The Iron Triangle

The blurred boundary that helped Carlyle to reap benefits

by Dan Briody

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In the second and final extract from his book Dan Briody examines how Carlyle rose to become the dominating global private equity firm it is today

THE election of George W. Bush to the presidency of the United States promised to be a major boost to Carlyle's business. Accordingly Carlyle handed out more than $427,000 in political contributions in 2000. Eighty-four per cent of the money went to Republicans, making Carlyle the most partisan of the top ten defence contributors.

After George W. Bush's swearing in, the national media immediately picked up Carlyle's scent. As a member of Carlyle's Asian advisory board, Bush Sr. was visiting the Middle East and, in particular, Saudi Arabia. Photos taken of a meeting between Bush Sr. and King Fahd started popping up all over the internet. A natural confusion arose over the nature of Bush's visits to foreign dignitaries. Was the former president representing US interests? Or was he just there on behalf of a money-making behemoth by the name of the Carlyle Group? The same questions arose in the United Kingdom over the actions of John Major, who accompanied Bush on the trips to Saudi Arabia.

Of greater concern was that Major and Bush Sr. had been to see the bin Laden family, the wealthy relatives of a known terrorist (by this time Osama bin Laden was unambiguously viewed as a terrorist threat to the United States and estranged from his family). It wasn't clear what either of the former world leaders were up to. And it was this confusion, on the part of both the public and foreign world leaders, that played to Carlyle's advantage. Carlyle repeatedly reaped the benefit of blurred boundaries, with foreign business owners and world leaders not knowing whether Bush Sr. represents American political interests or Carlyle's financial interests. That was, and still is, a very powerful tool for Carlyle.

On May 27, 1999, George Bush Sr. touched down in Seoul, Korea, for a whirlwind business trip. His visit was celebrated in Seoul, with newspapers hailing his arrival, excited about the possibility of American investment in Korea in the wake of the Asian Economic crisis of 1998. He met Prime Minister Kim Jong-pil, and president of the United Liberal Democrats party Park Tae-joon, a major political figure in Korea who had been advising Carlyle since 1998. He also met the chairman of Korea's Financial Supervisory Commission, Lee Hun-jai, chairman of SK Telecom, Choi Tae-won, and the president of an ailing Asian conglomerate called Halla. Again, it was classic Carlyle: a measured blend of business and politics that sufficiently blurred the boundaries between the two.

Carlyle was really starting to get busy in Korea now. That same spring, the company hired Michael Kim, a Harvard-educated native Korean, to open its new Seoul offices. Kim is the son-in-law of aforementioned Park Tae-joon. Carlyle and nepotism seemed to go hand in hand.

Following Bush's visit Korean newspapers lauded an announced $1 billion investment in the country by Carlyle, including a buyout of a division of Mando Machinery, a Korean industrial firm, owned by Halla, the same company Bush Sr. had visited weeks earlier. By now Michael Kim was working to put together another massive deal. This time Carlyle was looking to buy one of the few healthy banks left in Korea, KorAm Bank.

Carlyle gained approval for the buyout by the KorAm board, thanks to its highpowered connections with Park Tae-joon, who became Prime Minister of South Korea in January of 2000 and lobbied on Carlyle's behalf. By the fall of 2000, Carlyle had snagged 40.7 per cent of the bank for $450 million. Carlyle had invested close to a billion dollars into Korea's recovering economy. It was the best financial news Korea had seen in years, and it was largely Carlyle's doing. But the mirth would soon come to an abrupt halt.

When George W. Bush was sworn in to office in January 2001, everything changed suddenly and dramatically. One of the first things that young Bush did as President was call off the missile control talks that the Clinton Administration had been conducting with North Korea for years. Bush revealed open hostility toward North Korea, calling it a rogue state. It was a stunning reversal of American policy, which heretofore had been to use diplomacy in mitigating North Korea's military aggression to South Korea. Not surprisingly, the backlash was felt far and wide. This also threatened Carlyle's extensive investments in South Korea, which would plummet in value as instability in the region increased. At first it seemed as if this was a rare case in which being associated with the Bushes was not going to work to the benefit of Carlyle.

On June 6, Bush reversed course. After what the *New York Times* described as a "forceful'' discussion with his father, the President announced plans to resume negotiations with North Korea, picking up where the Clinton Administration had left off. Among the issues that the new Administration would work on with North Korea was improving relations between North and South Korea. The sigh of relief could be heard around the world, and especially from Carlyle's offices on Pennsylvania Avenue and in Seoul. Carlyle refuses to talk about how ex-president Bush is compensated for his work on their behalf. Former employees, however, say that he is invested in the funds that he helps raise and place. If that is the case, the senior Bush's involvement in foreign policy regarding South Korea is a clear conflict of interest. He stands to gain financially from decisions he is urging his son to make. It doesn't get any more egregious than that.

By now, the world outside of Washington, DC, had a vague and nagging notion that there was something wrong with the way Carlyle was conducting its business. They were just having trouble putting a name to it. Everyone was looking for the proverbial smoking gun. Little did they know that it was literally a smoking gun they would find.

The saga began in the summer of 1997, when Carlyle was raising money like mad, hiring world leaders, and, in general, becoming the dominating global private equity firm it is today. Among the investments Carlyle had targeted was a maker of armoured vehicles named United Defence.

The news around the defence industry was that General Dynamics had bid $1 billion for United Defence, far more than any other bidder. But at the last minute the company was sold to the Carlyle Group, which had submitted a low-ball bid of $850 million, 15 per cent less than General Dynamics had been offering. It turns out that rumours had begun to circulate around Washington that General Dynamics was going to run into antitrust issues. Eventually, the rumours grew so loud that General Dynamics was forced to back out of the bidding, and Carlyle was there to pick up the scraps. It was another stunning victory for Carlyle.

There was one drawback. Since 1994, United Defence had been working on a massive gun: a mobile howitzer that can fire ten rounds of 100lb shells per minute, 25 miles in distance, cruise at 29mph, and reload on the battlefield.

The Crusader was the most advanced artillery system the US Army had ever conceived. It is the kind of weapon that makes the United States unbeatable in large-scale, open warfare, lobbing multiple shells at varying trajectories so that they rain down at their desired target at the same time. It is a fearsome weapon. It was also United Defence’s cash cow.

But times had changed considerably since Crusader was first conceived in the early 1990s. In fact, the very nature of war had changed and had left Crusader behind. The gun had two very serious problems. It was too big, and it was designed to fight a type of battle that no longer presented itself to the US armed forces. At 40 tons each plus a supply vehicle that weighed another 50 tons, the Crusader was a Cold War-inspired weapon, rapidly approaching obsolescence in an age of swift deployment and agile forces. There were those in the Pentagon who wanted the Crusader programme dramatically scaled back and some wanted it cancelled outright. But, losing the Crusader contract, originally valued at $20 billion, would jeopardise the future of United Defence and would be a mighty hit to Carlyle.

The effort Carlyle put forth to save their precious gun would illustrate exactly how the Iron Triangle of defence, government and business work together to the benefit of all three. Carlyle had been built to prevail in situations like these, when the large amounts of money were riding on the decisions of a few men in public office. It was time to call in a few favours.

Carlyle and United Defence mounted a political battle for Crusader. In the cycle leading up to the 1998 elections, United Defence made campaign contributions of only $49,500. But by 2000, under Carlyle’s leadership, the company had spread around more than $180,000 to more than 70 senate and house members. The bulk of the company’s largesse went to politicians on the house and senate arms committees. And often, a good deal of money found its way to the house and senate members whose districts were expected to participate in manufacturing the Crusader. It was also uncanny how United Defence planned to build manufacturing facilities for the Crusader in the back yards of key members of the arms committees, creating jobs and wealth. These are the kinds of things that get politicians re-elected, and get businesses what they want. Carlyle was thorough and strategic, and it was starting to make up ground. Reports of Crusader’s death had been greatly exaggerated.

Carlyle representatives assure the public that their high-profile hires like George Bush Sr. and James Baker do not lobby. That, of course, is true. But to say that the Carlyle Group doesn't lobby is simply not true. Does the Carlyle Group register as lobbyists? No. Do they hire lobbying firms to do it for them? Yes. Do they influence key lawmakers and help shape policy? Of course they do. People like George Bush Sr. don't need to lobby, in the traditional sense of the word. They already know the lawmakers involved in key decisions, and the lawmakers know them. There are memorandums and meetings. There are unspoken understandings that are reached over a drink and a wink.

"It's impossible to say when people working for Carlyle are wearing more than one hat,'' Peter Eisner, managing director at the Center for Public Integrity, told me. It would be ludicrous to imagine George Bush Sr. fighting it out in the trenches with all the other registered lobbyists. But does George Bush Sr. have a say in policy decisions made by this White House? This has already been proven.

Regardless of your definition of lobbying, in the case of the Crusader Carlyle lobbied hard, spending more than $1.2 million in 2000 to wage battle on Capitol Hill on behalf of United Defence. The Crusader was saved for the time being. When Bush's proposed defence budget for 2002 was handed down in June 2001, it included funding for Crusader. And within two months of the decision by Bush, Carlyle took its first dividends from United Defence, a windfall of $289 million. But opponents continued to fight to have the programme cancelled.

The raging debate would not be settled until May 2002, when Secretary of Defence Donald Rumsfeld finally decided against Crusader and cancelled the programme. The last casualty was Secretary of the Army Thomas White, a former Enron executive, whose resignation followed a last-ditch battle for a hopeless cause.

Ultimately, the success of the Carlyle Group depends on its continuing ability to gain access to high-level government officials, thereby getting a jump on policy changes, both domestic and international. And that access hinges on Carlyle's remarkable track record of hiring the most powerful men in the world.

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