Trading places

A PROFILE OF EUGENE ROTBERG: MOVING FROM THE WORLD STAGE TO AN INVESTMENT HOUSE

By Sarah Priestley

Eugene Rotberg: "The intellectual skills are the same."

How does Eugene Rotberg square up what has to be the narrower aim of helping to boost the bottom line of an investment bank with the near-altruistic and larger concerns of his former position as vice president and treasurer of that august institution the World Bank?

"The role is different, the end-product is different – but the processes by which you get there are essentially the same," says the man whose crossing over to the private sector after 20 years with the World Bank has been something of an event in banking circles. He wisely eschews the bland value judgements that most would expect from him.

Rotberg's going to Merrill Lynch as its executive vice president – the latest in a string of defections by well-known figures to Wall Street – represents a coup for the investment bank. And it has come at a critical time for Merrill. Following an unauthorised trading loss of $275 million in the mortgage-backed bond market, the reputation of the securities house has been badly dented.

Rotberg will be responsible initially for risk assessment and monitoring the firm's securities trading operations. His first task will be to establish procedures of monitoring risks across Merrill's products range – equity, debt, synthetics, options and futures – and to advise on what action to take if the risk is excessive.

His new role will also encompass considering how much to hedge. With systems in place to evaluate and cope with risk, trading losses of the kind experienced in May are unlikely to be repeated – or so Merrill expects.

This should pose few problems for Rotberg, whose public service career spans 30 years in all. "The intellectual skills are the same," he says. "I have been trying to cope with the markets for the last 20 years.

"Essentially, the problems confronted are the same as those facing traders in an investment bank. Managing a portfolio of debt or investments involves the same risk analysis at the World Bank as at Merrill Lynch. The core business and uncertainties are the same."

Merrill wants to be seen to be cleaning up its image in the capital markets following the trading loss, which it publicly confirmed as soon as it happened. The new risk evaluation process will be coordinated to cover positions in London, New York and Tokyo.

Rotberg is, however, more concerned with the reality of his task at Merrill, rather than any redressing of the firm's public image.

Rotberg's value to Merrill lies in his expertise in the domestic markets and Euromarkets, particularly in the field of new financing where he is established as a pioneer of innovative techniques. The World Bank transacted the first currency swap in 1982, although Rotberg modestly declines to lay claim to the title of "inventor" of the market.

The World Bank has borrowed a total of $100 billion in 20 different currencies. One indication of the accelerating growth in its financing activity is that it now borrows in six months the same amount of funds that it raised between its inception in 1946-47 and the time Rotberg joined it about 20 years ago.

This knowledge of the securities markets, gleaned as treasurer of the largest borrower in the world, will be invaluable to Rotberg. Moreover, the World Bank's net long position of $20 billion in surplus liquidity has given its CFO a thorough grounding on the investment side as well. Rotberg's accumulated wisdom will be important in evaluating Merrill's trading risk.

"As a former client, I have been on the receiving end of investment banking services for many years. I know what I respond to, and the advice I find constructive," he says. "That may help me to improve the quality of service, although every client is different."

Rotberg developed a reputation at the World Bank for finding new ways to solve the debt crisis, such as swaps, rate caps or securitisation of loans. "Financial engineering can serve as a catalyst for transactions which would reduce the likelihood of financial or political trauma as developing countries seek new money or try to service the interest on debt," he recalls.

Rotberg insists his departure from the World Bank has nothing to do with dissatisfaction with the personnel changes instigated by president Barber Conable. "There comes a point in everybody's life when changes are called for. I chose to leave at this juncture because I have accomplished what I wanted, and am now ready for a new challenge."

Rotberg's responsibilities at the bank were threefold. First, he borrowed resources to finance development. Second, he invested the bank's liquidity. And most significant, he explained the bank to governments and the private sector so that they would be comfortable with investments made through the bank and pledge their continuing support.

One of Rotberg's greatest accomplishments both in terms of lowering borrowing costs and diverting private resources was to introduce market-based tools and processes to an institution which served the public interest. "I looked upon my role as a bridge between those who controlled wealth and those who looked to obtain resources for productive purposes to improve their standard of living. Usually that has rarely been done through markets, but rather by grant, transfer or gift," he explains. "The theory being that those who have little cannot be entrusted with money which has to be repaid. That is simply not true."

Instead, the World Bank treasurer decided to make room for using the most sophisticated tools of finance and create a financial structure which would attract private money, since the organisation would be trusted to take appropriate, not inappropriate, credit risks.

The World Bank is now able to attract money out of the private system because it can assure lenders of capital that it has subjected every lending project to the most rigorous scrutiny. That scrutiny is so well respected that the organisation enjoys the most prestigious rating in the long-term bond markets, and its paper is sought after.

"To use the tools of rational decision making for the public good – that has given me great satisfaction," Rotberg says proudly. And in the process he has built up a reputation and understanding of borrowing, swap and investing techniques that many investment bankers envy.

In contrast, private sector lending to LDCs, generally in the form of loans, utilises funds drawn from a deposit base rather than from publicly traded, long-term, fixed-rate bonds. The commercial banks' funding sources are of a different quality, according to Rotberg. Such funding is more fragile to hold but easier to attract. The World Bank, on the other hand, issues medium-term and long-term fixed-rate bonds. Its

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sources are more demanding and more conservative, and therefore the funds it raises are deployed correspondingly.

At the World Bank, the treasurer's job is to decide how much risk to take – whether to borrow in the fixed-rate or floating-rate market, whether to borrow in Swiss francs, Deutschemarks or yen, whether to borrow long term or short term, or whether to borrow directly or enter into a swap. At Merrill Lynch, Rotberg says, clients are also advised on these matters for their own borrowing purposes. Therefore the assessment of risk enters into both.

Moreover, in his capacity as chief financial officer at the World Bank, Rotberg's duties included investing the $20 billion in liquid balances which had already been borrowed but not yet redeployed to existing credit commitments. In this he had to decide how much risk to take on investments in terms of market, credit and liquidity. Merrill's trading operations have also to make similar evaluations such as whether to be long or short, how much to hedge or to leave unhedged, or what risk to take in terms of pricing a new bond issue in moving markets.

However, Rotberg does concede that one major difference between his past and future career is that in general organisations like the World Bank with a net long position of funds or any other institutional investor have the choice of whether or not to take on risk. "We could decide when to take a position. For investment banks that decision might be taken for you. You are, to some extent, in the hands of your customers, whom you service as a market-maker in securities. In that sense you may take risk involuntarily."

Rotberg adheres to four broad principles which have always driven his assessment of how to handle money and risk. These, he claims, are similar in many walks of life and are the key factors in any decision-making process. First, be aware of risk – define it. Second, be aware of what can go wrong. Third, measure opportunities which have been lost. And last, do not be paralysed by error. The last category no doubt has a particular poignancy for Merrill.

As to the relative social uses of an institution like the World Bank and a Wall Street securities house, Rotberg flatly refuses to make any cliché-ridden value judgements. "At the World Bank we have a major constituency – those who lend us money and who expect us to earn a profit. We have a number of other constituencies – the LDCs are crucial. Stockholders and managers at Merrill also expect the house to earn a profit. The end product of the two is different, but not the requirement for quality decision-making."

Last year the World Bank's profits came to $1.2 billion. Out of a total balance sheet of $100 billion, only $4 billion came from governments, underlining how commercially viable the organisation is. Earning a return on capital – for both a supranational agency and a private sector investment firm – is a prime objective.

"Alleviating poverty, lending to poor farmers in Brazil, to those who suffer at the margins of existence, yes, that's a different social utility from an investment bank," he says. "But there are a lot of constituencies in the world, and I'd be the last to put a value judgement on the utility of any activity. People should be productive and produce an honest and ethical result. There are in my mind no such things as important people or important jobs. Just do your work as best you can." ■