



## Cantor's Wager on Gambling

By Maureen Nevin Duffy

**Reiner**

February 20, 2006 - Back in the 1980s, when markets moved on tips and trades that were conveyed from lips to ears over phone lines, Cantor Fitzgerald was a pioneer of screen trading. Though the inertia in government bond trading, Cantor's forte, was in voice brokerage, Cantor saw the electronic future ahead of most others and decided to ride that tiger rather than get eaten by it. Today, the preponderance of on-the-run Treasury securities are traded electronically and other asset classes are following suit.

Advertisement Cantor and its technology offshoot eSpeed suffered tragically in the Sept. 11 attacks on the World Trade Center, losing more than 600 employees at that site. But the electronic infrastructure allowed the companies to pull through. Today they face more competition than ever--and eSpeed's future has become the subject of speculation around Wall Street--but they haven't lost the creative mojo.

Cantor is trying to repeat what it wrought in the financial markets. This time it sees the future in the frenetic, multi-billion-dollar, pop-up-screen world of Internet gaming. Marty Reiner, principal of Reiner Consulting in Chicago, has the distinction of having worked in the financial and gaming worlds, and he believes Cantor has the right idea in trying to transfer technology from one to the other. The financial markets and the global casino that the gambling market has become have more than a few structural and functional characteristics in common: extremely high, nonstop transaction volumes; a need for fault-tolerant systems with millisecond response times; payment and clearing requirements; order routing; and back-office accounting and client management.

"Cantor is uniquely positioned here, having taken trading up to e-speed," says Reiner, pun intended. "Europe is at least two to three years ahead of the U.S. with respect to Internet gaming, due primarily to antiquated U.S. anti-gaming laws." (Though the laws are widely flouted, online gambling is illegal in the U.S. under a 1961 anti-racketeering statute. That didn't prevent more than a half billion dollars from being wagered on the recent Super Bowl.)

Reiner was an undergraduate studying materials engineering at Massachusetts Institute of Technology in the 1980s, where he witnessed the wholesale recruiting of math majors who would become the geeks that would remake the trading business around technology. Another parallel: "Where casino and gaming were once traditional, they've evolved now to things that require math talent, especially poker," says Reiner, formerly SVP of business development at the Chicago Board of Trade and a derivative markets consultant with Eurex who now describes himself as an "i-gambling" consultant.

"Likewise, when the first options on stocks came along in '77, people didn't understand them," he

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Asher

recalls. "They treated them like corn or soybean futures. They didn't realize they were a mathematical derivative of something else. As the '80s unfolded, math-savvy people were moving into trading due to its greater complexity. This created a basis for firms like Cantor to evolve from cash to an entirely different dealing system. The markets became more and more appealing to quants as the complexity of the financial products increased and new arbitrage opportunities were facilitated by advanced electronic dealing systems like eSpeed."

Recently back from London's International Casino Exhibition (ICE), the Internet gaming industry's biggest convention in Europe, where the sport is mostly legal, Reiner observes: "The show was buzzing with excitement and opportunity. Remember when trading used to happen in a pit? Remember when gambling used to happen in Vegas? Gaming is wide open now--no longer a closed club." The ICE Web site says that the event hosted 186 exhibitors from 33 countries.

Regulators were at that convention--not in policing mode, but trying to attract casino operations--from offshore havens such as the Isle of Man, Malta and Gibraltar, says Reiner. They want in on the \$12 billion-plus in Internet-based revenues as estimated by Christiansen Capital Advisors, among other financial firms that have sized up the space.

"Technology will take both traditional, land-based and online gaming to a whole new level, just as it has done in the financial industry," says Reiner. Cantor Fitzgerald obviously agrees.

A business unit called Cantor Gaming plans to supply handheld devices for betting on casino as well as sports games to Nevada casinos in a front-to-back, packaged service that will spare those establishments from back-office drudgery. "I believe that we have more experience than anyone else in offering real-time, reliable and secure execution of financial transactions on mobile devices, and more experience than anyone else in wagering on mobile devices," says Joe Asher, managing director of Cantor Gaming.

Having written the legislation, Bill 471, which was nearly unanimously passed by the Nevada legislature--41-0 Assembly, 20-1 Senate--in June 2005, Cantor is awaiting final approval of the Nevada Gaming Control Board regulations by the Nevada Gaming Commission. One of the mandatory public hearings was held earlier this month. Once those approvals are in place, Asher expects the nonexclusive agreements with casinos to move ahead quickly.

As part of the regulations, which are posted on the commission's site, bettors won't be permitted to use the handheld devices in any private areas, which include the parking garage and guest rooms. They will most likely be signed for and returned at the end of the guest's stay.

Cantor will say only that it's in negotiations with major casinos "with a high level of interest" for the devices. They have names like Gizmondo, iPAQ, palmOne and VAIQ. Asher declines to explain the business model in any detail. However, it's likely that the well-capitalized Cantor may offer the devices and service for very little, in return for vigorish--a share of the players' and/or casinos' winnings on the bets placed over them. Says Asher, "We have the luxury of being in a very strong financial position, which allows us to offer systems to casinos on terms that they find very appealing."

Asher tells *Securities Industry News* that Cantor is respectful and cognizant of the investment the casinos have made in structuring their businesses, marketing to their clients and cultivating their brands. But will they ask for some of the purse? "We're a big believer in aligning our interests with those of the casino property owners," says Asher. "We like partnerships where our interests are aligned."

It could be a highly lucrative strategy. Although the world market for gambling on mobile devices is reported by U.K.-based Juniper Research to be roughly \$2 billion now, the research firm predicts a meteoric rise to \$19 billion by 2009--and that's without full legalization by the U.S.

In the U.K., where odds are legally available on the outcome of just about anything, Cantor offers Internet gaming out of a London base. Cantor has an Internet casino license from Alderney, an offshore site near the better-known Channel Island of Guernsey, which allows Cantor to offer Internet gaming wherever it is legal.

Through Cantor's Spreadfair product, gamblers bet on football, horse racing, cricket, golf, box office earnings of movies, the National Football League, Olympics, politics, rugby, snooker, tennis--and the financial markets. Ironically, proceeds from these bets are not taxable in the U.K., whereas stocks and shares are.

Cantor Index is the company's overseas-marketed brand, which offers 24-hour trading in shares, indices, currencies, options and interest rates over mobile devices. As an example, in the case of the instruments known as "contracts for difference," Cantor's literature states: "Unlike conventional share trading, the bet is tax-free, and with interest on accounts, maximum efficiency on capital and instant online account opening, financial spread betting has never been easier!" Cantor supports real-time prices for the instant online transactions through its Axess system.

That type of wager is only available on U.K. securities, but how would U.S. regulators weigh in on this sort of thing? Said a Securities and Exchange Commission source, declining to comment on any specific firm or product, "We regulate securities; we don't regulate gambling," which in the U.S. is a state-level concern. Still, the use of stock-price behavior as grist for wagering could have some influence on the markets--isn't that what derivatives do? To which the source replied, "I can't say the commissioners are not concerned about that."

According to Reiner, Cantor's main thrust at ICE was to push its white-label casino site service, which it offers in partnership with Australia-based Gaming & Entertainment Group, a developer of software for Internet casino sites. Cantor also demonstrated its mobile gaming devices. Cantor claims a considerable lead on the competition, having launched its mobile device in the U.K. in September 2003.

Cantor's Wall Street brethren, while cautious, are getting into the act. Merrill Lynch, Fidelity Investments and Goldman Sachs have a joint 15 percent stake in Party-Gaming, a Gibraltar-registered company that trades in U.S. dollars on the London Stock Exchange. The PartyGaming group reported a 65 percent increase in fourth-quarter revenues, to \$320.3 million. Its full-year profit report is due at the end of February; for the six months through June, earnings before interest, taxes, depreciation and amortization, and excluding share-option and IPO-related expenses, were up 70 percent, to \$258 million.

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