Haircut Snippets

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The First of…

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Give a guy a new NT computer and new tools like Microsoft Word, and who knows what he may generate? After years of working with WordStar (yes, I do have Luddite qualities), I have come roaring into the 20th century. And not a moment too soon.

Welcome to the first of what I plan to be an occasional newsletter intended to share bits of information (snippets, if you will) regarding LDB Consulting products in general and Risk Based Haircuts in particular.

Special Data File

The Special Data File in RBH is a dynamic file which requires the user to maintain specific information regarding options and futures, such as the shares per contract (multiplier or SPC) and mini leap divisor (MINI). These items are used to determine how many baskets may be hedged by a security and to generate a proper market value to assist in balancing between RBH and your back office system.

OEX Leaps and SP

Occasionally, products change their specifications. This was true late last year when the Merc split the S&P 500 future contract by halving its multiplier. A few weeks later, the CBOE split the OEX (S&P 100) contract in half, but did NOT split the specifications on the OEX leaps (OAX, OBX, OCX and OQX).

In the special data file, these changes required that the SPC entry for SP (S&P500 future) contain 250. The entries for the OEX leaps should now have 5 rather than 10 for mini leap divisor, since these strikes did NOT split.

DJX and DJ

DJX and DJ are derivative securities on the Dow Jones Industrial Average. The DJ should have SPC = 10 and Mini = 1. The DJX should have SPC = 100 and Mini Leap Divisor = 100. THESE VALUES ARE PROPER IF YOUR BASKET COMPOSITION FILE SHOWS THE PRICE OF THE DOW TO BE 8400 RATHER THAN 84.

Some clients prefer to show the price of the Dow as 84, corresponding to the underlying on the CBOE cash options (DJX). If you do this, set DJX SPC = 100 and DJX Mini = 1. Set DJ SPC = 1000 and DJ Mini = 1. This will properly allow for hedging, but will exaggerate the market value of DJ futures products by a factor of 100.

SPY, MDY and DIA

The AMEX trades depository receipts on the S&P 500 (SPY)and the S&P Midcap 400 (MDY), as well as Diamonds on the DOW (DIA). All of these securities can hedge baskets. They should all have SPC = 1. For SPY, MDY and DIA, set Mini = 10, 5 and 100, respectively. If, however, your composition file lists the price of the Dow at 84 rather than 8400, set Mini = 1 for DIA. See the discussion above regarding DJX index pricing.

Positions in SPY, MDY and DIA must be entered with a security type = F, denoting a future. This is a requirement to match against the OCC P/L file.

Cautionary Note

It is incumbent upon you, the user, to verify the accuracy of these suggestions and to remain current with new product information and product modifications. To the best of my knowledge, there is no service in place which provides notification of these changes. Rather, firms must respond to them when traders open positions in new or altered securities. I hear of many new products as clients consult with me regarding proper settings. I am happy to serve as a clearing house for this information, but I cannot guarantee that I will be up to date or that the data I have is accurate.

Warrants

A SEC interpretation states that listed warrants must be haircut in the same manner as listed options. Until now, warrants did not appear in the OCC P/L file. However, the OCC is testing warrants and hopes to introduce them in the P/L file in the near future. Apparently, a warrant will appear as a call option with an expiration date and strike price. The symbol will be the underlying stock symbol plus WS.

OCC is looking to include all listed warrants. Failing that, they will accept requests from firms for inclusion of specific warrants. If you would like me to notify you when I officially hear about the introduction of warrants, please email me at my address below.

New & Enhanced Products

Version 3.0

Version 3.0 has been the current version of RBH since March of 1998. It includes a number of new features:

1)computing convertible security haircuts;
2)generating the NYSE mandated OCC format position file;
3)displaying security counts and market values (long and short) by class, account and firm;
4)automatic alteration of those strikes which OCC demands to be multiplied by 10;
5)exporting of report files to delimited or column oriented files.

Basket Weaver

The Basket Weaver takes all of an account's positions, nets them and then determines which, if any, baskets can be constructed from and hedged with the remaining securities. This effectively keeps an account from incurring minimum charges on offsetting long and short positions in securities which are part of multiple baskets. Remnant holdings are put into baskets to allow the favorable treatment afforded basket stock as opposed to naked stock.

Fixed Income Securities

LDB Consulting, Inc has developed a fixed income haircut system. It accepts positions in government bonds, corporate bonds and Treasury futures and seeks to pair securities in a manner which produces lower haircut charges. Government securities are paired with other government bonds, corporate bonds with other corporate bonds and government bonds are further paired with corporate bonds in accordance with the 15c3-1 paragraphs having to do with government and corporate debt securities.

For further information

Please contact me if you would like more information regarding any of these new and enhanced products.

From You I Need:

I'd like to know if you are the person who should receive future copies of this newsletter. Also, are there others in your organization you would like me to add to the mailing list? Covering both sides of the street, if you would like to be removed from the mailing list, please let me know that as well.

The next planned upgrade for RBH is intended to be a 32 bit version. If you are a client, are you using a 32 bit operating system (Windows 95, Windows 98, Windows NT)? If not, do you plan on migrating in the future? When?.

What is your email address? Mine is LDB-LENBOLE@worldnet.att.net Would you prefer to receive this newsletter via email?

I'd also like to solicit ideas and suggestions for RBH. All the version 3.0 features listed above were the result of feedback from users.

Please feel free to respond by US Mail to the address above; via email to my email address; or by phone to (708)-672-7756. Thanks!