From:	Fuld, Dick <lbexec1@lehman.com>
Sent:	Monday, September 24, 2007 12:47 AM (GMT)
To:	Goldfarb, David <dgoldfar@lehman.com>
Subject:	Re: Barron's

Someone should shut this guy up- or maybe not//he just said we don't have do it again. Now is a good time to get paid for the risk we are taking. Let's see how he feels about that.
Outside of that-grandpa is doing great thank you.

----- Original Message -----
From: Goldfarb, David
To: Fuld, Dick
Sent: Sun Sep 23 20:37:53 2007
Subject: Fw: Barron's

How's the grandpa doing!!! Those comments by James is despicable, they should burn in hell!

----- Original Message -----
From: Berkenfeld, Steven
To: Redmond, Robert D; Stephenson, Ros; Miller, John R; Sullivan, Christopher; Konigsberg, Michael; Kirk, Alex (FID); Laguerre, Martin; Smith, Greg L; Orlan, Fred S; Seery, James; McGee III, Hugh E; O'Meara, Chris M (NY); Niebuhr, John J; Davis, Emily; Fox, Gary J; Goldfarb, David; Muller, Catherine V; Amin, Faruk K; Wieseneck, Larry; Weiss, Jeffrey L
Sent: Sun Sep 23 18:57:57 2007
Subject: FW: Barron's

Short article worth reading.

In particular, take a look at the discussion on bridge equity, including the comment from Tony James of Blackstone at a conference last week that the granting of bridge equity by banks marked a high-water mark in the LBO business. "We just couldn't believe that banks would give us equity bridges," he said.

I find that comment incredible remembering how aggressively they pushed us to provide it on deals like Sallie Mae. Let's hold on to this in case we ever see a bridge equity "request" from them again.

-----Original Message-----
From: Pelio, Tasha
Sent: Saturday, September 22, 2007 11:47 AM
To: Freidheim, Scott J; Lowitt, Ian T; Berkenfeld, Steven; Hughson, Paul A; Odrich, Michael J; Lazarus, David S; Hash, Steven R; Zackowitz, David; Walsh, Mark; Shabet, Rose; Burns, Hannah; Whitestone, Randall B; Cohen, Kerrie; Finnegan, Brian; Nadler, Mirey S
Subject: Barron's

The Deal Market Downshifts

By ANDREW BARY

THE SUMMER STORM IN THE CREDIT MARKETS that threatened more than $300 billion of leveraged buyouts has subsided, meaning all but a handful of major acquisitions announced previously are likely to close on schedule by the end of the year.

Shareholders of First Data (ticker: FDC) are breathing a sigh of relief because that $29 billion deal is likely to be completed this week at $34 a share, just over a month after the stock dipped below $31 on fears the credit crisis could jeopardize the transaction, which is being engineered by Kohlberg, Kravis, Roberts. First Data traded Friday at $33.84, near its takeover price.

Another deal that looked shaky this summer, the $21 billion buyout of Archstone-Smith (ASN), a real-estate investment trust, is on course to close in early October at $60.75 a share. Archstone traded as low as $54 in August amid speculation the deal wouldn't get done, but changed hands Friday at 59.50.

Other proposed deals that now look safe include Hilton Hotels (HLT), Harrah's Entertainment (HET), TXU (TXU), Alltel (AT) and Clear Channel Communications (CCU). Takeover-arbitrage spreads on these buyouts have narrowed sharply in the past month. In early August investors stood to generate annualized returns of as much as 100% if transactions closed on time, but projected returns in some cases have since fallen to 10%.

Three big deals that still look dicey are SLM (SLM), the student lender; Tribune (TRB), the newspaper and TV company, and Harmon International (HAR), a maker of audio products.

The LBO environment has improved as the credit markets have calmed, and as banks generally have shown no inclination to shirk their lending commitments. The junk-bond market rallied sharply last week, helped by the Federal Reserve's move to cut the federal-funds rate by half of a percentage point, to 4.75%.

Private-equity firms have scored big returns in recent years on LBOs such as as Hertz, Warner Music and Celanese. Yet the current crop of deals may prove much less lucrative due to high debt levels. Archstone-Smith looks like a particularly tough deal for the buyers, an investor group led by Lehman Brothers and Tishman Speyer. They are paying $21 billion, including assumed debt, for one of the country's top REITs, which owns apartment buildings in such desirable markets as Manhattan, the Washington, D.C., area and southern California.

Yet, even prime real estate can get buried in debt. As part of an institutional roadshow last week for Archstone debt and equity, the company revealed that annualized cash flow in the second quarter totaled $700 million, or only 70% of projected interest expense of $1.04 billion.

Archstone will carry $16 billion of debt, including $10 billion of secured loans, nearly all of which have been sold to investors. That debt carries a first lien on Archstone's buildings. Another $2.4 billion of bank debt will be offered to investors at an effective yield of about three percentage points above Libor, a key short rate now at 5.25%.

The equity in the deal may prove a tough sell. The bulk of the $5.1 billion offered will consist of a $4.6 billion bridge-equity commitment from Lehman Brothers, Banc of America Strategic Ventures and Barclays Capital. All three hope to resell their equity to institutional investors. The apparent pitch is that Archstone is a one-of-kind holder of prime properties, with great management and a strong development pipeline. The hope is it will generate high-single-digit annual gains in operating income from rent increases, although that may be tough to achieve given the weakness in the housing market.

Bridge equity is particularly risky because it sits at the bottom of a company's capital structure. Blackstone Group (BX) President Tony James said last week at an industry conference that the granting of bridge equity by banks marked a high-water mark in the LBO business. "We just couldn't believe that banks would give us equity bridges," he said.

Among the headwinds for the equity sale is that the REIT market has undergone a sell-off since Archstone agreed to go private in late May. Shares of some multi-family REITs are down 15% or more.

Some investors may question the merits of buying illiquid equity in a heavily leveraged company that isn't covering its interest expenses, especially when publicly traded REITs look more attractive. REITs have less leverage, carry a lower valuation, offer liquidity and generate positive cash flow and dividends. It will be a tribute to Wall Street's marketing prowess if Archstone equity is sold.

First Data, the transaction-processing company, is a classic example of a good company with a bad balance sheet. First Data will be shouldering some $22 billion of debt, and its combined interest expense and capital expenditures could exceed cash flow in both 2008 and 2009, creating potential operational and financial risks.

One investor calls First Data a "running-in-place" LBO, because KKR probably won't be able to cut debt anytime soon. Debt reduction is a prime way private-equity firms create value for their LBO investors. KKR is betting First Data will be able to grow its way out of its financial predicament. The company has said it's capable of generating annual revenue and profit growth of at least 8% to 10%.

KKR's equity in First Data likely is under water because there's little chance the firm could get anything close to $29 billion if it tried to sell the company. Financing for such a deal would be much more expensive than KKR's all-in debt cost of 9%, if it could be obtained at all.

KKR and First Data say profits will improve dramatically when the company is private. In a regulatory filing last week, First Data stated its actual cash flow was $1.8 billion in the year ended June. But the company prefers a more generous definition of cash flow, reflecting a series of assumptions about cost savings from outsourcing, technology initiatives and other factors. By that calculation, the company would have generated $2.5 billion of cash in the same period.

Even so, First Data could be in a bind. Its annual interest expense is running at $2.1 billion and capital expenditures around $400 million. If it generates $2.5 billion of cash next year, it will have no free cash after interest and capital expenditures. If cash flow is closer to $2 billion, it will burn cash.

Given that backdrop, a consortium of banks didn't have an easy time last week selling $5 billion of First Data secured debt. Assuming a $5 billion sale, the banks will be left holding $17 billion of debt, consisting of $8 billion of secured loans and $9 billion of junk bonds.

The unsecured junk bonds could prove a harder sale than the more senior bank debt. Due to First Data's high leverage, the junk debt is viewed as carrying equity-like risks and thus may require a yield as high as 13% or so to attract buyers. KKR's equity interest could take years to show a profit, and the deal could prove a rare setback for the firm.

With the credit crisis seemingly over, conditions in the buyout market are easing. For buyout specialists, however, the sweetest days may have passed.
