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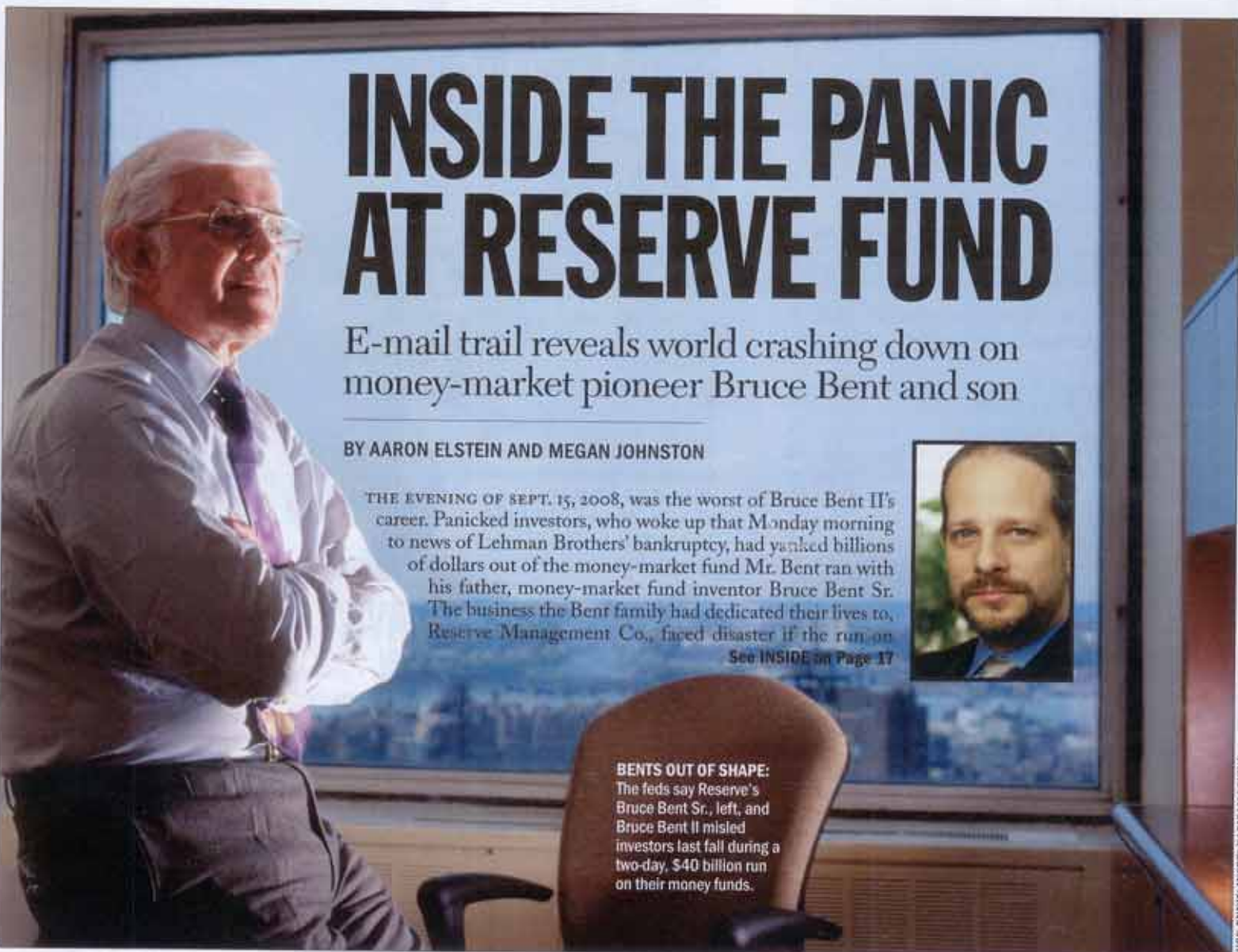
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INSIDE THE PANIC AT RESERVE FUND

E-mail trail reveals world crashing down on money-market pioneer Bruce Bent and son

BY AARON ELSTEIN AND MEGAN JOHNSTON

THE EVENING OF SEPT. 15, 2008, was the worst of Bruce Bent II's career. Panicked investors, who woke up that Monday morning to news of Lehman Brothers' bankruptcy, had yanked billions of dollars out of the money-market fund Mr. Bent ran with his father, money-market fund inventor Bruce Bent Sr. The business the Bent family had dedicated their lives to, Reserve Management Co., faced disaster if the run on Reserve Management Co. faced disaster if the run on

See INSIDE on Page 17



BENTS OUT OF SHAPE: The feds say Reserve's Bruce Bent Sr., left, and Bruce Bent II misled investors last fall during a two-day, \$40 billion run on their money funds.

Can Google guy turn around AOL?

Spinoff could bring Time Warner unit out of tech dark age

BY MATTHEW FLAMM

SINCE HE TOOK THE REINS of AOL just a month ago, Tim Armstrong has been traveling the globe, getting a feel for the long-troubled Time Warner division.

His goal, he has said, is to re-

claim the "magic" of the AOL name. That might not seem a stretch to someone whose résumé includes building Google's ad sales business into a juggernaut from scratch.

The only problem is Mr. Armstrong is not at Google anymore.

AOL's third chief executive in three years has been handed a company that's like a 21st-century version of the Edsel. Despite operating popular niche sites like gossip heavyweight TMZ and Engadget, AOL is still associated with the Internet's dial-up days—and with the most disastrous corporate merger in history.

Mr. Armstrong and fellow Google alum Jeff Levick, who was recently named president of global advertising, have a lot of damage to undo.

They'll be preparing AOL for a



RESTORING A RELIC: Tim Armstrong runs the 21st-century version of the Edsel.

likely spinoff, which would allow Time Warner Chief Executive Jeffrey Bewkes to finally rid the media giant of a property that has been a drag on its stock price since 2001.

The spinoff would also be good
See TURNING on Page 20

Bulk sales of condos spreading

Developers try package deals to lure investors

BY AMANDA FUNG

AFTER NINE MONTHS and a total of only four tentative sales at its six-story condominium in Harlem, owner Gaetano Development Group decided the time had come for a radical change of tack. Last month, the company began marketing substantially discounted bundles of some of the 18 unsold units at its Lore Condominium—not to people looking for a home, but to investors looking to make a killing in a depressed market.

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Tenants lobbying for rent cuts

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increasingly short supply. Leasing activity totaled only 3 million square feet in the first quarter, the lowest level in 25 years, according to Cushman & Wakefield Inc. Overall leasing activity tumbled 39% from the first quarter of 2008.

The asking rent for office space has dropped 11% since hitting a high of \$72.97 a square foot in the third quarter of 2008. But brokers say actual rents are down about 30%. Meanwhile, the vacancy rate rose to 9.6% in the first quarter, from 6.1% a year earlier.

Hedge funds a bad bet

THE RETAIL PICTURE looks worse. The Real Estate Board of New York said overall retail asking rents have dropped 11% since last fall. Brokers say actual rents are likely down by closer to 50%.

That backdrop creates a dilemma for landlords fielding calls for rent reductions. While landlords don't

want to cut their own income, they also don't want to lose a tenant if they can help it. The trick is figuring out where to place their bets, so they don't extend credit to companies that will only go belly-up anyway.

Sources say hedge funds are like-

Landlords don't want to cut their income, but they also don't want to lose a tenant

ly to get turned down by landlords because so many are likely to fail amid the explosion in redemptions and because they have so little in the way of assets to seize in a bankrupt-

cy. Long-term tenants and those whose leases have only a few more years to run have the most leverage.

Personal guarantees

ONE WAY TO SOLVE the problem is to offer them a chance to renew their leases earlier at the now lower market rates, notes Mr. Malkin. He's done that in two cases and is weighing a temporary rent reduction in a third. Mr. Malkin also points out that he fully expects the tenant to pay interest on what amounts to a loan.

Mr. Levy says he has granted temporary reductions ranging from 10% to 15% to about 25 tenants. While he doesn't ask for interest or a viewing of the tenant's books, he does demand a personal guarantee from a company's chief executive that the money will be repaid.

"I think that is a good way to smoke out the people who are really sincere about needing [a break]," Mr. Levy says. ■

Inside the panic at Reserve fund

Continued from Page 1

their fund continued.

As the younger Mr. Bent, Reserve's president, sifted through his e-mails, he reviewed a statement drafted by his marketing staff to calm investors. The final line proclaimed that Reserve was "confident in the underlying credit strength and quality" of its holdings, which included hundreds of millions in debt from Lehman and other free-falling institutions, including Washington Mutual and Merrill Lynch.

"Drop the last line," he directed, "and then go with it."

Unfortunately, this editing job represented one of the few times Mr. Bent or his father, the chairman of Reserve, were honest with shareholders in the three terrible days their firm spiraled downward, according to regulators.

The Securities and Exchange Commission last week charged the Bents and Reserve with fraud, alleging that they failed to provide key information to customers, board members and credit-rating agencies after Lehman collapsed. Reserve and the Bents said they would support the \$1-per-share asset value of their fund when in fact there was no such intention, the SEC contends. The agency also charges that Reserve misled directors and credit raters by significantly understating how many investors were yanking money after the Lehman bankruptcy hit.

By 8:37 a.m., \$5.2 billion yanked

THE DAY AFTER Mr. Bent approved his marketing staff's statement, disaster struck: Reserve, whose pioneering money-market fund in 1970 spawned a \$3.8 trillion industry, "broke the buck." In other words, the net asset value of its flagship \$62 billion Primary Fund fell below the sacrosanct \$1 a share because the fund held \$785 million in Lehman debt that was suddenly worthless. It was only the second

time in history a money-market fund broke the buck—and it unleashed such panic in the stodgy world of cash investments that the federal government had to intervene by week's end to guarantee money-fund holdings.

Court documents, including copies of e-mails and board minutes, show that Mr. Bent saw trouble brewing even before Lehman filed for bankruptcy. Late Sunday night, Sept. 14, he ordered senior staffers to work on a customer memo "that assumes Lehman liquidates" and warned that Reserve could see up to \$1.5 billion of client redemptions the next day.

It turned out much worse than that. "5.2 billion already?" a stunned Reserve executive wrote in an e-mail on Monday at 8:37 a.m. Meanwhile, Mr. Bent and his father, who was in Italy on vacation, were working behind the scenes. Some 45 minutes earlier, unbeknownst to their board, the SEC alleges, they had contacted the Federal Reserve Bank of New York for assistance. The Fed declined.

By midmorning, redemptions were accelerating—they reached \$40 billion over two days—and Reserve couldn't meet the demand because its bank, State Street, stopped wiring funds shortly after 10 a.m.

This was the moment. With his father far away, Mr. Bent had to show he had matters in hand. Was he up to it? Known in the industry as Bruce Two, his long hair and a beard hinted at his youthful past as a drum-playing philosophy major. "He was very quiet, very mellow, very introspective," says Peter Crane of money-market tracker Crane Data.

But the 42-year-old had greatly expanded his father's business. Assets under management grew from about \$4 billion in the mid-1990s, when he was handed day-to-day control of operations, to \$18 billion in 2002, and swelled to \$125 billion

last year. Reserve shifted from courting individuals to attracting big corporate accounts like Time Warner. Its biggest client last year, with \$5.4 billion in the Primary Fund, was China Investment Corp.

At 1:19 p.m. on Sept. 15, Mr. Bent e-mailed senior staffers, saying the firm would financially support the Primary Fund "to whatever degree is required" so it wouldn't break the buck. He added that Reserve was awaiting SEC approval, although the SEC contends it never heard from Reserve on the matter and alleges the Bents had no intention of producing the hundreds of millions of dollars necessary to support the ailing fund.

No cash lifeline, no acquirer

THE NEXT DAY, Sept. 16, Mr. Bent in New York and his father in Italy fruitlessly searched for a cash lifeline or an acquirer. Later that afternoon, Reserve announced that the buck had in fact been broken.

It was a stunning fall for a firm that had long touted its funds as the ultimate in safety. The trouble seems to be rooted in 2007, when the senior Mr. Bent, who oversaw investment decisions, began buying short-term debt from brokerage houses like Lehman and Merrill Lynch. Those moves boosted yields and attracted more customers for a while.

In a statement last week, Reserve said it "intends to defend itself vigorously" and the elder Mr. Bent said he is "confident that we acted in the best interest of our shareholders." The Reserve Primary Fund is being liquidated. Massachusetts regulators have also filed fraud charges, and nearly 30 shareholders have sued.

Perhaps in anticipation of the costly legal battle ahead—not to mention a seriously diminished income—the younger Mr. Bent has put his 10-room penthouse apartment in the West Village up for sale. Asking price: \$14.5 million. ■



MANHATTAN'S LORE AND 505 BUILDINGS: Developers place their bets on luring investors.

Condos by the gross

Continued from Page 1

"The developer has other jobs to move on to," says Stephen Kliegerman, executive director of development marketing at Halstead Property, who reports that a South American real estate investor is close to buying the first such package. "Bulk sale is a way to move units in a timely fashion, versus selling them one-off."

With thousands of unsold condo units weighing heavily on the market and the backlog mounting every month, more and more developers are following Gaetano's lead. In recent weeks, desperate landlords have put packages of anywhere from four units to entire buildings on the market at more than a dozen Manhattan and Brooklyn projects. Discounts range from 10% to 20% of already depressed listing prices—and those discounts are expected to widen.

A Florida phenom

NO BULK SALES have actually closed here yet, but trends in other states signal that the day will come soon. In Florida, where the market began to come unglued nearly four years ago, bulk sales are now commonplace. So far this year, there have been five big deals there. In one, the Related Group sold 101 units in its New Harbour House development in Bal Harbor for \$27 million—each was about half the price that some units were fetching there two years ago.

In New York, many observers note that landlords will have to come down further on their prices if they expect to make a bulk sale. Pressure is mounting for them to do just that. In Manhattan, the inventory of unsold condos hit 5,469 last month, up 21% from year-earlier levels, according to

appraisal firm Miller Samuel Inc.

In Brooklyn, there were 1,678 units on the market last month, up 4% from November, when Miller Samuel began tracking the borough's inventory. In Williamsburg alone, another 2,000 units are expected to come to market in the next two years, according to David Schorr, director of finance and development at brokerage AptsandLofts.com.

With the supply of units soaring and available financing shrinking, the time it takes to sell apartments is lengthening. In Manhattan, the average in the first quarter was 178 days—39% longer than the average over the past decade.

"Units can't stay vacant forever," says Ofer Cohen, managing director of TerraCRG, a commercial realty group that is currently working on a dozen bulk-sale projects in Brooklyn. "At some point, something needs to be done."

At The 505 in Hell's Kitchen, a package of four one-bedroom units is being offered for \$2.8 million. That is 10% under the cost of the apartments if purchased individually, according to Mr. Kliegerman.

Investors, though, are still waiting for New York to catch up to other markets like Florida, where prices are down as much as 60% from the peak. The hang-up is that even those developers that are willing to bite the bullet, cut prices and move on must get permission from their lenders first. With more tied up in most projects than what the developers put in, the banks are especially keen to minimize their losses.

"It takes a long time to adjust and reduce prices," says Mr. Cohen.

Works in progress

MANY OF THOSE arduous negotiations between the two sides are under way. Until agreements are actually struck, however, buyers are likely to remain on the sidelines.

"Unless these packages are discounted dramatically, there's no way they can be sold," says Andrew Geringer, managing director in charge of marketing new developments for Prudential Douglas Elliman. He and others note that for bulk buyers, the aim is to purchase at a price that will allow them to rent out their units and generate a return of at least 5%.

So far, Mr. Kliegerman has received 25 inquiries since marketing bundles at six developments in Manhattan and Queens late last month, but only one serious offer—at The Lore. Mr. Cohen has fared somewhat better. He has two contracts out, both for unfinished buildings—a six-unit building in Clinton Hill and a 100-unit building in Williamsburg. ■

A PLAN FOR UNSOLD UNITS

TALK ABOUT TURNING lemons into lemonade, City Council Speaker Christine Quinn thinks she may have a way to cut through the glut of unsold condos. She is pushing to have the city snap up vacant units from developers at bargain-basement, bulk prices and turn them into **affordable housing** for the middle class.

The scheme could give a big, yet relatively inexpensive boost to Mayor Michael Bloomberg's plan to create and preserve 165,000 affordable-housing units by 2013. However, many wonder whether the city's budget woes will impact the funds available for such an undertaking.