ACI THE FINANCIAL MARKETS ASSOCIATION

ACI BRIEFING

NEWS FROM THE FINANCIAL MARKETS ASSOCIATION
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A MESSAGE FROM THE PRESIDENT

DEAR ACI MEMBERS AND READERS,

Three questions dominate my message to you this quarter:

What is left of the money markets?
Where has all the trust gone?
What happened and why?

I start with a slogan that has provided one of the backbones of ACI – The Financial Markets Association since its launch more than 50 years ago…

MY WORD IS MY BOND

This slogan, which was strongly adhered to by all traders, created a well-functioning, healthy and liquid market for the entire world, but I fear those days are gone and we may never see them again. Now the markets are driven by news that is full of rumours, part-information and various personal hypotheses.

MANFRED WIEBOGEN

continued on page 2

Contents

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ACI Briefing is Published by: profit loss PROFIT & LOSS IN THE CURRENCY & DERIVATIVE MARKETS

This is not the time for us as traders, or for politicians, to seek to apportion blame for this disastrous evil, let us first recover, indeed survive, in order to ultimately restore confidence in the financial system. Then we may seek the answers to what went wrong and what we can do to avoid a similar occurrence in the future.

On the invitation of the French EU Presidency, ACI participated in EUROFI 2008 in Nice during September. The event is a two day think tank that works on EU priorities and to develop proposals to improve the financial services industry for the ECOFIN Council. It attracted high calibre politicians, lobbyists, central bankers and bankers, who met to discuss what was then the growing sub-prime liquidity crisis.

The messages from the meeting were, in short, very clear:

- The credit market turmoil of the previous year has cost banks more than $510 billion worldwide (up to September 14, 2008)
- EU Financial Services Commissioner Charlie McCreevy plans to issue a policy paper on bailouts next year – specifically looking at early intervention tools for dealing with ailing banks
- Edmond Alphandery, Chairman of CNP Assurances, urged, "It is high time to revamp crisis management plans"
- Capital and accounting rules must be revised "soon"
- The 27-nation European Union is implementing a "road map" to establish lines of authority to deal with the financial industry crisis
- Pervenches Beres, Chairwoman of the European Parliament's Economic and Monetary Affairs Committee, stressed, "There is still a lot to do"

During the Nice meeting, it was repeatedly stressed that there was more bad news to come and unfortunately the opinion was correct, for just days later the liquidity crisis developed into a crisis for the US investment banks and some insurance associations.

So, what demands is the financial industry likely to face? I would summarise them as follows:

- Transparency and, again, transparency!
- A focus on governance, especially ethical and moral standards
- A need for strong ethical leadership
- No "black boxes" – valuation needs to be clear
- A reappraisal of the role of the ratings agencies – do we trust them too much?
- The banking system will need to raise its buffer through more capital
- Closer cooperation between the industry and regulators

It may be that some regulation is needed – but we definitely do not need over-regulation in our markets. ACI's Council, which comprises more than 60 countries, will meet on November 6/7 to discuss and analyse the consequences of the crisis for our industry and how ACI needs to address these issues and help restructure the markets.

ACI invites you to provide your input for this workshop, which affects us all. We invite all of your thoughts and comments, as well as questions you feel need to be asked. Please submit your comments and questions to deputymanager@aciforex.com under the header ACI Market Crisis Workshop.

It is not all bad news in our industry, however, and the systemic crisis is overshadowing some good news. Foreign exchange reserves are up 32.4% since September 2007 and reported to be around $7,642 billion as at June 2008. The FX market is six times larger than trading in US Treasury Bonds and 30-times greater than trading on the New York Stock Exchange. Estimated FX volume in June 2008 was more than $3.5 trillion per day.

To engage all members of our industry and to discuss the opportunities and challenges, your Association has inaugurated a series of Q&A sessions entitled "Industry Talk". In this issue you will find the first of the series; we talked to David Woolcock, head of bank sales at FXall, and CEO of FXMarketSpace, Mark Robson for their views on transforming the FX industry.

ACI continues to evolve to better serve its members, soon after the last issue of ACI Briefing was published, ACI Asia was officially launched. The goal is to distribute more competence and responsibility to the various regions in which ACI operates. This will create additional value for all of us – more details can be found inside this issue.

Let me end by saying, "*there is a stronger need for ACI than ever before*". In the forthcoming weeks and months, ACI's Executive Board will seek to position ACI even further in the spotlight as it works with everyone in the industry to restore a functioning market environment.

Manfred Wiebogen
President, ACI – The Financial Markets Association

FOCUS ON THE NEW ACI OPERATIONS CERTIFICATE

On September 1, 2008 the ACI Operations Certificate became available in the German language. Over the past decade fundamental changes in global financial markets have resulted in more competition amongst market participants and a range of new supervisory regulations demanding high profile operations teams.

"Operational efficiency and best practice have become essential for operations teams to beat the competition by being a low-cost producer with high quality and controlled risk in this low- margin market," says Andreas Gaus, Member of Board of Education and Head of Operations Working Group.

ACI'S EDUCATION BOARD IN SESSION

In order to meet these demands ACI implemented in 2007, together with its new education partner Frankfurt School of Finance & Management, the new ACI Operations Certificate which replaced the previous Settlements Certificate. In 2008 it was translated into German language.

"Global financial markets are currently facing challenging times. More than ever, skilled and motivated people are a key success factor for leading market players", states Christoph Niggli, Chair of ACI Board of Education.

Now operations staff and related groups from all over the world have the opportunity to benefit from an education programme which will become the benchmark for foreign exchange and money market operations.

A redesigned syllabus with revised and updated topics and a large set of brand-new questions reflect the changing requirements of our business, supporting operations teams and related groups to cope efficiently with stronger competition in the financial markets and to smooth co-operation with supervisory bodies.

The new Operations Certificate also helps candidates to develop a front to end treasury view in terms of process, promoting a better understanding between the trading community and operations staff.

The Operations Certificate covers overall financial market issues, deal capture, trade entry and confirmations, settlement, netting and clearing, reconciliations and investigations, treasury systems and data management, risk management, controls, compliance and documentation, foreign exchange, money market, derivatives as well as short-term notes and bonds.

The Operations Certificate is designed in particular for operations staff with at least two years of experience and seniors who want to increase their skills and knowledge as well as prepare for future positions. It is also offered to operations-related groups such as other trading room support areas, internal and external auditors, compliance and risk officers, product control and vendors.

For further information on ACI education and the new Operations Certificate, please visit www.aciforex.org.

SAMPLE QUESTION. WHICH ANSWER DO YOU THINK IS CORRECT?

What does "modified following" business day convention mean?

a. The date will be the next common business day, unless that day falls in the next month, in which case it will be the first preceding business day.

b. The next common business day.

c. The preceding day that is a business day.

d. The next common business day that is on exactly the same numerical day as the preceding payment.

FREQUENTLY ASKED QUESTIONS

What happens to my ACI Settlements Certificate qualification*?*
The new Operations Certificate replaced the previous Settlements Certificate which expired in December 2007. But your existing Settlements Certificate qualifications remain valid.

What exactly is new compared to the Settlements Certificate?
Old topic baskets have been updated or restructured according to changing market requirements and supervisory regulations. There is now a greater emphasis on risk management, money markets, derivatives, controls and compliance. New topic baskets were added, such as overall financial market and front to end treasury views, as well as short-term bonds and notes. The number of questions in the examination has increased from 60 to 80.

Where can I get more information on the structure, the topics and the exam procedure?
The structure, the topics and the exam procedure as well as the grades are described in the syllabus which you can download from ACI's website www.aciforex.com under "Syllabi".

How can a candidate prepare for the Operations Certificate?
It should be noted that ACI provides an examination service and does not provide preparation courses for the exams. Such courses are delivered by third parties, and information including a study guide and a list of trainers can be found on our website www.aciforex.com under "How to Study ".

Where can a candidate register and sit for the examination?
A candidate can register and sit for the exam at one of Prometric's test centres (Prometric-Code: 310-010). More information can be found on our website www.aciforex.com under "How to Register".

Has the price changed compared to the old Settlements Certificate?
Yes, the price is now at 250 € plus VAT at the local rate.

(The correct answer to the sample question is "a")

Christoph Niggli
Chair of ACI Board of Education Andreas Emser
ACI Director of Education

ACI EDUCATION IMPLEMENTS NEW APPEAL SYSTEM

On 1st September 2008 a new appeal system for ACI's exams was implemented in order to give candidates the opportunity to have their failed exam reviewed.

An exam candidate can appeal according to the following regulation:

"The candidate has the right to appeal the result of his or her failed exam to ACI's Board of Education within four weeks after sitting the exam. Appeals may be made by candidates who experience physical, organisational or technical difficulties at the test centre, or who believe that doubts exist about an exam question. In the latter case, the candidate must offer a detailed submission about the specific question and topic basket. The request for an appeal is to be submitted on ACI's website exclusively by the candidate who failed the exam, and will only be accepted if the candidate makes a detailed statement on the reason for his or her appeal. Once a decision on his or her appeal is made the candidate cannot submit the same appeal again."

If the appeal request is accepted the Appeals Committee decides the appeal within a short period of time.

ACI MIXES WITH THE WORLD AT SIBOS

Reinforcing Vienna as this year's financial conference venue of choice, the city followed its hosting of ACI – The Financial Markets Association and ICMA meetings by staging SIBOS 2008. ACI's President Manfred Wiebogen, along with many other ACI members, attended the meeting and heard from a range of speakers on subjects as diverse as the establishment of an "SEC" for the European Union, the opportunity for the Russian rouble to become a reserve currency and the opportunity for global financial services firms in Asia.

Of course, given the events of late September, there was much discussion over the stability and future of the financial system. On the sidelines of the meeting, Wiebogen held an informal meeting with Rene Karsenti, President of ICMA to discuss the myriad of issues facing the financial markets today.

MANFRED WIEBOGEN WITH RENE KARSENTI

ACI ASIA INAUGURATED

The evolution of ACI – The Financial Markets Association took a major step forward in the Summer with the official launch and inauguration party of ACI Asia. The launch took place at the headquarters of the Hong Kong Monetary Authority and was attended by in excess of 100 guests.

Manfred Wiebogen, President of ACI – The Financial Markets Association, told the gathering, "The establishment of ACI Asia in Hong Kong is the result of the accumulative efforts of many during the past two years, and ACI is extremely proud and supportive of those efforts and the end result. I hope that further development of the financial markets in the Asia region will continue apace and that they will prosper in the future."

In response, Eddie Tan, Regional President of ACI Asia, said: "We hope to bring treasury market practitioners under one umbrella, establish common professional standards and work closely with the regulators, such as our good host the Hong Kong Monetary Authority, with which we will continue to maintain a close communication and cooperation. Amongst ACI Asia's many challenges are how to continue to be relevant to our profession and how to invest and motivate the next generation of leaders in our market place. ACI Asia will not take these challenges lightly."

ACI Asia brings together 14 National Associations in the Asia Pacific region – all of whom, along with honoured guests from mainland China and other Asian countries – were represented at the inauguration. In congratulating ACI Asia on its launch, Joseph Yan, Chief Executive of the HKMA, told guests: "Asia is a region of rising importance in the global context, particularly in terms of finance. It is therefore absolutely right for the first regional office of ACI to be established in Asia and, if I may add, for it to be established in Hong Kong, as the truly international financial centre in the region. The HKMA and the Treasury Markets Association will offer full support to the activities of ACI and ACI Asia."

For a report on the proposed activities of ACI Asia, please see the June 2008 issue of ACI Briefing, which is available at www.aciforex.com.

THE ACI FORUM – TRANSFORMATION OF THE FOREX INDUSTRY

As part of its ongoing strategy to engage all members of the industry, ACI – The Financial Markets Association is pleased to launch Industry Talk, a series of Q&A sessions with leading figures from different sections of the industry. In the first of the series, the Association is discussing The Transformation of the Forex Industry with Mark Robson, CEO of FXMarketSpace and David Woolcock, Head of Bank Sales at FXall.


MARK ROBSON

"E-trading has provided more customers with access to an increased number and range of currencies. It has been a major factor in the FX market's growth"

ACI: According to the latest BIS Annual Report in 2007, average daily turnover in FX instruments reached $3.2 trillion. This represents an outstanding annual increase of 18% over the past 6 years. What do you believe to be the main factors behind this growth?

Mark Robson, FXMarketSpace: I think electronic trading platforms and algorithmic trading have contributed the most. Most e-trading platforms were still relatively new in 2001 and concentrated on building their customer base.

In the years that have followed e-trading has become one of the most common ways to trade FX, allowing organisations to access increased price information, to trade an increased number of currencies, and to realise increased efficiencies in both trading FX and booking those trades. There have also been efficiencies for sell-side organisations, as e-trading has allowed them to offer FX prices and services to a larger number of participants, helping to enlarge the FX market.

Algorithmic trading has also driven market growth. As computer programs have become more sophisticated, being able to use an algorithm to not only identify a suitable trade but complete the trade as well, less reliance has been placed on human beings as less manual intervention has been necessary. The result of this is that the cost of FX trading

"Different participants have diverse requirements and it is important to ensure that all trading strategies and execution methods are fully supported."

has been reduced, meaning that even smaller, high frequency trades have become profitable if done by an algorithm. This in turn has led to an explosion in the number of FX trades being dealt and has increased market liquidity in general.

David Woolcock, FXall: There is particularly strong growth from the investment community, both real money asset managers and hedge funds, who are investing in currencies as an asset class, and we are seeing growth on both the relationship trading and anonymous trading sides.

Different participants have diverse requirements and it is important to ensure that all trading strategies and execution methods are fully supported. Asset managers, for example, value a complete workflow, control and compliance solution.

Active traders and algorithmic strategies have become an increasingly important part of this growth, which reflects their increasing role in other markets. According to BIS in December 2007 they accounted for half of the increase in total FX turnover over the past three years.

The credit crisis has undoubtedly contributed to the recent growth in volumes, and has been an interesting test-case regarding the structure of the FX market. This unusual period in the credit market has seen FX not only survive but thrive. The market has seen exceptional volumes and the prime broker/interbank cleared model has worked effectively and efficiently throughout the current period of stress.

ACI: The BIS estimates that as much as 20% of the daily spot FX transactions are linked to algorithmic trading. Various commentaries have reported that this type of auto trading has been growing rapidly since 2005. With that in mind, what are likely to be the main challenges to, and developments within, the FX market environment?

MR: I would categorise them thus: we may face trading platform capacity issues and speed and latency issues (the fastest have the advantage). How organisations reduce latency and reduce their total transaction cost will also be important. Transaction cost analysis (TCA) will become a bigger feature.

Elsewhere, I believe banks will focus more on the profitability of trades and assign a value to *both* flow and spread. There will also inevitably be an increased focus on risk reduction, especially in terms of both counterparty and settlement risk.

DW: The current ECN model is becoming increasingly popular, particularly with active traders who are used to ECNs for equities. Now that they are trading currency as an asset class, they are looking for similar functionality in the FX space. That is one of the reasons we launched Accelor, FXall's ECN.

The current liquidity picture is changing however, and in the current climate the balance has shifted towards relationship based trading over the past six months as participants see the value, and take advantage, of the relationships, credit lines and liquidity that are available. Relationship trading is seen as a valuable way of trading in the market, as prime brokers become less willing to commit credit lines to anonymous venues.

ACI: Although EUR/USD, USD/JPY and GBP/USD remain the most traded currency pairs, their share of overall turnover has declined over the past few years. Why do you think we are seeing growth in the other currencies?

MR: E-trading has provided more customers with access to an increased number and range of currencies. Previously when trading over the telephone customers had to call their sales person and ask for different quotes in perhaps less liquid currencies. Trading over the internet allows them to see streaming prices in these currencies, and then click and trade.

ACI: Where are you seeing growth?

DW: We are seeing strong growth outside the G10 currency pairs, in particular in the South African rand, Indian rupee and Turkish lira. These currencies are becoming more actively traded and volumes are being driven by the carry trade.

We are also seeing exceptional growth in the Russian rouble, and this was most notable between December 2006 and December 2007, and was predicated by convertability in July 2006.

ACI: As a consequence of the sub-prime and liquidity crises, volatility in the FX market has increased over the past year. Do you consider this as a good or bad development for the FX markets ?

MR: I think there is probably some happy medium level of volatility for the markets, but generally I think the question is where there is a satisfactory trade off between volume growth, profitability and risk. I think the market is handling this well for spot FX.

"The current environment has been an interesting test case for e-FX, with volatility driving huge volumes and systems more than standing up to the challenge, thus proving how stable FX is as an asset class."

DW: Despite the difficult conditions affecting those institutions exposed to more volatile asset classes, the FX market remains buoyant. The current climate has been an interesting test case for e-FX, with volatility driving huge volumes and systems more than standing up to the challenge, proving how stable FX is as an asset class.

In the current climate the balance has shifted towards relationship-based trading over the past six months as participants see the value, and take advantage, of the relationships, credit lines and liquidity that are available. Relationship trading is seen as a valuable way of trading in the market, as prime brokers become less willing to commit credit lines to anonymous venues.

However, demand for anonymous venues remains as institutions look to manage and offset the risk from relationship trading by using multiple venues. This practice is becoming increasingly important for institutions as advances in technology mean they can easily and efficiently connect to multiple venues, and the risk associated with connecting to only one venue has risen. Competition amongst anonymous venues will therefore be on speed, latency, price and efficiency.

ACI: Most FX Trades are nowadays conducted through electronic trading platforms. Thus the relationship between FX traders has been practically replaced by screens. How do you view this development for the FX Community?

MR: Electronic trading brings many benefits to the whole market, like lower costs, efficient processing and increased price transparency, but there will always be a need for manual trading for perhaps larger sizes or more difficult trades. For these trades relationships between FX traders remain vital. Electronic trading has allowed sales staff to move away from handling plain vanilla trades, towards helping them to develop deeper, high value customer relationships.

DW: This is a complex issue, because, for example, under MiFID, every bank, custodian or asset manager that provides FX as part of an investment service in Europe will be required to implement and document best execution policies. Best practice is a major driver for the adoption of online trading, because using an online trading system can help improve efficiency, transparency and auditability. It can facilitate compliance with corporate governance, reporting and accounting regulations, such as Sarbanes Oxley and IAS 39. It can also make it easier to achieve and prove best execution.

Industry associations such as ACI, which acts as a talking shop for traders who meet less frequently, also play an increasingly important role as a forum for discussion. Events such as ACI's are beneficial as an opportunity to speak with many participants from various geographies in one place, to discuss the important issues affecting the FX market.

ACI: What other, general, issues do you think the industry needs to focus on?

MR: Currently, and given recent events in the financial markets, risk has become probably the single most important factor. The market needs to reduce both replacement risk and settlement risk, whilst increasing efficiency and reducing costs.

"Risk has become the single most important factor in financial markets. The market needs to reduce both replacement risk and settlement risk."

DW: We view the role of technology as one of the most important enablers in the FX market. Rather than encouraging all participants to migrate to a single solution, technology has provided access to solutions that are tailored to their specific needs. FXall's focus is on providing its clients with a range of products which best support their diverse needs. Technology is facilitating solutions which allow banks and wider participants to choose how they are served, offering multiple ways of trading and combining different products where necessary.

Electronic trading is key to providing transparency in the FX market, and we are seeing this with the automation of a greater number of products, such as NDF's for example. Electronic trading provides full audit, compliance and control functionality, which is important for all participants, and asset managers in particular. FXall's priority is in providing the range of solutions that, together or in isolation, achieve the best results for clients.

ACI NETHERLANDS VISITS GERMANY

As part of its ongoing educational work, ACI Netherlands recently organised a two-day study trip to Frankfurt: the financial capital of Germany as well as the place of business of the European Central Bank.

The aim of the study trip was to visit different market participants in Frankfurt and attend different presentations centred on topics and themes which relate directly or indirectly to financial markets and in particular to money markets and FX-markets. The trip included visits to the ECB, Bundesrepublik Deutschland Finanzagentur, Clearstream Banking Frankfurt, Dresdner Kleinwort, Commerzbank and inter-dealer broker Carl Kliem.

The trip provided a unique opportunity to visit and meet interesting and major market participants in Frankfurt and take a look behind many scenes of financial institutions at the heart of our industry.

RUSSIA CELEBRATES DEALER'S DAY

ACI Russia was a leading player On August 18, 2008, when the Russian market "celebrated" the 10th anniversary of the Russia default, from which the modern Russian market has grown. The celebration was held in the Moscow club "Gogol" and the day was elected to be unofficial holiday for dealers and all financial markets' professionals due to great role which they played in the history of Russian financial markets – the events of 1998 being the first serious trial for local market professionals.

This event was offered as a Dealer's Day by Moscow International Currency Association in 1999 and since then has been sponsored and conducted by MICA for the previous nine years up. Usually it has been celebrated by a large party in one of the Moscow clubs with a concert from a rock group. This year the event was supported by ACI Russia and sponsored by "platinum" sponsor local electronic broker Delta and international electronic broker ICAP EBS, which is expanding its business in Russia. About 600 people from banks, brokers, exchanges, regulators came to the club to celebrate this memorable day.

It was not only a social occasion, however, for it was preceded by the General Assembly of ACI Russia, which saw the election of a new ACI Council. Serious talk about the future of ACI in Russia attracted the attention of all the community and during the party about 30 new application forms were filled in to became a member of ACI Russia.

Tradition stated that the cultural program of the party included a rock group concert and this was accompanied by an exhibition of the newspapers from those memorable says in August 1998. The Party was great success and appeared to be one of the most remarkable in this year for the Russian FX&MM community.

ACI SERBIA HOLDS GENERAL ASSEMBLY

ACI Serbia recently held its General Assembly from September 19th to 21, 2008, the Association met in Subotica (in the northern part of Serbia) for networking, discussing markets and to hold its 33rd Annual General Assembly.

The event was attended by170 delegates, of whom 32 delegates were from institutions abroad and 148 represented 35 financial institutions from Serbia. Amongst the guests were: Manfred Wiebogen (President, ACI International), Vojin Bjelica PhD (Honorary President, ACI Serbia), Godfried de Vidts (Chairman, Euribor ACI) and Edo Iglic (Deputy GM, National Bank of Serbia).

A special presentation on Collateral & Liquidity Management was delivered by de Vidts as part of the event.

48th ACI
WORLD CONGRESS

CAPE TOWN 2009

The 48th ACI World Congress comes to South Africa.

The hosting of the 48th ACI World Congress offers the Financial Markets industry an opportunity to showcase the prospects that exist in Africa.

The World Congress is a convergence of global intellectual capacity. The congress has been structured to provide ample opportunity for delegates to deliberate and explore new ideas. The event is well attended by captains of the industry where decision makers, deal makers and like minded individuals are all assembled in one place for three days of networking

Date: 12-15 March 2009
Venue: Cape Town Convention Centre, Cape Town, SA

For more information and to register, please visit www.aci2009CapeTown.com

US CFTC ESTABLISHES FX FRAUD "SWAT" SQUAD

As retail foreign exchange becomes a bigger part of our industry and continues to attract investors from other asset classes, so the global authorities are taking a keener interest in ensuring the market functions properly and according to stringent standards. Following the passing of the US Farm Bill by the US Congress, the Commodity Futures Trading Commission (CFTC), which was given extended powers under the act, is taking quick action by establishing a new special task force.

The task force is to focus on fraud in the retail forex market and will cooperate with other regulators and 'criminal authorities'. The forex swat team will be made up of an undisclosed number of dedicated staff and will start investigating and litigating fraud in the off-exchange retail FX market effective immediately, says a spokesperson for the CFTC.

It is part of the division of enforcement, led by acting director Stephen Obie, who was promoted to the role in July. Obie says: "Forex fraud impacts investors of all stripes. With the creation of the retail forex task force, the CFTC has committed the resources necessary to expand its efforts to identify and prosecute those who commit fraud in the retail forex market."

Even before the task force was created the CFTC was catching and prosecuting the fraudsters, and it is thought this will speed up now that there are dedicated resources and stricter capitalisation rules.

The Farm Bill sets down much stricter requirements for net capital to be held by Forex dealer members; a year after the enactment of the Farm Bill dealer members will be required to maintain net capital of $20 million. Data from the CFTC indicates that nearly half of all the 150 registered firms have less than $20 million in capital. Some of the larger online retail FX trading providers are waiting in the wings for the undercapitalised to flounder.

Reputational risk remains a key issue for many institutions in the foreign exchange market, especially as the lines blur between what were traditionally viewed as 'professional' and 'retail' markets. Improved access to the core markets through a series of linkages, means that some of the top banks are moving increasingly closer to interacting with retail clients, which in itself raises an issue for ACI members.

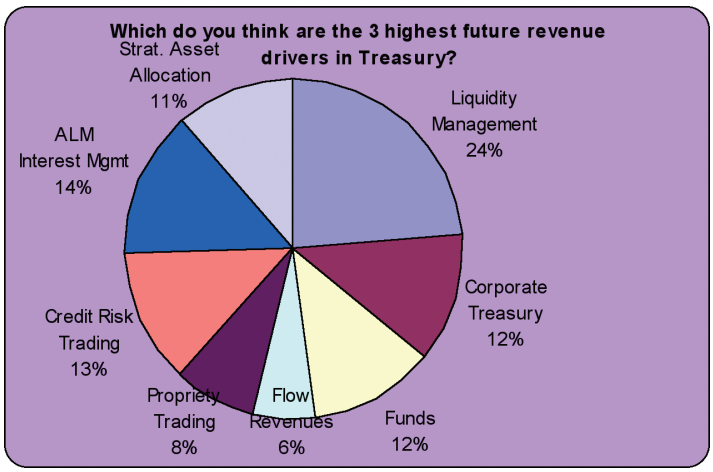
Manfred Wiebogen, President of ACI - The Financial Markets Association, says, "ACI believes it is critically important that all industry participants maintain the highest possible standards of professionalism and ethics. This was one of the main reasons ACI developed The Model Code, which promotes best practice in financial markets. ACI fully supports the regulatory agencies as they seek to improve industry standardsud in our industry."

FUTURE REVENUE DRIVERS IN TREASURY

At the occasion of the 47th ACI World Congress in Vienna earlier this year, hundreds of treasurers met from all over the world: not only from the Western hemisphere but also from the booming new finance centres in the Middle East and South-East Asia.

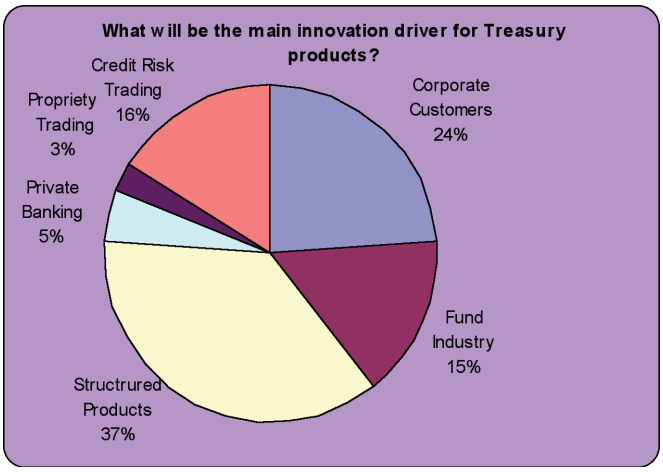
Finance Trainer, a provider of seminars and online training courses, took this excellent opportunity to get in touch with treasury personnel. The company conducted a survey asking treasurers for their opinions regarding future revenue drivers, the biggest challenges and main innovations in the treasury business. The questionnaire attracted 136 responses from Congress participants (representing some 20% of all delegates). Therefore the results can be considered as a fair representation of treasurers' opinions.

A majority of respondents believe the most important treasury revenue driver to be ALM (asset and liability management). Although the recent liquidity crisis might have coloured the results of this poll somewhat, the importance of liquidity management, interest rate management, cashflow management and strategic asset allocation is clear – these points were mentioned by more than 55% of respondents. Further important future revenue drivers are considered to be trading in credit risk and the corporate treasury function itself (more than 12% each). Less important for the future seems to be proprietary trading, as indicated in Chart 1.



These statements are supported by the answers provided

to the second question – which tasks are the biggest challenge for a successful treasury? First of all, treasury professionals want to have proper credit risk mitigation (more than 28%). In the second instance, treasury product innovation is considered a big challenge (19%). Stated as very important are also treasury support services such as IT solutions (17%) and back-office (16%). Banking regulation and accounting seem to be considered less important challenges (both about 10%, see Chart 2).



Respondents were most unanimous when answering the last question concerning the main innovation drivers for treasury products. General opinion (more than 60% of respondents) has it that structured products and corporate treasury are the most innovative areas. Further, credit risk trading was quoted by more than 16% and the fund industry by 15% of visitors. Private banking (less than 5%) and proprietary trading (less than 3%) seem to be regarded as less innovative.

The conclusion taken from the survey is that according to those treasury professionals present at the ACI World Congress in Vienna, the most important aspects of a successful treasury are asset and liability management, good risk mitigation and innovations in structured products and corporate treasury. While the second stage of the liquidity crisis in September has created short term issues, these opinions are very much based upon a longer term view of the industry.

Summary by Martin Macko, Finance Trainer and ACI

FX BUSINESS CONTINUES TO GROW

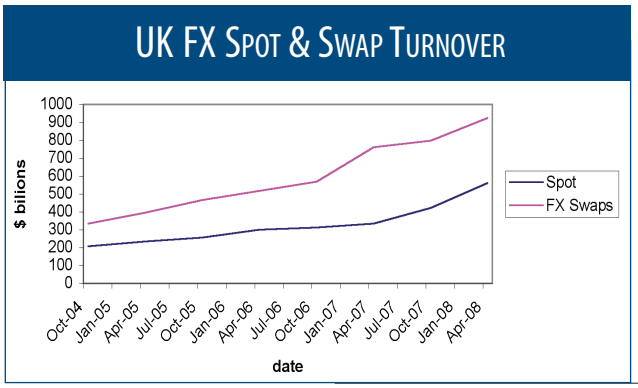
Whilst the credit crunch continues to dampen activity in certain financial markets, there is no sign of the foreign exchange market contracting given the recent data surveys from the world's FX committees. There were thoughts that the tremendous growth seen in FX turnover over the past four years peaked with last October's data which came amidst the volatility spike following the events of August 2007, however they can be put to rest.

Such is the growth in turnover that together, surveys from six committees (Australia, Canada, Japan, Singapore, UK and US) indicate an average daily turnover approaching $3.3 trillion per day in just those six centres. This compares to a figure set by the Bank for International Settlements last year which established average daily turnover at $3.2 trillion globally. Given that the FX committee surveys do not include Continental Europe or Hong Kong – both major centres in the global markets – turnover is clearly still rising strongly.

Whilst general turnover rose comfortably, there were darker signs for FX options markets, however, where turnover declined year-on-year in Singapore, US, Australia, the UK and Canada, and was flat in Tokyo.

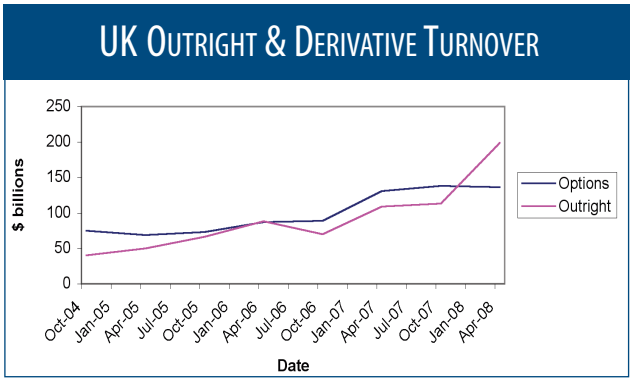
A good indicator of how much the foreign exchange market has grown can be found in the fact that at $1.82 trillion per day, the UK alone has all but matched global turnover in the 2004 BIS survey. The latest JSC survey offers a broader look at the UK market by not only including three additional institutions (bringing the total to 33), but also breaking out NDF volumes and breaking down volume by execution method. The latter brings it into line with the Canadian, US and Japanese surveys.

While all product groups saw gains in the UK survey compared to October 2007, FX options turnover fell from April 2007, registering $112 billion per day in the latest survey compared to $118 billion the year before. Overall derivative turnover was slightly higher at $136 billion per day, due to an increase in currency swaps turnover to $24 billion per day from $13 billion per day the year before.



Once again, for the second survey taken during the credit crunch period, a big part of the centre's overall growth came from spot transactions which saw a 67% year-on-year increase (and a 32.4% increase from October 2007) to $560 billion per average day. Although there were healthy increases in customer-orientated transactions – a 65.8%

increase from $82 billion to $136 billion per day) the eye-catching statistic is the doubling of turnover with non-resident banks from $150 billion to $300 billion per day. Turnover with UK banks also rose, but at a much slower rate from $103 billion in April 2007 to $124 billion in the latest survey.



In terms of spot transactions only, the dominance of the electronic broking systems is evident in the JSC report, which finds that a daily average of $260.4 billion is executed in this fashion. Next most popular venue for execution which will be heartening for the banks but may also reflect the impact of the credit crunch are the single bank trading platforms. The JSC says that a daily average of $102.5 billion is executed in this fashion, above the $85 billion dealt direct with customers, $71.7 billion on the multi-participant systems and $58.3 billion direct with other reporting banks.

Unsurprisingly given the dominance of electronic trading in spot markets, the lowest share of turnover by execution method is held by the voice brokers which execute an average of $53.2 billion. That story changes significantly if one looks at the overall picture, where voice brokers are actually the third most popular method. That, (an average of $347.6 billion is executed through the voice brokers per day) is the good news, because the most popular method is via electronic broking systems, probably the voice brokers biggest rivals. $509.8 billion per day is executed in this fashion, just in front of $494 billion per day direct with customers – something that reflects the advisory function.

Inter-dealer direct transactions saw $324.6 billion in April 2008, while the single bank platforms saw $204.9 billion and the multi-participant platforms $149.7 billion. As this is the first survey that the JSC has broken down by execution methods no comparisons are available, it should also be noted that the aforementioned numbers are not adjusted for double counting.

Overall, 42.6% of all foreign exchange business in the UK is executed electronically, in spot that number rises to 68.6%. This compares to 44.0% and 55.7% respectively in the US survey.

In other products, just over 50% of all outright business is executed electronically, 18.2% of NDFs, 30.5% of forward volume, 7.8% of currency swaps and 12.7% of FX options. This data set does not include those transactions that may be executed by the hybrid method, i.e. a voice broker using a proprietary system.

Customers seem quite happy to use electronic execution, overall 42.5% of non-bank customers' volume in the UK was executed electronically, 41.5%-worth of other financial institutions' business and 46.2% of non-financial institutions' activity. Again, comparing this to the US survey, customers overall execute 9.8% of their business electronically, other financials 41.8% and non-financials 30.2%.

The JSC survey also breaks out FX prime brokerage turnover and the survey indicates that in the spot market at least, penetration remains light with just over 14.3% ($80.3 billion) of turnover executed via a prime broker. The average ticket size of spot transactions was $1.78 million and the average prime brokerage ticket was just over $830,000.

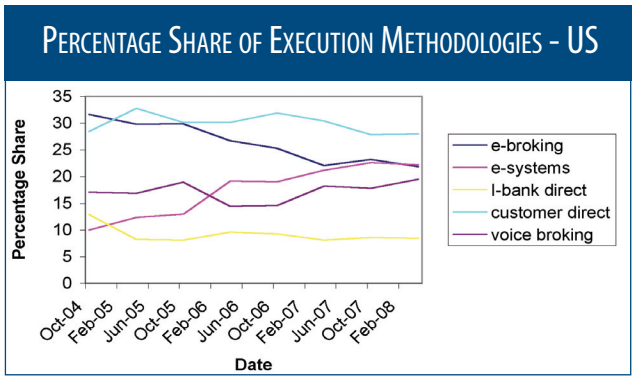
Overall, turnover via prime brokerage was measured at $182.3 billion per day, or 10% of overall turnover. Average transaction size in the UK market is a shade under $5 million at $4.92 million, this compares with 3.12 million for the US survey.

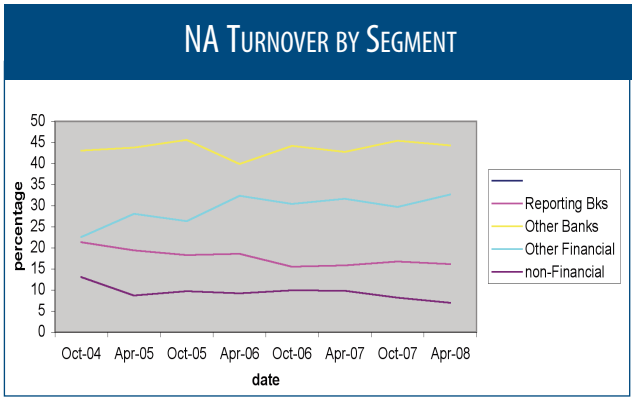
Back on the product front, outright forwards saw good business in April 2008, registering a daily average of $174 billion compared to $109 billion a year earlier. This is an even more impressive performance given that in the latest data the JSC breaks out NDF data ($25 billion per day) which was previously included in the outright forward category. Growth was spread evenly across bank and non-bank counterparty segments in outrights, NDF volume was primarily other banks ($16 billion per day).

In FX swaps the market shook off a dip in turnover in the October 2007 survey, rising from $799 billion a year ago ($755 billion in October 2007) to $925 billion in the latest survey. Year-on-year there was actually a steep decline in FX swap turnover with UK banks, from $273 billion in 2007 to $192 billion in the latest survey, but activity with non-resident banks ($507 billion from $335 billion) more than made up for the deficit. In customer terms, turnover rose steadily over the year and now registers $226 billion per day.

The decline in FX derivatives turnover was largely the result of a decline in usage by non-bank institutions, which saw turnover fall from $46 billion in April 2007 to $36 billion in the latest survey. This does represent a recovery form the nadir of October 2007 when turnover registered $25 billion per day with non-banks.

The top four currencies saw their share of turnover decline across the April surveys, in percentage share terms the US dollar, euro, Japanese yen, and Sterling represented 153% of turnover (as part of 200% - due to the fact that two currencies are involved in each transaction). In the April 2007 survey, these currencies shared 166% of turnover.





NORTH AMERICA IN GOOD SHAPE

Whilst the rate of expansion in the US could not match the pace of that in the UK, the centre – and Canada – did see growth in all products save for FX options. On a year-on-year basis, overall turnover was up 15.7% to $715 billion per day in April 2008, however it was only 2% higher that October 2007's $700.8 billion.

Spot trading, as was the case in the UK, rose strongest, by 43.5% year-on-year to a daily average of $393.3 billion. There was actually a 7.8% decline in the outright forward segment to $93.2 billion per day and FX swaps rose 2.5% to $194.1 billion per day. Both of the latter product segments showed small increases from the October 2007 survey.

As normal in the FXC survey, other dealers was the largest sector in turnover terms, registering 44.3% of business – slightly down from October 2007's 45.1% but up from April 2007's 42.8%. Next largest sector was other financials which was responsible for a 32.7% share, from 29.7% six months' previously and 31.7% the year before. The share of non-financial customers continues to decline in overall terms, from a 9.8% share of turnover in April 2007, the latest survey registers it at 6.95% (8.2% in October 2007).

In actual numbers, other dealers averaged $316.7 billion per day in April 2008 (up from $264.2 in April 2007); other financials averaged $233.6 billion ($195.6), non-financials $49.7 billion ($60.5 billion) and reporting dealers averaged $114.9 billion, from $98.0 billion a year before.

The e-channel's share of the US market remains a little volatile – while at 44.0% it is up on April 2007 (43.25%), the ratio of trades executed electronically has fallen from October 2007's 45.8%.

In trend terms there is similar volatility in how business is executed. Electronic broking systems represented 21.9% of turnover in the latest survey, down on 22.1% the previous April and 23.2% from October 2007. What will be heartening for the single- and multi-dealer platforms (the FXC does not differentiate) is that electronic trading systems saw an increased share from April 2007 (21.2%), registering 22.2%. This was slightly down on October 2007's 22.6% share, however.

Equally heartening will be that electronic trading systems have acquired 29.8% of all spot FX business in the US, which makes them the largest transaction venue. Electronic broking volumes declined year-on-year in percentage share terms (they rose in actual terms) to represent 26% of turnover from 30.1% in April 2007. This means that customer direct flow, which was slightly higher at 26.8% (from 26.4%) is the second most active method of execution.

Voice brokers continue to fare reasonably well, acquiring a 19.5% share of turnover in the latest data, up from 17.8% in October 2007 and 18.2% in April 2007. Customer direct business remains the largest sector at 28.0% of all turnover, this is down from April 2007's 30.4% and roughly similar to October's 27.9%. In spot terms, voice brokers' share of the market is steady at 11.6% from 11.7% a year before.

The top six trading firms accounted for 58.07% of turnover, the top 12, 83.13% of business. In spot terms the top six saw 70.46% of business and the top 12 had an 85.89% market share.

Meanwhile, traditional turnover in Canada rose year-on-year according to the Canadian Foreign Exchange Committee (CFEC), from $53.3 billion in April 2007 to $63.6 billion in April 2008. That said, turnover did decline slightly from the October 2007 survey when the CFEC registered average daily volume of $65.4 billion. In derivatives terms, Canada saw a daily average of $2.7 billion in April 2007, down from $3.1 billion in October 2007 and $3.0 billion in April 2007.

Again, spot volumes jumped to $17 billion per day from $14.8 billion in October 2007 and $11.8 billion in April 2007. Over the same period, outright forward volume registered $3.7 billion in April 2007, $4 billion in October 2007 and $5 billion in April 2008. FX swap volume at the same time registered $37.8 billion, $46.5 billion and $41.5 billion respectively.

Activity in the Funds market saw spot volumes driven higher from October 2007 to the latest survey by inter-dealer turnover, which rose a massive 326% in $/CAD for 302% growth in all spot currencies. While other financial counterparties saw turnover increase by 25%, that with non-financials fell by 8%.

In total, customer volumes declined by 6% from October 2007 to April 2008, this was entirely due to a 21% decline in non-financial turnover, which more that negated a 6% increase in other financial turnover.

Again, possibly reflecting the credit crunch and increase in volatility, Canadian traders continue to shy away from electronic trading platforms. Not only was the share of the single dealer and multi-dealer platforms stable at 1% and 2% respectively, but that of electronic

broking systems fell steeply from 31% in October 2007 (which was itself a decline from 32% in April 2007) to 23% in April 2008.

ASIA CONTINUES TO BUILD STEADILY

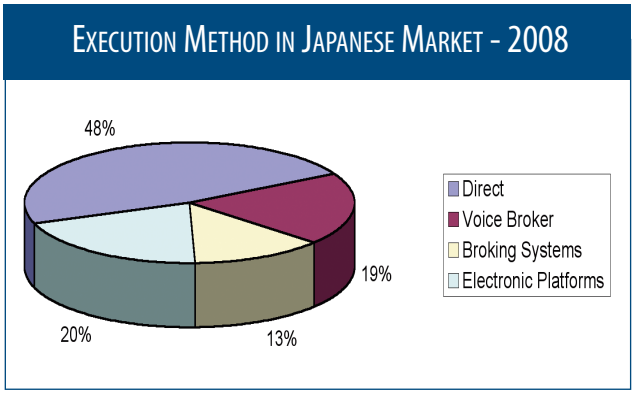
As far as the three Asia-Pacific surveys are concerned it was a steady picture. In Japan, average daily turnover rose to $302.5 billion per day from $240.3 billion the year before, while in Singapore turnover rose from $284.3 billion to $299.2 billion – this in spite of a sharp decline in FX derivatives turnover. In Australia, however, where the Australian Foreign Exchange Committee (AFXC) has also started releasing regular survey results, turnover declined slightly from a daily average of $176.3 billion to $163.0 billion. In Australia turnover is up, however, from the October 2007 survey, which registered $155.5 billion.

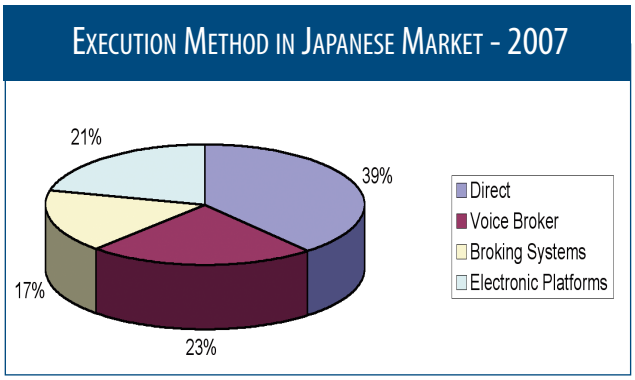
The Japanese survey bucked the global trend a little as FX swaps grew by the quickest rate, 37.7% to a daily average of $159.6 billion. FX derivative turnover was flat of the year, while outright forward turnover rose 28.9% to $28.4 billion per day. In contrast to the UK survey in particular, spot turnover under-performed in relative terms, rising 12.9% to $105.3 billion per day.

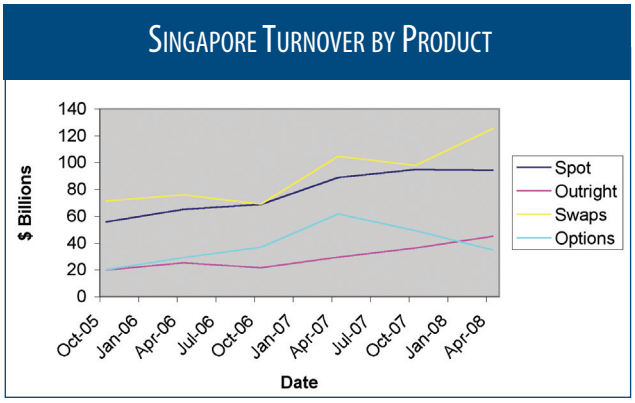
Customer transactions accelerated at a quicker rate that those between dealers, the former grew 42% to $64.4 billion per day, the latter by 22.1% to $238 billion. Customers were clearly keen to hedge exchange rate risk, spot turnover with this segment more than doubled from April 2007 to $26.3 billion (from $12.1 billion), while outright forwards rose 84.2% to $20.3 billion. FX swap turnover with customers rose 21.9% to $15.7 billion per day, while FX options business also increased, 2.1% to $2.1 billion. Inter-dealer turnover rose across the board, most strongly in FX swaps (50.3%) and outright forwards (26.8%).

In the latest survey, 71.4% of turnover is with overseas counterparties, compared to 69.5% in April 2007 and 63.3% in April 2006.

Japanese counterparties are still under-using electronic trading in relative terms, in the latest survey 33.0% of turnover is executed using electronic means, the bulk on the electronic trading systems (undefined between single and multibank platforms) which saw 20% of the overall turnover, and the balance on electronic broking systems, which saw 13.0% of the overall.







Whilst customers execute 7.5% of overall turnover on electronic trading systems, in numerical terms the trend is higher, as far as inter-dealer turnover is concerned, electronic trading systems saw their ratio of turnover fall as well as the headline number. There is a reasonable spread in terms of market share, with 58.7% of overall turnover shared among the top five firms, 28.6% among firms rated sixth to 10th and 10.4% between those rated 11th to 16th. Overall, 87.3% of turnover in Japan is shared between 10 institutions, a similar ratio to the US committee survey. CHECK

In Singapore, whilst it was bad news for derivatives turnover which fell in both categories, turnover in traditional products rose steadily across the board. Spot turnover rose by just over $5 billion per day to $94.1 billion, while outright forwards rose from $29.3 billion to $45.0 billion. Swap transactions saw turnover rose to $125.2 billion from $104.7 billion.

The vast majority of business is transacted with offshore counterparties, 89.7% of spot business goes cross border, slightly down from April 2007's 90.4%. Meanwhile 88.1% of outright forward business is cross border (up from 86.2%); 85.2% of FX swaps is offshore (82.0%); as is 89.1% of FX options business (91.1%).

The AFXC survey is more in line with those in the UK and US in that FX swaps turnover declined while spot rose. Average daily volume in spot was $56.3 billion per day, up from $44.3 billion in April 2007 ($46.6 billion in October 2007); that in outright forwards was $9.2 billion, down from $14.5 billion ($9.6 billion); and in FX swaps it was $91.9 billion, down from $110.7 billion in April 2007 ($93.1 billion). Currency swaps turnover rose slightly year-on-year, while that in FX options declined, the overall declined from $6.7 billion in April 2007 to $5.5 billion a year later.

Non-financial institution volumes declined year-on-year from an average $17.8 billion in April 2007 to $12.1 billion. Much of the decline was due to FX swap turnover with non-financials declining from an average of $9.3 billion in April 2007 to $2.8 billion in 2008 – evidence of the credit crunch in action perhaps.

MARKET PARTICIPANTS AND REGULATORS ALIGN OVER FX

A group comprising major dealers and buy-side firms active in pushing improvements in the operational infrastructure of the global over-the-counter (OTC) derivatives markets have for the first time included measures in foreign exchange.

The group, which has been working with the Federal Reserve Bank of New York to improve derivatives processing in credit and equity products, agreed to submit regular FX operating data and performance metrics to regulators on a quarterly basis.

"FX derivatives processing is at a more mature stage than that of other derivatives' asset classes. Dealers will begin to submit regular reporting of performance metrics to provide a basis for supervisory monitoring and possible future industry performance targets," the group said in a letter sent to the Federal Reserve Bank of New York and other international regulators.

Measures were also put in place in the OTC interest rate and commodities derivatives space for the first time.

The new measures are in accordance with the policy statement of the President's Working Group on Financial Markets from 13 March 2008. A new target was set in interest rate OTC derivatives. By 31 October, 65% of eligible trades are to be processed by an electronic platform. This will rise to 75% by 31 January 2009. Aged confirmations cannot exceed two business days of trading volume by 30 September.

The measures follow on from a series of meetings, the last of which was held on 9 June between US and international regulators and market participants.

The Managed Funds Association (MFA), which attended the meeting, has worked in tandem with the sell-side participants, composed of 17 major dealers, to improve efficiency and reduce systemic risk in the derivative space since 2005. Together with the major dealers the alternative investment industry body signed a letter to the New York Fed president with operational targets and commitments in March this year. These have now been improved upon with the latest proposals.

In a letter dated 31 July to New York Fed President Timothy Geithner, the group emphasises trade date matching as a key to reducing systemic risk in the derivatives arena. As part of the long term goal of matching on trade date it has set several interim goals.

Among these, market participants are committing to increase the timeliness and accuracy of immediate post-trade processing of credit derivatives beyond the target levels set in March 2008. The measures also include developing a robust central clearing infrastructure for OTC credit derivatives with the objective to launch index products in 2008.

Reducing the number of outstanding credit derivatives trades through multilateral trade terminations and incorporating an auction-based settlement mechanism into standard credit derivatives documentation by the end of 2008 are also highlighted.

The group is also committed to improving collateral management practices, including conducting weekly portfolio reconciliations by the end of 2008.

The major dealers first addressed the issue of improving efficiency in the credit derivatives market in 2005. Since then credit derivative confirmation backlogs have fallen approximately 93% while electronically confirmed trading has risen from 53% to more than 90%. During this time period, credit derivative volumes have risen by more than 200%. Equity derivatives backlogs have fallen 70% from levels in mid 2006. About 95% of interdealer trades are now processed on electronic platforms.

"These improvements to the derivatives infrastructure are important to strengthen the resiliency of the financial system," says Geithner.

Participants agreed to provide Geithner with a further update, detailing plans for achieving long-term processing goals in each OTC derivatives asset class, by 31 October.

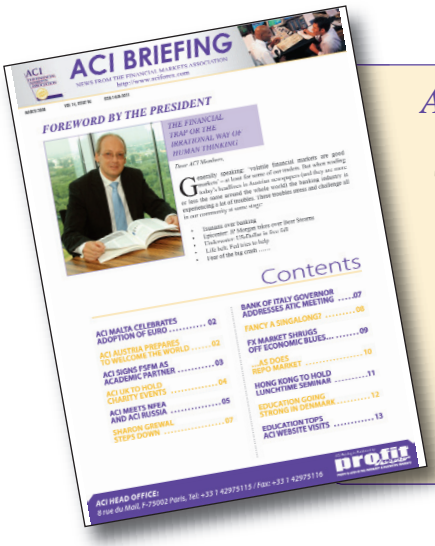
UPCOMING EVENTS - UPDATE

34TH ICA CONGRESS

SHARM EL SHEIKH
NOVEMBER 13-16 2008

48TH ACI CONGRESS

CAPE TOWN
MARCH 12-14 2009



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