FORETHOUGHT

The Top Ten Lies of Entrepreneurs

by Guy Kawasaki

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advice

The Top Ten Lies of Entrepreneurs

It's easy to turn off prospective investors. Just feed them the same old lines.

by Guy Kawasaki

ILLUSTRATION: EYEWIRE

For a few months, I've had a constant ringing in my right ear. The condition is called tinnitus, and my doctors say that it can be caused by an ear infection, too much salt in one's diet, a stressful lifestyle, or even a neuroma.

I have a different theory. I think that listening to the lies, exaggerations, and wishful thinking of entrepreneurs has caused the ringing. You see, I'm in the business of helping entrepreneurs raise venture capital, and I listen to hundreds of pitches every year. I hear the same fabrications and delusions over and over again. So, as a public service, I am now going to disclose the top ten lies told by entrepreneurs – and what investors say to themselves when they hear them. I'm not expecting to cure entrepreneurs of lying (fat chance), but I hope I'll at least encourage them to be a little more creative. And I may just save the hearing of a few VCs.

1. ENTREPRENEUR:

"Our projections are conservative."

INVESTOR:

"Multiply this forecast by .1 and add five years."

God bless the entrepreneur who forecasts sales greater than Exodus, JDS Uniphase, and Cisco and then states that the forecasts are conservative. Nobody believes the financial forecasts – investors simply want to see that the entrepreneur understands the industry, the logic involved in putting together a reasonable financial model, and how companies grow. If every man, woman, and child needs to buy two WAP phones for a company to reach profitability, something is wrong.

2. ENTREPRENEUR:

"IDC (or Jupiter or Yankee Group or Gartner Group) forecasts that our market will be $50 billion by 2003."

INVESTOR:

"This is the fifth $50 billion market I've heard about today."

When every plan makes the same grandiose claims about market size, investors have a hard time taking the projections seriously. Instead of trying to prove that the market will be big, enable investors to fantasize about its size. Give them the facts and the context they need to understand the scale of the opportunity for themselves. For example, if you can demonstrate that every corporate Web site on the planet needs your company's product, an investor can figure out that the opportunity is big.

3. Entrepreneur:

"Amazon will sign our deal next week."

Investor:

"Call me when you get Bezos's signature."

Few new economy companies ever definitively say no to any alliance, partnership, or offer. They're all afraid of missing the Next Big Thing. Instead, everyone says, "You have an interesting idea. We'll get back to you about it," and then they don't. Unfortunately, the entrepreneur hears, "Yes, we're doing it." Never talk about a Big Deal until it's a Signed Deal.

4. Entrepreneur:

"Key employees are set to join us as soon as we get funded."

Investor:

"Give me their phone numbers so I can verify this story."

There's no chicken-and-egg problem here. The order is clear: you get the human capital, you get the venture capital. If an entrepreneur can't persuade key execs to join because of the opportunity, she probably can't entice them with big salaries. Indeed, one of the litmus tests of fundability and entrepreneurial skill is the ability to attract talent without money.

5. Entrepreneur:

"We have no competition."

Investor:

"Either there's no market or you don't know how to use a search engine."

To this day, investors get business plans for on-line bookstores claiming a first-mover advantage. If an idea is good, five companies are already working on it. If an idea is great, ten companies are working on it. Claiming that there is no competition to an investor who's heard a similar pitch five times in the last six months is like screaming, "I am a bozo!" Bozos don't get funded.

6. Entrepreneur:

"We need you to sign a nondisclosure agreement."

Investor:

"You're clueless: no one signs a nondisclosure agreement."

Investors won't sign your nondisclosure agreement because they usually see several similar plans: what if they sign one company's nondisclosure agreement and fund another? In reality, the ability to implement an idea, not the ability to keep it a secret, is the key to a successful start-up. Investors don't fund treasure maps; they fund teams that can get the job done. If an investor is willing to sign a nondisclosure agreement, an entrepreneur might not want his money.

7. Entrepreneur:

"Cisco (or Oracle or HP or Sun) is too slow to be a threat."

Investor:

"If arrogance were venture capital, your deal would be oversubscribed."

These companies didn't get where they are by being big, dumb, and slow. I love Clayton Christensen's *Innovator's Dilemma* as much as anyone, but funding the next curve is a scary proposition. It's even scarier when an entrepreneur dismisses the current curve's gorillas. Show a healthy respect for the incumbents while demonstrating a compelling and believable way to compete with them.

8. Entrepreneur:

"We're glad the bubble has burst."

Investor:

"We are, too, because your valuation just dropped 50%."

Let's be honest: no one is glad the bubble has burst. For entrepreneurs, it's harder to get funded, valuations are lower, and due diligence takes longer. For investors, portfolios are worth a lot less (and the lockup period isn't over), and the employees of portfolio companies are quitting because their stock options are under water. Since the bubble burst, everyone has been trying to spin a silver lining, but the sun shines brighter and birds sing sweeter when Nasdaq is at 5,000.

9. Entrepreneur:

"Our patents make our business defensible."

Investor:

"Hire more engineers, not patent attorneys."

Unless you're a biotech or medical-device company, it's hard to support this claim. If an idea is worth copying, there's a will and a way to get around the patent. File all the patents you like, but investors believe that what makes a company defensible is the ability to out-implement, not out-litigate.

10. Entrepreneur:

"All we have to do is get 1% of the market."

Investor:

"I want to fund a company that will get 99% of the market."

I call this the "Chinese soda syndrome": if just 1% of the people in China drink a company's soda, it will sell a ton of soda. The problem is that getting 1% of the Chinese to drink the company's soda isn't so easy. Another problem is that no one wants to invest in a company that aspires to grab only 1% of the market. (It's every investor's dream to learn that his company is on the radar screen of the Justice Department's Antitrust Division.) Shooting for the top-dog position is much more attractive to an investor than claiming it will take only a miniscule market share to succeed.

So if you're an entrepreneur, do me a favor and don't repeat any of these whoppers in my presence. If you pitch me and I turn my bad ear toward you, I'm trying to tell you something.

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