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## MUTUAL FUNDS

**FUND TRACK** | *By Jed Horowitz*

# Peter Lynch's Ethos Lives On at Merriman

## *Manager Ledger Shuns Uncertainty, Follows Convictions*

It was Peter Lynch, the avatar of Fidelity's Magellan Fund, who taught Steven Ledger to avoid being wishy-washy about stocks.

"It's either a buy or a sell," Mr. Ledger, who worked at Fidelity as an analyst from 1983 to 1989, remembers Mr. Lynch telling him. "You've got to look at your portfolio every day, and be willing to show that conviction. There's no such thing as a hold."

Mr. Ledger now manages Merriman Focus Fund, which styles itself as a "special situations long-short conviction fund." That means his team uses what he calls "private-equity-like diligence" to determine whether particular stocks, including many that aren't widely followed, are heading for a fall or will be influenced on the upside by an unusual event, such as a takeover.

### **Bet Against Countrywide**

His conviction last year that large financial company stocks such as mortgage lender Countrywide Financial Corp. and bond insurer MBIA Inc. were overloaded with risky assets led the hedge fund to a cumulative return of 40.7% in 2007, he says, after fees and expenses.

Because the fund manages only about \$25 million, it isn't required to file reports about its holdings with the Securities and Exchange Commission.

"We were short pretty much all the investment banks and some other big-cap financial-services stocks whose prices we felt didn't reflect their balance-sheet risks," said Mr. Ledger, who also is president of Merriman Curhan Ford's MCF Asset Management division and who continues to be a bear on financial stocks. "That began to pay off in August."

Merriman Focus, which has a minimum investment requirement of \$500,000 and began trading in 2002 under the name Tamalpais Partners LLC, continues to have significant short positions in Countrywide, Lehman Brothers Holdings Inc., Merrill Lynch & Co., J.P. Morgan Chase & Co., insurer American International Group Inc. and several small-cap community banks. Since the beginning of the year, Countrywide shares are down 44.3%, Lehman and Merrill are off 43.7% and 18.4%, respectively, and MBIA is down 62.2%.

Merriman Focus's returns are down about 1.1% after fees through the end of April.

### **Burned by Congress**

Why the fund's drop this year? Mr. Ledger shorted mortgage agencies Fannie Mae and Freddie Mac, which rebounded more than 40% from their March lows after Congress and regulators liberalized some of their operating rules.

"You never know what can happen" with a financial stock, Mr. Ledger said. "There could be a rescue or rule changes and you can have a short squeeze very quickly."

J.P. Morgan, Mr. Ledger's most unusual "conviction short" at the moment,

is off just 1.8%, but he thinks the bank's dominance as a dealer in credit default swaps exposes it to major risks if the economic slowdown endures. The short position is an "insurance policy" against a systemic downturn, he says, but can fairly quickly be reversed because the stock is liquid, he says.

Merriman Focus's long positions—which typically make up the majority of its holdings—emphasize Mr. Ledger's stint as a venture capitalist who sold a start-up called LowerMyBills.com to Experian Group. The stocks tend to be small start-ups, and his first criterion of due diligence is to evaluate management and "bet the jockey."

InsWeb Corp., which has a market capitalization of just \$46 million and generates leads for auto insurance companies by providing comparative car insurance ratings for consumers, is one of his five biggest holdings.

Mr. Ledger also has invested more than 5% of Merriman Focus in Chindex International Inc., a bet on the growth of modernized health care in China. Chindex is based in Maryland, but the \$300 million-market-cap company, gets 100% of its revenue from distributing medical equipment in China and operating clinics and private hospitals there for expatriate Westerners.

"I'm sort of scared to death of China, but I look for ways to access the market with relatively low risk," says Mr. Ledger, noting his confidence in the company's managers and a recent \$50 million capital infusion in Chindex from J.P. Morgan's private-equity group.