THE WALL STREET JOURNAL

TUESDAY, JULY 18, 1995

The '80s Villain, Vindicated

By JONATHAN R. MACEY

As deplorable as Joe McCarthy's attacks on alleged Communists were in the 1950s, the government's attack on Michael Milken during the 1980s was even worse. It was more conspiratorial; it sent more people to jail, and it was, at bottom, an attack on such fundamental American values as entrepreneurship, individual responsibility and, ultimately, capitalism itself. This is the lesson of Daniel Fischel's "Payback" (HarperCollins, 332 pages, $25), a book that may well change our understanding of the "decade of greed."

Mr. Milken transformed his firm, Drexel Burnham Lambert, from almost total obscurity into America's premier investment bank. He did this by using high-yield securities ("junk bonds") to finance new firms and to restructure existing ones. Mr. Milken did not invent high-yield

Bookshelf

"Payback: The Conspiracy to Destroy Michael Milken and His Financial Revolution"
By Daniel Fischel

bonds, but he came very close to perfecting their use. And on his way he changed the face of corporate America, conducting a one-man industrial policy that largely created the basic infrastructure for the U.S. economy today.

Imagine the world without cellular phones, CNN or meaningful long-distance competition. Mr. Milken's deals provided $21 billion in financing critical for such firms as MCI, Warner Communications (now Time Warner), Twentieth Century Fox, Viacom, McCaw Cellular and Turner Broadcasting. Without Mr. Milken's vision for MCI, for example—which came in the form of $3 billion in financing when MCI had a mere $234 million in revenues—the U.S. still would not have the network of fiber-optic lines important to support cable TV.

And this is just to highlight Mr. Milken's contribution to the telecommunications industry alone. Junk bonds were used in all the deals where the threat of failure was too high to permit the issuance of equity or rated debt securities, or where banks' inability to diversify made commercial lending impractical. Mr. Milken's junk bonds provided access to capital for hundreds of firms that never would have gotten off the ground without them. His financings also forced firms like CBS, ABC and RJR Nabisco to restructure, and broke up inefficient conglomerates like Beatrice and Northwest Industries.

In "Payback," Mr. Fischel, a professor of corporate law at the University of Chicago, tells the story of the vengeful response by America's business and regulatory establishment to Mr. Milken's phenomenal success. The attacks on Mr. Milken were begun by prominent establishment competitors, particularly Felix Rohatyn of Lazard Frères and Nicholas Brady of Dillon, Read. When these competitors woke up to discover that Drexel was at the heart of American corporate finance (and not old-line firms like theirs), they responded by launching a public-relations blitz to frighten the public about the "over-leveraging of corporate America."

But, as Mr. Fischel carefully explains, Mr. Milken's deals created enormous value. This value triggered a rise in the stock market, which, in turn, meant that the only meaningful statistic, the amount of corporate debt relative to equity, was lower during the 1980s than it had been in the previous decade, and quite low by international standards.

Predictably, the bankers' cries of alarm were soon joined by second-rate academics like Robert Reich and corporate lawyers like Martin Lipton. Under public pressure, the SEC soon jumped on board. Politically ambitious politicians like Rudolph Giuliani were quick to exploit the situation.

The most frightening part of Mr. Fischel's book details how the politicians, prosecutors and regulators used obscure, highly technical regulatory violations as the cornerstone for criminal prosecutions of Drexel Burnham, Mr. Milken and others. Lovers of Kafka will enjoy reading about how the government refused even to define much of the conduct it was prosecuting, and how Mr. Giuliani used baseless charges against innocent people as a springboard for his own political career, even going so far as to abuse the RICO statute by converting routine civil tax disputes into major criminal prosecutions.

The most incredible part of Mr. Fischel's story is the way that the government used Mr. Milken as a scapegoat for the savings-and-loan fiasco, which eventually required a taxpayer bailout of more than $150 billion to save the most regulated industry in America. The government simply lied about the role of junk bonds in the S&L crisis: These bonds never accounted for more than 1% of the assets of the S&L industry. Indeed, the thrift industry's problem was that it didn't own *enough* junk bonds. Junk-bond portfolios, particularly those underwritten by Mr. Milken, have long been America's best fixed-income investment, even during the recession of the early 1990s.

As federal authorities pursued Mr. Milken, they succeeded in transforming the U.S. from a place where entrepreneurs were respected for their contributions to our country to a place where entrepreneurship was vilified as greed. That legacy is still with us. Our most notable corporate success stories—including, recently, Microsoft—are routinely attacked by the government at the height of their success. After reading this book, one wonders whether America will be remembered as the economy that ate its own young in order to appease the insatiable appetite of the regulatory state.

Mr. Macey is a professor at the Cornell Law School.