Oral History of Jack Wadsworth, part 2 of 3

Interviewed by:
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Hancock: Welcome back, Jack Wadsworth, to the Computer History Museum.

Wadsworth: Marguerite, thank you. It's good to be back.

Hancock: Part one of your interview was so interesting that we're going to continue your story. My name is Marguerite Gong Hancock here on behalf of the Exponential Center and today is April 15, 2019.

Wadsworth: Tax day.

Hancock: Tax day. So we wanted to just dial back and make sure that we caught some details about one very important story, the Apple IPO, and ask a mystery question, which is what is the significance of the blue ink in the Apple IPO story?

Wadsworth: The blue ink. So I was new to Morgan Stanley. The meeting on the organization for the Apple IPO took place in early 1980 and I had joined the firm in 1978. Morgan Stanley, being Morgan Stanley, has many traditions that go deep into its roots. And one of those traditions, I think probably Mr. Morgan decided, is that the cover page of a final prospectus would be a certain color of blue ink and in Ronaldson Slope as the type style. And so while this was important to Morgan Stanley and I was embracing the traditions of the firm, the whole idea was a bit off-putting to me not having been steeped in that tradition. But I knew I had to uphold the traditions of the firm.

So we got to the organization meeting, first meeting on the Apple IPO, and it was Larry Sonsini, it was George Quist, it was Steve Jobs, it was me. It was then a cast of the usual accountants and other lawyers, etc. As the meeting began, Steve pulled out of his pocket his rendition of a cover page for the prospectus and it had black ink, it was in Goldman Sachs type style, and it had a colored apple at the top with a bite out of it. The then-traditional apple was only the multicolored apple with the bite out of it; there were no other variations on that theme in 1980. So I was on the spot and I said, "Steve, Morgan Stanley has a tradition," and I pulled out of my pocket the Morgan Stanley cover page, which was blue ink in Ronaldson Slope and no apple on the front. We did not accept any logos of any kind in those days on the cover page of a prospectus.

Hancock: So how did he respond?

Wadsworth: He said, "Jack, this is our prospectus, it's my company, and we will have my cover page." I said, "Steve, you will find this hard to believe but this is a deal breaker." And he said, "Well, this is a test." So I packed my briefcase and walked out in the lobby fully prepared to go to the airport. He came out into the lobby and he said, "I apologize. We will have your cover page." What I learned later was that as I left the room, and thank God for George Quist, Steve turned to George Quist and said, "George, is he serious?" <laughs> and George said, "I'm afraid he is." So we had a handshake in the lobby and I remember saying to him specifically, "Steve, thank you. This is a test and let me promise you that if there is some day in the future when you do another transaction and the reputation of Apple exceeds the reputation of Morgan Stanley, we will have your cover page." He said, "That's a deal," <laughs> and I think he made it. <laughs>

Hancock: I'm so glad you shared that story. While we're on the subject of Steve's stories about you and Steve, are there others that we might have missed? They're so emblematic of these decisions that you were making.

Wadsworth: Well, the story goes on through the IPO.

Hancock: Let's follow that thread.

Wadsworth: Yeah. Another incident that is so typically Steve Jobs: the first stop on the road show was in Cork, Ireland, and I can promise you there were no investors in Cork, Ireland. But Apple had built an assembly plant there, so we had to go see it, and we had a lunch and a presentation. One of the members of our team was a Baker Scholar graduate from the Harvard Business School, a woman who was in her first year as an associate. We were getting on the bus and Steve said to this young associate, "I forgot my laundry. Will you go get it please."

Hancock: Uh oh.

Wadsworth: She did. And after the deal was over she resigned from the firm <laughs> and she told me, "That's not a good way to treat a Baker Scholar, Mr. Wadsworth, or any woman for that matter." That was Steve. In the road show meeting in Zurich-- I may have mentioned this before-- we said in every meeting that the deal was oversubscribed, that we were looking for long-term investors, that was the objective in our book. And a money manager in Switzerland raised his hand in the back and said, "Mr. Wadsworth, if you're looking for long-term investors the only way to accomplish that is to have the stock trade down 20 percent after you price it." <laughs>

We decided that was not a good idea. And in the final pricing, it was $22 a share. We had an extensive negotiation and there were possibilities that it would be lower, the usual back-and-forth about how good is the book and so on. I remember I was in New York and we had a conference call, and on the other end of the call in California were Mike Markkula, Mike Scott and Steve Jobs. There was a moment of silence after I said, "$22 a share" and it's the only time that anybody on the company side of a deal said, "God bless you, Jack," and it was Mike Markkula. <laughs>

Hancock: It was Mike?

Wadsworth: Right. <laughs> So that was the deal, and then came the closing dinner with lots of stories. Reflecting back on that moment in history for Apple, it was a small company, 115 million dollars in sales. We had expectations that they would grow 20 to 30 percent in 1981. They delivered precisely what they promised, and in the 12 months following the deal you could have bought the stock at 28 or 12, which is fairly typical.

I don't know if I told the banned in Boston story**,** but at the closing dinner we presented a certificate that said "Banned in Boston" across it, a giant-sized certificate. Every IPO has to be blessed by blue sky commissioners around the country and you can't offer in that state until you get their blessing. But the blue sky commissioner in Massachusetts decided that the price range, which was 20 to 22, was too high and it was too risky for investors, so he declined to clear the offering in Massachusetts. In the week after the offering when the stock went to 28, there was a human cry in Boston, not public demonstrations but articles in *The Boston Globe*. One week later the blue sky commissioner changed his mind, cleared the prospectus, permitted Massachusetts citizens to buy at 28 instead of 22. <laughs> Classic.

Hancock: Classic.

Wadsworth: Right.

Hancock: As you think back about Steve and your interactions with him, you shared a lot of the happier times. But along the way there were also difficult conversations and decisions. Do you have any stories along those lines as you worked out how this was going to turn out?

Wadsworth: Honestly, there were lots of complicated due diligence conversations, which is fairly typical for a young company. And lots of disclosure statements that were negotiated at length that were designed to say, "Don't buy the stock; it's very risky." I suppose one of the contentious issues along the way was a man named Charlie Finley who owned the Oakland A's and had bought some stock from some employee at Apple privately. He wanted to have a big allocation in the IPO and he didn't have an account at H&Q or Morgan Stanley. It was not within the purview of our rules to allocate any stock to him, and he filed a lawsuit claiming that he was being mistreated for not getting an allocation in the IPO.

Hancock: What was the timing on that?

Wadsworth: It was between the filing and the pricing, so it was in the red-herring period. I think Steve was confused. We had a lot of arguments and discussions about it. Charlie Finley was a prominent guy and a friend of Steve's. And in the end what we agreed to do was to print the entire lawsuit in an amended registration statement. I would say that's again outside of the box, a first, I've never seen it done before, but it certainly shut up Charlie Finley; <laughs> it embarrassed him as we hoped it would. <laughs>

Hancock: So this deal was not only a landmark for the company, but you were thinking out of the box all along the way and that was a precursor of things to come. Anything else we should talk about with Apple before we move on to Japan?

Wadsworth: I would say it was of great satisfaction to me that Steve and Mike Scott and Arthur Rock and Peter Crisp, all the people who were insiders to Apple, became close personal friends; there was a tremendous amount of respect going both ways that came out of that. As a consequence, Steve became a very good friend and I lived with him through his dismissal, through the next episode. I tried to help him finance NeXT. <laughs> He called me once after I'd gone to Hong Kong and said, "Jack, I've made an investment in this amazing company called Pixar; it's a software company and I want Morgan Stanley to take it public." I said, "Send me all the stuff," and he did. I called him back a week later and said, "This is not a software company, it's a movie company, and Morgan Stanley doesn't do movie companies. But I think you should call Sandy Robertson," which he did. In fact, Tim Cook said to a friend of mine about six months ago in a conversation about me, "Jack Wadsworth is one of the few people who stayed with Steve after he was fired." That to me is a great compliment. So it's a long story and a good story until he finally fired me from the board of Pixar, and that's another story.

Hancock: I think we'd better hear that one too.

Wadsworth: <laughs> Okay. Well, when I retired from Morgan Stanley and left Hong Kong I promised myself a number of things, one of which was that I would not go on the boards of any public companies for a lot of obvious reasons. I'd been back in San Francisco for about a year, and Steve called me one day and said, "I want you to go on the board of Pixar." I said, "No," and he said, "No is unacceptable."

We then had one of those walk-arounds, which he is famous for, over in Emeryville around the Pixar Building. Out in front of the Pixar Building is a green-grass amphitheater for gatherings of Pixar employees, and at the end of our walk we sat down on one of the seats in the amphitheater and he looked me square in the eye and he said, "Jack, Pixar is a very precious company; it's really important to me. We can make two movies every four years and we can't scale at that rate. I don't want to buy a company and I don't want to be bought. I want to grow organically, and Morgan Stanley is the only very complicated organization that I know about in history that has scaled organically. With your experience you're the only person I can think of that can come and help me scale Pixar." And you can imagine, he hit just the right button. I melted, and I said, "Oh, my God, okay." <laughs>

Well, fast-forward four years later after many board meetings and a lot of stimulation and exciting and interesting stuff. Ed Catmull who was the CEO really was the science guy who'd done a lot of the animation stuff, and John Lasseter was just a delight to be around, an incredible genius, creative guy. To this day, I think they're running the animation studio at Disney for sure and they've never made a bad movie. II don't know of a record like that anywhere.

But as I was an investment banker, you'd not be surprised to hear I was on the compensation committee and the audit committee. Those are the two worst committees to be on. It didn't take very long for the SEC to mount an investigation after one quarter's earnings forecast, which was wrong, and forecasting movie-company earnings is almost impossible and very complicated anyway. That was stressful, and then Apple was dinged for backdating stock options and the state attorney general assumed that Pixar would be in the same category. As chairman of the compensation committee I had to hire my own lawyer to defend myself and the company. In the final analysis there was absolutely no question about the fact that Pixar was squeaky clean, but in that process there were a lot of conversations about what to do to make it better and change things. Steve and I had a number of fairly stressful disagreements. He called me one Sunday and said, "Jack, you're not going to stand for reelection to the board," and we never spoke again. That was a very sad day and not atypical of Steve, but that was the end of that. And so my instinct was right, <laughs> I made a mistake joining the board. <laughs>

Hancock: It took four years to--

Wadsworth: <laughs> Right. Anyway--

Hancock: These details are very interesting. I'd like to now turn to Japan. We were talking about Japan before and we really want to make sure we ask those key questions. How did you persuade Moody's to do this, to get this kind of a rating when the country was having such serious financial issues? This was 1970--

Wadsworth: Five.

Hancock: 1975. Right? So how did that happen?

Wadsworth: Well, okay. The oil shock in 1973 devastated the Japanese economy because of their need to import oil, and so in 1975 all the financial parameters were negative. They had I think $12 billion worth of foreign-exchange reserves, about 25 billion of short-term debt in the Euromarkets through the banks, 30 percent inflation and a serious balance-of-payments problem. That's a classic profile for a country or a company that needs to raise money so—

Hancock: What were--

Wadsworth: --the investment banker is trying to figure out what to do. Now, prospectuses by and large are not very important, but every now and then something happens that is a poignant moment that is critical in describing a situation, and in Japan this was the case. I'd spent four weeks in Japan, and when we got there the focus was on the rating. There is a sentence in the prospectus that basically says, and I will paraphrase, "Important decisions in Japan are reached by consensus" and then there was a definition of the word "consensus," which was as I recall "sustained concentrated focus on the issue." Then it said, "In Japan there is a consensus among the government and business that economic growth is the most important objective for the country," and then it went on to talk about the homogeneous population of Japan and how that consensus, if arrived at at the top, could be executed by the country and the leadership. And I honestly believe that that concept at that time, which was then, and probably still is, in many ways unique to Japan, it's a strength and it's a weakness, was one of the important factors that led Moody's and Standard & Poor's to the conclusion that it was a good bet.

Having said that, because of the precarious financial structure of the country, even though the banks had this exposure in the international markets, they were publicly traded, widely held and there was no guaranteed central bank or government support for the banks. So it really was up to the Ministry of Finance to give assurance that the banking system would remain sound. Along with this consensus idea, the critical, critical question was would the Ministry of Finance ever let a Japanese bank fail? And so we got to the last dinner at a Western restaurant and Tariochi Yoshida, the vice minister of finance who was in charge of the project, and the most senior official in the government involved in the project, had been told by me that he would be asked this question at some point and he better have the right answer. And in the middle of dinner Brent Harries-- I can't believe that he actually went to Japan-- he was the chief executive officer of Standard & Poor's and a kind of boisterous New Yorker but smart-- and he said, "So Vice Minister Yoshida, will the Ministry of Finance ever let a Japanese bank fail?" and Yoshida-san put his knife down and his fork down and he crossed his hands and he looked at Brent Harries and he said, "No." <laughs> Brent Harries had a little piece of paper he was taking notes on, and at that point he wrote down the name of the restaurant, the location, the date, the names of everybody at the table.

Hancock: That was it.

Wadsworth: That was it. <laughs>

Hancock: That kind of assurance sets it apart, doesn't it?

Wadsworth: Right.

Hancock: So with looking at Japan this led to all this work. Can you give us an overview about what you built in Japan, that once you started it the gates opened; you grew rapidly? Can you just give us a summary of what you did there in Japan?

Wadsworth: Well, first of all from 1975 to 1987, when I went to Japan to start Morgan Stanley's business in Asia, Japan had delivered on those promises. I look back on it, that's an amazing moment in many ways for Japan because they delivered, and the reason they delivered is that it was an era that played to Japan's greatest strengths. MITI would chart the future needs for industry and the Ministry of Finance would tell the banks what to finance. There was essentially no equity market or bond market, so it was all kind of a closed circle of a consensus among government and business on what was right. They chose steel and autos and things that could be made in mass production. And it led to an incredible period of economic growth, and in many ways domination, for Japan in the world markets in the products that they chose. So there was book after book written in the '80s about, "Japan is a zero-sum game, they're going to take over the world" and—

Hancock: Japan, Inc. Right?

Wadsworth: Yeah, Japan, Inc. So when I got to Japan in 1987 the 15 largest banks dominated the financing market because there was no bond market. Nomura, Daiwa, Yamaichi, and Nikko had 60 percent of the volume on the Tokyo Stock Exchange. So as a little guy from New York contemplating what in the world am I going to do for a business strategy to make money in Japan, it was daunting. And Mike Armacost who was then the ambassador to Japan had a meeting once a month in his office where he gathered the leaders of American business: DuPont, General Motors, Ford, etc., and little old Morgan Stanley.

I remember at the first meeting I contemplated what to say when he posed the question, "Okay. I want to go around the table now and ask each of you what you're doing for America in Japan." Those were the Japan-bashing days; it was about opening up the market for trade and capital flows and all kinds of things. It was a great time for that question because Japan really was very closed. Interest rates in Japan by then were kind of two or three percent and the price-earnings ratio on the Tokyo Stock Exchange was 80, and these parameters were a reflection of administered economic policies. The stock market was really not free to trade and interest rates were not really determined by supply and demand. So after a month of being in Japan I had devised a scheme to deregulate the financial markets.

Hancock: I like the way you say that with such an even tone, “deregulate the financial market.”

Wadsworth: <laughs> There was a young guy in the U.S. Embassy who became my partner and his name was Tim Geithner; he was the treasury attaché in Japan. So we started meeting, Goldman Sachs, Merrill Lynch, First Boston, Salomon Brothers, Morgan Stanley. We couldn’t have those meetings in New York on any subject, we’d be put in jail for antitrust violation. But in Tokyo we had a common interest and we developed about 50 issues that we wanted to go systematically at the Ministry of Finance, the Tokyo Stock Exchange, the JSDA, the dealers association. And at the top of the list was a treasury auction. The treasury securities in Japan were sold directly to the banks and they never traded. So you didn’t have a treasury-bill market for a yield curve and Nomura could close any stock on the Tokyo Stock Exchange at any level they wanted to.

In fact, there were things called political stocks and if a guy in Osaka was running for the Diet and he needed to raise some money, they would tell him what stock to buy on Monday and Nomura would take it up on Wednesday and that would be his political campaign. So the second thing was a futures contract. Once you get a futures contract trading it’s really impossible not to link the market with the closing prices and the stocks. So at my first meeting at the embassy when it came around to my place at the table, I said, “Well, we are embarking on a plan to raise the cost of capital to Japanese industry.” <laughs> Everybody looked down at the table—

Hancock: I was going to say what was the response to that statement?

Wadsworth: <laughs> Where is this guy coming from? Well, sure enough that was exactly what we did and five years later the financial markets of Japan were supply and demand-driven markets. I think one of the gauges that I’m most proud of was, when we arrived in Japan with a fledgling operation basically, no P&L to speak of, 25 people, Nomura made a billion dollars net after tax in 1987 and we were nothing. When I left for Hong Kong in 1991 our Morgan Stanley branch in Hong Kong made a hundred million dollars and Nomura lost money. <laughs> They couldn’t figure out the markets. <laughs>

Hancock: So that’s a stunning change, right, in just a handful of years. Not only an audacious statement of vision of what the intention was but to actually implement that and with the complexities. There was timing involved, there were other things, but how do you explain that kind of an outcome in a short amount of time?

Wadsworth: Well, my secret weapon was one person; his name is Robin Radin-- he’s still alive and very healthy. But I decided that one of the key positions that I needed to fill in Tokyo was a general-counsel guy who could figure out all of this regulatory stuff, because that’s what it was about really and it was all in Japanese and there was nobody that spoke English at the Ministry of Finance. <laughs> So I had this idea. The execution was daunting. Robin Radin I found through a couple friends. He had a Ph.D. in Japan studies from Harvard and he was a fluent reader and speaker of Japanese. He had gone to the University of Miami in Florida to start a Japan studies program and nobody signed up so he went to law school. <laughs>

Hancock: That's a turn in events.

Wadsworth: When he graduated from law school he really was not interested in practicing law, and I found him and he came to Tokyo. The reason he was such a secret weapon: the Ministry of Finance was frightened to death of him because he spoke Japanese so they couldn't speak behind our backs when we went in to talk. And he knew more about the history of the financial markets in Japan than they did. So when we started down this path of deregulation he was the guy who figured out the list of 50 subjects. He was the guy who went in and argued our case, and that was the key I would say. It's design thinking; I often revert to that. It's such a simple idea. You identify a problem, you identify a solution, and then you execute and it's the execution that always trips you up. So in this case it was Robin. He's still a good friend. He introduced us to Japanese art because of his academic background and, as they say, the rest is history.

Hancock: As you look back at the historic import of that change, how would you sum that up?

Wadsworth: I would say it changed Japan dramatically in certain ways for the better and other ways for the worse. And I honestly think the long recession that Japan has been in, which they're in some ways still trying to figure out, is a manifestation of the fact that their financial markets are not as resilient as they should be in terms of providing public debt and equity as a real alternative to bank financing. And when the BIS rule came in and required eight percent capital in the banks, the Japanese banks were undercapitalized to begin with but then they had chosen to allocate a portion of their long-term holdings in their client base of equity as a part of their capital base. And so not surprisingly when the stock market went from 30,000 in the Nikkei down to 12, the banks were totally underwater.

So they entered a period where not surprisingly the capital allocation decisions that MITI had been making historically were not fundable through the banks and they didn't really have good alternatives. I think the investment that needed to continue to be made in the Japanese economy really suffered because of that and they're still trying to figure it out. And you combine that with the fact that the Japanese education system and maybe the DNA has created a society that is risk averse. So it doesn't have the overlay that we have, and the Chinese have to depend upon entrepreneurial new-company creation to fill the gap that is created by the big companies who are always shedding employment. It's as predictable as night and day.

And there are signs that Japan is kind of struggling out of this, but I look for ways to employ venture capital ideas in Japan and I have never succeeded; we invested in one company that worked and private equity in Japan is not that robust. So <laughs> I sort of hate to say it but I think their industrial-policy economic model worked for them and when the markets took over they never quite figured out Plan B. <laughs>

Hancock: So that's on the national level and global economic level. What about for the firm? I want to make sure that you talk about growing, was it 500 people eventually? And the scale of what you were doing there is just not a small portion of growing Morgan Stanley.

Wadsworth: Well, today it's a couple of thousand and it's a joint venture with Mitsubishi Bank. That's quite an outcome and it's not a surprising outcome. But the moment that caused the outcome was pretty scary. Thierry Porte, who succeeded me as President of Morgan Stanley Japan, and I cooked up a plan for a joint venture with several small Japanese securities companies, prominent ones but small ones. And the firm turned down the recommendation for a lot of complicated reasons. This was the late '90s when I was in Hong Kong. And the simple reason for that recommendation was that Japan never became a global financial center and for all the reasons that we tried to fix, some of which we didn't fix, it never had the attributes of a global equity market where a Sony or a Toyota would do a billion-dollar stock issue and it would be distributed in the world markets as is the case of New York. And one of the reasons that I believe that is the case is that the global financial industry has never gotten totally comfortable with the price-formation mechanism in Tokyo. Even after we did what we did to free up the market and create more supply and demand, the government would, from time to time, intervene in the stock market.

In the '90s when the Japanese banks were not meeting the BIS rule, everybody knew that if the Nikkei was at 20,000 they would be okay, if it was below 20,000 they wouldn't make it. So they literally had a policy called PKO, which is in English, and PKO stands for price keeping operation. So when the Nikkei would look like it was going below 20,000 the pension funds, blah blah blah, everybody would buy stock, so it just never was trusted. So the part of the business model that we were missing, which in our view required a joint venture, was the domestic market. The domestic market in Japan is a pretty big market and even with only one securities firm left really Nomura has a pretty good business dominating the domestic securities market. And without a Japanese name on the door, without the threat of being able to go up against Nomura, no Japanese company would ever pick us to be the book runner of a local Japanese equity offering. Then came 2008. The shotgun marriage of Morgan Stanley and Mitsubishi created the joint venture. They put nine billion dollars into the equity of Morgan Stanley, which is in the book *Too Big to Fail*, a famous chapter. As a part of that nine-billion-dollar investment, we agreed to have a domestic joint venture in investment banking. And lo and behold, here we are ten years later. Morgan Stanley/Mitsubishi joint venture dominates the domestic financial market for investment banking services. That's a good outcome.

Hancock: That's a great outcome. That's a spectacular outcome, dominant. Can you give some numbers around then, deals, dollars, employees, just for people that are not in it, just a--?

Wadsworth: I could but I'm not that familiar--

Hancock: Okay, that's fine.

Wadsworth: With it. Yeah, right. In the league table language, we're number one in equity and debt and all that sort of stuff on the investment banking side.

Hancock: So, that arc of a story of that was remarkable.

Wadsworth: Let me just say--

Hancock: Please.

Wadsworth: There's an employee in the Morgan Stanley investment banking division who we hired when I was there from Mitsubishi bank. He rose to managing director, a very successful guy. And when the negotiation began intensely around the details of the Mitsubishi investment into Morgan Stanley, it was the fall of 2008 and the world was coming apart. They committed to do the deal at twenty. Morgan Stanley stock was trading at six. And it closed. One of the keys, again, to that execution was this man, who Mitsubishi Bank trusted. I also think that the reputation that we created for the firm in Japan—ingenuity, integrity, smart, and tough—was one of the things that played very importantly in the minds of the leadership of the Mitsubishi Bank to make that investment. It wasn't just an accident. Morgan Stanley was not just a New York enterprise. We had a footprint in Japan. And that I'm pretty proud of that because who knows what would have happened if that were not the case.

Hancock: I'd like to explore a little, just before we leave Japan, this specific connection we raised a little bit by referring to Japan Inc. But the connection between these evolving capital markets and regulation with specifically Japan's efforts for innovation and entrepreneurship, and it had this incredible formation of a lot of companies right after World War II, which were significant and big players. And yet, there was this dearth, despite a lot of government efforts from METI and a lot of other people, academics, and investors, to really have meaningful entrepreneurship, and in a sense even with the semiconductor industry and others that came and went. How do you explain Japan sort of missing these successive waves of innovation and entrepreneurship?

Wadsworth: Well, Japan is not devoid of entrepreneurship and innovation for sure. But if you think of the companies that really demonstrate that kind of capability, they tend to be the Toyotas, the Sonys, the Hondas, the Kyoceras. These are companies that, by virtue of their leadership, I would say, had the courage to expose themselves to global competition. Too many of the other companies, I think the steel industry is the classic, are sort of commodity-oriented domestic manufacturing businesses who never built a plant in Tennessee. So the exception proves the rule. And these are hugely successful global companies.

Then you have kind of the one-off maverick of the century, Masayoshi Son. I mean where does he come from? He comes from Korea and Berkeley. I don't know. He's just sort of floating out there in the world with an address in Motoazabu. But I think it is that domestic kind of character of the country, the inward focus, the language. Everybody in Japan learns English, but they never speak it. And they don't travel much. We had a Japanese ski instructor at Whistler once who was just a delightful marvelous guy. And he said, "You know, I'm the only ski bum you'll ever meet from Japan." Anecdotes are worth what they are.

But when I was first in Japan, I'd had this mistaken idea that venture capital and entrepreneurship might be a shoe in the door for Morgan Stanley in the equity market. There was a venture capital firm called JAFCO, which is the Nomura kind of captive venture firm. I got the firm to put a million dollars into one of their funds and got Frank Caulfield, of all people, to join me on the board of advisors of JAFCO. And we went to the first advisory board meeting. They had very good returns, thirty, forty percent returns in their portfolio. And it became very apparent that those returns were arising from finding second-generation small private companies that they could invest in and then take public. They'd invest at twelve times earnings and go public at forty-eight. The guy that was running it was named Imahara. I can still see his face. At the end of the first meeting, Frank and I asked, "Imahara-san, what do you think about startups?" And he literally said, "Ah so, what is a startup?" Sorry. That's pejorative. But it was kind of like that. They just didn't recognize that that was part of the world. And where do entrepreneurs come from? They come from academic institutions, science programs, from school experiences that encourage them to take risk. The Japanese higher education system is sort of not that way. There are signs that it might be changing, but boy, they're at the margin.

Hancock: They're working on it. This is a fascinating topic. And I want to turn now to Hong Kong.

Wadsworth: Yeah.

Hancock: And China, another small part of the world that you helped change. First, let's start with your first interaction that turned your attention and focus and heart, I think really, to China. Tell us about that. Help orient us back in time when you started to turn your focus to China.

Wadsworth: Well, again a secret weapon, I keep going back to the importance of finding amazing people who can chart ways that I couldn't do by myself. And while I was still in Tokyo in 1988-89, I hired a man named Paul Thiel. I think I mentioned him before. Paul helped open up my eyes and helped me think about the future of China. And so, we made trips to China together. A good example is the first head of the CSRC, which is their SEC, was a man named Liu Hongru. He's still alive. Liu Hongru was a Russian trained engineer who spoke Russian and Chinese, no English. And after our first meeting with Hongru, I said, "This is a very American question. There's sort of no place for Morgan Stanley in China today. But you have a unique insight into the leadership's view of financial markets and whether or not they're going to be important or not. When do you think that Morgan Stanley could open an office in China and make money?"

Hancock: And make money.

Wadsworth: "And you have to answer both parts of the question." Without hesitating he said five years. And the day we got our license to start CICC was five years later. I've reminded him of that often. But so, even then if you had the insights that were available to somebody like Paul Thiel, I would never have been able to find Liu Hongru. I mean who the hell is this guy? Paul, I think I mentioned before, had taught finance in the People's Construction Bank business school. How many people on Earth even know there is such a thing? So, he had these insights through the students, and through what was going on at the margin on financial market thought. And that, together with the famous Deng Xiaoping trip in 1992, kind of put it all together for me that this is a place that's really going to change.

Hancock: And what did you envision at that point? This was so early. Did you see the path that you were going to explore, or was this a case of-- one of the Chinese aphorisms is crossing the river by feeling the stones. Was this a--?

Wadsworth: I wrote it. I wrote it in the 1991 business plan for Morgan Stanley Asia. I said, “We can get every country in Asia right. But if we get China wrong, we will fail.” That was the first sentence. One of the things that had been instructive about Tokyo, bizarrely enough-- and it's funny how these things sort of stay with you. We were one of the first six firms that were given a license to have a hundred percent owned business on the Tokyo stock exchange. And because we were among the first six, we got the best people, the best clients, the best everything. We were quick, and we were first. We had good ideas. And we really made a mark. We made money more quickly than anybody else in Japan. By the time the twenty-second license came, it was too late. It was over.

And the next sentence was, “The most important objective for Morgan Stanley is to be the first firm in the world that is given a hundred percent license on the Shanghai Stock Exchange,” period. That's it. Everything we do from now on is oriented toward that objective. And that was the reason for the joint venture. I reasoned that, after having gone to China a lot, China is not like Midtown Manhattan. Midtown Manhattan, you ask for the moon, and you get somewhere in between. In China, you have to give a lot before you ask for the moon. And so, I reasoned that one of the things that we could do-- and this is where the irony comes comparing Japan to China. When I got to China, I discovered that the government was my partner, not my enemy like in Japan, because they wanted a capital market. All of a sudden, there was this amazing reversal of roles. And my enemy was Goldman Sachs, and Merrill Lynch, and the usual guys. So I didn't talk to them anymore.

Hancock: You said something really interesting, which was that there are certain sentences in key documents, whether it's this business plan you wrote for Morgan Stanley in China or IPO prospectus where you now know that that wording was significant. Today, we've talked about two. Are there some others that, as you look across the landscape of these key documents or IPO prospectuses, that you can point to specific language that you now know this was a hinge point, this was significant?

Wadsworth: I'm sure there are many. The first one that pops to mind is investment banks should never do startups.

Hancock: What was that document and tell us the significance of why you point it out?

Wadsworth: I think I mentioned this before. After I got back to New York after the Apple IPO, and H&Q took home a twenty-five million dollar check, and we took home a two and a half million dollar check, I recommended that we get into the venture capital business. And that was the sentence that led into that recommendation. That's why we developed our relationship with Kleiner Perkins. If you're not going to do startups, but you recognize that that is the most important source of new investment opportunities, you better find out a way to get into that game if you're not going to do it yourself.

Hancock: Well, that led to a great partnership.

Wadsworth: Yeah, right.

Hancock: Any others that jump to mind? This is a challenge, but that was such a key insight that you pointed to, I wanted to see if others come--

Wadsworth: Yeah, it's a hard way to think about that. Another one that became very important for me in developing the culture of Morgan Stanley in Asia: never confuse principle with judgment.

Hancock: So, let's unpack that for a minute. That's very powerful.

Wadsworth: Yeah, the way I used to get into that was through Mr. Morgan's testimony before the Senate in 1933. Everybody knows, “First class business in a first class way.” But he actually said something more important than that. Of course the Senate was trying to regulate Wall Street so that they would focus on maintaining their reputation. And his assertion was, that's a stupid idea. You can't cause people to protect their reputation. That's their business. You can write regulations that make things against the law. But that's not one. And so, he said, "Seeing the future is difficult. So, we've all made mistakes in trying to plan for the future. But if I may speak for the firm that I am proud to be the general partner of, our mistakes have been mistakes of judgment, not mistakes of principle." That really resonates. And the way I used that was to say look, you kids are starting off in this business. You learn to take risk, and you'll make mistakes. But just be sure that you don't confuse principle and judgment because if you try and bat a hundred percent on judgment, you'll never make a decision. Be prepared to make mistakes. But principle is one hundred percent, not ninety-nine. You make a mistake there, you're dead. <laughs> So, yeah, that's an important one. Lots of learning lessons, I can give that one some thought and get back to you.

Hancock: Okay.

Wadsworth: Yeah.

Hancock: That's good, really good. The other topic that you've mentioned several times today, which we haven't had a chance to pursue. And again, you can give this more thought. But while it's fresh maybe we can just tee it up a little, is this importance of choosing good people that were able to help you build. Can you say more about that? You mentioned a few today. But what's your philosophy or approach about these people and empowering them? What are Jack's leadership lessons as a mentor, as a manager?

Wadsworth: Well, the first thing is sheer brilliance and knowledge. Knowledge and depth to me is key. That applies obviously a lot more to people with some experience than somebody straight out of school. I think then it's the search for intellectual honesty, and perseverance, and stamina, and the soft things that make it work. But there's no substitute for brilliance and knowledge.

Hancock: So, there are people with firepower that you identify that a raw, innate ability plus the expertise that's gained over time. Because you're growing so rapidly in so many places where it was new. How did you build your organization around it to enable these people to flourish in their leadership?

Wadsworth: Well, you almost have to go place by place. Another example is Ho Yang, the guy I found to head Korea for Morgan Stanley. I used to say, "I've never met an honest person in the securities industry in Korea. And then I finally met one." It took me five years to hire him. No, he's one of these rare guys who had a PhD from Vanderbilt, had taught economics at the University of Wisconsin, had gone back and was running kind of a rust bucket, family-owned securities firm. And the first time I offered him a job at Morgan Stanley, he said, "Jack, that's not a real job. I'm running a business. And what you want me to do is chase three convertible bonds each year. That's not a business." So, we finally opened up a branch. We got a license. We started hiring traders. We got distribution, and I went back to him. And he said, "Okay, I'm ready."

Hancock: You were ready. You'd found the right person and need to have the situation.

Wadsworth: Yeah.

Hancock: Interesting.

Wadsworth: There, he obviously had those attributes of knowledge and intelligence. But he also understood supply and demand, which is a big problem in Japan and Korea. He understood how markets worked. And that is so critical. If you think they're going to be administered, you get killed because you're looking at the wrong stuff.

Hancock: So, let's jump in with the CICC story. It's a big one, and it's so important for so many reasons. As we begin, do you want to just frame from your point of view, what was the significance of CICC for China, for all the rest of the players, before we get into the chronology of how it happened?

Wadsworth: Okay, well the original idea was to position Morgan Stanley to lay claim to the first seat on the Shanghai Stock Exchange owned a hundred percent by a foreign firm. Obviously that would have been a hollow dream were there not a serious capital market. And the presumption was that China, as an economy, as a society, as a dream itself, was, with the vision of Deng Xiaoping and those around his inner circle, going to be a dream that was realized on the back of a market economy. That was a big new idea. And it was really, I would say, only confirmed in the early '90s. It was talked about before that, but it was really confirmed in the early ’90s.

Anybody who had an MBA from the University of Chicago would know that to have a market economy, you had to have a capital market. And the creation of a capital market was to me a phenomenal opportunity in a number of ways. The capital markets of the world have evolved over a long period of time, have lots of flaws, have different philosophies, have different regulatory regimes, have different players, have different constructs. So in the broadest possible context, the idea of being a part of the creation of a capital market from scratch was just really a cool idea. And we thought about ways to be involved. In those days, in the early ’90s, the closest a foreign financial firm could come to even putting a toe in the water was to have a representative office inside China, which is like nothing. It's like, “Please have a hotel room and come and tell us what you think.” You can't do anything. So of all the crazy ideas, we cooked up the notion that a joint venture would be a way for us to put more than a toe in the water and actually get involved real time in facilitating of the creation of the capital market. That was the big idea. Certainly, that was, I would say, at the center. But it also contained the selfish idea of, if we gave something to China, we would be at the front of the line to get that seat on the Shanghai Stock Exchange. To be honest, we had no idea whether it would work, whether we could get permission. So that was the big idea and we started.

And I would say the start-- well, there were two aspects to the start. One was, what should we know about joint ventures in history to prepare ourselves for this joint venture? Because we had never done one before. One of the things I did was to make a list of countries that we could go into direct without a partner and then the countries that we had to have a partner to go into, and which of the countries where we had to have a partner to get in did we care. And there weren't many.

Hancock: That was a short list.

Wadsworth: Yeah. And we actually asked McKinsey to give us, from their files, some information on historical joint ventures and some ideas about which ones had worked and which ones didn't. In the end, we did most of the work ourselves. I mean the Eurobond market got invented in the '60s and '70s because of the, of all things, the interest equalization tax. I bet there's not many people that even remember what that was. The United States of America was having a balance of payments problem, believe it or not. And it was outflows of capital that were causing pressure on the dollar and on the economy. So somebody in Washington wisely cooked up something called the interest equalization tax. And it meant that if you shipped money offshore, you had to pay a tax. But if you raised money offshore to invest offshore, you didn't have to pay the tax. And so, some smart guy in Europe named Minos Zombanakis invented the offshore, Cayman Islands, blah blah blah subsidiary to issue bonds in the Euromarket guaranteed by General Motors and blah blah blah blah. So, this huge market came out of nowhere.

Hancock: I didn't realize that was the genesis of that.

Wadsworth: Yeah, yeah, yeah, that was the Euromarket. In fact, I can remember, as we first started selling those bonds in the international market, being asked by some naïve money manager what was the exchange rate between the Euro dollar and the U.S. dollar. Well, kind of zero. Anyway because of that particular phenomenon, there were lots and lots and lots of joint ventures created in Europe around the idea. Just to fast forward, there were two joint ventures in the financial services industry in the history of the world that worked. There were not three. Two. One was Credit Suisse White Weld. And the other was Jardine Fleming. And it turns out there is a very simple reason why they both worked, and the others didn't. In those two cases, one had the money and the other had the clients. And there was no crossover. White Weld had all the clients because they were U.S. issuers. And Credit Suisse had all the money. All those early bonds just got dumped into Swiss bank accounts. In the case of Jardine Fleming, surprise, surprise, Jardines had all the clients in Asia, and Flemings had all the money in London. So, that worked. And that, I must say, was one of the insights that gave us great confidence that we had a good idea because Morgan Stanley had the money, surprisingly enough. And China Construction Bank had all the clients, every one of the clients. So, that was number one.

Then the question was okay, we think it's a good idea. Who should our partner be? And why should China care about this idea? Again, this is where Paul Thiel comes into the equation. I asked Paul who did he think would be the most logical partner. And he said, “There's a guy named Wang Qishan at the China Construction Bank who is the guy who can get it done.” There again, Paul had been in China for four years with the U.S. Embassy. And he had insights that nobody else outside China had. He had gotten to know Qishan and his inner circle and his dreams. The second thing was okay, how do we give ourselves a chance to actually get this license? And so, we wrote a letter to Wang Qishan-- in fact, that's an amazing historic document.

Hancock: Where is that?

Wadsworth: I'll get it for you. It is just one of these amazing things, letters. So we wrote Qishan the letter. It was 1992. And nothing happened for a year. There was a foreign exchange trading crisis in Shanghai. And Qishan was seconded to go down and fix that. So he was sort of off the playing field for a while. He came back. Still nothing had happened. And a friend of mine in China having gotten wind of this idea, he said, "You know there's another person who has proposed a joint venture investment bank. His name is Ed Lim, and he's at the World Bank. He's the China Desk Officer." And actually, he wasn't. By then he was the Nigerian Desk Officer or something. But he had been the China Desk Officer in the early '80s when the protocol between China and the World Bank was first negotiated. And the person across the table from Ed Lim in that negotiation was Zhu Rongji. And he said, "I think if you could get Ed's attention and have a conversation with him, you might be able to close the loop because Zhu Rongji is the key guy." So I flew to Washington and had lunch with Ed Lim. In the usual sort of male format, we sparred for about a half an hour.

Hancock: I would have liked to have been a fly on the wall for that conversation.

Wadsworth: We finally each got our letters out of our pockets and compared them. They could have come out of the same typewriter, except Ed had written his letter to Zhu Rongji, and we had written our letter to Wang Qishan. We obviously were proposing Morgan Stanley as the foreign joint venture partner. And Ed was proposing Goldman Sachs, which of course was a stupid idea.

Hancock: You wouldn't be biased.

Wadsworth: <laughs> No. So in the ensuing six months I persuaded Ed to take a leave of absence from the World Bank. I made a compensation deal with him. He joined Morgan Stanley as a managing director. And we went to China and got it done. Then the next question was, why should the Chinese care? So we finally had our definitive meeting with Zhu Rongji. It was John Mack, and Ed Lim, and myself, a few others.

Hancock: Can you place this again in time? Month, date?

Wadsworth: '93, late '93, early '94. We had scripted the meeting carefully. And I drew the short straw on who would present the case to the big man. Predictably, he said, "Why should we do this?" And I said, "Well, there are three reasons. Number one is you are faced with the challenge of privatizing China. And privatizing is a complicated undertaking that requires restructuring of state-owned companies. Restructuring state-owned companies can be facilitated most effectively by lawyers and bankers who know what it's going to take to position that restructured company to raise capital in the international markets. And from personal experience, I can promise you that the Chinese government is not going to hire Morgan Stanley or Goldman Sachs to do that job. First of all, we expect to be paid fees. Secondly, it would require bringing us into the inner circle of Chinese state secrets.

But I think you would hire a joint venture if it had the expertise that these foreign firms had. We would be prepared to train a cadre of investment bankers who, in due course, could perform that function. The second reason is that eventually those restructured firms will have to participate in the creation of offering documents that will be used in the international markets to sell the shares. And that is something that China has no idea how to do. This joint venture could perform the same function. Thirdly, right now there is inward flowing capital at the rate of," I think it was then about twenty or thirty billion dollars a year. It rose to a hundred billion not too long after that, but, "That money is one hundred percent coming from industrial companies who want to build plants and overseas Chinese who want to build real estate. And I can promise you, that while they may not get it, their expectation of a return is probably north of forty percent.

If China is positioned to sell stocks and bonds into the international market, that cost of capital would be more like twelve percent. You're going to need a lot of capital. This is a way to lower your cost of capital." And Zhu Rongji, obviously, this is going through translation, got a little smirk on his face and he said, "I like the third one the best." Exactly. And I thought about it afterwards, there was probably a very short list of people on Earth who would even have understood the idea of lowering the cost of capital. He was a great man. He was such a visionary. He had such courage. And that was it. He said okay.

Hancock: Literally, he said okay in the meeting?

Wadsworth: Yeah, and he said, "This is very complicated. The reason it's complicated is that we have no investment banking regulations. And furthermore, because this is as important as it is, each member of the State Council will have to sign off. This is not me and some of my buddies. This is the State Council has to sign off," which they ultimately did obviously. But there was a long period of time where it was quite clear that there were factions in the State Council, conservative and liberal, who were on different sides of the question. But Zhu Rongji got it done. So that's the story. And we got the license, I don't know, in late '94 and opened the door.

Hancock: These people that you mentioned were so key because there was no precedent. There weren't institutional guidelines or things that were there. So those personal relationships that you had were so key, the conversations. You mentioned Wang Qishan, who was your partner or counterpart there. Can you say more about that relationship, how that unfolded?

Wadsworth: Well, Qishan, he's so well known now. There is so much written about him that it's hard to respond to that question without being influenced by what he became as opposed to what he was. I would say, from the very first series of encounters, it was quite obvious that he was a student of the West. He doesn't speak English, but he used to tell me stories about Alexis de Tocqueville. He'd read it, you know: "Democracy in America." He read it and he also spent the cultural revolution in the rice fields. He was up in Manchuria and a product of that generation as a survivor, as a tough guy, and he was clearly that. Also a man of few words, quite decisive and straight as an arrow. I have to say that given all the perception of graft in China, if there was ever an opportunity for somebody to ask for some money under the table, that license would have been the classic opportunity. There was never a whisper. I mean never, and it took us six months to negotiate the actual final joint venture contract and I spent months on just the paragraph on indemnity.

Hancock: What was that issue there?

Wadsworth: Well, they indemnified us. We indemnified them against misbehavior and Qishan said, “We don’t do that.” I said, “We don’t do deals without it so this is what you call a deal breaker.” So it took a long time and there were issues like that. I remember in the middle of that process I said, “There’re gonna be a lot of international financial transactions that come out of this joint venture and Morgan Stanley would like to have an exclusive on the book running of international equity deals.” He said, “Let me think about that.” And a colleague called me back the next morning and said, “The answer’s no,” and my response was, “He should have been fired if he said yes and I should have fired if I didn’t ask.” But there were many examples of things like that.

Most important that became a very contentious issue was about the approval of secondees [ph?]. Obviously the Construction Bank was gonna second some people and so were we. That, along with compensation, were probably the two most difficult things in the early days of CICC because we were like ships in the night. As soon as we got the license, and you don’t need to see this document to know what it said. I took the business plan that we had done forecasting the revenues and profits for the first five years—and obviously compensation is the biggest nut in any startup service firm—and the question was, how do you calculate? How do you justify these forecasts for compensation? And there is an organization that produces comparables for investment banking compensation worldwide called McLagan. So I thought up a McLagan report and then I took up a piece of paper that had the worldwide compensation of managing directors at Morgan Stanley, salary and bonus, and that was the last page in the book.

When we got there I thought Qishan was gonna choke and I probably presented for an hour and a half through translation. When I finished the last sentence, I said, “So what do you think?” And he said, “I’ll have to get back to you.” I mean that was classic, absolutely classic. But it was also the right answer. I mean God, it was really complicated stuff and in the early years we would fight and fight and fight over bonuses and compensation. I said, “But it’s fine for you to think that Morgan Stanley secondees getting paid in Hong Kong should come here and be happy with X minus Y. It doesn’t work that way. In fact, it’s probably hardship pay. It’s probably a premium and it’s also expat benefits and blah, blah, blah.” And his answer always was, “We don’t pay bonuses to people in Chinese companies that lose money.” I never really won that argument, so Morgan Stanley paid the bonuses out of our back pocket. I used to say to him, “You know, when you build a cement plant, Qishan, you can amortize the cost. When you build an investment bank you have to write off the expenses every year.”

Hancock: Every year.

Wadsworth: We can’t capitalize those. Anyway, those were great days. And your question about Wang Qishan, he just never missed a beat. He was smart. He was straight. We negotiated that Morgan Stanley had the right to appoint the head of the investment bank and we had the right to dismiss the CEO but not the right to appoint a new one. I don’t know how we ever got to those two things. But in the first board meeting Qishan reminded us that under Chinese law the chairman is the CEO. I should have looked that up before, but it’s true. So from then on it became clear that on issues that he cared about he was in charge.

Hancock: And you were okay with that?

Wadsworth: I had no choice. I fired one CEO and he gulped, but he wouldn't let me appoint the successor. So we played by the rules.

Hancock: This structure that you set up, can you just say a little bit about the amount of capital and the lines of business and everything, just for the record here?

Wadsworth: Well, the capital was a stab in the dark because we didn't know.

Hancock: How did you decide on that? Was it a hundred million?

Wadsworth: Hundred million.

Hancock: How did you decide on that? It could have been less and possibly could have been more?

Wadsworth: One day I just said, it's a hundred million. Really that's it. Obviously the initial capital was about having money to spend while you were losing money and I felt that was an adequate cushion. We weren't gonna spend that much money the first couple of years but it was unclear how long it would take to actually make money. So 50 million felt like the most we'd have to spend to break even and that was a cushion. The original structure was fifty percent Morgan Stanley, fifty percent the Construction Bank. Qishan wouldn't accept that and I don't blame him. So he suggested, "Why don't we bring in Goldman Sachs and Merrill Lynch?" I said, "That's not a good idea," so back and forth we came up with GIC and Mingly. They turned out to be really good choices. Mingly was a highly respected Chinese entrepreneurial real estate firm and the founder's name was Ming Cha [ph?]. Payson Cha was the next generation who was a board member, but Ming Cha was a very good friend of, who was the conservative president who sort of pulled the trigger on Tiananmen Square? The name will come to me in a minute. I mean by then Li Peng was the president and he had succeeded this guy, his favorite project was the Three Gorges Dam engineer.

Hancock: Oh, yeah. I was going to say Hu, but Hu Jintao [ph?] was later.

Wadsworth: But the important thing is that Ming Cha was his buddy. The day we had the final meeting with Wu Shangzhi and got the nod from Wu Shangzhi, Payson Cha had talked to his father in the hour after the meeting and his father had Wu Shangzhi's assessment of the meeting already. Anyway, that covered the conservative base in the state counsel. So that's the structure and the China Guarantee Corporation is still sort of a mystery. It's a funny Chinese state-owned something that doesn't really have a business model, but I learned later that they were sort of a bag carrier for Wang Qishan and could stand up to outsiders when Qishan needed it. So we never really had any contentious issues that came to a vote but it was fifty, fifty if we lined up against them. And Qishan always could get either GIC or Payson Cha to be on his side if it was a dicey question. They were afraid of him.

Hancock: So some people have asked about some of the decisions or the issues that came up and whether they were cultural, or what caused them. To what extent do you think that there were challenges of working together on a joint venture because it was a new structure, a new kind of form? Or was it more because of cultural differences? You were so early and there was a litter of failed joint ventures all around you, not financial but in the tech world, right?

Wadsworth: I come right back to the fact that basically China and Morgan Stanley had a compelling reason to make it work. And it was economic, it wasn't philosophical. It was like, if this works it's gonna make a ton of money and it's gonna change China and it'll enable China to privatize. Now that the history is history, CICC had one hundred percent market share of the privatization of Chinese state-owned companies. How can that be? That's huge. And of course they didn't charge fees for the restructuring.

You asked about the business model. The original business model, because I wasn't really sure about the international securities offerings, whether they would even work at that point in time. Witness the book and the presentation we did about China, it just wasn't clear that anybody would buy anything that came out of China. So I had cooked up a scheme where CICC would raise a fund so it would be an asset management business model: advice fees, asset management, some financings, but the flywheel was an asset management model. Obviously that didn't happen but it was out there as a revenue stream. And like every startup on earth, I mean Arthur Rock said to me the other day, "Only fifteen percent of the startups that I ever invested in that succeeded, succeeded on the basis of their original business model." That gets right back to plan B, I guess.

Hancock: Yeah.

Wadsworth: So, it started to work. I fired Ed Lim. We're still good friends. He made a lot of money out of it and he went back to World Bank, but in the end he was conflicted. He was so devoted to China and so one-sided in his way of thinking. He had no management experience outside the World Bank and he'd never compensated people. He never thought about do we do this deal or that deal? He just didn't work. So it was at that point that I introduced Harrison Young as the successor and Wang Qishan finally agreed. By then Levin Zhu was on the sidelines and beginning to have more and more influence, and I suppose that's where the cultural tension was greatest. And the secondees that the Construction Bank put up, you know, the famous Fang Fenglei who I said to Ed Lim when he introduced me to him, "Is this our driver?"

Hancock: Uh oh. <laughs> His name means wind and thunder, right?

Wadsworth: Yeah. Fenglei still reminds me of that. We're reasonably good friends although I still have problems with his approach to business. And there was a guy named Tong who was also seconded to CICC and he was the head of personnel. I didn't pay attention to him because I didn't think personnel was important. It turned out he was the most important guy in the place. <laughs>

Hancock: Funny how that turns out. Against this backdrop I'd like to talk about some of the big key technology company deals that were happening in China during this timeframe. AsiaInfo, right, first internet company. Charles in that group and we can also talk about China Telecom and that deal.

Wadsworth: Famous deal.

Hancock: Famous deal, so let's start with it.

Wadsworth: Well, Telecom was really the first privatization that went public. Of course, painfully, Goldman Sachs was the book writer. From a very early stage, in the founding documents there was a compensation arrangement that I would say was analogous to a split of the underwriting spread in any hypothetical deal. And the way I made the numbers work for the purposes of the Morgan Stanley Management Committee was to give Morgan Stanley ten percent of every underwriting fee as kind of an override. Qishan never liked that, and since he signed the agreement it was hard for him to negotiate unless he had another investment bank who would agree to a different compensation arrangement. I'm convinced to this day that that was one of the overriding considerations for his entertaining Goldman Sachs.

The second issue—which actually was Morgan Stanley shooting itself in the foot—there was a period of time where China Mobile was gonna buy a big chunk of Hong Kong Telecom and we got hired as the advisor to China Mobile. At the moment that happened, which was about nine months ahead of the actual international issue by China Mobile, I made a conscious choice that was based on the presumption that we couldn't do both those assignments and so we had to choose. At the time we made that choice the actual privatization was still a very iffy thing. So I made the wrong choice in hindsight. It never helped me with my colleagues in New York, who remained, I would say, modestly angry. <laughs>

Hancock: Slightly about that one.

Wadsworth: Yeah. In fact I had visions of coming home after that deal.

Hancock: It was a big deal right? It raised four billion dollars or something. It was a big deal.

Wadsworth: Yeah, it was a big deal. But fast-forward, we ended up doing fifty percent of the privatization book running assignments. That was the best we could have hoped for frankly. So in the end it worked out, but that was a painful year.

Hancock: So in a time when so many things went well how did you respond to that year? That was a painful year, a tough year.

Wadsworth: Yeah.

Hancock: What adjustments did you make, if any, following that year that paved the way for success that followed?

Wadsworth: I suppose survival for Jack was a key thing, so I went back to New York and explained to my colleagues what happened. And then I spent a lot of time in Beijing just to be absolutely sure that that was not a pattern for the future and that the competitive landscape would be fair. By that time we had deep, deep roots into CICC. We had transferred all of our back office stuff. We were basically supplying all of the knowhow around how you do investment banking deals. We had seconded a lot of people, some good, some bad. That's another story, but I would say we had our hooks into CICC quite deeply.

And there were a handful of people who then emerged as the leaders who had a more balanced view of the world. I would say the two most important were Wu Shangzhi, now Chairman at CDH and Bi Mingjian who's now the CEO of CICC. Real smart, honest, straightforward people who I still list among my best friends in the world. They're really great people. So it became a more balanced kind of working relationship. And I've always said that the most disruptive force around in business are investment bankers who are not busy. Once they get busy the world changes and they get happy and things start going well. So I would do my monthly trip up to Beijing and I had a talk that I would give about teamwork and trust and how great investment banking firms have collaborative collegial environments; people don't squirrel away important information in their drawer for their own benefit, and Fang Fenglei was that kind of person. The rest of the culture of the place finally even overwhelmed him and he started to toe the line. Obviously he at some point had different designs on his own career and ended up leaving. But I would say that was what eventually changed and I think it's one of the things that made CICC work, frankly.

Hancock: So if we were to kind of fast-forward again, by 2000 CICC was wildly successful. Revenue was streaming in.

Wadsworth: Yeah.

Hancock: Maybe $170 million or so in gross revenue. Can we talk about some of the deals that you remember during this time that were really defining?

Wadsworth: Actually, I think the first privatization was the airline China Eastern, which was before China Mobile. That was really a defining deal because of the complexity of the structure. It was actually owned by the regulator and that's kind of hard.

Hancock: Had you ever done a deal like that before?

Wadsworth: No.

Hancock: Had no reason to, right?

Wadsworth: No. I personally sat in on all the due diligence meetings just to be sure I understood. They had 62 brand-new airplanes and they had all their roots inside China, nothing outside China. To indicate how difficult it was, two weeks after the public offering, the stock was trading reasonably well in the international markets. The regulator announced that they had been paying subsidies for international travelers using China Eastern. They announced that they were gonna eliminate the subsidy and they didn't tell anybody including the management. And the stock went down big time, ten percent. So it's really serious growing pains, and that was pretty much the issue in almost all of the privatizations until they set up CICC and separated the ownership and regulation.

Hancock: In terms of tech deals, which ones would you put in your first tier of most significant ones?

Wadsworth: The only tech deals I would say in the privatization exercise were the telecom companies, so AsiaInfo and Sina.com are basically private companies. They were forerunners. That was really the first.

Hancock: Very first, right?

Wadsworth: Yeah.

Hancock: Charles and others were doing it so early.

Wadsworth: Yeah.

Hancock: So you were in a front seat, but it was more than a seat. You were driving at the front of all these new things, new private market, private companies, privatization, China taking its role on that domestic as well as international stage and the internet and these new areas. What was your perspective about what might be China's assets or capabilities in this area in tech that was new? What were you seeing at the time?

Wadsworth: I think the most important big idea is that we were witnessing the advantage of being backward. I still marvel at the first floor of the Shanghai Stock Exchange, which was 15 million dollars of software. To have a technical trading floor that had no specialists and no dealers, they were just a technical trading platform. Before they did that, given the technology that they employed, it would cost a 100 million dollars or 200 million or something. The next was Telecom, where they didn't have to wire the country. They could do it wirelessly.

Hancock: Skipped ahead to mobile, right? The landlines?

Wadsworth: Yeah. If you think about it, it's a huge advantage.

Hancock: Especially for a country like China where the last mile was impossible.

Hancock: Yeah. Transportation, same kind of things. And it was apparent pretty quickly that fiber optics were gonna be universal. I remember in those days before we left China, going to Lhasa, and there were people from the countryside doing their prayer wheels around the temple and checking their emails in the other hand.

Hancock: What an image.

Wadsworth: Yeah. And Duncan Clark and I were the guys on the ground in Telecom. We had a Telecom conference in Beijing at the China World Hotel. I want to say it was probably ’96, ’97, ’98. The cellphones were then those things that ...

Hancock: ... Brick.

Wadsworth: Brick. It was the minister of telecommunications and there we are on, I don’t know, CCTV or something at this little press conference. And he said, “So Mr. Wadsworth, what do you think?” I said, “I think from my perspective every investment banker is born with one of these things in his hand,” <laughs> went out to the world.

Then AsiaInfo and Sina.com, those were really the first two internet deals. And you know, Mary Meeker, our internet team, Netscape, Cisco Systems, Google. Morgan Stanley has kind of always owned that space. I think you’ve heard my story about Mary Meeker.

Hancock: Let’s see, did we get that full story? You mentioned her, but Mary is so central in the internet and all this. Go ahead.

Wadsworth: In those days research analysts made calls with investment bankers and they were the critical glue in actually getting deals. Mary wrote that famous research piece in 1995, which was the go-to place for knowledge about who’s gonna make it, who’s gonna survive in this new world. After that, everybody wanted her to be the analyst. And we were pursuing AsiaInfo and Sina.com and I sent her an email saying, “We need your help in Asia. Finally the internet has come to China and we need your help in soliciting this business.” Her answer back was, “How big are the deals?” I said, “It looks like these two deals are about $25 million each.” And her response to that was, “Jack, that’s the size of my fee,” literally. I still have the email. <laughs> So she didn’t come.

But the decision-maker in Sina.com was Lip-Bu Tan at Walden. Sina.com was his company and he had the CEO in his office in Menlo Park. Of all things, I was with the Asia Society in Dunhuang and there was cell service in Dunhuang, so I was the last conversation with Lip-Bu Tan on the way out to the caves. On that phone call he and the CEO said, “Morgan Stanley has the business. We want you guys to do this deal.” I said, “I am hard-pressed to say how important it is and how delighted I am. But let me add to that notion that I'm just about to lose cell service because we’re a few miles from Dunhuang Caves, and if there is a 20th century version of the Silk Road, it is the internet.” And I lost cell service.

Hancock: Beautiful. You couldn’t have planned that better. So the internet catapulted and forever changed China’s role in tech globally.

Wadsworth: Really powerful.

Hancock: With the benefit of hindsight now, since you were there at the very early stage, can you describe that impact, that arc that started then and the way that you look at it now?

Wadsworth: Somewhere in government there was the wisdom to see the importance of the internet, hence fiber optic. I would say the mindset that is deeply embedded in the current success of China is the conviction that investing in things like the internet and transportation and Belt and Road. There's this kind of unspoken word that the infrastructure is an obligation and an advantage if we get it right. I would say that's totally unique in the world, and that is probably one of the more important factors in the modern success of China.

Then around that, of course, you have the entrepreneurial stories. Jack Ma was certainly one of the earliest. I remember meeting him in the very early days. He used to say that his secret was that he understood nothing about technology, he didn't have a business plan and he had no cash. So, why not? Go for it. The first time he got on the internet he would say, "I was on for thirty seconds and then I got bumped off." But people like Jack saw the possibility and it's still happening.

And around that you had, again, the infrastructure of the state-owned Telecom companies. It was powerful that they would capitalize those companies and build that part of the infrastructure. But I think you fast-forward to today and China has again the advantage of being backwards. They have leapfrogged all of the mistakes that the West has made. I just came back from Beijing and the only place I could use a credit card or cash was in the hotel, period. Electronic payment systems are the order of the day. WeChat, Tencent. Baidu. All those things obviously popped up because of the entrepreneurial energy and vision of a pretty small group of people when you think about it. And venture capital didn't become a thing that worked until, I would say, 2005, 2006. Anybody who started before that lost their shirt, mostly. IDG was the first.

Hancock: With Hugo.

Wadsworth: So that was happening all at once.

Hancock: All at once.

Wadsworth: All at once.

Hancock: You said it's a small community of people. You mentioned Jack. Do you want to tell any other stories that you had with some of those early pioneers?

Wadsworth: Well, Morgan Stanley was not in the venture business in China. So it was only after I retired that I got involved, aside from personal relationships. There was no investment banking business to be done, really. It was all big state-owned companies that were being privatized, so those financings came after I retired.

Hancock: But you had been so involved with the state ones. Reflecting on your time there with CICC and your work in China, are there any lessons learned that you want to sum up?

Wadsworth: We've talked about it a lot. I think appreciating the culture and the attitude about making a contribution before you ask for the order, I would say is key. That to me is the ultimate lesson to be learned and to be understood by every Westerner. I see it happening today. We just did a big project for the Rocky Mountain Institute and climate change in China, and the only way it got done was to partner with the energy institute under the ministry to get their buy-in to the idea. Teach for China is, you know, the same sort of thing. Every Western move into China has to have that attribute. I think the other lesson is that there is buy-in to the idea of teamwork and trust. That takes time, but it can be understood and the value is obvious when it works. I think those to me are the two most important lessons.

Hancock: Thank you for that. Since earlier today I asked you about one word of advice, before we close this chapter of our interview I would like to ask you this question so many young entrepreneurs and others ask. So for somebody who's been successful, if you could boil it down, what would be one word of advice that you would give? What would that be and why?

Wadsworth: I have to be consistent, plan B. Seriously, I think it's about intellectual honesty. That's Art Rock's way of describing recognizing when you have to change course, not being bullheaded or belligerent or determined to stay the course. Intellectual honesty, and that's really about plan B.

Hancock: You shared along the course of our conversation already some examples. Is there another story that would help illustrate when you either figured out that this was an important principle, an aha moment, or when you applied this in your own life?

Wadsworth: Oh, there are lots. I think the course of the journey of CICC is full of examples. When it looked like we were not making progress in Beijing, I went to Washington. That's a plan B. When we weren't gonna build an asset management business, going to the investment banking privatization model was crucial, plan B. I'd love to talk to Wu Shangzhi about that, because of the hundred million of capital in CICC, we earmarked ten million for direct investment in private equity situations. And because he'd had experience at the World Bank, Wu Shangzhi got the opportunity to do that. It took him eighteen months to make his first investment and it was in a ceramics plant. I was chairman of the investment committee and I remember going up to Beijing saying, "If you don't pull the trigger, I'm going to pull the trigger. It's time to make an investment."

Hancock: Good stories. Jack, you've been incredibly generous with your time today and your stories and insights. So on behalf of the museum, I want to thank you again for this part of your oral history. Thanks.

Wadsworth: Well good.

END OF THE INTERVIEW

