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VOLUME 4 No. 26 - 2007

SKY'S THE LIMIT

Are the Chinese capital markets finally taking off?

IRELAND - FUNDS MARKET
EUROPEAN MARKET REVIEW - CUSTODY FOCUS
PERFORMANCE MEASUREMENT - TECHNOLOGY
JIM BUCKLEY OF SCOTIA CAPITAL - CEO PROFILE

LEGAL ISSUES - MIFID MONTH
ANALYSE THIS - GLOBAL CUSTODY
PANEL DISCUSSION - LUXEMBOURG
PAYMENTS - TREASURY SERVICES

THE GLOBAL SECURITIES SERVICES INDUSTRY JOURNAL

INVESTOR SERVICES JOURNAL

VOL 4 No. 26 - 2007

Glad tidings?

Given that most of the market has been predicting a tough 2008, it may not be such a happy holiday for the financial services community this year. According to figures from UK consultancy the Centre for Economic and Business Research (CEBR), the City bonus pool is due to shrink by 16% to GBP7.4 billion this year and GBP6.2 billion in 2008. To make things worse, job security has become a serious issue – CEBR has forecast a 6,500 drop in the number of City jobs.

Obviously this is not limited to the UK – the US was hit hardest by the summer's sub-prime mortgage crisis and its effects rippled across the globe over the ensuing months. The market turmoil has so far claimed the jobs of three chief executive officers and prompted more than USD45 billion in writedowns at the world's biggest banks. In fact, a recent conference in Florida for the asset backed securities industry was dubbed the "survivor's conference" and the atmosphere described as "grim", as speaker after speaker explained why 2008 may be their worst year ever.

It has not been bad news for all parties, however – there have been those that have profited from the market downturn – I imagine the consultancy business is seeing a significant increase in business, for example.

The emerging markets have also weathered the storm. On this subject, our cover feature examines the potential that China represents for the global custody and asset servicing market. The sheer number of M&A and JV deals that have gone down in China over the course of this year are indicative of the appetite of both the global players to get into the lucrative domestic market and the Chinese players to diversify and gain reach into the global market. Access to a JV partner's experience is also likely to reduce the potential of costly mistakes as Chinese institutions begin to venture into foreign markets. Many of these can be used as "test beds" for best practices in risk management, investment management and corporate governance with a Chinese flavour. See page 14 for the full story.

As it is the end of the year, we thought it timely to provide a selection of forward looking features on the future of both European custody (see page 39) and the securities lending market (see page 52).

Our panel discussion this month looks at the Luxembourg fund services market and explores how the jurisdiction has defended its position as a funds domicile, given the rise of the new contenders such as Malta and Dubai. Turn to page 28 for the expert opinions.

All that remains for me to say is season's greetings and a prosperous new year.

Virginie O'Shea
Editor

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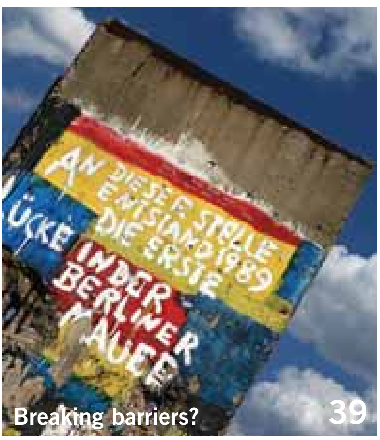

Breaking barriers?

Dublin or quits

The ISJ letter prize of a Cross writing instrument

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Winning Letter

Wanted: a new breed of manager

Clients are very cynical of the word innovation: it stands for the latest con trick, stated a well known UK pension fund we interviewed as part of our recent report (entitled "Convergence and Divergence: New forces shaping the investment universe") examining the investment management industry.

As institutional investors continue to demand hard asset products, like real estate, private equity and infrastructure, investment managers want to place more emphasis on those hedge fund strategies for which they can charge relatively high fees. The gulf between these sets of players could not be wider.

The expectation gap is largely led by the alternative investment industry, an industry that has successfully built a model around a management and performance fee structure, without any regard for the increasing complexity of trading strategies. Traditional long only managers can see an opportunity and are now fighting for their share.

A large part of inflows into alternatives has been made by long-only managers who have created in-house capacity to deliver new strategies in their original, or mimicked, form (for example, 130/30 strategies). The war for money continues and alternative investment managers would do well to take notes from the traditional industry. While clients chase returns and not assets, alternative investment managers will not only need to continue to deliver performance, but also minimise the risks their clients find hard to live with.

That the pool of alpha resides in the alternatives world is not in doubt; that there are no shortages of investment opportunities is not in doubt either. But this, in itself, will not ensure clients get the products they want. That requires processes that provide enhanced oversight of investments through standardisation, principal protection and independent reviews.

The future for the alternative industry remains bright and despite all that is written to the contrary, the era is now set for the rise of the structured product.

Anthony Cowell,
Financial Services audit partner
with KPMG in the
Cayman Islands

Client reporting concerns

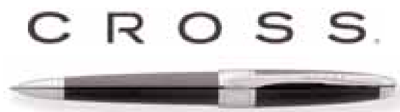
As a client retention tool and with a greater need for transparency, especially in light of new regulations such as MiFID, client reporting is at the top of the agenda. However, for some in the industry, outsourcing client reporting is for the most part, a no go area. It would be erroneous to conclude that outsourcing takes the process away from businesses, when outsourcing relieves this burden, by improving the overall reporting process so that firms can focus on their core competencies.

Companies have traditionally pieced together reports from multiple applications, faxing or posting them out to clients. Outsourcing can ensure timely delivery and eliminate manual processes. Yet, customisation of reports is certainly one of the main reasons why asset managers feel they cannot outsource to a third party. Outsourcing has the ability to create tailor made reports across a broad range of documents, rather than those produced in-house.

In order to take advantage of outsourcing, firms need to take a 'panoramic' view to determine what portions of their reporting process can be outsourced in order to retain the competitive edge. For that to happen, they must consider attitudes to, and the culture of, working with external partners.

It is wrong to dismiss outsourced reporting completely. It merits regular review and re-evaluation by senior executives. The case for collaborative outsourcing to deliver increased capability and results, demands that firms examine this question in more detail.

Abbey Shasore, managing director,
FactBook



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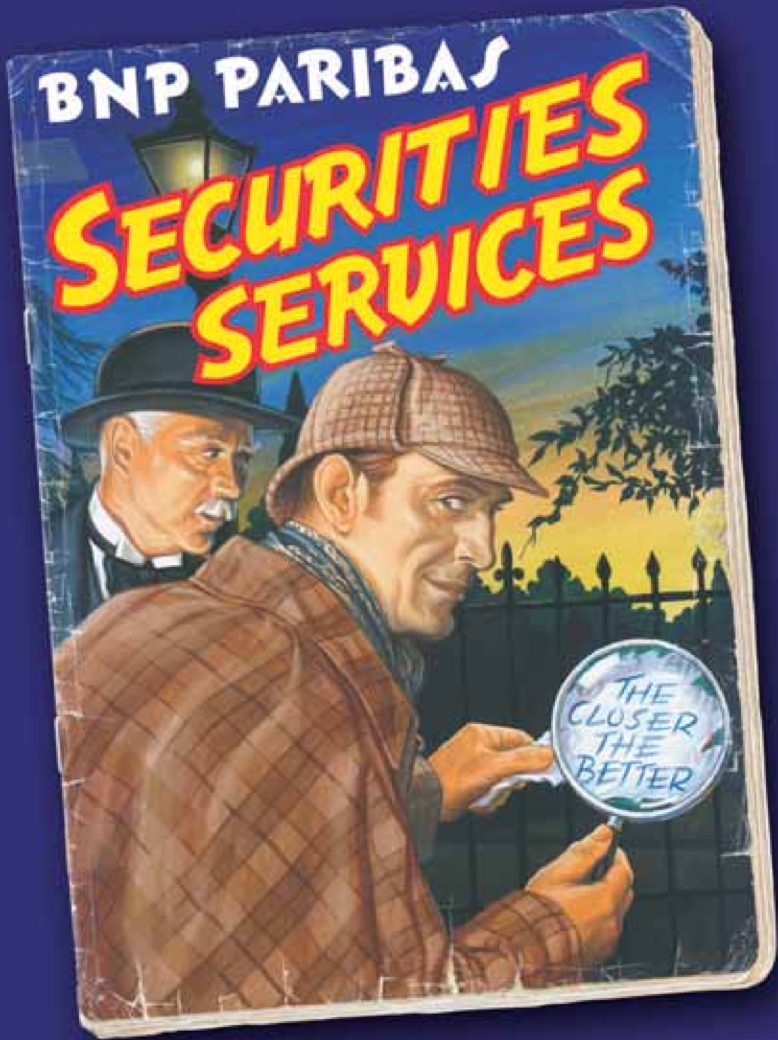
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News

CUSTODY, CLEARING AND SETTLEMENT

Casablanca - Citi Markets & Banking is to provide direct custody and clearing services to clients in Morocco, expanding Citi's proprietary direct custody and clearing network to 50 markets, the largest in the world. Andrew Gelb, global head of Direct Custody and Clearing for Citi's Global Transaction Services business, says: "Reaching 50 markets is a milestone for our direct custody and clearing business and a testament to Citi's unrivalled ability to support our clients as the globalisation of the capital markets inevitably continues. We are proud to provide our clients with a proprietary network that delivers a consistent high quality standard of service, technology and support in more markets than any other provider. The addition of Morocco showcases our commitment to expanding our network to meet the growing needs of our clients."

Paris - The American Depositary Receipt (ADR) programme of pharmaceutical company **Sanofi-aventis** has named **JPMorgan Worldwide Securities Services** depositary bank, succeeding the Bank of New York. The average daily trading volume of Sanofi-aventis ADRs is USD78 million year to date, with total ADR holdings in Sanofi-aventis exceeding USD9 billion at 30 October. Sanofi-aventis' ADR programme is the largest in France and is among the top 10 ADR programmes in Western Europe, as measured by number of ADRs outstanding. Claudine Gallagher, global head of depositary receipts at JPMorgan, says: "We are very pleased to be working with a blue chip company like Sanofi-aventis. We look forward to helping Sanofi-aventis fully leverage its ADR programme to support the company's global growth initiatives. This mandate is testament to JPMorgan's strong position in the depositary receipt industry, in both developed and emerging markets."

Moscow - Shares in five new issuers will now be serviced by the **NDC-DCC Bridge**, which allows same day transfers of securities between Russia's National Depository Center (NDC) and the DCC. The five new issuers include VTB Bank OJSC, Sistema JFSC, Sistema-Hals OJSC, Territorial Generating Company #5 OJSC, and Fourth Generation Company of the Wholesale Electric Power Market OJSC. NDC is Russia's only settlement depository servicing the full range of securities issued by Russian issuers. The NDC-DCC Bridge now services 97 securities on behalf of 62 issuers.

FUNDS AND ADMINISTRATION

Amsterdam - The Dutch associations of pension funds (**VB, OPF and UvB**) have published a report advising pension funds on how to approach ethical investments, encouraging funds to consider social, environmental and governance (ESG) criteria. The associations aim to encourage pension funds to consider ESG criteria in their investment policies as these fit with their mission and fiduciary duty. They also call for a joint effort across the industry and collaboration with asset managers among others, to design a policy for this. "The Dutch pension fund industry has been at the forefront of innovation in terms of investment strategies and we welcome the increased importance that is being given to ESG issues in this market because we believe these are fundamental drivers of long term corporate performance," says Karina Litvack, head of Governance and Sustainable Investment (GSI) at F&C.

Singapore - LaSalle Investment Management, real estate investment manager of the Jones Lang LaSalle group, has joined Taishin Investment Trust to launch a global real estate securities fund for Taiwanese investors. Taishin Global Real Estate Securities Fund, which will strategically invest in REITs across all regions, has been available to investors in Taiwan since 5 November, using the UBS Global Investor Index as its benchmark. It is distributed by Taishin, a subsidiary of Taishin Financial Holdings, with LaSalle acting as investment advisors.

St Helier - The NAV of funds under administration in Jersey has overtaken the level of bank deposits held on the island for the first time, reaching record levels of GBP221 billion, according to Jersey's financial regulator. Figures for the third quarter of 2007, compiled by the **Jersey Financial Services Commission**, indicate that all sectors of Jersey's Finance Industry are continuing to experience steady growth. While the NAV of funds under administration in Jersey has risen by 5% over the last quarter and by over 30% over the last 12 months, bank deposits have grown by 3.7% to GBP219.5 billion and by 17% since the same point last year. Meanwhile, expert funds continue to perform strongly, with numbers established rising by 9.4% and the NAV increasing by 13.6% during the quarter.

Shanghai - BNY Mellon Corporation and **Western Securities** have signed an agreement to establish a joint venture fund management company in China. The new company, which will be called BNY Mellon Western Fund Management and owned 51% by Western Securities and 49% by BNY Mellon, will be headquartered in Shanghai and is expected to launch in 2008, subject to regulatory approval. The joint venture will initially manage domestic Chinese securities in a range of local retail fund products. Over time it is hoped that the venture will develop further products using the scale and expertise of the Bank of New York Mellon group. BNY Mellon Western Fund Management will aim to leverage distribution within the Chinese banking and securities sectors, building awareness of the new company in the region.

LEGAL AND COMPLIANCE

New York - Eight pension funds representing institutional investors have again voiced their opposition to two SEC proposals that would limit shareholder rights. Directors of pension funds and industry associations, including the **California Public Employees' Retirement System, California State Teachers' Retirement System** and the **Council of Institutional Investors**, called

for SEC chairman Christopher Cox to delay a vote and "not act on these flawed proposals" until the SEC panel has a full bank of staff. One of the proposed laws would permit shareholders to get election bylaws changed only if they have a 5% stake or more in the company for at least a year. The other rule would limit shareholder access to proxy material.
In other news, the SEC has approved rules allowing overseas issuers to report using International Financial Reporting Standards (IFRS), eliminating the need for foreign companies to reconcile their financial statements prepared under IFRS with US Generally Accepted Accounting Principles. Charlie McCreevy, European Internal Market and Services Commissioner, said: "I very much welcome this historical step by the SEC on the road towards global accounting standards. I have congratulated SEC chairman Cox for this decision, which will benefit EU companies with a US listing."

MARKET INFRASTRUCTURE

Seoul - Shinhan Bank has become a shareholder of **CLS Group**, bringing the total number of banking and financial institutions as shareholders to 70 and joining a shareholder group that consists of many of the world's largest commercial and investment banking organisations. Shinhan Bank will in due course apply to become a settlement member of CLS Bank International, the provider of Continuous Linked Settlement (CLS), a global banking settlement system for the foreign exchange market.

Frankfurt - The real-time gross settlement (RTGS) system for large value payments across Europe, **Target2**, has been successfully launched, the European Central Bank (ECB) says. Target2 will replace the decentralised technical platforms operating under the name Target. The launch of Target2 saw the connection of the first migration group composed of the national central banks and the respective Target user communities in Austria, Cyprus, Germany, Latvia, Lithuania, Luxemburg, Malta and Slovenia.

London - Interdealer broker **Icap** has applied to the UK's Financial Services Authority (FSA) for the status of a regulated market under the provision of the Markets in Financial Instruments Directive (MiFID). Icap said in its first half results statement that it believes there are opportunities in several markets to offer trading on an "Icap Exchange" and it intends to apply to the FSA for regulated market status under MiFID so that it can launch new products in markets such as emissions, energy and transport.

TECHNOLOGY

Wickham, NSW - Australian corporate **Independence Group** has selected **Broadridge**'s International Shareholder Communications Programme to electronically distribute its general meeting information, corporate news and investor relations (IR) materials to its Australian and non-Australian shareholders. ■

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Mandates round up of awards

RBC Dexia had a typically strong month, expanding its relationship with the Australian asset management company Maple-Brown Abbott Funds, while also winning a mandate to provide global custody and securities lending services for Cayman National Securities.

The deals build on the bank's success over November, with a USD4.2 billion mandate win with Canada-based Seamark and a deal with Ark Fund in Toronto.

BNY Mellon Asset Servicing made significant progress expanding its toehold in China in November. The bank won its third mandate to act as overseas custodian for a Chinese Qualified Domestic Institutional Investor (QDII) fund.

BNY Mellon was appointed by the Industrial and Commercial Bank of China (ICBC) to service the overseas investments of China Southern's latest QDII launch. The fund launched at a capped USD4 billion in assets having received USD6.5 billion in subscriptions from Chinese investors.

Mandates awarded in November 2007

Month	Winner	Client	Location	Assignment	Mandate size
November	JPMorgan	Sanofi-aventis	London	Depository Services	USD9bn
November	RBC Dexia	Maple-Brown Abbott	Sydney	Custody Services	n/a
November	RBC Dexia	Cayman National	George Town	Custody/Sec lending	n/a
November	JPMorgan	Michigan State	New York	Reporting Services	USD61bn
November	BNY Mellon	Islington Borough	London	Custody Services	GBP718m
November	BNY Mellon	ICBC	Hong Kong	Custody Services	USD4bn
November	RBC Dexia	Ark Fund	Toronto	Custody Services	n/a
November	BBH	ICBC	Hong Kong	Custody Services	n/a
November	RBC Dexia	Seamark	Halifax	Custody Services	USD4.2bn
November	State Street	Royal Cosun	Amsterdam	Custody Services	EUR620m

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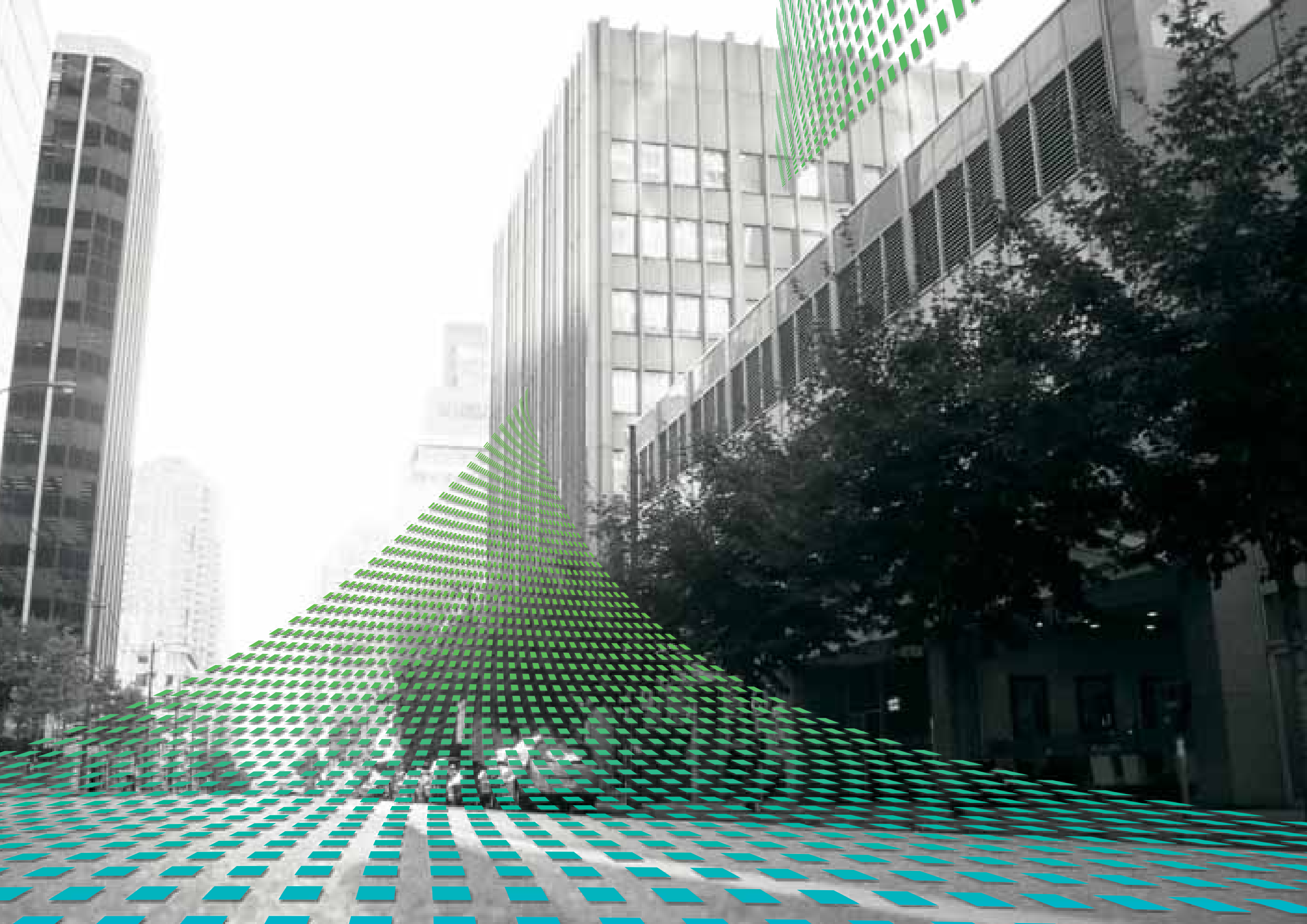


Peas in a pod

Will BlackRock give the superfund a vote of confidence?

The USD75 billion superfund, created by a consortium of Wall Street banks to help shore up the market for asset backed securities, may be managed by BlackRock, if recent reports are to be believed.

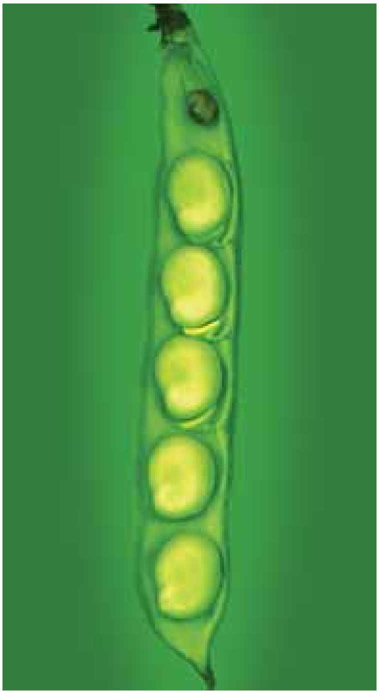
Should BlackRock be named as the main asset manager it will be responsible for managing the securities sold into the fund's portfolio, set up by Bank of America, Citigroup and JPMorgan. It would also prove to be a vote of confidence in the fund, which has come under harsh criticism over the last month.

It is understood that Bank of America, Citigroup and JPMorgan will invest between USD5 billion and USD10 billion in the fund. The remainder – USD60 billion – is expected to be raised by a multitude of US and global financial institutions. A custodian bank is yet to be named, but Bank of New York Mellon's name has been linked to the fund.

The fund was announced in mid-October, to a mixed reception from market participants, many of who questioned whether the plan would offer swift relief to the beleaguered credit markets.

Deutsche Bank chief executive Josef Ackermann, speaking on behalf of the Institute of International Finance, said in October that the group of financial institutions would welcome market-based initiatives, but it was "premature to make a firm judgment" about the fund.

The superfund will function by issuing short term notes, then use the proceeds to buy mortgage-linked assets from structured investment vehicles (SIVs). SIVs issue short term debt to invest in longer term securities. A lack of confidence in what these vehicles hold has put them under pressure to sell their assets. The fund will hold these shaky assets until investors can better evaluate



the default rates or the mortgages backing these bonds and other securities.

Former chairman of the Federal Reserve Alan Greenspan last month questioned the purpose of the superfund: "It is not clear to me that the benefits exceed the risks. The experience I have had with that sort of intervention is very mixed," he said. "What creates strong markets is a belief in the investment community that everybody has been scared out of the market, pressed prices too low and there are wildly attractive bargaining prices out there. If you intervene in the system, the vultures stay away. The vultures are sometimes very useful."

Further pressure is also being piled on the consortium's plans as a result of HSBC Holdings' announcement at the end of November that it would bail out its SIVs to the tune of USD35 billion. HSBC said it would move Cullinan Finance and Asscher Finance, two of its SIVs, onto its balance sheet to prevent forced sales of what it called "high quality assets".

HSBC's decision to tackle the problem alone shows the superfund – expected to be up and running in mid-January – will be too late to help some SIVs. ■

Making a splash

Is UCITS III set to cause a splash in the market?

Alternative investment funds will become more readily available to the mass market in the coming 12 months, as asset managers and banks either adapt old funds to UCITS III legislation or launch new ones.

Last month, ABN AMRO Asset Management converted 11 of its fixed income range of funds to UCITS III sophisticated status, while HSBC has released plans to launch new investments based on its HSBC GIF Climate Change Fund, a UCITS III compliant vehicle. Northern Trust Global Investments has been extending its list of Dublin domiciled, UCITS III qualifying, pooled, quantitative funds, with a Global Emerging Markets Index Fund.

UCITS III allows regulated funds to make greater use of derivatives and invest in a wider array of assets, something that is expected to take off over coming months as they are made available to retail investors across the globe where UCITS is accepted. 130/30 funds may be just the beginning, as hedge funds look to launch new and innovative products.

Hedge funds have also been active in creating UCITS III compliant vehicles in Europe. JPMorgan Highbridge has been particularly active in this space, with success from its Luxembourg domiciled Statistical Market Neutral fund – a Sicav with a minimum investment threshold of USD25,000 that raised USD10.5 billion before closing over the summer.

But it seems fund managers aren't quite ready to take up these products just yet. Over half of UK fund managers are not taking advantage of the UCITS III rules to hedge their portfolios in uncertain markets, according to research from Hargreaves Lansdown. The majority of managers polled said they do not currently use the additional powers in any of their funds, although some have received permission to do so or plan to in the future. ■

Deriving force

ISJ speaks to Jim Buckley of Canadian investment bank Scotia Capital about his career highlights and the complex world of derivatives

Jim Buckley, current managing director and head of Global Equity Finance for Scotia Capital, has worked across a number of financial market sectors over his career, beginning with Citibank as a management associate in treasury operations. "Citibank was a tremendous training ground. I learned the value of hard work and dedication early. The effort I put in was rewarded. One of my early mentors at Citibank gave me an analogy that I have not forgotten to this day: 'The only way to provide yourself self assurance on job satisfaction is to provide more value to your organisation than they provide to you through compensation and benefits.' I try to live by this philosophy day in and day out."

Buckley feels that this was a very valuable lesson for his future, as it made him responsible for his actions and development: "The people I worked for explained to me up front that I was expected to know what I was doing, and if I needed an explanation or assistance it was incumbent upon me to ask. I didn't sit back and wait for the organisation to provide me with learning or opportunities, I went and sought them out."

And Buckley is certainly not afraid of a challenge; his passion for derivatives is proof positive of that. He started in the business in the late 1980s, when derivatives were developing, he says: "We didn't learn about the math or the applications of the products in school, so all of the learning was done on the job." The first major project Buckley worked on was the conversion to present value accounting from accrual accounting for swaps. It was a complex project for a number of reasons but it taught him the most about the area, he explains. He thus learned all of the valuation standards, how to build and evaluate yield curves and see the financial implications of how the models work and prices change. "I recall that my assistant manager and I worked for 16 hours a day, five and a half days a week for a few months to complete the project."

Buckley has continued his championing of the issues around derivatives in the Canadian market – he was one of the founding members of the International Swaps and Derivatives Association's (ISDA) Canadian Steering Committee, which he then chaired in its third year. "The work I did with ISDA showed me the power, responsibility and accountability of industry groups. These groups have tremendous bargaining power and influence within the industry. ISDA has been successful in lobbying for changes in the law in many jurisdictions to support collateralisation and close out netting to support the integrity of the OTC derivatives market," he explains.

However, with that power, comes great responsibility: the responsibility for education. ISDA, as part of its lobbying efforts, did an excellent job of educating regulators and interested parties on the reasons for the reforms that were being lobbied for, says Buckley. One of the key factors in the education process was to balance the local country needs with those of the global financial markets. It was important to have an understanding of the local sensitivities and how individual markets function within the global financial system. According to Buckley, one of the keys to this was to ensure that the financial institutions within a particular country were not relegated to working from a competitive disadvantage to their peers in other countries as a result of local legislation.

"The organisation is ultimately accountable to its membership. The membership holds them responsible and sets the agenda for the year. This needs to be balanced across its many members all of whom have very different needs," he explains.

His passion for derivatives and furthering the industry agenda in this space was an integral part of the reason for his move to Scotia Capital. "I hadn't really considered Scotia Capital as an alternative for employment. However, while I was starting my job search, Scotia announced the hiring of John Schumacher (the current co-CEO of Scotia Capital). I took this as a sign that Scotia was looking to ramp up their presence in the OTC derivatives market. I had a friend deliver my resume to John and followed up diligently. After five or six interviews with John and Mike Durland (John Schumacher's current deputy head), they extended me an offer to start as their chief of staff."

Buckley is proud of Scotia's achievements and he states that Schumacher has led its trading businesses to reach new pinnacles of success. "His prudent risk management and forethought around industry trends has placed Scotia Capital in the right places at the right times. Through the growth of the businesses, John has been able to maintain the feeling of a small entrepreneurial organisation across his business line."

and in the end everyone was proud of what we had built."

Buckley began running the operations unit, which included accounting, valuation and risk. As back office and middle office functions were combined at that time, in the end this meant that he was responsible for everything other than

and the United States over the last two years. The challenge is to keep the desks talking to one another and keep the organisation efficient. It is easy for desks to feel isolated but I believe that our culture and team structure allows us to maintain the efficiency and close communication necessary to be

The work I did with ISDA showed me the power, responsibility and accountability of industry groups. These groups have tremendous bargaining power and influence within the industry

"I have been lucky to work for John and Mike for over 10 years now," adds Buckley. "I have been given every opportunity to succeed and believe that I have served them and the organisation well over the years. As the organisation has grown and evolved, I have been afforded many opportunities that may not have been available in other organisations."

Prior to joining Scotia Capital, Buckley was head of risk management and operations at TMG Financial Products (Canada), a subsidiary of Mutual Life Assurance Company of Canada, and this role represented a number of challenges at the other end of the spectrum. TMG was small and entrepreneurial, he explains: "My first interview was in the middle of the new office space before the walls were even planned. We were trying to carve out a niche that the banks were having difficulty servicing and specialise in particular product segments."

Just as there weren't walls, there weren't any policies or procedures either, he adds. The team therefore had to start from scratch based on their collective experience. This was both beneficial and challenging, he continues: "We challenged our ways of doing things at our old organisations and took the effective controls and processes and threw away the ones that we didn't believe in. We held each other to tough standards and worked towards building something special and unique. The people hired did whatever it was that was necessary to get things up and running and then maintain the business once we got operational. The small company atmosphere was conducive to everyone pitching in and helping out. We worked long and hard, trading and marketing. "We ran a proactive service model that was responsive to both marketers and traders to ensure that they could respond to client or market demands in a timely manner," he says.

Unfortunately, the good times at TMG did not last – the organisation went through a number of changes, and finally, its parent company decided to make a strategic exit from the business. One of the changes was a consolidation of the services into the US company. "I needed to inform all of my staff and provide them with their packages. It was the hardest thing I have ever had to do," Buckley explains.

It is lucky then, that he has found new challenges at Scotia to keep him as passionately engaged in the industry as ever. "My current position is all about strategy and building scaleable solutions. It is easy to just try and fix the current problems without a view as to how the world may look in five years. I don't just want to put out the fire of the day; I want to solve the real problem. Some of this is through systems, but quite often it is the infrastructure and people. Business strategy needs to be built and bought into. I need to sell my long term solutions to both business partners and clients. I also need to listen to their feedback and refine as required."

The next year will be full of exciting challenges, he explains. He will be focusing on a targeted growth strategy, as a number of markets may contract. Scotia's main aim has been and will continue to be the building out of the international prime brokerage infrastructure. "We have launched securities lending desks in Europe, Asia, successful," he elaborates.

Securities lending isn't the only component of the framework, however. The firm is constantly looking for more efficient ways to deliver its services, continues Buckley. The proper systems infrastructure to deliver information and processing is therefore a must: "This allows personnel to focus our customers' expectations rather than administration and fire fighting. It is incumbent on me to get the organisation as efficient as possible and empower people to be proactive and focused on our clients."

To Buckley, the people are the business. "I do not believe that you can sit back in an office and manage from afar. With offices in five countries and a diverse set of products and clients, I find myself travelling quite a bit to be in the offices and working with my people. I try to empower them and support them in each of their initiatives but phone calls are not enough. I believe I have to be on the ground with them regularly in order to show them the proper support," he adds. The internal organisation with Scotia's support groups also requires time and attention, he says. After all, Scotia is in a service oriented business that requires it to deliver the firm to clients every day.

The people with whom he works are also the most rewarding part of his career, says Buckley. This includes clients, co-workers and peers: "The industry attracts all kinds of people and getting to know the people and developing relationships with them has been tremendously rewarding. I only hope that I can exemplify the best that I have taken away from the people that have taught me." ■

Sky's the limit

The Chinese economy is the fastest growing in the world, but exactly how much progress has been made in the domestic capital markets space? **Virginie O'Shea** investigates

China's stellar ambitions for the future have moved one step closer to being realised this year. Not only has the country launched a satellite into orbit around the moon, the feverish Shanghai stock market has witnessed the rocketing of the share price of a number of Chinese stocks. Not least of these was the much reported price of the country's largest oil refiner, PetroChina, which soared to a phenomenal USD1 trillion at the start of November (equal to Exxon Mobil, Shell and BP combined). In fact, on the basis of its Shanghai share price, PetroChina was the world's most valuable company at that point in time.

If China's technological ambitions are being demonstrated to the world by its Chang'e satellite, which it says is the first step on the road towards a manned lunar mission, then its financial ambitions are surely indicated by the government's landmark announcement in August to allow individual investors to begin directly trading in Hong Kong listed shares. China's State Administration of Foreign Exchange (Safe) released the plans on 20 August for a "through train" pilot project to allow all Chinese residents to invest in Hong Kong's stock market for the first time via the Bank of China's operations in Tianjin.

The announcement had the immediate impact of buoying the Hong Kong stock market, as local and international investors were cheered by the prospect of an inflow of Chinese money (this may have already hit a stumbling block, but more on this later). Furthermore, the news at the start of November that the Hong Kong stock exchange is effectively being forced to increase its capacity in order to keep up with processing demands is indicative of the fervour that surrounds investment in the Chinese market. Hong Kong Exchanges and Clearing revealed its plans at the start of November that it will spend USD58 million on its computer systems before the end of 2008, in order to up its capacity to be able to handle 7.5 million trades per day, up from 1.5 million at the moment.

The spectacular performance of the Chinese stock market has helped to attract the flow of foreign investment into the country and this in turn has aided the development of the domestic fund management industry. The Chinese fund management market is just beginning to develop its experience in international investing and, as of the time of writing, four internationally invested funds have so far been launched under the Qualified Domestic Institutional Investor (QDII) scheme. The QDII scheme allows domestic investors to invest in foreign securities markets via certain fund management institutions, insurance companies, securities companies and other assets management institutions that have been approved by China Securities Regulatory Commission (CSRC).

The scheme, which was announced in April 2006, was initially limited to fixed income and money market products but this was extended to include stocks on 11 May 2007. The process of liberalisation has been progressing over the last year in order to allow outbound investment by Chinese nationals and provide a source of diversification away from the domestic stock market. The fourth fund launched at the start of November and gathered USD14 billion in subscriptions in the first day of sales. China International Fund Management had targeted an equivalent of USD4 billion, scaling back the offer to match the allocated quota. Two more funds are expected to be launched before the end of November.

Lisa Robins, JPMorgan's head of Treasury Services in China, believes that the interest and over subscriptions in the first QDII funds suggest that there is a growing and sustained interest in diversification of investments. Regulatory and legal infrastructure to support the development of capital markets is rapidly evolving and the symbiotic relationship of China's enormous economic base and Hong Kong's market expertise has been an excellent match. Robins cautions, however, that the right regulatory framework would be essential to continuing the momentum and the appropriate environment will only enhance safety and soundness.

Citic Securities was among the first batch of Chinese securities companies to receive approval as a QDII. Neil Daswani, global head, Securities Services, managing director, Transaction Banking, at Standard Chartered, believes the Bear Stearns partnership with Citic will facilitate its international strategy and represents one step forward for the Chinese brokerage's global strategy (see box on page 17 for more information). "This sets a precedent for entry of Chinese securities companies into global financial arena," he says.

As well as encouraging international investment from domestic investors, the Chinese government has started the process of approving new quotas for foreign investment in the country's stock market through the Qualified Foreign Institutional Investment (QFII) programme. In May, China and the US reached a preliminary agreement during their strategic economic dialogue to raise the quota from the current level of USD10 billion, to USD30 billion.

Chinese custody players

- Industrial and Commercial Bank of China (ICBC)
- China Construction Bank (CCB)
- Bank of China (BOC)
- Agricultural Bank of China (ABC)
- Bank of Communications (BoCom)
- China Merchants Bank (CMB)
- Industrial Bank
- Everbright Bank
- China CITIC (China International Trust and Investment Company)

Laurence Bailey, JPMorgan's Worldwide Securities Services APAC CEO, feels this would be a major step forward for the market: "Foreign investment via the QFII vehicle has been limited by the regulatory quota system and the ability to gain certain exposure to China via the Hong Kong market, but if and when the regulations ease, given the current economic mood globally, we expect to see a hearty pick up in foreign investment."

The government issued revised QFII rules in August 2006, but operating guidelines for foreign exchange, the stock exchanges and clearing and settlement policies have not yet been announced, adds LJ Jia, China country manager, Brown Brothers Harriman. Under the existing regulations, QFIIs are subject to a lock in period of one year, after which only 20% of the principal can be repatriated every three months. Until the new stock exchange rules are announced, QFIIs continue to be limited to investment through one broker, even though the new QFII regulations allow for up to three brokers.

Regardless of the spectacular growth of the Chinese market this year, there may be trouble ahead, as the global economic slowdown looms on the horizon and the ambitious plans of Safe are put on a backburner. China's commerce ministry has warned that a slowing US economy could trigger a drop in Chinese exports, which could mark a "turning point" for China's rapid economic growth. The drop in US demand that has ensued from this summer's sub-prime mortgage market woes could pose a significant threat to the stability of the Chinese economy, as domestic exporters are impacted by a rapid and continuous fall in orders. The government report, released in mid-November, also noted that continued turmoil in global financial markets could encourage greater capital inflows to China, straining the country's financial and regulatory system and increasing inflationary pressure.

The spectacular performance of the Chinese stock market has helped to attract the flow of foreign investment into the country and this in turn has aided the development of the domestic fund management industry

In many sectors, margins have come down – but only from unreasonably high levels, explains Daswani. The public accounts remain very robust, meaning there is considerable scope for a fiscal boost if private investment slows. "The chief risk remains a significant US slowdown – but China's exports are actually quite diversified, with only 20% going into the US. A short lived US slowdown would not present a big issue for China (perhaps it would lose one or two percentage points of growth) – although a longer and more widespread global downturn would clearly present a much bigger challenge," he elaborates.

The government has not been sitting on its laurels, however, and facing equity prices at unsustainable levels, Beijing seems to be aiming to quietly talk the market down. It has attempted to crack down on bank lending into the market (albeit tricky to achieve) and it has raised interest rates and reserve requirements. It has also been encouraging companies to list shares and may encourage blue chips to start selling their locked up legal person shares. It has encouraged capital outflows, for instance via QDII, adds Daswani.

On the bond side, there are also efforts underway to enliven the bureaucratic corporate bond market. These efforts involve regulatory authority passing from the National Development and Reform Commission to the China Securities Regulatory Commission, simplifying the issuance process, improving the credit rating and bankruptcy frameworks. This is taking some time but in the meantime, the central bank has been an active promoter of the short term corporate bill market, he explains.

far, the Chinese economy appears to have weathered the economic storm rather better than the rest of the world. The World Bank released a report on the East Asian region in November, which indicates it expects the region's economy to have grown by 8.4% this year and a further 8.2% over 2008. Rather than joining the chorus of doomsayers, the report highlights the precedent set by past economic crises in which US slowdowns have represented a "significant" but not catastrophic impact on the Asian market. The World Bank is therefore forecasting that China will continue to drive the region's economic expansion with expected growth of 11.3% this year and 10.8% in 2008.

"We still think there will be one more interest rate hike this year, of 27bps, and two more by the first half of 2008, although the risk of more clearly exists given People's Bank of China's concerns about inflation and recent official commentary about the real negative deposit rate," says Standard Chartered's Daswani. "In addition, loan growth quotas are now in place for the all banks

The process of liberalisation has been progressing over the last year in order to allow outbound investment by Chinese nationals and provide a source of diversification away from the domestic stock market

The bad news doesn't end with the impact of the summer's crisis and the threat of regulatory risk, however. Hong Kong listed shares suffered their worst fall since September 2001 at the start of November, following the confirmation by Wen Jiabao, China's premier, that the scheme to let Chinese investors buy Hong Kong stocks directly would be delayed. The Hang Seng China Enterprises Index, which tracks Chinese companies listed in the territory, fell by nearly 7% and the Shanghai Composite Index fell 2.5%, for example. The Hong Kong and international investors who were hoping to benefit from an inflow of Chinese money have been left hanging indefinitely as the Chinese government conducts "scientific judgment and analysis" about how to put the plans into action.

Despite the threats posed by regulation and market instability in the future, thus

(no lending growth in November-December is being recommended). The short term re-discount lending market has seized up. Lending quotas should be relaxed in 2008, but the risks are that constraints remain."

Standard Chartered's year end forecast shows that USD-CNY (dollar-yuan) has resumed a sharper appreciation pace over the last month and has now hit 7.42 against USD, he adds. "We have revised our views, becoming more bullish – and are looking for 6.8 at the end of 2008, or 7.5% against USD. There is also a revived debate in Beijing about the CNY, as we all recognise that 2008 will be a tougher year for Beijing, as inflationary pressures remain and political tensions with the US and EU rise. We also expect more volatility in USD-CNY, as the central bank attempts to undermine one way appreciation bets."

Hernan Rodriguez, managing director, Depositary Receipts, at the Bank of New York Mellon, is positive that, as far as portfolio investment is concerned, there is continued acceleration in the mutual desire of Chinese resident companies and international investors to finance start-up and established ventures in the country. "Along with India, China is offering the most varied and most interesting opportunities of the emerging markets. As investors rapidly abandon the 'sub-prime tainted' developed markets, vast pools of capital are looking at opportunities in the SME space within emerging markets; these opportunities are simply too few relative to the amount of capital seeking them out. An educated observer might take the view that it will take another unexpected market shock of some size to derail this trend in the short term," he explains.

China has also made significant investments in the domestic capital market, most noticeably in the regulatory framework for its capital markets, says Northern Trust's chief representative in China, Kevin Tan. "When the People's Bank of China created the China Banking Regulatory Commission, the China Insurance Regulatory Commission and the CSRC, it sent a clear message that China was prepared to adopt best practices in separating monetary policy from its regulatory function. At the same time, China adopted the principle of using custodians as a way to separate the investment decision making function from the safekeeping and valuation functions. These changes to the capital market infrastructure in China have presented opportunities for foreign institutions such as Northern Trust to provide services that were previously lacking in the Chinese financial services industry."

The growth of the equity markets in China, supported by the stock exchanges and the equities depository China Securities Depository & Clearing Corporation (CSD&C), has been remarkable, adds Philip Reichardt, director of international cooperation at Euroclear. The volumes transacted daily dwarf what most advanced markets experience; the Chinese authorities have invested in systems that are capable of handling these high volumes and their predicted growth, he explains.

Euroclear signed a Memorandum of Understanding (MoU) with the CSD&C a few years ago and with the government bond depository, the China Government Securities Depository Trust & Clearing Corporation, earlier this year. The purpose of these agreements is to share expertise about international post-trade processing standards for the benefit of the Chinese market. "In Euroclear's case, we have very regular contact with both depositories across a range of technical and operational topics, which are being analysed in China. Senior Euroclear management regularly visit executives at the Chinese depositories and they do likewise," says Reichardt.

According to Euroclear, its aim in sharing knowledge with the Chinese is to help the post-trade infrastructure service providers adopt international standards as early as possible so that they can more readily interconnect with international markets at the appropriate time. "By analysing practices from the US and Europe, which have taken many years to evolve, we can expect the Chinese market to take a much shorter period of time to reach a similar stage of maturity," he explains.

The CSD&C signed a similar MoU with the Depository Trust & Clearing Corporation (DTCC) in June this year, in order to foster greater international cooperation in the area of clearing and settlement. CSD&C vice chairman and general manager Ying Jin commented at the signing: "DTCC and CSD&C share the privilege of serving our respective capital markets industries, and both organisations have a common understanding of the importance of that role, which spurs the beginning of our cooperative relationship. CSD&C firmly believes that we have bright perspectives and enormous cooperative opportunities regarding securities clearance, settlement and depository business and hope that the signing of the MoU will promote our cooperative relationship."

Improvements are certainly required in the clearing and settlement environment, adds BBH's Jia. Under the current structure, securities are transferred on trade date, and cash on the following day and the environment does not allow for pre-matching. Transactions are settled based on the stock exchange's trading report sent to the depository. This introduces risk to the settlement process. There is no mechanism to prevent settlement occurring in the investor's account. In the event of a broker executing an error, it must be handled on a post-facto basis. There is a mechanism for correction of trade errors before cash settlement, but this is only to be used in the event the error results in an overdraft in the QFII's account. The nature of the QFII scheme requires that the QFII must have funds available in its account before a purchase order is executed on their behalf or securities for a sale transaction.

Kenneth Tse, senior vice president and head of Asia Pacific Depositary Receipts Group at JPMorgan, however, is positive about the future of the market infrastructure in China: "The clearing and settlement infrastructure in China was built relatively recently compared with other stock markets around the world, allowing it to taking advantage of the latest IT technology. Through its recent MoU with the US DTCC, China will gradually move more in line with international compliance, regulatory and corporate governance standards. This bodes well for the long term development of the China stock market. Also, the cooperation might lead to the cross listing of stocks between the two markets. While today Chinese companies list in US stock exchanges in the form of ADR, we might see in the future of US companies listing in China in the form of CDR."

Northern Trust's Tan feels that all parties in these MoUs will benefit: "The clearing and settlement environment in any country, not just China, should be constantly evolving and adopting best practices as new and more complex instruments are introduced to the market. The MoU between the DTCC and the CSD&C is a formalisation of the exchanges in information and experiences from which both institutions will benefit. Both institutions will learn from each other, and this will lead to faster development of more efficient clearing and settlement environments for the capital markets in general."

The Chinese are also building their experience base in the domestic and foreign capital markets, says Daswani. The Chinese government and the regulatory bodies have been very prudent in slowly opening the capital markets to more complex instruments such as derivatives. Deng Xiaoping talked about, "crossing the river by feeling for stones",

Give and take

This year has seen a flurry of M&A and joint venture (JV) activity in China, as Chinese banks scour the market for suitable partners and foreign suitors court them in a race to get a piece of the action. The latter half of 2007 has seen the Chinese banks take the initiative, as Western financial institutions have struggled to deal with the direct impact of the credit crisis. These banks are seeking to diversify out of the domestic Chinese market and gain foreign expertise and global reach via offshore acquisitions.

Industrial and Commercial Bank of China (ICBC) kicked off the year in January, when it bought a 90% stake in PT Bank Halim Indonesia for USD10 million. The acquisition trail sped up towards the end of the year, as Chinese banks profited from the fallout of the sub-prime mortgage market woes. In July, China Development Bank paid USD3.14 million for a 3.1% stake in Barclays UK. ICBC has had a spectacular year in the market – it picked up an 80% share of Macau's Seng Heng Bank in August and a 20% stake in South Africa's Standard Bank in October. Also in October, Minsheng Bank became the first mainland commercial Chinese bank to invest in a US lender, when it paid USD200 million for a 9.9% stake in UCBH Holdings.

The most recent acquisition, which has garnered a fair number of headlines over the last month, is Citic Securities' investment of USD1 billion for a 6% stake in Bear Stearns and the US bank's reciprocal investment of USD1 billion for a stake of just over 2% in Citic.

Chong Jin Leow, head of Asia Pacific, BNY Mellon Asset Servicing, explains the appeal for Chinese institutions: "These JVs continue to bring much needed capital, training, education, and stability to the Chinese domestic market. Global institutions have significant experience in domestic and global markets and are in an ideal position to train and educate China's future financial services professionals to recognise opportunity while also minimising risks."

and this is the model by which China is progressing. "The regulatory environment in China will always be a concern, but we must remember that the Chinese regulators will change regulations in their own time, at a pace that is appropriate for the level of expertise and experience that the Chinese capital market payers can manage," he explains.

BNY Mellon's Rodriguez feels that progress could be hastened on the regulatory front: "The rest of the world would be delighted with the opportunity to bring the latest technology and trading techniques to the Chinese market, but much of the drive would depend largely on the willingness of an unwieldy bureaucracy to permit the introduction of multiple simultaneous innovations."

JPMorgan's Bailey agrees that regulation is one of the main impediments to the speed of foreign investment: "The obtuse and dynamic regulatory framework in China is causing some sluggishness in foreign investment. As most local companies are still state owned and often not audited by internationally recognised accounting firms, foreign investors could be reticent about investing in local businesses."

Exploding onto the global stage

The growth of the equity markets in China - supported by the stock exchanges and the equities depository China Securities Depository & Clearing Corporation - has been remarkable

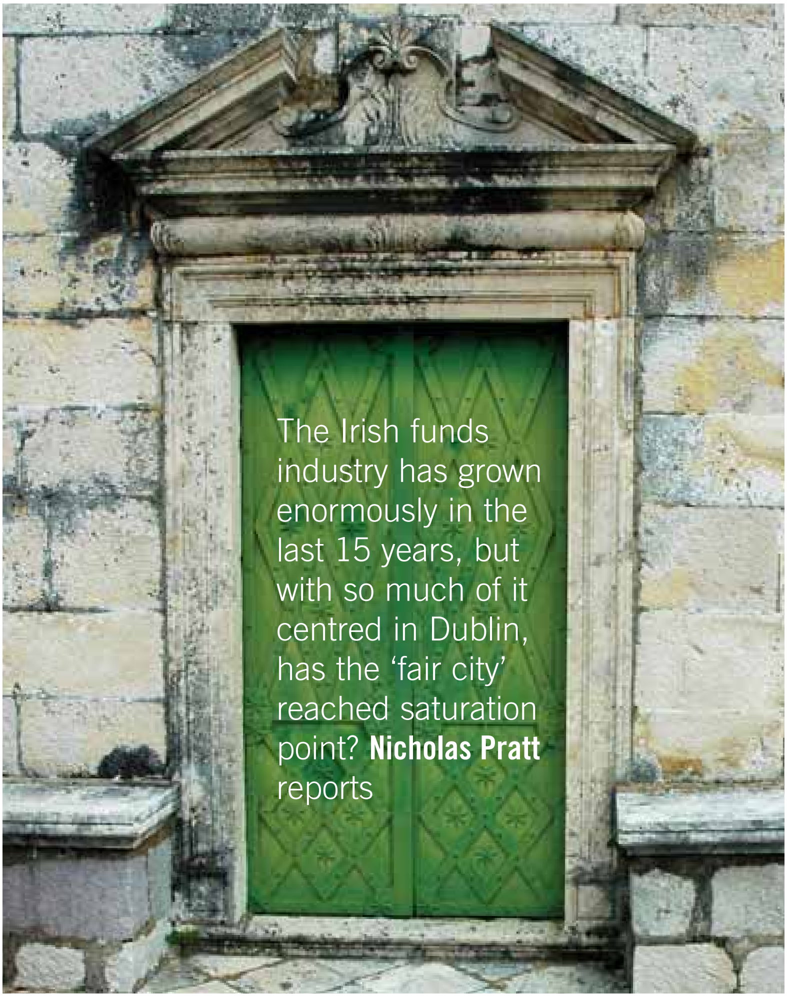
As a consequence of the barriers to entry, the domestic market is still dominated by local players. The Chinese fund administration and custody services market is dominated by big local banks as they have country wide distribution networks in place and have built up their client base, Daswani elaborates. "We see that in the near future, there will be increased competition from locally incorporated foreign banks and even second tier Chinese local banks with the evolution of securities market."

Chong Jin Leow, head of Asia Pacific, BNY Mellon Asset Servicing, agrees that for foreign assets coming into the Chinese market in the short term, the dominant players will continue to be the major regional custodians that have established custodial operations in China. The vast gap between these institutions and their Chinese competitors will ensure that the vast majority of global assets will be funnelled through these institutions. Domestic assets will continue to be the domain of the major Chinese custodial banks as they leverage their domestic corporate relationships as well as their wide distribution capabilities to secure additional assets.

"From a competitive standpoint, we expect to see competition intensify significantly among the domestic and regional custodians over the coming years. Regional custodians will continue to fight for global assets, while the domestic banks will compete for domestic assets, and although the competition appears stratified based upon the source of the assets, the point of leverage used by both custodians will be consistent: price. In a great majority of cases domestic Chinese banks operate the same underlying custody and fund administration systems (a by-product of a single software provider) and product differentiation is extremely limited, thus the ability of buyers to differentiate between providers is difficult and therefore price becomes the primary differentiator," says Leow.

The outlook for the Chinese custody market in the next five years is outstanding, says Northern Trust's Tan. The growth will come primarily from the cross border investments. As China continues to open its doors to domestic institutions investing overseas through the QDII programme, the opportunities for global custodians will only grow. "At the same time, as foreign investors seize opportunities to invest in domestic Chinese securities in order to participate in the growth story that is China, the opportunities for domestic custody in China will develop. This is an exciting time to be in the custody market in China, and institutions such as Northern Trust are making significant investments to grow our market share of what will be one of the largest capital markets in the world," he concludes. It seems for the Chinese custody market, the stratosphere's the limit. ■

When one door closes...



The Irish funds industry has grown enormously in the last 15 years, but with so much of it centred in Dublin, has the 'fair city' reached saturation point? **Nicholas Pratt** reports

It is 20 years since the International Financial Services District was established in Dublin – a move that, helped by a massively reduced corporation tax rate, rescued Ireland's economy from third world status. Over time, it has encouraged all of the major international fund servicing companies to set up shop in the emerald isle and Dublin more specifically.

As of June 2007 there were 5,646 funds being serviced from Ireland, with a value in assets of USD1.633.3 billion, according to the Ireland Fund Encyclopaedia, produced by Reuters-owned research firm Lipper. Furthermore, this is an increase of 35% from last year's total, which indicates that the industry is continuing to grow.

In terms of fund servicing companies, four companies share the majority of the market, with State Street, BNY Mellon, JPMorgan and Northern Trust accounting for USD740 billion in assets under administration and USD745 billion in assets under custody. All four have their main offices in Dublin, as do many others, including 342 fund management companies, a smattering of Irish law firms and the usual collection of consulting firms – PricewaterhouseCoopers, KPMG, Deloitte, Ernst & Young and Grant Thornton account for the majority of funds.

But such growth has placed a strain on Dublin which has been reflected in the high cost of living – Dublin property prices are now among the top five in the world – and the transport issues, as anyone who has ever experienced the daily commute to the capital will testify. Furthermore, Dublin is one of the few major European cities without an underground or metro network.

Efforts have been made to address these issues. The redevelopment of Dublin's docklands has continued to the extent that the financial district now stretches to a square mile. The government's Transport 21 initiative hopes to extend the city tram service – known as the Luas – introduce a Docklands light railway and city metro system, develop more motorways and revamp the country's train network.

But even with all of this work, Dublin still faces a stiff task to cope with the continual growth of the industry. This concern over the capital's capacity has been noted by the various government agencies and industry associations operating in the funds market. As a result, efforts have been made in the last two years to encourage firms to establish satellite offices in other parts of Ireland.

As Gary Palmer, chief executive of the Irish Funds Industry Association (IFIA), says: "An increased focus on operational efficiency through straight through processing is one way of relieving the need for greater capacity that is available to all but the one thing that Dublin's funds industry can count on is the rest of Ireland."

So far, there are 14 companies that have established offices outside of Dublin in nine counties – Louth, Meath, Galway, Kilkenny, Cork, Wexford, Limerick, Kildare and Waterford. The notable offices are Citi Hedge Fund Services (formerly Bisys) in Waterford; BNY Mellon in Cork; Northern Trust in Limerick and Fortis in Galway.

The Industrial Development Agency (IDA) Ireland, a government agency charged with attracting and maintaining the level of foreign direct investment in Ireland, has been a key influence in encouraging the funds industry to look beyond Dublin for business premises. IDA has developed a regional strategy for administrators and custodians based around a number of locations outside the capital. As part of the process of regionalisation, companies are taken to meet the local authorities, other companies working there, recruitment consultants, estate agents and, in most cases, spend a couple of nights there experiencing the local hospitality. Added to these introductory tours, the IDA in certain circumstances can offer financial assistance to companies looking to establish in these areas. There is also the promise of financial inducements in a selected few locations, which offer grant assistance to companies looking to set up there.

The strategy behind the IDA's efforts to grow the funds industry outside of Dublin was to give the fund administrators and custodians a new pool of talent to recruit from

"The strategy behind the IDA's efforts to grow the funds industry outside of Dublin was to give the fund administrators and custodians a new pool of talent to recruit from," says Deirdre Lyons, head of the International Financial Services Division of the IDA. "It was also to show that there was a strong infrastructure in these areas in terms of premises, education and broadband and to show that it was possible for people to move from Dublin and enjoy a high quality of life."

These satellite centres cater for all ranges of business activity says the IFIA's Palmer, dismissing the suggestion that they are merely low cost, processing centres devoid of any client facing functions. "There is no basis for any image of a high level/low level separation between these offices and their Dublin counterparts," he says. "The business model has been determined by the needs of each individual company involved."

BNY Mellon has the majority of its operations in Dublin but has established an office for its asset servicing business in Cork that employs 200 people. According to Harley Murphy, country head, Ireland for BNY Mellon's offshore business, the Cork office has the usual components of an asset servicing business and there is no real difference between the Dublin and Cork offices.

Due to the concentration of support services (audit and law firms, for example) in Dublin, it will remain the central destination for the commercial, client facing elements of BNY Mellon's fund services, but Cork does hold many different advantages, says Murphy. "Cork is an additional labour pool and the quality of life can be attractive to those that want to live outside of a major city. It is also a more stable market than Dublin because there is less competition and a less high turnover of staff."

Northern Trust opened the doors of its Limerick operations in March 2007, after beginning its search for a satellite office in the summer of 2006. "We felt a satellite office would be an advantage for those working at Northern Trust and they would have the option of working in the city or the country, relatively speaking," says Meliosa O'Caoimh, head of Northern Trust's Irish operations.

The company began its search 'beyond the pale' and in the neighbouring Dublin county regions, before deciding to spread its search further afield and to offer a true alternative to Dublin and eventually settled on Limerick. "It had a sizeable population, it was surrounded by other towns, it had two good colleges, a major airport nearby, good rail links to the rest of Ireland, a good quality of life and affordable house prices," says O'Caoimh.

There are now 69 people in the Limerick office, compared to the 430 in Dublin, but this is expected to rise to the mid 100s by next year, with the Dublin office likely to remain at the same level. "Limerick is our growth solution," says O'Caoimh. "Over 75% of our business comes from existing clients and they are telling us that they are planning to launch new funds so we are looking to grow with them."

O'Caoimh says there is no real difference between the two offices, with Limerick acting as a scaled down version of its Dublin counterpart. "Some of our competitors have taken a whole department to its satellite office but we preferred to take elements of it all so that we could offer a complete service out of Limerick." The only difference at present is the lack of client servicing in Limerick, something that O'Caoimh says will be decided by the amount of growth and volume of work that comes down to the town.

"It is really important that companies look to expand out of Dublin and across Ireland," says O'Caoimh. "There are very experienced people centred in Dublin but with the establishment of satellite offices, that experience is spreading out around the country with many management level people moving back to where they came from. It gives us all a bigger employment pool to draw from."

It has been three years since Citi Hedge Fund Services (or Bisys as it was then) began to look outside of Dublin as part of its capacity planning. Citi has a five year plan for the Waterford operation, by which time it expects to have 250 staff. Having just celebrated its second anniversary, the Waterford office now employs 90 people – meanwhile the Dublin office has grown from 300 to 360 people over the same period.

Tyrell also insists that there is no difference in the operations at Waterford and those at Dublin. "The fund accounting business is split into seven divisions, five of which are in Dublin and two in Waterford and everything is identical. Clients from the UK have visited the Waterford branch and even though it is 150 miles from Dublin, the reporting and communication lines between the two offices are very clear."

Recruitment was not an issue in Waterford, says Tyrell, something she puts down to the close link between the college in Waterford, the IDA and Citi. While this link has helped recruit graduate level employees, enticing more senior staff has relied on there being enough middle management types that have lived in Dublin for a number of years but would jump at the chance to

return to their roots and to get on the property ladder.

In all three cases previously mentioned, the advantages have been clear – recruitment costs are cheaper and because of the lack of competition in these cities, replacement and turnover costs are also lower. But how long will this remain the case? It is notable that, with the exception of Cork, where Citco, Apex and BNY Mellon have all established offices, it is largely the case that it is one major fund servicing firm for each county. Does this mean that the likes of Waterford, Limerick and other similar Irish counties are only big enough for one major player?

Tyrell feels that there is enough room for at least two players in Waterford, but suggests that over time certain counties will develop a good reputation for fund administration or some other specific funds related service and that will open the door for a second wave of smaller players. After all, she says, you cannot afford to be too remote and pick a location purely because you would be the only company there.

The IDA, through its grant assistance for selected locations, has played its part in encouraging firms to settle in specific locations and therefore spread the industry as far across the country as is feasible. "Our intention is to develop non-competing clusters," says Lyons. "However, we would not and could not prevent a company moving to where it wants to be, but the ideal scenario is to give a company establishing a satellite office every chance of succeeding."

There are some firms that have chosen to remain in Dublin, at least for now. JPMorgan has its main office in the IFSC, where 250 staff run its UCITS funds servicing business. The other office is on the north side of Dublin, in Malahide, where 200 staff work on the hedge fund administration side, a business that has grown out of the acquisition of Tranaut. So far there are no plans to look outside of Dublin, although should it need another office, it would look to alternatives outside of Dublin, says Carin Bryans, country head, Ireland for JPMorgan.

While there are various resources that can assist with the search for premises, notably through the IDA, there are more challenges around the recruitment of experienced management level staff, says Bryans. Additionally, the pressure on capacity that has threatened Dublin's continued success has eased somewhat over the last 12 months, allowing everyone to catch their breath. "I think this year has seen it calm down due to the amount of consolidation in the market and a general slowdown in the economy," says Bryans.

There is no basis for any image of a high level/low level separation between these offices and their Dublin counterparts

Another company that has resisted the urge to spread beyond Dublin is alternative investment services company SEI, which first established its Dublin office back in 1996. "We have seen a lot of competition in those 11 years," says David Morrissey, director for new business development and sales at SEI's European operations. "When we first came here there were less than 20 providers, whereas now there are closer to 60."

Nevertheless, Morrissey feels that Dublin has developed "really well", coping with the increased need for capacity and embracing regulatory change and sees no reason to move out of the city. He highlights the role of the various industry associations such as the IFIA in ensuring that the industry and its regulators remain in close contact and are able to monitor industry issues, from Swift implementation to the regulation of UCITS funds.

In terms of the funds industry itself, many of the providers are working closely with the associations and the Irish colleges of higher education to develop funds specific qualifications for both graduates and mature students looking to retrain. And although Dublin has become one of the top five most expensive cities in the world in which to buy property, Morrissey says that there has been no discernible effect on recruitment – particularly for the graduate and associate level staff they are looking to employ.

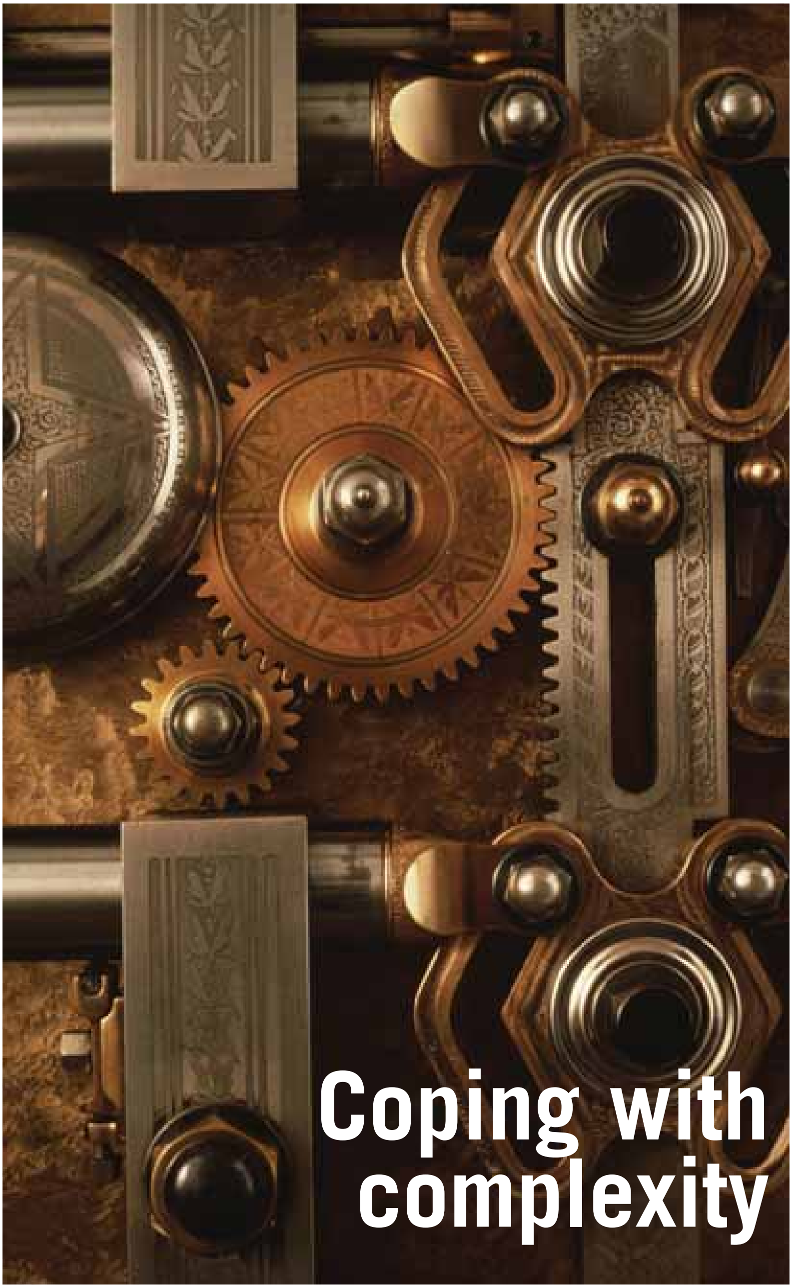
But Dublin and Ireland are facing renewed competition not only from the likes of long term rival Luxembourg, but also some of the newer jurisdictions in Eastern Europe, the Channel Islands and Malta. Can Ireland remain sufficiently competitive?

BNY Mellon's Murphy feels that Luxembourg has experienced many of the same 'saturation' issues as Dublin, while the likes of Malta can expect to have some capacity issues in establishing themselves as a rival to Ireland, says Murphy. "It has a population of 400,000 spread over several islands and does not have the same location advantages of Luxembourg, so I cannot really see it as major competition."

And while Luxembourg has its central European location as a key advantage, Ireland can count on its proximity to the UK and London, which is commonly viewed as the centre of the European hedge fund market. Thanks to the growth of shorthaul air travel, the development of the Port Tunnel in Dublin and the availability of City airport, a fund administrator can conceivably get from the IFSC to Canary Wharf inside three hours.

Unfortunately it can take longer to commute to Dublin from neighbouring Meath than it can to fly in from London. This is why it is so important that the various initiatives such as Transport 21 deliver on their promises – 2015 is currently the end goal – thus making Dublin more accessible to the rest of the country and vice versa.

Regardless of the improvements in infrastructure and the ability to exploit the rest of the country, it is vital that Ireland maintains its high standards, insists Palmer of the IFIA. He is perhaps wary of the fate that has befallen a number of football teams that invest in larger stadia with a greater capacity, only to see the team get relegated out of the big leagues. "Using the whole of Ireland as a means of increasing capacity is important, but so is the ability to keep Ireland as an attractive jurisdiction and responding to the industry's needs," says Palmer. After all, there is no point in extending Ireland's capacity if there is a decline. ■



Coping with complexity

Is it possible to price the unpricable? **Giles Turner** looks at the complex world of alternatives and the impact they have on the back office

As the hedge fund industry is burgeoning into a USD1 trillion industry, the need for an efficient back office is ever pressing. The funds themselves are busy luring back office specialists in compliance, accounting, marketing and technology away from banks and technology boutiques. New products are also springing up by the dozen. In mid-October, Merrill Lynch launched an 'outsourced, prime broker-neutral platform for various middle and back office services for the hedge fund industry'. These new developments are certainly needed, as the obsession with alpha is putting pressure on back office systems.

Exactly one year ago, Age Bakker, chief operating officer of Norwegian asset manager Storebrand Kapitalforvaltning, warned against creating a generation of "Excel professors", as the move into new alternative asset classes was forcing the back office to become dependant on manual processing techniques. Yet companies are unwilling to spend money on the back office because it remains a high cost area. According to a recent Tabb Group report, although electronic trading has created cheaper commission bills, the accompanying increase in transactions has resulted in higher back office expenses.

It is not only cost, but also complexity. Because a fund manager has to deal with an increasingly fragmented market, from dark pools to ECNs, he has to deal with a number of brokers and venues in one day, driving up the cost of trading for the clients of the fund. Matters will only get worse, as many managers will be looking to alternative asset classes after our sub-prime summer. As the volume of transactions in this area increases, so will the problem of clearing these trades.

Iain Roache, managing director, Investment Banking division, ea Consulting, explains: "A lot of the alternative asset classes are what I would call spreadsheet-based products. Anything that is bespoke is generally a spreadsheet, so basically it has a series of conditions and if those conditions match, you might receive a payment or you might not. Clearing in this case is very complex. There is a backlog already because the inputs into their various different systems cannot be homogenised. Plus if you hire someone in your operations group, they may not recognise them as being distinct. You end up with a queue in regards to offsetting the cash."

Alternative assets, if esoteric enough, can be near unpriceable. When you are trading an asset that has no observable price, you will find it hard to state where the asset traded today, what the best price was and what the worst price was. As hedge fund managers become more and more adventurous with their asset classes and modelling systems, so the back office has to try and keep pace.

David Aldrich, head of Securities Banking, Europe, at the Bank of New York Mellon, explains: "The challenge that we have is when we sit down with a manager and they say 'these are the asset classes we are going to invest in, this is our strategy, these are our volumes'. Because opportunities often arise and disappear very quickly, they will want to exploit that anomaly immediately. We have to be able to adapt and account for new instruments on a 24 hour notice; we have to be able to help them trade new markets at very short notice. If you look at the long-only world, they might take three to six months to make that move. The hedge fund managers see that as an opportunity in terms of first mover advantage. That's the challenge for us. There is no status quo."

BNY Mellon's response to the hedge fund addiction and the race for first mover advantage was to jump up the pace. In the past, third party administrators produced their clients' net asset value (NAV) on a monthly basis. As a result, a lot of work becomes concentrated around the end of the month. BNY Mellon has shifted to a daily environment, with a daily reconciliation on assets and cash to make sure that the books and records are up to date every day.

While this approach is very efficient, there may be problems dealing asset classes that are difficult to price. Ronan Daly, head of alternatives investment EMEA and Asia Pacific for Citi Global Transaction Services, states: "The two areas where you run into a bit more difficulty is, both on how you process them, and on how you price them, OTC derivatives for example. The reason why some funds can be cumbersome to process is because they can be very paper-based. They won't have common identifiers, you can get an OTC derivative where you and I literally agree the terms of deal, which is unique to you and I, and it's agreed on pieces of paper, which is backed up by swap documentation. Because they are bits of paper, you are adding a manual step that you don't get with equities or bonds. Similarly, because in the example I'm giving, which is a very bespoke, unique deal in trading, you won't be caught by the Bloomberg or the Reuters, you really have to flash your searchlight into the dark corners of very specialist pricing vendors."

Another difficult asset class that, according to Citi, is often overlooked is private equity. A significant number of hedge funds are trading pre-IPO equities, and although this is not a novel trading phenomenon, the problem arises when the fund buys a share in a company that is not listed anywhere. How do you price it?

The problem of pricing is something that should give one pause for thought. Hasn't it always been difficult to price assets? How else do people expect to make profits? Although this is a rather glib rhetorical question, it moves the problem of pricing away from the fund manager and towards the administrator. Fund managers are now listed on the stock exchange. No longer are they five old boys sitting in a small office in Mayfair. Now, hedge funds are 200 strong teams with compliance, HR and marketing departments, running a whole raft of investment strategies from plain vanilla hedge funds to 130/30 funds.

These funds need someone who can help them across the whole range of investment strategies. It is an inevitability that investment strategies are going to change, from the traditionalists investing in property to the mathematical magicians inventing ever innovative complex trading models. The problem is not that alternative investment strategies are becoming more complex and esoteric, but that hedge funds are demanding more and more from their administrators. As a result, the business itself is becoming increasingly institutional and will continue to become even more so in all its aspects.

As we have heard time and time again, if institutionalisation increases, then only the biggest will survive. Only the biggest third party administrators will be able to deal with the multitude of assets the funds are investing in. This will require the biggest accounting, custodial and risk management services for the pension funds and endowments investing in those hedge funds. The biggest prime brokers that have the broadest geographical reach, richest product offering and largest balance sheet capacity will thrive.

The past seems to point to consolidation. Most hedge fund administrators five years ago were small, privately owned companies. Almost all of these companies are now owned by large banks. Funds are also becoming extremely institutional and they like dealing with institutional counterparties, and they prefer to deal with service providers who can give them a whole raft of different solutions to different problems.

Size, it seems, matters. Yet time and time again we have been proven wrong. The growth in managing alternative assets opens up a large number of niche markets and administrators and brokers that specialise in various asset classes will pop up under the radar of the global financial servicers. Now matter how good a one stop shop the big boys offer, there will always be cracks in the market for niche third party administrators to exploit. Alternative asset classes will prove to be a challenge to third party administrators, but they will also bring a healthy dose of competition that is essential for any financial industry to perform effectively.

Anything that is bespoke is generally a spreadsheet, so basically it has a series of conditions and if those conditions match, you might receive a payment or you might not. Clearing in this case is very complex

View to 2008

Jersey and Guernsey report on the outlook for next year

Private equity success story

Since 2000, Guernsey has been growing its reputation as a leading private equity domicile. However, the events of the past few weeks and months have really crystallised the fact that the island is now the jurisdiction of choice for private equity.

The latest statistics released by the regulator, the Guernsey Financial Services Commission (GFSC), show that overall fund business in Guernsey grew by GBP8.9 billion (5.7%) in the three months to the end of September, despite significant market turbulence during the quarter. That took the total value of funds under management and administration to a new high of GBP164.5 billion – an increase of GBP44 billion (36.5%) year on year.

The value of private equity funds trebled between the end of 2002 and the end of 2006 and by the end of September this year, there were 226 such funds with a total value of GBP28.4 billion – up GBP8 billion (40%) in the first nine months of 2007 and GBP2.4 billion (9%) during the third quarter alone, in spite of the 'credit crunch'.

These impressive figures have also been backed up by third party endorsements from the likes of leading City of London lawyer, Bridget Barker of Macfarlanes. Speaking at a major Institute of Directors event on the island she asserted that Guernsey was "the jurisdiction of choice for private equity".

This was still being digested when Jon Moulton, founder and managing partner of Alchemy Partners and who now lives in Guernsey, told a local lecture lunch that the island was "a terrific place in which to do business". It is also understood that Terra Firma will soon be opening an office in the island.

These ringing endorsements come on the back of Guernsey listed fund transaction, KKR Private Equity Investors, from Kohlberg Kravis Roberts & Company, raising more than USD5 billion before being launched on Euronext Amsterdam.

Following on from KKR, there have been other notable Guernsey private equity funds, including the largest central European buyout fund – in excess of EUR1 billion – Mid Europa III; Valdivia Private Equity Fund; Energy Ventures III; AA Development Capital India Fund – a joint venture between Ashmore and Alchemy; and EQT V Limited (Clifford Chance), which raised EUR4.25 billion.

This body of evidence is just the tip of the iceberg but it clearly illustrates Guernsey's credentials as a jurisdiction of choice for private equity – the island is a private equity success story.

Peter Niven, chief executive of GuernseyFinance

Unregulated funds launch

The last couple of months have been busy and exciting for Jersey's funds industry. Months of preparation work culminated in Jersey's annual Alternative Funds Debate, held in London in October and organised by Jersey Finance and the Jersey Funds Association.

Around 150 delegates attended the event to listen to a range of speakers who led a discussion on Jersey as a leading centre for specialist fund administration services. In particular, the event unveiled plans for the latest funds development in the island – the introduction of an unregulated funds regime.

The new regime has been designed with simplicity, certainty and speed very much in mind – features that promoters and fund introducers undoubtedly look for when setting up certain types of specialist fund. A key feature of the new regime is that there will be no need to seek regulatory approval from the Jersey Financial Services Commission when establishing the fund.

Set for introduction in early 2008 following some fine tuning, the new regime includes an unregulated eligible investor category (UEIC) and an unregulated exchange traded category (UETC). Both of these are only suitable for professional and expert investors and a number of criteria are in place to ensure that this is made absolutely clear.

Amongst the key features of the UEIC is a minimum investment of USD1 million or a need to be a sophisticated investor, and its applicability to both open and closed ended funds structured using companies, unit trusts and limited partnerships. There is also no requirement for a Jersey domiciled administrator, directors, custodian or an audit.

The UETC, meanwhile, applies to closed ended funds only, again including a choice of structures, and a choice of exchanges on which a listing can be made. Similarly, there is no requirement for a Jersey domiciled administrator, directors, custodian or audit.

It is envisaged that these unregulated funds will offer fund promoters of structures aimed at high net worth individuals, sophisticated investors and institutions greater flexibility when choosing Jersey. The speed with which a product can be brought to market will also be appealing.

With specialist funds, including private equity, alternative investment and hedge funds now standing at a record GBP110 billion in Jersey, this latest development is seen as a natural, significant progression as the island attempts to widen its funds offering and establish itself as the European jurisdiction of choice for the alternative funds sector.

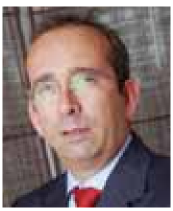
Graeme McArthur, representative of the Jersey Funds Association

Our panel of experts discusses the position of Luxembourg as an international fund domicile

ISJ PANEL DEBATE
Looking to Luxembourg

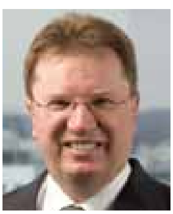
Francis Kass, Arendt & Medernach *Francis Kass is a partner in the Investment Management Practice at Arendt & Medernach, where he specialises in investment fund work, advising clients on the structuring, creation and organisation of investment funds. He has been a member of the Luxembourg Bar since 1996. He is participating in several working groups of the Luxembourg Investment Funds Association (ALFI) and he is a lecturer at the Luxembourg Institute for Training in Banking (IFBL).*

David Claus, Bank of New York Mellon *David Claus is head of sales and consultant relationships, Continental Europe, Middle East and Africa for BNY Mellon Asset Servicing. Claus runs the business development function for BNY Mellon Asset Servicing for Continental Europe, Middle East and Africa. Based in Brussels, Claus has been involved in the fund industry for the last 13 years.*



Olivier Storme, Caecis *Olivier Storme is head of business development and fund structuring with Caecis Bank Luxembourg. Prior to his current role, he was head of marketing and communication and in charge of the bank's Fund Administration network and European partnerships. Previously, Storme was general manager of Fastnet Europe, and has more than 10 years of experience in financial services activities.*

Simon Barnes, European Fund Administration *Simon Barnes is a key account, manager at European Fund Administration (EFA). The team of key account managers oversees the setting up of Luxembourg and foreign domiciled mutual funds, maintains strategic client relationships, and supports product development. Prior to this role, Barnes worked for 12 years at a major Dutch banking and insurance group, progressing through various roles within the investment funds department.*



Jean-Paul Gennari, UBS *Jean-Paul Gennari is head of Fund Services, Luxembourg and head of Operations Investment Funds, managing director, at UBS. He is responsible for the management and organisation of Fund Services in Luxembourg and a member of the Fund Services management board. He is also responsible for the daily provision of fund administration services in line with internal and external client expectations, quality standards and regulatory requirements.*

How has Luxembourg defended its position as a funds domicile, given the rise of the new contenders? What differentiates the Luxembourg market from the competition?

Kass: Luxembourg is Europe's leading investment fund centre and the leading hub for global fund distribution. This leadership position is the result of the combination of various factors such as: a very stable political and social environment; a modern, dynamic and flourishing economy; an advantageous position in the centre of Western Europe, where the major financial centres such as London, Paris, Brussels or Frankfurt can be easily reached; and a multicultural and multilingual working community.

This generally favourable environment, combined with a both flexible and robust legal and regulatory framework, a pragmatic and flexible supervisory authority, a favourable tax regime and an outstanding concentration of specialist service providers with a deep know how, is undoubtedly a major reason for the success of Luxembourg in attracting investment funds. As of today, statistics from the Commission de Surveillance du Secteur Financier (CSSF) show that as of 30 September 2007, aggregate net assets under management amounted to EUR2,059.1 billion, representing an aggregate number of 10,415 fund units.

Claus: In my opinion, Luxembourg did more than just defend its position as a fund domicile. Looking at the most recent EFAMA stats, I noticed Luxembourg doubled its asset size since the end of 2003; an impressive 98% growth rate, higher than the European industry in totality at 65%, which in turn did better than the worldwide industry at 55%. So Luxembourg has been able to increase its share of a growing pie - if you want to call that a defence, it's a pretty aggressive one.

I think the critical success factor lies in the excellent alignment between industry, supervisors and regulators to continue to create a favourable environment for the funds business to prosper. And as often happens in life, success attracts more success: the virtuous circle. This favourable environment has allowed the industry to develop and play a major role in the increasingly global world of fund distribution, which has fuelled further growth. Luxembourg is the major source of funds for global distribution, and attracts sponsors from all continents.

Storme: The combination of a regulator that is attentive to the needs of the investment community, a fund association that actively promotes the jurisdiction abroad and a group of service providers with a reputation for high quality and innovative services is key to maintaining Luxembourg's position as a funds domicile.

The regulator and the business community have a very close working relationship, so if for example, a new structure is required to help competition against a rival jurisdiction, the Association Luxembourgeoise des Fonds d'Investissement (ALFI) and its members are able to work with the CSSF to make sure new legislation is developed promptly.

The Luxembourg regulator has created a regulatory framework that is strict enough to address institutional investors' protection concerns, while remaining flexible enough to encourage continued growth and innovation in the fund industry.

The growth area of the investment fund market is alternatives, hedge funds, private equity and real estate. Luxembourg has set out to provide a favourable legislative environment, designed to attract more business and ensure the continued growth of its market.

Many of the smaller jurisdictions suffer from recruitment related issues, where they are finding it hard to recruit the skilled staff the investment fund industry requires. Luxembourg, located between Belgium, Germany and France is able to draw from a huge pool of people who have the technical and language skills the market needs.

Barnes: Luxembourg has reacted by putting in place SIF legislation, providing a product comparable to QIFs and PIFs from Ireland and Malta.

Luxembourg has a number of benefits and particularities as a domicile. The minimal investment restrictions and lighter regulation make Luxembourg one of the most attractive domiciles within Europe. A range of tax efficient structures is available. Funds are exempt from income tax and most of VAT and pay little or no capital tax, while benefiting from a large number of double taxation agreements. Luxembourg's main advantage stems from its size and maturity, producing a gamut of high quality service providers. As the world's second largest fund administration domicile after the US, it has the mass to attract all the main players in the market from the US, Europe, Asia and the rest of the world. Only in Luxembourg will you find such a concentration of specialist fund expertise. Service providers are well established and experienced in cross border distribution and related tax and regulatory issues. Luxembourg has a relative advantage in TA and distribution services for funds distributed throughout Europe. Its famously multilingual workforce is able to communicate with investors throughout Europe.

Gennari: Luxembourg has seen continued and quite impressive double digit growth over the last few years. With more than EUR2 trillion, Luxembourg has more funds and greater assets under management today than any other domicile, behind the US. This demonstrates that Luxembourg still manages to stay flexible as well as maintaining and further developing an environment that satisfies the requirements of the market for new products and services. Promoters continue to be attracted by Luxembourg's legal and fiscal environment, a unique concentration of specialist service providers, a multilingual workforce, and a strong expertise in retail distribution across the globe. ALFI has played a very important role in defending Luxembourg's position as well. As an example, 45 road shows have been organised over the last 22 months, in five continents, to promote the benefits of Luxembourg across the globe.

Competition is growing and offshore centres like Dubai and the Channel Islands are determined to grow market share. Luxembourg is aware of this and has been promoting itself in the Middle East for quite a few years. To date, over 640 Luxembourg domiciled funds are registered for distribution in Bahrain and companies are becoming increasingly familiar with the servicing of Sharia compliant funds.

Why was the Specialised Investment Fund (SIF) law introduced earlier this year and what are its aims?

Kass: One sector that over the past 10 years has seen a considerable development is the institutional investment sector. Indeed, between 1997 and 2006, the number of institutional funds has been multiplied fivefold, with an aggregate amount of assets under management of more than EUR78 billion as of 31 December 2006. On the basis of this constant development and in order to respond to the requirements of the investment funds industry, a new law on specialised investment funds (the Law on SIFs) was enacted at the beginning of this year.

As of 30 September 2007, aggregate net assets under management in Luxembourg amounted to EUR 2,059.1 billion

The Law on SIFs offers numerous advantages. Time to market is reduced and the regulatory approval of SIFs may be granted ex-post, meaning that a SIF may start its activities and file an application for approval with the month of the creation of the SIF. The scope of eligible investors has been broadened – the concept of "institutional investors" foreseen in the past has been replaced by the concept of "well informed investors", allowing sophisticated investors, including high net worth individuals, to access the flexible regime offered by SIFs. The investment purposes of SIFs may target a broad range of assets, such as transferable securities, debt instruments, money market instruments, real estate, private equity, commodities and financial derivative instruments. Furthermore, SIFs may adopt alternative investment strategies or may be created as fund of fund structures. The Law on SIFs maintains the principle of risk spreading, but does not set out any quantitative investment restrictions. A general quantitative investment restriction (a 30% rule) is only foreseen in an administrative circular, from which it may, however, be derogated on a case by case basis; SIFs may be launched by promoters that are not subject to regulatory approval.

Furthermore, there is no need for the investment managers to obtain regulatory approval. The Luxembourg supervisory authority will however examine the qualification, expertise and good repute of the directors, in order to ensure adequate investor protection.

Regarding investor information, there is no minimum content for the issuing document and no specific format required. Furthermore, the annual reports only need to disclose the most important quantitative and qualitative information permitting investors to make an informed judgment on the composition of the portfolio.

Claus: The SIF law was introduced to modernise a respectable but ageing piece of legislation, the 1991 law for institutional investor funds. It allows access to a significant range of investment strategies for a wider range of investors.

Storme: The SIF was launched to respond to the demands of the investment community for a structure that provides greater flexible to alternative strategies such as hedge funds, private equity and real estate funds. We have clients that are either just more comfortable with a European regulator or actively require one to sell their funds to institutional clients.

The SIF allows us to compete with structures in regulated and non-regulated offshore jurisdictions, as well as onshore structures such as Germany's Spezialfonds. Being able to set up a SIF fund without having to wait for formal authorisation from the CSSF allows our clients far greater responsiveness to marketing opportunities.

Barnes: This was partly a reaction to similar products in competing domiciles in Europe. The conception of the product is part of the Grand Duchy's efforts to increase the number of hedge funds domiciled and administered in Luxembourg. The SIF law enables Luxembourg to offer a structure comparable to a Cayman Islands SPC, with the advantage of an EU domicile.

Reduced regulatory requirements mean there is no need for the manager to be approved by the regulator. Other advantages include fewer regulatory reports and relatively few investment restrictions. At the same time, the SIF has same tax advantages as existing Luxembourg funds. Finally, the SIF has a fast issuing procedure – no pre-approval required before issue.

Gennari: The introduction of the SIF law in February of this year was driven by a market need for a 'lightly regulated' structure, with less stringent requirements on the promoter of a fund and a greater flexibility in terms of investment restrictions. The new SIF law significantly simplifies the setting up of fund structures and the distribution of them to 'informed investors' via private placement. Funds under SIF law will tend to be riskier, alternative types of funds, and are intended for institutional, professional and high net worth investors.

The introduction of the SIF law is a good example of the capability of the Luxembourg authorities to very quickly adapt to an upcoming demand and create the legal environment for the business development.

How has the introduction of the SIF affected the domicile and what are the main benefits for the market?

Kass: The lighter regulatory framework created by the Law on SIFs is expected, in particular, to benefit the real estate, private equity and hedge fund sectors. Indeed, the initiators of these types of funds often are small firms with a low financial surface that, under the previous regime, would not have been approved as promoters or investment managers of a retail fund. In addition, the previously outlined flexible provisions regarding the organisation, rules of functioning and eligible assets will broaden the scope of investment strategies that can be pursued within the framework of a Luxembourg fund vehicle, while at the same time limiting the regulatory or administrative requirements to be complied with.

Claus: The SIF law has given the sophisticated segment of the market a new boost. Sophisticated investors, whether institutional or private, now get access to a wider set of strategies from a wider range of product providers, in a very fast manner given the specific approval process. I think Luxembourg as a domicile has intelligently applied the 'segmentation' concept we all apply in our businesses, offering different products that cater for client types with different needs. That is a good move.

Storme: By launching the SIF, the Luxembourg regulator has demonstrated to the investment community that it is flexible, rapid and attentive to their needs. The SIF gives Luxembourg another, more flexible alternative focused structure, which should help the jurisdiction attract a more substantial amount of alternative business, while remaining the leading centre for vanilla retail funds.

We are now able to offer our clients a structure that really competes with alternative fund structures in rival jurisdictions. The SIF is an especially attractive structure for boutique promoters, many of which are currently operating out of unregulated offshore jurisdictions. The SIFs' flexibility, coupled with the security of the Luxembourg market, should see Luxembourg attract more new boutique business and may even help attract existing funds from the hedge fund powerhouse, the Cayman Islands.

Barnes: This year has seen a large increase in volumes, as Luxembourg wins business that may otherwise have gone to Cayman Island and Irish companies.

Service providers have had to adapt to the lighter regulations and use of unusual structures and products. New assets classes are possible: besides financial investments, we have seen requests for investments in wine, art and diamonds. The market is still finding new uses for the SIF: an unexpectedly large number of private banking SIFs have been set up this year, providing cost effective tax efficient investment vehicles for a family or small group of investors.

Gennari: The primary product for Luxembourg is and will be the UCITS fund. However, the market has seen an increasing need for 'lightly regulated' products for a specific group of investors. The introduction of the SIF law has now covered this need. Sponsors, who preferred Luxembourg as a domicile in the past but who may have had to launch their products in other offshore domiciles, can today realise their fund projects in Luxembourg. Since the introduction of the law on 7 February, more than 100 new funds have been launched under SIF

Have there been any negative impacts on the jurisdiction – for example, an increase in risk?

Kass: Although the legal framework within which SIFs may be set up is very flexible, it does, however, not seem that the new legislation has increased the risks in a manner that would be detrimental for the investors. Indeed, since SIFs remain subject to permanent regulatory supervision, the CSSF will ensure that there is an adequate level of investor protection. The CSSF will in particular verify the experience and reputation of the directors, the compliance with risk diversification requirements, as well as the appropriate disclosure in the issuing document of any specific risks related to each fund product.

Claus: I don't think it has negative impact on the jurisdiction along the lines you're suggesting. While these funds indeed benefit from a more flexible and lighter regulatory environment, they are also aimed at investor types that are old and wise enough to know what they are doing. The SIFs are not aimed at the general retail public, and hence there is no need to offer the same level of protection to investor types that are very different.

Storme: There are risks in allowing a fund to launch prior to being officially authorised, however, they are largely balanced out by a reduction in funds' time to market and the professionalism of the service provider, lawyer and fund promoter, which ensure that any launch dossier complies with regulations. If there is any doubt that a new fund project may not receive approval from the CSSF, a pre-check with the regulator can be made.

Barnes: Obviously, with wider investor choice comes greater risk as a wider range of products has been made available to investors. In principle, the risk to be managed by custodians is similar to that of existing funds, but as the range of instruments covered increases, custodians must adapt their processes to cover a wider range of investments. Custodians are more likely to sub-contract to specialist depositaries. They must adapt to the ensuing complex line of custody of assets. Change of work flows also brings increased operational risk.

Luxembourg has doubled its asset size since the end of 2003; an impressive 98% growth rate

Gennari: As with the introduction of any new law, the first experiences provide ideas for improvement or further precision. The SIF law did not, for example, specify any detailed investment restrictions or leverage rules. It simply stated that a SIF should apply the principle of risk diversification. This raised questions, when applied in practice.

The CSSF circular (07/309) on risk spreading in the context of specialised investment funds, dated 3 August 2007, complemented the SIF law and provided clarification on the investment restrictions that must be adhered to, in order to ensure adequate risk diversification.

From an operational point of view, we have decided at Fund Services to apply exactly the same processes and controls, as we would for the UCITS structures we administer.

Who are the main players in the fund administration and services market and why? Has this market become more competitive over time?

Kass: From a service providers' view, there is a unique concentration of specialist service providers in Luxembourg having expertise in the areas of fund administration, management and distribution. This expertise enables fund initiators to offer a wide range of investment products that can be tailored to meet the needs of specific market sectors. Given the large number of service providers in Luxembourg, fund initiators very often have the choice of appointing either Luxembourg service providers originating from the same country as the initiator, global service providers acting worldwide or smaller providers specialising on a limited number of specific fund products. Fund initiators will typically be able to compare the rates offered by multiple competitors and to choose the most cost efficient service providers, which meet their specific needs and requirements.

The lighter regulatory framework created by the Law on SIFs is expected to benefit the real estate, private equity and hedge fund sectors

Claus: Luxembourg is a competitive fund services market, and, indeed, competition has increased. This is partly due to a relative large number of fund admin providers - 74 based on Fitzrovia 2007. Interestingly, half of these players have less than USD10 billion under administration, and one may wonder if they have enough critical mass to support their business. Also, nearly half of the Luxembourg industry is in captive hands, and while that is certainly the case for smaller administrators I just mentioned, there are also a significant number of large administrators that are predominantly captive in nature. And, last but not least, there is the category of the third party service providers, like ourselves at BNY Mellon, whose core business is servicing clients that come to them without any ownership constraints, based on the competitive offering.

Storme: Although Luxembourg has many fund administrators, only the largest players are able to handle the complex processing requirements of alternative investments. This high level of complexity acts as a barrier to the smaller players.

Promoters seek a service provider that can handle their needs across the board, from fund administration to custody, foreign exchange services to securities lending, and traditional funds to sophisticated funds. Administrators with a network of local offices have a considerable advantage over those operating out of one single location. A network of offices increases infrastructure costs for the service provider, but this is outweighed by the benefits for the client in terms of proximity and understanding of their local market.

The main players are those that have the necessary size to exploit economies of scale and spread the high costs of IT development needed to automate the complex processes inherent in alternative funds.

The asset management industry has become increasingly competitive in recent years and in turn, the pressure to revise service providers' charges downward is ever present. Cost is always an important factor in the choice of service provider, however service quality and innovative products that really support the promoters' business objectives will remain the most significant factors.

Barnes: EFA is one of the main players in the fund administration services market – number one in terms of number of funds, number five in terms of assets under administration.

The market is very competitive and is becoming more so as volumes increase. This is good news for funds coming to Luxembourg, which can easily obtain competitive bids for their business.

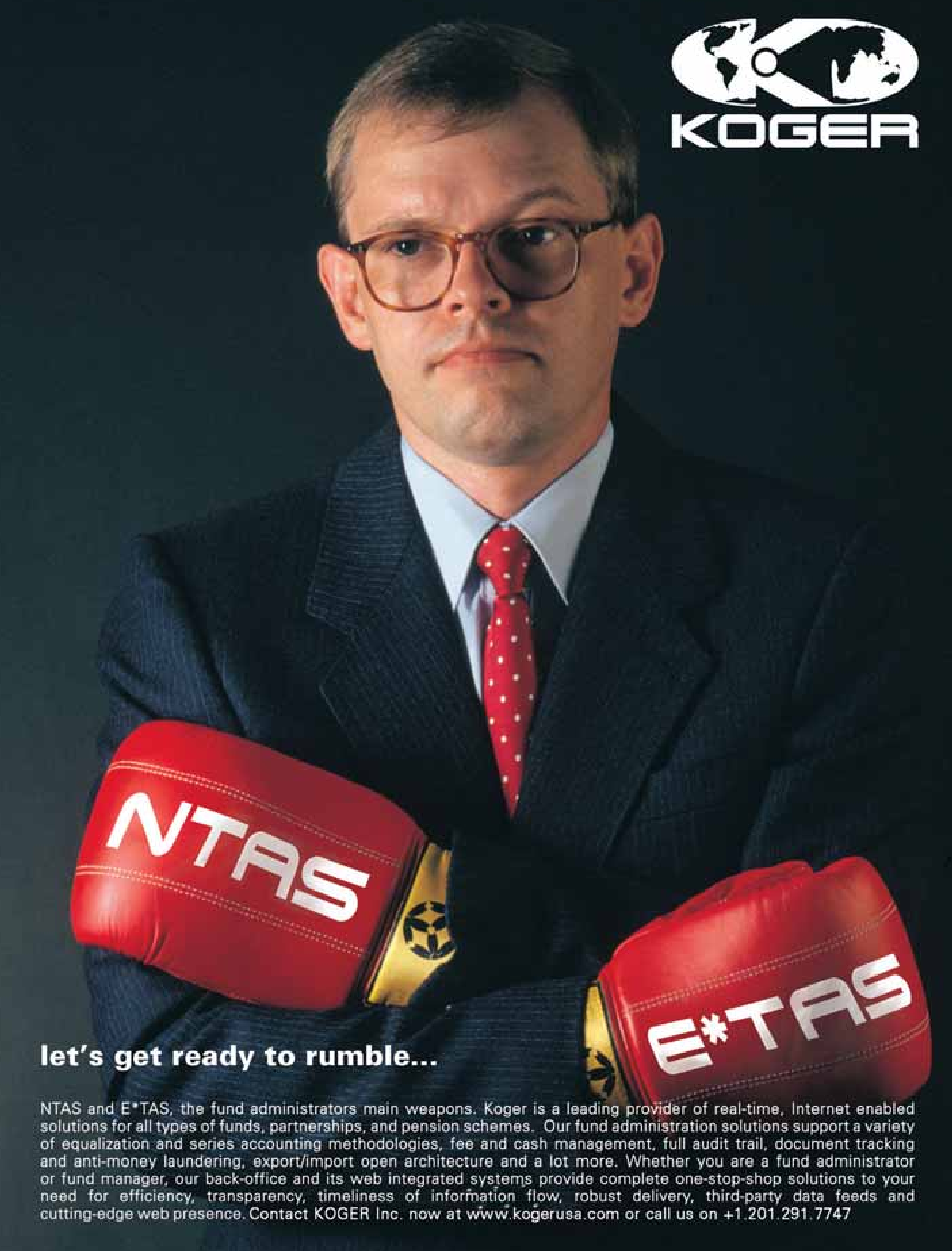
Gennari: In addition to UBS Global Asset Management – Fund Services, the largest administrators in Luxembourg include JPMorgan Bank, RBC Dexia, State Street, BNP Paribas and Brown Brothers Harriman. These are the biggest in terms of assets under administration and have a full service offering (TA, administration and custody). Fund administration requires continuous and considerable IT investment, so size does matter to a certain degree.

For traditional funds, administration has reached a high level of automation through the processing chain and an administrator has to offer more ancillary value added services in order to provide a competitive advantage. This could include be the full support in risk management or the provision of full brokerage services around the clock and in all markets.

What will drive the growth of the funds industry over the next few years in the jurisdiction? Where will the investment be coming from?

Kass: We expect that the flexibility offered by the new SIF regime will enable the Luxembourg fund industry to further increase in size over the next few years. The most recent figures show that as of 30 September 2007, 366 SIFs are in existence, totalling over EUR100 billion of assets under management. We expect that the new SIF regime will be of particular interest to the real estate, private equity and hedge fund sector. As a matter of example, the Luxembourg alternative investments market experiences a steady growth: as at 31 December 2006, total assets under management of Luxembourg domiciled single hedge funds and funds of hedge funds combined represented EUR104,464 billion, according to the ALFI annual report 2006-2007. Another driving force for the attractiveness of the Luxembourg funds industry is the fact that in the area of UCITS funds, the scope of eligible assets is constantly expanding. In this respect, building on the provisions of the Implementing Directive and CESR Guidelines on eligible assets, the CSSF's administrative practice is rapidly evolving.

Claus: In my view, as I mentioned earlier, the increasing globalisation of the funds industry will continue to drive growth. I see two main drivers here. First, funds domiciled in Luxembourg get registered and attract net new money from a growing number of countries – 75 or so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for the time being. That means Luxembourg is able to 'import' growth from places like Latin America or Asia Pacific, where economic and savings growth is faster than in the US or Europe. Second, based on that success, investment product providers keep coming to Luxembourg to domicile products they want to distribute globally. These two drivers reinforce each other – that is the virtuous circle I was alluding to earlier.

Storme: The ALFI's active promotion of Luxembourg abroad, which comprised an extended series of road shows on five continents, has contributed markedly to the jurisdiction's growth. Asia and Latin America were firmly in the scope of the ALFI delegations and we expect to see growth in fund distribution coming from there, but closer to home, there is still a massive potential in Eastern Europe.

The alternative fund industry will be the biggest growth driver. In Luxembourg, hedge funds have posted astonishing growth figures, reaching some 20% over the past six months, which show ALFI's efforts to position the Grand Duchy as a hedge fund domicile are starting to pay off. If the SIF is able to draw in more hedge fund start-ups, then Luxembourg can benefit from the growth of players that are potential giants of the hedge fund community.

Barnes: Luxembourg has been a private banking centre for many years, due to the tax efficient vehicles available to HNWI, and to the professional secrecy laws and traditions which pre-date Luxembourg's fund services industry. Hedge funds should be increasingly attracted to Luxembourg. The latest SIF regulations make it as easy to set up and run a hedge fund in Luxembourg as in the Cayman Islands. The EU domicile and double taxation agreements push the balance in Luxembourg's favour, and so we expect the rate of creation of SIF funds to stay at its present high rate for the foreseeable future.

Gennari: Alternative products continue to show very high growth rates and represent the largest number of inquiries/requests for the launch of new funds. In Luxembourg, assets in hedge funds have grown by more than 13% over the first six months of 2007 and almost 60% over the last 12 months to reach EUR77 billion in June 2007. The fund of hedge funds industry has increased by 19% over six months and 38% over 12 months to reach almost EUR110 billion in June 2007.

On the promoter side, we have started and are likely to continue to see increased interest from entities in Asia, Brazil, Russia and the Middle East. Within Fund Services, by the end of the year, we will have established a business development/client relationship management presence in Hong Kong to accommodate these developments.

Standardisation throughout the funds industry is key to growth, profitability and reduced operational risk

Is Luxembourg doing enough to promote itself as a funds centre of excellence? What more could be done?

Kass: The official representative body of the Luxembourg investment fund industry, ALFI, plays a very proactive role in making of Luxembourg the most attractive centre for fund promoters. ALFI is supporting the promotion of Luxembourg as an international fund centre, notably by helping the industry in developing new products, by participating in global economic missions, by organising road shows and financial seminars worldwide, in setting up international press relations and by organising professional training courses in collaboration with other organisations. Furthermore, the Luxembourg government and the main actors of the financial sector have created Luxembourg for Finance, an agency for the development of the financial centre, which will be active as from 1 January 2008. The objective of the agency is the development of the Luxembourg financial centre and its promotion abroad.

Claus: I would be worried if any of us answers yes to this question! Global brands require real promotion and marketing focus, and cannot purely rely on proven track record and word of mouth. I think Luxembourg as a whole has certainly stepped up to the plate in recent years, and I view those efforts, like the promotional tours to the main financial centres, similar to the recent one in Asia in conjunction with EFAMA, very favourably. It is a big step in the right direction, but the beginning of a journey, not at all the final destination.

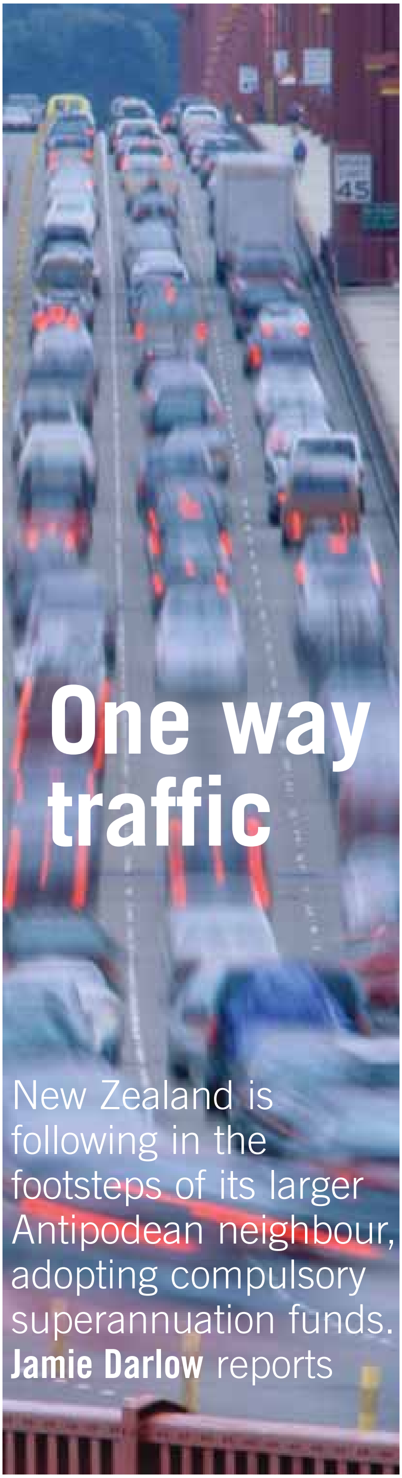
Storme: In recent years, ALFI has stepped up its promotion of Luxembourg, touring worldwide to educate markets about the Grand Duchy and its strengths as a jurisdiction. We are starting to see the fruits of ALFI's efforts reflected in the market's growth figures.

Standardisation throughout the funds industry is key to growth, profitability and reduced operational risk. Closer relationships between Luxembourg's fund association and those of other jurisdictions, such as Dublin and Caymans, can only help promote greater standardisation.

Barnes: Luxembourg has an active fund association, ALFI, which is frequently on the road in Europe and worldwide. The big players are active in marketing and promoting Luxembourg as a domicile. The financial regulator has proven itself to be effective and still relatively quick to react to changes in the environment. The challenge to Luxembourg is to maintain the momentum built up over the past years. Sourcing qualified staff appears to be a significant problem for employers.

Gennari: Luxembourg is in a comfortable position today but this certainly provides no guarantees that it will remain like this indefinitely in the future. We have to continuously evolve in order to maintain this position.

ALFI plays an important role in the promotion of Luxembourg. In addition to the 45 road shows around the world, the two annual ALFI conferences are another good platform for the promotion of Luxembourg. These conferences have seen an increasing number of visitors every year. ■



One way traffic

New Zealand is following in the footsteps of its larger Antipodean neighbour, adopting compulsory superannuation funds. **Jamie Darlow** reports

"Hang on a minute, I've just got to rescue a baby possum that's about to be killed by a cat," says David Travers, head of State Street's investor services business in Australia, as he suspends my interview with him, conducted from his car on route home from work. Possums were brought to New Zealand from Australia in 1837 and are now considered pests, their numbers verging on 70 million, but New Zealand's latest import promises to be more of a success: compulsory superannuation.

A glance at the Australian Custody Services Association's table of assets under custody, as of 30 June this year, reveals the usual array of global custody players and some domestic faces too, with very little change from previous years. True, Westpac has been replaced by HSBC after a lift-out of the Australian bank's custody services in July 2006, but otherwise there has been little change, apart from strong double digit increases in assets under management that is. A look at next year's table will reveal a different story, as Northern Trust has entered the market with a bang, scooping a AUD51 billion (USD42 billion) mandate from the Future Fund Board of Guardians.

Northern Trust won the mandate in May, the largest ever custody mandate to be awarded by an Australian institution. The Future Fund was created in 2006 by the Australian government to accumulate sufficient financial assets to offset the government's unfunded superannuation liability, which is expected to grow to over AUD140 billion by 2020. The win in Australia follows Guardians of New Zealand Superannuation's selection of Northern Trust as its custodian for the New Zealand Superannuation Fund's (NZSF) NZD11.5 billion (USD8 billion) assets. Northern Trust took custodial responsibility for the fund's assets on 1 July.

The New Zealand market, while relatively underdeveloped today, is hoping to emulate the successes of Australia over the last 15 years. The Australian market is currently the fourth largest in the world, which compares favourably with its seventeenth place in terms of GDP. "This is impressive when one considers we are a nation of 20 million people with an economy built on the back of a long property and commodities boom", says Bradley Kelly, product and strategy manager JPMorgan Worldwide Securities Services, Australia and New Zealand.

"Pension fund assets have recently exceeded AUD1 trillion, and are expected to grow to AUD1.8 trillion by 2011 and AUD3 trillion AUD by 2016, according to the Australian Finance Group, Global Funds Management Index," Kelly adds.

Australia has become the most important regional fund management centre outside Japan, with global providers choosing to run their Asia Pacific operations from the Commonwealth. Northern Trust has been the latest in a string of global players to establish a representative office in Melbourne, in the state of Victoria.

Driving the financial services sector ever onwards are the nation's compulsory superannuation funds, where mandatory contributions increased to 9% in 2002. "The favourable tax treatment of superannuation money has seen the tripling of investment fund assets since 1995, and the further simplification of tax introduced in 2006-2007 has encouraged further growth in saving for retirement and ultimately the continued expansion of Australia's superannuation funds," explains Jeremy Hester, Australia and New Zealand asset servicing sales, Northern Trust.

In contrast, Northern Trust expects the New Zealand market to double to USD100 billion by 2015, sizable growth indeed but not as exceptional as the Australian market, which is expected to triple in the same time frame. State Street's Travers explains: "The Australian market grows at a faster pace than the New Zealand market. Australia has a compulsory superannuation scheme and that fuels the size of the market, while New Zealand doesn't have a similar scheme."

The New Zealand market is much smaller than its neighbour's, with total assets of around USD50 billion, but the nation has a strong focus on saving for retirement and the market is about to dramatically change. The New Zealand government is set to introduce new legislation in April 2008 that will make contributions to the KiwiSaver scheme compulsory. The scheme is currently a voluntary savings scheme, with the government offering an initial NZD1,000 subsidy, tax relief and other incentives.

In Australia, the desire and compulsion to save money has fuelled an explosion in the fund management industry at large, explains Kelly. "The weight of money pouring into the system, coupled with a desire to continually seek new and innovative methods of investment return have fuelled the rapid rise in the number of funds and the assets within them," he says.

This weight of money has a spiralling effect as it needs to find a 'home' – which these days can be a challenge in itself, Kelly continues. "The fund management industry has responded in kind with a proliferation of products. The latest example of this is the drive by pension funds to find sources of cheap portable alpha and increase their risk adjusted returns. Trustees are leading the charge by awarding mandates in a broad range of non-traditional asset classes, including 130/30 strategies, hedge funds, infrastructure funds and private equity."

Hester says the Australian custody model is evolving in a similar fashion to the models we have seen develop on a global basis, but particularly in the US, UK and in continental Europe. "Clients in Australia have a full range of investment products in their portfolios, including alternatives, and are increasingly seeking a consolidated and fully integrated service model from a single provider – such as Northern Trust. In addition to core custody and consolidated accounting and reporting, custodians need to offer products that support alternative investments as well as more traditional value added products like risk and performance measurement, compliance monitoring and securities lending."

The hedge fund market in Australia is sizable and currently stands at around AUD35 billion, and has been experiencing growth rates of approximately 60% per annum. The weight of money Kelly spoke of is finding its way into alternative investment vehicles, the same evolution seen in the UK and Europe, where pension funds have elected to make money rather than just hold onto it. This practice is sure to be appropriated in New Zealand if the country continues to operate an increasingly global model, creating the capital to invest and welcoming the global players through which to invest it.

Global custodians have been drawn to the Australian market to take advantage of the burgeoning opportunities. National Australia Bank (NAB) and JPMorgan have the greatest presence in the master custody sector, with AUD409.6 billion and AUD342 billion respectively, as at 30 June 2007. Their dominance is primarily down to mandates from many of the largest superannuation schemes. State Street Australia and BNP Paribas also have a strong presence, but while State Street has been there since the early 1990s, BNP Paribas is a relative newcomer. And newer still is Northern Trust.

"The ability to compete is dependent on offering clients a unique and differentiated service proposition and focusing on core products with a global operating model, local client service and outstanding technology solutions," explains Hester.

Competition is fierce in the Australian market, but this is not a recent phenomenon, says JPMorgan's Kelly. "New service providers are entering the market because the Australian growth story is so compelling. We are in the incredibly fortunate position of having one of the most advanced national savings policies in the world, and as such, are regarded by many as the 'poster child' for the global pension industry; corporations recognise this, and want to be part of the story."

But Kelly warns that custodians new to the market may have over-reached themselves. "Because the Australian story is so compelling, the local market is currently over serviced. The litmus test will be the next sustained economic downturn, when many industry participants will be forced by their boards to re-examine their presence in the market," he explains. "The winners will be the global custodians who have made a strong commitment to the Australian market, and those that exit will likely be mid-tier and local market players who will find the competitive landscape extremely challenging."

Competition is set to get stronger still with the recent enactment of SuperChoice legislation, intended to help empower employees to more effectively direct their investments. Adding choice into the market has prompted pension funds to offer more comprehensive financial services, including home loans or health care, as they seek to differentiate themselves from the crowd.

JPMorgan's Kelly explains the effect SuperChoice has had on funds: "Trustees understand the economics of competition and portability, hence the central challenge they face in a post-choice environment is to provide a contemporary product offering that compares favourably with other funds in the market. Trustees now need to concern themselves with member retention and acquisition strategies and member lifetime value," he says. "As a result, marketing and brand management have become critical elements, as the battle for the 'hearts and minds' of fund members is played out. The rewards will go to the plan sponsor that 'takes a leaf' from retail banking customer relationship management approaches, and is able to tailor and intelligently apply them to the superannuation industry."

Heavy competition has also led to an increase of low cost options, such as indexed funds and premium high alpha alternatives, replacing more traditionally balanced funds. "We have noticed an increase in the prevalence of low cost products, particularly as increasing numbers of trustees pursue alpha-beta separation or core-satellite investment strategies, where the emphasis is on paying as little as possible for beta," Kelly says. "It's not yet clear if this approach is a fad, a trend, or a genuine sea change in investment management practice. Time will tell."

Both Australia and New Zealand will increase in size as custodial markets over the next decade, with New Zealand looking to adopt many of the best practices from its larger neighbour. However, it would be dangerous for market practitioners to assume the nation will follow exactly in Australia's footsteps, an offshoot with a population a fifth of Australia's size: "The New Zealand market should be considered on its own merits and, although smaller than Australasia, operates an increasingly global model," concludes the Northern Trust's Hester.

I never did find out what happened to David Travers' possum. ■

Breaking down barriers

Consolidation and aggressive M&A activity have dominated the custody market this year, explains **Jamie Darlow**

The buy-out and subsequent break-up of ABN AMRO has represented a milestone for custody servicing in Europe. It is the first time a major European bank had been divided up among its acquirers and it highlights that it is just as important for giant financial institutions to outperform, as for smaller ones.

Despite the size of the bank, one of the largest in Europe, investors had long been concerned about its lacklustre performance. ABN AMRO had set itself tough goals in 2000 to push its way into the top five of its peer group, measured on returns on investment, but this was a long way off when negotiations began in early 2007. Financial results had also proved less than impressive in 2006, with an increase in operating expenses. Acquisition was inevitable.

"The message it delivers to the marketplace is, if you are running a financial institution you have to make sure it's run efficiently, is profitable and you are performing better than your peers," explains Sebastien Danloy, global head of sales for Société Générale Securities Services (SGSS). "No one is untouchable and the only thing that can protect you is your profitability."

He points to other institutions that are now the subject of speculation regarding a buy-out – there are activist funds wondering about HSBC and questioning whether it's properly managed, Danloy says. "These hedge fund managers are questioning whether it should be broken down and split into different pieces as well. There were also recently the same comments made about Citi."

But before we get carried away, Danloy keeps his feet firmly planted on the ground, reasoning that a break-up of Citi or HSBC will probably not happen. "Would anyone have expected ABN AMRO to be broken down two years ago? The answer is no. Is it reasonable to consider HSBC and Citi could be split? You can never say never, but there would be many more hurdles to overcome," he adds.

What the biggest ever merger of banks worldwide does presage, however, is a regaining of momentum for the European banking landscape. "The remaining national banking champions - including those on the German market - are coming under increasing pressure to sharply increase their profitability or join forces with a strong partner, if they do not want to suffer a similar fate," suggests Moritz Ostwald, vice president, head of sales and relationship management at BHF Bank.

The consensus among custodians themselves is that consolidation is certain, the only question remaining is around timing and the nature of the consolidation itself. "Some say there will continue to be significant M&A activity, others have said we will see more partnerships formed," says Rowena Romulo, Securities and Fund Services branch management head for EMEA, Citi's Global Transaction Services. "At this junction there are four or five global players that have a significant market share."

Deutsche Bank was the first player to ditch its global custody business, selling to State Street at the end of January 2003. Deutsche's business was sizable, at USD2.2 trillion in assets under custody as of 31 August, 2002, but the German bank took the decision to exit the business to concentrate on sub-custody. Since then, UniCredito, HVB, RBSI, and Excel Bank have all elected to follow suit and leave the global custody space.

These institutions are following the first of three strategies for global custody in Europe, explains Danloy. Under the second, some institutions have chosen to focus on their local market and have no plans to expand, he continues. needs of individual clients," he says. This view is less than surprising, given BHF's position as a niche player, but a successful one at that. In its Custody and Derivatives Services, the bank achieved double digit growth rates for the year ending 30 June 2007 and assets under custody rose to more than EUR300 billion in the same period.

Would anyone have expected ABN AMRO to be broken down two years ago? The answer is no. Is it reasonable to consider HSBC and Citi could be split? You can never say never, but there would be many more hurdles to overcome

"The third is growing and acquiring, like Société Générale," he explains. "We acquired the UniCredito custody business, European Fund services in Luxembourg, Pioneer Investment Fund Services in Germany, all within the last two years. BNP Paribas is doing the same thing, as is HSBC but to a smaller extent. You have a few European players driving the consolidation. In the future, either you sell off or grow your business and those focusing on one or two markets will struggle in the coming years."

Citi's Romulo cautions against acquisitions for the sake of scale alone. "As long as the acquisition is the outcome of an acquirer looking to get a complementary set of capabilities or geographic presence, it will work out – it's all about synergies," she explains. "If it's purely driven by an ability to get scale, I think that's misaligned with the emerging need in the European marketplace."

Medium-sized custodians are the most likely to face consolidation because they are unable to offer the full range of custodial services the market now requires. BHF's Ostwald envisions a market where the mid-sized players are snapped up or forced out, to be replaced by larger units with economies of scale and standardised retail businesses.

"At the same time, there will remain a place for niche providers offering a few markets or products, that are more flexible, reacting more quickly to changes in the market, product innovations or the

Robert Mattsson, product development manager at Nordea Bank Securities Services, expects consolidation to continue, albeit with fewer potential cases. "But at the same time, mid-sized strong regional players still have a role to play as long as they have active product and service development," he explains. "I don't think consolidation will kill all of the mid-size strong players on a short and medium term. I see this trend also in the Nordic region and believe that in the future a few of the largest regional players will survive."

At first glance it might appear consolidation in Europe is originating from the US. Certainly, State Street's lift-out of Deutsche's global custody business began the trend, but it is really the exception to the rule. European consolidation is in fact originating from the European custodians themselves. The Bank of New York's merger with Mellon really focuses on the synergies between the US and UK, rather than continental Europe, for example.

Similarly, Citi's acquisition of Bisys in May for USD1.45 billion was not focused on entering the UK or Ireland, but on acquiring new client services for alternative asset managers. "We wanted to grow our hedge fund offering and we lacked a private equity platform, making Bisys an ideal partner for us," Romulo says. "Our rankings have gone up and we are now number four in assets under management in hedge fund services globally. We felt we had a gap and wanted to enter that space. Bisys greatly enhanced our fund of fund and mutual fund capabilities."

Citi Ireland is now ranked fifth (up from seventeenth) by Fitzrovia for funds under administration, with over USD100 billion in funds and over USD300 billion in total assets, including institutional assets, in the country.

"European players have an advantage in the European market over the US players as they understand the market better and have been there for much longer," contends SGSS's Danloy. "They have created ties with other financial institutions for a much longer period of time. European players have a better knowledge and a better fit. And in my view, we can better appreciate the cross selling opportunities when we acquire businesses in Europe."

US banks certainly have the scale to buy their way into Europe and offer a range of services thanks to economies of scale, but the European market offers particular barriers to entry. While the US is a true single market, Europe remains segmented with various legal and infrastructural barriers to entry, as well as cultural and linguistic inhibitors. A single regime in the custody business still remains a long way off, with the Giovannini barriers and the lack of standards around corporate actions just two obstacles of many to the realisation of a single market. Europe is working hard to resolve many of these problems, with MiFID opening increasing the opportunities to trade and Target2 introducing a single real time gross settlement system, but the region is not quite there yet.

Alongside this infrastructural change in Europe is a shift in the services funds now require. Securities lending is today considered a core service that most fund managers require, where only a few years ago this would have been termed a value added service. Danloy explains that risk and performance measurement is where the value added products now lie: "With MiFID and best execution we've had demand from our traditional client base (asset managers) but now also from broker-dealers, who want an independent valuation for OTC and structured products that they are buying from or selling off to customers. There's a new range of market customers in that area."

Nordea's Mattsson says value added services separate providers from each other, an area of growing importance. "But the question is what is a 'core' or a 'value added' service? Yesterday's value added service is today's core service, so with that evolution of the industry in mind, the core service will continue to be the most profitable business," he explains. "When a value added service becomes more profitable, it tends to change to a core service."

Custodians' profit margins are being put under increasing pressure when offering core services to clients because there are many institutions offering such facilities. Where margins become more attractive is through the addition of specific services to funds, something that is becoming increasingly attractive to custodians as the numbers of hedge funds swell. Danloy says hedge funds are more difficult to administer today and therefore present greater opportunity for higher margins.

"OTC products is an area with more and more demand and funds need to be serviced," adds Danloy. "All customers will be happy to pay a premium for that if you have the right quality of services. The same applies for funds looking for a one stop shop for fund distribution support services for the whole of Europe, rather than having to appoint 10 or 15 local providers."

This rationale explains why global custodians are consolidating in Europe – there's a certain level of fees under which it becomes unprofitable to do business, meaning those larger custodians with scale can force out mid-sized institutions. At the same time, the larger institutions can service funds looking for one single custodian, and can service hedge funds and those with particular requirements; the niche market. They have all their bases covered.

Of course this doesn't mean the larger institutions don't need to compete - far from it. BHF's Ostwald explains that the more complex the product, the greater the clients' requirements become. "This is very much the case in the fund segment, where the trend has been quite impressive in recent years," he says. "Accordingly, custodians are developing innovative products to meet these new requirements. This is the only way that we custodians can hold our own when competing for clients. Let's face it, yesterday's 'state of the art' is today's 'plain vanilla'."

The latest battleground to emerge for custodians is Eastern Europe, with the top banks jostling for position to enter the market and get their services in place. In truth, the top five custody banks have been investing in the region for a number of years, but with MiFID and harmonisation initiatives, the market potential can only increase.

Already, SGSS considers Eastern Europe the most important region for growth, according to Danloy, and has invested accordingly. Danloy points to the region as key for the bank, which has been active in acquiring businesses and banks in the area over the last few years. "We have a strong presence in a lot of countries and overall we are the second largest foreign investor in the financial industry in Eastern Europe," he says.

SGSS has acquired banks with a small, medium or large custody operation across Europe and is currently packaging all the offers from the different countries into one. "Until now we weren't actively setting this, but we are now restructuring in that region. We see that as the most important region for growth in coming years. Russia is very important to us too," says Danloy.

The largest foreign investor in the region is Citi, which has a direct custody and clearing presence in the Czech Republic, Hungary, Poland, Romania, Russia and Slovakia. Russia is a very important franchise, growing very rapidly and Citi is investing there also, Romulo says. "Overall, across Central and Eastern Europe (CEE) we have seen significant growth in our transaction volumes and assets under custody," she explains. Between 2004 and 2006 the bank experienced considerable growth in terms of assets under custody and transaction volumes in the region, with Russia in particular standing out with triple figure percentage growth. The more established markets have increased at a slower rate, but still feature double digit growth rates.

With the exception of Poland, where Citi gained a presence through acquisition, the increases are primarily through organic growth and a result of new client activity, Romulo says. "We are expecting further growth in Russia and throughout CEE, although these markets are maturing and not really emerging anymore, as they are increasingly aligning with the European standards."

Perhaps the most surprising element of the ABN AMRO buyout was that the consortium was able to raise capital at a time when it was hardest to find. What clinched the deal for RBS was that it could offer a higher a price, while Barclays was simply unable to borrow any more than it already had, Barclays chief executive John Varley's comments that RBS had paid too much notwithstanding. The European custody market will see greater consolidation in 2008, the ABN AMRO deal is an augur of things to come. ■

Regulatory review

The EU's Markets in Financial Instruments Directive (MiFID) came into effect on 1 November with very little fanfare, as most had predicted. What are the long term consequences for the European custody market from MiFID and from other regulations, such as Basel II?

Nordea's Mattsson says MiFID and other regulations will put pressure on moving the market to be more dependent on size. "In order to keep up and be able to cope with increasing regulations, you need the benefits of a big organisation. However, I believe that regulations could bring business opportunities for small focused business providers."

SGSS's Danloy suggests that regulation will cause both market fragmentation and consolidation, but in different spaces. "Whoever can achieve high liquidity levels will be the winner of tomorrow. Today, Target2-Securities is the means to consolidate post-trade information in Europe, while MiFID might cause more fragmentation of post-trade and trading activity."

BHF's Ostwald says Basel II is the first step in introducing heterogeneous market practices. "It will inevitably lead to custody providers moving closer together, rather like the step away from networks of local banks towards regional and global custodians in the past. The growing pressure on global custodians to consolidate is now the next step in this process."

In bloom?

Will Greek funds blossom under regulatory changes and opportunities? Asks **Jamie Darlow**

A USD300 million pipeline connecting Greece and Turkey opened in November, linking the rich natural gas fields in the Caspian Sea region to Europe and drawing the Hellenic Republic closer to its neighbours. Greece's physical infrastructural improvements have matched an overhaul to the financial services industry and the regulations that govern it.

The Greek financial market has grown in size in recent years. Trading volumes have risen from an average daily turnover of EUR140 million in 2004, to EUR210 million in 2005, EUR342 million in 2006 and EUR468 million so far this year. International investors' participation in the market is strong; non-domestic investors currently own 52% of the total Athens Exchange market capital and in the largest capital stocks (FTSE/ATHEX 20) their participation exceeded 57% during September 2007. Most of the total daily trading activity by value is made by foreign institutions (60%) and net inflows into the market from abroad approached EUR16 billion last year.

This growth must be, in part, attributed to legal and regulatory changes. Full deregulation has now allowed the stock exchange, held by the Hellenic Exchange Group (HELEX), to become fully dispossessed from its administrative competency and is now allowed to create its business objectives.

Panagiots Papapetrou, managing director of Société Générale Securities Services (SGSS) in Greece, says 2006 was a key year for the HELEX group as the common trading platform between the Athens Exchange and the Cyprus Stock Exchange was finally launched. "That was a 'big bang' for the region and especially for the Cypriot market as within the first four months of the common platform operation, daily turnover and market capital had a multiple impact, while foreign investors' participation increased from 3.6% to 6.5%."

While the common platform has been a success in linking Greece and Cyprus, foreign participation of 6.5% can hardly be termed vast. "As for remote members, the regulatory framework is there but unfortunately we have no participants yet," explains Alexios Kartalis, general manager of the Athens Branch of BNP Paribas Securities Services. "This was mainly due to the heavy requirements for participating in the guarantee fund."

In Greece the guarantee fund exists to support a permanent default in the market. The rule was that each new member of the exchange had to contribute EUR3 million upfront to the fund, a substantial cash amount for some to enter the Greek market, says Kartalis. "Some Cypriot brokers have become members of the Hellenic Exchange. These brokers did not wish to pay the EUR3 million, since they were already participating in a similar fund in Cyprus," he continues. The Capital Markets Commission, which has overall responsibility, took a relaxed approach and agreed to exempt them if they participated in a similar fund in another country.

"From what we are hearing, it's highly possible that if, for example, a London-based broker or a Paris-based one will apply for participation, they could possibly be exempt," Kartalis explains.

And now Société Générale in Paris is about to become that first remote member in the local market, Papapetrou says. "Most likely we will be the first foreign institution to hold this status. SGSS Athens will provide clearing services to them via a newly created section that is fully equipped and manned to serve all necessary needs, including regulatory tasks. This is actually a new service of SGSS Athens that will also be promoted to external (international) clients and prospectives."

Opening up Greece to external investors may provide growth for the subdued Greek fund market. Greek funds are not growing as expected, explains Kartalis. Last year they were at a stable level of EUR25-30 billion, he says, but there is potential for growth, especially from new tools like fund of funds.

Greece should become an increasingly attractive place in which to invest over the coming year, Kartalis says. "The major thing happening in Greece over the next six to 10 months is the liberalisation of OTC. It's going to be live as of 15 January. We are talking about a huge change in the market – we have clients who say they will switch the majority of their activity from the exchange to OTC activity," he explains.

There will also be a further liberalisation of the lending activity, which at present is extremely restrictive for securities borrowing and lending and is currently conducted through the derivatives exchange, Kartalis adds.

Whether this liberalisation and regulatory shake-up will be enough to encourage fund growth remains to be seen. Following the stock market crash of 1999 and 2000, equity and balanced funds suffered heavy losses, explains Papapetrou. "The investment public stopped recognising the 'expertise' of the asset management companies. It also believed that as the market approaches new highs, it is expected a large number of the '2000 trapped retail investors' will liquidate their investments to 'get their capital back'."

On the other hand, the adoption of the UCITS III directive in the local regulatory environment and the new products that have been introduced, such as fund of funds, have been welcomed by investors, Papapetrou says. This may spur domestic growth to match the ambitions of the Greek asset servicing industry. ■

Moving on

An evolution is happening in the area of performance measurement, argues **Fabien Buliard**

The world of performance measurement – assessing the performance of a given portfolio – and attribution – figuring out how that performance was achieved – is evolving. This evolution is being driven by the growing diversity and complexity of financial instruments, mounting requirements for transparency, and higher expectations from asset managers and clients. Becoming ever more sophisticated, performance and attribution tools are adapting to the proliferation of new asset classes, growing demand for outsourced services, and a soaring appetite for risk measurement.

Over the years, performance measurement requirements have progressed toward more frequent reporting, from quarterly or monthly measurement to daily measurement, and an increased level of detail and depth of the information provided. "Another thing we are seeing is greater demand for accuracy," says Fraser Priestley, managing director, Performance and Risk Analytics at BNY Mellon Asset Servicing. "For example, if you wanted to calculate a true rate of return that is 100% accurate, you would have to value the assets every single time a cash flow occurs, but that clearly isn't practical. However, we have seen for some time now the requirement to have market values when major cash flows occur."

For Jem Tugwell, managing director Asset Management Products at Odyssey Financial Technologies, changes in performance requirements are being driven by demands from the investment process. "One of them is that a lot of funds are now being run on a strategy basis, where the same security is being held for different reasons," he explains. "The performance and attribution needs to work that way as well, and support the concept of modelling on a strategy. The system has got to cope with the same security turning up as lots of little holdings, so it involves a fundamental design change in how that data is represented in the database and how you handle it."

Vendors also see a growing need for a flexible approach and the ability to adapt to an asset manager's process. Mark Elliott, director of Performance and Attribution Solutions at SS&C Technologies, feels that as people become more familiar with what attribution does, they are looking to customise it to meet their own investment process and really pinpoint decisions they are making and measure them. "We have traditionally been in the 'long only' asset manager space and we are now seeing that a large proportion of our client base is expanding into long-short strategies," Elliott adds. "That requires additional analysis on the attribution to separate the long from the short positions to attribute the success of that type of strategy."

One major challenge for the performance and attribution market has been the need to keep up with the constant flow of new asset classes, particularly derivatives, to reflect them accurately in the portfolio assessment. The pace of innovation can be especially difficult for vendors to sustain because, as Matt Nelson, senior analyst in the Securities and Investments research service at TowerGroup, points out, they tend to be constrained to their usual release cycles, which may deliver quarterly or twice a year.

For Tugwell, the difficulty stems from the pricing and analytics of derivatives, but he believes that a vendor's ability to cope depends on where its attribution offering originated. "Because we are predominantly a front office vendor with modelling systems that can price all the derivatives and calculate the analytics of them, it is easier for us than for software companies that have a more classical performance measurement background, where the return is effectively the difference between two prices," he explains. "With derivatives, you have to know much more about the asset and how it works. When you look at attribution for derivatives, each derivative will have different sensitivities and you have to have a model that can measure and separate each of them."

Fixed income attribution has been a major challenge for the industry, given the wide range of instruments being used and the inadequacy of models traditionally used for equity attribution, requiring a more tailored approach. "In the past, the tools and analytics necessary to start creating fixed income attribution were not readily available," says Tim Miller, European director, SunGard Asset Arena. "Besides, it is not as defined a science as equity attribution where the methodology is fairly standard. A couple of vendors have tried tackling fixed income attribution, but they haven't really come out with suitable models."

Miller says SunGard has been working with clients to understand their exact expectations from a fixed income attribution model. However, one of the main issues is to get the bond manager to buy into a third party source producing their attribution in the same way equity managers have, he says. "For equity managers, there has been a fairly good acceptance of the performance team," he explains. "In the fixed income area, there is more reluctance to let go. It is not always as easy to define a model for the investment process and it is therefore not as easy to quantify. It is really up to the software provider to deliver the right tools so that the performance teams can gain the confidence of portfolio managers."

SunGard is seeing a lot of interest around fixed income derivatives, with clients and prospects shifting from futures and forwards to instruments such as interest rate swaps and credit default swaps. "They want to know how to handle these types of instruments within our system," Miller says. "The main issue around this is that it can be really difficult to get the data required out of the accounting systems. A lot of times, in the performance world, you are limited by the data supplied to you. With some of these more complex instruments, it is really difficult for the performance system to fill in the data that is missing from the accounting system because they are generally over the counter rather than exchange traded."

Another growing trend is the development of outsourcing for part or all of a firm's performance function. Building on the existing tendency to outsource back office services, performance services transferred to third party providers tend to focus more on regulatory or simple client reporting, while more advanced assessments continue to be conducted internally.

SS&C's Elliott separates the performance function into two categories: the production side - with portfolio validation, getting the data into the system, reconciling numbers and monitoring exception - and the analysis itself. "You need to have intimate knowledge of the investment management process to be able to explain those performance results and add value, so most firms want to keep that analysis piece within their shop, but are completely prepared to outsource the production part," he says. "Technology and web-based delivery have evolved to a point where you can outsource the back office performance function, yet still leave the middle and front office function within the firm."

According to TowerGroup's Nelson, the attribution function is potentially more difficult to outsource than performance measurement itself. "It is very custom and very specific to portfolio managers themselves, and what he or she wants to look at and dissect within the portfolio," he says. "So I think that has typically been more of an in-house service. But the connectivity between performance and attribution is so tight and you are seeing vendors progress to the point where outsourced services are more and more compelling offerings."

While he admits that asset managers have different feelings as to what can be outsourced and what can't, BNY Mellon's Priestley considers there are huge advantages to having a wide ranging outsourcing deal. "If a client (already) takes custody and investment accounting, it makes perfect sense for them to take their performance from the same supplier, because the data is all in one place," he explains. "We have an integrated system, so there is no one having to manipulate data to make it fit into the performance system." He sees the outsourcing trend continuing to grow but at a relatively modest pace, as asset managers continue to put their toe in the water and test it out.

The complexity of a portfolio or strategy can constitute a potential hurdle to outsourcing. Carl Bacon, chairman of portfolio analytics provider Statpro, considers that more straightforward, simpler assets are better suited for outsourcing than more complex instruments, which require a deep understanding of the investment process. "The more complex your investment process, the more complex the tools you are using for that analysis," he explains. "And for those who are outsourced, that analysis is probably going to have to take place in the front office in the portfolio manager's systems. I don't think you can outsource that very detailed analysis, because you have to be close to the investment decision process to understand what is happening."

Over the years, performance measurement requirements have progressed toward more frequent reporting, from quarterly or monthly measurement to daily measurement

At the other end of the spectrum, some investment firms and large institutions might still turn to in-house development for their performance and attribution applications, which originally tended to be developed internally. But as Tugwell explains, only those firms wanting to protect their investment strategy would continue to resort to that kind of challenging endeavour.

"Writing software in-house is a significant undertaking," he says. "I think you would need to have a very different and proprietary investment process to make it seem worthwhile. However, the ongoing commitment of development resources in maintaining the model over time is easy to underestimate when starting a build project. Along with the model, you also need to build the checks and balances and data quality processes that vendors packages provide."

Changes in the approach to performance measurement are also being driven by regulation, as well as the development of voluntary industry standards, such as the Global Investment Performance Standards (GIPS). "To a certain degree, those standards have increased the professionalism of performance measurers," says Statpro's Bacon. "To be GIPS compliant these days, you have to have written policies and procedures, a consistent way of valuing instruments and assets, which is incredibly important, keeping in mind events of the last few months. You have to present your information in a certain way, with a number of set disclosures. These have been big challenges for performance measurers."

One major challenge for the market has been the need to keep up with the constant flow of new asset classes

Regulation itself, whether it is local or EU-wide like UCITS III, increasingly mandates the inclusion of forward looking risk measurement in client reporting. Philippe Carrel, executive vice president and global head of business development, Reuters Trade and Risk Management, considers that a directive like MiFID will oblige participants to rethink the professional/client relationship, and that risk weighted performance management should generalise in the aftermath of MiFID.

More generally, Carrel is witnessing an evolution of performance measurement tools toward risk adjusted performance measurement. "It has become critical to read return and benchmark reports in the context of compliance to predefined risk profiles," he says.

As a result of those trends, the performance and attribution space is showing increasing convergence with the risk function within firms. While on the vendor side, the inclusion of risk measurement capabilities into software packages is becoming more common. "We have seen convergence with a number of our clients who have gone through organisational structure changes, combining the head of performance with the head of risk," Elliott says. "For us, it makes logical sense because if you think about the whole investment management cycle, the last stage is measuring and communicating your performance, but then the following step is turning around and looking at what is going to happen in the next period."

He continues: "They are very closely aligned and we have done a number of things to address that situation. For example, we have integrated ex-ante risk reporting into the application, through a partnership with a major risk provider."

Elliott sees the trend towards a combination of the two functions as a good sign for performance measurement in general. This is largely because it means it is moving out of the back and middle office, into the front office.

Several specialists insist on the importance of consistency between the performance and attribution models and the risk decomposition model. "If you attribute returns to certain factors, you should attribute the risk to those factors as well," Bacon says.

The field of predictive (or ex-ante) risk analysis is particularly promising, as it complements performance measurement tools, which analyse a portfolio from a post-trade angle. "For many, risk analysis is nothing more than looking at the past and seeing how you performed," says Gregg Berman, co-head of Risk Business at risk management specialist RiskMetrics. "That is why risk and performance attribution tend to go together and sometimes actually get confused. Performance attribution is not predictive. It looks at what, within your strategy, drove your performance over a given period. It explains what you just went through, but it doesn't tell you what it's going to be in the future."

Predictive risk addresses the way the market can affect the positions held in a portfolio, looking at the various risk factors driving the underlying instruments, such as spreads, individual equity prices, volatility surfaces, or basis curves. "We do a bottom up approach, analysing each position, the correlation of positions between them, until we build a complete view by strategy, by sector, by currency, by region, by portfolio, and ultimately, by firm," Berman continues. "If the firm has a few hundred thousand positions, you can imagine it is a pretty large calculation."

Looking back at the recent market turmoil triggered by the US sub-prime crisis, Berman considers that the tools were in place to anticipate the risk, but that they were not being used properly. "This is a case of people putting more money into a bunch of instruments than might have been prudent without considering the circumstances," he explains. "This wasn't a matter of fancy formulae. It was just a matter of stress testing. Assuming those defaults would never happen was probably not a good assumption to base your portfolio on."

Berman considers that these types of market events will accentuate an existing strong trend towards a more frequent use of pre-trade risk analysis. "However, that is at odds with strategies that trade more and more frequently," he warns. "When making money is based on your ability to get in and out faster than anybody else, you don't necessarily have the time to know what you are buying."

While it may not drastically fuel the demand for risk analytics, the credit crisis and the market volatility that followed could see the demand for attribution tools rise, as investors seek to understand the sources of return in their portfolio, but also their sources of loss. "The main impact of this credit crisis has been an increased demand for performance and attribution tools," Elliott says. "When times are good, attribution is less important and clients don't ask as many questions. But when the markets turn, people are more keen to understand performance. There is an inverse relationship between market performance and demand for attribution systems."

Bacon agrees: "While attribution analysis is not a particularly predictive tool, it will certainly give you a good understanding about where you've lost the value, why your return is negative and which parts of your portfolio are exposed. It is especially good for articulating that explanation to clients. When you have the attribution tool in line with the investment decision process, you can explain it and keep the confidence of your client." In light of this, it seems that performance measurement is likely to be an area of focus for some time to come. ■

Pressure points

The current tumultuous financial environment has meant a greater focus on the bottom line and, combined with greater demands from their corporate customers, banks are feeling the squeeze. **Virginie O'Shea** reports

The treasury services industry is experiencing a period of great flux as its customers' requirements change and margins from payments operations significantly tighten. Corporates are under pressure to focus on the bottom line and as a result are transforming their operational models and rationalising the number of service providers they use to realise cost savings. The increased focus on risk against the background of wider market turmoil has meant that these corporates have prioritised the requirement for control over the management of cash and liquidity. After all, it is a logical choice to opt to see where the risk exposures lie and attempt to rectify them, rather than continue on in blissful ignorance.

Whenever the market is in turmoil, rates are more volatile and that situation creates challenges for treasurers, says Nancy Atkinson, senior analyst at Aite Group. Borrowing rates increase, making good management of working capital even more important. The better the cash flows are managed across corporate enterprises, the less borrowing is required. On the investment side, to the degree that capital needs are accurately forecasted for longer periods of time, higher investment rates can be achieved, she explains.

As Tim Martin, senior product manager, Cash Management, at STP technology vendor SmartStream, highlights, risk, and particularly operational risk, has now become a key project driver. "It is now becoming clear that all business processes must have control components incorporated with metrics included to determine exposure, risks and potential losses. The adage that a process cannot be improved until it can be measured, is being applied to treasury management," he elaborates.

These challenges can be more efficiently tackled with the assistance of the corporates' banks, contends Maurice Cleaves, regional product management head for EMEA, Cash Management, Deutsche Bank. "As with any credit squeeze, there tends to be a flight to quality and a tightening of liquidity impacting all sectors of the market. This would make it less likely that credit extensions would be available and limits will be scrutinised more closely than they would be under normal conditions. It is important in these times for corporate clients to have flexibility around the funding that they are able to obtain and there would tend to be a heavier reliance on their banks for this funding, as the market for short term funding – particularly the commercial paper market – becomes much tighter," he explains.

The treasurer is also no longer merely the keeper of a company's coffers – it has become a much more strategic role. As a result, treasurers have been gradually taking on responsibility for a whole gamut of functions that would traditionally lie outside the remit of the role, such as corporate financing, tax and investor relations. The impact of this evolution has been that companies now expect treasurers to have a broader understanding and knowledge of their financial position and strategic direction. This also involves their documented and reported accountability for the liquidity of the enterprise and the audit trail of decision taking that is tied to accounting best practices and regulatory requirements such as Sarbanes Oxley.

"This change is moving at a different pace in the treasury departments but it is fair to say that the treasurer is having to cope with a more diverse range of activities and therefore looks to gain efficiencies out of current traditional activities to free up capacity for this additional workload. As a result, the treasurer is also getting a broader view across the corporate business, which in turn makes him far more able to make decisions cross a broader span of control, allowing a better integration of the full business with their partners, for example the cash management bank," says Cleaves.

As a result of these changes, the need for actionable data from many other financial functions is even more critical. "Access to timely and accurate internal greater amounts of information are generated and are available in a timelier manner. For treasurers, information is the key to their ability to make decisions, so better and more timely data is a huge help, she explains.

These changes on the corporate side essentially mean that banks need to step up their game. Although some banks are sufficiently meeting their clients' needs today, this may not hold true for the next year or so. A major issue is that corporate clients are more demanding in terms of services needed, while still wanting to contain pricing, says Atkinson. In such an environment, it is difficult for banks to invest in innovation with little assurance that their innovations will be adopted. "A few global banks have developed solutions that most likely exceed the current demands of corporate clients, especially

To effectively do their jobs, treasurers need information from many different organisational units and external sources and, currently, no single tool provides all of that information

and external data is more important than ever before," says Atkinson. They have also introduced a level of caution around trading in derivatives products and more speculative investment instruments, adds Richard Spong, solutions marketing manager, Financial Services, EMEA at payments systems vendor Sterling Commerce.

However, according to Philippe Carrel, executive vice president and global head of business development, Reuters Trade and Risk Management, investment in systems specific to derivatives is unlikely in the near future. "Corporate treasurers and boards have typically been averse to financial operations outside the core business of their firm. Hence any treasury system able to manage portfolios, derivatives or investments would be seen as either unnecessary or even a dangerous toy to play with. In these conditions, few treasurers endeavoured to campaign for treasury systems beyond bare cash management functions," he explains.

The focus on operational risk has led to more investment in tracking, monitoring and reporting of operational processes, adds Atkinson. From those activities, with regard to Single Euro Payments Area (SEPA) solutions in the European Union. Speculative development is difficult to support with markets that expect quarter to quarter returns," she explains.

The introduction of SEPA is therefore more than just a technical issue for the industry – it is a cultural issue also. On a purely technical basis, a large number of vendors and banks appear to already be fairly well prepared, but there continues to be some scepticism about whether corporates and public institutions will actually buy in to the concept. For example, there appears to be no great incentive for these parties to switch to the ISO 20022 SEPA format. Joergen Jensen, director of product management at treasury management systems vendor Wall Street Systems, feels that this problem will be a major sticking point for SEPA: "We don't see many corporates rushing to start using this format at the moment. There is generally no immediate benefit to the corporate from changing to this format. It will probably only be done as part of other projects such as an upgrade or the implementation of a new system."

Another potential sticking point is the use of international bank account numbers (IBANs) and bank identifier codes (BICs). There is currently no universal process for converting from old legacy bank account numbers to IBANs and BICs. In some countries there are system providers and banks that offer this service but this only applies to certain regions. For some corporates, a major resource investment will need to be made to collect IBAN and BIC codes and update their records with this information. Furthermore, the delay in the direct debit directive has also lead to uncertainty, which means that corporates are less inclined to start any SEPA related projects until they have a clearer view of how this will be resolved. All of this means that SEPA has yet to have any major impact on the treasury business as a whole, says Jensen.

The real debate here is whether SEPA and the Faster Payments initiative in the UK are compliance requirements or catalysts for change in the cash management business, says Deutsche Bank's Cleaves. "Both will certainly alter the way that the payments business is operated with advantages to be gained for customers in retail banking and the treasury departments of corporate customers. If you take this along with changes in the card markets due to SEPA, the reforms in the cheque rules in the UK and infrastructure projects such as those being introduced by industry counterparties including Voca in the UK and SIT/STET in France, it can be seen that the payments infrastructure landscape is going through more change than has been seen for a number of years," he explains. "There will certainly be winners and losers in this evolving environment and it will be important that those that operate in the treasury space align themselves with a cash management bank that has a strong franchise and appetite to be a leader in the future."

There are also a number of clear areas where improvements need to be made in the corporate supply chain. Corporate to corporate interfaces in payments, trade finance, and cash management remain paper intensive and this would be a logical area in which banks could extend their value added services. Opportunities also exist to further facilitate the conversion of paper to electronic formats, says Atkinson: "Once this data is converted to an electronic format, it may be collected, manipulated, and analysed, and actionable reports may be produced."

To effectively do their jobs, treasurers need information from many different organisational units and external sources and, currently, no single tool provides all of that information. This is generally where our old friend the Excel spreadsheet comes into play. Treasurers pull information from multiple systems into Excel and manipulate it from there – with all the associated risks inherent in using a rather static and error prone system.

The primary reason for a lack of management buy in has been that a treasury department has typically been seen as a cost centre and not a profit centre, explains Cleaves. "Making the business case to invest in a highly complex treasury system would need to have significant savings to justify the investment and this has not always been possible, particularly at a mid-corporate level," he says.

However, there may be two areas of development that could alter that perception: the increased level of corporate regulation and the move to globalisation. "For a multinational corporate to take advantage of the services that a treasury management system could offer, they could now be driven by the need for more efficient information gathering; a need brought about by such regulation to improve corporate governance. In the move to globalisation, we see the growth of the corporate customer through mergers and acquisition or through expansion into new countries and markets. In order to make this change efficiently, a move towards a payment factory or centralised treasury function becomes more widespread, bringing with it the possibility to harmonise processes across the enterprise, where the return on the investment in a treasury management system may look more attractive," Cleaves continues.

Colin Day, vice president, Market Insights, SunGard AvantGard, Bancware and SteP, feels that despite the current low priority status of treasury management systems, the treasury function is often boosted by the quality of the staff in the area. He also seconds the notion that increasing regulation and oversight is forcing the culture to gradually change. "In addition, increased remits of treasury departments are forcing automation and improved productivity levels which necessitates better systems," he adds.

Process harmonisation need not necessarily involve investments in brand new systems. Many corporations with installed enterprise resource planning (ERP) systems want to leverage those systems and implement the treasury portion, according to Atkinson. "Treasury was not an initial driver for ERP implementation, so few of those modules are installed. With full implementation, internal data can be automatically collected for treasurers and fed into treasury workstations for further analysis and action. Still missing is the external data. Banks and technology vendors are trying to assist with the provision of this data through proprietary CPU to CPU feeds, online portals and report generation," she says.

The increased move towards globalisation and the trend for corporate customers to expand into new markets is good news for banks, adds Cleaves. "The corporate will often look to their trusted cash management provider to assist in opening up these new markets in their quest to be able to succeed in their own sphere of business," he says. Moreover, standardisation is a key driver in the market and technology investment is an integral part of being able to take the costs out of processes, both at the corporate and the bank level of operations, especially across markets.

"Some of this manifests itself in industry initiatives, some through regulatory change and some through innovation in discrete market segments. The consistent theme in all of this is that there needs to be investment to enable the efficiency gains to be made over time and if there is anywhere that there could be improvement, it would be that there is a common understanding and widespread agreement throughout the whole community about the new market standards going forward to enable this investment in change to be done in the most efficient manner," explains Cleaves.

SunGard's Day feels that it is not just the corporates that need to focus on systems improvement: "Most banks have systems that were simply not designed to meet the needs of today's changing demands, such as within the changing landscape of payments and the need for SEPA solutions. Changing these systems is often slow and expensive. Banks have a myriad of different systems that a client needs to access but are internally siloed. These barriers are coming down and are an area for potential improvement. The challenge will be to listen to the customers and deliver the right services with new technology in an efficient timely fashion."

This increasingly competitive environment is likely to result in a certain amount of consolidation among the banks servicing the treasury sector

The corporate voice is one that banks must heed, adds Jacob Jegher, senior analyst at Celent. Corporations are the ones driving demand for many bank services and they have particular needs in mind. Banks must follow their lead and make sure that they can offer the appropriate services to their most valued clients. It is quite difficult to build customer loyalty in the banking industry, so banks really have to go the extra mile and work on customer service and satisfaction, he explains.

This increasingly competitive environment is likely to result in a certain amount of consolidation among the banks servicing the treasury sector. Currently, 90-100 banks provide 85% of services for corporate transactions and the market is pretty fragmented, says Cleaves. "It is likely that there will be a move towards consolidation in the hunt for efficiency driven by bank mergers, corporate mergers, more outsourced services and consolidation of the clearing systems and increased use of technology, standards and automation to gain these efficiencies," he concludes. ■

Close-up focus

Did FIMA 2007 bring data management to the attention of the board? **Jamie Darlow** reports

Former UK Defence Secretary and Lady Thatcher's lackey Michael Portillo warned of the dangers of losing touch with your own organisation at this year's Financial Information Management conference (FIMA), where he was guest speaker. In a witty and well received speech, Portillo recounted Thatcher's last days in power, when she had lost the support of her party and become isolated from it – something FIMA delegates need to be wary of as their data projects increase in importance and scope.

More than 350 delegates attended FIMA last year and higher numbers in 2007 prompted the organisers to shift the event to larger premises, at London Olympia. Over 460 delegates came this time, of which 230 were from leading investment banks and other financial institutions. Just as the conference has turned its back on its previous venue, one of the ugliest of hotels in London, so data has shrugged off its dark and dingy façade and emerged into the mainstream consciousness of financial institutions.

HSBC's Alan Greenall, global head of reference data IT at the bank, summarised the mood of the data environment today, saying he doesn't just want consistent data, he wants consistent quality data. Data management has struggled for a long time to make it into the boardroom and now that it has, users can be more specific about what they want from their data.

"You don't need to clean all your teeth, just focus on the points of pain," Greenall explained. In other words, you don't need to clean all your debt, just the bits you're interested in cleaning.

Greenall named three important points to focus on in a data operation: to analyse and prioritise; to appoint data ownership and stewardship; and to get all the sections in place to cleanse. When asked his priority for data projects, he replied: "Getting the buy in from downstream systems to create the golden copy."

An industry-wide perspective on data management buying practices and initiatives was also provided by Carole Mahoney, a consultant with SunGard. She summed up the state of the market today and explained that enterprise data management (EDM) hasn't been implemented as expected, because of the input of time and the investment spend required. "What we have found is that companies are only willing to look at the components [of EDM], such as ASP services or hosted services."

Mahoney summarised the main challenge facing the industry: most firms are strapped into old technology, which restricts growth. There are new challenges and requirements that entail front to back consistency, for example identifying legal entities. Moreover, standards create a myriad of issues, as does the data itself.

John Carroll, vice president of product data services at Merrill Lynch, considered what it really means to have a centralised database. Carroll explained that although data is all of a centralised purpose, it doesn't all fall into one route – for example, corporate actions and reference data use difference requirements. "The ideal is to have a centralised database, but there are a couple of concerns: market expertise, and offshoring or outsourcing." Dublin and Singapore provide a great amount of expertise in their respective markets that people in New York could not support as they don't have the local market knowledge, he went on to explain.

Ian Webster, global head of market data at Barclays Global Investors (BGI), began the second day's agenda by describing four different business models for data management. While Webster pointed to a unified structure as the best approach, he pragmatically asserted: "I know very few companies that are there or even aspire to be there. Most are in the coordination box. We [the industry] need to recognise where we are. We have very complex problems to solve, because of all the different views and people involved, and because it's about money [for our clients]."

Webster followed the trend of the conference by suggesting firms need to ask themselves what they are trying to govern. Asset allocation falls into three categories, he said: asset type, investment style and geography. "Follow the investment style of your firm and stay out of prioritisation discussions – that's for the internal team," he said.

"Unnecessary standardisation is the hobgoblin of small minds," he continued. "You've got to look at what's appropriate and where to standardise. I never talk about centralisation, but standardisation – you need to work to standards but these need to be devolved and not centralised."

Webster concluded that firms should not forget about data governance, but advised them not to concentrate on that until there is actually something to deliver. They should then split the data levels and align them properly to where the decision makers are.

Bank of Scotland's (BOS) David Miller, director of Credit Systems, began his presentation to delegates by asking three rhetorical questions: how do I get world class reference data, is it the holy grail, and is there such a thing? World class reference data is where BOS wants to be, Miller said, and we have to meet our customers' expectations. "First we have to regard data as a business valuable asset in its own class and second we have to identify our clients' [data]." He went on to explain how to build a business case for good data – it saves money, up to 20% of revenue can be lost because of poor data, some estimates have shown, Miller said. "Tell that to senior management."

Ross Gourlay, senior consultant at BOS, reminded delegates that silos are not conducive to good data. "So why do we build them? Ignorance and arrogance – it's the easiest path," he explained. BOS has spent five or six years working on its own data management system, not an easy or short process, Gourlay said.

Todd Goldman, vice president of marketing at data vendor Exeros, followed with a presentation on accelerating reference data projects. "I'm going to dig a little deeper and look at why it's hard," he began. "The bad news is: sourcing data analysis is not trivial, and this is before you've even deployed the project. To map and populate the downstream master takes even longer; and the result is, deployment time and return on investment is more than one year."

The problems of constructing a data project also include people and personal communication. In many firms there is one person who knows the system and has the knowledge of how it works in his head, Goldman explained. "This is why the projects last forever, because we don't know our data, our relationship metadata. But yes, there is hope through technological advancements."

FIMA's panel discussion on the establishment of an effective data governance model and its implications for data quality and the reduction of operational risk began with comments from Jim Perry, global head of Reference Data, Goldman Sachs. "The challenge comes from legacy platforms and how to decommission them. Internal sources of data might be harder to solve than external sources."

Lisa Sully, head of Global Data Management at UBS Global Asset Management, summed up the position of UBS's governance model, explaining how the bank established a global programme in 2004-2005 based on the model operating in London. This model has now been expanded from pricing data to instrument data.

BGI's Webster, chair of the discussion, said: "We talk about sharing data across the industry but we have to get used to that across the business. I sometimes have more in common with Lisa [Sully] as an asset manager than people across my group." Webster went on to suggest to panellists they could become more efficient in their practices if they became more like vendors, internally. How comfortable are you taking the next step and outsourcing, he asked. "Not that comfortable at the moment – we like to have control there [of price validation]," replied Sully.

Goldman Sachs' Perry echoed her sentiments: "We are comfortable with price variance, but we don't outsource completely and still keep control of that internally. Numeric quantifiable data is harder to outsource, reference data is far more difficult and complex."

Following the debate was a presentation to delegates on the competitive advantage of mastering and managing international customer data, delivered by Holger Wandt, principal advisor at Human Inference. The data vendor uses natural language processing to answer a simple question: 'what is what', Wandt contended. In an interesting presentation, he explained why databases used by banks become unwieldy: "Processing, to a human, is easy, but it's harder for a machine. You need to teach it the dictionary, maths and linguistics."

Christoph Lammersdorf, chief executive officer of CounterpartyLink, began his presentation on managing the costs of collecting, verifying and maintaining compliant legal entity data in the face of new legislation, by telling delegates what should they want. "The drivers for good data are accountability, content, 'auditability' and flexibility – what I find is, you [banks] don't know the level of your data," he said. "Requirements change, so you need to be flexible, you would love to have standardised data."

The last panel debate of the day was entitled identifying counterparty automation efficiencies: improving client data quality across your business, chaired by Predrag Dizdarevic, executive vice president of Capco. Ken Price, chief executive officer and co-founder of Avox, part of the Deutsche Bourse Group, said the biggest problem to automation is not getting started.

Greenall from HSBC, added: "The idea of taking data externally is something all should strive for. The problem is, there's constant mapping required. The range of attributes is limited at the moment – externally available data is the only bit we can automate. The value add for local data is not there yet."

Price explained some of the difficulties in practical terms, in identifying counterparty data: "In the US there's no requirement for hedge funds to publish counterparty data, so the only way to get it is to ring up and get them to fire it through." One solution he suggested was for increasing cooperation between vendors. He also explained that Barclays Bank probably has the best data content, partly because they haven't bought a new bank every year. That lets them take advantages of new opportunities, he said.

Delegates were asked how they know their data is better off after data projects or standardisation models. "The only way we know is from feedback from downstream users," Greenall said. "We don't have metrics in place to judge the quality of data to start with. Anecdotally, we believe it's better and we experience fewer errors."

FIMA 2007 brought forward the issue of data management and moved the focus on from the acknowledgement of a problem to the scale and detail of it. Practitioners are now discussing what they need to standardise, rather than whether they need to do it at all. This is something that came through strongly from debates and presentations throughout the two days. Next year's FIMA might encourage some to go further still and reveal their specific problems, how hard their bottom lines are being hit by poor data and how much improved this might be with a data project. But don't hold your breath. ■

Weathering the storm

Brian Bollen looks for the silver lining in the liquidity crunch cloud

Every cloud has a silver lining, says the old proverb. And that can be as true in the financial services world as it can anywhere else. The market turmoil and subsequent credit crunch and liquidity shortage caused by the US sub-prime crisis has introduced new opportunities to securities lending, opportunities that could never previously have been dreamt of.

Some market participants have argued that, for the first time ever, the cash reinvestment tail began to wag the securities lending dog in the latter months of 2007. The benign market conditions that have prevailed in recent years were suddenly replaced by conditions that bordered on the malign.

The sudden steepening of what had long been a flat yield curve changed the rules of the game, creating a phenomenon that was not immediately recognised, or universally accepted, but which we believe is real nevertheless. The end result as it relates to securities lending is that existing lenders began to seek more opportunities to lend stocks or bonds, and other institutions that had not previously been lenders began to see how they might be missing out, and changed their behaviour.

"Those institutions that are long on securities, and especially fixed income, have realised they can make significantly more by lending their securities, taking cash on collateral and reinvesting that cash at much higher rates than have previously been available," explains Guy d'Albrand, global head of Liquidity Management at Société Générale Securities Services (SGSS). "The sudden steepening of the yield curve means that three month rates are significantly higher than overnight rates, for instance. The markets have entered a new era, with the creation of a spread between lending against cash, and lending against other securities. Beneficial owners long on securities began to look for counterparts to give them cash collateral to cash in on the yield curve spread."

Peter Fenichel, the recently appointed chief executive of SecFinex, the specialist marketplace in which Euronext bought a 51% holding in 2007, does not quite see eye to eye with d'Albrand on this point. He concedes that it is theoretically possible, but does not envisage much incremental business taking place. "The credit crunch affects everyone and has had an interesting impact upon our part of the industry," he says. "A couple of issues have arisen. One part of the three legged stool of stock borrowing and lending is collateral. When you're giving cash collateral, it can look like an interbank loan, which is consuming a credit line, so when credit limits are proscribed you will tangentially affect securities lending and borrowing; in some cases, lenders wanted to lend to borrowers who wanted to borrow, but they couldn't take cash collateral because they had no credit lines for that borrower. You can't net borrowing against cash, so it looks like an interbank loan when you report it. This has raised issues with our customers about central counterparties." When markets work well, he continues, lessons about weaknesses are only learnt in times of strength. Securities lending and borrowing has been slow to change, because there hasn't been a compelling reason to change, until now, it would seem.

He identifies two ways to get round the collateral issue. "Pools would help by eliminating collateral risk, sitting in the middle of trades; a central counterparty would eliminate bilateral credit risk and limit collateral risk, so facilitating an increase in trading activity."

To illustrate his point, he evokes memories of early days in the derivatives markets when growth, though healthy, was unnecessarily constrained by bilateral exposure and inadequate back office machinery, people and processes. "When they started trading through a central counterparty, it helped exponentially."

Turning away from the prospects of future growth in securities lending to driving forces for past growth, Fenichel pinpoints the impact of the trend towards hedge funds and absolute value investing and away from relative value investing. "Absolute value investors need to go short and hedge their positions; as this approach has become more mainstream, there is a lot more need to hedge, and securities lending needs to keep up with the growth opportunities. Growth won't happen without changes in the way it is managed, which is why Euronext bought 51% of SecFinex, to bring standardisation and anonymity to the market, a market that some participants and observers describe as 'medieval'. Part of that change involves creating a central counterparty, but that is not as easy as flicking a light switch." Watch this space, he urges readers.

A number of the thoughts being expressed by such a relative newcomer will surely ruffle some of the older feathers around in the market. He argues, for example, that the price differential between general collateral and special collateral is 'not right'. "It doesn't reflect supply and demand, it reflects relationships," he says. "Transparency brings a better balance to supply and demand, delivering more accurate pricing." He currently remains agnostic on whether the price of special collateral should go down, or whether the price of general collateral should go up. We won't know, it seems, until the market is doing what it ought to do, rather than what it is accustomed to do. "We're looking at how we can add value to the marketplace to make it more robust. We're working with all parties to find the competitive advantage they think can benefit everyone as markets evolve. It would be better for the market in the long term if we could find a way to manage collateral differently; a lot of people don't want cash collateral, because while they have the systems and procedures in place to manage treasuries, or gilts, or bonds, they cannot manage cash collateral."

On a broader note, Craig Starble, executive vice president State Street Securities Finance, believes not only that the securities lending industry will continue to evolve but also that there are limitless opportunities for the business. "Lenders are looking for better risk adjusted returns and they are interested in knowing their provider offers many routes to market, including custody, third party and auction lending," he observes.

The growth and increased demand for securities lending that we have continued to see in the past 12 months is primarily due to additional markets, an increase in the overall number of lenders and borrowers and the quantity of quality lendable assets that are available, he says. Further, the growing allocation to alternative investments that employ long/short 130/30 strategies have increased short interest lending opportunities and new markets. "As hedge funds become more global, we are seeing more and more non-US opportunities for lending activity, using Asia Pacific and Europe as examples. The evolution of third party lending, entry into emerging markets and the expanded use of alternative investment strategies, all will be major factors that contribute to industry growth."

He expects to see continued consolidation to occur throughout the market. "Not everyone - particularly those institutions with multiple lines of business with which to contend - has the capabilities to maintain the level of commitment necessary to be a superior lending provider. Lenders do not want to hire an agent that might exit the business in a few years, or that can not effectively service them with a full suite of products, globally."

On the question of risk adjusted returns, he expects to see – and actively encourages – every lender paying more attention to lending performance in the context of risk adjusted returns, especially in light of the current market where severe conditions have rewarded those programmes that offer a more conservative approach. "Lenders need to understand the risks they are taking and monitor events that alter those risks." Against this background, lenders will continue to look for dedicated global partners that have the technology capabilities, proven track record of success and expertise to provide guidance and a full array of investment operations services at scale as they grow their business, globally, he comments.

Lenders need to understand the risks they are taking and monitor events that alter those risks

Elsewhere, Asia continues to be a major growth area, with volumes increasing dramatically based on many markets that have seen index arbitrage and statistical arbitrage opportunities materialise and of which hedge funds and quant players are taking advantage of, says Sunil Daswani, Northern Trust's director for Securities Lending (Asia) and the current chairman of the Pan-Asian Securities Lending Association. "We see this primarily in Australia and Hong Kong where flows in these markets are almost matching that of Japan, which traditionally dominated Asia," he says.

"With the growth in the index and statistical arbitrage strategies, the need for automation becomes critical as most trading involves high volume low value transactions. Northern Trust continues to focus on automated platforms, be it internally built or through the use of industry accepted platforms like EquiLend," Daswani continues. "Not only now is there a focus to automate the pre-trade transactions but more so operationally to automate post-trade functions such as collateral marking and billing activities."

He elaborates: "Additionally with recent developments in emerging markets, slowly progressing to standard international best practices, we will continue to see greater flow in Asia. Emerging markets lay out interesting opportunities when they eventually open their doors. In Asia we have seen the opening of Taiwan and the Philippines recently. Malaysia will hopefully follow soon (around the first quarter of 2008). Outside of Asia, recent new markets where there has been pent-up demand and regulations have permitted for securities borrowing and lending are Mexico, the Czech Republic and Hungary and to some limited extent Russia, Turkey and Israel."

Daswani concludes: "There always seems to be a race to be the first to start lending in emerging markets, however, this is not necessarily the best position to be in when such markets have reduced liquidity, which could increase the risk of failed trades. Generally, in emerging markets the risk of fails can be greater than just a reputational issue as many of the regulators look stringently to apply a 'no fail' policy. To enforce this, regulators apply penalties or even temporary or permanent removal of licences from investors in those markets. This is why there is a huge emphasis to ensure that due diligence is carried out completely and tight controls are built around processes when lending in these markets, which each seem to have their own nuances. Northern Trust has seen increased volume in these markets; although flows are not as high as for developed markets, due to caution when entering such markets, revenue is greater due to the larger spreads which can be commanded." And who, if anyone, can resist the siren call of larger spreads? ■

Burning issues

From the floor of the RMA 24th annual Conference on Securities Lending, held in October in Boca Raton, Florida

The Risk Management Association's 24th annual Conference on Securities Lending, held 9-12 October in Boca Raton, Florida, once again drew more than 500 securities lending and borrowing professionals from across the industry and from both the US and Europe. The conference represented an opportunity for industry participants to attend an excellent business programme and to network with their peers.

This year's conference co-chairs, who coordinated the business programme, were Tim Smollen, global head, Dresdner Kleinwort, and Rosemarie O'Connor, principal, Banc of America Securities. "I believe this year's RMA Conference on Securities Lending was a great success, as it addressed key topics that are currently of significant interest, such as 130/30 strategy and proxy voting, as well as giving the participants an opportunity to gather and discuss general industry related issues," says O'Connor.

"As everyone knows, the RMA conference was held during what turned out to be a particularly difficult period in the credit markets, but, regardless, attendance and commitment was excellent," said Smollen. "The senior people I met with not only wanted to talk through the issues currently affecting our industry, but there was still a clear focus on how we move our industry to the next level of growth."

Wednesday, 10 October, the first full day of the conference, opened with welcoming remarks from RMA Committee on Securities Lending chair Tred McIntire, president, Boston Global Advisors, as well as remarks from both conference co-chairs. The first panel of the day was the industry leaders panel, with a lively give and take discussion between the moderator and panel members, who answered a series of questions starting with the effect of the sub-prime mortgage market, then discussed hedge funds and the 130/30 strategy.

The panel was followed by a discussion on the emerging markets of Eastern Europe, Asia, and Latin America, where each panelist addressed his specific market of expertise and where he thought growth opportunities and challenges existed. Hot markets in Europe include Turkey and Romania; in Latin America, Mexico is the 'market to watch', from all accounts (RMA and SIFMA will sponsor a conference on Latin American securities lending on 23-25 January 2008, in Coral Gables, Florida).

Speakers at the collateral management panel that followed shared their views on managing collateral in a securities lending programme. The issue of transparency – good, bad, or indifferent – continues to be a topic of discussion in the industry and at the panel, which closed out Wednesday's sessions.

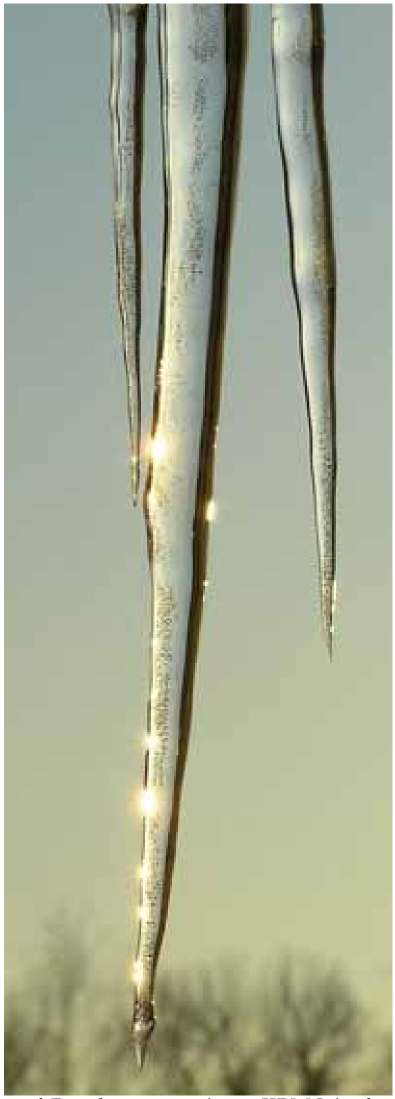
Thursday opened with a panel on understanding the 130/30 strategy and its impact on securities lending. Speakers talked about how this strategy is used as an investment option, how it affects securities lending, and why it is growing so fast. The proxy voting and governance panel, which closed the conference, continued the discussion of why these topics continue to garner so much attention from both the media and clients.

RMA Conference on Securities Lending was a great success, as it addressed key topics such as 130/30 strategy and proxy voting

A highlight of Thursday was the keynote address from John Bogle, founder of the Vanguard Group and president of the Bogle Financial Market Research Centre. In a presentation entitled "Black Monday and Black Swans," Bogle talked about how changes in the nature and structure of our financial markets are making shocking and unexpected market aberrations even more probable. He said the application of the laws of probability to our financial markets is badly misguided. The fact that an event has never happened in the markets is no reason to be confident that it can't happen in the future, he said. ■

Cold light of day

The deadline for MiFID has been and gone, but once the dust has settled, has anything actually changed? **Virginie O'Shea** investigates



Anyone would have been forgiven for thinking that 1 November was a business day like any other in Europe. Regardless of the clamour by the press, consultants and technology vendors over the last couple of years in the run up to the Markets in Financial Instruments Directive (MiFID), the deadline for compliance slipped by without so much as a pop, let alone a big bang.

Just in case you have been hiding under a rock over the last few months, the directive is designed to level the financial playing field across the European Union by ensuring investors have access to all markets at the same transparent price, regardless of location. According to the official line of the European Commission and the Committee of European Securities Regulators (CESR): "MiFID will simplify and streamline the passporting regime for firms doing cross border business, increasing competition and enabling greater EU financial integration."

Despite the Commission propaganda and the fact that the industry has had three years in which to get ready, a number of countries still have not transcribed the directive into national legislation. Notable stragglers include Italy, Hungary, Poland, Portugal, Spain and the Czech Republic (see box overleaf for full list). CESR was forced to take measures to "ease the transition" of these countries (read, give them some slack with regards to transposition) at the eleventh hour. As a result, on 22 October, CESR published a statement that was intended: "To give reassurance regarding the continuity of the current passports granted to investment firms based in the limited number of countries that will be late in transposing MiFID." I'm not entirely sure that 12 is what one would call limited, but that's up to the bureaucrats to decide…

Moreover, only three member states – the UK, Romania and Ireland – out of 27 met the 31 January 2007 deadline to transpose MiFID into national legislation. Many others have only just cobbled together the legislative requirements to scrape through the November deadline. Uneven implementation by member states means that only now are differences in member states' interpretations of MiFID requirements starting to emerge, raising the spectre of the very problem that MiFID was intended to eliminate: continued legal and regulatory uncertainty in respect of the provision of investment services in other member states on a cross border basis.

Until all the major European countries are fully MiFID compliant, the impact on the European market as a whole will be limited, says Alain Lesjongard, head of International Compliance at the Bank of New York Mellon. "National regulators in compliant countries will probably start to ensure that their regulated firms are complying with the new rules in the new year. It is less certain how much pressure and how quickly the EU will put on non-complaint countries to implement MiFID," he adds.

Banks doing business in countries that are late will need to study the legal ramifications quite carefully, including the possibility of forbearance, and make provision for dual operational processes, adds Dr Anthony Kirby, co-chair of the MiFID Joint Working Group (JWG). Late countries could face referral to the European Court of Justice and being named and shamed as less suitable locations to conduct financial business, thus incurring reputational risk.

Tristan Clarke, senior manager, Risk and Regulatory practice at KPMG in the UK, believes that even when the stragglers do transpose the directive, MiFID may not achieve its goal of a unified European regulatory environment. Although one of the main objectives of MiFID was to level the field between different regulatory jurisdictions, it is unlikely to accomplish this with any success because of the different cultures of the regulators, he says.

In transposing MiFID into their national laws, member states have sought to gold plate the EU legislation, which complicates the task for CESR in ensuring supervisory convergence between national regulators, adds Paul Richards, head of regulatory policy, International Capital Market Association (ICMA). In addition, a degree of national discretion in some areas, such as transaction reporting, has added to the scale of the implementation problem and pressure on the timetable. In other cases, CESR has not been able to reach a consensus among national regulators – for example, on market facing and client facing transaction reports – so pan-European firms are faced with different implementation requirements in different member states.

In order to tackle this problem CESR issued a common protocol at the end of October in an attempt to foster greater cooperation between its members in the exercise of their core supervisory functions over entities with cross border activities. The protocol sets out a framework for cooperation between competent authorities under two different models: joint supervision conducted through common oversight programmes; and requests for assistance based on efficient allocation of supervisory tasks.

However, Clarke is sceptical that the protocol will solve the issues: "The common protocol will help formalise communication but it is difficult to see the protocol revolutionising the way in which the regulators deal with each other."

Richard Young, manager industry programmes at Swift agrees: "While MiFID does provide a core common regulatory approach for all the impacted states, individual regulators are able to impose additional rules and requirements for their market. An example of this is MiFID transaction reporting, where a lack of agreement for a common approach on the format, scope and data content of reports has made this process much more difficult, especially for firms operating branches from a central location. Swift put forward proposals during 2007 to deal with the formatting issues for MiFID reporting, by defining an ISO 20022 compliant set of MiFID transaction report formats. With rising awareness, this standardised format should gain some traction during 2008. It seems, nevertheless, that differences in regulatory practices seem set to be with us for a while longer yet."

As well as late compliance and regulatory harmonisation, press coverage of MiFID's impact has tended to centre on the confusion surrounding the best execution requirements, but this is only half the story. Best execution, particularly in the equities space, has had the most media focus but, ironically, it is the area that probably needed the least. Most asset managers have been very aware of transaction costs and the importance of good execution for some time and the equities market is already quite transparent (in comparison to other asset classes that is). As Daniel Wiener, managing director at State Street Global Advisors (SSgA), notes: "The best execution policies that we have seen so far have been quite general in their approach." It seems therefore that it has been the area with the biggest fanfare but not the biggest impact.

In many national jurisdictions the securities and investments industry is a very insignificant element of national GDP. Why should they be overly concerned about this legislation?

This general approach to best execution is reflected by the discussions within the MiFID JWG's Best Execution Subject Group (BESG). The group has focused its discussions mainly on macro processes, such as models, transaction cost analysis (TCA), policies and the recording of evidence of conformance with processes. "The BESG deliberately did not go beyond processes to set out the aspirational context: the values, principles and especially the outcomes that firms try to achieve, not least as MiFID is outcome focused. The white paper did not answer these questions nor should it, because this is what firms have to do in their value proposition to clients. The relative importance of the factors, for example, depends very much on trading objectives and styles, the products being traded and the market structures. There is no way we can 'define' execution once and for all, nor can we compare ex-ante expectations with ex-post states of affairs," explains Kirby.

Overly prescriptive rules on best execution would be counter productive, adds Tony Freeman, executive director, Industry Relations and Market Growth, Omgeo. This is an area where principles-based regulation is most appropriate. The principle of best execution is now firmly embedded across the EU but it is at its most advanced in the UK. It is in nobody's interest to challenge best execution, as it is a key principle that everyone should apply, he contends.

Eric De Nexon, head of Strategy for Market Infrastructure at Société Générale Securities Services (SGSS), believes that clients will ask more of their service providers, regardless of whether the requirements for best execution are prescriptive or not. "Even if the text of the directive does not impose a minimum of venues, the firms will respect the fact that they have to offer the best for their clients. The industry wants to satisfy the clients and offer them the best possible execution," he says.

It is likely that best execution practices will be challenged if there is no valid rationale for use of certain venues, adds John Siena, assistant general counsel,

Systematic internalisers so far:

According to the Committee of European Securities Regulators (CESR) as of 23 November 2007, the list of registered systematic internalisers comprises:

- ABN AMRO (London Branch)
- Danske Bank
- Deutsche Bank (London Branch)
- Lehman Brothers International Europe
- Nordea Bank Danmark
- Citigroup Global Markets Limited
- Citigroup Global Markets UK Equity Limited
- Credit Suisse Securities Europe

director of European Legal Operations, Brown Brothers Harriman. "Because best execution is contextual and multifaceted, it is likely that firms providing their policies will be able to articulate good reasons for the approaches they take. However, buy side firms have always been at liberty to challenge price or adequacy of execution in the past and there is no reason to expect this to change."

SSgA's Wiener feels that there are other areas that may challenge market participants to a greater extent than best execution, such as consent to deal off exchange, limit orders, outsourcing, and suitability. In some of these cases these are things that were very much designed for the retail investor but they are applied to the institutional investor and that creates some issues.

Most of the impact this month has manifested itself in a blizzard of paper flying around the continent, adds BBH's Siena. This paper is in the form of client classification letters that MiFID investment firms were required to send to clients by 1 November. In addition to classifying clients as retail clients, professional clients or eligible counterparties, investment firms also included in these letters information surrounding conflicts of interest, best execution and order handling policies, as well as requests for express consent to trade outside regulated markets and not publish prices on limit orders.

"Recipients of these letters are only now digesting them – at the moment discussions are underway while everyone sorts out just how they want to be classified under MiFID. The level of client classification has implications for the kinds of protections clients are afforded under MiFID," he explains.

The issue of operational risk has also been underlined by MiFID, especially in the area of outsourcing arrangements. "MiFID in practical terms requires firms to re-examine their outsourcing arrangements. Sticking points may come in some jurisdictions, which politically would like to confine outsourcing to within the EU to ensure jobs are preserved. This may result in detailed scrutiny of outsourcing arrangements where these services are provided outside the European Union," says Bob McDowall, senior analyst at TowerGroup.

There was much debate about the rules surrounding outsourcing during the framing of the MiFID Level 2 text, and during the Level 3 implementation process. In essence it seems that regulators do not want to unduly constrain investment firms from taking advantage of such opportunities, but at the same time, a fairly clear set of oversight guidelines was established to keep this issue manageable. This is almost certainly one of the areas that the Commission and local regulators will keep under review to judge the effectiveness of the agreed measures over the next couple of years, adds Swift's Young.

But will MiFID have an impact on all areas or is there sufficient room to wriggle out of the requirements? The history of EU Directives shows they have many loopholes and MiFID will be no different, contends McDowall. "In many national jurisdictions the securities and investments industry is a very insignificant element of national GDP. Why should they be overly concerned about this legislation?"

KPMG's Clarke disagrees: "It would take some extremely aggressive interpretations of the underlying directives to avoid the impact of MiFID – it is bound to have some effect. The key will be the extent to which the local regulators pursue failures by the firms they supervise. A number of discretions and exemptions were drafted in to give an element of flexibility to regulators but the core requirements would be difficult to avoid completely."

It seems unlikely that the regulators will crack down on non-compliance this year and will instead take a pragmatic view of firms' difficulties with implementation, especially given the laggard countries across Europe. As long as firms have a plan in place setting out how and when they will become compliant and are demonstrating the intent to become compliant, the UK FSA is likely to be understanding, continues Clarke. Regulatory action will be more likely next year if there are firms who have not taken steps towards becoming compliant or if there are any outliers in terms of the approach taken. One example of this could be best execution – it would not be surprising if the FSA tried to ensure that some of the more aggressive interpretations of best execution were toned down, although this would not necessarily be through enforcement action initially.

The Danish FSA has also indicated that all inspections from 1 November and onwards will include MiFID, and we have no doubt the same will apply to the rest of Europe, adds Michael Villi Møller, senior executive director and global head of Legal and Compliance at Saxo Bank. MiFID is essentially concerned with investor protection, but it will take time before you will see customer complaints based on non-compliance. "At the end of the day, we are all being judged by our respective customers so either you perform or you don't. It is as simple as that. Customers will quickly recognise and expect the full MiFID protection and those who choose minimum solutions will soon lose out," he concludes.

It would take some extremely aggressive interpretations of the underlying directives to avoid the impact of MiFID – it is bound to have some effect

The Commission's hit list

Those countries yet to transcribe MiFID (Directive 2006/73/EC) into national legislation (as of 23 November 2007) according to the Internal Market's Commission website:

- Czech Republic
- Estonia
- Hungary
- Italy
- Latvia (only in part)
- Lithuania (only in part)
- Poland
- Portugal
- Slovenia
- Spain
- Iceland
- Lichtenstein

Future of custody

What is the current state of the global custody market?

SIMON WALKER, DEPUTY HEAD, GLOBAL CUSTODY PRODUCT MANAGEMENT, BNP PARIBAS

The state of the global custody market today is pretty interesting, especially from the consolidation standpoint. I think it's fair to say there are currently three major custodians with assets under custody (AUC) in the trillion dollar level – BNY Mellon, JPMorgan Chase and State Street – primarily because of their huge domestic USD portfolios. You then have the mid-tier providers, who may not have the size in terms of AUC, but have the capacity and expertise to offer comparable products.

From another perspective, there is increased talk of prime brokers looking to enter the market (not surprising, given the substantial assets they are holding on behalf of their, primarily, hedge fund clients). This could potentially see global custodians competing head-on with investment banks in servicing the full range of hedge fund requirements.

What is most interesting is that consolidations have taken different forms in the most recent past – not just the 'traditional' kind, such as State Street and IBT, but agreed mergers at the parent level, such as BNY and Mellon and joint ventures at the custody processing level, such as RBC Dexia and Caceis.

If this summer's credit crunch leads to lower market valuations (and therefore lower fees for global custody providers), this consolidation could well accelerate.

Another key development in the market has been the move into fund manager outsourcing, effectively broadening the traditional product offering to include fund administration and middle office outsourcing. Here, IT development will remain a critical benchmark of how much investment a firm is willing to make in its custody business.

BNP Paribas Securities Services was on the crest of the outsourcing wave with the Cogent acquisition in 2002 and this has also been a driver for many recent consolidations in the securities industry. Within this spectrum though, our collective challenge is to ensure that revenues are increasing at a higher rate than the underlying costs.

To help ease the dilemma, the market has accordingly been innovating with value added products such as transition management, while furthering the capabilities of existing FX and securities lending products. As clients diversify their investments and look to derivatives and unlisted investments, such as private equity funds, global custodians will also be required to link in the pricing of derivative instruments and cover these investments as part of a consolidated reporting package.

Regarding the state of the industry on the whole, I would say that the impact of MiFID will be a concern for some time to come as it has created the environment for growth in multilateral trading facilities (MTF) and the potential movement of trading activity and subsequent liquidity away from the traditional stock exchanges. I'd say it would be wrong to underestimate the knock on effects of MiFID on the global custodian market over the coming years, especially with the need to recognise and settle a single ISIN code across multiple MTFs, CCPs and CSDs.

In short, the global custodian market will be heavily influenced by its clients' mounting appetites for cross border assets, for new 'exciting' markets and for a wider range of financial instruments, topped off by a relationship with someone who can cover the globe for them. IT development will remain a critical benchmark of how much investment a firm is willing to make in its custody business.

To keep up, diversification is also one of the playing cards that global custodians are shuffling today; the tendency being to shift the client base away from domestic markets and get out into new territories and indeed new client segments. BNP Paribas Securities Services has been doing a lot of this lately, our strategy of growth culminating in numerous acquisitions this year already and full scale development of our plans for Asia and the Americas.

How are custodians adapting their services to meet clients' demands?

GUNJAN KEDIA, HEAD OF PRODUCT DEVELOPMENT, BNY MELLON ASSET SERVICING

The product development lifecycle in our business has certainly accelerated. Our clients' needs, the strategies and instruments they utilise, the regulatory environment, the solutions we need to develop and deploy to meet those challenges - all are becoming exponentially more complex. Risk mitigation and enhanced transparency are very much at the top of their agenda.

The challenge in 2008 for custodians is to continue to innovate rapidly. Clients want a true end to end service, one that encompasses front, middle and back office components. Just as importantly, they want their asset servicing provider to be able to bring servicing solutions to the table quickly and cost effectively.

Asset servicing providers, like ourselves, are constantly assessing changes in the market and investing a significant tranche of their technology budgets on more robust servicing solutions, particularly around alternatives and derivatives. There has obviously been an explosion in the use of alternative investments with the advent of UCITS III and the proliferation of hedge funds; 130/30 funds are also now a big consideration, along with expanded investment in private equity and real estate, making alternatives a major priority for asset servicing providers in 2008.

Given the complexity of these instruments, we have created an entire product management group that purely focuses on the alternatives space. The skill set of this team is quite different from traditional product managers and one of their biggest challenges is listening to clients and various industry contacts to develop a service model that can meet the needs of many constituents. We are off to a good start with introducing a new independent valuation service of OTC derivatives earlier this year and also have a pilot programme with 10 of our larger clients in expanding the servicing of private equity investments. The themes of valuation, transparency, controls and compliance monitoring highlight the direction in expanding our services in the alternative investment space.

The asset servicing business has a large appetite to be competitive and meet the ongoing service requirements of our global client base. We invest a third of our technology budget, roughly USD300 million, on new products and expanded capabilities. Beyond alternatives, there are key strategic investments in our risk and performance measurement products and in our industry leading information delivery platform, Workbench.

As clients look to expand and leverage their asset servicing providers, the ultimate challenge in 2008 and beyond is to have the ability to deliver new and innovative solutions. It is a big challenge and you need to execute and deliver each and everyday across the globe. People make important investment decisions based on what we do and to me, that's only going to continue to increase. I think it is going to be very exciting and interesting to see how that affects our industry.

What will the technology sector of custody business look like in five years' time?

CHRISTIAN HUDSON, CHIEF INFORMATION OFFICER, INFORMATION TECHNOLOGY GROUP, SWISS AMERICAN SECURITIES INC (SASI)

Competition, consolidation and globalisation in the custody marketplace are driving custodians to spend more on technology in an effort to differentiate themselves from their competitors. Custodians are focusing on providing solutions to their clients in the areas of enhanced client servicing, risk management and regulatory compliance.

Consolidation has, in many instances, led to opportunities for those who remain cognizant of the requirements of their existing and prospective clients. Consolidations have resulted in custodians having to change their focus from customers to trying to manage various disparate technology platforms and processes. Additionally, clients in many of these consolidations have had to migrate from one offering to another, at times offering a diminished level of functionality. Another area of client concern has been the fact that these newly combined organisations have even larger and more complicated infrastructures, which do not lend themselves to client level customisation.

At present, we are looking at all the client service areas that exist within a normal custody business and attempting to build better systems for each area. Fast forward five years and my guess is, instead of focusing on improving service in an area like corporate actions, we will be much more driven to integrate business intelligence tools across all areas to allow clients to access information at whatever time, and in which ever way, they need it.

In the next five years, there will be even more standardisation and globalisation and as a result custodians will have to provide an even greater level of client service and support. This support will probably require a closer relationship between the business and technology groups in both provider and recipient organisations. Technology will be much more focused on providing access to information and solutions to the global process.

In terms of consolidation, there is a natural cycle at work here where innovation often takes place in small, more nimble companies, much like SASI, and is then either copied or acquired by larger organisations.

The large providers will tend to get larger because of the cost efficiencies they are able to offer. The second tier providers will probably have to assess their offerings and make some strategic decisions based on their value proposition and how they want to differentiate themselves. In the secondary spaces some firms will most likely decide to specialise in a certain market segment or product. There is also the strong possibility that certain strategic alliances will be forged in the near term.

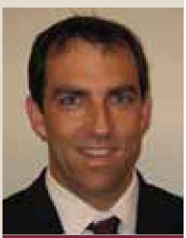
MOVING & SHAKING

Toronto - Royal Bank of Canada's Michael Lagopoulos, CEO and global head of International Wealth Management, has relocated from Toronto to London. Lagopoulos comments: "My relocation from Toronto to London signals RBC's commitment to growing our wealth management businesses outside North America. London will provide us with a better line of sight to assess international wealth management opportunities." In a separate move, RBC has appointed Nigel Rendell as senior European emerging markets strategist, based in RBC's London office. He will report to Nick Chamie, head of Emerging Markets Research and Russell Jones, global head of Fixed Income and Currency Research.


MICHAEL LAGOPOULOS

London - Northern Trust has expanded its asset servicing sales and relationship management teams, which focus on institutional investors across Europe, Middle East and Africa (EMEA). Damian Powell has been appointed as head of EMEA institutional sales responsible for a team of sales managers targeting institutional investors across this region. Rhonda Zoef joins as UK pension fund sales manager, reporting to Powell.

Dublin - Pioneer Alternative Investments (PAI) has made three hires to its fund of hedge funds (FoHF) research team with the appointments of Bob Puccio as global head of Macro, Quantitative, Fixed Income (including Convertible Arbitrage) and Multi-Strategy Research, David Siegel as junior research analyst and Ellen Cooper as junior operational due diligence analyst. In his new role Puccio will be responsible for research and due diligence on underlying hedge fund managers, looking at potential new investment opportunities as well as continuous monitoring of existing managers.

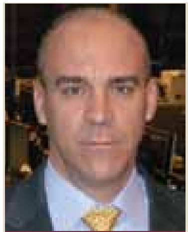

BOB PUCCIO

London - Baring Asset Management (BAM) has appointed Andrew Lamb and Paul Morgan as senior US equity analyst and investment analyst respectively. Lamb will join BAM in January as senior US equity analyst and his focus will be industrial companies. Morgan joins from Brown Shipley & Co and will take up his role early in the new year as part of the European large cap team.

Copenhagen - Saxo Bank has successfully concluded its search for a new member of the bank's senior executive management with the appointment of Albert Maasland, who will join the Copenhagen-based online investment bank as the new European COO on 1 December 2007. Maasland joins Saxo Bank's senior executive management from Standard Chartered Bank, where he was global head of business development, Global Markets E-Commerce, for the past two years. Saxo Bank is already operating with an Asia Pacific COO, Kevin Ashby, who is based in Singapore. As European COO, Albert Maasland will be the overall head and coordinator of all European, Middle East and US offices and regions.


ALBERT MAASLAND

New York - BNP Paribas has expanded its Hedge Fund Relationship team with the appointments of Conrad Johnson as a director in New York and Stephanie Wong as an associate director in Hong Kong. In his new role, Johnson will assist his team in optimising the firm's relationships across its various business lines with the world's leading hedge funds, the bank says.


CONRAD JOHNSON

London - Fund of hedge funds manager International Asset Management Limited (IAM) has appointed Alexander von Mühlen to a new role as head of client relations and products. von Mühlen joins IAM from ABN AMRO Asset Management where he was responsible for project managing the structuring and introduction of alternative products, including the IAM range of funds of hedge funds (FoHF).

Sydney - JPMorgan Worldwide Securities Services (WSS) has hired Jane Perry as head of WSS, Australia and New Zealand, joining from AXA Australia and New Zealand where she was chief operations officer. Perry will be responsible for all aspects of the WSS business in Australia and New Zealand, including sales, operations, technology, product, client service, people agenda and the strategic expansion charter.

New York - Paul Simpson is joining Citi Markets and Banking's Global Transaction Services division in December to head global efforts around the public sector and healthcare market segments. Reporting directly to Paul Galant, CEO of Global Transaction Services, Simpson will assume this new global role to sharpen the focus on solutions and services for clients in the public sector and healthcare markets.

London - Turquoise's clearing and settlement provider, European Central Counterparty Limited (EuroCCP), has finally named its permanent CEO and chief operating officer. Diana Chan has been named as the new permanent CEO of EuroCCP, and Trevor Spanner has been named chief operating officer.

Asset Servicing

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CACEIS is an Investor Services company with six offices across Europe. Owned in equal parts by Crédit Agricole and Natixis, CACEIS provides Custody, Fund Administration and Corporate Trust services to demanding Corporate and Institutional clients. We have considerable expertise in Cross-Border Fund Distribution Support as well as Alternative Investment and Private Equity servicing.

Our staff have the language skills and industry knowledge to develop business relationships into strong partnerships and our powerful IT systems are constantly updated to ensure high levels of process automation.

CACEIS is responsible for over EUR1.75 trillion held under custody, and over EUR850 billion under administration.

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With over 20 years of experience in the custody business, DBS' strengths lie in its ability to provide quality services, in depth knowledge and expertise of the Asian markets, as well as customized business solutions to support clients' businesses. Its clientele comprises the global custodians, international central securities depositories, broker-dealers, financial institutions, insurance companies, investment managers, private banks and corporate.

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The cornerstone of Handelsbanken's philosophy is to put the client and the client's needs in focus. Nordic Custody Services are locally present in all the Nordic markets and offer a wide product spectre to a diverse client base.

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Standard Bank	**Financial Asset Services** is the custody and investments-servicing division of **Standard Bank**, providing a unique suite of services to sophisticated investors in South Africa and eight sub-Saharan markets. Standard Bank has assets under custody to the value of **ZAR1.56 trillion** and an overall market share of approximately 40%. Standard Bank's unique selling point lies in its consultative approach to relationships combined with the bank's commitment to custody and investment administration services.	**A:**Standard Bank Financial Asset Services 3rd Floor 25 Sauer Street Johannesburg 2107 **T:** +2711 636 6615 **E:** adam.bateman@standard-bank.co.za **W:** www.standardbank.co.za

C: Neil Daswani, Global Head, Securities Services **T**: +65 6517 0022 **E**: Neil.Daswani@sg.standard-chartered.com **W**: www.standardchartered.com	**Standard Chartered** leading the way in Asia, Africa and the Middle East. Standard Chartered has a history of over 150 years in banking and is in many of the world's fastest-growing markets with an extensive global network of over 1,200 branches (including subsidiaries, associates and joint ventures) in over 50 countries in the Asia Pacific Region, South Asia, the Middle East, Africa, the United Kingdom and the Americas. As one of Asia's leading custodians, Standard Chartered has an impressive track record across the 16 Asian markets in which it provides securities services. It serves global, regional and local custodians and broker-dealers, as well as local and regional fund managers. The Bank plays a key role in promoting the development of these markets and keeping the international investor community informed of industry developments across the region.	Standard Chartered
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T: +43 50505-58510 **F:** +43 50505-58579 **C:** Andreas Petzl , Head of Sales and Relationship Management **E:** Andreas.petzl@ba-ca.com **W:** www.hvb-custody.com/	Unicredit Markets & Investment Banking (MIB) serves as UniCredit Group's global product and competence center for global financial markets and investment banking services, including Custody throughout Central and Eastern Europe, including Austria. Brand diversitiy under which the group operates (Bank Austria Creditanstalt, HVB, Bank BPH, Bank Pekao, Zagrebacka Banka and International Moscow Bank), has its roots in local market presence and knowledge, contributing into a single unified product across the region. In 2006 the group was recognised by no less than 3 independent surveys as being the best region custodian The group's ability to deliver service excellence across 13 markets is the cornerstone of our success. From participation in local market associations to our inter group training sessions, to a client consultative approach, the group continues to work towards making a single impression - excellence.	UniCredit Markets & Investment Banking

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Telekurs (UK) Ltd 15 Appold Street London EC2A 2NE **C:** Kimberly Neumann **T:** +44 (0) 20 7550 5000 **F:** +44 (0) 20 7550 5001 **E:** info@telekurs.co.uk **W:** www.telekurs.co.uk	Telekurs Financial, a company in the Telekurs Group, specializes in the procurement, processing and distribution of international financial information for investment advisory services, portfolio management, financial analysis and securities administration. A global network of local financial market specialists procures real-time stock exchange information at source from the leading financial centres. Containing over 3 million financial instruments, the database of structured, encoded securities information maintained by Telekurs Financial and its ten representative offices abroad is unparalleled throughout the world in terms of both depth and data coverage. Telekurs Financial is a founding member of the Association of National Numbering Agencies (ANNA) allocating Swiss security (Valor) numbers and leads the way in introducing standards aimed at simplifying trading and securities administration.	Telekurs Financial

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Butterfield Fund Services

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INVESTOR SERVICES

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IMFC
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Hedge Fund Administration

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International Finance Centres

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Securities Lending

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T: US- +1 617 204 4500 **T:** UK- +44 (0)20 7469 6000 **C:** Christopher Jaynes **E:** info@eseclending.com **W:** www.eseclending.com **A:** 175 Federal Street, 11th FL, Boston, MA 02110, US **A:** 1st Floor, 10 King William Street, London EC4N 7TW, UK	**eSecLending** is a global securities lending manager and a leading provider and administrator of customized securities lending programs. Its programs attract some of the world's largest and most sophisticated asset gatherers, including pension funds, mutual funds, investment managers and insurance companies. **The company has auctioned over $1. 3 trillion in assets** and has achieved significant growth in its client base, lendable assets and assets on loan. The firm awards principal securities lending business through a competitive auction process that has provided clients with higher returns compared to traditional program structures and improved transparency and objective criteria upon which to make decisions. **eSecLending** maintains offices in Boston, London and Burlington, Vermont. Securities Finance Trust Company, an eSecLending company, performs all regulated business activities.	eSECLENDING SECURITIES FINANCE TRUST COMPANY
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T: +44 (0)20 7260 1900 **F:** +44 (0)20 7260 1911 **C:** Elizabeth Gee, Sales Director of SimCorp Dimension **E:** elizabeth.gee@simcorp.co.uk SimCorp, 100 Wood Street, London EC2V 7AN UK **W:** www.simcorpdimension.com	SimCorp Dimension is a powerful, comprehensive and truly seamless investment management system. It can handle NAV and other calculations, with complete related accounting, for a huge variety of fund structures and product types, including regional specialities. Support for broader functions, such as performance attribution and risk management, are particular strengths of the system. SimCorp Dimension has been designed from scratch as an enterprise-wide system, handling all aspects of the investment management process, consistently. Data is recorded into a core database so that reporting is made easy, there is no reconciliation of data and no duplication of procedures.	SimCorp
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'Tis the season...

Our disaster recovery expert **Keith Ford** on festive follies

Well a big seasonal hello to everyone from Continuity Towers!

We are all here at the office, wondering if you had missed us over the summer.

To be honest, what with the major downsizing that has been going on here in the service departments, we have not had a great deal to write about. You know how all of your IT support departments simply exist to add to the cost of doing business and to have a good time and attend well funded parties? Well frankly, these have been a little thin on the ground of late.

As a huge effort to get all our readers back onside, we have been doing a little research for you on how much you can spend on the Christmas party and finding out how to do it properly and, of course, how not to do it!

We have heard many bad reports during our research, including a blinding corporate FX evening that coincided with the annual Christmas lottery draw. One of the traders' wives thought it might be humorous to encourage the DJ to pretend he was listening to the draw and call out the numbers 'live'. She of course handed him a list of the numbers that she knew her husband did each week (birthdays, anniversaries and house numbers). In a moment of high excitement, no doubt caused by a liberal supply of alcohol at the free bar and the fact he thought he had just won 10 million pounds, he decided it was time to come clean to his wife about the affair he had been having with her sister for the last five years and suggested she could have the house, cars and kids!

On a more serious note, what can you do to try and ensure that your party does not become a feature in the Sunday tabloids? We managed to garner a few tips from some of the folks in our HR departments.

Dress in an appropriate style for the theme of the party. There will probably be a dress code, which will usually be determined by the location and venue.

Time your arrival. Don't be the first to turn up or be the last to leave, both a recipe for over indulgence or confirming

A glass more than half full

your status as office bore. Make your own itinerary for the evening with a collective rendezvous meeting before the party and perhaps somewhere to go afterwards with your friends. Have an idea what timings have been agreed for the whole evening.

You knew they would say this, but avoid mixing your drinks, try to pace yourself throughout the evening and alternate your drinks with adult soft drinks or water. Slammers or Absinthe cocktails look better in road movies and holiday videos than on the back seat of a taxi.

Speaking of alcohol, it can affect your inhibitions, now is not the time to tell Paul and Ken that their dress sense stinks, or how much Mr Davies fancies Emmanuelle his PA. Remember this is the season of goodwill to all mankind and glass ceilings.

It may well be that there will not be an ever flowing river of alcohol to enjoy and the bar may revert to cash at some point during the evening (subprime lending exposure bankers take note). So remember to bring a few quid, at least for a taxi home.

Say hello to everyone, and try not to get stuck in with your little clique of friends and don't monopolise the conversation with senior bosses.

This is a party and not an extension of the office; so don't spend all night talking shop. The Christmas party is an opportunity to get to know your workmates on a more personal level, to try to network with them and demonstrate other positive aspects of your personality, if you should have any.

Avoid romantic liaisons. Research has shown that at least one third of all couples meet at work and considering how much time you spend there, this should not surprise you. However, thinking that the Christmas party is the place to make a move on Angela because she has had those two glasses of fizz, may not improve your career plan and, of course, you may have to work with her for the rest of the year.

Don't leave the party with those manic traders, or the HR tax planners. Make sure that you organise transport home (remembered to bring that taxi cash?), it can make all the difference to the end of the night.

Finally, have a great party, knock yourselves out and tell us about your best or worst parties over the season for that bonus bottle of champagne. ■