

VW spike forces Dax rule changes

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Rules for Germany's stock indices are to be rewritten after tumultuous trading in Volkswagen shares last month caused turmoil in equity markets.

However, the changes -the second set of alterations to come in the wake of the VW share price spike caused by a short-selling squeeze -are set to do little to address the use of the options that were instrumental in the VW case.

Deutsche Borse, the operator of the Frankfurt stock exchange, will from next month only include companies in its main indices if their "free float" - the proportion of their shares not in the hands of big strategic shareholders and thus available to trade - is at least 10 per cent. The free float requirement at the moment is 5 per cent.

The rules will apply to the Dax set of indices including the Dax-30, Germany's benchmark blue-chip index.

Deutsche Borse called the change "a key step towards ensuring liquidity in the indices. The higher a company's free float, the higher the tradability of the share in most cases," it said.

The free float calculation will take into account any options acquired by a company - for example, during a takeover - over an index member's shares.

But this excludes so-called "cash-settled" options, where a company agrees an option with the owner of a stock to acquire the value of the share, rather than the share itself. It was Porsche's revelation that it had acquired a large number of cash-settled options in VW ordinary shares, over and above its known VW stake, that triggered the extremely volatile trading in VW shares.

In effect, the free float of VW was reduced well below 10 per cent. Hedge funds scrambled to buy VW shares to unwind trades, causing the shares to rise so sharply that they distorted the overall Dax-30. Index tracking funds also had to try to acquire VW shares and sell other stocks.

Henning Gebhardt, head of German equities at DWS, the country's biggest fund manager, said: "These measures from Deutsche Börse are welcome but they only go so far and they are missing the point regarding cash-settled options, as used in the VW case. At the end of the day what is needed here is a change in the law that will make the use of such options transparent. "The Borse is doing what it can but its hands are tied in terms of the 'action it can take. More needs to be done at the government level to solve what has been a big problem for the German stock market and German companies."

Last month Deutsche Börse also introduced rules that would see companies excluded from the Dax if trading was excessively volatile and if their index weighting rose above 10 per cent. The change was viewed as a potential way of excluding VW's ordinary shares but no index change was made as VW's index weighting fell.

The free float changes may affect five companies now listed in Various Dax indices, including Continental, the car parts supplier. The company is in any case due to be acquired by Schaeffler, a rival, in a deal that was also shaped by Schaeffler's use of cash-settled options.

Fonte: Financial Times, London, November 25 2008, Companies & Markets, p. 25.