Piper Manager's Losses May Total $700 Million

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MINNEAPOLIS – Derivative investments made by a single portfolio manager at Piper Jaffray Cos. could result in more than $700 million in losses to investors.

The losses, which occurred in funds managed by Worth Bruntjen, include the already-disclosed losses in what was the company's $800 million Institutional Government Income Portfolio short-term bond fund as well as additional losses from other investment funds and a number of privately managed accounts. The Institutional fund has fallen 23.3% since the beginning of this year, according to Lipper Analytical Securities Corp. Edward J. Kohler, the president of Piper Capital Management, said the other fixed-income funds managed by Mr. Bruntjen have experienced losses of the same magnitude.

Worth Bruntjen

Since Mr. Bruntjen managed $3.5 billion in assets at the end of last year, that rate of decline suggests total losses of slightly more than $800 million. In an interview, Mr. Kohler said Mr. Bruntjen's investment accounts "had the same kind of objectives, so they had the same kind of investments – and the same kind of losses."

Robert Markman, president of Markman Capital Management, another Minneapolis-based money manager, asserts that "this is one of the most incredible debacles in the financial-services industry."

Mr. Bruntjen's portfolios affect every possible type of investor: municipalities and other public agencies, individuals, businesses and charities. For Piper, a respected regional brokerage firm that celebrates its 100th anniversary next year and prides itself on the loyalty of its clients, the losses are tremendously damaging.

Mr. Bruntjen, the manager of the fund, wasn't available for comment, but interviews with other Piper executives and industry analysts trace the losses directly to Mr. Bruntjen's aggressive investments in derivatives. Derivatives are financial agreements whose returns are linked to, or derived from, the performance of some underlying asset, such as bonds, currencies or commodities.

"We got caught in a market that we thought we understood," said Addison L. Piper, the firm's chairman and chief executive officer.

Mr. Bruntjen specialized in collateralized mortgage obligations, securities that are created out of bundles of residential mortgages as well as securities that were derived from them. As much of 60% of his investment portfolios were invested in derivatives. In addition, he heightened the returns – and the risks – by using borrowed funds to purchase securities.

A Piper spokewoman said the value of the assets managed by Mr. Bruntjen had declined to $2.795 billion as of the end of June. Although the drop from $3.5 billion could reflect, to some extent, investors withdrawing their money, Piper executives said very few investors have done so. A spokeswoman said the decline "really is the difference in the market value" of the assets managed by Mr. Bruntjen. Using the change in managed assets as a rough approximation, the investor losses would total about $705 million

While investment advisers generally aren't responsible for the losses of their investors, several firms recently have felt compelled to compensate investors who have lost money in derivative-laden mutual funds. Some of those firms have also removed the most damaging derivatives from their funds. Piper has thus far taken neither of those steps, although it has made a $10 million investment in the Institutional fund as a show of confidence.

Many investors are pressing Piper to do more. And a consortium of Minneapolis lawyers has filed a suit that seeks to obtain compensation for investors in the Institutional fund. The suit claims that the fund's prospectus didn't adequately disclose the riskiness of its investment strategy and that marketing materials and oral sales presentations described the fund as a low-risk, principal-preserving investment. Because of the huge losses suffered by Piper clients, if a court were to order the brokerage firm to pay substantial damages to its clients, it could threaten the future of the venerable Minneapolis financial-services firm. Piper had shareholder equity of $168.9 million at the end of June.

A lawsuit by clients seeking class-action status has already been filed in federal district court in Minneapolis.

Piper executives dismiss the idea that the firm's survival is at stake. "We have had a long and distinguished history," Mr. Piper said. "We have to keep this in perspective."

Mr. Bruntjen's investment strategy worked extremely well prior to the recent rise in interest rates, allowing his funds to produce total returns last year that were about twice as great as other mortgage investments. The Institutional fund had been the best performing of the short-term U.S. government funds, and Piper officials point out that many investors who have seen paper losses this year have made substantial gains from Mr. Bruntjen's investments in the past.

In any event, when interest rates began rising this year, the value of Mr. Bruntjen's investments crashed. The Institutional fund, which at its peak had more than $800 million in assets, has

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