



Workers assemble a Swiss bank UBS sign at the Marina Bay Street Circuit of the Singapore Formula One Grand Prix September 21, 2011. REUTERS/TIM CHONG

HOW A ROGUE TRADER CRASHED UBS

Alleged illegal trades at the Swiss bank have left it bruised and made it more likely that investment banks will face much tougher regulations

BY EMMA THOMASSON AND
EDWARD TAYLOR
ZURICH/SINGAPORE, SEPT 27

LATE LAST FRIDAY afternoon, as Formula One teams readied their cars for a practice session ahead of the Singapore Grand Prix, the entrance hall of the nearby Ritz-Carlton buzzed with activity.

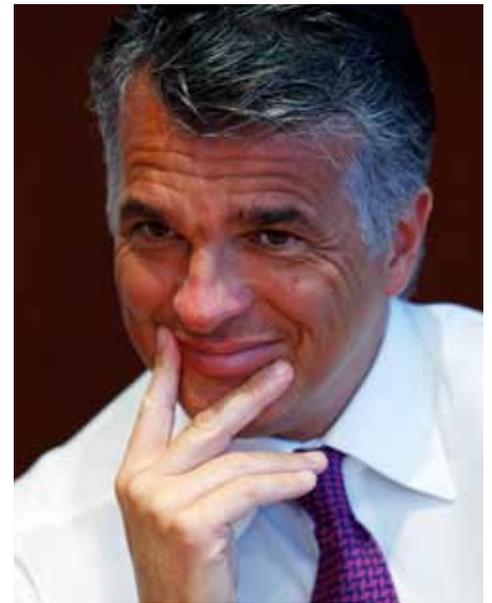
One by one, senior executives of Swiss bank UBS entered the lobby, which is designed by Pritzker-winning architect Kevin Roche and features a soaring glass

ceiling, and made their way to the gold-coloured lifts that whisk guests up to rooms that overlook the Marina Bay street circuit.

As the bankers sped past works of art by the likes of Henry Moore, David Hockney and Frank Stella, some made their way straight to a lounge UBS had hired to entertain clients during the race weekend. At its entrance stood three Singaporean women wearing red and white polo shirts, each holding a sign emblazoned with the UBS logo and the slogan "Welcome, the race starts here".

For UBS chief Oswald Gruebel -- and perhaps for UBS as it is currently constituted -- it was more like the end of the road. The bank's board had met in Singapore that afternoon to discuss the loss of \$2.3 billion by an alleged rogue trader in its London-based investment banking arm. Though the board had not yet gone public with the news, it had decided to accept Gruebel's resignation and appoint an interim replacement.

Gruebel's decision to leave a year or so ahead of schedule was not just a response



PASSING THE BATON: The decision by UBS chief Oswald Gruebel (left) to resign was an admission that the bank's latest scandal has effectively undone all his efforts over the past two years to lobby against tougher bank regulations. He will be replaced on an interim basis by Sergio Ermotti (right) who until now ran UBS's European operations. **REUTERS/CHRISTIAN HARTMANN/ALESSANDRO GAROFALO**

to the immediate crisis at UBS. It was also an admission that the bank's latest scandal has effectively undone all his efforts over the past two years to lobby against tougher bank regulations.

The alleged rogue trades have killed any remaining ambitions UBS might have to compete with the titans of Wall Street. They also cast a huge shadow across the entire industry and make tough new regulations far more likely, as the 67-year-old hinted in a memo to staff after he quit. "That it was possible for one of our traders in London to inflict a multi-billion loss on our bank through unauthorised trading shocked me, as it did everyone else, deeply. This incident has worldwide repercussions, including political ones," he wrote.

In the aftermath of the scandal, the Swiss parliament narrowly rejected a bid to ban investment banking outright. Governments elsewhere are now more likely to push through regulations such as the Volcker rule, which is under discussion in the United States and would ban proprietary trading by investment banks, and proposals in Britain that would force banks to "ring fence" their investment banking activities from their consumer banking side.

Global lenders such as UBS and Deutsche Bank have already cut the size of their balance sheets by at least a third since 2007, and are set to further shed risky assets to meet Basel rules on capital which will come into force in 2013. UBS said in August it would axe 3,500

"THIS COULD NOT HAVE HAPPENED AT A WORSE TIME FOR THE INDUSTRY IN GENERAL TERMS."

more jobs to cut 2 billion Swiss francs (\$2.2 billion) in annual costs, with almost half of those at the investment bank.

Interim CEO Sergio Ermotti, who until now ran UBS's European operations, told journalists on Saturday that his fellow bankers had to accept investment banking "is an industry that is due to shrink, not due to expand. Therefore anybody who wants to have a job and who is really keen to be in this industry will have to accept this new paradigm."

"This could not have happened at a worse time for the industry in general terms," said London-based banking headhunter Jonathan Evans, Chairman of Sammons Associates. "Investment banking activities have been under the spotlight too much in recent times for all the wrong reasons and this news will just produce further negativity from the man in the street."

Most of the bank's executives decided to fly home early from the Singapore board meeting. Chief Operating Officer Ulrich Koerner gathered with a few colleagues in a corner of the hotel's Chihuly lounge, looking glum and speaking in hushed tones as they shared a bottle of white wine.

A lawyer, part of the UBS team, paced up and down the marble-floored lobby muttering into his BlackBerry, "No ... no golden parachute".

As the cars began to wail on the track below, Gruebel appeared in the lounge through a side door. He had changed into casual clothes, and was sporting a black polo shirt and slacks. His hair was slicked back in its trademark style. As he moved across the room towards the grand piano he noticed Koerner and looked visibly relieved. He walked over to his colleague, who was perched on a low slung three seater couch, and stood behind him chuckling.

Speaking in Gruebel's native German, the two men reminisced about what a momentous day it had been. Each tried to reassure the other, until eventually Koerner looked up and said, "It has to be said: You know how to make the best of it, don't you?"

Gruebel chuckled again, smiled and walked back toward the lifts, waving goodbye as he retreated down a corridor towards a green glass sculpture called "sunset."

Asked to comment on his future by Reuters that evening, Gruebel shook his head and walked away. The following day, UBS announced his resignation.

METEORITE STRIKE

THE CALL THAT would eventually spell the end for Gruebel came at 4 p.m. on Wednesday, Sept. 14. The German was in Zurich in UBS's four-storey stone headquarters when Carsten Kengeter, who Gruebel had promoted less

than a year earlier to head the investment bank, phoned from London. Kengeter told Gruebel risk officers had uncovered massive unauthorised trades, according to the Swiss magazine Bilanz.

UBS had only recently started to win back the trust of its wealthy private banking clients after risky bets on subprime mortgages came close to felling it in the financial crisis of 2008. Kengeter knew only that the trades had left it exposed to massive new losses, probably amounting to billions of dollars.

Lawyers and executives were already grilling 31-year-old Kweku Adoboli, who had joined the bank five years earlier as a trainee and worked in the equities division. A UBS insider told Reuters that senior managers had been “flabbergasted” after discovering the alleged trades, which had come to light when controllers making routine checks demanded an explanation for positions that were due to settle on Sept. 22. Another insider described the news as like a “meteorite strike”.

Exposed, Adoboli had reported himself to his boss John Hughes who had alerted his bosses. Once senior management was informed, the bank told Britain’s Financial Services Authority as well as Switzerland’s regulator, FINMA.

Gruebel and Kengeter, both seasoned former traders, knew they had no time to lose. They ordered a small taskforce -- dubbed “Project Bronze” by those involved -- to immediately close Adoboli’s open positions.

Around 1 a.m. the next morning, as the extent of the problem became clearer, UBS informed City of London police who arrested the trader at around 3.30 at UBS’s London headquarters, and then took him to the nearby Bishopsgate police station.

A couple of hours later, executives in Zurich were called in to a pre-dawn crisis meeting to decide whether to go public with the news. Project Bronze was scrambling to unwind Adoboli’s positions in Asian trading. The bank had to balance its regulatory requirements with concerns that alerting the market could exacerbate losses.

The Swiss stock exchange had to be informed by 7.30 a.m. With two-thirds of Adoboli’s open positions closed out overnight, the scale of the losses was clear and executives agreed they would have to say something, especially as it would be almost impossible to keep the arrest secret.

UBS’s media department rushed to prepare a statement. Five minutes before European markets opened, the bank dropped its bombshell, first in German and minutes later



ACCUSED: UBS trader Kweku Adoboli arrives at City of London Magistrates Court in London September 22, 2011. **REUTERS/TOBY MELVILLE**

in English. It began: “UBS has discovered a loss due to unauthorised trading by a trader in its Investment Bank...”

That would be the only official communication from UBS for four days as the bank tried to get to the bottom of the scandal and close off the trader’s positions. Its stock tumbled, losing more than 10 percent on Thursday morning to close at a level last seen in March 2009 when UBS was grappling with a U.S. bid to force it to reveal details of 52,000 American clients suspected of dodging taxes.

Bankers said Adoboli’s positions were completely closed out by Friday lunchtime. Chairman Kaspar Villiger said Kengeter and

his team had done an “excellent job” to limit losses by moving so fast, contrasting their actions with the hesitation that compounded losses at Societe Generale after rogue trades by Jerome Kerviel three years ago.

“OOPS, WE DID IT AGAIN”

SPECULATION OVER the identity of the trader and the size of the losses began immediately. A banker in the London equities division said there was no gasp on the trading floor when the statement hit the screens, but people quickly noted that the desk which handled Exchange Traded Funds (ETFs) was “noticeable by its absence”. Another banker said early speculation focused on the fixed

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income division that had brought UBS to its knees in 2008.

Staff realised it was an issue in equities when investment bank head Kengeter appeared with other senior management and quickly did the rounds of the London trading floor to try to reassure staff.

"We understand that you have already had to contend with unfavourable, volatile markets for some time now. While the news is distressing, it will not change the fundamental strength of our firm," Gruebel said in a memo sent to employees that day.

That did little to stop the gallows humour among UBS staff, already worried about the looming job cuts. "Oops, we did it again," said one senior banker in Zurich. "The joke going around is that Gruebel didn't need to sack 3,500 people to save 2 billion. He could have just sacked ONE."

Emails circulated with a picture of a man wearing a UBS T-shirt with the slogan "It wasn't me."

Twitter was abuzz. Adoboli's boss John

Hughes -- who had already handed in his resignation -- was one name to emerge, but by early afternoon it became clear that the man in police custody was Adoboli, director of ETFs in the equities division.

Adoboli's profiles on social network sites such as LinkedIn and Facebook saw enormous traffic before they were taken down a few hours later. Reporters gathered outside the 1,000 pound-a-week flat in a trendy neighbourhood a few minutes' walk from UBS where he had lived.

The son of a former United Nations official from Ghana, Adoboli was well known around UBS as one of very few black employees on the trading floor.

Parallels were drawn with Kerviel, the

SocGen trader who racked up a \$6.7 billion loss in unauthorised deals and was exposed in 2008. Kerviel was sentenced to three years in prison last October. Both Kerviel and Adoboli were the same age at the time of their banks' scandals, and both worked with so-called Delta 1 products, which closely track underlying securities and give the holder an easy way to gain exposure to several asset classes.

A comment on Adoboli's Facebook wall fuelled rumours that his losses may have been linked to the huge volatility in the foreign exchange markets. "Need a miracle," read his final posting on Sept. 6, the day the Swiss National Bank (SNB) imposed a shock cap on the soaring franc.

That may have helped Project Bronze buy more time to finish closing the trader's final open positions, the Tages-Anzeiger daily wrote.

A MILLSTONE?

INVESTMENT BANK boss Kengeter made only a passing reference to the situation when he broke away from the bank's offices to deliver a speech at a fund-raising dinner at the Bridge Academy school in London's East End, which is supported by the bank. Chairman Villiger briefed the Swiss NZZ newspaper to say UBS remained committed to an integrated bank, combining core wealth and asset management with investment banking.

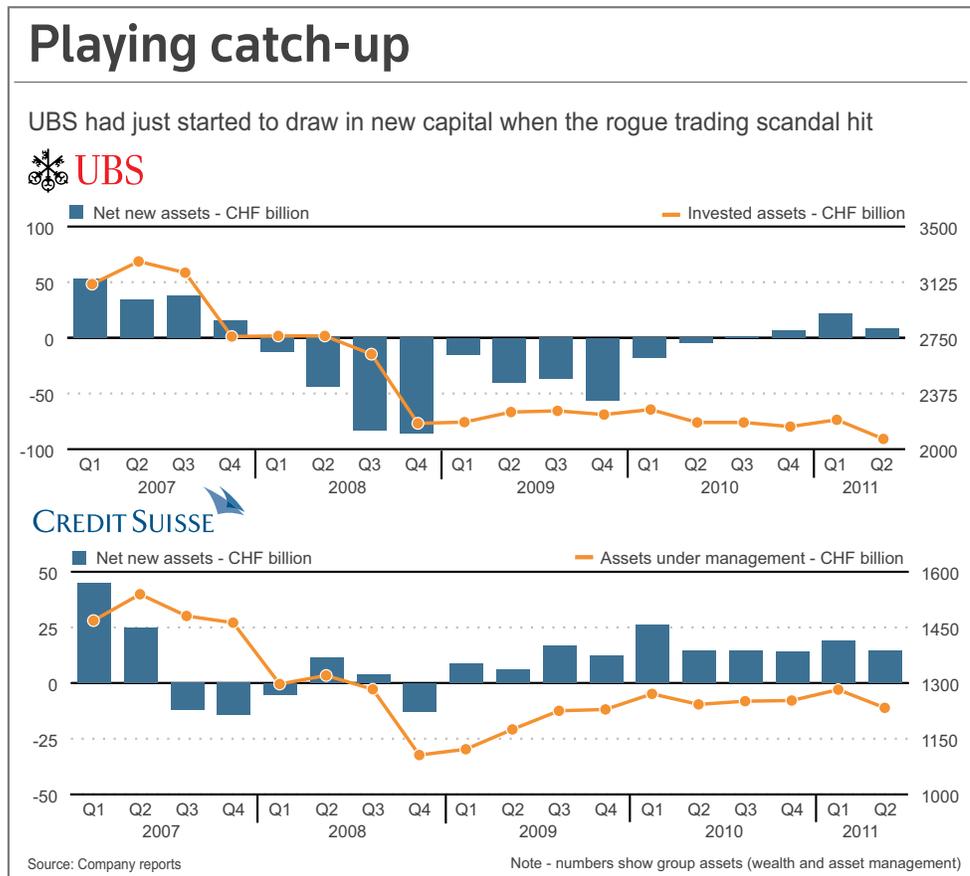
But the mood in the Zurich headquarters was bitter. "The trading disaster has driven a deeper wedge between wealth management and investment banking, adding credence to the idea that investment bankers are the millstone around our neck," said one manager. "We were all angry with London. And then we saw all the bad press about us, and this has changed the mood again. Now there is a sense that we need to show that this is not representative of what we stand for."

A UBS private banker told a Reuters reporter that while he had no direct knowledge of events "the thing we're all asking is why Carsten Kengeter is still there." Perhaps, he speculated, the investment bank boss was too young and dynamic to be made the fall guy.

In a sign of the chaos at the bank, UBS called and then cancelled a background briefing for Swiss journalists on "Delta One".

VIDEO

BVO package:
<http://link.reuters.com/zuq93s>



Reuters graphic/Vincent Flasseur, Scott Barber



At almost the same time, Adoboli was charged in London. In a Magistrates Court, he was accused of two counts of false accounting, and one count of fraud by abuse of position.

UBS advisers said the bank had planned to update the market with more information on Friday, but the police decision to charge Adoboli forced them to remain silent. UBS lawyers told them that any detailed explanation of events that explicitly pointed to Adoboli would risk putting UBS in contempt of court.

By the time markets closed on Friday, UBS stock had recouped half of the previous day's losses on hopes the scandal could prompt a restructuring of its investment bank. British and Swiss regulators announced that they were launching a joint investigation into the losses to be paid for by the bank, including why the trades had gone undetected.

An insider in UBS's wealth management division told Reuters there were rumours that the non-wealth management part of the investment bank could be listed separately, even though that would mean an investment

bank without the backing of deposits.

TITANIC DEFIANCE AND LAMENT

AS PRESSURE mounted on Gruebel, UBS Honorary Chairman Nikolaus Senn told Swiss television that he did not think the CEO would be able to resist the pressure to step down because he and the board had the final say on what happened at the bank. "I do not know how often Gruebel flew to London to ask the people in charge how the business was going," Senn said.

The Social Democrats, Switzerland's second-biggest party which wants to ban big banks from engaging in risky investment banking, demanded Gruebel's departure. "Arrogant and irresponsible managers like Oswald Gruebel must finally be replaced by people who have learnt the lessons of the 2008 financial crisis," the party said.

Gruebel, a former CEO of Credit Suisse who was brought out of retirement in 2009 to turn the bank around, seemed determined to tough it out. On Friday evening, two days after the scandal broke, he took his seat at a UBS-sponsored concert in the Swiss city of Lucerne with his partner Renate Haeusler. The programme of Mozart and Bruckner was called "Titanic defiance and lament".

"I am not thinking about stepping down," Gruebel told a journalist from Der Sonntag newspaper at the concert. "I am responsible for everything that happens in the bank. But if you ask me whether I feel guilty, I say no."

With the markets closed for the weekend, Gruebel and his staff could take their time drafting the next memo. The media team was called into the Zurich office on Sunday and after a few false starts issued a carefully worded release at 4 p.m. The bank said the rogue trades had lost \$2.3 billion and said the trader concealed "unauthorised speculative trading" in various index futures by creating fictitious hedging positions in internal systems over three months. "We have now covered the risk resulting from the unauthorised trading, and the equities business is again operating normally within its previously defined risk limits," it said.

The statement left many questions unanswered. How did the trades go undetected for so long? UBS insiders said controllers had started asking questions in July. Of particular interest were trades that used other parts of the bank to cover Adoboli's positions. Such trades, known as "internal futures", do not require confirmation.

With the controllers probing, one

REUTERS INSIDER

SIMON MAUGHAN
BANKS AND SPECIALTY FINANCE ANALYST

Video: UBS will cut riskier side of investment banking arm:
<http://link.reuters.com/tun93s>

Rogue's gallery

Rogue traders since 1992.

Name of trader (Company)	Loss – \$ billions	Year
Jerome Kerviel (Societe Generale)	~6.5	2010
Brian Hunter (Amaranth Advisors)	~5.5	2006
Kweku Adoboli – alleged (UBS)	~2.3	2011
Nick Leeson (Barings)	~1.5	1995
Various (Indian banks/brokers)	~1.2	1992
Toshihide Iguchi (Daiwa Banks)	~1.0	1995
John Rusnak (Allfirst*)	~0.8	2002
Alexis Stenfors (Merrill Lynch)	~0.5	2009
Joseph Jett (Kidder Peabody)	~0.4	1998
D. Bullen, V. Ficarra (National Australia Bank)	~0.3	2006
Evan Dooley (MF Global)	~0.2	2010
Steve Perkins (PMV Oil Futures)	~0.1	2009

* US subsidiary of Allied Irish Bank
Source: Thomson Reuters



bank insider who spoke on condition of anonymity alleged that Adoboli switched to forward-settled trades that used exchange-traded funds. Some banks do not require confirmation of such trades before the settlement date. Adoboli allegedly knew which these were, and by entering them as counterparties in the system, might have been able to fool the system into believing his fake hedges were real.

SINGAPORE BOUND

THE NEXT DAY, as Gruebel packed his bags for Asia, Switzerland's parliament debated plans to force the big banks to hold more capital than their global rivals to prevent a repeat of the state bailout of UBS in 2008. The latest scandal will surely fuel demands for such tighter rules.

Chairman Villiger said Gruebel decided to quit while in Singapore, despite the board asking him to stay on for at least another six months to help ensure a smooth succession. He denied Gruebel had jumped before he was pushed and rejected any connection to the investigation into the scandal as well as

suggestions that pressure from the bank's biggest shareholder, Singapore's sovereign wealth fund GIC, had played a role.

Gruebel spoke to the board's governance and nominating sub-committee, including Villiger, former Morgan Stanley CFO David Sidwell and ABB CFO Michael Demare.

"It was a very long and intensive discussion about what is good for the bank and what is not good for the bank and at the end we felt he didn't want to reverse this decision and we had to respect that," Villiger said.

Former Bundesbank chief Axel Weber, appointed in July as Villiger's successor from 2013, at first tried to keep out of the turmoil. But a senior banking source told Reuters Weber is now informally involved in every strategic decision at UBS; he joined the board meeting in Singapore. Weber has asked the

Bundesbank to give him the go-ahead for an earlier start.

"This is a catastrophe. They have had six CEOs since 1998. It is such a management merry-go-round," a senior Swiss banker who used to work at UBS told Reuters. "They have such a strong franchise but it is simply a problem of governance: too much change at the top and not the strongest board of directors."

Given those problems, it may take some time for UBS's logo -- three keys symbolising "confidence, security, discretion" -- to regain its shine.

(Emma Thomasson reported from Zurich and Edward Taylor from Singapore; with reporting by Peter Thal Larsen and Steve Slater in London, Martin De Sa'Pinto in Zurich, Alexander Huebner in Frankfurt, Philipp Halstrick in Washington and Luke Pachymuthu, Rachel Armstrong, Harry Suhartono, Christophe Van Der Perre, Charmian Kok, Eveline Danubrata, Anuradha Kanwar and Saeed Azhar in Singapore; editing by Simon Robinson, Alexander Smith and Sara Ledwith)

LIGHTENING STRIKES:

Lightning strikes over the headquarters of Swiss bank UBS during a thunderstorm over the Paradeplatz square in Zurich late August 24, 2011. REUTERS/ARND WIEGMANN



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