

# The lion reaps tonight

Between 15 and 50 companies which do business in Africa form the basis of an index created by Merrill Lynch that offers exposure to the continent. Capital is not protected, but there is a decent participation rate and daily liquidity on offer

## > Product description

The Merrill Lynch Africa Lions index is a research-based index offering investors exposure to companies with a certain level of operational exposure to Africa. The index comprises between 15 and 50 stocks. As of November 7, 2007, the index contained 35 stocks.

This product is an open-ended investment that is redeemable on and from December 17, 2008. It therefore has a minimum investment term length of one year. On the redemption date, the investor will receive a return equal to 100% of any growth in the index. There is an annual management fee of 1%, which is calculated on a daily basis and is payable upon redemption.

The strike date was December 10, 2007. The starting index level was determined by the average of the closing levels of the index on the strike date and the nine subsequent business days. The final index level is defined as the arithmetic average of the closing levels of the index on the exercise or redemption date and the nine preceding business days.

A certificate offering 90% capital protection with a 90% participation rate in the index is available from the provider for US dollar and euro investment, but in the case of these index

<b>Issuer:</b>	Merrill Lynch				
<b>Country of issue:</b>	Global				
<b>Currency of issue:</b>	Dollar				
<b>Product type:</b>	Tracker (capital not protected)				
<b>Points for:</b>	1. Exposure to a dynamic research-based African index via a decent 100% participation rate 2. Daily liquidity allows for redemption at any time after 17 December 2008				
<b>Points against:</b>	Capital is not protected				
<b>Asset exposure period:</b>	Open-ended				
<b>Underlying asset:</b>	Merrill Lynch Africa Lions Index				
<b>Final index level definition:</b>	Arithmetic average of the closing levels of the final 10 days of the investment.				
<b>Wrappers and investment vehicles:</b>	Direct investment	<b>Offer period</b>	Opens n/a	Transfers by n/a	Closes 7/12/2007
<b>Credit rating of investments made:</b> <small>(according to information from the product provider)</small>	Standard & Poor's: A+; Moody's: A1; Fitch: A+	<b>Key dates</b>	Strike set 10/12/2007	Final reading 10/12/2099	Maturity/payout n/a

certificates capital is not protected and any downside is passed on to the investor, who will be subject to capital loss at a rate of 1:1. The index certificates are available on a euro and Swiss franc settlement basis as well as on a US dollar basis.

The Merrill Lynch Africa Lions index is reviewed semi-annually. Index composition is weighted according to three categories: direct plays, South African plays and indirect plays. Direct plays are stocks listed either on an African stock exchange (excluding South Africa) or on a non-African exchange and which, as defined by Merrill Lynch Research, have their 'main exposure' in Africa – for instance a company generating more than two-thirds of its revenue on the continent. A South African play would include stocks that are listed on the Johannesburg Stock Exchange or that have their main exposure in South Africa. An indirect play includes a stock not listed on an African stock exchange or which does not have its main exposure in Africa, but is likely to benefit from growth in the African economy.

The index weighting is as follows: 70% is assigned to direct plays, 20% to indirect plays and 10% to South African plays. Individual stocks are subject to a maximum weighting of 10%.

Stocks such as Tullow Oil (oil and gas, UK listing), First Quantum Minerals (basic resources, Canada) and Banque Marocaine du Commerce (banks, Morocco) are examples of the direct plays. Examples of South African plays include Sasol (oil and gas) and MTN Group (telecoms). Indirect plays include stocks such as Mobile Telecoms (technology, Kuwait) and Investec (financial services, UK).

The product would therefore appeal to investors seeking diversified exposure to the African economy. As with other emerging markets, any economic, regulatory or political risks should be considered. However, it is likely that investment in the Merrill Lynch Africa Lions index would have a low correlation to other regional equity markets.

The analysis below assumes an investment term of five years, but the investment can be held for longer or shorter periods as it is open-ended.

### Pricing and risk

The index consists of listed stocks but the composition of the index can change twice each year in a review carried out by Merrill Lynch Research and according to its definitions of inclusion. Therefore the delta hedge needs to be carried out on at least the same basis by the issuing institution to cover its position.

Typically, in medium-to-high-growth areas such as investment in Africa (particularly in sectors such as oil and gas, financial services, mining resources, telecoms, infrastructure, information technology and retail and leisure, according to the product's literature) and in emerging markets where political, economic and legal risks are more likely to occur than in established markets, stocks may experience higher-than-usual levels of volatility. Such volatility makes it more difficult for the issuing institution to price the option. If the index's volatility increases after the hedge, the institution would, in effect, have undersold the option. But a decline in volatility once the option has been sold would boost the institution's profit. The institution takes on more risk and is therefore likely to increase its margin to counter the additional market risk.

The higher volatility is offset to some degree by the correlation between the current stock components. Greater correlation between the stocks would have made the option – and therefore the issue cost – more expensive.

### Product assessment

To see details about the scoring system, riskmap and probabilities please see the explanation of the research methodology

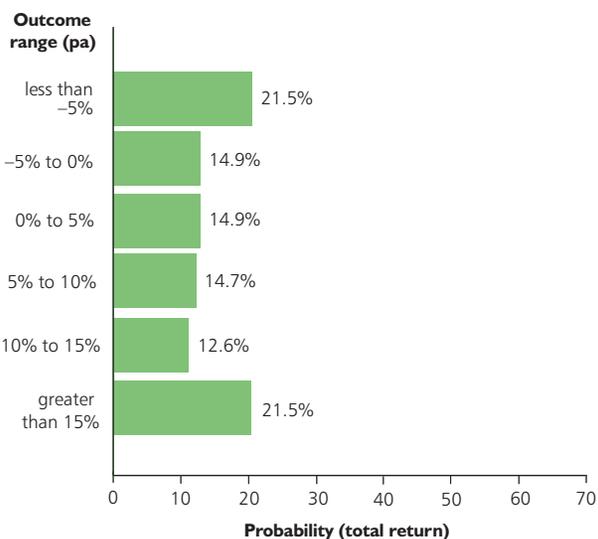
Investor rating  8.25/10  
(This rating does not take into account the tax treatment of the investment)

Riskmap rating  3.52/5

To compile the overall scores this product scored as follows in our different categories:

Transparency  9/10  
Value  8.25/10  
Returns  7.46/10

### Probability table of product return outcomes (based on simulated performances)



Greater correlation would also reduce the chance of one or more negative performances bringing the average growth of the index down. ■

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### EDITOR'S CALL FOR PRODUCT TERM SHEETS

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