



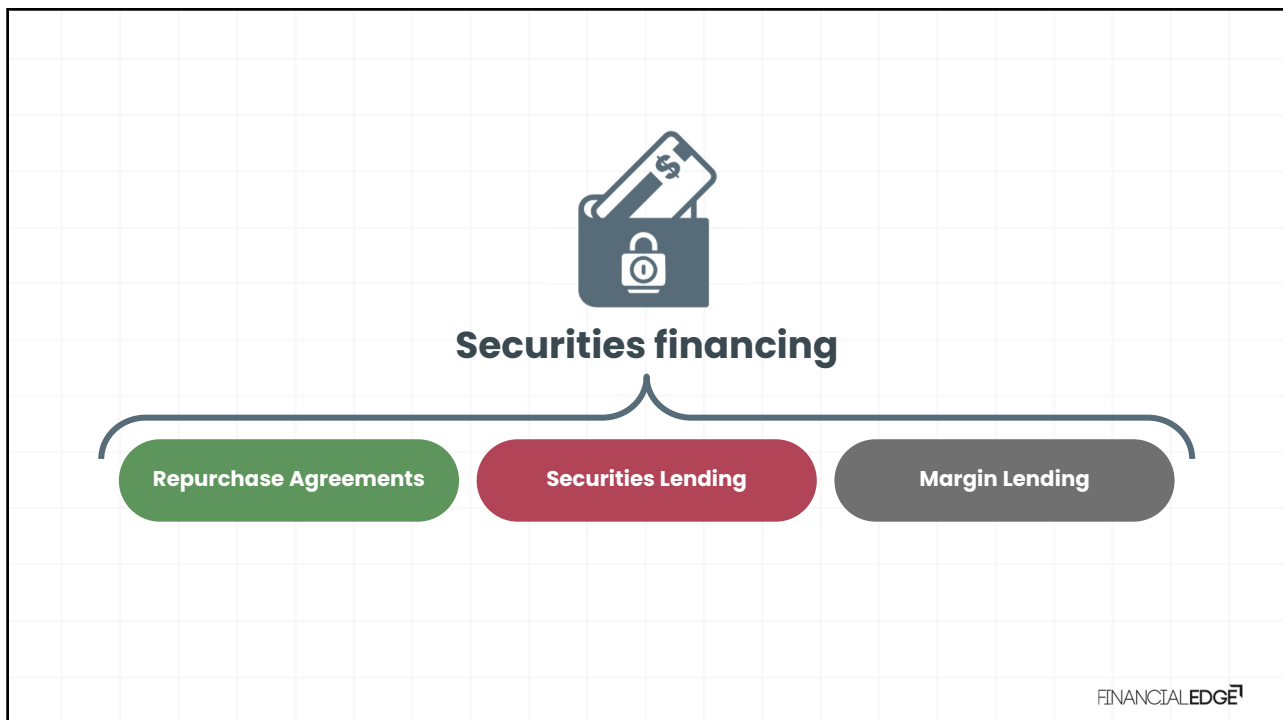
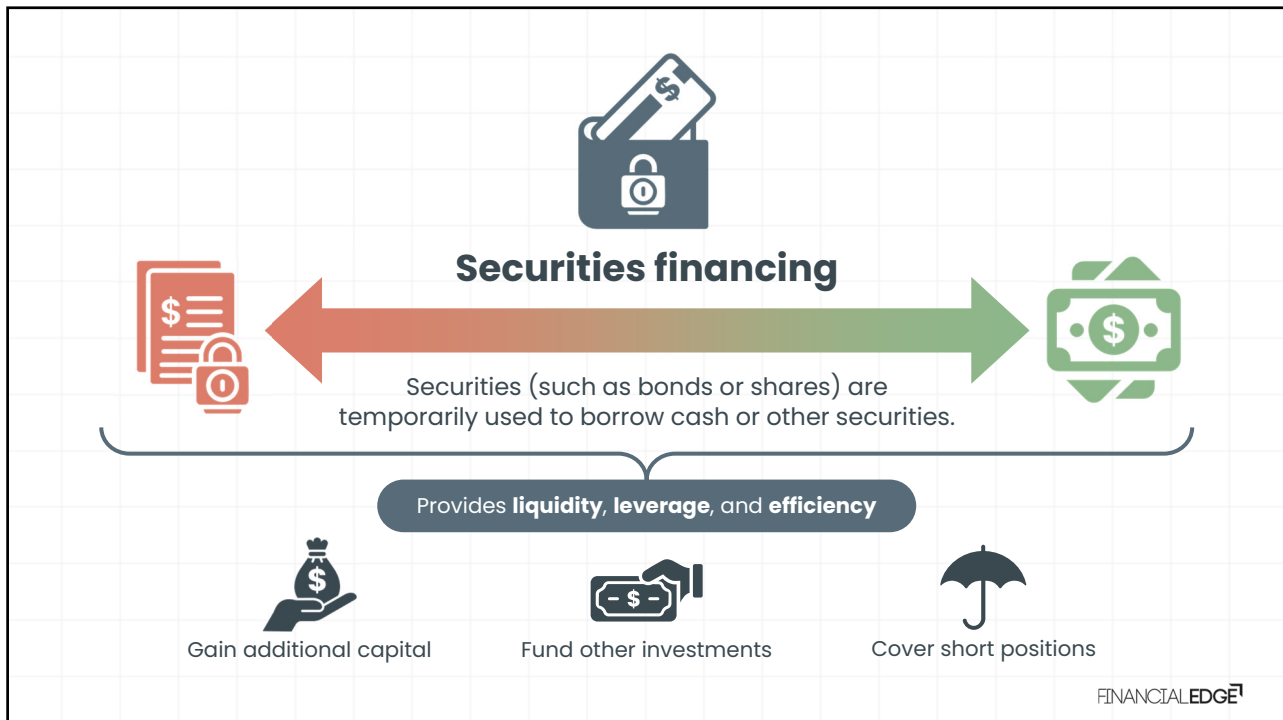
Securities Financing and Lending

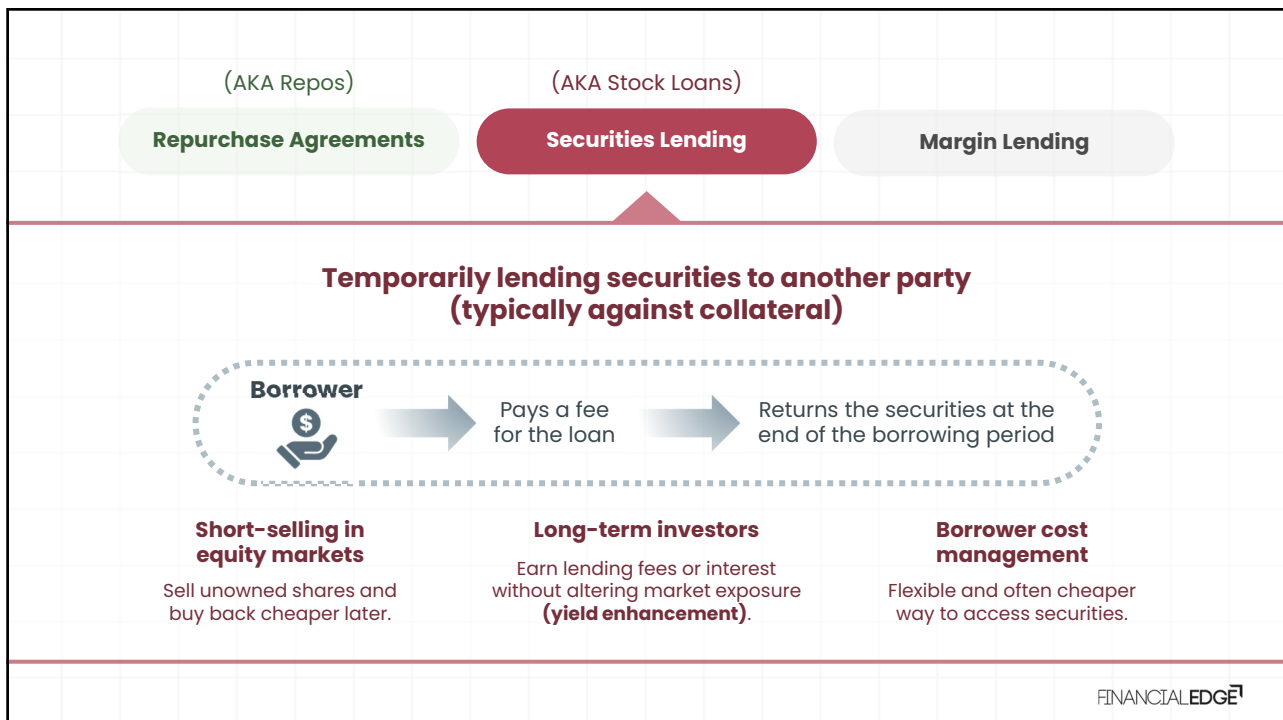
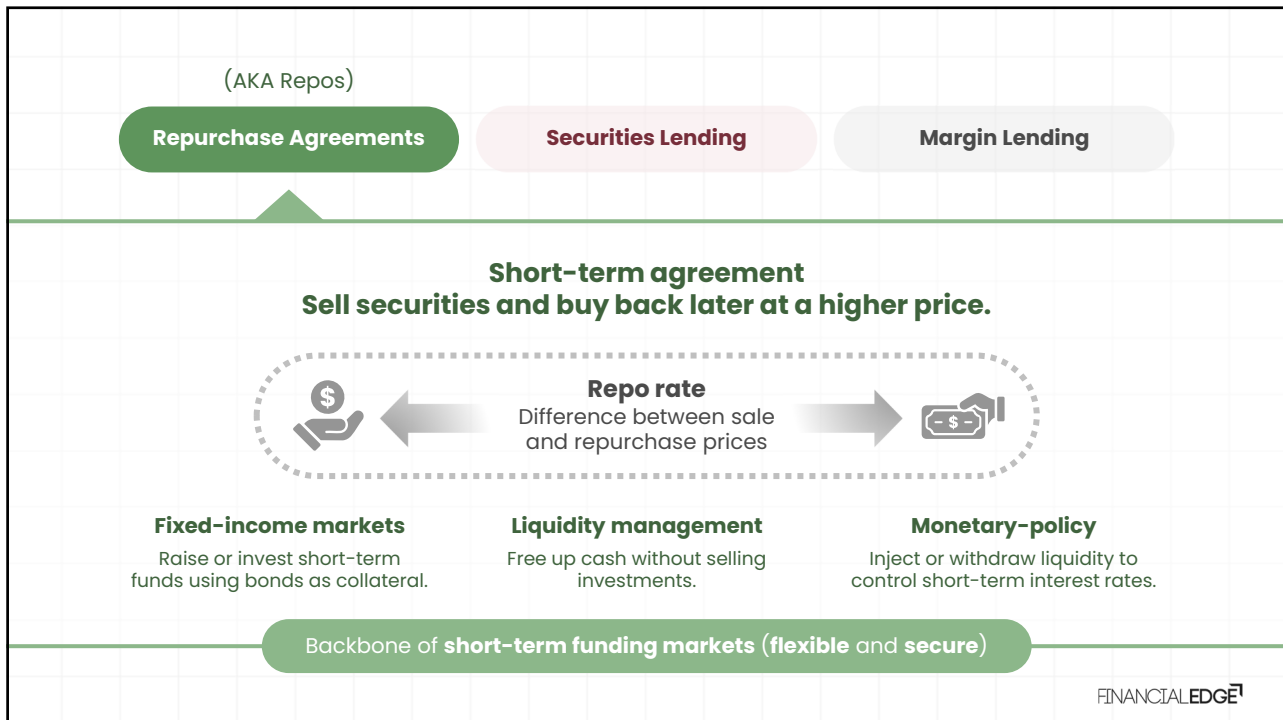


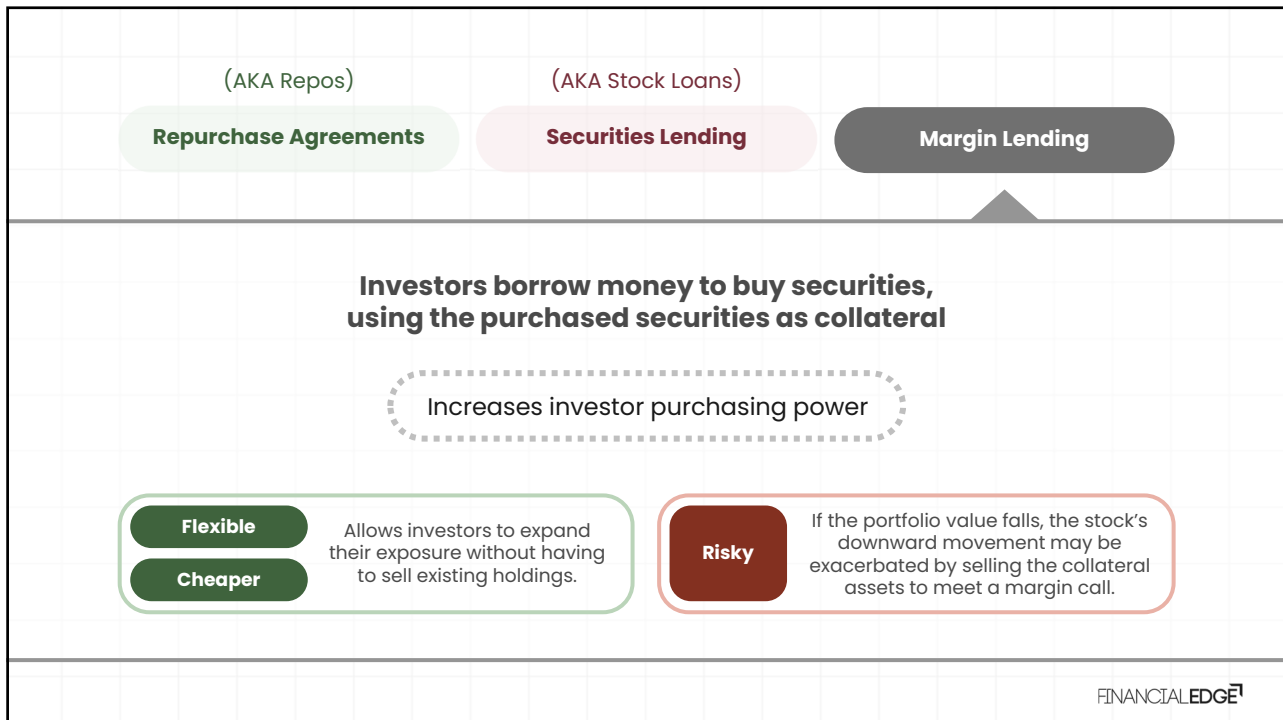
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Securities Financing Overview

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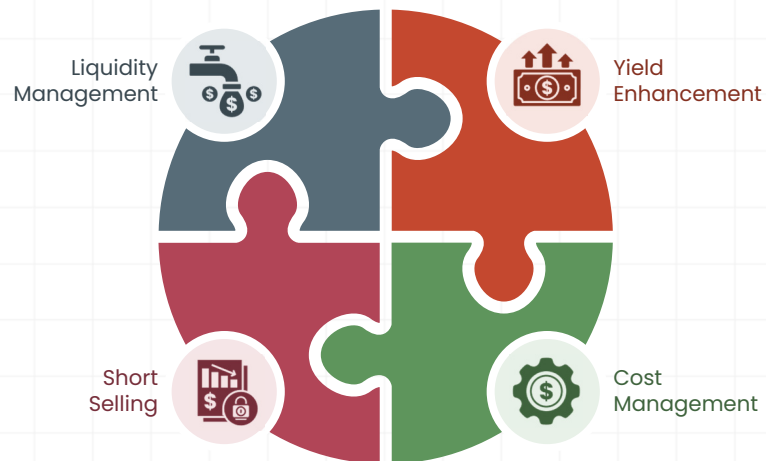




Securities Financing Motives



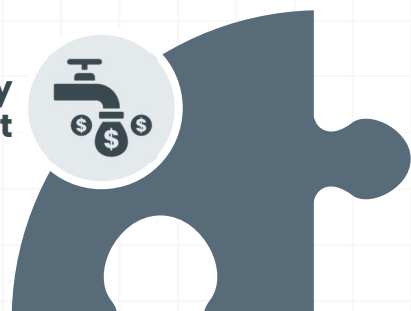
Securities financing key functions

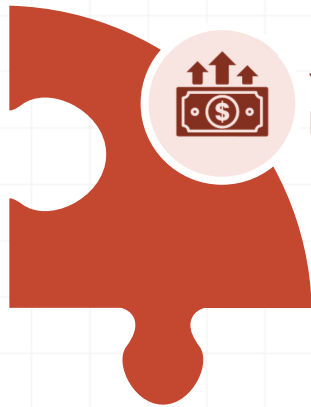
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Institutions use securities financing to manage their liquidity needs (**ensuring they have enough cash for operations**)

Often more **flexible** and **cheaper** than short-term bank loans

Liquidity Management

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Yield Enhancement

Lending out securities earns **additional income** (fees or interest)

Boosts the overall yield on their investment portfolio

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Borrow securities to sell them short (if the price declines, they can buy **back later at a lower cost and profit**)

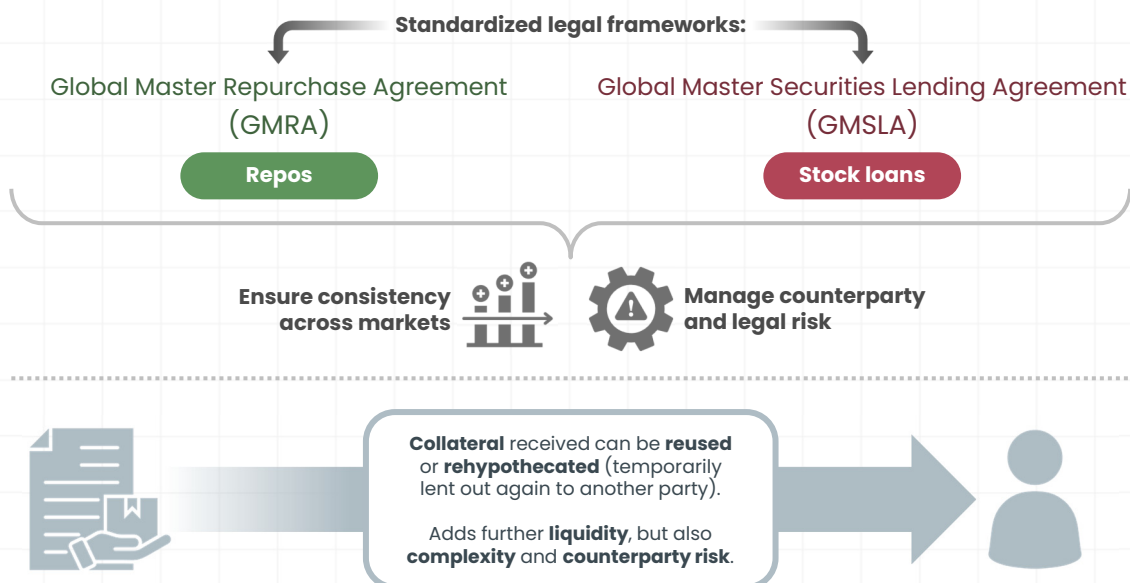
Adds **liquidity, price discovery**, and **depth** to the markets, but can create **short-term volatility** and **controversy**

Short Selling

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Repos and stock loans can provide **cheaper funding than unsecured borrowing** (especially for **short-term** needs)



Equity Trading Strategies

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Equity Trading Strategies

How investors use equities



Objectives



Risk appetite



Investment horizon

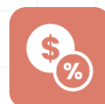
As a **liquid established** asset class, equity investing attracts a wide range of participants:



Pension funds



Insurance companies



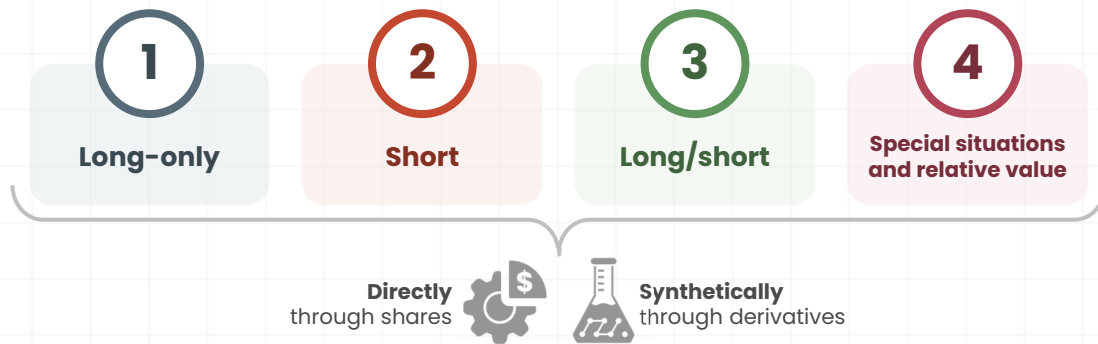
Hedge funds



Active traders

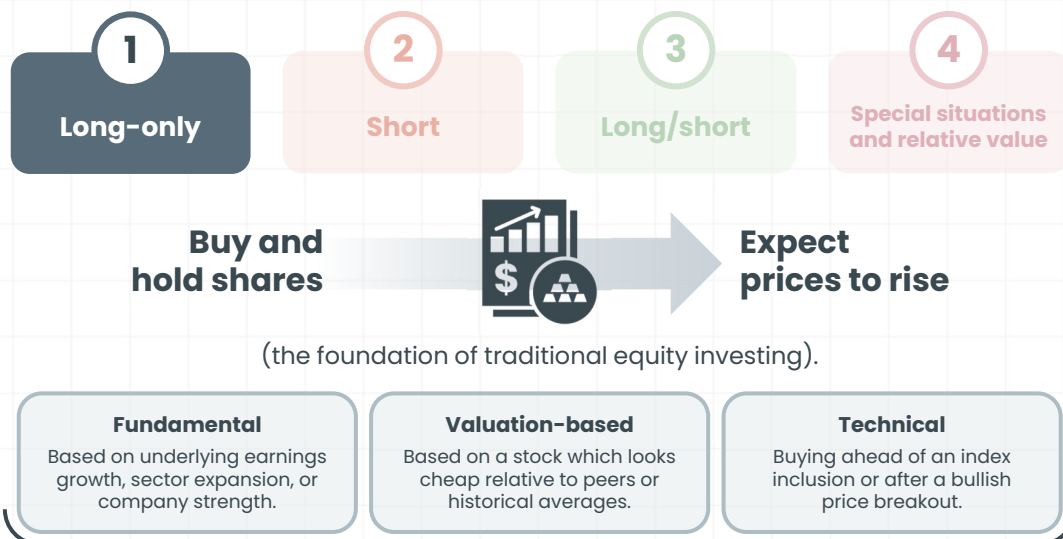
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Equity Trading Strategies



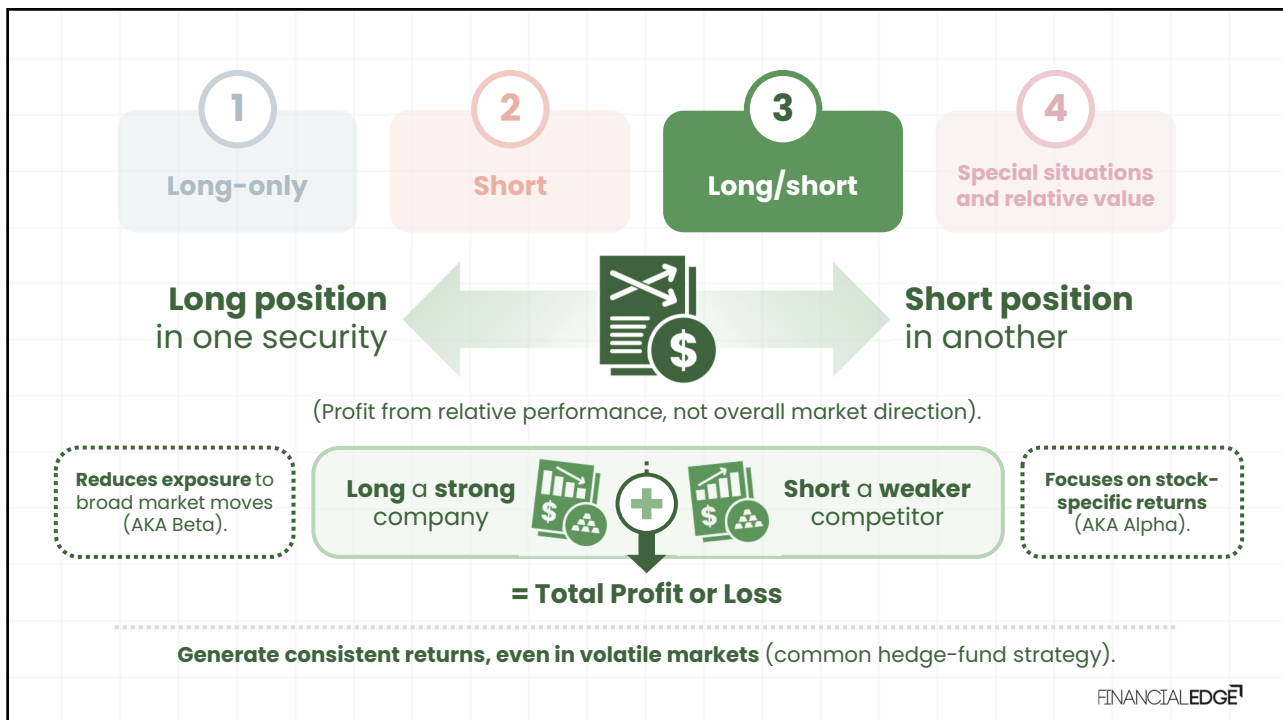
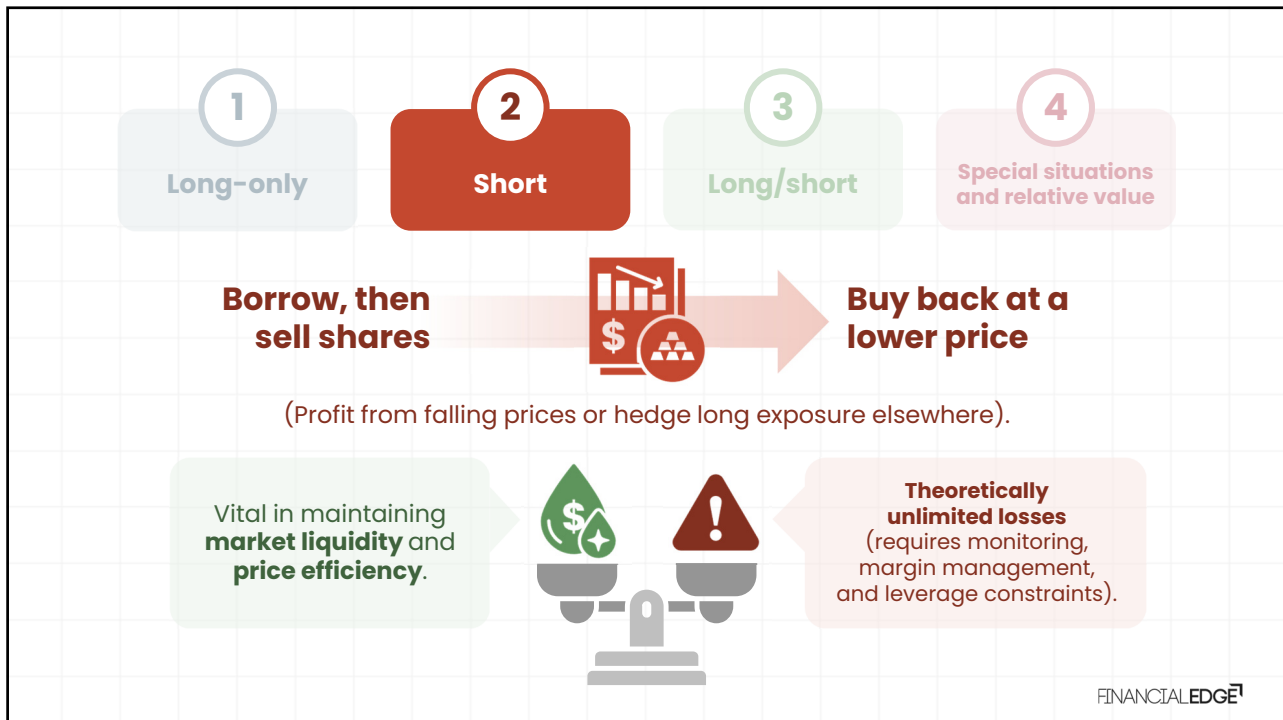
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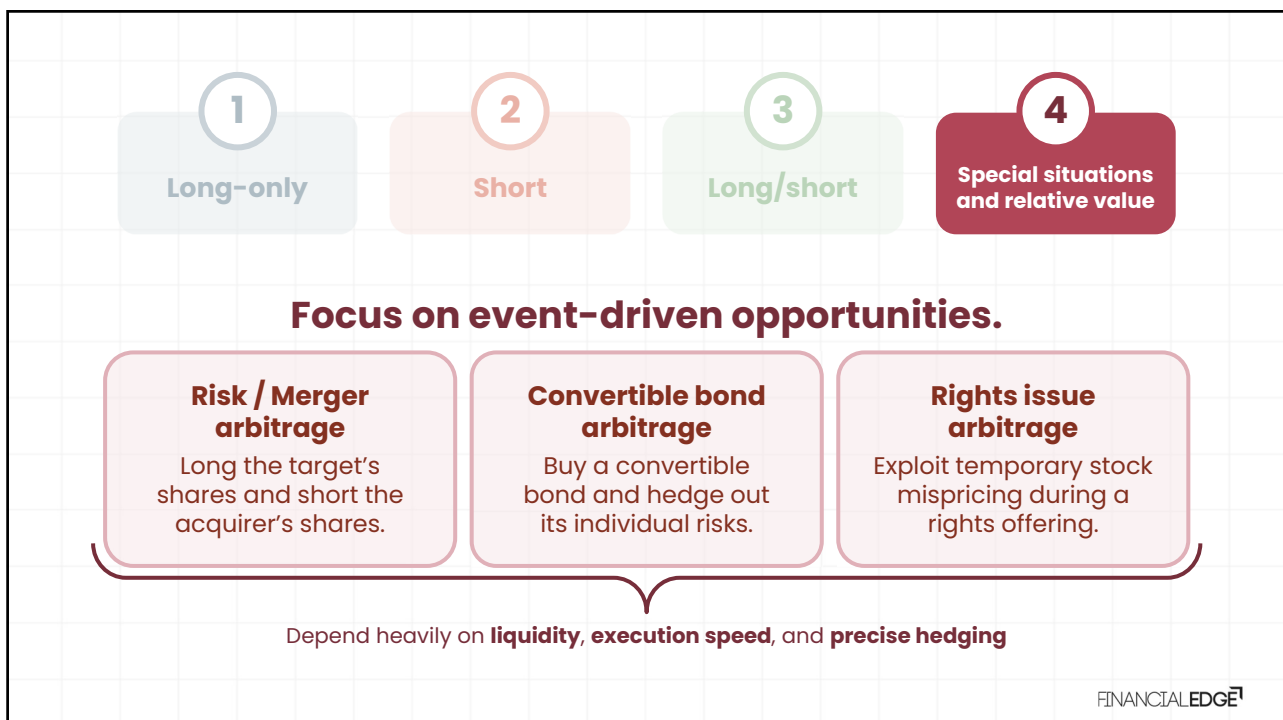
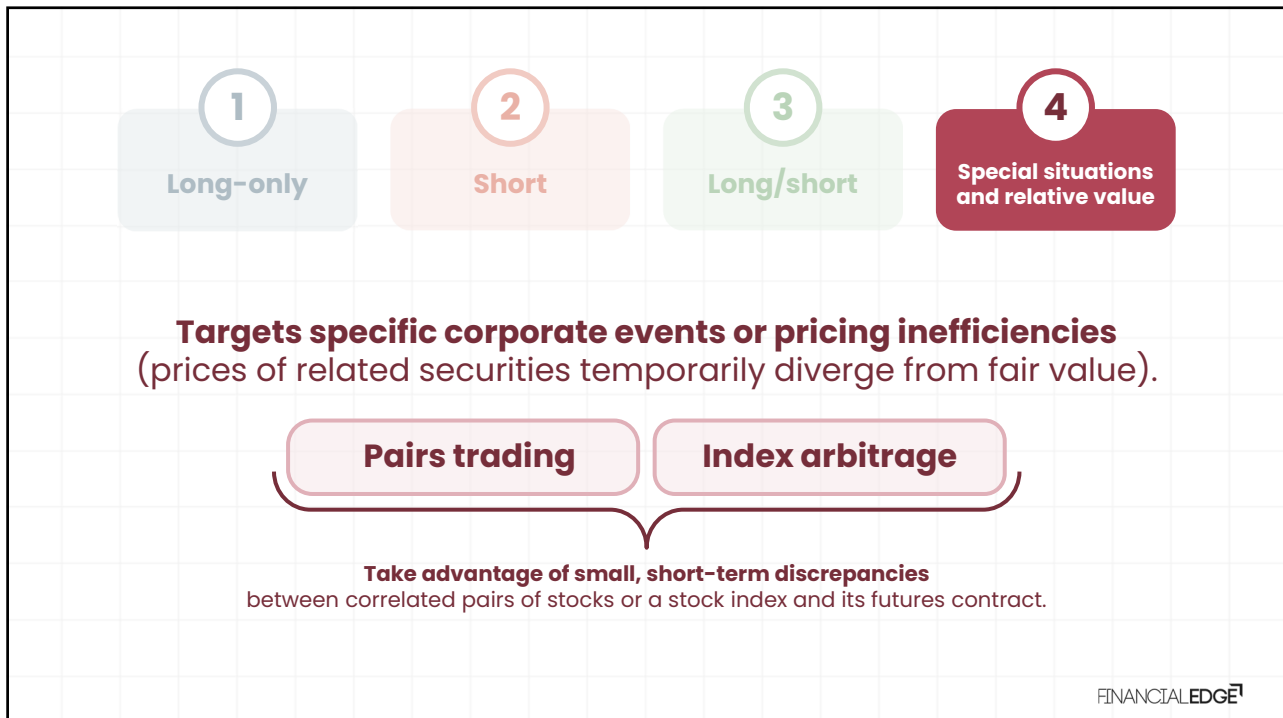
Gives flexibility in **shaping exposure, managing risk, and using leverage efficiently.**

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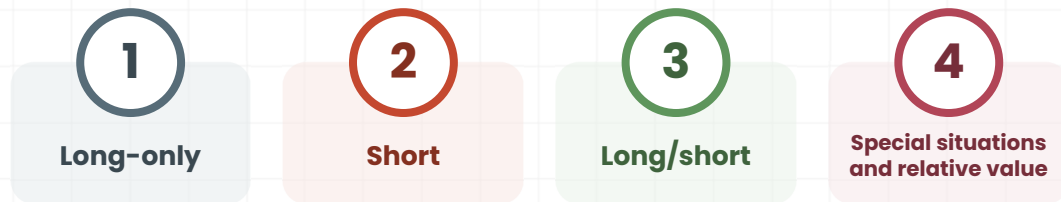
Goal: Benefit from **capital appreciation** and **dividend income**.

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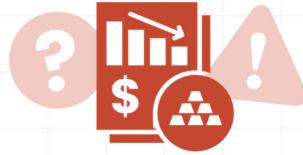


Equity Trading Strategies

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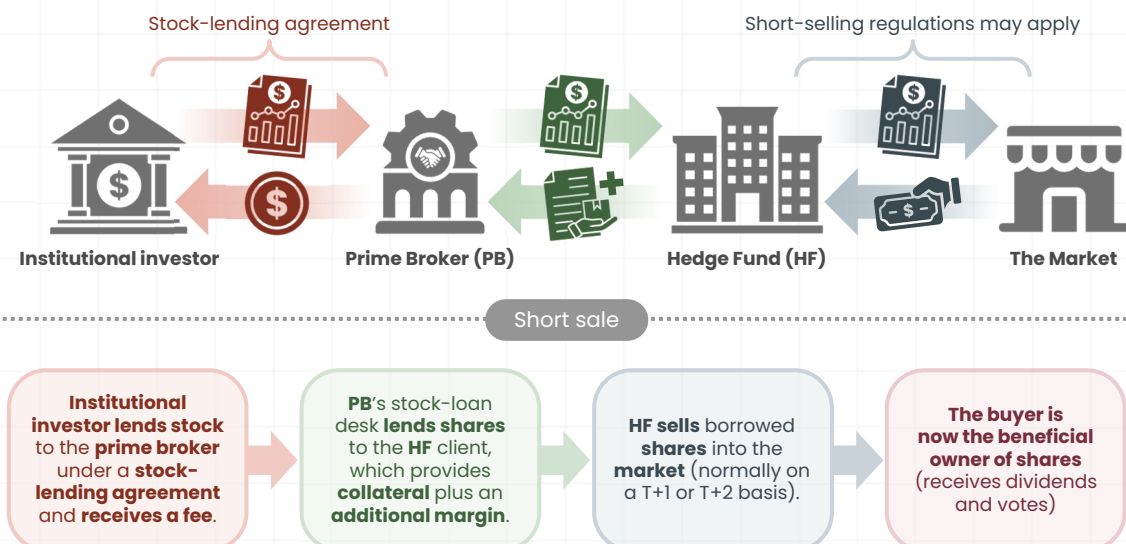
Short Selling Mechanics

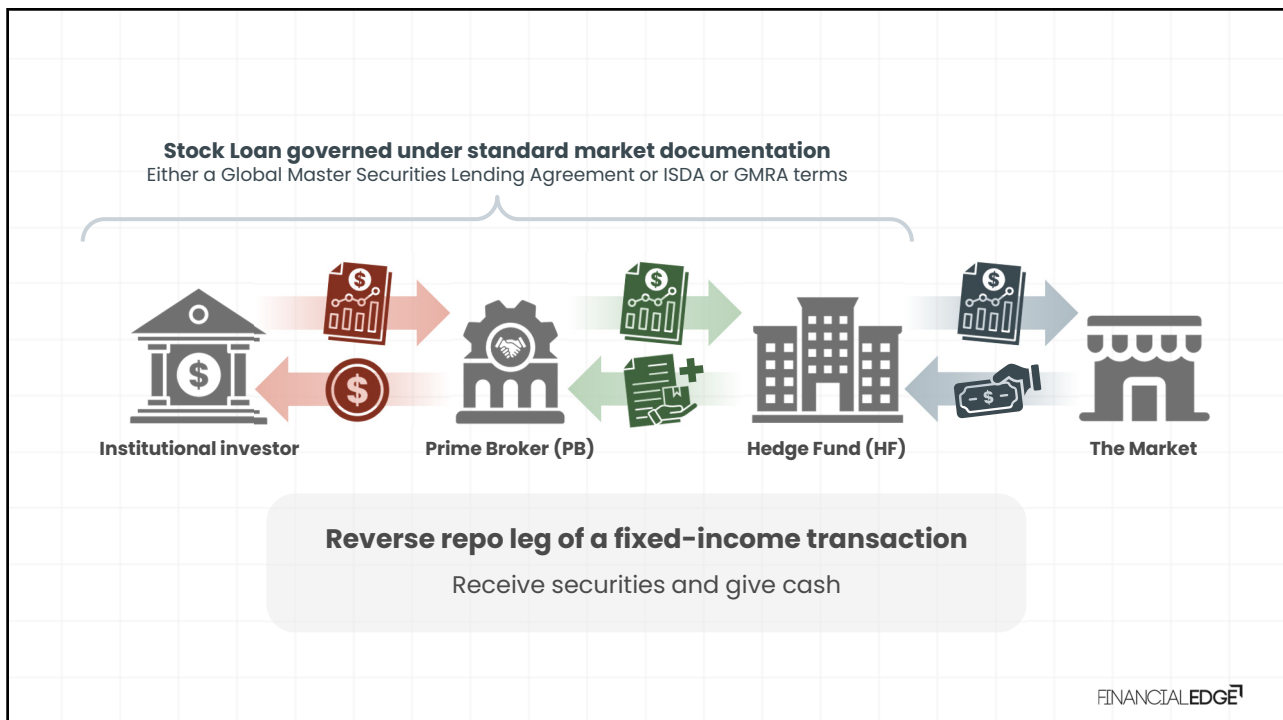
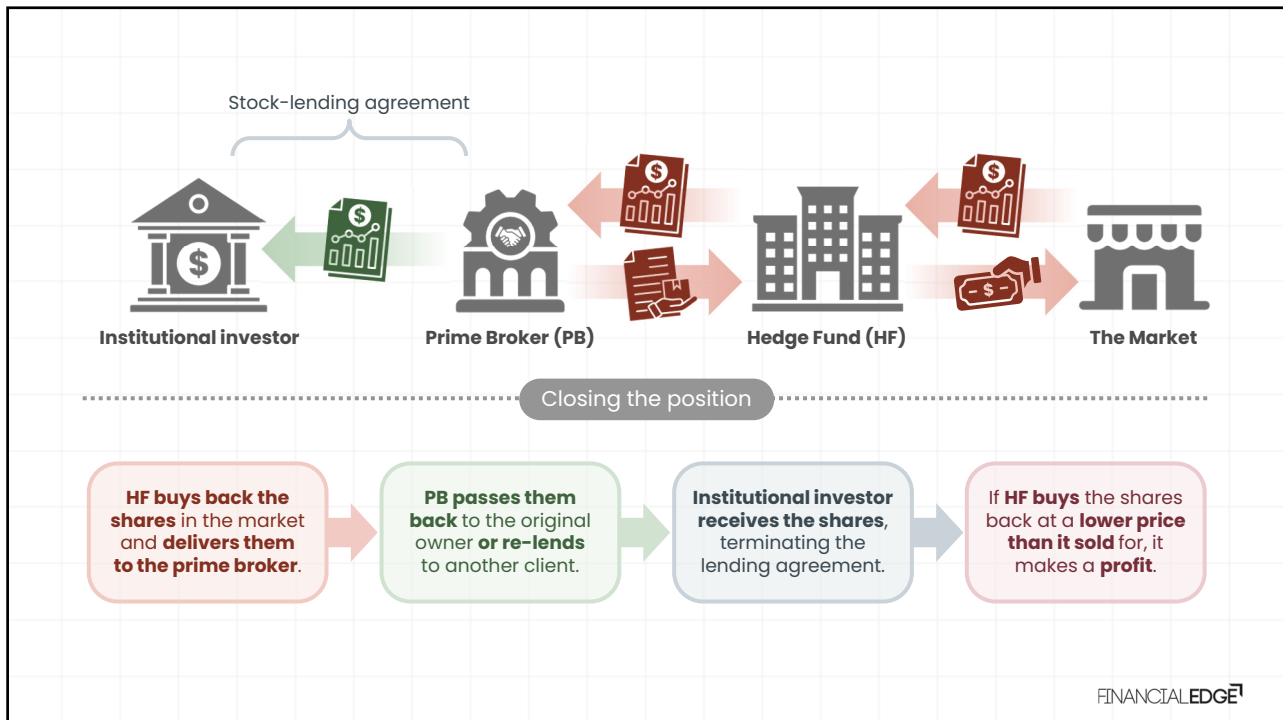
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Short selling

Just another way for investors to express a view on where prices are heading.

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Stock-borrow fees



Depend on **supply** and **demand**

Liquid (easy-to-borrow) stock

20 basis points per year

Specials (hard-to-borrow) stock

500+ basis points per year

If the borrow is difficult to find, the **prime broker or investor may require a term loan** (if the hedge fund covers its short early, it will still pay the full).



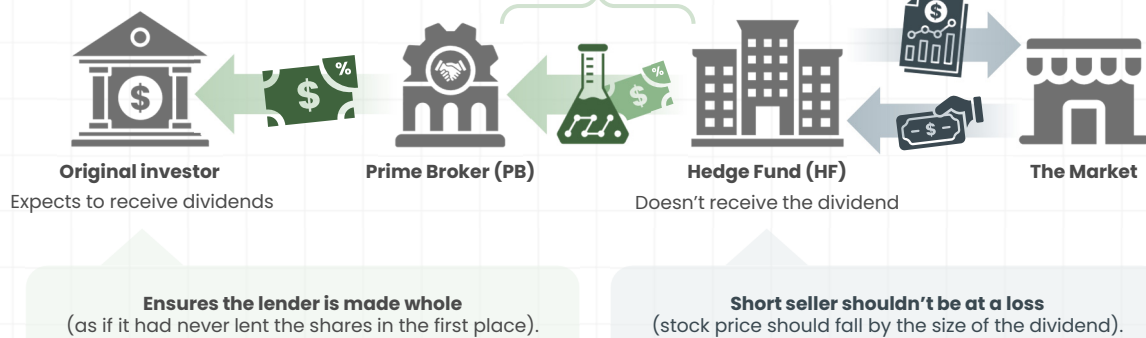
E.g. company is **in trouble** or heavily involved in a **merger-arbitrage trade**.

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Dividend payments



Synthetic cash-dividend



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Short Selling Risk & Regulations

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Short selling

Closely **monitored** and **regulated**



Uptick rule

Restricts new short sales once a stock's price has **fallen significantly** during the day.

Prevent short sellers accelerating a downward spiral.

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Uptick rule



If a stock has dropped by 10% or more from its previous day's closing price, short sales can only take place on an uptick (priced above the current best bid).



Best bid:
\$20.00



Best offer:
\$20.02



Short sale at any price
above \$20.00

Helps **slow momentum** and **stabilize trading** when markets become stressed

Historically, many countries have **temporarily banned short selling completely** for **certain sectors**.



Operational risks

Stock Recall

Short Squeeze



Original investor
can recall shares
if needed



Prime broker usually
replaces stock from
another source

In **tight markets**, recalls can **force short sellers**
to repurchase shares to cover their position.

Drives the price even higher.

Short interest



Expressed as either:

Percentage of total shares outstanding

"Days to cover" ratio (how many days it would take to buy back all outstanding shorts)

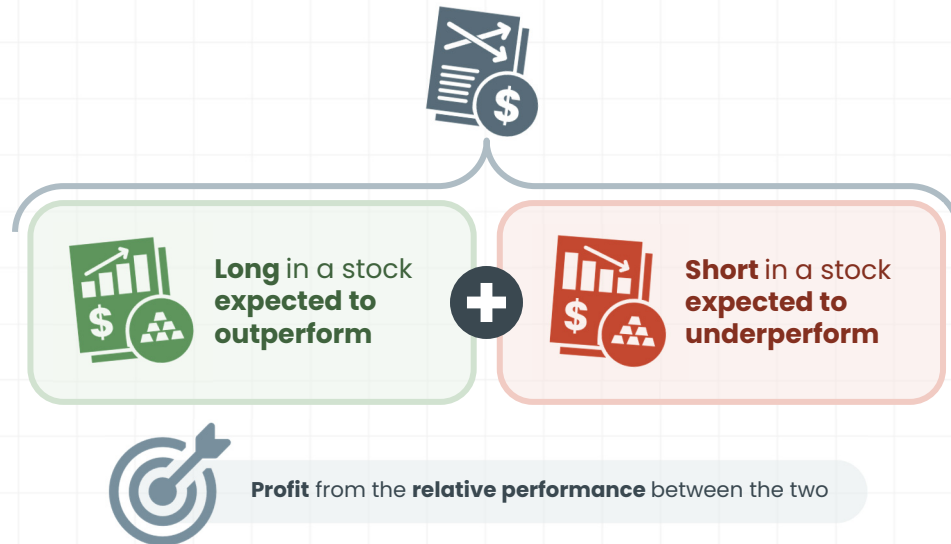
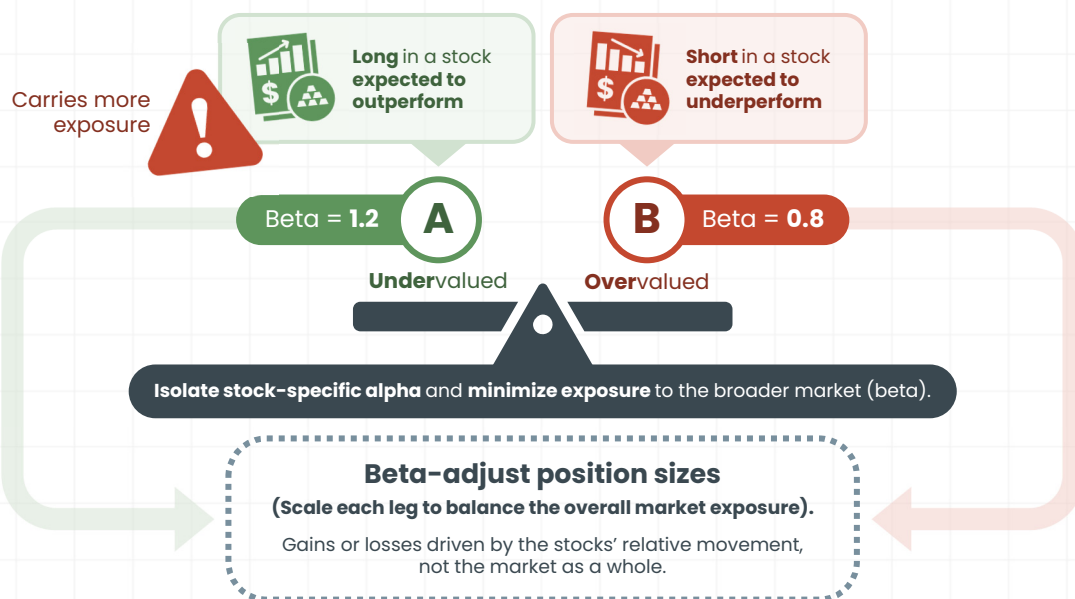
Rising short interest suggests **bearish sentiment**.



Declining short interest indicates **covering (confidence)**.

Equity Long Short Trading Strategies

Long/short equity strategy

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What drives returns?



Long in a stock
expected to
outperform

Earnings upgrades

New product launches or
corporate developments

Higher-than-expected
dividends

Positive news that attracts
equity investors



Short in a stock
expected to
underperform

Sector downgrades

Profit warnings

Earnings
disappointments

Rising financing and
input costs that could
pressure margins

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Long/short equity strategy

Idiosyncratic risk – specific factors affecting each company

If you're right (long position outperforms the short)
the spread between the two prices narrows in your favor.



Long in a stock
expected to
outperform



Short in a stock
expected to
underperform

If you're wrong (long position underperforms
and the short rallies) the trade loses money.

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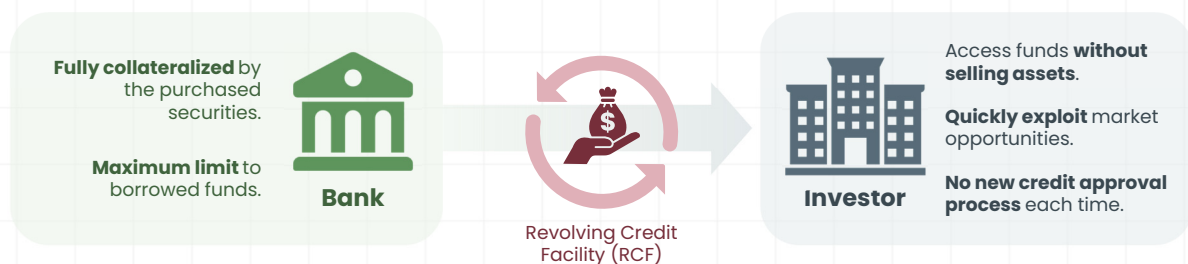
Margin Lending

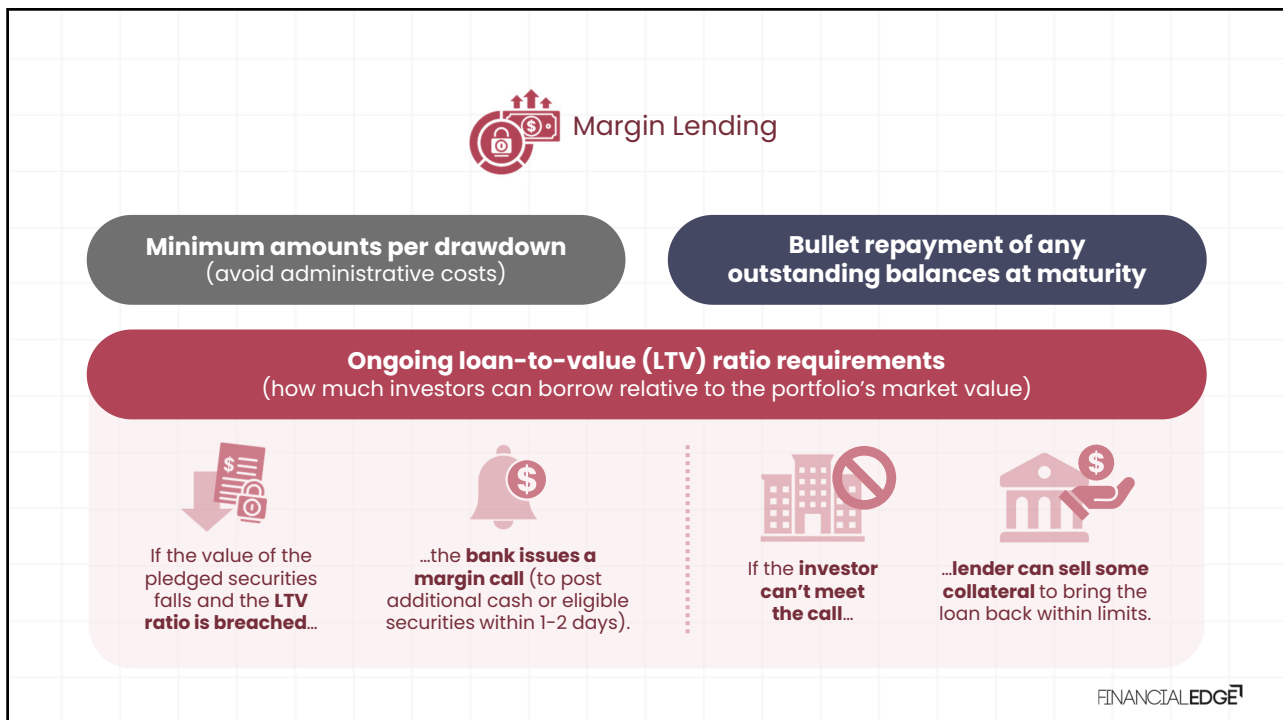
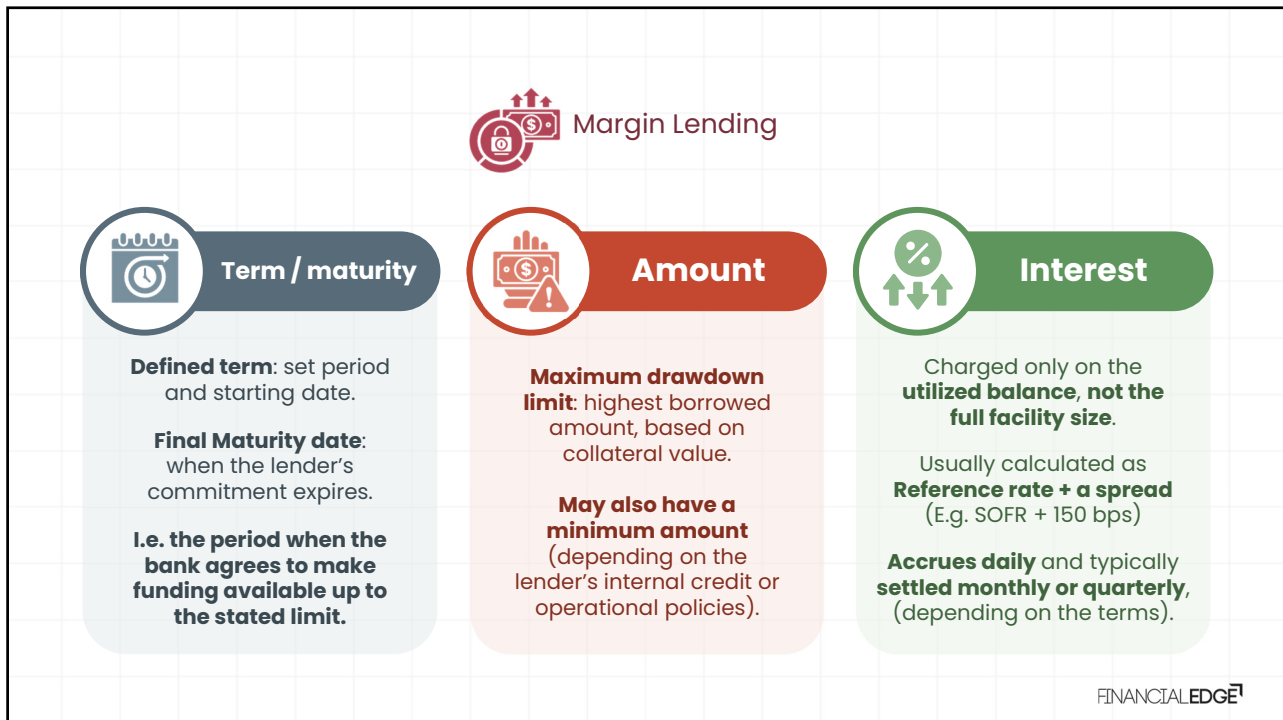
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Margin Lending

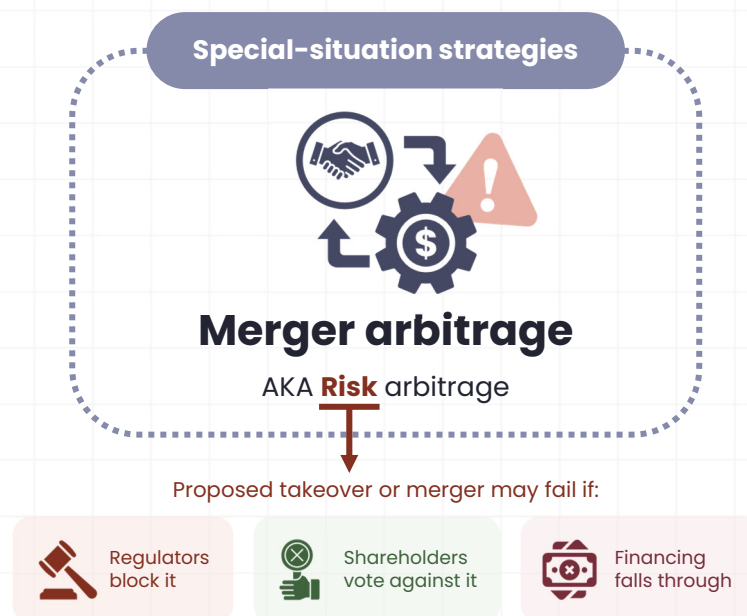
Raise or deploy cash using existing securities as collateral.

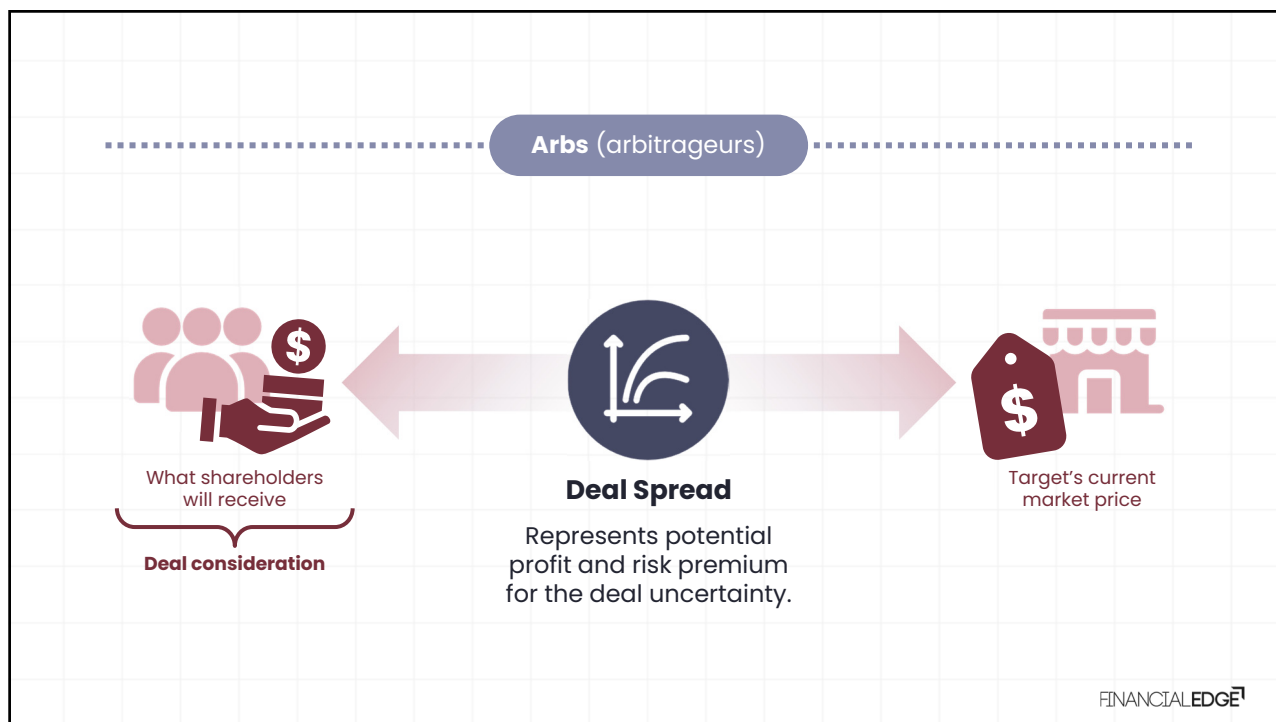
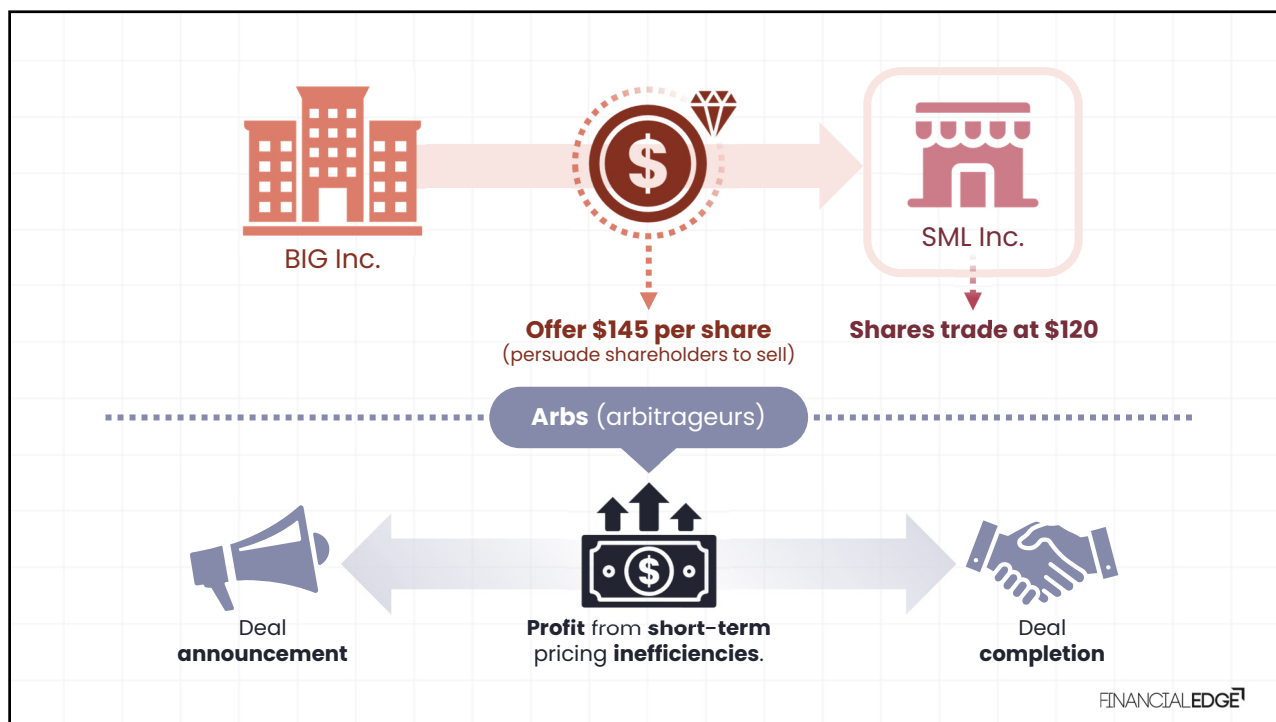
AKA **margin loans** or **securities-based lending**.

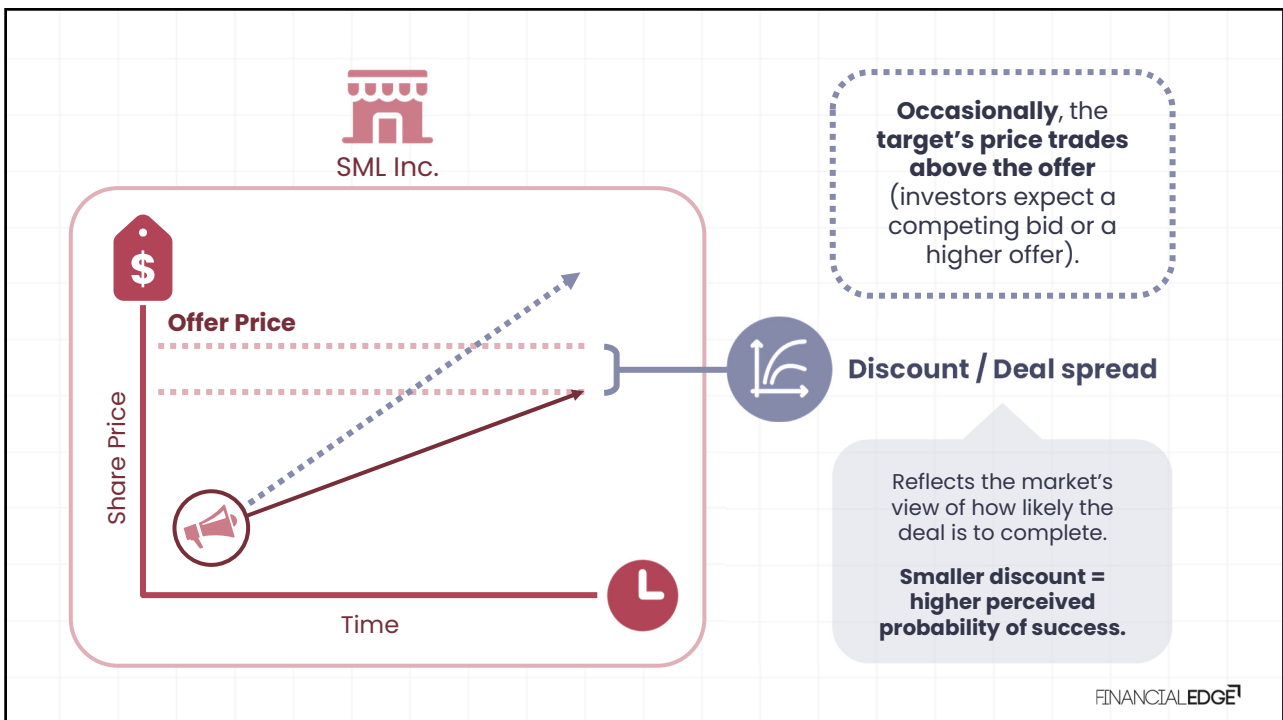
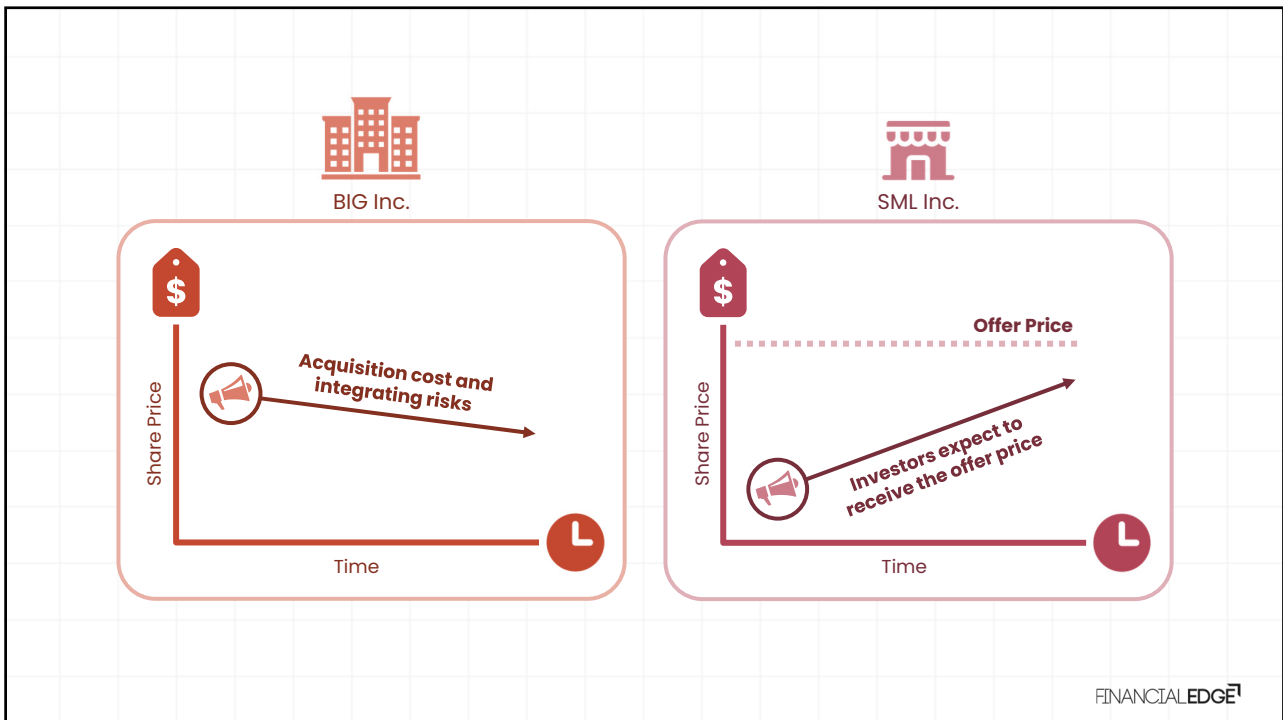
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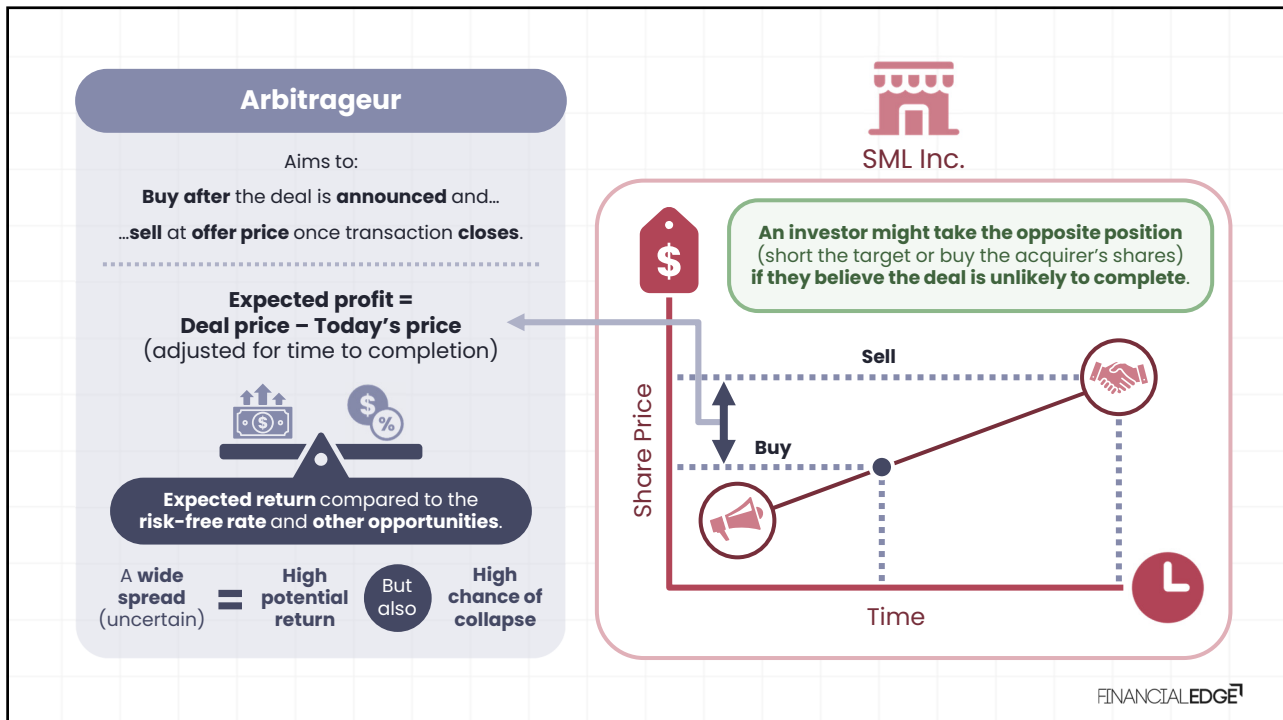


Equity Merger Arbitrage – Special Situation Investing

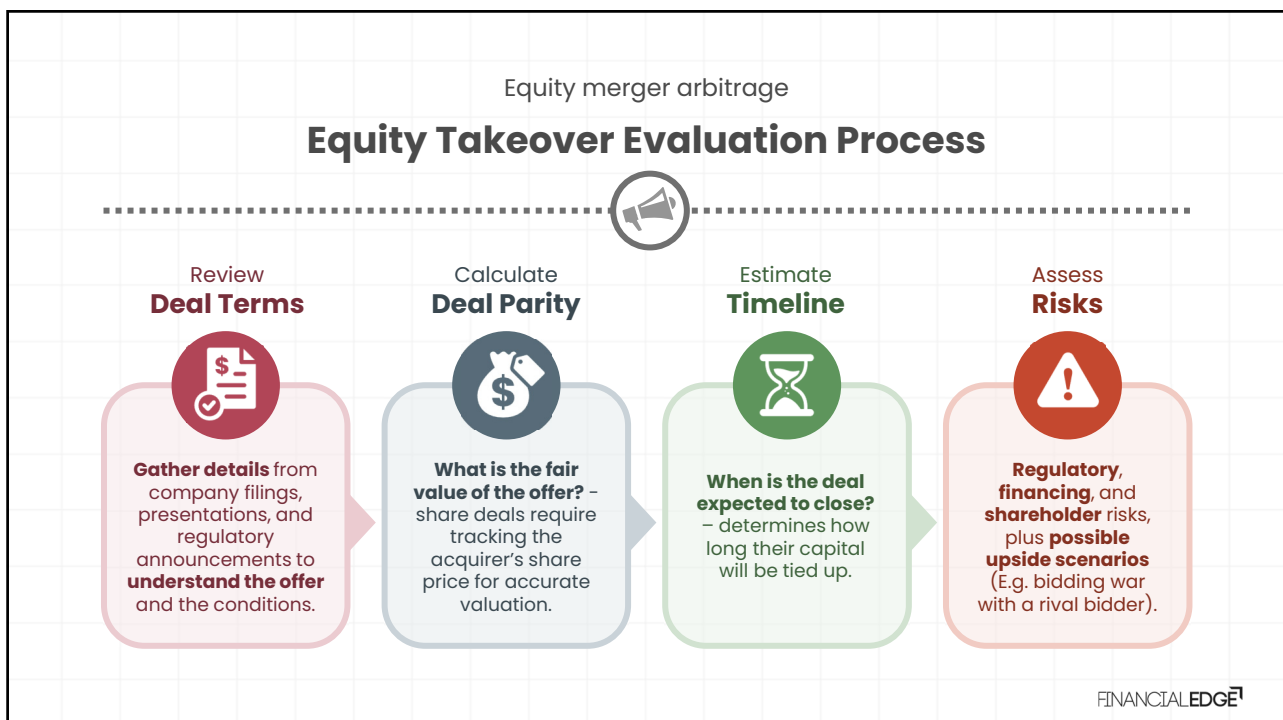
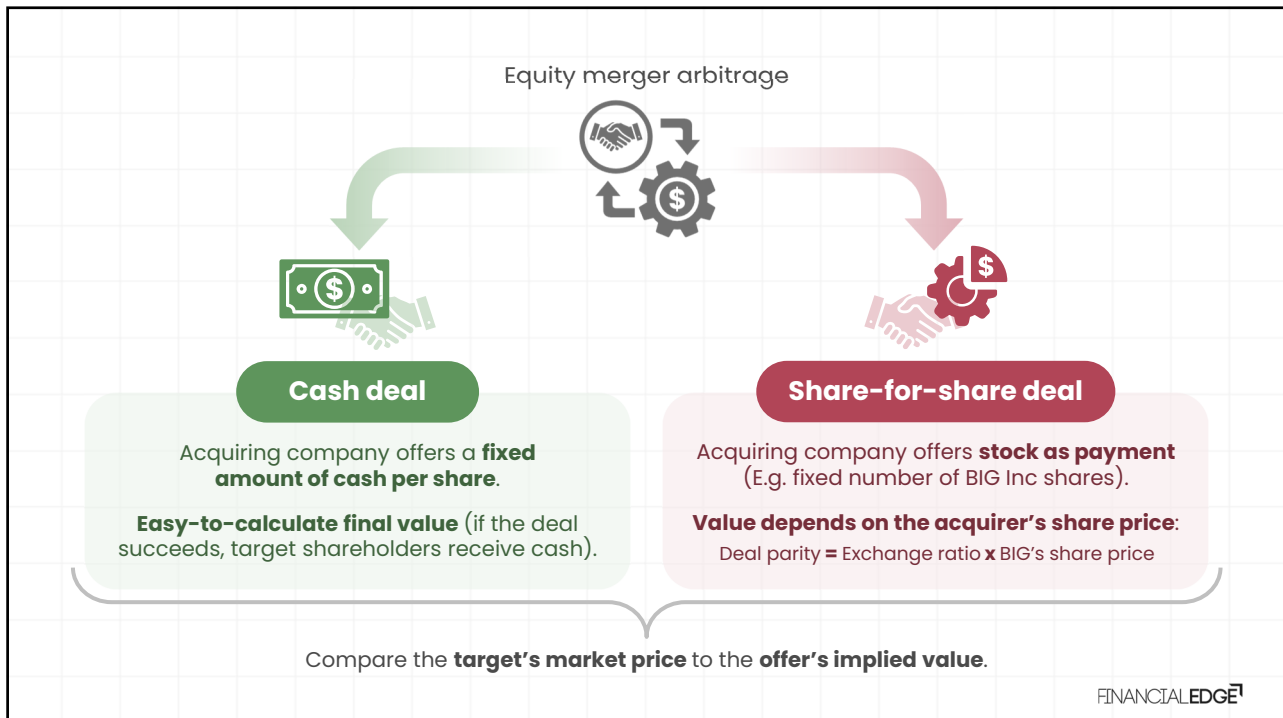
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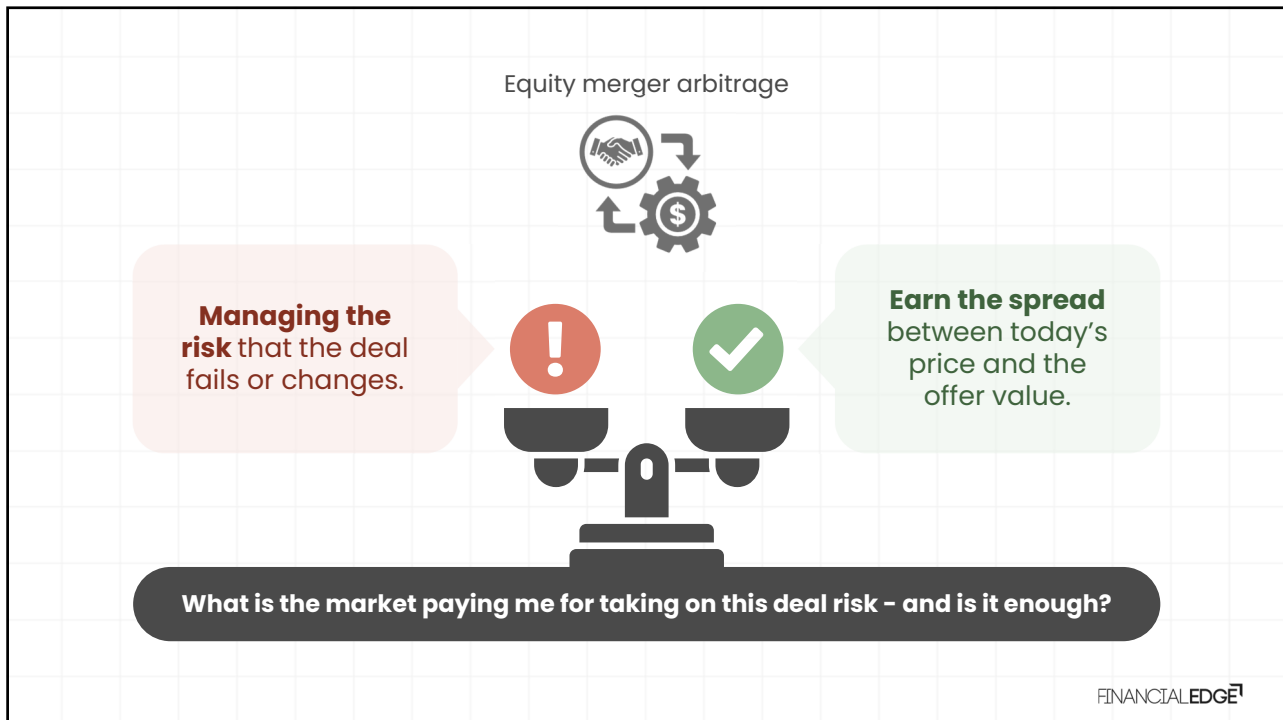




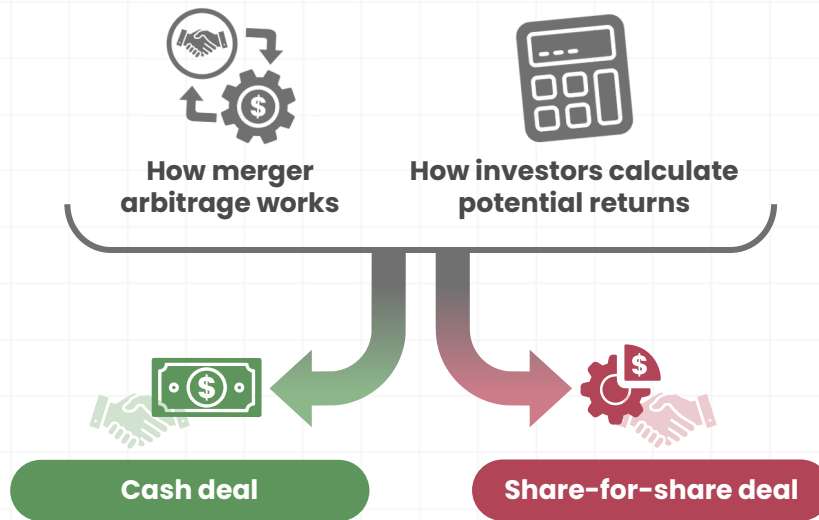


Equity Merger Arbitrage – Cash Deals and Share Deals





Equity Merger Arbitrage – Rate of Return on Cash Deals



Assumes the deal goes through

BIG announces it will **acquire SML** for **\$145 per share**

SML shares trade at **\$140**, and timeline is **180 days**

\$5 deal spread (potential profit for an arbitrageur)

Gross return: $(145 - 140) \div 140 = 3.57\%$

Convert 180 days to years: $180 \div 365 = 0.493$

Annualized rate of return (RoR): $3.57\% \div 0.493 = 7.2\%$

	A	B	C
1	Deal terms	\$145	Cash
2	Current SML US share price	\$140	USD
3	Discount (USD)	\$5	=B1-B2
4	Return (%)	3.57%	=B3/B2
5	Time to completion (years)	0.49315	=180/365
6	Annualized RoR	7.24%	=B4/B5

If the merger fails, SML's shares could fall back toward pre-announcement level (significant loss).

"Risk arbitrage"



Share-for-share deal

BIG offers 0.453 of shares for each of SML's shares

BIG current market price: \$320.09

Deal parity: $0.453 \times 320.09 = \$145.0$

SML shares trade at \$140

Deal spread: $145 - 140 = \$5$

Gross return: $5 \div 140 = 3.57\%$

Annualized rate of return (RoR):
 $3.57\% \div 0.493 = 7.2\%$

	A	B	C
1	Deal terms	0.453	Shares of BIG US
2	Current BIG US share price	\$320.09	USD
3	Current deal value	\$145.0	=B1*B2
4	Current SML US share price	\$140	USD
5	Discount (USD)	\$5.0	=B3-B4
6	Return (%)	3.57%	=B5/B4
7	Time to completion (years)	0.49315	=180/365
8	Annualized RoR	7.24%	=B6/B7

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Share-for-share deal

	A	B	C
1	Deal terms	0.453	Shares of BIG US
2	Current BIG US share price	\$320.09	USD
3	Current deal value	\$145.0	=B1*B2
4	Current SML US share price	\$140	USD
5	Discount (USD)	\$5.0	=B3-B4
6	Return (%)	3.57%	=B5/B4
7	Time to completion (years)	0.49315	=180/365
8	Annualized RoR	7.24%	=B6/B7



Offer value depends on BIG's fluctuating share price.

Hedge to Lock-in the spread value

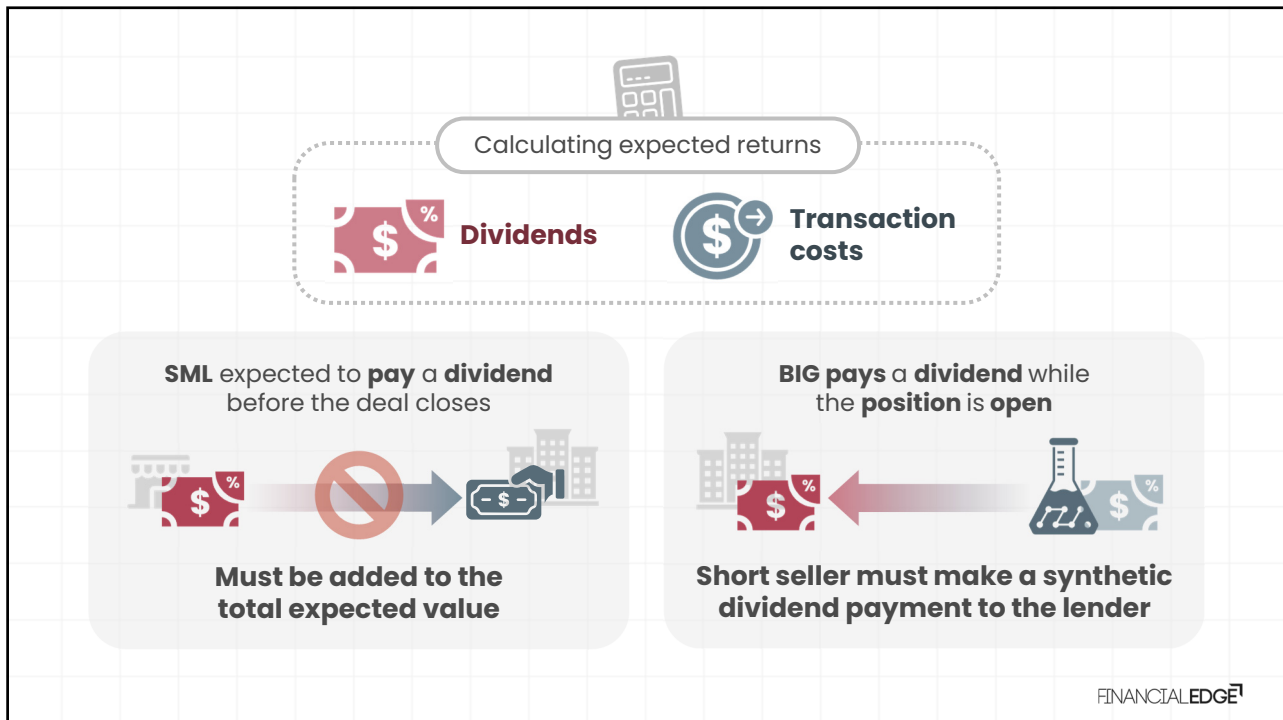
Buy 100,000 of SML's shares

100,000 x 0.453

Short-sell 45,300 of BIG's shares

Market-neutral position

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