

PROFILES

FUTURES MAGAZINE
SPECIAL ISSUE



It was a passionate commitment to an idea that consumed me entirely. . . . Nothing else mattered during those formative years of the IMM but the idea?

LEO MELAMED

Father of financial futures
builds exchange and industry

Someone tells a story about the time Leo Melamed and a contingent from the Chicago Mercantile Exchange (CME) were peddling the idea of currency futures in Europe in the early 1970s. The British Chancellor of the Exchequer asked Melamed what his office could possibly do for the CME.

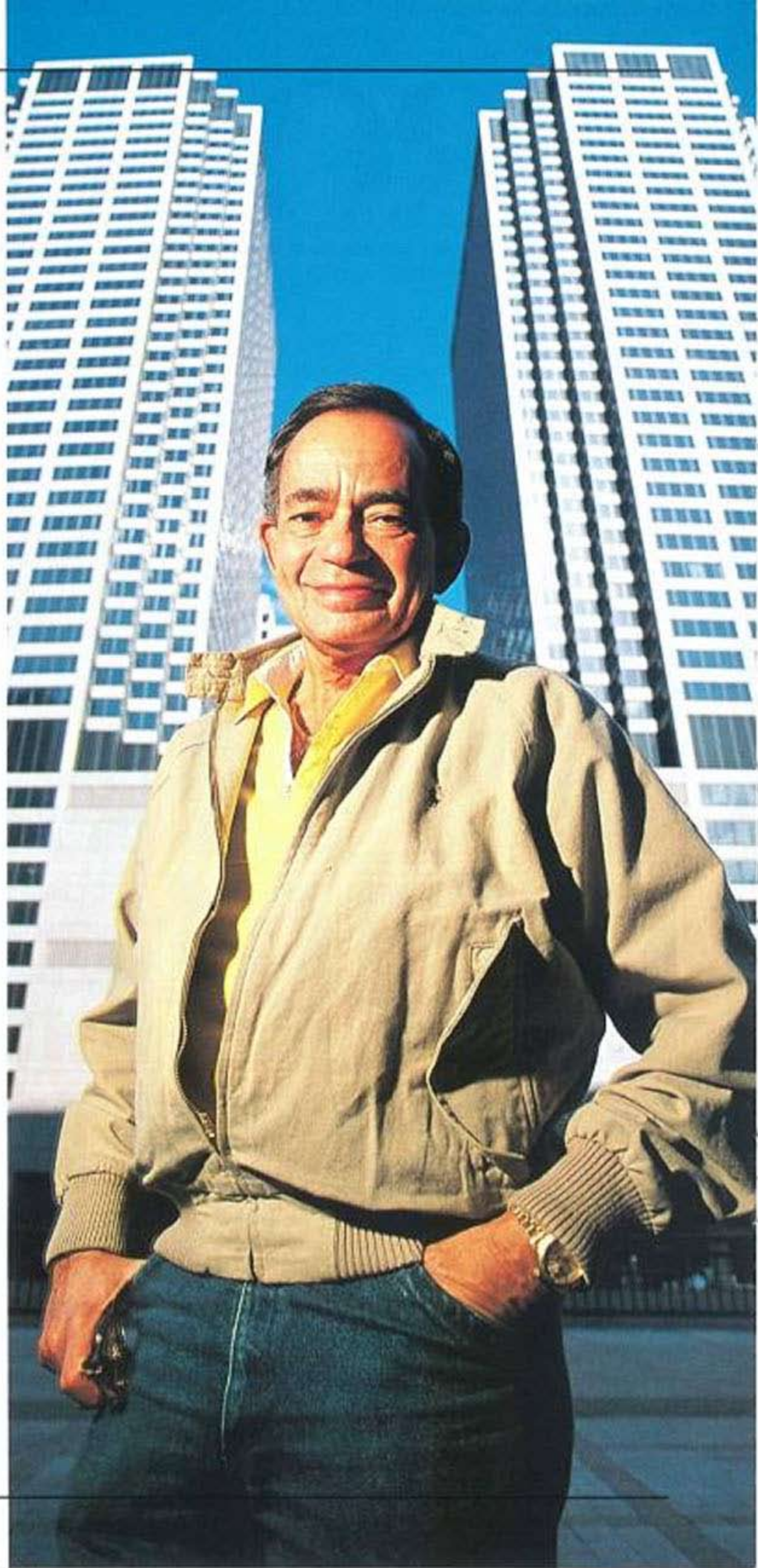
"Well, you could devalue the pound," Melamed said, half joking.

Indeed, days later Britain did devalue the pound. Although Melamed's request and Britain's action probably were a coincidence, it's almost typical of how Melamed's influence can alter a course of events.

Melamed has come a long way from his roots in Bialystock, Poland, in 1932. Commonly referred to as the "father of financial futures," Melamed is often credited not only with turning the CME, formerly an egg and butter exchange, into the innovative financial futures haven it is today but also with being the driving force behind many innovations in the futures industry over the last two decades.

Twenty years after joining the CME's board, Melamed sits at the head of the CME executive commit-

continued



continued

tee. He also is chairman of the National Futures Association (NFA), which he helped develop.

As a key industry representative, Melamed was the larger-than-life spokesman who stood up to the New York Stock Exchange and other critics of the futures industry after Oct. 19. He has spent hours testifying in front of congressional panels, met with most of the commissions that studied the crash and detailed the week's events to dozens of reporters.

Melamed denies he has a crystal ball, but he does have a certain instinct in knowing how to deal with changes in the industry's evolution. He is a doer, thinker, pusher and, he admits, sometimes a man obsessed.

"(I'm a) laborious perfectionist by nature and almost obsessive," he says. "There will be many who will tell you that. That's not a wonderful characteristic because it places great stress and demand on anyone working with me as well as on me. I don't expect anything more of a person working with me than I do of myself."

Melamed was introduced to the CME floor as a Merrill Lynch runner while working his way through John Marshall Law School. In 1954, he became an exchange member, although he still had a full-time law practice. By 1967, he had become a member of the board of governors, and the CME hasn't been the same since.

These days, Melamed spends his time trading and running the CME from his firm, Dellsher Investment Co. Inc., located on the 19th floor of the double-towered CME building, which opened in 1983.

Among his many accomplishments, Melamed considers the development of currency futures — the start of the financial futures era — the greatest.

"As a runner and clerk on the floor of the exchange, (I had) seen the near demise of the Chicago Mercantile Exchange in a very visible and frightening fashion because the exchange was dependent on one product line: eggs," he says. "I learned very quickly that an institution like an exchange is writing its own limit and perhaps death warrant if it depends on one product line."

By 1969, when Melamed became CME chairman, the livestock contracts introduced earlier in the decade were the major product line traded at the CME.

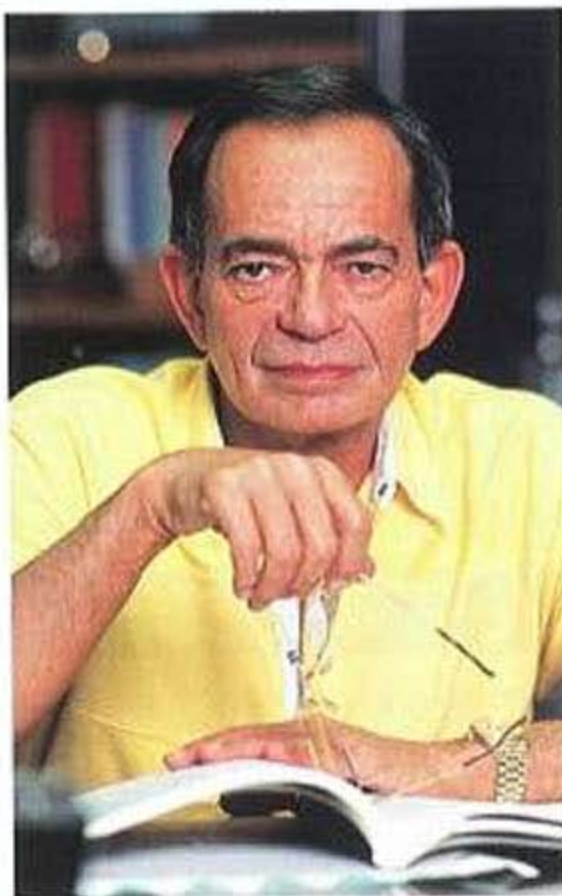
"I wanted to lead the exchange out

of that trap, so (my) No. 1 motivation (for currencies was) looking for a product line that was substantially different than the meats," Melamed explains.

At that time, Melamed sensed "deep financial rumblings going on in the world. They were going to erupt, and it was going to be a period of great upheaval, financially speaking."

If the CME were to capitalize on this, he decided it would have to develop contracts in the financial arena. Furthermore, he was frustrated by not being able to trade currencies as an individual.

"I think Milton Friedman would be the key person who influenced me because if I didn't think that he believed



in what I was doing, I would not have had the courage to proceed with the idea," Melamed says, pacing the floor of his spacious office, where the walls are blanketed with photos and plaques honoring Melamed. Family photos, alongside a bull and bear sculpture, sit behind him in a wooden bookcase.

Although Melamed was introduced to Friedman's free-market philosophy while monitoring some of the economist's University of Chicago classes, he never met the man until 1971. He and then-CME President Everett B. Harris went to New York to ask Friedman to write a position paper on whether a futures market in foreign exchange was a good idea and what role it could play in the financial markets. They also knew that Friedman "generally, philosophically em-

braced the idea," Melamed says.

So Melamed, armed with the idea and Friedman's credentials, went to government officials, "not because we needed their approval — legally we didn't" — but as a courtesy.

"I had a great deal of faith in the idea, so I didn't think (they would prevent it)," he recalls. "Maybe I was naive, but it turned out I was right. Every one of them, the first reaction was, 'It's a pie in the sky.' But is it a good idea? 'Probably.' Is anything really wrong with it? 'No.' Could we philosophically support it? 'Yes.'"

But they saw as a major hurdle the reaction of banks to a bunch of pork belly traders entering the foreign exchange markets. Unfazed, Melamed kept building his dream.

"I had no doubt the idea was great," he says, and his currency futures dream became a reality when trading began on May 16, 1972.

Then, after starting a gold futures contract on the last day of 1974, Melamed and the CME started looking at the interest rate market, which seemed to be the hot new ticket.

"In my first annual report to members, I wrote that, if the foreign exchange markets work, then the sky was the limit... because I recognized... in finance we had so much to choose from. I was like a kid in a candy store," Melamed says.

The CME launched Treasury bill futures, then started looking outward. "The trend of the world was going global. That led us to believe Eurodollars were going to be the bellwether of short-term interest rates," Melamed says.

The problem, though, was how to deliver something as nebulous as a Eurodollar interest rate that is not a single instrument. Thus came the development of cash settlement. The Eurodollar futures contract was the first to use that method of delivery.

"Once cash settlement became viable and acceptable, then truly what I said to our members became a reality: The sky was now the limit," Melamed says. "Because once you could create indexes to represent a product line rather than delivering the actual product itself, you could create indexes for many things."

The CME next looked for a stock market benchmark. Although the Dow Jones Industrial Average was a popular gauge, the CME wanted a commercial vehicle of trade so decided to go with the Standard & Poor's (S&P) 500 Index. The S&P 500 was

LEO MELAMED

continued

the third stock index futures contract introduced but quickly became the most successful. Volume continued to grow rapidly — until Oct. 19, 1987.

In retrospect, Melamed says his greatest challenge was the initial start of the International Monetary Market (IMM) and financial futures but adds, "Oct. 19 was a tough day," in jocular tones.

"The first three years of the IMM were difficult. I was hardly in one place at one time on any given week," he says. "I was still trying to trade... but the idea became my life. I had to do everything in my power to make the idea successful. And the first three years was when I had to convince the world that the idea was a good one — the world did not recognize the Chicago Mercantile Exchange as an important entity.

"(Developing financial futures) was a passionate commitment to an idea that consumed me entirely and would not let me live without working for its success. Nothing else mattered in my life during those formative years of the IMM but the idea."

Melamed thinks his intense drive came from his parents — teachers who escaped Poland during the German occupation by crossing the Soviet Union to get to the United States.

"I wasn't following their footsteps at all, but I was imbued with their way of total commitment to their idea and goal," Melamed says.

At 10 years of age, Melamed heard a philosopher talk about immortality.

"He said you do that by tying your life to an ideal, and it didn't matter what the ideal was, so long as it had a social value. I accepted that as a truism and a way of life," he says.

Another Melamed ideal was formed in the 1980s when he and several other industry leaders decided a self-regulatory organization for non-member futures commission merchants was needed.

"I am a great believer that, in numbers, one finds a lot more protection than if one is alone facing the wolves in either the world or government," he says.

Furthermore, Melamed realized that the industry was "on the threshold of big times," meaning government regulation was inevitable. So he thought that the industry should take its own lead.

He believes the NFA, of which he has been chairman since it started in 1982, has performed "even better than what anyone could have anticipated" but adds, "I don't want to be chairman forever."

However, Melamed admits he was not always an advocate for one major growth area, options on futures, because he believed they would pare business from futures. But when the competition started to edge in on the industry and the CME in the early 1980s, Melamed went to bat.



"We were in a pilot program for so long by the (Commodity Futures Trading Commission) that it was a joke," he says. "They held back the mechanism and the tool for the futures industry to a point that I personally went to Washington and finally beat down the door on that issue. It was held up unnecessarily. If there was a reason not to have (options), no one should have (them)."

The next light-year jump Melamed prodded was the development of the Post Market Trade system (PMT), announced last September and planned for 1989. This is a major step that will combine

24-hour trading, computers and open outcry by opening a computerized exchange on CME products when the CME is closed.

"I placed on the agenda about two years ago the issue that there was a growing competition, an erosion of our markets as a result of currency (exchange for physicals) that occurs after our market closes," Melamed recalls. "The idea was to create an after-hours trading system (and) not one that is geared to the pit."

Never one to put his head in the sand, Melamed pushed for a compromise of technology and pit trading, and the idea gained an overwhelming approval in a membership vote. He believes the move to computerized trading was going to happen "whether we do or don't participate."

Although Melamed seems to enjoy a good and fair fight, his competitive nature has not pulled him into the political spotlight. He says he was "never ready to give up my independence" to join the public arena.

That independence includes trading. During trading hours, it's typical for him to hold a conversation with one eye on a monitor and one ear on a phone. When away from a monitor, he carries a portable screen with a cordless phone. Yet, he still contends he doesn't have enough time to trade.

"I trade but don't have enough time to concentrate, thus my positions are at the mercy of not enough attention. That's very dangerous, and I lose a lot of time," he explains. "Sometimes I feel like sending (the industry) a bill."

Recently, Melamed broke away from representing the industry and trading long enough to write a science fiction novel, *The Tenth Planet*. He plans a sequel as well as an espionage book in the future.

"I think I can lose myself best in writing," he says. "If relaxation, by definition, is to get away from what you do normally, then writing is my safest and surest avenue for achieving that. I also like to play in the sun."

Ginger Szala

Reprinted from **Futures** Profiles 1988 Issue

The magazine of commodities & options

Copyright 1988 Oster Communication Inc. 219 Parkade, Cedar Falls, Iowa 50613