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Office of the Vice Provost for Advances in Learning



MODULE 3 UNIT 1

Casebook Video 1

Transcript

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LAUREN COHEN: Andrew Fisher loved to predict the future. He loved to predict the future so much that he made his life's work out of predicting the future. You see, Andrew Fisher was the managing partner of LXE Capital Group, which was a long/short equity hedge fund based right outside of DC.

Now when he heard about this company called Recorded Future, it piqued his interest and he had to get the meeting. Recorded Future was this company that had just made the crossover from the defense industry into the financial industry. Now, as he sat in dead-stop traffic on his way into Washington DC, Andrew couldn't help but think of all the different ways that he could potentially use Recorded Future at his investment firm.

Now, pan to Christopher Ahlberg who was the founder and the CEO of Recorded Future, and he was having a very different day. You see, Chris was trying to manage both the existing contracts that they had – mostly with the defense industry, so with the CIA, with the Department of Defense – and was now fretting about this first interview that he was having with the financial services industry and Andrew Fisher. Now, they just gotten into this financial services and just started to use the powerful, and what they thought the really great and potentially limitless uses of Recorded Future would be, into this financial space.

But first let's take a step back and understand what they did at the beginning and the real genesis of Recorded Future. So, if you take a look at the exhibit, it's going to show you the kinds of things they did in the defense industry. So, what this exhibit is showing us is how Recorded Future used their software to predict a terrorist attack that happened in Uganda in 2010.

So as you can see, what they did was they took all of the information that they collected across tens of thousands of websites, and they used that information to try to predict and show you that they could get pretty good predictive ability over this event. And in particular, they did things such as looking at forums and looking at blogs where they thought expected terrorists might be posting, and look for words like "plan to" and "we will" or "are looking to execute," and they aggregated all of these, used their machine learning framework to find where the aberrations occurred and predicted this attack was going to happen.

So fast forward to the financial services industry and you can see how they're trying to use that same technology and that same insight of using what's going on on the web right now to predict the future in financial services. So in this exhibit, you can see the returns to a strategy that Recorded Future had developed to try to predict the future of the stock market and of stocks. So in particular, from these two exhibits, you see that Recorded Future classifies each firm into its likelihood of appreciating in value, or having positive returns, or depreciating in value, or having negative returns, for every given day. And they do that every single day by downloading huge amounts of the web and processing that through their machine learning framework. And that produces this strategy which has not only outperformed most major benchmarks up to this point, but has had a pretty impressive out-of-sample return. And Chris was very confident in both its ability to perform today and its ability to perform in the future.



So you can imagine how surprised Chris Ahlberg was – then the CEO of Recorded Future – when his meeting with Andrew went disastrously. And so, why did it go so poorly? Well when Andrew came in and saw all of this massive amount of data that Christopher had, he demanded that Chris run 10 new studies and 10 new cuts of the data, and then to provide him and LXE Capital with their own proprietary version of this Recorded Future strategy. And at that, Andrew left and said, “I’ll hear back from you in a week.” The first thing Chris did was got his stress ball and squeezed it a few times, but then when he’d settled down, he went to his analysts to talk about what had happened.

Now, what Chris was figuring out is that financial services are a very shark-infested water for a data provider firm to be in. And in particular, data is such a valuable commodity within financial services, but not unstructured data alone. The data has to be turned in to a profitable investment strategy or it doesn’t provide any value. And now, that transformation into a profitable investment strategy, that can be done by the data provider itself – Recorded Future – or by the end-user, LXE Capital Group. But of course, for LXE to shell out a reasonable amount of money, they want to see some proof that it can be, this data can be transformed into a profitable investment strategy.

Therein lies the Herculean task of Chris Ahlberg. So, that is to say that Chris had to prove that Recorded Future provided this great investment value for hedge funds. But, the problem is that in itself provided its own negative feedback, in that if Chris were to show that this were a profitable investment strategy, then when he sold it to his first client – let’s say Andrew Fisher at LXE Capital – then Andrew’s incentive is, of course, for Chris not to sell that to any other person. Because, as you see, if Chris’s strategy were to say Apple is today priced at 90 and it’s going to 100, then, if he were to sell it to 10 of Andrew’s competitors, and were to tell them to buy Apple, then they would push up Apple’s price to 91, 92, 93, and maybe by the time Andrew got the news that Apple was a great buy, it would be at 95. And so he would have lost half of those potential profits he could make.

So as Chris sat back, this provided a real dilemma for him in terms of the prospects of Recorded Future in the financial industry going forward. Although he saw its promise as a FinTech firm, he wasn’t sure whether it made sense for them to invest a huge amount of resources in specializing in financial services, which could take away from their existing and very profitable defense business.

Andrew Fisher on the other hand was whistling a pretty happy tune, because you see, he saw the promise in Recorded Future and he had a very pointed idea about how Recorded Future could unlock a huge amount of value in this financial services space. So, he was planning to come back in one week with a proposal from his firm, LXE, and Recorded Future can partner up to really chart forward that path.

So what I want you to do is think about what Andrew Fisher’s proposition might be. How might he be thinking that he could take Recorded Future and mold it in to this value creating engine that he saw?

