Dean's Executive Leadership Series - 2008-2009

Transcript of Presentation by Ann Winblad, co-founder of Hummer Winblad Venture Partners – Part 1

About DELS: The Dean's Executive Leadership Series at the Graziadio School of Business and Management features in-depth audio or video interviews with today's top business practitioners and thought leaders. Listen or subscribe to the podcast to hear their views and insight on the current challenges and opportunities facing the business community.

Start

Narrator: The Graziadio School of Business and Management at Pepperdine University proudly presents the Dean's Executive Leadership Series. This podcast invites top business practitioners and thought leaders to share their view on the real world of business.

Dean Linda Livingstone: Well good evening every one, how are you, it's good to have such a great group with us tonight for our Deans Executive Leadership Series; this is the second year. We have come to Northern California as part of this series and so we appreciate you being here. We did candy last year with Jelly Belly and we're moving to software this year so very different perspectives but good all in their own. But I do also want to particularly recognize right now Daniel Chang of Farmers Insurance Group, where's Daniel? Right here; Farmers Insurance Group sponsors our Deans Executive Leadership Series and it is because of their enhanced sponsorship over the last two years that we've been able to bring this series to Northern California, so Daniel we appreciate you being here and. I also want to recognize Georgie O'Keefe, is Georgie still in the room, there, oh right here in front of me and her husband Richard is our photographer tonight but Georgie works for one of our alumni, Howard Show at EMC, and she worked with us to get Ann Winblad to come speak, so thank you so much for doing that and we're sorry Howard wasn't able to be with us tonight.

Before I introduce Ann, I do want to mention a few things that are going on in the school to give you a little bit of an update on some things that you can take advantage of up here in Northern California. I do want to mention that we are actually going to do a second DELS up here in the spring, we are going to have with us Priscilla Stewart-Jones who's the Vice President of HR for McKesson and she will be here I

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think it's April 7th, is that correct, on April 7th, so we will be back in the spring and hope that you will come and bring some of your friends with you.

Another wonderful opportunity, the university has just rolled out live YouTube university and iTunes university and so you now will have access on the internet to almost any speaker that comes to campus at Pepperdine, whether they're in the Business School or into other schools, you will have access as you already have had to the podcasts that we do for these events and so we'll have on YouTube university there are videos of all of the DELS speakers we've had for the last three or four years, so it's a tremendous resource particularly for our alumni that are not in Southern California and don't always have the opportunity to see as many of these individuals live.

A couple of other kind of interesting new programs that we're working on; I want to mention this one because I think it will resonate with some of you here. We as you know don't have an Engineering School or a Computer Science Program at Pepperdine; we are in the process of having some conversations with UCSBC Santa Barbara that's kind of up the road from our Malibu campus. They of course have a world renowned Engineering Program but they do not have a Business School and both of us have really strong entrepreneurial interests and efforts and so my Mike Sims who's our Executive Officer for Corporate and External Relations, he and some of our other staff have been working with UCSB to try to identify some ways we can partner together and really leverage the expertise as we each have to really create something interesting and new and so we're starting that by encouraging our students to partner together in our business plan competition. So we have business and business plan expertise, they have people that are creating really new and interesting products and technologies and so we're going to be involved in developing that relationship and we hope that we'll move beyond just the business plan competition.

But it's a new way for us to think about how we partner, we do a lot of international partnerships, we haven't done domestic partnerships and we think that one can be particularly interesting for us given the expertise's of the two universities and then the last new program I want to mention, we at Pepperdine have not had alumni travel programs in the past and in the Business School we are going to begin to provide some opportunities in that area and the first one is going to roll out in the late spring and we are going to be planning a trip to Australia. So you need to go see the movie and I'm not getting any plugs for that but go see the movie and then come on our trip to Australia in late May, early June, we'll be rolling out more information, I think you got flyers as you came in but it should be a tremendous opportunity, a great trip and a way to bring some of our alumni back together and see a part of the world that some of us may not have seen a lot of over the years.

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But tonight in addition to telling you about some of the wonderful things that are going on in the Business School, we are here to hear from Ann Winblad. Ann is co-founder Hummer Winblad Venture Partners and I wanted to tell you just a little bit about her background and then introduce her to you, she will share with us for about 20 minutes and then she and I will have a brief conversation before we open the floor to questions. So be thinking about what you would like to ask her, how you would like to pick her brain while we have her with us this evening. But Ann is actually a small town girl from Minnesota, her father was a coach, her mother was a nurse, she came from a fairly small high school. We were comparing notes, my high school's actually smaller than hers so and we both had coach's for fathers so we have some common experiences.

She has a BA in Mathematics and a Master of Arts in Education with a focus on international economics and she got both of those degrees from schools in Minnesota, College of Saint Catherine and College of Saint Thomas and after that she went to work for the Federal Reserve Bank in Minneapolis but decided after about 13 months that the entrepreneurial life was what she was most interested in and so she started a company called Open Systems Inc, they lost $85 in the first year that they were in operation, she actually had to go on food stamps for a while with her partners that she started that company with. But they invested $500 and six years later they sold the company for 15 million dollars, so not a bad return on investment and didn't use any venture capital I believe so she's gone a different route now with her life than she did then.

In 1989 she started the venture capital firm that she's now a part of with John Hummer, it's the first fund that was exclusively focused on software and they now manage more than a billion dollars in venture capital. She's also on the board of directors of several companies in this area and a member of the board of trustees of the University of Saint Thomas and I guess a fun tidbit about her, she actually dated Bill Gates when she was actually worth more than Bill Gates was, so has some interesting life experiences as well. I'm assuming you're not worth more than he is now, I mean that's my assumption tonight.

Ann Winblad: It depends on what you're measuring.

Dean Linda Livingstone: Well that's exactly right. But it is my pleasure to bring to you Ann Winblad, cofounder of Hummer Winblad Venture Partners.

Ann Winblad: I tried to edit that Bill Gates thing out of there several times but it keeps coming back. Anyway I always feel like I'm speaking to groups associated with universities during bad economic times. One of my worst speaking engagements was being the commencement speaker for the MBA class at the

University of St. Thomas in May of 2001 that was people were a little nervous about where they would go for their jobs because the market had just crashed. So today I'm going to talk a little bit about the economy and venture capital as a whole and I'm fortunate to have one of my colleagues from Selby Ventures, Bob Marshall here so he'll keep me honest if I say anything bad about venture capitalists I'm not supposed to.

I just came back from Dubai so I've been on a 12 hour time difference and I was at the Summit for the Global Agenda sponsored by the World Economic Forum and our job over two days in 70 working groups was to come with some advice to the G20 and to the World Economic Forum in Davos and the headliner from this is we needed to reboot the entire world economy. I was happy about that because when people use the word reboot I know that nerds are ruling the world. So today there are about 750 or so venture capital firms in the United States and we manage about 257 billion or so collectively. Despite the bleak economic forecast, a closed IPO window and dramatically few M&A assets although there are some right now, we'll invest about 20 billion dollars in promising private companies in 2008. So we've been in a pretty steady state of that 22 to 25 billion dollar number for the last ten years and it's unclear how much venture investing will slow in new companies as we will have some inward focus on our existing portfolio companies but there's no expectation at all that venture capital will dry up, especially here in Silicon Valley. Venture capital firms are really built for good times and bad times, we're long term investors and we don't abandon ship in down times. Our role in the best of times is to be part of the engines for growth and help companies build and scale but it also includes helping our portfolio companies tighten their operating belts to survive downturns and thrive in tougher economic times.

Although we didn't issue any press releases or PowerPoint's with tombstones, meat cleavers and death spirals we've been working closely with each of our portfolio companies to help them tune an operating plan that matches on certainty next year. But really all and all our job is we're risk reduction engineers, our real job is to face the challenges and lean forward. If you can't see a glass as half full you can't be a venture capitalist. Doesn't mean we ignore what the challenges are but we lean towards the future. As long term investors the reason that we have our jobs is we look for disrupters to current industry. So if you're in one of those large companies we're trying to disrupt you. We really are the essence of capitalism, companies succeed, companies fail, it's really creative destructionism at its best, it's what has built the country we live in and what might get lost here in some of the actions going forward by perhaps our government.

But we can't be confused, we as venture capitalists are mere opportunists, we have to be paired up with visionaries, we depend on entrepreneurs to define the breakthroughs and really point us in the direction of large market opportunities and we really have seen over our 20 years as a venture capital firm and my

32 years as a software entrepreneur that there's really no correlation between economic cycles and innovation and I will tell you the story from experience, not from reading history because I was there and I'm glad Bob and I are close to the same age because it doesn't make me feel so old.

Bob: You're nowhere close to me.

Ann Winblad: Okay, so when I left the Federal Reserve Bank, you know, I was a pretty young entrepreneur and I got this big job, it was right out of college, I was working on my masters in executive program. I couldn't do the MBA because I had a double major of Mathematics and Business under grad and I would have had to take the same business courses over again. So the only way I could get the international economics degree is to put education alongside of it. So after about 13 months I sort of felt like wonder woman, I had my masters degree, I was making a bigger salary than my dad, not hard because he was a high school basketball coach but it still is something to measure. So I quit my job to start a company, so this period which was now almost 1976 was really interesting and I never thought about it but unemployment in the state of Minnesota where I was, was over 11%, inflation was at 11.3% there was really interesting tax structures. I think there were 24 different tax brackets at the time and including a 49% capital gains tax at that time. As we moved into the '70s things got even worse, our President resigned, the Minnesota Vikings lost the Super Bowl one of those years. So to describe it as a period of inflation, mêlées, and mistrust is really just understating, you know, how horrible it was.

But if we look back at that period of time, I quit my job and started a little company, we became the 16th largest PC software company, FEDEX was started at that time, Bill Gates was convinced to drop out of Harvard by his friend Paul Allen and start Microsoft. Steve Jobs sold his VW bus in Oregon and started Apple, Genentech was started and towards the end of the '70s a little company down the street here Oracle got started. So all of us were entrepreneurs and we just walked away from the present and into the future with the belief that there was enough disrupters.

For many of us at the Federal Reserve Bank we started getting smaller computers and the reason that I thought I could start a company is I could afford to buy a computer and develop the software myself because I also had learned to be a computer programmer and in most cases with these companies the very young venture industry followed. There were only a few venture capital firms at the time because there were some issues, the ARISSA Laws weren't changed yet but in 1972 two firms we know well here, Sequoia Capital and Kleiner Perkins were started, so they were very, very young firms at the time. If we march forward and we look at the dotcom debacle and, you know, we won't have any comments on that because lots of us lived that, you know, out of that came Google another powerful combination of

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entrepreneurs and venture capital and it didn't come right away, I mean it grew to be a billion dollar company in the shortest time ever in the history of the software industry but it took a few years to find its way as well.

So in the last 30 years the venture industry has been an important partner to entrepreneurs and developing many of the sectors that are the backbone of our economy and world economies. So when we say we're gonna reboot the economy it means it's entrepreneurs that are gonna do it and we will be lucky to ride along as venture capitalists. Those sectors that, you know, I'm referring to are software, computer hardware, the semi-conductor industry, bio technology, communications and last year venture capitalists had obvious amounts invested in clean technology, alternative energy, pollution control, recyclings, conservation, so the power supplies and environmental companies. So if you look at what this has done for us, just quickly, since 1970 venture capitalists have created companies that accounted for 10.4 million jobs and over 2.3 trillion in revenue in 2006. So in 2006 which is the last time they counted all this stuff, venture capital companies generated almost 18% of the GDP in the US and 9.1% of all the private sector employment.

So it really will be this creative destructionism one more time that will actually allow, you know, us to bring this country back to vibrancy and for many of us to create a lot of new wealth for ourselves and employees. We think this result should continue and the other thing that's been added here is we're in a global economy. If I look back at the companies we funded 20 years ago, everybody was here, we could see everybody in the room, the engineers were down the hall, actually they were in the front at first until they hired a management team and now, you know, I have an open source company that I'm on the board of called Mule Source, it's an open source ESP doing very, very well and I was on the board of that company six months before I met all the engineers. They did a world meet up and twelve engineers that were the key contributors came from nine countries.

So we really have a broader base to really draw from. As was mentioned with your partnership with UCSB, most universities have incorporated entrepreneurship into their curriculum, many of them have schools of entrepreneurship. I think it's a brilliant idea that you-- they need your help at UCSB, I was down there about a month ago and spoke to all the computer scientists and, you know, pair fast, you know, it's been a lethal combination for, you know, our powerful combination here at Stanford in the Basis Program started by the School of Engineering and we funded a couple of companies out of that program. So I think that'll be really great for you. Technology has also created a lot of efficiencies in our cost structure so actually in the software segment, the cost of starting a company has actually gone down.

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Today any software entrepreneur anywhere in the world can launch a product in the cloud if they're-- I'll give you a good example; this is a company we did not fund but it's such a good example that I usually give it. A company got started and they were doing small protein modeling and their idea was to come up with improvements in compounds for drug discovery and they started before cloud computing. So they raised about 25 million dollars because every one of these models to a 50 server cluster and they actually spent a bunch of money at Capex, they couldn't run very many models simultaneously and the company blew up, was not one of ours. We're not deep enough in, you know, small proteins to know if it was a good company or not, but the company showed up at our doorstep and said "Look, you know, we bought back the IP last year and we got restarted and we've actually sold two compounds already to Merc and our computing resources cost $75 a month on the Amazon cloud, we don't actually even have-- we only have a couple of computers ourselves, we can run multiple models and turn them off and on because we don't have to commit to the 50 server cluster as somebody's data center," that's just one example.

Open source has also made a dramatic impact on companies started, so we're seeing the level of startups actually increase pretty dramatically because the barrier to entry is very, very, very low. When I started open systems I had to buy one of the first Intel based PCs and I needed to buy two of these computers and they each cost $25,000 and there weren't any venture capitalists around in 1976 who were funding software companies and the ones that were around, you know, were only four years old and we hadn't met each other, so I decided to go to a bank. So I went and looked at all the banks that there were in Minneapolis and St Paul and there were a lot then and I ranked them from the smallest to the biggest and thought, well maybe I'll try the small ones out first because I can't imagine a small bank giving me $50,000 and so there were about 12 of them and I was on bank 11 and I gotten no-- in fact I can now know when the person was gonna say no and I could just-- the facial expression, it was always a guy. So I thought, alright I got to try something new, so when I was in college I finished my majors really quickly but I was on a four year scholarship so you couldn't leave early, so the last semester I took the acting classes and I thought, okay now I know I can finally use those acting classes.

So as soon as I saw that facial expression on that banker that he was gonna say no, I cried and the guy gave me $50,000. It's a lot easier now because it doesn't take $50,000. As long as you can convince people to work for no salaries for a while, your capital requirements are virtually nothing including your software development environments. In fact even just last week and Bob knows this, Microsoft instituted a program that if you were venture backed, less than three years old and less than a million dollars in revenue you could join the Biz Smart Program and get all the Microsoft software that ever existed, development tools, office tools for free and you just had to pay them $100 which was, I don't know why, just so that you had to pay something because Microsoft can't really go free, it's too hard for them. So anyway all the expensive building blocks for most of the complex software is available to innovators in near zero costs.

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A lot of other things have happened, nano technology or the science of new materials has really reached past it's adolescence and that's really impacting not only the computing environment but also the sciences of new energy and we're not energy investing but it is a really interesting area and this is accelerating the pace of new business opportunities. This happens every time there's a down turn, we see more business plans, you know, people really see the reality that larger companies, while they're reconfiguring themselves, there's not a lot of new projects going on, at least for a short time so there's a window of opportunity where you can elbow your own space onto the market map. So that's the glass half full view.

The credit crisis, the demise of the leading investment banks, if we were going to try to take a company public today, we wouldn't even know who's an investment bank anymore and, you know, sort of the seismic instability in the capital markets has really shut the IPO window and this a first for Bob and myself. It used to be that great companies could go public anytime, even great companies cannot go public right now. So in the first half of 2008, only six venture backed companies went public and none went public in Q2 and I think only two so far have gone public in the second half and this is really unheard of for us. So exits are on the distant horizons. Now probably unbeknownst to you, we actually have a business model as well, our money comes from pension funds, endowments, family run foundations, some corporate and we have to return money to them for them to keep funding us. We usually-- most venture firms raise money every three to four years, three and a half years is probably an average. We just raised our last fund fortunately last year so we don't have to look out for three and a half years. But the lack of exits in the short term will win out some of the companies, not only some of the portfolio companies we have but some of the venture capital firms as well, they'll just be unlucky enough to not have capital to invest and have a hard time getting new capital during a window we don't know how long that will last.

In 1989 we raised our first fund and I was talking about that earlier, I didn't really intend to become a venture capitalist but I was kind of hunted down. After my company was acquired, it was one of the first PC software companies to get any liquidity and that's why I had more money than Bill Gates. He always had a hundred dollars in his pocket but he never spent it. So he had it just in case until they finally went public and then he actually had some cash. But when I moved from Minneapolis to California it was right after-- it was the follow on from the crisis of 82/83 when disk drives blew up and semi conductor companies blew up and so John Hummer had read about me and called me up and was hounding-- he hounded me, he stalked me. At five foot two and three quarters I'm the shortest venture capitalist in Silicon Valley and John is six ten, he was the first round draft pick out of Princeton before he got his MBA at Stanford and joined a small venture fund. So he hounded me to start a venture capital fund and he did not tell me that venture returns at that time were just like zero and that no one had created a new venture capital firm for five years.

So we had 133 meetings to raise our first 35 million dollars. Some of them are very memorable, most of them because software was not a big investing area at the time, people would say don't the assets walk out the door at night and I always liked to answer honestly, I know it's a yes, the intellectual capital is the core asset and they do go home at night, sometimes quite late but they do ultimately go home. So people didn't want to fund us. One big fund whom I will not name, the guy asked me if I would come into his private office and he wanted to show me his pictures from his trip to Sweden as I have a Swedish last name and it was a big, you know, kind of family fund thing and when he asked me if I wanted to sit on his lap and see the photos I thought we wouldn't get money from them. So we tried almost everything to raise this money and finally we did but not everything. So, you know, what happened then though, anyone who created a fund in that year, '89 vintage funds, the year we were created is our vintage, we're the best performing funds.

We funded 16 software companies, eight of them went public and we funded the A round companies like Wind River, we funded ten engineers, Hyperium, we funded two people, Scopus which went public and later became the Siebel CRM system, we funded four, you know, Israeli brothers. So these are at times of extreme challenges for raising new funds but, you know, I think anyone who has <inaudible> 2009, 2010 fund, you know, they're going to have a competitive advantage, they're going to be doing fresh deals, looking towards the future and those will probably be the best vintage funds, you know, for actually saying look there'll be fewer companies funded, less competition, it'll be a time for building the companies versus trying to sell products in market. So there will be unfair competitive advantages for those who are successful during this period of time, both from the venture side and from the entrepreneur side. But there's no, you know, kidding that this will be a lot of hard work.

So what does this mean realistically is that it's a great time to be an entrepreneur, you know, there's already-- it's already obvious because of the number of layoffs even here in Silicon Valley that the competition for talent which became quite intense about a year ago, the cost of engineers has gone down so that again is your cost of starting is lower but you'll have a better talent pool to judge from. You know, every time we tried to hire an engineer we were outbid by VM Ware, you know, and I think that's stopped at this point in time. So, you know, we're very, very fortunate in both this country and in Silicon Valley in that we have a culture that exalts entrepreneurs; so it's an unfair competitive advantage for us here and for those who have entrepreneurial economies. We recognize failure as a real life learning on the route to success that's very, very, very rare around the world, even though we tell people that, you know, that's what, you know, capitalism is really about and that's why we call it "Risk capital" you know, people really don't like to fail. So, you know, again we find our self with, you know, a small set of disciplined and experienced company builders, probably get a little bit smaller in the next couple of years and we can have a really major impact over time.

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For us as software investors we used to have to wait for platform shifts. Why we were so fortunate in 1989 is that it was kind of the end of the PC software era but it was just the beginning of distributor computing and client server computing and it was Oracle that kind of threw the torch in there with the distributed database. So the platforms changed, then came, you know, the internet for full distributor computing. But now we're no longer waiting for platforms. If you look at the computing environment, you know, the data center is a computer or cloud computing is really changing the landscape and the participants. Nokia is as much a participant in the software business as is Amazon, as is Microsoft. Who's led the way in cloud computing, Amazon. Open source, another big disrupter, virtualization, the list goes on and on. So like was we agreed at it in Dubai is that how are we gonna reboot the economy and how do we reboot ourselves during this is we do what we know how to do and we roll up our entrepreneurial sleeves and we create great companies and I hope some of you will have an easier time than I.

Although I will tell you one last secret which is that food stamp story; because I didn't have enough money to hire those engineers, I thought how I am going ever hire five engineers? So when an engineer would come and get interviewed, I would say "How much do spend a month on food?" And I discovered engineers really eat a lot so, you know, no engineer's going say $10, so when they said like, you know, $600 which was a lot then, I'd say "Great, what if I could give you $7200 a year free food, can I deduct that from your salary?" and they'd go "Okay." And so I'd gotten really good at qualifying anyone for food stamps in the state of Minnesota so that's how I was able to hire my five engineers. So thanks very much for inviting me tonight and I wish you all great success in opportunistic times, thanks.

End

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