



“Corporate DNA: Forensic Evidence Points to a Killer Combination”

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By this time, most of us are aware of the sweeping damages caused by the collapse of Countrywide Financial Corporation (CFC). In fact, problems were apparent as far back as October 24, 2006, when Countrywide announced a layoff of 2,500 employees due to struggles with subprime debt. At the same time, Countrywide informed the public it would repurchase \$2.5 billion of the Company’s stock, or approximately one-eighth of the shares outstanding. The stock was trading in the high \$30’s. Three days after the announced repurchase, top directors, officers and employees began a massive insider sell-off (see Table 1 below), and the corporate DNA of a shareholder murderer was revealed. *The combination of weakening operations with share repurchases and insider selling is a real killer.*

From the original announcement on October 24, 2006, the stock reached a high of the low \$40’s in January, 2007, and from there continued to plummet until it reached a low of \$4.25 in June of 2008 and was put out of its misery by the Bank of America takeover.

Throughout this period, even while bad news continued to mount, senior management was extolling the virtues of the Company. They were so good at weaving their story, that employees were persuaded to hold their stock even as management sold (see Table).

Of course, as the charade continued, numerous “value investors” remained convinced that the stock was a great value and that all would get better. I strongly suggest the contrary. When three genetic markers – repurchases; insider selling; and weak operating results – show their ugly heads, things can only get worse.

Another living example of the DNA phenomenon is Lehman Bros. (LEH). The first of the three deadly genes started to become noticeable in the summer of 2006, as Receivables began to accelerate at a rapid pace – the first indication of the mortgage mess that was to follow. On February 1, 2007, Lehman announced a repurchase of 100,000,000 shares, which represented one-fifth of all shares outstanding. The stock price was hovering in the low \$80’s. Within less than three months, key management began unloading over 60,000,000 shares.

Not unlike Countrywide, Lehman continued to slide following the announced repurchase. Within one year, Lehman was struggling for its very existence, raising capital at every turn and liquidating assets to meet capital needs. This deterioration continues. Shareholders hold stock that has declined 80% while the top insiders walked away with their winnings.

Forensic analysis is an important tool in detecting crime. Luckily, in the investment arena DNA evidence can be read and acted upon before the murder is committed. Each of these three “genes” – deteriorating operations, insider selling, and repurchases – may be harmless by itself, but in combination, they are deadly. Investors are well-advised to be alert to these signals and avoid becoming victims.

James A. Kaplan
CHAIRMAN

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Table 1
COUNTRYWIDE FINANCIAL CORPORATION (CFC)
INSIDER SELLING SCHEDULE
2006-2007

Date Recorded	SELLING (U.S. DOLLARS)			
	Top Directors & Officers	Employees	Total D&O and Employees	Total Selling over Assets (bp)
10/12/2007	13,366,624	0	13,366,624	1.253
8/17/2007	1,306,400	0	1,306,400	0.125
8/10/2007	5,730,663	0	5,730,663	0.548
8/3/2007	2,219,815	0	2,219,815	0.212
7/27/2007	5,160,113	356,400	5,516,513	0.510
7/20/2007	6,625,131	0	6,625,131	0.633
7/13/2007	6,894,833	0	6,894,833	0.659
7/6/2007	157,330	0	157,330	0.015
6/29/2007	152,813	0	152,813	0.014
6/22/2007	3,804,708	93,750	3,898,458	0.355
6/15/2007	9,012,795	528,985	9,541,780	0.856
6/8/2007	7,442,431	95,628	7,538,059	0.691
6/1/2007	4,561,380	299,073	4,860,453	0.435
5/25/2007	1,869,518	504,360	2,373,878	0.196
5/18/2007	7,549,244	1,423,277	8,972,521	0.762
5/11/2007	7,332,458	2,715,739	10,048,197	0.802
5/4/2007	6,145,693	94,625	6,240,318	0.571
4/27/2007	5,297,005	982,564	6,279,569	0.534
4/20/2007	5,954,181	415,918	6,370,099	0.568
4/13/2007	3,888,201	0	3,888,201	0.359
4/6/2007	3,836,438	0	3,836,438	0.354
3/30/2007	1,556,093	0	1,556,093	0.150
3/23/2007	4,651,247	292,000	4,943,247	0.481
3/16/2007	4,588,249	121,908	4,710,157	0.447
3/9/2007	8,986,070	0	8,986,070	0.864
3/2/2007	4,851,753	94,204	4,945,957	0.471
2/23/2007	5,271,729	504,124	5,775,853	0.531
2/16/2007	8,291,507	2,240,989	10,532,496	0.905
2/9/2007	10,831,470	19,239,570	30,071,040	1.967
2/2/2007	604,731	759,308	1,364,039	0.095
1/26/2007	8,250,642	502,345	8,752,987	0.818
1/19/2007	2,478,776	1,946,370	4,425,146	0.332
1/12/2007	6,481,894	526,304	7,008,198	0.649
1/5/2007	4,523,612	740,560	5,264,172	0.471
12/22/2006	3,497,171	2,164,922	5,662,093	0.458
12/15/2006	6,272,029	1,924,458	8,196,487	0.724
12/8/2006	7,175,166	967,261	8,142,427	0.766
12/1/2006	1,555,532	2,602,714	4,158,246	0.286
11/24/2006	5,281,058	2,488,653	7,769,711	0.653
11/10/2006	4,128,709	96,233	4,224,942	0.418
11/3/2006	4,097,737	1,628,635	5,726,372	0.491
10/27/2006	1,028,901	5,391,715	6,420,616	0.373

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