Axe falls in fixed income

A batch of senior bankers including big ex-Asian names have been fired over losses linked to defaulting sub-prime loans in the United States. The direct impact on Asia has been muted up until now, but there are sure to be repercussions for the region via team changes down the road, reports Richard Morrow.

The decision by United States investment bank Merrill Lynch to fire Osman Semerci, its former global head of fixed income, currencies and commodities (FICC), on October 3 marks the end of a 15-year rise for one of the bank's most promising stars, who had spent a large proportion of it in Asia.

The ethnically Turkish Semerci was regarded as one of the brightest and best traders in the world, and while heading Pacific Rim debt markets and then global markets – the latter from September 2003 to January 2005 – many credited him with transforming the trading platform into the region's best, after a few years of flat performance in the early part of the decade. His progression to head global emerging markets was a natural step, and the London-based Semerci was then promoted to head FICC in July last year.

But when an investment bank has to write off at least US$5 billion due to its exposure to troubled sub-prime mortgages and collateralised debt obligations (CDOs), it's no surprise that the man ultimately responsible for the trading exposure was axed. Dale Lattanzio, co-head of US fixed income and structured credit products, was also dismissed.

"I was surprised by Osman's [sacking] in that he was a star for them in Asia and by all rights did a supreme job," says the head of one recruitment firm in Hong Kong. "But he clearly found himself in a position where there were large amounts of losses for which he was ultimately accountable."

Other observers say a major contributing factor to Semerci's departure may have been the fact that the bank's exposure to structured credit was insufficiently hedged, leading to greater-than-expected losses. Semerci has been replaced by David Sobotka, formerly head of its global commodities business.

For industry observers, Semerci's departure is still a big surprise. "Semerci was a powerful guy and ambitious; he's tough and single-minded," says one observer familiar with the bank. "He had a tremendous sense of leadership; you knew someone was in charge and where the business was going. He wasn't warm or fuzzy though – but he could be charming when he wanted to be. Still, you didn't want to get on the wrong side of him."

The regional fallout for Merrill following Semerci's departure is uncertain. Asia's 35-year-old FICC head Jason Brand, for example, has only been in his role for a year-and-a-half and is not considered to have been close to Semerci. And under the leadership of chairman and chief executive officer Stanley O'Neal, who is tough on mistakes and tough on the perpetrators of mistakes, Merrill has become renowned for conducting senior management shake-outs every few years. However, one industry observer believes that this latest one could mean good things for the senior figures in Asia.

"Merrill Lynch's Asia-Pacific operations have done a great job in delivering revenue to the firm and a lot of that is down to Damian [Chunilal, the region's chief operating officer] and Jason," the observer notes. "I wouldn't be surprised if they left Asia due to being promoted."

Such internal movements would potentially put Sheldon Trainor, Merrill's self-confident head of Asia investment banking, in line for a promotion.

STANDISH STAND-DOWN

Semerci is not the only senior ex-Asia figure to have fallen by the wayside. Along with UBS' investment bank chief executive officer (CEO) Huw Jenkins, chief financial officer (CFO) Clive Standish appears to have been a casualty of US$4 billion in write-offs, mainly in relation to structured credit exposure and sub-prime loan-linked losses. Jenkins stepped down as CEO on September 30, while the 54-year-old Standish took early retirement.

Standish has long links with the region. Before stepping up to the CFO role he had been chairman and CEO for UBS in Asia-Pacific – although unusually he was based in Melbourne. He had held the CEO title in various iterations since 1994, when he headed SBC Warburg Dillon Read. He was then made co-chairman in 1997. During his time in the region, Standish was well-respected and considered a forthright, professional man who solidified the bank's franchise.

"Clive was very personable; an amiable guy," recalls one industry insider who used to work with him. "He was one of several people from Australia who moved abroad to bigger roles, and he presided during the beginning of the [economic] boom in Asia."

But it was UBS' financial woes in its third quarter report that have apparently led Standish and Jenkins to pay the ultimate professional price. Marcel Rohner has since become chairman and CEO, while Marco Suter, the bank's executive vice-chairman, has taken over as chief financial officer. UBS is also culling 1,500 jobs, although Asia is likely to be lightly affected, if at all.

"The buck has to stop somewhere and Clive was CFO; evidently UBS' risk management was not up to par," notes the insider. "Its exposure was mostly in AAA-rated assets but liquidity dried up and the bank had no choice but to raise its hand and say "*mea culpa*", especially given that it prides itself on generally managing risk well."

It is somewhat ironic that in an interview for *CFOAsia* back in September 2006, Standish had identified risk management as an area that UBS had worked very hard to improve.

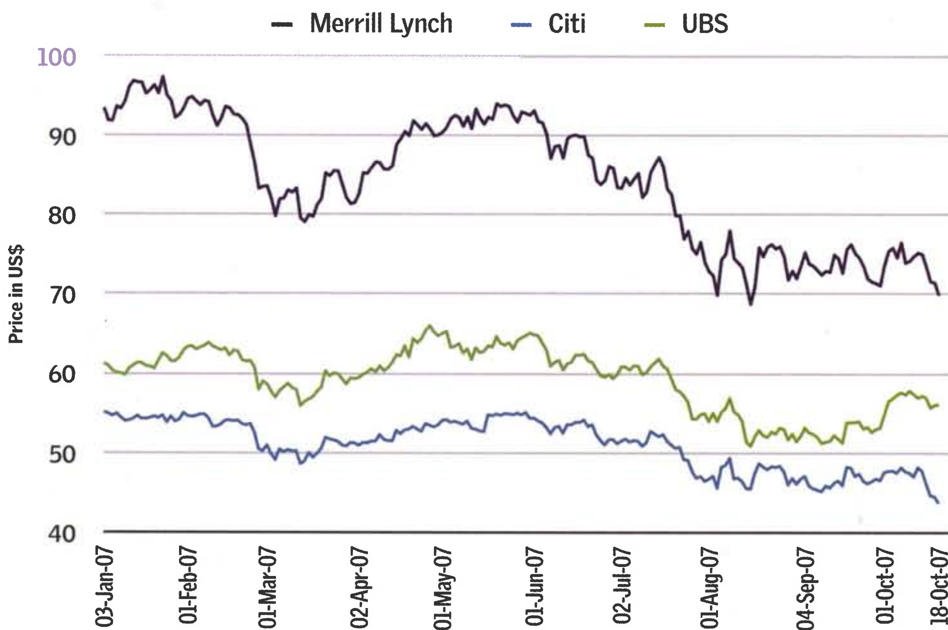
"We built a track record and have not stubbed our toes, even in the post-tech boom-bust in the early part of this decade," he said at the time, noting that the bank had a risk sub-committee of the executive board which included himself, the CEO, the head of risk, and each business groups' head, among others. "We're good risk managers," he concluded. Sadly, not good enough.

CITI'S FICC DILEMMA

The triumvirate in charge of Citi's global FICC operations also underwent some culling after the bank reported major write-downs of its own. The New York-based bank reported that its net income collapsed 57% year-on-year to US$2.38 billion in the third quarter, following US$3 billion of write-downs due to sub-prime loan exposures, trading losses and tighter market conditions.

Shortly before the results were announced, co-FICC head Randolph Barker left the bank and Citi said that Geoffrey Coley had been shifted to other responsibilities. That leaves Paco Ybarra as the sole remaining global head of the division. In addition, his old boss Tom Maheras, head of global capital markets, also left. Citi merged alternative investments with investment banking, promoting Vikram Pandit, who was in charge of the former unit, to head the new, united division.

Such a major shake-up could have ramifications across the bank's entire investment banking division – "it's pretty clear that Citi is in a world of pain right now," is the succinct opinion of one leading headhunter – but it is especially interesting for the Asian FICC operations. Jeremy Amias, Citi's regional head of the division, only resigned in August to join commodity trader Noble Group as its chief operating officer, and his position has not yet been filled.



With the situation in Citi's FICC in some state of flux, observers believe that two internal candidates are in the frame to get the FICC role for ex-Japan Asia. One is Aamir Rahim, the bank's polished long-standing head of ex-Japan Asia fixed income; the other is Rodrigo Zorrilla, who runs corporate sales and structuring for emerging markets in the region.

Opinions are mixed as to who would be better for the job – some observers reckon that the smooth-talking Rahim would seem the better fit, but it's possible that Zorrilla may have an edge, given that he shares a history with Ybarra stemming back to the pre-merger Citibank days.

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JOHN WRIGHT, CEO OF GLOBAL SAGE

BONUS BREAKDOWN

For the main part, the global fixed income turmoil has had a relatively light effect on the investment banks' Asian teams – so far. This is largely because the quickly growing region is the one area where all banks have been desperate to build their teams. They are unlikely to undo all that work so quickly, and will probably spend more effort to retain staff in Asia than either Europe or the US.

But despite this, expect some staff to start jumping houses – especially once the bonus period of January-March arrives.

"Banks are going to use this as a reason to cut back on bonuses," says one headhunter, who estimates that internal discussions within many banks have already led the available bonus pool to drop by up to 25%. "And the banks have been frantically hiring this past year, and guaranteeing people's bonuses to do so. Add a smaller pool and expensive new hires [with guaranteed bonuses], and long-standing staff could find themselves with very disappointing bonuses, and itchy feet."

Another recruitment consultant notes that it's not necessarily that simple – "there are ways and means to pay bonuses, offering company shares in lieu of money being one."

But after a two-year period when candidates could enjoy "30, 40, 50, even 100% pay rises if they were junior and also good percentage increases if they were senior," according to the consultant, the hiring momentum is definitely back with the banks. "Several banks looking to hire are now happy to wait until their targets get their bonuses because they know that the person will be disappointed and will accept less to move," notes a fixed-income specialist headhunter.

A STRATEGIC DIFFERENCE

The big losses sustained by some banks but not others also reveals how differing business strategies are panning out.

"There is a great amount of differentiation between investment banks at the moment – probably more than there has been for a decade," says John Wright, CEO of Global Sage, an international recruitment firm. "That differentiation is in profitability, business models and strengths and weaknesses. I think that alone will give rise to a lot of turmoil in the markets."

He believes it is the banks that have concentrated most on using their own balance sheets to invest in conjunction with private equity and hedge fund investors that have done best, principally Goldman Sachs. "Those firms that have integrated models of principal and agency businesses have done very well – and that differentiation is going to lead to an impact on pay."

For the coming months, it is best to keep an eye on those banks that have seen their share prices rattled the most and have announced the biggest write-downs of bad debt exposure. Any institution that has suffered big share price drops and write-downs will have to cut back on bonuses and will also face tough decisions about cost-cutting.

That could include reining back the money available for riskier trades and prompt disaffected regional staff to leave, especially in the leveraged finance, principal finance and trading divisions of these banks.

So far Citi, Merrill Lynch and UBS are the biggest candidates (Bank of America also reported US$4 billion in write-offs, but it has a limited Asian presence, while Deutsche Bank's exposure seems to have been balanced out by other divisions), but it is possible that some banks are slowly drip-feeding news of their total losses to the world. Eyes will remain on Merrill and also the likes of Bear Stearns and Lehman Brothers, as all of them have large fixed income presences. The latter two were hurt by market conditions – Bear Stearns' fixed income division saw profits drop 88% to US$117.6 million, while Lehman made US$700 million in write-downs – but overall they made third-quarter profits of US$166 million and US$887 million, respectively. Both have also been aggressively building their investment banking presences in Asia over the past 18 months.

Ultimately, the desire among all the banks to grow in Asia will still offer job opportunities. And while fixed income personnel are losing their jobs elsewhere, an import of talent could be on the cards. "There are some good people who've lost their jobs," observes one recruiter with London links. "I think it's realistic to expect some to look for jobs here."

The coming months promise some interesting, if unsettled, times ahead for Asia's investment banking community. ◢

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