

Tuesday, June 3, 2008

Newsflash: Some Web 2.0 Companies are Over Valued

I like Techcrunch a lot, and have always been proud that they're an easyDNS DNS hosting client, but sometimes I find myself shaking my head a lot as I scroll through their feed in my bloglines reader. The still pre-revenue Twitter just got something like a Q-round funding giving them a post-money valuation somewhere north of Canada's GDP and some of the A-rounds being announced stand less of a chance succeeding than bluetooth enabled salad forks.

While the current VC's of these deals may succeed in their own business plans (that of achieving subsequent fundings at ever higher valuations, or effecting a liquidation event where some large elephant with too much money takes the entire thing over), whoever ends up ultimately owning these start-ups at the highest valuation will never recoup that "investment" out of earnings from the venture.

With some of these Web 2.0 companies it's like trying to build a business plan and monetize a really hot knock-knock joke. It catches on like wildfire, soon everybody's telling it in the elevator or at the water-cooler. Your cab driver knows it and so did your waiter at lunch. And then some VC firm comes along throws 60 million into the pot thinking eventually people will pay to hear it, or that they can sell advertisements just before the punch line.

I don't see it happening.

Posted by Mark Jeftovic in Venture Capital at 11:31

Thursday, February 28, 2008

The Grand Swindle

LTCM, Bre-x, Enron, Subprime, oh my, will we wake up before the Visa IPO scam plays out?

Last week while I watched *Orwell Rolls in His Grave* and *Enron: The Smartest Guys in the Room* I began to experience the feeling that I was hearing the same story again, only describing a different setting and different characters. There was a great line by an obscure singer named Tony Carey which sums it up: "Nothing changes but the names, one more ace shot down in flames, in Tinseltown".

It seems to be happening on both macro and micro scales at all levels of our society: whether it's billion dollar hedge-funds imploding because they can't mark their bullshit derivatives to market, or some Hollywood glam-addicted celeb whose exterior life is coveted by the masses publicly unravels or dies with a whimper and a thud; the consistent theme of today's Zeitgeist is *The Flameout*. It's been happening for years, their intensity is quickening while their ramifications expand and compound and yet, we rarely learn a damn thing from any of them.

Concurrent with this, the Grand Lies abound and Grand Swindles are routinely run against a gullible public that seemingly wants to be taken to the cleaners over and over again. It still baffles me to this day that so many politicians, beaurocrats and pundits have been caught out in so many deceptions and blunders and we still listen to them and assign them a modicum of credibility: Bear Stearns issuing an "upgrade" on a financial sector in full-on meltdown mode, a panel of economists stating that the US will avert a recession that it's already knee deep in, "keeping all options on the table" with respect to Iran despite being completely, utterly and inexcusably wrong about "WMD in Iraq"; whether it's all lies or just plain stupidity it doesn't matter: we can't seem to get enough of it and continue to eat it up.

It begs the question, where do we get all these guys? And why act on their prognostications, or at least sign-off on the misadventures they steer us into? Looking at their track records, it would make more sense to hang every expert authority on a meathook every time one opened his mouth. Instead we take them very seriously. It always ends badly.

The correspondences in the patterns continue to permeate our culture:

In "*Orwell Rolls in His Grave*", Robert W. McChesney tells us that reporters and news media take the bulk of their stories from official sources.

In *The Sleuth Investor*, Avner Mandelman tells us that most Wall (and Bay) Street analysts simply formulate opinions based on data supplied by the companies and investment banks. In many cases, they work for the same investment banks which underwrite deals of the companies they are covering. Surprise surprise: Buy recos abound.

Whether it's Enron, LTCM, even Bre-X and now the Subprime sludge, it astounds me how Wall St./Bay St. and the banks are either willing accomplices to sociopathic criminality or frictionless conduits of incompetence.

In the aftermath of the Enron debacle, Andrew Fastow received 10 years and had that reduced to 6 years in a country club for co-operating. The most pathetic moment of the "*Enron: Smartest guys in the room*" documentary depicted Ken Lay giving a speech in which professed to be the biggest victim of the entire scam. Complaining to his audience that he had seen his net worth dwindle from over 200 million to "around 20 million, with only about a million in liquidity". While nobody likes to see 90% of their net worth evaporate, I consider the fate of the lower echelon Enron worker who had his entire life savings of \$375,000 in Enron stock in his 401K more tragic. He managed to sell it for \$12,000 after the trading halt was lifted. The latter was but an example of thousands of loyal employees who, lack of investing acumen aside, lost everything for the sole crime of believing in the company they worked for.

Ken Lay never made it to prison but I had side bets out that Bush was going to pardon him on his last day in office anyway. Maybe Jeff Skilling still will be. Watch that pardon list in January 09 - I'm sure it'll contain a few outrages.

So where do all these sociopaths come from? And why do we as a society allow them to be coddled and cuddled when everything falls apart?

Had Enron happened in China the three amigos of Skilling, Fastow and Lay would have been marched blindfolded into a windowless cell and been unceremoniously shot behind the ear with a revolver. Good riddance. Leniency for white collar criminals there isn't a prison term served in a country club - it's death by lethal injection instead of a bullet in the brain.

In the west we live in an entitlement saturated utopia, where political correctness is so extreme the criminals have more rights than the citizenry, and the white collar crooks are practically celebrated.

We have only ourselves to blame for collectively believing The Great Lie. That Grand Swindle that says Debt is Wealth, Pro Forma accounting is more important than positive net earnings, cashflow can be magically materialized out of our credit cards or home equity, teaser rates last forever, stocks always go up, savings are unfashionable, short-selling is unpatriotic, we think/they work, we have a strong dollar policy and the children are all above average.

As long as the above nonsense passes for conventional wisdom, Joe Public (a.k.a the "lumpeninvestor") will always be run off the edge of a cliff like a pack of lemmings while the insiders to this rigged game line their pockets.

That the game is rigged poses a deeper problem than the criminals running it getting rich while destroying lives en masse: because of the Grand Swindle, what passes for capitalism - isn't and free markets - aren't. We are constantly told that this all encompassing fraud is the free enterprise system and that's what will be blamed in the trough of the coming "Redepression".

The deception has been going on so long, and the imbalances and economic crises it is precipitating now will be so far reaching and bleak the words "capitalism" and "free trade" will be unusable after it all washes out.

As alluded earlier, what finally galvanized this post was my reaction to the news that Visa is to go public with the largest IPO in history. I had posited awhile ago that the wave of Private Equity IPOs like Blackstone and Carlyle Group seemed like a distribution operation for insiders more than anything else. Basically an attempt to create a market for otherwise unmovable debt paper. If you listen to Prem Watsa at Fairfax financial, that the subprime mess isn't over, and that it will be followed by meltdowns in the (pay attention to this one) credit card industry followed by auto lenders, the timing of the VISA IPO seems suspect.

Could the Visa IPO be one final mammoth swindle for the insiders to cash out their chips while the toxic waste gets sold to the general public just in time for the consumer debt bubble to implode? Who better to leave holding the bag? Why not the general public, by now they should be used to it.

Posted by Mark Jeftovic in Venture Capital at 22:17

Monday, January 28, 2008

Are domain names recession-proof? Probably not, next question?

I didn't see the Fortune article Are domain names recession proof until the weekend, and being the author of the now infamous Domain aftermarket overdue for an asset repricing last year I feel somewhat obligated to comment on it.

There can be no doubt now that the recession is here. I went on record nearly a year ago that it was coming, so I nearly gagged when I saw Jim Cramer say something along the lines of "I told you all this was coming" over the Christmas holidays. So now it's ok to say "recession" in polite company although the politicians and the pundits still try to soften it up by making sure they modify it with words like "maybe", "slight", "mild" and "possible". Make no mistake, it's underway and I think we're far closer to the beginning of it than the end.

So, how will domain names fare in a recession? The Fortune article was upbeat:

"Global markets are in a state of panic. Credit markets are all but closed. And recession fears are everywhere. But at the conference I attended in Hollywood this week, called DomainFest, you'd have little clue that the financial world was melting down.

The domain world - the people that buy and sell names and make money from pay-per-click ads on their websites - is booming. Downturn? Bring it on!

While the rest of the article is little more than a layman's intro to the domainer business model, the question is timely. Now that the recession is here and, to paraphrase the old detergent commercial "we're soaking in it", are domain names as an asset class a "safe haven"? Will they in general terms produce "above average" returns compared with other places to put one's money such as stocks, bonds, commodities or inflation protected t-bills?

The difficulty of treating domains as an asset class per se

One of the troubles with examining domains names as an asset class is the short amount of time they've been around: compared to mainstream assets and financial instruments, domain names and the DNS have been around a few microseconds. Thus, we don't have a lot of historical data to make inferences from. In the history of the commercial internet (say since 1994 or so), there's been one recession/bear market (2000-2002) and it's almost a stretch to call it a meaningful one.

One domain broker I know related that "aftermarket values tanked" after the Nasdaq bubble burst. I know that prior to the crash, one of my clients paid \$90,000 USD for a domain and he didn't even bother renewing its DNS last year. It's sitting right now on our "DNS expired" pages so I even have insight into its traffic and PPC value. It gets a steady 20 to 40 "type-ins" per day, but at current PPC revenues the domain will break even in 4,500 years.

So on one hand, we don't have much of a past track record to give us insight into how domains as an asset will perform through various stages of economic cycles, the other problem is to the future: will there even be domain names in 5, 10, 50 or 100 years? We can, with some confidence, assert that in 100 years time people will still eat, wear clothes and sleep indoors, putting some kind of a demand based floor under things like real estate, textiles and commodities.

Domains on the other hand, work because of "DNS", and even though my personal livelihood depends on "long live DNS", I am not fool enough to think that in 10 or 20 years some completely different method will be employed that enables computers and network services to uniquely identify and locate each other across disparate networks. I called this future protocol "quantum foam" once as a placeholder. Let's for our purposes just label it "QNL" for "Quantum Network Locator" and wonder if some kid in a garage is going to invent it at some point. Even if that event is 50 years out, paying 100X on a domain may not work out so well.

What is recession-proof?

Warren Buffet loves recessions because they enable him to pick up undervalued assets on the cheap. He's parlayed \$100,000 into a personal fortune worth over \$30 Billion doing just that. What attracts Buffet to investments are what he calls "durable competitive advantages", or what his mentor Benjamin Graham termed "moats". In tech land we often equate this with "barriers to entry" but they are not exactly the same thing. The phrase I personally identify with it is "the ability to defend". How defensible are domain names?

The problem there as I see it is that there are two pillars holding up domain values: PPC and direct navigation.

On the PPC side, there is very nearly a single-point-of-failure for the entire industry and that is Google. As Jay Westerdal pointed out, Google may very well have single-handedly killed the domain tasting industry last week, which is significant. The registrars' constituency tried to hammer out a consensus, the registries themselves have been scratching their heads over how to best deal with perceived abuses of the AGP and along comes Google, from completely outside the inner circle and toasts the entire sector in one edict: no more monetization of domains less than 5 days old. End of story, end of the AGP carry trade.

So GOOG has the power to kill an entire slice of the domain pie, what would happen to the rest of it if they failed completely? It doesn't matter how far-fetched that sounds, the point is that there is a lot of capital pouring into the domain monetization game and the entire domain monetization game is dependent on a single external entity. What if GOOG says "no more parked pages" next? They won't but they could.

The other aspect of domain monetization is, of course, direct navigation and again, this is where the rest of the domainer world and myself agree to disagree. Once again, there is the ability for entities outside the domainer's sphere of influence to have a huge impact on type-in. What if Google (them again) releases Gbrowser (or Gfox, or G-zilla) puts the search box where the location box is, puts the location box under Shift-Ctrl-F-L and grabs 20% or 30% of the market over the next few years? What if IE (who already has 20% on IE7 and another 30% on IE6) did it tomorrow?

Future input devices (the stuff we haven't thought of yet), likely won't interface with the computer using keywords with ".com" appended to it. When you think of it, typing that into your browser's location bar is a quite antiquated, not to mention uninformed method of getting around the internet. Future UI will succeed on the basis of infusing the user's known preferences with relevant search queries and agents. I don't know what it'll be or what it'll look like, but I know innovations will happen in UI and they will probably obsolete or at least end-run type-in.

So if you listen to me (don't worry, very few do), there are two gaping holes in the ability for domain names to defend or construct moats of safety around their current revenue models. The common factor in both is that too much crucial underpinnings of the PPC model are subject to control outside of the PPC/domainer industry. Unless Oversee can buy Google in the next few years.

Neither of these scenarios ever need happen to impact our assessment of domains as an investment vehicle and to ponder their value through a recession. If there's one thing I've taken away from my studies of value investing it's "margin of safety". All business is in a word, risk. So we want our entry points into our investments to offset the risks. At current levels, I think if any technical analysts existed in the domain aftermarket, they would call them "overbought". Hence no "margin of safety" against these risks.

What are safe havens?

During times of trouble, people flock to "safe havens". These havens have certain characteristics, including being dull, boring and thus (hopefully) safe. Such times are often eventful, tumultuous and are often by definition, not boring, so whatever people flee to during a crisis, they aren't looking for more excitement. Gold is a good example. We may not really understand exactly why a polished metal out of the ground holds its "value" perpetually but we are hard pressed to find a tailor anywhere in the world who won't sell you a suit for an ounce of it.

Everybody has to eat, everybody has to sleep, everybody needs shelter. Nobody must surf the net or send email. If you find yourself in tough economic times deflation or hyperinflation, typified by scarcity, fear, uncertainty and financial chaos and you have an ounce of gold in one pocket and the auth code for food.com the other, I doubt you'll be able to feed your family with the latter. While we all hope times don't get that dire, that is the thought process at the root of all flights to safety among the asset classes: "How useful will this be if the crap really hits the fan?" and "How much value will this hold in all dire circumstances?" (deflation, hyperinflation, stagflation, etc)

Some factors that favour of domain names relative to other asset classes.

I'm saving some optimistic thoughts for the true believers and I'll outline why "domains-as-asset" class have a few favorable factors going into a recession which may help them become a lagging casualty (meaning the damage will occur later, and may not be as deep).

Domains in general are not leveraged. This quite possibly can make the difference between suffering through a few lean years and going bankrupt. If there is a defining character of this financial meltdown it is illiquidity. The damage is coming from overleverage and compounded by the fact that in many sectors (mortgages, LBOs, etc) too much debt has been issued, and then packaged up and resold. The result are a flurry of crisis moments where entire books of instruments can't be marked to market and liquidity totally seizes up.

There may be a reciprocal effect in advertising mediums to the benefit of domain names. During recessions, many businesses reign in their marketing budgets. (This is often times a mistake but in many cases they don't have a choice). Institutional advertising may suffer declines and as companies pare back on, say, Superbowl ads, they sustain or even increase their online ad spending because ROI can actually be measured. Also, online spending tends to be more accessible to small businesses than institutional advertising so the more savvy small businesses may actually step up their PPC spends. But I must stress, I think all this happens against a backdrop of overall falling budgets and falling spending, lower bids. Good for the buyers (recessions always are), but bad for the sellers (which is what the domainers are).

So our examination of the question "Are domain names recession proof?" can be summarized, I would say that the lack of track record (domains haven't existed long enough to gain insight on how they will react under differing economic climates), means domains won't qualify as a safe haven asset during a recession or an economic storm.

I would go on to say that at current overbought, overheated aftermarket pricing, there is no "margin-of-safety" on buying domain names as an investment (either by PPC at inflated multiples, trying to flip into a cooling market, or just thinking generic .coms are the "real estate of the future" - real estate has bubbles too)

The good news is there is no pronounced leverage in the sector generally. Jay Westerdal may wish banks would "get it" and finance domain names, but going into this recession it may be a benefit to the domainers that there isn't a lot of debt overhanging the industry. Most domains are (assumed) to be owned outright, so if PPC revenues fall, there isn't the spectre of being underwater on debt service looming.

While I don't consider domains "recession proof", I will be looking for signs of a bottom on this one, and for those of us who are still solvent (hopefully you and me included), there should be some bargains to be had.

I think part of the fallout against my "Aftermarket Overvalued" article last year was people thought I was saying "domain names suck", and that wasn't my intent. I've always loved domain names, I'm a geek and I'm in the DNS business and I was collecting domain names before I ended up being a registrar. I just called an overbought aftermarket as I see it.

What happens during recessions? Overreactions to the downside. I'm not a permabear so stay tuned for my someday-in-the-future article "Domain name aftermarket screaming BUY". Hopefully it won't be 10 years from now.

Friday, January 18. 2008

The Economy: Time to Panic? (Not yet, but wear diapers)

As a child, my mother remembers peaking through a window into the bedroom of her grandfather, my great-grandfather, who would sit at a table frantically counting and recounting a few gold coins in a bag. He had gone off his nut, basically, and this was his obsession: emptying a few coins out of his bag and recounting them into it. I was told this tale at a fairly young age and had taken it as a cautionary tale against being miserly or otherwise obsessed with money.

It was only during a recent visit from my mom that I learned the other piece of my great-grandfather's story. He was rich, already a wealthy man before all that "Great War" unpleasantness. WWI ended and he had all of his wealth in (wait for it...) gold. What happened next is what broke the man. A business partner of his convinced him that gold was old news and about as valuable as it was ever going to get (A "barbarous relic" in today's parlance). My great-grandfather agreed he may be right and liquidated the vast majority of his gold bullion and coins into cash. This was in around 1920's Germany, better known then as "The Weimar Republic". Ask any halfway competent student of history about the Weimar Republic and they will all say the one thing it was remembered for the most: HYPERINFLATION.

What is the best possible thing to have oodles of during a period of hyperinflation? Gold What's the worst thing you can do with gold just prior to an episode of hyperinflation? Sell it for cash.

That's what my great-grandfather did and he spent the rest of his days a crazed pauper with OCD. For some reason that story really, I mean really resonates with me on a lot of levels. If I believed in re-incarnation, I would say "I'm that guy, and this time I'm going to get it right goddammit. "

When I flipped past Larry King's show last night and the headline was "The Economy: Time to Panic?" I realized just how badly spoiled we are here in the west. Sure, the stock market is down 14%. That's 14% down from an idiotic high it had no business being near in the first place. But all told, a 14% pullback is peanuts. But in the mindset of the typical lumpeninvestor, this is inexcusable and grounds for a massive government mobilization. What kills me about all this is the implicit assumption that consequences are for other people.

When this subprime unwinding really started to impact the market, the financial sector screamed bloody murder and demanded a bailout, the archetypical representation of the entire sector's ethos is captured beautifully by the now legendary Jim Cramer meltdown on CNBC. At around 52 seconds into the clip he says something interesting,

that something is along the lines

"he [Bernanke] has no idea how bad it is out there...I have been on the phone with the heads of all these firms in the past 72 hours and he has no idea how bad it is out there, my people have been in this game for 25 years, and they are losing their jobs and these firms are going out of business"

It is indeed a meltdown to behold and, as Bart Simpson would quip: "The ironing is delicious".

When GM or IBM or some other non-financial giant lays off thousands of workers, guys like Jim Cramer will quip that it's the way of the world and the stock price of those companies will actually bounce a bit. Who gives a crap, those workers are nothing more than cells in a spreadsheet. But when a bunch of bankers, who have been selling each other shit and calling it shinola for years finally get caught out and it all crumbles, the prospect of the consequences coming home to roost is unthinkable. That bankers lose their jobs and firms go underwater because billions of dollars of bullshit derivatives that they dreamed up themselves can't be marked to market is a bona fide crime against humanity.

Citigroup and Merrill Lynch coughed up a 20 billion dollar furball between them this week, then Bear Stearns (who kicked all this subprime mess off last year by having a debt auction that nobody showed up for) added the comedic punchline by upgrading the financial sector. With the exception of Goldman Sachs (who gave subprime such a wide berth they are being investigated by regulators, no good deed goes unpunished), the entire investment services sector looks like a bunch of financially illiterate retards and we're supposed to seriously heed their upgrade recos on the

financial sector? These are the same guys who called people like me (contrarians who shunned growth stocks and bought gold in 2002) a bunch of idiots that "just don't get the new economy".

Now the US president has mobilized into action, back from the middle east where he begged the Saudi king for lower oil prices he's crafting a 150 billion dollar stimulus package to ward off a recession that no talking head in Washington will even admit is happening. Everything is fine, but suddenly a 50 basis point cut on the 30th probably won't satisfy the street, it needs an unheard of 75 basis point cut now and if they get it, somewhere some twit will in the same breath re-iterate America's commitment to a "strong dollar policy". We live in truly Orwellian times folks.

I started off last year predicting predictions for a "second half recovery" in 2008 and I haven't heard that magic phrase...yet. The R-word (recession) has only begun to be usable in polite company the last couple weeks and suddenly it's everywhere, but it's still being used in a benign, unalarming context. "Recession? Yeah, I guess there's a remote possibility that we could have a mild recession" but if you read between the lines, alarm bells are ringing, central bankers and politicians are scrambling and the people who see behind the scenes are crapping their pants. Who knew?

Posted by Mark Jeftovic in Venture Capital at 13:23

Tuesday, October 30, 2007

The web 2.0 VC Roadmap, as blogged by Rick Segal

Just kidding Rick, I saw one of your posts the other day and couldn't resist. For those unfamiliar, Rick pens one of the premier VC point-of-view blogs at Post Money Value.

The CEO is way smarter than I am.

The CEO has built a team of people way smarter than he is.

The CEO has assembled an advisory board of incredibly smart people who just "get it". They're brilliant. Doc Searls, Rick Scoble, Seth Goodin, and Guy Kawasaki. Just to name a few.

The CEO works 16 hours a day, 7 days a week and is driven by total passion and intensity. He doesn't draw a salary and drives a 1983 Lada. He donated his founder's shares to charity and his family hasn't seen him in nearly a year.

The first three funding rounds all took place at successively higher valuations.

The developers are amazing. You should see the mashups these guys are cranking out. They came up with a very neat Facebook application that's going to be just killer!

The guy we brought in to replace the CEO made the company very attractive for subsequent funding rounds.

The revenue projections look very promising.

And then....

We sold the company for \$400 million, a great exit. Congrats to all involved.

or

Microsoft buys a 0.25% stake for \$200 million, valuing us at 800 billion dollars, not bad for a pre-revenue venture with oodles of mindshare.

Posted by Mark Jiftovic in Venture Capital at 16:35

Wednesday, August 15, 2007

More on panic containment and let the good times roll

I watched with bemusement the talking heads on BNN this morning, as is my habit since CNBC has been swapped out for a movie channel on my digital cable feed (a better value, I find). They were describing how "normalcy" is returning to the European financial markets and how other sectors are positioning for a "decoupling" from the financial sector being dragged down by the subprime sludge and credit tightening.

So all is well again, all it took was about a half-trillion dollar Hail Mary from Central Banks the world over and we're all supposed to either go back to buying houses with nothing down, no income, no visible means of servicing the debt and an adjustable rate mortgage to boot. Either that or we buy packages of these mortgages bundled together of other people doing exactly that and we're supposed to call it "investing". In any case, the talking heads obliquely referred to this last week of cratering stock markets as a "buying opportunity" that hedge funds will surely position for.

You'll excuse me if I stay on the sidelines, and call me "unpatriotic" if I pick up the short side of any positions (as short sellers were called during that last pretend recession and baby bear market from 2000-2002). I'm used to being called an idiot for saying so, we're heading into the Real Deal now, a full-on secular bear market coupled with a skull crushing recession. Which sucks, I was hoping for a couple more years of "normalcy" to build up my war chest (I've always hoped for a few more years to build up the war chest, get rid of as much debt as possible, etc) but it looks like the clock is running down.

We are here. On the edges of, as one book I read years ago put it, a financial desert we must all cross, one that will last 10 to 12 years. Which really really...sucks. Larry Wallman, who puts out the fantastic Stocks2watch newsletter (which I only subscribe to so I can read his weekly macro overview "Sunday comments"), thinks for various reasons that we still have until after the Chinese olympics until everything seriously goes into meltdown mode. George Ure asked me to posit a drop in the DOW to 7,000 over the next 60 days, which is understandable, George always posits a 50%+ drop in the indices over the next 60 days

But I wanted to update my post yesterday about the Central Bank of Canada where I tallied the nearly 4 billion the bank injected into the markets to pacify/stabilize/mollify them between Aug 7 and Aug 10, I note they dropped another 670 million on monday and 350 million so far today. A billion here, a billion there, pretty soon we'll be talking serious money.

Today the Financial Times carried an article In a world of overconfidence, fear makes a welcome return which I think should be required reading for mortgage applicants, brokers and bankers, there's even a paragraph in it about me:

The fourth stage is over-trading, when markets depend on a fresh supply of "greater fools". The fifth stage is euphoria, when the ignorant hope to enjoy the wealth gained by those who came before them. The warnings of those who cry "bubble" are ridiculed...In the sixth stage comes insider profit-taking. Finally, comes revulsion.

I'm the guy crying "bubble", being ridiculed, especially in the domain aftermarket, where for some reason people seem to think that despite the fact that the domain name aftermarket is exhibiting textbook symptoms of a bubble-mania and that the massive overpricing of even marginal quality names in the aftermarket has nothing to do with the excess liquidity induced by loose credit sloshing the world over looking for "aggressive returns".

So it goes. As Larry Wallman said in last week's Sunday Comments:

"As housing was going up and up and up, we suggested we were in a bubble and that it would end badly Somehow the idea of lending money to people with no visible way to pay it back seemed like a bad business transaction to us. How dare we suggest such a thing? It was obvious that we had absolutely "no idea" to coin a Cramer phrase. We were economic idiots of the highest order. "

And if you watch the talking heads today, we still are idiots. Idiots who may have made a pile on the short side over the last week but idiots all the same.

The only thing I'm treating as a buying opportunity in this climate is gold, which is one nice thing about BNN, being Canadian they aren't as hostile to gold as Cramer and Kudlow are (yeah Kudlow, I remember your "SHORT GOLD GO LONG USD" rant from a few years ago, you were yelling it into the camera...that was over \$300/oz and a few hundred

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pips in the other direction). The guy on BNN reported a Newmont executive saying "I see three zeros after the price of gold in a couple years, I just don't know what the number on the left hand side will be".

Still crazy? Guess we will all find out sooner or later.

Posted by Mark Jeftovic in Venture Crapital at 12:17

Tuesday, August 14, 2007

Canadian PPT hard at work

Background: the sky is not falling. Subprime woes will be confined to the subprime market, the contagion will not spread to other financial sectors. In fact, this is a non issue, there is even this video of Jim Cramer telling you as much last month, so it must be true.

Oh, then what happened?

Bear Stearns didn't get the memo. Weasels went and tried to sell off their subprime sludge /CDO's on an open auction market and found their paper wasn't worth the numbers printed on the paper! Oh my. The president get's fired for his troubles, two of their hedge funds seize up and then the same thing goes and happens in France.

Suddenly...everybody is going ballistic, Cramer has his own meltdown on CNBC and the Plunge Protection Teams the world over SPRING into action, pumping over 330 billion dollars into the markets under the guise of "stability facilitating operations". And after tall that, the markets barely broke even, today they're down again.

There is a headline on Reuters that the Bank of Canada is declining to comment on their stability operations (see: Bank of Canada mum on commercial paper troubles), so I called them up.

A very nice lady directed me to Bank of Canada monetary policy operations page which updates in realtime. She told me this page describes the BoC operations over a 5-day window and to find those emergency injections of "liquidity" to keep a lid on a full-on market meltdown, to look at the section labelled Daily Target Rate Intervention and the first line, SPRA (par value) is the amount of overnight repos that our central bank used to intervene in the markets during this subprime debacle:

DateAmount
Aug 7/07410 million
Aug 9/071.64 billion
Aug 10/071.68 billion
= 3.73 billion

So yes, it appears as once again the central bankers and teevee pundits have "called it" with sagacity and prescience worthy of an oracle, drink the koolaid and repeat after me: subprime woes are contained, subprime woes are contained, all is well, all is well.

In spite of the fact that my long term PUTs on the DIAMonds moved well into the money through all this, I was disappointed that Canada's central bankers played right along with this madness.

We live in dark times, where monetary policy is set by a gaggle of Central Bankers who are card carrying members of that Death Cult known as Keynesian Economists, against which a tiny band of jedi knights known as Currency School Economists chirp from the fringes of irrelevance "this will end badly, this will end badly". Surprise, now we're soaking in it. This is just the beginning.

Once again I must point people toward The Monetary Elite vs. Gold's Honest Discipline by Vincent LoCascio, and this excerpt may have been tailor made for this financial storm:

"[P]eople fail to consider that federal guarantees make bank failures more likely by artificially encouraging people to choose the highest interest rates available, which in turn causes bankers to seek riskier, higher-yielding loans and investments".

I have a new mantra, I doubt it will take hold, everybody now "bailouts are bad", the hucksters of pseudo financial instruments like collateralized debt obligations denominated in deadbeats have gotten more than enough rope to hang themselves...let them hang.

Blog Export: Exile From the Herd, <http://www.privateworld.com/>

Posted by Mark Jiftovic in Venture Crapital at 11:38

Tuesday, July 3, 2007

Wave of private equity IPOs the final stage of distribution?

First Blackstone went public, not to be outdone, the Carlyle Group decided to follow suit, and now KKR is jumping on the band wagon.

If the first part of '07 could be characterized by an orgy of private equity deals (subprime woes aside), and it looks like the back half of the year will be all about private equity IPOs (does that make them public equity funds?)

On the surface this looks like a fantastic buying opportunity! Now joe-six-pack can play in the big league, being co-owners with the high rolling Bush clan and Bin Laden's brothers (who are or were investors in the Carlyle Group) and if you jumped on that Blackstone IPO, don't fret that your shares are trading below issue price, you're the proud new owner of Hilton Hotels (and the 7 billion in debt that comes with it)

Now that the subprime meltdown has officially killed the housing bubble, it appears as though a wave of private equity IPOs may be the last house on the block of a global "investment" mania floating atop a veritable deluge of excess liquidity.

Fissures are already appearing in this private equity wave. As I already mentioned, Blackstone is already trading below issue price, Carlyle had to tone down their IPO prospectus, citing "market headwinds".

The paranoiac in me reads some of the fine print and begins to get a different take on this. When you consider that Carlyle's to-be-public fund Carlyle Capital, "will mainly invest in AAA-rated residential mortgage-backed securities, but also in loans, junk bonds and collateralized debt obligations." and that not even a week ago Bear Stearn failed in their efforts to unwind two of their hedge funds' portfolios of subprime sludge in an asset auction, a different picture emerges. One in which private equity funds are spinning off publicly traded funds to create a market for otherwise unmovable CDOs and other high risk debt.

This new private equity bubble could play some pernicious roles including

inflating yet another asset bubble to keep the equities party going
create a market to unwind the subprime sludge and the rapidly deteriorating repackaged CDOs
allow Wall Street insiders possibly their last chance to get their money off the table and their paper into the hands of the lumpeninvestor and joe-six-packs

The ratio of insider selling to buying has been north of 30-to-1 for years, and for some reason this smells like a blow-off distribution near the end of a crack-up boom. At the end of it, the average investor in the street will have been enticed into funds holding otherwise unmarketable debt and complex derivatives, who else to end up holding the bag?

Posted by Mark Jeftovic in Venture Capital at 23:17

Friday, January 26, 2007

I don't get the new "New Economy" (2.0)

Back in 1999 I was walking around in a mental fog because I was coming off of a multi-year bender and had recently stopped drinking, smoking and, uh, other related recreational vices. At the time I was worried I was going to die from boredom (turned out not to be the case at all. My life has been more exciting and fulfilling since I cleaned up than I ever could have imagined, but that's another story...)

So I decided to start daytrading. I took out a \$1,000 cash advance on my VISA card and opened an E-trade account. By March 2000, it was worth over \$9,000 and I thought Warren Buffet was a pussy. I keep that E-Trade account open to this day as a reminder. It's worth \$200 now.

Anyway, at the time I remember walking around the warehouse district where my office was thinking about "the new economy". I just couldn't wrap my head around it. A lot of the companies trading on the stock market weren't making any money. A lot of the start-ups getting funded had no prospects of revenues. "Aha" I thought. "I guess what it's about now, is the stock price and investment flow". Companies didn't make money by selling stuff at a profit, I realized, they made money by raising it in the capital markets!

It was one of the many moments I stood on the precipice of a major epiphany, had I thought it through properly I probably could have done well, but once again, I missed the point. My mind couldn't make the critical leap to where it needed to get in order to profit handsomely ("Aha! We're in the middle of a bubble! START SHORTING STUFF") and knuckled under to the flawed, murky newspeak "I guess that's how things work now. This is a new paradigm for wealth building. The old rules don't apply at this new, permanently high plateau of the New Economy", and I went along with it. Silly me.

Well lightning does strike twice. Here we are and the DOW is reaching new highs daily while insider selling outpaced insider buying 55 to 1 last month (this ratio has been higher than 30 to 1 for over two years). The new Kook-aid (that was a typo for Kool-aid but I think I'll leave it), is "Web 2.0".

Companies like Slide.com are getting third round VC fundings of \$20 Million and they are (as Michael Arrington politely calls it) "pre-revenue". It was interesting to find out about this shortly after yesterday's post about "remorasites". Slide is a remora to MySpace, and all it takes is one move from MySpace and Slide will get shafted for all that precious "mindshare".

Nowadays my biggest mental handicap is that I haven't had a decent night's sleep since becoming a parent nearly 11 months ago. But I don't need to be fully rested to realize we are in BUBBLE 2.0, echo bubble overdrive baby. Insiders are selling up a frenzy, most of the stock market's gains can be explained by inflation, no-revenue companies are getting close to 100 million dollar valuations and some VC's seem STUPIDER than MONKEYS.

Bearing in mind the old adage "The graveyards of Wall St. are littered with the bones of those who were too early", methinks it is a fine time to start thinking seriously about getting short, or at least well hedged.

Either that or it's time to learn ajax and start an aggregator with widgets that are tagable from social networks.

On mobiles.

Via RSS.

Can I have 20 million dollars now?

Posted by Mark Jeftovic in Venture Capital at 15:51

Wednesday, September 20, 2006

5 VC gambits start-ups should watch out for

I wonder if I'm the only person blogging about VC who has never had a VC investment? Over the years I've signed two term sheets:

Term sheet #1) Before easyDNS had its first customer, we had a fully functional platform ready to launch and VC interest. The deal never happened, and the night it fell through I went home to my apartment and cried like a baby murmuring "We're so fucked" over and over to myself.

Why I thought that, I guess comes back to pure naivety. I simply didn't know better than to think the start-up cycle included "funding" as a mandatory component. Besides, it all seemed so ...glamorous and it seemed then that we were going to miss out on all that glamour, fame and fortune.

Times change.

Term sheet #2) I was seeking funding for the buyout of my partners and it seemed the VC's were the last house on the street. I had already been to the vendors, the banks, the BDC and a couple angels and just couldn't quite piece together the funding I needed. On a complete and utter fluke, with all systems go and both sides committed to the deal, it blew up for what can almost be described as "clerical reasons".

When I got the phone call I was surprised at how it felt: it was an enormous release. I felt like I had just dodged a bullet and in retrospect I think that moment is the single, luckiest life-defining moment for me. Not a day goes by I don't thank my lucky stars that that second termsheet fell through. In the end I had to Plan-B it, and that is the single best thing that could possibly have happened in my business career thus far. But that's another story.

It was quite the education that I picked up in both of those funding processes, in no particular order, here's a few "VC Tricks" I had the good fortune not to learn the hard way...

#1) You're in charge (yeah, really): A looming VC investment may make the founders nervous about letting these suits into the company, taking over completely and relegating them to mere employees (which is pretty well what's gonna happen regardless of what they tell you or how it's framed).

So the VC may hand out titles in a way to allay those fears. Nervous about control? Well you're the president! How can you not be in control now? We're just going to appoint one of the fund partners CEO but he won't be micro-managing you. Honest. Or you get to stay CEO, but don't think for a second that the VC's won't control the Board, so either way, it's academic.

#2) Control the Board It is said the key to chess is to control the middle four squares of the board. The VC's will control yours. It may be take some elegant math but either they'll have more seats than you outright, or you will have equal numbers of seats on the Board plus an odd number of "independents". Try nominating any of your associates to the indie seats or especially to that crucial swing seat. Watch that get shot down. Any candidate presented from your side of the table will not be "mutually agreed upon".

The VC's have deeper rolodexes, they will just keep throwing candidates at you until you finally capitulate and "mutually agree" to one of their nominations. Guess which way they'll vote when the matter of firing the founding CEO (read: you) is on the table?

#3) You're the majority shareholder A lot of energy gets wasted by founders trying to retain majority control of the shares in the hopes that it'll keep them in charge. Combo deals like investment split into part equity/part debt but this is all just optics to suck in/lull/mollify the founders into believing they'll still have control after the funding.

But then the term sheet will have all kinds of kookiness. You can bet on having a special share class for the VC's and a whole pile of special conditions that require approval of the pref shares (the ones the VCs own, not the commons, which you own more of). At the end of it, special privileges will be attached to those preferred shares and embedded in the term sheet which make being the majority common shareholder meaningless (never mind liquidation premiums and preferences).

#4) A loyalty test This one is perverse. The VCs will want to make you feel part of their team and that by taking their money you will get to play at a whole new level. Kind of like being called up into the major leagues from that penny ante bush league you were languishing in before they came along.

In my case I was asked to meet with another partner at the firm to give him advice on another industry I have familiarity with, he was about to make an investment in that industry (or already had, can't remember). So after about an hour after we kick some ideas around he offers me the CEO job at this other company. I was floored and for a few days, tempted.

It all seemed so easy, why buy out my partners and forge ahead when I could instead sell, pocket the cash and come run this glamorous, funded, cool start-up instead?

In the end, I declined, another lucky decision. In retrospect it seems the entire exercise was sick mind game designed to test my resolve.

#5) Join us, become one of us Having passed the loyalty-to-the-plan test, I was then invited to sit on the advisory board of the above start-up. "Sure" I thought. I'm in the club now. These guys will fund me and I get to sit on advisory boards and join the startup jet set. A decade in the business avoiding minefields and I'm still susceptible to having ego stroked.

After the deal fell through, I rarely heard from the start-up upon who's advisory board I supposedly sit. Occasional email exchanges, "so how's XYZ Corp" going? "Oh great, thx", no mention of "We need to fly you out to California to meet the CEO" (plenty of talk like that when we had a signed termsheet though)

Finally after that VC emailed me the other day on an unrelated matter I asked him point blank "Am I still on your advisory board or were you just blowing smoke up my ass to help your firm get into my pants?"

No reply.

I guess there's my answer.

Posted by Mark Jeftovic in Venture Capital at 15:32

Tuesday, July 4, 2006

When are "exit plans" necessary?

My last post led me to think about "exit plans". When we started easyDNS back in the late 90's, I thought "exit plans were for wimps". It made no sense. "Before you even get started, you're supposed to have an exit plan". It smacked of dotcom bubble thinking and that was something we were all hoping to avoid.

Over the years, the lack of an exit plan came back to haunt us. As it turns out, I think I now know when exit plans are necessary:

When there is more than one shareholder
When any kind of external investment occurs or is sought
When you're actually executing against a business plan

We never did have a unified exit strategy and whenever opportunities, offers or traps presented themselves, the lack of a unified plan amongst the partners pretty well derailed "liquidation events" before they ever got rolling. I think that overall we came out ahead as a result and this lack of planning ended up saving us from what were probably company-ending blunders. We got lucky in that respect.

But when the time finally came for the partners to really evaluate our life paths with respect to the business, we probably would have been better served to have agreed on an exit strategy going in and revised it over the years as our circumstances changed.

Now that I'm the sole shareholder in the business, there is no exit strategy, and I don't foresee one in the future. I'm grateful to be where I am today and wouldn't want to live my life any other way. The business for me isn't a job, it's a lifestyle (that dreaded L-word VCs despise) and I'm not executing against a rigid plan that calls for targets, milestones and an eventual liquidation event.

While I don't exactly expect to my daughter to take over the business (she is after all, only four months old and may want to do something else with her life) I like to think I may likely still be running easyDNS in 20 years, even though we may not be in the DNS business anymore (by then who knows what things will look like, computers may use some sort of quantum foam to find each other).

When you're fortunate enough to be able to write your own ticket, you don't need an exit plan and I think if you dwell on one you run the risk of "building to sell" or trying for a "quick flip" and even hardcore veteran investors and VCs think that is an unsound approach.

When multiple stakeholders are involved, part of playing nice with others is coming to an agreement over a unified exit strategy. Again, while you don't want to get too distracted over it (arguing over whether "the buyout number" should be 20 million versus 50 million is pointless if you haven't earned a dime yet), it should probably be done sooner than later.

One way to get it done early, without wasting too much time over it, is to create some basic "shape of deal" criteria and a formula to serve as a simple screen going forward.

Example exit strategy formula: Any buyout has to be a share sale versus an asset sale, be all cash and be a minimum 2X revenues or 7X earnings.

If your business gets anywhere off the ground, offers of some shape or form will come. Most of them will be distracting snipe hunts and a waste of time. Without a basic screening formula you and your partners may waste precious time and energy arguing over it, but with the formula you can quickly evaluate it and if it comes up short simply dismiss it and get on with running the business.

Friday, June 9, 2006

Shareholder Agreements for Start-Ups

If there is a single piece of advice I can give to anybody starting out down the entrepreneurial path with a few friends or partners, it is this: get independent legal advice before you sign your shareholder/partnership agreement.

This document will be the most important legally binding contract in your life, especially if you succeed. My first time through for me was a lesson in what not to do. We had a VC term-sheet before we even launched, so we had to incorporate quickly and we made some serious errors:

we grabbed the nearest lawyer instead of asking around for a good one.
he pushed what he called "a standard cookie cutter" agreement in front of us and assured us "it was fine for our purposes"
we didn't each seek outside legal counsel
we signed it

Years later, when serious money was involved and trouble inevitably followed, we each had a rude awakening when we took it to real lawyers (now that we could afford them) and found out what we had actually signed on for. ("Complete bag of shit" is how my lawyer usually referred to it).

This was a clear cut case of springing for a few extra bucks up front would have saved ten's of thousands down the road, not to mention months of grief. Fact was, I was too cheap and too timid to spend 500 bucks on a couple hours of competent legal time at the beginning. Had I done so, and then had the balls to return to the table and say things like "The shotgun clause needs to be reworked", "There's no easy way out of this" or "This thing handcuffs us together for life and I don't want that", for a bit of awkwardness, time and money we would have prevented enormous problems later.

I consider the first shareholder agreement I ever signed the most expensive (albeit educational) mistake I've ever made.

Posted by Mark Jeftovic in Venture Capital at 14:05

Sunday, August 28, 2005

CAT5 "perfect storm" shaping up in the financial markets?

Speaking as a guy who believes it is inherently impossible to predict things like stock market crashes, earthquakes and alien invasions, I'm getting numerous signals today that are food for thought on their own and ominous in aggregate. On one hand there is Hurricane Katrina which is barreling down on New Orleans, and if it hits can cause a lot more damage and fallout than we're accustomed to seeing from hurricanes, even bad ones. Apparently there's only been three other CAT5's in history and tonight Stratfor Global Intelligence sent out a breaking news report titled The Geopolitics of Katrina. Stratfor's core business is meticulously researched analysis, they are not in the "breaking news" business. The last time I received a breaking news alert from them was about 10 hours before the Iraq War II started, telling readers that bombers had been spotted departing from bases in Europe.

The economic effects from a full-on Katrina hit on the oil refineries and ports of Louisiana could be hard hitting. In fact the overnight oil price has already spiked past \$70/barrel as I type this (gold is up a couple bucks an ounce in fairly short order as well).

This combined with the fedspeak out of Jackson Hole this weekend make for an interesting couple weeks ahead. The speeches contained a couple of startling nuggets once you remove the circular, double-talk which the Fed carefully crafts to glaze over as many eyes as possible while bluffing at an appearance of transparency. Greenspan pronounced the housing bubble all but "ready-to-pop" in that understated hocus-pocus which is his trademark: "The housing boom will inevitably simmer down. As part of that process, house turnover will decline from currently historic levels, while some house price increases will slow and prices could even decrease".

Which is nice non-threatening way to state that the housing bubble which has been fueled entirely by reckless credit expansion is about ready to pop.

Governor Donald Kohn waxed philosophic on the pitfalls of financial derivatives and had this to say:

The risk is that private agents overestimate the ability or willingness of central banks to damp volatility in asset prices or the economy, or that they fail to appreciate that future policy actions depend on an imperfectly predictable economic outlook. But developments should have partially alleviated some of these concerns. Investors have had an opportunity to observe that policy actions in 1987, 1998, and 2001-03 cushioned the economy, but they did not stop major declines in the prices of equity in 1987 and 2001 or of risky credits in 1998. Short-term rates have risen substantially in the past year, reducing the profitability of "carry trades" without triggering an unwinding that drove long-term interest rates higher or widened risk premiums. And expectations that policy tightening would remain gradual over the near-term have not stopped long-term rates from fluctuating substantially in response to incoming data; the movements of future or forward rates out the yield curve after surprises in data have been at least as large since 2003 as they were before.

That is not to say that we have nothing to worry about. As I already noted, Alan Greenspan, himself, has often been concerned about market complacency--as recently as his latest monetary policy testimony. People may well perceive the economy as more stable than it is or central banks with greater power than we have to smooth the economy or to foresee our own actions.

Which, as George Ure notes, sounds like a nice soft way to tell the financial bankers in fedspeak/doublespeak: "If the derivatives blow up, don't assume we (the Central Bank) will be able to fix it".

These long-winded innocuous sounding pronouncements sound unimportant, barely comprehensible and boring. They are carefully crafted to appear to be just that. They are not. These statements are analyzed six-ways from Sunday by hordes of financial analysts and trillions of dollars worth of assets and perhaps more importantly, derivatives of assets, will slosh around the global economy based on their conclusions.

Any one of these factors on their own could make things interesting. All of them coming together in one shot could be pretty wild.

Posted by Mark Jeftovic in Venture Capital at 21:48

Thursday, June 23, 2005

It's scary....

I'm watching Larry Kudlow tear apart some senator on CNBC about the hysteria over the Chinese bid for Unocal. I'm agreeing with every word he says. Wow.

Larry is right, if the US are the champions of the free market, then they have to always champion it, not only when its in their interests to so, but when somebody else plays the same rules to their own advantage.

Right now, the US is making three demands on the Chinese:

1. Keep taking US dollars, even though their value is being deliberately watered down by rampant credit and monetary expansion.
2. Revalue the Yuan. In other words: while we ramp up the printing presses and devalue our currency, we want you to keep taking more of it.
3. Take more and more of this US paper, but whatever you do, don't use any of it to buy anything of value to us. Especially energy.

That isn't the type of environment mutually healthy trading relationships are made of. As Warren Buffet opined earlier today, if the US is going to keep consuming more than they're producing to the tune of 2 billion a day, then they have to be prepared to sell off valuable assets. What else are the trading partners going to do with enormous piles of US dollars which are rapidly losing value?

On other fronts my Fedex \$75 Puts expired worthless on friday and today they warned and plunged over \$6 a share. As the old adage goes: "The graveyards of Wall St. are littered with the bones of those who were too early".

Posted by Mark Jeftovic in Venture Capital at 15:22

Thursday, June 2, 2005

So long and thanks for all the...chaos

I've often wondered how Dave Lewis' Chaos-onomics could be so overlooked among the contrarian/libertarian/goldbug crew. I can best describe him as an "economic philosopher" of the highest calibre, but what do I know? Large swaths of his writing simply go over my head. I don't have the philosophical let alone economic background to understand a lot of it.

Yet in his columns I recognized something rare in this day and age. Something informed, not only from a deep repository of a well read individual but from his experience in the financial markets and his first hand accounts of financial hinge moments like the Asian Crisis. Contrast with the unreasoned, biased cheerleading of a Kudlow or the appalling non-thinking drivel of a Cramer, Dave Lewis' columns were grounded in an authenticity and depth of knowledge unheard of in mainstream financial commentary.

And now, it's over. Lewis has announced in his swan song post that he set out to research Peak Oil two months ago, wound up doing some philosophical soul searching, and arrived at the conclusion not to bother with it anymore! I am reminded of Thomas Kuhn's arguments in *The Structure of Scientific Revolutions* these days as I watch the dance of politics and economics, particularly the view that such transitions, from paradigm to paradigm, are not graceful. I am also reminded of the waning stages of any great ethical faith and Capitalism, like representative government, was, in my view, such a faith. In the early stages only a few believe but their belief is strong and pure. Then the faith is diluted but spread to many. In the later stages the faith is assumed, by which I mean, to use chivalry as an example, initially Knights aspired to be chivalrous, and in later periods, as that age was ending, they were merely assumed, by themselves more than by others, to be so. That the United States is often considered to BE a Capitalist economy, rather than an economy which aspires to follow those tenets suggests to me that faith in that system among the powers that be is virtually non-existent. If the powers that be don't believe in Capitalism as ethic to allocate resource any more, why should I waste my time thinking about the world in that paradigm. Of course, I could be wrong and all is well. In either case, regular commentary on the lines I had been following seems pointless.

It's a shame. I hope he'll keep his writings up, he has stated he will keep a closed mailing list going.

Posted by Mark Jeftovic in Venture Capital at 21:43

Tuesday, May 24, 2005

Madmoney: The Horror! The Horror!

Clicking around to kill the 5 minutes between the end of Law and Order and the beginning of Jon Stewart I happen upon Jim Cramer's "Madmoney" on CNBC. (My "CNBC Deathwatch", btw, is still in effect. It posits that in this secular bear market which started in 2000 and is closer to the beginning than to the end: the bottom is in when CNBC goes off the air).

Cramer is a raving loon, sort of a combination morning drive DJ and a religious evangelist he jumps and shouts and screams wildly bullish slogans at the camera. Like a washed out hag who overstays in the aftermath of a wild party, single handedly hooting and hollering, the name of the game is "keep the party going", long after the host has crashed, the guests have left and interest has dissipated. It would be bemusing to watch if it weren't pathetic and sad. Keep the party going, keep the party going, is the mantra of Wall St. Buy Buy Buy. (Ironically, insider sales have been somewhere around 30-to-1 since the bear market rally started in 2002.)

Jim likes Google. What passes for fundamental analysis is actually a cursory comparison of Google's share price growth vs. the P/E multiples of Coke and Pepsi, from which he derives a price target of \$450 for GOOG. That isn't sarcasm, that's really what he did, with a straight face.

The way to profit from Google, IMHO, is through AdSense, not buying the stock. Build yourself a portfolio of websites that get 10K pageviews a day and 1% clickthru on AdSense, and what you have my friend, is a nice income stream that few equity issues can match.

Posted by Mark Jeftovic in Venture Capital at 00:52

Saturday, May 21. 2005

Waitin' for the derivatives blowup

Contrary to some of the cranks and financial doomsayers I follow, I am not a permabear and I don't really want to see the markets meltdown and the economy hit a recession (or worse). But over the years I've acquired an appreciation for how little I know about economics. Along with it I wonder if even I, an economic simpleton, can perceive the fundamental disconnect between the financial fairy-tale promoted by the US politicians and their cheerleading squad, CNBC, why isn't this painfully obvious to anyone with a pulse?

Example: So far there has been a conspicuous absence of fallout from the downgrade of Ford and GM's debt to "junk status". In a piece of jawboning worthy of an Orwell Award, "the car industry doesn't matter" to the economy anymore. George Ure has pointed out that conventional Dow theory posits that the Dow Transports Index lead the wider markets (if the transports tank, the rest of the market will soon after); and that at some point, all of the car manufacturers have been removed from the index.

The underground contrarian channels are abuzz with the fear of an impending derivatives blow-up brought upon by the downgrade and there is talk that some hedge funds are dutifully unwinding positions in anticipation of a particularly heavy redemption season this summer. The phrase "remember LTCM" is being bandied about.

In contrast to this, the USD has hit a 2005 high and gold is below its 200 day moving average and gold stocks took a beating. All this despite some pretty dismal news coming out in April and the economic news in May, like the jobs numbers, look pretty unrealistically massaged (over 90% of the "new jobs" created were a statistical construct based on "historical norms").

Having said all that, my personal maxim (Mark's Law of The Expected Unexpected?) is that meltdowns, disasters, market crashes, terrorist events and asteroid hits cannot occur when anybody is expecting it. And "anybody" includes contrarians, cranks and conspiracy theorists.

Contrarians can only position themselves ahead of a perceived shift, but they can't time it. As Douglas Casey once quipped, "Just because something is inevitable, doesn't make it imminent".

Cranks are usually onside with the contrarians but tend to hold their positions longer than necessary out of ideological beliefs. This would include goldbugs who were converts at the top of the 1980 spike and have been holding (or averaging down) ever since. Don't get me wrong, cranks are intelligent and entertaining and have my respect. My personal definition of "crank" isn't as derogatory as some may think. Kinda like 'nerd' used to be. Nowadays it's practically 'hip' to be a nerd.

I include George Ure's in this category. He's a well read economist and I have a deep appreciation for his self-sufficiency, but I've watched him try and fail to not only "time the market" (which he often nails on an intra-day basis but not long term) but to "time the meltdown". According to Ure, we're in a window right now which could see anything from a derivatives based market meltdown to "the big one", a large quake hitting the West coast, which George has been bracing for/calling for/hoping for? for such a long time it seems almost morbid.

Conspiracy theorists are always and by definition wrong. Asteroid hits which won't happen and world leaders who are not members of an alien reptilian race. As per the old maxim: Never ascribe to conspiracy that which can be explained by stupidity. For this reason I am not entirely sure I buy into the manipulation of the price of gold theory which has been floating around for a few years. I guess long term I'm not too worried about it. If paper currencies actually do blow up, it won't matter. If they don't, the secular uptrend is undeniable.

So will the markets meltdown this week? The contrarian/crank/conspiracy contra-indicator says no. I think over the medium term gold will head on to new highs and given the fact that Japan and China have all but ceased purchasing new US debt paper, the USD will sink, and once the French vote "oui" to the EU the Euro will surge, and when Iran starts selling in Euros next year World War III will start in earnest....(ah, off into conspiracy land again....sorry)

Posted by Mark Jeftovic in Venture Capital at 18:17