OUR 40TH ANNIVERSARY ISSUE

Institutional Investor

MAY 2007 WWW.INSTITUTIONALINVESTOR.COM

40 YEARS OF POWER & INFLUENCE

FEATURING

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Prince Alwaleed bin Talal
Michael Bloomberg
John Bogle
Emilio Botín
Warren Buffett
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Edward Johnson III
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Myron Scholes
Michael Milken
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Hans Tietmeyer
Paul Volcker
Sanford Weill
Allen Wheat
John Whitehead
James Wolfensohn
Muhammad Yunus

Can you name a couple of crucial points in your plan?
The headline figure was simple, but the strategy for making it happen was in the details. There were loopholes in the rules for measuring bank assets. I closed those loopholes and wrote the changes into the FSA bank inspection manual. I also set up a rule requiring banks to issue business improvement plans if they failed to come within 30 percent of profit targets.

These are the kinds of things that usually only bureaucrats talk about.
Exactly. What interested me was that the media and the politicians never discussed these kinds of details.

> "WHEN WE WERE DRAFTING THE PLAN, PRIME MINISTER KOIZUMI PHONED ME EVERY DAY. HE ALWAYS SAID THE SAME THING, 'MR. TAKENAKA, DON'T CHANGE YOUR OPINION.'"

So where are we now?
NPLs today are 1.9 percent of bank loans. We solved the problem.

On to the post office. What was the most difficult moment in the privatization process, and how did you get past it?
We had lots of difficulties. The ruling Liberal Democratic Party and opposition Democratic Party were both against it. The Democrats rely on labor union support, and the post office has the strongest union in Japan. So only the PM and I were in favor of privatization.

How did you get started?
I went to the PM and asked him to manage the process directly, not through the Ministry of Communications. This meant two things. First, we decided basic policy at the Council on Fiscal and Economic Policy, which came under my ministry. Then we had to draft the legislation. With privatizations this had always been done by the relevant ministry, but we set up a special body to write the law, the Office of Postal Privatization. Koizumi had to nominate someone to run this office. He nominated me.

What are the main benefits of privatizing the post office?
I like to use the term "reform dividend." Just look at the post office headquarters in front of Tokyo Station. It covers a huge site, but it's an old five-story building surrounded by modern skyscrapers. The post office can't develop it because, as a state institution, it can do only three things: provide mailing services, some banking services and insurance.

Once privatization takes effect it will be able to move into urban development, do real estate business, retailing and so forth. This doesn't apply only to Tokyo. The post office occupies some of the most valuable land in front of almost every major railway station in Japan — Osaka, Nagoya and so on.

Now apply the same idea to money. Japan has ¥1,500 trillion [$12.7 trillion] worth of household savings. Twenty percent of that goes to the government in the form of postal deposits, but the way the government can use the money is quite limited because it has to be invested in safe assets. Once Japan Post is privatized, it can lend money to the private sector so we can see much better results.

Why did you leave politics when Koizumi's premiership ended in 2006, even resigning a seat in the upper house of Parliament?
I stepped down because I never wanted to be a professional politician. My field is research. But I thought Koizumi was a kind of miracle prime minister, so when he asked me to join the government, I made up my mind to help.

Now that you are out of the firing line, what are your ambitions?
I'd rather talk about my hope. In this country we do not have a group of people whom I would call policy watchers: For example, in the U.S. someone who has worked in the White House may now be working in the Brookings Institution. I want to be Japan's first policy watcher, and I'm running a course to train young policy watchers. We need this kind of infrastructure to make the country work. *— Interviewed by Charles Smith*

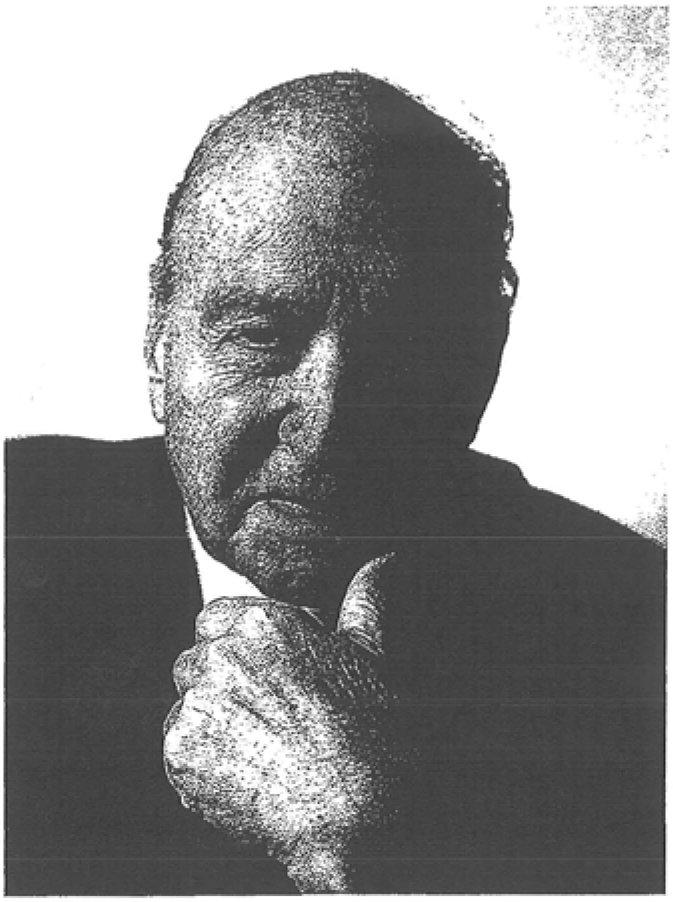
EUGENE ROTBERG

The Troubles I See

The former treasurer of the World Bank wonders what will happen to a country where all the smartest people go into hedge funds and his tax rate is lower than his daughter's.

The greatest change in the markets over the past 40 years has been globalization. It was not many years ago that if you were British, you couldn't take more than the equivalent of $200 out of your country. You couldn't borrow sterling or French francs or guilders unless you were a resident of those countries. The growth of the Euromarkets has permitted borrowers to tap into the world's savings, to tap into people's preferences for currencies or short-term versus long-term bonds, for example. That was a massive change. Whether or not that financial opening is a cause or effect of trade globalization is a meaningless question to me.

When Robert McNamara became president of the World Bank in 1968, he decided to massively increase lending to poor countries. The bank had accumulated only $3.5 billion in debt over the previous 22 years; McNamara wanted to lend a billion dollars a year, which meant he had to borrow a billion dollars a year. I was working at the Securities and Exchange Commission, and he hired me. At that time, the U.S. believed it had a capital shortage, and



•EUGENE ROTBERG

As treasurer of the World Bank for almost two decades, Eugene Rotberg built it into the biggest and most sophisticated user of the international capital markets, employing its AAA rating to pioneer many now-common financing techniques. These included one of the first currency swaps, a 1981 transaction in which the Bank exchanged its liabilities on a $290 million bond issue for deutsche mark and Swiss franc liabilities of IBM Corp. The onetime U.S. Securities and Exchange Commission official helped raise more than $100 billion before departing the bank in 1987. Now 77, he serves on the boards of several public and private sector bodies, including Development Alternatives, a Washington-based consulting firm for developing countries.

Photographed by David Deal on April 2, 2007, in Washington, D.C.

the Bank was not permitted to borrow in the U.S. Fortuitously, the Federal Republic of Germany and Japan were huge exporters and had begun to accumulate very large reserves. They were both afraid of the inflationary effect of their money supply, and they wanted a borrower, literally, to take that money out of the country. The World Bank was an appropriate vehicle. We simply asked investors and our underwriters, "What do institutions want on the asset side of their balance sheet to meet their obligations?" We shaped the instruments to fit their needs.

Most of the things that are happening now were fairly well predicted as far back as the '80s. The greatest difference is the enormous amount of credit swaps. When the World Bank did the first currency swap with IBM, we wanted to tell our board that there was not going to be any increased risk. So we went to Aetna Insurance, and they wrote us an insurance policy. It took two months to do the deal.

I don't think you can make money now on intellectual property, on having an idea. The idea's not patentable — everybody leaves their firms and there is such a broad base of techniques available that there are no great secrets. I am rather cynical about trading skills. Markets are unpredictable, and if people knew the direction of the market, they wouldn't be working. The greater wisdom comes from understanding risk and not having a system that rewards only for very high performance. If you pay a trader $10 million or $20 million, or more, for being right, he's simply going to take a great deal of risk. That's endemic today. I do not believe there is a correlation between compensation and performance in predicting interest rates or share prices in public markets.

The ones that fall short today are the regulatory agencies, whether it's the SEC or the Federal Deposit Insurance Corp. or the Federal Reserve Board. They do not know, day to day or strategically, exactly what is happening in these very complex derivatives transactions. Their knowledge is very thin and stale. As a result, they simply say to banks: "You've got to be careful with this. Watch it." They don't have the expertise. And they are concerned that if they tinker with or constrain the derivatives markets, they will affect the capacity of the U.S. to finance itself.

In coming years we're going to be talking about the political strength of China because of its unique position of being able to produce extremely sophisticated, educated people — and at the same time people who work for a dollar an hour. There are very few countries that have both ends of that spectrum, let alone with China's numbers.

The U.S. has two or three choices to avoid being eclipsed. It could launch a massive program to encourage the Europeans to bring their factories here because we have a fabulous legal system, great property rights and we integrate people very well. The U.S. could also create programs to make itself the center of intellectual development in areas like energy, alternative commodities and information technology. The private sector can't do it. Everything's too short term, and the smartest people go into hedge funds. It's a little hard for me to figure out how productive that is for the country. It's like putting people in Las Vegas. I'm not so sure that their enormous expertise can't be used for more productive kinds of things, but there's no incentive. And the reason there's no incentive is very simple: My tax rate is lower than my daughter's because this country has decided to lower aggressively the amount that you pay on dividends and interest and on capital gains. We are creating disincentives to go into areas that will have longer-lasting and more positive results for the country. We have a tax structure that I suspect is inadequate, to say the least.

— Interviewed by Tom Buerkle

“HAVING THE SMARTEST PEOPLE IN HEDGE FUNDS IS LIKE PUTTING PEOPLE IN LAS VEGAS. I'M SURE THEIR ENORMOUS EXPERTISE COULD BE USED FOR MORE PRODUCTIVE THINGS.”