Investing in LinkedIn in 2004

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7-9 minutes

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http://mashable.com/2011/05/19/linkedin-founder-ipo/

“That’ll Never Work”

The Best Investments Are Never The Obvious Ones

The best early-stage venture capital investments appear obvious in retrospect, however very few of them are actually obvious when you make them. In fact, we recently reviewed our process at Greylock and discovered that the best investments are non-obvious enough that they result in a mixed vote by our partnership. Such was the case with LinkedIn nine years ago.

The Context of the Investment

In October 2004, when Greylock invested in LinkedIn, it was strange times for the pioneers of what would become social networks.

The signs of Friendster’s decline into irrelevance were already evident. Though it would limp on for a number of years more, Friendster was clearly destined to be a tale like Icarus, not Sir Edmund Hillary. Its investors licked their wounds and those that hadn’t been investors counted themselves lucky, given how white-hot the investment had been. One thing that both groups had in common is that they vowed to learn from history.

MySpace was the new upstart. Founded in August, 2003, MySpace would go on to be the most visited social networking site in the world from 2005 until early 2008. In June 2006, it would pass Google as the most visited website in the United States. But in October, 2004, though growing rapidly, it was still relatively tiny — seeing roughly 5m users per month. Obviously, it too would have an Icarus-like ending, but that’s a different story.

And what of Facebook? Well, it had just been founded in February, 2004 by an unknown kid named Mark Zuckerberg at Harvard. It was called “thefacebook” (onewordalllowercase) and It was a small, closed college network at Harvard, Yale and Stanford with members numbering in the low thousands. In fact, at that time, the next biggest social networking site after MySpace and Friendster was likely Orkut, an internal passion-project launched by Google in January, 2004.

And it was on a Monday in August of that same year that LinkedIn co-founder and CEO, Reid Hoffman, visited Greylock to present to the team. You may think LinkedIn was an obvious investment in 2004. At the time, however, there were legitimate concerns:

- Friendster, MySpace, and Orkut were all massively larger than LinkedIn, which was still approaching its first million registered users.
- LinkedIn projected the ability to build revenue but didn’t have a dollar of revenue and hadn’t proven it.
- Most people were unfamiliar with the concept of professional social networking.

Reid’s Publication of the LinkedIn Series B Deck

With his usual focus on transparency in the interest of helping entrepreneurs, Reid recently published the pitch deck he used at Greylock that day with additional perspective, commentary, and advice. It’s a great read whether you are a founder of a company, thinking about becoming one, or simply a student of innovation and start-up history.

I thought it would be interesting to provide some perspective from our vantage at the time, so I dug out the investment memorandum that I circulated to the partnership prior to Reid’s presentation to complement and summarize my compiled due diligence. What follows are excerpts of the arguments I gave to support Greylock's and my investment thesis in LinkedIn.

- **Mission.** "LinkedIn's mission is to create the leading, business-focused network site for people where they can "find and contact the people they need, through the people they already trust."
- **Business.** "This is inherently a business with strong viral distribution and network effects… And because the whole context of the site is business networking, monetization areas are natural additions to the site, not diversions for users — many of whom at any given time are either looking for jobs, considering looking for jobs, looking to hire people/services/contractors, looking to do sales/BD oriented networking."
- **Path Forward.** "Development in three phases: (1) grow the userbase and establish breakaway network effects and scale of user-base/database … ; (2) focus on improving user value, repeat usage, and habit building through (a) better improvements in UI and ease of use, and (b) by building value-added applications and wizards on the database to improve user-mining of value from the network; (3) monetization of the user/network asset through (a) "Opportunities": …, (b) "InLeads": …, and (c) "Network Plus": …
- **Monetization.** "If the network remains robust, and they succeed in building value and habit, their monetization potential could be a significant portion of the existing Monster.com market as just a first monetization opportunity."
- **Challenge.** "My belief (and theirs) is that they have much work to do cleaning up the UI, and packaging relevant applications and wizards on top of their database to surface high-value, simple results matched to the networking processes that people are trying to mine out of the system. I am focused on making sure they get this right before driving too much into mining the user base for money. There is a significant risk in 'killing the golden goose' before it's fully hatched."
- **Scale.** "One of the hardest/riskiest parts of this type of business is getting scale on building a large, high-quality user base at reasonable cost — and this is almost fully behind them already."
- **People.** "I believe these are our kind of people. Bright, talented, aggressive/competitive, analytical, committed to excellence, hard-working, intellectually honest, and risk-taking."
- **Competition.** In those days, Linkedin was one of a bunch of early business-networking startups such as Plaxo, Spoke, Ryze, Zero Degrees, etc. All of these companies were relatively small, though a number were larger than Linkedin.
- **Summary.** "I am very enthusiastic about this opportunity. I think they are well on the way to being impossible to catch in their space from network development, and they have the potential to build a much more addictive experience on top of that userbase, and to monetize it in ways that are relatively non-jarring to their users, and with large revenues and margin potential. I also think Reid is world-class in this type of business and am excited to work with him."

Some Last Reflections

Re-reading our memo, I noticed that I didn't even use the words "social network." This was still a relatively new concept overall, and certainly not one yet applied to business networks.

With 900 thousand users, I was bold enough (crazy enough?) to assume that the hard work of getting to scale may have been behind them. Clearly the ensuing 9 years showed that they had plenty of hard work left to build a dominant platform for business users. Did I also mention that we are all ex-entrepreneurs and operators that are prone to optimism and falling in love with our companies and founders?

And finally, most importantly, though extremely enthusiastic about Reid, I still managed to underestimate the remarkable company-builder, innovator and person that I have been privileged to work with, first at LinkedIn, and now at Greylock as well.

The rise of Linkedin has been well documented, but it's still easy to underestimate on paper Reid's ceaseless determination and focus on the first two points made above: grow the user base, and increase value to our users. And his obsession with building a truly world-class team for every phase of the journey, punctuated by his lack of ego in finding the right long-term partner for the business in Jeff Weiner, remain an unparalleled lesson for me.

If you haven't already, please do take the time to Reid's pitch deck and commentary. It's a rare treat from a rare person.