

# BUSINESS

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## Melamed still nudging Merc into the faster lane

The Chicago Mercantile Exchange has risen from a clubby commodities market to the top of electronic financial futures trading

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Leo Melamed, who helped transform the Chicago Mercantile Exchange from a clubby trading floor where contracts on eggs and onions were traded face-to-face into the world's dominant electronic market for financial futures, is still at it at 74.

This spring Melamed helped forge the exchange's big moves into worldwide energy and over-the-counter foreign currency trading while also expanding its

footprint in Asia. Besides financial futures and electronic trading, in the past Melamed also had pushed to have trades settled in cash rather than by the physical delivery of assets, all innovations that led to its booming growth.

And he envisions "growth beyond anything we've had so far," he said.

Melamed chairs the steering committee of the Merc, whose market value has soared 15-fold to \$15 billion in the three years that its shares have been publicly traded. It was the first big U.S.

exchange to go public, in December 2002.

"He's a visionary who can implement ideas and lobby effectively for the CME in the U.S., Europe and Asia," said Nicolas Bertrand, 34, director of derivatives for the Borsa Italiana in Milan.

Melamed's leadership at the Merc spans nearly 40 years during which time he has served twice as its chairman and held other positions such as chairman of its early financial futures market and of the exchange's executive committee.

Since 2004 he has been a \$300,000-a-year consultant. His goal is to expand the exchange's electronic trading platform in order to raise revenue and to build alliances with other mar-

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Tribune photo by Bonnie Trotter

Leo Melamed has served twice as chairman of the Merc during his 40 years as an influential member of the exchange.

# MELAMED: A key move into energy industry

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kets and exchanges as the industry rapidly consolidates.

For example, Melamed was a key player in last month's deal that propelled the Merc to its long-awaited entry into the lucrative energy industry. The New York Mercantile Exchange agreed that for the next 10 years all electronic trading of its benchmark energy contracts would be done only on the Merc's Globex trading system. The Chicago Merc, for its part, will collect transaction fees on every trade and have its technology powering the movement of petroleum, fuel and natural gas futures contracts around the world.

While the Merc's chief executive, Craig Donohue, and its chairman, Terrence A. Duffy, led the negotiations, Melamed helped bring the parties together last winter.

"Leo was one of the leaders from the very beginning," said Richard Schaeffer, the Nymex chairman.

Moreover, Melamed lobbied for the deal despite the fact that the Merc's leadership was not in lock step early on, said Z. Lou Guttman, former chairman of the New York Mercantile Exchange, who joined Melamed in those early talks. Duffy and Donohue declined to comment on Guttman's observation. "Half the CME was against the deal. Leo was for it," Guttman said. "At first, they [the Merc] played hardball and tried to make a deal with ICE [the all-electronic energy trading Intercontinental Exchange based in Atlanta]. That didn't work."

In March, at a futures industry meeting in Boca Raton, Fla., the two mercantile exchanges started talking again, with Melamed greasing wheels in the back channels.

The deal, Melamed said, "gets us into energy and makes Globex the energy distribution platform worldwide."

For Nymex, which still does most trading in face-to-face auction, the prize was the Merc's electronic trading technology. On June 11, when Nymex launches on Globex, it hopes to stanch substantial losses of its market share to ICE.

Could this lead to the two mercantile exchanges eventually merging?

"It's a strategic investment that doesn't involve CME putting out a lot of money but aims to connect our markets with their markets," said Melamed, his eyes twinkling. "It's a way to begin a process."

## Well-known in China

While the Nymex deal was being finalized, Melamed and other Merc officials were wrapping up two years of negotiations for an arm of the Bank of China to become a Merc clearing member trading foreign currencies and interest rate futures on Globex. The Merc will earn clearing and transaction fees.

"The thorniest issue for the Chinese government was to accept a private sector institution as a partner," said Melamed.

A year ago he realized that his negotiations might succeed. He met with Chinese government officials at a retreat in suburban Beijing at a site lined with lakes, woods and walkways.

"They hosted me at a lunch in the main dining room of this gorgeous resort," Melamed recalled. "As the translator explained the deal to the officials their body language told me that they accepted it in principle."

Rigger deals in Asia and India will follow, he predicted.

"This deal gives us tremendous branding and goodwill," Melamed said. "We're making connections, electronic and otherwise, for an unimaginable amount of business later."

Melamed was an appropriate emissary, said Eugene Zheng, a Chinese-born technologist who is an adviser to the Chicago Board Options Exchange.

"Leo is well known in Chinese financial circles," Zheng said. "They want to develop financial futures and he's a pioneer."

Melamed knows firsthand that some transactions take a long time to consummate. Pushing the Merc into computerized trading, he said, has by far been the most "arduous" of all the deals he has worked on.

"It took 12 years," Melamed recalled of the gradual introduction of the electronic platform co-developed with Reuters Group PLC, which began operating in the mid-1990's. He had to overcome resistance from traders who saw it as a possible threat to the open outcry trading in which they thrived.

Back then the Merc was a non-profit run by its 3,000 members, who voted on proposals. Poll-ticking among factions was fierce.

To push through the electronic trading concept, Melamed, then the exchange's chairman, worked 18-hour days cajoling members at meetings, dinners and hallway encounters. He overcame objections by introducing computerized trading gradually, a few hours at a time alongside open outcry for some products. When he introduced financial futures he dispatched supporters to "remind" the faithful of promises to trade in the new products.

Earlier this month the Merc's association with Reuters bore new fruit: FXMarketSpace, a 50/50 joint venture to trade foreign currency in the huge \$2 trillion-a-day cash market.

The Merc's Duffy, Donohue and Melamed negotiated this deal and will sit on the joint venture's board.

Melamed is on the Merc's leadership team and the new board, said Duffy, "because we want the expertise we need at our fingertips." Melamed also leads a consultancy, Melamed & Associates Inc.

Trading in the cash currency market, Melamed said, "is a dream come true."

In the early 1970s, when the Merc was struggling to find new products, governments stopped establishing official exchange rates for currency and let them be set by the market. Anticipating more movements in currency values, Melamed used foreign currencies as the basis for the Merc's first futures contracts based on monetary instruments rather than agricultural commodities. Over time, this shifted Merc business so that financial futures now comprise 98 percent of its trading volume and bring in 74 percent of its revenue.

## Childhood training

Melamed's affinity for foreign currency dates to his childhood.

In 1939, when the Nazis invaded his homeland, Poland, his Jewish parents—both academics—fled with him to Lithuania, Russia, Japan and ultimately the U.S.

While on the run Leo's father taught him about currency fluctuations, and about official and black markets in which money could be bought and sold.

"He taught me that the official government rate was often political," Melamed said. "The real rate was what you could buy with it on the streets."

In 1941 the family settled in Humboldt Park. And no one had to teach the young immigrant to take charge, said lifelong friend Phillip Siegel, 72, a member of the state lottery board.

"He was an organizer, even then," Siegel said. "He was the one who said, 'Let's play ball.'"

In 1965 Melamed earned a law

degree from John Marshall Law School after attending the University of Illinois for two years. He paid his way by working as a runner at the Merc, where trades were hand-toted on a big board and traders communicated using rapid-fire hand signals.

"It was instant love," said Melamed who practiced law for eight years while immersing himself in the exchange. "The tumult, shouting, rushing. It was like walking onto the set of a Hollywood sci-fi thriller."

By 1967 Melamed had started a trading firm, Dellscher Investment Co., and two years later had enough supporters on the floor to get elected Merc chairman. The pay: \$25,000 a year.

As a trader he went broke twice and in 1991 sold his firm.

"I'm a better manager than trader," Melamed confessed.

From the 1970s through the 1990s Melamed helped revolutionize the exchange and the industry by promoting electronic trading, financial futures and cash settlement. "The most important market development in the past 50 years," said Michael Metz, 72, chief strategist for Oppenheimer & Co. "Leo is a pioneer with great foresight."

Melamed overcame many ob-

jections to lobby for these innovations within the exchange, in Washington, D.C., and on Wall Street.

"When I tried to explain the potential of futures on U.S. Treasury bills, Billy Salomon of Salomon Bros. thought I was wild and had me escorted out of his office," he remembered. "He didn't think anything important in finance could happen in Chicago."

Nymex's Guttman said Melamed often succeeds in lobbying and negotiating because "he puts himself in the position of the other guy at the table and knows how far to push."

Yet Melamed has not negotiated all that well for himself.

Since 1969, posts in which he served the exchange have included chairman, secretary and special counsel. His pay was a "token honorarium," he said, ranging from about \$25,000 to \$300,000, briefly reaching \$300,000 a year. Now, he earns \$300,000 plus expenses as a special consultant, he said.

In contrast, the last Merc chief executive, who served for four years and exited in 2004, received a package valued at about \$120 million. Craig Donohue, who in 1988 joined the ex-

change as chief administrator and in 2004 became chief executive, last year was paid about \$2.2 million in salary and bonus and has stock options valued at about \$45 million.

"Leo has helped so many people make fortunes, but he hasn't been rewarded like some employees who haven't done nearly so much for the exchange," said Barry Lind, a former Merc director and longtime Melamed ally. "If I were Leo I'd be very upset," added Lind, 67, the retired founder of trading firm Lind Waldock & Co.

During the Merc's 2002 initial public offering Melamed received 13,289 shares valued at \$465,115 for the seat he owned, "like any other member," he said. He has sold all but about 5,000 shares now valued at about \$2.2 million. He declined to explain why, as a key leader, his compensation was not near that of the hired managers.

He did say, however, "My personal motivation was to build the institution."

Guttman, who was chairman of the New York Mercantile Exchange when most exchanges were non-profits, said Melamed's pay reflects that era.

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