Lecture 9: How to Raise Money

Marc Andreessen

Sam Altman: I would like to start with a question for Marc and Ron, which is by far the number one question we are going to be looking at today, what made you decide to invest in a founder company?

Ron Conway: Well we have a slide on that-

Sam Altman: Marc can start while we get that up.

Ron Conway: So what makes us invest in a company is based on a whole bunch of characteristics. I have been doing this since 1994, right before Marc got out of the University of Illinois, so SV Angel and its entities have invested in over 700 companies. To invest in 700 companies that means we have physically talked to thousands of entrepreneurs and there is a whole bunch of things that just go through my head when I meet an entrepreneur. I am just going to talk about what some of those are.

Literally while you are talking to me in the first minute I am saying “Is this person a leader?” “Is this person rightful, focused, and obsessed by the product?” I am hoping—because usually the first question I ask is "What inspired you to create this product?"—I’m hoping that it’s based on a personal problem that that founder had and this product is the solution to that personal problem. Then I am looking for communication skills, because if you are going to be a leader and hire a team, assuming your product is successful, you have to be a really good communicator and you have to be a born leader. Now some of that you may have to learn those traits of leadership but you better take charge and be able to be a leader. I’ll switch back to the slide, but let's let Marc.

Marc Andreessen: Yeah, I agree with all of that. There is a lot of detail to this question that we can talk about. And we may be a little different than Ron, well we are different than Ron, in that we invest in across stages. We invest in the seed stage, the venture stage, growth stage. And then we invest in a variety of business models: consumer, enterprise, and a bunch of other variations. There are a bunch of fine grained answers that we could get into if there are specific questions.

Two general concepts I would share: one is the venture capital business is one hundred percent a game of outliers, it is extreme outliers. So the conventional statistics are in the order of four thousand venture fundable companies a year that want to raise venture capital. About two hundred of those will get funded by what is considered a top tier VC. About fifteen of those will, someday, get to a hundred million dollars in revenue. And those fifteen, for that year, will generate something on the order of 97% of the returns for the entire category of venture capital in that year. So venture capital is such an extreme feast or famine business. You are either in one of the fifteen or you’re not. Or you are in one of the two hundred, or you are not. And so the big thing that we're looking for, no matter which sort of particular criteria we talked about, they all have the characteristics that you are looking for the extreme outlier.

The other thing I would highlight that we think about a lot internally, we have this concept, invest in strength versus lack of weakness. And at first that is obvious, but it’s actually fairly subtle. Which is sort of the default way to do venture capital is to check boxes. So really good founder, really good idea, really good products, really good initial customers. Check, check, check, check. Okay this is reasonable, I’ll put money in it. What you find with those sort of checkbox deals, and they get done all the time, but what you find is that they often don’t have something that really makes them really remarkable and special. They don’t have an extreme strength that makes them an outlier.

On the other side of that, the companies that have the really extreme strengths often have serious flaws. So one of the cautionary lessons of venture capital is, if you don’t invest in the bases with serious flaws, you don't invest in most of the big winners. And we can go through example after example after example of that. But that would have ruled out almost all the big winners over time. So what we aspire to do is to invest in the startups that have a really extreme strength. Along an important dimension, that we would be willing to tolerate certain weaknesses.

Ron Conway: Okay, I don’t want to over dwell on the slide, but when you first meet an investor, you’ve got to be able to say in one compelling sentence that you should practice like crazy, what your product does so that the investor that you are talking to can immediately picture the product in their own mind. Probably twenty-five percent of the entrepreneurs I talk to today, still after the first sentence, I don’t understand what they do, and as I get older and less patient I say “Backup, I don’t even know what you do yet.” So try and get that perfect. And then I want to skip to the second column. You have to be decisive, the only way to make progress is to make decisions. Procrastination is the devil in startups. So no matter what you do you got to keep that ship moving. If it's decisions to hire, decisions to fire, you got to make those quickly. All about building a great team. Once you have a great product then it’s all about execution and building a great team.

Sam Altman: Parker, could you talk about your seed round and how that went and what you should have done differently for raising money?

Parker Conrad: Sure, actually my seed round, most of the stuff with my current company felt like, from a fundraising perspective, felt like it came together relatively quickly. But actually, one of the experiences I had, I started a company before this that I was at for six years, and my co-founder and I pitched almost every VC firm in Silicon Valley. We literally went to sixty different firms and they all told us no. And we were constantly trying to figure out how should we adjust our pitch? How should we do the slides differently? How do we tweak the story? That sort of thing. At one point there was this key insight that someone gave me when I was pitching at Khosla Ventures and this VC said “Guys," he was looking for some very particular kind of analysis that we did not have on hand, he was like “Guys, you don’t get it.” He was like, “You know if you guys were the Twitter guys, you guys could come in and just be like blublublubluh and put whatever up here and we would invest in you. But you guys aren’t the Twitter guys so you need to make this real easy and have all this stuff ready for us,” and all this kind of stuff.

And I took the exactly opposite lesson of what he wanted me to take away from that which was: geez I should really just figure out how to be the Twitter guys and that's the way to do this. So actually one of the reasons I started my current company or one of the things that I found really attractive about Zenefits is, as I was thinking about it, it seemed like a business. I was so frustrated from this experience of having tried for two years to raise money from VCs and I sort of decided, to hell with it. You cannot count on there being capital available to you. This business that I started seemed like one that maybe I could do without raising money at all. There might be a path to kind of, there’s enough cash flow it seemed compelling enough that I could do that.

It turns out that those are exactly the kinds of businesses that investors love to invest in and it made it incredibly easy. So I actually think it seems very kind and I said I was an expert for you guys. I don't actually think I am very good at fundraising. It is probably something that I am less good at than other parts of my job. But I think that if you can build the business where everything is moving in the right direction, if you could be like the Twitter guys, like nothing else matters, and if you can’t be like the Twitter guys, then it is very hard for anything else to make a difference for things to come together for you.

Ron Conway: Why did that VC say to be like the Twitter guys when the fail whale dominated that site for two years?

Marc Andreessen: Because it worked.

Ron Conway: The other point I want to make is, bootstrap for as long as you can. I met with one of the best founders in tech who’s starting a new company and I said to her “Well, when are you going to raise money?” "I might not," and I go, "That is awesome." Never forget the bootstrap.

Marc Andreessen: So I was actually going to close on this, but I’m just going to accelerate it. Parker, I think, gave you the most important thing you will ever hear. Which is also what I was going to say. So the number one piece of advice that I have ever read and that I tell people on these kind of topics is always from the comedian Steve Martin, who I think is an absolute genius, wrote a great book on the start of his career, which obviously was very successful. The book is called “Born standing up”, it's a short little book and it describes how he became Steve Martin. And the part of the book is, he says what is the key to success? The key to success is be so good they can't ignore you.

So in a sense, we are going to have this whole conversation and I am sure we will keep having it, but it is beside the point, because if you do as Parker has done and you build a business that is going to be a gigantic success then investors are throwing money at you. And if you come in with a theory and a plan and no data and you are just one of the next thousand, it's going to be far, far harder to raise money. So that is the positive way to put it, is to be so good they can’t ignore you. You are almost always better off making your business better than you are making your pitch better.

The other thing, that's the positive way to look at it, the negative way or the cautionary lesson is that, and this gets me in trouble every single time I say it, but I am on a ton of flu medications so I am going to go ahead and just let it rip, raising venture capital is the easiest thing a startup founder is ever going to do. As compared to recruiting engineers, recruiting engineer number twenty. It’s far harder than raising venture capital. Selling to large enterprise is harder, getting viral growth going on a consumer business is harder, getting advertising revenue is harder. Almost everything you'll ever do is harder than raising venture capital. So I think Parker is exactly right, if you get in the situation where raising the money is hard, it's probably not hard compared to all the other stuff that is about to follow. It is very important to bear that in mind. It’s often said that raising money is not actually a success, it's not actually a milestone for a company and I think that is true. And I think that is the underlying reason, it puts you in a position to do all the other harder things.

Sam Altman: Related to that. What do you guys wish founders did differently when raising money? And specifically, Marc, you mentioned this relationship between money and funding?

Marc Andreeseen: I think the single biggest thing that people are just missing and I think it’s all of our faults, we are all not talking about it enough, but I think the single biggest thing entrepreneurs are missing both on fundraising and how they run their companies is the relationship between risk and cash. So the relationship between risk and raising cash, and then the relationship between risk and spending cash. So I have always been a fan of something that Andy Rachleff taught me years ago, which he calls the onion theory of risk. Which basically is, you can think about a startup like on day one, as having every conceivable kind of risk and you can basically make a list of the risks. So you’ve got founding team risks, are the founders going to be able to work together; then you have product risk, can you build the product; you will have technical risk, maybe you need a machine learning breakthrough or something. Are you going to have something to make it work, or are you going to be able to do that? You will have launch risk, will the launch go well; you will have market acceptance risk, you will have revenue risk. A big risk you get into with a lot of businesses that have a sales force, is that can you actually sell the product for enough money to actually pay for the cost of sales? So you have cost of sales risk. If you are a consumer product, you have viral growth risk. So a startup at the very beginning is just this long list of risks, right, and the way I always think about running a startup is also how I think about raising money. Which is a process of peeling away layers of risk as you go.

So you raise seed money in order to peel away the first two or three risks, the founding team risk, the product risk, maybe the initial watch risk. You raise the A round to peel away the next level of product risk, maybe you peel away some of the recruiting risk because you get your full engineering team built. Maybe you peel away some of your customer risk because you get your first five customers. So basically the way to think about it is, you are peeling away risk as you go, you are peeling away your risk by achieving milestones. And as you achieve milestones, you are both making progress in your business and you are justifying raising more capital. Right?

So you come in and pitch to someone like us. And you say you are raising a B round. And the best way to do that with us is to say I raised a seed round, I achieved these milestones. I eliminated these risks. I raised the A round. I achieved these milestones. I eliminated these risks. Now I am raising a B round. Here are my milestones, here are my risks, and by the time I raise go to raise a C round here is the state I will be in. And then you calibrate the amount of money you raise and spend to the risks that you are pulling out of the business. And I go through all this, in a sense that sounds obvious, but I go through this because it is a systematic way to think about how the money gets raised and deployed. As compared so much of what's happening these days which is “Oh my god, let me raise as much money as I can, let me go build the fancy offices, let me go hire as many people as I can.” And just kind of hope for the best.

Ron Conway: I’m going to be tactical. For sure don't ask people to sign an NDA. We rarely get asked any more because most founders have figured out that if you ask someone for a NDA at the front end of the relationship you are basically saying, I don't trust you. So the relationship between investors and founders involves lots of trust. The biggest mistake I see by far is not getting things in writing. You know, my advice on the fundraising process is do it as quickly and efficiently as you possibly can. Don't obsess over it. For some reason, founders get their ego involved in fundraising where it is a personal victory. It is the tiniest step on the way as Marc said. And it's the most fundamental. Hurry up and get it over with.

But in the process, when somebody makes the commitment to you, you get in your car, and you type an email to them that confirms what they just said to you. Because a lot of investors have very short memories and they forget that they were going to finance you, that they were going to finance or they forget what the valuation was, that they were going to find a co-investor. You can get rid of all that controversy just by putting it in writing and when they try and get out of it you just resend the email and say excuse me. And hopefully they have replied to that email anyways so get it in writing. In meetings take notes and follow up on what’s important.

Sam Altman: I want to talk a little more about tactics here. Just how does the process go? Can people email you directly or do they need to get an introduction? And how many meetings does it take to make a decision? How do you figure out what the right terms are? When can a founder ask you for a check?

Marc Andreessen: That was six questions. It was a lot of things. Why don't you describe, you will describe seed then I will describe-

Ron Conway: Yeah so, SV Angel invests in seed stage startups, so we like to be the very first investor. We normally invest today at around the million to two million. It used to only be a million. So if we invest two hundred and fifty k, that means there’s five or six other investors in that syndicate. SV Angel has now a staff of thirteen people. I do no due diligence anymore, I am not a picker anymore. I just help on major projects for the portfolio companies that are starting to mature. But we have a whole team that processes. We, at SV Angel, end up investing in one company for every thirty that we look at, and we end up investing at about one a week.

I think what’s interesting is, we don't really take anything over the transome. Our network is so huge now that we basically just take leads from our own network. We evaluate the opportunity, which means you have to send in a really great short executive summary and if we like that, we actually vote, although I am not in this meeting anymore, but the group actually takes a vote on do we make this phone call. That's how important time is in this process. And if enough of the team at SV thinks it's interesting then they appoint a person to make a phone call to that founder. Usually somebody on our team that has domain experience. If the phone call goes well, bingo! We want to meet you. If SV Angel asks you for a meeting, we are well on our way to investing. If that meeting goes well, we’ll do some background checks, back door background checks, get a good feeling about the company, the market that they are going after and then make the commitment to invest. And then start helping get other value-add investors to be part of the syndicate. Because if we are going to have an equal workload we want the other investors in this company to be great angel investors as well.

Marc Andreessen: Okay, so I will talk a little about the venture stage, the Series A stage. I think it’s fair to say at this point, the top tier venture capitalists only invest in two kinds of companies at the Series A stage. One is if they have previously raised a seed round. So it's almost always the case when we are doing a Series A investment for the company when the company has a million or two million in seed financing, from Ron and the folks that he likes to work with. Almost always Ron, just to be clear and folks he likes to work with. So if you are going Series A, the first thing you to do is to raise seed, that is generally the way the progression works at this point. Every once in a while we will go straight to a company that hasn’t raised a seed round. Really the only times when that happens is when it is a founder who has been a successful founder in the past and is almost certainly somebody we have worked with in the past.

So actually, we have not announced, but we just did one of these we will announce in a few weeks where it was a founder, I was an Angel investor, actually I think Ron was also in the company in 2006. Then the company did it's thing and ultimately was acquired by another big company. And now that team is now starting new things. So in that case we are just going to jump it straight to an A. Because they are so well known and they have a plan all lined up for it. That's the exception, it’s almost always preceded by a seed round. The other thing is, I mentioned this already, but we get similar to what Ron said, about two thousand referrals a year through our referral network. A very large percentage of those are referrals through the seed investors. So by far the best way to get the introductions to the A stage venture firms is to work through the seed investors. Or work through something like Y Combinator.

Sam Altman: Speaking of terms. What term should founders care most about? And how should founders negotiate?

Parker Conrad: Probably precisely because of what Marc said, the most important thing at the seed stage is picking the right seed investors because they are going to lay the foundation for future fundraising events. They’re going to make the right introductions, and I think there is an enormous difference in the quality of an introduction. So if you can get a really good introduction from an someone that the venture capitalist really trusts and respects, the likelihood that that is going to go well is so much higher than a lukewarm introduction from someone they don't know as well. So the seed stage, probably the best thing you can do is find the right investors and then-

Sam Altman: How does the founder know who the right investors are?

Parker Conrad: Well, I think it’s really hard. I think one of the best ways, and not to give a plug to YC, is YC does a very good job at telling you who they think those people are. And can really direct you towards, and I actually found it to be pretty accurate in terms of who you guys have said were going to be the best people, they ended up being the most helpful as we were raising subsequent rounds that provided the best introductions. The people who I thought seemed okay, but were not as highly rated by YC that ended up being the case that they were real duds in the seed round.

Sam Altman: Someday we are going to publish some of these people-

Parker Conrad: Oh gosh there are going to be a lot of upset people if you do.

Sam Altman: So how do you think about negotiation? How do you figure out what the right evaluation of their company should be, what are the terms?

Parker Conrad: Well when I was starting out, I was raising my seed round and I didn’t really know. I mean, we had conversations about this. I probably started a little too high on the valuation side. As you guys know, Y Combinator starts this thing called Demo Day. You get all these sort of investors at once who are looking at the company. I started out trying to raise money for a twelve or fifteen million dollar cap. Which is not quite the same thing as a valuation but roughly the equivalent. And everyone thought that was crazy, you know, that's completely nuts. You are too big for your britches, that completely just wouldn't work. So I started working it down a little bit. Within the space of a couple days I decided I was going to raise at nine, and for some reason that hit some magical threshold on the seed stage that it was below ten that it seemed that there was almost infinite demand for the round at a nine million cap. So no one would pay twelve but at a nine million dollar cap it felt like I could have raised ten million dollars. And the round came together in roughly about a week at that point, once I hit that threshold.

There seemed to be, and they fluctuate over time, these thresholds particularly for seed stage companies that investors think that above this level is crazy, it doesn’t matter. And there is a rough kind of range that people are willing to pay. You just have to figure out what that is. Just get the money that you need, don't raise any more than you need. And just get it done. At the end of the day, whether you raise a twelve, a nine, or a six, it's not a huge deal for the rest of the company.

Sam Altman: Is there a maximum in the company that you think founders should sell in their seed round, their A round? Beyond what Paul was talking about.

Parker Conrad: I don't know the rules on this stuff. The tricky thing is, it seems like they are particularly rough for a Series A. You are probably going to sell somewhere between twenty to thirty percent of the company. Below, venture capitalist tend to be a lot more ownership focused than price focused. So you might find that it's actually, when companies raise really big rounds it is because the investors says, "Hey listen, I am not going to go below twenty percent ownership but I will pay more for it." Above thirty percent, probably weird things happen with the cap table, like it gets hard, you know, down the line for there to be a firm on the cap table for everyone. Everything seems to come in in that range, so that probably just is what it is. In most cases, in the seed stage from what I have heard, there doesn’t seem to be any magic to it, but it seems ten to fifteen percent is what people say, but that is mostly just what I have heard.

Ron Conway: I agree with all of that. I think it is important to get the process over with. But I think it is important for the founder to say to themselves in the beginning, at what point does my ownership start to demotivate me? Because if there is a forty percent dilution in an Angel round, I have actually said to the founder, do you realize you have already doomed yourself? You are going to own less than five percent of this company if you are a normal company. And so these guidelines are important. The ten to fifteen percent is because if you keep giving away more than that there is not enough left for you and the team. You are the ones doing all the work.

Marc Andreessen: We'll actually, we'll walk. We have seen a series of interesting companies in the last five years that, where we just walk, we won't bid simply on the basis that their cap table is already destroyed. Outside investors already own too much. There is a company we really wanted to invest in, but the outside investors already owned eighty percent of it when we talked to them. And it was a relatively young company, they just had done two early rounds that sold too much of the company. Literally, we were worried, and accurately so, it was going to be demotivating for the team to have that structure.

Sam Altman: One more question before we open up for the audience to ask questions. For Ron and for Marc. Could you both tell a story about the most successful investment you ever made and how that came to happen?

Parker Conrad: Other than Zenefits.

Ron Conway: For me clearly, it was the investment in Google in 1999. And we got a googol return out of it. Funny enough, I meet Google through a Stanford professor David Cheriton, who is in the school of engineering and he is still here. He was actually an angel investor in Google and an investor in our fund. Kind of the quid pro quo we have with our investors in the fund is you have to tell us about any interesting companies that you see. We loved it that David Cheriton was an investor in our fund because he had access to the computer science departments deal flow. And we were at this party at Vivek Wadhwa's house in full tuxedo, I hate tuxedos, does anyone here know David Cheriton? Because you know for sure he does not like tuxedos and he was in a tuxedo. But I went up to him and we complained about our attire. Then I said, hey what's happening at Stanford? And he said, well there is this project called backrub, and it's search. It's page search by page rank and relevancy.

Today everyone says pagerank and relevancy is obvious. Back in 1998 that was not obvious, that engineers were designing a product based on this thing called pagerank. All it was was a simple algorithm that said if a lot of people go to that website and other websites direct them there, there must be something good happening on that website. That was the original algorithm. The motivation was relevance. So I said to David, I have to meet these people. He said, you can't meet them until they’re ready. Which was the following May funny enough, I waited, I called them every month for five months. And finally got my audition with Larry and Sergey. Right away they were very strategic. They said, they we'll let you invest if you can get Sequoia, we don't know Sequoia but they are investors in Yahoo and because we are late to market, but we want to know we have a deal with Yahoo. So I earned my way into the investment in Google.

Marc Andreessen: I will tell one on the other side, which is Airbnb, which we were not early investors in, Airbnb is a growth round, we did the first big growth round under Airbnb at about a billion dollar valuation in 2011. And I think that will turn out to be, I believe that will turn out to be one of the spectacular growths of all time. I think this will really be a great company, so I will tell that story because it is not a story of pure genius.

We passed. I don't think we even met with them the first time around, or maybe one of our junior people did. I said earlier that venture capital is entirely a game of outliers. One of the key things of outliers is that their ideas often seem outright nuts up front. So of course having a website where you can have other people stay in your house, if you made a list of the ideas that were the most nuts that would be right there at the top. Well the second most stupid idea you can think of is having a website where you can stay at other people’s houses. Airbnb deeply combines both of those bad ideas. So of course it turns out, they have unlocked an entirely new way to sell real estate, they have unlocked this gigantic global phenomenon. So part was just coming to the fact that we just whiffed on our initial analysis of the idea and the numbers were clearly proving that we were wrong. And the customer behavior was clearly proven that we were wrong.

So one of the philosophies in our firm is we are multistage, a big reason for that is so we can fix our mistakes and we can pay up to get in later when we screw up early on. The other thing I will highlight on, the other reason we pulled the trigger at a high valuation when we did was because we had spent time at that point with the founders, with Bryan, with Joe, and with Nate. And there is a friend of mine who has a great line, he says when people progress in their careers they get bigger and bigger jobs, and at some point they get the really big job. Some of the people grow into the job, and half the people swell into it. And you can kind of tell the difference. There is a point when people just lose their minds. One of the issues with these companies that are super successful and hyper growth companies, Airbnb was sort of the classic case with these super young founders that haven’t ran anything before. How are they going to be at running this giant global operation? We were just tremendously impressed and are today every time we deal with all three of those guys; how mature they are, how much that are progressing. It's like they get more and more mature, they get better and better judgement, and they get more and more humble as they grow. So that made us feel really good, that not just was this business going to grow, but that these were guys who were going to be able to build something and be able to run it in a really good way.

Ron Conway: You know, people always ask me, why do you think Airbnb is going to be such a great company? Its funny, we are obsessing over Airbnb. It’s because all three founders are as good as the other founder. That is very rare. In the case of Google, two founders, one of them is a little better than the other... hey, he is the CEO. Every company has a CEO. Why am I saying this? When you start a company, you have to go find somebody as good or better than you to be the co-founder. If you do that, your chance of success grow astronomically. And that is why Airbnb became so successful, so quickly. The anomaly is Mark Zuckerberg at Facebook. Yes he has an awesome team, but the Mark Zuckerberg phenomenon where is it one person, is the outlier. So when you start a company, you have got to find phenomenal co-founders.

Sam Altman: Okay, audience members.

Q: So obviously the conventional wisdom of why you raise money is you need it. But the more I get off conventional wisdom the more I hear another story on why you raise money. I am actually hearing founders say it is more to facilitate the big exit. Or in the worse case the acqui-hire instead of fizzling out into nothing. To what extent is that accurate thinking?

Ron Conway: Well if you pick good investors who have good rolodexes and good domain expertise in what your company does, they are going to add a lot more value than the money. Those are the types of investors you should be looking for.

Marc Andreessen: So the answer to the question is yes but in a sense it doesn't matter. Because you can not plan these things according to the downside. I mean that is the scenario that you are obviously not hoping for. While the answer is yes, that should probably not play into the decision making process too much, it might enter into which investor to raise money from, it probably doesn't enter into the whether to raise money question that much.

Q: If you intend to start a business that is capital equipment intensive, do you guys have any advice on how to deal with demotivation? So not everything starts in software, viral, or anything else? What should founders do for capital equipment intensive companies?

Marc Andreessen: I would double down on my previous comments on the onion theory of risk and the staging of risk and cash. Which is the more capital has the business, the more intense you have to be about exactly what is going to be required to make a business work and what the staging of milestones and risks are. In that case you want to line up, you want to be very precise on lining up, because the risk is so high that it will all go sideways, right? You want to be very precise on what you can accomplish with your A round and what is going to be a successful execution of your A round. If you raise too much money in your A round that will seriously screw you up, right, later on down the road. Because you are going to raise a C seed then the accumulative dilution will get to be too much. So you have to be precise on every single round, you have to raise as close to the exact amount of money as possible. Then you have to be as pure and clean and precise with the investors as you can possibly be about the risks and the milestones.

This, by the way, is a big thing. I am really glad you asked the question. It kind of goes back to what Parker said. If you walk into our firm, and you have Twitter or Pinterest or you have something, and it's just viral growth and it's just on fire and it's just going to go, those are the easy ones. It's like, let's just put money in it. Let's just feed the beast. But if you walk in and you’re like, I got this really great idea but it's going to take three hundred million dollars staged out over the next five years probably across five rounds. It has a potential of very big outcome, but this is not Twitter. We will still do those but the operational excellence on the part of the team matters a lot more. One of the ways you convey the operational excellence is in the quality of the plan. Back to the Steve Martin thing, be so good that they can't ignore you. The plan should be precise.

Ron Conway: If you are capital equipment intensive, there are ways of borrowing money, in addition to venture capital.

Marc Andreessen: You can kick in venture debt and then later on lease financing, but then again that underlies the need for operational excellence. Because if you are going to raise debt then you really need to be precise on how you are running the company because very easy to trip the convenance on a loan and it'a very easy to lose the company. So it's a thread the needle process. The demands are just a more advanced level of management than the next Snapchat.

Q: What is a sign you should not work with an investor?

Ron Conway: Well it is the inverse of what I said about a good investor. If it is an investor that has no domain expertise in your company, does not have a rolodex where they can help you with introductions both for business development and in helping you do the intros for Series A, you should not take that person’s money. Especially if they are in it just to make money. And you can sus those people out pretty quickly.

Marc Andreessen: I'm glad you asked this question because it brings up a larger point. If your company is successful, at least the ones we want to invest in want to build big franchise companies, so we are talking about a ten or fifteen or twenty year journey. Ten, fifteen, or twenty years you may notice is longer than the average American marriage. This is significant. The choice of key investors, of particular investors who are going to be on the board for a company, I think is just as important as who you get married to, which is extremely important. These are people you are going to be living with, partnering with, relying on, and dealing with in positions, in conditions of great stress and anxiety for a long period of time.

This is the big argument I always make, and I make it all the time, sometimes people believe it, sometimes they don't. If everything goes great, it doesn't matter who your investors are. But almost never does everything always go great. Even the big successful companies, even Facebook, all these big companies that are now considered to be very successful, all along the way all kinds of shit hit the fan over, and over, and over, and over again. There are any number of stressful board meetings and discussions, and late-night meetings with the future of the company at stake where everyone really needs to be on the same team and have the same goals, be pulling at the same direction, have a shared understanding, have the right kind of ethics, and the right kind of staying power to actually weather the storms that come up.

And one of the things you will find is a big difference for first time founders versus second time founders is almost always the second time founders take that point much more seriously after they have been through it once. So it really, really, really matters who your partner is. It really is like getting married, and it really is worth putting the same amount, maybe not the quite as much time and effort as picking your spouse, but it is worth spending significant time really understanding who you are about to be partnered with. That is way more important than did I get another five million in the valuation order, or another two million dollars in the check.

Ron Conway: I know at SV Angel, our attitude is if you invest in an entrepreneur, we are investing for life. Because if we made the right decision, we are going to invest in every company they start. Once an entrepreneur, always an entrepreneur. We actually do consider it a marriage.

Parker Conrad: I always look for, in that first meeting, do you feel like you respect this person and do you feel like you have a lot to learn from this person? Because sometimes when you meet with VCs, you feel like they are slow on the uptake, they just don’t get it. Sometimes you walk in and they have just this incredible amount of insight into your business that you walk out of their like, man even if these guys didn’t invest that sort of hour that I spent with them was such a great use of my time, I felt like I came out with a much clearer picture of what I need to do and where I need to go. And that is such a great microcosm of what the next couple years are going to be like. If you feel like you would really want this person to be really involved in the company, even if they didn't have a checkbook that they brought with them, that is probably a really good sign. And if not, that is probably a really bad sign.

Q: What is the constraint on how many companies you guys have invested in? Time, money, or lack of good companies?

Ron Conway: SV Angel has kind of got comfortable with one a week. You certainly can’t do more that that, and that is a staff of thirteen. So it's really the number of companies.

Marc Andreessen: Ron if you had twice the number of hours, would you invest in twice the number of companies?

Ron Conway: I would advise against that. I would rather just add more value to the existing companies. SV Angel does have a written conflict policy. But when we do end up with a conflict, it is usually because one company has morphed into another space. We don’t normally invest in companies that have a direct conflict. If we do, we disclose it to the other company, to both companies, and keep in mind at our stage, we don’t know the company's product strategy anyway. We probably don’t know enough to disclose, but our conflict policy also talks about this really important word which is trust. In other words, we are off to a bad start if we don’t trust each other. With SV Angel, the relationship between the founder and us is based on trust. If someone doesn’t trust us, they shouldn’t work with us.

Marc Andreessen: Let me go back to the original question. This is the question that is talked about most in our firm. So the main constraint on a top-tier venture capital firm is the concept of opportunity cost. It's the concept that means everything you do, there are a whole bunch of other things that you can’t do. It's not so much the cost of we invest five million dollars into the company, the company goes wrong and we lose the money. That’s not really the loss that we are worried about because the theory is we'll have the winners that will make up for that.

The cost we worry about is, every investment we make has two implications for how we run the firm. Number one rules on conflicts. So our policy for sure on venture and growth rounds is that we don't invest in conflicting companies. We only invest in one company in a category. So if we invest in MySpace, and Facebook comes along a year later, we are out. We can't do it. Every investment we make locks us out of a category. And the nature, that is a very complicated topic when we’re discussing these things internally. You only know the companies that already exist, you don't know the companies that haven’t been founded yet. And god help you if you invested in an early company that was not going to be the winner and you were locked out by the time the winner came along.

The other issue is opportunity cost on the time and bandwidth of the general partners. Going back to the concept of adding value, we are a general firm, we have official partners. A partner can maybe be on ten to twelve boards in total if they are completely, fully loaded. Basically you want to think of it as a ticket that you have a limited number of holes you can punch, every time you make an investment you punch a hole. When you are out of holes to punch, you are done, you can't make any new investments. That is very much how venture capital operates. A way to look at it is, every board slot that our GP’s have at any given time is an asset to the firm. They can be deployed against an opportunity. But every time we make an investment, it takes the number of slots we can punch down by one. So it reduces the ability for the firm to do new deals. Every investment we make forecloses not just the competitive set but other deals that we will simply run out of time. This goes back to what I said earlier. This company is fairly good, it seems fairly obvious that it's going to get venture funding, why didn't you fund it? Well, on its own, if we had unlimited capacity, we probably would have, but relative to getting blocked by a competitive set, and not having that board seat for an even better opportunity, we pass on that basis a lot.

Q: What would convince you to invest in a company with no product to show. What do you make that judgement based on?

Ron Conway: What would convince us, is what usually convinces us, is the founder and their team themselves. So we invest in people first, not necessarily the product idea. The product idea tends to morph a lot. So we will invest in the team first. If it’s pre users, the valuation is going to tend to be correspondingly lower unless one of the founders has a success track record.

Marc Andreessen: For us, if there’s nothing at the time of investment it's always almost, other than a plan, it's always, usually a founder we have worked with before. Or a founder that is very well known. You know, in these conversations, the default assumption is that we're all starting consumer web companies or consumer mobile companies. You know there are other company categories. For example, enterprise software companies, SaaS, application companies. It’s much more common that there is no MVP, it’s much more common that it's a cold start. And it is much more common that they build a product in the A round. There is no point in having an MVP, the customer isn’t going to buy an MVP, the customer actually needs a full product when they first start using it. So the company actually needs to raise five or ten million dollars to get the first product built. But in almost all those cases that is going to be a founder that has done it before.

Q: What is the ideal board structure?

Parker Conrad: We are fortunate to have, there’s myself and my co-founder and a partner from Andreessen Horowitz. I think it removes the fear, creates a little more trust. It removes the fear that someone is going to come in and fire you arbitrarily because it's time for a big company CEO. But in most cases if you trust the people you are working with, it shouldn't really be an issue. Things almost never come to a board vote, and by the time they do it's something is deeply broken at that point any way. Most of the power that VCs have is outside of the board structure. There are protective covenants that are built into the financing round, you can't take on debt, you can't sell the company, there are certain things you can't do without them agreeing to it anyway.

It's less of a big deal than people make it out to be. What I found, as a founder, if things are going well at the company, you have unlimited power vis a vis your investors. No matter what the board structure is, no matter the convenants in the round. If you say, this is what I want to do, I think this is what we need to do. Even if it's a good investor, or a bad investor, they are like, let's make it happen. They want to ride this rocketship with you, and when things go badly it doesn't matter what protections you have built into the system for yourself.

Marc Andreessen: When a company gets in dire straights, it doesn't matter what the terms for the prior round are, they all get renegotiated. I have been on boards for twenty years, I have never been in an important board vote that mattered. It's never been a vote, many discussions, many controversies, never a vote. The decision has always been clear by the end. It's almost always unanimous. And so I think the decision is almost always around the intangibles and not around the details.

Sam Altman: Okay thank you guys for coming today!