

## FSC ANNOUNCES DECISION ON SHORT-SELLING BAN

FSC Chairman Eun Sung-soo held a press briefing on February 3 and announced the decision to extend the short-selling ban until May 2, 2021 and to allow a partial resumption of short-selling from May 3 on KOSPI 200 and KOSDAQ 150 stocks.<sup>1</sup>

### **SUMMARY OF CHAIRMAN'S REMARKS**

**(FSC'S DECISION)** The FSC has decided to extend the current short-selling ban until May 2 this year and allow a partial resumption from May 3 on KOSPI 200 and KOSDAQ 150 stocks. The partial resumption is intended to minimize the impact on markets, given these stocks have large market caps and liquidity so that the resumption of short-selling would have limited impact on stock prices.

Meanwhile, the short-selling ban will remain on the rest of stocks (2,037 stock items) with further decisions on the resumption of short-selling on these stocks to be made later based on market conditions.

The resumption date of May 3 has been decided to give the Korea Exchange (KRX) some time for system development and testing.

With the revised Financial Investment Services and Capital Markets Act scheduled to go into effect on April 6 this year, with stronger penalty rules for illegal short-selling activities, there will be no issue of a legislative gap.

Today, the FSC commissioners raised the same voice on the need to improve the short-selling system as there are investor demands for more transparency and fairness in the short-selling system.

**(IMPROVING THE SHORT-SELLING SYSTEM)** Prior to the May 3 partial resumption, the FSC will work on measures to improve the short-selling rules. First, The FSC will work to ensure the detection of and punishment on illegal short-selling activities. With the revised Financial Investment Services and Capital Markets Act, short-sellers will be required to keep their securities lending data for five years and the securities firms will be required to tighten monitoring of illegal short-selling activities. The securities firms are currently in the process of getting their systems ready according to the schedule. The KRX will also strengthen its oversight function. Within this month, a special team tasked with monitoring illegal short-selling activities will be launched and the monitoring period for naked short-selling will be reduced from once every six months to every month. The authorities will operate a real-time monitoring system to

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<sup>1</sup> KOSPI 200 makes up 22% of a total of 917 stock items and KOSDAQ 150 makes up 10% of a total of 1470 stock items.

be able to detect suspicious activities and take immediate actions. The penalties have also been strengthened on illegal short-selling—a fine of up to the amount of the maximum short orders and one year or more of imprisonment.

Second, the authorities are seeking improvements to the market maker rules to prevent market abuse. Market makers will be prohibited from short-selling mini-KOSPI 200 futures and options (*when acting in their capacity as market makers*)<sup>2</sup> and their market making function will be restricted on high-liquidity items to cut their short-selling volume to more than a half of the current level. Market makers will be subject to more stringent disclosure rules to help improve transparency. As the KRX has been working on rules change and setting up the system, the changed market maker rules will go into effect starting on March 16.

Third, the authorities will work to address the issue of discrepancy in terms of access to short-selling by institutional and retail investors. In effect, retail investors have been given less opportunities in the short-selling market compared to institutional and foreign investors due to the high risk involved in securities lending. In this regard, securities firms have been reluctant to lend stocks to individual investors. As such, the FSC in consultation with the Korea Financial Investment Association has decided to expand the securities lending system to retail investors upon which securities finance companies will assume the payment burden. On May 3, it is expected that about KRW2 trillion to KRW3 trillion in securities lending will become available. Through close cooperation with diverse institutions, more stocks will be available for lending in the future. In order to promote active participation from securities firms, the authorities will work to improve rules on credit exposure which is currently set at 100 percent of their equity capital. To this end, the authorities will work to improve the system so that credit exposure limits do not constrain their securities lending services.

There are also concerns about the risks of granting more short-selling opportunities to retail investors. In this regard, a balanced approach is needed between the retail investors' demand for more opportunities and ensuring investor protection. To this end, the FSC will gradually allow retail investors to engage in short-selling according to their individual experience and capabilities. First, all retail investors will be required to go through a pre-investment education program to become well aware about the risks and characteristics of short-selling, as well as a mock investment trial which showcases the real short-selling stages and process. In addition, there will be investment caps on retail investors to prevent excessive losses until they become more experienced. In this regard, the maximum short orders for beginners will be set at KRW30 million. For those with more than five times of short-selling investment experience over the recent two years with the cumulated amount of stock borrowing of KRW50 million or more, the cap will be set at KRW70 million. For professional investors or those with more than two years of short-selling experience, there will be no investment limit. These short-selling limits on retail investors can be adjusted depending on future circumstances and risk factors.

Prior to the resumption of short-selling, the FSC will work to improve the rules mentioned above while closely tracking the preparedness of different market

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<sup>2</sup> Italic added later for clarification.

participants. The FSC is currently operating a taskforce on improving the short-selling system. Its findings will be presented to the National Policy Committee of the National Assembly in February and April.

As there is growing public interest in the capital markets, the FSC will work to ensure that individual investors are making their investment decisions with trust in the market.

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