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FROM LIMELIGHT TO BLUE LIGHT

Eddie Lampert made his $4.5 billion fortune by investing in companies and turning them around. But the buyout cycle has ended, and the hedge fund manager who has been compared to Warren Buffett is now being forced to change his strategy.

1984

Lampert graduates with honors from Yale University and is hired by Goldman Sachs, where he works directly under Robert Rubin.

1988

Lampert leaves Goldman Sachs with the intention of starting his own firm. Rubin warns him that leaving would be a bad career move, but he does it anyway.

1988

Through contacts in the financial world, **Lampert hooks up with Texas investor Richard Rainwater,** who agrees to provide the majority of the $25 million in startup capital to launch ESL Investments, a hedge fund. Over the years, Lampert's client list would come to include the likes of Michael Dell, left, and David Geffen.

1997

Lampert's ESL starts purchasing shares of AutoZone. By 1999, it owns a 15.7 percent interest in the company, and he wins a seat on the board.

2002

Lampert begins buying bonds of bankrupt retailer Kmart. In 2003, he gains a majority interest and is named chairman of the board. He announces that he plans to merge Kmart with another struggling company, Sears.

2003

Lampert is kidnapped by four men, one an ex-Marine, in ESL's parking garage on a Friday night. He is held in a motel bathroom until he persuades his abductors to let him go in exchange for a promised ransom. —*DAVID LEVINE*

a protégé of Texas investor Richard Rainwater. He struck out on his own at the age of 27 and made a series of savvy, concentrated bets on undervalued companies. An early win was an investment in I.B.M. at an early point in Lou Gerstner's reign, a storied turnaround that Lampert refers to in letters to shareholders as a model for Sears.

For years, money managers like Lampert have been in the ascendancy, taking over all sorts of companies with the idea that they can manage them better or flip them for a quick profit. Financiers are now running some of the most storied names in American business—Chrysler, Hilton, Hertz, and *Reader's Digest*. Mostly, private equity firms have been taking over companies through buyouts. But Lampert-style activist investing has also been in vogue, reenergizing people like Carl Icahn and Nelson Peltz, who champion their strategies for companies and sometimes make takeover bids or grab seats on the board.

Many of these financiers insist they are in it for the long term. But in truth, they didn't have to be. Returns came easily. Companies could be flipped back to the public or another buyer in short order, generating huge gains. But now those tricks are played out. Financial markets have seized up. Cheap financing isn't available. For the first time, financiers are being forced—gasp—to manage their companies. They have claimed to have expertise in doing this very thing; now they have to prove it. And if Lampert's experience is any gauge, the challenge is going to be tougher than any of them expect.

This year, the cost cutting and slashing of capital spending caught up with Lampert. Net income at the company cratered, dropping 99 percent in the third quarter to $2 million. Sales at stores open a year or more, a key measure of retail performance, have continued to drop at both Sears and Kmart. And in the all-important holiday shopping season, things probably worsened. Sears stock fell nearly 40 percent in 2007. "We cannot blame our results entirely on the retail and macroeconomic environments," Sears C.E.O. Aylwin Lewis said in a prepared statement. "We have much on which to improve and are working hard to do so."

The problems at Sears and Kmart have also been costly for Lampert's hedge fund and for his status as a canny financier. His main $15 billion fund—made up substantially of Sears stock—was down a stunning 25.7 percent through November, according to a person privy to the results. Once hailed as the Warren Buffett of his generation, Lampert, at 45, now has another turnaround job on his hands: his own reputation.

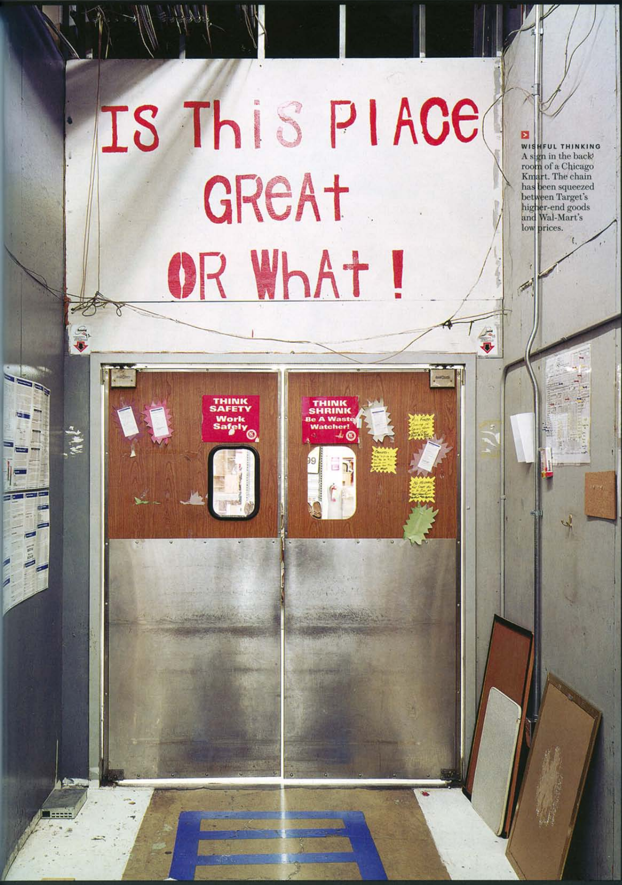
IN CONTROL

Lampert runs the $50 billion retailer in much the same way he runs his hedge fund—by overseeing the tiniest details, relying on a small coterie of advisers, and shunning conventional industry wisdom, convinced he knows better. He leans heavily on his No. 2 at the hedge fund, William Crowley, who has an underappreciated yet vital role in managing Sears. Crowley even served temporarily as the chief financial officer, as that position saw a succession of short-timers in recent years. Lampert and Crowley make almost every decision of significance at Sears Holdings, according to former colleagues at the hedge fund and employees of the company. Lampert is "trying to set an example that every penny counts, but no one feels empowered to make any decisions," says an ex-Sears official. "You wind up with a slower, more bureaucratic environment. People are more prone to be second-guessed."

Lampert rarely talks to the media or anyone on Wall Street. (The company declined to make Lampert available for this article.) Sears doesn't hold earnings conference calls, and analysts complain about how little contact they have with the company. Unlike the vast majority of publicly traded retailers, Sears Holdings stopped reporting its chains' monthly sales at stores open at least a year. Instead, Lampert writes letters to shareholders, taking a page from his idol Buffett.

When I ask some of Lampert's former colleagues what he was like, they answer like the brainwashed soldiers in *The Manchurian Candidate*. To a man, they say he is *(continued on page 130)*

PHOTOGRAPH *by* BRIAN ULRICH



WISHFUL THINKING A sign in the back room of a Chicago Kmart. The chain has been squeezed between Target's higher-end goods and Wal-Mart's low prices.