

URL: <https://ecorner.stanford.edu/clips/three-sources-of-edge/>

Josh Wolfe, co-founder and managing partner of Lux Capital, describes three essential sources of edge for entrepreneurs or investors in venture capital: informational, analytical, and behavioral. He advises aspiring entrepreneurs to have conviction in their own ideas and encourages thinking longer than other people instead of looking for a quick fix.



Transcript

- When you are an entrepreneur 00:00:04,350 and when you are an investor in venture, there are three sources of edge that you can have.. And it's really important that you understand this, because the third is the most important.. You can have an informational edge, you can have an analytical edge, you can have a behavioral edge.. Informational edge means that you get information that other people don't have.. In today's world, that's really hard, because information is abundant.. It wants to be free, in the proverbial sense.. It's flowing everywhere.. Analytical is that we get the same information.. Maybe Dina, my partner, gets a piece of information.. I get another piece of information..

It's the same piece of information, but I analyze it differently than she does.. Maybe she's closer to ground truth, and I'm wrong.. Also really hard, because there's brilliant people, and now we're all augmented by AI, and it's really hard to have a better analysis than somebody else.. But behavioral is the one source of lasting advantage, to identify where the herd is going.. Back then, in that example with nuclear, everybody in the herd was going in cleantech for alternative energy, and biofuels, and solar, and ethanol, and we took the other way.. So, if you as an entrepreneur, can identify, what is everybody else doing? And what can I do differently? And then be right, is really powerful.. This is a great example.. It's the Simon Ash experiment.. How many people have ever seen this before? The guy in the red sweater is the mark.. Everybody else is in on this..

It's a psychological study about group things.. So, watch what happens.. They're gonna show a bunch of lines, and the lines, they're gonna lie about which one matches.. And he's gonna look at them, and say, "You idiots, you've got it completely wrong!" Watch what happens.. Narrator In the first test, the correct answer is two.. 00:01:27,000 Speaker 1 One.. 00:01:27,900 Speaker 2 One.. 00:01:29,723 - One.. 00:01:36,003 - It's two.. 00:01:37,820 Instructor One..

00:01:42,090 Narrator Once again, the correct answer is two.. 00:01:43,492 Speaker 1 It's three.. 00:01:45,371 Speaker 2 Three.. 00:01:46,204 - Three.. 00:01:53,040 - Three? 00:01:54,383 - Now he knows it's not three.. (audience laughing) But the social pressure is so strong, and you will encounter so many situations that, I'm sure you already have, where that social pressure to conform, and go along with what other people are doing.. And again, have the belief and the conviction in your own ideas, and stand away from the crowd.. It's painful.. It literally feels like pain to be socially ostracized.. But if it's of your

own choosing to separate, it's a really powerful thing..

So, those three lines, if you flip 'em horizontally, you get a different advantage, which is time arbitrage, if you can think longer than other people.. So many people are looking for the startup that is the quick fix, something that's gonna pay off in a year or two.. But all the deeply technical stuff takes a long time, it takes a lot of money, it's a lot harder.. It's like taking a shot, and you don't know, if you're gonna hit a three pointer for, like, six years.. But sometimes the biggest payoffs are these longer-term things.. So, we like to invest in things where there's time arbitrage, where we're going further out than other people are, because there's just less traffic there to compete...