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Institutional Investor Profile: Knightsbridge Advisers

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Managing principals Joel Romines, Barbara Piette and George Arnold on early stage investing, on deal quality, on adding value to portfolio companies, on pattern recognition and on the finite nature of the industry.



Knightsbridge Advisers is a fund of funds manager with \$1.4bn in assets under management. The firm, founded by Joel Romines in 1983 in London, focuses on early stage venture capital partnerships. To date, it has established 17 investment vehicles.

Knightsbridge has an investment office in Cambridge, Massachusetts, and its finance and operations division is headquartered in Bartlesville, Oklahoma.

For the past 25 years, Knightsbridge has offered investment opportunities in US early stage venture, initially to European institutional investors and subsequently to global institutions.

Joel Romines is a former consultant to institutional investor, Horsley Bridge Associates. From 1980 to 1982, he served as vice president and director of a venture capital-backed start-up company. Previously, he was employed by Orion Bank in the UK from 1972 to 1980, where he was an executive director.

Barbara Piette joined Knightsbridge in August 2006 as a managing principal. She was a general partner of Charles River Ventures from 1986-1992, responsible for a portfolio of healthcare, technology and consumer companies. Piette served on the boards of seven companies, including Community Health Systems, Abacus Direct and FAO Schwarz. From 1992 to 1999, she was a partner at Schroder Ventures, where she invested in and served on the boards of several companies, including GelTex Pharmaceuticals, Allos Therapeutics and AmeriPath. From 2000, she was president of Blackwood Capital, investing in and advising private and public company management teams.

George Arnold joined Knightsbridge as a managing principal in May 2007. Previously, he was director and head of venture/growth equity fund investments for Citigroup Private Equity. From 1998 to 2003, he invested directly in private technology companies alongside venture investors and on behalf of Citigroup, serving as a director or observer on many company boards, including Insurance.com, ConvergeNet, Guardent, Mobile365 and Openwave.

What is your investment strategy?

'We are quite clear in our mission: we back only those company-building venture capitalists, usually early-stage, with proven track records and persistent returns. What Knightsbridge has always believed, and what academic research is now pointing out, is this notion of persistence - that the best venture firms tend to perform consistently over time. There is always some fall-out from that, but, essentially, there is a high correlation between top tier and continued performance in the top tier.'

What is your average bite size?

'Our sweet spot is about \$15m and our range is between \$10m to \$20m. We offer our investors a balanced portfolio, without overweighting any manager too much. We attempt to keep most of our portfolio funds in that range.'

Do you make direct investments?

'No. Direct investing is a different business. Contrary to buy out, where LPs frequently co-invest, on the venture side co-investments are rare. It is very difficult to co-invest with a top-tier early stage fund in Series A. The questions then are: which deals can you get into in a later series, what type of valuations you have to pay - and ultimately whether you are able to get into the best deals. We certainly think that the best way to participate in the best deals is not through a co-investment programme, but through accessing top early stage venture capital funds.'

What is your opinion on country-focused versus international funds?

'We seek to invest with the best venture capital funds in the world. Historically, the best funds have been in the Silicon Valley and Boston areas. Today, there are other geographies where we see attractive managers, and we have established some relationships outside Silicon Valley and Boston.'

In the US, we have a number of funds that have operated on a more global basis over a long period of time. More recently, some of these funds have established affiliated funds abroad or are directly active in working with local businesses abroad. Historically, we have invested in very few funds that are headquartered outside of the US. They account for a small fraction of our portfolio but we are seeing more international exposure through our existing fund investments.'

Israel is an interesting example - great technology, great teams, but a very small market. Israeli entrepreneurs typically create a product and then look to team up with some of the best venture capitalists in the US, who help them penetrate the US market.'

Another international model is America, where US venture capitalists in our portfolio invest in companies based overseas, which may pursue a business model that has already been proven back in the US. Similarly, they may have companies that target markets in Europe or Asia. Overall, the venture capital business is becoming an increasingly global business.'

What is your average number of investments per year?

'While we do not have a specific target, our range has been between eight and ten investments per year. This is also dependent on the pace of investing in the venture capital market.'

How do you find out about good investments?

'Usually, the select type of funds that we are most interested in are not offered broadly to new investors. They are accessible only by invitation. If it is an existing firm, we are tracking them, even if we are not already an investor. If it is a new firm, we will typically hear about it in a few different ways: from the founding general partners, from other venture capital firms that we are involved with, or from other limited partners and investors with whom we are close.'

Do you invest in first-time funds?

'We have invested in new funds. But - going back to the original mission - we look to invest in the best venture firms in the world. Part of the hurdle associated with that is that we look for teams that have an established track record or that we have known from their prior venture capital partnerships. The team may be a reformulation of another entity or franchise, but track record is part of the criteria. The business of venture capital is an apprenticeship business.'

What are the characteristics that you look for in a team that would encourage you to take the next step?

'It's a matter of pattern recognition. Because we have all been in the business for so long, we tend to have almost an intuitive feel for what we want. Individual characteristics would include the past track records of success of the individual general partners, including particular companies that they have been involved with, rates of return, strategic focus and whether this aligns with our aim to back the best early stage and

start-up venture capitalists.

The key concept is that we invest with those venture capitalists who are company builders rather than stock pickers. The 'company builders' are those venture capitalists that add value to their investments by building the business on a number of levels.

The 'stock pickers' come in late and tend to compete on personality and price. We prefer to back teams that go in early and add value; they are known throughout the entrepreneurial community. If they have built great companies previously, the entrepreneurs all know that and want to work with that team or general partner. This is one of the reasons for persistence, and it is that success that attracts the best entrepreneurs of the next generation.

Essentially, we would like the funds that we back to receive the first contact from the best entrepreneurs in the market place. Venture capital is a business where there is high persistence, where success breeds success, time after time. We are typically seeking to invest in venture funds that have this cycle with entrepreneurs. These venture funds also tend to have the strongest limited partner investors in the industry.

Another key success factor in venture capital is the fund's ability to reinvent itself. Times change, markets change, and the teams that were doing the brilliant telecom deals a decade ago cannot continue to do the same kind of deals. We are looking for people who have the passion, the intellectual curiosity, the technical background and the sheer competitive force to be constantly finding new markets and opportunities.'

How do you conduct your due diligence?

'An important distinction between Knightsbridge and most of the other firms, not just funds of funds, but other limited partners in general, is that in Barbara and George we have two individuals at Knightsbridge who are deeply experienced from the venture capitalist side of the boardroom table. Barbara had a long career as a venture capitalist; George has a decade of experience focused on investing in venture-backed private companies.

For us, due diligence is something that does not start with getting a PPM. We are so focused on the venture capital industry, and so networked in the industry, that we are essentially doing due diligence on an ongoing basis as we meet with new and existing managers. It is an ongoing process. We treat a re-up decision in the same way as we treat a new relationship investment decision.

The way we think about it is both top-down and bottom-up. Our top-down approach deals with partnership structure, economics and awareness of the industry. We have been on the other side, investing directly in early stage companies. We can recognise signs that companies could be in trouble or indeed signs that companies could be performing well.

Looking at it from the portfolio company level up, we try to make a determination that the VCP is investing in, and helping to build, substantial next-generation companies in areas of profound market disruption.'

And how long does this take?

'We do not think about it in terms of time. We really think about it in terms of the depth and quality of the information that we have. Again, we do due diligence every day. With every meeting we take, we are hearing information about firms that we are already invested in, and also other firms that are out there.'

Are there any industry sectors or segments that you feel are of particular interest?

We do not target by industry sector. We invest in the best venture capitalists, who in turn select market sectors. There are substantial opportunities across various sectors. We continue to see tremendous opportunities on the IT side and on the life sciences side, such as medtech and therapeutics. Over the last eight or nine years, a number of our venture capitalists have built cleantech, energy and material science practices. Last year a number of these companies were accessing the public markets and had very nice exits. We think all of those sectors are attractive, and we have exposure to all of them as a result of the relationships that we have.

We believe that one of the most important criteria that investors can use to track the success of any limited partner is to look at the percentage share of exits. Each year we track the IPOs that our venture capitalists participated in and believe that we stack up very strongly on this metric.

Who are your investors?

'Without mentioning individual examples, they fall into the foundation, endowment, pension funds, wealth management and family offices, in the US and globally.'

What do you feel is the most pressing issue currently facing the private equity industry?

'We believe the issues are more on the buy-out side. It is similar to the late 1990s when people thought that things would just continue to scale up. With the difficulties in the debt markets today, it is not clear what the future holds for buy-out funds. Not having any exposure to debt on the venture side, we feel comfortable but it remains to be seen what impact it all has on the US or world economy. A deteriorating US or world economy would obviously have an adverse impact on our portfolio companies although some of the great venture start-ups have occurred during troubled economies.'

Are there any developments that you can anticipate? With your experience, is anything completely unexpected for you any more?

'We embrace the unexpected because it can produce fantastic innovative technologies in huge and growing marketplaces. The mistake that people make is to assume that venture is scalable and infinite like other segments of the private equity or public equity businesses, and it is neither. It is an extremely finite industry. While we believe strongly that innovation will inexorably produce fantastic opportunities that will in turn create huge markets, there is only a small group of people in the world that have proven to have the expertise to capture returns in those areas.'

One of the positive aspects of venture is that today, more than ever, you can build a larger company with more sustainability more quickly than ever before, in large part due to the fact that there are global resources and markets in place to build these companies.'

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