

Wind of Change

Brian Sentance, CEO of Xenomorph, finds time out of the company's busiest period in 14 years to speak to Eileen Lee about the change wrought by the financial crisis

Enduring budget cuts and cost control as the financial crisis sweeps across the globe, Xenomorph has found the pot of gold after the storm. Although institutions have held off buying over the past year, an increased emphasis on data and risk management has brought the company's offerings into demand. Brian Sentance finds time out of the company's busiest time in 14 years to speak to Eileen Lee about what the company has been up to for the past year and if the financial crisis has brought about any change.

Has there been any change to Xenomorph's general mission or direction because of the financial crisis?

Ironically, the crisis has had some positives coming out of it but, of course, not without its difficulties during it. The crisis seems to have driven people more in our direction. Our clients want to manage all the data that feeds their risk management and trading systems. In light of

the crisis, there has been a lot more emphasis on risk. I think people are aware that data and better management of data, better control and understanding of the data being used to feed the pricing models, the pricing models themselves, valuation, and risk management need strengthening. That plays into our integrated approach of combining the reference data, market data, and derived data, and allowing it to be cleansed, controlled, and analyzed further.

How has the increase in regulation and emphasis on risk management, stemming from the credit crunch, subprime crisis, and failure of quant funds, affected Xenomorph?

On the regulation side of things, everyone is more aware of it, and trying to understand where it eventually settles and what effects it will have. The broad theme is there will be more regulation, both in the areas of risk management and how you bring products to market, more complex products, and the

procedures around that. Everyone is more aware that greater regulation means the regulators will be looking at things more stringently. That puts another driver on top of their own business needs to understand risk.

Seeing what has happened with the crisis, senior management at some companies realized that risk management needs to be improved out of the interest of the shareholders and the company in general. From a vendor perspective, increased regulation can sometimes drive some of the business opportunities. The risk management process may be alright, but the quality of data going into them is something that is driving new business for us.

From the clients' perspective, there are three main motivators to do things currently. One is their own vested self-interest for improvement in risk management. The second is more pressure from their clients for better risk management, valuation, and better reporting of exposure to particular counterparties. Lastly, there is regulatory pressure.

The crisis has also brought about a convergence of market and reference data management. Data management, like most technical terms, is a very vague term, and its meaning differs from one vendor to another. However, reference data management has long been an area of the market that is reasonably clear. That area has to do with how you might identify different securities, different entities, or maybe some of the data terms and conditions for all the securities that are being traded. Basically, reference data management is a well-defined market.

Market data management is a less clear term. There are a number of companies, for instance in the USA, where they are looking at man-

agement of real-time data and tick databases, and where the problems are more related to large volumes of real-time data, but comparatively simple data types. The sheer volume of it makes the data management problem difficult. Xenomorph seems to fit well into this changing market, as we have elements of both of those areas; we are able to cope with reference data, market data, and particularly in the area of the management of more complex data and instruments, making it easy to manage data such as curves, spread curves, volatility surfaces, swaption cubes, etc. – things related to derived data.

You can have great data management, as well as fantastically clean and complete data, but why bother if ultimately you defer to a trader pulling data down into spreadsheets from Bloomberg or other sources for pricing and risk management? Put another way, if transparency is to be achieved, data management needs to extend to the front office. Ultimately, the data that gets used, probably the derived data and calculated data coming out of it, is the most valuable data of all, but yet that is secondary or even ignored by many in the field of data management. We want to completely integrate the analytics and the data management so that end users get all of the functionality they need in one place. Some of the reference data management companies have picked up on this change in the market relating to the management of more complex data, the curves surfaces, derived data, etc. We have been doing a bit of work with GoldenSource Corporation, which is one of the leading companies in the reference data management space. Version one of a product they put together based around some of our technology will be released over the coming few

months. We are also working on a number of other partnerships, in the area of both data management and instrument valuation.

We have also noticed that the needs coming from different regions have different flavors. In Europe and Asia, there seems to be a lot of interest in the area of data management for risk management, management for curves, time series data, all of the reference data. The risk managers don't really think the same way as data management companies, which like to separate data by type, but rather they just need all of the

data sets used by the risk management system together. Europe and Asia seem to be good markets, as people recognize the need, whereas in the USA there seems to be more of a gap between the management of tick data in the front office and the management of reference data in the back office.

I find that a bit peculiar because US banks are dealing with risk management just as much as the rest of the world. This is possibly because Europe and Asia have more experience or historically have slightly more complex products than the USA, whereas the USA has more emphasis on exchange-traded products and higher-volume data problems.

In Asia and Europe, our clients

tend to come from investment banks and asset management institutions that either have projects in risk management or valuation of derivatives, where our data and analytics infrastructures are needed.

We find ourselves dealing with more hedge fund clients in the USA, as it tends to be more on the trading side of things. Although the hedge funds market has contracted, there are still quite a lot of new funds being set up, and it has been an area we have been working on. The emphasis tends to be more front office, tick data, backtesting of trad-

ing with the hedge funds client base we have in the USA.

We also find that the US market is a harder one to break into at an institutional level. Many of the US institutions want to know who our client references are, but when we list big UK or European names, even tier one banks, they still want to see who the American institutions are. I guess it's very much a chicken and egg situation for any foreign company that is growing in the USA. We actually did secure a large US bank as a reference client; however, the crisis caused this bank to cease trading, which was one of the less positive aspects of the crisis for my US colleagues, unfortunately. But we keep working hard, we have great product, and it will come in the end!

How have the requirements and demands from customers changed or evolved during 2009?

It has been a real year of contrasts. At the start of the year, sales opportunities were few and internal cost control was vital to the company. Now, there seem to be many sales opportunities around and the challenge is one of controlling the growth of the company. Right now is probably the busiest we have been in the whole 14 years that we have been around.

As you enter any downturn, clients hold off from any buying. A year

ago, people were panicking about doing any projects because nobody knows where the market is heading. Eventually, you get to a stage where human nature and optimism causes people to panic about not doing something. They get a bit worried about competition, that they have not invested for a while, and they get back to projects. I believe people are entering into that frame of mind. This latent demand is also combined with a crisis that has brought about a stronger emphasis on data, data management, and risk.

For the software community, things were hard, as budgets were put on hold. For the past year, we have been trying to make sure that existing clients are happy, and that the cost control side of things

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doesn't inhibit the business. I think we have done quite well in terms of moving ahead with product development and progressing existing relationships with our clients. Those were the main challenges at the start of the year. Later in the year, we found ourselves moving into hiring mode; it's a matter of meeting cost control with a different emphasis – how can we meet the needs of the sales that we are

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achieving but at the same time not increase the risk of the company and what we're doing, both in the negative economic environment and the positive.

What have been the priorities for product development this year and have they been impacted by the events of the past 18 months?

The main priority is coming to market with what we have been doing with Microsoft on getting our time series databases to work inside of the SQL server – that has been the main area of work. We are just about to go into beta test with one of our clients. There are so many advantages from a technology and management point of view for clients, and they seem very interested in it. We have a number of clients lined up to beta test and eventually take on this new version of the product.

With that offering, we are combining the performance of better and faster databases, designed for very specific kinds of data, historical data, more complex data sets, etc., but hosting it within a standard space, a relational database management system. We are getting the combination of standard database management tools, but still able to offer the database performance with historical data that some of the

quants and risk managers are needing as well. So, that has been the main area of work in terms of product development – it really hasn't diverged, instead it has probably been made more important due to the increased emphasis on risk over the past 12 months.

How do you envision the requirements of the quantitative community changing as we enter the next decade?

There has been a lot of debate in the areas of pricing models. There is probably more work to be done to find a sweet spot between increasing the complexity of a pricing methodology to cope with new risk factors in light of the financial crisis, and ensuring that this complexity does not make the model less robust.

Sometimes it doesn't necessarily mean that a complex model is always

better; what you are trying to find is something which is a sweet spot around complexity combined with robustness. I think there will be a lot more emphasis on the usage of data and understanding of how data feeds those models, why data isn't always perfect, how the model responds under different scenarios, and the sort of stress testing of the input parameters. I think in the derivatives mathematics area, there will be a change in emphasis. From our perspective, it means that there might be more projects in the area of pricing model validation and valuation, which we definitely see growing.

There has been a lot of interest in the valuation services market, where there has been a number of companies trying to provide valuation services. We see valuation management as a growing area, together with risk management. These are the two areas that we will be looking at in Europe and Asia, with the regulatory-driven background to some of the clients' projects.

In that regard, we are strengthening the pricing infrastructure, the management of analytics, and the management of data within our system. Because we see that the management of derived data, analytics, and pricing models should all be part of the same integrated process. Now, the systems that are available in general are very much siloed around a particular kind of data. The pricing-model vendors don't know as much about data as they think, the risk managers assume the world of data is perfect, the reference people don't know as much about market data as they should. Sitting in between all of these different areas is Xenomorph, and given the way the market has changed, I think it's a good position for us.

From a technology perspective, we will keep emphasizing our strengths in dealing with large data problems and complex data sets. We will try to use our knowledge of all of these different areas – pull them together to help our clients manage their valuation, risk management, backtesting on trading. So, we'll be looking at greater integration between all types of data, statistical analytics, and pricing models – all of those processes together as an integrated framework for them to look at those kinds of problems and do them quicker.

What are Xenomorph's goals and plans for 2010 and beyond?

Geographically, there are a few interesting things going on. We plan to open one or two offices in mid-2010. We have recently increased the number of clients we have in Paris, so there may be a little bit of expansion in that direction. South America has been generating some sales for us, as Brazil seems to be an emerging market with some interesting ideas and problems to deal with.

There are firm plans in terms of an Asian expansion. We are looking to strengthen some of the regional sales that we are doing, maybe strengthening some local resources and building upon what we already have.

There is a little bit of internal debate in terms of the exact location, but we will have some Asian time zone support and a development office as a bare minimum, perhaps in Singapore or Hong Kong. We already have some Asian clients, so we may be looking to expand on the sales side out there as well. Currently, we are managing the global support we have out of our London and New York offices.