Saturday Interview: Nova Scotia native Bob Kelly

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Nova Scotia native Bob Kelly has risen from being one of the most powerful Canadians on Wall Street to one of the most powerful bankers, period.

As chief executive of Bank of New York Mellon -- one of America's largest and healthiest banks -- Mr. Kelly, 55, had a front-row seat as the global financial system teetered on the brink of collapse. He huddled in meetings at the New York Federal Reserve building the weekend Lehman Brothers blew up. When it came time to clean up, Barack Obama, the U.S. President, invited him and a dozen other top bankers to discuss how to shore up the banking industry.

Mr. Kelly's bank emerged from the meltdown as the strongest bank on Wall Street, even healthier than Goldman Sachs.

He sat down with the Financial Post in his wood-paneled office 10 stories above Wall Street to discuss his career, the crisis and what's coming next.

Q. You started out your career in Halifax?

A. I was in public accounting for about six years with a firm that is now KPMG. I was doing a little bit of computer consulting as part of that. Of course, I figured the place to do that was in Toronto and I joined a bank, which was Toronto-Dominion.

Q. After a 19-year tenure at TD, you were a contender for the CEO slot, but there was a bit of a power struggle?

A. It wasn't so much that. There was a merger between Canada Trust and TD and I was a candidate at TD. Ed Clark was already CEO of Canada Trust and very effective and doing a great job and I saw it as an opportunity to do something different. A job as CFO at First Union in Charlotte, N.C., came up. I'd never worked in the U.S., although I had worked in the U.K. We thought it would be great for the kids, too, to get exposure to the U.S. schooling system and have greencards and all that cool stuff. And good weather, too.

Q. Did you envision yourself where you are now back then?

A.No. I won't call it a random walk but I've been very lucky. I've had the opportunity to be involved in some pretty exciting things in my life, whether with TD or Wachovia, which merged with First Union, or our new combined Bank of New York Mellon. It's the oldest bank in the United States, started by the guy on the US$10 bill. It's our 225th anniversary this year. We have 45,000 people around the world in 38 countries.

Q. How did Bank of New York Mellon get through the crisis as one of the strongest, if not the strongest, U.S. bank?

A. We are modeled a little different from most banks. Our model is really focused on asset management -- we have over a trillion dollars in assets under management -- and asset services -- there is a little over a hundred trillion of bonds and equities on the planet and we have custody for US$20-trillion of it. We've very much enjoyed a flight to quality over the last 12 months.

We're always trying to figure out what to do, though, with all of the deposits because we don't lend a lot of money, but we do buy securities.

Looking back on it now, if I could change anything, it would have been the fact that we bought a lot of securities that were Triple-A rated by S&P and Moody's that turned out, at best, to be Triple-C in terms of quality. Shame on us because we should have done a lot more work in understanding the fundamental cash flows and other characteristics of those securities instead of relying on ratings agencies.

Q. Was there a particularly scary moment in the whole crisis?

A. One of my mentors from TD, Robin Korthals, once told me that as head of the bank he only had to make one or maybe two difficult decisions a year. Our team was making them almost every day in late September and early October. Clearly, the weekend before Lehman Brothers' collapse and what happened to the credit markets resulted in the U.S. financial system literally walking to the edge of an abyss. Very aggressive and creative things were done by the Treasury, as well as by the Federal Reserve Board, that allowed us to very, very slowly start backing away from that abyss. It was extraordinarily scary. I could have pictured any and potentially all financial institutions disappearing during that period.

Q. How do we thwart the next financial crisis. Do we need caps on the excessive pay given to bankers?

A. If you ask me for a top 10 list, I'd say compensation would be one of them, but I'd put it at the bottom of the list. The No. 1 issue in the United States is fixing the mortgage business. We do not have any underwriting standards, particularly compared with Canada, including basic stuff like mortgage brokers who are not registered and trained. In Ohio, 18% of mortgage brokers had criminal backgrounds. Having a 20% down payment in Canada versus 3% here makes a huge difference. That's just unsafe for U.S. consumers. And it varies state by state. What we need are national standards. This stuff is not rocket science and frankly, it's exactly what kept Canadian banks healthy.

Beyond that, a number of banks didn't have enough capital. A lot were very, very short funded. Also, unlike Canada, where you have one regulator, the United States has multiple regulators. The problem with that is it's difficult to be accountable and to see the big picture. They need to modernize.

To have capitalism and Darwinism in the financial system, no company should be too big to fail. The only question is how do you wind down a bank holding company in a way that it doesn't hurt the entire system. I think that's solvable and I think the government is going to figure out ways to do that.

Q. Canada's financial systems and its banks have been lauded as the most sound in the world. Are they really so great?

A. The quality of Canada's bank management teams and the country's regulations are highlighted by the fact that in the worst financial downturn in 80 years, most Canadian bank stocks are trading at 12-month highs. The thing that distinguished Canada the most is its mortgage product. Even with the tougher standards there, Canada has higher home-ownership rates than in the United States.

Q. Where are we on the road to recovery?

A. The bad news is we're not out of the woods yet as a country. The housing markets have not bottomed out and we need to put that behind us. Residential housing is now down 32% peak to trough. It probably has another 5% to 10% to go. Commercial real estate is a much smaller asset class, so I don't think the impact will be as big on the economy. Commercial real estate is now down 35%, more than residential. Banks hold about US$1.7-trillion worth of debt tied to the commercial real-estate market. There will be losses on that, particularly at smaller banks in the southeast and southwest, because a lot of them relied very heavily on commercial real estate.

We’ll see a lot of those banks disappear over the next year or two. But that information is already reflected in bank stocks.

The good news, though, is that the banking system is stronger than it was three months ago, six months ago and 12 months ago. The banks here are going to be tough competitors a couple of years from now.

My fear is that when we’re sitting here this time next year, the unemployment rate will be stubbornly north of 9% and that will have real implications for growth going forward.

Q. You must have a lot more free time now that the crisis has subsided.

A. For three months last year -- September, October, November -- it was pretty intense. My wife came downstairs one weekend morning and looked at me and said, ‘Well, this is interesting.’ I said, ‘What’s that?’ She said, ‘This is the first weekend you’ve been home since Labour Day.’ I’ve done a lot more visiting with clients around the world since then. We made an acquisition of an asset manager in the United Kingdom.

Q. And when you’re not working?

A. I biked about a thousand miles this year. I was in France a couple of weeks ago on a bike trip for a week. That’s 800 miles without the trip. That’s a lot of trips around Central Park. I’m also a history buff. I like to read biographies.

Q. How do you think this period in history will be remembered?

A. I think when people look back on this five years from now, they’ll see what our government did as essentially brilliant. I don’t think the average American, and probably the average Canadian, realizes how dire was the state of the economy at that particular point in time last fall. We could have easily slipped into a global depression. Not everything worked. In hindsight, should Lehman have been allowed to go down? No. But the aggressiveness and creativity that was shown by Ben Bernanke, Hank Paulson, Timothy Geithner and others was really impressive.

About 20% of the U.S. government bailout money has been repaid so far and at very nice returns for taxpayers. As it applies to the banks, I’m willing to bet that taxpayers won’t lose a dime.

Source: Financial Post
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