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The past six months have seen a steady parade of humbled business and financial leaders coming to Washington to explain what went so terribly wrong -- or to plead for salvation in the form of government assistance. The car makers, commercial banks, investment bankers, Freddie Mac, Fannie Mae – a once impressive list of who was who in the American economy.

In this prolonged atmosphere of crisis that bleeds from one sector to another, and amidst a chorus of expert commentary, I'd like to give you the view of a public exchange. My particular prism is as head of the largest exchange company in the world that operates markets around the globe. And when I say we operate markets, I mean just that. We don't control the direction of indices -- though we would like to -- but rather we focus on providing a transparent market where there is equal access for investors, and where values are real and posted in real time for all to see.

What has been gratifying to us during this crisis is that America's licensed markets have performed. They did not freeze, they worked as advertised. We enabled investors to trade and provided needed transparency, despite unheard of volatility and volume.

Amidst this meltdown, an important objective for us is to find constructive ways to help the new Administration succeed, and to ensure that liquid, efficient capital markets are part of the solution. The first step to finding answers is to arrive at a clear understanding of how we managed to sink into to the greatest economic crisis of our lifetime.

So, how did we get where we are today? The short form answer is that there was irresponsible speculation in real estate, and that speculation was enabled, multiplied and securitized by Wall Street. Securitization moved the asset 10 iterations away from the root investor. In another time and place, the local bank that held the mortgage understood the value of the asset and the risk for default - their neck was on the line. But Wall Street took on this "10 iterations away" risk, and the actual risk and value was not immediately apparent to anyone – not to the public and not to the executives of these institutions.

So the question becomes, how did we have very smart financial services CEOs making disastrous decisions about their business? Did they ignore the fundamental business metrics that CEOs rely upon each day, to make business decisions?

I believe the crucible of the problem was bad decision making based on bad information.

What was wrong with the information?

Throughout the economy, trillions of dollars in investment instruments were never subject to the rigor of trading on a transparent, well regulated market. In the absence of a market determined price, firms, which were 10 iterations away from the risk, valued these assets on a theoretical model which, in the words of Warren Buffet, turned out to be a myth. As a result we had a tremendous number of complex instruments on the books of banks and businesses whose value was opaque and ultimately horrifically mispriced.

These particular credit instruments were traded “Over the Counter,” or OTC in the industry jargon, which essentially means they are traded between a limited number of parties with no external validation and based on information not available to everyone. In the OTC world, values were distorted in fashion not unlike the game of “Telephone” you might have played as a kid. Because these instruments were not valued in the real market, because they were not transparent and lacked a central clearing facility, unrecognized risk piled on unrecognized risk.

CEOs are not stupid and not all are greedy. We saw that highly respected, household names in the banking world came to work in the morning and left everyday without any idea of the true value of the assets that went on their books each day. The former heads of Citi, Merrill and other institutions never got a report that said “Your OTC derivative portfolio lost \$5 billion in the market today.” In fact, these CEOs -- based on the information their “mark to model pricing” calculated, -- continued to double down their bets on subprime in the period leading up to the Bear Stearns meltdown.

Example 1:

Merrill Lynch’s decision to invest in mortgages was so profitable that at the end of 2006 their share price was up 40%, and on Dec. 30 of that year it doubled down its bet by purchasing First Franklin, a lender specializing in risky mortgages. The cover bid for the company was \$300M, but Merrill agreed to pay \$1.3 Billion. Merrill went on to make even more deals. From January 2005 to January 2007, it made 12 major purchases of residential or commercial mortgage-related companies or assets, based upon a belief in the model derived value of these assets.

Previous financial scandals have involving knowing financial services executives, foisting inappropriate products on unknowing investors. In this crisis we have witnessed that these financial executives, even though they were ten iterations away from the real underlying assets, so believed in their mark to model valuations of these assets, that they foisted these mis-valued assets on their own balance sheets.

The other driving factor here is the structure of executive compensation. I am not commenting on the amount of compensation, but on the fact that compensation must not be paid on the interim performance but on the completed performance of an employee. Many financial services executives were paid for transactions that hadn’t fully played out. Football players get paid based on what they get over the goal line – here people were getting paid based on a ball still in flight. The short-term nature of the compensation caused many executives to take action, or not take action, which was to the immediate advantage to themselves and their institution, instead of actions for the larger long term benefits to themselves and their institutions.

Greed is said to be the root of all evil and it is easily a culprit here. If there have been proper asset valuation information available to boards and executives and compensation plans based upon that proper information, our situation would be dramatically different.

I have identified the problem, but here is what we can do.

The negative aspects of the OTC market can be changed. NASDAQ was once upon a time an OTC market.

We were born out of a need to share information about stock trading in a central fashion accessible to all, a system designed to protect investors and facilitate discovery of the right price for a particular security. We continue to operate on a simple principle that goes back to the cave man – a willing buyer and a willing seller agreeing, is the only valid price discovery mechanism. It was true five thousand years ago, it is true today.

It is possible to transform an over the counter market to one that is centralized and visible to all -  
- we've done it.

These OTC instruments need to be centrally cleared to better distribute or mutualize the risk. Central clearing fundamentally means more parties are backing a transaction, vs. a few, as in “bilateral clearing” where all parties are only as strong as the weakest link in the chain. Central clearing gathers strength from more parties and the benefits of netting multiple risk exposures.

We have the clear and present ability to take the mystery out of the markets through the value of transparency, and this is powerful.

Let me give you a specific example of how our markets can help.

When NASDAQ was founded over 37 years ago, our primary mission was to bring order, discipline, and fairness to the OTC stock market.

Building on decades of experience, we are now moving to bring these values including transparency, real valuations, and central clearing to the \$400 trillion OTC Interest Rates Swaps market – a market six times larger than the Credit Default Swap or CDS market.

NASDAQ OMX recently purchased an 80% interest in the International Derivatives Clearing Group and – with thanks to the CFTC for timely approval – we have begun operating a highly efficient market to clear and settle U.S. dollar interest rate swap futures. We have seen how bilateral contracts have contributed to the current credit crisis. And – we are certain that basic market mechanisms such as central counterparty clearing systems can reduce credit risk while increasing the efficient use of capital.

We look forward to the day when vast swaths of the over the counter market are no longer stored in the back rooms of brokerage houses but held in well capitalized clearing houses, transparent to all. And the most liquid of those products can trade, like any instrument found on an exchange

today. As we go forward in time we will see the advantages of having central counterparty clearing systems and the benefits of having price discovery being transparently displayed.

If we fix these markets, we will create a better foundation for President-elect Obama's long-anticipated and much-discussed trillion dollar stimulus package. We believe in the need to jump start the economy but we should not turn up the heat on an oven that is broken.

That brings us to regulatory structure. We have a wonderful opportunity in front of us to fundamentally rethink regulation – and it is not just a matter of modernizing rules from the 1930s, though modernization is important.

The objective should not be more regulation or less regulation: it should be re-regulation -- smarter and more efficient. We need new rules on the books, reflective of the world that exists today, but we also do not need rule reflective of the world that existed in the 1930s. And government agencies should utilize self-regulation where it is well proven and where government resources can be freed up for higher priorities.

When we look at a regulatory body like the SEC, there is a clear prioritization problem. A hearing earlier this week questioned whether the SEC needed more authority or more resources. That can be debated, but where the SEC failed was in focusing on the wrong issues - it was not about authority or resources. Their priorities did not match the priorities driving the financial market. The SEC was policing obscure business issues while investors fell prey to schemes such as those of Madoff. The functioning of the financial services sector -- as we have been reminded by this crisis and most recently by the Madoff scandal -- is based on trust. Victor Ponzi propagated his scheme in 1930 and I am sure what is now called the Ponzi scheme pre-dated even him. Villains driven by greed will always be there – the key is to find them. One simple recommendation is that the regulators needs to be at the heart of the action virtually and physically. The location of senior regulators in the New York City office is advisable.

It is also incomprehensible that we have two regulators – the SEC and the CFTC – at a time when financial products have evolved into instruments virtually indistinguishable from one another. In other words, two different agencies with very different approaches essentially monitor the same securities. I don't see how we can address systemic risk without a regulator with an overall viewpoint and mandate. The financial markets will always stay ahead of regulators, and particularly regulators who wield static rules. Rules have embedded loopholes, and it is a certainty that loopholes will be found. We need a regulatory agency with a broader mandate around systemic risk - one driven by specific objectives governed by principles, not rules.

I'll give you another example of how market-based innovations can be part of the solution. Nasdaq OMX introduced a new Government Relief Index that tracks companies participating in government-sponsored programs like TARP. With this Index, taxpayers and investors will be able to measure the performance of companies participating in the government's financial relief plan. Investors will also be able to evaluate the government's investments and the impact of the relief plan. It will provide investors with another option, another perspective in an uncertain time.

At NASDAQ OMX we have huge respect and esteem for the people the President-elect has chosen to lead his economic team. We have confidence in their ability to lead, innovate, manage our economy back to robust growth – and win this battle against economic retrenchment.

We are anxious to work with the new administration to support the rebuilding of our economy. With respect to President-elect Obama's much-discussed stimulus package, I think the message is loud and clear. This stimulus will serve as the starting gun for what promises to be an uphill, marathon race to reinvigorate the American economy and preserve American leadership in the world. So I urge Congress and our new President to think comprehensively and think big; underfunding our hopes for a recovery is our biggest risk at this point.

We have a new Administration, new thinking and new ways of doing business. The time has come for best practices and a comprehensive program of re-regulation that protects investors from risk. It bothers me a bit when I hear people – some really smart people – suggest that free markets are dead, or that our economy is on the road to socialism. I don't believe that for a minute – and you shouldn't either. This economy is resilient. It will come back – as it always has. And that resurgence will rise from America's tremendous entrepreneurial spirit combined with the world's best capital markets – the crucible of our free enterprise system. Our systems work; our infrastructure is in tact. Our faith in America has never been stronger.

Thank you very much.