A REVIEW OF BRYAN BURROUGH'S AND JOHN HELYAR'S: BARBARIANS AT THE GATE:THE FALL OF RJR NABISCO

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This book is a non–fiction account of the leveraged buyout (LBO) of the RJR Nabisco Corp., referred to as the largest such maneuver ever to be attempted, with the winning bid amounting to a sale value of 25 billion dollars. The main story covers roughly a two–month time period from October through November of 1988, from the moment RJR Nabisco's CEO, Russ Johnson, motivated primarily by the desire to boost the price of the company's stock, proposes an LBO to the Board of Directors to the awarding of the purchase rights to the investment firm of Kohlberg Kravis Roberts & Co. The authors Burrough and Helyar, however, devote a considerable portion in the earlier part of the book to telling the story of Russ Johnson's spectacular rise to power and wealth: from his enterprising youth (he earned money by a variety of odd jobs, including renting out comic books to his friends from his personal collection), through the undistinguished early years of his professional career ("...he would muddle along for twenty years with little distinction.") (pp. 12–13), and through a series of job changes, viz.: GE Canada; T. Eaton, the Canadian department–store chain; General Steel Works, Ltd., where he became the number–two executive; and when he was 40 years old, to the position of president of the Montreal–based Canadian arm of an American food company, Standard Brands. In 1973, Johnson was promoted to head of the international operations of Standard Brands, which necessitated that he move to New York. A single incident from this period serves adequately to convey an idea of Johnson's cleverness and business skill:

> Johnson thought Weigl (his boss, with whom he did not get along) was trying to trip him up. He was given Mission Impossible: sell the company's hapless chemicals division. Miraculously, he drew an offer of $23 million. Stubbornly, Weigl wouldn't sell it for less than $24 million. Deftly, Johnson struck a side deal. The buyer would pay $24 milion, but get $1 million of it right back under the table from a Standard Brands subsidiary. Weigl, not knowing about part two of the deal, approved it. "My greatest sale", Johnson would recall. (p. 19)

Eventually, Johnson's popularity, combined with other forces, led to his being appointed to the position of CEO of Standard Brands, where he used his position of power to transform what had previously been a dull and conservative organization to one which expressed his own breezy personality. He ran the company according to an "overriding rule he felt free to invoke at any time: The chief executive can do whatever he wants." (p. 23) But, after five years, Johnson became restless, and was ready for some sort of big change.

> The opporturnity came in a curious phone call from a fellow chief executive in March 1981. Bob Schaeberle, chairman of the food giant Nabisco, told Johnson his people had gotten a call from that fellow in Connecticut working for Standard Brands. Johnson didn't know what Schaeberle was talking about. You know, the Nabisco chief said, the fellow who had the idea of merging Standard Brands

> and Nabisco. Johnson didn't know. "Maybe there's something there, and maybe there isn't," Schaeberle said, "but I think we should talk about it." Um, sure, Johnson replied. (p. 28)

Again, Johnson's luck held, and, after the successful merger of the two companies, he became president and chief operating officer of Nabisco Brands, as the new company was called. By 1985, he had become CEO. Then,

> On a spring day in 1985, less than a year after being tapped Nabisco's chief, Johnson took a call from J. Tylee Wilson, chairman and chief executive officer of R. J. Reynolds Industries, the North Carolina–based tobacco giant. Would Johnson be interested in getting together for lunch ? Maybe. Wilson said, they could do some business. (p. 39)

One year later, Ross Johnson was appointed CEO of the newly merged companies, RJR Nabisco, a rise to power which, in the authors' words, occurred with "blinding speed".

The story of Johnson's career to the point of his becoming CEO of RJR Nabisco merely forms the background for the main story of the book, which concerns the intense, competitive bidding contest for ownership of the company, which began after the board of directors issued a press release following it's approval of Johnson's LBO proposal that said, in effect, that "RJR Nabisco is up for sale". Johnson's original intention was to offer to buy the company back from the shareholders with funds borrowed from various merehant banks and investors, but, once the board of directors made it publicaly known that the company was for sale, they were obligated to the shareholders to hold an auction and to sell the company to the investment group which made the highest and most reliable bid, thereby insuring that the shareholders got the greatest financial return on their investment.

The bidders, none of whom could possibly buy the company outright for cash, had to borrow enormous sums of money from merchant lending banks all over the world, who were willing to lend the investors such great amounts of money because of their confidence in the strength of the company being sold. Once the LBO, or takeover, had been done, the new owners would have to take a variety of measures to pay back their bank loans: typically, such measures included considerable cutbacks in expenditures, layoffs and firings of personnel, organizational restructurings, including sales of less profitable divisions, etc. Another method, which became very popular in the 1980s and which was designed to raise the huge amount of capital necessary to "pay down debt", was the issuance of high risk "junk–bonds".

If it is necessary to name a "hero" in this book, this writer would nominate Theodore J. Forstmann. Among the many people belonging to the various investment groups who tendered bids for RJR Nabisco, Ted Forstman, along with his brother, Nick, and their partner, Brian D. Little, were the only ones whose (unsuccessful) bid did not contain a financial plan which relied upon the issuance of junk–bonds, for reasons which the authors make perfectly clear:

> Ted Forstmann fervently believed junk–bonds had perverted not only the LBO industry, but Wall Street itself. Almost alone among major acquirers, Forstmann Little refused to use them. To Forstmann, the junk–bond was a drug that enabled the puniest ac-

> quisitors to take on the titans of industry, and he held it responsible for twisting the buyout world's priorities until they were unrecognizable. No longer, Forstmann believed, did buyout firms buy companies to work side–by–side with management, grow their businesses, and sell out in five to seven years, as Forstmann Little did. All that mattered now was keeping up a steady flow of transactions that produced an even steadier flow of fees–management fees for the buyout firms, advisory fees for the investment banks, junk–bond fees for bond specialists. As far as Ted Forstmann was concerned, the entire LBO industry had become the province of the quick–buck artists. (p. 233)

At first, Forstmann thought he and his partners had a chance to make a winning bid without financing that relied on junk–bonds:

> Forstmann found himself thinking of the Revlon deal. The junk–bond cartel had risen to power on Ron Perelman's take–over of Revlon. He again felt a pang of responsibility for that loss and the damage the raiders had wrought. He had been defeated in that fight. But now...
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> An image began to form in Forstmann's mind. *The junk–bond hoards are at the city gates,* Forstmann thought. *We could stop them, once and for all. This is where we could stand at bridge and push the barbarians back. Wouldn't that be phenomenal* ?
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> He would do it. (p. 306)

It is from this idea in Forstmann's mind that the authors took the image for the title of the book.

Eventually, however, when Forstmann Little & Co. realize that they are not able to raise the required capital without the use of junk–bonds, their ethical philosophy makes them withdraw from the bidding. This leaves three main contenders: Kohlberg Kravis Roberts & Co., The First Boston Group, and Russ Johnson's group, represented by Shearson Lehman Hutton and Salomon Brothers. The competition is fierce, and the bidding price steadily rises through a series of first and second bids, from Johnson's original bid of $75 dollars per share to the final, winning bid of $109 per share made by the Kravis group:

> At 8 A. M. on February 9, 1989, Kravis opened the floodgates for a torrent of money. That morning, Drexel Burnham delivered $5 billion worth of checks–the bridge loan it had promised. Kohlberg Kravis transferred $2 billion from its own bank account to RJR's. Manufacturers Hanover gathered $11.9 billion from banks throughout the world and deposited the loaned money into an escrow account for Kohlberg Kravis.
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> The funds totaled $18.9 billion, the amount needed to pay the cash portion of the buyout. It was the largest river of money ever to course through the financial system in a single transaction. The Federal Reserve Bank couldn't wire money in amounts over $1 billion, so the banks moved it around in increments of $800 million to $950 million. The flow was so big it made U. S. money–supply statistics temporarily bulge as it roared through the system. (p. 506)

After the smoke of the bidding battle had cleared, RJR Nabisco was owned by Kohlberg Kravis and Roberts, and Russ Johnson has lost his job: "Before resigning Johnson sent each director a dozen roses with a note: 'Congratulations on a great job. The shareholders won.'" (p. 507) It is difficult for the reader to view him as a loser, however, for the simple reason that on the day he resigned, Johnson received a "golden parachute" severence package worth $53 million !

As to the effect on Wall Street of the "fight", the authors write as follows:

> In the months follwing the RJR Nabisco buyout many on Wall Street sensed a new civility in the takeover world, a backlash, they reasoned, against the unfettered displays of greed and hubris seen during the momentous fight. "This transaction was a watershed event," Peter Cohen said in August. "Everybody on Wall Street looks and acts very differently when they look at deals now. It's made everyone a little bit more conservative, calmed them down, took some of the fight out of them. No one's got the appetite after RJR." (p. 512)

Finally, the authors conclude the story of the greatest LBO in history in a philosopical mood:

> In one way, Johnson was no different than the rest of Reynolds's post–Moravian breed, just more extreme. In the last decade Reynolds had become less a great company than a great dream machine. Its torrent of tobacco money allowed egos to run wild and fantasies to come true. Paul Sticht could walk with Kings. Ed Horrigan could live like kings. Directors could be treated like kings.
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> Hoisted onto the auction block, RJR Nabisco became a vast

> prism through which scores of Wall Streeters beheld their reflected glories. Jim Maher could restore First Boston's greatness. Ted Forstmann could pursue his final jihad. Peter Cohen could go from administrator to merchant banking prince. Henry Kravis could rise above the clamoring hoards of competitors. John Gutfreund could get the left side of the ultimate tombstone.
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> The founders of both RJR and Nabisco would have utterly failed to understand what had happened to their companies. In the mind's eye, it is not so hard to see R. J. Reynolds and Adolphus Green wandering through the carnage of the LBO war. They would turn to each other, occasionally, to ask puzzled questions. Why did these people care so much about what came out of their computers and so little about what came out of their factories ? Why were they so intent on breaking up instead of building up ? And last: What did all this have to do with doing business ? (p. 515)

One might wonder why the authors wrote such a long book, fully five hundred and fifteen pages long, when the major events of the story need only have filled a few pages ? The answer to this question is two–fold. First, this is not simply a documentary report of the RJR Nabisco LBO, but a thoroughly researched *dramatization* of events told in such a way as to give the reader a deep understanding of the forces at work in the particular instance, and in the world of LBOs generally. In order to do so, the authors felt it necessary to delve not only into the histories of all the companies involved, but also into the personalities, lifestyles, careers and interrelationships of all the major "players" in the drama, and a good many of the minor players, too; in addition to the 67 people listed according to their companies in the section entitled "The Players" in the very front of the book, these same names are accompanied by no less than 293 others in the Index at the rear. And secondly, the authors have tried, as best they could, to let the "players" tell the story in their own words by reproducing in detail the conversations which actually took place. In doing so, the authors have conveyed not only the thoughts and ideas essential to the understanding of events, but have captured also the intense emotions felt by the people who played important roles in the drama. Thus, the book is, in this writer's opinion, a remarkable feat, whether viewed as a work of historical documentation, a work of psychological analysis, or as a work of socio–economic reportage.

The inclusion of the actual language of the players in the story, along with the smoothly flowing style of the authors' explanations of events, personalities, and motivations makes for enjoyable reading. This writer's criticisms are only two: namely, that the authors' assume a bit too much prior understanding of certain technical ideas and terminology with which he, as a layman, was not very familiar. And secondly, the inclusion of so many names of both people and organizations, without repetition of identifying information, at times left his head spinning, so that he lost track of the story and had to "backtrack" to remind himself "who was who". One can suppose that this is to be expected in any "epic drama", especially one entitled Barbarians at the Gate ! If this book were ever to be made into a movie, the most suitable director, in lieu of Cecil B. DeMille, who, alas, is no longer alive, would surely be Akira Kurosawa ! Look for it at your local movie theater around, say, June 1995 ?