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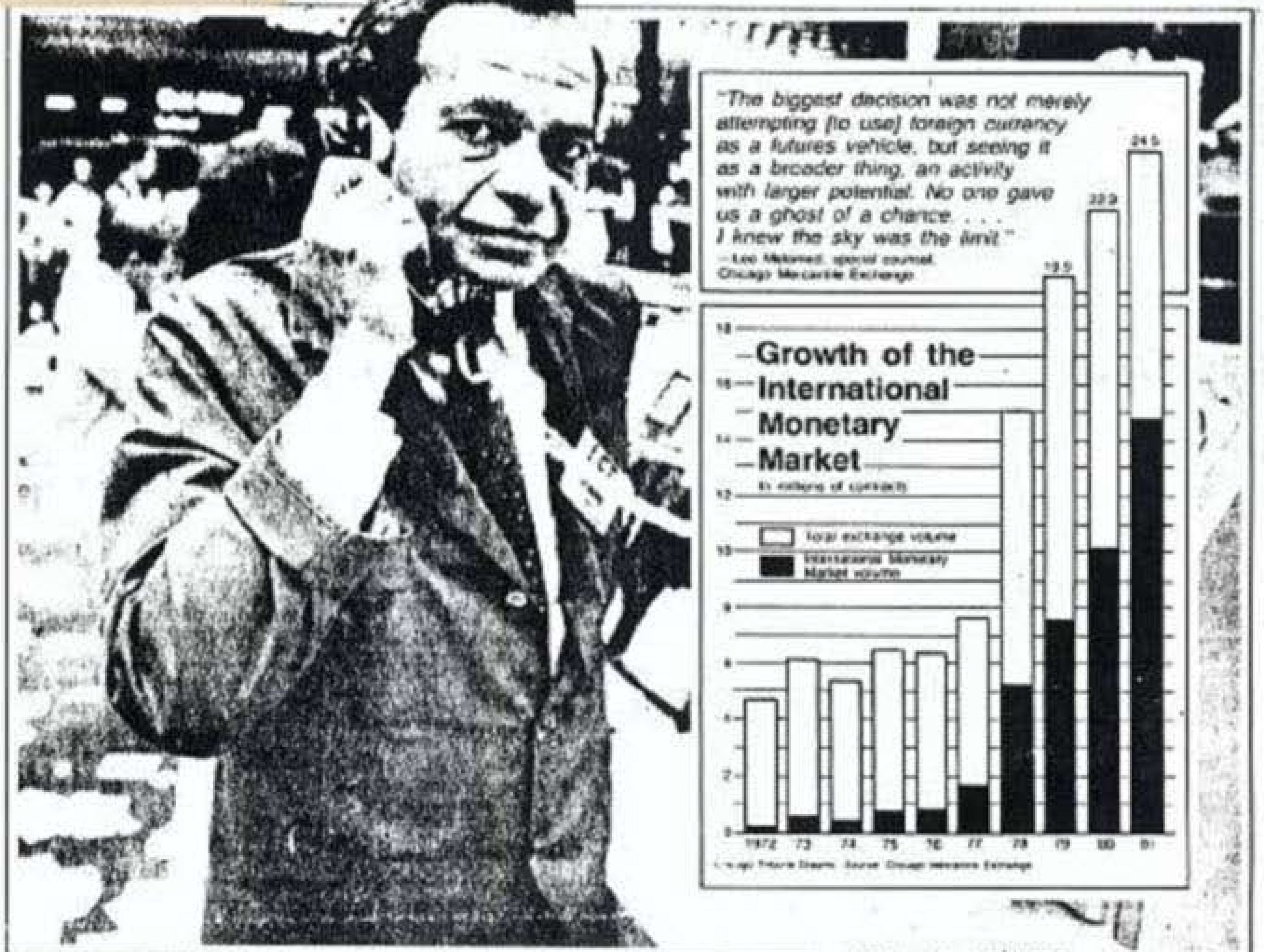

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Helped transform futures

Melamed Merc's wizard of the exotic

By Laurie Cohen

TEN YEARS AGO, Leo Melamed was an unknown young trader from Chicago trying to sell an exotic idea to the country's biggest banks and brokers. The idea was to trade futures contracts based not on soybeans or pork bellies, but on the world's most universal commodity: money.

Up and down Wall Street, Melamed and other executives of the Chicago Mercantile Exchange peddled the plan with little success. "They laughed, yawned and looked at us as if we were quite crazy," Melamed recalls.

Today, as they mark the 10th anniversary of the Merc's International Monetary Market division, Melamed and his exchange are having the last laugh. It is widely agreed that financial futures—covering contracts for future purchase or sale of foreign currencies and fixed income securities—have helped shift the financial center of the United States westward from New York. Together, the Merc and the Chicago Board of Trade account for 80 percent of the nation's financial futures trade.

The growth "has been amazing, more than I would ever have expected," says Donald Riefler, head of asset and liability management at venerable Morgan Guaranty Trust Co., New York. Riefler, one of those who spoke to Melamed in the early days of the International Monetary Market, now says: "If you don't watch the futures markets, you're really missing what's going on."

THE STORY OF how the Merc transformed itself into a widely known financial institution is a tale of farseeing leaders and energetic members. At the center is Melamed, 49, whose powers of persuasion are legendary in commodity trading circles.

"He's the only man I ever saw who could get up and tell exchange members that black is green and get an 85 percent vote," one admiring member of another Chicago exchange says. "That's the confidence people have in him and it's well placed."

In a membership organization like a futures exchange, the ability to be convincing is crucial. "Everybody has ideas," says Everette Harris, who retired in 1978 after 25 years as Merc president. "What's important is Leo's ability to implement ideas and carry the day with the membership. He's able to get membership backing for projects they don't even understand."

MELAMED ALSO HAS critics who contend his dominance at the Merc has drowned out other voices. Some observers, noting that the Board of Trade's Treasury bond futures contract has become the most popular futures offering, say the exchange made a strategic error by not entering the market for long-term financial instruments. (The Board of Trade is the nation's oldest and largest futures exchange.)

But "I bet many exchanges wish they had a Leo to become a driving force and tap the latent energies on the floor," says John Bliss, senior vice president of the New York Futures Exchange.

Melamed's efforts have extended beyond the walls of the Merc to encompass the development of an industry self-regulatory body, the National Futures Association. He has also led the industry's lobbying drive in Washington, powered by the well-stocked coffers of the Merc's political action committee.

ON A RECENT morning the wiry, chain-smoking Melamed paced his office, lecturing a reporter. Occasionally he interrupted himself to glance at a computer screen, pick up a telephone and call an order down to the trading floor to buy futures contracts on Treasury bills or Japanese yen.

One wall of the office is filled with photographs of Melamed with politicians of both parties, including President Reagan, House Majority Leader Thomas P. "Tip" O'Neill, Daniel Rostenkowski (D., Ill.), chairman of the House Ways and Means Committee, and William Wampler (R., Va.) ranking minority member of the House Agriculture Committee.

A skillful politician himself, Melamed is wary of receiving too much credit for the Merc's growth. "No initiative can be the result of one person or even a few people," he says. Still, he regards the International Monetary Market as his child. "Can you deny that a mother gave birth to a child? No," he says.

WHEN MELAMED JOINED the exchange in the early 1950s as a $25-a-week floor runner for Merrill Lynch, Pierce, Fenner & Smith Inc., the principal commodities traded were eggs and onions. Melamed, whose family fled Poland in 1939, took the job to help support himself during law school.

By the early 1960s, when Melamed decided to stop practicing law and devote himself full time to futures trading, the volume and reputation of the old butter-and-egg market were foundering. Plagued by scandals, onion trading was banned by the government. Egg markets were painfully slow, and pork belly futures, launched in 1961, hadn't taken off yet.

The Merc accounted for less than 4 percent of total futures volume in the United States, compared with about 30 percent today. Membership prices sank to a low of $3,000; today, they sell for about $270,000.

THE EXCHANGE began remaking its image in 1964 with the introduction of a revolutionary concept: trading in live cattle contracts. As Harris, a prominent crusader for the contract, notes, the idea was regarded as radical because it was widely believed that a commodity had to be storable to be the basis of a futures contract.

At the same time, a new, younger group of directors, known at the time as the "young Turks," took control of the exchange board. "A lot of people who weren't in the butter and egg crowd were clamoring to have a voice," says Stephen Greenberg, who was named chairman in 1964.

Melamed, elected to the board two years later and named chairman in 1969, was instrumental in updating the exchange's rulebook and creating a powerful busi-

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ness conduct committee, designed to curb the trading abuses by members that had given the Merc a bad name.

He rose quickly to exchange leadership partly because, as a lawyer, "I could verbalize," he says.

IN THE LATE 1960s and early 1970s, the exchange was looking for new products. "We were very conscious of the fact that we were about to be driven to oblivion (in the early 1960s) because we were a one-commodity exchange—eggs. The lesson I learned is that an exchange to be viable has to diversify. So searching around was what we were doing."

Meanwhile, the Merc had hired a young pork belly specialist from the University of Wisconsin to be the first professional economist at a futures exchange. Mark Powers, who had encountered the idea of trading futures based on money instruments in his college textbooks, decided "just out of the blue" to call Milton Friedman and ask for the noted economist's ideas on the subject.

Melamed and other exchange officials, convinced that the breakdown in the world currency system would come quickly, set Powers to the task of developing contracts on currency futures. Friedman was hired as a consultant to write a paper on "The Feasibility of Currency Markets."

Friedman "was the key to get to these people," Melamed says. "Our credentials were zilch."

"The biggest decision was not merely attempting (to use) foreign currency as a futures vehicle but seeing it as a broader thing, an activity with larger potential," he says. "No one gave us a ghost of a chance. . . . I knew the sky was the limit."

IN FACT, ANOTHER exchange, the now-defunct New York Produce Exchange, attempted unsuccessfully to launch foreign currencies in 1971. The Merc decided to create a separate corporation with a new name—the International Monetary Market—that was free of the flavor of pork bellies.

In December, 1971, the fixed-rate currency system collapsed, clearing the way for speculation on exchange rates. The International Monetary Market opened on May 16, 1972, with Melamed as its chairman.

IT TOOK THREE years, but by 1975 activity was brisk in most of the new market's five currency futures contracts. That year the Board of Trade entered the field with futures on Government National Mortgage Association securities. In addition to Treasury bills and bonds, the current list includes Treasury notes, certificates of deposit and Eurodollars.

The International Monetary Market, which also offers gold, accounted for 60 percent of total Merc volume last year of 24.5 million contracts.

Melamed's influence is demonstrated by his role in the merging of the monetary market back into the exchange in 1976. After stepping down as Merc chairman in 1972, he assumed the position again four years later to oversee the merger. "It had turned into a them or us situation" between the Merc and monetary market, he says. Many Merc members were selling their monetary market seats, thus separating the interests of monetary market and Merc traders.

Melamed says he had a private discussion with every member, and the merger motion was approved by 75 percent of voting.

BY APPEALING TO members' patriotic instincts, Melamed has made the exchange the industry leader in successfully launching new contracts and in collecting contributions for its political action committee.

Melamed, who has chaired the political action committee since it was established, "is a very effective lobbyist," a Washington source says.

"We haven't gotten them to vote our way for sure every time, but that hasn't been our purpose," Melamed says. He cites as an example the loss of the tax-straddle loophole in the 1981 tax bill. "This allows us to tell our story."

SINCE 1978, Melamed's title at the exchange has been special counsel. However, he still devotes about 75 percent of his time to exchange business. (Melamed, who is known to be a very successful trader, won't comment on his personal wealth.) It is widely believed that "nobody gets very high up on the board of directors if they're not smiled on by Leo," one member says.