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FORBES

The Money Men

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A Lover, Not a Fighter

So you're thinking about a fling in the commodities market? Leo Melamed is the man to talk with. At 39, Leo is that rare animal, a highly successful commodity trader. He is also retiring chairman of Chicago's Mercantile Exchange, which has so prospered under his leadership that it is soon to move into a gleaming new Chicago building.

Before you go any further, we will warn you about a price Leo has paid for his success: He has ulcers. "During the course of a trading day," he says, "I'm as cool as a cucumber. I won't show an emotion, and I try never to let on to anybody on the floor whether I'm in a losing position or a winning position. That's my style and that's how you get ulcers; you keep it all inside.

"When I first found out I had ulcers, my doctor told me, 'You've got to change your way of living. Stop playing poker with the world and start showing your emotions, start letting them out.' I couldn't do it, though. You can't give vent to your feelings and trade in commodities."

So Forbes learned requirement No. One for a successful commodity trader: You have to accept ulcers. You have to be as cool as a cucumber. You can't exult when you're winning or panic when you're losing.

And then, says Melamed, you have to develop your own style, fitted to your own personality. During his first three years, he studied each and every trade he made, analyzing his successes and his failures. Out of this analysis, he began to develop a set of tactics.

"At first I was a scalper, operating with small capital and making dozens of trades daily, trying to catch whatever little swings there might be.

"I found out you couldn't make much money that way, not even as a member of the Exchange where you didn't have to pay much in the way of commissions. So I went in for positioning, holding my contracts for a few days or weeks. This worked better."

In the course of developing his "positioning" approach, Melamed adopted two "laws." He has framed them and they hang on his office wall:

I am married to my wife, not my commodity position. This means holding no position for more than two weeks. "I wasn't looking to capitalize on the entire move of any swing. I didn't want the entire bottom or the entire top—just a slice out of the middle of a market move."

Be a lover, not a fighter. This takes a bit of explaining. Melamed decided he could not make good decisions unless he had the right psychological attitude. He learned that he rarely accumulated a winning position when he had losses on his first purchase. If at the end of the first day his initial trade is at a loss, he closes it out because he will not begin a position from a losing trade.

Mere superstition? "No. Absolutely a must. The way to accumulate a position in which you have a good chance of making a profit is from the winning side. If you allow it to start from a loss position, you can lose your correct perspective in the market. You're beholden to a loss and you want to make the loss good. There is too much influence of that loss position on your rationale in staying or not staying in the market. Whereas with a profit, it's much easier to rationalize clearly because you can always get out taking a profit. There's no emotional thing to hold you from getting out.

"Everyone can't fight his own emotions all the time. But I try to be a lover and go with the trend of the market. I won't fight the market. The fighters don't end up with any money at the end of the year."

Beyond this, Melamed uses all the standard tools: charts plus fundamental studies—mainly material about future supply and demand released by the Government. But he is not trying to catch the big, fundamental changes. Instead, he tries to anticipate changes that other people will react to in the short run.

Melamed says he makes money in ten out of every 12 months. Often he makes as many as 500 trades a week, instantly aborting any trade that looks like a mistake. "In a really good month I can make maybe $25,000, and in a bad month only lose $3,000."

He puts strict limits on how much he puts at risk—100 carloads of a commodity such as pork bellies. This would require $50,000 capital. "I know my limitations and I stick by them. Everyone should."

Melamed's training for this nerve-wracking occupation was rigorous if unplanned. His father was a Polish refugee from Hitler's invasion who escaped with his family through Siberia in two years of touch-and-go terror. Leo got his first job as a runner for Merrill Lynch's commodity department. He took the job because the hours let him catch afternoon law classes at John Marshall Law School.

He got his law degree in 1955 and began to practice, but he couldn't get commodities out of his mind. "The noise and the clamor are enough either to scare you or fascinate you. It did both for me."

In the early Fifties the Mercantile Exchange was in a state of decline, with futures trading mostly in eggs and onions, where daily fluctuations were relatively minor. While still at school, Melamed borrowed $3,000 from his father and bought a seat on the Mercantile Exchange. When he was 21, he started trading. ("One of the floor brokers was carrying me. He figured that even if I lost out trading, I'd earn enough in law to pay him back.") Melamed started practicing law and trading in commodities on the side.

But here's something else that should give you pause if you're thinking of messing around with commodities: Melamed finally dropped his law practice. Commodity trading and other interests just didn't mix.

You *still* want to trade in commodities? Well then, Melamed has some advice for you.

To begin with, he points out that the public cannot trade commodities as it does stocks. You can't begin with all your capital. Margins are as low as 10%, and you surely will lose it all and that will be that. "Those who say they've got $10,000 and they're going to shoot it, as if they're playing dice, will surely lose it, and most of them never come back because that was all they had to lose. So a newcomer has to put aside some money to lose and learn, and have enough left over so he can stay in the game."

Melamed doesn't see commodities as a path to riches. Gone are the days of *The Pit*. But for the man who has the temperament and the time and who doesn't mind the danger of getting ulcers, there are compensations. "If a guy starts with $10,000 and ends up after a period of two to three years having lived well and now has $50,000 to $100,000, I'd say he's done very well." Meaning Leo Melamed, of course.

"Your stockbroker will tell you you may enhance your investment by 10% over a year in stocks, even 20%. If you went into commodities with $10,000 and made it $20,000 within a year, which a good trader should easily be able to do, that's 100% enhancement. So that's what the comparison should be.

"But that still doesn't make you a millionaire. If you start with $500,000, it probably will not make you another $500,000, because commodities are a limited thing. More money doesn't necessarily mean an equivalent amount of more profits, unfortunately. Your trading habits change and you won't move as quickly with a bigger position because they're not as flexible."

Of course, this kind of speculating is only one small part of commodity trading. The really big dealing is done by big corporate hedgers, who are producers, processors, or warehousers of commodities. Melamed has seen to it that his Mercantile Exchange has played an ever bigger role in this important economic function. He forced the once-sleepy exchange to expand trading in such items as pork bellies, cattle and—last month—into foreign currency. Since he took the chairman's job in 1969, the Merc has become much more important in national commodity trading. In 1971, $40 billion or so in futures contracts were traded there. He has seen to it, too, that the exchange is policed as never before.

When things get really hectic, Melamed thinks how close he came to an early grave in Poland or Siberia. Then he slips behind his desk to a store-sized gumball machine where he keeps a big supply of his ulcer pills. ■

Commodity Trader Melamed