BUYING, SELLING AND SHORTING UK & EUROPEAN EQUITY

Has there been a post-Brexit sell-off of the UK?

Yes, and it accelerated in August: all investor regions are still actively selling UK stocks as they were in July. In percentage terms, domestic UK sales have remained consistent at around -3%, North American sales of the UK have risen sharply from -1.2% to -2.1%, along with Western European sales increasing from -3% to -4.2% and Rest of World sales nearly doubling from under -4% to -7%.

What are they selling?

Most sold sectors were consumer services, down 4.7% followed by basic materials -3.9% and industrials -3.8% followed by consumer goods -3.4%, technology -3% and financials -2.9%. The least sold sectors in Q3 have been energy and healthcare, both at 0.9% down, and utilities at 1.6% off.

Has there been a post-Brexit sell-off of Europe?

The Bank of America Merrill Lynch September survey indicates that irrespective of what the vote means for the UK, the knock-on effect of Brexit is directly on Europe: post-Brexit disequilibrium within the European Community is cited as the top global concern among investors.

"Europe must realize that Italy poses the biggest risks from an economic, financial and political standpoint. Post-Brexit polls show an alarming rise in anti-European sentiment in Italy. Therefore, if Europe wants to avoid another wave of political uncertainty and rising unemployment, it must address Italian banks, maintain the positive credit impulse and deliver more economic growth. Our investment process leads us to maintain an underweight position to European equities and the euro."
Alessio de Longis, portfolio manager & macro strategist at OppenheimerFunds, Q3 2016

The answer is no - but Europe is not seeing inflows. Historically net change is at very low levels, supporting all the other points noted by BoAML, namely that cash is king & any notion of a rush for opportunity (notably value) is not backed by the evidence. Comparison of UK and western European fund flows indicates two substantial differences, one relating to style:
- UK selling is 50% growth driven, 25% value driven, GARP 8.4%, alternative 5%, index 4%
- WEU selling has just two drivers, **growth** and **index**, but completely unlike the UK has significant value **inflows**; suggesting that issuers have to focus on value funds for easier inflows while selling a growth story is a much harder task in Europe as in the UK. It's also made more difficult by recent world trade figures suggesting that growth rates in both the US and China are now slowing substantially.

"A seemingly cruel irony of Brexit is that having retained its own currency, strain in the UK can be partially relieved through a weaker pound boosting exports and the translated overseas earnings of UK companies. No such relief valve exists for individual members of the Eurozone and this ties into our second concern – that Brexit precipitates a return to crisis in the Eurozone periphery."
Alessio de Longis, portfolio manager & macro strategist at OppenheimerFunds, Q3 2016

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Issuers can and should distinguish between investors in each major investor region who are selling both the UK and Continental Europe, and those selling the former and buying the latter.

- UK institutions have sold $21.4B of UK stocks making up 55% of total sales of the UK market. Of that $21.4B, half is made of investors selling Europe as well as the UK, led by **Henderson, Columbia Threadneedle, Aviva UK** and **Fidelity International Ltd.** A small subset of UK firms have been selling the UK market and buying Europe. Led by index investor **BlackRock Investment Management UK,** along with **Morgan Stanley Investment Management UK** and **Newton Investment Management**, they are not numerous and the scale of their selling of the UK dwarfs their buying of Europe - but they are buying there.

North American investors in the UK are divided into two principal groups:

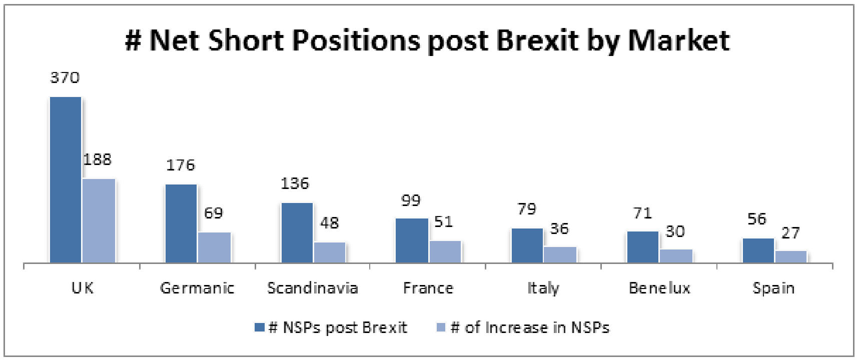
- ✓ Those across all major investment styles selling UK and buying Western Europe, led by growth investors Fidelity Management & Research, Morgan Stanley Investment Management, and Jennison Associates, GARP investor **Manulife Asset Management** and value investors **Lazard Asset Management**, **AllianceBernstein** and MFS Investment Management
- ✓ Those just selling UK (notably **Capital World Investors**, **Capital Research Global Investors**), no European activity filed as yet in Q3 - although Capital Group was a significant buyer of Western Europe in Q2 reversing long-term trend
- ✓ Western European investors also divide into the two main groups - one selling UK equities, buying Continental European, the other selling both. **Deutsche Bank** said before Brexit that the UK offered more opportunities than mainland Europe. What have German investors done since?

Deutsche Asset Management Investment is a top UK seller, Western Europe buyer. At firm level Deutsche is buying mainly in France and Germany - **BMW, Siemens, Danone**, has bought back into **Air France-KLM** (shorted heavily pre-Brexit and fell sharply in price post-Brexit), **Technip** and **Infineon** – along with selected other mega-caps (**Unilever, Roche**) and selling in Europe (top domestic sales **Stada Arzneimittel, Wirecard, BASF, Heidelbergcement, freenet)** and in the UK **(BAT, Sky, Prudential**).
Other major sellers of UK, buyers of Western Europe include **Handelsbanken Asset Management, Deka Investment, Pictet Asset Management** and **UBS AG (Asset Management Switzerland)**.

- This is in distinction to Western European investors selling both markets, UK and European – a list headed by **Nordea Investment Management** and including major French investors **Société Générale Gestion**, **BNP Paribas Asset Management and Edmond de Rothschild Asset Management**.

BUYING, SELLING AND SHORTING UK & EUROPEAN EQUITY

What, if any, correlation is there between selling and shorting?



Just two markets have seen the **increase** in net short positions (NSPs) make up more than half of shorting positions declared since 24th June, the UK (51.8%) and France (51.5%) Germanics and Scandinavia have seen the least increases in declared NSPs with 39.2% and 35.3% respectively.

Most shorted sectors in Europe since 24th June have been consumer services, industrials and financials. Sectors seeing highest increase in net short positions are financials (53% of all shorts declared in the sector have been increases), consumer goods (49%) and consumer services (45%). Least shorted sectors in Europe with the lowest rate of increase in NSPs have been utilities, healthcare and energy.

Most sold sectors in Q3 in Europe have been **financials** (heavily driven by sales of **Deutsche Boerse** and to a lesser extent **ING Groep**, neither of which has been shorted) healthcare and energy. In Q2 financials saw net buying, healthcare was the 2nd most stock after industrials, so it retains its position (but industrials move from negative in Q2 to flat in Q3) and energy was positive with the substantial exception of **Royal Dutch Shell** (which saw massive selling).

Italian financials, seen as the weakest component of the European financial system, and recognisable as such as the core of shorting of the financials sector across Europe, have seen net buying, with purchases of **Intesa Sanpaolo** and **FinecoBank** exceeding sales of **UniCredit** and **Assicurazioni Generali**. Spanish financials were driven by heavy buying of **Banco Santander**.

Healthcare saw continued selling of **Bayer** and **Fresenius**, heavily sold in Q2, along with sales of Scandinavian pharma stocks **Novo Nordisk** and **Meda** (shorted but seeing its shorting decrease since 24th June). **Roche** has switched from being net bought in Q2 to being sold in Q3 but seen no shorting activity.

Consumer goods has seen **Daimler** move from bought (in Q2) to sold, along with **Renault** and **Peugeot** (which has seen one shorted position increase slightly since 24th June), where **BMW** is being bought and in luxury goods **LVMH** has seen buying in Q3. Consumer services saw big buying of merger stock **Ahold Delhaize** (shorting unchanged since 24th June) along with Germany's **ProSiebenSat**.

In the UK the largest number of short positions, by far, have been declared in consumer services and industrials, with basic materials, energy and consumer services seeing the most increases. This is in direct correlation with the most sold sectors in Q3 - consumer services down 4.7% followed by basic materials -3.9% and industrials -3.8% - and the least sold sectors, energy and healthcare, both at 0.9% down, and utilities at 1.6% off have seen fewest shorts (along with basic materials and consumer goods).