Global Entrepreneur Alternative Asset Class Predictions
Interim Report Two: October 2010
Dr. Sally Ernst

Summary of Findings

According to the findings of this latest global survey, entrepreneurs currently have a negative sentiment about investment in alternative assets. The majority of entrepreneurs predict gold prices will rise but residential and commercial property prices will not increase significantly. Entrepreneurs across the world predict the environmental/green energy and health services sectors are the top industries for future growth, a change from their choice of biotech in the May 2010 Indicator.

Global: Interim Findings – Second Survey (October 2010)

*With an Indicator benchmark of 4.53 (out of 10), entrepreneurs globally have a negative viewpoint overall about alternative asset class performance— a decline in sentiment compared to the May 2010 Indicator.*

Currently, entrepreneurs across the world invest in the following alternative asset classes: residential real estate (63%), commercial real estate (36%) private equity (14%), art (12%) and precious metals (11%).

In the next 12 months, entrepreneurs globally are looking to invest in residential real estate (29%), commercial real estate (27%), private equity (11%), precious metals (10%) and green energy/clean technology (10%).

**More entrepreneurs predict commercial property prices will rise, but this is still a minority opinion.**

Slightly more than one-third of entrepreneurs globally (35%) predict an increase in residential property prices, less than in the previous survey (46%). Very few (0.8%) predict a significant increase in residential property values.

Similarly, one-third (33%) of entrepreneurs globally predict an increase in commercial properties, a notable increase on the 23% who predicted the same in the last survey. As with residential property prices, again very few (0.8%) expect a significant increase in commercial property value.

Only the Asia Pacific region predicted property prices to increase.
Most entrepreneurs predict the price of gold will continue to rise, but not significantly.

More than half of entrepreneurs globally (55%) predict an increase in the value of gold in the next 12 months, although very few (3%) predict its value will increase significantly. With the exception the Latin America-Caribbean (LAC) region, many entrepreneurs (42%) remain unsure about the average return on hedge funds and managed futures.

Entrepreneurs predict environmental/green energy and health services to be the sectors most likely to grow, yet only 1 in 10 entrepreneurs are investing in green tech themselves.

Entrepreneurs globally predict that environmental/recycling/green energy (70%), health/medical services (70%), technology (65%), biotechnology (64%) and business services (64%) will be the sectors most likely to grow in the coming year. While entrepreneurs rated the green energy/clean technology sector highest for growth, only 1 in 10 are planning to invest in that industry in the next 12 months.

Entrepreneurs do not expect clarity on currency exchange rate fluctuations in the near future.

On average, one-third of entrepreneurs globally believe that major currency exchange rates are too volatile to predict against their own currency. Just more than one-quarter of entrepreneurs (28%) believe that their currency will weaken against other major global currencies across the coming 12 months.

Entrepreneurs are unsure what to expect from the world credit markets.

Nearly half of entrepreneurs globally (49%) believe that interest rates will decrease in the coming quarter. Half (50%) predict that access to lines of credit in their country will become more difficult in the coming quarter.
About the Research

This report is part of the Global Economic Indicator research program conducted by the Entrepreneurs’ Organization in partnership with The Standard Chartered Private Bank. This research program began in May of 2010 and consists of a five-year series of quarterly surveys of Entrepreneurs’ Organization members. The full report and findings are available at: http://www.entrepreneurindicator.com/.

The significance and uniqueness of this global research program lies in the very tight definition of a successful entrepreneur represented by the Entrepreneurs’ Organization’s membership base. All those surveyed have successfully founded a business grossing more than US$1 million in revenue annually. Overall, EO members average US$18.4 million in revenue per year. Between them, these entrepreneurs employ more than 1.3 million workers, with an average of 191 employees per entrepreneur. The average age of the entrepreneurs surveyed is 40. This group is generally very difficult to gain access to and poll. However, the Entrepreneurs’ Organization holds a member base fitting these criteria that are captive to the organization, providing the ability to gain an entree to this highly important sample of the successful entrepreneur population.

This initial research surveyed more than 7,300 entrepreneurs in 42 countries from the Entrepreneurs Organization, achieving a response rate of 20% based on a minimum reach of 7,300.

Global Entrepreneur Indicator: Alternative Asset Classes

This is the second report providing readers the interim findings of a series of research activities over an intended period of five years being undertaken by Entrepreneurs’ Organization (EO) in partnership with Standard Chartered Private Bank. At the time of writing, The Global Entrepreneur Indicator for Alternative Asset Classes is the first of its kind globally, which measures entrepreneurs’ predictions on Alternative Asset Class performance.

Six versions of the Alternative Asset Class indicator have been produced:

- Global Indicator – aggregate of all respondents globally
- Country and Regional Indicators – aggregate for each country with a discrete response rate above 50. For this survey, the countries and regions include:
  - US
  - Latin America and the Caribbean (LAC)
  - Canada
  - Asia Pacific region (ASAP)
  - Europe-Middle East-Africa (EMEA)

Detailed Interim Research and Regional reports will appear at http://www.entrepreneurindicator.com/.

Acknowledgements

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Methodology

Survey

The survey incorporates elements of cited Alternative Asset Class investments as described in the research report literature scan below. The test for the choice of key indicators for the purposes of this research is that they are later measurable against actual asset class performance.

There are seven categories measured in the indicator:

- Currency
- Residential real estate
- Commercial real estate
- Precious metals
- Managed futures
- Hedge funds
- Selves/own businesses

Some additional questions of interest to Entrepreneurs’ Organization about their members’ opinions, which are not used in the calculation of the Indicator, have also been included in the Indicator survey. These, as well as data from Indicator questions, may be used in the Alternative Asset Class Indicator or other Entrepreneurs’ Organization Indicators.

The Indicator is calculated as the category score, or averaged upper end and neutral percentages divided by 10, which are then averaged across all category scores with equal weighting to give the final Indicator benchmark out of 10.

Limitations

- Not all respondents may have received the email
- Over 50% surveyed were based in the US and represented 58% of respondents.
- Some regional Indicators have a small response rate relative to their size. These reports can perhaps be used in the context of the longitudinal data as a benchmark made richer over time
- There may be anomalies in the membership data, such as an owner or major shareholder rather than founder may be included in respondents or other anomalies.
- There may be anomalies caused by technology in the process from data extraction, to survey delivery, to responses, to first stage analysis. While noted as a limitation, this is for probity as these are estimated to be minimal.
- Per the below statistics, most of the membership base is categorized as founder or cofounder, however, more founders and cofounders could be included in the owner and major shareholder categories. Members in these additional categories could potentially be categorized as entrepreneurs, dependent on the nature of intent to innovate or innovation.

<table>
<thead>
<tr>
<th>Category</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Founder or Co-Founder</td>
<td>53%</td>
</tr>
<tr>
<td>Owner</td>
<td>34%</td>
</tr>
<tr>
<td>Controlling Shareholder</td>
<td>9%</td>
</tr>
<tr>
<td>Other</td>
<td>4%</td>
</tr>
</tbody>
</table>
Response Rates Summary

<table>
<thead>
<tr>
<th>Region</th>
<th>Count</th>
</tr>
</thead>
<tbody>
<tr>
<td>Asia/Pacific</td>
<td>237</td>
</tr>
<tr>
<td>Canada</td>
<td>118</td>
</tr>
<tr>
<td>Europe/Africa/Middle East</td>
<td>85</td>
</tr>
<tr>
<td>Latin America/Caribbean</td>
<td>55</td>
</tr>
<tr>
<td>United States</td>
<td>712</td>
</tr>
<tr>
<td>Global Total</td>
<td>1207</td>
</tr>
</tbody>
</table>

Background to Alternative Asset Classes

Entrepreneurs are a special group, given their ability to assimilate the information available to the general population differently to generate opportunity and create new things. This group continues to be a generally understudied population at scale.

There is some evidence that alternative asset classes may improve investment returns as part of a portfolio. While loose and broad, the definition of alternative asset classes may exclude stocks, bonds and cash.

For the purposes of the Global Entrepreneur Indicator, alternative asset classes were defined as either tangible or intangible goods that have a proven economic value but are not typically included in standard investment portfolios. Investors may look to alternative asset classes to diversify their portfolios. Due to their nature, it can be difficult to arrive at an objective valuation of alternative asset classes.

Bonds, stock and cash are generally excluded from the definition of alternative asset classes, as they represent, in most cases, the fundamental constituents of portfolios.

About Alternative Asset Classes

Given its broad definition, the Global Entrepreneur Indicator carves out the alternative asset classes and/or components of alternative asset classes that are most easily measurable for their return and are subjectively perceived to be more accessible, attractive and/or applicable to entrepreneurs. They have then been ordered by the alternative asset class’ ability to be consistently and clearly valued and measured.

For example, Private Equity has been excluded for the purposes of the research, as these investments are usually relatively large, available to qualified investors only and may not be applicable to the majority of entrepreneurs. Another example is philanthropy, which may not be clearly valued or measured. In the case of education, it has been excluded because the risk is not easy to assess. Even though education is perceived by some as an investment with a high return—higher even than bonds or gold—it is difficult to quantify when considered against ‘conventional’ assets such as bonds or equity for which return is justified by risk (Judd, 2000).

Hedge Funds

Hedge Funds became popular as an investment vehicle in the late 1990s as an alternative to stocks, which were then characterized by high prices and low returns (Edwards & Liew, 1999). According to HFR (2010) hedge-funds have recovered in the first quarter of 2010 from the low values reached in early 2009. Globally, hedge funds now manage approximately US$1,670 billion of assets. During the first quarter of 2010, hedge funds have recorded an average return of 2.56%. Relative-value funds have recorded higher values, returning on average 3.58% in the first quarter of this year (Jones, 2010; HFR, 2010).
Natural Resources/Commodities

The Bloomberg Global Poll of investors, traders and analysts conducted on 19 January 2010, revealed that after stocks, commodities were considered as the most promising asset class (Dorning & Dodge, 2010). Commodities may be perceived by some to be an attractive investment as, being strongly linked to supply and demand, this alternative asset class has the advantage of potentially protecting portfolios from inflation (Bloemker, 2010). Examples of investible commodities are:

- Gas
- Oil
- Corn
- Cotton
- Copper
- Soybean
- Precious metals (Platinum, Gold, Silver)

According to the Halifax Assetwatch press release published 6 March, 2010, precious metals overall increased in value by 242% in the decade December 1999 to December 2009. Respectively, gold registered an annual average increase in price of 14.2%, platinum of 12.7% and silver of 12.6% (Halifax Assetwatch, 2010).

Managed Future Accounts

Managed future accounts are investment vehicles managed by Commodity Trading Advisors (CTAs) (Investopedia, 2010a). CTAs trade a portfolio of futures, forwards or options in global currency, interest rate, metal, energy and agricultural markets (Morgan Stanley Smith Barney, 2009). Although the strategies that CTAs employ on their portfolios can vary greatly, these managers all trade highly liquid and regulated financial products (Barclay Hedge, 2010).

Investors may perceive managed futures as an attractive way to diversify their portfolio due to their potential non-correlation to stocks and bonds (Barclay Hedge, 2010). Successful managers generally use modern portfolio theory to pick assets that will maximize returns against the level of risk they have chosen to take (Investopedia 2010b). Since their introduction in 1980, according to the CASAM CISDM CTA Equal Weighted Index, managed futures had a compound average return of 14.52%, almost double the return of U.S. stocks over the same period (based on the S&P 500 total return index).

Real Estate

Investment in real estate can be directed to the purchase of any of the following categories of estates and may be perceived by investors as a hedge against inflation (Skidmore, 2010):

- Commercial real estate
- Residential real estate

In the UK, returns on residential and commercial properties respectively recorded an average 11.1% and 5.8% return between December 1999 and December 2009. However, in 2009 alone residential properties recorded a return of 8.7%, and commercial properties recorded a return of -1.4% (Halifax, 2010).

Even though real estate is often considered an alternative asset class, it is sometimes considered an ‘additional’ asset class to stock, bonds and cash. One reason is that before the emergence of stocks and bonds, real estate was the preferred asset class. Upon the invention of stock and bonds, these were considered alternative asset classes to real estate. Additionally, real estate is often considered as a fundamental and indispensible component of a well-diversified portfolio (Anson, 2006).
Microfinance
Socially Responsible Investments ("SRIs") are investments aimed to generate financial return and social, environmental and ethical improvements. Of all SRIs, microfinance is currently the sector that attracts the largest number of investors.

Microfinance is a term that describes the provision of financial services to poor parts of the population that otherwise would not have access to banking services. Micro-loans are aimed at poor individuals who are able to engage in a productive entrepreneurial activity. Examples of micro-borrowers are street vendors, small farmers and fishermen.

According to a study conducted by The MIX on a sample of around 704 microfinance institutions, for the year 2007, the leading 176 MFIs recorded a RoE of 17.2% (The MIX, 2006). Investments in microfinance are expected to rise to around USD 20bn by 2015 (Deutsche Bank Research, 2007).

Wine
Wine investment has registered steady growth since the early 1990s, with an average annual growth rate of 17.64%. Compared to other alternative asset classes, wine investment has some perceived advantages: wine is easy to store, is likely to increase in quality with time, is not subject to fashions and may be shown to increase value with rarity. Increasing global demand and the existence of professional investment advice services appear to be making wine an interesting investment opportunity (Golding, 2009).

Collectibles and Luxury Items
Categories of goods that can be included in the collectibles and luxury items alternative asset class are:

- Art (produced by famous artists and emerging artists)
- Photography
- Stamps and coins
- Antiques
- Classic cars and motorbikes
- Vintage watches
- Yachts
- Designer fashion
- Sport and music memorabilia and autographs
- Toys

Let’s take the example of art. Even if the return is almost impossible to measure accurately, it appears an increasing number of investors perceive art as an interesting alternative investment opportunity. Bernard Duffy, manager of the “Emotional Assets” fund, which invests in art and other collectibles, thinks investors can make a 15% profit per year (Papworth & Collinson, 2009). However, art may be perceived as a long-term investment that is likely difficult to value, and may be unlikely to guarantee immediate liquidity. On the other hand, art may also be considered by some as a hedge against inflation.

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References and Further Reading


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