markit®

4th floor
Ropemaker Place
25 Ropemaker Street
London
EC2Y 9LY
United Kingdom

tel +44 20 7260 2000
fax +44 20 7260 2001
www.markit.com

Markit Commentary

October 28th 2015

UK bears retreat in Q4

UK shares have been on a tear so far this quarter, which has prompted short sellers to trim their positions from the recent highs seen at the end of the last quarter.

— Average short interest in the FTSE 350 has fallen by 8% from the September highs
— Eight of the ten most shorted FTSE 350 constituents at the end of Q3 have seen covering
— ETF investors are staying on the sideline as UK equity funds have seen outflows in Q4

After a torrid third quarter which saw the FTSE 350 drop 12%, UK shares are having a resurgence in the closing months of the year. The index of large and mid-cap UK shares has managed to climb 5.5% in the opening weeks of Q4 putting it within 1% of breaking even for the year to date.

This resurgence in UK equities has seen short sellers pare back their positions in the index's constituents over the last three weeks. The current average short interest across the FTSE 350 index stands at 1.71% of shares outstanding, marking a 7% retreat from the highs seen in the closing days of the last quarter.

While the covering marks a significant climb-down from the highest levels of shorting activity seen by the index in over 18 months, the current demand to borrow shares in the index is still over 50% higher than the levels seen 18 months ago.

Covering across the board

The most shorted firms at the peak of the recent shorting cycle have led the charge as six of the ten most shorted firms at the end of September have seen a fall in demand to borrow.

This trend was led by dairy firm Dairy Crest, which has seen a significant 22% fall in demand to borrow its shares after its shares surged in the last week. This sudden covering saw Dairy Crest fall out of the top ten most shorted list, with the firm now the 16th most shorted constituent of the index.

Better than expected results also saw Sainsbury shares surge by over 15%. This has seen some tapering off of the demand to borrow the firm's shares, with short interest in Sainsbury's now 5% off the levels from October 1st.

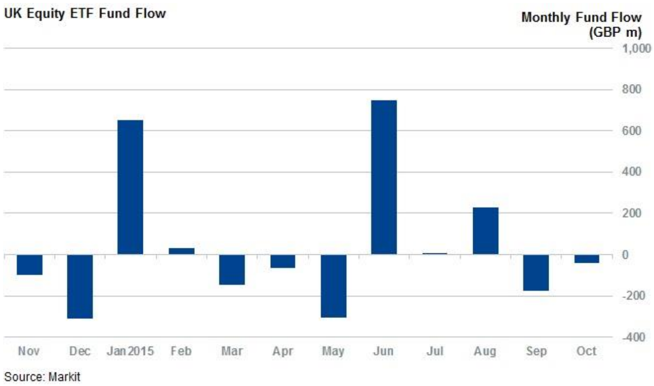
Morrison's and Tesco shares are also up sharply over October, and both firms have seen some covering from the all-time highs seen four weeks ago.

Sector wise, the covering has been pretty much across the board with shorting activity decreasing for 21 of the 24 components of the GICS level 2 sectors in the last four weeks.

One particular standout in the last few weeks has been utility firm Drax Group, which has seen its short interest surge by 17% so far in October. This surge in shorting activity coincides with the UK inking a deal with China to partner up to build the country's first nuclear power plant in over 20 years.

ETFs don't see the trend

Interestingly, ETF investors have not been getting behind the UK's equity rally as UK equity ETFs have seen a modest £40m of outflows so far in October. While not material from an AUM point of view, the outflows show that the recent rally still has to convince investors.



*To receive more information on **Securities Finance** or any other product or dataset please **contact us**

To read this article on our commentary website please click **here.**

Simon Colvin

Analyst

Markit

Tel: +44 207 260 7614

Email: simon.colvin@markit.com

For further information, please visit **www.markit.com**

The intellectual property rights to this report provided herein is owned by Markit Group limited. Any unauthorised use, including but not limited to copying, distributing, transmitting or otherwise of any data appearing is not permitted without Markit's prior consent. Markit shall not have any liability, duty or obligation for or relating to the content or information ("data") contained herein, any errors, inaccuracies, omission or delays in the data, or for any actions taken in reliance thereon. In no event shall Markit be liable for any special, incidental, consequential damages, arising out of the use of the data. Markit is a trademark owned by the Markit group.

This report does not constitute nor shall it be construed as an offer by Markit to buy or sell any particular security, financial instrument or financial service. The analysis provided in this report is of a general and impersonal nature. This report shall not be construed as providing investment advice that is adapted to or appropriate for any particular investment strategy or portfolio. This report does not and shall not be construed as providing any recommendations as to whether it is appropriate for any person or entity to "buy", "sell" or "hold" a particular investment.