FINANCIAL INSTRUMENTS AND RISKS

The investment firm may provide investment services related to all kinds of financial instruments on the Bulgarian and foreign capital markets pursuant to MFIA, in particular:

- Securities (shares, bonds and other securities according to the definitions of Art. 2 of the Public Offering of Securities Act);
- Money Market Instruments;
- Shares of collective investment undertakings;
- Options, futures, swaps, forward contracts and other derivatives, margin contracts according to Art. 4 of MFIA.

1. Shares.

Shares are instruments that give their holders the right to ownership of a certain share of a company. Ordinary shares give their holders the right to vote at the general meeting of shareholders, entitled to dividend and liquidation share proportionate to the nominal value of the share. The preferred shares issued by public companies, may entitle to additional or guaranteed dividends, or guaranteed liquidation share or redemption privilege. Private companies may issue shares with other privileges. The preferred shares may not have voting rights. By increasing the capital of the company, the shareholders are also entitled to the right to subscribe for new shares in proportion to their holdings before the increase. Holders of shares in a company can earn income from dividend, if the company distributes such, as well as from the rise of the market price of shares.

Risk related to transactions with shares:

a) Price risk

Price risk arises from changes in the prices of certain shares, as a result of which shareholders could realize loss from re-sale of their holdings of securities. The change in the price of shares depends on the impact of various types and degrees of influence factors: net asset value of the company, financial results, reputation, supply and demand, economic conditions and forecast for development of the country and others. The issuer cannot guarantee that the price of the offered securities will retain and increase its value. It will buy back their securities in order to maintain current market prices.

b) Liquidity risk

Liquidity risk arises from the uncertainty about the presence of active market demand and supply of shares for a certain period. Poor liquidity would hamper the prevention of possible losses or realization of capital gains due to the inability to dispose of shares. This risk is relatively less in stocks that are traded on a regulated market than non-traded publicly.

c) Inflation risk

Inflation risk is likely to increase the general level of prices in the economy, due to which the purchasing power of the local currency. Inflation processes lead to a decrease in the real rate of return that investors receive. There is also an inflation risk in the purchase of instruments in foreign currency, if the general price level of the economy improved, but a company in which the investor owns shares fails to pass the increased costs to their customers by increasing prices.

d) Currency risk

The currency risk associated with shares relates to the fact that they are denominated in a foreign currency. The change in the exchange rate would alter the return that investors expect to receive, compared to the return they would receive from an investment denominated in other currencies. On the other hand, the decrease in profitability would lead to a decline in investor's interest and thus to a reduction in stock prices. Currency risk can be controlled with derivative instruments that eliminate most of the risk but also a potential profit in a favorable movement in the FX.

e) Lack of guarantee for the payment of dividends.

The financial result depends on many factors - the professional experience of the management of the issuer, the development of the market in which the issuer operates, as well as the overall economic development in the country and region. Moreover, the decision to distribute the profit as dividend is adopted by the General Meeting of Shareholders of the Issuer. Investors should be aware that it is possible for a given year the issuer not to make profit, and even if any, the General Meeting may not adopt a decision for distribution as dividend.

e) Macroeconomic risk

This type of risk is determined by the fact that although a company may be functioning properly, operational, macroeconomic and systemic unforeseen circumstances and financial results worsen and even lead to bankruptcy. Macroeconomic risk can be reduced through diversification of the investment portfolio.

g) Risk of accounting fraud

Although the international organizations (IASC, AICPA, ICAEW, etc.) that govern auditing and accounting companies are making efforts to prevent accounting fraud and misleading data, the risk of accounting fraud still exists when trading shares.

h) Brokerage risk

Brokerage risk includes several possibilities for failure in carrying out a transaction. It is possible that the agent is not sufficiently capitalized and in a given moment cannot meet its obligations to its counterparties. There is a possibility for problems in settlement of a transaction and the transaction to be declared invalid.

2. Corporate bonds.

Corporate bonds are means of raising financial resources by the shareholders in the form of loan. The risk of each bond issue depends on the performance, financial condition and credit rating of the issuing company, as well as the presence or type of collateral at issue. Incomes from them are usually higher than income from government securities, mortgage or municipal bonds.

Risks related to bonds:

a) Credit risk

Credit risk is the risk of default in payment (interest and/or principal) or non-payment by the issuer of the due interest and/or principal on the bond on maturity. This risk is minimized when the bonds are secured; the issuer has a "clean credit history". This risk decreases proportionally with the approach of the maturity date of the bond.

b) Inflation risk

Fixed income bonds could expose to risk associated with a decrease in the profitability of investment in raising inflation. The increase in inflation reduces the purchasing power of income generated by the bonds (interest payments). Because of this bondholders should set their expectations for nominal and real inflation rate for the term of the bonds, as well as their expectations for the real return on the investment made on the basis of nominal income. Should inflation be higher than expected for the period, investors will realize a lower real income than projected. In such a situation, is a normal bond price in the secondary market to suffer a fall, as investors in the higher levels of inflation will require higher nominal return on investments in order to achieve the same or similar real returns. Inflationary risk can be limited through bonds, which are risk protected (such as US government bond), as well as through the purchase of shares.

c) Interest rate risk

Interest rate risk relates to possibility of changes of market interest rates by the central bank. The interest rates fluctuations directly affect the supply and demand of debt instruments, fixed income, due to the inverse relation between prices and bond yields. When the interest rates increases, the price of fixed income bonds decreases. Lower market interest rates bonds at a fixed price bear lower yield compared to alternative investments which is the reason investors to sell securities, which under the new conditions would be expected to be at a lower price than the acquisition price, and to seek alternatives to investing in other types of instruments. The opposite situation is in lowering market interest rates when the price of bonds with fixed income rises. In this situation, investors would benefit from increased bond yields compared to alternative options for investment and the higher price of bonds on the secondary market.

The assessment of interest rate risk for investors is a measurement of relationship between the change in the bonds prices and their profitability, indication of which is bond duration representing the level of change of the price under one basic point change in the interest rate for all terms of the maturity curve of key interest rates.

d) Liquidity risk

Liquidity risk in bonds is similar to that of shares. This risk is directly related to the liquidity on the securities market, where bonds are traded and expresses the possibility for buying or selling in the short term. Lack

of liquidity in the secondary market is a serious issue for any investor whose investment horizon is shorter than the maturity of the bonds. Because in most cases the bonds are traded outside the stock exchange and there is no ongoing assessment of their value, as for the shares, liquidity risk is higher.

e) Currency risk

Currency risk on bonds is similar to currency risk in the shares, except for the fact that the bonds are much more related to interest rates and currencies, which can make them more vulnerable to movements in volatile courses.

f) Risk of change in credit rating

Many bonds are valuated by rating agencies based on the financial performance. Because of the credibility of the major rating agencies (Moody's, Standard and Poor, Fitch) changes in credit ratings can affect noticeably the price of a bond. Bond investors can be protected from the risk of sudden change in the credit rating by periodical analyses.

g) Risk of redemption

In bonds, which has a built-in option that gives the issuer the right of the issuer to redeem the bond at a given price. If the fair market value exceeds a certain price there has a risk to redeem the bond.

h) Risk of re-investment

The risk of re-investment is linked to risk of decreased interest rates and risk of redemption. If interest rates falls there is a probability the issuer to redeem the bonds in circulation and to replace them with new ones with a lower interest rate. However, at low interest the investors in bonds have to seek profitable investment for capital, which it has received through redemption.

i) Risk of bankruptcy

The risk of bankruptcy is associated with reduced risk of credit rating and credit risk. The bankruptcy of the company that issued bonds shall compensate investors with a certain portion of collateral or other assets of the company. However, there is no guarantee that such security will cover hundred percent the invested money.

3. Mortgage bonds.

Specifics of mortgage bonds are that they are secured by mortgage loans. Although the mortgage bonds are identical as risk profile to the corporate ones, the risks related to them are different because some of them have partial or full guarantee. The collateral for mortgage bonds is the real estate which value can sharply decrease in general economic crisis.

4. Government securities.

Government bonds are debt securities issued and guaranteed by the government's ability to collect taxes. Investors in government securities remain creditors of the country issuing securities to cover the short, medium or long-term needs of financial resources. Government securities may be nominated in local or

foreign currency. Local currency securities have lower risk of bankruptcy because of the ability of many countries to print additional money supply, although there are cases in history when countries fail to bonds in their local currency. Government securities are considered a low-risk or risk-free financial instrument in theory.

5. Securities (bonds) issued by regional or local authorities of a country.

Such securities aimed to raise funds for the implementation of the investment program, improvements of municipal infrastructure and similar activities. Could be secured (by municipal real estate or other assets) and unsecured (only guaranteed by the reputation of the issuing municipality). In good financial situation of the municipality - issuer or collateral quality, this type of debt securities is also considered as low-risk financial instruments. In general, the risks associated to debt securities also relate to municipal bonds. Cases of bankruptcy of a municipality are rare because of government support.

6. Exchange-traded funds (ETFs).

ETFs are investment means on the main stock exchanges mainly stocks and bonds. ETF is a set or "package" of assets - stocks, bonds, futures or other instruments. Institutional investors may buy shares of the ETF against shares of the underlying assets or, conversely, to exchange shares of the underlying assets with shares of the ETF. This issue and redemption of shares enables institutions to carry out arbitration and binding value of the ETF with total value of the underlying assets. Most ETF are attached to an index such as the Dow Jones Industrial Average or the S&P500. ETF in the form of a collective investment scheme is traded on the securities exchange at prices close to net asset value. Thus, ETF combines the evaluation function of the mutual fund or the separate investment fund opportunities for trading, typical of the closed fund. ETF exist in the US since 1993 and in Europe since 1999. ETFs are traditionally index funds, but in 2008 the Securities and Exchange Commission of the United States had allowed actively managed ETFs. ETF allows you to easily diversify and reduce risks arising from trading only in certain shares. ETF also allows individual investors to participate in the economic growth of a particular industry or economic sector. All investments are associated with a particular type of risk and therefore ETF is no exception. Some of the risks associated with investing in the ETF are listed below:

a) Market risk

The market prices of securities and stocks of ETF are constantly changing due to the impact of many factors, such as economic situation, world events, investors' preferences and specific securities themselves. Possible market crisis and its subsequent impact on the prices of traded securities and, consequently, the prices of shares of the ETF can be considered as general market risk associated with investing in the ETF.

b) Credit risk

Credit risk relates to the inability of the issuer to make payment of principal or interest. Suspension of payment by company in which the ETF is investing, may adversely affect the value of the shares of the ETF or its ability to pay dividends. It is important to remember that equity investments (including investments

in the ETF, based on equity) bear credit risk. Insofar a company, in which the ETF has invested, is in default or bankruptcy, the equity securities of this company may lose value. Thus, ETF will bear the credit risk associated with these shares.

c) the risk of incompatibility between the price of the fund and the tools in it

Although the arbitrage opportunities attract investors who by buying and selling instruments equalize the price of the fund, there is a risk that in some periods these two prices will be the same

d) Liquidity risk

Liquidity risk in the ETF is similar to shares.

e) Currency risk

Currency risk at ETF is similar to that in the shares.

7. Money Market Instruments

Money market instruments are debt securities with maturities under 1 year. They have a lower credit risk than other debt in the long maturity and are more liquid. They are used by companies and others people for short-term investments of equity.

a) Currency risk

The currency risk in money market instruments is similar to that in the shares.

b) Inflation risk

Due to the relatively low yields of these instruments there is a risk that unexpected inflation will reduce the real value of capital invested in them.

c) Price risk

Price risk arises from changes in interest rates and the credit rating of issuers of the instruments in the money market, which can reduce the price of these instruments.

8. Shares of undertakings for collective investments.

Undertakings for collective investments - mutual funds, hedge funds and other aim of pooling of investors capital to a fund managed by experienced investment professionals. Various types of collective investment undertakings have different characteristics and therefore the risks may defer, but major risks in this type of investment are the financial instruments in which to invest. The following risks (explained in detail above) apply also to collective investment undertakings.

a) Currency risk

b) Inflation risk

c) Price risk

d) Liquidity risk

e) Credit risk

f) Risk of bankruptcy

g) Market risk

h) Inflation risk

i) Risk of accounting fraud

k) Macroeconomic risk

l) Brokerage risk

9. Options, futures, contracts for differences and other derivatives in accordance with Article 4 of MFIA.

Derivative financial instruments are used for speculation and hedging of risk when investing in securities., although derivatives that are considered as high-risk instruments. The main risks are:

a) Risk of default of the counterparty.

When the derivatives are traded off-exchange, there is a risk of default of the counterparty and uncovered obligations.

b) Currency risk

c) Price risk

d) Liquidity risk

Derivatives are complex financial instruments and might not be suitable for all clients.

9.1. Futures

Futures are derivative financial instruments, which incorporate the right and the obligation to purchase or sell a certain number of securities, currencies, commodities or other instruments (underlying asset), at a pre-agreed fixed price, on a given future date. Futures are standardized agreements which are traded on the exchanges.

9.2. Options

Options are derivative financial instruments, the buyer of which has the right, but not the obligation, to purchase or sell a certain number of securities, other financial instruments, or currencies, at a pre-agreed fixed price, until the expiration of a fixed term, or on a fixed date. The seller of an option has the obligation to purchase or sell the relevant underlying under the same conditions.

9.3. Contracts for differences

Contract for differences means a derivative other than an option, future, swap or forward rate agreement, the purpose of which is to give the holder a long or short exposure to fluctuations in the price, level or value of an underlying, irrespective of whether it is traded on a trading venue, and that must be settled in

cash or may be settled in cash at the option of one of the parties other than by reason of default or other termination event.

10. Risks from the leverage effect

When trading using leverage, the invested amount is relatively smaller to the notional value of the position in the financial instrument. In the same time the market exposure for the investor is with the magnitude of its notional value. Therefore, any market move will have a greater effect over the client's capital than if the client has opened position without leverage. The client may lose more than his initial investment. Trading with leverage involves high risk and is not suitable for all clients.