

## UK short sellers cover, defying Brexit anxiety

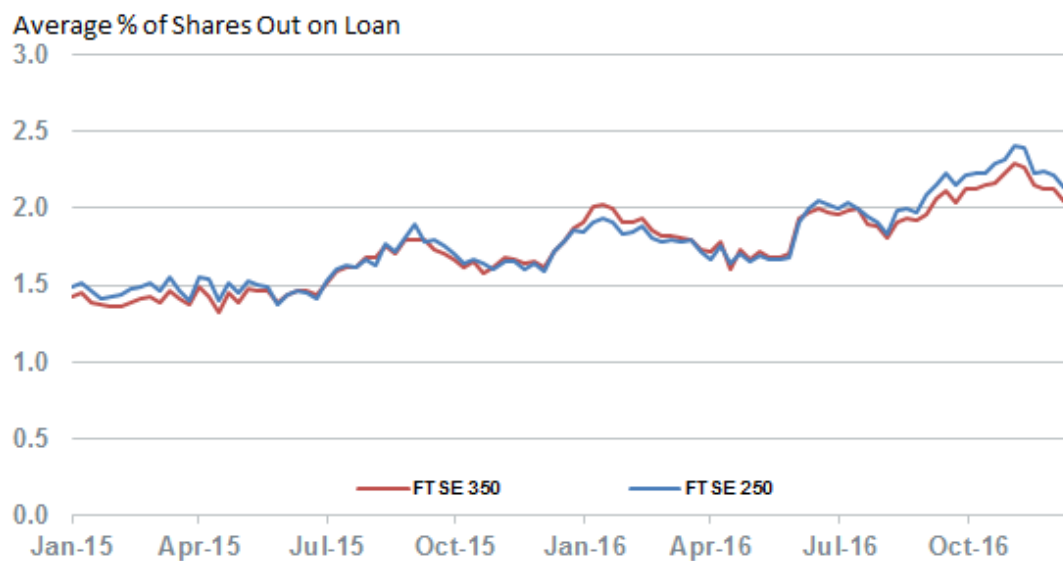
Monday, January 16<sup>th</sup> 2017

UK equities are enjoying their longest positive streak on record and investors are showing no desire to short the rally as current average short interest across the FTSE 350 stands at a three month low.

- FTSE 350 average short interest is back below 2% of shares, FTSE 250 constituents have led the covering
- The five most shorted FTSE 350 constituents have seen covering in 2017
- ETF investors from both sides of the Atlantic plough into UK funds

The potential impact of the “hard Brexit” plan has sunk the pound to recent lows on the eve of Theresa May’s long awaited speech on the issue. However this anxiety has by and large been constrained to the sterling market as both large and midcap UK equities have managed to sustain the rally initiated in the closing weeks of last year. This rally has not only pushed the FTSE 350 index to new highs, but has also tamed many UK equity skeptics as short sellers have actively been covering their positions in the index’s constituents over recent weeks.

### FTSE 350 Shorting Activity



In fact the average demand to borrow the constituents of the FTSE 350 constituents now stands to a three month low of 2% of shares outstanding; 12% lower than the average registered in early December last year. This covering marks the largest monthly fall in average UK short interest since the referendum back in June, underscoring the improving investor mood.

A further dig into the numbers shows that the covering has been led by the midcap FTSE 250 end of the index, whose relatively large UK exposure made them favourite short targets following the referendum. While these companies still see relatively more shorting activity than at the same time last year, the fact that domestically exposed equities see covering indicates that the market is choosing to focus its attention on buoyant economic indicators, such as the latest [service](#) and [manufacturing](#) UK PMI published by [Markit Economics](#), rather than the possible impact of a falling pound.

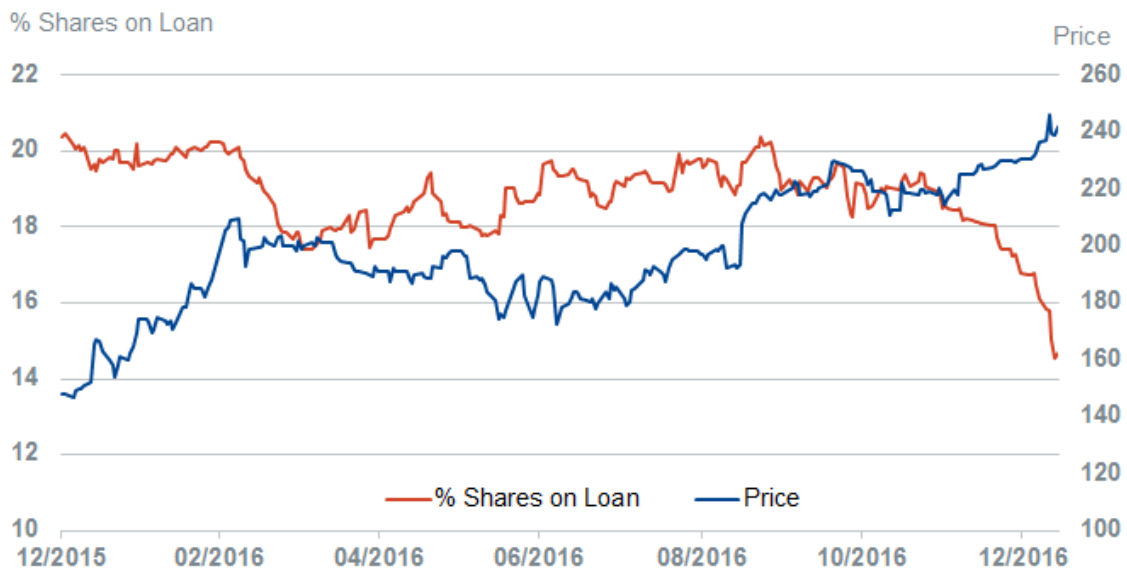
### High conviction shorts lead the covering

Short sellers have been just as eager to trim positions in their high conviction plays as the rest of the market, as 17 of the 20 most borrowed constituents of the FTSE 350 index have seen shares on loan returned over the last four weeks.

Chief among the stocks experiencing covering is supermarket WM Morrison whose demand to borrow has sunk by a fifth in the last month. This covering has been spurred on by its [best performance](#) over the Christmas trading period in over seven years which has propelled its shares to the highest level in nearly three years.

Morrison's peers Ocado and Sainsbury's, which also feature among the high conviction short plays, have also experienced covering over the last month with an 8% and 9% fall in demand to borrow respectively.

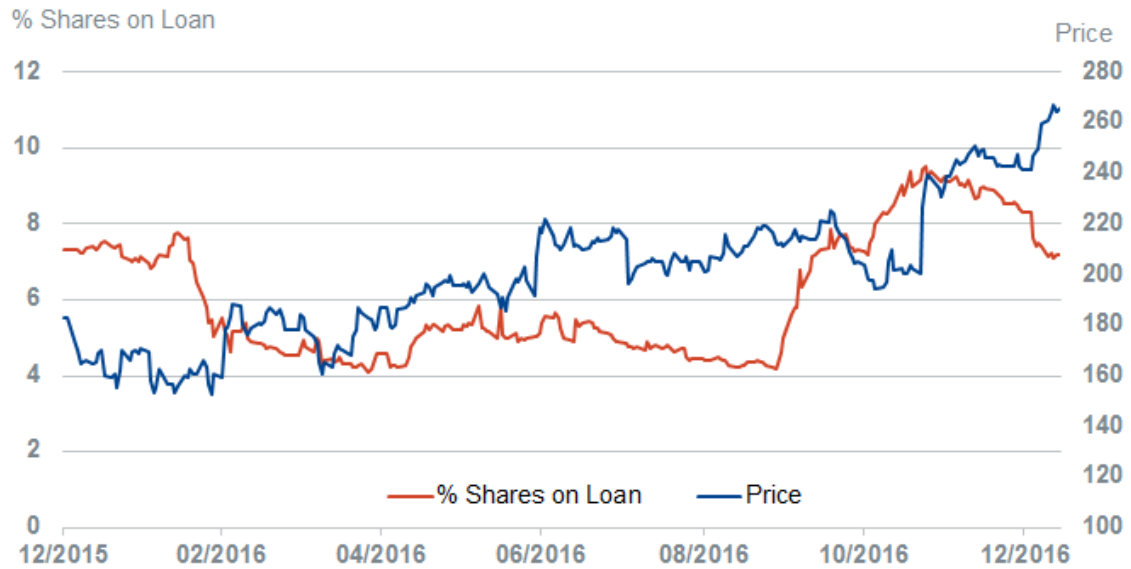
### Wm Morrison Supermarkets Plc



Source: IHS Markit

Covering isn't confined to retailers, as engineering and automation firm Rotork has also experienced a significant fall in its short interest as 19% of its loans have been returned in the last four weeks. The pound's crash is likely to disproportionately benefit the firm as it earns over 88% of its revenues from overseas.

## Rotork Plc

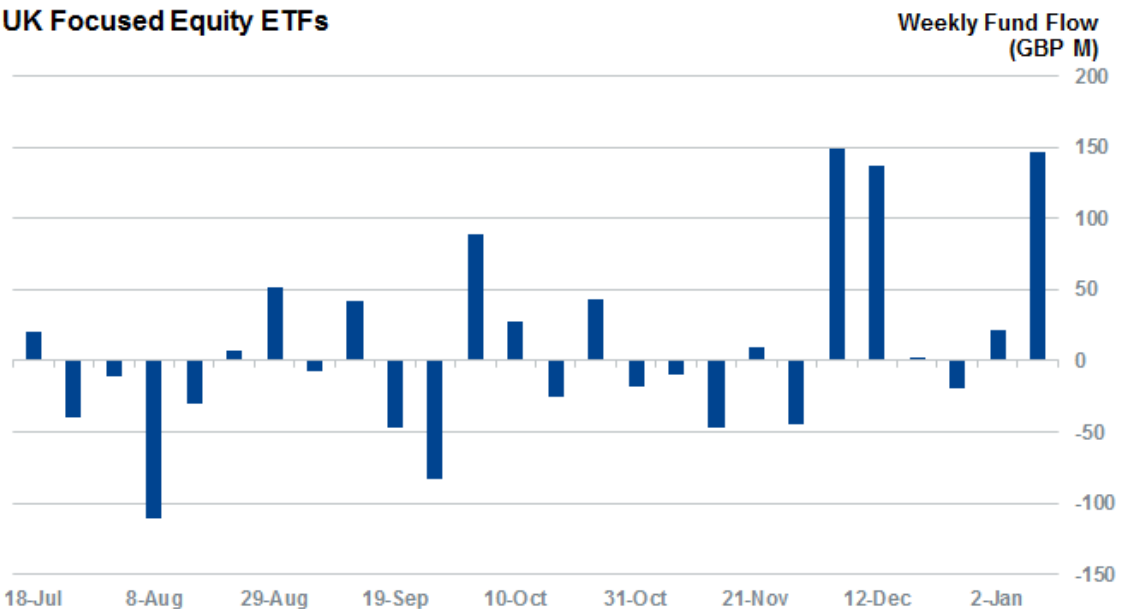


Source: IHS Markit

## ETF investors pile in

ETF investors have also been keen to ride the surging trade as UK equity ETFs have seen over £160m on inflows year to date, with flows coming from both European and overseas listed funds. US investors have driven two thirds of the inflows after £117m of new assets were parked into the iShares MSCI United Kingdom ETF last week alone.

## UK Focused Equity ETFs



Source: IHS Markit

Despite the falling pound, products that hedge against the further falls in the UK's currency have continued to see lukewarm demand from investors as these funds have only attracted £17m of new assets over 2017 or 10% of the year to date inflows.

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