



Haircut Snippets

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The Files, They are a- Changing...

Len Bole

For the second time in the brief history of Snippets, the OCC grabs page one headlines.

Some time later this year, probably fourth quarter, the hallowed formats of BOTH the Risk Based Haircut (RBH) position and PL files will change. That means that RBH and the Basket Weaver™ will have to be updated in order to continue to function.

If you are on the OCC RBH mailing list, you have already received (or will shortly receive) an announcement regarding the changes.

Strike price will now become a pure decimal and it will no longer be necessary to decide if a strike price should be presented after multiplying by 10 or if the fraction should be shown in eighths or decimals. All strikes will represent the true, economic strike.

It will now be necessary to identify options on futures with a security type of 'F'. This will eliminate the possibility, however remote, of confusing options on futures (like SP, DJ, R) with options on stocks (SP = Specialty Labs, DJ= Dow Jones, R = Ryder).

The Market Maker indicator, which historically has had values of Y, N or blank, will now only accept C, F and M for customer, firm and market maker. This is in preparation for Risk Based Margining.

The PL file will now contain a Position Percentage field. This field will be used to allocate PL numbers for a single option to multiple classes. Spin-offs and reorganizations require a change like

this. The implementation of this new feature should result in lower haircut charges for pre- and post-corporate action options.

The P records for baskets will now also contain the minimum hedge percentage for the baskets. RBH will grab the percentage from these records and update existing records in the Minimum Hedge file automatically.

When the dates for implementation are announced, I will contact users and let them know when version 5.0 of RBH and version 5.0 of the Basket Weaver™ will be available.

Fixed Income V. 2.5

The latest version of fixed income haircuts, version 2.5, is now available. Here are the enhanced features:

Groups and Selected Accounts

Many users feed their inventory to the system by trader, putting each trader's positions in a separate haircut Account. Previous versions would haircut each account and the combined firm.

Version 2.5 will allow users to maintain account groupings, assigning Accounts to one or more groups to get haircuts by desk, portfolio, supervisor, whatever.

In addition, rather than running for all accounts at once, the user may select one or more accounts in a mini-haircut run.

Unattended Batch Run

Like its cousins, RBH and Option Margin Optimizer, the fixed income system will now be capable of running in unattended batch mode.

In batch, the system can be launched and left unattended. It will scan for the existence of a semaphore file and, when it finds the file, will import and haircut positions according to INI file settings.

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The system is capable of launching a user-defined application upon completion and will either go back to sleep, waiting for another semaphore file, or exit.

Some people may prefer to have their positions downloaded during off-hours and to have the system run without having personnel involved in hitting the buttons.

Basket Weaver™ 5.0

Version 5.0 of the Basket Weaver™ will handle the position and PL file format changes discussed in the lead article of this newsletter.

In addition, it will include the Exchange Traded Fund (ETF) logic discussed in the last issue of Snippets. At the risk of being repetitive, here's what that's all about:

ETFs

Exchange Traded Funds (ETFs) have become increasingly popular as an investment and hedging tool. Examples of these products include Spiders, Diamonds, Qubes, Holders and iShares.

These products may be **created** by converting a basket of stocks into an ETF or **redeemed** for a basket of stocks. Fees and the payment/receipt of cash are involved.

It would appear that an ETF and a basket are securities that are "exchangeable for or convertible into the underlying security within a period of 90 days."

Version 5.0 of the Basket Weaver™ will now analyze positions and perform the creation and redemption of ETFs, computing the appropriate fees, cash payments and any loss on conversion.

The system requires the Domestic Portfolio file from NSCC. The minimum size for creation and redemption, the exact shares of stock required for creation/redemption and the amount of cash involved are gleaned from this file.

The system demands that all components of the long basket are available in proper quantities and that the user is short the ETF before doing a Creation. By the same token, the system demands that the user be long the ETF and short all components of the basket in proper quantities before doing the Redemption.

These strategies may result in significant haircut savings.

Option Margin Optimizer

As the Option Margin Optimizer (OMO) approaches its first birthday, a number of firms have licensed the software and others are preparing data to see first hand how the system can lower maintenance margin requirements.

OMO calculates customer margin charges according to NYSE Rule 431, as revised in January 2000. The charges calculated are often the **LOWEST** allowable by the rule for a given option position. The system will calculate charges for all the newly allowed spreads including reversals, conversions, collars, boxes, butterflies and hedges.

Please contact me if you would like to test-drive the system.

OCC RBH Mailing List

If you are involved with RBH, I think it is imperative that you be on the OCC's mailing list. This will assure that you are notified of changes such as the file formatting discussed in the page one article. In addition, you will be notified of new and changed basket IDs, a partial list of which is contained below.

To be added to the list, please contact Denise Sikorski. Her email address is dsikorski@theocc.com.

The following Basket IDs should be added to the **Minimum Hedge File**. At the moment those marked with an * require 50% capitalization; the others

require 95%. Check with the OCC for proper requirements.

- *10501 Fortune e-50 iShare
- *1DSV DJ US Small Cap Value
- *1ELG DJ US Large Cap Growth
- *1FFF Fortune 500 Index Fund
- 1IBB NASDAQ Biotech iShare
- *1IJK S&P400 MidCap Growth
- *1IWN Russell 2000 Value iShare
- *1IWO Russell 2000 Growth iShare
- *1MKH Market 2000 Holder
- 1OIH Oil Service Holder
- 1SWH Software Holder
- 1WMH Wireless Holder

Basket Changes:

- 10501 was 1FEF
- 10502 was 1SMH
- 10503 was 1UTH
- 10504 was 1RKH

Deleted Baskets:

- 10109 MS Emerging Growth

Other ETFs have been added, but they have been added as part of another product group. As such, they do NOT require a separate entry in the Minimum Hedge file.

- MII MS Internet iShare
- MTK streetTracks MS High tech
- OEF S&P 100 iShare

Electronic Newsletter

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