European Securities and Markets Authority

Date: 03 June 2013
ESMA/2013/649

PRESS RELEASE

ESMA publishes review on impact of short selling regulation

The European Securities and Markets Authority has published its *Technical Advice* evaluating the impact of the *Regulation on short selling and certain aspects of credit default swaps* (Regulation) on European financial markets.

ESMA has prepared this in response to a European Commission request for Technical Advice to inform its report to the European Parliament and Council on the impact of the Regulation, due by end of June 2013.

The advice was requested only a short time after the implementation of the Regulation on 1 November 2012 and so there were limits to the market data available, and limited regulatory experience in supervising the Regulation's requirements to draw on. The report makes a number of recommendations that would help to improve how the Regulation works in practice, with the overall recommendation that the regime be re-assessed at a future date when more data and experience have been accumulated.

ESMA was asked to report on the observable effects of the Regulation and carried out an analysis on:

- the market impact of the transparency requirements, restrictions on uncovered short selling and uncovered sovereign CDS and of any temporary measures restricting short selling; and
- whether the current provisions of the Regulation and their application are fulfilling the needs of market participants in terms of transparency and the needs of the regulators to perform their supervisory functions.

Steven Maijoor, ESMA Chair, said:

> "ESMA's review has found that the introduction of the Short Selling Regulation has had some positive effects in terms of enhancing market transparency and reducing risks of settlement fails in EU financial markets.

"Due to the short period of operation of the Regulation, ESMA was subject to severe limitations in terms of available data and practical experience in supervision under the Regulation. However, ESMA is advising the European Commission to consider adjusting a number of aspects in the Regulation that do not alter its main elements."

Impact of the Regulation on market conditions

Notwithstanding the review's limitations in terms of data and timespan, its key findings were that:

- there were mixed effects on liquidity of EU stocks, with a slight decline in volatility, a decrease in bid-ask spreads and no significant impact on traded volumes. Price discovery speed seems to have decreased compared to the period before the entry into force of the Regulation;
- overall, settlement discipline has improved; and
- no compelling impact on the liquidity of EU single name CDS and on the related sovereign bonds markets could be noticed (except in a few countries). The liquidity in European sovereign CDS indices has been somewhat reduced.

ESMA recommendations

The technical advice key recommendations relate to the following areas:

- Transparency and reporting requirements:
  - ESMA considers that the current reporting and disclosure thresholds are appropriate and only suggests considering some technical improvements in the method for calculating net short positions in shares; and
  - ESMA mainly recommends to revisit the method of calculation of net short positions in sovereign debt, particularly the duration-adjusted approach, and to review the thresholds for notifications.

- Restrictions on uncovered short sales in shares and sovereign debt:
  - ESMA recommends considering some adjustments to the regime to allow internal locate arrangements within the same legal entity;
  - ESMA also suggests revisiting the issue of the definition of "liquid shares" for the purpose of locate arrangements at a later stage, when proper regulatory data on securities lending would be available.

- Ban on uncovered sovereign CDS transactions:
    - ESMA suggests that higher legal certainty could be pursued by clarifying wording in the legal text (e.g. on the correlation test) and that refinements to the detailed provisions could be envisaged:
        - use of sovereign CDS indices for hedging purposes;
        - cross-border hedging under certain liquidity and correlation circumstances; and
        - group hedging by a particular and dedicated entity.

- Shares exempted from the Regulation on the basis of turnover calculations:
    - ESMA suggests an alternative approach to draw up this list.

- Regarding the exemption for market making activities, further clarifications are needed and changes to the Level 1 text may be worth considering, including:
    - the scope of the exemption and the conditions for being able to make use of the exemptions, particularly the trading venue membership requirement; and
    - ESMA suggests to consider a change in the instrument per instrument approach for the purpose of notifications and not to apply the 30 day period for objecting to use of the exemption to newly admitted instruments.

- Emergency measures in case of a significant fall in price:
    - ESMA considers that the approach for introducing such temporary bans should be reconsidered with the view to simplify the regime and ensure more consistency in their application.

Notes for editors

1. ESMA is an independent EU Authority that was established on 1 January 2011 and works closely with the other European Supervisory Authorities responsible for banking (EBA), and insurance and occupational pensions (EIOPA), and the European Systemic Risk Board (ESRB).

2. ESMA's mission is to enhance the protection of investors and promote stable and well-functioning financial markets in the European Union (EU). As an independent institution, ESMA achieves this aim by building a single rule book for EU financial markets and ensuring its consistent application across the EU. ESMA contributes to the regulation of financial services firms with a pan-European reach, either through direct supervision or through the active co-ordination of national supervisory activity.

Further information:

David Cliffe
Senior Communications Officer
Tel: +33 (0)1 58 36 43 24
Mob: +33 6 42 48 29 06
Email: david.cliffe@esma.europa.eu

Reemt Seibel
Communications Officer
Tel: +33 (0)1 58 36 4272
Mob: +33 6 42 48 55 29
Email: reemt.seibel@esma.europa.eu