



Demystifying complexity

As regulators hone in on OTC derivatives in an effort to elicit transparency, financial services firms are recognizing the importance of reference data for all asset classes, but complex assets present their own set of challenges. Gregory D. L. Morris reports.

In mid-May, US regulators proposed sweeping measures that would bring most exotic investments under their control for the first time. That was just the latest round of intended reforms in the wake of the credit crisis, and it came as the financial sector works to get an accounting and record-keeping handle on complex asset classes. By all accounts, reference-data management for complex assets is still a “home-grown” operation. Taken together, all of the commercial installations are estimated to have penetrated not more than 10% of the potential market of USD 1 billion to USD 2 billion worldwide.

Some financial institutions indicate that they feel able to handle exotics as part of their broader EDM (Enterprise Data

Management) programmes. Others say they are waiting for firm regulatory guidance before going too far down any one path. “The financial crisis has caused a greater recognition of the importance of reference data for all asset classes,” says Neil Edelstein, senior director, product solutions, GoldenSource. “In many cases there are separate repositories for derivatives and other complex assets. What we are looking for is foundational risk, a basic repository for equities, fixed-income securities, and things like collateralised mortgage obligations, all of which can feed the risk system from a regulatory, audit and compliance perspective.”

The challenge, says Edelstein, “is that there is no way to store all this data together right now. Typically we would

see attributes and descriptive data in the security master file, but you would not see counterparty data in the same place. The answer is a simpler database that can be parsed, compared, and triggered.” The whole idea, he says, is to demystify reference data and bring it to the front end for business users.

Financial institutions that have had EDM processes in place for some time agree that is the goal, but some banks and brokerages maintain that because of their nature, complex assets are not likely to be fully integrated with other reference data. An executive director at one large bank says that his goal is to have exposure-reporting capabilities for all asset classes, complete with attributes, counterparty information and

accounting data. To do that, the bank is in the process of consolidating its reference data systems. At Société Générale, data management is not simply an archival exercise, but a part of real-time asset management. “We have mathematical rules that allow us to calculate on the fly,” says Rachid Lassoued, global head of financial engineering, Société Générale Securities Services. “Volatility can be based on strike price or on time to maturity. We need the ability to take a three-dimensional cross-section of the data including all market correlations.” Lassoued says there are four stages to complex asset data management: acquiring, backdating, normalising, classifying and recording to the repository. Around all of that, SocGen needed the ability to calculate within the repository and set formats for new assets.

It's all in the detail

Yet for all the upheaval of the financial crisis, not much has really changed in reference data, even for complex asset classes, says Phil Lynch, president and CEO of Asset Control. “What has changed,” he stresses, “is that people cannot rely on third-party evaluations of data any more.” Lynch says that the credit crisis has given corporate officers and IT leaders “a rare opportunity to use political capital to get people on the bus for reference data,” especially for complex asset classes. “It is hard to dispute the importance of these issues after everything we have gone through,” he says. Bringing the reference data loop

full circle, Brian Sentence, CEO, Xenomorph, suggests that the people who know the most about complex assets are not necessarily the technologists in the back office. The key, he says, is to make reference data available to all non-technology people. “What is more important, knowing SQL or knowing the asset?” asks Sentence. “The barrier between knowledge of product and knowledge of system has got to be broken down.” Much of the historic problem with installations in this sector had to do with the sponsoring person or department within the client’s organisation, and whether or not there was sufficient authority, says

had one positive effect in that it has put a spotlight on clients’ internal costs. “This is a business that traditionally was plagued with long-running and very expensive implementations,” says Plane.

“We are maturing,” says the director of a merchant bank in New York. “But to create one standard for complex asset classes is a far-reaching idea.” He agrees that “identification and classification are the two lynchpins of data management,” but also notes that reference data are tools, not business objectives. That is why existing structures and previous efforts to organise reference data



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Stuart Plane, Cadis Software

Sentence. While that situation has improved, he states the problem is with vendors who take installation to mean customisation, when it is supposed to mean deployment. Yet even with faster installations, the competition is still in-house proprietary solutions, says Stuart Plane, director, sales and marketing, Cadis Software. However, he says the current economic environment has

must be retained, says Plane. Whatever has already been done in-house should not be ripped out root-and-branch. “The process in place is the foundation for our installation,” Plane continues. “We often come in on the back of two or three previous internal attempts. Those may not have been completely successful, but they are crucial to our overall design.” //