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A Bigger Truth About Restaurant Food Delivery

I was listening to Dan Primack's podcast on Pro Rata and he was interviewing Senator Klobucher who is now publicly and vocally speaking out against Uber purchasing Grubhub and has tried to mobilize against this.

Her argument is that if Uber buys Grubhub (which itself once merged with Seamless) it would mean that Uber Eats / Grubhub would control half the market and that with DoorDash the two together would control 90% of the market. I think that's a largely flawed fight to be picking and of all the uses of Senator Klobuchar's I could think of some much more productive fights to be having.

For starters Uber itself has had to lay off 27% of its workforce due to the pandemic and has been severely impacted financially from the crisis with no immediate respite in sight. Its core business was already struggling to become profitable, so having tertiary businesses like food delivery that can deliver needed profits would be welcome to their financial stability. And the market would still have DoorDash and PostMates duking it out as well as the potential that players like Instacart broaden their business one day or Amazon gets into food delivery.

Even more likely is eventual technology disruption where drones deliver foods and make it hard for existing car delivery services to compete. It won't happen right away but I've seen some innovative companies doing exactly this in places like Australia where they are taking a more liberal approach to allowing drone deliveries. Therein lies the advantages of free markets and competition and if we really believed it were that easy to buy off your largest competitor and be a monopolist we'd all be surfing on AOL TimeWarner portals.

But the broader issue that hasn't garnered much press attention is how the restaurant industry itself is being transformed and what tools a modern restaurant will need to compete. What is the Shopify of the restaurant industry? I have some compelling data that suggests it may just become ChowNow.

We know that the restaurant business already operates on thin margins and many struggle to survive. So when delivery services came along many were willing to pay the fee to try and increase business. It was only about 10–15% of their actual total revenue per month so for many it wasn't a battle worth fighting — they just put up with the food delivery company fees. Customers were happy and restaurants focused on their in-store business.

The problem for the restaurants is that the more successful the "aggregators" of customer demand become over time, the less power the restaurants themselves have individually. This will largely be true whether you have 2 strong competitors or 5 because unless a delivery company can make a profit it won't continue to stay in business.

The delivery companies own the customer relationship and can drive traffic to the most profitable restaurants for them. Obviously if you have a great restaurant brand with differentiated food people search for you by name but for many people looking for pizza, sushi, Mexican food, Thai food, whatever, you might go with the choice put in front of you if it's being recommended or delivered more quickly. The delivery companies also own many of the assets like the photography so they can make certain options look much more attractive.

So just like when Groupon came out many small merchants welcomed the uptick in traffic, without owning the customer you lose the most valuable asset — the ability to re-market to your customer base and encourage them to become more loyal and more frequent customers. You lose the ability to up-sell and cross-sell products. And just like with Groupon the small businesses ended up having many unprofitable customers.

At Upfront we always took the approach that we wanted to back startups that enabled merchants to own the customer relationship and to increase profits by becoming excellent at marketing and serving ones most loyal customers.

So several years ago we backed a company called ChowNow that enables restaurants to offer self-service ordering for pick-up or delivery and the restaurant owns all of the customer information and relationship — ChowNow is simply a SaaS enablement product.

The company has done well over the past several year but never really captured the same press mindshare as the food delivery companies because when a company shows up at your house you get to know that brand rather than the tech that enables restaurants.

Covid-19 has changed all of that. Whereas pickup & delivery may have been 10–15% of a restaurant's business before it's currently 100% and when it's your entire business the thought of paying huge commissions to a third-party delivery service becomes much less attractive. So while many restaurants knew they eventually needed to invest in better order management software, many had been putting it off.

But just as many product or apparel companies were happy selling at Amazon, Walmart or Nordstrom in the past and have lately realized the importance of Shopify and serving customers directly — so, too, are restaurants. Enter ChowNow.

What data do I have to make the case?

- ChowNow now has 17,000 restaurants using its SaaS platform for take-out and delivery and is adding more than 2,000 / month right now (and trending up)
- 10 million diners now use the ChowNow ordering platform vs. 24 million for GrubHub, so like Shopify while they built the customer base slowly and with capital efficiency they are now rivaling the bigger players in footprint
- Last year they were serving 50,000 customers / day through their platform and did approximately $500 million in GMV (the value of the orders placed), this year they are on track to do $3 billion (with a B) and expect to end the year at a revenue run rate that may top $100 million (yes, I asked for permission to publish these numbers).

If you want to see a short spot that outlines the importance of the restaurant industry arming itself with better software tools to serve and market to their customers you may enjoy this 60-second video that makes it clear why it matters. It speaks volumes to why we all love our local restauranteurs and want to see them survive …

Or if you want to see the argument laid out clearly by a customer, look no further than Motorino Pizza in NYC who posted this note that appears before you enter their website:

Bevy is Emerging as a Leader in Software for Building Virtual Communities — with $15 million to Prove It

The venture capital world has started firing up a few cylinders again and looking for businesses that it believes will help us all succeed in ways that resonate with new ways of working as we begin to return to work. It's clear things have changed for good and the need for managing remote communities of employees, customers and partners has become ever more important. So it's no surprise that Bevy is announcing a $15 million fund-raising closed in the midst of the WFH era of the Covid-19 pandemic.

In marketing materials founders often refer to their customer base as a "community", but there's a huge gap between having customers and creating a community. The best businesses understand the difference and that communities are the single best advocates for others to buy your products.

When I worked at Salesforce we had "city tours" in which a senior exec on our team would fly to a city in America (eventually globally) and host an event with customers and prospects. Marc Benioff was the master at community building and he knew that it was far better to let his customers stand up and talk about how they were using Salesforce in front of prospects. This had a dual purpose — the customer on stage showing your product turns into an advocate or evangelist while the prospect is far more likely to be persuaded by a customer presentation than a salesperson's pitch.

92% of consumers trust peer recommendations, while only 22% of brands are trusted.

And when communities work best these new advocates form their own support groups to help each other out and work together on initiatives and once they're a "member of the tribe" there's a benefit of attracting other members.

You see it in the consumer world in obvious ways like with CrossFit, Barry's or Peloton. These aren't merely exercise methods — they are communities and tribes. A key goal of the community manager is to help like-minded people within the customer base find each other and find prospects and bind together. Peloton has recently done a big push to get users to add hashtags that they create — this is classic community management.

Community-building is advice I give to nearly every startup team with whom I work. Competitors can leapfrog you on features or outspend you on customer acquisitions but communities are very hard to disrupt. It's what venture capital teams at innovators like First Round Capital and True Ventures realized 15 years ago — they could invest in entrepreneurial communities and the best founders would then bring in new founders. It's no wonder they've both performed so well.

Building a community goes well beyond hosting events. You can think of your event (whether physical or virtual) as the iceberg above the water that is the physical representation of a community event but building a community is so much more about what you do before and after. If SaaStr were a mere annual conference it wouldn't be as valuable as it's become. Jason Lemkin nurtures his community throughout the year.

Years ago I came across a young community builder named Derek Andersen, the founder of Startup Grind. The enthusiasm that Startup Grind members had to meet, to connect, and to build relationships far outpaced the company's ability, financial resources, and available tools to manage those events. I hadn't known Derek before but he knew I was a huge fan of the late Clayton Christensen, the HBS professor and author of the highly influential book, "The Innovator's Dilemma." Ever the community builder, Derek booked Clay to speak at his event but instead of interviewing him he asked me — somebody he knew from afar — to do the interview. I became an advocate for Derek and for Startup Grind, speaking several more times. I connected with Clay Christensen and stayed in touch until he passed. (If you want to watch my interview from 7 years ago it's here or you can read the summary notes I wrote up)

Derek built Startup Grind from 2011 with 20 people in one room for a conference into a global phenomenon with 600 chapters all over the world and more than 2 million members. As he built this organization he realized the limitations of tools that existed to help recruit, nurture and manage communities so he set out to build these tools and capabilities to enable other companies to launch communities more effectively and with fewer resources.

Derek founded Bevy — a platform to allow local communities police and manage themselves through in-person events and meetups.

Bevy launched in 2017 and quickly helped companies like Atlassian, Duolingo, and Salesforce to scale hundreds of monthly in-person meetups and events. Led by my partner Kobie Fuller, we've been a proud investor since the early days and it was exciting to see customers bringing people together IRL via Bevy.

And then came March 2020 and events globally were being cancelled.

In a matter of weeks, most of us went to strict shelter-in-place with no possibility of even seeing family members, much less attending a community event. What happens to an events company when businesses can no longer hold in-person events?

What we all quickly realized in a period where we can't be together physically is that there's still a need for community — possibly even more so. We still want connection with like-minded people around a shared set of passions and challenges. That hasn't changed. But how we do it has totally shifted and while businesses were quick to host online events of all kinds, very few companies had a good sense how to facilitate true community.

Probably many of you have had the experience of 50 people in a Zoom call with no moderation tools, no one in charge, and no sense of how it flows. More often than not people talk over each other or don't talk at all. Maybe we hear from one droning speaker and the rest of us are passively consuming information. It's the opposite of community.

Although a lot of companies are scrambling to create tools and better collaboration on virtual interactions, Bevy has been doing this at scale for years. So within a matter of days post shelter-in-place, Bevy took everything they were already enabling offline and started applying those tools to running remote communities and meetings. In just six weeks, Salesforce has hosted 650 virtual events with nearly 20,000 attendees, and Duolingo hosted 1000 virtual events — just to name a few.

That's because Bevy isn't simply a video-hosting company, it's a platform for managing groups before and after your virtual event as well. So instead of having to use a CRM, and an email platform, a video-hosting tool, a chat function, and a video publishing platform like YouTube, you have one complete solution in one product. Plus, because it's built expressly to scale virtual communities, it doesn't require a bunch of people to run; many of Bevy's customers host hundreds of monthly events with a single in-house manager.

As an investor, it's been incredible to see how quickly the team has optimized its product, but as a long-time colleague and admirer of Derek's, it's not surprising at all. Nor should anyone be surprised that today the company announced its $15 million Series B funding, led by Accel. Ryan Smith, the founder of Qualtrics, also invested and has joined the board of directors.

To an outsider, it might sound crazy that an events business was able to raise funding on the cusp of complete physical isolation. And it would be — but Bevy has never just been about events, it's about community. They've had a huge head-start on the competition and are well-positioned to maintain leadership as we adjust to building community in this new COVID era.

At Upfront, we've put a lot of effort into building in-person community, including our annual Upfront Summit event. This will always be important to us, but we also see tremendous opportunity to expand our virtual community to include friends and colleagues worldwide. You can stay in touch with us at out own Upfront community page via the Bevy platform, where you'll find a few upcoming events (and many more to come in the next weeks and months.)

My Thoughts on the Current Market: on 20-Minute VC

Several years ago I made an appearance in a burgeoning new podcast called "20 Minute VC," which by now needs no introduction. Harry was gracious enough to invite me back so this past week we recorded an episode discussing the current market environment.

Please download the episode here, if for no other reason than to make Harry happy :) but I've also included some quick notes below including a few notes I didn't share in the podcast (and vice versa by the way — if you listen you'll pick up much more than my quick notes below).

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Topics we covered:

B2B Companies

You haven't seen the full extent to how the correction is going to affect you. We discussed why in Q4 you will see large renegotiations of SaaS contracts and increased churn rates. We talked about what startup CEOs should do in these situations and how to think about these renegotiations. Nobody will be immune because in a bull market executives are paid to "innovate" so they sign software contracts and run projects. In a bear market executives are paid to: consolidate the number of contracts and renegotiate prices.

What Do You Need to Prove to Raise an A Round?

Should you focus on growth? If you go more slowly will you die anyways because you haven't shown more traction, more quickly? Harry posed these questions. I pointed out that throughout history building companies has always taken time and we as a market have put an urgency to rush growth rates. It takes time to sell in your software, get it implemented, prove the value, build a business case, gain executive support and then roll it out more broadly. In a market where people aren't just paid to "innovate" but will need to show real economic value, expect gains to come more slowly. Burn through your cash quickly at your peril.

B2C Companies

We talked about how some companies saw an immediate decline in purchasing (for example if you're in travel or hospitality). Other companies have only seen a slight decline and may be expecting demand to return to normalcy later in the year. That may happen. But I doubt it. The reality is that when unemployment sinks in demand is likely to get worse. 22 million filed in just 4 weeks — for comparison there are only 17.6 million people EMPLOYED in California. And only 8.7

million people lost their jobs in the whole of the Great Recession. When the dust settles from the initial joblessness and people have lost savings, don't immediately find new jobs and this weighs on the stock markets, people will inevitably cut personal spending.

Biggest Advice I Give to Portfolio Founders?

We know that marketing dollars have fallen dramatically in Q2 so if you're reliant on that, you have no choice but to act immediately. This is not a 2-month v-shaped correction. Get your costs down, renegotiate your supply contracts and extend your runway. Some people tell you not to waste your time talking with VCs right now. It won't surprise you that I disagree with that. I stand firmly on "Lines, Not Dots" and think that if you want a decision in the Fall, planting seeds right now is sensible. It may take much longer to close deals than you'd like.

Do I Believe VCs Are Really Open for Business?

In a word: Yes. But not all deals are equal. Seed deals, for example, are easier to get funded than a late-stage deal for obvious reasons. A seed deal hasn't already been "priced up" to a range where a new investor might be concerned about the valuation relative to performance. A seed company hasn't ramped up its cost base. A seed deal requires a $2–5 million commitment, which is easier to consummate in a series of Zoom calls than committing $50 million, which calls for some in-person contact. But there are some deals that will get funded even though not necessarily seed:

- If you're in an anointed category that will serve a post Covid-19 world well. Food production and distribution, group collaboration, remote training or education, sensor technology (tracking people movement, temperatures, etc), certain biotech deals.

- If you're a clear "market winner" like Stripe, Robinhood or Airbnb. There are large sums of money to be invested and if investors can get comfortable with "downside protections" they'll still write checks.

Of course I believe the market has slowed down massively. That's not surprising since VCs are going through triage and also waiting for more certainty to return back to the market. I spoke about that more in [this deck that I wrote for the SaaStr conference in early March 2020](#).

How Do I Advise People When Raising Money in a Hard Market?

Be humble. Raise when you can. A strong balance sheet will matter in the years ahead. Optimize for a 1 not a 0 more than exact valuations now. Valuations may have changed and "price discovery" in private markets is harder to determine. Public markets are transparent and resetting mental mindsets is easier because market expectations are very clear. In the private markets it's much harder to know and you'll have VCs who don't want to take "mark downs" so may not immediately encourage you to accept a new reality.

We also discussed what the M&A market looks like now but I'll leave that if you listen to the podcast.

We Talked About VC Reserve Strategies

This is an "inside baseball" topic for VCs. But when a fund writes checks into a portfolio company it typically "reserves" money to invest in future rounds. Every firm has a different reserve policy but reserves are especially difficult for smaller funds. Many solved this problem by writing "SPVs" (special purpose vehicles) to fund their best deals as they scaled. But you can't easily raise an SPV in a downmarket to help bridge a company going through a transition so firms that haven't set aside proper reserves may find themselves wiped out in some deals in a down market. We spent time talking about why "pay-to-play" deals are back on the table and why these deals happen.

The podcast also has a detailed discussion about how we at Upfront think about reserves in terms of:

- The importance of diversity across time (to pick up technology shifts / platform changes and market changes)
- Why we create a portfolio with some diversity on the "J curve" (we do 89% Seed & A, 11% B's. Of our early-stage deals we do 33% Seed, 66% A's)
- Why recycling is important, but why without exits you might even be forced to stop paying management fees for a while

What Will Happen with LPs in this Economic Market?

Harry asked me whether I thought LP "defaults" (not funding the VC commitments it made) would go up. I discussed why I didn't think this would be a widespread problem. What will happen is that some LPs will need to scale back the number of VC managers they have on their roster.

What is the Most Important Role a VC Plays?

1. **Picking great talent**. We are fundamentally in the business of backing exceptional people, and knowing how to find them, judge their skills and future potential and then earn their trust IS the job. We of course need to understand markets and market dynamics but many people understand this from an analytical perspective. Understanding markets AND people (and earning the respect of the most talented people) is much harder.
2. **Knowing the limitations of the founding team.** Every great player from MJ to Kobe to LeBron needs a supporting cast. Our job is to know the strengths of the leaders of the companies we invest in and knowing their weaknesses. We need to be able to show them why complementing their skills with other talented executives and sharing in the power will yield better results. We need to have access to great executive talent and they need to trust us to join the companies we back.

3. **Paying close attention to the psychology of founders.** We need to know when teams need to be left alone to work and know when they need help sorting out problems. We need to spot when a founder is hitting a major stress phase in life or work and be there to help and also know how to get the most out of people through being great mentors.

We Discussed My Biggest Weakness

Being jaded by seeing what "didn't work" and assuming it therefore won't work now. I discussed that extensively in my post about being fooled by your expertise (which is really worth reading). In short, many founders have "naive optimism," which is to say "they don't know what they don't know." So sometimes the fact that they haven't learned what ISN'T possible makes them try anyway and have a blind belief it can be done. We discussed that in the show.

How Do I Encourage Dissent Between Amongst the Partners?

At Upfront we value conviction over consensus. We are looking for a strong opinion, well researched and with strong conviction. We are willing to underwrite deals where a partner has conviction (usually with at least a second supporting it) even if some others disagree. They have to be "down the fairway" for Upfront: a $3–5 million check, 19–22% ownership in a sector we know well. But if they are we don't mind dissent. We actually encourage it.

Do I Think That the Days of Owning 20% as an Investor are Over?

In short: No.

Some founders prefer to spread their investor base across many different VCs in an early round. That's ok. That's a decision every founder gets to make. If that company does incredibly well from start to finish that may work out better for them because they kept stronger control over governance and may have been able to negotiate better personal economics.

But when companies go through tough moments — and let's face it most companies go through tough moments at one time or another — having a strong lead who has long-term conviction in your business can be a large benefit.

So there are different approaches and different kinds of founders. There are also different kinds of VC firms and not all are worth taking that bet on.

Ultimately we look for founders who want to go on a long-term journey with us. So I say that at Upfront we really look for three things:

1. Product-Market Fit
2. Founder-Market Fit
3. Founder-Upfront Fit

I discussed these extensively in the podcast.

Quick Fire Questions:

1. **Favorite Book**: (For the times I recommend: The Accidental Superpower, The Absent Superpower, Disunited Nations, all by Peter Zeihan)
2. **A Great Board Member I Worked With: Rory O'Driscoll:** (did the work, rolled up sleeves, cared, had great humor)
3. **Hardest Thing in My Job?:** It's hard being a VC right now. Not anywhere nearly as hard as being an entrepreneur. But since asked, I covered some reasons why it's tough out there being a VC right now.

4. **Is It Important for a VC to Build a Brand?:** Yes, critical. To win the best deals entrepreneurs need to trust you and want to work with you. Decisions on whom to work with are very emotional and the intangibles of brand plays a big role in the final decision.

5. **What Do I Know Now That I Didn't Know When I Started:** Sometimes it's ok to let a problem simmer, even when I think I know the answer. Let founders work some things out for themselves.

6. **A Recent Company I Invested In**: Solve. A "true crime" video game. Here's a bit more about the company but tune in to the podcast if you want to hear me talk a bit more about why I was so excited to back Tom Wright.

How to Make Sense of the PPP Loan Program for VC-Backed Startups

There is so much confusion and misinformation out there about the government sponsored "payroll protection plan" loans to companies that the heads of every small business CEO in the country must be spinning. We have been advising a lot of entrepreneurs so I thought I'd "open source" some of the advice I have been sharing.

I am not claiming to be the world expert on this. But I have been in close contact with the NVCA, many of the major law firms and many of the major VC firms. Along with my partner Stuart

Lander, who runs operations at Upfront and is a former lawyer, we have scoured through, debated and helped scores of companies make this determination. So my only goal is to give you insights into the conversations we've been having in case you don't have the same access or advice.

I am not a lawyer nor can you use my advice for the basis for your application but I'd rather provide more public information to help you have the right conversations so please take this posting for what it is (and accept that I may have typos or inaccuracies, which I will amend if pointed out).

Am I eligible for the PPP Loan?

If your US-based business is adversely affected by Covid-19 such that you would need to lay off employees imminently and having access to capital would enable you to keep more employees on the payroll then you might be eligible. You need to:

- study the rules,
- make sure that you don't violate the "affiliate rule" (more later),
- consult with your Company Counsel,
- consult with your board and investors and then make your own determination.

If you do apply you must certify that your information and application are true and honest.

Who is this program for and why does it exist?

The CARES (Coronavirus Aid Relief & Economic Security) Act provides $2 trillion to businesses and individuals affective by Covid-19.

$350 billion of this money is dedicated to small businesses under a loan program called the PPP (payroll protection plan). This money is administered by the SBA (small business administration) and is obtained through an approved bank who reviews your application.

The goal of the program is in the name — payroll protection. The US government believes that keeping more workers employed, even if they're not immediately productive due to WFH (work from home) or loss of revenue is better than all of these employees being laid off, where they will likely seek relief via unemployment insurance claims. There were 10 million claims in the past 2 weeks alone, the largest 2-week request in history. The government believes that it not only is better keeping employees in jobs where possible but also in helping these businesses remain solvent.

Am I ineligible since I'm VC-backed?

There is nothing in the rules that state that VC-backed businesses are ineligible. There are certainly some people who are publicly saying that VC-backed businesses shouldn't take government money. There are some business people who think this is ethically wrong for a VC-backed business with a highly-educated founder and there are also likely to be some populist outcries that the money should have been reserved for Main Street workers and not tech workers.

This is a matter of opinion or belief system but not a matter of legislation or policy. The program is designed to keep employees on the payroll so ultimately it's up to you to decide whether you are a worthy recipient and to weigh the benefit to your company and your employees against the potential perception the market may (or may not) have in the future.

One thing that is clear. If you plan to lay off employees and if the PPP Loan will help you to keep more people on your payroll and you ultimately believe that getting through the next couple of months will enable you to productively employ these people on your own dime in the future — this is precisely the policy goal of the US Government. Perception is not equal to policy or legislation. If you want to be perceived well in the future then make sure that your grounds for applying are sound and that you're truly preserving jobs.

If the US Government didn't want to support VC-backed businesses they easily could have excluded them and they knowingly did not.

I am hearing from all of my peers that everybody's applying — shouldn't I?

The short answer is "no." Applying for a government loan that was created to serve US small businesses and employees in the times of an economic crisis is not something you should do just because all of your peers are telling you that you should. It is not "free money." You should apply if your business is in duress, if the loan can help you preserve jobs, if you qualify and if you're supported by your board and your investors.

Do I need to repay the loan?

You might. It depends. Below lists how the loan program is calculated. If you maintain your employment level at your current rate much of this loan can be forgiven but it's likely that a portion of it will not be. If you do massive layoffs (RIFs) you can assume that you will need to repay your loan since the intent of the loan is to protect jobs.

Do I need to rush my application?

One of the most unfortunate aspects of the legislation is that it states that applications will be approved on a first-come, first-served basis. That means that every business who believes it qualifies is rushing in its applications, which doesn't leave much time for reasoned discussions with your relevant stakeholders on whether or not you should and it means that banks and lawyers are being forced to rush things. I get that in a crisis the government needs to act quickly and fix things later. But this FIFO approach has created undue urgency. So sadly you do need to rush things if you want to improve your chances of being approved.

Why is there so much confusion about whether banks accept applications?

Banks have a difficult task. They don't want to hand out loans and later learn they gave money to fraudsters. They have regulations that dictate things like KYC (know your customer) and AML (anti money-laundering) and other regulations designed to avoid abuse of our financial institutions. As a result, many banks are only taking applications from existing customers and in some cases only customers who have existing credit arrangements. Additionally, some Main Street banks aren't able to process VC-backed applications because they are designed to handle individual owned, local businesses.

The two primary banks that service the VC industry are SVB (Silicon Valley Bank) and FRB (First Republic Bank) and both understand the intricacies of VC-backed businesses and are more easily able to assist you.

Everybody is talking about the "Affiliate Rule" — what is that?

Ok. Now things get complicated.

Step 1 is deciding "am I qualified for a loan under the rules" and step 2 is determining whether or not you can validly apply based on something called the "affiliate rule." It's complicated but essentially if a ***SINGLE VC*** can veto certain actions that are approved by the board then you violate the Affiliate Rule (or if a single firm owns > 50%). There is a lot of chatter about companies that own > 20%. This is completely unrelated to the Affiliate Rule. The application form states that any

> 20% owners must disclose certain information in the application process so it often gets confused as being related. It is not. The NVCA (National Venture Capital Association) Guidelines are below.

Am I free and clear as long as no investor owns more than 20% of my company?

No. This is another misconception. The 20% threshold has nothing whatsoever to do with eligibility. It simply determines whether you have to provide additional information.

So to be clear, if a company owns 8% of your company but has negative blocking rights as outlined above in the NVCA guidelines, you are ineligible for the program unless you modify your legal governing documents.

How do I amend my legal documents so that the Affiliate Rule doesn't stop me from applying for a loan?

For starters you will require investor consent to amend your governing documents and since some of these terms were negotiated to protect shareholder rights they may approve the changes and they may not.

I have found that it is easier to get VCs to amend the governing documents when there are several VC investors such that none has the overwhelming majority ownership relative to others. This is because the affiliate rule is only tripped if one single firm has blocking rights. Therefore you can amend the governing documents to a "simple majority of the preferred shareholders" can block one of the known affiliate rules rather than a single firm. I have found VCs to work collaboratively on these to help entrepreneurs in this time of need.

It's slightly harder if you've only done an A-round and therefore have just one VC around the table who owns more than a majority of the preferred stock. In this instance they would need to give up the right entirely. If your company is in dire straits (let's say you're a transportation company or a hospitality company) then you're likely to find an amenable investor. If you're in a company where the investor views your application as more of a "gray area" then you may not easily receive consent for changes.

Finally, there are several discussions about how to "get around" the Affiliate Rule. Please be careful because having a "side agreement" (verbal or written) to "spring back" to the old agreement in the future is tantamount to fraud. You can expressly mention that the governing docs are only valid for the period of the loan but I believe this may open you up to the SBA second guessing the validity of your loan on a "look back basis" (meaning in the future they come back and state that you violated the rules).

If you're going to amend, then amend. If you're playing games — don't apply.

When the $350 billion is fully invested will more be made available?

Nobody knows for sure. There are lots of discussions about the need for more stimulus and the lasting effects of the Coronavirus, etc. Ultimately whether there is a further SBA stimulus will depend on whether it was deemed effective, whether the crisis is longer-lasting and deeper than expected and whether handing more money to small businesses is deemed politically acceptable.

I'm getting so much conflicting advice, whom should I listen to?

Ultimately it is up to you to make the determination if the PPP Loan program is meant for you. You should have a discussion with your legal counsel first. You should discuss with your board second. You should discuss it with your investors third. If you are convinced after this that you are eligible and worthy, then the only remaining thing before applying is to decide how the markets will judge your actions in the future. If you saved jobs, saved your company and are a productive member of our economy and if you feel that this program played an important role in helping you succeed and you didn't have other options that were as immediately able to help — you can at least sleep better at night believing that this SBA Program met its intended goal.

Hard Decisions Require Empathy

In the past two weeks we have entered perhaps to most surreal experience in any of our lives. I think intuitively many of us believe it may be a more lasting impact than just "60 days at home," which is why we almost have a nervous laughter when we call (Zoom!) somebody we haven't spoken to since before the crisis and acknowledge how bizarre we all feel right now. I have seen the insides of more people's homes and apartments than I probably ever have as we're invited into this intimate world of videoconferencing.

Just two weeks into it we are just starting to come to grips with what will no doubt wreak big financial, emotional and obviously dire health consequences and suffering for many.

In our business lives we're having to deal with decisions that could have lasting impacts on our companies without any compass to guide us in the direction we're heading . It feels a bit like choosing a fork in the road amidst dense fog and with nobody to guide us what to do.

In our personal lives we're having to change our routines and figure out how to remain productive — often with other people sharing our homes who have their own ideas of how to use our collective space and time. What do we eat? Where do we shop? What is safe? What are my parents doing — are they being safe? Can I plan a Winter vacation or attend a wedding or travel anywhere again this year?

Who the fuck knows.

But you should know that everybody is in exactly this mind space. That's what makes this so surreal. I find myself struggling to fully relax at bedtime, with my mind spinning about the world that lies ahead and the infinite amount of weekly decisions I'm having to process. I imagine many of you are, too. It goes without saying that if you find yourself in a really negative headspace PLEASE reach out to any trusted mentor, friend or family member. I promise we'll all get through this some way and there's always tomorrow, whatever that holds. I have lost friends who didn't see the light at the end of the tunnel in past economic hardships.

For founders of startups or for executives tasked with making decisions with all of this incomplete information, the moment calls for decisiveness on every front:

- how to deal with customers,
- what to do about expenses,
- what to tell board members / investors,
- what happens with fund raising,
- do I need to lay off employees or deal with a furlough,
- do I qualify for government assistance?

If your head isn't spinning you haven't fully grasped the severity of the situation.

Each of these decisions could be a blog post in its own right but for today I want to avoid tactical advice and offer something more about your temperament as you wade through complexity and deal with decisions that affects the lives and the livelihoods of others. To say it simply ….

Show empathy.

I know that I shouldn't have to say that, as it seems obvious. But in the past two weeks I've heard many cavalier comments about: cuts, renegotiations, changing terms, "the market environment dictates this" or "never waste a good crisis" or "you just need to cut 25% of your staff" because it seems everybody is doing it. I know that many people are just short-handing given stressful times but do try and pause and think about your actions & words and how they will affect others (or whether they're the right actions in the first place).

In the words of my friend and a CEO with whom I work,

> "Yeah, I know I need to make some cuts because our demand has changed, but I want to do this with a scalpel and not with an axe."

He produced a very detailed analysis of his customer base and which would be affected. He enacted a program to proactively offer payment holidays to customers in obviously "hit" industries like travel & entertainment. He showed industries where demand was likely to hold strong and he outlined a case for how he could protect as many jobs as possible. He asked for a few more weeks to gather market signals before enacting change. It was the thoughtful response of an empathetic leader.

The driver of your decisions must be logical, rational and economically sound. You need to consider:

- Has demand for my product fundamentally changed in ways that will persist?
- How long is my cash runway if this demand doesn't recover for the foreseeable future?
- Is there a viable path to raising money / strengthening my balance sheet as one solution?
- If not, how much must a reduce costs to give our company enough runway to weather this current storm?

The inevitable decisions may mean you shed employees, suppliers, offices, bonuses, contractors — you name it. But here is where empathy becomes most critical. It is very easy to want to insulate yourself from feeling the extreme emotions that will come from the loss of a job or for a supplier of yours with the loss of an important customer. Don't insulate yourself — handle things personally and be a leader that is present in times of crisis. And if you have to make these hard decisions, empathy goes a long way.

If you have to let employees go or have to furlough them do it 1–1 or have senior members of your staff divide up employees and do each one 1–1 (or 2–1 if you need to have HR in the room (or "in the Zoom") but my point is that each affected employee deserves a private meeting. And they deserve compassion because whatever stress level you are under, your actions are going to make their stress levels just as bad if not worse.

They don't need to hear you say in an antiseptic way, "Look, we have no choice. It's your job or we all run out of cash." That might be true, but it lacks empathy. It should be something more like, "Sadly we have made a decision that your job is being made redundant. I'm very sorry that this will affect you and I don’t take lightly what a burden it must be to you.” Of course that doesn’t change the outcome, but it’s the humane thing to say.

You can insert you own wording or phrasing but the point is to acknowledge the pain, the cost, the consequence of your actions — even if you had no choice. Let the other person speak. Let them emote. It might be that they have to cry or they might have to yell at you — whatever. This isn’t the time to argue back that you had no choice or that “they weren’t really pulling their weight anyways” or whatever else is playing in your head. This is the moment to let them have their say. It doesn’t change anything. This is a moment to be calm, let others vent and politely move on.

Empathy can also be financial. You need to make sure that you’re making sound economic decisions for your company so I’m not advocating being cavalier about money because ultimately if you run out of cash then everybody loses his or her job and every investor loses his or her money. But at the margin if there are things you can do to be compassionate about severance or medical benefits or helping people navigate government assistance — you should do all that you can. If your company can help with job search, or resume writing or providing references or calling other companies to tell them you did redundancies — you should do it.

The month of March, 2020 has been hard on our country and on the world and the sad reality is that this is still likely just the first act in a long series of heart-breaking stories and circumstances around the world. In times like these your friends, family, associates, colleagues, employees and business partners need you more than ever.

If we know each other personally and you think I can help you please reach out. I promise I will make time.

Funding in the Time of Coronavirus

I am due to speak at the SaaStr conference next week: Wednesday, March 11th at 10:45 AM. I had originally signed up to talk about the “VC Market Trends” overall but it seemed inauthentic to speak about VC funding without addressing the virus in the room. So I wrote a brand new deck outlining some Upfront views on what we may see in the funding markets ahead.

This is a message we have been delivering to our portfolio privately so we figured it made sense to make it more public broadly in case its of any help to others.

No doubt it’s a richer presentation with audio and voiceover so I hope that SaaStr is recording and releasing presentations. But for now you can have view the deck I plan to use below (or click to go to SlideShare if you’d like to download it).

I welcome any feedback. Feel free to open source and use any information you find useful.

Why Meg Whitman is Betting on Quibi as“The Da Vinci Code of Content”

Every year, a personal Upfront Summit highlight is getting to sit down with experts in a field I care about. Sometimes that’s venture capital generally (like last year’s conversation with Reid

Hoffman) and sometimes it's in a space where I've invested (like mobility and city innovation with Bird's Travis VanderZanden, one of our portfolio founders.)

I've spent a lot of my career thinking about digital and online video (with investments in companies like Maker Studios) so for that reason amongst many, I was excited to open the Upfront Summit a few weeks ago by interviewing Meg Whitman about Quibi and the digital media space.

Of course you've probably known of Meg as a business leader for many years, formerly as President and CEO of Hewlett Packard and the CEO of eBay before that, but since late 2018 she has been the CEO of Quibi (joining founder Jeffrey Katzenberg as the first employee). Between the heavy hitters at the helm, the more than $1.4B raised (more on that later), and the A-list names they've signed up for their first batch of content, they've certainly raised a lot of expectations and more than a few opinions. So I was excited for the audience to have the chance to hear from Meg in advance of Quibi's April 6th launch.

I encourage you to watch the entire 30 minute video (below or here) both for insights into Quibi and understanding how a leader like Meg thinks about innovation, but I'll also pull out a few highlights.

Why (and who) she thinks will pay for premium Quibi content

In a world of Netflix, Hulu, HBO, and YouTube, why would a customer choose to pay the $4.99 monthly subscription (or $8 ad free) for Quibi? Meg shared the perspective that Quibi is targeting a different kind of viewing experience (mobile-only video, which she say is only 10% of the viewing for other streaming services and virtually none during the day) and a different kind of content than what exists currently.

They’re primarily thinking about 7 AM — 7 PM mobile viewing of movies, lighter scripted and unscripted programming, and daily news/sports/politics, in the kinds of 10-minute content chunks you can consume on your commute or waiting at the dentist. Hence, her analogy of content like “The Da Vinci Code” which had 464 pages and 105 bite-sized, fully realized chapters. In essence, you’re not intimidated by the size of each episode so you dig in and might just read 8 chapters in a sitting before realizing you read 35 pages. And so it is with video.

(Quibi = “quick bites”). But unlike some of the existing mobile video on YouTube or IGTV which typically costs at most $1-5K/minute to produce, Quibi is focusing on high-quality production value content, spending up to $100K/minute on some programming (in line with typical streaming services like Netflix.)

“We would argue that our movies are world-class movies, just designed entirely for mobile.”

She also spoke about how they’ve seen premium content creators respond creatively to Quibi’s unique portrait — landscape format, and how they’re banking on what could be seen as a constraint to really produce unexpected, innovative content. For example, she spoke about how Steven Spielberg wanted to create a horror-based program that viewers could only watch at midnight. To time-restrict content requires an entirely new platform, one that only Quibi can support to date.

How Quibi is a technology platform first and then a content platform

Being an investor in LA and having seen a decade’s worth of video startup ideas, one of the reasons many video startups fail is because they think they can just distribute content online the way they’ve done it offline for a hundred years, without the innovation of technology. (And of course there are the Silicon Valley video startups who think it's all about the tech and ignore the storytelling.)

Meg spoke about how Quibi first built out the technology platform and only then exposed it to content creators, and how technology is primary to the platform both in content creation as well as how customers will experience the content. That includes things like:

- **Structure** of the "turnstile" content — the content needs to be originally filmed and edited to deliver a seamless portrait and landscape edit, with the sound synced. This is an entirely new way of filming
- **Personalization** — to provide a curated feed new each day, they're not just tagging every piece of content, they're metatagging each frame of content to get viewers what they want, faster
- **Interactivity** — by designing or mobile consumption, they can eventually take advantage of every aspect of the phone including the camera, the touchscreen, the gyroscope, etc.

"There's a long history in Los Angeles and Hollywood of technology enabling new ways to tell stories … We've created a really interesting technology platform that has inspired creators to do things in a completely different way. "

She also spoke about the importance of 5G and why they think Quibi will be a perfect use case for the technology.

Why they raised so much initial funding

As I said in the interview, we at Upfront come from the land of small first rounds of financing. But Quibi has raised $1.4 billion and counting, before they've ever released a piece of content (I jokingly called it a $1 billion seed round). Why?

Meg shared their reasoning that Quibi would face two big challenges. First, given their unique format, they would have no existing library of content. But when you're serving up 10 minute bites of content you can't launch with just four shows. So they felt they needed to invest heavily in creating a breadth of high-quality content from day 1.

Second, no one had ever heard of Quibi, so they felt they needed to spend a lot of money on marketing to build the brand and awareness. If you watched the Oscars recently, you probably saw ads for a few Quibi shows — definitely a big and expensive promotional bet for a "startup".

"We decided that to give ourselves a real fighting chance to make this work, we had to raise enough money to be able to create, at launch, a completely immersive experience."

April's launch will give us a lot more insight into Quibi's big bet but I appreciated having the chance to hear Meg's vision for the service. I hope you'll enjoy the interview as much as I did.

What Did I Learn From the First VC Check I Ever Wrote?

I became a VC 12 years ago in 2007 when the pace of deals was much slower. I had just left Salesforce.com where I was VP, Products, after they had acquired my second startup. As I was trying to figure out the role I wanted to play in the VC world I decided I wanted to focus on businesses that were building deeply technical products to solve problems for business users.

Just as I was getting the swing of things the world shifted beneath my feet and the stock market went into a free fall and venture capital all but shut down for nearly a year. It proved to be fortuitous because it allowed me the time & space I needed to get to know tons of founders and VCs and to hone my craft.

The first check I wrote was just over 10 years ago into a company called Invoca who just announced a new $56 million in funding led by Scott Hilleboe at HIG Growth Partners. I thought this was a good time to reflect on some lessons of the past 10 years.

1. VC is a long-term business

Some businesses are overnight successes but few of them really move immediately up and to the right. Invoca is now doing 10s of millions in recurring revenue and is growing > 75% year-over-year but it took the first 3 years to really build out the technology and acquire our initial enterprise clients. We now serve many large clients like Dish Networks, Dignity Health, and U.S. Bank as well as many startups like Gusto and MakeSpace and innumerable massive clients that weren't on my approved list of clients I could disclose ;) but we partner with Google, Adobe, Salesforce and many others.

At Upfront, our partners have been fortunate enough to be part of 18 companies that have reached north of $1 billion and the average tenure of an investment that exits at this scale is more than 10 years. But like the company Kyriba, where we recently sold our position at above $1 billion, it took time until the revenue exceeded $100 million recurring and then the industry really competed to back this amazing company since it had scale, defensible technology and long-term, committed customers.

2. Ownership Matters

At Upfront we focus our energy on fewer companies where we take meaningful ownership and we continue to invest throughout the lifecycle of the company. We not only have our Series A funds that can write $500k — $15 million first checks but we also have three growth funds. The advantage is that in many of our best deals we now have $50+ million invested so we can really support entrepreneurs as their businesses scale. In the case of Invoca we led both the seed round and the A round and didn't wait for somebody else to come and provide more capital. Accel led the B, Morgan Stanley the C and now HIG the D. We have invested in every round and as a result our ownership has actually gone up over time.

I have to admit that there is a weird dance with LPs until it's time to send them actual cash money. If you invest early and then pull back in the next 3 rounds your multiples on cash invested are much higher than if you keep writing checks. VCs have different views and strategies on this. Some prefer to get in, buy cheap and show a big multiple. At Upfront when we know we have a winning hand we prefer to put more capital to work, which both helps the entrepreneurs succeed and drives more aggregate financial returns for our LPs. An example was that while we were in the seed round at Ring and followed in the A, B, C and D … we were also able to lean into the E round when Jamie really wanted to scale up his funding and the final check was still > 420% IRR!

3. Cash Money

Ultimately VCs are measured on sending cash back to the people who fund us and while our industry has done really well at paper markups, LPs ultimately want to see money.

I mentioned that we sold our position in Kyriba for > $1 billion but when we invested it had virtually no revenue. We followed it all the way up and continued to invest at the same stage as Invoca is today. When we exited our position in Kyriba we were able to return hundreds of millions and returned 2x one entire fund with just that one deal. I know you've never heard of Kyriba and many of you have never heard of Invoca. That's ok, their customers adore them, their revenues speak volumes to this and we're totally fine to back some of the plumbing that makes businesses online work more effectively.

Over the past 2.5 years we have generated $533 million in cash proceeds (more expected by year end) and that has come by having early conviction, following our winners, maintaining ownership and being patient, long-term capital partners.

4. Defensible IP

When I'm asked by newer, younger VC partners for advice on our sector, one of the things I always emphasize is looking for companies who have built defensible intellectual property (IP). Of course everything could be replicated if a massive juggernaut like Amazon or Google wanted to pour all of their resources into it but I'm talking about technology that is hard to replicate, takes years of know-how and once adopted is significantly valuable.

If I use Invoca as an example: we handle tens of millions of phone calls for customers who want to drive sales calls into call centers. Why does that matter? For start, there are many types of businesses that are large or complex "considered purchases" that have higher close rates over the phone than on a web form.

But here's the big "aha." When you think about what makes Google so valuable — it's this. Users type a search query into their search bar and Google knows the "purchase intent" of the customer. If you type "baby stroller" into the search bar they're able to statistically validate whether you're likely to buy more baby products in part based on your search queries and in part based on the websites you visit (your clickstream). What Invoca allows the call center is even more power than that. We allow them to know whether you spent time on their website (or competitor's websites) prior to the call and we allow them in real-time to know much more than the key words of a Google search because in real-time we evaluate the query in the call for the sales rep and use AI to help predict what your needs are or were (after the call). So if you called for a phone upgrade but didn't close we help the phone company retarget you on Facebook or if you called with a product complaint we can feed you into the customer's retention marketing program.

With 10 years of serving some of the largest enterprise customers in the US, our machine learning advantages actually get better with more data and more time and the value of our IP has been growing exponentially. We know that competitors can put "AI" on their websites but in benchmarks they can't come close to us given the volume advantages we've built.

Defensible IP becomes insanely valuable — particularly as you achieve scale.

If you have any interest in hearing a bit about what Invoca does from one of our largest customers, Dish talks in this video about how they increased conversions 15x (no, that's not a typo)

5. Some Teams Create, Others Scale (Some do both)

There is so much focus these days on founders and whether they should always remain in the CEO seat. Of course the media doesn't do nuance well so this is an emotional topic.

What I've learned is that at times you need to have the dialogue with the Founder / CEOs and ask them to be participants in the conversation about whether they're the right person to scale the company (and frankly whether they would enjoy it).

In the case of Invoca it was founded by Jason Spievak who is an amazing innovator and has been part of three very successful businesses that have scaled from startup to enormously valuable. After several years we had a discussion about whether he felt he was the right person to take Invoca to the next level and he reflected over a 6-month period and determined he wasn't. He participated in the process of deciding "what next" and that allowed us to bring in Gregg Johnson as the CEO.

Jason went on to help Apeel Sciences get off the ground, helping the Founder & CEO raise all of his initial VC money and helping him build out the executive team and board. As a result that company is now as valuable as Invoca (last round raised >$70 million) so Jason ended up with two very valuable equity positions and has now raised an early-stage seed fund.

Gregg was a friend and colleague of mine as Salesforce.com where he worked in the group that build products for marketers so he knew this space incredibly well before joining.

Jason was a creator and saw a market opportunity that others didn't. Gregg was built to scale large companies and build the processes and team to enable it.

And my friend and Invoca co-founder Colin Kelley has done both. He built all of the initial technology and telecoms infrastructure required to build a large, enterprise software company but he has remained the CTO of Invoca as we have achieved scale.

Some start, some scale, some can do both. It takes all types and helping people realize their best skills and interests is an incredibly important part of the job.

Summary

In the press we celebrate the "overnight successes" in the tech sector but the reality is that the largest successes were built over longer periods of times and with many ups but also many downs or lateral moves.

The reality is that defensible IP takes years to build, takes large teams of dedicated staff to develop and then market, sell and service clients.

In venture it's very easy to want to chase yesterday's trend by funding what you're reading about in the press but what you're reading about today if you haven't already funded it's likely too late.

As I tell our LPs,

> "if I'm not making you slightly uncomfortable when I'm writing my first check I'm not doing my job. Since my job is to fund things that aren't obvious and other people aren't doing them today — almost be definition you should be scratching your head. I will get some wrong but venture is about the 3 you got very right, not the 7 that didn't go as well as expected."

Congrats to all of the hard working founders, executives and team members at Invoca. It's been such a pleasure watching you grow over the past decade and I'd be thrilled to continue to be a shareholder many more years from now.

Some Seriously Great News. No, Seriously …

Exactly six years ago today I received an email from my friend Ynon Kreiz introducing me to Andrew Stalbow and Petri Järvilehto. Ynon had been the CEO of Maker Studios and I trust his opinion a great deal so of course I took the meeting.

Andrew and Petri had left game developer Rovio (of Angry Birds fame) and were creating a new games company called Seriously that would combine compelling intellectual property (characters), great narratives, and fun game play in a mobile-first application. Their initial release would be a product called "Best Fiends," which is now one of the most successful mobile games.

Our meeting was memorable both because the pitch was compelling but also because it was the first pitch meeting I ever took in our new Santa Monica offices. By "first" I mean — we hadn't even signed a lease, it was a building site, there was nowhere to sit and the building itself looked somewhat dilapidated. But I thought it would be fun to meet on the (someday would become) roof deck with ocean and meet in makeshift environs. I imagined what it would feel like if we worked in this location. It felt pretty, pretty good.

Their vision was “if Disney were going to build a media company today they wouldn’t start by creating films, they would build compelling characters in a mobile game and then create media products and physical goods in support of the game. With mobile we can reach hundreds of millions of players very cheaply and once they fall in love with our characters the stories will be revealed.”

We went on to lead Seriously’s first round of financing and since I’m not a video games expert and we do have a video games expert as a partner at Upfront (Kevin Zhang) — he went on to eventually be the lead partner for Seriously at Upfront. In case you aren’t aware, the video games industry globally is now larger the the global film industry, which is why we have a practice area that funds this sector. The video games industry is worth > $150 billion and mobile gaming is now the largest sector of it.

And while Kevin went on to guide our role on the board at Seriously and deserves 100% of any Upfront credit, Andrew went on to become a dear friend. Not only was his commitment to LA tech enormous but we happened to have kids on the same traveling soccer team where Andrew was the assistant coach! I’m sure he could have done without his VC asking him on the sidelines our latest revenue forecasts :) but we really just kept it personal. Ok, I did occasionally pepper him with questions about Seriously.

Petri built the studio and they developed the majority of game play in Finland, where there are a deep pool of talented video games professionals. We found tremendous value in this idea of a two-city startup with some business leadership / management in one city (LA) and much of the development in another (Helsinki). Essentially we got the best of both worlds and we find ourselves investing in more companies with this model.

I guess by now you have figured out the next chapter in the story. Today the company announced it was acquired by gaming powerhouse Playtika.

It is an understatement to say that I am thrilled for Andrew and Petri who have both been delightful to work with all of these years. They had a vision, executed perfectly and deserve every amount of success they have achieved. They innovated on so many fronts including being one of the first game developers to seriously engage video game influencers on YouTube and well as building world-class video shorts that “aired” inside of the game itself and paid for the production++ by driving increased game engagement.

Oh, and when I asked Andrew how he wanted to celebrate together he said, “I want to grab fish & chips.” How very British. We did just that. :)

I am also thrilled for my partner Kevin. Kevin has been a fantastic investor and board member all of the companies he serves (I know because co-investors always pull me aside to tell me) and it’s wonderful to see a younger partner get their first big win. Congrats, Kevin. We’re proud to call you our partner.

How Much Should You Raise in Your VC Round? And What is a VC Looking at in Your Model?

There’s a quick litmus-test conversation any early-stage VC will have with the founder and it’s one that you should be as prepared for as your elevator pitch. It goes something like this …

VC: “How much money are you raising?”

Founder: “$8–10 million”

VC: “What’s your current burn rate?”

Founder: “$250k / month.”

VC: “So at a constant rate of burn rate you’d be raising enough for 2.5–3 years. Why are you raising so much?”

Founder: “Um. Let me check my plan.”

Usually that’s the point in the meeting where a VC realizes that this meeting isn’t going to go very well.

There are many things a VC is looking for in reviewing your business plan but beyond things the like the quality of revenue, margins, OPEX and CAPEX there’s a really simple rule I call, “Cash In, Cash Out, Milestones Achieved.”

Simply put, a VC wants to evaluate how much cash you're raising and whether this amount is realistic. He or she wants to know how long the money you will raise will last and whether this is long enough to warrant taking a risk on funding you. Finally, the VC wants to know what your progress will look like at the end of this period to know how easy it will be for you to raise your next round.

If you don't have a firm grasp of these concepts and how a VC thinks your meeting is dead.

Cash In

Cash in. It's the amount of money you're raising. A VC is looking for reasonableness. Are you raising an appropriate amount of capital relative to your progress, relative to your team size and relative to your needs?

Of course the VC is looking to have specificity in how you plan to spend the money you're going to raise and plans that show a pie chart that says, "25% on marketing, 30% on technology and R&D, 20% on infrastructure, 25% on G&A" do not get funded. Yes, I see plans this pedestrian.

VCs want you to raise the "appropriate" amount of capital, which I would define as what is reasonable given your progress to date, your resources and your needs for an 18–24 month period. VCs tend not to want to fund founders who raise too much money in a given round also because they know that sometimes having too many resources will lead to founders burning through cash too quickly. Conversely many VCs believe that constraining cash can often lead to increases in creative solutions at a startup.

One entrepreneur refrain I sometimes hear is "We want to raise some extra money for M&A activities." This is a red flag for VCs. A VC wants to know that you have a solid plan to execute a stand-alone business and if you require capital for an acquisition they'd rather evaluate it at the time rather than over-fund you now. It's true that some later-stage private equity firms like to fund "roll ups" (a company that acquires many related companies in it sector), but this is seldom the domain of VCs.

Every VC knows that the amount you raise is often a proxy for your valuation. VCs in early stage round assume that you will likely take 20–25% dilution for your funding round so if you're raising $8–10 million they will assume your expectation is $24 million pre at the low-end of the range ($8m x 4 = $32m post money with $8m capital injected buying 25% of the company) and $40 million pre at the high end ($10m x 5= $50m post money with $10m capital injected buying 20% or $40m pre).

So when you say $8–10m is your goal and you aren't at all thinking about your valuation know that a VC hears "$24–40 million pre-money valuation expectations." Of course there are times where 15% dilution is more appropriate and other times it can be 33% but in a first meeting we're just trying to establish general ranges for reasonableness.

If you've only ever raised $500k, have limited revenue, have 7 people at your company and aren't a serial entrepreneur it's a pretty tall order to imagine going straight to $8–10 million unless your data is very compelling or you've otherwise become "hot." If you've raised $3 million previously, have $250k in monthly recurring revenue and 23 staff an $8–10 million round might be more down the fairway.

One big mistake I see many founders make is asking for an unrealistic amount of money in the fund raise. VCs will quickly qualify themselves out in what might have otherwise been a chance for you to get them to engage in a process. I always advise people to ask for slightly less than they need because if your ask is reasonable and you get multiple firms interested then it's easy to increase round size and valuation later in the process. Every VC wants to fund a deal that seems to have too much demand. Having too little demand leads to bankruptcy.

A VC won't necessarily tell you that they find your months of cash unrealistic, your plans not well formed or your valuation out of range — they're more often likely to tell you, "It's not a great fit for us at the moment. We'd love to see you again when you have a little bit more traction." That's what's called a "soft no."

Annoying, I know. But that's the reality. So it's incumbent on you to know what a smart business plan and use of cash looks like.

Cash Out

Cash out is when you're out of money. In general it is expected that you'll be raising 18–24 month's of cash in a VC fund raising. If you have a shorter runway than that the time you'll have to make enough progress to raise more capital is too short. Assume that you'll need to be raising for 3–6 months prior to closing your next round so the last thing an experienced VC wants is you on the fund-raising trail in 6–9 months. Having a minimum of 18 months runway means you have 12–15 months to make progress before the market will weigh in on your progress.

On the other side, VCs often don't want to see a plan that funds longer than 2 years and seldom do they want to see 3 years. Sometimes I hear entrepreneurs make claims like, "I'm raising extra cash as a cushion" but this usually falls on deaf ears with a VC. They don't want you experimenting for many years on their capital — they'd rather you come back to market in 2 years and they can see what you've accomplished before deciding whether to give you more money. You might not like this — but if you know it's how most VCs think it you will be better prepared for your conversations.

At the top of the post I've attached a simple example graphic of a cash burn down chart that any VC will want to see in spreadsheet or visual form and doing it on your own will help you internally with scenario planning well before you're even fund raising.

In the example I've provided I assume you're raising $5 million by month 4 of your plan. In the normal case you'd be running out of cash after 16 months or just one year after you raise money. I built a "plan b," which in this case just holds burn rate constant at $350k and has you out of cash in month 19, which gives you more runway. In reality this fund-raising plan should take you to month 22, which would be 18 months since you've raised.

[Note: If you enjoy or are learning from this series please subscribe by entering your email below — it saves me from having to spam you too much on Twitter :)]

Milestones Achieved

Assuming a VC has shown interest in your team, your plans, your market and they believe that you're raising an appropriate amount of capital, sooner or later they'll begin thinking about the milestones you would have achieved by the time you're raising your next round of capital or by the time you're out of money.

Most VCs lead one round of financing in your company and are looking for other VCs to lead subsequent rounds. Knowing that it's more likely that an outsider will fund your next round a VC will be thinking the following:

- What will you have accomplished by the next time you go out to raise?
- Will this be enough for another VC to show interest?

- Will these milestones be enough that a VC would pay a higher price in the next round of financing?
- If you're not able to raise from outsiders and I need to lead this round, will you have made enough progress for me to face my partnership and tell them why we should fund an inside round? Will your burn rate be sufficiently low that I won't worry about the amount of capital you'll need in the next round of financing?

VCs want to fund innovations but they are also very cognizant of how much firm risk they can take on given the size of their fund and the number of deals they want to do per fund.

Summary

Raising money is a daunting process. This part of a series to help you raise venture capital — the first post is in that previous link along with the whole outline.

If you know the financial factors that a VC is evaluating: cash in, cash out & milestones, you'll have a much easier time in your VC meetings. In the next post I'll give some advice on how to talk about valuation when a VC asks.

Happy raising.

Of Course #BlackLivesMatter — How Could Anything be LESS Controversial?

Black lives matter. Saying it out loud is obvious. And important.

Agreeing that Black lives matter does not make one anti-police — it simply acknowledges that we understand there is a white privilege in the United States that has existed since our foundation.

Having grown up in the US but having lived in Europe for more than a decade gives me a unique perspective to know this problem is more pronounced in America and we have a responsibility to continue to chip away at the problem.

As a white person I cannot accept that the GOP candidate for office was the leading voice in the United States for the "birther movement," which questioned the citizenship of the president of the United States because his father was from Kenya. If you can't see that and see that we have a racist problem in America that this despicable man won his parties nomination then I think you can't objectively understand the problem.

America in 2016 is no place for "dog whistle" politics and it's time that more people say out loud, "Black Lives Matter" to make sure that the terrible people trying to undermine the movement don't have air cover for continued vitriol, hatred and racism.

It's important to stamp out the overt racism of Sarah Palin (who called Black Lives Matter a farce) ...

It's important to stand up to Texas Lieutenant Governor Dan Patrick (who called black protestors 'hypocrites,' or to take on the very ugly comments by former *congressman* and right-wing radio commentator Joe Walsh.

“Real” America? Doesn’t he just make the point with one Tweet? Is ‘Real’ America white? And Christian? And hetero?

And Black Lives Matters supporters are Punks? “Watch out Obama?” — threatening the president of the United States? Inciting violence? And then CNN had the temerity to put this racist on the air. Since hatred always speaks louder than support — rational people like you and me will be drowned out unless we speak up.

Speaking up is important because even though we haven’t walked in the footsteps of our black friends we can show empathy that we support their frustrations and very real struggles.

How can we as a community not speak up? After Eric Garner? Trayvon Martin? Freddie Gray? Alton Sterling? Philandro Castile?

Black lives matter.

I find the movement to say #AllLivesMatter offensive. Of course all lives matter. It doesn’t even need to be said. Black Lives Matter doesn’t say *ONLY* Black Lives Matter. It doesn’t exclude other people — it calls attention to the unique prejudices black people face in America. And saying “all lives matter” is a direct attack to say that black people can’t unify around their unique problems and grievances.

I see Black Lives Matter as an attempt at: Black unity, creating awareness of the problem and showing the country that there is a problem with how black people are still treated in America. If you take offense to a group trying to call attention to its plight then it’s you who have a problem.

Nowhere is the point made more poignantly than the 47-second video below by Jane Elliot in which she poses the question to the (all white) audience ‘how many people would be happy to be treated how black people are treated in society?’

She asks those who agree to stand and of course nobody stands, to which she rightly says …

“That says very plainly, you know what’s happening, you know you don’t want it for you, I want to know why you’re so willing to accept it or to allow it to happen for others.”

We need to stop hiding behind the ruse that being pro #BlackLivesMatter means you are anti police. You can stand with the police while demanding that they treat our African American citizens better. You can stand with the police while wanting to be sure their leadership feel accountable for the actions of the rank-and-file. That bad behavior won’t be tolerated and will be prosecuted.

Of course Micah Johnson who shot many police officers this week in Dallas killing 5 officers is despicable. Of course his actions weaken the movement of pushing for police reform because it hardens those who already refuse to acknowledge change is needed. Of course it’s unacceptable and terrible and there are police officers to be mourned.

But a demented person who shoots policemen does not change the fact that we need accountability for our police system and our penal system and need to end the double standards in our society that disproportionally affect people of color.

As President Obama cited from years of research at a speech last week:

- African Americans are 30% more likely to be pulled over that Whites

- African Americans & Hispanics 3x more like to be searched after being pulled over
- African Americans are shot by polices > 2x the rate of Whites and arrested 2x the rate of Whites
- African Americans are 75% more likely to be charged with offenses carrying mandatory minimums;
- African Americans received sentences that are 10% longer than comparable arrests for Whites for the exact same same crime
- African Americans & Hispanic make up 30% of population but make up 50% of the incarcerated

And as added by news commentator Fareed Zakaria

- In Maryland 29% of population is African American while 72% of the prison population is African American

Whatever the origins of these disparities it is undeniable to say that we have a problem and one that we all own responsibility for both acknowledging and helping to fix.

Like most of you, this week I watched and I read and I shared and I wept (as I watched the 15-year-old son of Alton Sterling crying for his dad) and I mourned and I boiled and I discussed.

It was a terrible week in America.

The video below knocked me out and is so important for people to watch and understand. It's a StoryCorps video about a young black man, Alex Landau, with a white mom and who is stopped for making an illegal left turn and is beaten senselessly by three members of the Denver police without provocation. He has a gun pulled to his head and he hears, "If he doesn't calm down we're going to have to shoot him."

His passenger, who was white, had weed in his pocket and escaped any violence.

When police officers feel it is ok to beat an unarmed person senselessly without fearing that their colleagues will turn them in — you know you have a systemic problem. If you watch this important video it should turn the stats listed above into an individual human narrative of daily injustice that many people of color face in this county.

Talk to any black person in the US and ask about their experiences with the police. I've never met one who didn't at least have one story. It's not acceptable to live in a country where black families have to coach their children how to behave around the police for fear of being killed. Yes, we should all be respectful of police officers — but this situation clearly goes beyond that.

As a coincidence, even before the recent shootings I had been thinking a lot about race relations in America this past week because I had been watching "OJ Simpson: Made in America" — a 5-part, 7.5-hour documentary about OJ.

It is the story about OJ's life from childhood in the projects, through high school, his time at USC, his storied football career, his abandonment of the black community, the murder, the trial, his spiraling out of control and ultimately his arrest for armed robbery and sentencing to 33 years in jail.

It is some of the most compelling television I have ever watched. It recounts much of my childhood in the US and growing up an OJ fan but it also presciently captures race relations in America and some of the injustices endured over decades and longer.

The documentary covers the LA police killing of Eulia Love who was arguing over her $22 gas bill and armed with a kitchen knife and the police officers weren't punished. They profile the Rodney King beating in which none of the police were initially found guilty. They cover Latasha Harlins, a teenage black woman who was shot in the back of the head and killed by a grocery clerk who received no jail time. They show LA police chief Daryl Gates defending a police chokehold and saying it only killed black people because they had different attributes than "normal" people. The community started calling cop cars, "Black and Normals."

When your police chief talks like this there is no denying you have a problem.

There is no denying the history of racism in our country brought to the surface again both by the recent police killings and by the ugly, dog-whistle presidential campaign of Donald Trump. "Mexicans are rapists. And some, I assume, are good people" or the overt racism of questioning Obama's citizenship or religion.

Many white, heterosexual, high-income men struggle to speak up on social, racial or gender issues for fear of being targeted for insensitivity. I understand this because when I speak up I try to be careful not to represent that I understand the struggles of people of different color, gender or sexual orientation. I try to be sensitive about not making it *my* fight or looking for any special recognition for speaking up.

But saying nothing about intolerance or racism is far worse than risking being misunderstood.

I wrote on the topic of black mistreatment in America 18 months ago after Eric Garner was killed and the officers weren't charged. A (white) friend of mine emailed me that he was "shaking his head when he saw the headline of my post" that was titled, "Why I'm Standing Today with My Black American Friends, Family & Colleagues." He then proceeded to tell me that after reading the post he actually felt relieved that I had covered the topic with humility, compassion and open-mindedness.

But why would a friend of mine even second guess me for speaking up or second guess the title of my post? Why wouldn't we ALL speak up? When I hear my non-Jewish friends showing support and sympathy for anti-semitic attacks I feel heart-felt appreciation for somebody acknowledging that Jews are still marginalized in many places in the world — including America.

When others speak up for me I feel supported.

My father is from South America and I take great offense to Trump vilifying Latinos. I remember my father in tears at one Passover dinner talking about how Latino immigrants are treated in America. He wept for the journey of his friends from Central America coming to the US illegally to escape the violent conditions in that region and saying how much easier he had it arriving legally in the late 1950s.

I feel more supported when people say they won't support trump because they choose country over party. I feel more supported when people stand up to anti-semitism or anti-Latino rhetoric.

So let's not hide behind the fact that we know that of course all lives matter and that without brave policemen we would have no civil society. Of course these things are true and shouldn't have to be said.

That’s not the point. The point is that the black community has a right to demand equal treatment in America by our police, by our legal system and by our penal system.

And they have a right to know that they are supported by white people.

#BlackLivesMatter.

I would also encourage anybody who wants a depiction of the issues facing the urban communities in America including: drugs, race, policing, the education system, longshoremen, politicians and the press — there is no greater show ever created in the US than The Wire. It’s simply a must watch for every American.

Why Misunderstanding Startup Metrics Can Cost You Your Business

There has been a lot of public debate over the past several weeks about whether it’s a good thing to be “gross margin positive” or not and commentary always reminds me that some people at startups don’t quite understand financial metrics or even how to think about which ones are healthy.

When I publicly Tweeted that all companies should be gross margin positive many people pointed out that Amazon wasn't profitable for many years. Gross margin positive != profitable and companies like Amazon who chose to focus on growth > profitability were not losing money on each book sale (ie they were gross margin positive).

The key to being able to run a business that isn't yet profitable (on operating margin) is **availability of capital** to finance losses and preferably at a cost that isn't too punitive to the founders and employees. The reason one would accept losses is when they are investments in fueling faster growth.

There are good reasons why one would raise capital and make investments that lead you to be unprofitable (hiring more sales people in an organization that has found product/market fit or hiring engineering to expand product lines to have more products to sell to existing customers) and bad reasons (having bad unit economics but raising money to "figure it out").

In general I find that raising large amounts of money when you haven't figured it out ends up papering over problems more then helping solve fundamental issues in the business. It's funny how scarcity of capital can focus one's mind.

I've written about the trade-offs between growth and profitability before and if you don't fully grok the topic I suggest you click through to that post.

Perhaps the most misused terms I see these days from entrepreneurs involve CAC (customer acquisition costs) and LTV (life time value) and a lack of understanding these critical components is driving many companies to premature failure.

The tl;dr version is this: Many have been taught to focus on LTV/CAC ratio and if that number is substantively > 1 said entrepreneur feels great. That can be a trap for three primary reasons:

1. Payback period may be long even if LTV/CAC is large, and having a long payback period requires you to be able to raise capital to fund this deficit period. So if you're able to raise easily no problem. If you can't raise — you're dead. End of story. No matter what you were taught about this fucking ratio. So I spend an inordinate amount of time with entrepreneurs focused on payback.

2. LTV is imprecise. In product business it is often measured over multiple purchases and assumptions are made about the repeat rates, and in the enterprise or services world LTV can be based on churn rates, which are notoriously hard to predict in an early-stage business. Poorly calculated LTVs can become BVs (bankruptcy values).

3. CAC is often measured incorrectly and often doesn't capture the true costs of acquisition. And even when calculated correctly often CAC's are assumed to be constant but of course they're not. If you acquire 10 customers a month at $100 per customer and this scales to 100 customers at the same price you may make assumptions about 1,000 customers that don't hold. The reality of CAC is both that when you scale your acquisition "channel," costs usually go up plus when you find a great channel others notice it and drive up the costs as they compete with you in that channel.

So here are some more details ….

CAC

Let me start with the easy stuff and graduate to the punch line in the final section.

The first input is CAC. Customer acquisition cost. This is how much you spend to get a new customer. That bit is easy. In an eCommerce or Internet Services business it is often the marketing costs (if purchased online) and in an enterprise software company it is often marketing plus enterprise sales reps.

The first mistake that mostly only rookies make is to measure the CAC by looking at the attributable marketing costs of acquiring a user. So if you paid $100 for a customer who converted via a Facebook ad or Google search ad (SEM) that is not your CAC.

Let's say you had a budget of $1,000 to spend on Facebook Ads and they cost you $100 each and you got 5 customers. If you had no other spend in your company to acquire the customers then your CAC is $200 / customer, not $100. That's because CAC needs to take into account all of your marketing spend to truly understand how much each customer costs you.

If you're spending $200 to acquire a customer and you want to spend less you can either test out other channels to see whether you can acquire customers more cheaply or you can try to optimize your funnel through your Facebook Ads to convert better. This is often called "funnel optimization."

If you converted one more customer (6 in stead of 5) your CAC just went down to $167.67 ($1,000 / 6). So it might actually be more productive for you to improve your conversion than to improve your ad buying, for example.

But often this doesn't tell the whole story because often companies are also spending money on PR and other marketing activities in order to support the sales process. Generally you should take your full marketing spend including PR divided by your customers acquired to get your "fully loaded CAC."

Of course this is an imprecise science which is why you measure both methods. PR and non programmatic marketing often have a lagging effect so if you ran a big out-of-home marketing campaign that created brand awareness you may find that conversion actually takes place 60–90 days later.

In many senses the KPIs of a business should be driven by the finance / ops team more than the sales & marketing teams because the latter is wont to use the most liberal definitions of CAC to justify spend where the former has to make sure you don't run out of cash. Of course it's a collaborative effort — I'm just saying to involve bean counters in the discussion!

Enterprise software companies also should measure CAC even though it, too, is an imprecise science. SaaS companies need to estimate the amount of sales resources spent on clients (can be measured by activities like visits, sales calls, etc) / the clients who convert to look at sales productivity.

Equally you'll want to measure the total sales costs / clients converted to get a fully loaded sales rep cost / acquisition. And then of course you need to layer in marketing to understand the true SaaS customer acquisition costs.

I'm sure there are way more detailed blogs than this one that can help you with a deep dive on CAC methodologies — my point is the bring the issue to the attention of more early-stage founders who probably aren't developing enough cycles to thinking about metrics.

LTV

The second TLA (three letter acronym) all entrepreneurs are now taught to measure is LTV or "life time value."

In eCommerce it's easy to measure the first time purchase value (AOV, average order value) but that doesn't tell you the "life time" value. To understand that you need to understand repeat purchase rates and of course that is harder to know in a startup company. Estimating your assumptions and testing how cohorts perform over time is critical to perfecting your LTV calculations over time.

In SaaS (or any recurring revenue business) this is also a very difficult task. What you need to figure out is "churn" or the number of customers (and dollar of customers) that leave your business every month. So measuring LTV requires that you look at cohorts of data over time to see how they perform and then make assumptions for the rest of the data set.

The problem with LTV is that many SaaS companies assume customer lifetimes of 5+ years and of course you can't reasonably predict that because it doesn't take into effect technology or competitor disruptions that may have profound impacts on churn or pricing.

One big, beginner's mistake people make in LTV is to measure revenue. The correct way to think about LTV is to measure the profits gained by the customer. The reason is that you're trying to understand whether you're cost effectively acquiring customers.

So in the case above if you are spending $200 to acquire a customer who buys 3 times from you at $100 each time ($300) this may seem like a great idea. But if your profit margin is 50% then you're only making $150 in profits. So you actually lost $50 acquiring that customer. This is a simple example but I promise you as businesses layer on complexity they often make simple accounting mistakes that can lead to disastrous results.

Now. The thing about LTV is that you may rationally make assumptions that would persuade you it's a good idea to lose money on acquiring customers. An example is that you may assume you're going to launch a second product line that you can market to existing customers and if you had strong penetration rates that might layer on profitability.

If your economic case is built on increasing LTV over time or on retaining recurring revenue streams please remember to layer on “re-marketing or retention” costs into your equation. In this case, CAC isn’t sufficient to look at long-term profitability.

I’m guessing much of this was 101 to many readers. You were taught diligently to look at LTV / CAC ratios and somebody told you a magic number (maybe 2 or 3, preferably 4 or 5) that they asserted was the magic number to know whether you had a healthy business. Some even suggestion and LTV/CAC ratio of 1 while you’re growing to capture market share.

But LTV / CAC is just one measure. There is another that is critical and that surprisingly few have paid attention to in the past few years. I have been shouting it from mountaintops to companies I’ve invested in for years.

“Payback Period!!!”

Payback Period

In eCommerce it may be a perfectly reasonable assumption to wait for the second or third purchase to make a profit. In enterprise software it likely makes a ton of sense to sell to customers who don’t churn and who yield recurring revenues for 5 years and hugely positive LTV/CAC ratios.

But none of this matters if you run out of money. Sustaining short-term losses is all predicated on ability to finance the losses through venture capital or other means. The dreaded trade-off between profitability and growth!

What I talk with entrepreneurs I like to focus on:

- What is the fully burdened CAC?
- What are the re-marketing or retention cost assumptions?
- What is the LTV? And …
- What is the payback period?

The payback period is when you have paid off your CAC. I am on the board of some companies with multi-million dollar LTVs calculated over a 7-year period (with proof over time that they do retain these customer) but where the payback is longer than 18 months. This can be a spectacular situation IF there is freely available capital to fund the company at good valuations. That is what finances rapid growth.

But when the venture markets slow down, when capital is less freely available, when prices start to decline — the balance shifts from growth-at-all-costs to profitability. And this isn't theoretical and it isn't just about your company. It's also about how much you pay to acquire customers and how long it takes you to recoup this investment.

I would say that the obsession with LTV/CAC and the laissez-faire attitude to Payback Period is amongst the chief reasons you have a lot of companies that have raised a lot of capital and are now struggling.

In a market less focused on hard metrics, sales growth feels amazing and validating. In a market that discovers sobriety, investors start asking the tougher questions about acquisition costs. In a market where capital is no longer freely available and always increasing prices, people start to focus on payback on spend. And of course ultimately on profitability.

It’s probably worth boning up on these metrics in your business.