JPMorgan trumps Goldman, Morgan Stanley as Wall Street's top commodities trading unit

(Reuters, NY, Mar.2, 2012) - Blythe Masters, JPMorgan's global head of commodities, has steered the bank's expanded franchise to record revenues exceeding $2.8 billion in 2011, more than long-time industry leaders Goldman Sachs and Morgan Stanley, the three banks' data showed this week.

The more than threefold surge in revenues marks a dramatic turnaround for British-born Masters, one of the top female executives on Wall Street, who came under pressure in 2010 as revenues fell following the acquisition of RBS Sempra's large metals and energy trading desks, according to sources and company data.

By contrast, Wall Street's commodity trading pioneers have stumbled, with Morgan Stanley's revenues shrinking for a third consecutive year -- the worst streak since at least 1995 -- and Goldman Sachs commodity unit J. Aron is nursing a large drop in revenues since raking in more than $4.5 billion in 2009.

George Stein, managing director of headhunting agency Commodity Talent in New York, said Masters' strategy of "dominance through acquisitions and size" had been vindicated.

"Only a short while ago, top commodity executives at her rivals were wondering how long she could survive," Stein said. "Now it's their turn to wonder."

The data illustrate the shake-up of a sector long dominated by the oldest commodity franchises on Wall Street, which are struggling after being forced to shut down riskier proprietary trading and amid the threat of losing top talent

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to aggressive merchant traders. Whipsaw market volatility has also cut into trading and hedging activity by their clients.

Goldman's Isabelle Ealet, who was promoted out of the division in January after leading it for years, saw revenues stagnate at $1.6 billion last year, according to a regulatory filing by the firm.

Morgan Stanley revenues fell 18 percent in 2011 due to "lower levels of client activity", the bank said, taking its three-year decline to nearly 60 percent. Based on Reuters' calculations, revenues peaked at around $3 billion in 2008, declining to some $1.3 billion last year, the lowest since 2005.

To be sure, the raw numbers themselves are not a definitive indicator. JPMorgan described itself this week as one of the three largest commodities players, and some say it still lags behind Goldman Sachs when adjusting the data for accounting differences among the banks. But the trajectory is clear.

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Last year, JPMorgan's commodities revenues made up more than a quarter of the bank's total "principal transactions", up from around a tenth in the previous years.

For Goldman Sachs, commodities made up 15 percent of total "market making and principal transactions" revenues. At Morgan Stanley, commodities' share of total sales and trading revenues fell to 10 percent in 2011 from 14 percent in 2010. It wasn't immediately clear whether the figures were directly comparable.

All three banks declined to comment for this story or on the revenue figures.

Jes Staley, JPMorgan's chief of

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investment banking, told analysts on Tuesday the bank was now among the top three in commodities, with 600 professionals and 10 offices globally.

"I think the extraordinary movement that we've made in the commodities business pretty much demonstrated in 2011 that this business had arrived," he said.

CAVEATS

The revenue figures have not been widely reported, although Goldman Sachs and JPMorgan began releasing commodity trading revenue figures in their regulatory fillings in 2009, lifting the veil on data that had been zealously guarded in the past.

The data come with many caveats. They do not reflect the costs of running the businesses and the banks use different methods to account for certain investments and fees. Gains in one division may be offset by losses on another trading desk.

Goldman Sachs may yet be on top when adjusting for these factors, according to Seb Walker at British financial markets consultancy Tricumen.

Using its own product definition, Tricumen estimates that Goldman Sachs and JPMorgan's normalized commodity-related revenues are in the region of $2 billion each, with Goldman Sachs a notch ahead. Morgan Stanley has fallen behind in recent times, with 2011 revenues of around $1 billion.

"Morgan Stanley is a step below now. One of the main reasons is that they have taken a much more conservative line on Volcker than Goldman over the last couple of years," Walker said in reference to the law barring proprietary trading.

To further complicate the figures, JPMorgan published a second set of numbers for principal transactions revenue. A bank spokesman declined to say which set of data was more representative.

Morgan Stanley has been reporting a year-on-year percentage change figure for its commodities revenue since 2003,

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and prior to 2001 reported revenue in dollars as well. Its total revenue figures were calculated by Reuters based on an estimated decline of 35 percent in 2002 revenues.

Other U.S. banks appear far behind. Citigroup reported just $76 million in commodity revenues last year, less than a tenth as much as in 2009, before it sold the proprietary trading unit Phibro to Occidental Petroleum. Bank of America does not provide any data on its commodity division.

MASTERS' RISE

Until 2008, JPMorgan had struggled to achieve its big ambitions in oil and base metals, finding only moderate success in things like natural gas after buying part of failed hedge fund Amaranth's trading book. The bank first dipped a toe into the business in the 1990s, prior to its merger with Chase in 2000.

John Fullerton, head of the bank's commodity business at the time, said it was seen as a strong opportunity for the bank.

"Our strategy was to use our derivatives and risk management expertise to complement our financial commodities trading, right at the time that Enron was going great guns," Fullerton said in an interview in February.

"We wanted access to the physical markets to more efficiently manage the risk. But we were client risk management focused, not in the league of a J.Aron (Goldman) or Phibro, which were commodity trading firms at their core."

But CEO Jamie Dimon saw commodities as a central pillar of growth, and during the financial crisis he and Masters were able to cherry pick some of the key assets and franchises of struggling rivals, as they went bust or exited the business.

Over the next two years it bought up or absorbed Bear Stearns' physical power and gas trading business, UBS's Canadian and agricultural commodity arms, and a large chunk of RBS Sempra's business, including metals warehousing firm Henry Bath.

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Then came JPMorgan's big move -- buying RBS Sempra for $1.7 billion, a deal that gave it a major global oil and metals trading operation when completed in July 2010.

That year the bank was to learn some hard lessons about an expanding operation. Traders put on a wrong-way bet on coal that hit the bank for some $200 million in losses in 2010, industry sources say, drawing unwanted attention at a time when curbing banks' trading risk was a hot political issue.

Masters was called before the board at the end of 2010 and handed a target of at least $1.2 billion in revenue for 2011, the Wall Street Journal reported last year.

Now, the bank makes an average of 140,000 metals trades a quarter and 50,000 energy trades, according to an investor presentation this week. On average its metals operation generates $75 million, or $600 per trade, in revenue per quarter; energy generates $250 million, or $5,000 per trade.

"During 2012, the ambition here is to continue to consolidate the client franchise that we've got in commodities and to achieve the profitability targets that we set for ourselves on the back of the Bear acquisition and Sempra acquisition," Staley said this week.

WALL STREET TRAILBLAZERS

In 1981, Goldman Sachs was one of the first Wall Street firms to jump into commodities, with the outright purchase of trading firm J. Aron & Company, a former coffee importer that had become one of the preeminent precious metal, oil and soft commodity traders of the era.

After an initial struggle to integrate rough and tumble oil traders into Goldman's white shoe culture, the business would soon grow to provide at times more than 10 percent of the bank's multibillion dollar revenues and become one of its most profitable divisions. Two J. Aron traders, Lloyd Blankfein and Gary Cohn, would rise to the very top of the company.

But the bank now faces curbs on

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its proprietary trading and the loss of some key traders. It exited proprietary trading in commodities in the first quarter of last year.

And now change is afoot. Ealet was promoted this year to co-head of the bank's securities division, where she will divide her time between equities, fixed income, and currencies as well as commodities. Top metals traders left the firm this year to join Swiss merchant Mercuria, part of an industry-wide exodus spurred by shrinking bonuses.

Ealet, who has been with the bank for more than 20 years, had spearheaded the bank's move into the physical metals market in 2010, purchasing metals warehousing firm Metro International for around $550 million, according to industry sources.

Morgan Stanley has faced similar changes since the financial crisis. Neal Shear and John Shapiro, who oversaw a more than tenfold rise in revenues running the commodities division from the late 1990s, left the unit in 2008.

Olav Refvik, the mastermind behind a bank strategy to lease millions of barrels worth of oil storage tanks around New York Harbor in the 1990s, also left the firm in 2008 to join a hedge fund.

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