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A guide to Financial Spread Betting

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Hargreaves Lansdown

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Hargreaves Lansdown

Before you continue, a word of caution

Spread Betting involves initially depositing only a small percentage of the total trade value, and so losses could quickly exceed your initial deposit requiring you to make further payments. This makes it higher risk, and is why it should only be considered by more experienced and sophisticated investors.

This guide does not constitute personal investment advice. Spread Betting is not suitable for everyone; please understand the risks involved and if you are in any doubt of its suitability for your circumstances you should seek personal advice.

Any examples contained within this guide are for indication purposes only. Please ensure you fully understand the terms of any bet before opening a position.

One of the most flexible cost-efficient ways to trade the world's markets

Colin Dewar
Head of HL Markets

Most investors reading this guide will have bought and sold shares through a traditional stockbroker - but what if you could access more markets and have more investment choice? What if you had the potential of being able to profit in any market condition and initially pay only part of the full market value of the deal? What if there was no separate commission and everything was built into a narrow spread?

A growing number of experienced private investors are already doing this by using Financial Spread Betting for shorter term trading as part of a balanced portfolio.

If you understand the risks and want to trade commission free, then this could be exactly what you've been looking for.

Here's why

- There is no separate dealing commission to pay. Instead everything is built into the spread.
- You can profit from falling prices as well as rising prices, if you bet the right way.
- You don't have to pay the full cost of the deal up front.
- You have access to a wide range of investment choice.
- It's exempt from UK Stamp Duty, and profits are exempt from UK Capital Gains Tax.

Tax laws are subject to change and depend on individual circumstances. Tax laws may differ in a jurisdiction other than the UK.

What is Financial Spread Betting?

Spread Betting is a way of dealing in the price movements of investments such as shares, forex, commodities and indices without actually owning the underlying asset. Like share dealing, the aim for investors is to profit from the price moving in their favour.

Many people think that Spread Betting is similar to backing a horse, in that the odds are set so that the broker always wins.

This is not the case

- The price you pay is based on the price set by the market, and not the whim of a bookmaker.
- Spread Betting providers make their money on the difference between the buying and selling price, and not entirely on whether you win or lose.
- You can close your bet at any time during market hours whether your position is winning or losing.
- It is not necessarily a 'win or lose everything' bet, as your returns will depend on how successful, or unsuccessful, your trade is – but you could end up losing more as this is a leveraged (also known as geared) investment product.
- Spread Betting gives you the potential to profit in any market condition - provided you trade the right way, of course - and deal in a very wide range of investments, at the click of a button.
- Before Spread Betting, this type of transaction could only have been achieved through relatively complicated derivative transactions, and were used mainly by banks, city traders and institutions.
- Spread Betting for the private investor is in principle far simpler. All you have to do is predict whether a particular stock, security, or market, anywhere in the world, will go up or down over your chosen timeframe. If you're right, you win; but if you are wrong, you lose and could end up paying more than your initial deposit if you don't close your bet in time.

Is it really tax free?

Spread Betting is currently one of the most tax-efficient ways of investing in the stock market.

But exactly how tax free is it?

- You pay no UK Stamp Duty, which means you save 0.5% on UK equity buy bets (a saving of £50 on every £10,000).
- There's no UK Capital Gains Tax on any profits.
- No Betting Levy.
- No need to declare it on your tax return.
- It's only tax free if you are a UK resident.

Dividends: The holder of a Spread Betting contract is not entitled to any dividends. However, if a company is likely to go ex-dividend before your bet expires, the brokers will often adjust the price of the bet by building the value of the estimated net dividend into the price you are quoted.

Please remember that Spread Betting is aimed at short term traders, and consequently the impact of any dividend can often be ignored.

Stick to what you know – Although there is a huge choice, investors generally stick to companies, indices or currencies that they know and watch carefully.

Important – The levels and bases of taxation may change and are subject to individual circumstances. In addition, any capital losses cannot be netted off against capital gains from other investments.

HUGE RANGE OF INVESTMENT CHOICE

Most providers will give you access to a range of bets and contracts, including:

UK Shares: Most commonly on the UK Stock 100 Index, although, some providers will allow smaller companies.

US, Asian & European Shares: Allowing you to deal in '000s of international companies.

Indices: Including UK Stock 100 Index, Wall Street, Germany 30, France 40, and more.

Forex: Including sterling, US dollar, yen and euro.

Commodities: Including Oil, Cocoa, Coffee and Wheat.

Precious Metals: Including Gold, Silver, Platinum and Palladium.

Sectors: Take a view on a market sector such as Banking or Telecoms.

Government Bonds: Including UK, US, Japanese and European government bonds.

Interest Rates: Bet on the next move of the Bank of England Base Rate.

Options: Including UK Stock 100 Index, Wall Street, and Forex Futures.

How to get started

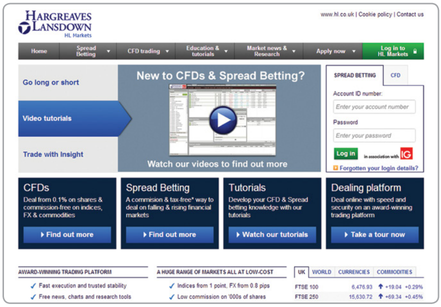
Simply visit **www.HLMarkets.co.uk** to watch video tutorials, learn more, or apply now.

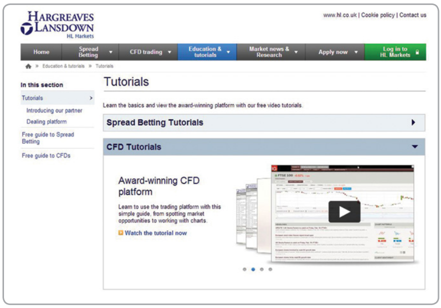
In our opinion there is no better Spread Betting service. The costs are low, the information is second-to-none and the online, mobile and telephone service is exceptional. Hargreaves Lansdown provides Spread Betting in association with IG who are an award-winning execution-only provider. They offer:

- Permanently tight spreads are offered across markets
- A huge range of markets, including: global stock indices, 70+ forex pairs and commodities
- Over 6000 shares, binaries, options and much more

You can analyse and trade the world's financial markets with speed and security on an award-winning platform, which provides:

- Price improvement technology and fast execution
- Deal through market-leading charts; using quick charts or advanced charting
- Free financial news: live market news feeds
- Fully customisable layout; personalise the layout to suit your dealing
- Insight; live data, analysis and aggregated views of what other clients are trading
- Trusted stability: 99.96% core platform uptime (average per month, IG globally, 12 months to February 2016).





All dealing, administration and settlement is carried out by IG and any contract you enter into will be a contract between you and IG. IG provide an execution-only service. Hargreaves Lansdown is not responsible for any functions they perform. IG is a trading name of IG Index Ltd.

How does it work?

The price

When buying and selling the underlying shares, you are quoted two prices, for example:

Vodafone Ordinary Shares 199 - 200

199p This is the amount per share you receive if you sell

200p This is the amount per share you pay if you buy

The principle is the same with Spread Betting. You are quoted two prices and you buy at the higher price and sell at the lower price. Your objective is to correctly predict which way the price will move, so that the price you receive when selling is HIGHER than the price you pay when buying – the difference between the two prices is used to calculate your profit or loss.

Going short – Unlike conventional share dealing, Spread Betting also allows you to sell first and buy back later with the aim of profiting from a falling price - this is known as “going short”. See Page 8 for more information.

Pounds per point

There is one crucial way in which Spread Betting differs from conventional share trading. Instead of buying a quantity of shares you simply decide how much money you would like to bet per point.

- For shares, each point is normally equivalent to a 1 penny movement in the share price (or 1 US cent for US shares, 1 euro cent for European shares, and so on).
- For indices, each point is normally equivalent to a 1 point movement in the quoted price of the index.

Let's look at how this works in practice, taking the previous example, where Vodafone is quoted at 199p to sell, and 200p to buy.

You might decide that Vodafone is due to rise and choose to buy at £10 per point. This means that when you close your bet you would receive £10 for every point that the Vodafone price rises above the price you paid; similarly you would pay £10 for every point that the price falls below.

Important: All of the examples included within this brochure are for illustration purposes only. This example shows the impact of a price movement on your profit and loss only, and excludes the impact of financing, margin etc.

Going short

'Investments can fall as well as rise'

Investors have traditionally bought shares in the hope of profiting from a rise in the price. The view that the price will rise, and the

How price movements can affect your profit and loss – GOING LONG			
Price goes up 10p to 209p - 210p		**Price goes down 10p to 189p - 190p**	
Opening purchase value	200p	Opening purchase value	200p
Closing sale value	209p	Closing sale value	189p
Points moved	9 points	Points moved	11 points
Profit per point	£10	Loss per point	£10
Profit	**£90**	**Loss**	**£110**

IMPORTANT: the above examples are for illustration purposes only, to show the impact of price movements. These exclude the impact of margin, financing and dividends. Ensure you fully understand the terms of any contract before opening any position.

resultant instruction to buy, is described as ‘long’ or ‘going long’.

‘Going short’ or ‘shorting’ is simply the flip side of going long. If you think the price will fall, your aim is to sell at a higher price than the price you buy it back for. Shorting is a way of potentially making money from a falling price as opposed to a rising price.

The ability to go ‘long’ or ‘short’ is an important investment tool, since in any market condition you will be able to take advantage of rising or falling prices.

The main problem investors have in understanding this concept is how you can sell something that you don’t own. However, a Spread Bet simply takes a view on the direction in which the price moves, and you will not be expected to own the security in the first place.

Let’s take our previous example and assume you want to go short. Remember the quote for Vodafone is 199p to sell and 200p to buy. You might decide that Vodafone is due to FALL and choose to SELL at £10 per point. This means that when you close the bet you will pay £10 for every point that the Vodafone price rises above the price you previously sold at; similarly you will receive £10 for every point that the price falls below.

If you think	You go	opening deal	closing deal
The price will rise	Long	Buy	Sell
The price will fall	Short	Sell	Buy

How price movements can affect your profit and loss – GOING SHORT			
Price goes up 10p to 209p - 210p		Price goes down 10p to 189p - 190p	
Opening sale value	199p	Opening sale value	199p
Closing purchase value	210p	Closing purchase value	190p
Points moved	11 points	Points moved	9 points
Loss per point	£10	Profit per point	£10
Loss	**£110**	**Profit**	**£90**

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Introducing margin

‘Dealing on margin’, ‘margin trading’ or ‘gearing’ are all terms associated with Spread Betting. When a bet is opened you are only required to pay part (for example, 10%) of the full value of the deal up front, and in effect you borrow the rest from the provider.

The initial amount you pay is known as the deposit or initial margin.

Dealing on margin can significantly increase your profits, but can also significantly increase your losses; that is why Spread Betting is riskier than buying shares through your stockbroker.

ONE WAY TO UNDERSTAND MARGIN IS TO COMPARE IT TO BUYING A HOUSE

Imagine two investors buy identical houses for £500,000 each. Investor A pays cash, and Investor B puts down a 10% deposit and borrows the rest. For the sake of simplicity we will assume the loan is interest free. After a few years the value of the houses rise to £750,000 and both investors decide to sell.

Investor A is very happy, his £500,000 house is now worth £750,000 and he has made a 50% profit on his original investment.

However, Investor B is even happier. He has only paid £50,000, and borrowed £450,000. He pays off his loan of £450,000 from the sale proceeds, and is left with £300,000 in cash. He therefore has a £250,000 profit on his original investment, or a profit of 500%.

Had the price of the property fallen to £250,000, both investors would be looking at a loss. If they sold their properties, Investor A would make a loss of £250,000 (50%), and Investor B would lose his £50,000 deposit and need to pay a further £200,000 - a total loss of £250,000 (500%) - negative equity. This clearly demonstrates the high-risk nature of dealing on margin.

The principle is the same when comparing conventional share dealing with Spread Betting

When buying shares from a stockbroker you will be asked to pay for them in full. If you asked to buy £10,000 worth of Vodafone shares, you will be expected to pay the full £10,000.

If you open a £10,000 Spread Betting position in Vodafone, most providers will ask you to pay initially only £500 or 5% of the value. This means that you control the same size asset with a much smaller amount of money – in this case £10,000 worth of Vodafone for just £500.

IMPORTANT: the above examples are for illustration purposes only. Any margin requirements are subject to change. Ensure you fully understand the terms of any contract before opening any position.

Put another way, Spread Betting gives you the same exposure as a conventional share deal with, in this example, just 5% of the initial cost. As you would have only paid 5% margin, your investment would have been geared twenty times, or a 20:1 ratio, meaning your profit or loss would be magnified by twenty times relative to your initial outlay.

Ongoing margin: If your position starts to lose money and you do not have enough money in your account to cover the loss, you may also have to pay ongoing margin. Your position may be closed out if it falls negative.

Ongoing margin and margin calls

Like dealing in ordinary shares, profits or losses from Spread Betting are only realised when you close the deal. However, with a Spread Bet you must always ensure that you have enough money on your Spread Betting account to cover not only the initial cost of the trade, but also any running losses.

A 'margin call' will occur when the running losses on all your positions exceed the amount of money your broker requires you to have on account. But how do you know how much is needed?

Different brokers will apply different rules and you should make sure you fully understand what your broker requires from you. See table at the bottom of the page for an example of how it could work.

Let's assume you've put £3000 into your account. Using that money, you have opened up several positions with a total initial margin requirement of £2000. Look at the difference in these examples, depending on whether your positions make or lose money:

As soon as your account has a negative balance, your broker could contact you and ask you to top up your account so that your total position remains in credit.

Most providers would recommend that you keep some extra cash on your account to cover any small price movements against you.

	At open	Up £1500	Down £500	Down £1500
Account balance	+£3000	+£3000	+£3000	+£3000
Aggregate profits/losses	+£0	+£1500	-£500	-£1500
Total initial margin	-£2000	-£2000	-£2000	-£2000
Total position	+£1000	+£2500	+£500	-£500

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Choosing the right timeframe

It's one thing deciding whether a price will go up or down; but when you place a Spread Bet, you also need to specify a timeframe. This doesn't mean you are predicting what the price will be at a precise moment in the future; instead, you are simply selecting an 'expiry date' when your bet will come to an end. You can close your bet and take any profit or loss at any time before that date.

When you look for a particular instrument, you will normally be given a choice of the available timeframes.

When you open a position, certain costs are incurred for the time you hold your position open. These are financing costs, and they reflect the cost of borrowing or lending the underlying asset.

FOR EXAMPLE

You'll see that each bet will have a slightly different spread. This is because for bets with a longer expiry, the broker has to build in the additional costs involved in running that position for a longer period; therefore the spread will be slightly larger.

Bets with a stated expiry

Bets which state a specific month will most likely expire towards the end of that month. The months are usually the last month of a calendar quarter i.e. March, June, September and December. Details of expiry dates can normally be found on the provider's website or dealing platform. Daily bets will expire at the end of the trading day.

Need more time? Roll it over!

In some circumstances you might want to keep a bet open beyond its expiry date. This could be because it hasn't reached your target, or you are waiting for news which will hopefully move the price in your favour.

Rollovers allow you to convert a bet which is near its expiry date into the next contract period. This will involve the bet being briefly closed and then reopened.

Market	Period	Sell	Buy	Change	% Chg
Vodafone Group PLC	DFB	222.28	222.72	4.65	2.13
Vodafone Group PLC	JUN-16	222.52	223.41	4.65	2.13
Vodafone Group PLC	SEP-16	222.68	224.46	4.65	2.12
Vodafone Group PLC	DEC-16	222.78	225.47	4.65	2.12

FINANCING

When you open a bet, the cost of running it to its expiry date is factored into the quoted price. If you close a weekly or quarterly bet before it expires, or close out a Daily Bet the same day you open it, then additional financing will not be a consideration, i.e the cost of financing the bet is lost.

If you roll over a long position you will have to pay more. Typically your bet will be closed and opened at a new price; the price difference reflects the cost of financing rolling forward. In principle it is equivalent to the interest that you would pay on your mortgage when you buy a house – the longer the mortgage, the more the financing charges will affect you.

Automatic rollovers

Many providers will offer you the facility to automatically roll your bets forward. This will typically be available via their dealing platform.

The 'rollover cost' is charged by widening the difference between the buy and sell price (the spread). Although the position is rolled over at the mid-price, the spread around the mid-price will generally be widened by 1 to 2 points. This is commonly the case when rolling a bet on an index and is calculated in a similar way for equities. For a UK share, the annual cost will typically equate to LIBOR +/- 2.5% depending on whether you are long or short.

Libor: Is the London Interbank Offered Rate, and is usually close to the Bank of England Base Rate. The actual rate varies and can be found everyday in the Financial Times newspaper.

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Available order types

The variety of order types available to investors through Spread Betting is yet another reason for its popularity. Of course this is in addition to the standard 'buy' or 'sell' market orders. You can place trade instructions to help manage your potential exposure to losses, to take profits at your chosen level, and set instructions to buy or sell at a price better than the current market level.

Stop Loss order

A Stop Loss is an order which closes your position at a specified price if the market moves against you. You can place a Stop Loss when you open a trade and with most providers you will be able to adjust or cancel the Stop Loss as the market moves. Stop Losses are frequently used by stockmarket professionals but are underused by private investors dealing on margin. But why?

Professionals use Stop Losses to reduce their risk and to cut their losses – they set parameters of what they are willing to lose and stick to it. Private investors still aren't fully harnessing the benefits of Stop Losses and all too many hold onto positions that are running away from them. It's impossible to monitor your portfolio constantly, and unless you use a Stop Loss you could get a nasty shock when you next look at your account. Some providers will also allow you to have a 'trailing' Stop Loss, so that you can protect your profit as the price moves.

Guaranteed Stop Loss orders

Occasionally, prices move quickly and jump or 'gap' past certain price levels, perhaps due to a profit warning or a record set of figures. This can be fantastic news if your position is the right way, but a potential disaster if you're not. An ordinary Stop Loss order will be triggered if the market trades at the price you set, or if the market price gaps past your level; in which case your position will be closed at the next available price.

A Guaranteed Stop Loss (GSL) order gives you complete protection and acts as a type of insurance policy. You pay a small premium – for example, just 1 point on a UK 100 daily bet – to the provider, who in turn guarantees executing your trade at the Stop Loss price you set.

Limit Orders

As well as using Guaranteed Stop Losses to control your risk and limit the downside of your investment, most providers will also give you the facility to set a Limit Order to buy or sell if the price moves to a more favourable price than the current level. Limit Orders can be used to open or close a bet.

For example, you may have a long position in Vodafone at 200p. You might decide that should the price reach 220p you would like to take your profit and therefore set a 'Limit Sell' order at 220p. Alternatively, you might have a keen interest in Vodafone but think it is over-priced and decide to set a Limit Buy order to open a position should the price go down to 180p.

A linked order allows you to place two orders against the same trade e.g. both a Stop Loss and a Limit Order. If one order is executed the other one will automatically be cancelled.

Good for Day (GFD) & Good Till Cancelled (GTC)

When placing a limit or stop order, you will normally have two options of how long you can leave your order open for; 'Good For Day' (GFD) which means your order will be valid until the end of the day, or 'Good Till Cancelled' (GTC), meaning your order will be valid until you instruct the provider to cancel it.

Stop loss		
If you go	**You will**	**you will set your Stop Loss**
Long	open your position with a buy	below current sell price
Short	open your position with a sell	above current buy price

IMPORTANT: the above examples are for illustration purposes only, to show the impact of price movements. These exclude the impact of margin, financing and dividends. Ensure you fully understand the terms of any contract before opening any position.

How much does it cost?

We've already mentioned that there is a very wide range of investments in which you can trade. Each type of investment has its own way of calculating how much money you need to pay when placing an opening bet – this amount is often known as the initial margin payment. We will look at the two most common forms of margin, on equities and indices:

When you have calculated your initial margin payment, you will need to ensure that when you place a bet you have sufficient money on your Spread Betting account to cover it.

Your broker will supply you with more information via the dealing platform, or you will be able to speak to a dealer to clarify how the margin is calculated for a specific instrument.

EQUITIES

The amount you pay up front is normally calculated as a percentage of the full value of the bet, which in turn is your stake multiplied by the price. Margin for equities in the Daily UK 350 index can be as little as 5%, so the initial margin payment for a £20 bet on Vodafone at 200p would be calculated as follows:

Stake	£20 (or 2000p) per point
Price	200p
Contract value	£4000 (20 x 200)
Initial Margin	£200 (=£4000 x 5%)

INDICES

Each index has a fixed margin factor associated with it - for example a Daily index might have a margin factor of 0.5%. Initial margin payment is calculated by multiplying the bet size x price x margin percentage. So for a £10 bet on the Daily UK 100 index (with a current value of 6000), it would be:

Stake:	£10 per point
Price:	6000
Initial Margin:	£300

IMPORTANT: the above examples are for illustration purposes only, to show the impact of price movements. Ensure you fully understand the terms of any contract before opening any position.

Calculating the cost of your trade

We've now looked at the two main factors that determine what your bet will cost – whether the price goes up or down, and also the margin. Let's put these together and look at a couple of examples so you can see how they work in practice.

In this example, you are going long (i.e. buying) a September UK 100 stock index contract, at a value of 6000 points. You bet £10 a point that the value of the UK 100 index will rise above 6000 by the time your bet expires.

The initial margin payment, i.e. the amount needed to open the bet, is:

Bet size (£10) x price (6000) x margin factor (0.5%) = £300

So if your initial margin payment is £300, you will need to make sure there is enough money in your Spread Betting account to pay for this.

Now look at what happens if the index goes up by 100 points, and down by 100 points.

EXAMPLE 1 – UP BY 100 POINTS

The Trade	Opening value	6000
	Closing value	6100
	Difference	+100
You Spend	Initial margin (IM)	£300
Profit	Profit per point	£10
	Profit (100 x £10)	£1000
	Profit %	333%

You are left with a balance of £1300 (£300 initial margin + £1000 profit)

EXAMPLE 2 – DOWN BY 100 POINTS

The Trade	Opening value	6000
	Closing value	5900
	Difference	100
You Spend	Initial margin (IM)	£300
Profit	Loss per point	£10
	Loss (-100 x £10)	-£1000
	Loss %	333%

You are left with a balance of -£700 (£300 initial margin - £1000 loss). As soon as your account has a negative balance, your broker could contact you and ask you to top up your account so that your total position remains in credit. Your broker could close out any negative positions.

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TIPS ON BECOMING A BETTER TRADER

Ultimately, whether you make or lose money is down to you and the strategies you adopt. When Spread Betting, the risk and reward are always there in equal measure and the successful trader is one who knows how to minimise one and maximise the other. Here are a few tips that might help:

- Only trade with money you can afford to lose.
- Don't get carried away by trading up to your margin limit – it is usually better to trade small amounts over time, than risk losing one huge amount very quickly.
- Never open a position without setting a Stop Loss order to protect yourself.
- Never invest on a whim, but identify your target price and invest at the right time. Most investors will enjoy more success from a handful of companies or markets that they watch closely.
- Get to know the trading platform first by using a trading tutorial. Learn how to take profits using Limits and cut losses using Stop Losses.
- Greed is always a big factor when investing. Set yourself profit targets and stick to them.
- Think about how much you are willing to lose. Set your Stop Loss and keep to it, don't keep moving your Stop Loss further away in the hope that the price will recover. Cut your losses and look for other opportunities.
- Only open a Spread Betting account and start trading once you fully understand the concept and all the risks involved.

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Binary Bets

Some providers will also offer Binary Bets on a number of markets. Binaries are a fast-moving yes/no proposition on an index from 0-100.

How Binary betting works

Binaries are a special type of bet that allow you to trade on the performance of a financial market over a specific time with only two possible outcomes, either settling at 0 or 100.

For example, there might be a Binary quote on whether the UK 100 index will settle up on the day. If the event occurs (in this case, UK 100 index settling at a higher price than the previous day's close) the bet settles at 100; if it does not, the bet settles at 0. These are the only two possible settlement prices.

Binaries give you a simple win-lose proposition, just like a traditional fixed-odds bet. Except that you can also close your bet out before the final settlement, to cut your losses or take your profit early. Instead of quoting odds, the quote is a continuous two-way price for every Binary Bet.

You should note that Binary Betting is not subject to regulation by the Financial Conduct Authority. Providers offering Binary Bets will have information on responsible gambling on their website and will be licensed and regulated by the Gambling Commission.

Frequently Asked Questions

Q. How do I find out about different margin requirements and trading?

A. Nearly all Spread Betting providers will provide you with details on their dealing platform, but you can always check the details of a specific instrument by calling a dealer.

Q. How much money do I need to open an account?

A. This will vary from provider to provider; you can often open an account without having to deposit.

Q. How risky is Spread Betting?

A. Spread Betting is high risk as you're trading on margin. You can limit your risk by using Stop Losses and Guaranteed Stop Losses. Remember don't use all your money on just one trade – start small and build up.

Q. How long should I hold a Spread Bet for?

A. Although bets have expiry dates but you can hold them open for as long as you like by rolling them over. However, they are generally seen as short term investments due to the risk and financing elements. You will be able to close a bet at any point during the trading hours.

Q. How important are Stop Losses?

A. Stop Losses are an essential tool for successful traders. They are generally underused by private investors who do not take advantage of one of the most important investment tools available.

Q. Because it's risky do I need to constantly watch the markets?

A. Not if you place a Stop Loss. Although the margin element of Financial Spread Betting means that gains or losses can be achieved more quickly than via conventional trading, you will have all the investment tools you need to be able to set your Limits and Stops, so that you can manage your losses and take your profits without having to sit in front of your computer 24 hours a day.

If you have any questions
please call 0117 988 9915