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The global newsweekly for over-the-counter derivatives professionals

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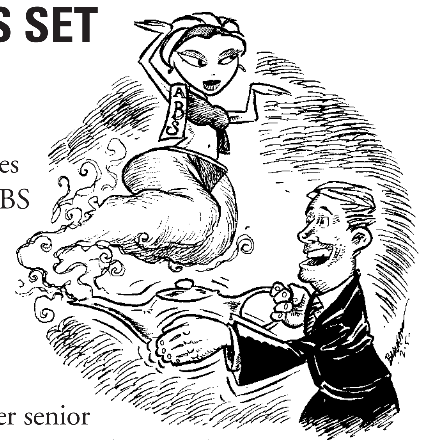
Web Exclusive

Morgan Stanley has hired an executive director in equity structured products from **Citigroup** in New York.

For the full story, go to *DW*'s Web site (www.derivativesweek.com).

LEVERED SENIOR SYNTHETIC ABS SET TO TAKE OFF



Leveraged super-senior tranches of collateralized debt obligations which reference synthetic asset-backed securities figure to take flight as shops with significant mezzanine ABS inventory are eyeing the play as a way to offload senior risk from their books. "We have placed a decent amount of mezz and don't want to run ahead of ourselves and place more risk than can be managed," said an official at one European house.

Goldman Sachs closed the first leveraged tranche of super senior ABS last month in a private deal, according to market players. One player said

(continued on page 15)

OPTIONS ON DIVIDENDS APPEAR ON DEALER RADAR

Client demand is driving dealers to look at ways of pricing options on stock dividends. Dealers have built up exposure to dividends through selling equity forwards and in the last few years have sold this exposure in swap form on to hedge funds at a discount. But the funds, now sitting on substantial gains from the swaps, want to purchase downside protection. And dealers have also started to see that being able to sell dividend exposure in option form would be more attractive to a wider range of clients—for a start, it could be packaged up as a bond for real money managers.

Firms including **Barclays Capital**, **Citigroup**, **Goldman Sachs** and **Deutsche Bank** are

(continued on page 15)

Oil Me Up!

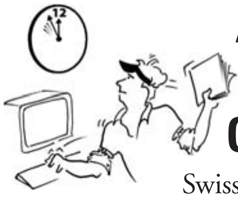
INFLATION TRADERS TAKE TIPS ON ENERGY MART

Inflation traders in the U.S. are honing energy trading skills, on the back of fuel-price induced volatility in the front end of the inflation market. Consumer price index inflation has been buffeted by rising oil prices in the U.S., whereas in Europe, because much of the price at the gas pump is tax, increases feed through less directly to inflation figures. One strategist said September's U.S. CPI inflation was 1.2%, of which 1% was attributed to energy prices.

The U.S. inflation market is dominated by receivers of inflation and this makes shops extra sensitive to inflation volatility, as their books are one-sided. In Europe, traders can use liquid inflation futures to hedge, but in the U.S., CPI futures have struggled to gain liquidity.

One trader in New York said he was starting to learn how to trade energy in order to

(continued on page 15)



At Press Time
Swiss Re Preps Structured Credit Push

Swiss Re is to launch into credit structuring, particularly CDOs, in Asia on the back of setting up a desk in Hong Kong. "CDOs are the main driver, but we're open to all potential derivative products," said **Xin Fu**, v.p. in Hong Kong. Fu and **Jack Vogel**, managing director, transferred to Hong Kong from New York this summer to establish the desk. "There's a lot of potential growth in Asia, including Japan, and we expect to close our first CDOs as well as hire additional staff before the middle of next year," added Fu.

Increasing acceptance of credit derivative products in the region as well as regulatory easing in such markets as Taiwan, which has opened its insurance sector to CDO deals, led Swiss Re to the desk. Fu noted that in addition to structuring credit deals, the team will also look at making markets and potentially buying existing outstanding CDOs from clients, which separates the firm from much of the competition in the region. Vogel did not return calls by press time.

Rivals said Swiss Re should be able to carve out a niche in the market given its large balance sheet, strong credit rating and ability to buy deals for its own book.

ABN Honcho Heads To DWS

Rupertus Rothenhaeuser

ABN AMRO's **Rupertus Rothenhaeuser**, head of the private investor group in Hong Kong, is joining **DWS Investments**, the asset management arm of **Deutsche Bank.** He joins in a new role as head of structured fund sales in Frankfurt, to spearhead the development of derivative-wrapped fund products for the German market. Starting in January, he reports to **Stephan Kunze**, head of distribution for Europe and Asia-Pacific at DWS in Frankfurt, who also joined from ABN earlier this year (DW, 7/1) to build up retail structuring.

Rothenhaeuser said he is looking forward to the challenge of building up the business in his home market. "There's so much potential here," he noted, explaining that with large amounts of money flowing into funds on a monthly basis in the country, there is a good opportunity to offer structured fund-linked instruments that offer additional upside over traditional products. Initially Rothenhaeuser said he will start with interest rate related fund products, given the anticipation in rate rises but eventually will offer derivative wrappings across asset classes.

Rothenhaeuser said a handful of structured product marketers will be added to the team early next year.

At ABN, Rothenhaeuser oversaw the firm's re-entry into the Hong Kong warrants market this year (DW, 5/13), and prior to that he was the global head of retail derivatives at **BNP Paribas** in Paris. **Hui Yuk Min**, spokeswoman at ABN in Hong Kong, confirmed the departure, but declined to comment on a replacement.

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Delphi To Lead Charge Into Cash-Settled Indices…

The credit market was gearing up to test out cash settlement of credit derivative indices last week. If an auction to determine the recovery value of outstanding index-linked credit-default swaps referencing **Delphi Corp.** runs smoothly, dealers said, it could make cash settlement the industry standard for resolving future credit events affecting the indices. Officials predicted the next CDX index roll in March will likely include procedures for cash settlement.

"Physical settlement made sense until the development of index trading," said **David Mengle**, head of research at the **International Swaps and Derivatives Association**, at an ISDA seminar on credit derivatives last week. The popularity of index trading has allowed more market participants to reference bonds than actually hold them, making physical settlement impossible for index players.

The Delphi auction, scheduled for last Friday after *DW* went to press, follows similar procedures established after the bankruptcy filings by **Collins & Aikman**, **Delta** and **Northwest**. Five hundred seventy eight firms, including all the major dealers, many hedge funds and other counterparties, signed up to ISDA's amended Delphi CDS Index Protocol for participation in the auction, which will be administered by **Markit** and **Creditex**.

…Set For Painless Physical Single-Name Settlement

Dealers were expecting physical settlement of single-name credit-default swaps on **Delphi Corp.** to be smoother than anticipated on first news of the default. Last month, when the corporate defaulted, dealers were believed to have tens of thousands of outstanding contracts—more contracts, it seemed, than bonds they could physically deliver. Since Delphi's default Oct. 8, however, dealers have been netting CDS exposures and tearing up contracts. Officials this week said they have only a fraction of the contracts they had a few weeks ago and that they expect to physically settle well under half of them.

The **International Swaps and Derivatives Association**'s hybrid settlement procedure called for cash settlement of index trades and physical settlement of single names (DW, 10/21).

Citi MD Cites Equities Chief In Discrimination Suit

Ramesh Menon, **Citigroup**'s head of U.S. structured products, is suing the firm for racial and national origin discrimination, and singled out **Jim Forese**, global head of equities, and **Joseph Elmlinger**, global head of equity derivatives, as the two individuals responsible for allegedly creating an environment that favors white males over minorities and women. Menon doesn't see discrimination as a company- or division-wide phenomenon, said his lawyer **Richard Horowitz**.

In a complaint filed on Oct. 21 at the U.S. Southern District Court of New York, Menon lays out a detailed case citing what he deems to be a consistent pattern of preferential treatment of white males at the expense of minorities he claims were equally or more qualified for promotions and bonsuses. He lists a series of recent departures from the equities business in the complaint and suggests a number of the individuals felt their opportunities for growth were limited at Citi. Menon is suing for a combined USD138 million: USD38 million in damages and USD100 million for the discrimination. "My client believes that it's not an overt white man's club, but when push comes to shove, it always falls one way," said Menon's lawyer.

Meanwhile, Menon continues to work at Citi and although he and his colleagues are aware of the suit, work relations remain largely intact. "[Elmlinger and Menon] chat about business all the time," said a person close to the situation.

Forese was not available to comment and Elmlinger referred calls to spokeswoman **Christina Pretto**, who said Citi believes the lawsuit is without merit and will contest it vigorously. "Citigroup is fully committed to fair employment practices and to providing a respectful and professional work place free of discrimination," she added. Menon referred calls to his lawyer, who said his client is willing to pursue the claim as long as necessary.

Record Low Vol On CDS Index Sparks Option Buying Spree

Implied volatility on the European iTraxx Crossover hit an all-time low of 35% last week and sparked an uptick in long-dated option buying on the index. Investors viewed the fall on December-dated options as confirmation of fourth quarter stability and in response stacked up on at-the-money options, combined as straddles, with maturities to March. One trader said volumes were five-times that of last quarter. **David Pasquier**, credit products manager at **JPMorgan** in London said investors, many of them real-money accounts, were buying put and call options as well as positioning themselves to take advantage of any increase in volatility in the new year. The most popular option strikes were between 300 basis points and 325 bps, with the index trading at around 300, said one trader.


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Citi Loses French Fixed-Income Sales Chief

Pierre-Henri Denain, a managing director and head of French fixed-income sales at **Citigroup** in France, has left the firm. Market officials have connected him with a similar role at **IXIS Corporate and Investment Bank** in Paris where he will manage sales of structured credit products to Europe.

Denain could not be reached for comment and officials from IXIS did not return calls by press time. **Nicole Curtin**, spokeswoman for Citi in Paris, confirmed Denain had departed and said he has not yet been replaced.

BNP Paribas Readies Cash Effort To Boost Synthetics

BNP Paribas is setting up a cash collateralized debt obligation business in New York, which will complement its existing synthetic CDO operations. An official close to the firm said by offering cash, BNP will be able to access a broader range of potential clients for its synthetic business.

The French firm hired **Tim Drayson** Oct. 13 to head the effort as global head of securitization in New York. Until this summer, Drayson was head of capital markets and managing director in the European securitized products group at **Morgan Stanley** in London (DW, 6/17).

CAAM, BNP Paribas Expand Credit CPPI Offering

Crédit Agricole Asset Management, the French fund manager with EUR355.1 billion in assets under management, and **BNP Paribas** are preparing a second tranche of their European capital-protected credit fund Dynamo and looking to raise USD200 million.

This latest offering will expand the portfolio to include assets across a suite of currencies and will also take the transaction to Asian investors. The portfolio of credit indices and long and short credit-default swaps, wrapped as a 10-year note using constant proportion portfolio insurance to protect capital invested, will be open to U.S. dollar, sterling, Swiss franc, yen and Australian dollar investors.

Jean-Francois Boulier, head of European credit and fixed income at CAAM in Paris, said the firm will actively manage the different interest rate exposures of the currencies, moving leverage and exposure in line with its view of the credit market. **Hervé Besnard**, head of credit derivatives product development at BNP in London, said the transaction was structured to capitalize on the success of Dynamo I (DW, 8/5), which raised EUR525 million and is performing between 20 and 40 basis points above targets. He noted the firm is targeting clients in Asia, as well as European investors that showed interest in the first tranche, but did not have time to approve the investment.

Dynamo II has a target size of USD200 million and is expected to close later this month.

Wachovia Structured Equity Honcho Exits

Eric Glicksman, managing director and former head of equity structured products at **Wachovia Securities** in New York, has left the firm. Glicksman did not respond to an email sent via Bloomberg. **Elise Wilkinson**, a spokeswoman for Wachovia, said the group has been co-headed by **Rick Silva** and **Rick Sandulli**, since their hire from **Morgan Stanley** this summer (DW, 6/17). She declined comment on Glicksman's most recent title at the firm. It is unclear why he left or where he has gone.

Glicksman joined Wachovia last year from **Lehman Brothers** (DW, 5/2/04), where he was head of equity structured products.

Deutsche Bank Equity Trader Moves On

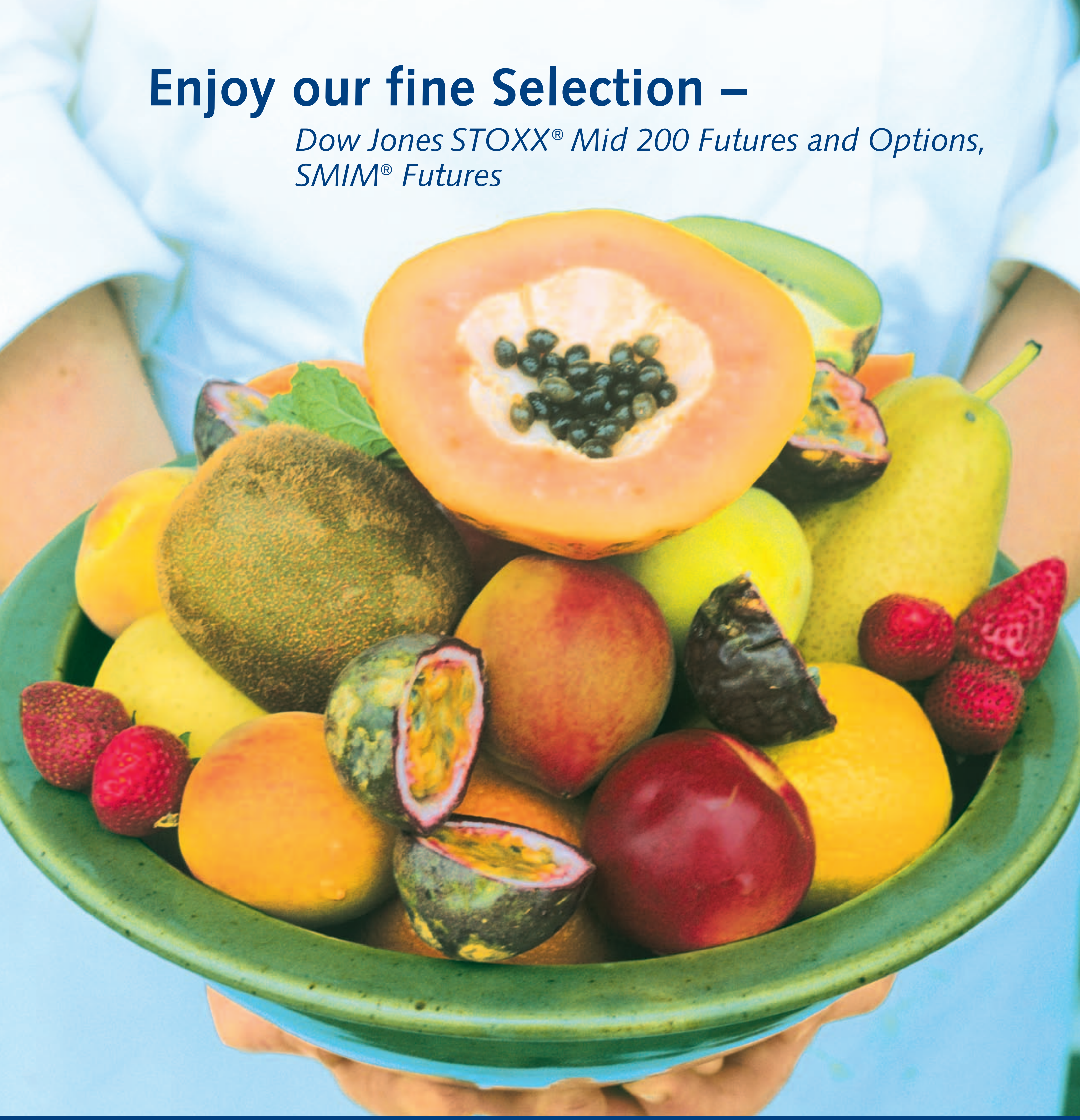
Philippe Lacour, index equity derivative trader at **Deutsche Bank** in London, has left the firm. Lacour could not be reached and it could not be determined if he was heading to another shop. **Nino Kjellman**, responsible for flow trading in Europe, was traveling and could not be reached. **Anna Watson**, spokeswoman for Deutsche Bank, confirmed the departure, declining further comment.

Asia Pacific

Merrill Equity Strategist Joins Tokyo Hedge Fund

Merrill Lynch's **Ken Chang**, co-head of Pacific Rim equity derivatives strategy in Tokyo, has joined hedge fund **Oasis Advisors** as a senior strategist in Tokyo. Chang, who landed last week, said the fund primarily looks at event-driven plays and quantitative strategies in the Japanese market but will start to look at convertible arbitrage and derivative-linked strategies. "At a later stage we'll look at both listed and OTC derivatives," noted Chang, explaining that developing derivative-related trades is part of his remit going forward.

Officials at Merrill said **Arik Reiss**, co-head of Pacific Rim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equity derivatives strategy in Hong Kong, has been named head of the team and has assumed overall responsibility.

IXIS Widens Structuring Scope

IXIS Corporate & Investment Bank is widening the scope of its alternative investment group mandate in Asia. The group, which has focused on fund-linked derivatives, is pushing into such areas as weather derivatives and insurance solutions. "Many investors are looking to diversify their risks across the product spectrum and are willing to take a look at catastrophic bonds as well as life-expectancy risk," said **Fabien Labouret**, Asian head of structured alternative investments in Hong Kong.

Labouret recently transferred from Tokyo to Hong Kong to establish a regional alternative investment structuring desk (DW, 7/23), initially targeting fund-linked derivative deals. IXIS expects to close its first weather and insurance transactions in the coming weeks. He explained the move piggybacks on the development of the firm's business in Europe, which has already rolled out catastrophic risk bonds.

Mixed-Basket CLNs Take Flight In Korea

Credit-linked note baskets incorporating both ABS and corporate names have emerged in Korea, as investors search for yield and diversification. "This is similar to traditional structures but the underlying is not just corporate names but also ABS," said an official at **Barclays Capital**. Market officials said such instruments have been sold to insurance companies, for instance, allowing the insurer to hold a different risk profile from existing CLNs and CDOs in their portfolios.

Lehman Nabs JPMorgan Trader

Lehman Brothers has brought aboard **Levan Shanidze,** v.p. and equity derivatives trader at JPMorgan in Hong Kong, for a similar role. Market officials said the hire is an expansion of the desk, but further details could not be ascertained. Shanidze hasn't started yet and could not be reached. **Prakash Krishnan**, spokesman at JPMorgan in Hong Kong declined comment and **Jonathon Wharton**, spokesman for Lehman at **Gavin Anderson**, did not respond to messages by press time.

User Strategies

Dublin Player To Manage CLO With Cross Currency Swap

Dublin-based **Harbourmaster Capital**, an investment manager running EUR4 billion (USD4.79 billion) in assets, is gearing up to manage a EUR500 million (USD600 million) collateralized loan obligation. The structure will feature a portfolio cross-currency swap to hedge the currency mismatch between sterling assets and its euro-denominated liabilities.

In the swap, Harbourmaster CLO 6, an offshore special purpose entity, will pay floating sterling principal and interest and receive floating euro principal and three-month EURIBOR minus a spread. The spread is determined by an asset-weighted foreign-exchange rate which adjusts every time Harbourmaster adds an asset to the portfolio.

In addition, the transaction features a string of deep out-of-the-money sterling put options to partially hedge the fx risk of the assets. Harbourmaster CLO 6 will purchase the options with strikes expected to be set at 30% of the spot rate at closing and that will mature on each note payment date.

Bank of America is counterparty on the swap and options, as well as transaction arranger. **Alan Kerr**, credit analyst at Harbourmaster in Dublin, declined comment on the deal, referring calls to BofA. Officials at BofA in London did not return calls by press time. The trade is expected to close this month.

Harcourt Natural Resources Fund Reassesses Strategy

A natural resources fund of hedge funds managed by USD3.1 billion Swiss firm **Harcourt Investment Consulting** has performed poorly since it launched earlier this year, prompting the fund to reassess its allocation strategies. The *Belmont Natural Resources* fund, with just under USD100 under management, is down between 2.47% and 3.06% across its U.S. dollar, euro and Swiss franc share classes.

"We're certainly lagging others," acknowledged **Stephen Williams**, analyst. But the firm is still bullish about the strategy and will make concerted efforts to improve performance, added **Martin Zulauf**, business development. Specifically, the firm plans to increase the fund's diversification across all commodities. For example, its minimal exposure to weather derivatives could be increased, said Williams.

The fund has made gains in crude oil and natural gas and has seen "steady, if not stellar" returns from exposure to the metals sector, said Williams. It suffered more in electricity and problems of liquidity and increased volatility have adversely affected returns, he continued.

European CDO Summit

More than 200 CDO professionals congregated at the Fairmont in Monte Carlo last week for Opal Financial Group's 2005 European CDO Summit. ***Laura Cochrane****, reporter, filed these reports.*

Greenhorn Managers Flood Market

A plethora of CDO managers have entered the synthetic market, both as arrangers and third-party administrators. The move comes as investors jump on highly-managed structures to guard them against an expected downturn in the credit cycle. "There will be more defaults, there will be volatility and there will be losses," said **William Bohnsack**, chief operating officer at **Oak Hill Advisors,** a New-York based investment firm.

Managers Curtail Delphi Losses

The damage felt by CDO investors exposed to U.S. auto parts marker **Delphi Corp.** was lessened by managers who traded out the name from portfolios before it hit rock-bottom. "It had been taken out of many transactions and therefore had a limited impact," said **Katrien Van Acoleyen**, analyst at **Standard & Poor's** in London. Of the 700 CDO tranches with exposure to Delphi only 177 were downgraded by S&P.

Leverage Doubles On LSS Tranches

The leverage factor on leveraged super senior structures is around 20 times—double the standard 10 times—as firms are looking to extract juice from tightening spreads in the senior tranches of CDOs and lure investors. In addition, houses are reducing the level spread-based triggers must hit before a trade unwinds.

Seen 'N' Heard

- "P.A.U.G. sounds like a Soviet car. I was relieved to find out it meant pay-as-you-go."—**Claude Brown**, partner at **Clifford Chance**, finding levity in **ISDA**'s CDS on ABS documentation template.

- "They piss away money."—**Sam Derosa Farag**, managing director in research at **Credit Suisse First Boston** in New York, on the credit hedging methodologies of derivative houses during the current credit cycle.

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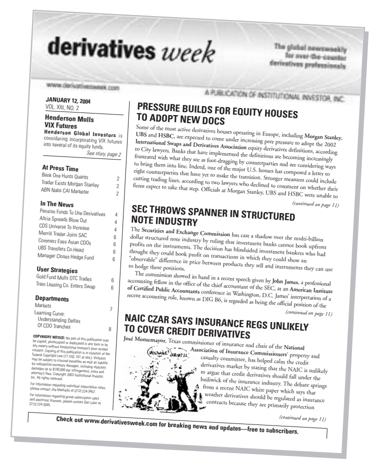

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Henderson Mulls VIX Futures
Henderson Global Investors is considering incorporating VIX futures into several of its equity funds.
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PRESSURE BUILDS FOR EQUITY HOUSES TO ADOPT NEW DOCS

Some of the most active derivatives houses operating in Europe, including **Morgan Stanley**, **UBS** and **HSBC**, are expected to come under increasing peer pressure to adopt the 2002 **International Swaps and Derivatives Association** equity derivatives definitions, according to City lawyers. Banks that have implemented the definitions are becoming increasingly frustrated with what they see as foot-dragging by counterparties and are considering ways to bring them into line. Indeed, one of the major U.S. houses has composed a letter to eight counterparties that have yet to make the transition. Stronger measures could include cutting trading lines, according to two lawyers who declined to comment on whether their firms expect to take that step. Officials at Morgan Stanley, UBS and HSBC were unable to

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SEC THROWS SPANNER IN STRUCTURED NOTE INDUSTRY

The **Securities and Exchange Commission** has cast a shadow over the multi-billion dollar structured note industry by ruling that investment banks cannot book upfront profits on the instruments. The decision has blindsided investment bankers who had thought they could book profit on transactions in which they could show an "observable" difference in price between products they sell and instruments they can use to hedge these positions.

The commission showed its hand in a recent speech given by **John James**, a professional accounting fellow in the office of the chief accountant of the SEC, at an **American Institute of Certified Public Accountants** conference in Washington, D.C. James' interpretation of a recent accounting rule, known as DIG B6, is regarded as being the official position of the

(continued on page 11)

NAIC CZAR SAYS INSURANCE REGS UNLIKELY TO COVER CREDIT DERIVATIVES

José Montemayor, Texas commissioner of insurance and chair of the **National Association of Insurance Commissioners**' property and casualty committee, has helped calm the credit derivatives market by stating that the NAIC is unlikely to argue that credit derivatives should fall under the bailiwick of the insurance industry. The debate springs from a recent NAIC white paper which says that weather derivatives should be regulated as insurance contracts because they are primarily protection

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Key Differences Between CDS Of ABS End Investor And Dealer Templates

Background

In 2004, the **International Swaps and Derivatives Association** formed a committee to draft a form of credit-default swap for asset-backed securities with a view toward jump starting the synthetic ABS market. Before the committee issued its draft, a dealer subgroup presented its own draft—the Dealer Template—to the committee. Many end users raised concerns regarding elements of the Dealer Template. In response, ISDA published the Dealer Template and encouraged objecting end users to prepare a separate End Investor Template. An initial draft of the End Investor Template was given to ISDA Sept. 13, 2005, and discussed in a conference call convened by the trade group Oct. 12, 2005. ISDA has invited members of the committee to comment on the End Investor Template.

The End Investor Template is designed for use in documenting synthetic pay-as-you-go flow transactions. Under a pay-as-you-go instrument, the seller of protection pays if an interest shortfall, a write-down or a principal shortfall occurs with respect to the reference obligation.

The Key Differences

(1) **Elimination of physical settlement at buyer's option and use of credit events.**

Under the Dealer Template, if a credit event occurs (including a failure to pay principal, a write-down, a distressed ratings downgrade or a maturity extension), the buyer has the option to reduce all or part of the reference obligation notional amount via physical settlement.

The End Investor Template eliminates the buyer's option for physical settlement and does not use the credit event concept.

(2) **Elimination of implied write-downs/implied write-down reimbursement provisions.**

Implied write-down and implied write-down reimbursement provisions in the Dealer Template apply. Payments are required by the seller and buyer respectively, if—under the underlying instruments of the reference obligation—certain write-downs, applied losses, principal deficiencies or realized losses occur that do not reduce the outstanding principal amount of the reference obligation, or are subsequently reimbursed. Under these provisions, the calculation agent determines the amount of the implied write-down/implied write-down reimbursement.

The End Investor Template eliminates these implied write-down provisions, requiring seller payments only if write-downs occur that are contemplated under the underlying instruments and that reduce either (a) the reference obligation's outstanding principal amount or (b) the amount of interest payable on the reference obligation.

(3) **Elimination of buyer's option to terminate the transaction upon the occurrence of a step-up**

Optional step-up provisions in the Dealer Template provide if a step-up occurs the buyer has the option to terminate the transaction or to continue the transaction at the higher rate. A step-up is defined as an increase in the reference obligation coupon due to the failure of the issuer or a third party to redeem, cancel or terminate the reference obligation, as the case may be, in accordance with the underlying instruments.

There is no such option under the End Investor Template: changes in the coupon of a fixed-rate reference obligation or spread of a floating rate reference obligation are given effect, and the transaction continues. If the coupon or spread of the reference obligation increases, the fixed rate also increases.

(4) **Interest shortfall cap provisions/available funds cap**

The Dealer Template determines interest shortfalls without giving effect to available funds cap or other provisions in the underlying instruments which limit distributions and provide for capitalizing or deferring interest, or that provide for extinguishing or reducing such payments.

As a corollary to the foregoing, the Dealer Template contains optional interest shortfall cap provisions that can be used to limit interest to either a fixed cap or a variable cap.

The End Investor Template takes the opposite approach. It eliminates the interest shortfall cap provisions and determines any interest shortfall after giving effect to all available funds cap reduction provisions. This includes any provision of the underlying instruments that (a) provide for capitalizing or deferring interest on the reference obligation or (b) limit the interest entitlement or rate at which interest is determined in relation to the reference obligation pursuant to a prepayment interest shortfall, basis risk shortfall, relief act shortfall, net weighted-average coupon rate cap or similar available funds cap provision.

(5) Adjustments in connection with reference policy
Under the End Investor Template, if the reference obligation is guaranteed under a reference policy that by its terms excludes any component of the expected interest amount or the expected principal amount for purposes of determining the liability of the relevant insurer, or the terms of the reference policy otherwise do not require the insurer to pay any such amounts, the relevant component or amount also is excluded for purposes of determining interest shortfall amounts and principal shortfall amounts, as applicable.

The Dealer Template has no corresponding provisions.

(6) Period for payment of additional fixed amounts
Under the Dealer Template, the seller may receive recoveries of amounts previously paid in respect of interest shortfalls, write-downs, and principal shortfalls, but only if a notice of the occurrence of the recovery has been delivered within one year of the earlier of:

(i) the legal final maturity date of the reference obligation;
(ii) the date when the reference obligation notional amount is reduced to zero; and
(iii) the date when the assets securing the reference obligation notional amount are fully liquidated and the proceeds are fully distributed.

Under the End Investor Template, the seller may continue to receive such recoveries until the later of either the date when the assets securing the reference obligation are liquidated, distributed or otherwise fully disposed of and the proceeds are distributed or otherwise fully disposed of or—if such disposition is at the direction of an insurer—the date the insurer is no longer obligated as to principal and/or interest amounts in respect of the reference obligation under the reference policy.

(7) Amendments
Under the End Investor Template, all amendments to the reference obligation are given effect, including any amendment that extends the legal final maturity date. In consideration of the seller's obligation to give effect to each such amendment, the buyer is required to pay the seller the applicable percentage of any payment received in connection with such amendment.

Under the Dealer Template, an amendment, on or after the effective date, which extends the legal final maturity date is a credit event.

(8) Make-whole premiums payable to seller
Under the End Investor Template, a make-whole premium payment (the payment or distribution of any make-whole, redemption, call or prepayment premium to holders of the reference obligation in connection with any prepayment, redemption, early amortization or similar event under the terms of the underlying instruments) constitutes an additional fixed payment event and the buyer must pay the applicable percentage of such make-whole premium payment to the seller.

There is no similar concept in the Dealer Template.

(9) Delivery of servicer reports
Under the Dealer Template, a counterparty is required to provide a servicer report only to the extent that such servicer report is reasonably available to the counterparty.

Under the End Investor Template, the buyer is required, without exception, to provide the seller with a servicer report promptly following the delivery of such servicer report to the holders of the reference obligation.

In many cases, ABS servicer reports are available only to holders of the reference obligations. The End Investor Template provision is intended to move the market in the direction of providing parties to ABS CDS transactions with broader access to these servicer reports.

(10) Determination of amounts
Under both templates, the calculation agent generally is responsible for determining fixed amounts, floating amounts and additional fixed amounts. Both templates also state that such determinations shall be based solely on servicer reports, to the extent such reports are reasonably available to the Calculation Agent.

In order to address situations in which a servicer report is not reasonably available to the calculation agent, however, the End Investor Template permits the calculation agent to make its determination based on publicly available information from at least two public sources. The End Investor Template further clarifies that in the absence of both a servicer report and such publicly available information, no floating amount shall be payable.

(11) Optional physical settlement and voting rights
Finally, the End Investor Template includes optional provisions relating to physical settlement—at the seller's option only—and voting rights that can be used to address certain moral hazard issues. Since moral hazard issues generally should not arise in true synthetic pay-as-you-go flow transactions, it is anticipated that these provisions will rarely be used.

*This week's Learning Curve was written by **Craig Mills**, an associate, and **Mark Rae** and **Jeffrey Stern**, partners at **Stroock & Stroock & Lavan**.*

Foreign Exchange & Credit Derivatives Markets

Dollar Gains Keep Traders Busy

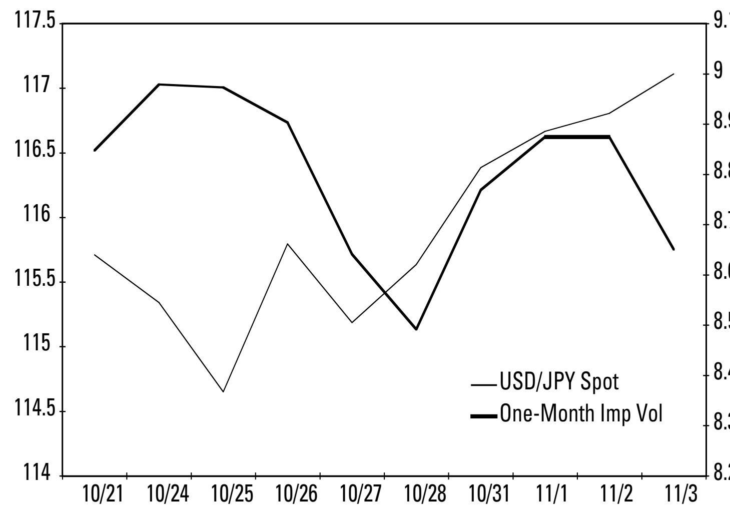
The U.S. dollar gained steadily against the yen in the spot market last week, prompting solid demand for dollar/yen upside options. Dollar/yen had been close to yearly highs the previous week, but last week players were buying into the view the rally is not yet over. The greenback climbed to JPY116.805 Wednesday from JPY115.185 last Thursday, while implied volatility rose slightly to 8.01% Wednesday from 7.75% last Thursday.

"There is a lot of interest in the upside of the dollar/yen," said one trader, noting that investors are taking a bullish view on the dollar and selling front-end options. Typically, players were buying one-week calls, striking at JPY116 with knockouts above JPY118.

David Woo, head of global FX strategy at **Barclays Capital** in London, said the yen's decline since the Japanese election in July surprised investors, the consensus of whom believed the yen was undervalued. "Volatility has been well contained despite spot moving higher," Woo said. "But that could change."

He said, and traders agreed, volatility will likely move in line with spot for the next few days or even weeks. But they noted, if barrier positions are knocked out at JPY119, that could increase volatility dramatically. "If that happens," a trader said, "All bets are off."

USD/JPY Spot & One-Month Implied Volatility



Source: **JPMorgan**

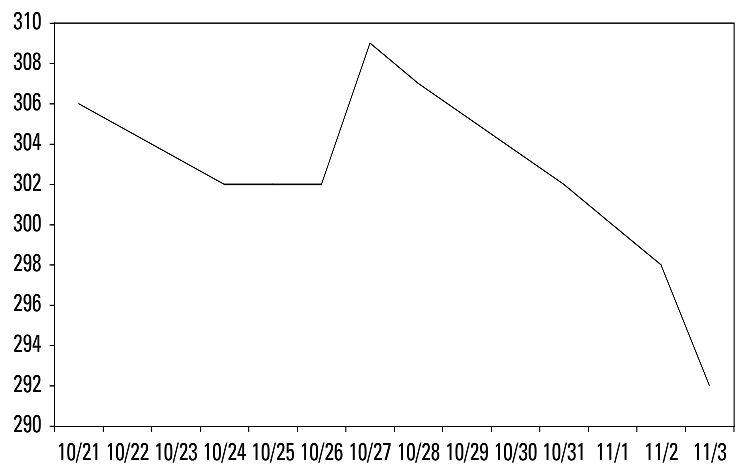
Crossover Spreads Drop In Line With Equity Rally

The price of protection on the European iTraxx Crossover index fell last week, after an equity market rally fed market confidence through to the credit sector and pushed spreads on the index tighter. It drew in more than 10 basis points, to 296 bps on Thursday from 309 bps the week before. "Negative sales numbers released by the U.S. autos on Tuesday did not increase volatility in equity and this showed in CDS spreads," said one trader, adding, "Credit has certainly been more closely linked to the equity markets recently."

The draw-in surprised many CDS players and as a result people who were long the Crossover sold positions, traders noted. "People thought if spreads are not going to widen now they never will, so turned to short covering," said one official. "The emphasis is definitely on shorting," agreed another trader. Five-year trades were the most popular, but there was also activity at seven-year, said one trader at a European house. "This has come from structured dealers reorganizing after tightening and playing single names versus the index basis," he said.

Market officials agreed that the tightening of spreads despite volatility in the auto sector and uncertainty over U.S. interest rates indicated a robust CDS market. "There were no major changes and it [the market] is strong," said one trader. He also noted there was activity on the iTraxx HiVol, where spreads tightened to 76 bps from 80 bps the week before.

Five-Year Spreads On iTraxx Crossover



Source: **JPMorgan**

Markets

Five-Year Credit-Default Swap Levels

November 2, 2005

U.S.

Name	Bid	Offer	Bid Change (Weekly)
AOL Time Warner	59	59	0
Bear Stearns	26	26	-1
Citigroup	15	15	-1
Disney	42	42	-2
Federated Dept. Stores	45	45	0
Ford	722	722	56
General Electric Cap Corp.	20	20	0
GMAC	264	264	27
Goldman Sachs	24	24	-1
Hertz	349	349	41
Hewlett Packard	28	28	0
IBM	17	17	-3
Lehman Brothers	25	25	-1
Morgan Stanley	24	24	-1
Philip Morris	79	79	-6

Europe

Name	Bid	Offer	Bid Change (Weekly)
ABN AMRO	10	10	0
Akzo Nobel	24	24	0
Aventis	32	32	0
BAE Systems	36	36	-2
Carrefour	23	23	1
Credit Lyonnais	10	10	0
Deutsche Telekom	45	45	1
Dixons	69	69	-2
Endesa	29	29	0
France Telecom	45	45	2
Halifax	11	11	-1
Iberdrola	23	23	-1
Marks & Spencer	64	74	-4
UBS	9	9	0
Vodafone	26	26	0

Asia

Name	Bid	Offer	Bid Change (Weekly)
Amcor	53	53	-1
BHP Billiton	25	25	0
Fujitsu	35	35	2
Hutchison Whampoa	37	44	-2
Mizuho Bank	18	18	0
Qantas Airways	48	48	2
Sony	37	37	-2
Telstra	33	33	0
Toshiba	21	21	-1
Australia	2	2	0
China	22	22	0
Japan	5	5	0
Korea	28	28	1
Malaysia	28	28	1
Philippines	314	314	-24
Thailand	39	39	1

North America	**3-Nov-09**	**28-Oct-09**	**Spd change week**
CDX.NA	49.00	48.75	0.25
CDX.NA.HY	296.76	311.38	-14.62
CDX.EM	155.00	155.00	0.00
Europe	***3-Nov-09***	***28-Oct-09***	***Spd change week***
iTraxx Main	37.00	37.75	-0.75
iTraxx Non Financial	42.26	42.95	-0.69
iTraxx High Vol	77.50	80.25	-2.75
Asia	**3-Nov-09**	**28-Oct-09**	**Spd change week**
iTraxx Japan	29.35	28.55	0.80
iTraxx Asia	47.45	48.01	-0.56
iTraxx Australia	31.06	30.46	0.60

This data is updated every Wednesday

Source: **JPMorgan**

LEVERED SENIOR

(continued from page 1)

derivative shops, including **Morgan Stanley**, **Deutsche Bank** and **Merrill Lynch**, are considering the trades to hedge ABS exposure and are expected to print before year-end. Officials at those three firms declined comment and **Rebecca Nelson**, Goldman spokeswoman in London, did not return messages by press time.

The firms are also keen to take advantage of investor demand for non-risky ABS and developing liquidity in the asset-class. "There is now a natural two-way flow in the ABS market," said an official at a U.S. house in London, adding, "The market is looking for more yield with ABS and is comfortable with leverage."

Analysts at the three major rating agencies reported a plethora of inquires for leveraged super senior referencing specific, rather than diversified, ABS portfolios. **Perry Inglis**, managing director and head of the European CDO group at **Standard & Poor's** in London, said he is working on six transactions which comprise portfolios of CMBS or RMBS and which feature spread-based triggers. The first will be rated within two weeks, **Olivier Toutain**, v.p. and senior analyst at **Moody's Investors Service** in Paris, said a lack of data on specific ABS spread movements and concerns about the liquidity of the assets has made rating the trades challenging, but that rating criteria remained the same as a corporate LSS deal.

—Laura Cochrane

OPTIONS ON

(continued from page 1)

looking at hedging and pricing the options. Goldman is driving the activity, and is already showing prices for the instruments.

Equity salesmen at several houses said they have fielded inquiries from hedge funds in the last few weeks and one equity strategist said his firm had also discussed wrapping a dividend option in a medium-term note for an institutional client. "Demand is key," noted a hedge fund salesman at a French firm. The salesman said his firm had looked at offering options on dividends a few years ago, but had not had much client interest in the idea. This time round, hedge funds' demands are driving the buzz on the Street.

Traders noted, however, although there's a lot of talk they have not yet seen anything traded. One official noted dealers may be holding back to gauge the scale of demand before offering the instruments, because of hedging concerns. While hedging an option on a dividend swap is possible because of the increasing liquidity of the swaps, pricing options on realized dividends is harder because dividends are ultimately the result of a corporate decision, rather than a technical factor that can be modeled.

The likelihood is if demand is high enough, dealers will simply carry the risk. Selling options could help dealers lay off their dividends exposure with a wider range of clients. Institutional fund managers are put off dividend swaps because when the realized dividend is very low, that could mean a negative flow from them in the swap, explained one salesman. But fund managers could purchase call options on the dividends which would mean paying only the initial premium. This could be particularly attractive in a capital-protected note form, he added.

—Elinor Comlay

INFLATION TRADERS

(continued from page 1)

hedge the firm's inflation book. A U.S. inflation trader at a U.K. firm said he now has authorization to trade certain energy-linked securities, such as gasoline and energy futures. But he noted his firm is looking at a hedge that's broadly energy rather than asset-specific, and may look into wider energy indices as a hedge.

Gasoline prices are already a factor in inflation derivative models, said one strategist. But when there are sharp moves in inflation from month to month, linked to commodities and energy, it makes sense to look at hedges, he added. **Alan James**, inflation-linked strategist at **Barclays Capital** in London, declined comment on the firm's inflation trading strategy, but noted the correlation between inflation, energy and commodities is also being driven by the rising popularity of commodity-linked investment products. Because dealers collectively are selling commodities and energy on to investors, the Street is short and some players are choosing to hedge with inflation rather than directly with the commodity and energy components in the note.

—E.C.

Quote Of The Week

"There's so much potential here."—**Rupertus Rothenhaeuser**, *head of the private investor group at* ***ABN AMRO*** *in Hong Kong, on his return to his native Frankfurt as head of structured fund sales at* ***DWS Investments*** *(see story, page 2).*

One Year Ago In Derivatives Week

Calyon was preparing a novel capital-protected leveraged note linked to iTraxx tranches. [Capital-protected credit derivative notes and funds have taken off this year, with all major shops issuing the deals.]

WE COULD TELL YOU WHAT WE'VE ACHIEVED IN THE CDO MARKET.

BUT THE RESULTS SPEAK FOR THEMSELVES.

#1 GLOBAL UNDERWRITER OF CDOs IN 2004

February 25, 2004	$602,000,000	Declaration	Independence V CDO, Ltd.	Lead Placement Agent
March 10, 2004	$296,750,000	TERWIN money management	Glacier Funding CDO I, Ltd.	Lead Placement Agent
March 25, 2004	$362,800,000	CB Cohen Bros. & Company	Alesco Preferred Funding III, Ltd.	Lead Placement Agent
March 31, 2004	$1,501,500,000	Vanderbilt Capital Advisors	Lakeside CDO II, Ltd.	Lead Placement Agent
April 13, 2004	$352,250,000	Rabobank	Vermeer Funding, Ltd.	Lead Placement Agent
April 15, 2004	€514,300,000	MIZUHO	Harvest CLO I S.A.	Lead Placement Agent
April 29, 2004	$414,700,000	CB Cohen Bros. & Company	Dekania CDO II, Ltd.	Lead Placement Agent
May 18, 2004	$415,500,000	CB Cohen Bros. & Company	Alesco Preferred Funding IV, Ltd.	Lead Placement Agent
May 27, 2004	$449,625,000	ACA	ACA ABS CDO 2004-1	Lead Placement Agent
May 27, 2004	€304,400,000	SOLENT Solent Capital (Jersey) Ltd	Rhodium I B.V.	Lead Placement Agent
July 7, 2004	$1,108,200,000	TCW	South Coast V, Ltd.	Lead Placement Agent
July 22, 2004	$449,375,000	RBC Capital Partners	Hudson Straits CLO	Lead Placement Agent
July 26, 2004	$402,700,000	TERWIN money management	Cascade CDO I	Lead Placement Agent
August 25, 2004	$501,000,000	PIMCO	Crystal Cove	Lead Placement Agent
September 14, 2004	$364,800,000	CB Cohen Bros. & Company	Alesco Preferred Funding V	Lead Placement Agent
September 28, 2004	$301,250,000	TCW	South Coast VI	Lead Placement Agent
September 30, 2004	$998,000,000	Vanderbilt Capital Advisors	Streeterville ABS CDO	Lead Placement Agent
October 12, 2004	$497,750,000	TERWIN money management	Glacier Funding II	Lead Placement Agent
October 21, 2004	€308,500,000	AXA	Adagio CLO I B.V.	Lead Placement Agent
October 26, 2004	$502,800,000	MBIA	Reservoir Funding	Lead Placement Agent
October 28, 2004	$402,000,000	Declaration; StraitsLion Asset Management	Straits Global ABS CDO I	Lead Placement Agent
November 3, 2004	$753,130,000	FundAmerica Management	Mercury CDO 2004-1	Lead Placement Agent
November 9, 2004	$354,937,000	Lyon Capital Management	LCM II Limited Partnership	Lead Placement Agent
December 2, 2004	$502,250,000	TRICADIA CDO MANAGEMENT LLC	TABS 2004-1 CDO	Lead Placement Agent
December 2, 2004	$753,280,000	MAXIM Advisory	Jupiter High-Grade CDO, Ltd.	Lead Placement Agent
December 14, 2004	$300,865,000	Rabobank	Vermeer Funding II, Ltd.	Lead Placement Agent
December 16, 2004	$584,000,000	FriedbergMilstein	FriedbergMilstein Private Capital Fund I	Lead Placement Agent
December 16, 2004	$502,500,000	Vanderbilt Capital Advisors	Dunhill ABS CDO	Lead Placement Agent
December 21, 2004	$692,800,000	CB Cohen Bros. & Company	Alesco Preferred Funding VI	Lead Placement Agent
December 22, 2004	$302,800,000	E*TRADE Financial	E*Trade ABS CDO III	Lead Placement Agent

Merrill Lynch

Global Markets & Investment Banking Group

Ranking Source: Thomson Financial, 2004