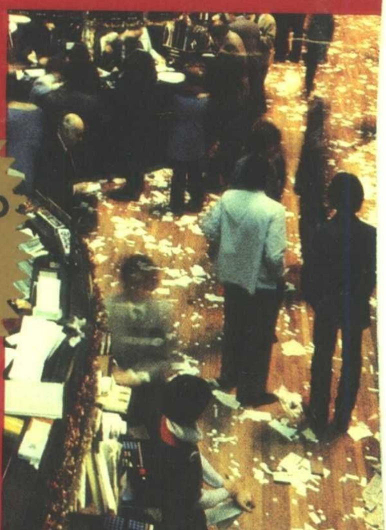
THE PREDATORS BALL

NATIONAL BESTSELLER

The Inside Story
DREXEL BURNH
and the Rise of
Junk Bond Raid

THE BOOK WALL STREET COULDN'T STOP — NOW UPDATED



CONNIE BRUC

"WALL STREET'S READING LIST STARTS OFF WITH A SIZZLER: *THE PREDATORS' BALL.*"—*USA TODAY*

During the 1980s, Michael Milken at Drexel Burnham Lambert was the Billionaire Junk Bond King. He invented such things as "the highly confident letter" (I'm highly confident that I can raise the money you need to buy company X) and "the blind pool" (Here's a billion dollars: let us help you buy a company), and he financed the biggest corporate raiders—men like Carl Icahn and Ronald Perelman. And then, on September 7, 1988, things changed. . . .

The Securities and Exchange Commission charged Milken and Drexel Burnham Lambert with insider trading and stock fraud. Waiting in the wings was the U.S. District Attorney, who wanted to file criminal and racketeering charges.

What motivated Milken in his drive for power and money? Did Drexel Burnham Lambert condone the breaking of laws? *The Predators' Ball* dramatically captures American business history in the making, uncovering the philosophy of greed that has dominated Wall Street in the 1980s.

"Connie Bruck traces the rise of this empire with vivid metaphors and with a smooth command of high finance's terminology."
—*The New York Times*

"*The Predators' Ball* is dirty dancing downtown." —*Newsday*

Cover design by Melissa Jacoby
Cover photograph by Dick Luria/FPG International

A PENGUIN BOOK
Business

ISBN 0-14-012090-4

90000

9 780140 120905

PENGUIN BOOKS

THE PREDATORS' BALL

Connie Bruck is a senior reporter for *The American Lawyer.* Her articles have also appeared in *The Atlantic, Manhattan, inc., The Washington Post, The New York Times,* and *Regardie's.* She received the John Hancock Award for Excellence in Business and Financial Journalism in 1984. Connie Bruck lives in New York City with her son.

THE PREDATORS' BALL

The Inside Story of Drexel Burnham and the Rise of the Junk Bond Raiders

CONNIE BRUCK

PENGUIN BOOKS

PENGUIN BOOKS
Published by the Penguin Group
Viking Penguin, a division of Penguin Books USA Inc.,
40 West 23rd Street, New York, New York 10010, U.S.A.
Penguin Books Ltd, 27 Wrights Lane,
London W8 5TZ, England
Penguin Books Australia Ltd, Ringwood,
Victoria, Australia
Penguin Books Canada Ltd, 2801 John Street,
Markham, Ontario, Canada L3R 1B4
Penguin Books (N.Z.) Ltd, 182–190 Wairau Road,
Auckland 10, New Zealand

Penguin Books Ltd, Registered Offices:
Harmondsworth, Middlesex, England

First published in the United States of America by
The American Lawyer/Simon and Schuster 1988
Published with a new chapter in Penguin Books 1989
Published simultaneously in Canada

10 9 8 7 6 5 4 3 2 1

LIBRARY OF CONGRESS CATALOGING IN PUBLICATION DATA
Bruck, Connie.
The predators' ball: the inside story of Drexel Burnham and the
rise of the junk bond raiders/Connie Bruck.
p. cm.
Reprint. Originally published: New York: American Lawyer: Simon
and Schuster, 1988.
Includes index.
ISBN 0 14 01.2090 4
1. Consolidation and merger of corporations—United States.
2. Junk bonds—United States. 3. Milken, Michael. 4. Drexel
Burnham Lambert Incorporated. 5. Stockbrokers—United States.
I. Title.
[HD2746.5.B78 1989]
332.63'2'0973—dc19 88-7993

Printed in the United States of America
Set in Aldus

For Ari Schlossberg

CONTENTS

Prologue: The Ball

In the third week of March 1985, the faithful, fifteen hundred strong, came to Beverly Hills to pay homage to Michael Milken, the legendary junk-bond guru of Drexel Burnham Lambert whom many of his followers called simply "the King." For the next four days, they would savor the world he had created for them.

By five-thirty each morning, an armada of about one hundred limousines glided into position around Beverly Hills. Dozens of them ferried guests from the lush green-and-pink medley of the Beverly Hills Hotel—then owned by arbitrageur Ivan Boesky, his wife and his in-laws, and completely booked by Drexel for these four nights—through the city's wide, stately, palm-tree-lined streets. Their destination was the Beverly Hilton, where the annual Drexel High Yield Bond Conference—*by now known as the Predators'* Ball—was being held, just a few blocks from Drexel's West Coast office.

Breakfast was served at 6 A.M., a concession to popular tastes by Milken, who was at his desk each day by 4:30 A.M. Then came the perpetual round of presentations, sometimes three simultaneously in different rooms, given by heads of companies. These were nearly all Drexel clients, typically the small and medium-sized companies—run by entrepreneurs with healthy ownership stakes—with whom Milken had carved out his historic franchise when he started doing financings for them, back in the late seventies and early eighties.

Because of their small size, or their lack of credit history, or their leveraged capital structure, these companies had been rated below investment grade by the rating agencies and thus had not been able to raise money by issuing bonds in the public market. The only way for them to borrow money was in short-term loans from banks or in private placements with insurance companies, which carried covenants so restrictive that they made the money almost not worth having.

Then, one day, Drexel's investment bankers had come knocking at the door. Drexel would underwrite their bonds, low-rated though they were, for the public marketplace. Michael Milken, a most extraordinary junk-bond trader, could raise $50 million, $100 million or more—the kind of long-term, relatively covenant-free capital that was available to these companies nowhere else. All they had to do was pay the price: a high yield to the investors, and an enormous fee to Drexel.

Now hundreds of buyers were in the audience for these presentations. There were the players who had turned nondescript or failing financial companies into dazzling success stories, based on the yield of the bonds that Milken offered them. And there were the money managers—people who ran investment portfolios for thrift institutions, insurance companies, public and private pension funds, mutual funds, offshore banks, college endowments, high-yield funds.

Many of them had been converted into believers by Milken back in the seventies, when he had begun tirelessly preaching an esoteric gospel: that in a diversified portfolio of high-yield bonds, otherwise known as "junk" bonds, the reward outweighs the risk. This was a proven theory, well documented by academician W. Braddock Hickman in his enormous multivolume tome *Corporate Bond Quality and Investor Experience*, published in the fifties. All that remained, for everyone to make money, more money probably than they had ever imagined, was to put theory into practice.

Hand in hand with Milken, these buyers had put theory into practice—and now they were players in a $100 billion market. The intense young man with the ill-fitting toupee, the set jaw, the air of utter confidence and the greatest sales pitch that any of them had ever heard had been right.

Some of these buyers thought nostalgically of the way it had been at the beginning. Just six years earlier, Milken had staged his first West Coast high-yield-bond conference at the Beverly Hills Hilton for about sixty people. The buyers had sat around conference tables with the issuers and engaged in the kind of substantive dialogue, replete with hard data, that allowed them to decide whether they wanted to own a company's debt or not. That immediacy was gone now. The presentations were made to hundreds of buyers in huge conference rooms with floor-to-ceiling screens on which the speaker's immensely magnified image appeared, and they were driven not by hard data but by slick, soft-sell videos. "Instead of a dialogue, it's like watching TV," complained James Caywood of Caywood-Christian Capital Management, who manages about $2.2 billion, mainly for savings-and-loan associations (S&Ls), and is an old-timer in the junk market. "The conference has become—excuse my language—a gangbang."

It had also, this year, become the Predators' Ball. There was a new gospel—or, more, a kind of added liturgy—being preached these days by Milken, who had become more messianic, more fevered, more *wired*, than ever. His message, received with wild excitement by this congregation, was that they should save corporate America from itself.

Milken had long professed contempt for the corporate establishment, portraying many of its members as fat, poorly managed behemoths who squandered their excess capital and whose investment-grade bonds, as he loved to say, could move in only one direction—down. He had made fortunes for himself and his investors by identifying assets undervalued by the market. In the seventies Milken had done this primarily with the debt securities of troubled or bankrupt companies. But by the early eighties the clearly undervalued asset was corporate America, and the biggest play was in the takeover game.

This was a game for which Milken was a natural by temperament and talent. When Wall Street's elite investment banking firms were pocketing huge fees from the mergers-and-acquisitions (M&A) game, Milken and his corporate finance partners at Drexel had been left out in the cold, too déclassé to be hired by the major corporations that had bank lines big enough to play. Unable to attract those clients, they had finally decided to do something beguilingly simple: they would create their own.

Who needed Chase Manhattan or Manufacturers Hanover when Carl Lindner, Sam, William, and Hyman Belzberg, Saul Steinberg, Victor Posner and the entire host of institutional junk-bond buyers were ready—at Milken's behest, and on hours' notice—to sign up to buy the junk bonds that would finance a takeover? Just as Milken had given medium-sized companies access to amounts of capital that had been wholly out of their reach before, so now his chosen takeover artists could set their sights on targets that but for him would have remained the stuff of their dreams.

"Capital is not the scarce resource," Milken had been instructing his followers for several years and, to their delight, proving over and over again.

Now, in March 1985 at the Beverly Hilton, on the eve of an assault that would shake corporate America to its roots, he declared that the combined buying power of his assembled guests was three trillion dollars.

It was a heady message, and made more so by events of the preceding two weeks. The junk-bond-financed takeover had not sprung, fully functioning, from the minds of Milken and his Drexel colleagues; it had needed crafting and fine-tuning. T. Boone Pickens Jr.'s peanut-sized Mesa Petroleum had made a run at mammoth Gulf Oil in early 1984. Pickens had ultimately driven Gulf into the arms of its white knight, Standard Oil of California. Then Steinberg's Reliance had mounted its raid against Disney. Carl Icahn had launched his bid for Phillips Petroleum, after Pickens' Mesa had taken its turn and been bought out. These raids—all financed by Drexel junk bonds, except for Pickens' run at Phillips—had thrown off hundreds of millions of dollars to the raiders and to Drexel. But not one had acquired its target. Corporate America, therefore, had been able to deride these bids as nothing more than stickup artists' bluffs.

They couldn't do that anymore. A week before this Predators' Ball, the first Drexel junk-bond-financed takeover had actually swallowed its target. In a deal that started hostile but turned friendly, the Coastal Corporation was acquiring American Natural Resources Company for $2.46 billion—$1.6 billion of it from bank loans and $600 million from Milken's junk (an amalgam of notes, or debt, with high-yielding interest and preferred stock with high-yielding dividends). Oscar Wyatt, chairman and CEO of Coastal, had become a sudden star.

There were lots of people at this conference who were shaking Wyatt's hand, wishing him luck—and picturing themselves in his shoes. One of them was Nelson Peltz. Just a week earlier, Triangle Industries, a company with a $50 million net worth run by Peltz and Peter May, two unknowns, had made a $456 million bid for National Can, to be wholly financed by Milken's junk bonds.

Coastal was a substantial company, and Wyatt, while he was anathema to the corporate establishment, was an experienced operator. But if Triangle Industries, a vending-machine, wire and cable company with little to its name besides the cash raised from previous junk-bond offerings, could succeed in taking over a major industrial company like National Can, then that meant that no prey was too large and no predator too inconsequential—so long as Milken could tap into his magic pools of capital. Overnight, all the rules of survival in the corporate jungle had been rewritten. The weak could become the strong, and the strong the weak. It must have not only excited but tickled the fancy of Milken, an amateur magician who occasionally does tricks for his friends, to be able to wave this particular wand.

The honored guests of this conference, therefore, were the takeover artists and their biggest backers—men like T. Boone Pickens, Carl Icahn, Irwin Jacobs, Sir James Goldsmith, Oscar Wyatt, Saul Steinberg, Ivan Boesky, Carl Lindner, the Belzbergs—and lesser lights about to shine, such as Nelson Peltz, Ronald Perelman, William Farley. The names tend to meld into a kind of raiders' litany, but they are not all the same. For Milken, they would have separate roles during the coming months, performing discrete functions in a vast, interlocking machine of which he alone would know all the parts.

What all these men did share, of course, were enormous egos and appetites, and they did not think of themselves as Milken's functionaries. Each thought he was using Milken to attain his own goal. This was true. But the larger truth was that they were joined in an effort to satisfy an appetite that dwarfed all of theirs, so enormous that all that their deals would throw off to Drexel and to Milken—billions in fees and in equity stakes—would only whet it.

On the second night of the Predators' Ball, while the lower-ranking troops (money managers and executives of medium-sized companies) were sent in buses to a show at a movie lot, some one hundred of the real players—takeover entrepreneurs, major investors, arbitrageurs, deal lawyers—attended a cocktail party at a bungalow at the Beverly Hills Hotel. From there they were chauffeured to dinner in a private room at the swank Chasen's in Beverly Hills.

In addition to Drexel's female employees, there were a number of extremely attractive young women at this dinner—so good-looking, in fact, that one takeover lawyer, George Katz of New York's

Wachtell, Lipton, Rosen and Katz, renowned for his naiveté, remarked to a companion, "I've got to hand it to these guys—I've never seen so many beautiful wives!"

In fact few if any wives attended this dinner. An assessment closer to the mark was made by arbitrageur Martin Weinstein, who, noting that Irwin Jacobs had been deep in conversation for hours with one of these women at the far end of the room, commented to a friend, "Tell Irwin he doesn't have to work so hard. She's already paid for."

According to Julian Schroeder, a former corporate finance partner at Drexel, the "girls" have been a staple of the conference since the early years. They were seen as necessary bait for clients in the days when Drexel was "laughed at" by those whom he and his colleagues called for business. These women were recruited chiefly by Donald Engel, a close associate of Milken and a longtime managing director of Drexel. In 1984 Engel resigned and became a "consultant" to the firm, but he continued to carry out his traditional function vis-à-vis the "girls."

Fred Sullivan, chairman of Kidde, Inc., who has attended the conferences for years, confirmed that the women were paid by Drexel—"varying amounts, depending on how pretty they are, and what they'll do," said Sullivan, with a chuckle. "Don [Engel] always says to me, 'How could I get all these guys to come, if I didn't have the girls?' "

Following the dinner at Chasen's, many of the guests and the women had repaired to Bungalow 8 at the Beverly Hills Hotel, where the cocktail party had been held earlier that evening. Bungalow 8, the one Engel traditionally occupies for the conference, is situated at a far remove from the hotel and most of the other bungalows, and is therefore quite private. As in past years, Engel was sharing it with a Drexel client, Joel Friedland, a partner of the Pritzkers. As one participant who partied there late into that night puts it, "All these big takeover guys were in that place together, and we've all got tremendous egos, we're all trying to prove ourselves all the time, to show we can get the girl we didn't get in high school, we're basically a bunch of exhibitionists—things just got out of hand."

On the final night of the conference, there was a gala dinner and show for all fifteen hundred guests, held in a huge auditorium at the Century Plaza. During dinner, Milken did a video presentation, courtesy of Lorimar, a Drexel client. There was a takeoff on the E. F. Hutton commercial. "When E. F. Hutton talks . . ." says the buttoned-down gray-suiter, pausing as a woman sashays by him. "Did you see the tits on that broad?" There was an adaptation of the theme from *Ghostbusters*, with the chorus "When you need money, call Drexel!" Milken tried for levity, but his natural demeanor is so unmistakably serious and intense that the strain showed. It didn't matter. The applause was deafening. He was the King.

Then it was time for the performer of the evening. In the early years of these conferences, Stephen Wynn of Golden Nugget—who, as he has said, was "made" by Drexel—was the dinner speaker. Then, in 1984, Wynn recruited Frank Sinatra as a surprise guest. This year too, the identity of the performer was a well-kept secret. It had been a matter of speculation among some of the lesser troops at this conference, who were awestruck at being in such proximity to this tidal wave of money and power that was building. "Everyone was saying," recalls one portfolio manager for a savings and loan, " 'It's going to be either Michael Jackson or God.' "

It was Diana Ross. According to Wynn, Ross entertained gratis, in return for the chance to invest in one of Milken's investment partnerships, Reliance Capital Group, L.P. She was in the same well-heeled company there that she was on this night—with Wynn, Steinberg, the Spiegel family, Ivan Boesky, Victor Posner, the Belzbergs, Mantar Associates (a partnership of Milken and his Drexel colleagues) and others.

After about forty minutes of a dazzling performance, Ross began circulating among the guests. Finally she settled on the lap of straitlaced Baptist Carl Lindner and sang to him.

MILKEN IS SAID by close associates to spend barely a moment in his twenty-hour workday that is not dedicated to business purpose. It is not surprising, therefore, since this extravaganza was his creation, that it was such an intensely purposeful event.

It was an evangelical happening that stirred a mass excitation in its participants, many of whom felt they were part of a large and unstoppable force destined to change the world. It was deal heaven. There seemed to be a deal for everyone. Money, as Ivan Boesky once told a group of prospective investors in his arbitrage partnership, was falling off the trees. It was a glorified road show for the buyers and for the scores of companies that made presentations, many of whom would soon be doing junk-bond offerings. It was a reunion for Milken's high-rollers, whose camaraderie, if not collusion, he encouraged. One Drexel lawyer later recalled having seen Ivan Boesky, Carl Icahn, Carl Lindner and Irwin Jacobs huddled in a corner. "*Anything* could have been happening there," he remarked with a laugh. It was a good time. Bungalow 8 would not soon be forgotten, and client loyalty gets forged in sundry ways.

And it launched Milken's now full-blown tour de force. Within the first two weeks of April 1985, hard on the heels of the Predators' Ball, five more Drexel clients—in addition to Triangle Industries—would make bids for companies, all backed by Milken's junk bonds.

Mesa Petroleum, with a net worth of $500 million, would go for Unocal.

Lorimar, with a net worth of $105 million, would offer $1 billion for Multimedia.

Sir James Goldsmith would make a bid for Crown Zellerbach Corporation for $1.1 billion.

Golden Nugget, with a net worth of $230 million, would go for Hilton Hotels for about $1.8 billion.

And Farley Industries, with earnings of $6 million, would go for Northwest Industries, for about $1.4 billion.

Other bids would take longer to germinate—but they would turn out to be the most fruitful of all.

NELSON PELTZ went through the four days of the Predators' Ball, as he would later say, as a "nervous wreck." Peltz, who had a track record in business that can be described as lackluster, saw National Can as the opportunity of a lifetime. He had run his family's frozen-food business, expanding it through acquisitions and then selling it in the midseventies; it later went bankrupt. Peltz had struggled for years, been close to broke, finally managed in 1982 to acquire with Peter May a controlling block of Triangle Industries, which he intended to leverage up as his vehicle for acquisitions. Until now, nothing had worked. And he was terrified that this deal too would somehow get away from him.

What had probably gotten Peltz to this point, however—to be one of Milken's players, on the verge of acquiring one of the largest can-manufacturing companies in the United States—was his long-time conviction that he would someday make it very, very big. This