GUIDE TO UNDERSTANDING ASSET CLASSES :

EQUITIES

U Wealth : Your partner in mastering financial instruments.

We want you to feel comfortable making suitable investment decisions based on knowledge of the opportunities and risks of given financial instruments.

SEPTEMBER 2026

FINANCIAL INSTRUMENTS: OPPORTUNITIES AND RISKS

The higher the complexity of a financial instrument, the higher its potential risk –but the higher, too, the opportunities for returns.

WHAT ARE EQUITIES?

Equities (also called 'shares' or 'stocks') are a **share of a company's capital**. A shareholder participates in the success or non-success of a company's business results by sharing its financial risks but also returns.

There are **different types of shares**. In particular, there are registered shares, where shareholders' names are logged in a share register, and bearer shares, where there is no such registration.

Shareholders have **various rights**, such as financial, information, subscription, compensation, exchange, settlement, and voting rights, as well as the right to participate in liquidation proceeds.

There are normally **two reasons to invest in shares**: 1. to generate wealth by participating in the long-term capital gain of a company's value (capital gain). 2. to generate income by participating in a company's business results in the form of a distribution of dividends payments.

ADVANTAGES/DISADVANTAGES

Share prices are a function of supply and demand. Demand is strongly dependent on a company's economic performance, as well as on the overall national and international economic environment.

If a company requires additional capital, shareholders may receive a so-called 'subscription right' that allows them to subscribe to new or additional shares at a predefined price and subscription ratio. Depending on whether the right is tradeable or not, the price of the right is included in the share price. If the right is traded on an individual basis, the share price is reduced by the value of the right's price.

Advantages

- Shares afford **direct participation** in a company's financial future.
- **Accessibility, liquidity, and versatility**: publicly traded shares are usually liquid financial instruments that offer a wide range of investment opportunities worldwide.
- There are two types of **investment return**: dividend yield and capital gain.
- Equities have historically outperformed other asset classes over the long term.

Disadvantages

- **Predictability:** past performance is no indicator of future returns.
- **Medium-term fluctuations:** past performance trends can reverse in the medium term.
- **Volatility:** stocks are subject to sudden price changes, the cause of which is not always clear to the investor.
- **Brokerage costs** decrease the return from the investment.
- **Dividends are not guaranteed**; they can be omitted or cancelled. For example, when a company is in liquidation, shareholders rank behind other creditors in terms of the order of payment.

IMPORTANT RISKS TO CONSIDER

Shares are traded according to the balance between supply and demand. The **price of a share** expresses **investors' expectations regarding the future value of, and return from,** that share. When deciding about these expectations, investors evaluate **two main risk factors**: the **economic environment** (market risk) and the specific situation of the company invested in (**company-specific risk**).

Risk factor	Type of risk	Explanation	Consequences
Market risk	General economic environment	All equities are equally exposed to market risk in terms of the general economic environment. For example, a change in the interest rate usually affects share pricing in general, without a specific relation to the individual company's development.	Shares can be subject to sudden price changes, the cause of which may be unclear to the investor (predictability).
	Market psychology	A regulated market is a market of expectations. Not all expectations are rational. In particular, market participants tend to enforce and even exaggerate trends.	Shares are volatile investments on a short-term basis.
Company-specific risk	Profitability	Shareholders are entitled to participate in the profitability of the company invested in. The company's economic situation and management success determine whether a return can be distributed in the form of a dividend, and if so, in what amount.	Dividend payments are not guaranteed. Past performance is no indicator of future returns.
	Insolvency	In case of insolvency, shareholders only participate in the liquidation capital after other investors have been compensated (e.g. bondholders).	A shareholder bears the risk of a total loss of the invested capital.

When equities are traded in currencies other than the home currency, there is an additional risk of changes in foreign exchange rates.

WHAT TO EXPECT FROM EQUITIES

Investment horizon

- Medium term
- Longer term
- Short term

Income expectation

- Capital gain
- Irregular dividends

Market expectation

- Increasing (1)

(1) There are trading strategies that cater for other market expectations (i.e. short selling). Such strategies can increase investment risks.

IMPORTANT TO KNOW BEFORE INVESTING IN EQUITIES

Maximum gain

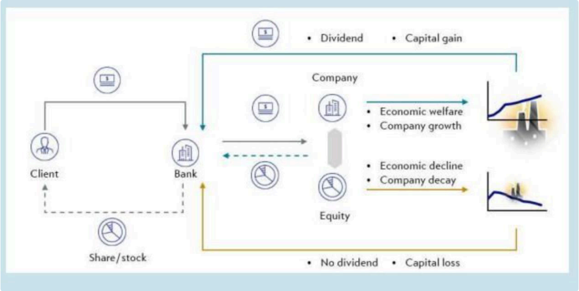
Unlimited : Dividends earned plus any capital gain realized.

Maximum loss

Total loss of capital in case of insolvency of the company invested in.

Profit/loss

The return from an investment in a specific share cannot be predicted. The investor participates in the economic performance of the company, sharing its risks and returns.



A CLOSER LOOK AT EQUITIES

EQUITIES VS EQUITY

The term 'equity' in finance refers to:

- the residual value of a company when all liabilities are deducted from the assets
- any type of security that claims an ownership participation

Equities are the most common form of such securities.

They represent an investor's share in the ownership of a company.

GENERAL TYPES OF SHARES

Shares are usually very liquid investment instruments. They are extremely versatile and easily accessible. Shares can be classified in many ways. It is common to classify them according to voting rights and to the potential to transfer.

According to voting rights

- **Common stock:** holders of common stock bear the right to vote on company decisions.
- **Preferred stock:** holders of preferred stock do not usually bear any voting rights, in exchange for preferred treatment on dividend payments.

According to the potential to transfer

- **Registered shares:** the holder's name is entered in a share register; these shares are not easily transferable. Registered shares involve higher administrative costs, but allow companies to know who their shareholders are and make hostile takeovers more difficult.
- **Bearer shares:** there is no registration; these shares are easily transferable.

While shares are a form of participation in a company, investors lack specific rights/possibilities, mainly concerning the access to internal information (e.g. current financial situation, strategic decisions) that would influence their investment decisions.

VALUE AND RETURN OF A SHARE

The **value of a share** is determined mainly by the performance (and **performance expectation**) of the company and the wider market environment (**economic conditions and climate**).

Companies listed on a stock exchange **publish their results** at regular intervals.

Additionally, listed companies are obliged to publicly **notify investors about any corporate events** that may **influence** investors' expectations about the companies' future performance and **hence the price of the companies' shares**. Such events include:

- takeover bids
- mergers with other companies
- launch of new products.

Shares create **two types of return** for investors.

Capital gain

If the company is prospering, its value and consequently the price of its shares will rise accordingly.

Dividend payments

A dividend is a distribution of a part of the company's income to its shareholders. The board of directors decides whether to pay a dividend, and if so, in what amount, after taking into account other needs and requirements (e.g. investments, reserves). Dividends can take the form of cash payments or additional shares.

COST TYPES

The purchase and sale of shares create **costs for the investor.**

Bid/Ask Spread

The amount by which the ask price exceeds the bid price for an asset in the market. The bid/ask spread is essentially the difference between the highest price that a buyer is willing to pay for an asset and the lowest price that a seller is willing to accept.

Broker & Bank Fees

Brokers and banks charge fees for their services depending on the type of asset, the market place, and transaction volume. Minimum fees per transaction can apply.

Commissions

Can be charged by exchanges. Stock exchange fees can vary markedly from one exchange to another.

Taxes

Such as stamp duty, can be levied when buying shares of a company.

Currency Conversions

Can create additional costs.

ORDER TYPES

Stocks are traded continuously. There is always a time lag between the placement and the execution of an order. Thus, when placing an order, the price at the exact time of execution is unknown.
Order instructions can be given when placing orders. Such instructions may include 'market', 'limit', 'stop', or 'stop-limit' orders.

1 Market Order

An order to buy or sell a stock at the best available price. Generally, this type of order is executed immediately. However, the price at which a market order is executed is not guaranteed. It is important for investors to remember that the last-traded price is not necessarily the price at which a market order is executed. In fast-moving markets, the price at which a market order is executed often deviates from the last-traded price or 'real time' quote.

2 Limit Order

An order to buy or sell a stock at a specific price or better. A buy limit order can only be executed at the limit price or lower, and a sell limit order can only be executed at the limit price or higher.

3 Stop Order

Also referred to as a 'stop-loss order', is an order to buy or sell a stock once the price of the stock reaches a specified price, known as the 'stop price'. When the stop price is reached, a stop order becomes a market order. A buy stop order is entered at a stop price above the current market price. Investors generally use a buy stop order to limit a loss or to protect a profit on a stock that they have sold short. A sell stop order is entered at a stop price below the current market price. Investors generally use a sell stop order to limit a loss or to protect a profit on a stock that they own.

4 Stop-Limit Order

An order to buy or sell a stock that combines the features of a stop order and a limit order. Once the stop price is reached, a stop-limit order becomes a limit order that will be executed at a specified price (or better). The benefit of a stop-limit order is that the investor can control the price at which the order can be executed.

FOR FURTHER INFORMATION ON RISKS OR ON OTHER AVAILABLE FINANCIAL INSTRUMENTS, PLEASE REQUEST TO YOUR RELATIONSHIP MANAGER ON U WEALTH EDUCATIONAL MATERIAL.

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