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Bear Seeks Fallen Fund Solution

By JEREMY HERRON AP Business Writer

NEW YORK — Bear Stearns Cos. narrowly averted the very public collapse of two hedge funds this week after rivals balked at forcing their immediate dissolution.

But now that investor Merrill Lynch has auctioned off some of the best assets and other Wall Street firms are cashing out of their stakes, Bear still has to figure out what to do with what's left.

The most likely outcome, experts say, is that the remaining investors agree to private transactions to recoup their money and Bear buys any assets it cannot unload.

"The fund doesn't have much of a future," said Mark Zandi, chief economist at Moody's Economy.com. "It's just a matter of retiring it in a relatively orderly fashion."

Bear Stearns declined to comment.

According to people familiar with the situation, speaking on condition of anonymity because they were not authorized to speak publicly, two major investors _ Bear rivals Goldman Sachs & Co. and JPMorgan Chase & Co. _ agreed to unwind their positions in private transactions.

Zandi expects the other Wall Street investors, including Deutsche Bank and dozens of other creditors, will give Bear even more time to sell the funds' assets.

"That's in everyone's best interest because then they won't have to revalue assets in their own portfolios," he said.

The value of the assets in these types of funds is difficult to determine because there is no active market setting prices. Once there is a sale of similar securities, though, funds have to re-value their assets based on those prices. A fire sale of Bear assets likely would trigger lower asset values on the books at numerous funds.

Merrill Lynch did request collateral for its investment and sold some of the bonds in an auction Wednesday, covering its position. But those assets were highly rated and apparently readily found buyers on the market.

What's left, though, is a portfolio with a higher percentage of risky investments. And Bear might have trouble selling them in private or on the market, said Axel Merk manager of the Merk Hard Currency Fund.

One option is for the firm to buy the assets itself and hold onto them until they mature,

"If they just carry it on the books, it's not going to cause any great harm," Merk said. That's because the underlying bonds will continue to pay interest, even if their market value drops further.

"The problem comes when you try to sell these investments," he said. "They are not standard and not very liquid so it's hard to put a price on them."

The main fund, called High-Grade Structured Credit Strategies Enhanced Leverage Fund, was started 10 months ago and invested mostly in securities related to risky mortgages, known as subprime loans. It held about $600 million in invested capital and had total borrowings of about $6 billion. Its sister fund, the High Grade Structured Credit Strategies Fund, had a similar strategy.

Merk said there is no need for Bear to write off the funds as a total loss because the assets have some value. But the prices of the underlying bonds in the funds probably will continue to fall as investor confidence in subprime mortgage-related securities wanes. That makes it unlikely that the fund will receive additional money to keep it afloat.

"I can't imagine investors would be interested in putting more money into it," Zandi said.
