

This week: Jerome Kohlberg

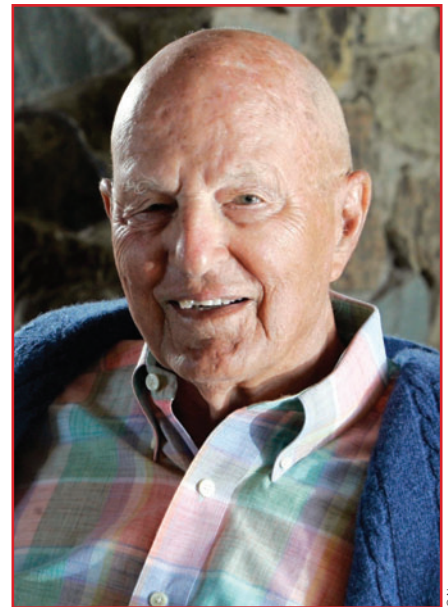
## The “spiritual father” of private equity who favoured integrity over hardball tactics

You may not be familiar with Jerome Kohlberg, who has died at his home in Martha's Vineyard, aged 90. But you will almost certainly have heard of the firm he founded and the industry it spawned. Kohlberg, says the Financial Times, was “the first K” in Kohlberg Kravis Roberts, which evolved into the “fearsome” force known as KKR, and became infamous in the 1980s for its buyout raids on corporate America, as recounted in the bestseller *Barbarians at The Gate*. Having pioneered the original leveraged buyout model (see box), Kohlberg is, as Fortune notes, “the spiritual father” of the \$2.6trn modern private equity industry.

The novelist Tom Wolfe coined the phrase “Masters of the Universe” to describe aggressive, ostentatious Wall Street go-getters of the era, says Forbes. “Jerry Kohlberg was their antithesis.” Small, baldish, with wire-framed glasses and “a sweet smile”, he seemed happiest playing knock-about Sunday softball games on his Massachusetts island retreat. Last week, his former partners, Henry Kravis and George Roberts, described him as “a man of integrity and moral courage”. He was certainly that. But ultimately his principles led to a bitter struggle with his two younger partners that resulted in him leaving the firm in 1987.

Born in New York in 1925, an importer's son, Kohlberg attended Swarthmore College in Pennsylvania, a private school founded by Quakers. Its philosophy had such an impact on him that he called himself a “Jewish Quaker”, says The New York Times. After a stint in the US Navy in World War II, he gained degrees at Harvard Business School and Columbia Law School, later joining Wall Street bank Bear Stearns, where he rose to head the corporate finance unit. Kohlberg was “the odd man out” at a firm that “favoured loud-mouthed, coarse personalities”, says Forbes. But in the 1960s he developed a speciality on the side, which he called “bootstrap” deals. The idea was to help ageing business owners looking to sell up. Kohlberg would buy and restructure the companies, often using borrowed money, with the aim of later floating them.

He mentored two promising financiers, cousins Kravis and Roberts, who took to his form of deal-making. When Bear Stearns refused them time to pursue the model, they left to form KKR in 1976. At first all went well. But by 1983, Kohlberg was “uncomfortable” with his partners' hardball approach. Matters came to a head in 1986, when he opposed the firm's \$8.7bn hostile acquisition of the dairy giant Beatrice, believing it



unprincipled. In 1987, says the FT, he left to form Kohlberg & Son, a more “demure” private equity outfit, with his son James. Kohlberg never achieved the riches gained by his erstwhile partners. It didn't trouble him. A peaceable man who disliked conflict, he was renowned among fellow ballplayers for his wisdom. If a row broke out, recalls one, Jerry would always plead to end it. His motto in sport, as in life, was “can we just play ball?”.

### “Buying anything with over 50% debt is ungentlemanly”

When Kohlberg left KKR in 1987, the split was portrayed as amicable, says Laurence Arnold on Bloomberg. In practice it was anything but. As Bryan Burrough and John Helyar relate in *Barbarians at The Gate*, their account of KKR's landmark 1989 acquisition of the conglomerate RJR Nabisco, Kohlberg became known within the firm as “Dr No”, as his protégés pressed for bigger and more aggressive leveraged buyout (LBO) deals.

Kohlberg believed that “buying anything with over 50% debt was ungentlemanly”. He saw it as vital to the success of his bootstrap deal model to keep owners and management on side, favouring smaller, friendly deals, “initiated by pull-up-a-chair talks”. When that approach was dismissed by his partners, Kohlberg didn't mince his words, says Michael de la Merced in The New York Times. At his last investment conference at KKR he railed against “the overpowering greed that pervades our business life” and threatens “to kill the golden goose”.

Kohlberg lost that battle, but he won the war, says Dan Primack in Fortune. The non-hostile deals he favoured “would later be emulated by almost the entire private equity market”, including KKR. “I think the thing I brought to the buyout business, more than anything else, was the idea that management had to be an integral part of what we were doing,” he later said.

Many “Wall Street operators try to make deals happen by being the most strong-willed personality in the room”, writes George Anders, author of *Merchants of Debt*, in Forbes. “Kohlberg had the humility – and the genius – to speak softly” and let others “persuade themselves”. The trust he inspired ensured that “what was a mere financing technique to others” became the starting point of a “full-fledged industry”. It is one of the great Wall Street ironies that Bear Stearns, which dismissed his LBO model, no longer exists – while the tiny outfit he began with just \$120,000 is “one of the world's premier investment firms”.