

SECURITIES OPERATIONS WEEK

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► GLOBAL OPERATIONS

EUROPEAN CENTRAL BANK PROMOTES RESEARCH ON EMERGING FRONT: "TOO NETWORKED TO FAIL"

The financial crisis that began to emerge in 2007 and that gained steam in 2008 famously gave rise to the oft-cited slogan "too big to fail." It also saw the coinage of a lesser-known catchphrase kicked around commonly now in research circles: "too networked to fail."

A summation released last week by the **European Central Bank** offers what may be the best discussion to date on the subject. It is based on an October conference in Frankfurt that revealed how research economists are documenting deep systemic risks associated with the interconnection of financial institutions. The phenomenon is simple enough on its surface – as one domino goes, so go the others – but researchers describe a global web of securities firms that are connected more intimately and extensively than perhaps was previously known.

"An important aspect of the analysis of systemic risk is that an apparently robust system may in fact be very fragile," the ECB asserts. "This comes from the fact that a high number of interconnections within the network will serve as shock-amplifiers rather than as absorbers."

The bank also argues that the problem of network risk is compounded by the too-big-to fail phenomenon, in which a relatively few institutions pose a disproportionately big potential threat to the global web of finance "Network analysis is crucial for the identification of such systemically important institutions and markets which are critical players in the web of exposures," **Gertrude Tumpel-Gugerell**, a member of the ECB executive board, writes in an introduction to the paper. "Monoline

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► TECHNOLOGY

EXPERTS ANTICIPATE A 2010 BOUNCE IN IT SPENDING AFTER LAST YEAR'S SLOWDOWN

Researchers are predicting an upswing in spending on information technology in 2010 as companies reverse last year's slowdown, but expectations are that most IT investment will go toward maintaining old systems rather than replacing them.

Broadly speaking, 2009 was the IT industry's "worst year ever," according to a report by **Gartner Inc.** that estimates global business investment in IT will surge to US\$3.3 trillion in 2010, a 3.3% increase over 2009. A more recent report, by **Celent**, drills down into the financial services industry but

closely mirrors the larger trend Gartner sees. The Celent report, "IT Spending in Financial Services: A Global Perspective," predicts a 2.9% increase – to US\$357.5 billion – this year in the financial sector and anticipates spending to grow at about the same rate through 2012, to US\$393.5 billion.

IT spending in financial services fell by about 3% in 2008. The Celent report, by banking analyst **Jacob Jegher**, says that an "astronomical" portion of IT spending will remain dedicated to maintenance (although Jegher says the ratio will inch lower,

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EUROCCP PROPOSES TRUCE AMONG EUROPE'S DIVIDED CLEARINGHOUSES

Angling to break a logjam in Europe over a 2006 regulatory initiative to expand “interoperability” among clearinghouses, EuroCCP has proposed a treaty among rivals.

In a whitepaper published this week, London-based EuroCCP, a relative newcomer that opened shop in August 2008, says competing clearinghouses – which include EuroCCP itself, **European Multilateral Clearing Facility, ICE Clear Europe, LCH.Clearnet, X-Clear** and more than a dozen others – should adopt what it calls an “Interoperational Convention.”

The central idea behind such an agreement would allow a securities firm to use any of several reputable clearinghouses to clear trades conducted in any EU country. Though the original impetus for multilateral interoperability dates to November 2006, when the **European Commission** wrangled clearinghouses into agreeing to broad interoperability, little progress has been made. The market developments of the past year and a half have rekindled the debate, however, as regulators have begun to force more trade through central counterparties as a way to mitigate risk. As a result, questions have been raised over whether clearinghouses can handle a wave of new demand.

“There are new risks associated with interoperability,” said **Diana Chan**, the EuroCCP chief executive. “These need to be transparent to all the stakeholders, which means market participants, regulators and trading venues must know where these risks are and how they are managed.”

Although Europe’s system of equities clearing now typically has a trading venue pick two CCPs, the inevitability of more complicated linkages raises the specter of bigger systemic problems. “Now that several

competitive link arrangements are nearing completion, each governed by a different bilateral agreement, a number of European regulators are focusing on the potential for liquidity, credit and systemic risk that can arise amongst multiple interoperating CCPs,” asserts the paper published last week by EuroCCP, which is a subsidiary of the New York-based **Depository Trust & Clearing Corporation**.

“The imminent implementation of more than two CCPs clearing for the same trading venue has surfaced a number of concerns among regulators and in the industry, some of which are equally valid even if only two CCPs interoperate,” it adds. “These concerns reinforce the need to re-examine existing link arrangements and establish a transparent and standard set of conventions.”

The systemic threat, as EuroCCP described it, is distilled in this passage: “When multiple CCPs interoperate, each CCP becomes a counterparty to the other interoperating CCPs and requires additional financial resources to cover its exposure from the possible failure of any of the other linked CCPs ... Alternatives that are both scalable and sustainable and cover normal as well as extreme market conditions should be considered.”

A key piece of the agreement EuroCCP is proposing – perhaps *the* key piece – is a clause that would require members to post more collateral with clearinghouses and that would relieve them of posting collateral with each other. “Take the example of eight or nine CCPs in Europe interoperating,” Chan said. “If all of them were to have bilateral agreements, there would be over 30 agreements, which is clearly unmanageable.”

Chan said the EuroCCP proposal also has an element of democratization to it: “Interoperability will benefit trading firms by ensuring there is competition and by ensuring a choice of which CCP they want to use.”

“True competition in theory in Europe will depend on full interoperability,” she said. “Patchy interoperability is not going to deliver to market participants what they need, which is the ability to choose the CCP they wish to use, regardless of which trading platform they trade on.”

The paper, “Recommendations for Reducing Risks Among Interoperating CCPs,” puts forth four recommendations:

- “CCPs should augment their existing default funds to cover potential close-out losses in the event of an interoperating CCP’s default.”
- “An Interoperability Convention, to provide transparency of arrangements between interoperating CCPs, should replace confidential bilateral agreements.”
- “Commercial barriers to interoperability should be removed. Each market participant should be able to

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Securities Operations Week

A Publication of Capital Markets World Inc.

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Annual subscription: US\$695

MARKIT STEPS UP PROJECT TO STREAMLINE W-8 COMPLIANCE

Responding to heightened scrutiny by the U.S. government on how foreign investment income is reported, **Markit** has stepped up its promotion of a tax-form service that would consolidate certain investment-income documentation.

The project, which is in partnership with Boston-based **Compliance Technologies International**, aims to streamline the traditionally cumbersome process of keeping investors' W-8 forms readily available and up to date by making them electronic and by storing them centrally so that they can be easily accessed and shared by tax-reporting intermediaries.

W-8s are used to demonstrate that foreigners who invest in the U.S. aren't subject to U.S. tax withholdings on dividends, interest payments and so on. **The Internal Revenue Service** in the past year has become more aggressive about tracking investment income. The new posture was most vividly on display when the agency forced UBS last year to disclose the names of thousands of Americans who were hiding investment income in secret Swiss bank accounts. The IRS is now turning its attention more broadly to other cross-border taxation issues.

"Regulations are about to get more strict," **Lansing Gattrell**, director of **Markit Document Exchange**, a suite of document-management and repository services that would include the W-8 offering, said in an interview. "This is a crackdown that will require more documentation."

The expectation is that the IRS shift will create greater demand by regulators – typically through bank audits – to see W-8 forms, which by law have to be kept on file in original form and renewed every three years. What

Markit and CTI are seeking from the agency is a memo of understanding that would permit the securities industry to take part in the W-8 sharing project. "As cross-border tax issues remain at the forefront of governments' priorities, we expect the administrative burden associated with collecting and evaluating withholding tax forms to grow dramatically over the next few years," Markit said in a published statement outlining its pitch.

When the service was first proposed last June, several big names endorsed it, including **Bank of America/Merrill Lynch, Citi, Deutsche Bank, J.P. Morgan, Loomis Sayles, PIMCO** and **Royal Bank of Scotland**. "By allowing us and our clients to go through a one-time online process," **Tracey Jordal**, senior vice president of compliance at **PIMCO**, said the IRS would be lifting "an enormous personnel and paper burden from us and our clients who would typically need to fill out paper forms multiple times over each time an original tax form is needed or needs to be renewed."

Caroline A. Lumley, a Markit director of corporate communications, said in an e-mail message this week that the IRS had recently signaled a willingness to permit the service to go forward. "The IRS appears to recognize that the desire for stricter regulations must be coupled with increased flexibility for meeting those requirements (using electronic tax forms for example as opposed to hard copy which is an operational nightmare)," Lumley said. "This could have a big impact on operations and compliance departments." ✍

EXPERTS ANTICIPATE A 2010 BOUNCE IN IT SPENDING

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from 72.7% in 2008 to about 70% in 2012).

"While there are many ways to split the spending pie, the most telling indicator of future spending and growth relates to investments in new IT projects," **Jegher** says. "Unfortunately, economic conditions and the financial crisis are resulting in a slow-moving shift to increased spending on new investments."

"However, this stagnation can only last so long," he adds. "Banks will need to spend on new investments at least partly as a result of needed system upgrades. Frequently, financial institutions are running systems that are too obsolete, too slow, and inflexible. Slowly but surely, many financial services firms that rely on technologies that are nearly 30 years old are realizing the competitive advantage of modernizing their core systems and byzantine legacy systems."

Jegher's report includes several bits of geographic minutiae that collectively offer a world view of trends. Among them:

- The fastest increase in financial services IT spending

will occur in Asia-Pacific, at a compound annual growth rate of 6.2%, to US\$101.7 billion.

- Most spending still occurs in Europe and North America, which invest, respectively, 33% and 36% of global IT spending. Firms in Asia-Pacific account for 25.2% of IT spending; Latin America and Africa account for 5.7%.
- IT spending will continue to grow through 2012 at a good clip in financial services in North America and Europe at a compounded annual growth rate of 4.4% (to US\$128.8 billion) and 4.7% (US\$141 billion), respectively.
- Spending in Latin America and Africa will grow more slowly, at a rate of 3.2%, to US\$21.2 billion.

The report makes other distinctions. It finds that within the financial services industry, banking accounts for almost 50% of all IT spending. Jegher predicts that "across all industry groups and regions" securities firms in Asia-Pacific and insurance companies in Europe will have the fastest IT-spending increases through 2012

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► DERIVATIVES

AFTER RECORD YEAR, OCC SET TO CHANGE ITS SYMBOLOGY

After reporting a record number of transactions in 2009, the **Options Clearing Corp.** last week announced it would launch its **Options Symbolology Initiative** on its Web site on Feb. 12.


The clearinghouse on Monday posted details of the impending change in a note that explains how information will be reformatted on its site across seven categories of reports it publishes. The switch will affect reports on series searches, series added, series downloaded, flex prices, OCC series/contract volume and OCC daily volume.

The initiative, which is being implemented with the cooperation of the seven options exchanges in the U.S., will eliminate OPRA codes and fractional strike prices with exact expiration dates and base underlying symbols. Replacing the symbolology – named after the **Options Price Reporting Authority**, which processes U.S. options trades – is a move that is meant to offer more market information and broader standardization in reporting.

Industry-owned OCC is the biggest derivatives-clearing

organization in the world by contract volume and open interest. Its activity mirrors a steadily growing market in options contracts over the years, and defied expectations in 2009 that the market would shrink. Instead, investors – many of whom were using options for the first time – hedged their bets against the magnitude of losses they incurred in 2008.

In 2009, the clearinghouse processed 3.625 billion contracts, an increase from 3.587 billion in 2008, according to statistics posted on its Web site. It was the seventh consecutive increase on record. OCC volume in 2006 was 2.04 billion, in 2003 about 910 million and in 2000 about 727 million. In 1974, the second year the clearinghouse was open, it cleared roughly 5.7 million contracts.

The OCC is the central counterparty clearing and settlement service to 13 exchanges and platforms for options, financial and commodity futures, security futures and securities-lending transactions. 

► SETTLEMENT

DELAY IS REPORTED IN ECB'S TARGET2-SECURITIES INITIATIVE

Published reports this week say that the **European Central Bank** will put off until 2014 its **Target2-Securities** initiative. It was originally scheduled for launch in 2013.

The ECB has not publicly acknowledged the delay, but the Financial Times and Reuters have confirmed it, citing anonymous sources close to the project.

Target2-Securities, known as T2S, would create a common European securities settlement medium. The ECB's glossary of clearing-and-settlement terms defines T2S as a "single technical platform enabling central securities depositories and national central banks to provide core, borderless and neutral securities-settlement services in central bank money in Europe."

Work on the project began in August 2008 in response to growing dissatisfaction with a patchwork of European clearing and settlement whose costs have been estimated to be 10 times higher than those in the U.S. T2S would bring the euro-based platform to separate national securities depositories in 15 countries. Under the current system, investors and broker-dealers use agents to handle settlement with the hodgepodge of depositories. T2S would allow central settlement through one point of contact.

The FT reported that T2S would be delayed by nine to 12 months; Reuters quoted an ECB official saying he would "not be surprised" if it were delayed for six months.

"The project has been complicated by questions over pricing and governance, specifically how central securities depositories and their users in European

member states influence the development of the platform," the FT said. The newspaper said an ECB group would meet Friday in Amsterdam to discuss T2S, and it said the project has been problematic since its inception.

"People familiar with the matter said the initial phase of T2S, involving deciding what features the T2S system would provide, was already four months behind schedule. A four-month buffer was built into the planning for T2S but the people said it was unlikely this could be made up and likely further delays to the whole project meant it would now not be completed until 9-12 months after the original deadline. One person said: "They are running with delays on the project and they have used up all of the contingency."

In the meantime, Frankfurt-based **Clearstream Bank** co-sponsored the March 2009 launch of **Link Up Markets**, a joint venture meant to solve some of Europe's cross-border settlement issues. Its partners include securities depositories in Austria, Cyprus, Denmark, Greece, Norway, Spain and Switzerland, and its Web site says its goal is to improve efficiency and reduce costs of post-trade processing of cross-border securities transactions by streamlined interoperability on the CSD layer."

Brussels-based Euroclear provides a similar securities settlement service in a partnership between CSDs in Belgium, Finland, France, the Netherlands, Sweden, the U.K. and Ireland. 

NY FED PUSHES 4-POINT PLAN ON OTC OPERATIONS

A new report by the **New York Federal Reserve** lauds advances in the infrastructure that supports OTC derivatives clearing but says more are needed.

The report singles out the **Depository Trust & Clearing Corporation's** data repository as an example of progress. Its authors report that in the past 12 months "the market has successfully settled 50 credit-default swap corporate credit events" a drastic increase over the average of three per year from 2005-2008.

It states, however, that "stronger operational and risk-management practices" should be taken up, and that they should include better collateral management and more multilateral portfolio compression.

The authors of the report – two Fed staff members, **Theo Lubke** and **Ada Li**, and **Darrell Duffie**, a Stanford University finance professor – assert that over-the-counter derivatives weren't a "central cause" of the financial crisis of 2008-2009, but that it was exacerbated by "weaknesses in the infrastructure of derivatives markets."

"As a result of failures of risk management, corporate governance, and management supervision, some market participants took excessive risks using these instruments."

The report encourages what it calls a holistic approach and cautions against overemphasizing "one risk-reducing element," saying that "various components must function robustly on their own and synchronously."

Beyond general operational improvements, the report calls specifically for infrastructure expansion on four points:

- More clearing through central clearing counterparties "by encouraging clearing initiatives by market participants and through harmonization of capital regulations that provide additional incentives for central clearing."
- Mandatory reporting to repositories of OTC derivative trades that aren't cleared through central counterparties.
- Open publication of market prices and volume.
- Using exchanges and electronic trading platforms "for sufficiently actively traded products."

The paper – which is open for public comment – includes an endorsement of OTC derivatives as risk-management tools and sources of liquidity "if used responsibly."

In a nod to recent advancements, it elaborates on four:

- DTCC's CDS data repository. "Regulators insisted that

market participants create a central repository to log all credit derivatives trades. In addition to facilitating the processing of various lifecycle events, in late 2008, this central repository ... became a key source of credit derivatives data for regulators and the general public. Similar efforts are now underway for derivatives linked to interest rates and equities."

- A reduction in trade-confirmation backlogs. "Immature infrastructure and lack of automation had led to long processing lags between the times at which trades are executed and the times at which they become legally matched contracts. These backlogs made it difficult for market participants to adequately measure their risk exposures. Regulators set stringent targets and deadlines for dealers to reduce their backlogs and increase both automation and processing efficiency for OTC derivatives. The processing lags and backlogs of legally uncertain trades have been largely eliminated for credit derivatives and dramatically reduced for other types of OTC derivatives."
- Broader acceptance of counterparty transparency. "A dealer would commonly assign its trades to other dealer counterparties through a process known as novation – without all parties being informed of the assignment. This led to a lack of awareness by dealers of the identities of their ultimate counterparties, resulting in trade-match failures and breaks in payment flows. To address this, regulators required market participants to set up a mandatory protocol by which novating parties would obtain the consent of those parties remaining on the trade. This ensured that all parties would henceforth be aware of the identities of their counterparties at all times."
- Improvements in how bankruptcy record-keeping is handled. "A default or other market event triggering the settlement of CDS contracts could cause a scramble for sufficient deliverable bonds, artificially driving up the prices of those bonds. In response to regulatory pressure, market participants have committed to use an auction process that allows parties to settle CDS contracts without the need to deliver bonds. The auction determines a settlement price for the bond that leaves most parties indifferent between settling the CDS through physical delivery of bonds in return for cash, and settling in cash only for the net value." ✍

EUROCCP PROPOSES TRUCE AMONG EUROPE'S DIVIDED CLEARINGHOUSES

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choose which CCP they use."

- "Longer-term, further consideration should be given to inter-CCP netting, whereby a netting agent would be established to determine each CCP's net securities and cash position against the other CCPs."

The EuroCCP paper says the biggest hurdle to broad interoperability is free-market resistance to it: "It is unnatural for a CCP to volunteer to share its market with competitors. The more protected a CCP's market position, the less willing a CCP is to collaborate with other CCPs to achieve full interoperability." ✍

ECB PROMOTES RESEARCH ON “TOO NETWORKED TO FAIL”

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insurance providers and **AIG** provided an example of such critical institutions; key custodian banks or large correspondent banks play a similar role.”

“The global financial crisis that erupted in August 2007 clearly illustrated the role of financial linkages as a channel for propagation of shocks,” Tumpel-Gugerell adds. “Indeed, the spreading of the financial turmoil from the U.S. subprime mortgage market via the securitization instruments to the banks’ off-balance-sheet vehicles, and further to the banks’ balance sheets, and to other financial and non-financial sectors exposed unforeseen counterparty linkages and eroded confidence in a way which further amplified the effect of the initial shocks.” In a statement accompanying the summation, the ECB states the central assertion, that simulations designed to demonstrate ties “between financial sectors of the economy or across entire national financial systems” can expose weaknesses that would otherwise remain unseen.

“Network theory” is the until recently obscure discipline described by the researchers whose work is compiled in the report, and its proponents say its application transcends academia, and that it is a guide for central bank policy changes that could ward off the kind of systemic frenzy that saw markets collapse and credit freeze in 2008-2009.

“INTERLINKAGES” EXPOSED

“Interlinkages within the financial system are nothing fundamentally new,” the report begins. “However, business strategies developed by financial institutions over the last 20 years and financial innovations have made the system much more interconnected.”

The “business strategies” mention is a thinly cloaked reference to how the securities industry by last year had grown heavily dependent on leverage and on derivatives that included credit-default swaps, the unregulated instrument that helped create much of the carnage. The paper presents a brief and instructive chronology of events that began with a sharp decline in asset-backed commercial paper values in the summer of 2007 “when investors realized that money market mutual funds had invested in paper backed by subprime assets.” This realization led to an abrupt distrust “of all forms of private credit, especially structured products and other complex and opaque instruments, and this caused the funding for structured investment vehicles and special-purpose vehicles to dry up.”

Indeed, one unanticipated event led to another. “Difficulties faced by conduits and other asset-backed programs in rolling over their short-term funding forced them to look to bank sponsors for liquidity (this was the case, for instance, for **IKB Deutsche Industriebank** and **Sachsen LB** in Germany) or to sell assets. A crisis of confidence ensued which gripped money market mutual funds and the commercial paper market, notwithstanding their distance from the U.S. housing market.

“Such unstable dynamics, set off by increasing uncertainty

about the size of losses in the system and, maybe more importantly, about their exact location, continued in the course of 2008. Then, the collapse of **Lehman Brothers** in September 2008 transformed a pessimistic and disoriented mood into full-blown panic and paralysis.”

In short order, money market funds were affected – as in the case of New York-based **Reserve Primary**, which “broke the buck” – and a wave of money market redemptions dealt the credit markets a crippling blow. “Again, banks and companies relying on short-term funding through commercial paper or ABCP (i.e. debt backed by mortgages, credit cards and other consumer loans) could not roll over their debt, except at overnight maturities.”

THE ULTIMATE COMPLICATION

Perhaps the ultimate complication was the disconnect of information on what securities firms were doing from one country to the next or even from one market sector to another. “A key challenge is to transcend a purely national or sector-specific perspective and to take an approach that matches the global nature of financial networks,” the paper asserts.

The chief hurdle to the kind of market integration the paper implicitly proposes is an absence of good, global data. “This holds true, especially on a cross-border basis, but also at bank level,” Tumpel-Gugerell wrote. “Going forward, regulators and overseers should continue to develop ways to systematically collect and analyze data. The crisis has clearly demonstrated that data confidentiality must not stand in the way of improvements in systemic risk analysis and assessment by policy makers.”

Acceptance of better risk controls – be it through forcing OTC derivatives onto exchanges or making banks hold more capital – is of course beyond the power of any one securities firm. “Systemic risk is, in principle, outside the control of each individual institution,” the report notes. “But, by keeping liquidity buffers and capital reserves and by limiting large exposures and addressing dependencies, banks can contribute to an increase in the resilience of the system as a whole.”

Kimmo Soramäki, a researcher and software developer for Barcelona-based **Financial Network Analysis**, detailed at the October conference his work on how “agent-based modeling” can help predict sudden changes in global finance networks. “Concerning the possibility for policy makers to promote safer topologies, Soramäki referred to [London-based] **CLS Bank**, the world’s largest settlement system for foreign exchange trades, as an example where the financial links of an institution are severely restricted for the purpose of financial safety,” the ECB paper reports. “CLS is not allowed to have any non-FX settlement-related links to the financial infrastructure.”

Another example: “Sectoral barriers to banking,” like the Glass-Steagall Act of 1993 that separated U.S. commercial banking from investment banking but that was repealed in 1999. A third example: The introduction of central

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ECB PROMOTES RESEARCH ON “TOO NETWORKED TO FAIL”

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counterparty clearing for credit-default swaps through clearinghouses like those opened recently by Chicago-based **CME Group** and Atlanta-based **ICE Trust**.

Soramäki also proposed that central bankers monitor risk levels and liquidity conditions at commercial and investment banks by tapping “the same kind of network techniques used by credit card companies on customers’ payment behavior to detect card frauds.”

“For instance, payment data could be used to detect features in the timing of payments sent to and from the bank, in net outflows across different systems, in the bank’s money market activity or in the volume of cash withdrawals/deposits made by the public, factors which are rather common across available examples of failed banks.”

CREDIT-DEFAULT SWAPS; CROSS-BORDER LINKAGES

Described in one presentation at the October meeting as having played a “unique, endemic and pernicious role” in the financial crisis, credit-default swaps were pinpointed by a group of researchers who suggested that central banks implement a system of stress-testing for the CDS network. These researchers – **Sheri Markose**, **Simone Giansante**, **Mateusz Gatkowski** and **Ali Rais Shaghghi** of the **Centre for Computational Finance and Economic Agents at the University of Essex** – said they welcomed the introduction of a CDS clearinghouse, but they argued for an additional step.

“Markose et al. propose the use of agent-based stress-tests to estimate the amount of capital that a CCP should hold and the use of network indicators to make members’ contributions to the CCP’s capital or clearing fund proportional to their potential systemic impact,” the ECB report says. “The

authors also mention the possibility of changing the existing requirements on initial and on variation margins that market participants are required to post and hold as part of their risk controls.”

Johannes Lindner, an ECB economist, said that although clearinghouses increase market liquidity and transparency, they also concentrate systemic risk. “This makes the establishment of a strict risk-management framework and adequate oversight by regulators essential,” Lindner said. “Similar to the need to regulate systemic risk and systemically relevant market players in the financial sector more broadly, the risk concentration in a CCP requires the combination of different risk controls – participation requirements, initial and variation margins, and financial resources (i.e. CCP’s own capital or clearing fund) – to address the risks stemming from its participants.”

Juan Solé, an economist for the **International Monetary Fund**, proposed network analysis as a viable way to assess cross-border linkages. Solé, who has published work on the subject with two colleagues, **Marco Espinosa** and **Kay Giesecke**, borrowed medical terminology to describe how network modeling could help monitor risk.

The discipline “could give regulators a metric to identify institutions that are potential sources of contagion,” he said. “Furthermore, it can help to track contagion paths and offers a metric that can be used to find out when and whether a financial entity is ‘too connected to fail’ in times of financial stress.”

In an exercise to prove his point, Solé ran global simulations to show how credit shocks in some countries could create havoc in others. Banking systems were found especially vulnerable in four countries, all of which failed three or more of 15 simulations: Belgium, the Netherlands, Sweden and Switzerland. ✍

– *Karl Cates*

EXPERTS ANTICIPATE A 2010 BOUNCE IN IT SPENDING

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and that the slowest growth will be at banks in North America and Europe.

The Gartner report, which throws its net much wider, says IT development will probably become more customized and that it will be tailored in many cases to regional preferences. “By 2012, the accelerated IT spending and culturally different approach to IT in these economies will directly influence product features, service structures, and the overall IT industry. Silicon Valley will not be in the driver’s seat anymore,” said **Peter Sondergaard**, the global head of research at Gartner.

The report stresses what Gartner researchers say is a growing emphasis in many industries on operational technology. “OT is devices, sensors, and software used to control or monitor physical assets and processes

in real-time to maintain system integrity,” it says. “The rapid growth of OT is increasing the need for a unified view of information covering business process and control systems. OT will become a mainstream focus for all organizations.”

And in an assertion that applies across the corporate spectrum but may be especially applicable to the securities industry, it notes “the increased age of IT hardware,” and estimates that one million servers – 3% of the global total – have had their replacement delayed by a year.

“If replacement cycles do not change, almost 10% of the server installed base will be beyond scheduled replacement by 2011,” Sondergaard said. “That will impact enterprise risk. CFOs need to understand this dynamic, and it’s the responsibility of the CIO to convey this in a way the CFO understands.” ✍

► GLOBAL OPERATIONS

SUNGARD CONTINUES TO BOOST ITS PRESENCE IN BRAZIL'S BM&FBOVESPA

Brazil's **BM&FBOVESPA**, the local exchange for securities, commodities, and futures, has expanded its work with **SunGard** to further develop the exchange's automated clearing for financial and agricultural futures and options exchange-traded derivatives.

The **BM&FBOVESPA** utilizes SunGard's **GMI** clearing and accounting solution, which helps U.S.-based futures commission merchants process and clear trades on the Brazilian exchange. **GMI** also allows FCMs to have direct connectivity as clearing members with the **BM&FBOVESPA**.

The **Commodity Futures Trading Commission** approved the trading by U.S. investors of **BM&FBOVESPA** derivatives based on the **Ibovespa**, the primary representative index of the Brazilian equities market; the initiative is also expected to increase trading on a global scale. The derivatives module for the **BM&FBOVESPA** will be ready by the second quarter of 2010, and will make it easier for users to automate the loading of trades, perform bookkeeping, and calculate margins and fees.

The **CFTC's** approval may prove to be the catalyst the Brazilian market has been waiting for to let U.S. investors flood into the market. The anticipated increase in trading will be accompanied by an increase in post-trade volume, for which most back-offices in Brazil are woefully unprepared. Post-trade accounting systems for the most part are outdated, but some firms have begun to steel themselves for the coming surge. The **BM&FBOVESPA**

has seen a steady rise in its trading volumes, most notably in derivatives, and currently ranks sixth in volume globally.

Venue	Volume
CME Group	3,277,645,351
Eurex ISE	3,127,704,773
Korea Exchange	2,865,482,319
NYSE Euronext	1,675,791,242
CBOE CFE	1,194,516,467
BM&FBOVESPA	741,889,113

(As of 12/31/2008, Futures Industry Association)

The **CME Group** established its strategic partnership with the **BM&FBOVESPA** in February 2009, allowing U.S. customers of the **CME Group** access to **BM&FBOVESPA's** trading and clearing platform. The **CME Group** has a 4.9% stake in the **BM&FBOVESPA**, and the **BM&FBOVESPA** has a 1.7% stake in the **CME Group**. Over 3.5 million contracts have been traded on this link between the two venues, and the figure continues to climb – the pressing question facing the largest (and only) venue in Brazil is whether its local clients' back offices will be able to handle the volume. ✍

► SECURITIES OPERATIONS CALENDAR

Intro to the Securities Industry
Financial Markets World
January 19, 2010
New York City, NY
www.fmwonline.com

Intro to Hedge Funds
Financial Markets World
January 26, 2010
New York City, NY
www.fmwonline.com

Hedge Fund Operations
Financial Markets World
January 27, 2010
New York City, NY
www.fmwonline.com

Global Tax Reclamation
Capital Markets Consortium
January 27, 2010
New York City, NY
www.cmconsortium.com

SEC Customer Protection Rule 15c3-3
Financial Markets World
January 28, 2010
New York City, NY
www.fmwonline.com

Derivatives 101
Financial Markets World
February 2, 2010
New York City, NY
www.fmwonline.com

Derivatives 201
Financial Markets World
February 3, 2010
New York City, NY
www.fmwonline.com

Annual Operations Conference
NCSA
February 14 – 17, 2010
Miami, FL
www.nicsa.org

16th Annual Industry Forum &
Vendor Show – ISITC
Mar 21 – 24, 2010
Renaissance Boston Waterfront
Hotel, Boston, MA

Operations Conference & Exhibit
SIFMA
May 4 – 7, 2010
Desert Springs, CA
www.sifma.org

Technology Management Conference
SIFMA
June 22 – 24, 2010
New York City, NY
www.sifma.org

SIBOS
SWIFT
October 25 – 29, 2010
Amsterdam, The Netherlands
www.swift.com