

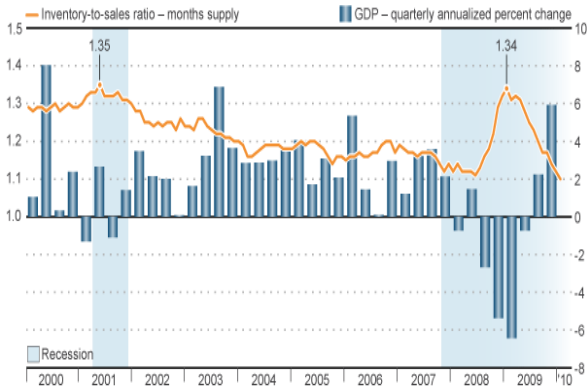
# INSIDE DEBT

PRODUCED BY REUTERS IN PARTNERSHIP WITH ICAP

Wednesday, March 10, 2010

## CHART OF THE DAY

### U.S. wholesale inventories



U.S. wholesale inventories unexpectedly fell in January, while sales rose much faster than expected to their highest level since October 2008.

## TODAY'S TOP NEWS

- U.S. wholesale inventories fall, sales surge
- U.S. Sen Corker: no exemptions in new watchdog bill
- Greece warns of worse downturn as strikes loom
- Euro stability top priority in fund debate -Germany
- U.S. sale of \$21 bln of 10-yr debt draws good demand
- U.S. govt posts record \$220.9 bln budget gap in Feb
- French, Italian output jumps, euro zone uncertain
- ICE, CME clearing membership rules challenged for CDS
- Brown says UK to maintain triple A credit rating

## ECON WATCH

FOR THURSDAY MARCH 11

ET	Indicators	Unit	Reuters	Prior
08:30	US Initial Claims	k	460	469
08:30	US Jobless contin claims	mln	4.49	4.500
08:30	US International trade mm \$	bln	-41	-40.18
08:30	CA Trade balance C\$	bln	0.10	-0.25
08:30	CA Exports C\$	bln	32.60	32.19
08:30	CA Imports C\$	bln	32.60	32.44
08:30	CA Capacity utilization Q4	%	69.9	67.5
08:30	CA New housing price index	%	0.4	0.4

### SPECIAL REPORT-The death of a boutique bank

In September 2008, as Lehman Brothers was breaking into a million pieces, a young investment bank was pushing up through the rubble.

For more please click here

## MARKETS TODAY

**TODAY'S TOP STORY:** U.S. wholesale inventories fell modestly in January, while sales rose to their highest level since October 2008, suggesting that inventories would continue to support economic growth in the first quarter. **For more please click here**

**TREASURIES:** U.S. Treasuries prices slipped as traders cut prices to draw buyers to securities the U.S. Treasury is auctioning this week.

- Treasury sold \$21 billion of 10-year notes at a high yield of 3.735 pct, awarding 70.9 pct of the bids at the high. The bid-cover ratio was 3.45.
- 10-yr notes, which fell 9/32 immediately before the auction's bidding deadline. It was down 5/32, to yield 3.72 pct.
- 30-yr bond prices fell 8/32 to yield 4.69 pct.
- 5-yr Treasury notes shed 7/32, yielding 2.38 pct from 2.34 pct.
- 2-yr notes fell 2/32 to yield 0.91 pct.
- 2-10's part of the yield flattened by 2 bps to 281 bps.

**FOREX:** The dollar slipped against the euro while the yen fell, as risk appetite improved in general with a rise in European and U.S. stocks, boosting demand for higher-yielding but riskier currencies.

- Euro gained 0.39 pct to \$1.3651, after hitting a session low of \$1.3546 and a peak of \$1.3679.
- Dollar was up 0.64 pct to 90.52 yen, after climbing as high as 90.82.
- The euro rose 0.97 pct to 123.54 yen.

**CORPORATES:** U.S. corporate bonds spreads narrowed, lifted by a broadly firmer tone for riskier assets.

- The CDX.IG-13 index remained unchanged at 83 bps.
- GMAC launched \$1.5 bln of 10-yr notes.
- Hovnanian CDS has fallen to 969 bps, after trading over 4,000 bps in March 2009.
- U.S. money market fund assets fell by \$31.54 bln to \$3.067 trln in the week ended March 9, the Money Fund Report said.

**STOCKS:** Bank and technology shares lifted Wall Street on hopes a revival in business demand will boost corporate profits.

- Dow rose 0.03 pct to 10,567.33, S&P was up 0.45 pct to 1,145.61 and Nasdaq gained 0.78 pct to 2,358.95.
- Citigroup was up 3.66 pct to \$3.96, JPMorgan Chase rose 1.20 pct to \$42.93.
- The KBW bank index rose 2.16 pct and earlier hit its highest intraday level since November 2008.
- S&P financial index rose 1.12 pct, S&P energy index gained 0.63 pct and S&P technology shares rose 0.77 pct.

**C & E:** Oil prices settled higher in choppy trading after a government report showed that gasoline stocks in the United States dropped unexpectedly.

- U.S. crude prices rose 0.54 pct to \$81.93 per barrel, falling from a fresh eight-week high of \$83.03 earlier.
- Gold was down 1.24 pct to \$1,107.3 an ounce.
- Reuters-Jefferies index shed 0.06 pct at 274.62.

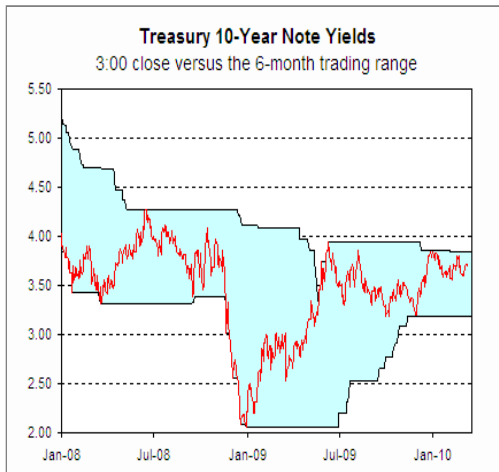
• For MARKET SNAPSHOT click here

• For NEXT UP click here

• For DEEP DIVE click here



MARKET SNAPSHOT as of 3:00 pm EST



TREASURIES <5> <500>

	BID	ASK	YIELD	CHANGE
1-Mo Bill	0.130	0.095	0.132	0.001
3-Mo Bill	0.150	0.140	0.152	-0.002
6-Mo Bill	0.205	0.200	0.208	0.001
1-Year	0.373	0.368	0.379	0.005
2-Year	99.922	99.953	0.916	-0.070
3-Year	99.727	99.758	1.469	-0.156
5-Year	99.969	100.016	2.382	-0.188
7-Year	99.125	99.172	3.141	-0.180
10-Year	99.188	99.250	3.723	-0.156
30-Year	98.938	99.016	4.691	-0.180

EQUITIES

	INDEX	CHANGE
DJIA	10575.64	11.34
NASDAQ	2358.53	17.91
S&P 500	1146.15	5.50

OIL

	PRICE	CHANGE
NYMEX	82.0	0.5
BRENT	78.2	1.4

EURODOLLAR FUTURES

	CLOSE	CHANGE
Mar-10	99.740	0.003
Jun-10	99.625	-0.010
Sep-10	99.435	-0.020
Dec-10	99.140	-0.025

FUTURES

	PRICE	CHANGE
CBOT 5 yr	116.56	-0.22
CBOT 10 yr	117.88	-0.20
CBOT 30 yr	117.78	-0.41

REPURCHASE AGREEMENTS

G/C		MORTGAGE REPOS	
O/N	0.190	O/N	0.220
2-Week	0.220	2-Week	0.220
1-Month	0.220	1-Month	0.240
3-Month	0.230	3-Month	0.290
AGENCY REPOS		i-REPO <sup>SM</sup> INDEX	
O/N	0.200	10:00 AM	0.130
2-Week	0.220	3:00 PM	0.130
1-Month	0.230		
3-Month	0.250		

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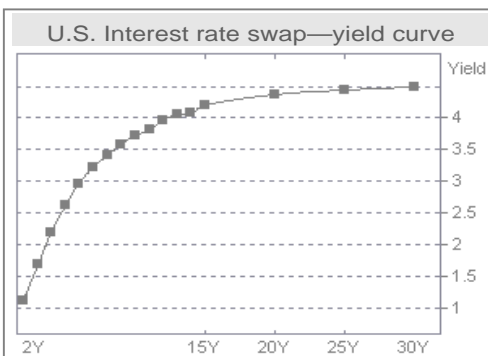
	SPREAD		RATE	
2-Year	19.00	23.00	1.10	1.12
3-Year	22.50	26.50	1.69	1.70
5-Year	23.75	27.75	2.61	2.62
7-Year	7.75	11.75	3.21	3.21
10-Year	0.75	4.75	3.73	3.71
30-Year	-19.50	-15.50	4.49	4.47

CURRENCIES

	BID	ASK
Euro	1.3646	1.3648
Sterling	1.4965	1.4970
JP Yen	90.50	90.52
Swiss Franc	1.0707	1.0710
Can Dollar	1.0268	1.0272
Mexico	12.6000	12.6056

EURODOLLAR DEPOSITS & OIS STRIPS (ASKED)

	BID	ASK	BID	ASK
O/N	0.140	0.160	-	-
1-Month	0.200	0.280	0.154	0.164
3-Month	0.220	0.400	0.171	0.181
6-Month	0.250	0.450	0.206	0.216
12-Month	0.600	1.000	0.359	0.369



FED FUNDS NYFR<sup>SM</sup> - 10AM

Open	0.1500	1m	0.2175
High	0.1500	3m	0.2575
Low	0.1000		

ACTIVE FANNIE MAE AGENCIES

TERM	COUPN	MATURITY	YIELD-SPREAD	YIELD
2-Year	1	04/04/2012	18 0	1.09
3-Year	1.75	22/02/2013	17.5 0	1.64
5-Year	2.875	09/02/2015	27.5 26.5	2.66
7-Year	5.125	18/10/2016	19.25 18.5	3.33
10-Year	-	-	- -	-
30-Year	6.625	15/11/2030	35.5 35	5.05

ACTIVE FREDDIE MAC AGENCIES

TERM	COUPN	MATURITY	YIELD-SPREAD	YIELD
2-Year	1.125	15/12/2011	-3.25 -3.75	0.88
3-Year	1.625	15/04/2013	25.5 25	1.72
5-Year	2.625	20/11/2014	16.5 15	2.56
7-Year	5.25	15/09/2016	18 17.5	3.32
10-Year	3.75	27/03/2019	22 20	3.94
30-Year	6.25	15/07/2032	38.5 38	5.08

Active MBS 15YR

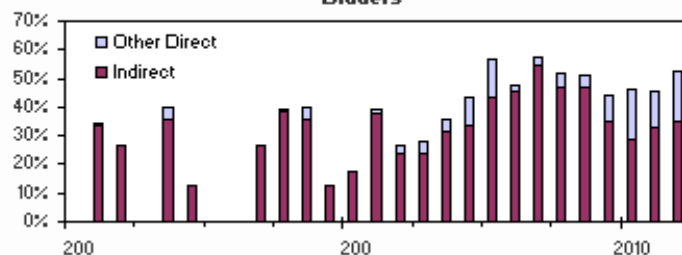
	CPN	BID	ASK	YIELD
FNMA	5.0	105.2460	105.2660	2.469
FHLMC	5.0	105.2460	105.2660	2.469

Active MBS 30YR

	CPN	BID	ASK	YIELD
FNMA	5.5	105.0960	105.1160	3.013
FHLMC	5.5	105.2270	105.2470	2.790
GNMA	5.5	106.0510	106.0710	3.386

Wrightson ICAP<sup>SM</sup> Chart of the Day

Percentage of Tsy 10-Yr Note Auctions Awarded to Non-Dealer Bidders



## TODAY'S TOP NEWS

**U.S. wholesale inventories fall, sales surge**

U.S. wholesale inventories fell modestly in January, while sales rose to their highest level since October 2008, suggesting that inventories would continue to support economic growth in the first quarter.

The rise in sales pushed the inventory-to-sales ratio to a record low of 1.10 months' worth from December's 1.12 months, the Commerce Department said.

Total wholesale inventories slipped 0.2 percent, smaller than the revised 1 percent drop in December.

Sales at wholesalers rose 1.3 percent to \$346.7 billion in January, after rising by a revised 1.2 percent the previous month.

Separately, U.S. mortgage applications nudged higher last week, reflecting increased demand for home purchase loans even as interest rates trekked higher, data from an industry group showed.

The MBA said its seasonally adjusted index of mortgage applications for the week ended March 5 increased 0.5 percent. The four-week moving average of mortgage applications was up 0.8 percent. The MBA's seasonally adjusted purchase index increased 5.7 percent, while its seasonally adjusted index of refinancing applications decreased 1.5 percent.

The MBA said the refinance share of mortgage activity decreased to 67.2 percent from 69.1 percent the previous week.

**Greece warns of worse downturn as strikes loom**

The Greek economy is set to shrink by more than expected this year, the government said, as it braced for nationwide strikes protesting its plans for bringing the country's budget deficit under control.

Greece told the European Union that 2010 GDP would "most likely" shrink by more than the 0.3 percent currently forecast.

Economists and ratings agencies have warned that a sharper than expected slowdown in the economy is one of the biggest threats to Greece's commitment to cut its budget deficit to 2.8 percent of GDP by 2012 from close to 13 percent last year.

The finance ministry said it could not provide precise GDP estimates, citing planned revisions to data against which 2010 numbers will be calculated, but a finance ministry official said a new forecast should be ready by the end of April.

Separately, Greek Prime Minister George Papandreou said his country was working to get its fiscal house in order and wanted markets to recognize that.

**U.S. sale of \$21 bln of 10-yr debt draws good demand**

The U.S. government sold \$21 billion worth of 10-year debt in an auction that attracted surprisingly strong demand, which bodes well for an upcoming 30-year long bond offering.

The 10-year sale was the second of this week's three bond offerings totaling \$74 billion and benefited from a pre-auction sell-off that cheapened the market enough to attract investors in strong numbers.

The auction attracted bids worth 3.45 times the amount on offer, which was well above the average of 2.88 at the last six reopenings of 10-year notes.

Yields at the auction came in below expectations, based on trade in the when-issued market at the deadline for bids.

In one weak note, foreign central bank and large institutional investor demand was lackluster, based on the indirect bidder category, which accounted for about 35 percent of the sale.

This was below the average of 41 percent in the reopenings since June, which has become a benchmark for comparisons due to changes in calculations that have boosted this category.

**U.S. Sen Corker: no exemptions in new watchdog bill**

An influential Republican in U.S. Senate talks on financial regulatory reform said there are no special exemptions for particular institutions in a proposed new government financial watchdog agency.

Senator Bob Corker said: "There are no carve-outs for anybody." U.S. businesses including financial services firms and payday lenders have been lobbying the Senate to water down a White House plan to create an agency to regulate consumer financial products, such as mortgages, credit cards and payday loans, which are short-term loans made against the borrower's next pay check. Corker stressed at a conference that he was not aware of any carve-outs and suggested that reports that said otherwise were incorrect.

Separately, U.S. Health Secretary Kathleen Sebelius ratcheted up the pressure on health insurance companies, urging them to forgo short-term profits and stop fighting President Barack Obama's health reform plans. Sebelius called for more transparency in premium pricing and to work with the administration to pass comprehensive healthcare reform.

**Euro stability top priority in fund debate -Germany**

Germany believes the euro's stability must take top priority in the creation of any European monetary fund, and EU rules on curbing budget deficits must in no way be softened, a government spokesman said.

Chancellor Angela Merkel was still interested in the idea of such a regional fund, which could bail out a euro zone nation which faced insolvency, but many questions remained on how it might be financed, he said.

With Greece battling a debt crisis, German Finance Minister Wolfgang Schaeuble gave his backing to the idea in a weekend interview and Merkel has also given a degree of support.

But Germany's two representatives on the ECB's Governing Council are less enthusiastic.

Such rules include the Stability and Growth Pact, under which euro zone countries are supposed to keep their budget deficits under three percent of their gross domestic product.

Separately, the euro zone should reform its fiscal framework allowing budget gaps and run surpluses to avoid debt problems in the future, the euro's godfather Robert Mundell said.

**U.S. govt posts record \$220.9 bln budget gap in Feb**

The United States posted a record \$220.91 billion budget deficit in February, Treasury Department data showed.

The February deficit was in line with analysts' consensus forecast in a Reuters poll for a \$222 billion budget gap but well above the \$193.86 billion for the same period a year ago.

The department said the budget gap for fiscal year 2010 to date was a record \$651.60 billion, well above the \$589.80 billion posted for the same period in fiscal year 2009.

The government has now posted a budget deficit for 17 straight months, the Treasury Department said.

Separately, U.S. Treasury Secretary Timothy Geithner welcomed moves by some big banks to cut overdraft fees and said he hoped all banks will do so.

He said the Obama administration's strategy to halt recession and contain the financial crisis has been effective, but vowed to continue stabilization efforts. Geithner, in prepared testimony to a U.S. House of Representatives Appropriations subcommittee, said the economy and financial system still faced challenges, but the stake of taxpayers in the banking system was dramatically smaller than a year ago.



## TODAY'S TOP NEWS

**French, Italian output jumps, euro zone uncertain**

Industry output figures for Italy and France were stronger than expected in January but analysts said there was little in the data to suggest a broader pick-up in euro zone economic growth.

Data released showed industrial output in France grew 1.6 percent month-on-month in January.

In Italy, output jumped 2.6 percent on the month, again ahead of a Reuters forecast for growth of 0.6 percent.

German exports, adjusted for seasonal swings, fell by 6.3 percent on the month to 67.9 billion euros, with imports rising by 6.0 percent to 59.2 billion euros, the Federal Statistics Office said. This yielded a trade surplus with the rest of the world of 8.7 billion euros in January, down from 16.6 billion euros in December. The U.S./German 10 year bond yield spread widened to 59 basis points, from around 57 basis points at midnight on Tuesday, its highest level since mid-2007.

Separately, Italy is readying its first CDS index of Italian corporate issuers and a green light could come as early as June, sources close to the operation said.

**ICE, CME clearing membership rules challenged for CDS**

The membership rules for the divisions of the IntercontinentalExchange Inc and the CME Group that will clear CDS are being challenged by firms who say the exchanges' requirements may limit participation to established dealers.

ICE and CME are the only clearinghouses in the U.S. that have begun clearing trades in the \$31 trillion CDS market, but participation by "buyside" firms has been slow due to concerns about the protection of collateral backing the trades.

Potential new members are being discouraged by capital requirements which limit membership to only the largest firms, critics said. A rule that clearing members provide their own pricing for CDS contracts also effectively restricts membership to large CDS dealers.

The SDMA wants clearing models for over-the-counter derivatives to function in a way that is similar to futures markets, where trades can be routed to central clearing members by a wide range of brokers or other participants.

**Brown says UK to maintain triple A credit rating**

Prime Minister Gordon Brown said he believed Britain would maintain its coveted top credit rating and announced a pay freeze for senior civil servants and military officers to help tame a record deficit.

Setting out his economic plans weeks before an election, Brown said recovery remained fragile and that to change course now would risk plunging Britain back into recession.

Brown said cuts should only come once recovery was assured; but jittery markets should take heart from a government commitment to halve the deficit over four years. Brown said he believed that the longer maturity of British government debt put it in a better position than other countries with large deficits.

Meanwhile, Britain's FSA said, there is no case for emergency action to crack down on naked selling of CDS, as called for by some EU states.

Separately, Britain's economy grew by 0.3 percent in the three months to February and has expanded by 0.7 percent since last September's trough, the National Institute of Economic and Social Research said.

**Dubai creditors to get multiple options -sources**

Lenders to Dubai World will get a range of options including full repayment once Abu Dhabi decides how much additional support it will give its debt-laden neighbor, sources close to the discussions said.

Bankers in London and the Gulf are divided over how Dubai should restructure the \$26 billion debt pile dogging its flagship holding company, leading the emirate to consider parallel offers in an effort to please all, the sources said.

Local banks with little lending power may want whatever they can get from Dubai World quickly, while international lenders with big balance sheets can afford to wait for full repayment.

Two of the restructuring options include repayment over three to five years with the principal discounted, and repayment over seven to nine years with no discount.

No real decision on the exact shape of the deal has taken place yet, said one London source.

## NEXT UP

**POLL-U.S. GDP to slow in Q1, Fed rates on hold to Q3**

After a growth spurt at the end of 2009, the U.S. economy will slow in the months ahead, keeping the Federal Reserve from raising borrowing costs until the final three months of the year, a Reuters poll showed.

The survey of over 70 economists suggests U.S. GDP will grow at a 2.6 percent annualized rate between January and March, less than half the pace of the fourth quarter of 2009, when it expanded at a 5.9 percent rate.

The poll predicts it will grow by 2.9 percent in 2010 on an annual basis. Economists expected the core CPI to grow 1.4 percent in the first quarter of the year and to average 1.3 percent over the course of 2010 before edging up to 1.6 percent in 2011.

That suggests the Fed won't need to raise its benchmark federal funds rate until the final three months of the year. Median forecast from respondents see a rise of the fed funds rate to 0.75 percent between October and December. After hitting 0.75 percent by year end, economists expect rates to rise relatively slowly, reaching 1.5 percent by mid-2011. Headline inflation is likely to rise at a 2.5 percent rate in the first quarter and a 2.1 percent rate for the whole of 2010, the survey showed.

**POLL-G7 recovery still on course but listless**

A distinct lack of momentum will drag on the rich world's economic recovery this year, according to the latest Reuters economic outlook in which economists largely bucked a recent trend of rising forecasts.

Median forecasts from the survey of around 250 economists showed slight downward revisions to 2010 quarterly growth forecasts for the United States, while those for Britain and Japan were mostly unchanged from February's poll.

But with increasingly confused economic data now clouding the outlook, forecasters also pushed back expectations for interest rate hike in the euro zone.

Economists kept their full-year GDP forecasts for 2010 and 2011 largely unchanged from February's poll.

Japan is expected to grow this year at 1.6 percent and 1.2 percent in the euro zone and Britain, down slightly in the euro zone's case from 1.3 percent in last month's poll.

Greece's debt crisis has called the euro zone's credibility into question and economists in the latest poll said they expected the country to endure a much deeper recession than currently forecast by the Athens government.



## DEEP DIVE Commentary and Analysis

## SPECIAL REPORT-The death of a boutique bank

By Elinor Comlay

In September 2008, as Lehman Brothers was breaking into a million pieces, a young investment bank was pushing up through the rubble.

Pali Capital, a boutique firm specializing in derivatives and fixed-income trading, was one of the few financial outfits hiring traders and bankers -- often from the likes of imploding Wall Street behemoths like Lehman and Merrill Lynch.

With its annual revenue on pace to top \$200 million that year, Pali appeared to be an oasis of prosperity. Rodin sculptures adorned its offices and a corporate jet ferried its executives around the world.

The key to Pali's success was its charismatic co-founder and chief executive, Bradley Reifler, a master salesman who was as good at wooing clients as he was at spending money -- his own as well as the firm's. He sometimes commuted to work by helicopter from his sprawling horse farm in upstate New York.

But last month, Pali itself shattered. The firm said it was winding down after failing to sell itself to a group advised by former Bear Stearns Chief Financial Officer Sam Molinaro.

The bank's swift demise surprised industry observers. As with many firms that suddenly fail, not everything at Pali was what it seemed.

For all his enthusiasm and charm, Reifler had a combative side. Most conspicuously, he had a tendency to sue, launching at least a dozen lawsuits against people and companies over the last 10 years.

Reifler's spokesman said he declined to comment and Bert Cohen, Pali's other co-founder, could not be reached and his lawyer did not return calls. But interviews with more than 10 former employees of Pali and Reifler and examination of 11 lawsuits paint a picture of a man who spent freely and had few qualms about going to court if he felt threats to his control.

According to former employees and people who reviewed the company's financial statements, Reifler's penchant for litigation helped destroy the bank he spent so many years building.

## THE PANAMANIAN CONNECTION

Reifler and family friend Cohen co-founded Pali in 1995. For the first few years, Reifler maintained his job at Refco, the now defunct commodity trading business started by his grandfather, Ray Friedman.

In 2000, Reifler left Refco to become chief executive of Pali, and it began to flourish. He immediately set out to expand the bank into areas including merger advisory, asset management and hedge fund investments. At its peak, the firm employed more than 200 people.

"He was a phenomenal salesperson," said one former employee, noting how Reifler managed to persuade Panamanian bank Grupo Mundial to invest \$25 million in the company. He also secured a \$6.5 million loan from a Bear Stearns Cos unit by offering a personal guarantee.

Reifler hired good people -- and paid them well, often offering guaranteed bonuses. Richard Anthony, then a little known trader, joined Pali in 2002 and built an equity derivatives sales and trading effort catering to hedge funds. The business generated big profits for the bank, contributing as much as 20 percent to total revenue, according to people who worked for Pali and others who looked to buy the company.

Like his boss, Anthony was a flashy salesman. His 'Pali Poker' nights -- charitable fundraisers held at top New York locales including Capitale, The Box and the Hammerstein Ballroom -- were big draws. They featured dancers from the Rockettes or the New York Knicks; John Legend performed at one. Some

Pali clients would do more business with the company in the run up to these events, just to ensure they got a ticket, two people familiar with the company said.

## FORTUNATE SON

Reifler was born to privilege.

He grew up in Southern California, where his mother owns a Malibu beach house designed by Getty Center architect Richard Meier. He went to the elite Harvard School for Boys, and later bragged to colleagues that one of his schoolmates was Joseph Gamsky, also known as Joe Hunt, the man behind a Ponzi scheme and murder scandal known as the Billionaire Boys Club.

As Pali prospered, Reifler's income soared. He received 3 percent of all gross brokerage revenue. And he knew what to do with it.

In 2000, after his wife and children took riding lessons at the exclusive Chelsea Equestrian Center, he sold the family's multi-million dollar Manhattan townhouse, bought a 150-acre estate in Millbrook, New York and hired a team of professionals to look after as many as 12 horses.

The estate, known as Sky Blue Farm, also has an ice hockey rink, tennis courts and indoor and outdoor swimming pools.

When Reifler was not commuting by helicopter, a driver took him into Manhattan in a custom-fitted SUV with a trading screen and seats that reclined for sleeping, allowing the boss to rest during the almost two-hour journey from Millbrook, according to one person who had seen the vehicle.

At work, Reifler wore finely tailored suits and hosted \$1 million holiday parties for Pali employees at venues such as the Guggenheim Museum. Clients and key staff were taken on trips in the Pali jet. Some got invitations to the shooting range at Sky Blue Farm.

"He was fancy," said a former junior Pali employee, who recalls being impressed by Reifler when he went to interview at Pali. Reifler met the prospective hire in his corner office, filled with artwork, expensive-looking furniture, and a model of Pali's Falcon 900 jet. During the interview, he touted Pali's entrepreneurial culture while an assistant brought in freshly-brewed espresso in gold-rimmed china cups.

"The office reeked of excess," said Ron Simoncini, president of Axiom Communications, a public relations firm that was hired by Studio U, an arts and craft store in Chester, New Jersey, set up by Reifler and his wife, Ashley. The shop sold specially-designed craft projects and held children's parties, as well as classes and events for adults.

Reifler relished Pali's success. The collapse of big Wall Street firms created an opening for nimble trading firms, and by 2008, Pali and Reifler had acquired a fair amount of cachet on Wall Street.

"Everyone was very excited about working there," said Lauren Schachter, chief executive of LBS Staffing, which recruited employees to Pali in 2007. "They had a great reputation."

The junior employee said the firm was regularly mentioned in newspapers and on cable channel CNBC as being among the few that were hiring while other banks were closing down. "We thought, 'We're not just a boutique any more,'" he said.

## SEE YOU IN COURT

Reifler's extreme litigiousness was rattling the firm, but few inside the bank were willing to confront him about it.

By June 2008, Pali Capital's holding company had seven directors and only one -- Bert Cohen -- was independent, according to one lawsuit, filed that month by three shareholders.

Other board members included Kevin Fisher, who later became co-Chief Executive after Reifler departed; derivatives boss Rich-



## DEEP DIVE Commentary and Analysis

ard Anthony; London-based trading head Richard Abrahams; chief financial officer David Wasitowski; and chief legal officer John Fedders. All of them reported to Reifler.

"He could make your life miserable," another former employee said. "He appointed himself head of everything, including compliance, and everyone reported to him," he said, adding, "If you crossed him, you didn't get a bonus."

In January, Reifler filed a lawsuit accusing Derrelle Janey, Pali's head of strategy, of failing to repay a one-year \$50,000 personal loan Reifler made him in May 2008.

Lawyers for Janey said Reifler was trying to buy his loyalty. They also said the funds Reifler lent him were likely not his but Pali's, according to the lawsuit filed on Janey's behalf in response to Reifler's claim.

Public relations firm Axiom Communications said in its lawsuit that Reifler used Pali to finance Studio U, his arts and crafts store. Axiom is suing Pali and Studio U for payment of more than \$76,000 that the company says it is owed for Web site development and other contracted services. Axiom alleges Pali Capital guaranteed it would pay for work the agency did for Studio U.

By the summer of 2008, Cohen and other large shareholders had become concerned that Reifler had "secretly run Pali as his own private fiefdom," according to the June 2008 lawsuit filed by shareholders Ronald Weinstein, Stuart Sloan and WGS Verwaltungen.

That lawsuit alleges that Reifler paid himself millions in additional compensation, without board approval, by claiming among other things "loan guarantee fees" and consulting services to other companies that he owned.

"His penchant for ignoring fundamental rules of corporate governance and lining his own pockets appears to have touched every aspect of Pali's business," the plaintiffs' lawyers wrote.

Reifler and Cohen became mired in a toxic battle for control of Pali. According to the lawsuit filed by shareholders, Reifler sent Cohen emails calling Cohen "a bitter lonely ass" and saying "you should just kill yourself...do everyone a favor."

## BOOTING OUT REIFLER

In the summer of 2008, Cohen and other Pali shareholders -- including Seattle-based businessman Sloan and Sam Zell's SZ Investments -- began an effort to oust Reifler, according to a separate lawsuit filed in response by Pali Holdings, Pali Capital's parent.

The shareholders had accused Reifler in a lawsuit of forging a proxy document to support Reifler's legal claims against Cohen and the other shareholders. A document obtained by Reuters indicates the person whose proxy Reifler is accused of forging believes Reifler acted "in good faith" on a voting arrangement he discussed with Reifler. Both lawsuits have since been discontinued.

Reifler left Pali in October 2008. According to lawsuits filed by Reifler's lawyers, he resigned voluntarily. Lawsuits filed by Pali lawyers say he was fired.

Soon after his departure, the multiple lawsuits began to take a toll on Pali's financial health.

According to a letter that Reifler's lawyers sent to a New York State Court judge, in 2009 the company reported \$13.4 million in expenses for "external services," most of which the letter said were believed to be legal fees.

That sum was almost triple the \$4.8 million in unpaid legal expenses that the firm had by the end of 2008, according to a filing with the Securities and Exchange Commission. The legal obligations were onerous for Pali, which had just \$1.1 million of cash on its balance sheet at the time, according to court filings. Company statements for 2009 have not been filed with the SEC and

could not be obtained.

Reifler is suing Pali for release from the loan he guaranteed and he also began an arbitration proceeding through brokerage regulator FINRA to settle a dispute over compensation he says he is owed from Pali. The arbitration is scheduled to start in May.

## BUYER BEWARE

The bank had plenty of prospective buyers, including mortgage trading boutique Braver Stern and middle-market investment bank Rodman & Renshaw. Some were even willing to swallow the high legal expenses; one made an offer in mid-2009.

But Pali's board believed the company could do better, and held out for an offer from Braver Stern, according to people briefed in the matter.

Anthony, the firm's star performer, became frustrated by the slow pace of the deal and left for BGC Partners in December, taking a team of traders with him. Losing Anthony's revenue was a final straw for struggling Pali. Buyers lost interest after Pali's most profitable division walked away.

Reifler was not in favor of selling Pali. Last January he founded a group called the Committee of Concerned Pali Shareholders and sent a letter arguing that the proposal to sell Pali was not in shareholders' best interests. "Pali should be pursuing alternative forms of recapitalization that would result in less dilution for existing shareholders," the letter said.

Used to getting his own way, and always more of a trader than a business man, Reifler may have seriously miscalculated Pali's state of affairs and the cost to the company of his litigation, say people close to him. He is now on the hook for the \$6.5 million loan he personally guaranteed

His company is gone -- but not his combativeness. According to his Twitter page, he is launching a new firm with what he refers to as "non-criminal" partners.

## Greek CDS overtures fall on deaf ears in Washington

By David Lawder and Rachelle Younglai

Greek leaders' overtures for far tougher curbs on credit default swaps fell largely on deaf ears in Washington, but they'll go back to Athens with some sage advice from local policy wonks: look in the mirror and don't blame market messengers for your debt woes.

"It's fairly common for finance ministers and political leaders under threat to blame the speculators. But sometimes the speculators are right," said Edwin Truman, a former U.S. Treasury and Federal Reserve international finance official.

For a second day this week, Greek Prime Minister George Papandreou and his finance minister, George Papaconstantinou, urged backing for tougher rules for credit default swaps and a ban on some activities such as "naked" short-selling of sovereign debt or trading "naked" credit default swaps (CDS) without owning the underlying bonds.

Hedge funds have been accused of aggravating Greece's debt crisis by using such trading activities to bet on a government default.

Credit default swaps have been condemned by many U.S. lawmakers because of the \$62.5 billion taxpayers handed global banks to unwind CDS contracts written by bailed-out insurer American International Group. But any outright ban is highly unlikely.

## STRONG, IF UNFLATTERING, SIGNAL

The trading of CDS on Greece's sovereign debt -- essentially an insurance policy against a default -- provided a valuable market signal about worrisome policies, said Douglas Elliott, a senior



## DEEP DIVE Commentary and Analysis

fellow at the Brookings Institution in Washington and a former JPMorgan investment banker.

"The Greek bond market could directly deliver the same bad news by itself and Greek bond yields would widen," he said. "The CDS gives you one more pretty liquid way of delivering the signal from the markets. Just because you don't like the signal, you shouldn't blame the messenger," said Elliott.

The Obama administration effectively said it would prefer to stay on its own course for reforming derivatives markets by making them more transparent and increasing capital requirements. CDS and other standardized derivatives contracts would be moved away from opaque over-the-counter trades onto exchanges or sold through central clearing houses under reform plans backed by the White House that are currently stalled in Congress.

An administration official also said regulators will get enhanced tools to crack down on market manipulation and abuse through position limits and tougher prudential requirements.

"But the central task before the Greek government is to continue to move forward on their plans to restore fiscal stability and growth to its economy," the official said. "We commend them for the bold steps they've already taken and have confidence that their European partners will support them on this difficult road."

CDS on sovereign debt are seen as likely standardized contracts that would be put onto an exchange or central clearing under the Obama plan, making manipulation difficult.

## LIMITED INFLUENCE

A recent report by Citigroup analysts in London said the sovereign CDS market is still tiny compared to the sovereign debt market, limiting its impact. There are \$9 billion in Greek sovereign CDS outstanding relative to \$406 billion of government bonds. For Europe as a whole, there are only \$108 billion in sovereign CDS versus \$11 trillion in debt.

The Citigroup analysts, who say that much of the trade in sovereign CDS is legitimate hedging, argue that the inability to arbitrage

between CDS and bonds makes it difficult to push sovereign yields higher as is often alleged.

Conversely, they say it is easier for CDS to drive bond yields tighter: a shrinking spread on a CDS will often cause higher market demand for the underlying bonds.

While European Union members and other G20 economies may be more amenable to Greece's call to rein in speculators, a global ban on sovereign CDS would not be possible without the support of the United States, home to one of the largest CDS trading centers.

And a ban on naked credit default swaps without owning the underlying bonds, would be difficult to define, administer and police, experts say.

An investor might not hold the same debt security in the same amount as the CDS reference security, but may hold other debt securities from the same issuer, which may be senior or subordinate to the reference security, said Denis McCusker, a partner at the Bryan Cave law firm.

"If the euro zone were to ban naked CDS transactions but the U.S. not, or vice versa, it would be expected that traders and speculators would find a way to move across the borders for these transactions," he said.

If the U.S. Securities and Exchange Commission and the Commodities Futures Trading Commission get the authority to regulate the private swaps market under the Obama plan they could prevent investors from amassing large positions in a particular derivative such as a CDS.

The regulators could also make it unpalatable for issuers to write swaps by imposing onerous capital requirements.

But the Citigroup analysts, who titled their report, "Don't blame the mirror for your ugly face," suggested that CDS bans would not stop markets from beating up on Greece over its debt woes.

"We strongly believe that the medium term likelihood is that many of these legitimate hedgers would simply sell or short government bonds instead," they wrote.

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