

CNBC

"BARTIROMO/THAIN"

INTERVIEW WITH JOHN THAIN

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MARIA BARTIROMO:

11:07:20:00

Thanks very much. Well, while I'm in Davos, Switzerland, right now covering the World Economic Forum, John Thain is in New York City. And he joins us now with this exclusive interview to talk about the events of the day. John, thanks very much for sitting down with us. We appreciate your time.

JOHN THAIN:

11:07:34:00

It's no problem, Maria. It's happy-- I'm happy to talk to you.

MARIA BARTIROMO:

11:07:38:00

Last week you were asked to step down from your job of running Merrill Lynch, just three months after agreeing a deal-- to a deal with Bank of America. Can you tell us what happened?

JOHN THAIN:

11:07:48:00

Well, Maria, I would first say I was surprised. We were only 20 days into the combination. I had agreed to stay because I thought there was a great opportunity-- for the companies. I thought the strategy made sense. And I thought I could help a lot with the transition process. And it's always difficult when you're combining two organizations. And I thought-- my ability to try to help-- with that transition and-- and help build the team going forward would be-- a good opportunity. And, frankly, the first 20 days, the results were very good. So I-- I was surprised.

MARIA BARTIROMO:

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What was the biggest surprise, from your standpoint?

JOHN THAIN:

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Well, that-- after such a short period of time and after at least-- very early but still very good results-- that-- that-- there would be a change made-- at my level.

MARIA BARTIROMO:

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John, let me turn to those results. And, of course-- most stunningly is the fourth quarter loss for Merrill Lynch, more than \$15 billion in premerger losses, \$27 billion in losses for the year. How did that happen?

JOHN THAIN:

11:09:02:00

Well, Maria, as you know, over the course of the year-- we continued to have-- positions-- that really were there when I first started-- primarily in mortgage and mortgage-related assets and-- and later in the year in credit and credit-related assets-- that-- continued to deteriorate in value. And so over the course of the year that I was at Merrill-- I was constantly shedding assets, selling assets. And then, of course, because-- they continued to fall in value, constantly having to be able-- be able to raise more capital.

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And that process really just continued-- into the fourth quarter. The-- the deterioration of the

market-- moved away a little bit from mortgage-related products into credit-related products. But-- it was really just a continued decline in asset values and particularly towards the end of the year-- really a complete breakdown in the functioning of the marketplace itself.

11:10:06:00

So cash assets completely separated from their derivatives. There were huge spreads between the prices of cash assets and credit default swaps as an example. And any type of forced selling drove asset prices down. And we were in a position of owning very illiquid things that really could not be sold and-- and had to be marked down.

MARIA BARTIROMO:

11:10:33:00

There's no doubt in I think most people's minds, John, that you arrived at Merrill Lynch and inherited a very, very tough situation. You were able to raise capital, as you said. And then you made a tough call to actually sell the firm and hopefully-- put the-- combined company in a-- in a better place over the long term. But there are

real questions-- about whether or not you allowed more risk to be taken on and if you came clean about that to Ken Lewis.

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How much of the loss of that \$15 billion loss in the fourth quarter do you attribute to those legacy losses that were already there, tough decisions that you could not get rid of, and how much of it was new position? Did you allow Montag (PH) and the trading desk to take on more risk in this troubled environment?

JOHN THAIN:

11:11:21:00

Maria, virtually all of the losses were from legacy positions that had already been there and the declined in the prices of those-- positions. Did we-- did we continue to trade? Yes. Did we put on-- big risky positions that-- were significant contributors to that \$15 bill-- billion loss? No.

MARIA BARTIROMO:

11:11:46:00

So there is no truth to any speculation that there was further risk taken on and you weren't

upfront about it to Ken Lewis and that irritated him?

JOHN THAIN:

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Well, I-- I can't comment specifically on what irritated him. But-- the vast majority of the losses in the fourth quarter were from positions that had been there since I started.

MARIA BARTIROMO:

11:12:09:00

John, were-- so you were aware of these losses then in September when you did the deal with Bank of America?

JOHN THAIN:

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Well, no, Maria, the-- the-- in September the-- the positions were there. And-- the results-- we-- we obviously don't report-- we don't report results other than quarterly. But the market-- the market deteriorated in both November and December.

MARIA BARTIROMO:

11:12:33:00

Let me ask you about what Ken Lewis and the Bank of America team knew because there is also that-- way of thinking that there was some kind of a

surprise there. They moved into your building-- a number of-- of the Bank of America people moved into the Merrill Lynch building. They were seeing the same P-- P&L every day?

JOHN THAIN:

11:12:51:00 They were seeing exactly the same information that we saw. We gave them complete access to everything that we had.

MARIA BARTIROMO:

11:13:00:00 So can you categorically say that Ken Lewis was aware of the road that was being taken at Merrill, that the losses had gotten worse because of the marks?

JOHN THAIN:

11:13:11:00 Well, let me say it this way. The-- the acting chief financial officer had come from Bank of America. He was their formal-- former chief accounting officer. He and his team, which were-- for all practical purposes, our day-to-day CFOs, they had direct access to our daily P&Ls, to our positions, to our marks.

MARIA BARTIROMO:

11:13:36:00

John, at this moment in time, is the Merrill trading book clean? I mean, how many more quarters would you expect-- toxic asset losses?

JOHN THAIN:

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Well, Maria, that would require me to predict what was gonna happen in the market itself-- which I obviously can't do. The-- as I said before, the market in November, but particularly in December, the credit markets were basically broken. Any forced selling simply drove asset prices down. The-- the correlations that should exist between derivatives and cash also broke down.

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And I would expect that those conditions that existed then will actually get better. They actually have improved somewhat in the first 20 odd days of the month. But I can't make any predictions for what will go forward in the future.

MARIA BARTIROMO:

11:14:31:00

But, I mean, would the book be clean if, in fact, we were not to see further market movements-- and-- and a further collapse?

JOHN THAIN:

11:14:39:00

Well, I-- again, I-- I-- I think the-- the way to answer that is we-- we, or-- now Bank of America/Merrill, you know, continue to have-- positions, legacy asset positions, that can create risk. I think that the dislocations that we saw at the end of December are-- are not likely to-- to-- resume but they could. So there still is risk there.

MARIA BARTIROMO:

11:15:06:00

John, let me move on to something that has certainly angered people and that is when it comes to bonuses. Merrill paid out \$4 billion to bon-- in bonuses to Merrill top players. How can you justify losing \$15 billion in a three-month period and still be paying out bonuses at a time when you were forced to-- to sell to a larger player, you're going to the government for

backstops as well as needed capital? How do you justify paying out all of that money?

JOHN THAIN:

11:15:37:00

You know, Maria, it's a very fair question. And the answer is you have to believe that there's value in the franchise. So, yes, we lost an incredible amount of money. But that loss was concentrated in primarily mortgage- and credit-related assets. We have a much broader business space. We have an entire investment banking organization.

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We have an equity trading team. We have other business that did relatively well. If you don't pay your best people, you will destroy your franchise. Those best people can get jobs other places, they will leave. So the necessity to maintain the franchise is why you really have to pay-- some amount of bonuses because, as you know, in Wall Street-- people's salaries tend to be relatively small. And their bonuses are the vast majority of their compensation for the year.

MARIA BARTIROMO:

11:16:36:00 You also have to resize the business when you're faced with new realities of the economy, right? I mean, do you look back and regret some of the high price tags you paid to lure in new talent when you first-- went to Merrill?

JOHN THAIN:

11:16:49:00 Well, you have to-- pay market prices at the time. And the world is resetting. Compensation levels are being reset. We are not gonna see the type of compensation on Wall Street-- that we've seen in the past. And-- that's a-- that's a fundamental change. So compensation levels going forward to definitely gonna be much, much lower.

MARIA BARTIROMO:

11:17:14:00 What about your bonus, John? You had a hypothetical or philosophical conversation with one or more board members before the actual board meeting when you wanted a bonus, correct?

JOHN THAIN:

11:17:26:00 Well, no, that's not exactly correct. I did have discussions with my board, as you would expect a

CEO to have, on compensation, philosophy, and-- and levels of bonus. But I also had an agreement with Bank of America that-- any bonus that I would get, if any-- would be less than-- anything that-- Ken Lewis would get.

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And that understanding really fits in with what we did with the overall levels of bonuses because we knew that we had to bring into line the Merrill-- compensation and the Bank of America compensation. So there was an agreement that if Ken Lewis didn't get a bonus, that I would not get a bonus. Whatever Ken Lewis's bonus, if he got one, mine would be less. So, of course, in the end-- Ken did not get one. And my only recommendation, the only thing I ever asked my board, was that I receive no bonus.

MARIA BARTIROMO:

11:18:28:00

You know, the way that you're-- the way that you're explaining it, John, obviously seems natural to be having these discussions with the board. Do you think you were treated fairly?

And do you believe that Ken was aware of everything you did? Or is there something else going on?

JOHN THAIN:

11:18:48:00

Well, I-- Maria, I really don't know how to answer that. You know, I think that-- I think that the transaction makes sense. I believe in the strategic value of the transaction. I believe that-- the combined organizations-- will, in fact, be successful. And-- I was certainly willing to be a part of that. And, you know, we-- we are where we are.

MARIA BARTIROMO:

11:19:14:00

Having said all that, John, after having seen the environment that you entered and the clear deterioration-- for the-- the-- the system, the industry, do you regret selling Merrill to Bank of America?

JOHN THAIN:

11:19:29:00

No, not at all. I think there is-- no question that-- the decisions that we made on that weekend in September were the best interests of Merrill

shareholders, were in the best interests of Merrill's employees. And I do not regret for one moment-- initiating that first phone call with Ken and ultimately getting this deal done over that weekend.

MARIA BARTIROMO:

11:19:54:00

Would Merrill have been better off-- or I would-- I-- I assume you're gonna say clearly-- had Lehman not gone done? Was it a mistake that there wasn't a savior there for Lehman Brothers?

JOHN THAIN:

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Well, I think there's no question that the bankruptcy of Lehman Brothers is what forced us to search for an alternative-- to simply staying independent. The consequences of the Lehman bankruptcy-- were-- tremendously negative in the marketplace.

MARIA BARTIROMO:

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I know that those talks from some of the members in that room were-- were heady and-- and-- and there was that moment when everybody realized they were all in this together-- that the

implications of a Lehman bankruptcy would be severe. How much pressure did you get from Paulson and Geitner to do a deal? We all know that they basically orchestrated a number of deals in this.

JOHN THAIN:

11:20:48:00

Yeah, Maria, I think it-- I depends a little bit on the timeline. And there's been some-- I-- I think-- inaccuracies in-- that have been reported about this. It became clear on Saturday that it was unlikely that-- Lehman was gonna be rescued or that a deal could be put together-- that was going to work, although the-- the conversations had been-- were still continuing.

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And the first-- set of discussions that I had-- with Ken-- were really not pressured by anyone. As a matter of fact, I was a little bit concerned because at least at the time there was some hope that Bank of America would still pursue Lehman. I didn't want, in any way, to-- to-- make that transaction less likely. But when I first talked

to Ken it's obvious that he was not gonna pursue Lehman without-- government assistance, which at least did not seem to be forthcoming. And so we began our discussions on Saturday.

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When-- when Secretary Paulson and-- and-- and Tim Geitner became aware-- that we were having those discussions-- they were very encouraging of those. And they definitely wanted to make sure that I found a solution-- that weekend-- because they were concerned what the consequences might have been to Merrill-- following the Lehman bankruptcy.

MARIA BARTIROMO:

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John, I wanna ask you more about the-- the-- environment that we're in. But I've gotta ask you-- first about the office. You spent more than \$1 million renovating your office; is this true?

JOHN THAIN:

11:22:21:00

Well, first of all, it-- it is true. This was a year ago or actually a little bit more than a

year ago in a very differ-- different-- ec-- economic environment and a very different outlook for Merrill and the financial services industry. It was my office. It was two conference rooms and it was a reception area. But it is clear to me in today's world that it was a mistake. I apologize for spending that money on those-- on those things. And I will make it right. I will reimburse-- the company for all of those costs.

MARIA BARTIROMO:

11:23:01:00

Why did you need to renovate the office? What was wrong with Stan O'Neil's (PH) office?

JOHN THAIN:

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Well-- his office was very different-- than-- the-- the general décor of-- Merrill's offices. It really would have been-- very difficult-- for-- me to use it in the form that it was in. And-- you know, I-- it needed to be renovated no matter what. It would have been better for me to simply-- I should have-- simply paid for it myself (UNINTEL).

MARIA BARTIROMO:

11:23:36:00

So it is an environment where jobs are being cut and clearly salaries are being cut. And the firm is reporting all of these losses. At-- at-- did I occur to you at some point over the process to say this is probably not the best judgment, I better put this off? Or, I mean, clearly not but when did you start feeling like perhaps it would have been a-- a sore thumb? Or were you totally blindsided by it?

JOHN THAIN:

11:24:01:00

Well, Maria, remember, this was back in-- it really started in December of '07. So the financial industry hadn't melted down yet. I-- I had every expectation-- that-- Merrill Lynch would be a large successful company-- that-- these office renovations-- would be used by me for many years in the future. And we were also doing lots of other things-- to-- to bring down costs. So in-- in-- with 20/20 hindsight, it was a mistake. And-- and as I said, I-- I'm sorry that we-- that I did that. And I'm willing and

I-- and I intend to fully-- reimburse the company.

MARIA BARTIROMO:

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So, John, it-- it sounds like as far as the loss, the \$15 billion in the fourth quarter, Ken Lewis and his team knew about it. As far as the bonuses, did the board approve those bonuses?

JOHN THAIN:

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Well, let's-- let's go back a second to the-- to the whole-- discussion of bonuses. It was always contemplated, even in our merger agreement, that we would pay bonuses at the end of the year. And just like the discussions of my own-- potential bonus-- we were very transparent and coordinated with Bank of America about the aggregate levels of bonuses that we would pay.

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So they were completely plugged into what the total amount of discretionary bonuses would be. We actually changed the cash/stock mix-- that that-- we would normally have used. We normally would have used 60 percent cash, 40 percent

stock. They asked us to move it to 70/30, 70 percent cash, which we did. And the-- the timing of the payments-- including the portion that was cashed and the portion which-- which-- which was stock.

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And remember the stock part was Bank of America stock. So there was complete transparency and complete agreement-- with Bank of America as to what levels the-- that bonus pool would be and how it would be paid out. The-- compensation committee of Merrill Lynch's board did approve those. And ultimately, the-- it was ratified by-- by the entire board. And so there was-- there-- there was complete transparency here.

MARIA BARTIROMO:

11:26:16:00

And you-- did you-- say that to Ken Lewis when you had the discussion in your office last week? I mean, did you ask him, you know, all of this was known, the board approved? What was the reasoning for asking you to step down?

JOHN THAIN:

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Well, the-- the-- the conversation was very brief. And-- we-- we mutually agreed-- that-- that this wasn't working out.

MARIA BARTIROMO:

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John, I know that-- we-- we focused a lot and it's been-- it's been a tough-- weekend and a tough-- certainly-- couple of months-- as far as the integration. I saw some of your quotes-- recently about that. Let me switch gears and just ask you-- broadly where we are right now. Do you think the worst is to come for the-- for the industry? Or have we seen the worst?

JOHN THAIN:

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Well, as-- as you know, throughout the course of 2008, everyone who predicted that we were in the seventh inning or eighth inning or ninth inning was wrong. And-- I would say that the economic environment continues to be very difficult. The U.S. economy is still contracting. Housing prices are still falling.

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So there still is significant downward pressure-- asset prices. And the combination of falling asset prices and a-- and a weakening economic environment are all bad for the financial services industry. That being said, there has been at least a little bit of improvement-- in the credit markets-- in the first part of January. And, you know, I-- I think we are definitely not out of this difficult period.

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As a matter of fact, I think 2009-- the entire year are going to be difficult. But-- it's-- it's hard to imagine that things could be worse than they were in 2008. And I certainly hope they're not.

MARIA BARTIROMO:

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What are your plans now, John?

JOHN THAIN:

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Well, because as you started this interview I said this was a surprise to me on Thursday, I-- I haven't really thought much about that yet.

MARIA BARTIROMO:

11:28:22:00 John, thanks very much for joining us today. We
so appreciate your time.

JOHN THAIN:

11:28:25:00 Thank you, Maria.

11:28:29:00 (OFF-MIC CONVERSATION)

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