

## The Silicon Valley VC Disease

Yesterday at the Mobile Web Wars event (here's video of that) <http://www.techcrunch.com/2008/07/25/mobile-web-wars-live-stream/> , held right before the TechCrunch party, David Hornik, partner at August Capital (he's the host of the TechCrunch party) told the audience that he would not invest in pure iPhone apps because the iPhone had too small a market share and that anyone who wanted to get big in the mobile space should go after all phones, not just the iPhone, which, while it's hot with early-adopter types and is seeing people waiting in lines to buy around the world, hasn't yet made a dent in, say, Nokia's market share of cell phones overall.

Let's call this the Silicon Valley VC Disease. This disease has been going on for a long time. Seagate's CEO Bill Watkins told me a few months ago that Seagate almost didn't get started because they couldn't get funding from VCs who didn't see a potential market for hard drives. UPDATE: See the comments below where I learned that August Capital is one of those who funded Seagate.

It's a corrosive disease, too, and is why we get tons of stupid Facebook apps and tons of easy-to-make and likely-to-go-viral iPhone apps. Quick: explain why we don't yet have a really brilliant travel app or even a single political app for the iPhone, despite lots of interest in those topics (especially in this political year). Not to mention many brilliant apps like Evernote (my favorite app so far)?

What is the disease? That you must make bucketloads of money (or at least have a shot at doing that) in the first two years of business.

If you have a plan to make just a reasonable amount of money, or if it will take decades to make a big amount of money, don't come to Silicon Valley.

Walmart would NEVER have gotten funded by Sand Hill Road. It took decades to make bucketloads of money. That kind of business plan would never fit in here.

Why? We have the Silicon Valley VC disease.

I imagine that if we went back in time to 1977. Imagine a small group of geeks wanted to get funding to build apps for the Apple II. It didn't have much market share yet. But imagine those developers wanted to build just Apple II apps. Would they have gotten funded? Probably not. And types like David Hornick would have told them "you gotta build apps for mainframes and DEC's, because that's where the market is, not in that Apple II toy."

So, is Hornik wrong? No, he's exactly right. The much bigger market is with regular-old-single-chip-cell phones. You know the type. They are the kinds of phones that make phone calls and

maybe do SMS texting. If they have a Web browser it's a small tiny black and white one that can only look at WAP-style text-centric sites, not the full-blown Web that the iPhone has.

But while Hornik is right, he also has the Silicon Valley Disease. He forgets that the small, seemingly unimportant platform today that gets early adopters excited will become the large, dominant platform of tomorrow. It might take 10 years, though, which is too long for VCs to care about. How long did it take Visicalc to happen on the Apple II? Or Aldus Pagemaker to happen on the Mac? A few years at minimum. iPhone is only one year old.

But already we're seeing the writing on the wall. If you can get past your Silicon Valley VC Disease.

First, our society's most valuable audiences are getting iPhones. Last week when I was in Los Angeles, both of the famous architects I interviewed already had 3G iPhones.

Those two guys are HUGELY valuable for advertisers. They are representative. They aren't the only ones.

But even better than the demographics that the iPhone is getting is the usage patterns.

See, I have two Nokia phones and a Microsoft Windows Mobile phone too. They all suck for using the Web. Fine for email and for texting, but really suck for using the Web.

Go see Google's Vic Gundotra (he's Vice President and runs a bunch of the teams that build things for mobile phones). He told me that usage on the iPhone is "off the scale" when compared to other phones.

Simply translated: people who have non-iPhone phones simply aren't using them for anything other than email. This is easily verified. Sit next to a Blackberry user and watch what they do. I do that all the time. All you see them doing is email and light Web use. Now sit next to an iPhone user and watch what they do. Much more heavily used on photos, maps, Web, and video.

An iPhone user is easier to reach and is easier to get to try new things. Plus, the iPhone app store makes it very easy for an app to be tried out and loaded.

But back to the Silicon Valley VC disease. It's the same disease that Microsoft execs have. Or, really, most big company execs, or worse yet, our government workers, have truth be told.

They won't adopt anything until "it's safe" and until there's a HUGE business reason to do it. It's why huge parts of our government are still run on paper. Why there isn't a database anywhere of all of our elected officials in the United States. Why Microsoft didn't compete with Google

until too late. Why General Motors won't build great all-electric cars until after Tesla or Toyota beats them to the punch.  
Etc. Etc.

Luckily the Silicon Valley VC Disease is having less and less effect lately.

You can startup a company with very little cash, because you can build it on cloud-based services like Amazon's S3, which let you get started and show the world you're getting adoption even before you go for VC money.

And, luckily, not every VC has the Silicon Valley VC Disease. Lots invest in stupid, small, weird, ideas for platforms that only have a percent or two of market share. Go see Jeff Clavier, for instance. He's been doing that a lot lately. I met him in the office of Tapulous last week <<http://qik.com/video/129890>> , which makes iPhone apps.

Why shouldn't you listen to Hornik and others who have Silicon Valley VC disease?

1. It's easier to start a company on new platforms. Why? Because the big money probably hasn't moved in yet, or at least they haven't become established.
2. People who buy new things are FAR EASIER to convince to buy other new things than people who have had the same stuff for years.
3. It's easier to build a brand on a new technology than it is to do that on an older, more established one (hey, everyone has a radio in their cars, but you don't see VC's funding new radio stations, do you?  
Why is that?)
4. The best, most transactional and monetizeable audiences are those that pick up new things. Think about it, would you rather have a customer like Dan Meis, one of the world's best architects or someone like my dad who still uses the same TV that he bought from me in the mid-1980s? My dad is a nice guy and very smart, but he's a horrible customer to have and is going to be very expensive to get to adopt something new.
5. It's a lot cheaper to get adoption when influencers (read bloggers and journalists and Twitterers and FriendFeeders) are talking about you. What are they talking about right now? iPhone apps. Look at Summize, the search engine Twitter just bought <<http://search.twitter.com/>> . What's one of the trending topics on the home page? iPhone. Get over it. They ain't talking about Nokia or Microsoft.

Anyway, I just find it interesting when VCs start telling people not to support a platform when there's lines around the world waiting to buy that platform. If everyone listened to that sentiment we'd never see any innovation in the world.

So, who is working to prove Hornik wrong? Drop me a line.

Oh, and David's a nice guy and throws great parties. Thanks David for letting me in last night and for giving me something interesting to blog about today. :-)

UPDATE: As usual lately a much more interesting conversation about this post is happening over on FriendFeed <<http://friendfeed.com/e/7ebe4a62-d238-508d-bb02-8929b21583b4/The-Silicon-Valley-VC-Disease/>> :

[The Silicon Valley VC Disease](#)

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I actually read the title as "The Silicon Valley VD Disease" ..and nearly jumped out of my seat !! :- ) - [Peter Dawson](#)

I think the bigger issue is the fact that startups want to scale quickly. What happened to starting slow and small and letting the product naturally develop, grow a natural user base, before getting VC and super expanding? I guess it's not as sexy... - [Johan Lieu](#)

Johan: startups have this attitude forced on them by the VC's. The VC's only give you enough money to go a year or two. If you don't build a business by then you either have to convince more VCs to give you another two years of cash, or you have to have a business up and running and generating more revenues than expenses by then. And the VCs don't like it if you just sit on the cash. They are hoping you come up with some dramatic business success. - [Robert Scoble](#)

I hope it's not contagious - [paul mooney](#)

Good post - my phone is not used to connect to the web but to text message. I can't get a handle on the iPhone yet, though. My daughter loves it and that's good enough for me. - [LPH](#)

The other term for this: Short-sightedness. - [Eric Florenzano](#)

ok I jumped off the seat and now back w/beer. :)\_ yeah but if you have the right product and applications , you dot need to shop for VC funds in the first place. The issue is that too many startups are in the markets and nothing really is getting innovated. VS are in to make money. Show me the money and I'll show you my term sheet. Simple investment talk. DONT waste our time - [Peter Dawson](#)

+1 for Peter's "Silicon Valley VD Disease" .... LOL - [Mitchell Tsai](#)

Unfortunately VCs are not the best investors. Most are running scared. Even with their efforts, 85% of their investments fail (50% for the top firms). Creates a me-too mentality evident also in the Pharmaceutical industry. Real break-throughs may have less than 1% success rate. That is too scary for most VCs and pharma companies. - [Mitchell Tsai](#)

And you can only imagine how frustrating this is for biotech (and explains the lack of funding). Takes 10 years to see some results, 3-5 if you are providing services) - [Deepak](#)

Thanks for writing this post, Robert. You're saying better than a lot of us what I'm sure some of us are thinking. It's unfortunate that this kind of thinking can actually prevent innovation and seems counter to the original American entrepreneurial spirit. We all lose when a good idea doesn't get funded to grow as well or as quickly as it could. - [Cathryn Hrudicka](#)

There's also the ROI and IRR disease in the VCs. Typical businesses have maybe a 50% success rate (where success is not the VC - 5X my money in 5 years, but includes I-just-want-to-pay-my-salary companies). The VC pressure to provide decent returns pushes many companies to failure. Rule of thumb: If you aren't willing to take out a loan at 40% annual interest (because your company's opportunity is so big & needs fast speed), don't ask VCs and smart angels. "Inexperienced" angels is ok. - [Mitchell Tsai](#)

P.S. I'm sitting on a lot of worthless pre-public stock. It's tough to be an investor too. - [Mitchell Tsai](#)

the home-run, quick-hit mentality is a disease, sorry ... softer, slower, wider is the way to grow the future we all want ... - [gregory lent](#)

basically VC are getting funding via the global Hedge Funds bowl, w/multi legged swap options. so they (VC's) need ROI's to ensure that they can pay back what they took and make a profit at the same time. They win some and lose some, its a gamble.. Follow the money trail for dynamics of this landscape - [Peter Dawson](#)

VCs want companies to make money so they can recoup their investment and it's called a disease? The sickness is that many of the companies that get funded get funded when there is no hint of a business/revenue plan in place or even on the horizon. If more VCs had a strategy to invest in companies destined to actually make money of course there would be less SV whiny minor millionaires and more real business. - [Brian Sullivan](#)

VC/Angel is the "lottery for the rich": (A) ~15-20% annual returns (B) lottery chance to make \$25 million on your \$25,000 if you hit a Netscape, Yahoo, or Google. Most mathematicians who make a profit at Vegas gambling move on to stock markets, futures/commodity trading, financial derivatives, hedge funds, etc... - [Mitchell Tsai](#)

+1 for Brian: In the VC biz, that's called "pressure to invest". Not enough good ideas & teams to invest in. Conservative VCs won't find enough investments, thus the "pack" disease of VCs all funding hard drives at the same time. Much more fun chasing pictures on the internet. :- ) - [Mitchell Tsai](#)

Brian: the companies that get funded that have no obvious business model (PodTech and Twitter, for example) are part of the VC Disease of go for a home run. They were hoping that PodTech would turn into the next YouTube and that Twitter turns into the next Google. Remember, Google didn't make money for the first four years of its existence, and, in fact, were almost shut down because they weren't paying their bills at Exodus. - [Robert Scoble](#)

Liking mostly because you say not to listen to Dave Hornik. I think I might actually be starting to like you, Robert. - [Cyndy](#)

Echoing Robert: Google burned through \$26 million before finding profitability with Bill Gross's (Idealab) [http://idealab.com/about\\_ideal...](http://idealab.com/about_ideal...) sliding-scale ad fees <http://en.wikipedia.org/wiki/S...> I would have been too chicken to put that much money into Google. The sliding-scale ad idea of Goto.com wasn't a "proven" revenue model either. "In November 2001 Gross defaulted on a \$50 million personal loan he had taken from the Bank of America to invest in Idealab". - [Mitchell Tsai](#)

Using Google as an example of a company that didn't have a business plan but ended up a big success is getting tired as an argument for support of investment of clueless "businesses" and their founders. Investors in Google and the founders won the lottery -- that doesn't justify investing in the lottery as business strategy. Investing in iPhone apps in my mind would also be a waste of money (maybe not quite as idiotic as investing in Facebook apps though). iPhone will not be the winner in the mobile computing sweepstakes- in my mind it is destined for the same scrap heap as the beta tape format. Investors really should be looking outside the SV echo chamber for potential investment successes. - [Brian Sullivan](#)

VCs have to see a deal in this way: 3-5 years to get to 10X return. They can't wait 10 years for a payback, their fund is usually only 10 years as far as I know. So they can't fund things that are too far out. Although it seems clear that the iPhone can create opportunities that fit in this framework of 3-5 years to 10X return, so not sure why Hornick was down on it. Nice, controversial post to get us thinking... I think the disease is more like "groupthink" than it is "lack of long-term vision" - [Elliott Ng](#)

+1 Brian - [Cyndy](#)

Interesting post Robert. May be what Dave is saying is that when a company has proven their concept on the iPhone is ready to scale to other platform, then the time is right to actually go after a bigger VC round. I think that both people like Jeff and Dave are key to the entrepreneurship ecosystem: they just target different stages of the company lifecycle. Another way to prove that is that 1) raising too much money on day 1 is the best way to lose the focus necessary to survive and 2) traditional VC firms can not scale to manage 100 x \$1-2M deals. - [Edwin Khodabakchian](#)

Brian: when I went to Israel a high percentage of developers there proudly showed me their iPhones. And there's not even an Apple store in the country. I HAVE GONE outside the country. Tons of the best iPhone apps are from outside of SV. I also totally disagree about iPhone not being the winner in mobile computing sweepstakes. At least not as the market is today. But I hear Nokia is coming out with something cool in January, so we'll see. And Microsoft told me they are bringing out something cool next year. - [Robert Scoble](#)

Brian, maybe the iPhone will wind up like the Atari, who knows. And I would add that many times investments are at least as much due to the people than to the initial technology. However, the iPhone is a game changer. I find that I'm using it more and more to read news, check the weather, etc--some which is new behavior for me, but also some of which I used to do on my notebook. The iPhone is winning out. Is it perfect yet? No. I want more, but there's a systemic change going on here. - [Loren Heiny](#)

Loren: the problem with people who don't own iPhones is they just don't see how big a game changer it is. I wish I could get Brian to carry around the four phones I currently have to see how bad these things all are compared to iPhone. The iPhone isn't perfect, either, but it's years ahead of the others. Of course, back in 1989 the Macintosh was years ahead of everything too and see what happened... - [Robert Scoble](#)

Deepak: Agreed, look at Amgen and Genentech as classic Biotech examples - [Sally Church](#)

Scobles , are yo sure that iPhones are just not hype ? - [Peter Dawson](#)

Mr. Scoble - I'll tell you... this disease causes Myopia too. There are SO many fine business opportunities being pitched right here in Tulsa, Oklahoma City, Wichita... Sevin Rosen Funds has a guy here in Tulsa. EARLY stage oriented. Pre-money oriented. Why KPCB or Charles River (or whoever) doesn't grab some initiative and park a good couple of partners in middle-America and work some new land is beyond me. - [Gerald Buckley](#)

You'll get little disagreement from me on this one, Robert. But it's not just VCs, it's inertia. OTOH, Brian Sullivan a few comments up makes a great comparison...iPhone (and Facebook for that matter) are heading the way of BetaMax and MiniDisc, and MemoryStick. I may not use MySpace, but they're the VHS of the Social Network game right now. What we need is for someone to invent the DVD. - [Andrew Feinberg](#)

Robert: I have absolutely no need for the Iphone (or any "smart" phone) and certainly would not pay the ridiculous prices some people are paying to use them. These products and their supporters are making a couple of fundamental assumptions that I think are flawed: that most normal people are like California geeks that feel the need to be connected at all times and that people will continue to commute and move about daily and have waste travel time to consume using these devices. That may make me an apparent Luddite (or maybe I am a generation removed from understanding the need)but I am still offended by people that answer mobile phones in the middle of a person to person conversation and am equally offended by people at a "real" social gathering with their eyes glued to a 3" screen and thumbs/fingers flailing wildly. - [Brian Sullivan](#)

Peter D. define "hype"? I can't be sure that iPhone will "win" the mobile space (I seriously doubt it given current pricing). But they're bound to be closing in on their 10 million units worldwide goal, and especially given the price, that doesn't strike me as hype. - [Robert Seidman](#)

I completely respect yet disagree with this post. Most designers are not businessmen, VCs help in other ways than a chequebook. You bring the skills and the idea, they teach you how to squeeze money and create revenue. Great ideas change the world but they're not always profitable. VCs are there strictly for the money and you have to respect that. - [Cains](#)

What's wrong with investing in Facebook apps, if you get the exposure it's like advertising on Taxi wheels (I've seen this one). As for the iPhone, it has changed the way people are surfing on mobiles and this advertising market is just at the beginning so i see many companies getting inside. The only question

i ask myself is either the company can generate money within 3-5 years or not and should i put my money in as if it was after the bubble burst. - [Nir Ben Yona](#)

Brian, here are a couple non-California uses of an Internet connected device like the iPhone. Imagine you're in Nebraska in the spring. A storm rolls in. Tornado sirens blare. If you've got your iPhone with you in the closet or basement or wherever in anticipation of a tornado, you've potentially got access to an Internet radio, weather radar maps, 911, etc in your iPhone. Another example: You're visiting friends/relatives you haven't seen in years. The cameras in the car. You take a pix with your iPhone, email it to family/friends that moment. All of this can be done with other devices, but the iPhone does it in one. - [Loren Heiny](#)

Great post. I see no excitement surrounding any other phone. People I know who use Windows Mobile phones have to in order to have access to corporate email. Maybe that will change with Apple licensing ActiveSync. - [Brett Nordquist](#)

Peter: I'm absolutely convinced that iPhones are not hype. Brian: mobile didn't get hot in California first. You really need to visit Europe or Japan or Korea. There we look pretty stupid in our usage of mobile. As for "needing" stuff, you probably 10 years ago would have told me you don't "need" a cell phone, but today I can't name a single person that I know who doesn't have one, except my baby. You need to travel more and watch what people do when a plane touches down. Everyone starts up their mobiles. - [Robert Scoble](#)

Has anyone decided if Apple's implememntation of ActiveSync is any good? - [Andrew Feinberg](#)

I guess I'm glad I can have whatever phone I choose, and no need to worry about syncing anything, as I'm not tied to a corporate and all the associated bloatware that goes with it... - [Ian May](#)

"First, our society's most valuable audiences are getting iPhones." Really our most valuable audiences? Archeticts are these type of people? What about doctors, nurses, firemen, policemen, etc. They are way more valuable then any single architect in LA. Get over yourself.... That comment alone made me snort my coffee. I know 4 people who iPhones, neither of them would be somoen who i would define as society's most valuable audiences. - [Jonathan Jesse](#)

@Loren Heiny I have a co-worker who used his Windows Mobile device in a Tornado to upload video of the tornado, let people know about that he was safe via email all w/o an iPhone. and from the hotel's bathtub which was the safest place. - [Jonathan Jesse](#)

@Loren Heiny: when my son was born i used my windows mobile phone to take pictures and email those pictures to everyone i know from one device.... from a windows mobile phone - [Jonathan Jesse](#)

@Brian Sullivan: I completly agree.. I have a Windows Smartphone from work, it is also the only cell phone I have. try taking a vacation when you get constantly reminded that work needs you through emails. I am amazed about how rude it is for people to interrupt converstations and text/sms/email/twitter whatever instead of talking with the person face to face in front of them. this is



something that i am struggling with as my phone is always "buzzing" with something new. - [Jonathan Jesse](#)

Ok its not hype.. but with over 715Million users of Mobile technology in China alone. What does a 10M unit sold slice in terms of market penetration to these segments ? Just asking.. So you can see how thin of a slice that iPhone really has in terms of market share. A product may have all the bells and whistles on it, but if major user base is not buying into it. then it could be some real issues. - [Peter Dawson](#)

I think the whole VC model is broken. We don't need millions of dollars for our startups anymore, we need \$25k or \$50k. When I hear about companies getting millions of dollars, I always think, what the hell are they doing with it!? - [Dawn](#)

To add scale to the 10M figure, <http://en.wikipedia.org/wiki/L...> roughly 70% of those will be changing their phone within 5 years. ChinaMobile signs up almost 10M subscribers per month! - [Cains](#)

I'll offer this, just me speculating. I'm not sure that the price point of the iPhone is the biggest factor these days. I think we're more bottlenecked by the thought of paying ridiculous prices for sub-par mobile web. I mean seriously, what the heck is with the current rates for cell phone plans. Also, the thought of paying for SMS in 2008 is just silly. It should be included in all plans. Not for the purpose of cutting profits from our providers but rather for American's to catch on to the technology. - [Ben Pettit](#)

@ben I vaguely recall Mr. Scoble interviewing someone (was it the FCC commissioner conversation maybe) that had the US basically foregoing SMS and being off & onto the next big thing. SMS won't really stand a chance against what's coming is what I heard. Robert...? Care to put that in better context for us? - [Gerald Buckley](#)

Dawn: \$25K, \$50K, \$100K These are the lower-price points for qualified angel investors, who work the lower levels below the first tier of \$500K-\$3M VCs. One VC person can maybe manage 10-20 investments, so you can divide the size of fund by the number of active partners (x10-20) and figure out what size investments are in a VC-fund's sweet spot. Complicating the issue are some micro-VC funds, angel-type funds, and \$5-20K Y-combinator-type-groups. - [Mitchell Tsai](#)

Scoble: Great post. Hornik is a very smart guy, but he is hamstrung by the current VC model. VCs need a huge upside because the model dictates that they need to put in a ton of cash on the front end. Most of today's web startups don't require the kind of cash that VCs are used to putting in. That's why Hornik doesn't want to invest in iPhone apps. He wants to invest in companies with hundreds of millions in near-term valuation, not tens on millions. Imho, that is the VC disease -- in SV or out. - [Christian Anderson](#) via [fftogo](#)

During the last tech bubble my partner and I pitched our idea to McKinsey and some VC's. We were "traditional" businessmen (organic measured growth, control costs etc) and after the pitch the response we got was "Great Idea but forget profits and acquire users at any cost and give us a plan with a 24 month exit, then we can talk". Needless to say we walked. - [Michael Sheehan](#)

Robert, I left a long comment on the post with my thoughts. I appreciate that some investors don't have the patience to bet early and let an idea run its course. That said, I don't think I am a good poster-child for that problem. August Capital has a long history of betting early and supporting our companies for as long as it takes to create an interesting business. - [David Hornik](#)

@cyndy Curious what I said or did to deserve your comment? - [David Hornik](#)

David: thanks, I just wrote a new post about this new world where people like you help us arrive at the truth by participating. Appreciate that a lot. - [Robert Scoble](#)

Gerald: SMS is seeing some pickup here, but, really, look at Twitter, which is what my son is using now increasingly, or Facebook. If you have an iPhone both of those are a lot better than SMS. Also, my phone is increasingly getting SMS spam, which will really piss people off and keep them from adopting that system. - [Robert Scoble](#)

This is not too dissimilar from the Innovator's Dilemma concept by Christensen. The "right" business decision ("right" as in profit-maximizing) would be to invest in big, rich markets: that's precisely why there is an opportunity for disruptors to enter the market. - [Tito Costa](#)

+1 for Michael Sheehan. - [Mitchell Tsai](#)

None of this seems like rocket science. Valley VCs want big returns in short amount of time. Asking them to invest in small slower-growing but sustainable markets is like going to Ford Motor headquarters and asking to buy a windshield wiper. It isn't the scale that they're working at. - [Michael](#)

While you make some valid points, Robert, I don't it is fair to call it a disease. Looking for investments with a short-term return potential is certainly a legitimate investment strategy. I can't fault them for opting for preferring lower risk, quicker payoff investments, rather than longer-term (and thus higher risk) investment that \*may\* payoff huge in 10 years. That said, there are other types of investment strategies out there -- I think your post highlights a void that needs to be filled. - [Mark Carey](#) via [Moopz](#)

I still think, after reading the post, the follow up and this thread, that a VC is perfectly entitled to pick and choose investments based on the return. And I'm sure there will be a few start-ups that have a Walmart business plan - take two aspirin and call me in ten years. Because that's the way it is in technology (not just SV). The issue here is that we don't hear from these companies. We may well get the next Google, Microsoft, Sun, HP, etc from there. - [Roberto Bonini](#)

I think this disease is more of a symptom of greed and ego vs. making a difference in the tech world. But then again, isn't that what business is about? It is very hard for traditional business to grasp this concept, and is why real innovation won't be found there. - [Venson Kuchipudi](#)