Taking Stock: Investments for the ethically challenged

by Malcolm_Berko

Dear Mr. Berko: You advised me against buying Blackstone Group at $33 after it came public and earlier this year you recommended that I sell Fortress at $34. You said that you did not like these types of firms and I'd like to know your reasoning behind these recommendations. Those private equity take-over firms are making billions of dollars and they sound like a great way to get on the bandwagon and make some really big money.

P.C.

Bend, Ore.

Dear P.C.: You can get on the bandwagon but I doubt there will be enough horses remaining to pull it during the next few years!

Private equity firms like Blackstone, Fortress, Cereberus, Kohlberg Kravis, Clayton Dubilier, etc. make scandalous profits and add nothing to society except a culture of insatiable greed and avarice. This rapacious industry makes its lucre by purchasing a private or public company for (let's say) $6 billion using a combination of "private equity" ($3 billion) money and borrowed ($3 billion) bank funds. After the $6 million purchase they will sell $3 billion in bonds (guaranteed by the remaining assets of the purchased company) to repay their private equity investment, then a year later they will take the company public once again selling $4.5 billion of new stock to the public. With the $4.5 billion proceeds from the public offering the private equity firm repays its $3 billion bank loan keeping a $1.5 billion profit while the partners snicker and snigger as they deposit huge fortunes in their personal checking accounts. Meanwhile, the newly issued public company has $3 billion in additional debt it never had before.

In my opinion, most private equity firms are whoremongers and investors who purchase the newly minted initial public offering shares from Merrill, UBS and Smith Barney are dumber than size 15 bowling shoes.

Cereberus Capital Management may have enormous difficulty selling bonds to pay for its $7.5 billion buyout of Chrysler. Apax Partners will have big problems selling bonds to finance its $7.8 billion buyout of Thompson Learning. Clayton Dubilier is going to have a difficult time marketing bonds to finance its private equity takeover of U.S. Food, Home Depot's supply business and Service Master. Kohlberg Kravis may have even shamed banks and hedge funds into buying billions of dollars of bonds to finance its takeover of Texas Utilities, First Data and Dollar General.

There isn't an iota of economic good in the purchase and resale of these egregiously over-indebted companies

to investors at higher prices. Private equity firms have been flipping public companies like real estate speculators were flipping houses in the past few years and I think it may soon "bubble." Meanwhile, Blackstone's chief executive officer, Steve Schwartzman, who recently took his company public at $31 put $7.7 billion of those public proceeds in his bank account. I'm told that he was smirking like a Cheshire cat as he motored to the drive-through window.

Most private equity firms make me feel unclean because: (1) their end-game is like a necrotizing cancer, (2) the debt they incur to pay for the purchases is unscrupulous, counterproductive, and borders on misfeasance, (3) their buyout activities spawn mountains of new debt the weight of which becomes an anchor to a company's growth, (4) their business plans create zero economic benefit for the target firms and their employees and (5) these Wall Street carpetbaggers are basically paying Paul so they can rob Paul in order to steal from Peter.

Many private equity firms and many of their associated hedge funds represent capitalism in its most evil and virulent form. They are the robber barons of the 21st century to whom legal rape and pillage of a company's balance sheet for personal gain is all in a good day's work. I suspect that some of the banks and hedge funds participating in this perversion of corporate structure are becoming nervous about the excessive accumulation of junk debt they've had to purchase and hold in inventory. And some of the brokerage firms who eagerly participated in this corporate defilement are looking to exit this cabal of collusion and complicity.

Firms like Blackstone, Fortress, Cereberus, Kohlberg Kravis, etc. are a pox. Their principals loot the corporate landscape so blatantly that the public is beginning to view them as pariahs. The principals have no more conscience than a fox in a poultry farm and their piratical activities are no more necessary to our economy then are maggots to molten steel.

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