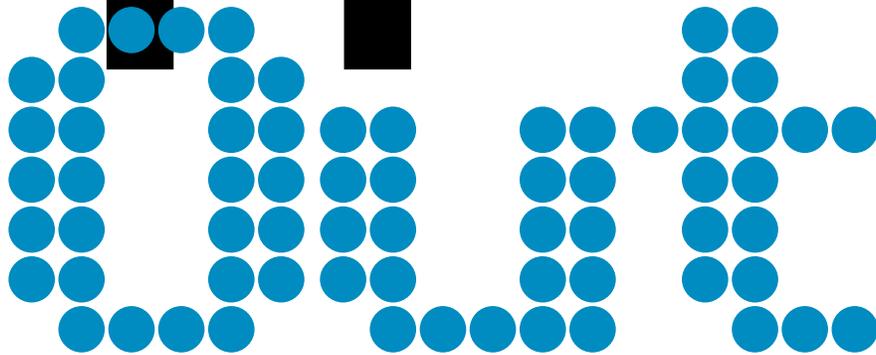


Flipping



Is **Paul Rotter** a devious market machinator or a victim of his own success? The biggest trader on the Eurex and the most controversial man in electronic trading speaks out

By Imogen Rose-Smith ■ Illustration by William Duke

JUST BEFORE CHRISTMAS,

a group of around 30 London prop traders gathered in a comfortable suite at the Guildhall complex for a seminar being given by fixed-income analytics firm GannCorner. A handful of locals began chatting about a notorious Eurex own-account trader known in European trading circles by a not-so-flattering nickname, “the Flipper.”

Over the past year, dozens of prop traders had engaged in a sporting manhunt aimed at uncovering the identity of a mysterious, supposedly Ireland-based trader accused of steering German government-bond futures markets in a tactical manner — posting substantial

lot blocks, not all of which are traded upon, and doing so on both sides of the order book in numerous but nonetheless interconnected markets — that birthed the Flipper moniker. Using the anonymity afforded by the cyber realm of screen-based dealing, traders say, this unknown figure lured others into a costly game in which he held the cards, through sheer volume and shrewd maneuvering.

Eventually, in a fervent chase akin to the decades-long search for the identity of Woodward and Bernstein’s Deep Throat, a single name had emerged. Right before the GannCorner seminar was about to start, one attendee asked the firm’s Juliette Clark, the



woman who was leading the session, if she had ever heard of Paul Rotter.

“Yes, I know Paul Rotter,” Clark said plainly. “He’s one of my clients. And he’s sitting right behind you.”

Agog, the roomful of traders spun around in unison. They couldn’t have been more shocked if Queen Elizabeth herself was sitting among them wearing a tube top and leather chaps. Rotter, a clean-cut, smartly dressed 32-year-old, sat quietly waiting for class to begin.

That an unassuming guy like Rotter could rise to such infamy in the electronic-trading world while remaining such an enigma is testimony not only to the power of suggestion but also to the complexities and rivalries within this burgeoning global arena. In this world, Rotter is a lightning rod. The mere mention of his name — or his nickname, for that matter — among Eurex traders can inspire bilious hatred, reverence or even fear. To those who despise him, Rotter’s strategy is upending livelihoods and undermining the Eurex. His fans call him the single most successful individual futures trader on the planet.

Rotter dismisses the tempest out of hand. “There’s just this one group of unlucky

people, two of whom are traders. Currently he’s managing outside money on behalf of wealthy individuals and some institutions (the minimum investment is €1 million), but he won’t say how much.

All of this success has coincided with the rise of the Eurex, the German/Swiss electronic futures exchange, which has taken international derivatives trading by storm since its creation in 1996. A Czech native who moved to Germany at age 9, Rotter started out as an apprentice on the bond desk of a German bank in Frankfurt. Borrowing from a corporate credit card, Rotter quickly went broke buying options, only to resurface in the Frankfurt office of Daiwa Securities.

Nearly bankrupt, Rotter worked his way up, and within two months was trading the *bund* in lots of five, crafting his own style with little guidance from his superiors. By the time he left the bank in 1996 for Dublin-based Midas Trading House, Rotter was already the biggest single trader in German debt futures on the DTB, Germany’s precursor to the Eurex.

“We couldn’t believe our eyes when we saw how quickly he’d change positions from

without ruffling some feathers. “Paul has sometimes played a controversial role,” Kinski acknowledges. “Some traders didn’t like him because he was changing his position so quickly.” In 2001, Rotter formed Rotter Invest and eventually moved his operations to Zug, Switzerland, an affluent town that’s home to its share of traders — and its share of notoriety: For the past two decades, it has also been the home of fugitive financier Marc Rich.

IT WAS EARLY 2004 when traders of the *schatz*, short for the German two-year note, or *bundesschatzanweisungen*, began noticing something funny happening on their screens. “You would see giant orders on one side of the market that would flip and go the other way,” says one Eurex trader.

The traders, and a former Eurex official, say someone was posting massive buy orders, waiting until the market moved toward that price and then selling instead — a massive head-fake. Many believed the alleged Flipper was playing the same trick on the German five-year notes (known as *bobles*) and 10-year notes (*bunds*). “The Flipper does so much volume in the *bund*,

“I probably stepped on the tail of some

traders in London who somehow found out that I’m doing the most volume in Eurex debt futures,” says Rotter, who until now has remained silent about the “Flipper” issue but agreed to conduct a series of interviews with *Trader Monthly*, appropriately enough, electronically.

“They’ve tried to blame me for their trading losses,” he says of the people he calls “funny guys.”

But many locals aren’t laughing.

BY ANY ALIAS, the mercurial Rotter is a hugely successful trader. Though he wouldn’t confirm any compensation figure beyond saying that he takes in more than \$5 million per year, some say he pulls down at least that much per *month*. He’s a surefire candidate for this year’s *Trader Monthly* 100 list. His Switzerland-based firm, Rotter Invest AG, employs a dozen

one side of the book to the other,” recalls Oliver Kinski, a former managing director with Midas and the man who hired Rotter. In January 1998, Kinski, Rotter and some other traders formed a Dublin-based prop-trading firm, Greenhouse Capital Management.

Rotter’s balls-to-the-wall modus operandi helped Greenhouse prosper, but not without some tense moments. The firm began life with \$1.3 million in seed capital and featured, in addition to Kinski and Rotter, two other standout own-accounters, Pino Curcio and Florian Albrecht, the latter one of Rotter’s closest boyhood pals. As a unit, they worked well together, though Rotter was clearly the star. “It was do or die,” Kinski recalls. “We knew Paul would have these large positions — in one day we could have been out of business.”

By the end of its first day, Greenhouse was up \$526,000. Within three months the firm had made \$6.5 million, though not

the *boble* and the *schatz* that he’s able to influence the whole yield curve and catch people out,” adds another outraged trader. “The Flipper *is* the market.”

If a trader posts a bid on the Eurex and someone hits him for it, according to the rules of the exchange, the trader is duty-bound to honor the transaction. There is, however, nothing to stop a trader from posting a price for a large volume and then taking it down if no one bites. And while it is illegal to trade with oneself, it is perfectly OK to switch back and forth between the bid and the ask. The only requirement is that the trader be sufficiently well-financed to honor the bid if someone hits him up for the entire lot (the par value of one underlying *schatz* bond is €100,000).

Rotter admits to handling large volumes on both sides of the book but insists he was not trading the *schatz* inappropriately. He says his trading style — best described as

aggressive scalping, only done on a massive level — benefits the market. “I am a kind of market maker who provides liquidity with many orders in different markets,” Rotter says. “When I’m active, I am permanently involved in market transactions through fills at both sides in different contracts.”

Rotter stresses he never pulls orders quickly but rather “leaves an order working for a couple of minutes.” He also insists there are other big fish, and therefore it’s unfair to attribute every large post to him.

“The problem for the locals,” says the former Eurex official, “is that the herdlike mentality they learned in the pits is very hard to break. And the Flipper was taking advantage of that trading style. A lot of the locals probably made a good deal of money in the pits just following the crowd, and now they can no longer do that.”

Rotter, characteristically, is more blunt: “I probably stepped on the tail of some monkey who was making great money on the *schatz* and couldn’t compete anymore,” he says.

MANY TRADERS ARGUE that placing offers on the market and then canceling them is a bush-league ploy some-

led by prop trader Chris Eldred, took the investigation into their own hands. Rumors began spreading among Eurex traders in London that the Flipper was actually an own-account trader in Dublin (they apparently didn’t get his change-of-address cards) who was making nearly \$7 million a month trading German debt futures. (Eldred declined to comment.)

“They somehow found out that I am doing the most volume in Eurex debt futures and made me responsible for their losses,” Rotter says. “Eldred invested so much time writing in forums, talking to Eurex officials, sending me e-mails, crying and talking about market ethics. He could have made millions in the market in that time and with that effort. But he is probably a monk and is not interested in money.”

IT TAKES A mighty big trader to personally prompt a market to change its tick size or value. Yet Rotter may have done that. While Eurex wouldn’t comment on the possibility of one trader or a group of traders gaming the system, one of the key selling points of electronic exchanges is

more attractive. A trader who met with Danielski and the Eurex to discuss the Flipper insists he was specifically told that the change in tick size of the *schatz* was implemented in an effort to thwart the Flipper.

These two views can be reconciled: The former Eurex official explains that while the new tick policy, which went into effect this past June, was in the works before the complaints emerged, the timing of its implementation was in part influenced by the hue and cry over the Flipper. For his part, Rotter says he was never contacted by the exchange as part of any investigation.

Regardless of the reasons behind the tick-size change, it seems to have worked: Rotter soured on the *schatz*. “After the *schatz* went to half-ticks, I almost completely stopped trading it,” he says.

NOT ALL TRADERS view Rotter as a villain. “There is no Flipper,” says Eurex trader Martin Duncanson, who has been impressed by the Czech’s strategy. “I personally think that what Paul Rotter has achieved as a trader should be everyone’s ideal — starting as a small guy and building up to

monkey who couldn’t compete.”

times referred to as “spoofing” — the spoofer has no intent of trading at that price; rather, he’s simply showing a sizable offer to entice traders to take the other side just before canceling. Rotter counters that he’s able to trade at the prices he’s offering, per the exchange rules, and his volume shows that he’s more than willing to follow through.

For an individual, Rotter’s scale is stunning. Last year, his personal trading volume alone accounted for about 180,000 contracts a day, or almost \$70 billion on peak days, dwarfing all but the very biggest institutional players. “My average market share in the German *bund* was around 10 percent for many years,” he claims (the *bund* is the world’s second most-traded futures contract after the Eurodollar). “I didn’t trade the *boble* and the *schatz* that heavily; I used them mainly for hedging purposes.”

Yet until recently, few even knew Rotter’s name. A group of London own-accounters,

their claim that they’re a more level playing field. The Eurex needed to act.

According to a well-placed market participant, many locals and at least one investment bank, ABN AMRO, complained either formally or informally to Eurex. Neither Eurex nor the bank would confirm any involvement in the dispute, though a source with knowledge of Eurex operations says that Ralf Danielski, head of global fixed-income products there, has been personally involved in handling complaints about the Flipper. Danielski declined comment.

Last April, the Eurex announced it was halving the minimum tick size for price movements in contracts on the *schatz* from €10 to €5. According to a Eurex spokeswoman, the change in tick size had nothing to do with complaints over alleged market shenanigans, but instead was designed to reduce hedging costs by producing tighter spreads — thereby making the bond future

a huge size. I admire his success.”

Yet there is a part of Rotter that obviously enjoys the role of market bogeyman. He began receiving antagonistic messages last March as rumors of his identity emerged. “There were some anonymous letters and some phone calls,” Rotter says. One e-mail he was sent read, “I hope you have to spend the rest of your days looking over your shoulder.”

Rotter says the threats just turned up his heat. “Of course it was motivation for me to get more involved in the markets and set more competition for these funny guys,” he says. Simultaneously, however, he insists that he’s taking things a bit easier now. “I have pretty much reached all my goals,” he says. “I don’t want to spend all day in front of the screen anymore.” The 32-year-old who has spent as many as 11 consecutive hours in the market now says he’s down to around four hours a day.

Then again, he might be bluffing. ■