Peter Spacek for Barron's

The Way It Was

The sun has set on options-trading cowboys

BY RICK ACKERMAN • The job would have sounded too good to be true if it had been advertised in the classifieds: "Be Your Own Boss. Work six hours a day, and in just a few months make the kind of money that plastic surgeons, malpractice lawyers and even movie stars make. Ski Telluride and Gstaad, hunt for seashells in Madagascar, explore the jungles of India in a *howdah* and perfect your tan in Cabo San Lucas, all while you rake in the big bucks. Just a few thousand dollars will get you started. No experience necessary."

While such an ad never appeared in any newspaper, the job itself was real enough. In fact, the guy who came one day to find himself riding in a *howdah* – an Ivy League biology graduate, as it happens – made about $1.5 million when he was traveling from Jaipur to Agra. He didn't know he'd struck it rich until he phoned the office the next day.

Like all opportunities that sound too good to be true, however, there was a downside: In this job, you could lose more money before breakfast than Marlon Brando gets paid for a walk-on.

The business was derivatives – specifically, listed put and call options – and the license to create them out of thin air and sell them to the public was for a while the quickest route to riches since the California Gold Rush. It was possible to start a business for $10,000 that could generate 10 times that in a year. It didn't take long for the word to get out.

Options mania at first attracted to the Pacific Stock Exchange the kind of fortune-seekers who a century and a half earlier wouldn't have thought twice about trading an apron for a pickax and heading West. Like the Forty-Niners, the new speculators on the PSE were a remarkably diverse bunch – real-estate developer, trucker, Marine, electrician, cab driver, physicist, movie maker, policeman, dry cleaner, ad man, bartender, lawyer, sport fisherman, potter, lifeguard, restaurateur, engineer, guitarist, physician, card counter, stockbroker, tow-truck operator, hod carrier, ski bum, fireman, architect and chess master. They were all down there, plus a few drug dealers to buffer the mix.

It was hard to stand out in such a crowd, but a few did. One trader of legend, whose net worth caromed spectacularly – and frequently – between negative and positive seven figures, had begun his professional life as a catcher for the Washington Senators. His spittoon was a fixture on the options floor and was avoided as though it contained some recombinant mixture of smallpox and plutonium. Another trader was said to have been a mercenary – a soldier of fortune who'd seen action in some equatorial sweat box where war had raged for 50 years.

There were also a few women traders. On the exchange floor, where shrewdness and guts were all that counted, women could play as equals, and did. Chivalry existed only to the extent it was considered bad form for a male market-maker to challenge a female to step into the alley. It was considered good sport to cuss them, though – at least until a notorious 10-letter word was misapplied to a female broker who evidently did not take herself to be one of the guys. After that, too-salty language became a fineable offense.

Male or female, most successful floor traders have a few traits in common. They possess the steel-trap mental reflexes that one associates with the best gin and backgammon players, which quite a few of them are. The skilled trader can also hear as a conductor hears, filtering out extraneous noise and tuning in only the relevant voices when necessary. After a few months' practice, traders can read price monitors from a distance that would cause a fighter pilot to squint. They have the stamina to stand for six hours without a break and the vocal cords to shout all day long 200 days a year. Predictable occupational hazards include hemorrhoids, mild deafness, failing eyesight, ulcers and fallen arches. A few traders in their 40s have died of "natural" causes. A few committed suicide. And another was driven by financial adversity to attempt the robbery of an Alameda bank, neglecting to consider that all conceivable escape routes from this island community crossed bridges.

A few who struck it rich on the floor of the Pacific seemed to possess neither brains nor stamina. One story that made the rounds concerned the novice who, first time out, sold 200 contracts, thinking the transaction had left him short the equivalent of 200 shares. Actually, it left him short the equivalent of 20,000 shares, but by the time he learned of his stupidity, the stock had dropped just enough in his favor to make him a quick $15 thou.

When the PSE Options Exchange opened for business in 1976, it was not difficult to make lots of money. It was a seller's game then, and the risk premium that professionals received, mostly from public customers, for their puts and calls was in retrospect exorbitant.

Those were the days when floor traders were predators, the public their prey. Ten years later, when the retail trade had largely abandoned an almost unwinnable game, the floor traders themselves became the prey of institutional sharpies – the "big boys." The floor brokers who handle their business are as subtle as belled cats but, surprisingly, the mice still want to play. If you've ever laid out more than five bucks trying to knock the milk cartons over, you know the temptation the market-makers face each time Morgan's broker walks into the pit with an offer that sounds too good to be true.

Of course, it's still possible to make plenty of money on the options floor. But it's a very different sort of game. During the 1980s, success slowly began to skew toward the rocket scientists. Now, being a rocket scientist isn't enough; you need to be a rocket scientist with megabuck backers merely to play even-up with the big boys.

Ultimately, the days of floor trading are probably numbered. The rocket scientists are taking their action upstairs, where they can better apply certain refinements of the information superhighway to the business of picking off their old buddies still in the pits. Moreover, federal regulators are giving a strong push to new technologies, in the belief that quickening and broadening the dissemination of price information will create better put and call markets.

Perhaps. But it is worth considering that even though traders shouting and spitting in each others' faces to effect commerce may seem like a bottleneck in the otherwise cybernetic loop of securities trading, it is also one of the last reality checks left against the ethereal drift of global finance. When the cowboys have all hung up their guns and retired to computer rooms, the Code of the West may have breathed its last. ■

RICK ACKERMAN, a former newspaper reporter, hung up his trading jacket in 1991, after 13 years on the options floor of the PSE.