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Leslie Brinkman at Versutia Capital

Leslie Brinkman, CEO and founding partner of the hedge fund, Versutia Capital, sat in her comfortable new office on Fifth Avenue in New York City. She felt awful. Leslie did not understand how Versutia's performance could have deteriorated so rapidly. Only three months earlier, she and her team were receiving congratulations from the fund's investors regarding Versutia's 21% gain in 2004 versus the S&P 500 stock index gain of 11%. Now, in early April 2005, the fund had just finished its first "down" quarter, having lost 6% of its value while the S&P 500 index had lost only 2%.

As she looked at her desk covered with papers on key stock positions, Leslie thought back over each significant fund investment that had declined substantially during the first quarter. She could not help being furious that she and her staff had failed to anticipate the impact of key macroeconomic trends on specific stock market industry sectors and recognize warning signals relating to specific stocks. She wondered whether the firm's performance was indicative of broader issues relating to flawed investment processes, personnel inadequacies, deficiencies in organizational design or shortcomings in her management style. Leslie knew that she and her team were working 70-hour weeks and could not work any harder -- they were exhausted.

Leslie was painfully aware of how much work it would take to overcome this poor start and still have a successful year in which they outperformed the major market indices. She had begun to receive concerned, and sometimes angry, calls from investors -- including several who had called just three months earlier to congratulate her. She worried that some of these investors would redeem all or a portion of their holdings. She started to question her decision to sign a 10-year lease for the new office location. She also worried how these results might impact her team. While Leslie tried to keep a brave face for the staff, she could not help occasionally venting her frustration directly with them. She held numerous staff meetings attempting to understand what went wrong and scrutinizing each remaining investment position held by the fund.

Leslie was not sure exactly what to do. There were nine months left in the year and she knew that this next quarter would be critical to stabilizing the fund's performance and calming its investor base. Looking out the window at the trees beginning to bloom in Central Park, she wondered how she'd gotten herself in such a bind. "I now had 11 mouths to feed, a \$600,000 annual lease payment on my shoulders and a pool of unhappy investors ready to withdraw their money any time." Leslie knew she needed to collect herself and develop a plan for where to go from here.

Professors Julie Battilana and Rob Kaplan prepared this case. HBS cases are developed solely as the basis for class discussion. Certain details have been disguised. Cases are not intended to serve as endorsements, sources of primary data, or illustrations of effective or ineffective management.

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Leslie Brinkman

Leslie Brinkman was the younger of two sisters. She grew up in a middle class family in Potomac, Maryland. Her father was first a stock broker for Dean Witter in the 1960s and then an economist for the Department of Transportation. Her mother was a budget analyst for the FDA. Her mother's brother was a long time partner at a major Wall Street firm and was involved in many of the large contested takeover battles of the 1960s and 1970s. Leslie enjoyed listening to his stories and was intrigued by a number of the characters in these epic takeover battles.

In high school, Leslie was not interested in either the stock market or the business world. Her passion was sports and she aspired to be a sports journalist. She explained, "I always liked the combat in hockey. The fights, the intensity, even the blood on the ice." In 1990, she entered the University of Michigan as a political science major and, during the summers, took reporting jobs at local newspapers. In the summer of 1992, she closely followed and wrote about the presidential election. She became particularly interested in the discussion of macroeconomic issues that were being hotly debated between candidates Bill Clinton and President George H.W. Bush. During this period, she also began working on specific research projects for her uncle. He wanted data that focused on macro developments relating to specific industries. "I loved studying the macro trends in industries and thinking about how these trends impacted individual companies."

As Leslie began to think about her first job after university, she noted that many of her classmates were heading to New York to work for large investment banks and other financial services businesses. "I knew I was as smart as these people. Also, my parents were originally from New York City. My father went to New York University and my mother went to Brooklyn College. I thought it might be interesting to go to New York." Leslie also began to believe, based on the work with her uncle, that working in the stock market might allow her to combine her interests in macroeconomics and politics. So, "I decided to go to New York to learn about the stock market."

She arrived in New York City in the summer of 1994 and began her job search on Wall Street. "I interviewed anywhere people would talk with me. I told them that I would accept any kind of position and did not care what they paid me. I just wanted to go to work and learn." After being turned down at several firms, she received an offer at Abraham and Karfenmuller, an old-line Wall Street firm that specialized in risk arbitrage and money management. "They started me as a junior analyst at an annual compensation of \$24,000 per year. I would have done anything. I just wanted to get my foot in the door."

The Hedge Fund Industry

The term "hedge fund" was commonly used to describe investment pools that were created to buy "long" positions in common stock as well as to "short" common stock. Typically, mutual funds and other types of investment vehicles were "long only" funds that were unable to "sell short" securities. (A "short sale" is a transaction where an investor sells a stock he or she does not own, hoping that the stock price will decline so that the investor can then buy the stock back at a lower price in order to generate a profit.) Short selling was thought to provide a "hedge" against a portfolio of "long" positions -- i.e., positions that generate a profit when stock prices increase. It was believed that, in cases of a market downturn, profits from short sales would offset investment losses in an overall portfolio (there by "hedging" the portfolio).

The hedge fund industry grew dramatically during the 1980s and 1990s as it was found that buying and selling short securities could produce an enhanced return over "long only" funds. It was

also believed that this enhanced return could be achieved with lower volatility and “beta” (the term used to measure correlation of a fund with stock market return). By being long and short, hedge funds were able to modulate the return swings from up and down moves in the stock market and in individual stock positions.

Hedge funds were typically small firms (often 20 or fewer employees). Generally, the senior partner of the firm was the “portfolio manager,” who was responsible for selection of long and short positions and overall portfolio construction. Below this level, the firm typically would have a chief financial officer (“CFO”), several industry analysts, and a trader. The CFO was responsible for keeping books and records and developing reports for investors. Industry analysts were responsible for covering stocks in several market industry segments (i.e., transportation, retail, industrial, oil and gas, etc). These analysts were responsible for learning about companies in their segments and developing “long” and “short” recommendations for the portfolio manager. The trader was responsible for executing trades (buying or selling shares) based on the decisions of the portfolio manager working in conjunction with industry analysts.

Hedge fund economics were quite attractive to the participants. Typically, funds would charge investors an upfront annual management fee of 2% of assets (intended to cover rent, salary and other expenses), plus an annual profit allocation, or “override”, of 20% of the fund net profits. The bulk of hedge fund employee compensation came at the end of the year as a percentage of the override. For example, in a \$500 million fund, the annual management fees would be approximately \$10 million dollars. If that fund earned a 15% return, the fund management would receive 20% of that amount of gain (i.e., 20% of \$75 million, that is, \$15 million). As a result of these economics, hedge fund managers often earned several million dollars per year. The larger the fund and/or the higher the fund’s return, the larger the resulting compensation for employees of the fund. Of course, in those years where a fund earned zero or negative return the fund employees would be paid accordingly.

In case of a year where a fund lost money, it was often typical to have a “high water mark” provision which required the fund to first make back the amount of the loss in the next year, before the management was entitled to earn “override” in that year. In some cases, this provision caused funds to lose employees after a losing year because of the need to recoup the previous year’s losses before they could again begin to earn incentive fees in the subsequent year.

As hedge funds outperformed mutual funds and other long only asset classes, billions of dollars flowed into this segment. Due to the lucrative compensation characteristics of these funds, talented traders and market analysts from the financial sector increasingly gravitated toward hedge funds. The number of hedge funds grew dramatically from approximately 610 in 1990 to an estimated 7500 firms in 2006, managing, in aggregate, over one trillion dollars.

Hedge funds were evaluated against “benchmarks”. For example, a long/short common stock fund might be evaluated against the Standard and Poor’s index of 500 stocks (the “S&P 500 index”), as well as a composite of other hedge funds of similar style. Investors closely scrutinized hedge fund performance versus benchmarks in order to determine whether to continue to invest in a particular fund and whether to invest new money in a fund. As a result, the hedge fund industry was extremely competitive with managers intently focused on generating investment returns that outperformed benchmarks and their competitors. A hedge fund with consistently poor returns was likely to face redemptions (and potentially risk survival), while a fund that outperformed would find it much easier to attract new money and grow the size of its business. This competitive dynamic created a meaningful degree of stress within each firm. In addition, because of the enormous financial benefits in managing a hedge fund, younger employees often left their existing firms to start their own hedge funds and receive a larger share of the firm’s overall economics.

Learning the Ropes

Until 1994, Leslie had been “aware” of companies, but not familiar with specific stocks. Because she had no background in accounting, she decided to enroll in an evening course at a local college. During her first 18 months at Abraham and Karfenmuller, Leslie worked directly for an industry analyst. “I was a slave. I typically began work at 6:00 am every morning and worked until 2:00 am every night -- and I loved it!”

While still only a junior analyst, Leslie recalled, “I knew that I got it and was good at this business. I had good instincts about company executives, and was good at sizing executives up and figuring out how effective they might be in managing their businesses.” She began to spend an increasing amount of time with the firm’s portfolio manager. He was a seasoned investor and helped her understand how to make sound portfolio investment decisions. Leslie remembered, “I might spend days working on an analysis of US Airways and would proudly bring the analysis to the portfolio manager. He abruptly told me that I had been wasting my time and that he wanted to stay away from this company and this industry. While frustrated, I realized that portfolio management was certainly as important as company analysis.”

In the summer of 1997, after three years with the firm, Leslie decided to join Lithium Capital, a new partnership started by two former Abraham and Karfenmuller executives. This new firm managed \$3 billion of “long only” funds. From 1997 to 2001, she focused on 10 to 12 industries. Leslie remembered, “If a certain industry was hot, I jumped in and learned all about it. There were only five analysts at the company so we all had to be flexible and opportunistic. It was a great place to learn. We had a buddy system. I was always teamed with one of the two founders. One of them usually let me do most of the talking when we met with the management of a company and he would quietly listen and observe. The other one dominated company meetings and could never stop talking. I learned two very different styles and thought processes.”

Leslie’s compensation grew from \$300,000 in 1997 to \$3.5 million in 1999. “After 1999, I stopped worrying about money. I just wanted to win!” Even though she earned more than \$3.5 million in 2000, Leslie decided to leave Lithium. She recalled, “I felt the culture was dysfunctional. It pitted people against one another. Bottom line is I wanted to be at a firm where I could have more impact on the culture and the portfolio.”

In January of 2001, Leslie, then 29 years old, joined a new firm called Valley Stream Capital to be the “number two person.” The firm’s founder served as CEO and recruited an initial staff of 12 employees. Leslie’s job was to pick stocks and work with investors in the fund. The fund initially performed well but Leslie found working with the CEO to be very challenging. “He was brilliant and volatile. He was a huge risk taker and had a furious temper. Depending on the day of the week, he either hated you or loved you.” During 2001, as Valley Stream’s performance lagged the market, Leslie and the founder were often unable to agree on what positions to buy and/or sell. On several occasions, Leslie was surprised to find out that the CEO had sold positions she had just purchased the previous week. This tension culminated in July 2002 when Leslie left Valley Stream. She and the CEO never spoke again.

Time to Take a Risk

In the summer of 2002, Leslie was back on her own again and thinking about what to do next with her career. At this point, she was also four months pregnant with her first child after marrying in 1999. She contacted her long-time friend and mentor, Jim Smith, a well known and highly successful

portfolio manager. Leslie had met Smith in 1997 and they had formed an immediate friendship. They talked frequently over the years about stocks and the overall market. Smith recalled, "We liked to swap stock ideas and give each other investment advice." When Leslie called Smith to ask for advice in the summer of 2002, Smith immediately suggested that she should start her own firm: "Do it your way and I'll back you." He proposed making a \$50 million investment in a new fund which would be "locked up" for five years. In return, he would own 10% of the management company. Leslie immediately accepted Smith's proposal. "I was 30, ready to take a risk and as smart as others in the industry if not smarter." With Smith "in her corner," Leslie embarked on creating her new firm.

Starting Versutia Capital

By autumn of 2002, Leslie had a clear idea of the type of team she wanted to build:

I had been exposed to many companies and outstanding management teams. I loved to read stories about people like Steve Jobs and Jeff Bezos. I saw that the most successful people had partnership mindsets and a team orientation. In the asset management business, it is always "me, me, me." So, I thought that a team orientation would be very differentiating. The goal was to build a firm really focused on people, on process, and on a team-oriented culture. I thought that if we could create a good team, we would have more fun.

People do better when they are happy. If we could build a nice culture where people enjoy coming to work everyday and have freedom to think and dream about companies, I was convinced that we would be successful. I also wanted to build something for the long term with people I would enjoy working with. I wanted people with different, even bizarre, backgrounds. I wanted people with strong work ethics, who could admit when they were wrong and wanted to learn. Experience did not matter much to me as long as the person was capable of learning, was team oriented, shared my passion for building something and was ambitious and hungry. I also wanted people who could be generalists, had some sector expertise but with the ability to learn about new industry sectors opportunistically. I guess maybe I was looking for mini me's. People who would be open minded, flexible, willing to think outside the box and willing to work long hours.

As Leslie reflected about the design of her new firm, she wrote down a list of maxims intended to capture her philosophy on life and business (see Exhibit 1). She wanted each Versutia employee to keep these maxims in mind as they went about building the firm.

By January 2003, Versutia had six employees; Leslie as portfolio manager and all-purpose industry analyst, three dedicated industry analysts, one trader and a firm CFO. The first industry analyst hire was Peter Wilson, whom Leslie had met at her previous firm. Wilson was 29 years old. He had retail industry sector expertise. He also had been in her wedding party and was good friends with her husband. She was confident that Wilson would be a "great analyst and a great person to work with." Her second industry analyst hire was Joan Sullivan, who was an aerospace and defence analyst at a large Wall Street firm. Sullivan was 25 and was "smart, hungry, and ambitious."

Leslie also hired Kevin Blake, who had been working at a small private equity firm. Blake was 38 years old and Leslie believed that his years of experience as an industry analyst could add valuable perspective to the firm. In addition, she recruited Michael Ben, 34, a trader from a large Wall Street

firm. Finally, she hired Simon Ryley, 30, as CFO. Ryley was previously the treasurer at Valley Stream. Leslie trusted him and was looking forward to working with him again.

Leslie did not want to create titles or levels of hierarchy at the firm. Each employee reported directly to her. "I wanted the organization to be very flat." She also gave considerable thought to the design of the firm's compensation system:

At other hedge funds, people only get credit for the performance of their own stocks. At Versutia, there is one profit and loss -- that of the overall fund. It does not mean that an individual's performance is not evaluated, but if an analyst is spending his/her time helping another analyst because it is the best use of the firm's capital, they should get credit for helping.

Leslie decided that everyone would have an employment contract which specified their minimum percentage participation in the firm's profits ("points"). All team members were also eligible to receive additional bonus compensation based on Leslie's assessment of their overall performance. "There is a floor, not a ceiling, and there are points in both the management fee after expenses and the incentive fee. This is unique in that most firms only give employees participation in the incentive fee but not the management fee." In addition, Leslie commented "My assessment of professionals is based not only on their performance that year from a stock perspective, but I care about whether or not they are team-oriented." She described her philosophy:

Everybody here knows they are overpaid and hope to continue to be overpaid. I want to overpay people because the people who are here and should stay here have done a great job. The compensation motivates them to continue to do a good job and also proves to them that I really appreciate their hard work and their efforts, that they really are partners here. I do not want to worry about someone calling them and people here getting picked off. The best way to retain people is to create a great work environment and give people a path to growth and success and to compensate them more than other firms.

In December 2002, Leslie went on the road to raise Versutia's first fund. After numerous one-on-one meetings with potential investors (who had nothing to go on except her previous track record), Leslie officially "launched" Versutia Capital in March 2003 with an initial fundraising of \$115 million, which included the \$50 million commitment from Smith.

Managing Her Own Fund

In January 2003, Leslie allocated industry coverage responsibilities among the firm's industry analysts. Each analyst was responsible for making stock recommendations to Leslie, and she would make the final investment decisions. Wilson explained "Leslie encouraged us to think about what companies would look like three to five years from now. We had to be very well prepared to convince her to make an investment decision. We learned to start talking about a potential position ahead of recommending it and to be very thorough and strategic in the presentation."

To facilitate the decision-making process, Leslie created a one-page report format that each analyst was required to complete on companies they followed. It served as a training tool to help each analyst learn what information she wanted to see before making an investment decision. "I wanted them to do the fundamental analysis, but I also wanted them to dream the dream, the upside of a company and to also think about what could go wrong." Leslie also created a portfolio blotter that everyone in the firm could review to know the firm's positions and, in particular, what positions the firm owned in each analyst's designated industry sectors. In addition, she developed guidelines

limiting investment sizes for all long and short positions. "I wanted transparency here and I wanted to always be teaching people. I also had learned from my previous experiences that position size guidelines were necessary to avoid excessive volatility in the portfolio."

Leslie's typical day as CEO of Versutia Capital started with a staff meeting at 8:00 a.m. During this meeting, she and her staff reviewed each of the firm's positions and brainstormed new ideas. One of the analysts recalled how stressful these morning sessions could be.

Leslie reacted to any material changes in stock price. She kept asking the same question over and over again: "What's happening with your stock?" If you said "nothing", she told you, "There has to be a story behind it, find out what it is." Then you had to call analysts on the street to figure out what was happening, and they would tell you that they did not know what was happening. Sometimes there is no glaring reason "why" -- it's just the nature of the ups and downs of the market -- but Leslie would continue to ask the question. It was a lonely feeling to have recommended a stock that was down -- and not being sure exactly why.

In addition to her other responsibilities as head of the fund, Leslie also specifically assigned herself to particular industry sectors that needed to be covered. She regularly visited companies, attended conferences, and read periodicals and press stories relating to her sectors. As a result, Leslie usually travelled one to two days a week (either for her own sectors or to accompany one of the other industry analysts). She made a habit of attempting to listen to any earnings call pertaining to one of the firm's holdings (approximately 70 positions in 2003). She tried never to reject an invitation for a company lunch or conference. "I always wondered: what if I miss the next idea? I should attend because I could learn something and meet new important people. When you are new, you want to build relationships; you do not want to piss anybody off."

Leslie also regularly met with potential new investors and existing fund investors. In these meetings she would describe the firm, its investment philosophy and, for existing investors, review portfolio positions. At the end of each day, Leslie attempted to make time to deal with staff/personnel issues. She recalled:

I was not taking a salary. I knew that at any moment we could be out of business. I was out of pocket a million bucks and I was doing a lot of stuff I had never done before. I used to be a stock analyst. Now I was people's boss, a stock analyst, I had investors to manage, and administrative documents to take care of. It was just a completely different ball game.

Leslie found herself working and thinking about the firm on days, nights and weekends. Having put the processes and building blocks of the firm in place, she hoped that the team she assembled would begin to "gel" during 2003. She also hoped the processes she had designed would establish a routine and create a learning atmosphere at Versutia.

Life at Versutia Capital

The atmosphere at Versutia was frenetic and exciting. The working space was relatively cramped. Versutia's employees sat within shouting distance of each other -- usually two per glass walled offices for the young analysts and one per office for Leslie and Wilson. Phones were constantly ringing. Research analysts frequently went into Leslie's office to review a model or a new stock idea. There were ongoing interactions between Leslie and the trading desk. One of the research analysts

remembered, “You could always hear the trader yelling out stuff to Leslie and Leslie yelling out to the trader asking questions about stock movements or shouting orders.”

Another analyst described the work environment:

It was a very stressful job. I always felt responsible for my recommendations. I really did not want to disappoint Leslie. There was nothing worse than disappointing Leslie. When you made a wrong investment decision, she was all over you and you could be under the gun for weeks. When you were under the gun, you had to be ready to defend your position and to answer Leslie’s constant questions. She was not a yeller. She did not need to yell to make you understand that she was disappointed. She was very honest. She told you, “You screwed up, why didn’t you do this?” If you were under the gun, even if the conversation was on a completely different subject, her underlying displeasure was still evident. You just knew it.

The staff would usually arrive at 7:30 am and often stayed until after 7:00 p.m. Industry analysts, in particular, worked long hours. During the evenings, it was not at all unusual for Leslie to communicate with analysts via BlackBerry. Recalled one analyst, “It was not unusual to go to dinner with friends and check my BlackBerry to see that I had three emails from Leslie regarding stock positions that I was responsible for. It was understood that I needed to respond and, if I did not, I would often receive a follow up from Leslie asking whether I had received her previous message.” Leslie recalled that “I really ate, slept, and generally lived this business 24/7. I wanted our people to develop the same rigorous approach and passion that I felt.”

Leslie created a “buddy system”: whenever possible either Wilson or Leslie would attend key company meetings along with one of the industry analysts. While teamwork was emphasized, analysts typically did not have much time to help each other because of the workload each had to handle. Staff members were also particularly sensitive to Leslie’s view of their individual performance. They knew that, ultimately, Leslie had 100% responsibility for compensation decisions. There was sometimes “chatter” in the office as to who was “in” and who might be “out” at any given time, based on observing Leslie’s tone toward a specific employee.

While Leslie wanted to maintain a friendly and collegial atmosphere, she usually did not socialize outside of work with her team members with the exception of Wilson. Wilson explained, “Leslie and I are friends so we socialized but, besides our Christmas party, we did not usually socialize with everyone else.” Other employees socialized outside of work. The young industry analysts often met for drinks after work and even sometimes on the weekends. Employees often shared “war stories” about working with Leslie. One of the analysts explained, “Leslie is the best professional I know. Working with her can be extremely rewarding. We all learn a lot. But working with her is also stressful at times. You really do not want to be the one under the microscope and if someone else is under the microscope, you do not want to be next.”

Off to a Good Start

At year-end 2003, Versutia had achieved returns of 17% versus the S&P of 26%. The firm had 33 long positions and 27 short positions. Leslie felt this was a “solid” first year performance, particularly given that the firm was ramping up its investment activities during the year. She also understood that, given a hedge fund is “short” a meaningful percentage of its assets, it is typically more difficult to outperform in particularly robust market environments. Leslie believed that the team had matured during 2003 and that individual team members had begun to develop a comfort

with each other and settled into a shared approach to the business. Funds under management had grown to \$500 million.

Versutia continued to mold its team composition in 2003 and 2004. Kevin Blake, the experienced analyst, left in spring of 2003. Leslie believed that he was accustomed to working at a large firm with a number of direct reports and did not fit in with the “do-it-yourself” mentality at Versutia. Others observed that “Kevin also had a problem reporting to Leslie because she was a young woman.” Leslie made a number of new hires beginning with industry analyst Karl Steiner, 25, in late 2003. He had briefly worked in investment banking and was highly recommended by one of Leslie’s former colleagues at Valley Stream. During his first three months, because of his inexperience, Steiner worked very hard to learn the basics of stock analysis, spending many late nights at the firm. Peter Wilson took on the role of coaching Steiner, patiently answering his questions and teaching him key fundamentals of the business. Steiner was grateful for Wilson’s patience, and for the opportunity to sit with him almost every evening, learning from him the essential elements of securities analysis.

In early 2004, Leslie hired William Grant, 29. Grant had investment banking experience and an MBA from MIT. Wilson also spent time helping to integrate Grant into the firm. Grant liked working with and admired Wilson who, he believed, “was very good at looking at companies in a unique way and at looking beyond the basic quantitative models to recognize value.”

In February of 2004, the firm’s trader resigned. Leslie explained that “he had the big firm culture embedded in him. He always wanted the most fancy and expensive systems because he knew his friends at his former firm had them. We were not a big Wall Street firm; we were a start up.” The firm ultimately hired Sarah Douglas, 32, as its new trader in mid 2004. Douglas had been a trader at a large Wall Street firm, but Leslie was convinced that she could adapt to a small firm like Versutia.

By July 1, 2004, Versutia Capital was managing approximately \$800 million which was invested in 64 positions (33 long and 31 short). The firm achieved an investment performance of 14% for the first half of 2004 (versus the S&P gain of 3.4%). By December 31, 2004, Versutia had more than \$1 billion under management, and recorded a 21% return for the year (versus the S&P gain of 11%) At that time, the firm was invested in 69 positions (40 long and 29 short).

As the fund size increased, position sizes also increased and Leslie initiated coverage of several new industries in order to develop additional long and short investment ideas. However, by fall of 2004, she had started to be more cautious about further growing the fund. She was concerned about the increased workload, and also recalled, “People who did not want to talk to us in 2003, now saw our track record and they wanted to give us money. It started coming in too quickly, and I was concerned that these people were not good investors. I made the decision to slow down the growth in new investors.” Leslie also decided to hire Margaret Lange a marketing specialist who would be in charge of managing the firm’s relationships with investors.

Pressures Mount

Even though 2004 results were impressive versus the benchmark and hedge fund peers, Leslie began to feel increasingly concerned. Versutia’s assets had grown rapidly and the demands on Leslie and her staff had increased accordingly. She was conscious of the fact that most of the employees were still relatively young and that half of the team had been with the firm for less than one year. Leslie was also concerned that the staff was feeling increasingly overloaded. One analyst recalled, “We were working night and day. It was such an intense period.” Leslie worried that there had been insufficient time to properly integrate new employees into the firm.

Leslie was keenly aware of the fact that each team member reported directly to her (see Exhibit 2) and that this put a large burden on her to be available to discuss their individual situations. Increasingly less able to spend meaningful time with each team member, she was often rushed and impatient. She no longer had time to walk into employees' offices and ask about their personal lives as she had done before. Certain employees began to feel more insecure about Leslie's opinion of them even though they were paid well. They also became more hesitant to actively raise issues with her. One of the analysts recalled, "You had to catch her at a good moment or on a good day if you wanted to talk with her -- otherwise she might fly off the handle or jump down your throat." Another analyst remembered, "I was feeling increasingly burdened by the number of industries I was asked to cover. I knew everyone else was also extremely busy and I wanted to carry my share of the workload but I found I had less time to spend on each of the companies I was responsible for. I didn't want to complain to Leslie and I wasn't sure she would be sympathetic."

Wilson himself was feeling the pressure,

The day I came back from my honeymoon in the fall of 2004, one of my stocks was down 18%. There was some work that I should have done that I did not do. You know the market always exposes your weaknesses. Leslie yelled at me. She basically said 'Lock yourself in your office and work on this and figure it out and come back to me in two days.' She did not talk to me for two days. Afterwards, she did not let it go. I knew I had disappointed her.

Despite her own concerns, Leslie spent the year end reminding herself that, even though the firm was only two years old and was experiencing some growing pains, it had become well established with a strong reputation in the hedge fund industry. She encouraged staff members to steal away as much time as they could over the holidays and be ready to return with the determination to make 2005 another successful year.

First Quarter of 2005

In the first three months of 2005, Leslie felt that the firm went from one crisis to another. "It seemed like every day there was a new problem -- a new position that blew up that we should have anticipated." In January, one of the firm's largest positions declined substantially after the company announced disappointing earnings. The following week, another key holding announced a negative earnings "surprise," and this kicked off a steady multi-week decline in the stock. Because Versutia did not allow any single long position to exceed 8% of fund assets, these two setbacks by themselves would not have been sufficient to ruin the fund's first quarter results. Unfortunately, over the next several weeks, a number of additional situations emerged where positions declined in value despite what had appeared to be thorough analysis. Leslie wondered whether this was just a bad luck streak or whether something more systematic was transpiring.

As the fund's negative performance persisted, investors began to request in-person meetings. Leslie was spending an increasing amount of time reassuring fund investors. She recalled, "I was shocked that the people who loved us just three months earlier were now being so aggressive -- and in such a negative way."

As the first quarter progressed, Leslie began to feel more and more pressure. She was "beating herself up" over each specific setback. Although she attempted to shield her staff from her concerns, Wilson recalled that, during this period, "There was not a single day when Leslie would not come to my office several times to tell me that we had to quickly figure out a solution if we did not want to be run out of business."

Where To Go From Here

Sitting in her office in April 2005, Leslie reflected on her situation. Jim Smith had cautioned her that most asset managers eventually went through a “rough patch.” He counselled her that it was critical to stay focused on the fundamentals of the business and avoid overreacting by making radical changes. He encouraged her to get out of the office more, maybe read more books and even see a few movies with her husband. While Leslie saw the merit in avoiding drastic changes, she also sensed that the firm had become unfocused and less exacting over the previous six months.

The firm had 12 employees (including Leslie) and more than \$1 billion under management, which was invested in approximately 74 positions (44 long and 30 short). She wondered whether they had grown assets too rapidly, expanded the staff size too quickly, and/or increased the number of long and short positions too substantially. Maybe there was an imbalance between the number of positions and the firm’s human capacity? Was there something inherently problematic about the stocks they were buying or about their overall investment process? If these were issues, then what should she do about them?

Leslie knew that the firm’s staff was exhausted and upset. Morale was low. While she tried to stay outwardly calm, there were a number of situations in which she couldn’t help but be furious with individual staff members. In a small office, everyone watched these incidents, and Leslie feared that all this had a chilling effect on morale, judgment and creativity. It was not the “fun”, team-oriented atmosphere that Leslie had dreamed about when she created the firm.

She wondered whether she was part of the problem. Was she doing too much herself? Did she delegate sufficiently? If she did want to delegate further, whom should she delegate to and what tasks should she delegate? Should she get an outside coach to come in and observe her and give her advice on her management and leadership practices? She had heard stories about this being done at large Wall Street firms, although it had previously struck her as somewhat self-indulgent and a waste of time and resources.

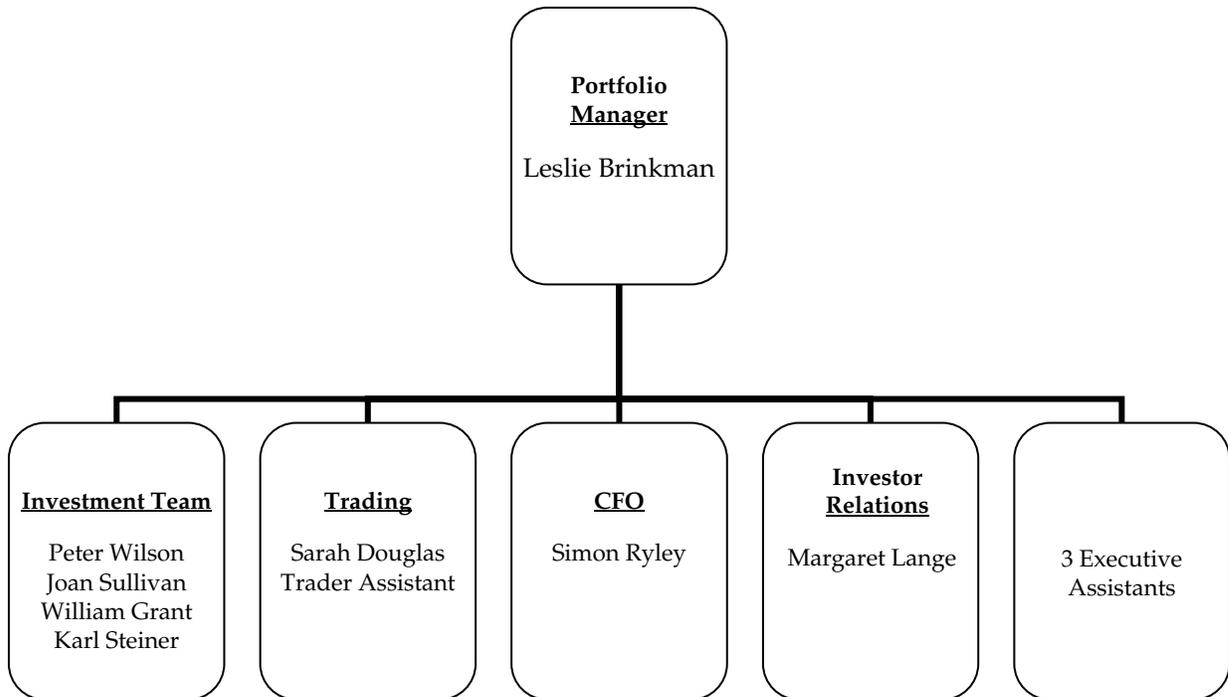
Leslie had always believed that passion was key to success in this business. Was her team losing its passion? She had not lost her passion, but why did she feel that she had more passion than her colleagues at Versutia? Exhausted, she needed to get home to spend more time with her young family. Before leaving the office, she couldn’t help but instinctively check her email messages, and saw a new message from Jim Smith. She smiled as she read, “You are great, but you would be even better if you relaxed.” Maybe he was right, but she was too tired to think more about this -- it would have to wait until tomorrow.

Exhibit 1 Versutia Capital Maxims

- Life is short
- Do not be afraid to take chances
- If journalists knew how to pick stocks they would be in our business not writing articles
- Do not be afraid to be an X among the O's
- Happiness makes you better at your job
- If a stock is keeping you up all night – we need to talk about it
- Being part of a winning team is a thrill
- People matter
- Patience – Just because you buy a stock today does not mean it will start going up today
- We are investors
- Think
- Common sense is key - if it does not meet the smell test, there is usually a reason
- The market is not dumb: if something seems too good to be true, it most probably is
- Persistence – do not give up
- This is a long-term business
- Dennis Kozlowski was one of the 25 business leaders to watch in Business Week's 2001 edition
- Enron was one of the Most Admired Companies in the US
- Everyone said Amazon was going bankrupt
- Success usually comes from plain old hard work
- If people like you, they will call you back first
- If a company usually calls you back and this time they do not, short the stock
- Ego is not your friend

Source: Company documents.

Exhibit 2 Organizational chart of Versutia Capital in the first quarter of 2005



Source: Company documents.