

Fireside Chat: Money and passion

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Interviewer: Um, thank you. Um, we're going to get started with our last session of the day. Uh, this session features, uh, two investors. Um, you call yourself an investor, right?

Paul Graham: Yeah.

Interviewer: Okay. Uh, Paul Graham from Y Combinator and Mike Moritz of Sequoia Capital. Um, arguably the, it's sort of, I'm not exactly two ends of the spectrum, but towards the beginning of the spectrum, two very prominent, very interesting, and in Sequoia's case, very successful, uh, investors. Paul is just early in the game, right? We have a lot of potential.

Paul Graham: Yeah. Yeah.

Interviewer: Um, and I thought that there could be no better two people in the world to discuss early-stage tech investing, the role of revenue in investing, um, those kinds of topics and these two gentlemen. So, I'll first let Paul introduce himself and explain Y Combinator, and then I'll let Mike, uh,

Paul Graham: Y Combinator invests in a whole bunch of startups all at once, sort of mass production for startups. So, we'll invest in like 25 or 30 startups at a time, twice a year, in batch mode. Um, and work with them intensively for 3 months, at the end of which we have a presentation uh, day where they all present to investors. Uh, there's so many of them now, they only get 5 minutes a piece. So, that big day is called Demo Day. And then after that, we hope they get the next round of money. So, we're just trying to be first gear.

Interviewer: Okay. And during that time period that they're with you, do, are they incubated? Are they, you know, what's the, what do you do?

Paul Graham: Uh, we talk, the main thing that we do that's useful is, uh, well, we do a bunch of things that I wish I didn't have to do, like, you know, arbitrate conflicts between founders and stuff like that, right? Um but the main thing that we do that's useful is try and figure out what to build first. Okay?

Interviewer: Okay. But Okay, Michael, go ahead.

Mike Moritz: So, I'm with Sequoia and uh we like the um Paul, what's your average investment?

Paul Graham: It's about \$25,000. \$20,000. \$20,000.

Mike Moritz: And um we like to invest um small amounts of money um as well. Uh and I've never really understood why uh people uh people would say in the venture businesses they often do that they have minimums to invest and that it isn't worth their while unless they can invest \$5 million or \$10 million. Um I've always thought that if somebody offered you an opportunity to buy a quarter of a company or a fifth of a company for a million dollars, I don't know why you'd want to pay \$5 million for the same privilege. So, it's always puzzled me and um I think also uh companies with very small amounts of money tend to work better over the long term as well for a whole variety of reasons um uh that we can talk about later if you're interested. And our business is trying to find and be in business with the most imaginative, most enterprising, most creative souls that we can find within easy range of the offices that we have. And the offices that we have are here. And they're in um China. And they're in India, and they're in Israel, because much of the most stimulating, interesting development is happening, unlike 30 years ago, um, is happening outside of this wonderful place where all of us uh, happen to live, and some of the leading-edge applications in particular genres are not built by startups in, uh, Silicon Valley. They're built by startups, uh, that get their, um, uh, that are, uh, based elsewhere. And so, we think over the next 25 years, um, that's going to be, while Silicon Valley is always going to be an incredibly important place for us, and we uh, have as many people here in Silicon Valley as we have ever had. Um, the, uh, currents of history are undeniably running faster elsewhere.

Interviewer: Yeah. You know, if you ask most venture capitalists, what are they looking for in a company they they fund, they will tell you they want a proven team with a proven technology with a proven business model. Mhm. So, if I were to ask Mike Moritz of Sequoia that question, and Paul Graham of Y Combinator, what was the answer?

Mike Moritz: When we invest, nothing seems to be proven. The market isn't proven. The people usually are unknown. And the product or the technology, um, at the time that we invest in in the venture business, uh, frequently, um, barely works, or perhaps might just, you know, on its most elegant day, barely limp. But, so, I I think if you're looking for proven things, um, you wind up too much uh, in the conventional uh, um, portion of the universe where uninteresting things tend to happen.

Interviewer: Do you think that completely different orientation from most VCs is an essential part of Sequoia's success?

Mike Moritz: I don't know. We've always tended to have an affinity for the underdog, the offbeat, the immigrant. Um the Uh that's a very serious observation um actually. Um it's part of the reason

we're in China, India, and Israel because those people don't come to Silicon Valley anymore.

Interviewer: And you yourself are an immigrant.

Mike Moritz: I Yeah, I am. There's only one person in and it's no accident. There's only one person who works at Sequoia in uh Silicon Valley who was born in Silicon Valley. Everybody else has come from else.

Interviewer: Who Who's that?

Mike Moritz: Kwame. Mark.

Interviewer: Huh. He's our minority hire. He's the tall white guy?

Mike Moritz: Yeah. He's the white boy, huh?

Interviewer: Okay. Um Paul, what is your you know proven What's your prove What What are you What qualities are you looking for? Because you you get many more applicants than the people you take, obviously. So, what are you looking for?

Paul Graham: We look for people who are um determined, smart, have a sense of design, um and get things done. And so we do look for certain kinds of provenness, but not the kind you might think. You talk about proven entrepreneurs, right? What we want is evidence that someone really likes to build things, right? We want people who are really good at building stuff, technology. Um And to be really good at something you have to actually like it. You can't just be doing it out of a sense of duty because it's your job, because it's you know something you have to do in a class, right? And so it's very hard for someone who really likes programming, for example, to get to age 23 without having built something outside of school or work. So, the big question we ask is what have you made outside of school or work because you liked it? Because if you don't like it, you're not going to do well as a startup founder. And it has to be something other than the opposite sex. That you do well.

Interviewer: Okay. Um And and in this we're at something called revenue bootcamp, so we're talking about revenue. Mike and and Paul do you really give a [unclear] about their forecast for their revenue? Do you believe an ounce of what they say? Do you Do you care? Just make a guess. Are you You know, are you crunching your HP 12 and looking at the internal rate of return for their four-year forecast? I mean, how do you How do you interpret the lies they tell you about revenue?

Paul Graham: We have a don't ask, don't tell policy on revenue projections. We don't even ask. I

mean, Sequoia, you guys probably ask at least to see what they're going to say, right? But, we don't even ask.

Mike Moritz: But, we don't inhale. Certainly not the forecasts. I I think it's much more important to feel that you're investing or that the company is positioned in an area where the currents are flowing in its favor and you have no idea how strongly those currents are going to flow. And when we look at forecasts, as you alluded to, we take them with a with a grain of salt. Our premise really is how do we get through the first year. Um do we think that the company has the wherewithal, the means, that enough money to be able to survive the first year if things don't happen as forecast because they usually don't. And if we survive the first year, we can worry about the second year and so on. And, you know, 5-years plans aren't worth the uh ink cartridge that they are um that they're written with.

Interviewer: Now Now Now But we have to be very specific and careful here. Now you're saying you don't rely on the Excel spreadsheet printed out plan. But can someone come into both of your organizations saying we're just a bunch of young immigrants and we finished a lot of projects in our time and now we want to build this cool thing and we have no freaking idea if we can have any revenue doing it. Would that Not Not Yeah, said that way, but would it work?

Mike Moritz: I I think if somebody said it with the blaziness that you just said.

Interviewer: So they have to fake sincerity.

Mike Moritz: No, no, you have to care. It's not that you have to lie. You have to be determined and you have to have a passion and you have to have an intensity about it and you have to leave people feeling without faking it that you're sincere, that it is the single most important thing in your life. You don't have to say you know, you shouldn't say like we have no idea how to make money and it's not a problem, but it's okay if you say we have no idea how to make money. We're worried about that. We know that's a problem. Talk to us. Let's figure out how to make money. You know, you guys are supposed to be investors. Tell us how to make money, right? That's fine. Together that we invested in the little I mean, this is a wonderful example of it, right? Dropbox, little company. Mhm. How do you think they make money? Uh Just saying. So um but this was um two people at the beginning, right? Yeah. Um who had come from MIT. They came from Boston because they just didn't feel that the environment and the atmosphere there was right and they'd be able to hire all the people that they needed. These are um two young guys from MIT. They relocated to the West Coast thanks to Paul and his offices. They set up shop with an idea about cloud-based storage and backup and syncing and services. And my goodness, these two characters, they're really smart. They had an incredible passion. They were doing something enormously useful for people where there was real value in it and it was very obvious that if they could crack the code and deliver something of value, people would pay for it.

Interviewer: So, is it fair to say that in a sense, the best kind of financial forecast that an entrepreneur could present is one that it's a picture that they paint where you fantasize about the revenue potential, not not because they've drawn it out on some spreadsheet.

Paul Graham: I've heard people give that advice specifically for convincing investors and it works fairly well, you know. I think the best financial forecast is a sense that you're developing something that people will really care and want. Mhm. And if they really care and want, the money will follow. But if you're developing something that no one cares about or is just like everything else, there's going to be no money.

Interviewer: But Mike, I mean, you'd have to be a real idiot to walk into your office and say we're presenting something that people really don't care that much about, but we want funding to do it. I mean, doesn't every entrepreneur say we really believe in this and it's going to be great and our beta sites are loving it?

Mike Moritz: Yeah, but we have look, we have fairly tuned antennas. Uh and red flashing lights that come on and alarms that go off when the BS level rises, you know.

Interviewer: Okay. And maximum alert, maximum alert. Uh so uh What sets off your BS detector?

Mike Moritz: Uh Nobody wants to answer this. There's so many things.

Interviewer: Well, just give us a few.

Mike Moritz: Well, when people use generic language. Like when people describe how they feel about their idea using the word passion. Um like never use the word passion. I mean you should

Interviewer: Show passion. Like you shouldn't tell, you shouldn't say the word passion. You should just seem like you care. Right? But um Okay, so don't use the P-word. Don't don't say that you care. Just care, right? Um How about the R-word, revolutionary? You know, I don't think there's anything revolutionary. I Now, the PR masters and the marketing departments will tell you the and the evangelists of yesteryear, the reformed evangelists, will uh tell you that here are lots of revolutionary there are lots of revolutionary companies and revolutionary products, but I think if we're all very candid with ourselves, almost every single company that gets uh organized uh in Silicon Valley is is an evolutionary company and an uh evolutionary product. I don't think you can fake sincerity, and I don't think you can fake uh the pursuit of excellence or a cause to which you have devoted uh more time and thought than almost any other pe- uh than than other people around you. I just uh you may be able to fake it for a few minutes, but it's not going to survive close scrutiny. Okay. Um Let's another very sticky topic with entrepreneurs is how do we present

our competitive analysis? Right? So, the typical entrepreneur puts up a grid, and guess what? Their column is everything's checked off, and their competitors' column is nothing's checked off, right? So, and I it's at Garage we've never had anybody come in where their column wasn't fully checked off. So, what's your advice for how entrepreneurs should present a competitive landscape?

Paul Graham: Well, you know, all of these questions, it depends on the kind of investor they're talking to. Basically, the smarter the investor, the more you should just be candid. Cuz a smart investor will just like if you lie, they'll notice you're lying, right? Um so that the that the entrepreneurs that came into the garage thought we were stupid, so

Interviewer: Well, they might have mistakenly thought you were stupid. Right? I'm not saying whether they were correct or not. But did you live up to expectations?

Paul Graham: We exceeded them. In several cases, we exceeded them, yes. But the smarter the investor, like you should when you're talking to really smart investors, which are the kind whose money you presumably want, then you should just tell them what you would say amongst yourselves, right? Like, "We're worried about such and such company because of such and such, but you know, we think we have an edge because of this, right?" Just tell people what's going on, you know? It's like the better the investor, the more it should be like going to the doctor. Like, don't lie about your symptoms. Tell them exactly what's going on, right? You know.

Interviewer: Okay, Paul. Uh no, Paul. Mike. No, I agree with what uh Paul said. Yeah, just being honest about the competitive landscape. Cuz most entrepreneurs would say, "Wow, if I admit that our competitor is better, they won't want to fund me." No, I think it's better for everybody, and we always say this to people, and they they never say this to people, and they they never believe or they rarely believe us, but we tell them, "Look, you you don't want any surprises or you want to minimize the number of surprises that you have about us if you'd like to choose us as your partner in business. So, go out and talk to people that we've been in business with and make up your own mind." And we also would just we know that they're going to be bumps and we're going to hit potholes and have hiccups in the as the way that the business develops, but the the fewer surprises, the better off everybody's going to going to be. So, it's a very unhealthy way to begin a long business relationship where uh an investment is won, and then in the first formal meeting uh after the wire has uh crossed the line, um the bad news and truth is conveyed. Um so, it's way better to just uh be forthright, minimize the surprises. The entrepreneurs aren't going to have all entrepreneurs aren't going to have all the answers. We're certainly not going to have all the answers. And I think people have to understand that when you make a very early stage investment, a very early stage venture investment, it's the entrepreneurs and the investors against all odds. And it's a very small group of people, entrepreneurs and investors, um waging this massive battle where everybody, the large companies, the everybody, the large companies, the

everybody, the large companies, the competitors, parents, friends, relatives, other people in the investment community, uh think it's a wacky pursuit that you're off on.

Interviewer: I've I've um obviously watched many of the Sequoia successes. I've been to you know, I've spoken for you at Y Combinator several times. And I'm always struck that the people that both of you fund, the companies that both of you fund, are 25 or younger. There's no old people there, right? We've had some. We've had some. is that a random observation of mine? Do you believe there's some causative relationship? You know, on the other hand, you hear many VCs, they say, "Well, we would love this senior team that worked at uh Microsoft, and he was senior VP of engineering, and now he's senior VP of engineering, and now he's senior VP of engineering, and now he's going to start a startup. That's a proven guy, proven gal. So, what's age got to do with this?"

Paul Graham: Well, I think the reason we've I mean, the average startup founder we fund is probably 25 or 26, but I think the reason is just more people start ups at that age. By the time people are in their 30s, they have, you know, families and mortgages, and their friends that they wanted to start the startup with or more tied down to, right? Um so you get this sort of exponential effect of tied downness as people get older. 25-year-olds, they can just say, "What the hell, we'll try it." Right? So there's just more 25-year-olds starting startups. starting startups.

Interviewer: Okay. Mike. Mozart was dead at 35. Which Or 33, I don't know. But he was proven. He was a proven composer at that point. So so what? Are we So are you saying that Is the is the sweet spot for Sequoia? You know, Larry, David, Jerry, PhD student at Stanford University, not business school, engineering department. school, engineering department. And You know. Bingo, bingo, bingo. Yeah. Yep. No doubt about it. Um Are they Are they creating products that they themselves want to use or they themselves want to use or they believe they read that there's a huge market, so we're going to go after that market? What are they doing?

Paul Graham: It's ideal if they're building something they themselves want to use. The next best thing is something, you know, that someone very close to them, like their wife or sibling wants to use.

Interviewer: Okay. That's right. That's right. It It means you have a very deep understanding of what's essential in the product. Which is something you can't intellectualize. Um and uh You know, I agree with Paul and obviously there are examples of people at later stages of life uh who develop very interesting ideas, but you think across Like who? Well, I'll leave you to come up with it. Uh but extraordinary people when you can go across all of the sciences um and most people have done most of their incredibly fertile, imaginative, and creative work because of the reasons that Paul mentioned, because of the lack of distraction, because of uh you know, Evelyn Waugh said that in a in a in a in a different business, he said, "You know, the greatest enemy" He was a

writer, obviously. He said, "The greatest enemy to good art is the sight of the perambulator in the hallway." Sight of the baby pram to convert it into English in the hallway. And me there for a second. The stroller. The stroller. Stroller, baby carriage. I got it. The greatest enemy, guy, the greatest enemy to good art is the sight of the stroller in the hallway. Okay. And I think that that's the same. It's a similar issue very much with um with young companies. How about the cane? Um for the benefit of this audience, I would love you to explain what they should reasonably expect a Y Combinator or Sequoia to do for them. Because My answer is very simple, which is beyond all the all the promises and everything. Our goal is simple, and if we don't live up to it, our business perishes, which is Miss or Mr. Entrepreneur, if X number of years from now, 5 years, 7 years, 8 years from now, you can't say to a buddy of yours or an acquaintance or a friend that having us as a business partner was one of the very best decisions that you made in your business life or in the evolution of your company, then we failed you. Okay, that's that's a good general answer, but does this mean you're giving them 5 hours a month, 10 hours a month? Are you opening up your Rolodex? Are you calling up Jeff Bezos to put in a new server from two guys in a garage? I mean, what can they reasonably expect from Sequoia to do?

Paul Graham: I think these these companies all have their arcs. Mhm. The needs and challenges of three people are very different from the needs and challenges of if everything goes well in the company 3 years later is 300 people and it's got a completely But think of the little company where it's three people and you're trying to convince a few engineers to join you and the engineers don't want to leave, and then engineers don't want to leave, and then engineers don't want to leave, and then you're trying to convince the management to join you and the management doesn't to join you and the management doesn't to join you and the management doesn't want to leave, and then you've got a product and the customer says, "Why should we buy from this rinky-dink little startup?" Those are very different challenges to the ones that he more mature company is going to the more mature company is going to have. And we have got to be able to help the really small startup with uh answering uh those sorts of tasks and challenges. They may want, you know, we're an investor I noticed in one of your sponsors here, Rackspace. They may want special deal from Rackspace, for example. Well, we're going to see what we can do on on It's all those little nitty-gritty things at the beginning. And with a great intensity in the first 12 months in particular of one of these companies, because you get the first 12 months right, chances are the next 60 months and the next 10 years are going to go right. If you get the first 12 months wrong, you are um you're going to have a really tough time changing it around. And I think also you've got to recognize we're investors, we're not managers, we're not confused. Our job is to bring the people into the company, help get the company into the market, help if we've got to go out on customer calls, go out on customer calls. But then the very best thing for all of us is the company's able to recruit its own people, the company's able to point to its own customer list to bring in new customers, and then the nature of the challenge changes, and you're 5 years into the company, and then um you'll find that there's some massive huge deal that they can't get where there's, you know, uh an emergency call, and and and things happen, or the conversation changes to how do we enter the

Japanese market, or what's the best way to figure out how we survive in China, or you know, what are the perils of outsourcing a whole bunch of stuff uh stuff in India, and then the issues of you know, raising more money, or going public, or all of those sorts of things. So, the nature nature of it all uh changes over time, as does the relationship. And the relationship with a startup that runs the arc, I mean, in the first few months, we can be on the phone every day, or have meetings every day, or certainly be on email every day. And then, the frequency of the contact as the startup survives, the frequency of the contact in the healthy relationship should diminish. Not unlike uh the sort of experience everybody has they and like all analogies, this is this is a little tired is a tired analogy, but it's the evolution of a family if you're a parent, where there's every

Interviewer: Every moment early on. You're attuned to the needs of the infant, and then over time, you know, by the time it's college age, you don't want to know anyways. Um your your answer to that question about, you know, what not or specifically Y Combinator, but in general, I mean, is the Y Combinator, you're with me for 90 days, I help you, we push you out, sink or swim, aloha, or

Paul Graham: No, no, we stay we stay in touch with people after the 90 days. All that stops after 90 days is we don't have dinner once a week. Um We we We have dinner with everybody once a week for the first 3 months. Um Uh until uh a year ago, I used to actually cook the dinner. Um but it got to the point where it was really ridiculous. Um I think everybody's glad I'm not actually doing the cooking anymore. Um We work We focus on two things cuz we're so early, right? Like a VC fund like Sequoia, they can give you advice about how to do an IPO, right? I don't know anything about IPOs. Um what I know about is the kind of problems that people face in the very beginning. Like for example, there's three of you starting a company. Oh, no, sorry, it's two, right? That's the kind of thing that happens in the Well, you know, that Yeah, that happened at YouTube. YouTube was three people when they when we encountered them. And within the first week, there was a head count reduction of 33%. And it was two people. And that's our life. And um you know, the the YouTube people needed more than \$25,000, but um the intensity of the relationship when it's just two people, it's uh you know, if you haven't been involved with it, if you haven't lived it, if you haven't seen it day-to-day, it is hard to imagine the extent of the uh emotional connection we have with these things. And you you may interpret that as just venture BS, but believe me, talk to the people that we've been in business with. Okay. Uh subject that very few people ever discuss is You know, you you always hear about the story about perseverance and gutting it out and all that, but is there a point in a company's life where it really should give up? It should return the money that it has, if any. It should sell its assets. It just wasn't meant to be. Not necessarily the people were bozos or, you know, whatever, but just is there a point and when do you how do you know what what is it?

Interviewer: If the founders have given up. As long as the founders haven't given up, they can morph the company into anything. I mean, maybe you could get into some case where you'd like gotten deeply in debt and there was no way to dig yourself out, but as long as you're in the in the

early phase and you're just like a couple of guys in an apartment, you know, eating beans and writing code, you can turn turn thing around tomorrow if you want to. The So, sometimes founders will come to me and say, "Can I give up now?" Right? And basically, if they're asking me, probably the answer is yes, because if they're asking me, they've already decided they're giving up and they just want me to be okay with it. But as long as they're willing to say like we're doing it's a we're a year in, our software still sucks, we have no customers, but we're not giving up. I'm like, "Okay, keep going. I'll help you, you know." I'm willing to help them as long as they're willing to keep fighting. What about you, Mike? Because you're willing to help them as long as they're willing to keep fighting, but they want your money to keep fighting.

Paul Graham: Well, the year one answer is an easy answer. Where it gets hard is year five. Mhm. And where things just haven't worked perhaps. And where everybody is very well meaning, but the market has rejected the product. Um the next product doesn't look very promising and there's not much hope for it. And uh everybody understands that including the founders. There are people prepared to continue investing money in what seems like a futile charge in a futile battle. That's where the uh issue is is very difficult. We had a I can think of two companies that both are actually chip companies where we had calamitous experiences early on. The best known one of these is uh Nvidia, uh which everybody knows today, but people don't remember 1993 and 1994. And Nvidia's first device was a bomb. It failed in the marketplace. This was a semiconductor company. Semiconductor companies, you can't finance with two people writing code, living on rice and beans. They're more expensive endeavors to get off the ground. And there um it would have been very easy to say, "My goodness, the original idea didn't work, um and it's curtains. Um and Jensen and the rest of the people there had another product that they were very convinced about. And ourselves and Sutter Hill in that case um continued supporting the company, but it would have been very easy to blink and say, "Look, the original premise didn't work, but also, I think there are some battles that are worth fighting and some battles that aren't worth fighting. And we may well be wrong about both. We may be well eventually have our nose bloodied in the battles we want to continue fighting. We may well perhaps give up too early on the things that uh that we think are futile. But uh as long as we think there's a a way that we can survive and then eventually prosper, and it makes economic sense to do so, we're going to do it. Where we think it's futile, where we think and frequently the conversation, well, actually as infrequently as you can have these conversations a bit. But frequently the conversation when you have to have these horrible conversations with uh the people who've just, you know, worked so hard for four or five years, haven't seen their families, they're up to their uh eyeballs in debt, they're overweight, they're stressed out. They haven't been on vacations. I mean, this is a dreadful and it's a dreadful dreadful thing. But the conversation is, "Do you know, you're only going to live once. Do you want to waste the next three or five years of your life on something that's an enterprise that is is doomed to failure? That's the conversation.

Interviewer: Okay. A a real tactical question. What makes a good board meeting? What should

happen in a board meeting, an ideal board meeting? Cuz I've been in many of them and

Paul Graham: We're not in it. Okay. That's for me, that's ideal. We're not here.

Interviewer: That's an answer. Yeah.

Paul Graham: I have never been on a board and I never will. We don't take board seats and uh I think you can do a lot of the things, not all of the things a board member can do maybe, but I think you can do a lot of the things a board member can do without being a formal board member. I mean, any advice you want to give as a board member, you can give not as a board member. It just doesn't have any standing, right? Like if it's good, they'll listen, one hopes. Um But that was a that was a a silly answer. You should You can give the serious answer. No, I think the most interesting and most important things at companies happen between board meetings not at board meetings and the board meetings usually just ratify those sorts of things and uh if the involvement of a company is just the board meeting, you know, it's just the investors showing up at the board meeting, um it's it from my point of view, I'm not very interested. That is just not a very interesting or fulfilling uh thing to do. So, um So, I you know, usually the best ones are brief, they're short, there are no surprises, but that's because all of the important things have basically been discussed, talked about, um chewed over uh beforehand. And sometimes if they're different parties and constituencies associated with the company, um you uh um you have to resolve those uh during board meetings, but our obligation is pretty intense with these companies. You know, if Y Combinator elects if Paul elects not to invest the next \$25,000 his company is not dead. If we've made a commitment to a company and said we're going to be your investor and sign up and if we don't invest the next \$2 million or million dollars or something, that company is going to have a very very tough time. So, there's an enormous obligation. It's easy you know, Paul's in a in a slightly different part of the business to us, but we can't abdicate the responsibility that we've signed up for with these companies.

Interviewer: What if a CEO specifically has bad news? Sales are down, big sale didn't happen, product is late, whatever. How do you play that scenario? Do you Do you call you up and before the board meeting or you spring it at the board meeting? Obviously not. What do you do?

Paul Graham: CEO CEOs usually do not have good news. Okay. I met with one this morning who emailed me two days ago saying he needed When you see the phrase in the email, need to get together. Need to get together means the VP sales just quit, we missed the quarter, or I'm actually far closer to running out of money than I thought I was. I was not disappointed at 7:30 this morning. So, it happens all the time. And that is usually people people tend to want to give good news when there's a big crowd around they can celebrate not to impart it one on one, but most of the time when we hear when people do call and they want to have an urgent meeting, it's always bad news. I've never heard anyone say, I really need to come to see you to tell you how great

everything's going.

Interviewer: Yeah, same here. Well, I've noticed this in the news actually. If you look at headlines, I mean, bad things happen more suddenly than good things, right? Um unless you have some artificial thing like a a publication deadline for some research study or something like that that makes it artificially happen fast. You know, all the news about sudden changes, it's because it was a plane crash, you know, not because Plane landed. Right. Yeah. Or air air safety statistics gradually got better, right? That's the bigger story. I mean, the the Air France crash is just anecdotal evidence, right? Actually, aircraft plane traffic travel gets gradually safer and safer, right? But that's a boring headline. No no plane landed in the Hudson today. Yeah. I saw that tweet, yeah. Let's take some questions from the audience. Hello, yes. Can you hear me there? Yeah. Okay. Yeah, I'd just like um to know all three of yours opinion on what do you think the next um big wave of innovation's going to be in the next 5 7 years as you see it? Okay. Who's going first? You know, this kind of silence. It's well If I if I knew what it was going to be now, right? I would be making all the companies we fund do it, right? So, kind of by definition, you can't answer that. It's like asking, you know, if there's a new paradigm for physics after the standard model, what's it going to be? Well, if you actually knew the answer to that, you'd be eligible for a Nobel Prize. Just submit to some journal. Um so, it's It's it's it's hard to answer questions like that. I can tell you a specific version though. Like I was thinking about this uh while people were talking about Twitter um before. I can tell you what platforms are going to be big. If you want to know how to predict if how to predict what platforms are going to be big, look at the ones that hackers themselves use because they build stuff for the platforms that they use. We have a ton of companies building stuff for iPhones right now and it's because they all have iPhones, right?

Interviewer: Not one is building stuff for the BlackBerry because none of them use Blackberries. Blackberries have some amount of market share but like not among startup founders, right? Um so look for the platforms that hackers themselves use and those are the ones exciting things are going to happen to you and that's like really bad news for RIM by the way. How about Nokia? Nokia, what's that? They is like this Finnish company that makes cell phones? How about Pre then? Yeah, nobody's building anything for Pre either. They would like to build things for Android but um but like where where are the Android phones, right? You know. Okay, Michael, your prediction?

Paul Graham: I don't know what the next big people frequently ask what the next big thing is. I I don't know and uh you know, one of the truisms of the business that we're in is that when if we've done our homework before an investment, we're rarely ever surprised if the business teeters or or doesn't succeed. It's when the business really takes off that we're surprised and in in all candor, it's true. Um you know, I was I been at Sequoia for about a year when um at the end of um 1987, there were four or five people from Stanford who had an idea about how to network networks. And um and the company had sold four or five hundred thousand dollars worth of products. The um one

early customer had been Hewlett-Packard. The Hewlett-Packard engineers were very upset with this little company, and they were threatening to return a few of these um these early units. Um there was there was um there have been a number of strains and tensions inside the company, and if anybody had said, you know, this company is going to be known around the world as a company called Cisco Systems, I mean d all of these things that happened to and all of these things that happened to that company happened over the ensuing 18 years. I mean, we would have thought we'd landed on a different planet. We were just looking at trying to survive the first year. Um what's the lesson to learn from that, Cisco?

Interviewer: So, that's a I never heard that story. That's a great story. So, was it

Paul Graham: But but I think it's true of of most companies. I was not at Sequoia when Don uh elped to organize the original helped to organize the original financing of Apple, but somebody sent me in the last few months sent me and I read it years and years ago for different reason. Um sent me the original Apple business plan. Actually, it was the gentleman who sent who had helped with Mike Markkula who had written the original uh Apple business plan, and we were chatting about it, and he said, you know, we were sitting down there needing to devise and invent things that we could put in here because we couldn't get to a market size that was large nough, and we had absolutely no idea. enough, and we had absolutely no idea. We thought this, you know, the original application was going to be for uh people keeping their recipes at home. And uh the uh and they had no idea about So, here uh the most stunning revelation back to the point Paul was just making about the iPhone. The idea of the independent software developer back then, but even before you joined that guy, '76, '77, nobody had conceived of the independent software developer. Nobody had conceived of a company writing VisiCalc for a computer like the Apple was completely completely blindsided. So, I think trying to imagine what the next big thing is, I I long ago gave up on that. And I will offer my opinion, I also don't know. You know what? I'll tell you, if you want the source of a really good idea, think of something that you guys yourselves have needed in some company that you worked for that didn't exist and you were sitting in the company saying, "Boy, if somebody would just make blank, we'd pay a lot for that, right?" If you can think of any answer to blank, you are on onto a gold mine.

Interviewer: I I have that uh Mike I'm a software programmer and I have a uh I invented computers that go in golf cars. My question uh I put \$500,000 into my own business into my uh software developing company. The question I have is I'm looking to raise two and a half million dollars. I put 500,000. What does a venture capitalist look like as far as evaluating a company? How do you determine what the value of a company is and what percentage of that company uh you're going to own uh in the developing stages moving forward?

Paul Graham: Okay. Valuation. Valuation. Um It moves around. Depends how much perceived risk is uh seen in the company. Um But, I can tell you what we don't like. And this will sound

really weird, but it's true. We don't like owning too much. Um because it means several things. It means the company probably needs too much money. But more particularly, it means that the founders aren't very shrewd. And it also means that there isn't enough left for all the other people that we need to bring into the company and incense. So usually we we wind up I'll give you a very direct answer for a very early stage company. Um, the low band is around 20% and it ends to go up to around 35% but I get ends to go up to around 35% but I get ends to go up to around 35% but I get very nervous if we own more than 35%. I'll give you an answer. The the observation I would make is that for every full-time engineer, you have a pre-money valuation of half a million dollars. For every MBA, you subtract a quarter million. So if you have three full-time engineers and you know, two MBAs, three times half a million is a million and a half, you subtract two times 250, you're back at a million. So that's how you that's how you figure it. It's very simple. Very simple. Next question?

Interviewer: Yeah, Mike Mike, you've already mentioned that you start to get nervous about the five-year point. Um, there are twin themes I'd like you to comment on. A current theme of socially responsible investing and the theme of patient capital. Both oxymorons, huh?

Paul Graham: Well, um, there are there are businesses that we don't invest in because uh um, they appear unseemly. Um, and we don't want to wander into a gray zone. We've worked very hard over a very long period of time uh building our reputation and it's a reputation that can get eviscerated if you make the wrong choice. I I think um Yeah, on the question of patient investors, um I think Guy, to some extent, is right. Look, it's a mixture of both patience and impatience. When you're running a company, when you're an investor in a company, things can never happen quickly enough. You want the next product out. You want o get more sales. You have all these to get more sales. You have all these impulses about how you want to go quicker and how you want to go faster in a presumably um uh organized fashion. But, simultaneously, you also know, you know, I always chuckle when a newspaper or you know, on the on the net these days, and in the in the times when IPOs occurred, as they will occur again, and inevitably the media will say, uh here's a particular company, and in the next sentence, "Another Silicon Valley overnight success story." And they've forgotten about the preceding 6 years. I think I we've we've learned that uh it actually takes considerable patience to endure the overnight.

Interviewer: How How do you handle a situation where it takes If we could go back in time, you find out that wow, lots of porn are buying Cisco equipment. Or there's lots of copyrighted material going up on YouTube, and you're trying to remain the squeaky-clean investor, but you know, what do you do? You tell Cisco not to sell to porn sites, or you tell YouTube, what do you do?

Paul Graham: Well, we also had the issue of PayPal, where we had Mhm. uh there the issue was that the site was being used for gambling. Mhm. And aroused the ire of, you know, there was every attorney general in the in the country, including the ones, interestingly enough, in Mississippi. Um

who I'm not sure that they had a background of moral rectitude, but um

Interviewer: How about New York?

Paul Graham: Yeah. Well, they did in New York City. It was just when they ventured out of the state that they ran into problems. Um Uh Look, we we want to I think the You know, you look at the trend The early traffic at Yahoo, and sex queries were probably among the highest, but we're not going to We're not on a mission to improve the human character. I mean, our That's a quote. VC not interested in improving human character. Um but so our companies, they operate clearly within the confines of the law, but they come inevitably to represent all the good things about the society that we live in, and they also inevitably come to represent some of its flaws, as well. It's just life. Okay. Next question.

Interviewer: Um this is actually for all three of you. How do you feel about husband and wife teams, and have you ever funded one?

Paul Graham: Yes. Um both male female and male male. Um Uh They Up to the repeal profit. They seem to work fairly well. Um Uh It's better if it's it's What you want to have What you want to make sure is that the husband-wife team like they would have both been in the startup even if they weren't married. Right? You don't want the case where someone's doing a startup and they drag their spouse in because they're their spouse and not because they're the right person for the startup. As long as they're the right people, then it seems to be okay.

Interviewer: Okay. Why?

Paul Graham: Um we've we've financed um companies like that. Um Cisco. Um Sandy Lerner and Len Bosack, uh the two founders were uh usband and wife. I think uh usband and wife. I think uh usband and wife. I think uh I can think of other places where we've had brothers or sisters or in some cases sons or daughters working inside of the same company as well. I think it it does require uh heightened sensitivity because clearly um it creates uh a certain set of social dynamics that uh aren't in m- that aren't apparent in in most companies, but uh but it's clearly something that that uh we've learned to live with in a company. But on the whole, look, 98% of the companies that we financed, they don't have that sort of setting anyway.

Interviewer: But you you certainly wouldn't view it as a positive that husband and wife are starting a team, would you?

Paul Graham: I don't Ideally, you shouldn't care either way. Ideally, they're just good either way. Ideally, they're just good people and the fact that they have ex relationship to one another or not, it shouldn't make that much difference. Okay. Ideally.

Interviewer: Hi guy. So, this is the token China question. Um I think we met 9 years ago in 60th floor of the Grand Hyatt in Shanghai. Um yeah, what was I doing there? I don't know. So, um uh so before at that time, Sequoia had not entered China. They entered China, I think, a few years later. Um and I I kind of watched it methodically in how you guys did that. So, my question now is four or five years later after you really cut your teeth there, what are the obstacles you're going through now? Um, how is that different from what you go with in startups here in the US? And then, is your horizon longer because my feeling about China is barring some speculative backdoor listing on the Hong Kong Stock Exchange, the M&A market's a lot less. So, what is your horizon on these investments?

Paul Graham: Well, there are multiple questions there. Um, and when we went to China, we didn't for a moment think it was an it was started with the first business that we built outside of California was in Israel. And it took us multiple years. And Israel obviously is a much more confined geography, smaller population, uh, less of a language uh, barrier than one contends with in China. But, um, it also informed us and taught us a lot about what was required to operate uh, in an arena where in a different time zone, um, thousands of miles away. Um, and so when

Interviewer: We went to China, we knew that this was uh, not an overnight undertaking. This was a big move for us. We were signing up for a very long-term commitment. And the business and it was a move for the next 15 or 20 years, not for the next three or five years. And so, think of all the things that you have to do. Build the team, build a presence, begin to uh, make investments, develop. And we felt that the the the investment process that we've worked on so hard here can be translated into other places. What we cannot translate or pretend to hope to translate is all the network of connections, and understanding of the market, and the nuances of the local setting, which are completely obviously uh, obviously foreign to us. We knew too that there would be all sorts of surprises, bad surprises, bad news. Didn't know what they would be, but we knew we'd braced ourselves for that. Um, but also felt that my goodness gracious, despite all of those things, despite the unpredictability of uh of the topography, the underlying trends were so dramatic, so wonderful. The hunger, the desire, the ambition, the work ethic so intense in China compared to anywhere else in the world. Um, that we really wanted to do it. And we're now 5 years or so into this and feel very, very vindicated. Um, in fact, literally on the way here uh or just before I left the office, I was writing a little note that we were circulating internally. Um, we distributed holdings uh today from two investments that we made in China 3 to 4 years ago. And uh I can tell you, you know, I was in China a few few weeks ago and there was a CEO of a company who was very, very apologetic and about his growth rate. And I said uh and you will chuckle. Uh he said, "Yeah, you know, it's a really bad year." What do you mean it's a really bad year? Last year, revenues profitable company, last year revenues were \$120 million. This year, revenues \$180 million. And if you haven't been there, if you haven't spent time there, if you haven't immersed yourself there, it's difficult to translate to the US the scope of what is happening in China. And in particular arenas, I

mean, we're investing in a broader swath of companies than we invest here because some of these markets that we have considered mature here are obviously embryonic in China. But, there are particular applications, I you know, particularly in mobile where China is leagues ahead of anything happening in the US or in Europe.

Interviewer: So, so when he told you that, did you act pissed off?

Paul Graham: No, I uh I told him the truth. I I said uh you know, companies like yours this was a retailing company that'd be delighted to be growing 5 or 6% a year uh in America. You know, um with open source and just he the lower cost of everything the the lower cost of everything when a company comes to Sequoia or Y Combinator and pitches you, do you have higher expectations that they're further along, that they have you know, a working prototype where as 5 years ago you know, they would just have an idea and not a prototype, but now because of MySQL and Drupal and Rails and all the good stuff you ex- you have higher expectations of when they first pop into your door? They ought to be able to at least make some sort of demo. Yeah. Unless they're unless they're building something that's really going to take a long time like, you know some kind of hardware device or something like that. I mean, between the point where we invite them to interviews and when the actual interview comes, we give them like 3 weeks so they can get plane tickets, right? In 3 weeks, they ought to be able to throw together something so that we don't just have to talk. Right? We ought to be able to look at something. It's a good sign if they do.

Interviewer: What about you?

Paul Graham: It hasn't changed very much. Um and I think, you know, we also we invest in networking companies and systems companies where um as Paul uh mentioned, it's it's much more difficult to have a working, you know, okay, you're you're you're you're going to build a firewall that takes on Cisco. Are you not going to cobble that together in the time that it takes you to reserve a cheap airfare from uh from the East Coast. So, I think it's true and and and but we've also been you know, over the years we've invested in we've made the mistake of investing in snazzy-looking prototypes or sexy-looking PowerPoints. And I think you also have to uh make the big leap of uh you know, you've got to have the judgment to for what lies behind turning the idea or the product or the power or the prototype or the PowerPoint into something that is real and works.

Interviewer: Okay. Next question. As a follow-up to the email to portfolio CEOs from not too long ago, what would be the prognosis you guys have for the economy right now?

Paul Graham: Well, uh in our great innocence, this was a slideshow that got much wider distri- It People We We chuckle people thought it was a PR stunt. Actually, what happened was we had a meeting up in up on Sand Hill Road last September or so where we invited CEOs and founders to

uh come and uh listen and then do what they chose with the information to our views about what was happening in the world around us. And then a couple of people asked us to email this um slideshow for a very interesting reason. There was a couple of CEOs asked us to email Several CEOs asked us to email the slideshow. We said, "Why?" And they said, "Well, I believe you, but none of my management team believes me when I go back and tell them this. I need the materials." So, so it got wide distribution. I think um and you know the the really good news about that um event was the people understood and I think a large part of it was because um CEOs and founders of companies had lived through 2000 and remembered it. And boy, uh people adjusted in the grand scheme of things incredibly quickly. Uh but I think everything that we said back then about a really dreadful patch was correct. And I think what we said back then about an extremely slow, torturous recovery, I think that's also that's also right. For us the the really bad news uh from companies probably, you know, the rate at bad news decay started to really tail off uh towards the end of February. And um uh for the most part, everybody has adjusted to a world where they have to be self-sufficient. They know that they can't rely on cheap outside money and um everything has been adjusted. Um and in part, particularly for the younger companies, we've actually been um pleasantly surprised by revenue and bookings in in the last couple of quarters because one of the benefits, and it's quirky, of a real setback in an economic setback like this one that we've gone through is oddly enough, it makes it easier for the small company, particularly if they're selling to the enterprise, to get a hearing because the customers are in such desperate need for either increased performance or lower cost, whereas in far better times, when they have money to burn, the little company won't get a hearing. So, um it's it's oddly enough a little easier for the unknown company to get a foothold in uh a market than in times that are really flush.

Interviewer: Okay. How about one last question? Who's got it? Yep.

Paul Graham: So, I found the the remarks about kind of the prototypical CEO a little sobering because I'm not a 25-year-old engineer. I mean, what what advice do you give someone who's more experienced, if you will? I mean, would you Should I be going out to recruit some 25-year-old take my place?

Interviewer: I don't think that was actually the answer. I think the question the guy had asked was about founders. It wasn't about CEOs. Why did the founder Mhm. I He's the founder, though. Ah. Well, we live in a state where there's no discrimination. In investing or in employment? In both, actually. I mean, uh all jesting aside about Mozart dying at the age of 35, we've also invested in a company that was started by a grandfather. That's avoiding the the question. Look at your audience. Huh? Look at your audience. How many people here are entrepreneurs and are over 30 years old? Raise your hand. Mhm. Would any of us be able to present to you?

Paul Graham: The honest answer to that is absolutely yes. The easiest way to get a response is to send direct email either to Paul or to myself. And if the idea has, in our warped mind, real merit,

absolutely guaranteed.

Interviewer: All right. There's I'll open the book. The problem they the problem is they all heard, "Oh, he's interested in my deal." WHICH IS NOT EXACTLY WHAT MIKE just said. No. To to quote our departed leader, bring it on. So, thank you very much. Uh please join me in thanking uh both Paul and Mike. Um it is clearly the end of our day here. And uh I just wanted to thank you all for attending the first revenue boot camp. Perhaps we'll have some more in the future. Um we started off this morning with a sobering panel with some young people about what they'll pay for and what they won't. Um that was pretty interesting. And then we had a very good panel about traffic, how to generate traffic, which I think the general story we learned is that, you know, it's all about good content. And it's not about all this black magic. Uh it is truly a simple deal. Great content generates traffic. Um we heard from some advertising experts about uh making advertising relevant and putting the right kind of advertising in people. Um I particularly enjoyed the session where um I learned that IMVU sells hundreds of millions of dollars of gift wrapping? I was amazed. I mean, I just love that. That was my favorite session cuz I learned that IMVU is selling hundreds of millions of dollars of gift wrapping, and some people are charging \$400 per tweet. I mean, that just made my whole day. And then we capped it off, I think, with two, you know, really great investors, great advice. This The advice that you heard from Paul and Michael are I think 180° from what you'd hear in most venture capital panels. I mean, most venture capital panels tell you, "We want proven teams with proven business models with proven business proven technology." And they'll tell you just about everything the the And so, um it's just been a great day. I hope you learned a lot about generating revenue and that you will take this information and not only generate a lot of revenue, change the world. So, thank you very much. Thank you very