Kohlberg Kravis stands by ailing firms

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A spokesman for the Wall Street firm that acquired RJR Nabisco disputes the idea that the company has any financial trouble because several firms it acquired have failed to make interest payments.

"You've got to look at the whole portfolio," said Thomas Daly. "There's always going to be one or two characters that are in trouble."

Despite problems with certain companies, Daly said Kohlberg Kravis has made its reputation as the type of firm that will stand by ailing corporations and try to help.

"Wall Street will be on to the next deal while KKR is still there, working with the management," he said.

When Kohlberg Kravis Roberts and Co. completed the purchase of RJR Nabisco in April, it became the largest acquisition in Wall Street history, totaling $24.7 billion.

The former record-holder was Chevron Corp.'s $13.1 billion buying of Gulf Corp. in 1984, according to *Mergers & Acquisitions* magazine.

"It's really quite impressive," said Campbell Harvey, an assistant professor of finance at Duke University's Fuqua School of Business. "Especially when you consider the size of the management there."

At least two companies Kohlberg Kravis has acquired have failed on their interest payments — SCI Television, which consists of six network stations, and Seaman Furniture, the second-largest national furniture retailer.

Daly was quick to point out that just because some acquired companies may be late on interest payments doesn't mean Kohlberg Kravis deserts them.

"This isn't the kind of firm that goes in, works for the money and then gets out," he said. "They work with the companies."

Daly — with Kekst & Co., the New York firm that handles public relations for Kohlberg Kravis — said the idea that anything is wrong with the firm or with leveraged buyouts is ludicrous.

"What's the trouble in leveraged buyouts? Nothing," he said. "This is the way it's supposed to be. There are winners and there are losers, but that's capitalism."

Kohlberg Kravis was formed in 1976 by Jerome Kohlberg Jr., Henry Kravis and George Roberts, and 13 years later, had acquired 35 companies at a cost of more than $62 billion. It's supervised by five general partners and 14 associates.

KKR introduced the concept of leveraged buyout to the financial world, proving what could be done with a small amount of money by Wall Street standards.

"They take a firm and look at it the way it's being run," Harvey said. "They look at structure and how the firm is being operated. These people are valuing the firm on the basis of expectations of the management. These guys sit down and look at each divison to see what would happen if the company was run right."

Then they send in outside or in-office managers to run things in a profitable way, he said.

"Leveraged buyouts are usually associated with management of the firm," Harvey said. "In the RJR case, they actually went into the firm and took over."

When the companies fail to make their payments, Harvey said the acquiring companies are the ones to take up the slack — much like a co-signer to a bank loan. But that also means the buyout firms are losing money.

"Essentially, the whole use of leveraged buyouts is going into the debt market in a huge way to buy something," Harvey said. "If you've got a firm that's financed mostly with debt, especially junk debt, you've got a huge obligation in terms of interest payments every year."

Leveraged buyout firms earn money three ways:

- They charge investors a 1.5 percent fee for managing their money.
- They keep 20 percent of any gains they generate.
- They charge the companies they acquire a fee — typically 1 percent of the size of the deal — for negiotiating and arranging the transaction.

"Basically, the Wall Street firms are in it for the fee," Daly said. "KKR is in it for the equity. They make their money on the equity, working with the management."