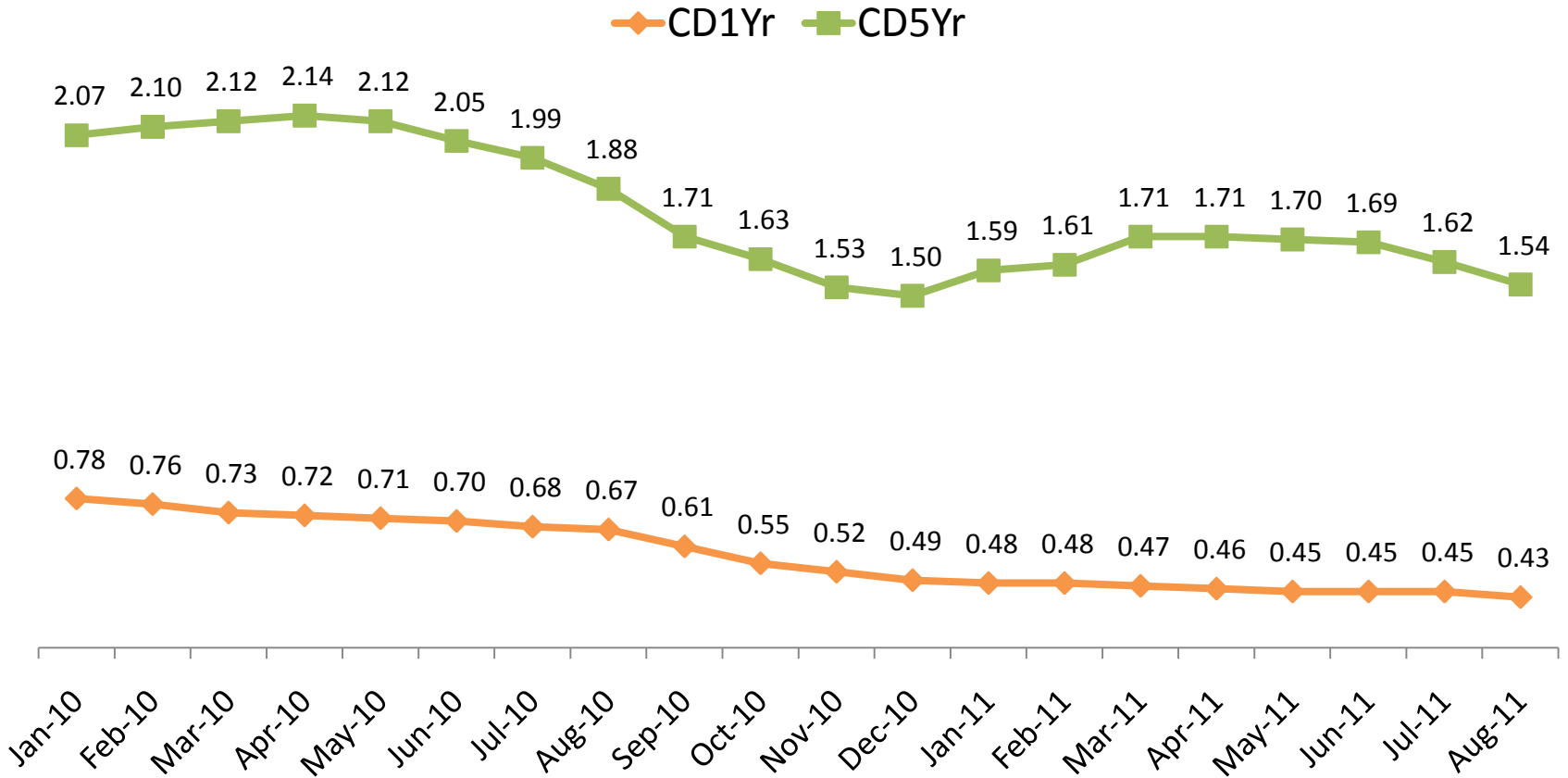
- Total reported structured product sales exceeded \$54.8 billion in 2010 up 62% from 2009
 - Structured notes up 58%
 - MLCDs up 83%
- It is estimated that there are an additional \$10-15 billion in structured note sales, as well as \$10-15 additional in MLCD sales that are unreported
 - Total 2010 sales est. @ \$75-85 bil
 - 2010 MLCD sales est. @ \$19-24 bil



Source: StructuredRetailProducts.com

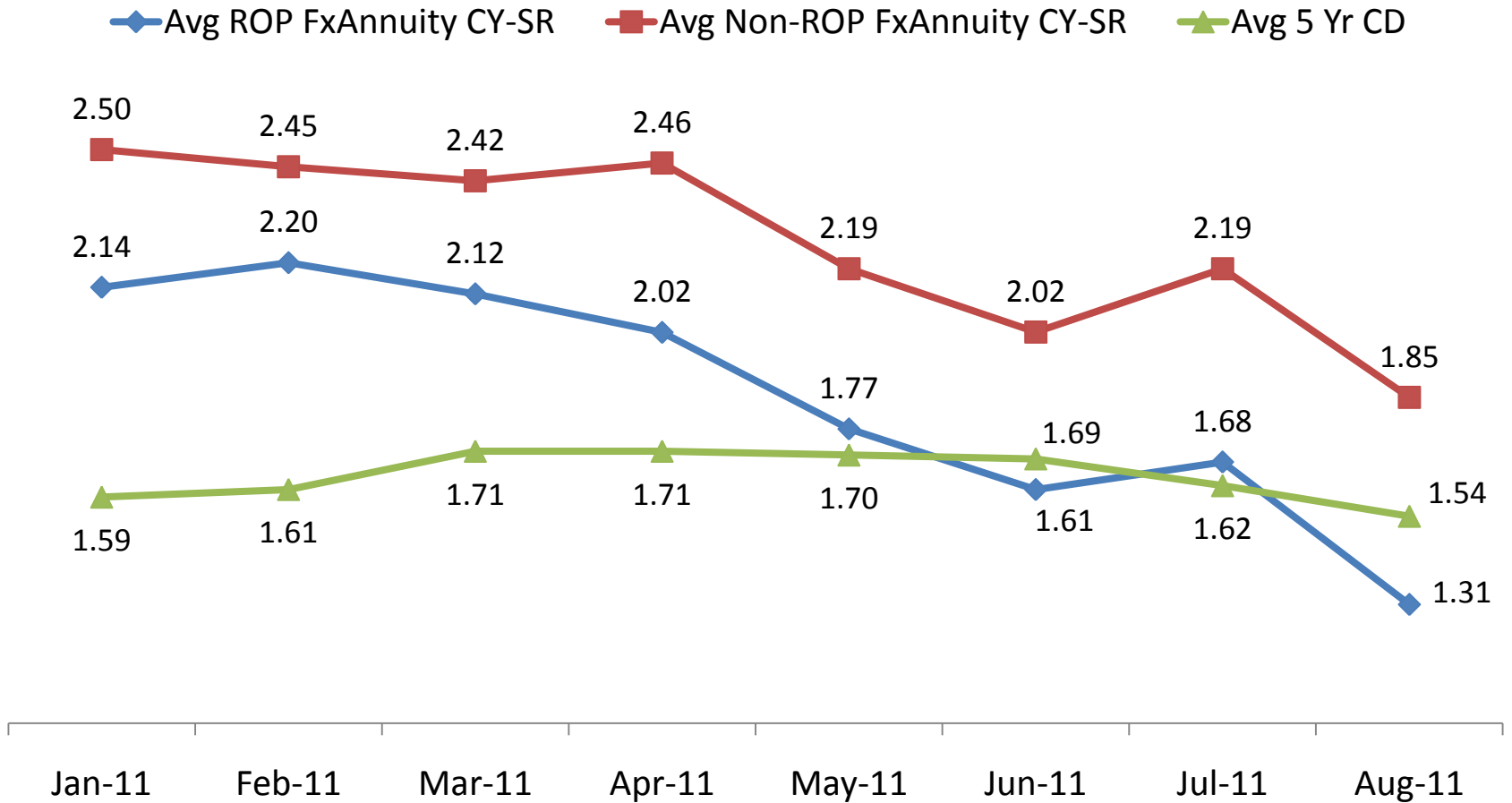
Structured Notes figures represent registered notes only. MLCDs exclude internal offerings

CD Yields



Source: Bank Rate Monitor, National Averages

Fixed Annuity Yields (ROP/Non-ROP) vs. 5 Yr CD



Source: Saltzman Associates, LLC: *Kehrer-Saltzman YieldTrend Report*



MLCD Attributes

Key Characteristics of Market Linked CDs

Principal Protection	Market Linked CDs provide principal protection for the deposit amount if held to maturity.
Growth Potential	All or part of the return on a Market Linked CD is based on the performance of an underlying market measure.
Investor Protection	The deposit amount of a Market Linked CD <u>may</u> be insured by the FDIC up to applicable limits.
Diversification	Can complement a portfolio by providing exposure to a variety of markets, including equities, commodities, foreign currencies and fixed income.
Access to Investment Strategies	Provides investors with access to investment strategies that may not be readily available through traditional investments
Estate Feature	For a MLCD that includes an estate feature, if at any time the owner dies (or sometimes, legally incapacitated), the estate can redeem for the full deposit amount or hold to maturity



MLCD Example

Term/Index

- 4 years / S&P 500

Indexing Method:

- Sum of 16 Quarterly Percentage changes, subject to a quarterly cap of 3.50% (no downside limits)

Minimum Return:

- 2% at the end of the 4 year term (0.50% APY)

Maximum Return:

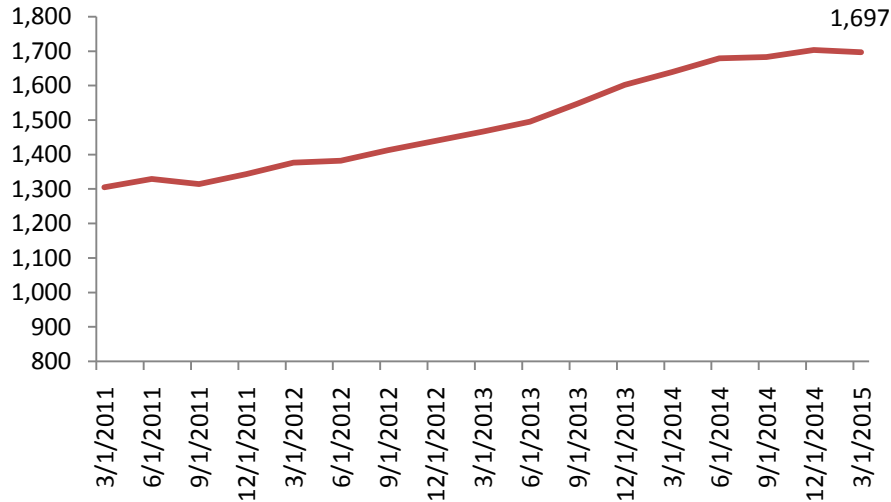
- 56% at the end of the 4 year term (11.75% APY)

Selling Concession:

- 2.75% of the Deposit Amount

MLCD Example

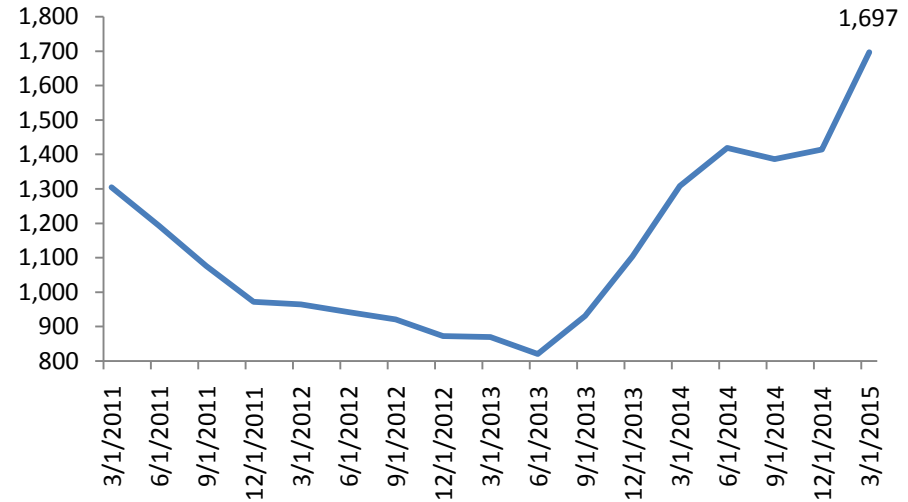
Scenario A: Index Value



Sum of Qtrly Changes	28.00%
Quarterly Change Cap	3.50%
Investment	\$ 1,000.00
Indexed Interest Amount	\$ 280.02
Minimum Indexed Interest Amount	\$ 20.00
Maximum Indexed Interest Amount	\$ 560.00

Payment at Maturity \$ 1,280.02

Scenario B: Index Value



Sum of Qtrly Changes	-27.40%
Quarterly Change Cap	3.50%
Investment	\$ 1,000.00
Indexed Interest Amount	\$ (274.00)
Minimum Indexed Interest Amount	\$ 20.00
Maximum Indexed Interest Amount	\$ 560.00

Payment at Maturity \$1,020.00



MLCDs

PROS

- Provide a broader product offering for the bank's clients
- Selling concessions to the BD in the range of 2-3%
- In the case of proprietary offerings,
 - Leverage of the bank's brand equity
 - lower cost source of deposits

CONSideRations

- Potential disintermediation of higher revenue product sales
 - such as fixed or indexed annuities
- Products can be complex, especially for new buyers
- Different risks vs. traditional CDs
- Advisor Training
- Regulatory Scrutiny



Risk Considerations: MLCDs

Performance Risk —

- While Market Linked CDs provide for a return of the deposit amount at maturity, there may be no assurance of any return above the deposit amount.
- Clients may experience an “opportunity cost” if the market-based return is less than the return a client could have earned in a conventional interest-bearing instrument with a similar maturity.
- The potential return of certain MLCDs may be limited by a predetermined maximum return, a participation rate of less than 100% or other structure-specific features.



Risk Considerations: MLCDs

Liquidity Risk —

- Contrary to the typical bank issued CD, early redemption of MLCDs prior to maturity may produce a substantial loss for the client- assuming that a secondary market exists.
- Although distributor or its affiliates may purchase MLCDs from depositors prior to maturity, they are not obligated to do so.
- There is no right to early termination of a MLCD prior to its scheduled maturity

Limited Pricing —

- There is no active secondary market or major data provider that disseminates a current market value for Market Linked CDs.



Risk Considerations: MLCDs

Market Risk —

- If an investor must sell a MLCD before maturity, the amount received upon any sale (assuming a buyer is available) will be subject to market risk.
- The value of the MLCD is subject to a number of variables, including changes in the underlying market measure, interest-rate fluctuations, and issuer credit quality, as well as market volatility during the term of the investment.
- If a MLCD is sold before maturity, the client may receive less in sale proceeds than the deposit amount. Such secondary-market trading losses are not FDIC-insured.
- The value of a MLCD will not necessarily directly reflect changes in the value of the underlying market measure.
- A change in one factor may be offset by a change in another factor that affects the valuation of a Market Linked CD.



Risk Considerations: MLCDs

Credit Risk —

- Although MLCDs may be FDIC-insured, any investment in a MLCD that exceeds the applicable FDIC insurance limits is subject to the credit risk of the issuing bank.

Call Risk —

- A MLCD may be callable at the option of the issuing bank.
- Banks are under no obligation to call and any decision to call the MLCD will be made in their sole discretion when it is most advantageous for the bank to do so.
- If a MLCD is called, it is possible that the client may not be able to reinvest the proceeds at the same or greater yield.



Tax Considerations

- Most MLCDs are subject to special regulations relating to “contingent payment debt instruments.”
- As such, they would be considered to be issued with original issue discount and ordinary income taxes would be paid on ascribed interest income each year
- Any gain or loss realized upon sale, early redemption or at maturity are generally treated as ordinary income
- Does not apply if held in a qualified tax-exempt or tax-deferred account