Leveraged and Inverse Product Disclosure

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This disclosure statement is in place to provide you with information regarding the risks associated with holding leveraged or inverse products.

What are leveraged and inverse products?

Leveraged and inverse products are generally issued as mutual funds, exchange traded funds (ETF), or exchange traded notes (ETN).

Leveraged products seek to deliver multiples of the performance of the index or benchmark they track. Inverse products seek to deliver the opposite of the performance of the index or benchmark they track. Some leveraged and inverse products track broad indices, some are sector-specific, and others are linked to commodities, currencies, single stocks or some other benchmark. Inverse products often are marketed as a way for investors to profit from, or at least hedge their exposure to, downward moving markets.

Leveraged inverse products seek to achieve a return that is a multiple of the inverse performance of the underlying index. An inverse product that tracks a particular index, for example, seeks to deliver the inverse of the performance of that index, while a 2x (two times) leveraged inverse product seeks to deliver double the opposite of that index's performance. To accomplish their objectives, leveraged and inverse products pursue a range of investment strategies through the use of swaps, futures contracts, and other derivative instruments.

Most leveraged and inverse products "reset" daily and are designed to achieve their stated objectives on a daily basis. Their performance over longer periods of time—over weeks or months or years—can differ significantly from the performance (or inverse of the performance) of their underlying index or benchmark during the same period of time. This effect can be magnified in volatile markets. As the examples below demonstrate, an Exchange Traded Fund (ETF), which is a product that may utilize leverage or inverse objectives, is set up to deliver twice the performance of a benchmark from the close of trading on Day 1 to the close of trading on Day 2 and will not necessarily achieve that goal over weeks, months, or years.

Real-life examples

The following two real-life examples illustrate how returns on a leveraged or inverse products over longer periods can differ significantly from the performance (or inverse of the performance) of their underlying index or benchmark during the same period of time.

- Between December 1 and April 30 of the following year, a particular index gained 2 percent. However, a leveraged ETF seeking to deliver twice that index's daily return fell by 6 percent—and an inverse ETF seeking to deliver twice the inverse of the index's daily return fell by 26 percent.
- During that same period, an ETF seeking to deliver three times the daily return of a different index fell 53 percent, while the underlying index actually gained around 8 percent. An ETF seeking to deliver three times the inverse of the index's daily return declined by 90 percent over the same period.

How can this apparent breakdown between longer term index returns and product returns happen? Here's a hypothetical example: let's say that on Day 1, an index starts with a value of 100 and a leveraged product that seeks to double the return of the index starts at $100. If the index drops by 10 points on Day 1, it has a 10 percent loss and a resulting value of 90. Assuming it achieved its stated objective, the leveraged product would therefore drop 20 percent on that day and have an ending value of $80. On Day 2, if the index rises 10 percent, the index value increases to 99. For the leveraged product, its value for Day 2 would rise by 20 percent, which means the ETF would have a value of $96.

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On both days, the leveraged product did exactly what it was supposed to do—it produced daily returns that were two times the daily index returns. But let's look at the results over the 2 day period: the index lost 1 percent (it fell from 100 to 99) while the 2x leveraged product lost 4 percent (it fell from \$100 to \$96). That means that over the two day period, the leveraged product's negative returns were 4 times as much as the two-day return of the index instead of 2 times the return.

Things to consider before investing

The best form of investor protection is to clearly understand leveraged or inverse products before investing in them. No matter how you initially hear about them, it's important to read the prospectus, which provides detailed information related to the product's investment objectives, principal investment strategies, risks, and costs. The SEC's EDGAR system, as well as search engines, can help you locate a specific prospectus. You can also find the prospectuses on the websites of the financial firms that issue a given product, as well as through your Financial Professional. Before investing in these instruments, you should consider the following:

- **How does the leveraged or inverse product achieve its stated objectives?**
  And what are the risks? Ask about—and be sure you understand—the techniques the product uses to achieve its goals. For example, engaging in short sales and using swaps, futures contracts, and other derivatives can expose the product—and by extension investors—to a host of risks.
- **What happens if I hold longer than one trading day?**
  While there may be trading and hedging strategies that justify holding these investments longer than a day, buy-and-hold investors with an intermediate or long-term time horizon should carefully consider whether these products are appropriate for their portfolio.
  As discussed above, because leveraged and inverse products generally reset each day, their performance can quickly diverge from the performance of the underlying index or benchmark. In other words, it is possible that you could suffer significant losses even if the long-term performance of the index showed a gain.
- **Is there a risk that an inverse or leveraged product will not meet its stated daily objective?**
  There is always a risk that not every leveraged or inverse product will meet its stated objective on any given trading day. Be sure you understand the impact an investment in an inverse or leveraged product could have on the performance of your portfolio, taking into consideration your goals and your tolerance for risk.
- **What are the costs?**
  Leveraged or inverse products may be more costly than traditional products. Use "FINRA's Fund Analyzer" at https://tools.finra.org/fund_analyzer/ to estimate the impact of fees and expenses on your investment. The "SEC's Mutual Fund Cost Calculator" at https://www.sec.gov/investor/tools/mfcc/mfcc-intsec.htm can also help you estimate and compare costs of owning mutual funds.
- **What are the tax consequences?**
  Leveraged or inverse products may be less tax-efficient than traditional products, in part because daily resets can cause the products to realize significant short-term capital gains that may not be offset by a loss. Be sure to check with your tax advisor about the consequences of investing in these products.

  Neither RBC Capital Markets, LLC, nor its affiliates provide legal, accounting or tax advice. All legal, accounting or tax decisions regarding your accounts and any transactions or investments entered into in relation to such accounts, should be made in consultation with your independent advisors. No information, including but not limited to written materials, provided by RBC CM should be construed as legal, accounting or tax advice.

Only invest if you are confident the product can help you meet your investment objectives and you are knowledgeable and comfortable with the risks associated.

ADDITIONAL INFORMATION

Investors should carefully consider the investment objectives, risks, charges and expenses of a fund before investing. Prospectuses containing this and other information about the fund are available by contacting your financial professional. Please read the prospectus carefully before investing to make sure that the fund is appropriate for your goals and risk tolerance. Hard copies of this disclosure document can be obtained upon contacting your financial professional. See "Leveraged and Inverse Product Disclosure" on our public websites at: www.rbcwm.com/disclosures, or www.rbcclearingandcustody.com/disclosures.