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Mickey Roth-Express News Article I

The news this past week about Bernie Madoff was a jolt to me. Bernie is the gentleman who, according to press reports, was running a \$50 billion Ponzi scheme, and confessed that to his sons who called the FBI. What made this tough for me was that I've known Bernie for almost 15 years.

The press keeps referring to Bernie as an "investment manager". That's not how I knew him. His firm provided a valuable service to USAA Brokerage. They executed the vast majority of the trades which customers brought us and did that excellently. Their execution prices were always no worse than those on the New York Stock Exchange and very often they were able to execute at a better price. As a sidelight, Bernie's methodology provides a model which could have avoided the debacle that occurred with auction-rate securities.

It is apparent that Bernie ran some kind of fund. And when his fund fell on hard times, it appears he felt that he must continue its excellent record, so as new players came in he used their funds to reward old players. And that's called a Ponzi scheme.

It took me a day to get over being sad about Bernie. Then I got angry, and not just at Bernie.

Our nation has lost something. It has lost much of its idea of what is right and what is wrong.

I was raised in El Paso, Texas, as Bernie was raised in New York, by Jewish parents. They instilled in me their values; I should never discriminate against anyone, I must never use a racial epithet, and, above all, tell the truth. In 1959 I entered the United States Air Force Academy and one of the first things I encountered was our Honor Code; "We will not lie, steal or cheat nor tolerate among us those who do". It was a concept that was tough, but also well thought out. We were taught, for instance, that should a lady ask your opinion of her hideous hat, the Honor Code did not compel you to describe it using that word. But in terms of academic work and military matters the Code was rigid. Indeed, two days before my graduation, it fell to me, as Cadet Wing Commander, to inform two of my classmates that they would not graduate because they had cheated on tests for years.

But, the world has changed. Today, my classmates could have gotten a second chance because the USAFA Honor Code has changed. There are just too many people in our society for whom cheating is the norm. And we also tolerate.

Then there's Bernie Madoff. He apparently thought if you have a bad year in your portfolio, go ahead and steal from your new investors so you can satisfy your old investors. And it's not just Bernie. In the mortgage business, the norm was to go ahead and deliberately offer prospective borrowers an option not to verify or reveal their income. That means it's highly likely they'll be unable to repay the loan and we gave that the name "liar's loan". The New York Times reported that AIG was crippled by a 300 person office in London whose boss led a massive effort to create credit default swaps. He never explained his activities and no one at headquarters bothered to look. AIG survives today only because

our government has given it tens of billions of dollars. Then an investment advisor reported to me that the new CFO of Citicorp stated that his predecessor “had not revealed” that the firm held tens of billions of dollars worth of toxic mortgage securities effectively as an investment. This deliberate withholding of a highly risky activity occasioned another multi-billion dollar bailout.

In the investment business, the most important thing I’ve learned is that no one is always right. When you’re wrong you face it, you learn from it, you adjust and you keep going. But you don’t lie, steal or cheat. Nor do you act that way in any part of your business or your life.