Barrier Options

Product Disclosure Statement ("PDS")
(This Product Disclosure Statement is to be read in conjunction with the Terms and Conditions available on this website).

Purpose
The purpose of this document is to provide you with key information about various products offered by ICICI Bank. ICICI Bank is providing you with this PDS, so that you receive adequate information about Barrier Options. It will help you understand their features, risks, benefits, an illustration of how the product works and assist you in making an informed decision about entering into a Barrier Option and also facilitate comparison with other products (please refer to the PDS for key information on other FX products). Please read this PDS in full, before deciding to enter into a Barrier Option.

Components determining the value of options
The Option value would be determined by the prevailing spot rate, strike rate, forward rates, barrier strike, type of barrier, volatility, tenor and interest rate differentials.

Termination
If you wish to terminate the Barrier Option before the expiry date, the Barrier Option will be terminated at the prevailing market rates. The termination value may either be positive (gain) or negative (loss).
The termination value would be a function of the prevailing spot rate, strike rate, barrier strike, type of barrier, forward rates, volatility, residual tenor, discount factors and interest rate differentials for the residual tenor. Any illiquidity in the market for the specific currency or tenor or notional could lead to a wider bid-offer spread, which would adversely affect the market value of the outstanding derivative contract.
Currency markets are highly volatile and the prices of the underlying currencies can fluctuate rapidly and over wide ranges and may reflect unforeseen events or changes in conditions. Thus, fluctuations in the underlying currencies will affect the benefit or cost to you when you terminate a Barrier Option.
The risks mentioned in this document are not exhaustive. There may be other risks that are relevant to you when entering into a Barrier Option.

Costs and fees
Any specific transaction of this nature will be concluded at the all-inclusive price and there would not be any separate costs, fees and charges. The break-up of all-inclusive price will be provided as per the extant RBI guidelines. The statutory levies and charges will be recovered separately as applicable from time to time.

General information
Please refer to the disclaimer at the end of this document.

Please note that all products are also subject to regulatory risks (not limited to change in regulation, product discontinuation by the regulator, etc.)

Barrier Options

Description and Features:
Barrier options are (call or put) options with a barrier condition. The barrier condition can be a

- Knock-in ("KI") The spot level at which the option becomes alive
- Knock-out ("KO") – The spot level at which the option becomes dead.

The barrier condition may be triggered at expiry (European barrier), or anytime from the trade start time until expiry (American barrier), or only during a specified time period (Window), or during specific time intervals (Bermudan).
Further, a single option can have multiple barriers. For example, an option that has two KIs, is called a Double Knock-in ("DKI"). Similarly, an option with two KOs, is called a Double Knock-out ("DKO"). The option may also be a combination of a KI and a KO. This is called a Knock-in and Knock-out (KIKO).

Purpose

A bought call (put) option with a barrier, helps the buyer of the option in hedging the risk of foreign currency payables / (receivables) against movements in the exchange rate beyond the strike rate of the bought call (put) option, provided the option knocks-in / does not knock-out.

The barrier helps reduce the cost of the option, as compared to the purchase of a vanilla option.

Illustration for a USD/INR Call Option with an American Knock-in (AKI)

Parameters:

1. Strike: Buy a USD call /INR put at <75>.00
2. Knock-in Barrier (American): <78>.00
3. Spot reference: <74.37>
4. Forward:<1.77>
5. Tenor: <6> months
6. Notional: USD <1> Million
7. Upfront Premium: INR <1.42>/USD

Pay off Profile / Possible Scenarios at Expiry

If the barrier level of <78>.00 is seen during the life of the option, the option will become alive. Thus, the option pay-off at expiry will be that of a vanilla option:

- **If a USD/INR spot rate is below <75>.00 at expiry**, for example if a USD/INR spot rate at expiry is <74.50>, the buyer of the option will not exercise the option and may buy the USD/INR at the prevailing market rate of <74.50>.
- **If a USD/INR spot rate is above <75>.00 at expiry**, for example a USD/INR spot rate at expiry is <76.75>, the buyer of the option will exercise the option and will buy the USD/INR at <75>.00.

If the barrier level of <78>.00 is never seen during the life of the option, the option will never come into existence.
The contract holder can buy the USD/INR at the prevailing market rate.

Benefits:

- Lower cost than a vanilla call of the same strike/maturity.
- In case of a bought barrier option with a Knock-in, if the barrier condition is met, the option with provide a protection like a vanilla option.

- In case of a bought barrier option with a Knock-out, if the barrier condition is never met, the option will provide protection like a vanilla option.

Predominant Risks:

- Premium is payable for the bought option, irrespective of the spot at expiry and the whether the barrier condition is met.
- In case the barrier is a Knock-in barrier, then the buyer will have protection against adverse movements in the underlying, only if the option gets Knocked-in. For example, in the above illustration, if the KI barrier level of <78>.00 is never seen till expiry, there is no hedge for the buyer of the option.
- In case the barrier is a Knock-out barrier, then the buyer of the option has no protection, once the barrier is touched.

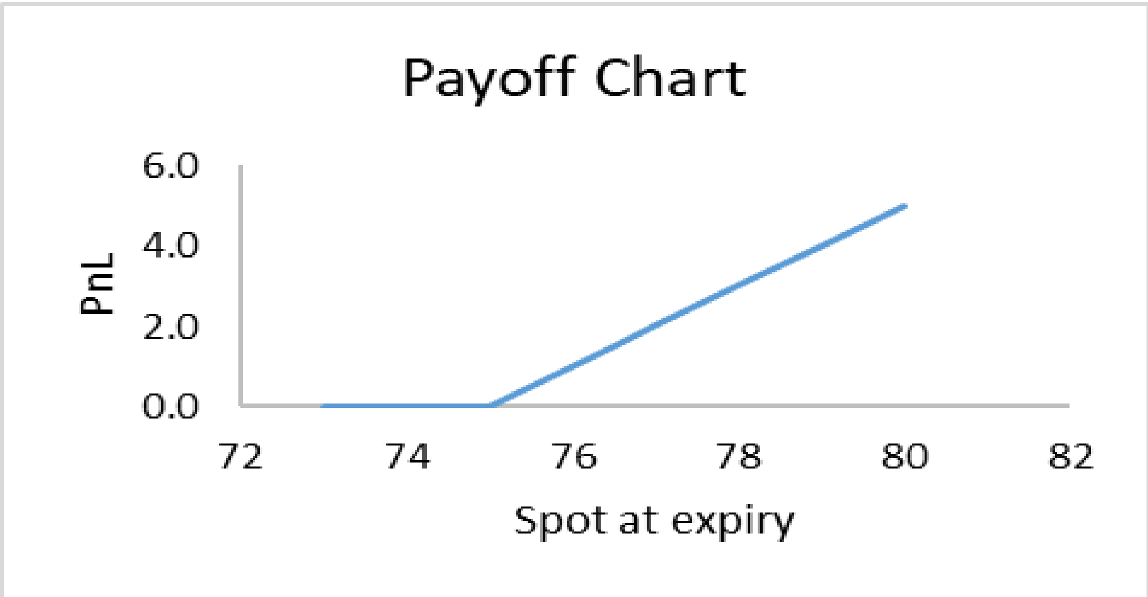
Other Risks

- Please refer to the section 'Various risks associated in the transaction.'

Alternates

- The type of barrier condition could be changed (e.g. KI/DKI/KIKO) and so could the barrier type (e.g. American/European).

Payoff of the structure illustrated above, if <78> is observed at any point of time till expiry (excludes premium)



Various risks associated in the transaction:

The Counterparty acknowledges that before entering into derivative transactions, it understands the underlying risk of the above mentioned transaction. The Counterparty acknowledges that derivative transactions are in general exposed to various types of risk, including but not restricted to the following:

1. **Credit risk:** the risk of loss due to Counterparty's failure to perform on an obligation to the institution. Credit risk in derivative products comes in two forms:

   a. Pre-settlement risk: the risk of loss due to a Counterparty defaulting on a contract during the life of a transaction. The level of exposure varies throughout the life of the contract and the extent of losses will only be known at the time of default.

   b. Settlement risk: the risk of loss due to the Counterparty's failure to perform on its obligation after an institution has performed on its obligation under a transaction on the settlement date. Settlement risk frequently arises in international transactions because of time zone differences. This risk is only present in transactions that do not involve delivery versus payment and generally exists for a very short time (less than 24 hours).

2. **Market risk:** the risk of loss due to adverse changes in the market value (the price) of an instrument or portfolio of instruments. Such exposure occurs with respect to derivative instruments when changes occur in market factors such as underlying interest rates, exchange rates, equity prices, and commodity prices or in the volatility of these factors.

   a. Liquidity risk: the risk of loss due to failure of an institution to meet its funding requirements or to execute a transaction at a reasonable price. Institutions involved in derivatives activity face two types of liquidity risk: market liquidity risk and funding liquidity risk.

   b. Market liquidity risk: the risk that an institution may not be able to exit or offset positions quickly, and in sufficient quantities, at a reasonable price. This inability may be due to inadequate market depth in certain product (e.g. exotic derivatives, long-dated option), market disruption, or inability of the bank to access the market (e.g. credit down-grading of the institution or of a major counterparty).

3. **Funding liquidity risk**: the potential inability of the institution to meet funding requirements, because of cash flow mismatches, at a reasonable cost. Such funding requirements may arise from cash flow mismatches in swap books, exercise of options, and the implementation of dynamic hedging strategies.

4. **Operational risk**: the risk of loss occurring as a result of inadequate systems and control, deficiencies in information systems, human error, or management failure. Derivatives activities can pose challenging operational risk issue because of the complexity of certain products and their continual evolution.

5. **Legal risk**: the risk of loss arising from contracts which are not legally enforceable (e.g. the counterparty does not have the power or authority to enter into a particular type of derivatives transaction) or documented correctly.

6. **Regulatory risk**: Regulatory risk is the risk of loss arising from failure to comply with regulatory or legal requirements.

7. **Reputation risk**: the risk of loss arising from adverse public opinion and damage to reputation.

8. **IBOR Discontinuation:** If the Counterparty transacts in any derivatives linked to an interbank offer rate (IBOR) such as LIBOR, or any synthetic rate (such as MIFOR) that use an IBOR in its calculation, please note that there is a risk that such IBOR may be discontinued prior to the maturity of the derivatives contract. There are public consultations by different industry groups, including by ISDA for derivatives contracts, to develop contractual fallbacks that will apply in the event of an IBOR discontinuation. A contractual fallback will define the events that will trigger the benchmark fallback and the methodology that will determine the fallback rate. ISDA has consulted on technical issues related to new benchmark fallbacks for derivatives contracts that reference certain IBORs. As and when the benchmark fallbacks are finalized, market participants are expected to incorporate them into existing derivatives contracts, by way of bilateral amendment or multilateral protocol adherence, to enhance contractual robustness. Please note that application of the benchmark fallbacks may cause a change in value of existing derivatives contracts. In addition, there is no assurance that the same trigger events and fallback methodologies will be incorporated into cash products (such as bonds, loans or other non-derivative products). Accordingly, you may run basis risks if you are using derivatives contracts to hedge your obligations or investments in cash products (or another financial instrument) that adopt different triggers and fallbacks. The potential mismatches may impact the hedge effectiveness, financial reporting and value of existing derivatives contracts.

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ICICI Bank, its related companies, their directors and/or employees may have interests or positions in, and may effect transactions in the underlying product(s) mentioned in this document.

Transactions in respect of the products mentioned in this document can be executed only as per the regulatory guidelines of the geography of the proposed execution and other laws and guidelines applicable to such transactions. The Counter Party should note that the sensitivity analysis and scenario analysis of products would be contained in the Confirmation provided to the Counter Party, in respect of executed transactions.

For any further information in relation to the subject matter of this document, the Counter Party may contact its treasury Relationship Manager.