

BLACK SWANS AND VENTURE CAPITAL

Executive Summary

Venture capital should be considered a good alternative long term investment option when more classical investment assets fluctuate offering huge risk profiles at low upside potentials.

Subprime crisis, so what?

House related crisis was somehow expected. Something had to happen to the euphoria that for over four years captured the attention of "savvy" investors all over the world.

However, there is one consequence of the subprime crisis that will appear in the next months/years to come. A new investors' dilemma. What to do when even the "safe harbour" investments, brick and mortars, house related, fall.

There is no internet to blame on now, no technology, no forecast problems on consumer demand, no wrong innovation take up assumptions. The problem was on greed and mis-pricing of tangible assets, as tangible as bricks ("el ladrillo" they used to say in Spain).

In the other hand, the efficiency of the stock markets, and their relationship to debt, makes stocks also riskier than we used to think about them.

Private equity, what to say about it will surely suffer from the subprime crisis. Sale multiples reduce, but purchasing prices do not follow suit, mainly due to the excess of competition for getting the deals, any deals.

Conclusion, the investor has a problem. It either gets in cash, cash, cash and tries to deal with inflation, or...?

... A new investment perspective?

Nassim Nicholas Taleb, author of the very recommendable "the black swan" would have blamed a lot of what has happened on how investment models, based on historical data and complex mathematical formulae, persistently fail to anticipate real changes in the markets, the black swans. How our short perception of risk (and what risk means) makes us take "informed" decisions on the wrong assumptions.

Therefore, considering we have not yet understood, and perhaps never will, how markets work. Considering that, even if we did, others would too and returns would automatically be reduced to "efficient" levels... what is the point in creating complex portfolios that bear little relationship with fundamentals?

One simple solution NNT suggests, invest approximately 85% in fixed income; leave rest to VC. What do you achieve?

- simplify portfolio
- get all the upsides of disruptive events
- reduce risk exposure, understanding what risk means

We doubt many analysts and managers will follow our advice. Hopefully money owners will.