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COVER STORY

Valley Boys

Digg.com's Kevin Rose leads a new brat pack of young entrepreneurs



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- It was June 26, 4:45 a.m., and Digg founder Kevin Rose was slugging back tea and trying to keep his eyes open as he drove his Volkswagen Golf to Digg's headquarters above the grungy offices of the *SF Bay Guardian* in Potrero Hill. This was the day Rose would test everything. Two years earlier, Rose had gambled on his idea to change newsgathering, letting the masses "dig up" the most interesting stories on the Web and vote them onto his online "front page" on Digg.com. Rose had given every last piece of himself to the project -- all his time, all his cash, and even his girlfriend, who fought with him after he poured his savings into Digg instead of a downpayment on a house. Today, Digg, Version 3, the one that would go beyond tech news to include politics, gossip, business, and videos, was going live. At 29, Rose was on his way either to a cool \$60 million or to total failure.



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As Rose sat in the middle of the office, managing a final countdown, a Puma cap yanked over his eyes, his posse of twenty- and thirty-something engineers sat at their desks with contingency plans and extra servers ready. They flipped the switch. Stories started trickling in. The pace picked up, and suddenly, it was a deluge. Digg staffers grew frenzied, screaming at one other to stay one step ahead of the traffic. By 4 p.m. on launch day, the site had signed up more than 13,000 new registered users, eight times the average number. Traffic was clocking in at four times the volume of the previous Monday. The news of Digg's launch was lighting up the blogosphere. An exhausted Rose collapsed for a snooze under his desk.

Digg's stature changed dramatically that day. It is now the 24th-most popular

Web site in the U.S., nipping at the *The New York Times'* (No. 19) and easily beating Fox News (No. 62), according to industry tracker Alexa.com. More than 1 million people flock to Digg daily, reading, submitting, or "digging" some 4,000 stories. As on many Web 2.0 sites, people register and create online profiles. Then these "diggers" can upload links to stories and blogs they want to share from other news portals like Yahoo! ([YHOO](#)) News or mainstream media sites like *The Washington Post*. Users can click a "digg it" button that essentially casts a vote for the content. They can also hit the "bury" button. The stories with the most "diggs" zoom to the top of the page. Of the free labor that is the "Digg Army," 94% are male; more than half are IT types in their 20s and 30s making \$75,000 or more. It's a demographic advertisers lust after.

COMMUNITY FIRST, ADS LATER

That's why some smart money is on Digg to become an ad magnet à la MySpace.com. ([NWS](#)) Some even refer to Digg as the new *New York Times*. News sites are discovering they can benefit too: Get a story on Digg's front page, and in comes a flood of traffic from people clicking on the link to read the story on your site. Digg gets advertising via Federated Media, the company Silicon Valley veteran John Battelle created to pair Web sites with advertisers (Digg sparingly places ads in a narrow band at the top of the Web page). So far, Digg is breaking even on an estimated \$3 million annually in revenues. Nonetheless, people in the know say Digg is easily worth \$200 million.

It's not as dot-com déjà vu as it sounds. YouTube, the enormously popular video site, posts similarly fledgling revenues, but some experts say it could easily fetch \$500 million. What's more, Digg registered users have been doubling every three months. As such, Digg is attempting to follow the path laid out by Google Inc ([GOOG](#)), and now being adopted by many Web 2.0 companies: focus on building a user community, and the ads will follow. "It's one of those things where we know we could put crazy ads all over the site and clutter it up, but we don't want to do that," says Rose. "We have a clear path toward becoming a profitable company, and we're fully funded. We don't have to worry about it now, as long as we keep hitting our numbers."

So far, Digg has succeeded. But success has also brought copycats and stress. A rumored \$40 million offer from Yahoo! Inc. ([YHOO](#)) surfaced in January, which Yahoo denied. Two weeks before the Digg.3 release, AOL launched a rival under the old Netscape brand. (It was headed up by former Silicon Alley superstar Jason M. Calcanis, owner of Weblogs, who early on offered Rose an investment in Digg and an option to buy it for \$5 million. That deal would have left Rose with no control. Forget it.) On July 18, AOL tried to lure Digg's top 50 contributors with \$1,000 a month to switch to its site, which led Rose to rant on his weekly podcast that Calcanis and AOL were trying to "squash Digg." The corporate giant's failure to gain inroads so far shows that simply copying Digg won't work. It also spells out why Old Media types are so afraid of being eaten alive by the creative destruction these young new players are delivering. The barriers to entry are now

so low that all it takes is a laptop and a \$50-a-month Internet hookup to make a kid the next mogul.

Rose hints that there's going to be more to Digg than just democratizing the news. In six months, he says, as he polishes off a Belgian beer at Fly Bar in San Francisco's Hayes Valley a week after the launch, the site will unveil new features he can only describe as "some really cool stuff." He's beaming as though he's talking about a new girl, and it's all he can do not to blurt out what all that cool stuff is. "Why would you sell unless you feel you've played your hand?" he asks.

The thought of selling all or even a large piece of his venture brings back some bad memories. Rose and all the other geeks know someone from the last boom who was worth millions one month, only to move into his parents' basement the next. Indeed, Valley-wide, guys like Rose, his entourage of buddies, and many others are haunted by the years when the weekly rooftop parties died, the traffic thinned, and no one needed restaurant reservations. This time around, the entrepreneurs worry that, within a moment, the money -- and their projects -- could vanish.

ROCK STAR STATUS

But for now, Rose is the "It" boy among a new wave of entrepreneurs running the hottest of the top 100 Web 2.0 companies sprinkled around the Bay Area. Together, this network of mostly Valley boys -- Six Apart Ltd. co-founder Mena Trott is a rare female among them -- fill SF bars like Anu and Wish and Cav and parties at their sparsely furnished lofts.

Rose's social stock has climbed, too. He has more than 11,000 friends on MySpace. He was a runner-up in blog ValleyWag's "Hottest Guy in the Valley" contest (think Tom Cruise's doughier little brother), and he co-hosts a hot weekly video podcast called *Diggnation*. It's like a techie version of the *Saturday Night Live* skit "Wayne's World." He and Alex Albrecht, a former TechTV co-host, sit on a couch, drink beer, say "dude" a lot, and talk about the biggest stories that week. At a party for the 50th show, Rose was mobbed by fans and even photographed signing a pretty brunette's cleavage. The snapshot was posted on Flickr the next day, prompting one viewer to comment: "When did they become rock stars?"

Clearly much has changed since 1999, and Rose and his fellow wealth punks have little in common with the sharp-talking MBAs in crisp khakis and blue button-downs who rushed the Valley as the NASDAQ climbed. In the late 1990s, entrepreneurs were the supplicants, and Sand Hill Road, dotted with venture-capital firms, was the mecca. Dot-commers relied on VCs for the millions needed to buy hardware, rent servers, hire designers, and advertise like crazy to bring in the eyeballs. For their big stakes of, say, \$15 million for 20% of a company, venture capitalists received board seats, control of the management levers, and

most of the equity.

Now, it's more like: Maybe we'll let you throw a few bucks our way -- if you get it. Otherwise, get lost. That's possible because the cost of jump-starting a good idea has plummeted. At the same time, the sources of money have multiplied, swirling in from new VC shops, angel investors, and strategic partners galore. The awash-in-capital environment has flipped the power dynamic. Sure, they'll take money from the "sweater vests," as Digg CEO Jay Adelson calls the VCs, but they'll do it on their own terms. "It's a good time now for the entrepreneur," says John Freeman, a professor at University of California at Berkeley's Haas School of Business. "There are lots of different pots of money. It gives them the ability to modify when they take it, [and] how much they take, and leaves them with more control."

Who are some of the new geek elite? Besides Rose, there's his pal and Wall Street transplant Joshua Schachter, who recently sold Del.icio.us, a Web site to exchange favorite links, to Yahoo for an estimated \$31 million; gaming whiz kid Dennis Fong, a.k.a. Thresh, co-founder of gaming company Xfire, which sold to Viacom Inc ([VIA](#)) in April for \$102 million; Mark Zuckerberg, who started the social networking site Facebook in college; and Jeremy Stoppelman and Russel Simmons, co-founders of Yelp.com, a consumer review site. The elder statesmen of the group are Hot or Not founder James Hong and his best friend, Max Levchin, who sold his company PayPal to eBay Inc. ([EBAY](#)) for \$1.5 billion at 26 and is now engrossed in Slide.com, a startup that delivers images to computers in a slick slide show format.

Digg is emblematic of the ethos of Web 2.0, new consumer and media sites revolving around social networking and do-it-yourself services. Others include YouTube, which serves up some 100 million requested videos a day, rivaling the audience of NBC. Then there's Facebook, where the college crowd practically lives. The average gamer on Xfire spends an astounding 91 hours a month on the site -- it's like a part-time job. As a result, superhigh valuations are again coming out of the Valley. In a world in which Facebook turns down \$600 million deals, the \$580 million that Rupert Murdoch's News Corp. ([NWS](#)) shelled out for MySpace.com in July, 2005, is widely considered to be a steal.

Those in the know believe that Digg could become a new kind of clearinghouse for news and that its interactive community concept could snowball. That could be a jackpot for Rose, who owns 30% to 40% of the company (he won't specify) - - a massive stake for a founder in a world in which investors routinely demand up to 20% with every outlay. But it's still only paper wealth, which he and many others have learned can evaporate. "I was here in 2000," he recalls in an instant message.

It was just two years ago that Rose was the host of an obscure cable show, *The Screen Savers*, on a low-rent channel called TechTV. One day, he was at lunch

with Apple Computer Inc. ([AAPL](#)) founder Steve Wozniak, a favorite interview subject. Woz was in a deep riff about the glamour of Apple's garage days, and Rose realized he was jealous of Woz's place in Valley history. This guy has actually done things, Rose remembers thinking, while I'm, like, a visual stenographer. That night, Rose returned to his five-person Santa Monica house, head down, and plopped in front of his computer. Like every other night, he explored the back caves of the Internet, scavenging for hidden gossip and unearthed news that eluded most mainstream editors. They were all so clueless, Rose was thinking. And then it occurred to him: Oh my God. I could do this SO. MUCH. BETTER.

BOTTOM-UP MEDIA

Soon, Rose was blabbing about his idea to his girlfriend, his buds, his bartenders. This would be bottom-up media. Citizen journalism. In the fall of 2004, Rose withdrew \$1,000 -- nearly one-tenth of his life savings -- and paid a freelance coder \$12 an hour to mock up a Web page. He got a deal on server space over the Web for \$99 a month. Only one big expense was left: the domain name. He tried Dig.com. *!@#! It was owned by Disney. He offered the owners of digdig.com \$500. They wouldn't sell. Ouch. Finally he settled on Digg.com and forked out \$1,200 to its owners. The site launched on Dec. 5, 2004.

Today, Rose is like one of those guys he used to interview. But he and his ilk have their detractors. Some say Digg is just regurgitating news. Others accuse Web 2.0 entrepreneurs of trying to build businesses around little more than one cool feature. As always in the Valley, say critics, the froth floweth over.

Rose is listening to his gut, he says. Digg arose out of his everyday life, just as Facebook and YouTube and Xfire did for their founders. During the boom, MBAs dreamed up stuff they thought could nab money. Today, the geeks insist they're looking at ways technology can fill the gaps in their own lives. Then they build those services and share them with their friends. Once something works, they start to dribble it out to the world. But nothing too fancy that needs money to get started.

So the VCs aren't so mighty this time. There's intense competition among funders for pieces of Web 2.0. Two decades ago, nearly 300 VC firms invested in high tech. Last year, that number soared to 866 in the U.S. Meanwhile, deal sizes for Internet companies are contracting, even as valuations for those deals almost doubled from 2004 to 2005 and are rising still. That means investors are forced to take smaller stakes in Web deals, while entrepreneurs holding on to more. Money is also coming from legends like Marc Andreessen of Netscape fame, who's backing Web 2.0 projects, as are rich friends Levchin and Hong. "Until capital becomes important again, venture capitalists are screwed," says Andrew Anker, a former VC at August Capital in Menlo Park, Calif., who decamped in 2003 for blogging startup Six Apart.

Rose grew up in Las Vegas. His father is an accountant, and his mom "just chills," he says. They lived in a three-bedroom house on a cul-de-sac. Standard middle-class America. His computer love affair drew scorn from schoolkids so Rose transferred to a public vo-tech in 1993 to study computers and animation. "It was a chance to be with other nerds," he says.

In 1999 he dropped out of the University of Las Vegas to join the action in Silicon Valley, where he took coding jobs for dotcoms. That led to his gig as the TechTV host, which transferred him to Los Angeles in 2003. But Rose was bored. He hated L.A. If it hadn't been for his friendship with Adelson, he might never have pursued the Digg idea. The two met when Rose interviewed Adelson, 35, founder and chief technology officer of data center company Equinix, on TechTV in 2003. Here was another guy actually doing something. Rose and Adelson quickly hit it off. Adelson played the grown-up, a role he still relishes, saying things like, "Kevin, you're 29 now, you need to stop wearing your pants lower than your boxers" (advice Rose still ignores). But he believed in Digg from the beginning.

FORGET PORTALS

In February, 2005, Rose cashed Digg's first investor check. It was for \$50,000 and came from a friend, Chris Hoar, who had founded Textamerica, a site that enables you to post cell-phone photos to your blog. When Rose was desperate for servers, Hoar cut him a check on the spot. Digg didn't even have a company bank account yet, so Adelson walked Rose through the accounting and helped him drum up the next round, which was several hundred thousand dollars in investments from angel investors, including Andreessen and Reid Hoffman, CEO of social networking site LinkedIn.com Corp.

Rose asked Adelson to sign on as chief executive. Adelson had been burned during the last boom, when his net worth dwindled from a high of \$55 million, but he decided to take the job, even though it would mean commuting between New York, where his wife and three kids live, and San Francisco. There was something about Rose: He reminded Adelson of his younger, single self.

By spring 2005, the venture set had caught on that something was happening at Digg. Adelson was fielding a call per week begging for a meeting, but he kept stalling. He wanted Digg to get more traction, to wait until they really needed the money. "I don't want to be someone's ticket into a market," Adelson says. When they started talking with VCs last August, Adelson recalls, a few asked about Digg's plans to convert its site into the next Yahoo or Google. "They are still back in the 1998 belief system that it's all about portals," Adelson says, laughing. "Grow up, man."

At an obscure office complex in San Mateo in August, 2005, the reception was different. Greylock Partners is a storied VC firm with many home runs to its credit, but few dot-coms among them. Yet Greylock partner David Sze seemed to dig Digg. He himself was a member of the Digg Army. He understood Rose's of-

the-people vision. "There were not a lot of in-between kind of guys," Rose says. "David got it, and most everyone else didn't."

Then Sze, 40, stunned them. Rose and Adelson were seeking only \$1 million or \$2 million, pocket change to most Silicon Valley firms and hardly worth their time; VC firms usually make big bets to win big stakes. What firm has the resources to keep an eye on 100 companies? Funders had been trying to persuade them to take \$5 million, even \$10 million, but Adelson stood firm. Sze agreed they didn't need it and got his his partnership to change the rules and green-light the small deal: \$2.5 million, divided between Greylock and another firm, Omidyar Network, the venture fund of eBay founder Pierre Omidyar.

Digg was finally flush with enough cash to pay salaries, rent an office, and keep employees in standard startup snacks like Twizzlers and Vitamin Water. Adelson did the hiring and managed the business, while Rose worked on Version 3.0. On trips home to Las Vegas or to see friends in L.A., Rose dreamed up at least one new feature per trip, like the Digg "stack," which visually shows users how stories are being ranked in real time, and a module for tracking friends' activity on the site.

But the consumer Web is still a crapshoot. As early social networking sites like Friendster learned the hard way, audiences can be fickle. "It's kind of like the entertainment business," says Berkeley's Freeman. "If it hits, it's big."

So far, Digg's traffic just keeps growing. And Rose is picking up a bit of swagger. His shyness is fading, and his wardrobe has gotten a hipster upgrade. Girls on MySpace swarm him. But the pain of losing his girlfriend isn't gone, and he says that no matter what happens with Digg, he won't put business first again.

The tech bust notwithstanding, the Valley is still the only place on earth where geeks with good ideas can become celebrities overnight. But wannabes be warned: As nearly everyone found out six years ago, the fall from rock star to pariah can be just as quick -- and not nearly as much fun.

By Sarah Lacy and Jessi Hempel

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